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The impact of debt financing on performance of Small to Medium Enterprises (SMEs): A Case of Bindura District

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Dedications

I dedicate this project to my family.

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Psalms 118;22 This is the Lords doing, it is marvelous in our eyes. I would like to thank the Lord almighty for giving me strength to carry out this project against all odds. My most profound gratitude goes to Mrs Mazodze and my family for their encouragement, love and support. I would also want to appreciate my supervisor Dr Mauchi for her patience and guidance in carrying out this research. Not forgetting my friends who helped me and stood by me during the toughest times.

Abstract

This study was conducted to determine the impact of debt financing on performance of SMEs in Bindura. Debt finance was the independent variable and performance was the dependent variable. Performance was measured by three indicators namely sales growth, profitability and assets growth. The following were the objectives of the study; to analyse the impact of debt finance on sales growth, profitability and assets growth and to also determine how SMEs can use debt finance to improve their performance. Primary method of data collection was used in the form for questionnaires. The study had a target population of 45, a sample size of 40 but 35 respondents completed and returned answered questionnaires. Stratified sampling technique was used in determining the sample to make sure that SMEs in various businesses were included in the research. Tables, pie charts and graphs were used to present data which was analysed by SPSS 21. Findings of the study indicated that debt financing had a negative impact on sales growth and profitability. Results further showed that debt financing had a positive impact on assets growth. The major finding shown by the regression model showed that debt financing had a negative impact on overall performance of SMEs in Bindura. This was mainly due to the fact that it is expensive. The author also discovered that a number of SMEs are highly leveraged and that is why it has a negative impact on their performance. The author recommended that SMEs should seek for cheaper sources of finance to improve their performance.

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List of abbreviations and acronyms

AG	Asset Growth
GDP	Gross Domestic Product
GPM	Gross Profit Margin
SMEs	Small to Medium Enterprises
NPM	Net Profit Margin
NPV	Net Present Value
MFIs	Micro finance institutions
RBZ	Reserve Bank of Zimbabwe
ROA	Return on Assets
ROE	Return on Equity
SG	Sales Growth
SMEDCO	Small and Medium Enterprises Development Corporation
SMEAZ	Small to Medium Enterprises Association of Zimbabwe
ZSE	Zimbabwe Stock Exchange
ZIMRA	Zimbabwe Revenue Authority

CHAPTER I

INTRODUCTION

1.0 Introduction

This research serves to unearth the impact of debt financing on performance of Small to Medium Enterprises (SMEs). This chapter will explore the following areas, background of the study, the problem statement, research objectives, research questions, significance of the study, assumptions of the study, delimitations and limitations of the study.

1.1 Background of the study

Capital structure is one of the elements that holds a bearing on improving firm's performance (Sheikh and Quresh 2017). They go on to emphasize that management is tasked to make financing option decisions depending on the risk appetite and risk tolerance of the firm. Ehrhardt and Brigham (2011) agreed that one of the four strategic financial decisions include determining how much of capital should be debt and how much should be equity thereby determining the capital structure of a firm. According to (Tuovila 2021), capital structure is the particular combination of debt and equity adopted by an organisation to finance its overall operations and growth.

Mostly, a firm's capital structure comprises of debt and equity (Erhardt and Brigham 2011). They go on to define equity as shareholders injections into the firm and debt as any form of external borrowing. Strategic financing decisions on the appropriate levels of debt and equity at the lowest cost to the company have a big impact on firm's performance (Davies, Boczko and Chen 2008). The agency theory formulated by Meckling and Jensen (1976) prove that debt financing is a better source of finance because it reduces costs associated with agency problems thereby improving firm's performance. Brealey, Myers and Marcus (2001) emphasize that interest on debt is tax deductible, meaning that it is subtracted from a firm's earnings before tax is charged. This tends to reduce earnings attributable to tax thereby increasing the firm's net profit. These examples show that debt financing enhance firm's performance and must be adopted by companies as a source of financing (Magot 2018). However, Myers and Majluf (1984) discovered that firms prefer internal sources of finance as compared to debt and equity due to high costs of debt and volatility of the stock market.

A study by Aziz and Abbas (2019) shows that in Pakistan, there is a negative and significant relation between debt financing and manufacturing firm performance. Findings of the study recommend firms to finance their institutions using retained earnings because they are inexpensive and quite reliable. This is in tandem with the pecking order theory by Myers and Majluf (1984) which encourages firms to fund their organisations in the following hierarchy; retained earnings, debt finance and equity. Another one conducted in Vietnam by Pham and Nguyen (2020) postulated that debt financing had a negative and significant impact on firm performance.

In Africa, a study was carried out by Nwude, Itiri, Agbadua and Udeh (2016) discovered that external borrowing has a negative and significant relation with performance of quoted entities in Nigeria. These findings also concur with the pecking order theory which states that debt financing does not improve performance of firm. The authors recommended that firms should only use a limited amount of debt and more of retained earnings to be better off.

Mushipe (2017) conducted a study in Zimbabwe and discovered that debt financing is associated with high agency costs, exorbitant interest rates and high bankruptcy costs which have an adverse effect on a firm's performance. Muzeya (2017) stated that debt financing had negative statistics and significantly firms financial performance which was measured using Return on Assets (ROA) which holds a significance level of 5%. This study will add on to the existing body of knowledge on the impact that debt financing has on performance of SMEs in Bindura.

1.2 Problem statement

Back in the days, it was difficult for SMEs to acquire external financing. A Finscope survey carried out in (2012) emphasized that SMEs in Zimbabwe struggled to access debt financing, purchase raw materials and work spaces which are important factors that enhance financial performance. A study carried out by Mapeto (2015) also shows that small firms had limited access to funding. Nowadays with the help of organisations such as SMEAZ, SMEs are being assisted to qualify for debt from financial institutions such as banks, microfinance companies and also from the government. After all these efforts, it can be seen that most SMEs sales are not growing, they are not operating profitably, their assets are not growing in relation to their liabilities. Basically, SMEs in Bindura are not growing to become large firms as is the case in developed nations as a matter of fact they are shutting down on a daily basis. This has prompted the researcher to find out if there is any change at all after SMEs acquire debt finance and the impact that those debts have on the performance of SMEs in Bindura.

1.3 Research Objectives

The main objective of this research is to analyse the impact of debt financing on performance of SMEs in Bindura. In vision of the main aim of the study, sub objectives include;

- To analyse the impact of debt financing on sales growth of SMEs in Bindura.
- To analyse the impact of debt financing on profitability of SMEs in Bindura
- To analyse the impact of debt financing on asset growth of SMEs in Bindura
- To give recommendations on how SMEs can use debt financing to improve their performance.

1.4 Research Questions

The main research question is to find out what is the impact of debt finance on the financial performance of SMEs. In-order to satisfy the above-mentioned objectives, the researcher has the following research questions;

- What is the impact of debt financing on sales growth of SMEs in Bindura?
- What is the impact of debt financing on profitability of SMEs in Bindura?
- What is the impact of debt financing on asset growth of SMEs in Bindura?
- How can SMEs use debt financing to improve their performance?

1.5 Significance of the study

1.5.1 To the researcher

The study will empower the researcher in making wise decisions when composing the financing mix as a start-up entrepreneur. It also aims to improve the researcher's ability to carry out research, thereby preparing the researcher for future practical tasks in the finance sector and in her career. The project will also increase the researcher's knowledge on ways that debt financing can improve performance of SMEs in Zimbabwe. Furthermore, the research was done in partial fulfilment of the Bachelor in Commerce Honours Degree in Banking and Finance.

1.5.2 To SMEs in Bindura (and other SMEs worldwide)

The research will assist various organisations to identify merits and demerits of debt finance. In addition to that, it will enlighten them on the impact that debt financing has on performance of their firms. This study will also give them recommendations on how debt financing can improve performance of their organisations.

1.5.3 To the academia

The project will provide information to future Bindura University students on their Finance endeavours. Also, the research will be used as a guide to other students as it will serve as empirical review.

1.6 Assumptions

The researcher has the following assumptions;

- The participants will give true information to enhance credibility and relevance of the study
- The limitations will not affect the purpose and validity of the study.
- Data collected will be adequate to produce findings, conclusions and recommendations
- Limitations of the study will not have any effect on data validity

1.7 Delimitations of the study

- The researcher will make use of data given by willing SMEs in belief that there is other relevant information left out as it may be commercially sensitive.
- Data collected is geographically bound to Bindura town and some of it may not be applicable to other firms in various towns and cities
- This study does not look at other specifics that affect performance except for debt finance only.
- The researcher only looked at sales growth, profitability and assets growth as measures of performance but there are a lot of other measures. Considering that most SMEs do not prepare financial statements, the chosen performance measures were the most ideal

1.8 Limitations of the study

It was difficult to find participants who were willing to give information pertaining to their SMEs. The author overcame this by assuring them that this study was solely for academic purposes.

