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CHALLENGES FACED BY SMALL AND MEDIUM ENTERPRISES IN RAISING FINANCE IN UGANDA

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ABSTRACT

The purpose of this paper was to discuss challenges faced by SMEs in raising finance in Uganda. Basing on the critical document review, the paper uses social capital theory to demonstrate that Ugandan SMEs continue to face challenges in raising finance. Such challenges include inadequate collateral to secure loans; information opaqueness; low level technical and management skills; lack of professionalism; competition; inability to afford long term financing among others. The paper suggests various ways in which these challenges can be addressed. Such suggestions include; developing social capital through networks; SME friendly policy framework; proper information management; and improvement of management skills. Alternative sources of finance available to SMEs include; investment into capital markets, long term financing, leasing and franchising. The paper concludes that SMEs should put emphasis on the development of social networks as a mechanism to develop financing opportunities.

Introduction

Finance is one of the most important resources needed to start and develop Small and Medium Enterprises (SMEs) (Badagawa, 2003; Gilbert, McDougall & Audretsch, 2006). Finance is needed to give birth to an SME through the creation of other factors of production such as land and labour. However, in Uganda,over 50% of all SMEs close shop before they celebrate their second birth day (Mbabazi, 2012). Whereas the collapse of SMEs has been attributed to their lack of ability to raise finance (Kasekende &Opondo, 2003; Calice,Chando &Sekioua, 2012), little attention has focussed the challenges these SMEs face in trying to raise finance and how the challenges can be mitigated. In addition, there is evidence from the existing literature that discussions on the alternative ways of raising finance by the SMEs in Uganda has not been given the attention it deserves. The purpose of this paper is to discuss challenges faced by SMEs in raising finance to fund their operations, ways of reversing the trend, and recommendations of alternative source of funding.

Methodology

This paper relies on critical literature/document review. Literature review is the use of secondary data (Amin, 2004) to justify the particular approach to the topic, the selection of methods, and demonstration that this research contributes something new (Hart, 2001). The review of literature has been discovered to be reliable in conducting desk research which is central to this paper. Authors such as Onwuegbuzie, Leech &Collins (2012) have recently emphasized the importance of literature review. They consider it as the foundation and inspiration for substantial, useful research. In addition, Randolph (2009) explains that conducting a literature review is seen as a means of demonstrating the author's knowledge about a particular field of study. This implies that an academic discussion devoid of literature analysis backed by theory is no more than personal impression, anecdote or conjecture. Indeed the paper relies heavily on document review and the social capital theory to

examine and discuss phenomena in review and links the discussion to the theoretical framework examined subsequently. The discussion identifies gaps in the existing literature and evaluates possible alternatives to filling them. This approach is fit for a theoretical paper such as this.

What are Small and Medium Enterprises (SMEs)?

In order to have a meaningful discussion, it is imperative to shed light on the ontologies of SMEs. This will provide phenomenological and epistemological venture into the various aspects of the discussion. There is no universally accepted definition of SMEs (Oteh, 2010). Every country or region has developed its definition whichvaries across national statistical systemsOECD (2000). This has surrendered SMEs to the subjective definitions of convenience and interpretivistic sentiments. For example, scholars like Kurokawa, Tembo, & Velde, (2008) maintain that the definition of an SME depends on number of employees, firm size, total assets, sales and investment level.Banks define SMEs in terms of average annual sales, with thresholds that vary by country according to the size of the economies and structure of the corporate sector (Torre, Soledad, Peria, Schmukler, 2010). The World Bank defines SMEs as enterprises with up to 300 employees and total annual sales of up to US$15 million (Zavatta, 2008). This definition may not apply to all economies. This therefore calls for a definition tailored to the economic situations of developing countries.

