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Article

Catalysts For Growth: The Role of Microfinance Services in Empowering SME's in Western Province, Sri Lanka

Minusha Weerakkody[a], Kusal Nissanka[b]

a University of Sri Jayewardenepura, b Colombo Stock Exchange

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ABSTRACT

This study investigates the impact of microfinance services on the financial performance of Small and Medium Scale Enterprises (SMEs) in the Western Province of Sri Lanka. Recognized as a crucial sector for economic growth, regional development, employment generation, and poverty reduction, SMEs in Sri Lanka benefit significantly from the tailored financial and non-financial services provided by Microfinance Institutions (MFIs). Despite the recognized importance of SMEs, many in Sri Lanka face significant challenges in accessing traditional financial services, hindering their growth potential. This study addresses the gap in understanding how microfinance services, including micro credit, micro savings, and training programs, contribute to the financial growth and sustainability of SMEs in the region. Primary data was collected through a structured questionnaire administered to a random sample of 162 SME owners in the Western Province. The analysis employed descriptive statistics, correlation, and multiple regression analysis to examine the relationships between these microfinance services and financial performance indicators, including net profit margin and return on assets (ROA). The results reveal that both micro credit and micro savings significantly impact SME financial performance, particularly net profit margin and ROA, while training programs, although beneficial, did not demonstrate a statistically significant effect on these financial outcomes. The findings emphasize the need for more tailored microfinance initiatives that focus on credit and savings services while improving the accessibility and relevance of training programs. These insights offer valuable implications for policymakers and microfinance institutions (MFIs) aiming to enhance the effectiveness of microfinance in fostering SME growth, regional development, and economic sustainability in Sri Lanka

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* Corresponding author. Email: minushaw@sjp.ac.lk
Institution: University of Sri Jayewardenepura

Introduction

1.1 Background of the Study

Small and Medium Enterprises (SMEs) have been recognized as one of the key drivers of economic growth and the promoter of the equitable development of all countries (Olusegun & Festus, 2023). Gamage (2003) highlights that SMEs play a crucial role in driving economic growth, particularly in developing countries like Sri Lanka. They are instrumental in creating jobs, fostering innovation, and contributing to regional development (Kalfas et al., 2024).

In Sri Lanka, SMEs account for a significant portion of the industrial sector and are seen as vital to the country's long-term economic strategy. Recent articles represent that SMEs participate in the economy by fulfilling over 75% of the total enterprises and over 45% of total employment and making a 52% contribution to the GDP in Sri Lanka approximately (Bandara et al., 2021). There are almost 500,000 SMEs in Sri Lanka, with each employing three to five people on average (Piyumal et al., 2021). However, despite their importance, SMEs often face substantial barriers to growth, including limited access to traditional financial services (Beck & Demirguc-Kunt, 2006). This lack of access to credit, savings, and training programs significantly hinders the ability of SMEs to scale their operations and achieve sustainable growth (Niranjala & Jianguo, 2017).

Microfinance Institutions (MFIs) have emerged as a key solution to this challenge. According to Wasike (2023), MFIs offer financial and non-financial services specifically tailored to the needs of SMEs, including microcredit, micro-savings, and training programs. In addition, some MFIs provide non-financial services such as group formation, development of financial literacy and self-confidence, marketing, and improvement of technology for SMEs (Piyumal et al., 2021). As per the study conducted by Sarfo et al. (2024), these services are designed to empower SMEs by providing the necessary resources to overcome financial constraints, improve operational efficiency, and enhance their market competitiveness. This study focuses on the Western Province of Sri Lanka, a key economic region where SMEs are integral to both local and national economic development (Weerasinghe & Jayawardane, 2015).

