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Original Article

## Effects of Microcredit on Micro, Small and Medium Enterprises Performance in Tanzania with Reference to Selected MSMEs in Iringa Municipality

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**Keywords:**

Microcredit,  
Loan Amount,  
Interest Rate,  
Initial Capital  
and MSME  
Performance.

The purpose of the study was to assess the effects of microcredit on Micro, Small and Medium Enterprises (MSMEs) performance in Tanzania, with reference to selected MSMEs in Iringa Municipality specifically, to examine the contribution of the loan amount on the performance of MSMEs, to examine the influence of interest rate on the performance of MSMEs and to determine the effect of initial capital on the performance of MSMEs. The targeted population was 874 MSMEs benefiting from microcredit services from Iringa Municipality, where a sample size of 274 MSMEs was drawn. A descriptive research design was employed, and a quantitative approach was applied to analyse data. Stratified sampling technique, simple random technique and Convenience sampling technique were used to select loan benefiting. The findings revealed that loans benefiting MSMEs at Iringa Municipality receive loans from financing institutions and use them to improve performance. Moreover, the study found that interest rate has no statistically significant on the performance of MSMEs in Iringa Municipality. In addition, findings revealed that there was statistical significance in the effects of initial capital on the performance of MSMEs. In the case of the normal regression output, the adjusted R<sup>2</sup> equals 0.698, implying that the model explains about 69.8% variations in MSMEs performance. The study recommends that the Government should ensure that MSMEs receive appropriate loan amounts and should take proactive measures to regulate interest rates on microcredit loans. MSMEs should have a clear strategy for how these funds will be used. Financing institutions should recognise that loan provisions to MSMEs should be based on the specific needs of the business. Also, they should provide micro-loans at competitive rates that balance affordability for MSMEs and sustainability for the institution. For further studies, the researchers should conduct similar research in different regions or countries that will allow scholars to ascertain the general ability of the findings. Also, the researchers should conduct longitudinal studies that can provide invaluable insights into the long-term effects of microcredit on MSMEs' performance.

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## INTRODUCTION

Globally, Micro, Small and Medium Enterprises (MSMEs) are recognised as important contributors to economic development and poverty reduction. MSMEs create jobs, generate income, and promote innovation and entrepreneurship (Akpan, 2018). The microcredit industry has gained significant attention in recent years due to its potential to support micro, small, and medium-sized enterprises (MSMEs). In the United States, MSMEs account for over 99% of all businesses and employ nearly half of the country's workforce (United Nations Industrial Development Organization, 2017). However, MSMEs often face challenges in accessing traditional sources of financing, such as banks, due to their size, lack of collateral, or credit history (Agyapong & Osei, 2020).

By providing access to credit, microcredit can help MSMEs finance their operations, expand their businesses, and create jobs (Gugerty & Karlan, 2018). However, the effectiveness of microcredit in improving MSMEs performance, growth and development in the United States is still debated. Some studies have found that microcredit has a positive impact on MSMEs' performance. For example, a study by Karlan and Zinman (2019) found that microcredit helped MSMEs in the United States increase their profits and create jobs. Similarly, a study by Armendáriz and Morduch (2016) found that microcredit had a positive impact

on the performance of MSMEs in the United States, particularly for women and minority-owned businesses. However, other studies have questioned the effectiveness of microcredit in improving MSME performance. For example, a study by Mehta and Udell (2015) found that microcredit had little impact on the performance of MSMEs in the United States. Similarly, a study by Berger and Udell (2014) found that MSMEs that received microcredit in the United States did not experience any significant improvements in their financial performance.

In the European context, the microcredit industry has gained significant attention in Europe as a potential solution to support MSMEs (European Commission, 2021). Some studies have found that microcredit has a positive impact on MSME performance in Europe. For example, a study by Crespi et al. (2016) found that microcredit had a positive impact on the growth and survival of MSMEs in Italy. Similarly, a study by Muñoz-Bullón and Sánchez-Bueno (2017) found that microcredit had a positive impact on the performance of MSMEs in Spain. However, other studies have questioned the effectiveness of microcredit in improving MSME performance in Europe. For example, a study by Casu and Girardone (2013) found that MSMEs that received microcredit in Italy did not experience any significant improvements in their financial performance.