From the Africa perspective, an SME is a firm employing 0-250 employees (Ayyagari, Meghana, Thorsten, *etal,* 2005). For the case of Uganda, however, discrepancy exists in the definitions of SMEs. According to Mbaguta (2003), an SME is that firm that employs a maximum of 50 employees, with a working capital of about 50 million Uganda shillings and the turnover value of 10-50 million Uganda shillings. This definition is in agreement with that of Kasekende and Opondo (2003). Yet, Uganda Investment Authority (UIA) (2008) defines SMEs as firms or enterprises which employ 50 or more people with a revenue turnover of maximum Ugandan Shillings 360 million and total assets of maximum Ugandan Shillings 360 million. Although the discrepancies in definitions could be caused by temporal factors, it is without doubt that definitional variations complicate the design of interventional and mitigational policies (Apire, 2003). That notwithstanding, the attention directed to the definitions of SMEs by different practitioners and academicians renders credence to the importance attached to these Small and Medium firms as explained below.

Importance of SMEs in Uganda

There are two fundamental questions to address here. First, is it possible to map the location of SMEs in Uganda? Second, does it make sense for a management specialist to study and examine the challenges facing SMEs in raising finance in Uganda? The available literature provides answers to both questions. For example, the UN report (2003) estimates 800,000 SMEs in Uganda majority of which are located in rural areas and on the outskirts of urban areas. This number is contrasted by Mbabazi (2012) who contends that there are over 1.5 million SMEs in the country. Considering the lapse of ten years between the publication dates, Mbabazi's contention may present a true picture of the number of SMEs. A common denominator here is that both authors acknowledge the fact that SMEs exist in Uganda. In Kampala, these enterprises are located in Katwe, Nakawa, Wandegeya and Ndeeba, and produce items such as steel windows, steel gates and furniture.

In answering the second question, the section examines the importance of SMEs in Uganda. SMEs have created an indelible mark in the employment sector. This is supported by Kasekende & Opondo (2003) and Ishengoma&Kappel (2008) who confirm that SMEs have not only improved the number of employment opportunities for the poor but also provided an environment to foster a knowledge economy. Currently, SMEs employ between 2.5 to 4 million people (Tushabomwe, 2006, 2010; Mbabazi, 2012; Tusubira & Nabeta, 2013; Uwonda, Okello & Okello, 2013). Employment and knowledge economy are closely related as Seghers,

Manigart, & Vanacker (2009) demonstrate that human capital is necessary in creating wealth and more wealth is used to develop human capital. This symbiotic relationship leads to national economic growth and calls for a special attention to SMEs.

Besides fostering employment, research shows that SMEs are the engine behind proliferation of economic growth in Uganda. They are seen as critical for for economic growth of Uganda (Kisaame, 2003; Nangoli, Basalirwa, Kituyi & Kusemererwa, 2013). In the same vein, scholars like Tusubira, & Nabeta (2013) explain that SMEs contribute 75% of GDP and constitute 90% of the private sector, improving standards of living and ensuring social and political stability. SMEs are therefore responsible for entrepreneurial development, poverty alleviation and improved quality of life, resource mobilization, business adaptability and sustainability (Tushabomwe, 2010). Mbabazi (2012) adds that SMEs provide the economy with a continuous supply of ideas, skills and innovation necessary to promote competition and the efficient allocation of scarce resources. Today, SMEs are estimated to contribute over 80% of manufactured goods output. This explains why SMEs should be closely monitored to ensure that risk and vulnerability do not impede their growth. Despite the important role of SMEs in the Ugandan economy, the rate at which they are running out of business stands at 50% annually leaving a lot to be desired (Uwonda, Okello & Okello (2013). The main reason for quitting business is lack of sufficient finance to fund their operations. But why should SMEs face challenges in raising finance? What theoretical explanations justify these financial challenges? How can such theoretical explanations provide answers to these challenges? The following discussion provides a theory to guide the seeking of answers to these questions.

