THE EFFECT OF INTEREST RATES ON FINANCIAL PERFORMANCE OF PRIDE MICROFINANCE

A CASE OF PRIDE MICROFINANCE NATEETE BRANCH

By

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DECLARATION

I NANKUNDA HARRIET do declare that the work provided in this book is of my original work and has never submitted to any higher institution of learning for the award of any academic qualification

Signature ……………………………………..

Date …………./……………/…………………

APPROVAL

This is to certify that the research report was under my supervision and is now ready for submission.

SUPERVISOR'S NAME:

Signature

…………………………………………………..

Date

…………………………………………………….

DEDICATION

I dedicate my report work to my family members which includes my mother, Sisters and Brothers, and many more relatives not mentioned for their financial and other forms of support they have rendered to me.

My parents, thank you for giving me a chance to prove and improve myself through all my walks of life please do not ever change, A special feeling of gratitude to my loving Mother, your words of encouragement and push for tenacity ring in my ears.

ACKNOWLEDGEMENT

I thank the Almighty God the most gracious for the gift of life, wisdom, energy and knowledge he has given me throughout the entire exercise of compiling this research. May all attributes belong to him.

I wish to acknowledge the following for their assistance and support in ensuring that this project is complete. My supervisor for her timely professional guidance and support throughout this dissertation.

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ABSTRACT

The study was conducted on the effect of interest rates on financial performance of micro finance institutions using pride micro finance Nateete branch.

It was later guided by the following objectives; to examine the factors determining the financial performance of pride microfinance, to find out the Challenges faced by pride microfinance in Uganda, to establish the relationship between interest rates and financial performance of pride microfinance

The study was conducted in Pride Microfinance Nateete branch which is located within Nateete town along Kampala Masaka road, 5km away from Kampala city Centre. The study therefore used descriptive research design when collecting data and information from the respondents because it helped to describe the characteristics of population, the study also adopted a correlation research design which is the type of non-experimental research where the researcher employs the data derived from pre-existing variables,

The study used a total sample of 52 respondents from different departments of Pride Microfinance Nateete Branch that were selected from different departments such as accounts and finance department, procurement and logistics department, physical planning departments and others. Customers will also be included in the sample size.

From the researcher's findings and point of view it can be concluded that to a larger extent interests rates has a greater impact on the financial performance of pride microfinance since it was revealed that interest rates increases the profits realized by the financial institutions. Interest rate as the independent variable was linearly regressed with the dependent variable financial performance. The findings reveals that there is a positive relationship between interest rates and financial performance for both Market rate of return and return on equity when all firms are considered together. However, the relationship was not considered significant. On disaggregation of

The researcher recommends that the government should increase their efforts in encouraging microfinance banks and institutions to support the small businesses.

CHAPTER ONE

GENERAL INTRODUCTION

1.0 Introduction

This chapter presents the background of the study, statement of the problem, research objectives, research questions, scope of the study, and significance of the study.

1.1 Background of the study

One of the major roles of financial institutions is to advance credit facilities to their customers at a specified interest rate. Indeed, the primary source of revenues for financial institutions such as commercial banks, Saving and Credit Cooperatives (SACCOs), microfinance banks (MFBs) and microfinance institutions (MFIs) is the interest they charge on the loans they lend their customers. MFIs ordinarily thrive on the interest they charge borrowers; a fact that underpins the importance of the subject of interest rates to these firms. However, the interest rates are capped by specific regulations. Usury laws and restrictions on interest rates could affect the operations of MFIs (Avgouleas, 2007). The afore stated laws are put in place purposely to protect customers from MFIs by placing a ceiling above which interest rates should not be charged. This, however, is argued could negate the financial performance and viability of MFIs (Delfiner, Pailhe & Peron, 2006).

Gashaw (2014) analyzed MFIS in Ethiopia, Uganda and Kenya in regard to loan outreach to the poor and the quest for financial viability. The author notes that the concern of enhancing financial inclusion to the poor is exceedingly relevant to developing countries that go for right policies towards financial inclusion. However, it is acknowledged that even the microfinance sector faces challenges in its strife to reach the wider poor. Statistics indicate that regarding microfinance operations, Kenya and Uganda are ranked first and second respectively in Africa and fifth and eighth in the world in that order. Ethiopia is also fast emerging though it lies outside of the ranking (EIU, 2013). In spite of this feat in microfinance in the aforestated countries, Gashaw observes that, the credit accessibility falls short of the escalating demand.

According to Lloyd (2006) and McConnell (2009), interest rates are a price paid for borrowing funds expressed as a percentage per year. According to Atieno (2011), there has been a challenge to credit accessibility in the country which is blamed on supply-side constraints, that is, the financial institutions. The author observes that, the MFIs emerged purposely to address the foregoing problem by targeting the hitherto unbanked population growing in leaps and bounds since the 1980s, their capacity to grow has significantly been affected by their failure to operate within legal provisions (Republic of Kenya, 2005). The major challenge to their financial growth has been high default rates. Notably, MFIs in Kenya have over the time been witnessing high levels of non-performing loans which are, needless to say, occasioned by high default rates. The foregoing trend is a threat to their financial performance and very existence (Moti, Masinde, Mugenda & Sindani, 2012).