In Africa, MSMEs account for over 90% of businesses and employ over 60% of the labour force, making them crucial drivers of economic growth and development. However, MSMEs in Africa face numerous challenges, including limited access to credit, markets, technology, and business development services. Microcredit has emerged as a popular tool for supporting MSMEs in Africa, with many microfinance institutions (MFIs) providing credit to small entrepreneurs (African Development Bank Group, 2019).

In the East African context, microcredit has been widely used as a means of providing financial support to MSMEs. In Tanzania, MSMEs account for over 90% of businesses and employ over 70% of the labour force, making them important contributors to economic growth and poverty reduction. However, access to credit remains a significant challenge for MSMEs in Tanzania, particularly in rural areas such as Iringa Municipality. For example, a study by Ngowi and Mwakalila (2018) found that MSMEs in Tanzania faced challenges in accessing credit due to limited collateral, high interest rates, and unfavourable loan conditions. Microcredit has been identified as a significant source of financing for MSMEs in Tanzania, with the potential to enhance their performance and growth. According to a study by Kanywanyi and Mboya (2020), microcredit has a positive effect on MSMEs' performance in Tanzania. The study found that MSMEs that accessed microcredit had higher sales, profits, and employment levels than those that did not access microcredit. Another study by Ng'eno et al. (2019) found that microcredit had a significant positive effect on MSMEs' performance in Tanzania. The study found that MSMEs that accessed microcredit had higher sales, profits, and assets than those that did not access microcredit. The study also found that microcredit had a positive impact on MSMEs' access to markets and networking opportunities, which enhanced their competitiveness.

MSMEs in Tanzania face various problems that hinder their growth and development. One of the major challenges faced by MSMEs in Tanzania is the lack of access to finance. According to the World Bank, only 4% of MSMEs in Tanzania have access to formal financial services (World Bank, 2020). This lack of access to finance limits the ability of MSMEs to invest in their businesses, leading to limited growth and development. Another challenge faced by MSMEs in Tanzania is limited access to technology and skills; lack of access to technology and skills limits the ability of MSMEs to innovate and produce quality products, limiting their competitiveness in the market (International Finance Corporation, 2019; World Bank, 2020). Likewise, an unfavourable business environment is another challenge to MSMEs (National Trade Policy, 2015). According to the National Micro Finance Policy, 2015, MFI and SMEs shall be protected and focused on objectives, targeted groups, and areas in which the policy shall be implemented in order to give room for access to finance investment environmental as well as capacity of MSMEs. Considering the above problem MSMEs face, it is important to assess the aspects of microcredit finance and its impact on the MSMEs' performance in Tanzania.

### **General Objective**

The general objective of this study was to assess the effects of microcredit on the performance of MSMEs in Tanzania, a case of selected MSMEs in Iringa Municipality.

### **Specific Objectives**

The following were the specific research objectives that guided this study

- To examine the contribution of loan amounts on the performance of MSMEs in Iringa Municipality.
- To examine the influence of interest rates on the performance of MSMEs in Iringa Municipality.

- To find out the effect of initial capital on the performance of MSMEs in Iringa Municipality.

## LITERATURE REVIEW

### Theoretical Reviews

This section presents a theoretical framework adopted in this study. The theoretical framework presents three theories: financial intermediation theory, resource-based theory, and pecking order theory:

#### *Financial Intermediation Theory*

Financial Intermediation Theory is a field of economics that has been developed by several scholars over time such as John Hicks (1969), who introduced the concept of financial intermediaries and their role in channelling savings into investments. Franco Modigliani and Merton Miller (1958) developed the theory of the “irrelevance of capital structure,” which suggests that the financing decisions of a firm (i.e., debt vs. equity) have no effect on its overall value. Financial Intermediation Theory suggests that financial intermediaries, such as microfinance institutions, play a critical role in allocating capital to firms that would otherwise face constraints in accessing finance (Fama, 1970). The theory proposes that financial intermediaries mobilise funds from savers and channel them to borrowers, providing credit to firms and individuals that would otherwise be excluded from the formal financial system (Fama, 1970). In the context of microfinance in Tanzania, Financial Intermediation Theory explains how microfinance institutions contribute to providing access to finance for micro, small, and medium enterprises (MSMEs). These institutions mobilise funds from savers and channel them to borrowers, thereby facilitating the inclusion of individuals and firms in the formal financial system. The theory acknowledges that financial intermediation helps alleviate credit constraints faced by small entities, enabling them to invest and grow. It also provides a framework to assess the

impact of microcredit on the performance of MSMEs in Tanzania.