The theory of social capital and SMEs in Uganda

The theory of social capital was propounded by Putman (1995). It refers to the ability of the actors to gain benefits from their social network, personal relationships and the quality of association (Portes, 1998). The theory contends that individuals and organizations will always engage in social networks inorder to generate profits (Lin, 1999). Social capital is the sum of the resources, actual or virtual, that accrue to an individual or a group by virtue of possessing a durable network of more or less institutionalized relationships of mutual acquaintance and recognition (Bourdieu & Wacquant, 1992). The theory is based on assumptions that;

1) The more the networking, the greater the social capital.
2) The greater the social capital, the higher the priority of the norm of equality.
3) The greater the social capital, the easier to mobilize support for problem solutions.

Social capital is multi-dimensional and occurs at both the individual and organizational levels (Nahapiet & Ghoshal, 1998). As explained by Schmid&Robison (1995), the concept of social capital includes: obligations, expectations, and trustworthiness of structures; information channels; and norms and effective sanctions. All these have a positive impact on the growth of SMEs. According to Davidsson & Honig (2003) social networks provided by extended family, community-based or organizational relationships are theorized to supplement the effects of education, experience, and financial capital through reciprocity. SMEs which develop and maintain strong social networks are likely to raise finance to finance their operations and the reverse is true for SMEs which do not have social network programmes. This is explained further by Coleman (1988) that social capital can be a useful resource both by enhancing internal organizational trust through the bonding of actors, as well as by bridging external networks in order to provide resources. At the centre of this social network is trust and fulfillment of obligations which carry sanctions (Coleman, 1988; Knack & Keefer; 1997; Lin, 1999).

In order for the social network to produce positive results, there should be strong ties among the individuals or organizations in the network. In this regard, Davidsson and Honig (2003) attest to the fact that weak ties though

useful may not enhance the generation of desirable social capital from a network. That is why Cook & Whitmeyer (1992) and Quillian & Redd (2006) advocate for strong ties, such as those derived from family relationships as they provide secure and consistent access to resources. Moreover, the more personal resources one has, the less likely one is to rely on strong ties. Like most theories in management science, the social capital theory has not been spared by critiques. For example, Bourdieu & Wacquant (1992) believe that social capital is a tool of the elite deployed to ensure that the wrong people do not enter their circles. That the social capital derived from these social networks benefits only members of the network. Whereas this may be true for individual level networks, strategic SMEs can build networks strong enough to generate social benefits. However, SMEs may be blocked by larger social networks of financial institutions which target large business enterprises.

It is prudent to point out that social relationships may also have negative consequences (Quillian & Redd, 2006). Social capital can be used to achieve goals that are negative. Criminal networks are one of the clearest examples of this sort of consequence. Even in cases where the direct consequences of a network are to facilitate production of a valued good as in family owned SMEs (Tushabomwe, 2010; Tusubira & Nabeta, 2013), the exclusionary nature of social networks raises equity issues (Perkins, Hughey & Speer, 2002). This may be a big challenge for SMEs as they try to accomodate all mebers in the social network. Whereas some institutions may be well intentioned to join the SMEs network, it is hard to predict behaviour. Even the level of trust advocated for by Coleman (1988), Putman (1995) and Lin (1999) may be difficult to guarantee. However, constant evaluation of engaments and equitable distribution of social capital may prove benefitial to the SMEs.
Another important point to note is that networks produce better results if information sharing is enhanced. However, SMEs in Uganda face information asymmetries that make it hard to share information with potential funders (Kasekende & Opondo, 2003, UIA, 2008). Without the free flow of information regarding the nature of business, annual returns and strategic plans, it may be difficult for the SMEs to derive desired benefits from the social networks.

Notwithstanding the critiques labeled against social capital theory, social capital gained from formal and informal networks has been found to benefit business both large and small. It is through networks that markets are created and maintained. The same networks help to identify business partners and well-wishers who potentially fund the SMEs. The application of this theory in identifying and neutralizing challenges faced by SMEs in raising finance is a paramount. On the basis of the theory, the challenges faced by SMEs in raising finance to fund their operations are discussed below.

Challenges faced by SMEs in raising finance in Uganda

The interconnection between the theory of social capital and challenges faced by SMEs in raising finance cannot be under-estimated. In the subsequent discussion, such an interconnection is revealed as inherently embedded in every challenge that SMEs encounter either consciously or unconsciously. The main focus here is on dissection of challenges such as; inadequate collateral to secure loans; information opaqueness; low level technical and management skills; lack of professionalism; competition; inability to afford long term financing among others.

