THE EFFECT OF MICROFINANCE CREDIT ON THE
PERFORMANCE OF SMALL AND MEDIUM
ENTERPRISES IN NAIROBI

BY

SRI SADHANA SURYADEVARA

UNITED STATES INTERNATIONAL UNIVERSITY-
AFRICA

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A Research Project Report Submitted to the Chandaria School of Business in Partial Fulfillment of the Requirement for the Degree of Masters in Business Administration (MBA)

UNITED STATES INTERNATIONAL UNIVERSITY - AFRICA

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STUDENT'S DECLARATION

I, the undersigned, declare that this is my original work and has not been submitted to any other college, institution or university other than the United States International University in Nairobi for academic credit.

Signed: __________________________  Date: __________________________

Sri Sadhana Suryadevara (ID 637191)

This project has been presented for examination with my approval as the appointed supervisor.

Signed: __________________________  Date: __________________________

Kepha Oyaro

Signed: __________________________  Date: __________________________

Dean, Chandaria School of Business
ABSTRACT

The purpose of this study was to investigate the effect of Microfinance credit on the performance of Manufacturing SME’s in Nairobi County in Kenya. The study was guided by the following research objectives: To assess the effect of credit accessibility on the sustainability of SME’s, to determine the debt rating and performance of SME’ and to determine the favorability of MFI credit terms in comparison to those of the traditional banking institutions.

This study used a descriptive research design to find out the effect of Microfinance credit on the performance of SME’s in Nairobi County in Kenya and this involved the calculation of mean and standard deviation of the variables under study. The population for the study incorporated all the accounts and finance managers working with manufacturing SME’s in Nairobi County which were 145 in total. Using a Yamane (1967) formula a sample of 59 respondents was arrived at. The researcher issued a total of 59 questionnaires and only 50 were filled and returned representing a response rate of 85% which was considered appropriate for the study. Statistical Package for Social Sciences (SPSS) was used for data analysis. A correlation and regression analysis was undertaken to investigate how the various variables relate to each other.

Firstly it was established that respondents rely on MFI credit financing for their business. It was also noted that MFI credit has been beneficial in expanding this business. Despite this, quality of service of financial institution’s staff, and low interest rate/cost of borrowing, as well as convenient repayment period which were important in the MFI sustainability.

Secondly, it was established that micro-finance institutions are particularly important for startups; high growth and innovative SME’s. Large institutions have comparative advantages in transactions lending’s than small SME’s. Person correlation test was carried out to determine the relationship between Debt Rating and Performance Of SME’s and the results show that there was a positive and significant correlation between debt rating and performance of SME’s.

Lastly, it was noted that among the problems that hinder SME’s from accessing credits is management. It was also noted that respondents disagreed that they do not apply for loans from micro finance and banks due to fear of being rejected. Despite this, respondents did agree that banks are to blame for poor and difficult evaluation of SMEs creditworthiness.
The study was concluded that Most SMEs have relied on rotating savings and credit association or chamas and MFI credit financing for the business this has been beneficial in expanding this business. In order to be able to approach the MFIs, quality of service of financial institution’s staff was important. Secondly, Micro-finance institutions play a big role in the growth of SME’s, and depending on the size of the firm large institutions have comparative advantages in transactions lending’s than small SME’s. Lastly, banks have played a role in the evaluation of SMEs creditworthiness; this is because they demand high collateral in order to select profitable and reliable clients.

The study recommended that MFI need to review the requirement needed for SMES credit financing. Secondly, the study recommended that there is a need of educating the SMEs about what they need to do in order to have good rating and be able to access to funds at cheaper rates and better terms. Lastly, Management also requires training to better handle the financial aspects of the business. The loan providers need to give the SMEs a chance to grow by ensuring that they gain their confidence. For study recommends that a similar study needs to be done in other counties so as to generalize the findings. In addition, variables such as entrepreneur’s characteristics, SME characteristics of SMEs and management as well as customers and markets intelligence need to be studied to establish how they influence SMEs performance.
ACKNOWLEDGMENT

Professor thank you for helping me complete my project.
DEDICATION

To my family, I dedicate this project to you. Thank you for believing in me.
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ACRONYMS AND ABBREVIATIONS

SME- Small and Medium Entreprises
MFI – Micro Finance Institutions
GDP- Gross Domestic Product
CHAPTER ONE

1.0 INTRODUCTION

1.1 Background of the Study

The critical role played by small and medium enterprises in a growing economy cannot be underestimated. Small and medium enterprises (SME’s) are characterized by rapid growth and the potential to create employment and boost the gross domestic product (GDP) of and economy (Aremu & Adeyemi, 2011). Studies in fact indicate that SME’s play a similar role even in developed economies. Developed countries like Japan and Taiwan credit the stability of their economies to their large SME sectors, Switzerland a highly developed country is one of the countries that continued to generate surplus even during the 2008 financial recession. The country recorded a 2% to 2.5% growth rate each year from 2008 through to 2012 (Guo & Woo, 2016). The economic stability experienced by Switzerland is credited on the fact the country has invested significantly on efficient small- and medium-sized companies (SME) alongside the large, competitive multinationals. The situation was different from the rest of Europe which had much of its investment in large multinationals that focused on the export market (Guo & Woo, 2016).

An economy therefore really stands out largely because of SMEs firms of between 100 - 1,000 employees and focus on a global outlook for both advanced and developing economies. SMEs account for an average 60 percent of the total employment in most developing countries (Jamali, Lund-Thomsen & Jeppesen, 2017). In African economies, the contribution of the SME sector to creating Opportunities is very significant. Its contribution of the informal sector, is especially large accounting for about 75% of total employment in manufacturing (Giaoutzi, Nijkam & Storey, 2016). The significance of SMEs in Kenya was first recognized following a report by the International Labor Organization on Employment, Income and Equity in Kenya in 1972. It highlighted the SME sector as an engine for employment and income growth. SMEs count for nearly 85 percent of employment (Cagno, & Trianni, 2013) Debt financing for SMEs in developing countries is mainly concentrated on bank loans and trade credit (Gbandi, & Amissah, 2014). According to Rungani (2009) commercial banks are a principal source of debt finance for SME’s. Commercial banks offer SMEs’ a wide range of services in their own right or through wholly or partially owned subsidiaries.
Commercial banks are in a better position to gather information on SMEs through established relationships which they and their staff have with SMEs and their owners. In addition, commercial banks have extensive branch networks that can be accessed by new SMEs even in remote locations. Furthermore, the financial conditions of small firms are usually rather opaque to investors and the costs of issuing securities directly to the public are prohibitive for most SMEs. Thus, without financial intermediaries like banks it would simply be too costly for most investors to learn the information needed to provide the credit, and too costly for the small firm to issue the credit itself. Banks, performing the classic functions of financial intermediaries, solve these problems by producing information about borrowers and monitoring them over time, by setting loan contract terms to improve borrower incentives, by renegotiating the terms if and when the borrower is in financial difficulty. In addition, Feakins (2005) points out that overdrafts and term loans are the two major products offered by commercial banks to new SMEs.  

found that SMEs who are the members of SME representative societies or enterprises such as the Chamber of Commerce have a high probability of accessing bank finance. According to Pandula (2011) these societies have close contacts and relationships with SME owners/managers and are aware of the problems and needs of their members. Therefore, these societies and other business associations can play a key role in assisting their members to access bank loans from banks Pandula (2011).

However, access to credit is still a challenge to most SMEs, especially those in developing economies and it is also still a key issue both within the private and public sector. In Kenya, the lack of adequate access to credit is the leading factor stifling the growth of small and medium enterprises (Wanjohi and Mugure, 2008). Hogan (2010), asserts that the financial sector focuses its success on the effective management of credit risk. Most economic enterprises in Kenya and East Africa however fall under the informal sector which is characterized by fluctuating income and may be hard to monitor making them non-viable Lonnie’s for the banking sector. Micro entrepreneurs also engage in economic activities which may yield a low turnover. Traditional economic activities include street food vending, tailoring, and retailing of consumable goods. Micro enterprises have been constrained by many factors especially limited access to financial services from the Formal Sector. Most SME owners also do not have marketable collateral for loans and banking institutions may charge high interest rates on loans which may scare away traders from borrowing funds. Without finance, SMEs cannot acquire
new technologies to compete effectively in the global market or establish linkages with larger firms that may boast their growth. (UN, 2012).

Very demanding requirements, in addition to the bureaucratic lending procedures by the financial institutions is the biggest challenge to credit access by SMEs. This has led most 3 SMEs to resort to informal financial institutions such as savings and loans companies, friends and relatives which may not be sufficient leading to creation of savings and credit groups like chamas (informal savings groups among families, friends or business people sharing similar interests. Some of these groups eventually graduated to Savings and credit corporative organizations (SACCO’s) which have been very resourceful in financing small businesses. These organizations fall under the Umbrella group referred to as Micro Finance Institutions (MFI’s)

Introduction of MFI’s has provided a reliable alternative source of financial services for low income earners and their SMEs as a means to raise their income, hence reducing their poverty level and contributing in country economy (Kessy & Urio, 2006). The service of microfinance institution to majority of small business owners has created opportunities for managing scarce household and enterprises resources more efficiently, protection against financial risks by taking advantages of investment opportunities and gaining more economic returns (Olowe, Moradeyo & Babalola 2013). Micro finance enables clients to protect, diversify and increase their incomes, as well as to accumulate assets, reducing their vulnerability to income and consumption shocks (Robinson, 2002).

Insufficient capital tops the list of barriers to socio economic development threatening the success of SME’s. Due to the small sizes of most SME businesses and the fact that most of them may not have lived beyond 5 years, a lack of resources in capital means small entrepreneurs need micro-financial services in order to grow and service their business. However, due to insufficient mechanisms and inadequate information in on credit markets of these businesses, banks are discouraged and unwilling to lend to small businesses. It is against this background therefore, that the researcher is trying to find out the impact of microfinance credit on the performance of small businesses in Kenya.

1.2 Statement of the Problem

Microfinance is a source of financial services for startup entrepreneurs and small businesses owners lacking access to banking services and other forms of financial credit. These include financing small businesses in small towns and rural areas, at minimal interest rates, without tying them collateral, whilst maintaining flexible installment
payment plans. Borrowers in MFI’s are organized into groups, which minimizes the risk of defaulting. Most microcredit programs also target groups in society that may have minimal assets by providing opportunities for self-employment. Currently, most small business entrepreneurs have adopted the culture of getting capital from MFIs, rather than the commercial banks due to the easier payment terms and less stringent financial requirements.

MFI’s are characterized by the tradition of saving and acquiring loans within the contest of SHGs. Dellien (2011) discusses key differences between the concept of group lending and individual lending programs. Owing to the fact that much time and effort is invested in growing social networks that enable MFI groups select members who are creditworthy under group lending, the role of loan officers usually is to provide structure and training on loan processes and offer administrative support. Under individual lending principles, loan officers bear responsibility for loan decisions; they screen, and monitor their clients which enables them come up with effective mechanisms of enforcing repayment. The principle incentive for repayment of group loans is joint liability, group reputation, credit rating and future access to credit for each member, all of which are directly contingent on each member upholding their obligations. Individual lending programs on the other hand use a variety of incentives such as collateral requirements, co-signees and guarantors to ensure repayment and repayment discipline is ascertained by strict enforcement of contracts. Several studies have been done on this area, Bauchet and Morduch (2013) did a research to on SME’s and finance focusing attention on the question on whether Micro is too small highlighting the challenges that small businesses go through when trying to access credit.

