Market Information and its Contribution to SMES' Access to Loans From Banks in Tanzania: A Case of Selected SMES in Dar Es Salaam City

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ABSTRACT

Market information is a necessary ingredient for SMEs performance, as it enables SMEs to solicit funds for expansion and improvement for business. Banks also need information that helps them understand creditworthiness of SMEs and operators in order to minimize risks of default and losses. This study assessed business-related information flow between banks (financial institutions) and SMEs operating in Tanzania. The study was carried out in three Municipalities of Dar es Salaam, namely, Ilala, Kinondoni, and Temeke. A survey involved fifty SMEs, five banks (four local and one foreign), one foreign non-bank financial institution and two micro-financial institutions which were purposively selected in order to collect data from a wider range of the targeted financial institutions (macro and micro) and to cover different industries in which SMEs operate. Interviews were conducted using a semi structured questionnaire guide that provided a checklist of questions relating to banks and financial market information to SME operators. The results showed that, a serious information asymmetry exists between these two parties and that; several factors underlie its existence. Market failure, inefficiencies existing among players in the private sector on the one hand, and banks on the other was the main cause of market information asymmetry. The study revealed further that SME operators have limited knowledge and skills of operating business, and financial management; and majority of them lack business ethics especially when they are required to disclose information required by bankers and other Financial Institutions for determining their creditworthiness. Thus, many SME operators resorted into deliberate cheating or presenting inappropriate information, in most cases and ending up being disqualified for loans. The study concluded that, there are serious information gaps between SMEs and FIs. Additionally, some FIs hide some important information. This increases repayment burden among some SMEs upon securing loans because of lacking all the required information. The study recommends for the enhancement of market information among the SME's from FI's. Further studies on information dissemination methods are also recommended.

Key words: *SMEs, market information, banks and access to finance*

1. INTRODUCTION

Market information is important to Small and Medium Enterprises (SMEs) in order to improve their access to financial services worldwide. Studies (e.g. Magesa *et al*., 2014; Temba *et al*., 2016) admitted that, market information is a key parameter in improving markets and the entire production cycle. On the other hand, lack of sufficient information among the banks about SMEs especially in terms of their business and credit status compel them to cut down consciously loans lending to SMEs (Huang *et al*., 2014). Limited market information and market access have negatively affected farming entrepreneurs in Tanzania as well (Aku *et al*., 2018).

According to Beck and Cull (2014), Africa's SMEs have little access to finance triggered by limited access to bank loans. Lack of collateral assets and information about payment abilities have been the main reasons for SMEs failure to access loans from the banks. These reasons implicitly suggest that there is a lack of effective bilateral information relationship between the banks and SMEs. According to Bbenkele (2007), it is important build a good relationship between SMEs and the commercial banks as a way of improving access to finance.

Therefore, in order to increase SMEs access to finance, market information on credit services and its appropriate dissemination is inevitable. Non availability of market information denies SMEs from making decision on how to finance their businesses. Moreover, literature reveals that, information asymmetry between financial institutions and SMEs constrain deny SMEs access to financial services (Huang *et al*., 2014); according to Harelimana (2017), access to finance improves SMEs profitability, efficiency, and solvency, solves liquidity problems, and increases assets quality. Hence, for SMEs to realize profitability, efficiency, and increase asset quality, the banks need to have adequate and appropriate market information for SMEs operators. Likewise, SMEs must get all the necessary market information on availability of financial services. Such information is paramount for both parties as it may upscale their business relations.

Although theories of information asymmetries and transaction costs aim at resolving the differences on information held between the two parties and reduce the implied costs, SMEs and financial institutions still have widened the information gap. Financial institutions consider SMEs as unprofitable business and unreliable for credit hence their applications for credits are mostly rejected. On the other side, SMEs fail to launch loans applications to financial institutions, as they are not sure of the criteria the banks impose or use for lenders to qualify for loans. Hence, each side remains hesitant to approach the other for a mere simple reason that market information sharing has been blocked by the worry created by one part or the other.

Despite the existing gap, both SMEs and banks are important pillars and among key stakeholders in the overall economic development. SMEs have a huge contribution to socio-economic development through employment creation, supporting economic development and improving social welfare in general (Ayyagari *et al*., 2011). In the other words, the banks contribute through financing economic projects by channelling money into economic system. Therefore, for the economic system to function efficiently, the two parties must work together harmoniously. Furthermore as IFC (2007) argues, supporting SMEs is a key factor in alleviating poverty as it contributes one third of GDP and creating employment in both developed and developing countries.