### Pecking Order Theory

The Pecking Order Theory (POT) is a financial theory that explains how firms finance their investments and capital expenditures. It suggests that firms prefer to use internal financing, followed by debt financing, and lastly, equity financing, in order to fund their investments (Myers, 1984). Internal financing refers to the use of retained earnings or profits generated from the company's operations to finance new projects or investments. According to the Pecking Order Theory, firms prefer to use internal financing because it is less expensive and less risky than external financing (Myers, 1984). By using internal financing, firms do not need to pay interest or dividends to external investors, which reduces their overall cost of capital. Moreover, internal financing does not involve any additional debt, which reduces the risk of financial distress. One of the strengths of the Pecking Order Theory is its ability to explain the behaviour of firms when it comes to financing decisions. The theory has been supported by empirical research, which has shown that firms prefer internal financing over external financing, and when they do use external financing, they prefer debt financing over equity financing (Frank & Goyal, 2009). The Pecking Order Theory is a financial theory that suggests that firms prefer to finance their investments through internal funds such as personal savings, profits and retained earnings before seeking external funding through debt or equity. This theory is relevant to the assessment of the effects of microcredit on the performance of micro, small, and medium enterprises (MSMEs) in Tanzania. MSMEs may prefer to use internal funds to finance their operations before seeking external financing from microcredit providers. Therefore, while the Pecking Order Theory may provide some insight into the financing decisions of MSMEs, it is important to consider the unique institutional and economic



factors that may influence the financing behaviour of these firms in Iringa Municipality, Tanzania. This requires a more in-depth analysis of the local market conditions and the financial needs of MSMEs in the region.

### ***The Resource-Based Theory (RBT)***

The Resource-Based Theory (RBT) is a theoretical framework that explains how a firm's unique resources and capabilities can lead to a competitive advantage and superior performance. The RBT posits that a firm's resources can be classified into tangible and intangible assets and that a firm's performance is determined by how effectively it can leverage and manage these resources (Barney, 1991). The RBT suggests that firms can achieve a sustained competitive advantage by developing and utilising resources that are valuable, rare, inimitable, and non-substitutable (VRIN). In the context of microcredit and MSMEs in Tanzania, this theory suggests that the firms that effectively utilise microcredit resources to develop and enhance their existing resources and capabilities will be better equipped to compete in the market and achieve superior performance. The theory can be useful in assessing the effects of microcredit on the performance of MSMEs in Tanzania, particularly in the case of Iringa Municipality. By examining the resources and capabilities of MSMEs in Iringa Municipality and evaluating how effectively they are leveraging microcredit resources, researchers and policymakers can gain insights into the factors that influence firm performance in this context. For example, a study by Ngowi and Aloyce (2020) found that access to microcredit can enhance the capabilities of MSMEs in Tanzania, which can in turn, lead to improved performance.

### **Empirical Review**

This section presents the empirical literature review based on specific research objectives.

### ***Effects of Loan Amounts on the Performance of MSMEs***

Ali and Rehman (2019) examined the "Impact of Loan Amounts on the Profitability of MSMEs in Pakistan" using a quantitative research approach. The authors collected data from 108 MSMEs through questionnaires and used regression analysis to analyse the data. Their findings showed that loan amounts had a positive impact on profitability but only up to a certain point. After that point, the positive impact starts to diminish. They recommended that financial institutions should provide MSMEs with adequate loan amounts based on their needs and financial capabilities.

Olokoyo and Apanisile (2019) investigated the impact of loan amounts on the growth of MSMEs in Nigeria using a quantitative research approach. The authors collected data from 150 MSMEs through questionnaires and used regression analysis to analyse the data. Their findings showed that loan amounts had a positive impact on the growth of MSMEs. They recommended that policymakers should create a conducive environment for MSMEs to access loans and that financial institutions should provide MSMEs with adequate loan amounts based on their needs.

Mwambeo and Nkunya (2018) investigated the impact of loan sizes on the performance of small and medium enterprises in Tanzania. Their study used a quantitative research approach, specifically a cross-sectional survey design to collect data from 100 SMEs in Tanzania. Data was collected through structured questionnaires administered to business owners and managers of SMEs. The study also utilised secondary data from financial institutions in Tanzania. The study used descriptive statistics and regression analysis to analyse the data. The study found that loan sizes positively affected the performance of SMEs in Tanzania with a significant impact on business expansion and profitability. The study recommended that financial institutions should increase loan sizes for SMEs to enable them to expand and improve their performance.