Another study done by Madole, (2013) on the impact of microfinance credit on the performance of SMEs in Nakuru The study found that access to credit positively influenced the growth of 92% of SMEs. Most SMEs were found to be hindered by high cost of finance and lack of collateral for the new SMEs. Ochanda, (2014) A study on the effect of financial deepening on growth of small and medium sized enterprises in Kenya: a case of Nairobi county the study found that while financial innovate was found to have a positive influence on the growth of SMEs. Stringent financial sector rules and regulations, and high interest rates were continued to hamper the ability of SME’s to attain credit eventually hindering their growth of. The study recommended an
establishment of subsidized credit for SMEs and setting up of a financial innovations that will work for SME’s. This study will hence seek to assess the role that MFIs play in addressing the credit challenge faced by SME’s by examining the effects of micro-finance credit on the performance of small and medium enterprises in Nairobi.

1.3 General Objective
The effect of Microfinance credit on the performance of SME’s in Nairobi

1.4 Specific Objectives
1.4.1 To assess the effect of credit accessibility on the sustainability of SME’s
1.4.2 To determine the debt rating and performance of SME’s
1.4.3 To determine the favourability of MFI credit terms in comparison to those of the traditional banking institutions

1.5 Significance of the study

1.5.1 Microfinance institutions
The Study will be useful for microfinance institutions to assess the impact they have had in financing SME’s and provide a platform for future innovations in the financial sector to facilitate their contributions to the SME sector.

1.5.2 Researchers
Researchers will be able to use this document as a source of information in future studies related to Micro financing of SME’s

1.5.3 Policy Makers
The study will provide information on debt rating of SMES, and conditions for SME and entrepreneurship financing that may be resourceful for policy makers in the financial sector to come up with more suitable financial solutions for SME’s

1.5.4 Government
Since SME’s are crucial in ensuring sustainable and inclusive growth of an economy, their role in development is critical in enabling governments create employment for its citizens. SME’s can only achieve this role if they are provided necessary finance to and grow their business. Governments play a critical role in ensuring SME’s have access to capital and information provided in this document will enable the government addressing
1.6 Scope of the Study
The main aim of this research is to examine the effect of Micro Finance Credit on the performance of SME’s in Nairobi. The study sought to assess the effect of credit accessibility on the sustainability of SME’s, determine the Debt rating and performance of SME’s and determine the Favorability of micro finance credit terms in comparison to those of the traditional banking institutions in relation to small and medium enterprises for a three month period from September to October 2017. The sample of the study was based on the population of small enterprises in Nairobi. Since the study focused on a sample of Nairobi, the findings may be more applicable to the target population. Time constraints arising from limited time provided for the study may also limit the depth of the study.

1.7 Definition of Terms

1.7.1 Debt Rating
Debt rating is a method of measuring the credit worthiness of a borrower, with respect to a particular financial obligation or debt. The ratings are done by credit rating agencies to evaluate the ability or likelihood of an individual, corporation, provincial authority or sovereign government to meet interest payments or full redemption of the issue (Madole, 2013).

1.7.2 SME
Small and medium-sized enterprises (SMEs) are non-subsidiary, independent firms which employ fewer than a given number of employees. This number varies across countries. The most frequent upper limit designating an SME is 250 employees, as in the European Union. However, some countries set the limit at 200 employees, while the United States considers SMEs to include firms with fewer than 500 employees (Anane, Cobbinah, & Manu, 2013).

1.7.3 Micro finance
Microfinance is the provision of a broad range of financial services such as deposits, loans, payment services, money transfers and insurance products to the poor and low-
income households, for their microenterprises and small businesses, to enable them to raise their income levels and improve their living standards (Bauchet, & Morduch, 2013).

1.7.4 Microfinance Loan

Microfinancing loan are small loans granted to the basic sectors, on the basis of the borrower’s cash flow and other loans granted to the poor and low-income households for their microenterprises and small businesses to enable them to raise their income levels and improve their living standards. These loans are typically unsecured but may also be secured in some cases (Odebiyi, & Olaoye, 2012).

1.8 Chapter Summary

This chapter presents background information to the research problem, highlights the gap to be studied in the problem statement, states the main purpose of the study and lists the research questions to be addressed in research project. It also presents significance of the study, highlights the scope and definition of terms used. Chapter two is a literature review of existing research literature on financing of SME’s. it discusses the specific objectives effect of credit accessibility on the sustainability of SME’s, determine the Debt rating and performance of SME’s and determine the Favorability of micro finance credit terms in comparison to those of the traditional banking institutions in relation to small and medium enterprises. Chapter three outlines the Research Methodology that will be used for the study providing the research design, population and sampling design, data collection methods, research procedures and data analysis methods used in the study. Chapter four presents findings and results of the study. Chapter five presents an analysis of the collected data, a summary of the study, conclusions on the findings, and recommendations for action and further research.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction
This chapter will look into previous literature on the effect of Microfinance credit on the performance of SME’s in Nairobi. It will study in-depth the specific objectives of the study which are to assess the Effect of Credit Accessibility on the Sustainability of SME’s, determine the Debt rating and performance of SME’s, determine the Favorability of MFI credit terms in comparison to those of the traditional banking institutions

2.2 The effect of Credit accessibility on the sustainability of SME’s
There has been increased focus on access to finance for small firms since the 2008 crisis, and the fallout has focused attention on access to finance for small and medium sized enterprises (SME’s). The financial crisis was mostly strengthened by overvalued assets especially those backed by mortgages. But as they began to lose value it became unclear who owned them and so was exposed to the loses. Banks were unwilling to lend to each other and restrictions in lending fed through into the economy; the ‘credit crunch’ (cowling et.al, 2012). Bank lending was not recovered since especially when it comes to the small firms and this has held back the economy of many countries including the United Kingdom (UK) (Fillipetti & Archibugi, 2011). This has therefore brought about the rise of micro-finance institutions and other informal finance institutions that mostly facilitate SME’s with credit. Their ability to access credit has brought about great significance in their economy.

2.2.1 Organizational growth
Agencies are faced with sources of strain in choose of alternate: outside and internal. In phrases of outside factors, companies are trying hard to stabilize inflows and outflows. For example, an agency may use a system simply in time for the control of fabric sources and trying to acquire quality products that allows you to comfy orders. On the other hand, however, the quantity to which the enterprise is capable of manipulate the environment is greatly decreased; environmental changes ought to be compensated with organizational adjustments, if the employer is to stay powerful. Alternate may be determined by means of the forces of the internal surroundings of the employer. Low productiveness, absenteeism, turnover, sabotage, strikes are factors indicating that trade management has
become essential. In lots of cases, internal forces that arise in reaction to organizational adjustments are designed to cope with external things (Maurer & Weiss, 2010).

There is considerably less evidence on the existence of any cyclical affect, at least for innovative firms especially (Archibugi et al. 2013). Firms will replace older products, services, and processes with newer and more efficient versions. But firms with less efficient models are weaker will be forced to close. This dual process shows how recessions can contribute to technological progress. External financing has also in a greater way enabled firms to bring products to a wider market and take advantage of a return to economic growth.

The legal and regulatory framework in Rwanda is one of the most conducive to the provision of SME finance in Sub-Saharan Africa. The legal framework for the creditor’s rights and financial infrastructure has witnessed for reaching reforms over the past years. A new framework for secured transactions in both movable and immovable assets and the establishment of a new privaleted bureau collecting both positive and negative information from a variety of providers as well as new land registry are some of the implemented reforms. The reforms have been regarded as positive developments by the finance and credit institutions which have led to an increase in the use of movable assets as security for SME sector thereby leading to a general expansion in lending to the sector. The country has thereby experienced considerable growth in the private sector and more jobs have been created to the citizens. SME’s represent over 90% of Rwanda’s private business and contribute to more than 50% of employment and of Gross Domestic Product (GDP).

Like in most countries, Kenyan commercial banks have not effectively addressed the financial needs of low-income earners, due to stringent baseline requirements. They perceive low-income earners, hereby SME’s, as uncredit worthy due to lack of assets which they would use as collateral against credit facilities (World Bank, 2009). This therefore makes micro finance institutions (MFI’s) play a major role in filling the gap for financial services among low-income earners, majority of them being women. Services provided by MFI’s are flexible and tailored to meet the financing needs of women in rural and urban settings (Chandrasekhar, 2004). About 1.3 million SME’s were operational in Kenya by 2001 and they provided job opportunity to about 2.4 million people and accounted to about 70% of economic activities (Hospes et al; 2002).
By 2008 SME’s created employment for about 75% of the national workforce and contributed up to about 22% of the national Gross Domestic Product. Access to micro-credit has had a positive effect on borrower’s average income, food security, nutrition, treatment adherence as well as education of orphaned and vulnerable children.

2.2.2 Economic growth

In Nigeria, credit has recognized as an essential tool for promoting small and micro enterprises (SME’s). About 70% of Nigeria’s populations are engaged in the informal sector or in agricultural production or aquaculture sector by extension. The country has experienced accelerated growth in terms of the economy due to increased production and improved efficiency in the small and micro enterprises sector. Poverty has been eradicated and the gap between the rich and the poor has been narrowed.

Infrastructure has also improved due to increasing number of SME’s, more jobs have been created and there has now been food security in the country. Similarly, microfinance institutions through the funding of SME’s have contributed to the Kenyan economy majorly in areas such as job creation, training of entrepreneurs, generating income and eventually poverty eradication by financing law income households. External funding have seen enterprises grow in terms of assets base, level of stocks, services and also in the number of employees that the businesses can hold.

Most of the SME’s that have sorted for loans from micro finance institutions have experienced growth. A strong relationship has also been created between the rate of employment and credit advanced to SME’s. due to the reducing number of unemployed adults in Kenya, there has been a great economic growth. The rate of employment has grown from a mean of 2.09 employees per SME to a mean of 3.48 employees per SME in the last four years. The reasons cited include increased business activities (increased assets, investments, output, net sales) that required more human capital to manage. This highly supports Kevan and Wydick (2001) that provision of credit to the poor increases capitalization of business, employment creation and long-term income.

recently the function of SMEs in economic development and employment introduction has occupied maximum of the discussions among authorities, coverage makers, academicians/ researchers/ pupils and economists in Kenya and other international locations. An observation made by Kongolo (2010) installed that small commercial enterprise proprietors globally have the identical traits, face the same obstacles but
range in their knowledge of how small groups assist in financial growth. SMEs have capacity to gasoline financial growth due to the fact they devise new jobs, increase the tax base, and are drivers of innovation.

According to Beck and Levin, (2005) SMEs decorate opposition and entrepreneurship therefore have outside advantages on financial system extensive performance, innovation and combination productivity. They're the primary motors with the aid of which new entrepreneurs offer the economic system with a non-stop deliver of thoughts, abilities, and innovations (CACCI,2003). Globally there is an agreement that MSMEs keep the key to monetary increase primarily based on the quick increase of corporations and the role of SMEs in generation of employment.