According to AMFU (2010), evidence indicates that interest rates in some leading MFIs in Uganda have been falling from about 5% a month prior to 2000 to around 3% a month currently and some are shifting from a flat rate to declining balance as a basis for charges and improving the lending terms. However SMEs are still uncomfortable with such credit extended to them (Sendawula, 2002) despite the improved interest rates and terms. Key issues may be that SMEs over-borrow from more than one MFI and at time beyond their ability to repay. This creates lack of adequate financial resources to meet their working capital needs and at times affects the relationship with the MFIs due to contribute over 30% of GDP, over 30% of employment and over 80% of manufactured output (Byaruhanga, 2005; Katto, 2008), there is therefore need to investigate whether there is a relationship between the MFI credit accessibility in relation to interest rates in Uganda taking on a number of selected MFI institutions in Kampala district, Makindye division through eyes of pride microfinance.

Pandey (2010) in a study on financial management in India opined that MFIs and other financial institutions are required to develop a credit policy to govern their operations. In the same light, the author noted that, given that MFIs obtain their revenue from interest accruing from advancing credit facilities to low income persons, the loan repayment may be uncertain. In the same respect, Ditcher (2003) advised that the success of lending out finances is based on an extensive appraisal of the risk of extending such facilities and also the characteristics of the borrower. Yet, it is lamented that lending decisions by these financial institutions are more often than not based on the subjective feelings regarding risk in relation to repayment by the borrower. The MFIs' justification of employing this appraisal is that it is both simple and inexpensive (Horne, 2007).

Pride micro finance limited (PMFL) is a micro finance deposit-taking institution (MDI) in Uganda. It is licensed by bank of Uganda, the central bank and national banking regulator. The headquarters of PMFL are located in Victoria Business Park, in Bukoto, a northeastern neighborhood in Nakawa division, an administrative area with in Kampala, Uganda's capital and largest city. It provides financial services to that segment of the Ugandan population who were not served or are unable to access financial services through the Ugandan commercial banks thus making it an ideal case study for the investigation

1.2 Problem statement

Interest rates are ordinarily the drivers of financial institutions' financial performance. They are the ones that determine the size of the profit margin for every transaction between a financial institution and its customers (Kim 2013). Yet, there are many reported cases of defaults in loan repayment in MFIs. Presumptively, the interest rates partly contribute towards this. When borrowers default in repaying the credit facilities advanced to them, the MFI concerned will be negatively affected.

There will be limited finances to run its operations and also to loan out to other potential borrowers. In the event the challenge of non-repayment persists for long, the firm will have huge bad debts; a situation that is likely to result in downsizing its workforce, stall its market expansion, and ultimately collapse (Kenedy 2010). The MFIs play a huge role in enhancing accessibility of financial services especially to the poor and low-income earners in the society. This implies that any challenges affecting these institutions are bound to have far reaching impact on the society and the country's economy at large. The foregoing explains why this study was necessary to be conducted with the aim of examining the extent to which interest rates charged by MFIs affect their loan performance.

Therefore this study seeks to investigate the effects of interest rates on the growth and development of micro finance institution using a case study of Pride Microfinance Nateete branch.

1.3 Objectives of the study

1.3.1 General objective

The main objective of the study will be to assess the effects of interest rates on the growth and development of micro finance institutions in Uganda.

1.3.2 Specific objectives

1. To examine the factors determining the financial performance of pride microfinance
2. To find out the Challenges faced by pride microfinance in Uganda
3. To establish the relationship between interest rates and financial performance of pride microfinance

1.4 Research questions

1. What are the factors determining the financial performance of pride microfinance?
2. What are the Challenges faced by pride microfinance in Uganda?
3. What are the relationship between interest rates and financial performance of pride microfinance?

1.5 Scope of the study

Geographical scope

The study was conducted in Pride Microfinance Nateete branch which is located within Nateete town along Kampala Masaka road, 5km away from Kampala city Centre.

Time scope

This research covered the period of three years thus from 2016 to 2019. This period was enough for the researcher to find out the contribution of interest rates to micro finance growth and development.

Content scope

The study sought to investigate the factors determining the performance of pride microfinance, challenges faced by pride microfinance in Uganda and relationship between interest rates and performance of pride microfinance.

1.6 Significance of the study

The findings of the study may be of practical significance to different stake holders and Enumerated below;

The study may help the researcher to achieve her bachelor's degree.

To the academicians, the findings and conclusions may add to the existing literature in higher institutions of learning in view of the credit terms and performance of the MFIs and this may act as a source of reference to those who may wish to undertake further investigations.

The study may portray the challenges faced by microfinance institutions in Uganda, this will help the managers of MFIs to design and adopt different strategies to overcome the challenges affecting development of MFIs.

The result may go a long way to help the MFI loan officers to analyze their borrowers, supervise the credit and repayment that will make them maintain their customers as well as the business sustain ability and the sustainability of the MFI.

The study may be of importance in showing the factors determining the growth and financial development of microfinance institutions.

1.7 Definition of key terms

Crowley (2007) defined interest rate as money borrower pays for the use of money they borrow from a lender/financial institutions or fee paid on borrowed assets.

According to Lloyd (2006) and McConnell (2009), interest rates are a price paid for borrowing funds expressed as a percentage per year.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter presents a review of related literature that has been written by other Researchers and Authors in line with interest rates and development of MFIs. It will further portray show challenges faced by microfinance institutions, relationship between interest rates and Micro finance development.