Besides their significant contribution, SMEs' long term growth and competitiveness have been compromised by chronic and acute constraints on access to finance in the formal sector through banks and other lenders of capital (Wattanapruttipaisan, 2003). Therefore, the SMEs' contribution to economic development is constrained. In addition, there is a general view indicating that, SMEs override other type of businesses. For example, among the European countries more than 90 percent of businesses are SMEs, while in Africa more than 95percent of businesses are SMEs. in Tanzania in particular, more than 95 percent are SMEs, which contribute about one-third of GDP and thereby stimulate economic growth (Mwita, 2012). However, it is reported that SMEs' contribution could have been greater if the constraints on access to finance were reduced by the provision of market information to both parties.

Several studies have been carried out to address the constraints of SMEs' access to finance (Kauffmann, 2005; Evans *et al*., 2015; IFC, 2007; Lindvert, 2017). The challenges mentioned include capital constraints, lack of access to finance, bureaucratic loan procedures, and poor partnership (Makorere, 2014; Mashenene and Rumanyika, 2014; Mashenene *et al*., 2014; Mashenene, 2015; Kimathi 2015; Anderson, 2017). other challenges include lack of business training, lack of motivation among business owners, lack of social capital, inborn individual attributes, and inadequate human and social resources (Anderson, 2017; Isaga and Musabila, 2017; Juma and Said, 2019; Nkwabi and Mboya, 2019).

However, most SMEs feel that information about financial services and products is kept to the commercial banks and not disseminated to them (Kauffmann, 2005), whereas some studies argue that lack of SMEs' access to financing is due to lack of collateral particularly land (Kasekende and Opondo, 2003; Wattanapruttipaisan, 2003; Kauffmann, 2005; IFC, 2007). Moreover, Evans *et al*., (2015) cited other factors to include problems associated with managerial skills, lack of equipment and technology, lack of collateral and the fear of taking risk.

Although many analytical studies have been carried out to address SME financing challenges, little attention in Tanzania has been directed to the investigation of the status of market information flow between SMEs and the banks. Other assessments were focused on limited market information and low SMEs performance in Kenya (Kiyeu and Ofafa, 2013), and limited information among women entrepreneurs in Tanzania (Nyangarika, 2017). Hence, this study seeks to investigate this status and provide information that would be used in enhancing relationships between financial institutions and SMEs. The study will address the following questions: i) what is the extent of market information flow from the banks to SMEs. ii) What type of market information do SME operators consider important to receive from the banks to qualify for loans? iii) What information do the banks need to get and verify in order to disburse funds to SMEs?

The study is justifiable because it will feed into developing Financial Economic Empowerment programme. This programme will make financial markets work better for the needy groups including SMEs scattered across Tanzania. According to Currin (2007), information is central for the sound functioning of financial markets. Further, the study will benefit the banks and FIs because it has revealed potential information they require from SMEs. On the practical point of view, this study will define information to be exchanged, the needed behaviour and benefits of realizing both parties. The appropriate information needed will strengthen the relationship between financial institutions and SMEs owners. The study has also contributed to the efforts of other stakeholders such as the Government and development partners who are striving to upscale the role of private sector in the economic development of the country.

Theoretical Framework

The study adopted two theories to describe the existing relationship between SME's and FI's, and the extent in which these parties can benefit from the component of market information. Specifically, the description of this relationship is confined on the component of market information in the operation of these partners. These theories include The Theory of Information Asymmetry and the Agency Theory.

The Theory of Information Asymmetry holds that it is difficult to distinguish good and bad borrowers (Auronen, 2003). This results into adverse selection and the problem of moral hazard because the banks as lenders may make wrong choices and lend to someone who is not credit worthy and also may lend to people who actually have bad intention on money borrowed and therefore all the costs will fall to the lenders.

According to the agency theory, the relationship between the principal (lender) and agency (borrower) diverges because both parties have different interests and utility function. This situation normally makes the principal and agent prefer different actions because of different risk preference (Mori, 2018).

These two theories explain the situation existing between the banks and SMEs in the lending process. In the process of lending, the banks have been keen to ensure that they lend to reasonable and profitable businesses. Therefore, they take keen measures to ensure that the money advanced is not lost and it yields profits by making good selection of people and businesses that have good future. On the other hand, the banks and SMEs act as a principal and an agent respectively. The principal's interest is to maximize profits while the agent aims at gaining benefits from the execution of its activities. The relationship between the principal and the agents breaks due to the differences in views, interests, and the risks embedded on each other. These theories explain the lending behaviour given the existence of the agency problem and the imperfect information existing between lenders and borrowers.