In accordance to Normah (2007) the attention of SMEs has a close relationship with the dominant monetary sports. SMEs dominate the world economies in terms of employment and wide variety of organizations, yet their full potential remains remarkably untapped (Omar, Arokiasamy & Ismail, 2009). This is because of a number of reasons (e.g. legal, institutional, cultural, societal and many others.) which make the position of SMEs on economic development different across nations.

Until the SMEs in Kenya are promoted, the imaginative and prescient 2030 may additionally in no way be a reality. studies has shown that new firms formation is an important indicator of entrepreneurial interest and monetary improvement (Venesaar &Loomets, 2006). In Kenya the rate of formation of new companies has stagnated for lengthy and except that maximum new corporations do now not grow to adulthood given that they collapse earlier than the 5th year. SMEs make a contribution to economic improvement by means of distinctive feature of their sheer numbers and growing percentage in employment and Gross home Product (GDP).

In recent years the SME region has continuously registered higher growth compared to the overall business region globally. There’s a trendy agreement amongst students and policy makers that the essential benefit of the arena is its employment capability at low capital price. Consistent with European, Micro, Small and Medium-sized businesses are socially and economically important, for the reason that they represent ninety nine percent of all firms. They provide round 90 million jobs and contribute to entrepreneurship and innovation. But, SMEs face precise problems which the EU and national rules try and deal with by granting them diverse benefits.
The United States are at the upward thrust lately, seventy five eight percent have been commenced through the entrepreneur's savings and approximately 12.1% were because of contributions from household in general 81.9% have used equity financing instead of 6.1% which have been as a result of debt financing. The authorities has additionally helped a few entrepreneurs in financing their organizations with 3% of SME’s having received starting capital from the government financing projects which include teenagers and ladies agency budget. only a few have sourced from commercial banks and succeeded because of the stern situations attached to the borrowing phrases through industrial banks. the provision of both debt and equity financing will subsequently cause the boom of the enterprise organisations.

Idowv (2009) found that a primary barrier to rapid development of SME’s region was a shortage of both debt financing and equity financing. Financial increase in advanced international locations including Japan, Korea, Taiwan and lots of others, changed into considerably generated through SME sports. the share contribution of SMEs to Gross domestic Product (GDP)/overall cost delivered stages from 60.0 percentage in China, 57.0 percent in Germany, fifty five.3 percent in Japan and 50.0 percentage in Korea, in comparison to 47.3 percentage attained by using Malaysia. SMEs have also played a totally critical position in the economic improvement of China. At gift, there are more than 10 million of SMEs comprising 99 consistent with cent of the entire variety of enterprises in China. SMEs make contributions 60 in keeping with cent of industrial output quantity and forty per cent of the overall taxes and earnings found out with the aid of establishments in China. The contribution of SMEs in output in Japan is 65 percent, Germany forty eight percent at the same time as in USA its 45 percent. SMEs in the US generate over half of the nation’s gross home product (GDP).

2.2.3 Credit Purpose in SME’s
Credit seeking SME’s are mostly after the idea of expanding their business. Especially with the fact that most lenders are after the idea of evaluating the running of your business before they can offer credit, 75.6% of credit borrowed from MFI’s are for business to another and only a few have sought to pay personal expenses (paying various bills). Brown, Earle and Lup (2004) employed panel data techniques to analyze a survey of 297 new small enterprises in Romania containing detailed information from the start-up date through 2001. They found strong evidence that access to external credit increase
the growth of both employment and sales. Surveys conducted in Asia, South America, Carribean region and in Africa indicated that microfinance institutions have significantly been able to access friendly micro-credit loans nad have ventured into entrepreneurial activities. In addition to earning a profit, sustainable micro-finance providers are in a better position than their subsidized peers to expand their operations and share of the market. Santem (2010) argues that through the provision for the poor to set up businesses. Provision of credit to the poor increases capitalization of business, employment creation and long term income growth.

2.3 To Determine the Debt Rating and Performance of SME’s

Debt rating is a method of measuring the credit worthiness of a borrower, with respect to a particular financial obligation or debt. The ratings are done by credit rating agencies to evaluate the ability or likelihood of an individual, corporation, provincial authority or sovereign government to meet interest payments or full redemption of the issue. Agencies such as Moody’s investors service, standard and Poors (S & P) and Fitch evaluate issues worldwide and are very closely followed. A top rating means there is almost no likelihood of the borrower failing to meeting the terms of the credit borrowed.

2.3.1 Credit Worthiness of SME’s

Banks and microfinance lendings are the most common sources of external finance for many SME’s worldwide, which are often heavily reliant on straight debt to fulfill their startup, cash flow and investment needs. In particular, debt financing appears to be ill-suited for newer, innovative and fast growing companies, with a higher risk return profit. The financing constraints can be especially severe in case of startups or small businesses that rely on intangibles in their business model, as these are highly firm specific and difficult to use as collateral in traditional debt relations (OECD 2010a). Therefore, micro-finance institutions are particularly important for startups; high growth and innovative SME’s. This necessitates the need to broaden the range of financing instruments available to SME’s and entrepreneurs, in order to enable them to continue to play their role in growth, innovation and employment.

When it come to debt rating, large institutions have comparative advantages in transactions lendings to more transparent SME’s based on hard information, while small institutions have comparative advantages in relationship lending to informationally
opaque SME’s based on soft information (e.g. Brger, Miller, Petersen, Rajan, and Stein forthcoming).

In Uganda, the cost of borrowing elements i.e. interest rate and loan processing costs, are associated with SME performance and the cost of price and risk of small business credit.” Journal of money, credit and Banking. Berger, Allen N, W., Scott Frame and Nathan H Miller forthcoming; “credit sconing and the availability of borrowing as a whole accounts for 31.1% of the variation in the performance of the SME’s. initiatives should therefore be intensified to encourage greater understanding and acceptance of cost of borrowing, select appropriate elements such as wan processing costs and interest rates in order to be able to provide affordable financing for peace to start and grow SME’s, provide employment to citizens and also contribute to the country’s GDP. This will therefore be arrived at by enabling improved access of credit by SME’s resulting from their ability to most commercial bank credit terms, leading to survival, increased sales higher profitability and low cost of doing business (Ogujiuba, 2004).

In Kenya, most SME’s and start-ups are funded by formal and informal money lending institutions or from own savings. In most cases, commercial banks have failed to cater for the credit needs of smallholders, however mainly due to their lending terms and conditions. It is generally the rules and regulations set by the institutions that have created the myth that the poor are unbakable and since they can’t afford the required collateral they are unbankable uncredit worthy (Adera, 1995). The failure of specialized financial institutions to meet the credit oriented financial system for those considered non creditworthy. Especially women have formed savings groups where they have greater access to informal credit facilities than to formal sources. According to Peachey and Roe (2006) access to finance should be considered as a basic need alongside the provision of education health and water. One of the problems that hinder SME’s from accessing credits is management. Due to their small side, a simple management mistake is likely to lead to sure death of the enterprise. Low productivity is also a barrier in SME’s accessing funds from.

2.3.2 Factors affecting SMEs Credit Worthiness

Over the past two decades in particular, there has been substantial debate as to how best to maximize the small and medium enterprises’ (SMEs) contribution to local economic
development in the light of the failure of many financial institutional models and programs for poverty alleviation (World Bank Group, 2004; Berger et al., 2006). According to Kibaara (2006), between 1960 and 1969, close to US$1 billion was provided to the developing countries by Inter-American Development Bank (IDB), International Bank for Reconstruction and Development (IBRD) and the United States Agency for International Development (USAID) for credit programs to SMEs.

World over, the SME subsector is dogged with a number of challenges. In Africa, for instance, their failure rate is approximated at 85% out of every 100 SME’s start-ups. The major reason attributed to this failure is lack of skills and access to capital (GOK, 2007). The SMEs are only able to source and obtain micro finance mostly from the informal sector like friends and relatives. Bank credit is not available to SMEs because they generally considered high credit risks by financial institutions and most of them do not have adequate collateral. (Nduba, 2010) Other challenges include, discriminatory cultural practices which make it impossible for women entrepreneurs to borrow on own assets and land title deeds, high transaction costs etc. This limitation in access to finance by SME’s undermines the critical role of in economic growth.

The lending factors which govern the distribution of the available funds are the terms of lending. In a perfectly competitive market the credit is allocated to the prices (interest rates), borrowers are willing to pay. Interest rates influence the movement of credit among the various sectors of the economy (Kimeu, 2008). The factors that affect the structure of interest rates include the availability of collateral to obtain credit, the supply and demand conditions which produce change in interest rates, the opportunity costs and the availability of credit to SMEs, the scope of competition and the services if any, provided by the lenders. Low interest rates are defended on the grounds of being a special incentive for the SME’s. Research has shown how efficient allocation of resources including borrowed capital and their willingness to seize potentially profitable opportunities.

2.3.3 How to Improve Credit Worthiness of SME’s

Considering the role played by SME’s in the economy of so many countries, and the attention placed on them in the Basel Capital Accord, behavior of financial measures should be analyzed and the most significant variable in predicting their creditworthiness selected in order to construct a default prediction model. SME’s being reasonably
considered the backbone of the economy of many countries, they provide approximately 75% of the jobs in the private workforce, representing 99.7% of all employers. Therefore applying a default prediction model developed on large corporate data to SME’s will result in lower prediction power and likely a poorer performance of the entire corporate portfolio than with separate models for SME’s and large corporate. In Uganda, borrowers seek to play an active lender-borrower relationship which, in turn, influences decisions made by loan officers. But borrowers have had a tendency of manipulating the information they disclose to loan officers in order to enhance their chances of getting credit from banks.

This creates distrust between the borrower and the lender hence limiting chances of getting a loan. Similar to the situation in U.S as said above, banks have been recommended to design lending guidelines that integrate both supply and demand factors, instead of focusing only on supply factors like project viability and collateral availability. More consultations with borrowers and loan officers have also been recommend in order to develop a mutually set of lending policies. The private sector foundation (2005) highlight that informal financing arrangements are the most commonly used financing mechanism for SME’s in Uganda. The main informal sources and re-investment of profits, loans and grants from a social network of family and friends, liqutation of assets, rotating savings and credit institutions, informal operating leases, reciprocal asset usage arrangements and of recent money lenders. Such funds are often insufficient to start and run a business or investment in long term assets. Micro-finance institutions therefore come in and provide an additional financing though they have the disadvantage of offering only small loans and short repayment periods which may not meet all SME’s financing needs (Kasekende and Opondo, 2003).

Mutesasira, Osinde and Nthenya, 2001) points out that in the case of reciprocal asset usage arrangements SME’s device schemes to share tools amongst themselves based on goodwill and mutual support. Other SME’s may also use rental arrangements with owners of assets employing a scheme akin to an operating lease but on an informal basis. The SME’s and owners of assets enter a mutual verbal arrangement to use an asset which is paid for at agreed regular time intervals. The informal operating lease arrangements are found across different SME sectors such as small scale transporters, fish mongers, construction workers, small minors, fishermen, tailors and coffee processors. Mutesasira
et al. (2001) and ministry of Finance, Planning and economic Development (2004) shows there are rotating savings and credit associations in which members create a pool of funds over a period of time by making regular contributions whereby later they can receive shares and/or loans to use at their discretion. Similar to other countries SME’s in Kenya form the backbone of the economy with a significant of 30% in terms of GDP and 74.2% of the total persons engaged in employment. SME’s in Kenya source most of their capital from micro finance institutions and informal money lending sectors such as rotational groups and Saccos.