### ***The Influence of Interest Rates on the Performance of MSMEs***

Asante and Adu (2020) examined the impact of interest rates on the Performance of MSMEs in Ghana using a Qualitative Research Approach. The authors collected data through interviews with 20 MSME owners and used content analysis to analyse the data. Their findings showed that high-interest rates negatively affected the performance of MSMEs. They recommended that MFIs should create a more conducive environment for MSMEs to access loans with favourable interest rates.

Njau and Nnko (2021) investigated the impact of interest rates on the Performance of MSMEs in Tanzania using a mixed-methods research approach. The authors collected data from 150 MSMEs through a survey and used both quantitative and qualitative analysis to analyse the data. Their findings showed that favourable interest rates had a positive impact on the performance of MSMEs. They recommended that financial institutions should provide MSMEs with loans with favourable interests to improve their performance.

### ***Effect of Initial Capital on the Performance of MSMEs***

Isiaka and Olokundun (2020) investigated the Impact of Initial Capital on the Performance of MSMEs in Nigeria using a mixed-methods research approach. The authors collected data through a survey of 300 MSMEs and used structural equation modelling to analyse the data. Their findings

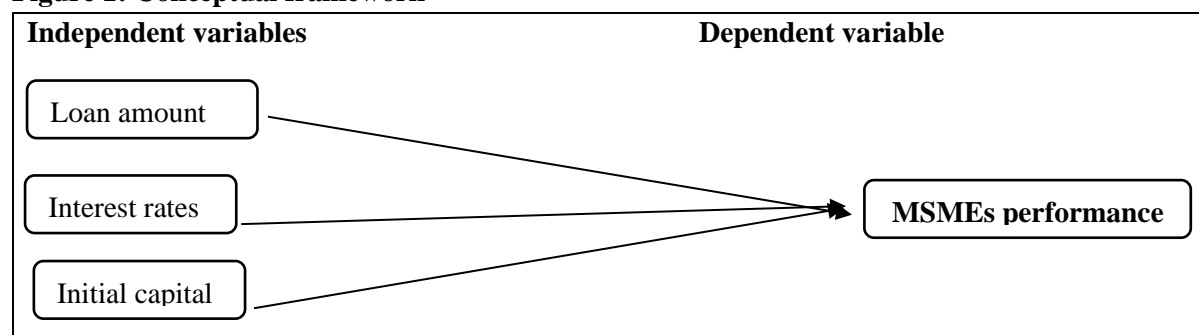
revealed a positive relationship between initial capital and business performance, specifically in terms of revenue growth and employment creation. The authors recommended that MSMEs should prioritise obtaining adequate initial capital to improve their performance.

Mboya and Mwasha (2021) investigate the Impact of Initial Capital on the Performance of Small and Medium Enterprises in Tanzania, Specifically in Morogoro Municipality. This study used a quantitative research approach, specifically a cross-sectional survey design, to collect data from 100 SMEs in Morogoro Municipality, Tanzania. Data was collected through structured questionnaires administered to business owners and managers of SMEs, as well as interviews with loan officers from financial institutions in Tanzania. The study used descriptive statistics and regression analysis to analyse the data. The study found that initial capital had a significant positive effect on the performance of SMEs in Tanzania, particularly in terms of sales growth and profitability. The study recommended that financial institutions should provide SMEs with adequate initial capital and also offer training and mentorship programs to help SMEs manage their businesses effectively.

### **Conceptual Framework**

A conceptual framework is a set of interconnected concepts, variables, and constructs that are used to define the research problem, guide the research design, and interpret the research findings (Creswell, 2017).

**Figure 1: Conceptual framework**



**Source:** Research Construction, (2023)

## RESEARCH METHODOLOGY

The research was conducted at Iringa Municipality. Iringa Municipality is located in the Iringa Region of Tanzania. The selection of Iringa Municipality as a study area was based on the following factors. Firstly, Iringa Municipality is known to have a high number of MSMEs, particularly in the informal sector. According to the Tanzania National Bureau of Statistics (2017), the Iringa region had a total of 78,635 MSMEs, of which 52,339 were in the informal sector. Secondly, Iringa Municipality has a relatively well-developed microcredit sector, with a number of microfinance institutions operating in the area (Arora, 2018). The study used a quantitative research approach. The quantitative research approach is a type of research method that uses numerical data to test a hypothesis or answer a research question. This approach is used to study a large number of cases and aims to identify patterns, trends, and relationships between variables (Creswell, 2017).