Inadequate collateral to secure loans

Much of the SME financing is provided primarily by banks with loans being backed by credit guarantees or collaterals (Park (2006). The theory of social capital puts emphasis on social networks and reciprocity arising from such networks (Putman, 1995; Lin, 1999). In the absence of social networks, SMEs continue to grapplewith scarcity of collateral to secure bank loans. Yet, there is evidence that inadequate collateral continues to cripple the financial needs of these SMEs (Apire 2003; Griffiths, 2003; UNEP, 2007). This is not to imply that SMEs do not secure loans from banks. Infact financial analysts like Kasekende & Opondo (2003) explain

that some SMEs get loans from financial institutions. However, they reveal that when banks lend to SMEs, they tend to charge them a commission for assuming risk and apply tougher screening measures, which drives up costs for SMEs.

In addition to collateral, SMEs are required to demonstrate that they have sufficient equity to contribute to their businesses, which many of them lack (Kiiru, 1991; Tomecko & Dondo, 1992; Oketch, 2000; UIA, 2008). Evidence from the Uganda Securities Exchange (USE) Brochure (2013) indicates that banks consider lack of collateral as high credit risk because of the transaction costs associated with availing credit to such SME companies. The same view is held by Kurokawa, Tembo, & Velde, (2008) and Ruffing (2003). There is no single explanation for lack of collateral by SMEs. What is clear is that limited social networks impede the ability of SMEs to secure non-collateral securities.

Informational opaqueness

No business enterprise can survive early mortality without communication and effective information management (Adler & Rodman, 1997; Defleur & Everette, 1999; Maicibi, 2003). And there is no best way a business enterprise can propel to greater heights if information management is not channeled through social networks in which social capital is derived (Putman, 1995; Lin, 1999; Davidsson & Honig, 2003). In fact Petersen (2004) draws a distinction between hard and soft information, with hard information being more numerical and encompassing such items as financial statements, payment history and output numbers. While soft information is more qualitative and includes opinions, ideas, rumors, and statements of future plans.

Much of what banks use in relationship lending and lending to more opaque small businesses would be characterized as soft information. However, SMEs have always been susceptible to information asymmetries (Zavatta, 2008; Oteh, 2010) or information opaqueness (Torre, Soledad, Peria & Schmukler, 2010). Opaqueness makes it is difficult for banks to ascertain if SMEs have the capacity to pay or willingness to pay if credit is extended to them. This is exacerbated by lack of established information network such as a credit reference bureau for tracking defaulters (Apire, 2003) and unverifiable history of past credits and lack of adequate historical records of the firm's transaction (Oteh, 2010). As Ruffing (2003) explains, lack of financial information increases the transaction costs of banks, or even worse makes it impossible to evaluate the chances of getting their money back if they lend SMEs.

Owners or managers of SMEs sometimes keep three sets of books: one for the revenue authority, one for themselves and one for their ex-wives (Kasekende & Opondo, 2003). At the end of the day they do not know where their profit centres are (Namisango & Lubega, 2014). Other scholars DeYoung, Glennon, Nigro & Spong, (2012) argue that informational asymmetries between borrower and lender may limit the types of lenders and the lending technologies that may be used. In the same accord, Petersen (2004) contends that the amount of information available on firms will influence their access to capital and the structure of financial markets and financial institutions.