The researcher suffered a time constraint as this research was carried out in her final year. Besides her courses, she had to conduct this research as well. The researcher had to work extra hard to meet the deadline.

As a student, the researcher did not have enough time to distribute questionnaires to a larger population. To overcome this challenge, the researcher focused on Bindura District where she currently stays.

1.9 Definition of key terms

1.9.1 Debt Financing

Is when a firm raises money for working capital or capital expenditures by selling debt instruments to individuals and or institutional investors (Chen 2021). In simpler terms, it is the borrowing of funds and paying it back with interest.

1.9.2 Firm performance

Is a thorough evaluation of an entity's capacity and ability to utilise its resources in an efficient and effective manner to consistently achieve set goals and objectives (Taouab and Issor, 2019). These resources include human and material resources. Performance also involves the firm's ability to create value for its customers.

1.9.3 SMEs

There is no clear definition for an SME as each country has its own definition. Liberto (2021) defines SMEs as organisations who maintain revenues, assets or a number of employees below a certain threshold. According to Njanike (2009), SMEs are classified according to capital base and others according to number of employees. He also states that SMEs contribute more to the GDP and they also create more jobs. Most SMEs in developing nations are unregistered. The same applies to Zimbabwe as a study carried out proved that 85% of SMEs in the country are informal and financially excluded, (Maseko and Manyani 2011).

1.10 Chapter summary

This chapter serves as the introduction to the study. It involves bringing out the background of the study, identifying the problem statement, research objectives, limitations and delimitations. It is a guide into the research. The following chapter will look at the study's literature review.

CHAPTER II

LITERATURE REVIEW

2.0 Introduction

This chapter will explore already existing information about the subject matter. Literature reviews are designed to give an overview of sources one has explored while researching a particular topic and to demonstrate how the research fits within the field of study. It is divided into 3 major sub headings and these are conceptual framework, empirical evidence and theoretical framework.

2.1 Conceptual Framework

2.1.1 Debt Financing

Debt financing occurs when a firm raises money for working capital or capital expenditures by selling debt instruments to individuals and or institutional investors Chen (2021). In simpler terms, it is the borrowing of funds and paying it back with interest. Examples of debt financing include bank loans, loans from microfinance companies, loans from friends, bonds, debentures, to mention but a few. Bank loans are the most popular source of external financing. The first debt financing that many young firms undertake is a bank loan, however, even large established companies use bank loans as part of their debt financing (Berk *et al* 2013). As postulated by Bierman (2012) corporations in the post-World War 11 period used debt rather than newly issued common stock because of high tax levels and the tax structure, which provided a tax advantage to debt. Interest paid to debt holders is a tax deduction to the corporate issuer, thus the interest expense acts as a tax shied.

However, debt has a lower explicit cost than common stock, it generally has a fixed maturity and since the debt holders are senior to stockholders, the issue of debt adds to the risk of stockholders

(Bierman 2012). This shows that debt financing tends to have an effect on performance of SMEs and the researcher shall shed more light on the matter later on in the project.

2.1.2 Sources of debt finance

2.1.2.1 Long-term debt

Brealey, Myers and Marcus (2001) define long term debt as debt obligations that mature in over a year's period. This means that they do not have to be honoured within a year. Securities such as bonds, term loans, debentures, mortgages and many others are examples of long-term debts (Guerard and Schwartz, 2007). Most of them are secured in order to prevent default risk. Default risk is the risk of loss due to the failure of the borrower to pay back (Bierman 2012). Peria and Schumkler (2017) cite that long-term finance is useful for both the government and firms because it can be used for long-term investments.

2.1.2.2 Short-term Debt

Guin (2011) describes short-term finance as debt securities that mature within a year. Those kinds of securities have to be paid back in the duration of the year depending on the terms and conditions governing the agreement. Short-term debt instruments include banker's acceptance, treasury bills, negotiable certificates of deposit, bank overdraft, to mention but a few Du and Palia (2018). Short-term securities are most popular in Zimbabwe due to the volatility of the Zimbabwe financial system. Most SMEs in Zimbabwe rely on short-term debt because they lack collateral to access long-term debt.

2.1.3 Advantages of debt financing

- There is no need for the owners of the business to give up ownership of their business
- Both the principal and interest payments are deducted from the business's income taxes
- Long-term loans are considered a cheaper source of finance and they help boost an SME performance.
- Debt financing helps firms to establish and build business credit. SMEs struggle to get funding because most of them do not have collateral, they do not keep proper financial reports and they have low credit ratings. It is therefore seen that those SMEs who wish to acquire debt work tirelessly to establish and build their creditworthiness

- Microfinance have loans suitable for any business size as long as they meet their requirements. This makes it possible for all SMEs to get funding.

2.1.4 Disadvantages of debt finance

- Coupon payments are fixed and must be met whether the business makes profits or not. In the case that losses are incurred, interest payments strain the businesses liquidity
- Some external sources of finance charge high rates for example bonds, short-term debts and lines of credit
- Debt affects a firm's credit rating. The moment that a business acquires a loan, it is noted on their credit rating. If a firm has huge debts, it causes its credit scores to drop thereby affecting their ability to keep borrowing

2.1.5 Firm Performance

Is a thorough evaluation of an entity's capacity and ability to utilise its resources in an efficient and effective manner to consistently achieve set goals and objectives (Taouab and Issor, 2019). These resources include human and material resources. Performance also involves the firm's ability to create value for its customers. As postulated by Omaliko, Okeke and Obiora (2021), firm performance is determined by asset growth and profitability growth rate. This means that fluctuations in assets and profits are used to measure firm's performance. Lebans and Euske (2006) orates that there are financial and also non-financial performance measures that are used to indicate how well a firm has achieved its set objectives and accomplishments.

Performance appraisal is important for SMEs because it paves way for improvement, helps to identify strengths and weaknesses and create benchmarks for the firm (O' Neill, 2018). According to Harash, Al-Timimi and Alsaadi (2014), there is no one way of measuring SMEs performance meaning that there is a wide range of performance measures. For the purpose of this research, the author used sales growth, profitability growth and asset growth to measure firm performance.

2.1.6 Indicators of firm performance for the study

2.1.6.1 Sales growth

One major objective for most firms is sales growth because at most it results in increased profits (Sam and Hoshino, 2013). As postulated by Nazir, Azam and Khalid (2021), Tauseef, Lohano, Das and Khan (2015), an increase in sales leads to an increase in profits. According to Habib, Khan and Wazir (2016), sales growth is the percentage change in sales from one period to another. Sales increase due to improved marketing and promotional strategies. Sales growth is influenced by internal and external factors. Internal factors include increase in capital, increased labour force, mergers and acquisitions (Ghozali, Handriana and Hersugondo, 2018). External factors include competitors, prices of raw materials and many other things. An increase in all these things help to improve firm performance.

2.1.6.2 Profitability

According to Hofstrand (2015), profitability is the extent to which a business yield financial gain in its endeavours. The author orates that profitability is the most important performance measure. Profit is the difference between income and expenses. Traditionally, a statement of profit or loss and other comprehensive income is used to measure profitability (Habib et al, 2016). Simply put, it is a financial statement in which income and expenses of a business are recorded. A comparison of statement of profit or loss and other comprehensive income for different years is used to determine a firm's profitability. It is imperative for profits to grow especially for SMEs because it shows the firm's ability to meet its day-to-day activities.

2.1.6.3 Asset growth

As postulated by Sookharee (2014), assets refer to things that a business owns. There are two classes of assets and these are current assets and non-current assets. Current assets are intangible in nature and they include inventory, trade receivables, cash at bank, cash in hand and prepaid expenses. Aziz and Abbas (2019) study show that there is a positive relation between debt finance and assets growth. Non-current assets on the other hand are tangible goods and they include but are not limited to plant and machinery, motor vehicles, land and buildings. Assets are used to generate income for the businesses. SMEs that are still developing in most circumstances do not own many assets and some may use debt financing to purchase these assets. It is a good idea if they invest in non-current assets using long-term debts because when the debt matures, they would have generated a lot of income with those assets. That is one of the reasons why Aziz and Abbas

(2019) orate that there is a positive and significant relationship between debt finance and asset growth.

2.1.6.5 How can SMEs use debt financing to improve their performance?

SMEs can use debt financing to take advantage of tax exemptions. Principal and interest payments are tax deductible. They are subtracted from taxable income before tax is charged. This reduces earnings of the company that are attributable to tax thereby increasing the firm's net profit. An increase in net profit leads to increased profitability of the firm.

Furthermore, SMEs can use debt financing to reduce agency costs. According to Jensen and Meckling (1976), agency costs arise in trying to make managers operate in the best interests of the shareholders. Shareholders main interest is to increase shareholder wealth whilst managers are interested in giving themselves higher rewards. Agency cost arise in trying to align managers interests with shareholder's interests. Excess funds that could be used by managers to reward themselves can then be used to pay financial obligations that arise due to debt financing. This shows that debt financing can be used to reduce costs associated with the agency problem and increase a firm's performance through meeting financial obligations as and when they fall due (Mamaro and Legotlo 2020).