The total population for this study was 874 loan beneficiaries MSMEs operating within Iringa Municipality, where a sample of 274 respondents (loan beneficial MSMEs) was drawn by using the Yamane (1967) formula with a level of precision of  $\pm 5\%$ .

$$n = \frac{N}{1+N(e^2)}$$

The study used stratified, random sampling techniques (probability) and convenience sampling to select respondents of the study (MSMEs) and data for this study was collected by using questionnaires. The study used questionnaires to collect quantitative data from 274 enterprises.

Data from the questionnaire were analysed using both descriptive statistics and multiple regression models; the model was used to observe the magnitude and direction of loan amount, interest rate and initial capital on MSMEs performance.

### Validity of the Study

According to *Table 1* below, Bartlett's Test of Sphericity showed that the data variables obtained after the data reduction process were significant (0.000) to measure the dependent variable with a Kaiser-Meyer-Olkin value of 0.881 in accordance to Kaiser who states that the results from factor analysis can be considered acceptable if the Kaiser-Meyer-Olkin value (KMO) is 0.5 or greater, and Bartlett's test of sphericity is statistically significant,  $p < 0.05$ , therefore, the Factor Analysis was valid; hence the researcher was confident that factor analysis is appropriate for these data.

**Table 1: KMO and Bartlett's Test**

Kaiser-Meyer-Olkin Measure of Sampling Adequacy.		.881
Bartlett's Test of Sphericity	Approx. Chi-Square	3897.908
	Df	120
	Sig.	.000

**Source:** Research findings, (2023)

### Reliability of the Study

The researcher used the Cronbach's alpha test for reliability of data. Based on the results in *Table 2* below show that the data were consistent because Cronbach's Alpha coefficient ranges from 0 to 1,

with higher values indicating greater internal consistency reliability, and the findings show a coefficient of 0.910. This suggests that the items in the scale are highly correlated with each other and are measuring the same underlying construct with a high degree of consistency.

**Table 2: Reliability Statistics**

Cronbach's Alpha	Cronbach's Alpha Based on Standardised Items	N of Items
.910	.901	16

**Source:** Research Findings, (2023)

## FINDINGS AND DISCUSSION

### Loan Amounts

*Table 3* provides information on the amounts of loans received by MSMEs from financing institutions. The data is based on a sample of 274 MSMEs. There were 87 MSMEs which received loan amounts below 5,000,000 Tshs, 128 MSMEs that received loan amounts between 5,000,000 Tshs and 20,000,000 Tshs, 43 MSMEs received loan amounts between 21,000,000 Tshs and 45,000,000 Tshs, and 16 MSMEs received loan amounts above 45,000,000 Tshs. The largest proportion of 46.7% received loan amounts between 5,000,000 Tshs and 20,000,000 Tshs indicating that this range was the

most common loan amount received, 31.8% received loan amounts below 5,000,000 Tshs highlighting a considerable number of MSMEs accessing smaller loan amounts, 15.7% received loan amounts between 21,000,000 Tshs and 45,000,000 Tshs indicating a moderate number of MSMEs securing loans in this range and only 5.8% of MSMEs received loan amounts above 45,000,000 Tshs suggesting that a limited number of MSMEs obtained larger loans. The findings show that the financing institutions mostly provided loans within the range of 5,000,000 Tshs to 20,000,000 Tshs to MSMEs. This indicates that a significant portion of MSMEs were accessing moderate-sized loans.

**Table 3: Amount of Loans Received by MSMEs from Financing Institutions**

Amount received	Frequency	Per cent
Below 5,000,000	87	31.8
5,000,000 – 20,000,000	128	46.7
21,000,000 – 45,000,000	43	15.7
Above 45,000,000	16	5.8
<b>Total</b>	<b>274</b>	<b>100.0</b>

**Source:** Field data (2023)

### Interest Rates

*Table 4* presents the research findings on the interest rates charged by Financial Institutions to MSMEs. The interest rates charged by FIs to MSMEs are divided into three categories: 1%-10%, 11%-20% and above 20%. Out of the total sample of 274 MSMEs, 34 MSMEs were charged interest rates ranging from 1% to 10%, 88 MSMEs were charged

interest rates between 11% and 20% and 152 MSMEs were charged interest rates above 20%. The findings show that a substantial proportion of the interest rates charged by FIs to MSMEs fell within the above 20% range with 55.5% of the cases having interest rates above 20%. This suggests that a significant number of MSMEs might have faced relatively higher interest rates from FIs, which could have implications for their performance.