Low level technical and management skills

There is a strong interdependence between human capital, social capital and financial capital. Technical and manegement skills will determine the amount of social and financial capital generated for the SMEs. In human resource management studies, greater attention has focussed on the importance of human capital as a preliquisite for the survival of organizations including SMEs(Byars, & Leslie, 2000; Bernardin, 2003; Maicibi, 2003; Armstrong, 2006). Inadequate human capital hinders the ability of SMEs to strengthen their capacity to receive financing (Longenecker,Petty, Moore, & Palich,2006). This is because human capital provides management skills (Kasekende & Opondo, 2003; Tusubira & Nabeta, 2013), entrepreneurial skills (UIA, 2008) and

knowledge of business opportunities (Tushabomwe, 2006). As such, SMEs lack good quality human capital which also means limited marketing and financial planning, lack of good business plans; poor business records and deficient corporate governance (Apire, 2003, UNEP, 2007). In addition, due to their small size, a simple management mistake is likely to lead to collapse of SMEs hence no opportunity to learn from its past mistakes (Bowen, Morara & Mureithi, 2009).

Lack of professionalism both internal and external

Ethics in business is an important element for the survival of enterprises regardless of size. One of the most important ingredients of ethics is trust. Ethics is closely related to professionalism. The theory of social capital underscores the importance of trust in social networks at both individual and organizational level (Bourdieu & Wacquant, 1992; Putman, 1995; Portes, 1998; Lin, 1999). However, there is evidence to the effect that SMEs in Uganda lack professionalism (Apire, 2003; Tushabomwe, 2006). This is exhibited in corrupt tendencies (Kurokawa, Tembo & Velde, 2008), disrespecting business contracts (UIA, 2008) and deliberate concealing of business records on transactions (Kasekende & Opondo, 2003). Other ethical issues include unfair treatment of stakeholders and manipulation of organizational structure (Tushabomwe, 2006; Ndagu & Obuobi, 2010). There are also concerns of lack of professionalism outside the control of SMEs such as dubious legal systems (Kauffmann, 2005). These ethical concerns have discouraged banks from lending to SMEs. In the absence of ethical environment and trust, SMEs lose out on capital financing as well as deprivation of social capital advocated for by the theory of social capital.

Competition from large enterprises

SMEs always face competition in accessing finance and markets (Griffiths, 2003). A number of survey-level studies have found that SMEs face greater obstacles than large firms both in terms of accessing finance and the underlying cost of credit (Leo, 2011). Yet, limited accessibility to markets constrains SMEs from generating capital needed to run daily business operations. Compared to large enterprises, SMEs are less efficient and incur high costs per unit of revenue (Ishengoma&Kappel, 2008). They use labor-intensive technologies compared to larger firms which are more capital-intensive. Besides, Ugandan SMEs face competition from the global economy (UN report, 2003). With poor technology, competition for markets and inadequate finance, SMEs cannot expand to serve global markets or even establish business linkages with larger firms. Moreover, they cannot acquire credit ratings that satisfy investors (Kumar, Krishna, Raghuram, *et al*, 1999; Park, 2006). SMEs are typically required to demonstrate that they have sufficient equity to contribute to their businesses, which many small business owners usually lack (Kasekende & Opondo, 2003). However, larger, older, and foreign firms have a much easier time accessing expansion and development capital than SMEs (Leo, 2011). Consequently, many SMEs stay small and informal and use simple technology (Kauffmann, 2005). The non-symbiotic relationship between large firms and SMEs due to competition implies that the duo may not develop social networks from which to derive social capital. This continues to affect the ability of SMEs to access finance.

Inadequate capacity to afford long term financing

There are four major sources of long term financing in Uganda. These are; capital markets, long term bank loans, leasing and retained earnings. Although long term financing favours enterprises in perfect markets, SMEs tend to suffer greatly due to their inability to secure long term financing even in such markets (Park, 2006). This is true with Uganda where scarcity of long term finance is a key impediment to greater investment and growth of SMEs.Moreover, Ugandan SMEs tend to have short-term business outlook(UIA, 2008) and operate under very difficult business conditions (Mensah, 2004; Kauffmann, 2005; Ishengoma&Kappel, 2008). In addition, SMEs

tend to rely on informal sources of funds such as family, friends and customer advances instead of relying on bank loans(Ruffing, 2003). As such, SMEs continue to operate in the vicous cycle of inadequate financing. Given the important role played by SMEs in the Ugandan economy, it is paramount to mitigate these challenges by focussing on strategies that enhance favourable financing conditions. Such strategies are discussed below.