Although access of credit by SME’s is not easy to measure, financial depth (total loan outstanding) can be used as an approximate indicator with direct and indirect effects on financial firms. Greater depth is to be associated with greater access for firms. Demiurge Beck and Martinez (2007) identified geographic and demographic penetration, average size and numbers of deposits as indicators. There have been a number of reasons as to why SME’s have little or no access to credit. The rate of interest is the amount of money the borrower is obligated to pay above the principal sum of money lent. High interest rate discourages SME’s from borrowing since they increase the cost of credit and the fact that they usually spread over a short time usually a year.

This reduces the accessibility of credit among them therefore reduction of interest rates reduces the cost of credit and increased accessibility of credits among SME’s access to credit from both formal and informal channels require a certain amount of collateral. At times the security required is unaffordable and this becomes a constraint to SME’s most of whom may not have deeds to capital assets to present as security against the loans. Institutions may also require the individual or the group goodwill of guarantors which acts as a major hindrance. Most financial institutions do not accept just any guarantor therefore they have to scrutinize them. Because of the fears of the borrower running bankrupt, most people don’t agree to be guarantors thereby making it harder for the SME’s owner to access funds from the financial institution. Doing away with such strenuous requirements will in a major way increase the borrowing rate of SME’s
2.4 To Compare MFI Credit Terms and Those Of The Traditional Banking Institutions

2.4.1 Developments In Microfinance And Traditional Banking

As recently as the early 90s, the concept of microfinance was still unknown in Europe yet governments hardly considered the need to encourage small enterprises by offering small loans to low-income earners. It was only registered in 1997 following a microcredit summit in New York and a follow up meeting in Bulgaria to address issues on the region’s microfinance Programs, necessitating reinvention of the wheel. Two decades later, microfinance is recognized globally and improvements and innovation solutions have been done to improve access to finance and business skills for low-income and micro entrepreneurs (Bendig et al. 2012). According to Bendig et al. (2012), the main objectives of European microfinance has been to create jobs, promote micro-enterprises, encourage social inclusion, and empower the specific target groups. By 2011 some of the MFI’s were financed by commercial banks, the governments gave direct and indirect tax incentives preferential rates, protection against default risk and business development services to facilitate the sustainability of MFI’s (Hudon and Traça, 2011). MFI’s were ideally created to serve the poor and the unemployed, promote job creation, and so reduce the burden on social welfare (Cozarenc and Szafarz, 2014). In developing countries, microfinance is treated as a complement rather than a substitute product (Bauchet and Morduch, 2013).

In developed countries the division between businesses served by regular banks and businesses served by MFIs is blurred, some MFIs serve client who have the ability to borrow from banks. The banking sector’s response to the development of microcredit is mixed. Some banks have ventured into the micro finance business by creating MFIs and collaborating with MFIs. On one hand, the banking sector has been asking for better market delimitation and strict supervision of microfinance activities adding to the challenges of SME borrowing. Due to repeated effects where many SMEs borrowers have been denied loans for various unacceptable reasons, like ethnicity or sex borrowers have shied away from applying for external funding to avoid the stringent due bureaucratic systems Deakins et al (2010). Some firm owners do not even apply for loans for fear of being rejected
A study by Njoora, and Kyal (2014) on effects of microfinance credits on SMEs in Ngong of Kajiado County in Kenya, the research established that the amount of credit granted to SMEs by microfinance organizations was equivalent to the amount applied for. Seventy two point three percent of the respondents were not granted as much as they had requested from the MFI’s. It was established in the findings that only 6.1% of the respondents had sought credit from traditional banking institutions. These finding confirm the critical role played by MFI’s in meeting the financial needs of the SME’s in Ngong. This is due to strict conditions attached to the borrowing terms by commercial banks. The availability of debt and equity financing will be instrumental in enhancing the growth of business enterprises.

These findings are supported by Idowu (2010), who observes that a major barrier to the development of the SMEs sector was a shortage of debt financing and equity financing. In dealing with the challenges in access to credit for a majority with only 39.6% of Kenyan adults being able to access it, (FSD, 2009), factors such as rising costs of living that have contributed to many citizens inability to access loans ought to be dealt with. Little to no access to credit inhibits both consumption and investment further accelerating poverty levels. A bivariate probit model, applied on Fin Access 2009 national survey data revealed that social capital enhanced financial inclusion through increased access to informal loans. The study recommended that financial institutions factor in group affiliations in designing their loan products in order to increase financial outreach seeing that Kenyans are more receptive to MFI loans.

2.4.2 Assessment Of Credit Worthiness And Loan Security Requirements

Given a choice, a majority of micro-entrepreneurs would prefer microcredit to a regular bank loan because socially-oriented MFIs screen loan applicants less rigorously than regular banks. MFIs are also appealing because besides having attractive credit conditions, they also take the initiative to provide business guidance to their borrowers. Banks therefore consider MFIs as a threat to their functioning. Due to this fear the banking Sector in developed countries like Europe have created new regulations for MFI’s like introducing limiting loan ceilings, interest caps and setting criteria for eligibility in borrowing in order to ensure their survival in business (European Micronance Network, 2012). Olomi (2009) highlights that information asymmetry challenges arising from poor or non-existent financial records by an SME limits the
borrower’s creditworthiness evaluation making it impossible for them to acquire loans from banks. Studies highlight several restrictions faced by firms in attempting to obtain finance from banks (Woldie, et al., 2012; Beck, et al., 2008). Previous literature identifies several key factors that add to this problem. Woldie, et al. (2012); Deakins, et al. (2010) highlight a divide between the demand and supply sides in reference to the SME and the bank. While SME’s are blamed for absence of Financial and accounting statements, Improper accounting standards and unprofessionalism and Illicit manipulation of statements. Banks are to blame for Poor and difficult evaluation of firms' creditworthiness, adverse selection and Poor Follow up and inappropriate Financial monitoring.

In the West African community, SMEs were found to be incapable of providing audited financial statements and accounting reports based on the accounting standards prescribed by the Organization for the Harmonization of Business Law in Africa (OHADA) increasing the reluctance of banks to provide loans required by SMEs. Otherwise, the problem of information asymmetry reflects a risk imbalance in disfavor of the firms. This problem is linked to the inadequate business experience and financial illiteracy of SMEs promoters as well as insufficient risk-based credit assessment of the credit application. Banks often increase interest on loans so as to compensate for this issue. They can however not increase the interest rate beyond a certain level for fear of attracting bad borrowers with unsound projects. Banks are therefore forced to focus on alternative criteria like heavy screening and asking for high collateral in order to select profitable and reliable clients. (Ghimire & Abo, 2013).

Information asymmetry between banks and the potential SME borrowers has severe implications on lending methodologies used by bank loan officers. In the absence of sufficient financial information, banks generally rely on high collateral values, in the view of the bank reduces on the risks associated with the problem of adverse selection and hazards resulting from imperfect information (Ghimire & Abo, 2013). Unfortunately, banks are trying to mitigate lending risks through a capital gearing approach rather than focusing on the future income potential of SMEs making collateral or “loan securitizations” prerequisites to accessing bank loans. Azende (2012) on a study in Nigeria notes that SMEs struggle to access finance from banks due to stringent collateral requirements and inefficient guarantees schemes. Young SMEs have little tangible assets to give as collaterals. SMEs in West Africa were also found incapable of providing
audited financial statements and accounting reports required by banks. In the even
accounts were provided, a lack of competent and credible accounting practices interfere
with the quality of the information provided thereby increasing reluctance of the banks to
provide loans. Banks inturn make it harder for SME’s by further increasing interest as a
way of compensating (Ghimire, & Abo 2013)

Woldie, et al. (2012) in Tanzania observes that SME’s under 5 years of age are more
dependent on informal financing rather than bank financing. It is difficult for new firms
to obtain bank financing due to the issue of information asymmetry and collateral
requirements. Young SMEs are also more susceptible to failure compared to older firms
thus increasing on the reluctance of banks to invest in their businesses. The study by
Ghimire & Abo (2013) in West Africa an analysis on relationship between a several
variables including size, age, financial information availability, SME-banks relationships,
availability of collateral, economic activity and their relationship with processing of credit
applications reflected a high dependency in relation to access of finance in a bank. the
challenges in a ccessing credit is hence blamed on the habit of hedging by lenders to
borrowers in that they demamnd unrealistic collaterals from these SME’s. SME’s are also
unable to provide essential financial statements.

Credit markets in Kenya have evolved mechanisms that circumvent the above mentioned
credit constraints. Borrowers, who lack collateral assets to give against their loans
resorted to the use of social capital so as to improve their accessibility to credit. Social
capital refers to connections amongst individuals sharing common characteristics norms
and are trustworthy. They are a networks who interact frequently comprise groups of
people who interact directly and frequently in multi-faceted ways. These networks may
involve colleagues, business people, friends, students, professionals and gangs.
Interpersonal trust among the participants in these networks provides Sanctions against
those who deviate form the norms and acts as a substitute for institutional and legal
deficiencies. Informal finance therefore thrives more in the Kenyan markets. Clients of
informal finance seek no legal enforcement for their activities contracts rely more on a
sense of moral duty rather than absolute rights. Nonetheless, these groups institute
effective borrowing channels governed by reputable relations thus promoting investments
and supporting economic growth and development. Social capital therefore enables
access to private information helps monitor members and punish individuals who defy the
social norms. Sharing information amongst members reduces transactions costs, creates a
sense of belonging and facilitates collective decision making. Solidarity and reciprocity emerges from these networks diminishes opportunistic behavior. The networks have been resourceful in building businesses in rural areas and small towns who have suffered challenges accessing credit due to lack of assets to secure credit.

2.4.3 Loan size

In most developed countries, regulators have imposed loan ceilings on microfinance institutions (MFIs). Micro-entrepreneurs needing above-ceiling loans are forced to take the co-financing option, in which they apportion the loan between the microfinance and a regular bank loan. Co-financing is an attractive option for MFI’s who are now able to free-ride on regular bank screening processes. French MFIs for instance became subject to a ceiling limit of EUR 10,000 by April 2009 (Cozarenco, & Szafarz, 2014). In order to work in favor of poor entrepreneurs, US and European regulators set upper limits on the size of loans microfinance institutions (MFIs) grant. This threshold may however lead to small businesses being crowded out from the microcredit market since micro-entrepreneurs holding large business projects will be forced to secure above-ceiling loans with regular banks. As far as loan ceilings are concerned, France has one of the most restrictive rules in the developed world. The French Monetary and Financial Code (2007) stipulates that licensed MFIs are forbidden from granting loans above EUR 10,000. In contrast, the U.S Small Business Administration, a federal agency promoting the creation and development of small businesses, has set a USD 50,000 cap to microcredit (Lieberman et al., 2012). The European Union recommends the use of a EUR 25,000 ceiling (European Commission, 2007). In practice, however, EU member states state their own ceilings. For instance, Hungary, Portugal, Slovakia, and the UK allow MFIs to grant loans exceeding EUR 25,000 (European Commission, 2007).