2.1 Interest Rates

Crowley (2007) defined interest rate as money borrower pays for the use of money they borrow from a lender/financial institutions or fee paid on borrowed assets. Fisher (1930) considered interest rate as the price of money and the link between income and capital. He defined interest rate as the price of money or the “per cent of premium paid on money at one date in terms of money to be in hand one year later”. Therefore, interest on loans is the price the lender charges the borrower for using the borrowed funds.

According to Lloyd (2006) and McConnell (2009), interest rates are a price paid for borrowing funds expressed as a percentage per year. It can also be defined as the price a borrower needs to pay to the lender for transferring purchasing power to the future. Lloyd (2016) continues to argue that interest rates rank among the most crucial variables with macroeconomic word in the world of Finance.

In their study, Gardner and Cooperman (2005) found out that interest rates represent the cost of borrowing capital for a given period of time. Price changes are anticipated in the real world and these expectations are part of the process that determines interest rates.

Keynes (2016) indicates that rate of interest represent the cost of borrowing capital for given period of time, given that borrowing is a significant source of finance for the firms, interest rate are of great importance to them since it greatly affects their income and by extension their operations. According to Cargill (2011), interest rates for lending and other financial intermediaries represent both a composition for the loss in value of the loaned capital arising mainly from inflation as well as profit margin to compensate the lender for the default risk he exposes himself to during the loan period.

Saunder (2015) asserts that interest rates influence the overall economic activity including the flow of goods, services and financial assets within the economy and as well as the whole world. He points out that interest rates relates to the present value to the future value of money. A high interest rate leads to a high discount rate thus the present value of money. On the other hand, a low interest rate leads to a future cash flow at a lower discount rate.

Reilly (2019) noted that interest rates including those for the deposit taking microfinance institution are determined by three main factors: inflation, level of government borrowing and risk involved. He further found out that inflation sets the floor for the interest rate.

According to a study by Bernstein (2016), developing countries have liberalized interest rates by allowing the markets forces to determine interest rates. Hence uncompetitive banking systems, inadequate regulatory framework and borrowers that are insensitive to interest rates undermine the efficiency of market based credit allocation and disrupt the transmission of monetary signals with adverse consequences for macroeconomic policy.

In her study, Naude (2015) found out that interest rates were maintained below the market rates and direct control of credit was the primary monetary control instrument of the authorities. The Kenyan government adopted the CBK amendment Act (the Donde Act) in 2001. The act allows CBK to regulate interest rates. Interest rate influences the overall level of economic activity, flow of goods and services and financial assets within the economy. It is believed that fluctuations of market interest rates exert significant influence on the performance of commercial banks. According to Samuelson (2015), under general conditions, financial institutions' profits increase with rising interest rates. He argued that the banking system as a whole is immeasurably helped rather than hindered by an increase in interest rates. Interest rates are set by the Monetary Policy Committee (MPC) of the Central Bank of Kenya and are used to control inflation. MPC maintained CBR at 18% in 2013 implying that Commercial banks and DTMs charged loans in excess of this rate (CBK Annual Report, 2012/2013).

2.2 Financial Performance of MFIs

Financial performance is an indicator of how profitable a company is relative to its total assets. It is measured by return on asset (Nduati, 2013). There has been a wide variety of definitions of firm performance that have been proposed in the literature. Performance is the ability to sustain income stability and growth. A profitable banking sector is better able to withstand negative shocks and contribute to the stability of the financial systems. The overall financial performance of the Banking industry in Kenya in the last two decades has been improving. However, this doesn't mean that all players in the industry are profitable; there are those that are declaring losses (Oloo, 2009). This does not leave out the Microfinance Institutions. Over the past two decades, institutions that make microloans to low-income borrowers in developing and transition economies have focused increasingly on making their lending operations financially sustainable by charging interest rates that are high enough to cover mall their costs. They argue that doing so will best ensure the permanence and expansion of the services they provide (Rosenberg et al, 2009). Profit is the ultimate goal of these micro finance institutions. However, this does not mean that MFIs have no other goals. They could also have additional social and economic goals.

To measure the profitability of DTMs there are variety of ratios used of which Return on Asset, Return on Equity and Net Margin are the major ones (Murthy and Sree, 2013). Financial measures are expressed in monetary units. The techniques widely used for analytical purposes include; ratio analysis, trend analysis and cross sectional analysis. A ratio is a mathematical expression of an amount in terms of another. Chandra, (2005) noted that ratio analysis gives an objective picture of a company's financial performance because ratios eliminate the size effect. Two different firms whose sizes differ can be compared.

According to Winfield and Curry (2014), computation of financial ratios can be grouped into five broad categories namely; liquidity, leverage, turnover, profitability and valuation ratios. Analysis and assessment of MFIs financial performance calls for the use of various financial ratios. Profitability, Economic efficiency, Operational efficiency, cost of operation, asset quality and size was used to analyze financial performance in this study. Profitability ratios were used to analyze financial performance of MFIs in Kenya.

Profitability ratios consist of tests used to evaluate a firms earning performance. The major types of profitability ratios are calculated in relation to sales and investments. Profitability in relation to sales ratios includes; gross profit margin, net profit margin, contribution ratio, operating expenses ratio while profitability in relation to investments includes; return on investments (ROI), return on equity (ROE) and return on total assets.

Robinson (2015) asserts that the potential impact of interest rates on Commercial Banks financial performance has long been a concern for policy makers and bankers. Banks and to the extension Micro finance institutions earnings are therefore affected by unanticipated changes in interest rates. The exposure of banks profitability and net worth to unanticipated changes in interest rates is what is meant by the term interest rates risk.