SMEs can also use debt financing to improve their performance by seeking for cheaper sources of debt financing (Koshita) 2018. This includes borrowing from family and friends, crowd funding and getting assistance from the government. These have lower interest charges and can be useful in improving growth and performance of SMEs.

According to Evgeny (2015), SMEs can use debt financing to improve performance by using the borrowed funds for investment in assets and inventories that boost a firm's performance. As mentioned earlier on, assets are used to generate income for the firm. A firm's performance is improved through increased earnings (Hofstrand, 2015).

2.1.8 Small to Medium Enterprises (SMEs)

According to OECD (2017), SMEs definition vary due to different legislation amongst countries significantly because the extent to which firms are identified as small and medium is distinguished by the relative size of the economy. In the United Kingdom, SMES employ less than 250 people whilst in China and United States of America they can employ up to 3,000 workers depending on the sector. The International Accounting Standards Committee Foundation IASCF (2007, p.15) cited in Maseko *et al* (2011) define an SME as a business entity that does not have public accountability and therefore produce general purpose financial statements for external users. In Zimbabwe, the Zimbabwe Revenue Authority (ZIMRA) defines SMEs as businesses that employ between 5-40 people with annual turnover and assets ranging from a minimum of $50,000 to $2 million (Financial Tribune 2018). Furthermore, Small to Medium Enterprises Association of Zimbabwe (SMEAZ) define small (turnover less than $240,000 or assets less than $100,000) and medium (turnover and assets above the thresholds for small enterprises, but less than $1 million each (SMEAZ 2018). As cited in Karedza (2020) The Ministry of Small and Medium Enterprises and Corporative Development (MoSME and CD) policy document in 2009 defined an SME in Zimbabwe as a legal business entity taking into account the following factors;

- asset turnover of less than $USD 800,000.00
- it is not a branch, subsidiary nor an associate of a large organisation
- the maximum number of full-time permanent employees is as follows;

Table 2.1 Definition of SMEs

Sector/sub-sector of the economy	**Size/Class**	**Maximum total number of full-time employees (paid)**
Agriculture, manufacturing and mining	Micro Small Medium	5 50 100
Construction, transport, retail, tourism, catering, arts and crafts, wholesale and fisheries	Micro Small Medium	5 30 50

(Source: MoSME & CD Policy Document 2009)

According to the World Bank, SMEs account for the majority of businesses worldwide and are important contributors to job creation and global economic development. It also emphasizes that finance is a key constraint to SME growth as it is the second most cited obstacle facing SMEs to grow their businesses in emerging markets and developing nations.

In Zimbabwe, SMEs are governed by a constitution Act which is known as Small Enterprises Development Act [Chapter 24:12]. The Act was enacted on the 11^{th} of November in 1984. It was established to provide for the functions thereof; to provide for the constitution and functions of the Small Enterprises Development Board; to regulate the financial affairs of the Small Enterprises Development Corporation and to provide for matters incidental to and connected with the foregoing (Small Enterprises Development Corporation Act [Chapter 24:12]). This establishment has greatly contributed to the growth of SMEs in Zimbabwe. (Nyoni 2019) reported in the national research and development survey on SMEs and cooperatives that SME sector now employs over 60% of Zimbabwe's workforce, contributes to over 50% of GDP and constitutes 70% of business in Zimbabwe.

2.2 Theoretical framework

2.2.1 Pecking Order Theory

Theory also known as the Pecking Order Model and is used to describe firm's capital structure. It was made popular by Myers and Majluf in (1984) but it was developed by Donaldson in (1961). The Pecking Order Theory states that managers of a company follow a certain hierarchy when deciding on sources of finance**.** Ehrhardt and Brigham (2011) stated that firms should structure their capital structure as follows: retained earnings, debt financing and equity financing respectively.

The pecking order model's roots emanate from asymmetric information Myers and Majluf (1984). According to Ehrhardt and Brigham (2011), asymmetric information is when one party in a business set up has more information than the other. Ordinarily company managers have all information concerning the business as opposed to outsiders such as debt holders and potential investors, therefore the latter demand higher returns to compensate for risks associated with the corporation. That is why managers prefer to fund their investments with retained earnings first before they explore other sources of finance which are debt and equity. According to Thakur and Vaidya (2019), companies prefer retained earnings to the other sources of finance because costs of doing so are almost zero as no bankers are involved. However, if the project does not succeed, the company bears all the risk. Retained earnings are not tax deductible, therefore debt would be much better as it provides a tax shield to the company. It is quite hard for SMEs in Zimbabwe to fund their investments with retained earnings because of high rates of inflation they hardly have anything to spare.

After they have exhausted retained earnings or if they are not enough, managers go on to acquire debt from creditors to finance their projects. As postulated by Erhardt and Brigham (2011), issuing debt certificates often indicate that the firm's stocks are undervalued and the board is confident that the investment will be profitable. This shows that debt finance leads to increased financial performance. Managers also prefer debt over equity because cost of debt is lower than equity. However, debt reduces the company's credit rating. If lenders find out that a company has too much debt, they may not be willing to provide them with desired funds because they have high credit risk. In the long run, failure to honour credit obligations leads to bankruptcy.

Issuing shares is the last option because it is proof that the company's stock is overvalued and management is trying to generate financing by diluting shares of the company Erhardt and Brigham (2011). The pecking order theory therefore suggest that issuing shares highlights that management knows that the future of the company is bleak (poor financial performance). Investors then try to overcome this obstacle by bidding for a lower price.

In trying to measure the applicability of the Pecking order theory to SMEs, debt financing is the most feasible as compared to retained earnings and equity. This is due to the fact that most SMEs do not have retained earnings due to terrible economic conditions in Zimbabwe being fuelled by inflation and inconsistent government policies. Also, most SMEs do not meet the listing requirements of the Zimbabwe Stock Exchange (ZSE), therefore, they are unable to raise funding by issuing shares.

A number of authors view Pecking Order Theory as theoretical. Businesses operate in the real world and require practical solutions to solve practical problems. It is recommended that the Pecking Order Model is used with other practical mechanisms to help businesses come up with ideal capital structures.

2.2.2 The Signalling Theory

This theory was brought about by the existence of information asymmetries between the owners of a business and management (Ross 1977). Managers issue debt securities first when they believe that their entity is undervalued and they are certain that their firm is overvalued, they issue debt certificates first. This shows that, managers have insider information and their choice of financing is a signal to market participants.

The above information shows that when managers issue debt securities, it shows that they are confident about their future earnings. Therefore, Baker and Wurgler (2002) agree that this theory can be used to analyse the impact of debt finance on the financial performance of firms. An increase in leverage is a sign that managers are confident that the business will grow and have sufficient cash flows to cater for their interest obligations. This research is anchored on this theory as it will be the able to analyse the impact that debt finance has on performance of SMEs in Bindura.

2.2.3 Agency Theory

The agency theory, also known as the principal-agent model was developed by Jensen and Meckling in (1976). An agency relationship is an agreement between two parties, whereby one party named principal engages the other person called the agent to carry out certain tasks on his or her behalf. The agreement involves allowing the agent to make decisions on behalf of the principal. With regards to this paper, the principal is the shareholder whilst the agent is the manager. The agency theory is used to explain the interdependence between the capital structure of a firm and its performance, Jensen and Meckling (1976).

The theory states that shareholder's interests are different from managers interests. Managers make decisions aligned with satisfying their selfish needs at the expense of the main shareholder interest which is wealth maximisation that ultimately leads to increased financial performance Pradhan and Khadka (2017). Agency costs are therefore incurred by the company due to the actions of the agent and the principal. They arise due to inefficiencies and disruptions caused by conflicts of interest between managers and shareholders (Chen and Kindness 2021).

Agency costs can be reduced by acquiring more debt. This is known to reduce excess cash available to managers for luxurious offices, expensive cars and hefty bonuses. According to Jensen and Meckling (1976), an increase in debt leads to a decrease in agency costs and due to that fact, Evgeny (2015) points out that high levels of debt may improve firm's financial performance. More debt means more fixed interest payments to creditors therefore leaving little for unnecessary spending. Ehrhardt and Brigham (2011) emphasised that increasing debt bonds cash flows as much of it will be used to service debt. However, excessive borrowing strains a business and leads to bankruptcy.

If there is excess cash available, proprietors prefer that it is distributed to them as dividends. However, if there are possible profitable projects or investments, business owners prefer that cash is invested in those to yield future profits. It is therefore important that a company has an efficient and effective board that monitor and assess managements decisions (Carse 2000). Increased monitoring of management by the board leads to increased agency costs. SMEs are least affected by this adversary because most of them are managed by the owners therefore they try to always make sure that the business operates into the foreseeable future (Magot 2018).