This situation contrasts with the rapid expansion of microfinance in developing countries (Armendariz and Morduch, 2010). MFIs in developing countries typically supply standardized products to a large number of unbanked people. MFIs in developed countries target a limited number of micro-entrepreneurs disregarded by commercial banks. These MFIs are meant to address a market failure and facilitate self-employment.
2.5 Chapter summary
This chapter discusses previous literature review on existing research on financing of SME’s with respect to the specific objectives. The next chapter outlines the Research Methodology that will be used for the study providing the research design, population and sampling design, data collection methods, research procedures and data analysis methods used in the study. Chapter four presents findings and results of the study. Chapter five presents an analysis of the collected data, a summary of the study, conclusions on the findings, and recommendations for action and further research.
CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction
This chapter describes the research methodology, research design, the population and the sampling technique to be used for the field research. The chapter highlights the data collection and analysis procedures that was used in the study.

3.2 Research Design
Methodology refers to the principles, procedures and practices that govern a research (Mugenda & Mugenda, 2005). According to Mugenda and Mugenda (2005) research design specifies the methods and procedures for collecting and analyzing the needed information. It indicates a framework or blueprint for the research as well as the research methods chosen to determine the information needed. It defines the sampling method, sample size, measurement and data analysis processes. In this study, a descriptive research design method was used to carry out the research (Schindler and Cooper, 2003). A descriptive research design was essential in studying the effect of MFI credit on the performance of SME’s.

3.3 Population and Sampling Design

3.3.1 Population
A Population can be defined as a set of individuals, objects, or data from where a statistical sample can be drawn (Saunders, et al., 2009). Population is the entire group of individuals, events or objects having common observable characteristic (Copper and Schindler, 2000). Cooper and Schindler (2003) further add that a population is the total sum of collected units from which the researcher draws conclusions for a study. The population for the study incorporated all the accounts and finance managers working with manufacturing SME’s in Nairobi County found in various areas in Nairobi. The total number of registered manufacturing SME’s is 145 according to the registrar of companies 2016

3.3.2 Sampling Design
A research sampling design is that part of the research plan that indicates how cases are selected for observation. The design therefore maps out the procedure followed to draw
the study’s sample. According to Cooper and Schindler (2011), a good sample should be a representative of the population. This study used convenient sampling method which will lower costs, and ensure a greater speed of data collection based on the availability of population elements.

3.3.2.1 Sampling Frame
A sampling frame is the list of individuals or events, source material or device from which a sample is drawn (Mugenda & Mugenda, 2005). It comprises a list of all those within a population who can be sampled, and may include individuals, households, organizations or institutions (Saunders et al., 2009). The list of managers was requested from the organisations that was involved in the study.

3.3.2.2 Sampling Technique
Sampling technique explains the method deemed relevant for the study in which the researcher wants to investigate whether the characteristics of a certain phenomenon cut across the units of observation with maximum variation. (Mugenda & Mugenda, 2005). The sampling technique that was used for this study is convenience sampling to collect ready information from the survey. The method that was used in drawing samples for the population was driven by the objectives of the study. The sampling process was regulated by the parameters in the population in line with specific objectives of the study (Cooper and Schindler, 2011). The study assumes a convenient random Sampling approach to ensure ease in accessing respondents for the study.

3.3.2.3 Sample Size
A sample size is typically one that bears some proportional relationship to the size of the population from which it is drawn. In order for the researcher to get a representative sampling size, then, the sampling size must be large (Cooper et.al, 2001). Ligthelm and Van Wyk (2005) describes the sample size as a smaller set of the larger population. With a population of 145 at 90% confidence level and a 10% (+10/-10) margin of error, the sample size of 59 respondents was reached at using the Yamane (1967) formula as follows. The sample size was sufficient and representative of the entire population.
\[ n = \frac{N}{1 + N(e)^2} \]

Where \( n \) is the sample size, \( N \) is the population size and \( e \) is the margin of error.

\[ n = \frac{145}{1 + 145 (0.10)^2} \]

\[ n = 59 \]

The sample size distribution was as presented on Table 3.2. Besides, the sample size of 110 was included in the study.

### 3.4 Data Collection Methods

The data collection method that was used for the Study is primary data collection method. In this study, structured questionnaires was used to collect the required data from the respondents. Questionnaires refer to collection of information about the population (Mugenda & Mugenda, 2003). Structured questionnaires are an inexpensive way of gathering data from respondents who may have tight schedules. The steps the study took to develop the structured questionnaires include defining the objectives of the survey; determining the sampling group; constructing the instrument and administering the instrument to respondents.

The structured questionnaires detailed five key components, namely: the background information; the influence of education strategy on the performance of Equity Bank; How health strategy has influenced Equity Bank’s organizational performance; ways in which Equity Bank’s environmental strategy has influenced the firm’s corporate performance; and the influence of Equity Bank’s sports strategy in the performance of the bank. A likert scale structured questionnaires made it possible to collect views and opinions that can be analyzed using descriptive statistics.

### 3.5 Research Procedures

The researcher provides a complete account of the research process including pilot testing, scheduling of the subjects or participants distribution and collection of the data collection instruments, the questionnaires (Saunders, et al., 2009). The researcher first
developed the questionnaire and distributed it to 5% of the respondents in a pilot test to ascertain the instruments suitability and eliminate any typological errors as well as other problems that may be inherent in the tool. The researcher made sure that the questionnaire was as short as possible, precise and to the point. The purpose of this is to avert certain common challenges including interviewee fatigue and the subsequent refusals as well as collecting redundant data.

The results of the pilot phase was used to improve the questionnaire and assess the feasibility of the study. After the pilot test and the assessment of the feasibility of the study and the suitability of the instrument, the research process will proceed. Screening forms were randomly distributed to determine eligible respondents for the survey. The data was collected within a period not exceeding three weeks. In the course of the survey, the researcher randomly approached and administered the questionnaires to potential predetermined respondents within the selected Equity Bank branches.

3.6 Data Analysis Methods

Data analysis is the process of editing and reducing accumulated data to a manageable size, developing summaries, seeking for patterns using statistical methods. All completed research materials were assembled and information organized (Cooper and Schindler, 2003). The researcher used descriptive methods such as mean, mode, median, percentages, tables and frequency distribution to compute data analysis. To ensure easy analysis, the questionnaire was coded according to each variable of the study. This study used descriptive statistics. According to McDanile and Gates (2001), descriptive analysis involves a process of transforming a mass of raw data into tables, charts, with frequency distribution and percentages, which are a vital part of making sense of the data. In this study, the descriptive statistics such as percentages and frequency distribution were used to analyze the demographic profile of the participants. Correlation analysis and regression analysis was used to establish the relationship between Microfinance funding and the performance of SME’s. A correlation analysis was done to establish the relationship between the dependent and independent variable. A regression analysis was also done to determine what percentage of the debt rating and credit accessibility influenced SME Performance.

Where the multi linear regression equation \( Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 \) become:

\[
Y=14.059 - 0.526 X_1 - 1.879 X_2
\]
Where $Y$ is the dependent variable SME performance

$X_1$ – Credit accessibility

$X_2$ – Debt rating

3.7 Chapter Summary

This chapter outlines the Research Methodology that was used for the study providing the research design, population and sampling design, data collection methods, research procedures and data analysis methods used in the study. The next chapter presents findings and results of the study.
CHAPTER FOUR

4.0 RESULTS AND FINDINGS

4.1 Introduction
This chapter presents the results that were established from the data analysis done. This included results relating to the demography of the respondents and specific research objectives that were aimed at establishing the effect of Microfinance credit on the performance of SME’s in Nairobi

4.1.1 Response rate
The research issued a total of 59 questionnaires and a total of 50 were filled and returned giving a response rate of 85%. This was considered sufficient for the study as indicated in table 4.1

Table 4.1: Response Rate

<table>
<thead>
<tr>
<th>Variable</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Filled and returned</td>
<td>50</td>
<td>85</td>
</tr>
<tr>
<td>Non-response</td>
<td>9</td>
<td>15</td>
</tr>
<tr>
<td>Total</td>
<td>59</td>
<td>100</td>
</tr>
</tbody>
</table>

4.2 Demographical Factors
The research also analysed data in line with the demographic features and the results were presented as follows:

4.2.1 Gender
Analysis of the respondents gender revealed that male were 29% and represented 58% of the respondents interviewed while female were 21 and represented 42% of the total as shown in the figure 4.1. This indicate that there was a balance in gender representation
4.2.2 Age

To analyse the age levels the result established that majority of respondents accounting for 56% were aged between 31-40 years while 28% were below 30 years, on the other hand, those aged above 50 were 16% as shown in table 4.2 below. This implies that the respondents represented both old and young as a result offered varied opinion in regard to the objective of the study.

Table 4.2: Age

<table>
<thead>
<tr>
<th>Variable</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 30</td>
<td>14</td>
<td>28.0</td>
</tr>
<tr>
<td>31-40 years</td>
<td>28</td>
<td>56.0</td>
</tr>
<tr>
<td>Above 50</td>
<td>8</td>
<td>16.0</td>
</tr>
<tr>
<td>Total</td>
<td>50</td>
<td>100.0</td>
</tr>
</tbody>
</table>

4.2.3 Highest Level of Education

To analyse the literacy levels the result established that majority of respondents accounting for 66% had college education while 34% had a university education as shown in table 4.3 below. This implies that response were very literate to comprehend the questions asked.
Table 4.3: Highest Level of Education

<table>
<thead>
<tr>
<th>Variable</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Primary</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Secondary</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>College</td>
<td>33</td>
<td>66.0</td>
</tr>
<tr>
<td>University</td>
<td>17</td>
<td>34.0</td>
</tr>
<tr>
<td>Total</td>
<td>50</td>
<td>100.0</td>
</tr>
</tbody>
</table>

4.2.4 Duration of Operation

To analyse the duration of operation, the result established that majority of the firms had been in existence for more than 10 years accounting for 34%, it was also established that 28% of the firms have existed for 6-10 years, while 18% had been in operation from 2-5 years. Those that had been in operation for less than a year was 10% as shown while 10% failed to respond as shown in table 4.4 below. This implies that response had enough experience in the sector.

Table 4.4: Duration of Operation

<table>
<thead>
<tr>
<th>Variable</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 1 year</td>
<td>5</td>
<td>10.0</td>
</tr>
<tr>
<td>2 to 5 years</td>
<td>9</td>
<td>18.0</td>
</tr>
<tr>
<td>6 to 10 years</td>
<td>14</td>
<td>28.0</td>
</tr>
<tr>
<td>More than 10 years</td>
<td>17</td>
<td>34.0</td>
</tr>
<tr>
<td>Total</td>
<td>45</td>
<td>90</td>
</tr>
</tbody>
</table>

4.2.5 Number Of Employees in The Firm

To analyse the number of employees present in the firm, the result established that majority of the firms had been 11-50 employees accounting to 82% of the respondents while, only 10% had over 50 employees. It was also established that 8% had only 1-5 employees as indicated in table 4.5.