MFIs are facing a double challenge: they have to provide both financial services to the poor and also cover their costs in order to avoid bankruptcy (sustainability). Hence to assess MFIs performance both dimensions must be taken into account (Meyer, 2010).

2.3 Challenges faced by Pride Microfinance

According to Nwanyawu (2012), the following are some of the issues faced by microfinance institutions.

Diversion of Micro Finance Fund: There have been several cases of corrupt public officials, diverting credit meant for small scale farmers. It could be seen that because of the high level of poverty in the country, loans are diverted into solving problem of feeding. Thus, micro finance is supposed to meet the need of the poor to raising their financial sustainability, which in this case is not so (Brock, 2013).

Inadequate finance: One of the critical problems facing microfinance institutions in Nigeria is the lack of finance needed to expand financial services to clients Nwanyawu (2012). This primarily arises from low capital base of the institution, inordinate fixed asset acquisition, ostentatious operational disposition, inability to mobilize deposits, poor lending and questionable governance and management arrangement.

Unfavorable/Frequent Changes in Government Policies: Instability has impacted negatively on the performance of primary institutions responsible for policy monitoring and implementation. There were cases of sudden reversal of policy which has resulted to incomplete and abandoned projects. This creates distortions in the macro-economic structure and low productivity.

High Risk and Mounting Loan Losses: According to Anyanwu (2012), about 70% of micro credits given to micro enterprises via government microfinance scheme were not recovered. Some people see the loans as their own share of the national cake and do not see any need for the repayment. The consequence of this is that it leads to other applicants not getting loan.

Low Capacity and low Technical Skills on Micro financing: Management of micro finance institutions would require a pedigree of knowledge on micro financing to successfully operate in the industry; however, most staff recruited in the microfinance institutions, particularly at management level, have little or no experience in microfinance practice Nwanyawu (2012).

2.4 Effect of Lending Interest Rates on Performance of MFIs

The level of interest rates charged by Commercial Banks and other financial institutions in Kenya has remained high and has faced a lot of criticism from time to time. Despite the efforts by the Government to bring it down they have still remained high. These high interest rates are against the regulation in the current finance bill which proposes that interest rates should be pegged against the Treasury bill/maximum interest rate that a bank or any financial institution may charge for a loan or monetary advance (Ngugi, 2014).

Finance Bill (2011) bill states that no interest rate should exceed four percent of the base lending rate of the central bank. This however may not be applicable if the financial institution that is making losses. Since these rates can be justified by high transaction costs and risks associated with micro lending, it is often difficult to differentiate between sustainability, profitability and greed (Fernando, 2016). This is because lending to the poor and so the MFIs has to make much more money as possible up front to cover the cost of the loan due to the assumed high likelihood that the borrower will default at some point. CBK has also come up with a bench mark lending rate which commercial Banks and DTMs are supposed to comply with in their lending.

The impact of interest rate on bank's profits operates via two main channels of the revenues side. First, a rise in interest rate scales up the amount of income a bank earns on new assets it acquires. But, the speed of revenue adjustment will be a function of speed of interest rate adjustment. Second, the effect hinges on the amount of loans and securities held (Were and Wambua, 2013).

A rise in interest rates is good for MFIs due to higher returns on new investments, increased profit margins on loans. As a result of this i.e. increase in interest rates which lead to good financial performance of the financial institution sends signal of good returns in the form of dividends. Interest on loans is behind a banks dismal profitability (Njihia, 2005).

2.5 Relationship between interest rates and financial performance

When the central bank increases the base rate, banks increase the rates that they charge to their customers to borrow money. Individuals are affected through increase in credit card and mortgage interest rates, especially if they carry a variable interest rate. This has the effect of decreasing the amount of money consumers can spend, save or invest. People will have to pay bills, and when those bills become more expensive, households are left with less disposable income. This means that people will spend less discretionary money, which will affect business revenues and profits (Ndung'u, 2003).

Prevailing interest rates affects the financial performance of firms as was observed in the research by Wolfgang and Opfer (2003) when they compared the financial performance of financial institutions and five other industries and found out that financial institutions have a greater sensitivity to changes in long term interest rates.

Fama and French in their 1998 test for the effect of debt in the firm's capital structure find that the coefficient on the interest expense variable has a negative sign, this indicates that interest negatively affects the financial performance of a firm which contradicts the prediction of MM's second proposition thus concluding that value of a levered firm is actually less than that of unlevered firm.

A rise in the interest rates affects the valuation of stocks. The rise in the value of stocks raises the expectations of the market participants, who demand better returns to commensurate with the increased returns on bonds (Musa, 2011). The seminal works of McKinnon (1973) and Shaw (1973) argue that high real interest rates tend to encourage savings whilst savings determine investment. Interest rate liberalization and low inflation can therefore promote capital accumulation and economic growth in less developed countries. Interest rate liberalization was introduced in Kenya in 1992 with the objective of keeping the general level of interest rates positive in real terms in order to encourage savings and to contribute to the maintenance of financial stability; to allow greater flexibility and encourage greater competition among the banks and non-bank financial institutions to enhance efficient allocation of resources, to reduce the differential to maximize lending for banks and non-bank financial institutions. With liberalization, the interest rate policy aimed to harmonize the competitiveness among the commercial banks and NBFIs by removing the differential that had existed for maximum lending rates to allow greater flexibility and encourage greater competition in interest rate determination so that the needs of both borrowers and lenders could be better met through the cooperation of market forces and to maintain the general positive levels of interest rates in real terms in order to encourage the mobilization of savings and contribute to the maintenance of financial stability (Kithinji, 2012)

Different researchers have observed varied relationships between interest rates and financial performance of a firm. Some have argued that high interest rates are likely to curb business investments and innovation. Rising interest rates could also increase loan defaults in the banking system and bank vulnerability, drive the cost push inflation due to medium term increase in prices associated with higher costs of business financing and affect business revenues and profits negatively. The effects of interest rates on the financial performance of a firm may differ depending on diverse factors such as the amount of debt in the firm's capital structure, the sector of theeconomy in which the firm operates and the rate at which a firm acquires its debt capital.