**Table 4: Interest Rate Charged**

Interest Rate Charged	Frequency	Per cent
1% - 10%	34	12.4
11% - 20%	88	32.1
Above 20%	152	55.5
<b>Total</b>	<b>274</b>	<b>100.0</b>

**Source:** Field data (2023)



### Initial capital

Table 5 presents the research findings on the amount of money invested by MSMEs in Iringa Municipality when starting their businesses. Out of the sample of 274 respondents, 69 respondents invested an initial capital below 5,000,000 Tshs. This category represents MSMEs that started their businesses with relatively low initial capital; 128 respondents invested an initial capital ranging from 5,000,000 Tshs to 20,000,000 Tshs; this category represents MSMEs with a moderate level of initial capital, 56 respondents invested an initial capital ranging from 21,000,000 Tshs to 35,000,000 Tshs; this category represents MSMEs that started their businesses with relatively higher initial capital, 21 respondents invested an amount of money above 35,000,000 Tshs when starting their businesses; this category represents MSMEs with a significant

amount of initial capital. Most of the respondents (46.7%) fell into the 5,000,000 - 20,000,000 Tshs range, indicating a prevalent trend of moderate investment levels. A substantial number of MSMEs (25.2%) started their businesses with initial capital below 5,000,000 Tshs, representing businesses with limited financial resources at the outset. On the other hand, a smaller proportion of respondents (20.4% and 7.7%) had invested relatively higher initial capital in the ranges of 21,000,000 - 35,000,000 Tshs and above 35,000,000 Tshs, respectively. The findings imply that the effects of microcredit on MSMEs' performance can vary based on the specific circumstances and the utilisation of the initial capital. While microcredit can provide essential financial support to MSMEs with limited resources, the impact on performance may depend on the amount of money invested in a startup of the business operations.

**Table 5: The Amount of money used for starting a business**

Amount of money invested into business	Frequency	Per cent
Below 5, 000, 0000	69	25.2
5,000,000 – 20,000,000	128	46.7
21,000,000 – 35,000,000	56	20.4
Above 35,000,000	21	7.7
Total	274	100.0

**Source:** Field data (2023)

### Regression Analysis

The research conducted a multiple linear regression analysis to determine the relationships between independent variables (loan amount, interest rate, and initial capital) and a dependent variable

(MSMEs performance). Multiple regression analysis allows for the examination of how two or more independent variables collectively influence a single dependent variable. The table below presents the findings of this analysis.

**Table 6: Regression Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.837 <sup>a</sup>	.701	.698	.38732

**Source:** Research findings, (2023)

Table 6 shows that the coefficient of determination, which is adjusted R square of 0.698, indicates that 69.8% of MSMEs performance is determined by the amount of loan, interest rate and initial capital. Also, the R coefficient of 0.837 means that there is a correlation of 83.7% between the independent

variable (loan amount, interest rate and initial capital) and the dependent variable (MSMEs performance). This shows that the independent variables (loan amount, interest rates and initial capital) are predictors of the dependent variable (MSMEs performance) in Iringa Municipality.

**Table 7: Analysis of Variance – ANOVA**

	Model	Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	95.065	3	31.688	211.226	.000 <sup>b</sup>
	Residual	40.506	270	.150		
	Total	135.570	273			

**Source:** Research findings, (2023)

Table 7 shows that the dependent variable can be explained by the model to the extent of 95.065 out of 135.570 or 70.1%, while other variables not captured by this model can explain 34.9% (40.506 out of 135.570) of MSMEs' performance. The F value of the model produces a p-value of 0.000,

which is significantly zero. A p-value of 0.000 is less than the critical level of significance of 0.05 for normally distributed data. This means that the model is highly significant in MSMEs' performance in Iringa Municipality.