Table 4.5: Number of Employees in the Firm

<table>
<thead>
<tr>
<th>Variable</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-5</td>
<td>4</td>
<td>8.0</td>
</tr>
<tr>
<td>11-50</td>
<td>41</td>
<td>82</td>
</tr>
<tr>
<td>Over 50</td>
<td>5</td>
<td>10</td>
</tr>
<tr>
<td>Total</td>
<td>50</td>
<td>100</td>
</tr>
</tbody>
</table>
4.3 Effect of Credit Accessibility on the Performance of SME’s

The first objective set to establish the effect of credit accessibility on the sustainability of SME’s. Respondents were asked a set of questions to indicate to what extent they agree or disagreed with statement related to credit accessibility. Using a five point Likert scale where 1 - Strongly Disagree 2 - Disagree 3 - Neutral 4 - Agree 5 - Strongly Agree

4.3.1 Loans borrowed

An analysis of the borrowing revealed that 74% had borrowed loans from rotating savings and credit association or chamas. At the same time those who haven’t borrowed were only 26%

![Figure 4.2: Borrowing](image)

4.3.2 Total Borrowed

For those who had borrowed the findings show that much in total have you borrowed from the association in the last three years. And the findings revealed that in 2015, majority of the firms had a loan of 100,001-150,000. While in the year 2016 most of the firms borrowed over 200,000. In addition, the findings revealed the in 2017 majority of the firms borrowed between 150,001-200,000 as shown in table 4.6

Table 4.6: Total Borrowed

<table>
<thead>
<tr>
<th>Year</th>
<th>Less than 100,000</th>
<th>100,001-150,000</th>
<th>150,001-200,000</th>
<th>Above 200,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>5</td>
<td>13</td>
<td>10</td>
<td>9</td>
</tr>
<tr>
<td>2016</td>
<td>1</td>
<td>12</td>
<td>10</td>
<td>14</td>
</tr>
<tr>
<td>2017</td>
<td>3</td>
<td>9</td>
<td>17</td>
<td>8</td>
</tr>
</tbody>
</table>
4.3.3 SME Credit

Respondents were asked to state the level of agreement in relation to SME Credit accessibility and respondents were asked to rate by either strongly agree (5) or strongly disagree (1).

The findings revealed that respondents agreed that they rely on SME credit financing for our business (Mean=4.38, SD=1.105). It was also noted that SME credit has been beneficial in expanding this business (Mean=4.18, SD=1.380). There was uncertainty if SME credit is easy to access (Mean=3.56, SD=1.013), or SME credit attracts reasonable interest rates (Mean=3.08, SD=1.192).

Table 4.7: SME Credit Accessibility

<table>
<thead>
<tr>
<th>Statement</th>
<th>Mean</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>We rely on SME credit financing for our business</td>
<td>4.38</td>
<td>1.105</td>
</tr>
<tr>
<td>SME credit has been beneficial in expanding this business</td>
<td>4.18</td>
<td>1.380</td>
</tr>
<tr>
<td>SME credit is easy to access</td>
<td>3.56</td>
<td>1.013</td>
</tr>
<tr>
<td>SME credit attracts reasonable interest rates</td>
<td>3.08</td>
<td>1.192</td>
</tr>
</tbody>
</table>

4.3.4 Getting a Loan from a Micro Financial Institution

The respondents were asked to rate the factors they consider when getting a loan from a micro financial institution (Rate from 1 to 5, with 1 being least important and 5 very important):

It was noted that the convenient location of financial institution was not a factor when seeking funding (Mean=3.54, SD=1.216). It was also noted that there was uncertainty on the importance of SME assisting the SMEs in disbursement of loan (quick processing of loan application) (Mean=3.66, SD=1.062). Despite this, quality of service of financial institution’s staff was important (Mean=4.18, SD=1.058). It was also noted that Low interest rate/cost of borrowing (Mean=4.66, SD=1.189) was important, same to convenient repayment period (Mean=4.04, SD=1.087). Similarly, absence of requirement for immovable property as collateral was also considered necessary (Mean=4.12, SD=0.922). There was however uncertainty on availability of other financial services from same financial institution (Mean=3.56, SD=0.907).
Table 4.8: Getting a Loan from a Micro Financial Institution

<table>
<thead>
<tr>
<th>Statement</th>
<th>MEAN</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Convenient location of financial institution</td>
<td>3.54</td>
<td>1.216</td>
</tr>
<tr>
<td>SME have assisted us in disbursement of loan (quick processing of loan application)</td>
<td>3.66</td>
<td>1.062</td>
</tr>
<tr>
<td>Quality of service of financial institution’s staff</td>
<td>4.18</td>
<td>1.058</td>
</tr>
<tr>
<td>Low interest rate/cost of borrowing</td>
<td>4.66</td>
<td>1.189</td>
</tr>
<tr>
<td>Convenient repayment period</td>
<td>4.04</td>
<td>1.087</td>
</tr>
<tr>
<td>Absence of requirement for immovable property as collateral</td>
<td>4.12</td>
<td>.922</td>
</tr>
<tr>
<td>Availability of other financial services from same financial institution</td>
<td>3.56</td>
<td>.907</td>
</tr>
</tbody>
</table>

4.3.5 Correlation Analysis between Credit Accessibility and Performance of SMEs

Person correlation test was carried out to determine the relationship between SME Sustainability and Credit Sustainability. Table 4.9 shows that there was a negative and insignificant correlation between SME Sustainability and credit sustainability, $r(50)=-0.50, p>0.05$

Table 4.9: Correlation Analysis of Credit Accessibility and Performance of SMEs

<table>
<thead>
<tr>
<th>Performance of SMEs</th>
<th>SME Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Pearson Correlation</td>
</tr>
<tr>
<td>Credit Accessibility</td>
<td>-.050</td>
</tr>
</tbody>
</table>

4.3.6 Regression of Credit Accessibility and Performance

A simple linear regression analysis was used to establish how credit accessibility affect SME Performance. The model summary as presented in Table 4.10 shows that credit accessibility explained 3% of the variability of Performance of SMEs ($R^2=0.03, F(1,48)=0.121, p>.05$) and the strength of the relationship ($r=0.05$).
Table 4.10: Regression Credit Accessibility and Performance of SMEs

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Change Statistics</th>
<th>ANOVA*</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>R Square Change</td>
<td>F Change</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>.050*</td>
<td>.003</td>
<td>-.018</td>
<td>.83512</td>
<td>.003</td>
<td>.121</td>
</tr>
</tbody>
</table>

ANOVA*

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>.085</td>
<td>1</td>
<td>.085</td>
<td>.121</td>
<td>.729</td>
</tr>
<tr>
<td>Residual</td>
<td>33.477</td>
<td>48</td>
<td>.697</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>33.561</td>
<td>49</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: SME Performance  
b. Predictors: (Constant), credit accessibility

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>4.279</td>
<td>.824</td>
<td>5.192</td>
</tr>
<tr>
<td>credit accessibility</td>
<td>-.080</td>
<td>.229</td>
<td>-.050</td>
<td>-.348</td>
</tr>
</tbody>
</table>

As shown in Table 4.10, the linear regression ANOVA showed that credit accessibility statistically had a significant effect on SME Performance $F(1,48) = .8$, $p > .05$. The regression coefficient findings as indicated in Table 4.10 revealed that credit accessibility statistically had a significant effect on SME Performance ($\beta = -.08$, $p > .5$). This implies that one unit increase of credit accessibility would lead to 0.08 declines in units of SME Performance. Based on the coefficients results, the general form of model equation established is as follows:

$$MP = 2.801 + 0.165CA$$

Whereby $SP = SME$ performance and $CA = Credit$ accessibility

4.4 Debt Rating and Performance of SME’s

The second objective set to establish the effect of debt rating and performance of SME’s. Respondents were asked a set of questions to indicate to what extent they agree or disagreed with statement related to credit accessibility. Using a five point Likert scale where 1 - Strongly Disagree 2 - Disagree 3 - Neutral 4 - Agree 5 - Strongly Agree.
4.4.1 Descriptive of Debt Rating and Performance

As indicated in table 4.11, micro-finance institutions are particularly important for startups; high growth and innovative SME’s (Mean=4.06, SD=0.818). Large institutions have comparative advantages in transactions lending’s than small SME’s (Mean=4.00, SD=1.429). Respondents neither agreed of disagreed that; one of the problems that hinder SME’s from accessing credits is management (Mean=3.4, SD=1.40), low productivity is a barrier in SME’s accessing funds (Mean=3.84, SD=1.376), rating by independent, trusted third party has led into increased credit worthiness of SMES (Mean=3.74, SD=0.853) or rating enables SMEs to ascertain the strengths and weaknesses of their existing operations and take corrective measures to enhance their organizational strength (Mean=3.98, SD=0.869).

It was however affirmed that good rating enables SMEs to access to funds at cheaper rates and better terms (Mean=4.08, SD=0.877). Rating facilitates prompter credit decisions from Banks on proposals of SMEs (Mean=4.08, SD=0.665). On whether good rating enhances the acceptability of the SMEs with their customers and buyers there was uncertainty (Mean=3.94, SD=1.058).

Table 4.11: Debt Rating and Performance of SME’s

<table>
<thead>
<tr>
<th>Statement</th>
<th>MEAN</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro-finance institutions are particularly important for startups; high growth and innovative SME’s</td>
<td>4.06</td>
<td>.818</td>
</tr>
<tr>
<td>Large institutions have comparative advantages in transactions lending’s than small SME’s)</td>
<td>4.00</td>
<td>1.429</td>
</tr>
<tr>
<td>One of the problems that hinder SME’s from accessing credits is management</td>
<td>3.40</td>
<td>1.400</td>
</tr>
<tr>
<td>Low productivity is a barrier in SME’s accessing funds</td>
<td>3.84</td>
<td>1.376</td>
</tr>
<tr>
<td>Rating by independent, trusted third party has led into increased credit worthiness of SMES</td>
<td>3.74</td>
<td>.853</td>
</tr>
<tr>
<td>Rating enables SMEs to ascertain the strengths and weaknesses of their existing operations and take corrective measures to enhance their organizational strength</td>
<td>3.98</td>
<td>.869</td>
</tr>
<tr>
<td>Good rating enables SMEs to access to funds at cheaper rates and better terms</td>
<td>4.08</td>
<td>.877</td>
</tr>
<tr>
<td>Rating facilitates prompter credit decisions from Banks on proposals of SMEs</td>
<td>4.08</td>
<td>.665</td>
</tr>
<tr>
<td>Good rating enhances the acceptability of the SMEs with their customers and buyers.</td>
<td>3.94</td>
<td>1.058</td>
</tr>
</tbody>
</table>
4.4.2 Correlation Analysis between Debt Rating and Performance Of SME’s

Person correlation test was carried out to determine the relationship between Debt Rating and Performance Of SME’s. Table 4.12 shows that there was a positive and significant correlation between debt rating and performance of SME’s, $r (50)=.754 p<0.05$

Table 4.12: Correlation Analysis of Debt Rating and Performance Of SME’s

<table>
<thead>
<tr>
<th>Performance</th>
<th>Pearson Correlation</th>
<th>Sig. (2-tailed)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt Rating</td>
<td>.754**</td>
<td>.000</td>
</tr>
</tbody>
</table>

* Correlation is significant at 0.05 level (2-tailed)

4.4.3 Regression of Debt Rating and Performance of SME’s

A simple linear regression analysis was used to establish how debt rating affect performance of SMEs. The model summary as presented in Table 4.13 shows that debt rating explained 55.9% of the variability of performance of SMEs ($R^2=0.559$, $F(1,48)=1$, $p<.05$) and the strength of the relationship ($r=0.754$).