1.2 Research Problem

Studies have suggested that entrepreneurial drive in Sri Lanka is rooted not in the need for individual achievement, but in a conscious or unconscious need to satisfy a sense of social intimacy. Studies have also recognized business failure upon the exit, bankruptcy, or liquidation of the enterprise. The rate of business failure among SMEs in Sri Lanka stands at an alarming rate of 45% (Kuluppuarachchi, 2021). According to statistics published by the Small Business Administration (SBA), at least 30% of new establishments fail within the two years from their inception, while 49% fail within five years. Lack of finance is a major influential problem that most SMEs have to face in every country (Gamage, 2003). As discussed by Bakhtiari et al. (2020), SMEs' financing sources can be mainly categorized into two parts: internal sources and external sources. The common internal financing methods are own money and borrowed money from family, friends, relations or neighbours. Nevertheless, there are many external sources of financing for this sector, such as business angle, trade credit, leasing, bank finance, venture capitalist and listing. However, as pointed out by Sewwandhi and Kuruppuarachchi (2021), due to fewer collaterals, limited financial reports, weak financial literacy, and poor internal and external controls, the sources of financing for SME's have become scarce. Çankal & Edema (2019) identified Microfinance as a development tool that goes beyond banking traditions, which can be utilized by the SME sector to address this problem.

Despite the recognized importance of SMEs and the availability of microfinance services, there is a gap in understanding how these services specifically impact SME development (Sarfo et al. (2024) in the Western Province of Sri Lanka. Kumari (2020) describes Western Province as a vital economic hub in Sri Lanka, contributing significantly to the national economy. It houses a large concentration of SMEs that play a crucial role in employment generation and economic activity. According to recent studies, SMEs in this province are pivotal for achieving broader economic goals, including poverty reduction and economic

diversification (Dharmawansa & Madhuwanthi, 2023).

While microfinance has been widely studied in the context of poverty reduction and individual entrepreneurship, its role in supporting the growth and sustainability of SMEs in this region remains underexplored (Weerasinghe & Jayawardane, 2015). This study seeks to address this gap by examining the relationship between microfinance services and SME growth in the Western Province.

1.3 Objectives of the Study

The primary objective of this study is to investigate the impact of microfinance services on the development of SMEs in the Western Province of Sri Lanka. Specifically, the study aims to analyze the contribution of microcredit, micro-savings, and training programs to SME growth.

1.4 Significance of the Study

The findings of this study have significant implications for both policymakers and microfinance institutions. Focusing on the Western Province allows for an exploration of specific policy implications that could enhance microfinance's effectiveness. The concentration of financial institutions and supportive government policies aimed at promoting entrepreneurship in this region provides a conducive environment for studying the impact of microfinance on SME empowerment (Upulwehera et al., 2021).

By providing a detailed analysis of how microfinance services influence SME development, the study contributes to the broader understanding of SME growth drivers in Sri Lanka (Amaradiwakara et al., 2017). Furthermore, the research offers practical recommendations for enhancing microfinance programs and policies, with the goal of fostering long-term economic sustainability in the Western Province. The insights gained from this study can also be applied to other regions in Sri Lanka and similar developing economies, making it a valuable contribution to the field of economic development.

2.0 LITERATURE REVIEW

The hypotheses of the study are underpinned by well-established theoretical frameworks that elucidate the relationship between microfinance services and SME financial performance. First, the Resource-Based View (RBV) (Ahamad et al., 2023) posits that access to resources, such as the financial capital provided by microfinance institutions, enhances an SME's capacity to achieve a competitive advantage and improve performance metrics. Second, Social Capital Theory (Boudreaux et al., 2021) emphasizes the role of social networks and relationships fostered through microfinance institutions, which can lead to enhanced business practices and improved outcomes for SMEs. Third, under Financial Inclusion Theory, Febrian et al., (2018) highlights the importance of providing financial services to underserved segments, which is critical for fostering economic participation and promoting growth among SMEs. By grounding the study's hypotheses in these theoretical perspectives, several authors have established a robust foundation for examining how microfinance services contribute to the development of SMEs in Sri Lanka.

2.1. Microfinance Services and Their Role in SME Development

Microfinance services have become a pivotal tool for fostering the growth of SMEs in developing economies. These are aimed at empowering SMEs by providing them with the necessary resources to overcome financial constraints. According to Çankal and Edema (2019), microfinance plays a significant role in enhancing financial inclusion by offering underserved segments of the population access to essential financial services, which is critical for economic growth.

SMEs, particularly in developing countries, often face challenges in securing traditional financial services due to their lack of credit history, insufficient collateral, and perceived high-risk profiles (Niranjala & Jianguo, 2017). Microfinance services address these barriers by offering more accessible and tailored financial solutions, enabling SMEs to scale their operations. For example, a study by Rajapakshe (2021) found that microcredit significantly contributes to business expansion and income generation among SMEs in developing economies. Similarly, findings from Sri Lankan studies highlight the critical role of microfinance in facilitating entrepreneurship and improving SME performance (Bernard et al., 2017).