Definition of key terms

Small and Medium Enterprises (SMEs)

SMEs are the emerging private sector in both developed and developing countries and form the base for nation's development and growth. Definition of SMEs differs across different countries. Small businesses in Europe are not the same as those found in developing countries like Tanzania. However, in most cases, SMEs definition includes some key words such as capital size invested, employment size, gross profit of the firm and of the sector involved (OECD, 2005). According to Tanzania, SMEs are defined as the micro, small and medium size enterprises in non-farm activities, which include manufacturing, mining, commerce, and services (URT, 2003).

These types of business are differentiated by the number of employees, capital size invested, and turnover. Table 1 shows the main categories of SMEs according to Tanzania perspective.

Table 1: Categories of SMEs

Category of Enterprises	Number of Employees	Capital Invested (Tshs) in million	Turnover (Tshs) in million
Micro	1 to 4	up to 5.0	12
Small	5 to 49	5.1 to 200	150
Medium	50 to 100	201 to 800	300
Large	101 and above	Above 800	300

Source: *URT, 2002.*

Banks

The banks are very important part of the economy because they provide vital services for both consumers and businesses (McLeay *et al*., 2014). A bank is defined as a financial institution licensed to receive deposits and disburse loans (Demirgüç-kunt, 2008). The lending activities of a bank can be performed directly or indirectly through capital market. Banks may also provide financial services such as wealth management, currency exchange, and safe deposit boxes. There are several different kinds of banks including retail banks, commercial or corporate banks, and investment banks. Due to its important in the financial stability of the country, banks are regulated by the national government or central bank. For the purpose of this study, a bank is regarded as the lending institution that provides access to financial services to both individual and entities adopted from the definition of Demirgüç-kunt (2008).

Market information

Market Information means information such as price curves, volatilities, interest rates, and similar information for which quotes are customarily available from reference market makers (Palumbo, 1970). In the previous management, marketing was area, which was often, neglected. It is only recently that many corporations have become aware of the need of marketing data for decision making process. This is true for the banks and financial institutions because market information takes a back seat to the operational system. The market information that SMEs needs from financial institutions and the banks includes interest rates, criteria, or condition for lending, collateral assets, and repayment modalities.

Access to finance

Access to finance is defined as the ability of an individual to obtain financial services, including credit, deposit, payments, insurance, and other risk management services (Demirgüç-Kunt *et al.*, 2008). The World Bank (2007) defines access to finance as an absence of price or non-price barriers in the use of financial services. This does not mean that all individuals and SMEs should be able to borrow unlimited amount at prime lending rates. This study has adopted a definition of access to finance that refers to the availability of financial services at affordable rates (Claessens, 2006).

2. METHODOLOGY

The study was carried out in Dar es Salaam City in three municipalities namely, Ilala, Kinondoni, and Temeke. The city was selected based on the fact that it is the largest commercial city in Tanzania hosting majority of SMEs (Magembe, 2019). A case study was adopted to collect data in the selected municipalities. The lists of registered SMEs were obtained from these municipalities, which were utilized as sampling frames. From each list, simple random sampling was utilized to select the required number of SMEs based on investment worthy between TZS 5 million and TZS 200 million guided by the classification criteria stipulated in the Tanzania SMEs Policy (URT, 2002).

The Operator for each selected SME was thereafter contacted and interviewed through a semi structured questionnaire guide. These SMEs were drawn from both urban and peripheral areas of the chosen municipalities. Overall, 50 SMEs were selected where 18 were from Ilala, 16 from Kinondoni and 16 from Temeke Municipalities. Furthermore, five banks (four local and one foreign), one foreign non-bank financial institution, and two micro-financial institutions were involved. One representative from each was interviewed as a key informant using an interview checklist.

The study utilized both qualitative and quantitative data. Views and opinion from key informants were analysed through thematic content analysis. Quantitative data elicited through surveys were subjected to SPSS programme. Descriptive statistics were utilized in which frequencies and counts were produced. Furthermore, a desk work review was extensively done on the existing literature to establish the existing debate on SMEs performance and its collaboration with FIs. This review was particularly key to supplement the primary data, which were collected through surveys and key informants interviews.