How the above challenges can be addressed to reverse the trend

In addressing the above challenges, the discussion here makes a link between social capital, human capital and financial capital. This is based on the premise that if social networks are developed by SMEs they will realize social capital which also leads to an increase human capital and financial capital as already discussed in the theory.

Development of social capital through networks

There is enough evidence to confirm that if SMEs develop and maintain social networks, they will reap social capital which in the end enables them to obtain finance capital to fund daily operations. This is because, social capital builds trust among SMEs and their network partners, brings about social insurance which translates into business insurance and gives access to relevant information which SMEs need for ease of business transactions (Spence, Schmidpeter & Habisch, 2003). This strategy has worked for banks which establish social networks with SMEs (DeYoung, Glennon, Nigro, & Spong, 2012). Perhaps hiccups arise in making choices of which firms to engage in the social networks and which infrastructural mechanisms to establish inorder for the networks to operate successfully. SMEs should build networks with non-rival firms in order to enhance their capacity to enter into, and observe contractual exchanges as well as legal protection from unfair practices by other firms (Spence, Schmidpeter & Habisch, 2003; Mensah, 2004).

Policy framework

The government should provide for a policy environment for reducing collateral requirements and providing safeguards. AS Ruffing (2003) explains, if an enabling policy, legal and regulatory framework and the necessary infrastructure to reduce the cost of doing business are accompanied by a stable macroeconomic environment, SMEs can play a significant role in economic development. Currently, the government of Uganda has made some initiatives to uplift the capacity of SMEs to raise funds. Such initiatives include provision of non-fiscal incentives like Plan for Modernization of Agriculture (PMA), Business Uganda Development Scheme (BUDS), Microfinance Outreach Plan, UNIDO Master Craftsman Programme (MCP), The Jua Kali Initiative and the Youth Fund (UIA, 2008). However, such initiatives have lacked multi-sectoral approaches (Oteh, 2010). Worse still, there are concerns over the distribution of these incentives to all intended beneficiaries. Moreover, there is still much effort needed for the government to draft policies aimed at the protection of SMEs in Uganda. Currently, interest rates on loans are higher than what SMEs can afford and money lender firms operate like sharks that devour SMEs' financial capital. Many SMEs are closing business because of inadequate collateral demanded by these firms. More incentives targeting youth should be established because they dominate the SME world and have proved to be more innovative and creative, yet lack of collateral hinders their operations (Nangoli, Basalirwa, Kituyi & Kusemererwa, 2013).

Enhancing information management in SMEs

One of the critical challenges limiting SMEs from accessing finance in Uganda is informational asymmetry. There are two ways in which SMEs can neutralize this challenge. First, relationship lending enhanced by social networks (Torre, Soledad, Peria &Schmukler, 2010) has the potential of mitigating opacity problems because it

relies primarily on soft information gathered by the loan officer through continuous, personalized, direct contacts with SMEs, their owners and managers, and the local community in which they operate (Torre, Soledad, Peria &Schmukler, 2010).However, SMEs should not wait for the loan officer to solicit for the soft information. Through social networks, SMEs can learn best practices from other firms on how information is managed for effective business transactions. This is possible if SMEs understand their deficiencies in information management and the desirable way forward so that information availability is enabled and sustained to build their competitiveness (Namisango & Lubega, 2014). Secondly, adopting clear accounting standards, setting up independent, competent and reputable accounting firms and creating more credit bureau supplying data on the solvency of firms, banks can able to obtain relevant information from SMEs without having first to hustle with them (Kauffmann, 2005; Berger & Udell, 2006)