Despite these advantages, literature also points to challenges and limitations associated with microfinance services. For instance, Sarfo et al. (2024) argue that while microfinance can provide short-term financial relief, it may not always lead to sustainable long-term growth for SMEs. Additionally, some studies suggest that MFIs often prioritize microcredit over

other services like training and micro-savings, limiting the holistic development of SMEs (Dahal & Fiala, 2020). This underscores the need for a more integrated approach to microfinance, one that includes non-financial services aimed at building the managerial capacity of SME owners.

2.2. Impact of Microcredit on SME Development

Microcredit is one of the most well-researched aspects of microfinance, and its impact on SME development has been widely documented. Microcredit allows SMEs to access small loans to fund their operations, purchase inventory, and invest in business expansion. Numerous studies have shown that access to microcredit significantly enhances the growth potential of SMEs (Banerjee et al., 2015; Longo, 2023). For instance, a study conducted by Khandker and Samad (2014) in Bangladesh found that microcredit had a positive effect on business revenue and employment generation among SMEs.

In the context of Sri Lanka, research has shown that microcredit plays a crucial role in supporting SMEs, particularly in the Western Province, where economic activity is concentrated (Gamage, 2003). Microcredit allows entrepreneurs to bridge the financing gap, enabling them to invest in new technologies, expand their production capacity, and enter new markets. However, some studies have highlighted the risks associated with microcredit, including over-indebtedness and the potential for default (Pattnaik et al., 2024). This suggests that while microcredit can be a powerful tool for SME growth, it must be carefully managed to avoid negative consequences.

2.3. Role of Micro-savings in SME Growth

Micro-savings, though often overshadowed by microcredit, are equally important in promoting SME growth. Savings allow SMEs to accumulate funds for future investments, manage cash flow, and build financial resilience. According to Pu et al. (2021), micro-savings provide a safety net for small business owners, enabling them to cope with unexpected expenses and reduce reliance on debt. Research by Dupas and Robinson (2013) in Kenya showed that access to savings accounts significantly improved business investment and income among small entrepreneurs.

In Sri Lanka, micro-savings programs have been particularly beneficial for SMEs in the Western Province, where access to formal banking services is limited in certain areas (Sewwandhi & Kuruppuarachchi, 2021). Micro-savings not only help SMEs to manage their finances more effectively but also contribute to long-term business sustainability by fostering a culture of saving and financial planning. This is particularly important in a context where many SMEs operate on thin margins and are vulnerable to economic shocks.

Despite these benefits, the literature suggests that micro-savings programs are often underutilized by MFIs, with a greater emphasis placed on microcredit (Beck & Demirguc-Kunt, 2006). This indicates a gap in the provision of comprehensive financial services that cater to the diverse needs of SMEs. From a similar perspective, Kamara and Kamara (2023) have also highlighted that enhancing micro-savings programs could significantly improve the financial health of SMEs and contribute to their long-term success.

2.4. Training Programs as a Non-Financial Service

Training programs offered by MFIs are critical in building the managerial and operational capacity of SME owners. These programs typically cover areas such as financial literacy, business planning, marketing, and inventory management. Studies have shown that training can have a significant impact on the performance of SMEs by improving their operational efficiency and decision-making skills (Dammert & Nansamba, 2023). A study by Barron (2020) found that business training provided by MFIs in Peru led to improved business practices and higher sales among SME owners.

In the Sri Lankan context, training programs have been identified as a key factor in enhancing the competitiveness of SMEs, particularly in the Western Province where competition is fierce (Upulwehera et al., 2021). Training helps SME owners to develop the skills needed to navigate complex business environments, improve productivity, and capitalize on new opportunities. However, the literature also highlights challenges in the delivery and effectiveness of training programs. Some studies have suggested that training programs may not always be well-targeted or sufficiently tailored to the specific needs of SME owners (Idris et al., 2023). This points to the need for more customized and context-specific training initiatives that align with the unique challenges faced by SMEs in different regions.