3. FINDINGS AND DISCUSSIONS

Extent of Information Flow from Banks to SMEs

The study was interested in establishing financial information, which SME operators have regarding financial services. The questions were focused on the sources of information, the type of information they received, and the type of information they would prefer to get from the banks. Generally, all interviewed SME operators reported that they had information that the banks need SMEs in order to lend money to them (Table 2). However, of all respondents, 40percent of the operators were able to distinguish different sub types of financial institutions that lent money (i.e. different categories of macro- and micro financial institutions). For example, they mentioned banks and non-bank macro-financial institutions that provide loans in Dar es Salaam and were able to demarcate the threshold amounts these institutions could disburse as loans.

Nonetheless, 60percent had limited awareness of the subtypes of these institutions as they distinguished only two major types of financial institutions (macro- and the micro-financial institutions). Apart from distinguishing these FIs on the basis of the size of loans they could offer, no further attempt these entrepreneurs could make to describe other characteristics of the FIs. For example, they could not explain how the government regulated the operations of these organizations. Other forms of financial-lending firms that exist in Dar es Salaam, but were unrecognized by these SME operators include international non-bank financial institutions that offered loans/credits using diverse funding mechanisms, majority of the operators reported to have not been aware of them.

Table 2: *Distribution of the Respondents on Information Flow from Banks to SMEs*

Respondents	Number of respondents	Percent
Low awareness	30	60
More aware	20	40
Total	**50**	**100**

SMEs' Information Sources

Regarding sources of information, SME operators mentioned a number of sources from which they derived information. These were media (TV, radio and newspapers) and normal conversation from their colleagues who had already secured loans from the banks. Others reported that some financial institutions were sending their officers to market their products directly to the SME operators; yet others had information about financial services from promotional activities of the FIs (mainly the banks). Normally, these banks went around the city suburbs on specially-made promotion trucks to promote their products.

In adapting to technological advancement, majority of the banks now own websites through which customers can browse and access the information they need. However, the issue of concern is whether the type of information displayed in these websites satisfactorily enables potential and ongoing customers to make right decisions. The National Bank of Commerce (NBC Ltd) for example summarized services it offered to her customers to include overdraft and term-loans, but did not explain issues related to collateral and how repayment was deducted on a monthly basis from borrowers, unless the borrowers had to read NBC's Credit Policy which was not available at the website (www.nbctz.com, 2020).

Furthermore, SME operators were requested to explain their knowledge about computer and ICT application. Of all interviewed operators, 81percent reported that, they did not know how to use internet services. This linked their low understand with the lack of knowledge on computer application (Table 3). They argued that they were too busy to dedicate their time to learn computer applications. In this case, very few operators were able to use the bank websites to access market information to improve performance of their SMEs. Here are the views of the SMEs owners contacted.

One SME operator based in Mbagala, for example, said,

> "*the information displayed by CRDB Bank PLC regarding corporate loans threatens SMEs, because it required a lot of supporting information which was too costly for entrepreneurs to bear.*"

Another operator in Mwenge area was quoted saying,

> "*Although we occasionally hear about financial services offered by the banks from different sources, we cannot rely on every information source; we rely much on information sourced from our fellow entrepreneurs who have already secured loans and exhibit the benefits.The reason behind is that, some information sources that is, information delivered during promotion programmes is exaggerated to attract customers, hence, not much reliable. In addition, there is a limited chance of asking all necessary questions we would like to know their answers.*"

Opinion regarding limited access to information sources on modern technology is also supported by a study of other scholars (e.g. Mpunga, 2016; Kabanda and Brown, 2017) who mentioned poor technological adoption as a barrier confronting SME development. Results from this and the other studies reinforce that utilization of electronic information sources among SMEs' operators encounter challenges. However, science and technology remain key parameters in SMEs development. This necessitates further intervention to enable SMEs increase ICT applications in their operations. On the other hand, more devotion among SMEs to adopt new technology is inevitable to enable their prosperity and sustainability.

Information Type SMEs Receives from Banks (Financial Institutions)

The type of information SMEs have on services offered by the banks is a key in making appropriate decision. This information can positively guide operators, or in the other way round it can mislead them and trigger poor decision making. Due to this fact, the study was interested in ascertaining the type of information SMEs have on financial services offered by the financial institutions. Distribution of SMEs operators and information they had received from FIs is presented in Table 3. The findings reveal that 88percent of SMEs operators who had already received loans from the banks (FIs) indicated that they received information about interest rate and the amounts they were required to pay on monthly basis and time they would spend to pay the loans. This is however, not the only information SMEs needed.

