Evaluation of the Influence of Cost of Credit on the Financial Performance of SMEs in Juba County, South Sudan

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Abstract: ***The importance of Small and medium-sized enterprises in South Sudan is at a high level due to their contribution in offering employment, spurring economic growth and social good, as well as empowering the youthful population of South Sudan to gain economic relelvance. However, the level of cost of credit has a negative impact on this noble sector as the players in the SME sector are largely viewed as high risk borrowers by the mainstream financial sector, thus levying higher interest charges to borrowers from this sector. For the SME sector to grow the level of cost of credit to players in this sector has to be addressed. The main purpose of the study was to evaluate the influence of cost of credit on the financial performance of SMEs in Juba County, South Sudan. The study sought to determine how the cost of credit affects the financial performance of SMEs in Juba, South Sudan. The study was limited to Juba County, South Sudan. The research objectives were anchored on three theories; The Pecking-Order Theory, The Credit Rationing Theory and The Microfinance Theory. A descriptive research strategy was used in this research. A population of 30,000 SMEs in Juba County of South Sudan was taergetted. Juba County was selected for this study using a purposive sampling approach. Descriptive and inferential statistical methods were employed for analyzing the sample's characteristics. This included utilizing measures like frequencies, percentiles, as well as the mean and standard deviation. Inferential techniques such as Pearson correlation and multiple regression analysis were applied to explore the connection between independent and dependent variables. The regression model focused onthe significance of the cost of credit to financial performance. Itis recommended that lenders adopt a flexible approach towards determination of the cost of credit to SMEs.***

Keywords: Collateral Requirement,Cost of Credit,Enterprise and Financial Performance

1. Introduction

This paper seeks to investigate the influence of cost of capital on the performance of SMEs in Juba County of South Sudan. SMEs in South Sudan have been identified as playing a momentous part in building competent entrepreneurs as well as the country as a whole (Akoy, 2019; Deng, 2019). Tax money is responsible for the country's economy, the well-being of its people, and the progress of South Sudan cities. According to research by Garwang (2020), without access to loans, small and micro-enterprises are unable to purchase or absorb new technology, grow to strive in international markets, or even create commercial alliances with larger corporations. Borrowing is a critical source of capital for the vast majority of SMEs. According to Akoy (2019), SMEs in South Sudan regularly claim a lack of credit. Credit access terms are applied to present themselves in a variety of ways in South Sudan, where the lack of a developed capital market requires businesses to rely on equity or borrowing from friends or family. As a result, the influence of a firm's cost of credit accessed by SMEs on its fianancial performance is the focus of this paper.

According to Mawejje (2020), the SME sector accounts for 18% of South Sudan's GDP and employs 60% of the workforce. South Sudan's small businesses experience financial restraints as a result of their inability to acquire financing, stifling their growth and plummeting their capacity to fuel the domestic economy largely due to the cost of borrowing that has escalated over time.

Notwithstanding the prominence of SMEs in the economy of South Sudan, financial institutions were unable to lend to small enterprises which was the primary cause of stalled growth among small-sized firms in South Sudan.

Cost of Credit and Financial Performance

Profit is the driving force behind any SME's financial progress. The cost of credit on the financial performance of small and medium-sized businesses in Juba County, South Sudan, was investigated. When the cost of operating capital is much lower, more profit is made. In Mexico, a recent study found that the cost of credit hurts the financial performance of small and medium-sized businesses (Bakhtiari, Breunig, Magnani& Zhang, 2020). Likewise, high-interest rates on loans issued by financial institutions were found to have a negative influence on business earnings among youth-owned SMEs in Japan (Tala, 2021). SMEs, unlike large businesses, suffer higher interest rates on loans from financial institutions, as well as greater limitations, because they are seen as riskier and loan defaulters, and so their access to credit is limited. Loans to SMEs sometimes, as posited by Madi (2021) come with high-interest rates, high transaction costs, and short repayment terms (less than a year) in developing nations like Libya. This concept demonstrates the financial institutions' desire to prevent small businesses from getting loans (Ahmad &Atniesha, 2018). A higher interest rate is usually reserved primarily for small businesses that can demonstrate a strong track record of financial responsibility. A study conducted in Machakos County by Mutinda (2020) in Kenya looked at the effect of the credit cost charged on the financial growth of women entrepreneurs. According to the report, the cost of financing had a significant bearing on the financial performance of these small and medium-sized businesses sponsored by women. Babu (2017) while conducting research in KiambuCounty, Kenya, on SMEs to determine what factors affect their ability to secure financing, it was unearthed that, SMEs had difficulty getting financing because of high-interest rates and short repayment terms on loans. According to the findings from a study by Ngumbi, Waweru& Rita (2020) in Meru town, Kenya, the cost of a loan held a statistically significant bearing on the financial performance of the participants. Every loan to a Tanzanian SME had a loan processing fee of more than 30% of the total loan amount, and this was an expense that the borrower typically had to pay in advance as deposit assets (Sansa, 2019). South Sudan has a dearth of research on loan costs and financial performance. Studies have shown commercial lenders in South Sudan have exorbitant interest rates, transaction costs and fees that force SMEs from applying for commercial bank loans (Tenoy, 2021). In South Sudan, high transaction costs not only increase borrowing costs but can also hinder specific borrower groups' access to external credit. Most of South Sudan's youth entrepreneurs had difficulty getting access to credit because of the enormous cost of credit, which includes high loan processing fees, legal fees, interest rates, and costs of credit insurance, as posited by (Dube & Dube, 2016).