2.6 Factors for growth and development of MFIs

The performance of an MFI is influenced by various factors such as lending interest rates, leverage, size of the firm, economic growth and risk.

Lending Interest Rate

A higher percentage of revenues generated by MFIs come from interest income on lending. This means MFIs with quality loan portfolios tend to have a positive growth. Many investors prefer investing in MFIs with a positive growth since they are assured return on their investment (Fernando, 2006). According to Saunder (2015) lending interest rates influence the overall economic activity including the flow of goods, services and financial assets within the economy and as well as the whole world. He points out that interest rates relates to the present value to the future value of money.

Leverage

Leverage also has an influence on firms' performance. According to Stiroh (2008), entities with higher profit ratesp will remain low leveraged because of their ability to finance their own sources. On the other hand, a high degree of leverage increases the risk of bankruptcy of companies. Total assets are considered to positively influence the company's financial performance, assets greater meaning less risk (Barton and Gordon, 2017).

Size of the Firm

The size of the company can have a positive effect on financial performance because larger firms can use this advantage to get some financial benefits in business relations. Large companies have easier access to the most important factors of production, including human resources. Also, large organizations often get cheaper funding (Akhigbe and McNulty, 2005). Also, large organizations are able to get cheaper source of funds to enable them to be competitive. Such funds however, come with conditions which can be easily met by large organizations (Morgan and Samolyk, 2009).

Risk and Economic Growth

Risk and growth are two other important factors influencing a firm's financial performance. Since market value is conditioned by the company's results, the level of risk exposure can cause changes in its market value. Economic growth is another component that helps to achieve a better position on the financial markets, because market value also takes into consideration expected future profits (Bekan, 2011). Since market value is conditioned by the company's results, the level of risk exposure can cause changes in its market value and thereby how it is perceived in the market (Montgomery, 2008).

2.7 Summary of Literature Review

The studies done so far in this area have focused mainly on the relationship between interest rates and financial performance and development of the commercial banking sector as indicated by Wensheng (2002), Boldbaatar (2006) and Njihia (2005). From the overview of these studies, it is apparent more light needs to be shed in this area of research by widening the scope of the study to concentrate on MFIs. It is thus imperative that the gaps be filled hence the study set to answer the following questions. What is the relationship between interest rates on growth and development of Microfinance institutions?

CHAPTER THREE

METHODOLOGY

3.0 Introduction

This chapter explains details of how the study was conducted. It presents the research design, study population, sampling procedures and sample size, data collection methods and instruments, data analysis and processing, and the limitations of the study.

3.1 Research Design

Creswell (2003) defines a research design as the scheme, outline or plan that is used to generate answers to research problems. The study therefore used descriptive research design when collecting data and information from the respondents because it helped to describe the characteristics of population, the study also adopted a correlation research design which is the type of non-experimental research where the researcher employs the data derived from pre-existing variables, this was used since the study involves to investigate the relationship between interest rate and performance of pride micro finance Nateete branch. The study was also be both qualitative and quantitative research.

3.2 Study Population

A population is a complete set of individuals, cases or objects sharing some common characteristics from which a study sample is taken for the purpose of data collection (Mugenda, 1999). In this research, the total population of the study constituted to 60 respondents and these were from different departments of Pride Microfinance Nateete Branch such as Human resource department, administration department, accounts and finance department, procurement and logistics department. Customers were also included in the study population.

3.3 Sample Size

According to Krejcie & Morgan (1970), the study used a total sample of 52 respondents from different departments of Pride Microfinance Nateete Branch that were selected from different departments such as accounts and finance department, procurement and logistics department, physical planning departments and others. Customers will also be included in the sample size.

Table 3.1 showing the sample size and total population of the study

Respondents	**Total population**	**Sample size**
Loan department	10	9
Tellers	10	9
Human resource and administration	8	6
Accounts and finance	7	6
Procurement And Logistics	5	3
Customers	18	17
Total	**60**	**52**

3.4 Sampling Technique

According to Matthew (2012), sampling is the process of selecting a number of people or objects from a population such that the selected group contains elements representative of the characteristics found in the entire group. According to Adam Hayes (2019) Stratified random sampling method is a method of sampling that involves the division of the population into smaller sub groups known as strata, it was used to obtain appropriate data for the research, respondents was grouped into strata that was later be randomly selected to get sample size required and this ensured that each and every member of the population under consideration has an equal chance of being selected. The method rules out bias, simple to use, cheap and flexible to the researcher and does not have bias.

3.5 Data sources

Data was got from both primary and secondary sources.

3.5.1 Primary data

According to drew (1980) Primary data are information collected by researcher specifically for research assignment. Primary data involved direct extraction of information from the respondents using self-administered questionnaires and interview guide.