Improving management skills

There is consensus among management practitioners and academicians that effective management fosters qualitative and quantitative organizational development (Robbins; 1980; Tobbins, 1984; Koontz & O'Donnell, 1986; Pearson, 1990; Ivancevich& Gibson, 1990; Rosen Bloom, 1993; Habbard, 2001; Zondo, 2001; Ndagu &Obuobi, 2010; Maicibi, 2013). This paper concurs with scholars such as Seghers, Manigart & Vanacker (2009) whose research findings demonstrate that human capital and finance are linked. Entrepreneurs with high quality human capital can use more of their personal funds to mitigate their venture's finance constraints. The implication here is that if SMEs invest in human capital, it willincrease their ability to raise finance for funding their operations.In the same accord, Ugandan SMEs should improve management skills with a focus on entrepreneurial training and skills development (Mensah, 2004). In addition, proper supervision and business skills training will supplement and synergize management efforts (Tushabomwe, 2010).Above all, SMEs should hire competent and motivated workforce who are achievement-oriented (Nangoli, Basalirwa, Kituyi, Kusemererwa, 2013). It is important that SMEs transcent family and informal ties that potentially block effective management decision making.

Alternative sources of funding for SMEs in Uganda

This section examines how SMEs in Uganda can raise funds through alternative ways. Financing is necessary to help SMEs set up and expand their operations, develop new products, and invest in new staff or production facilities (Kasekende & Opondo, 2003).

Financing through capital markets

SMEs may raise funds in capital markets in two forms: equities and bonds. However, it is not easy for SMEs to raise funds through equities as the equities issued by SMEs are not liquid enough to attract investors because they are not usually listed on exchanges (Parker, 2006). This can be mitigated by social networks in which social capital increases the social and financial strength of the SMEs to raise funds through equities and bonds (Putman, 1995; Lin, 1999).

Long term financing

There is a need to review and establish opportunities that will help expand financial instruments and improve access to business finance. Specifically, opportunities such as equity financing and other non-bank loan financing, including issuance of bonds, asset leasing and venture capital (Badagawa, 2003; Torre, Soledad, Peria &Schmukler, 2010). Knowledge of long term financing and business and financial literacy are synonymous, yet, most SMEs in Uganda are dominated by semi-illiterate or illeterate entreprenuers. It is therefore prudent to

contend that long term financing requires long term planning embedded in the comprehensive national skills development framework.

Leasing

Renting of tangible and marketable assets through leasing can help overcome costly contract enforcement processes by SMEs including ambiguous commercial laws and inefficient bankruptcy procedures(Kasekende & Opondo, 2003; Parker, 2006; UIA, 2008).When good financial information is not available to gauge capacity or willingness to pay, banks can use other types of hard information and incentive-compatiblemechanisms to increase the likelihood of repayment. In this way, banks can compensate for weaknesses in the institutional environment (Kauffmann, 2005). These mechanisms free banks from having to rely on government subsidies to lend to SMEs. If leasing is to succeed in Ugandan SMEs, they should have assets to lease out. Whereas medium enterprises may have these assets to lease, small firms operate in a hard environment with almost no asset to lease. The remedy to this is investment in social capital which translates into financial capital without having to incur heavy monetary costs.

Franchising

Apart from the need to boost SME capacities, some financial instruments can help provide missing information or reduce the risk stemming from some SMEs' lack of transparency. Franchising, which is very popular in Southern and East Africa, allows use of a brand name or know-how that reduces the risk of failure (Kauffmann, 2005; EOCD, 2013). However, it may not be feasible for SMEs which are grappling with start-up capital to think of investing in franchising. This financing option only makes sense for SMEs that have strengthened their financial capacity.

Conclusion

SMEs have been recognized as important contributors to the economy. As such, several financial institutions especially banks are focusing on SMEs and are coming up with special packages to finance SMEs. In most banks there are now departments to cater for the often unique banking requirements of these entities (Mbabazi, 2012). However, the major aim of banks is not to uplift SMEs' financial status but to use them in expanding their business accumen. Moreover, bank loans are still a major source of funding for SMEs yet the interest rates are high. It is important that government hears the outcry of SMEs regarding reduction of interest rates (Nangoli, Basalirwa, Kituyi & Kusemererwa, 2013). Through social networks and linkages, SMEs will be able to expand their social capital and later financial capital.

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