2.3 Empirical Literature

This section seeks to present existing articles and researches done by other authors on the impact of debt financing on performance of SMEs. Some do not bear the same topic but are closely linked to the topic understudy.

2.3.1Aziz and Abbas (2019). Effect of Debt Financing on Firms Performance: A Study on Non-Financial Sector of Pakistan

This study was conducted in Pakistan to examine the effect of debt financing on performance of firms in the Non-Financial Sector only. Secondary data was used to collect data from 14 sectors of the country from 2006 up to 2014. Performance was measured using firm size, sales growth, asset growth, ROA, ROE and earnings per share and gross profit margin. Findings of the study show that there is a positive relationship between debt financing and asset growth, sales growth and firm size. The results further indicate that there is a negative relation between debt financing and ROE, ROA and Earnings per share. The major finding of the research postulates that there is a negative and significant relationship between debt financing and firm performance in Pakistan. Aziz and Abbas (2019) recommend that firms should use retained earnings because they are inexpensive and reliable in Pakistan.

2.3.2 Habib, Khan and Wazir (2016). Impact of Debt Finance on Profitability of Firms: Evidence from Non-Financial Sector of Pakistan

Another study was carried out by Habib, Khan and Wazir (2016) in Pakistan to analyse the impact of debt finance on profitability of firms. Long-term debt, short-term debt and total debt represented independent variables which is debt finance. Dependent variable, (profitability) was determined by asset growth, sales growth and firm size. The research focused on data from non-financial firms in Pakistan for a period of 10 years, that is from the year 2003 to 2013. To analyse data, regression analysis was done and the findings were as follows; there is a negative relationship between debt finance and sales growth, a positive relationship between debt finance and asset growth and firm size. Furthermore, the regression model exhibited that debt finance is negatively related to ROA and the relationship is significant. The major finding of this study showed a negative relationship between debt finance and profitability. This meant that an increase in debt finance led to a decrease in profitability of firms in the non-financial sector. Their recommendation was in tandem with the pecking order theory which states that firms should use internal sources of finance to enhance profitability.

2.3.4 Nazir, Azam and Khalid (2021). Debt Finance and Firm Performance: Empirical Evidence from the Pakistan Stock Exchange.

Nazir, Azam and Khalid (2021) did a study titled debt financing and firm performance in Pakistan. The study aimed to determine the relationship between debt finance and firm performance of firms listed on the exchange. Data for a period of 5 years was collected from a sample of 30 listed entities and performance was measured by profitability and asset growth. The findings of the study stipulated that debt finance is negatively related to asset growth and profitability. The trio concluded that there is a negative relationship between debt finance and performance of firms listed on the Pakistan Stock Exchange. These results are contradictory to the agency theory by Jensen and Meckling (1967) which states that debt finance improves firm performance but it agrees with the pecking order theory which states that debt finance has a negative impact of firm's performance.

2.3.5 Badi and Ishengoma (2021), Access to debt finance and performance of Small and Medium Enterpises

The research analyses the effects of access to debt finance on the performance of SMEs in Tanzania. They used data collected from SMEs which were being served by Private Agricultural Sector Support (PASS) to acquire debt from formal financial intermediaries. A total of 152 questionnaires were issued, but data from 115 respondents was actually used to carry out the research. It was revealed that accessing debt finance was one of the biggest challenges for SMEs around the world and that it greatly affects their financial performance. Access to debt finance variables in the thesis were affordability, timeliness and adequacy. Performance was measured in terms of profitability ratios which are GPM, ROA and ROE. It was revealed that indeed there are effects of access to debt finance on the performance of SMEs but they are not so significant (Badi and Ishengoma 2021). The study shows that effects of access to debt finance are high on ROA than they are on GPM and ROE. This is because debt finance increases SMEs profitability relative to the business's total assets. Furthermore, the research emphasised that debt finance helps to boost SMEs performance and SMEs that do not acquire external funding may take a long time to realise their performance potential.

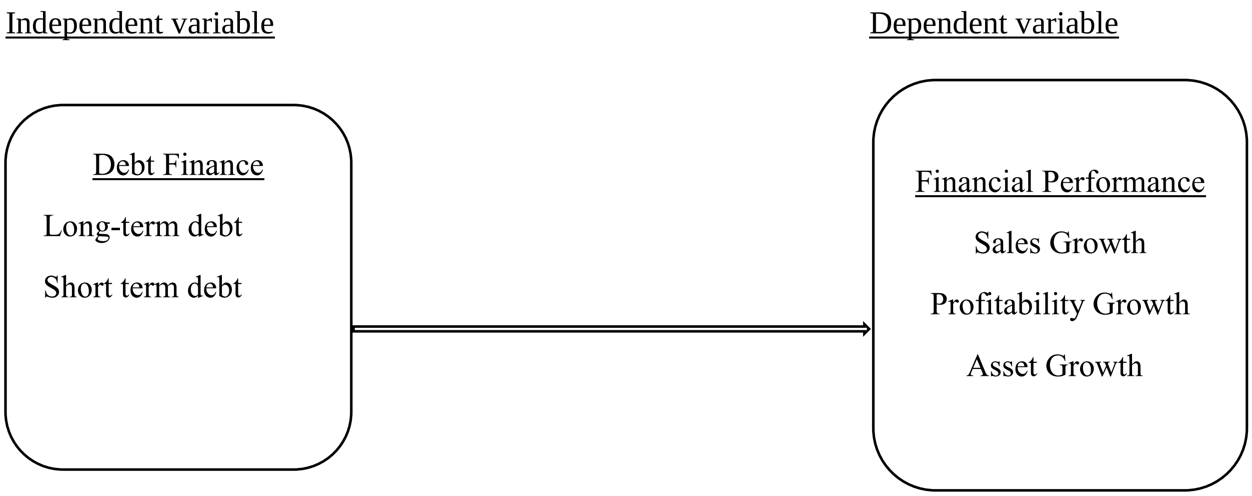
2.3.6 Koshita, (2018). The Impact of Debt Finance on the Financial Performance of a SME: A Case of Workman Pvt Ltd

Koshita (2018), was influenced to carry out the research after noticing recurring decline in profits of Workman Pvt Ltd from 2015 to 2017, high coupon rates and also high gearing ratios. This prompted the researcher to look at the impact that debt finance has on the financial performance of the case study. Primary and secondary data was obtained through interviews, questionnaires and the firm's management accounts. The study shows that debt finance cause significant variances between budgeted and actual cash. All in all, the research shows that debt finance negatively affects firm's financial performance with short term debt having the greatest impact. Investing in employee motivation, diversification, use of advanced technology and improved marketing strategies were suggested as initiatives that boost firm's financial performance. Also, acquiring long-term debts rather than short term debts is helpful as it is less costly.

2.3.7 Pradhan and Khadak (2017). The Effect of Debt Finance on Profotability of Nepalese Commercial Banks.

To assess the effect of debt finance on profitability of commercial banks in Nepalese, the two authors used 148 observations from a total of 22 commercial banks. They collected secondary data from the banks financial statements over a period of seven years. Their model shows a positive relation between short-term debt and profitability and a negative relation between long-term debt and profitability.

Fig 2.1. Conceptual Framework



2.4 Research Gap

According to the authors literature review, other scholars have written a lot about the impact of debt finance on performance of SMEs in their respective countries. Researchers from Zimbabwe have done the same research but on particular companies located in Harare. There is nothing on impact of external funding on performance of SMEs in Bindura. Therefore, my research gap is based on geographical location which is Bindura. The research will look at various businesses such as agriculture, hardware, retail, wholesale, mining, fast food restaurants to make sure that all businesses are represented and analysed to give a critical analysis. In addition to that the study seeks to find out why SMEs are failing to pay back, why they are not growing and if there is any kind of change that follows after SMEs acquire debt finance.

2.5 Chapter Summary

The above chapter sought to give an account of the literature review of debt finance and its impact on SMEs performance. This chapter focused on the conceptual framework which explained core areas related to my research topic. It also explained theories of capital structure under theoretical framework. Last but not least, empirical literature which shows past researches and findings by other authors about the subject matter. The next chapter will focus on research methodology.

CHAPTER III

RESEARCH METHODOLOGY

3.0 Introduction

Research methodology is a chapter that focuses on how the research was developed and conducted. It explains techniques used to identify, select, process and analyse information about a research topic. It aims to explain methods used in data collection, analysis and presentation. This chapter ensures smooth flow of the study and also provides reliability and legitimacy of the findings.