3.5.2 Secondary data

According to Oschman (2009) Secondary data are data collected by a party not related to the research study that collected these data for some other purpose and at different time in the past, Secondary data was collected from journals, text books, management reports, previous dissertations and internet. These sources will help derive meaningful interpretation of findings.

3.6 Methods of data collection and instruments

Administered interviews were given to a selected sample of the MFIs staff. Questionnaires ensured increased response rate due to their clarity and simplicity. The study collected data from a cross-section of respondents using a combination of study instruments and these included;

3.6.1 Interview method

The interview method was employed to collect data from banking officials in the loan department. It was preferred basing on the fact that most of the administrators are usually more respective to detailed discussions especially when conducted at their workplaces. The face-to-face interviews certainly allowed in-depth investigation. An interview format was designed to guide the interviews and as a tool that ensured consistency in the interview process.

3.6.1 Questionnaires

A questionnaire is a predetermined written set of questions used to obtain data from the respondents by having the responses in writing. The researcher used questionnaires in order to gather quantitative data from both categories of respondents. Questionnaires were preferred in the study because they are a convenient method since respondents give their responses independently and secretly.

3.7 Data Analysis

Data from the field were carefully classified, edited, basing on clarity, completeness, accuracy and consistence to ensure reliability. Data analysis was based on the objectives of the study and done by use of Statistical Package for Social Sciences on collected data to draw meaningful interpretation and conclusion to give findings and suggestions.

3.8 Ethical Considerations

Ethics in this study was adhered to by the following processes;

The researcher attained an introductory letter from the university to be used for accessing different targeted respondents.

The researcher observed and respected the privacy, confidentiality and anonymity of all the participants and respondents in this study.

The researcher also avoided plagiarism; this is where she acknowledged the works of other scholars and other researchers.

3.9 Limitations of the study

The following might be the limitations to this study;

i. High costs to cover all the research requirements.
ii. Inconsistencies in information given by different respondents.
iii. Difficulty in data sourcing; the researcher may find difficulty in getting the right information from the selected population.
iv. Problems in coding and data analysis.

CHAPTER FOUR

ANALYSIS, PRESENTATION AND INTERPRETATION OF RESEARCH FINDINGS

4.0 Introduction

This chapter presents and discusses the implications of the results of the findings. The findings are presented in a table format, which was later analyzed using frequencies and percentages.

4.1 Findings on the demographic characteristics

4.1.1 Findings on the gender of respondents.

Table 4.1: Showing the gender of the respondents

Sex	Frequency	Percentage
Male	31	60
Female	21	40
Total	52	100

Source: Primary data 2019

From the 52 questionnaires that were distributed to employees of Pride Microfinance Nateete branch, all of them were answered and findings show that 60% of the total respondents were male and 40% of the total respondents were females. This implies that pride micro finance employees more of males than females.

4.1.2 Findings on the age range of respondents.

Table 4.2: Showing the age range of the respondents

Age in years	Frequency	Percentage
Below 27yrs	18	35
27-38yrs	22	42
Above 38yrs	12	23
Total	**52**	**100**

Source: Primary data 2019

From table 4.2 results revealed that 35% of the total respondents were below 35 years of age, 42% of the total respondents were between 27 to 38 years, 23% of the total respondents were above 38 years. This implies that most of the respondents were youths between 18 to 35 years.

4.1.3 Findings on the educational level of respondents.

Table 4.3: Showing the educational level of the respondents

Educational level	**Frequency**	**Percentage**
Secondary	5	10
Certificate	2	4
Diploma	12	23
Degree	33	63
Masters	-	-
Total	**52**	**100**

Source: Primary data 2019

Findings from table 4.3 shows that 10% of the respondents had stopped in secondary level, 4% of the total respondents were holding certificates, 23% of the total respondents were holding diplomas, 63% of the total respondents were holding bachelor's degree. This implies that most the respondents were educated which makes the finding to be relied on.

4.1 Findings on the forms of credit services provided by micro finance institutions

4.2.1 Findings on whether Pride Microfinance Nateete branch offers group lending as form of credit services

Table 4.4 showing findings on whether Pride Microfinance Nateete branch offers group lending as form of credit services

RESPONSE	**FREQUENCY**	**PERCENTAGES (%)**
Strongly agree	42	80
Agree	6	11.5
Not sure	4	8.5
Disagree	-	-
Strongly disagree	-	-
Total	**52**	**100**

Source; Primary Data 2019

Basing on the findings in the table above the results shows that 80% of the total respondents strongly agreed that Pride Microfinance Nateete branch offers group lending as form of credit services, 11.5% of the total respondents agreed that Pride Microfinance Nateete branch offers group lending as form of credit services, 8.5% of the respondents were not sure and this implies that Pride Microfinance Nateete branch offers group lending as form of credit services.

4.2.2 Findings on whether Pride Microfinance Nateete branch provides individual lending to its customers.

Table 4.5 showing findings on whether Pride Microfinance Nateete branch provides individual lending to its customers.

RESPONSE	FREQUENCY	PERCENTAGES (%)
Strongly agree	22	42
Agree	30	58
Not sure	-	-
Disagree	-	-
Strongly disagree	-	-
Total	**52**	**100**

Source; Primary Data 2019

Basing on the findings in the table 4.5 above, the results shows that 42% of the total respondents strongly agreed that Pride Microfinance Nateete branch provides individual lending to its customers, 58% of the total respondents agreed to the statement. This implies that Pride Microfinance Nateete branch provides individual lending to its customers.