Table 4.13: Regression Debt Rating and Performance of SME’s

<table>
<thead>
<tr>
<th>Model Summary</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mode</td>
<td>Unstandardized Coefficients</td>
<td>Standardized Coefficients</td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>.149</td>
<td>.490</td>
</tr>
<tr>
<td></td>
<td>.986</td>
<td>.124</td>
</tr>
<tr>
<td></td>
<td>.304</td>
<td>.754</td>
</tr>
<tr>
<td></td>
<td>.762</td>
<td>.000</td>
</tr>
</tbody>
</table>
As shown in Table 4.13, the linear regression ANOVA showed that debt rating statistically had a significant effect on MFI performance $F(1,48) = 1, p < 0.05$. The regression coefficient findings as indicated in Table 4.13 revealed that debt statistically had a significant effect on MFI performance ($\beta = 0.986, p < 0.5$). This implies that one unit increase of debt rating would lead to 0.986 declines in units of MFI performance. Based on the coefficients results, the general form of model equation established is as follows:

$$SP = 0.149 + 0.986DR$$

Whereby SP = SME Performance and DR = debt rating

### 4.4.4 Effects of Credit Accessibility and Debt Rating on SME Performance

A multi linear regression analysis was used to establish how debt rating and credit accessibility affect performance of SMEs. The model summary as presented in Table 4.14 shows that debt rating and credit accessibility explained 51.7% of the variability of performance of SMEs ($R^2 = 0.511, F(1,48)=1, p < .05$) and the strength of the relationship ($r = 0.719$).

#### Table 4.14: Effects of Credit Accessibility and Debt Rating on SME performance

<table>
<thead>
<tr>
<th>Model</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Change Statistics</th>
<th>R Square Change</th>
<th>F Change</th>
<th>df1</th>
<th>df2</th>
<th>Sig. F Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>0.719*</td>
<td>0.517</td>
<td>0.511</td>
<td></td>
<td>0.517</td>
<td>76.090</td>
<td>2</td>
<td>48</td>
<td>.000</td>
</tr>
</tbody>
</table>

**ANOVA**

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig. F</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>23.282</td>
<td>2</td>
<td>11.641</td>
<td>76.090</td>
<td>.000b</td>
</tr>
<tr>
<td>Residual</td>
<td>21.725</td>
<td>142</td>
<td>.153</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>45.007</td>
<td>144</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: SME Performance

b. Predictors: (Constant), debt rating, credit accessibility

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Constant)</td>
<td>14.059</td>
<td>1.110</td>
<td>12.662</td>
<td>.000</td>
</tr>
<tr>
<td>1</td>
<td>Credit accessibility</td>
<td>-0.526</td>
<td>-.116</td>
<td>-.338</td>
</tr>
<tr>
<td></td>
<td>Debt Ratig</td>
<td>-1.879</td>
<td>.308</td>
<td>-.457</td>
</tr>
</tbody>
</table>
As shown in Table 4.14, the linear regression ANOVA showed that debt rating and credit accessibility had a significant effect on SME performance $F(1,48) = 76$, $p < 0.05$. The regression coefficient findings as indicated in Table 4.14 also revealed that debt and credit accessibility had statistically significant effect on SME performance ($\beta = 14.059$, $p < 0.5$). This implies that one unit increase of debt rating and credit accessibility would lead to 14.059 increase in units of SME performance. Based on the coefficients results, the general form of model equation established is as follows:

Where multilinear regression equation $Y = \beta_0 + \beta_1 + \beta_2 X_2$ become:

$Y = 14.059 - 0.526 X_1 - 1.879 X_2$

Where $Y$ is the dependent variable SME performance

$X_1$ – Credit accessibility; $X_2$ – Debt rating

### 4.5 Favorability of MFI Credit Terms in Comparison To Banks

The third objective set to establish the Favorability of MFI credit terms in comparison to banks. Respondents were asked a set of questions to indicate to what extent they agree or disagreed with statement related to favourability of MFI credit terms. Using a five point Likert scale where 1 - Strongly Disagree 2 - Disagree 3 - Neutral 4 - Agree 5 - Strongly Agree.

From the analysis it was revealed that respondents disagreed that due to repeated effects many SMEs borrowers have been denied loans for various unacceptable reasons like ethnicity or sex (Mean=2.44, SD=1.580). Respondents also disagreed that borrowers have shielded away from applying for external funding to avoid the stringent due to bureaucratic systems (Mean=2.88, SD=1.172). Respondents agreed that among problems that hinder SME’s from accessing credits is management (Mean=4.76, SD=1.117). There was uncertainty of low productivity being a barrier in SME’s accessing funds (Mean=3.74, SD=0.723). It was also noted that respondents disagreed that they do not apply for loans from micro finance and banks due to fear of being rejected (Mean=2.00,SD=0.857).

There was uncertainty on wether SMES have been granted full amount of credit applied for by microfinance organizations over the years (Mean=3.24, SD=1.170), or whether SMES have sought credit from traditional banking institutions compared to micro finance institutions (Mean=3.16, SD=0.976). Other areas where there was uncertainty was
Information asymmetry challenges arising from poor or non-existent financial records by an SME limits the borrower’s creditworthiness (Mean=3.61, SD=0.829), and also evaluation makes it impossible for banks to acquire loans from banks (Mean=3.22, SD=1.112).

Despite this, respondents did agree that banks are to blame for poor and difficult evaluation of SMEs creditworthiness (Mean=4.08, SD=1.441). Also compared to MFIs banks ask for high collateral in order to select profitable and reliable clients (Mean=4.34, SD=1.154). The findings revealed that SMEs struggle to access finance from banks due to stringent collateral requirements (Mean=4.48, SD=1.334). Finally it was also noted that it is difficult for new firms to obtain bank financing due to the issue of information asymmetry and collateral requirements (Mean=4.30, SD=1.249).

Table 4.15: Favorability of MFI Credit Terms in Comparison to other Banks

<table>
<thead>
<tr>
<th>Statement</th>
<th>MEAN</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Due to repeated effects many SMEs borrowers have been denied loans for various unacceptable reasons like ethnicity or sex</td>
<td>2.44</td>
<td>1.580</td>
</tr>
<tr>
<td>Borrowers have shielded away from applying for external funding to avoid the stringent due bureaucratic systems</td>
<td>2.88</td>
<td>1.172</td>
</tr>
<tr>
<td>One of the problems that hinder SME's from accessing credits is management</td>
<td>4.76</td>
<td>1.117</td>
</tr>
<tr>
<td>Low productivity is a barrier in SME’s accessing funds</td>
<td>3.74</td>
<td>.723</td>
</tr>
<tr>
<td>We do not apply for loans from micro finance and banks due to fear of being rejected</td>
<td>2.00</td>
<td>.857</td>
</tr>
<tr>
<td>SMES have been granted full amount of credit applied for by microfinance organizations over the years</td>
<td>3.24</td>
<td>1.170</td>
</tr>
<tr>
<td>SMES have sought credit from traditional banking institutions compared to micro finance institutions</td>
<td>3.16</td>
<td>.976</td>
</tr>
<tr>
<td>Information asymmetry challenges arising from poor or non-existent financial records by an SME limits the borrower’s creditworthiness</td>
<td>3.61</td>
<td>.829</td>
</tr>
<tr>
<td>Evaluation makes it impossible to acquire loans</td>
<td>3.22</td>
<td>1.112</td>
</tr>
<tr>
<td>Banks are to blame for poor and difficult evaluation of SMEs creditworthiness</td>
<td>4.08</td>
<td>1.441</td>
</tr>
<tr>
<td>Compared to MFIs banks ask for high collateral in order to select profitable and reliable clients.</td>
<td>4.34</td>
<td>1.154</td>
</tr>
<tr>
<td>SMEs struggle to access finance from banks due to stringent collateral requirements</td>
<td>4.48</td>
<td>1.344</td>
</tr>
<tr>
<td>It is difficult for new firms to obtain bank financing due to the issue of information asymmetry and collateral requirements</td>
<td>4.30</td>
<td>1.249</td>
</tr>
</tbody>
</table>
4.5.1 Performance of SMEs

To analyze the performance of SMES it was noted that effective entrepreneurship has led to growth of SMEs in the country (Mean=4.28, SD=0.757). It was established that appropriate human resource is vital for increased profitability in SMEs (Mean=4.08, SD=0.986). In addition, SMEs has used marketing information to improve profitability (Mean=4.00, SD=0.857). There was uncertainty on how use of Information Technology plays a major role in SME effectiveness (Mean=3.62, SD=1.260) as shown in table 4.15.

Table 4.16: Performance of SMEs

<table>
<thead>
<tr>
<th>Statement</th>
<th>MEAN</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Effective entrepreneurship has led to growth of SMEs in the country</td>
<td>4.28</td>
<td>.757</td>
</tr>
<tr>
<td>Appropriate human resource is vital for increased profitability in SMEs</td>
<td>4.08</td>
<td>.986</td>
</tr>
<tr>
<td>SMEs has used marketing information to improve profitability</td>
<td>4.00</td>
<td>.857</td>
</tr>
<tr>
<td>Use of Information Technology plays a major role in SME effectiveness.</td>
<td>3.62</td>
<td>1.260</td>
</tr>
</tbody>
</table>

4.6 Chapter Summary

This chapter has presented the results from the data analysis done on 50 questionnaires. The first section looked at the demographics of the respondents while the other subsequent parts focused on the findings from the specific objectives which were to assess the effect of credit accessibility on the sustainability of SME’s, to determine the debt rating and performance of SME’s, and to determine the favourability of MFI credit terms in comparison to those of the traditional banking institutions. The next chapter offers the conclusions and recommendations drawn from the study.
CHAPTER FIVE

5.0 DISCUSSIONS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

The aim of this study was to investigate the effect of Microfinance credit on the performance of SME’s in Nairobi County in Kenya. This chapter will provide a summary, discussion, conclusions and recommendations arrived at from the study, this was purely based on the research objectives of the study.

5.2 Summary of the Study

The purpose of this study was to investigate the effect of Microfinance credit on the performance of SME’s in Nairobi County in Kenya. The study was guided by the following research objectives: To assess the effect of credit accessibility on the sustainability of SME’s, to determine the debt rating and performance of SME and to determine the favorability of MFI credit terms in comparison to those of the traditional banking institutions.

This study used a descriptive research design to find out the effect of Microfinance credit on the performance of SME’s in Nairobi County in Kenya and this involved the calculation of mean and standard deviation of the variables under study. The population for the study incorporated all the accounts and finance managers working with manufacturing SME’s in Nairobi County found in various areas in Nairobi. The researcher issued a total of 59 questionnaires and only 50 were filled and returned representing a response rate of 85% which was considered appropriate for the study. Statistical Package for Social Sciences (SPSS) was used for data analysis. A correlation and regression analysis was undertaken to investigate how the various variables relate to each other.