3.1 Research design

A research design is the overall technique that one chooses to build up the various components of a study in a coherent and cohesive manner in order to effectively address the research objectives and answer research questions, (De Vaus 2001). This entails that the research design must address the research problem in the most logical and clear manner. Mugenda and Mugenda (2009) posits that a research design is a plan of action implemented to achieve research objectives and answer research questions. It is of paramount importance that a research design follows through a designated channel of events in a sequential and systematic way. Choudhurg (2012) agrees to this as he orates that a research design is utilised as a guide to effectively conduct a research step by step in a calculative and cautious way within the stipulated time frame and cost. According to Kothari (2004) research design is there to assist in making decisions about what, where, when and how much concerning a project. Objectivity, reliability, validity and generalisability are the expected conditions to be met in order to justify a good research design. For this research, the author intends to use descriptive research design.

3.1.1 Descriptive Research Design

Descriptive research design involves looking at the methods that describe the characteristics of variables understudy (Vetter *et al,* 2021). Descriptive research design entails studying research questions, design of the study and data analysis of the research topic. It is important to note that descriptive research aims to answer questions relating to what rather than why. Idswater (2020) subscribes to the same notion as he states that descriptive research design answer what, where, when and how questions only. The researcher used descriptive research design for this study. The main objective of a descriptive research design is to describe the nature of demographics of the study. Also, a descriptive research design is regarded as an observational research method because its variables are not and cannot be influenced in the duration of the study (Vetter *et al* 2021). This is because the variables cannot be influenced in any way. The researcher had no control over the variables.

3.2 Research approach

As postulated by Babbie (2010), a quantitative research design is one that focuses on collecting numerical data for analysis. It is collected through polls, questionnaires and surveys. Determining the relationship between variables is the main objective of conducting a quantitative analysis. In a bid to assess the impact of debt financing on performance of SMEs in Bindura the author will used the quantitative technique.

3.3 Sources of data

Data is the foundation of the success of any study. Basically, there are two major sources of data and that is primary and secondary data. The researcher will use primary data to gather information pertaining to this research.

3.3.1 Primary data

It is also known as raw data. This is due to the fact that primary data is collected for the first time directly from the main source (Saunders *et al,* 2009). The source would have acquired data from observations, personal experience and physical evidence. Most researchers acquire data through questionnaires, surveys, interviews, observations to mention but a few. To determine the impact of debt financing on performance of SMEs, the researcher used questionnaires to collect data.

Using primary methods of data collection allowed the researcher to ask tailor made questions specifically required to fulfil the purpose of the study. Unlike secondary data, primary data is collected by the researcher herself therefore she gets the opportunity to collect it in an accurate manner. Makoni (2019) states that primary data is regarded as sublime, pure, free from bias and credible. However, the collection process is costly. This is because there are transport and printing costs involved. Generally, collecting primary data is time consuming. It requires dedication and a lot of time which is the most dominant constraint to most researchers.

3.4 Research Instruments

Research instruments are tools used by scholars to collect primary data from participants. The researcher used questionnaires to gather data for this study.

3.4.1 Questionnaires

Questionnaires are primary data collection tools used by researchers to carry out investigations. Kumar (2011) defines a questionnaire as a document consisting a series of structured questions used to find answers from respondents about a particular research topic. According to Annum (2014), a questionnaire is a set of questions designed to collect data. There are various types of questionnaires, but for this study, a self-administered questionnaire will be used. A self-administered questionnaire is one that is completed by the respondent without the researchers help. This helps to reduce bias of the researcher.

The researcher used questionnaires because they are cheaper and easier to administer to participants. As mentioned earlier on, questionnaires are self-administered and that makes them free from bias of the researcher (Kothari 2004). However, some respondents took time to respond, others were unwilling to respond and this delayed progress of the research process. Another disadvantage is failure to get clarity from the researcher due to the fact that it is a self-administered questionnaire. The researcher designed a clear and straight forward questionnaire to curb these challenges.

3.5 Population

It is a selected number of people with common characteristics required by a researcher to conduct his or her work (Kothari 2004). Bhandari (2020) defines population as a group of people that a study seeks to draw conclusions on. A targeted population has to be distinguished because it is tedious to gather data from a vast and wide population. It is not entirely impossible but it is expensive and time consuming. In the 19th century as highlighted by Banerjee and Chaudhury

(2010) researchers used the entire population to come up with their findings but nowadays, they use only a common fraction of the entire population known as the target population. Population may have restrictions in terms of geographic location, specialisation, sex and many others. Due to insufficient information about the total number of SMEs in Zimbabwe, Mutengezanwa (2018) conducted her study with 152 SMEs in Bindura. Due to time and resource constraint, target population for this research is 45 located in Bindura town closer to where she stays. These are the owners of SMEs who finance their operations using debt within the town.

3.6 Sample

In Vushomas (2016) study a sample is defined as selected representatives of the target population. Kenton (2022) defines a sample as smaller manageable elements of the population. A sample must consist of characteristics of the larger group. Their main objective is to try and simplify huge population sizes in the most effective manner. Samples are not selected haphazardly, there are selection methodologies solely for that. Broadly, there are two core sampling methods, probability and non-probability sampling. Selecting a sample helps to reduce costs associated with data collection for instance time.

To find sample size for this study, the author used a formula by Yamane (1967). It is a commonly used formula and therefore considered accurate (Uakarn *et al* 2021). The researcher chose this formula because it is simple, easy to understand and was used by other researchers in carrying out related researches.

$n = N/1+N(e^2)$

Where:

n = Sample size

N = Population Size

e = acceptance level of error (reliability level is 95% therefore level of precision is always 0.05)

Source: Uakarn *et al* (2021)

$n = 45/1+45(0.05^2)$

n = $\underline{\underline{40}}$

The above sample size is 88.9% of the target population

3.7 Sampling procedure

Sampling as explained earlier on is the process of selecting some elements of the population in order to draw conclusions about the population. It is quite a crucial initiative because selected elements address the objectives of the study. Therefore, it requires accurate selection, measurement and analysis in order to produce the best possible results. Kothari (2004) shared the same sentiments as he orates that a sample must be a true representative of the population without bias so as to obtain conclusions that are valid and reliable. There are two major sampling techniques, probability and non-probability sampling. McCombes (2019) cites that probability sampling involves random selection of elements and it enables acquisition of powerful statistical inference of the population. Kothari (2004) goes on to define non-probability sampling as a sampling mechanism that does not give a fair chance to all elements in the population to be selected.

For this research, the researcher used stratified random sampling. The population is divided into homogeneous subgroups called strata where members of each group share the same attributes and or characteristics (Hayes 2022). Thereafter, random samples are then collected from each stratum to complete the survey. Stratified sampling is ideal for this study because SMEs in Bindura are into various trades including retail, wholesale, manufacturing, hardware, pharmacies and many others. It was necessary that each of these trades were represented in the population. Stratified random sampling is also considered more accurate as compared to simple random sampling as it takes into consideration the need for classification of population elements.

This technique is superior to simple random sampling because the entire population has a representative. Kothari (2004) emphasizes better metric precision in stratified sampling as there is commendable representation of overall population. Dividing the entire population into strata brings about administration convenience thereby saving costs and time

3.8 Validity and reliability

Kubai (2019) explains the need for believability and trust in the researchers work and findings. That brings about the importance of validity and reliability. He goes on to define reliability as stability of measurement over a variety of conditions. This means that under different conditions, an instrument is expected to produce the same results. As cited by Kothari (2004), reliability is affected by two factors namely random error and systematic error. Random error is caused by external factors that affect some elements of the sample and not others. Systematic error is caused by factors that systematically affects all elements of the sample. Reliability shows that the scale is dependable.

Drost (2011) cite that validity is the ability of a scale to effectively measure that which it is purported to measure. The main aim of validity is to justify research findings. According to Kubai (2019), it can be measured using theoretical and empirical evidence. The researcher conducted a pilot test to ensure validity of the research instrument. Schade (2015) describes a pilot test as a small-scale test used to assess the feasibility of the proposed larger study. 15 questionnaires were distributed to a few business owners before the actual one was drafted and distributed to the target population. Those participants in the pilot test were not included in the actual study.

3.9 Data collection procedure

As highlighted above, data was collected through questionnaires. As stipulated by Kumar (2011), a questionnaire is a data collection tool that contains structured questions for respondents to provide their knowledge and opinions about a certain research topic. According to Bhandari (2022), questionnaires can be classified as self-administered and researcher-administered.

This research was conducted using self-administered questionnaires. They were distributed online via email and WhatsApp and as hard copies. The researcher used self-administered questionnaires because they are less expensive and easy to make and administer. During my Part 2.2, the university offered us a course titled Research where we were taught how to prepare a questionnaire. Reference was made from there and from online tutorials on how to prepare the questionnaire. Self-administered questionnaires are standardised, that means that all respondents get a copy with the same questions. This made using self-administered questionnaires easier and time saving. Most SMEs do not prepare financial statements or want to talk about their debts because they consider it private. That is why the researcher used questionnaires to ask questions relating to SMEs performance. The other reason why the researcher used questionnaires is that they preserve confidentiality and anonymity.