This research utilized a descriptive research approach. Chandra (2020) describes a descriptive research design as a collection of techniques and procedures that elucidate the variables being studied. Employing this approach allowed the study to make broader inferences applicable to the entire observed population (Schreier, 2018). This stems from the fact that the survey methodology facilitated the extraction of information regarding participants' perspectives, stances, actions, and principles concerning the subject of investigation (Evans &Mathur, 2018; Siegrist, 2021).

2. Findings, Analysis, and Presentation

Cost of Credit

Using a rating system spanning from 1 to 5, this study sought to evaluate the extent to which finance costs affected the financial outcomes of SMEs. The results revealed that a notable segment of the participants (45.6%) shared the perspective that finance costs wielded a markedly significant influence on financial performance. In parallel, 33.0% of respondents expressed that finance costs had a notably substantial impact on financial performance.

Those recognizing a moderately influential impact of finance costs on financial performance represented 14.5%. The table below discloses that a minority of respondents, specifically 6.9%, maintained the viewpoint that the finance costs had only a minor impact on financial performance.

Cost of Credit

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Little Extent	22	6.9	6.9	6.9
	Moderate Extent	46	14.5	14.5	21.4
	Great Extent	105	33.0	33.0	54.4
	Very Great Extent	145	45.6	45.6	100.0
	Total	318	100.0	100.0	

Descriptive Statistics

The research examined how different factors related to obtaining credit can impact the financial outcomes of small and medium-sized enterprises . These factors encompassed conditions such as collateral prerequisites, credit expenses, credit scores, and the assigned credit threshold. Descriptive statistics for the study were presented using both means and standard deviations.

Financial Performance of SMEs

The research was conducted with the intention of assessing the economic accomplishments of small and medium-sized enterprises situated within Juba County. The survey utilized a Likert scale containing five levels, enabling respondents to opt for different alternatives to express their perspectives. From the results, it was established that access to credit has increased the monthly profit of most SMEs with a mean of 4.75 and that the employee's productivity had improved hence increasing enterprise performance (4.74). Moreover, the respondents strongly agreed that the businesses had expanded and grown in size and operations due to favourable terms of credit as evidenced by a mean of 4.53 and that the SME working capital has increased due to credit accessibility from banks (4.50). It was also established that the terms applied to credit access have greatly affected the SME's profits with a mean of 4.19 and that the asset base of most of the SME enterprises has grown due to credit access with a mean of 4.18.

Effect of Cost of Credit on Financial Performance

The analysis revealed a high statistical significance. The results indicated that most participants had a strong agreement that the loan repayment period affected the sales growth of their businesses with a mean value of 4.47 and that the high-interest rates imposed on their SMEs limited their ability to access credit (4.43). Further, the study established that rates of interest influenced growth in business sales substantially and this is evidenced by a mean of 4.41. Moreover, it was found that rates of interest influenced the profitability of the SMEs negatively (4.35) and that bank interest rates affected negatively the financial growth of the enterprises (4.31). Additionally, it was unravelled that the presence of low-interest rates encourages SME owners to apply for a bank loan with a mean of 4.30 and that the flexibility of the loan repayment affects loan amounts and loan terms eventually given by the financial institutions (4.28).

These findings provide strong evidence that high costs of credit hinder the growth and profitability of SMEs, as they often struggle to access affordable financing as such, addressing the issue of high credit costs and improving access to affordable financing is crucial for enhancing the financial performance and viability of SMEs in Juba County, South Sudan.

3. Conclusion

This paper arrives at the determination that credit costs encompassing factors such as interest rates, transaction expenses, penalty charges, and loan processing fees, significantly affect the financial outcomes of SMEs within Juba County. Further, the research concludes that high-interest rates and transaction costs increase the overall cost of borrowing, reducing the profitability of the SMEs and limiting their ability to invest in growth opportunities. Additionally, a conclusion is made that penalty fees for late payments or defaults lead to additional financial burden, further straining the cash flow of SMEs and that the presence of loan processing fees adds expense to the borrowing process, making it more challenging for SMEs in Juba county to access necessary funds for expansion or operational needs. Therefore, the high cost of credit acts as a barrier for SMEs, hindering their financial performance, limiting their growth potential, and potentially increasing their vulnerability to financial instability. The financial performance of the SMEs is, therefore, adversely affected by cost of credit, leading to reduced profitability, and potential liquidity issues.

4. Recommendations

Cost of Credit

This study recommends that SMEs in Juba County should work towards improving their creditworthiness. By doing this, they would stand a sound ground to negotiate better terms with financial institutions. To achieve this, the SMEs should focus on building a strong credit history, maintaining a good payment record with suppliers, and improving financial ratios such as debt-to-equity and current ratio.

Further, this study also recommends that SMEs should conduct thorough loan analysis. As such, before accepting a loan offer from any financial institution, they should carefully evaluate the terms and conditions, including interest rates, transaction costs, penalty fees, and loan processing fees. Comparing multiple loan offers and negotiating with lenders can help SMEs secure more favourable terms hence reducing the cost of credit.

This study also recommends that lenders should offer customized loan products. In this regard, financial institutions should develop loan products specifically designed for SMEs, taking into account their unique characteristics and needs. These products can offer more flexible terms, lower interest rates, and reduced transaction costs compared to generic loan offerings. This will have an ultimate positive impact on the financial performance of these firms.

Finally, this study recommends that policymakers should facilitate access to credit information on SMEs in Juba County. As such, they should establish robust credit reporting systems that provide comprehensive and accurate credit information on SMEs. This enables lenders to make more informed credit decisions, reducing the information asymmetry that often leads to higher credit costs. Policies should also encourage SMEs to maintain good credit records and provide mechanisms for dispute resolution.

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