**Table 8: Regression Coefficients**

	Model	Unstandardised Coefficients		Standardised Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	.279	.116		2.405	.017
	Loan amount	.311	.077	.233	4.039	.000
	Interest rates	-.194	.053	-.012	-1.785	.075
	Initial capital	.651	.066	.594	9.934	.000

**Source:** Research findings, (2023)

The table above presents the findings of a multiple regression analysis, examining the relationship between independent variables (loan amount, interest rates, and initial capital) and a dependent variable (MSMEs performance). Based on the regression coefficient analysis in Table 5, the results indicate that a unit change in loan amount causes a 0.311 increase in the MSMEs performance, holding other variables constant. The standardised coefficient (Beta) of 0.233 suggests that loan amount has a positive impact on MSMEs' performance. The t-value of 4.039 indicates that the parameter estimates are statistically significant. A unit of change in interest rate is -0.194. Indicating that a one-unit increase in interest rates is associated with a -0.194 decrease in the dependent variable, holding all other variables constant, the t-value of -1.785 is not statistically significant ( $p = 0.075$ ) at the conventional significance level of 0.05. This shows that the parameter estimates interest rates do not affect the performance of MSMEs in Iringa Municipality. A unit of change in initial capital is 0.651, indicating that a one-unit increase in initial capital is associated with a 0.651 increase in

MSMEs performance, holding other variables constant. The standardised coefficient (Beta) of 0.594 suggests that initial capital has a substantial positive impact on MSMEs' performance. The t-value of 9.934 shows that the parameter estimate is statistically significant because it is greater than 2.405. A p-value is  $< 0.001$ , indicating a strong relationship between initial capital and MSMEs performance.

The findings show that loan amount and initial capital have significant effects on MSMEs' performance. Specifically, one increase in loan amount leads to an overall increase in performance, while an increase of one unit in initial capital leads to a 0.651 increase in performance. However, the relationship between interest rates and MSMEs' performance is not statistically significant in this analysis, suggesting that interest rates do not statistically influence the MSMEs' performance in Iringa Municipality.

## DISCUSSION

### Contribution of Loan Amount on Performance of MSMEs in Iringa Municipality

The findings revealed that MSMEs at Iringa Municipality request and receive loans from financing institutions and use them to improve performance. MSMEs primarily utilise the loans received from Microfinance Institutions (MFIs) for developing new products/services and expanding their businesses. These activities are considered the most useful applications of loans, and the majority of MSMEs received adequate loan amounts to finance their activities so as to promote their performance; this means that loan size has a significant positive effect on the performance of SMEs in Tanzania.

The results are supported by Kazimoto et al. (2019), who examined the impact of loan size on micro, small, and medium enterprises' performance in Tanzania. The study found that loan size has a significant positive impact on the performance of SMEs in Tanzania, particularly in terms of revenue growth and business expansion. The study recommended that financial institutions should increase loan sizes for SMEs while also providing training and mentorship programs to help SMEs manage their loans effectively.

### Influence of Interest Rate on the Performance of MSMEs

The finding indicates that high interest rates tend to have a negative impact on the profitability of MSMEs. A significant number of businesses experienced reduced profit margins, while only a small minority managed to maintain stable profit levels. The findings also indicate that the majority of MSMEs faced difficulties in repaying their loans due to high interest rates and indicates that MSMEs faced challenges in planning and making financial decisions due to fluctuating interest rates.

The findings are supported by Alwi and Tahir (2019) their findings showed that loan conditions,

such as interest rates and other charges, negatively affect the performance of MSMEs. They recommended that policymakers should develop loan policies that are more flexible and cater to the specific needs of MSMEs.

### Effect of Initial Capital on the Performance of MSMEs

The findings suggest that the effects of initial capital on the performance of Micro, Small, and Medium Enterprises (MSMEs) can vary based on specific circumstances and the utilisation of the capital. While microcredit can provide essential financial support to MSMEs with limited resources, the impact on performance may depend on the amount of money invested at the startup of business operations. MSMEs utilise their own funds for asset acquisition, in addition to accessing microcredit, demonstrating commitment and financial stability. This combination of resources enhances operational efficiency, productivity, and overall performance. Having sufficient initial capital is generally viewed as beneficial for MSMEs, as it provides resources for various business needs and enables them to compete in the market. It should be noted that not all MSMEs may experience the same positive impact; a smaller portion of surveyed MSMEs reported a negative impact from the amount of initial capital invested. This could be due to various factors, such as improper allocation of funds, mismanagement, or external market conditions.