2.5. Empirical Gap

While the existing literature provides valuable insights

into the role of microfinance services in SME development, several gaps remain. First, much of the research has focused on microcredit, with less attention given to other critical services such as micro-savings and training programs. Second, there is a need for more region-specific studies that examine the impact of microfinance services in different economic contexts. In the case of Sri Lanka, few studies have specifically explored the relationship between microfinance and SME development in the Western Province, a region that plays a pivotal role in the country's economy (Sewwandhi & Kuruppuarachchi, 2021). This study aims to fill these gaps by providing a comprehensive analysis of how microfinance services contribute to SME growth in this key economic region.

Furthermore, the literature often overlooks the interconnectedness of financial and non-financial services. While microcredit is essential for immediate financial needs, micro-savings and training programs play a crucial role in ensuring the long-term sustainability of SMEs (Amaradiwakara et al., 2017). Therefore, this study has taken a holistic approach, examining the combined effect of these services on SME development.

3.0 METHODOLOGY

This section presents the methodology employed to examine the role of microfinance services in empowering SMEs in the Western Province of Sri Lanka. It outlines the research design, population and sample selection, along with the data collection and analysis methods used to investigate this relationship.

3.1 Research Design

The study adopts a positivist philosophy, which assumes that reality is objective and can be measured through empirical evidence (Park et al., 2020). This approach aligns with the study's aim of quantitatively examining how specific microfinance services such as microcredit, micro-savings, and training programs can influence SME development in the Western Province. The deductive approach was employed, as the study tests pre-existing theories and hypotheses regarding the role of microfinance in SME growth, using statistical analysis to validate the relationships (Wanigasuriya & Ramanayake, 2023).

The research utilizes a quantitative strategy due to its ability to collect numerical data and test hypotheses. This strategy is appropriate for understanding how the independent variables (microfinance services) affect the dependent variable (SME growth) by analyzing the perceptions of SME owners through structured data collection techniques. The data were gathered via a survey questionnaire, allowing for the standardized collection of responses from a large number of participants (Ghanad, 2023).

The study was conducted in the Western Province of Sri Lanka, the country's most economically significant region. This area is home to a large concentration of SMEs, which are vital to the nation's economic activity and contribute substantially to employment and regional development (Sewwandhi & Kuruppuarachchi, 2021). Microfinance institutions (MFIs) play a crucial role in providing these SMEs with access to financial services that would otherwise be unavailable through traditional banking channels (Khandker & Samad, 2014). Given the Western Province's economic importance and the prevalence of SMEs, this region was deemed suitable for studying the impact of microfinance services on SME growth.

3.2 Conceptual Framework

The conceptual framework implies the relationship between independent variables and dependent variables. The dependent variable is the financial performance of SMEs, and the independent variable is microfinance. According to the factors identified by the previous literature, microfinance is evaluated from microcredit, micro saving, and also training programs.

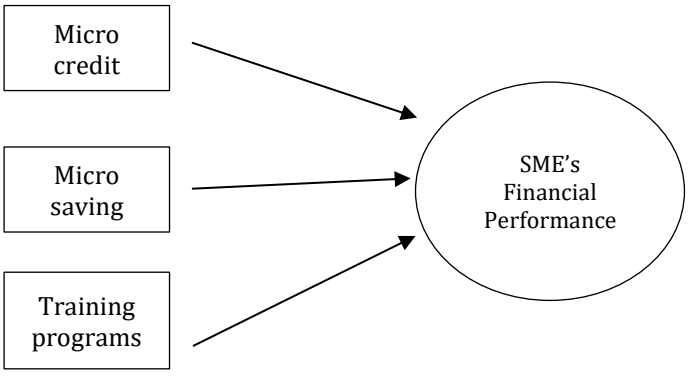

Figure 1: Conceptual framework

The dependent variable named SMEs' financial performance was evaluated using net profit margin and Return on Assets (ROA). Hence, the overall research study is based on these dependent and independent variables.

Based on the conceptual framework, six hypotheses were developed as follows.

H1: Microcredit significantly impact the net profit of SMEs in the Western Province

H2: Micro savings significantly impact the net profit of SMEs in the Western Province

H3: Training programs significantly impact the net profit of SMEs in the Western Province

H4: Microcredit significantly impact the ROA of SMEs in the Western Province

H5: Micro savings significantly impact the ROA of SMEs in the Western Province

H6: Training programs significantly impact the ROA of SMEs in the Western Province

3.3 Population and Sample

The study targeted SME owners operating in various sectors, including manufacturing, retail, and services, across the Western Province. These SMEs were selected due to their reliance on microfinance services for operational support and growth. A simple random sampling technique was employed to ensure every SME owner had an equal opportunity to participate, reducing bias and ensuring representativeness (Noor et al., 2022).