4.3 Factors determining the financial performance of pride microfinance

Table 4.6 showing findings on Factors determining the financial performance of pride Microfinance.

Statement	Strongly agree	Agree	Not sure	Disagree	Strongly disagree	**Total**
Lending interest rates charged on loans	20(38%)	19(36%)	11(21%)	2(4%)	-	**52(100%)**
Size of the firm in terms of loan department	37(71%)	8(15%)	3(6%)	4(9%)	-	**52(100%)**
Economic growth and risk	18(35%)	4(9%)	17(33%)	9(17%)	2(4%)	**52(100%)**
The number of customers the bank has	4(9%)	32(60%)	15(29%)	-	1(2%)	**52(100%)**

Source; Primary Data 2019

Findings from table 4.6 shows that 20(38%) of the total respondents strongly agreed that Lending interest rates charged on loans determines financial performance of pride micro finance, 19(36%) of the total respondents strongly agreed, 1(21%) of the total respondents were not sure, 2(4%) of the total respondents disagreed.

Findings from table 4.6 shows that 37(71%) of the total respondents strongly agreed that Size of the firm in terms of loan department determines financial performance of pride micro finance, 8(15%) of the total respondents strongly agreed, 3(6%) of the total respondents were not sure, 4(9%) of the total respondents disagreed.

Findings from table 4.6 shows that 18(35%) of the total respondents strongly agreed that Economic growth and risk determines financial performance of pride micro finance, 4(9%) of the total respondents strongly agreed, 17(33%) of the total respondents were not sure, 9(17%) of the total respondents disagreed, 2(4%) of the total respondents strongly disagreed.

Findings from table 4.6 shows that 4(9%) of the total respondents strongly agreed that the number of customers the bank has determines financial performance of pride micro finance, 32(60%) of the total respondents strongly agreed, 15(29%) of the total respondents were not sure, 1(2%) of the total respondents disagreed.

4.4 Findings on the challenges faced by MFI that hinder economic empowerment of small scale business.

Table 4.7 showing findings the challenges faced by Pride Microfinance Nateete

Statement	Strongly agree	Agree	Not sure	Disagree	Strongly disagree	**Total**
Diversion of micro fund and inadequate finance	38(73%)	12(23%)	2(4%)	-	-	**52(100%)**
Unfavorable/frequent changes in government policies	19(36.5%)	-	1(2%)	30(57.5%)	2(4%)	**52(100%)**
High risk and mounting loan losses	42(80.5%)	9(17.5%)	1(2%)	-	-	**52(100%)**
Low capacity and low technical skills on micro financing	-	3(5.5%)	16(31%)	19(36.5%)	14(27%)	**52(100%)**
Stiff competition from commercial banks and SACCOs	38(73%)	12(23%)	2(4%)	-	-	**52(100%)**

Source; Primary Data 2019

From table 4.7 findings showed that 38(73%) of the total respondents strongly agreed that diversion of micro fund and inadequate finance is among the challenges faced by pride microfinance, 12(23%) of the total respondents agreed, 2(4%) of the total respondents were not sure.

From table 4.7 findings showed that 19(36.5%) of the total respondents strongly agreed that Unfavorable/frequent changes in government policies is among the challenges faced by pride microfinance, 1(2%) of the total respondents were not sure, 30(57.5%) of the total respondents disagreed, 2(4%) of the total respondents disagreed.

From table 4.7 findings showed that 42(80.5%) of the total respondents strongly agreed that High risk and mounting loan losses is among the challenges faced by pride microfinance, 9(17.5%) of the total respondents agreed, 1(2%) of the total respondents were not sure.

From table 4.7 findings showed that 3(5.5%) of the total respondents agreed that Low capacity and low technical skills on micro financing is among the challenges faced by pride microfinance, 16(31%) of the total respondents were not sure, 19(36.5%) of the total respondents disagreed, 14(27%) of the total respondents strongly disagreed.

From table 4.7 findings showed that 38(73%) of the total respondents strongly agreed that Stiff competition from commercial banks and SACCOs is one of the challenges faced by pride microfinance, 12(23%) of the total respondents agreed, 2(4%) of the total respondents were not sure.

4.5 Findings on relationship between interest rates and financial performance of pride microfinance

Table 4.8 showing Findings on relationship between interest rates and financial performance of pride microfinance.

Statement	Strongly agree	Agree	Not sure	Disagree	Strongly disagree	**Total**
Coefficient on the interest expense variable has a negative sign of financial performance.	6(11.5%)	39(75%)	6(11%)	1(1.5%)		**52(100%)**
Interest negatively affects the financial performance of a firm.	-	-	3(5%)	33(63.5%)	16(31%)	**52(100%)**
High real interest rates tend to encourage savings whilst savings determine investment.	14(27%)	32(63%)	4(7%)	2(3%)	-	**52(100%)**

Source; Primary Data 2019

From table 4.8 findings showed that 6(11.5%) of the total respondents strongly agreed that Coefficient on the interest expense variable has a negative sign of financial performance, 39(75%) of the total respondents agreed, 6(11%) of the total respondents were not sure, 1(1.5%) of the total respondents disagreed.

From table 4.8 findings showed that 33(63.5%) of the total respondents disagreed that Interest negatively affects the financial performance of a firm, 3(5%) of the total respondents were not sure, 16(31%) of the total respondents strongly disagreed.