3.10 Ethical considerations

(Bhandari 2021) describes ethical considerations as principles that must be adhered to in an author's research design and practices. Others describe it as a code of conduct followed during data collection. Researchers are not allowed to overlook people's feelings and that which is considered right and wrong. These principles are put in place to protect research participants rights, maintain research integrity and improve research validity.

For the purposes of this research, the researcher submitted her proposal to the supervisor for approval to ensure that the research aims and research design are ethical. Participants took part on voluntary basis. Those who are unwilling were not be coerced to do so. Participants were rest assured that information collected from them is for academic purposes only and that is to fulfil the partial requirements for the Bachelor of Commerce Honours Degree in Banking and Finance. This research was guided by previous researches done by other authors. Therefore, the author made it a point to reference information gathered from other authors to avoid plagiarism. Names of respondents were not required on questionnaires to enhance confidentiality and anonymity.

3.11 Data presentation and analysis procedure/techniques

Depending on data collected figures, tables, graphs, pies charts were used to present quantitative data. These tools are better communication tools as they make collected data more understandable. They are also attractive to readers and simplify complex data. A software called SPSS 21 was also used for data analysis.

3.12 Chapter summary

This chapter is one of the most important chapters in all research projects. This is because it depicts processes that the research goes through to meet the objectives of the study and answer research questions. The process includes the research design, research approach, population, sample, research instruments, sampling procedure, validity and reliability, ethical consideration, data presentation and analysis technique.

CHAPTER IV

DATA PRESENTATION ANALYSIS AND DISCUSSION

4.0 Introduction

This chapter focused on the impact of debt financing on performance of SMEs in Bindura. Data obtained is presented in the form of graphs, tables and pie charts. SPSS version 21 was used for data analysis, the relationship between the dependent and independent variables was computed using regression statistics. The findings of this study were compared and contrasted to those of previous research of the similar topic

4.1 Questionnaire response rate

The table below explains the response rate of the questionnaire.

Table 4.1 Questionnaire response rate

Respondents					
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Not returned	5	12.5	12.5	12.5
	Returned Questionnaire	35	87.5	87.5	100
	Total	40	100	100	

Source – Primary data

Table above shows the response rate obtained during the survey. From a sample size of 40 participants 87.5% responded while 12.5% did not respond. A high response rate was obtained because the author put on tight follow-ups, and redistributed questionnaires to those who failed to respond to the first session. Jackson (2013) emphasized that, high response rate highlights that research findings are free from bias and at the same time ensures validity and reliability.

4.2 Demographic Findings

Demographic findings present the summary of descriptive statistics of active participants. The characteristics considered were gender, age, highest level of education, marital status and position held in the organization. Statistics below reviews this demographic setting as analysed through the use of SPSS version 21.

4.2.1 Percentage distribution by gender

As mentioned earlier on, 35 participants responded to the issued questionnaire. The table below seeks to explain gender composition of the sample.

Table 4.2 Respondents gender

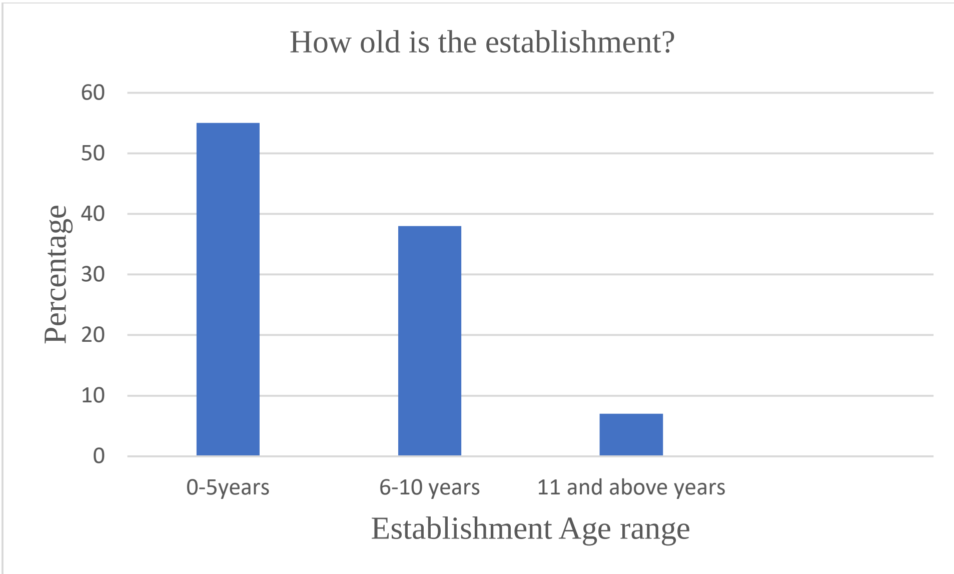
Gender					
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Male	11	31	31	31
	Female	24	69	69	100
	Total	35	100	100	

Source – Primary data

The above table shows that the sample composition comprised of both males and females. Females had the highest response rate of 69% as compared to their male counterparts with 31%. This means that most SMEs used in the study are owned by women.

4.2.2 Percentage distribution by establishment age range

Fig 4.1: How old is your establishment?



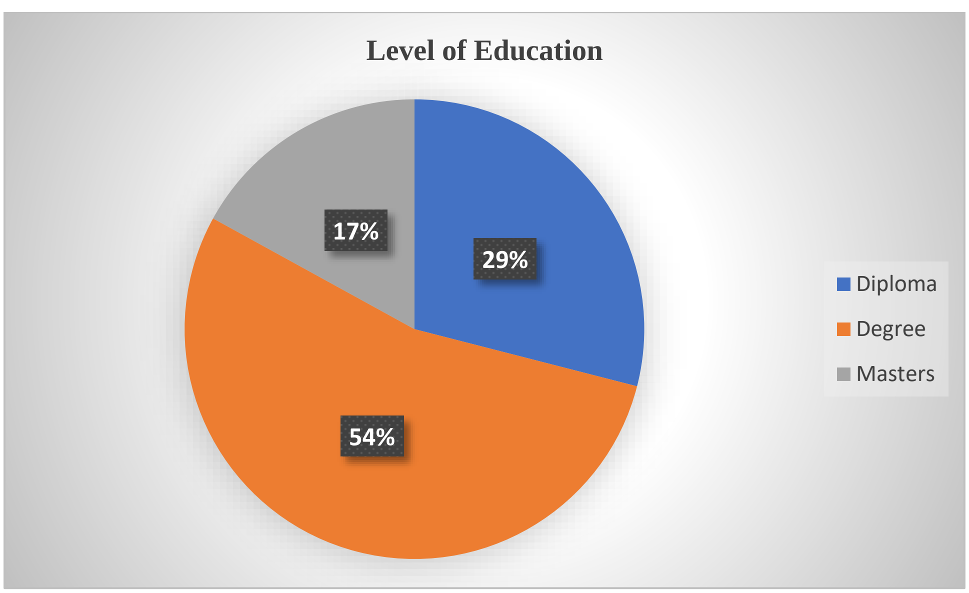
Source – Primary data

Fig 4.1 shows how old the SMEs are. The results are as follows 55% of SMEs have been operating for a period of 0-5 years, 38% for 6-10 years and 7% for 11 years and above. This information shows that the highest number of SMEs are in their early ages of operations.

4.2.3 Percentage distribution by level of education of the owner.

SME owners were asked to indicate their level of education and the results are as follows;

Fig 4.2: Level of education



Source – Primary data

A majority of SME owners have college degrees as highlighted by 54%, followed by those with diplomas 29% and finally those with masters 17%. These results show that all SMEs in the study are owned by people with academic qualifications. This means that they are quite knowledgeable and can provide important input on the impact of debt finance on performance of the SMEs in Bindura.

4.2.4 Percentage distribution by registration status

Table 4.3: SMEs registration status

Registration Status					
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Registered	24	69	69	69
	Unregistered	11	31	31	100
	Total	35	100	100	

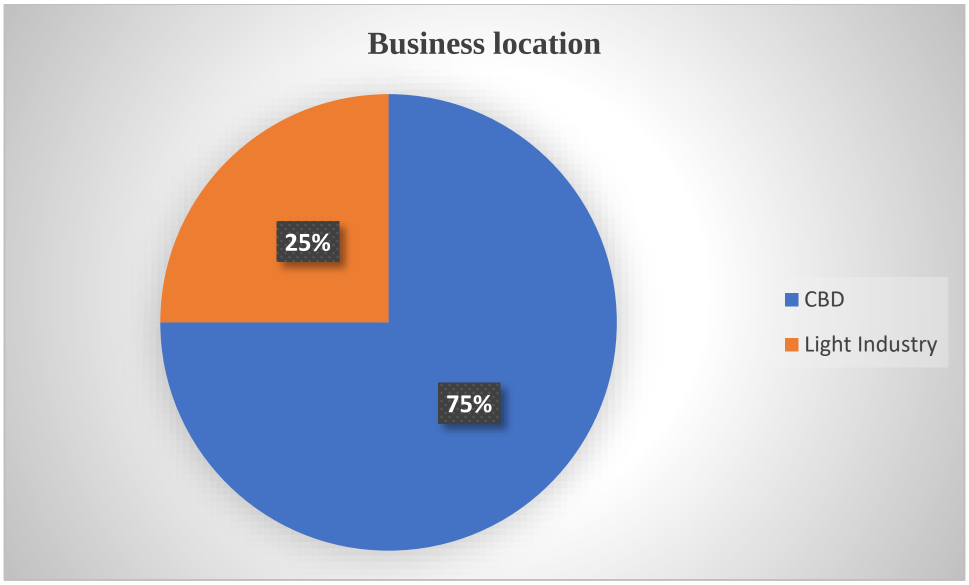
Source – Primary data

The 4.3 shows that 69% of SMEs in the study are registered whilst 31% are unregistered. This means that SMEs that are registered provided the most input to this research as they qualify for debt financing from recognized financial institutions.