A total of 162 SME owners were selected as the sample size for the study. This number was determined using Yamane's (1967) formula for calculating sample sizes for large populations. The inclusion criteria required SMEs to:

- Have been operational for at least two years,
- Have located in the Western Province,
- Have utilized microfinance services such as microcredit, micro-savings, or training programs.

The sample size was adequate for running statistical tests, such as multiple regression analysis, and for making inferences about the entire population of SMEs in the Western Province (Sewwandhi & Kuruppuarachchi, 2021). Additionally, this sample size aligns with previous studies examining similar populations (Hiebl, 2023).

3.4 Data Collection Method

Primary data was collected using a structured questionnaire administered to SME owners. The questionnaire was designed to capture the impact of microfinance services on various aspects of business growth, such as revenue increase, employment generation, and access to capital. The survey consisted of both closed-ended and Likert-scale questions to quantify participants' perceptions of the benefits of microfinance services (Likert, 1932).

3.5 Data Analysis Methods

Data collection took place over a period of two months, with SME owners providing responses either through face-to-face interactions or via email. This method ensured a high response rate (87%) and reliable data collection. The study adhered to all ethical standards of research, including obtaining informed consent from all participants. Respondents were assured of the confidentiality of their responses, and participation was entirely voluntary. Collected data was then analyzed by using the Statistical Package for Social Science (SPPS 25) software. To test the hypothesis and identify the relationship between microfinance and the financial performance of SMEs in the Western Province, the researcher used Pearson correlation and, to test the impact between variables, used multiple regression analysis. Cronbach's alpha has been used to measure reliability.

4.0 DATA ANALYSIS AND RESULTS

This chapter presents the results of the study, connecting the data analysis techniques used with the research objectives and hypotheses. The chapter follows a systematic approach to analyze the data gathered from SME owners in the Western Province of Sri Lanka regarding the impact of microfinance services on their financial performance. Statistical analysis techniques, including descriptive statistics, correlation analysis, and multiple regression, are applied to test the hypotheses.

4.1 Data Collection and Preliminary Analysis

The study collected data through a structured questionnaire from a sample of 162 SME owners who have utilized microfinance services such as microcredit, micro-savings, and training programs. The response rate was 87%, resulting in 141 usable responses for analysis. Data was cleaned and checked for missing values, outliers, and inconsistencies. The data was coded and entered into SPSS Version 25, where all analyses were conducted.

4.2 Demographic Profile of Respondents

The demographic profile of the respondents is critical for understanding the context within which SMEs operate and the characteristics of SME owners.

As seen in Table 1, the majority of respondents were male (64.5%), with a significant portion of the sample

aged between 31-50 years (68.1%). The SMEs represented were primarily involved in retail (42%) and manufacturing (34%) sectors.

independent variables (microcredit, micro-savings, and training programs) and the dependent variables (Net Profit and Return on Assets). These statistics provide an overview of the data distribution and central tendencies.

4.3 Descriptive Statistics of Variables

Descriptive statistics were calculated for the

Table 1: Demographic Profile of Respondents

Variable	Frequency (n = 141)	Percentage (%)
Gender		
Male	91	64.50%
Female	50	35.50%
Age Group		
18-30	22	15.60%
31-40	44	31.20%
41-50	52	36.90%
51 and above	23	16.30%
Sector		
Manufacturing	48	34%
Retail	59	42%
Services	34	24%
Years of Operation		
2-5 years	38	27%
6-10 years	54	38%
Over 10 years	49	35%

Source: Compiled by author

Table 2: Descriptive Statistics for Study Variables

Variable	Mean	Standard Deviation
Micro credit	4.23	0.65
Micro savings	4.12	0.71
Training programs	3.87	0.84
Net Profit (NP)	3.95	0.78
Return on Assets (ROA)	4.05	0.68

Table 2 shows that the mean scores for microcredit and micro-savings were above 4, indicating that most SME owners highly valued these services. Training programs had a relatively lower mean score, reflecting mixed perceptions about their impact on business performance.