The findings are supported by Fakir et al. (2019), who investigated the impact of initial capital on the survival of MSMEs in South Africa using a survey research approach. Their findings showed that initial capital has a significant positive impact on the survival of MSMEs. Isiaka and Olukandun (2020) investigated the impact of initial capital on the profitability of MSMEs in Nigeria. They found that initial capital has a significant positive impact on the profitability of MSMEs, and they recommended that policymakers should develop policies that improve access to finance for MSMEs.

Therefore, the findings emphasise the importance of having sufficient initial capital for MSMEs. When combined with microcredit, it can enhance their ability to compete, improve operational efficiency, and contribute to overall performance. However, the specific outcomes may vary depending on how the capital is utilised and the unique circumstances of each MSME.

## CONCLUSIONS AND RECOMMENDATION

The study investigated the effects of microcredit on the performance of Micro, Small, and Medium Enterprises (MSMEs) in Tanzania, focusing on selected MSMEs in Iringa Municipality. The study aimed to address three specific objectives: the contribution of loan amount, the influence of interest rate and the effect of initial capital on the performance of MSMEs.

The findings indicate that the loan amount has a significant impact on the performance of MSMEs in Iringa Municipality. MSMEs that were able to secure higher loan amounts demonstrated better performance compared to those with lower loan amounts. This suggests that access to adequate funding through microcredit plays a crucial role in enhancing the overall performance of MSMEs.

The research reveals that interest rates do not have a significant influence on the performance of MSMEs. High-interest rates increase the borrowing costs and limit the financial access to MSMEs, which can result in hindering the overall performance of MSMEs,

The finding shows that the initial capital invested in MSMEs has a positive effect on their performance. MSMEs that have sufficient initial capital demonstrate better performance outcomes compared to those with limited capital. Adequate initial capital enables MSMEs to invest in critical areas such as marketing, production, hiring skilled staff, and adopting technology, which ultimately enhances their competitiveness and overall performance.

## Recommendations

Based on the study findings, the researcher provides recommendations to the following groups;

### *Government and Policy Makers*

Based on the research findings, the study recommends that:

The government should ensure that MSMEs receive appropriate loan amounts and should take proactive measures to regulate interest rates on microcredit loans, ensuring they remain at levels that do not burden MSMEs with unsustainable debt.

Policymakers should actively collaborate with financial education institutions to design and implement comprehensive financial literacy programs. These programs should target MSME owners, equipping them with the knowledge and skills to navigate complex financial landscapes.

### *MSMEs*

MSMEs should recognise the positive influence of loan amounts and initial capital on their performance. When obtaining microcredit loans, it is important to have a clear strategy for how these funds will be used. Entrepreneurs should plan and allocate the funds strategically to maximise their impact. Whether it is enhancing production, expanding operations, or exploring new opportunities, a well-thought-out plan ensures that the borrowed funds contribute directly to business growth and profitability. Also, MSMEs should take a proactive approach to interest rate negotiation. Demonstrating a clear understanding of their financial situation, business plans, and growth potential can provide leverage when discussing terms with lenders. And MSMEs should be Strengthening financial management practices is crucial for MSMEs to ensure the efficient utilisation of loan funds.

### Financial Institutions

Drawing insights from the research findings on the effects of microcredit on MSMEs' performance in Tanzania, the study recommends that:

Financing institutions should recognise that loan provisions to MSMEs should be based on the specific needs, growth potential, and industry dynamics of each business is essential. Also, financing institutions should explore ways to provide microcredit loans at competitive rates that strike a balance between affordability for MSMEs and sustainability for the institution.

### Other Scholars/Researchers

For further studies, the researchers should conduct similar research in different regions or countries that will allow scholars to ascertain the general ability of the findings. Also, for further studies, the researchers should conduct longitudinal studies that can provide invaluable insights into the long-term effects of microcredit on MSMEs' performance and business growth. In this study, objectives were only able to explain 69.8% of the total variation of MSMEs performance in Iringa Municipality. This means that these objectives might have missed out on some important contributing factors to MSMEs' performance. By adhering to these recommendations, scholars can contribute to the expanding body of knowledge on microcredit and its implications for MSMEs. Through rigorous research methodologies, thoughtful replication, and comprehensive longitudinal studies, researchers enhance the precision of insights and contribute to evidence-based decision-making in the field.

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