From table 4.8 findings showed that 14(27%) of the total respondents strongly agreed that High real interest rates tend to encourage savings whilst savings determine investment, 32(63%) of the total respondents agreed, 4(7%) of the total respondents were not sure, 2(3%) of the total respondents disagreed.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATION

5.0 Introduction

This chapter presents a summary of the major findings, conclusions reached and the researcher's recommendations derived from the study of the relationship between interest rates and financial performance of microfinance institutions.

5.1 Summary of the Findings

5.1.1 Findings on the Challenges Faced By pride Microfinance Nateete branch

In responses the questions that were designed by the researcher, the findings were collected and basing on the study findings, the following revealed as the challenges; diversion of micro fund, inadequate finance, unfavorable/frequent changes in government policies, high risk and mounting loan losses. It was also revealed that Stiff competition from commercial banks and SACCOs is one of the challenges faced by pride microfinance and MFI have Low capacity and low technical skills on micro financing as its evidenced by Nwanyawu (2012)

5.1.2 Findings on the Factors determining the financial performance of pride microfinance

The findings regarding the responses about factors affecting financial performance of pride microfinance the study revealed the following factors; lending interest rates charged on loans, Size of the firm in terms of loan department, economic growth and risk, the number of customers the bank has, as it was researched by Saunder (2015)

5.1.3 Findings on relationship between interest rates and financial performance of pride microfinance

From the findings that were collected it was revealed that Coefficient on the interest expense variable has a negative sign of financial performance, interests positively affects the financial performance of a firm and high interest rates tend to encourage savings whilst savings determine investment as it was noticed by McKinnon (1973) and Shaw (1973)

5.2 Conclusion

From the researcher's findings and point of view it can be concluded that to a larger extent interests rates has a greater impact on the financial performance of pride microfinance since it was revealed that interest rates increases the profits realized by the financial institutions. Interest rate as the independent variable was linearly regressed with the dependent variable financial performance. The findings reveals that there is a positive relationship between interest rates and financial performance for both Market rate of return and return on equity when all firms are considered together. However, the relationship was not considered significant. On disaggregation of the firms and grouping the firms in their respective industries however, the study found that the relationship between interest rates and financial performance was diverse among industries. A near perfect negative relationship was found out in the energy and petroleum industry, while the investment industry had a strong negative relationship.

5.3 Recommendation

The following are recommendations for the better financial performance of microfinance

- The government should increase their efforts in encouraging microfinance banks and institutions to support the small businesses.

- Microfinance banks should expand the repayment period of their customer's asset loans, make use of the collective group-based loan disbursement strategy, as this will minimize the rate at which clients default in payment and the level of portfolio at risk.

- Microfinance banks should support their clients by offering trainings on credit maximization.

- Microfinance banks should try to find long-term capital from Pension and Insurance Companies within Uganda. This helps minimize their rate of lending and allow them distribute their interest payment through a longer time period.

Areas for Further Research

Assessment of the links between micro-credit in the crossroad to macro entrepreneurship in Uganda.

QUESTIONNAIRE

MUTEESA I ROYAL UNIVERSITY

Dear respondents,

I am a student of Muteesa I Royal University pursuing a bachelor's degree in business management; I am carrying out research on the topic entitled "***Effect of interest rates on financial performance of pride microfinance***" your organization (Pride microfinance Nateete branch) was chosen as the case study. I kindly call upon your cooperation to this research and the information provided will be treated confidentially. Thank you in advance.

SECTION A; BACKGROUND INFORMATION

Please tick in the box with correct answer

1. Gender

   Male ☐ Female ☐

2. Age Range

   Below 27yrs ☐ 27-38yrs ☐ Above 38yrs ☐

3. Education level

   Certificate ☐

   Diploma ☐

   Degree ☐

   Masters ☐

   Others ☐

If others in (3) above please specify. ……………………………………………….

SECTION B

THE FORMS OF CREDIT SERVICES PROVIDED BY THE PRIDE MICROFINANCE

a. Pride microfinance Nateete branch offers group lending as form of credit services.

Strongly agree	Agree	Not sure	Disagree	Strongly disagree

b. Pride microfinance Nateete branch provides individual lending to its customers

Strongly agree	Agree	Not sure	Disagree	Strongly disagree

SECTION C; Factors determining the financial performance of pride microfinance

Factor	Strongly agree	Agree	Not sure	Disagree	Strongly disagree
Lending interest rates charged on loans					
Size of the firm in terms of loan department					
Economic growth and risk					
The number of customers the bank has					

SECTION D; Challenges faced by pride microfinance in Uganda?

Challenge	**Strongly agree**	**Agree**	**Not sure**	**Disagree**	**Strongly disagree**
Inadequate Finance/Funds					
Unfavorable/Frequent Changes in Government Policies					
High Risk and					

Mounting Loan Losses					
Low Capacity and low Technical Skills on Micro financing					
Stiff competition from commercial banks and SACCOS					

SECTION E: Relationship between interest rates and financial performance of pride microfinance

Option	**Strongly agree**	**Agree**	**Not sure**	**Disagree**	**Strongly disagree**
Coefficient on the interest expense variable has a negative sign of financial performance.					
Interest negatively affects the financial performance of a firm.					
High real interest rates tend to encourage savings whilst savings determine investment.					

THANK YOU

END

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