4.4 Reliability and Validity Testing

To ensure the internal consistency of the variables, Cronbach's alpha was calculated. All variables displayed satisfactory reliability, with Cronbach's alpha values exceeding the acceptable threshold of 0.70.

Table 3: Cronbach's Alpha for Variables

Variable	Cronbach's Alpha
Micro credit	0.82
Micro savings	0.79
Training programs	0.76
Net Profit (NP)	0.81
Return on Assets (ROA)	0.85

The results in Table 3 indicate that the scales used to measure the study variables are reliable and can be used in further analysis.

Further, the authors conducted additional validity testing to ensure the robustness of the measurement model. The Kaiser-Meyer-Olkin (KMO) test was employed to assess sampling adequacy, with all variables exhibiting values above 0.6, indicating suitability for factor analysis. Additionally, the Average Variance Extracted (AVE) was also calculated to assess convergent validity. All constructs demonstrated AVE values above the recommended threshold of 0.5, confirming adequate convergent validity.

4.5 Pearson Correlation Analysis

Pearson correlation analysis was conducted to examine the relationships between the independent variables (microcredit, micro-savings, and training programs) and the dependent variables (Net Profit and ROA). The correlation matrix is presented in Table 4.

Table 4 shows significant positive correlations between microfinance services and SME financial performance indicators. Specifically, micro-savings exhibited the strongest correlation with both Net Profit ($r = 0.589$, $p < 0.01$) and ROA ($r = 0.532$, $p < 0.01$).

4.6 Multiple Regression Analysis

Multiple regression analysis was conducted to test the hypotheses and determine the impact of microfinance services on SME financial performance. The regression results for Net Profit and ROA are presented in Tables 4.5 and 4.6.

The regression model for Net Profit was significant ($F = 32.48$, $p < 0.001$), with micro-savings having the highest impact ($\beta = 0.422$, $p < 0.001$), followed by microcredit ($\beta = 0.371$, $p < 0.001$), and training programs ($\beta = 0.189$, $p = 0.035$). This supports H1, H2, and H3, confirming that all microfinance services significantly impact the Net Profit of SMEs in the Western Province.

4.6.1 Impact of Microfinance Services on Net Profit

4.6.2 Impact of Microfinance Services on Return on Assets (ROA)

The regression model for ROA was also significant ($F = 28.21$, $p < 0.001$), with micro-savings again having the largest impact ($\beta = 0.405$, $p < 0.001$), followed by microcredit ($\beta = 0.352$, $p = 0.001$). Training programs had a marginal impact on ROA ($\beta = 0.172$, $p = 0.067$), which partially supports H6. Overall, H4 and H5 are supported.

4.7 Summary of Hypotheses Testing

4.8 Discussion of Results

The analysis confirms that microfinance services—particularly microcredit and micro-savings—play a significant role in improving the financial performance of SMEs in the Western Province. Micro-savings exhibited the strongest positive impact on both Net Profit and ROA, suggesting that it is a critical factor in fostering long-term growth. Microcredit also had a substantial effect, reinforcing the role of access to credit in SME development. Training programs, while having a positive effect on Net Profit, showed a weaker and only marginally significant impact on ROA.

In line with the study's objectives, the results highlight that microfinance services are instrumental in SME growth, providing tangible financial benefits through improved profitability and asset management. These findings are consistent with previous research by Khandker and Samad (2014) and Sewwandhi and Kuruppuarachchi (2021), who found that access to microfinance enhances SME performance in

developing economies. The weaker effect of training programs suggests that more tailored or industry specific training may be needed to maximize impact, aligning with the observations of Bernard et al., (2017).

This analysis contributes to the understanding of how microfinance services can empower SMEs, supporting both academic theory and practical applications in enhancing SME development.