4.2.5 Percentage distribution by business location

The figure below describes where SMEs within the target population are located.

Fig 4.3 Business location



Source – Primary data

Fig 4.3 shows the following percentage distribution by business location. It shows that a majority of SMEs used in the study are located in the Central Business District (CBD) 75% and 25% in the light industry area. This means that SMEs used to conduct this study were strategically located in Bindura town.

4.3 The impact of debt finance on sales growth of SMEs in Bindura

Table 4.4 Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
Debt financing increased inventory levels over the past years	35	1	5	2.40	1.193
Using debt financing has resulted in sales growth	35	1	5	2.46	1.291
Debt financing resulted in the achievement of economies of scale	35	1	5	2.20	.964
Valid N (listwise)	35				

Table 4.4 sought to determine the impact of debt finance on sales growth and the findings are as follows; respondents disagreed that debt financing increased inventory levels shown and this is shown by a mean of 2.40 and a standard deviation of 1.193. a mean of 2.46 and a standard deviation of 1.291 shows that owners of SMEs disagreed that debt financing resulted in sales growth. Findings also indicate that participants disagreed that debt financing resulted in the achievement of economies of scale.

These findings stipulate that debt financing has a negative impact on sales growth. The researcher's findings contradict with Aziz and Abbas (2019); Habib, *et al* (2016) who found a positive impact between debt financing and sales growth in Pakistan.

4.4 The impact of debt finance on profitability of SMEs in Bindura

Table 4.5 Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
Debt financing has increased profitability of our firm	35	1	5	2.43	1.378
Debt financing resulted in economies of scale which reduced our cost of production and increased profits	35	1	5	2.37	1.352
Debt financing increased sales volumes hence profit level also increased	35	1	5	2.20	1.052
Valid N (listwise)	35				

Source-SPSS analysis of primary data

This section sought to determine the impact of debt financing on profitability of SMEs in Bindura. Three statements were designed to get the respondents perspective on the afore mentioned issue. Data presented on table 4.5 showed that majority of respondents disagreed that debt finance has increased profitability of their firms. This is shown by a mean of 2.43 and a standard deviation of 1.378. This means that debt financing has decreased SMEs profitability in Bindura. Results further indicate that a number of respondents disagreed that debt financing has increased economies of scale which reduced cost of production and increased profits by a mean of 2.37 and a standard deviation of 1.352. Findings of the study also show a mean of 2.20 and a standard deviation of 1.052. This means that most respondents disagreed that debt financing increased sales volumes and increased profits of SMEs. Sales volume have not increased therefore profits did not increase as well.

Findings above indicate that debt financing has a negative impact on profitability of SMEs in Bindura. An increase in debt financing will not result in an increase in profitability of SMEs. These findings are in tandem with those of Habib, *et al* (2016), Nazir, *et al* (2021); Koshita, (2018) who discovered that debt financing has a negative impact on profitability of firms in their respective countries. However, Pradhan and Khadak (2017), Badi and Ishengoma (2021) found a positive relationship between debt financing and profitability of Nepalese commercial banks and their results are contrary to those of this research.

4.5 The impact of debt finance on asset growth of SMEs in Bindura

Table 4.6 Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
Debt financing has increased our current assets	35	2	5	4.09	.702
Debt financing has increased our non-current assets	35	1	5	4.34	1.136
Debt financing has increased the firms net worth	35	1	5	4.34	.906
Valid N (listwise)	35				

Source-SPSS analysis of primary data

To analyse the impact of debt financing on asset growth, the author formulated statements to measure the level of agreement of respondents to those statements. Mean 4.09 and a standard deviation of 0.702, respondents agreed that debt financing has increased current assets in their respective SMEs. To further analyse the impact of debt financing on assets growth, respondents agreed that debt financing has increased non-current assets of SMEs in Bindura District with the following results; mean equal to 4.34 and standard deviation equal to 1.136. This means that an increase in debt financing leads to a proportional increase in non-current assets of SMEs. In addition. In addition to that, owners of SMEs under study also agreed that debt financing has increased their firms net worth. This is indicated by an average mean of 4.34 and a standard deviation of 0.906. Net worth is the total worth of a company. The above information shows that debt financing has caused an increase in assets of SMEs thereby increasing their net worth.

The above results show that debt financing has a positive impact on assets growth. An increase in debt financing leads to an increase in total assets of SMEs in Bindura. These results are in harmony with Aziz and Abbas (2019); Habib, *et al* (2016) who also discovered that there is positive relationship between debt financing and assets growth in firms in the non-financial sector in Pakistan. However, these results contradict with the results of Nazir, *et al* (2021) who found that debt finance has a negative impact on firms listed on the Pakistan Stock Exchange.

4.6 Regression model summary

Table 4.7 Model summary

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.441[a]	.195	.170	8.57593

a. Predictors: (Constant), Debt finance
b. Dependent Variable: performance

Table 4.7 is a regression model summary that seeks to examine goodness of fit of the model. It does so by determining the co efficient of determination (R^2) which is 19.50%. It shows that debt financing only explains 19.50% of variations in SMEs performance. It means that debt financing has a negative impact on firm performance. These findings augment those of Koshita (2018) which depicted that debt financing has a negative impact on performance of a Zimbabwean SME. This information further highlights that 80.50% of SMEs performance is explained by other factors not included in the study.

R of 44.10% indicates that that there is a negative correlation between debt finance and performance of SMEs in Bindura. This result is in harmony with Aziz and Abbas (2019) who produced a negative correlation between debt finance and performance of firms in Pakistan.

4.7 ANOVA

ANOVA is an acronym which stands for Analysis of Variance. ANOVA is a statistical tool used to conduct significance test. It aims to determine the level of variance amongst study variables.

Table 4.8 ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	569.010	1	569.010	7.737	.009[b]
	Residual	2353.490	32	73.547		
	Total	2922.500	33			

a. Dependent Variable: performance

b. Predictors: (Constant), Debt finance

The table depicts a significance p value of 0.009, the alpha being 0.05. This shows that there is a significant relationship between the dependent and independent variables because the p value is less than the alpha (0.05). There is a significant relationship between variables when (p value < 0.05). The study p value of 0.009 shows that there is significant relationship between debt financing and performance of SMEs.

Table 4.9 Regression Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	44.519	6.293		7.074	.000
	Debt finance	-9.644	3.467	-.441	-2.781	.009

a. Dependent Variable: performance

The above coefficients table indicates the following:

Performance= 44.519-9.644X1

The study shows that performance of SMEs in Bindura has a constant value of 44.519 ceteris paribus. SMEs performance for this study was measured by three variables namely sales growth, profitability and assets growth. These variables were transformed to make one dependent variable which is performance to make calculations using SPSS21 easier. The study findings reveal that B value of -9.644 supported by a significance value of 0.009 indicates that there is a negative and significant relationship between debt finance and performance of SMEs in Bindura. This means that an increase in debt financing leads to a decrease in SMEs performance. It augments the findings of Nazir *et al* (2021) which revealed that debt finance negatively affects performance of firms listed on the stock exchange.

4.8 Debt financing and performance of SMEs

Respondents were asked about their views on debt financing and performance of SMEs. The following were their responses;

Response A (26%)

"Debt financing does not improve performance of SMEs"

Response B (22%)

"Debt financing is causing more harm than good"

Responses from respondents indicate that debt financing does not lead to improved performance and growth. This shows that debt financing is not helping SMEs to grow as indicated by quantitative data presented above. These results are in agreement with previous studies done by Aziz and Abbas (2019), Habib *et al*, (2016) who found out that debt financing does not enhance performance. However, the results contradict with previous researches conducted by Badi and Ishengoma (2021) and Koshita (2016) who recommend SMEs to use debt financing in order to improve their performance and growth.

