**Abstract**
This paper examines the effect of financial constraints on firm performance using a sample of small business owners who are client at a microfinance institution (MFI). In developing countries, a lack of access to finance is seen as a key obstacle to successful entrepreneurship and economic growth. However, empirical evidence on this is still fragmented and sparse. This study contributes to the literature by applying an alternative measure of financial constraints based on actual lending and borrowing behavior to test how borrowing affects firm productivity. We use survey data of 615 entrepreneurs from Tanzania to analyze the relationship between financial constraints and labour productivity. Using OLS regression and propensity score matching techniques the results show that financial constraints impede labour productivity and are important barriers to successful entrepreneurship. Further tests suggest that financial constraints matter regardless of the measurement method used, thereby comforting researchers in a fragmented field which applies a wide range of financial constraints variables.