Table 4: Correlation Matrix

		Micro credit	Micro savings	Training programs	Net Profit (NP)	ROA
Micro credit	Pearson Correlation	1				
	Sig. (2-tailed)					
Micro savings	Pearson Correlation	0.621**	1			
	Sig. (2-tailed)	0				
Training programs	Pearson Correlation	0.487**	0.512**	1		
	Sig. (2-tailed)	.000	.000			
Net Profit (NP)	Pearson Correlation	0.562**	0.589**	0.411**	1	
	Sig. (2-tailed)	.000	.000	.000		
ROA	Pearson Correlation	0.518**	0.532**	0.398**	0.672**	1
	Sig. (2-tailed)	.000	.000	.000	.000	

**. Correlation is significant at the 0.01 level (2-tailed).

Table 5: Multiple Regression Results for Net Profit (NP)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.142	.335		3.411	.001
	Micro credit	.326	.087	.371	3.743	.000
	Micro savings	.394	.092	.422	4.281	.000
	Training programs	.168	.079	.189	2.124	.035

a. Dependent Variable: Net Profit (NP)

$R^2 = 0.53$, Adjusted $R^2 = 0.51$

Table 6 : Multiple Regression Results for ROA

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.265	.345		3.672	.000
	Micro credit	.312	.091	.352	3.433	.001
	Micro savings	.365	.089	.405	4.101	.000
	Training programs	.149	.081	.172	1.840	.067

a. Dependent Variable: Return on Assets (ROA)

R^2 = 0.47, Adjusted R^2 = 0.45

Table 7: Summary of Hypotheses Testing

Hypothesis	Supported/Not Supported
H1: Microcredit → Net Profit	Supported
H2: Micro-savings → Net Profit	Supported
H3: Training Programs → Net Profit	Supported
H4: Microcredit → ROA	Supported
H5: Micro-savings → ROA	Supported
H6: Training Programs → ROA	Partially Supported

5.0 DISCUSSION OF FINDINGS, CONCLUSION, AND IMPLICATIONS

This chapter summarizes the key findings of the study, interprets them in the context of the research objectives and hypotheses, and discusses their implications. It also outlines the contributions of the research to theory, methodology, and practice, and concludes with recommendations for future research.

5.1 Discussion of Findings

This study aimed to analyze the impact of microfinance services—specifically, microcredit, micro-savings, and training programs—on the financial performance of SMEs in the Western Province of Sri Lanka. The financial performance indicators used were Net Profit (NP) and Return on Assets (ROA). Six hypotheses were formulated to test these relationships. The findings are summarized and discussed below in relation to the research objectives and previous literature.

5.1.1 Impact of Microcredit on SME Financial Performance

The results showed that microcredit significantly impacts both Net Profit (H1) and ROA (H4) of SMEs. This is consistent with previous research, which suggests that access to credit allows SMEs to invest in productive assets, expand operations, and increase their profitability (Khandker & Samad, 2014; Ghanad, 2023). The positive relationship between microcredit and SME performance highlights the importance of financial accessibility in enabling SMEs to overcome capital constraints, a common barrier in developing economies.

Microcredit had a stronger impact on Net Profit than on ROA, suggesting that while SMEs may see immediate

profit gains from credit, improving asset efficiency requires more time or additional resources. This finding aligns with Wanigasuriya and Ramanayake's (2023) conclusion that the benefits of credit may manifest differently depending on the financial metric used to assess performance.

5.1.2 Impact of Micro-Savings on SME Financial Performance

Micro-savings had the strongest impact on both Net Profit (H2) and ROA (H5) among the three microfinance services. This supports previous literature emphasizing the role of savings in stabilizing SMEs and providing a buffer for reinvestment (Bernard et al., 2017). The findings suggest that regular savings contribute significantly to an SME's ability to sustain growth, especially during periods of fluctuating income or market volatility.

The results also imply that micro-savings enable SMEs to self-finance, reducing their dependency on external credit. This enhances financial independence, allowing SMEs to make strategic decisions without the pressure of loan repayment schedules. The importance of savings as a contributor to both profitability and asset management underscores the role of financial discipline in SME development.

5.1.3 Impact of Training Programs on SME Financial Performance

The findings related to training programs were mixed. While training programs significantly impacted Net Profit (H3), their effect on ROA was marginal (H6). This suggests that while training may help SMEs improve profitability by enhancing skills, knowledge, and business practices, it does not directly influence asset management efficiency in the same way that microcredit or micro-savings do.

This is consistent with the argument that the benefits of training are often more qualitative, improving managerial capabilities, innovation, and decision-making (Noor et al., 2022). However, the relatively weaker effect on ROA suggests that the training programs may need to be more tailored to specific industries or operational needs to fully optimize SME performance.