Other respondents discredited debt financing because it is expensive and this is what they had to say about debt financing and performance of SMEs;

Response C (20%)

"Financing using debt is expensive and an inappropriate source of funding for SMEs"

Response D (20%)

“Debt financing is expensive for SMEs as we are considered as high risk clients. This is why debt financing is compromising performance of SMEs”

The above information further augments quantitative data presented earlier on in the chapter which showed that debt financing has a negative impact on profitability of SMEs. These findings are in harmony with a study by Nazir *et al* (2021) which proved that debt financing is expensive and leads an increase in total expenses that lower profitability. The results contradict with the agency theory which states that debt financing reduces firm’s expenses and increase performance.

A few respondents had this to say about debt financing and performance of SMEs;

Response E (6%)

“Debt financing has been helping us increase our asset base”

Response F (6%)

Debt financing is helping us nurture our business credit and this has improved our company’s performance.

These results indicate that minority of the respondents agree that debt financing has improved their performance through asset growth and nurturing their credit worthiness. This means that an increase in debt finance has led to an increase in asset growth. The results are in tandem with the signaling theory which states that debt financing has a positive impact on growth of firms.

Results indicate that 88% of respondents are of the view that debt financing does not improve performance whereas 12% agree that debt financing leads to business growth. This shows that debt finance is negatively affecting performance of a large number of SMEs in Bindura.

4.9 Chapter summary

This chapter focused on data presentation, analysis and discussions. Tables generated from SPSS reviewed the results obtained during the study. Regression analysis and descriptive statistics were employed to analyse the behavior of independent and dependent variables. Chapter five will cover up the research recommendations and conclusions.

CHAPTER V

SUMMARY, CONCLUSION, FINDINGS AND RECOMMENDATIONS

5.0 Introduction

This chapter aims to give a summary, conclusion and recommendations on the impact of debt financing on performance of SMEs in Bindura District.

5.1 Summary

The main aim of this study was to determine the impact of debt financing on performance of SMEs located in Bindura. Chapter one showed that most SMEs now had access to debt finance but most were failing to pay back, some are highly leveraged and are not growing to become large firms. This prompted the researcher to carry out research and examine the impact that debt financing has on performance of SMEs in Bindura. The objectives of the study were to determine the impact that debt financing has on sales growth, profitability, assets growth and how SMEs can use debt financing to improve performance of SMEs.

The second chapter of the study mainly focused on the conceptual framework, theoretical framework and empirical literature. Conceptual framework looked at core concepts to be covered in the research and definition of key terms. Theoretical framework focused on presentation of theories that are related to the subject matter and these were theories of capital structure namely the pecking order theory, signaling theory and agency theory. The research was anchored on the signaling theory which explains that managers issue debt instruments when they are certain of their future earnings. Empirical literature explored previous studies conducted by other researchers in the world which are related to this study. They were used as a guide and to help with discussion of findings in chapter four.

Chapter three of the study presented the research methodology. It explained how the research was going to be carried out and issues covered include research design, research approach, sources of data, population, sample, sampling procedure, validity and reliability, data collection procedure, ethical considerations and a brief description of data presentation and analysis. A descriptive research design was used to collect primary data using questionnaires. The research targeted respondents from 45 SMEs in Bindura. A sample size of 40 was calculated using a formula by Yamane (1967). Stratified sampling was used to make sure that SMEs in various types of businesses were represented and they included those from retail, wholesale, manufacturing, hardware, pharmacies and many others. To ensure validity and reliability of the research instrument a pilot test was conducted. The researcher also highlighted how she made sure that the research was conducted in an ethical manner.

Collected data was presented and analysed in chapter four. Tables, pie charts and graphs were used to present collected data and SPSS 21 was used to analyse data. The research findings were as follows; there is a negative relationship between debt financing and sales growth and also between debt financing and profitability. This means that an increase in debt financing resulted in decrease of sales and profitability of SMEs in Bindura. Results also showed a positive relationship between debt financing and assets growth. This means that respondents agreed that an increase in debt financing leads to an increase in assets. The regression model indicated that there is a negative and significant relationship between debt financing and performance. This was highlighted by co efficient of determination R^2 of 19.50% and a significance of 0.009. R^2 o 19.50% shows that debt financing only explained 19.50% of variations in performance of SMEs and 80.50% variations were explained by other factors outside of the model. P value of 0.009 shows a significant relationship because it is less than 0.05 which is the alpha. This shows that there is a negative and significant relationship between debt financing and performance of SMEs in Bindura.

Results further indicated that 86% of respondents said that debt financing negatively affects performance because it is causing more harm than good and it is expensive.

5.2 Conclusion

Based on the research findings, the researcher concludes that debt financing has a negative impact on sales growth and profitability. This means that an increase in debt financing leads to a decrease in sales and profitability of SMEs in Bindura District. Results further showed that debt financing has a positive relationship with assets growth. This means that an increase in debt financing leads to an increase in assets. The major finding computed by regression analysis shows that there is a negative and significant relationship between debt financing and performance of SMEs. This means that an increase in debt financing leads to a significant decrease in performance of SMEs. These results are in harmony with the pecking order theory which discourages firms from using debt financing but rather use retained earnings because they influence growth.

5.3 Recommendations

These are some of the ways the researcher recommends on how SMEs can use debt financing to improve their performance. SMEs can use debt financing to take advantage of tax exemptions. Tax exemptions on principal amount and interest lowers taxable income and this cause an increase in net profit.

After carrying out the study, the author realised that most SMEs use less of debt financing to fund their businesses. The author recommends that SMEs should seek for cheaper sources of debt financing for example loans from family and friends, crowd funding and government grants. These have cheaper to zero cost and can improve performance of SMEs.

SMEs should use debt financing to finance projects with positive Net Present Values as this improves performance. This means that they should carry out capital budgeting to determine projects that yield high returns and invest in those to get high profits that boost their growth.

The author further recommends regulatory authorities to revise their interest rates downwards to allow SMEs to acquire cheaper debt financing and improve their growth. Currently corporate lending rate is pegged at 158.46% (RBZ, 2022). This shows that cost of borrowing is too high. SMEs shun borrowing even though they might have great ideas that can further create employment and increase the nations GDP. It can be seen that those that are borrowing are failing to pay back and this is not good for the economy as a whole. SMEs are the greatest employment creators in the world and assisting them to grow means creating employment for a lot of Zimbabweans.

5.4 Suggestions for further study

This study only looked at debt finance as a source of capital and the impact that it has on performance of SMEs. Other scholars can look at the impact of retained earnings and equity to analyse the contribution that each source has on SME performance. This can help SMEs to choose financing options that improve their performance.

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BINDURA UNIVERSITY OF SCIENCE EDUCATION

FACULTY OF COMMERCE

DEPARTMENT OF BANKING AND FINANCE

Dear Respondent

My name is Lorraine Tatenda Kamvura (B1953565), a fourth-year student at Bindura University of Science Education. I am working towards attaining a Bachelor of Commerce (Honors) Degree in Banking and Finance. Currently I am working on research titled **The impact of debt financing on performance of SMEs. A case of Bindura District**. The project is a requirement in the partial fulfilment of the above-mentioned undergraduate degree program.

I am kindly asking for your assistance in answering the questionnaire below to the best of your ability and knowledge. Kindly note that information provided will be used solely for academic purposes and your identity will be kept confidential. I request you to respond to all questions on the questionnaire and would really appreciate it if you return the answered questionnaire at your earliest convenience. Your cooperation will be greatly appreciated.

Yours sincerely,

Lorraine Tatenda Kamvura.

APPENDIX 1: QUESTIONNAIRE

Please do not write your name on anywhere on the questionnaire

Answer questions either with a yes, no, or a tick in the box

SECTION A: Demographics

1. **Please indicate your gender**

MALE ☐ FEMALE ☐

2. **How old is your establishment?**

0-5 years ☐ 6-10 years ☐ 11 and above ☐

3. **What is the owner of the SME level of education?**

Diploma ☐ Degree ☐ Masters ☐

4. **SMEs registration status**

Registered ☐ Not registered ☐

5. **Where is your business located?**

CBD ☐ Light Industry ☐

Question 1: To analyse the impact of debt finance on sales growth of SMEs in Bindura

Statement	SD %	D %	N %	A %	SA %

Debt financing has increased inventory levels over the years					
Using debt financing has resulted in sales growth					
Debt financing resulted in the achievement of economies of scale					

Question 2: To analyse the impact of debt finance on profitability of SMEs in Bindura

Statement	SD %	D %	N %	A %	SA %
Debt financing has increased profitability of our firm					
Debt financing resulted in economies of scale which reduced our cost of production and increased profits					
Debt financing increased sales volumes hence profit levels also increased					

Question 3: To analyse the impact of debt finance on asset growth of SMEs in Bindura

Statement	SD %	D %	N %	A %	SA %
Debt financing has increased our current assets					
Debt financing has increased our non-current assets					
Debt financing has increased our firm's net worth					

Question 4: What is your view on debt financing and performance of SMEs?

<u>Instruction</u>

Kindly give your answer in brief and explain

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THANK YOU FOR YOUR COOPERATION