The study also established whether the SME operators had received information about the total cost of borrowing money (fees, insurance and interest etc.), types of loans/credits offered, mortgage and collateral-related issues, repayment period, and models (reducing balance or constant rate models). Even those who received the information regarding these aspects, such information was cumbersome since it is in technical or legal language, which they could not understand. Due to their financial needs, many operators were obliged to comply with the conditions, which were imposed by FIs without really understanding the other hidden aspects. This eventually leads into the negative impacts resulting from the unforeseen increased loan charges.

This appeared to be a serious challenge among the SMEs operators who eventually encounter loan repayment problems. Coupled with low capital among most of SMEs (Kimathi, 2015; Mashenene, 2015; Lindvert, 2017) this challenge negatively affects the growth of most SMEs. This challenge partly emanated from their limited knowledge coupled with lack of transparency among some FIs. This calls for the joint collaboration in order for each part to benefit from the existence of the other.

Discrepancy elaborated in Table 4 implies existence of an information gap between what the financial institutions provide and what SME operators expected to receive. There is a serious information asymmetry surrounding SME lending. Regarding the information indicated in Table 4, 74percent of SME operators indicated that little initiative is pursued by banks to inform SMEs about loan charges unless they were requested to do so. This tendency appeared to be very serious among micro-financial institutions. These institutions do not inform SME but eventually they charge higher interest rates per month than the banks do.

Table 3: Distribution of Information Type SMEs Received

Information type	**Number of respondents**		
	Yes	**No**	**Total (%)**
Interest rate	50 (100%)	0 (0%)	50 (100)
How to calculate interest and principal	2 (4%)	48 (96%)	50 (100)
Total borrowing cost (fees and interest)	6(12%)	44 (88%)	50 (100)
Repayment schedule and modalities	23 (46%)	27 (54%)	50 (100)
How long it takes to pay back the loan	50 (100%)	0 (0%)	50 (100)
Collateral related issues	47 (94%)	3 (6%)	50 (100)
Legal aspects to be met	11 (22%)	39 (78%)	50 (100)
Loan evaluation procedure	1(2%)	49 (98%)	50 (100)

Moreover, one of the implications is that enterprises had to pay extremely high interest per annum, which reduced their sales margins. For example, an interview with one SACCOS' management staff in Mbagala and Kigamboni indicated that they were charged 3-5 percent that is accumulated to 36 to 60percent per annum. These rates were comparatively too high for some enterprises to bear particularly the microenterprises.

Further, SME operators indicated that they were aware of the two major loan facilities offered by banks (FIs) especially, the macro financial institutions (Banks and non-banks). Thirty nine respondents (78%) indicated that they knew two major loan facilities offered to the SMEs, the term loans and overdraft, but the remaining 22 percent indicated that they were unable to distinguish between the two. How could these decide whether to apply for a term loan or overdraft? The answer is probably an obscurity.

4. CONCLUSIONS AND RECOMMENDATIONS

The study established that, despite the fact that most banks (financial institutions) have tried to provide some information to assist SMEs to make decision before approaching them for loans/credit. SMEs reported that part of the information received was inappropriate to guide them towards making sound loan-application decisions. This leads to the conclusion that, majority of SMEs are not empowered because they were not well informed about FIs products. Consequently, this creates hardships for SMEs to access services from FIs especially securing loans for improving productivity. In particular, some SMEs operators were regretting after securing loans from some of the financial institutions because they were not transparent on certain important information. This leads to a conclusion that, some FIs do not really consider financial needs of SMEs as their potential stakeholders. Furthermore, the type of information available to SMEs on banks is more limited to collateral, interest rates, and the amount to be paid. This indicates the existence of low transparency among FIs to SMEs as their stakeholders in business.

The study recommends to FIs to enhance information awareness among SMEs in order to enable them to make the right decisions about loans applications. This may go hand in hand with establishing a strong network that may link the two parties and may have a value addition in information up scaling across these parties.

Furthermore, FIs should not confine themselves with particular loan information, rather they should increase transparency on different aspects involved on loan and the applications processes. This will increase the scope of clients especially, SMEs who will be empowered through the process.

Finally, the present study was limited on market information between two stakeholders namely SME's and FI's. This necessitates further studies to explore information dissemination methods and their effectiveness across these parties. This will increase a win- win attitude among these and other business partners.

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