5.2 Conclusion

The study provides empirical evidence that microfinance services play a significant role in enhancing the financial performance of SMEs in the Western Province of Sri Lanka. Both microcredit and micro-savings demonstrated strong positive effects on the financial metrics of Net Profit and ROA, confirming that access to financial services is critical for SME development in a developing economy.

Training programs had a significant but less pronounced effect, indicating that while they are beneficial, there is room for improvement in their design and delivery. Overall, the findings suggest that microfinance services contribute to the financial sustainability and growth of SMEs, making them an essential tool for economic development in Sri Lanka.

5.3 Contributions of the Study

5.3.1 Theoretical Contributions

The study adds to the existing body of literature on microfinance and SME development by providing new insights into how specific microfinance services affect different aspects of SME financial performance. Previous studies have explored the role of microcredit, but this research emphasizes the distinct contributions of micro-savings and training programs. It shows that micro-savings, in particular, have a more substantial impact on financial performance than previously recognized.

The study also contributes to understanding the different ways in which financial services impact profitability (Net Profit) versus asset efficiency (ROA), thereby offering a more nuanced view of SME performance.

5.3.2 Methodological Contributions

This study employed a robust quantitative methodology, using Pearson correlation and multiple regression analyses to test the hypotheses. The use of SPSS 25 for data analysis ensured that the results were reliable and valid. By focusing on SMEs in the Western Province of Sri Lanka, the study provides region-specific insights, contributing to a growing body of localized research in developing economies.

5.3.3 Practical Contributions

The findings have several practical implications for policymakers, microfinance institutions, and SME owners. Policymakers should prioritize increasing access to both credit and savings facilities, as these are proven to drive SME growth. Microfinance institutions can improve their services by offering more flexible saving schemes and developing training programs tailored to the specific needs of different industries.

For SME owners, the findings emphasize the importance of maintaining regular savings and seeking training opportunities to improve management practices. These actions will not only enhance short-term profitability but also contribute to long-term financial sustainability.

5.4 Implications for Policymakers and Practitioners

The results of this study have important implications for how microfinance services can be leveraged to support SME growth in Sri Lanka.

a. For Policymakers

- Policymakers should consider expanding access to micro-savings programs, as they have the most substantial impact on both Net Profit and ROA. Encouraging a culture of savings among SMEs could lead to more sustainable business practices.
- It is essential to develop policies that make microcredit more accessible, particularly for SMEs in rural or underserved areas.
- Government support for SME-specific training programs should be increased, with an emphasis on industry-specific needs.

b. For Microfinance Institutions (MFIs)

- MFIs should develop more flexible and customizable savings products for SMEs, which will allow for better cash flow management and reinvestment.
- Credit offerings could be made more accessible, with lower interest rates or more extended repayment terms, to help SMEs manage their financial commitments.
- MFIs should evaluate the effectiveness of their training programs and focus on providing targeted, practical training that directly correlates with business growth.

c. For SME Owners

- SME owners should prioritize building savings to create financial security and enable future growth opportunities.
- While access to credit is important, SME owners should be cautious in managing debt to avoid financial strain.
- Engaging in relevant training programs can help SME owners develop the necessary skills to manage and grow their businesses effectively.

5.5 Recommendations for Future Research

While this study provides valuable insights, it has certain limitations that should be acknowledged. The study focused only on the Western Province of Sri Lanka, limiting the generalizability of the findings to other regions or countries. In addition, the data collected was cross-sectional, which does not allow for analysis of long-term trends or causality (Sewwandhi & Kuruppuarachchi, 2021). Moreover, the study relied on self-reported data, which could introduce bias or inaccuracies.

Future research can address these limitations by conducting longitudinal studies to examine the long-term effects of microfinance services on SME performance. Additionally, studies that explore the impact of microfinance on SMEs in other provinces of Sri Lanka or other developing economies would provide a more comprehensive understanding of the subject. Moreover, further research could explore other variables such as innovation, technology adoption, or market expansion strategies as factors that may mediate the relationship between microfinance services and SME performance.

Conclusively, this chapter has provided an overview of the key findings, discussed their implications for various stakeholders, and offered recommendations for future research. The study confirms that microfinance services are crucial to SME development and highlights areas where improvements can be made to maximize their impact on financial performance.

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