An analysis of the borrowing revealed that 74% had borrowed loans from rotating savings and credit association or chamas. The findings revealed that respondents agreed that they rely on SME credit financing for our business (Mean=4.38, SD=1.105). It was also noted that SME credit has been beneficial in expanding this business (Mean=4.18, SD=1.380). It was noted that the convenient location of financial institution was not a factor when seeking funding (Mean=3.54, SD=1.216). Despite this, quality of service of financial institution’s staff (Mean=4.18, SD=1.058), and low interest rate/cost of borrowing
(Mean=4.66, SD=1.189) as well as convenient repayment period (Mean=4.04, SD=1.087) were important in the SME sustainability. Similarly, absence of requirement for immovable property as collateral was also considered necessary (Mean=4.12, SD=0.922). Person correlation test carried out to determine the relationship between SME Sustainability and Credit Sustainability show that there was a negative and insignificant correlation between SME Sustainability and credit sustainability, $r(50)=-0.50 \ p>0.05$

It was established that micro-finance institutions are particularly important for startups; high growth and innovative SME’s (Mean=4.06, SD=0.818). Large institutions have comparative advantages in transactions lending’s than small SME’s (Mean=4.00, SD=1.429). It was however affirmed that good rating enables SMEs to access to funds at cheaper rates and better terms (Mean=4.08, SD=0.877). Rating facilitates prompter credit decisions from Banks on proposals of SMEs (Mean=4.08, SD=0.665). Person correlation test was carried out to determine the relationship between Debt Rating and Performance Of SME’s and the results show that there was a positive and significant correlation between debt rating and performance of SME’s, $r (50)=.754 \ p<0.05$. A simple linear regression analysis was used to establish how debt rating affect performance of SMEs. The model summary as presented in Table 4.13 shows that debt rating explained 55.9% of the variability of performance of SMEs ($R^2=0.559$, $F(1,48)=1, \ p<.05$) and the strength of the relationship ($r 0.754$).

From the analysis it was revealed that respondents disagreed that due to repeated effects many SMEs borrowers have been denied loans for various unacceptable reasons like ethnicity or sex (Mean=2.44, SD=1.580). Respondents also disagreed that borrowers have shielded away from applying for external funding to avoid the stringent due to bureaucratic systems (Mean=2.88, SD=1.172). Respondents however agreed that among problems that hinder SME’s from accessing credits is management (Mean=4.76, SD=1.117). It was also noted that respondents disagreed that they do not apply for loans from micro finance and banks due to fear of being rejected (Mean=2.00,SD=0.857). Despite this, respondents did agree that banks are to blame for poor and difficult evaluation of SMEs creditworthiness (Mean=4.08, SD=1.441). Also compared to MFIs banks ask for high collateral in order to select profitable and reliable clients (Mean=4.34, SD=1.154). The findings revealed that SMEs struggle to access finance from banks due to stringent collateral requirements (Mean=4.48, SD=1.334). Finally it was also noted that it
is difficult for new firms to obtain bank financing due to the issue of information asymmetry and collateral requirements (Mean=4.30, SD=1.249).

5.3 Discussions

5.3.1 Effect Of Credit Accessibility On The Sustainability Of SME’s

An analysis of the borrowing revealed that 74% had borrowed loans from rotating savings and credit association or chamas. The findings revealed that respondents agreed that they rely on MFI credit financing for our business (Mean=4.38, SD=1.105). This sentiments have been expressed by the World Bank (2009) report where it was noted that SME’s, are viewed as uncredit worthy due to lack of assets which they would use as collateral against credit facilities by main stream banks. Chandrasekhar (2004) findings claimed that this therefore makes micro finance institutions (MFI’s) play a major role in filling the gap for financial services among low income earners, majority of them being women. Services provided by MFI’s are flexible and tailored to meet the financing needs of women in rural and urban settings.

The findings reveal that MFI credit has been beneficial in expanding this business (Mean=4.18, SD=1.380). This highly supports Kevan and Wydick (2001) finding the most of the SME’s that have sorted for loans from micro finance institutions have experienced growth. A strong relationship has also been created between the rate of employment and credit advanced to SME’s. due to the reducing number of unemployed adults in Kenya, there has been a great economic growth. Fillipetti and Archibugi (2011) confirm that as such the rate of employment has grown from a mean of 2.09 employees per SME to a mean of 3.48 employees per SME in the last four years. The reasons cited include increased business activities (increased assets, investments, output, net sales) that required more human capital to manage.

Despite this, quality of service of financial institution’s staff was important (Mean=4.18, SD=1.058). This is in line with Jeffery (2013) study to investigate the role of staff in the informal governance over IMF lending. The finding showed that indeed when country officials are unable to commit to policy goals of the IMF, the IMF staff may bypass the formal channel of policy dialogue through informal contacts and negotiations with more like-minded actors beyond the policymaking process. Exercising informal governance in
these ways, the staff is motivated to offer very favorable treatment to borrowers thus achieve success and an opportunity to support officials who share their policy beliefs.

Similarly, absence of requirement for immovable property as collateral was also considered vital (Mean=4.12, SD=0.922). Bougheas et al. (2005) contend that collateral is a critical factor for SMEs in accessing debt finance. Collateral reduces risk of a loan by giving the loaner a claim on a tangible asset without diminishing any of its claims on the outstanding debt. Coco (2000) point out that collateral aids firms from asymmetries in valuation of projects, and risk of borrowers, it also reduces moral hazard problems. Barbosa and Moraes (2004) argue that SMEs owners/entrepreneur that invest in tangible assets benefit from higher financial leverage as they borrow at lower interest rates by using such assets as collateral.

The findings also show that low interest rate/cost of borrowing was vital in determining SME performance (Mean=4.66, SD=1.189). Irjayantia and Azis (2012) study to investigate the barrier, factors and potential solutions for Indonesian SMEs revealed that economic conditions faced by SMEs may include many aspects such as fiscal and monetary policy, inflation, interest rates, and currency exchange rate.

5.3.2 Debt Rating and Performance of SME’s

Micro-finance institutions are particularly important for startups; high growth and innovative SME’s (Mean=4.06, SD=0.818). same has been established by OECD (2010) report where it was noted that micro-finance institutions are particularly important for this necessitates the need to broaden the range of financing instruments available to SME’s and entrepreneurs, in order to enable them to continue to play their role in growth, innovation and employment.

Large institutions have comparative advantages in transactions lending’s than small SME’s (Mean=4.00, SD=1.429). The failure of specialized financial institutions to meet the credit oriented financial system for those considered uncreditworthy. Especially women have formed savings groups where they have greater access to informal credit facilities than to formal sources, this according to Peachey and Roe (2006) is a challenge and access to finance should be considered as a basic need as this has become a major problems that hinder SME’s from accessing credits is management. Due to their small size, a simple management mistake is likely to lead to sure death of the enterprise.
It was however affirmed that good rating enables SMEs to access to funds at cheaper rates and better terms (Mean=4.08, SD=0.877). Wang Wenying (2004) affirmed this and added that to make the process flawless, SMEs rating should not only concern enterprises, but also take the enterpriser into account as well. He adds that this needs to be based on their personal track record of tax duty, laws, social, commercial insurance, personal deposit and debt, and thus better contribute to predicting the SMEs credit risk.

Rating facilitates prompted credit decisions from Banks on proposals of SMEs (Mean=4.08, SD=0.665). According to Berger and Udell (2006) traditional debt finance, the extension of the credit is primarily based on the overall creditworthiness of the firm and the lender considers the expected future cash flow of the firm as the primary source of repayment. However, the techniques to assess and monitor the firm’s creditworthiness, thus addressing the problem of information asymmetry between lender and borrower, may vary significantly. Liberti and Mian (2009) note that different lending technologies combine different sources of information about the borrower, screening and underwriting procedures, structure of the loan contracts, monitoring strategies and mechanisms. The literature distinguishes transaction lending, based primarily on ‘hard’ quantitative data, and relationship lending, largely based on ‘soft’ qualitative information.

Person correlation test was carried out to determine the relationship between Debt Rating and Performance Of SME’s and there was a positive and significant correlation between debt rating and performance of SME’s, $r (50) = .754 \ p < .05$. Similarly, a simple linear regression analysis was used to establish how debt rating affect performance of SMEs and it explained 55.9% of the variability of performance of SMEs ($R^2 = 0.559, F(1,48)=1, \ p < .05$). Chou and Tenguh (2008) also research on the relationship between bank performance and credit risk management established that there is a significant relationship between financial institutions profitability and credit risk management and as such concluded that credit risk management results in better performance. They concluded that it’s very importance that financial institutions practice prudent credit risk management and protect the investor’s interests. In other research Matu (2008) carried out a study on the sustainability and profitability of microfinance institutions and established that efficiency and effectiveness were the main challenges facing Kenya on service delivery. Soke Fun Ho and Yusoff (2009) study on credit risk management
strategies of selected financial institutions in Malaysia noted that banks suffer losses
that stem from default as a result of customers failure to meet obligations in relation to
lending, trading, settlement and other financial transactions.

5.3.3 Favorability of MFI Credit Compared To Traditional Banking Institutions

Respondents agreed that among problems that hinder SME’s from accessing credits is
management (Mean=4.76, SD=1.117). European Microfinance Network (2012)
highlighted that given a choice, a majority of micro-entrepreneurs would prefer
microcredit to a regular bank loan because socially-oriented MFIs screen loan applicants
less rigorously than regular banks. MFIs are also appealing because besides having
attractive credit conditions, they also take the initiative to provide business guidance to
their borrowers. Banks therefore consider MFIs as a threat to their functioning. Due to
this fear the banking Sector in developed countries like Europe have created new
regulations for MFI’s like introducing limiting loan ceilings, interest cups and setting
criteria for eligibility in borrowing in order to ensure their survival in business.

It was also noted that respondents disagreed that they do not apply for loans from micro
finance and banks due to fear of being rejected (Mean=2.00, SD=0.857). Deakins et al
(2010) confirmed that in developed countries the division between businesses served by
regular banks and businesses served by MFIs is blurred, some MFIs serve client who
have the ability to borrow from banks. Deakins et al (2010) notes that banking sector’s
response to the development of microcredit is mixed. Some banks have ventured into the
micro finance business by creating MFIs and collaborating with MFIs. On one hand, the
banking sector has been asking for better market delimitation and strict supervision of
microfinance activities adding to the challenges of SME borrowing.

Despite this, respondents did agree that banks are to blame for poor and difficult
evaluation of SMEs creditworthiness (Mean=4.08, SD=1.441). Idowu (2010) notes that
due to repeated effects where many SMEs borrowers have been denied loans for various
unacceptable reasons, like ethnicity or sex borrowers have shied away from applying for
external funding to avoid the stringent due bureaucratic systems some firm owners do not
even apply for loans for fear of being rejected.
Also compared to MFIs banks ask for high collateral in order to select profitable and reliable clients (Mean=4.34, SD=1.154). Ghimire and Abo (2013) noted that in West African community, SMEs were found to be incapable of providing audited financial statements and accounting reports based on the accounting standards prescribed by the Organization for the Harmonization of Business Law in Africa (OHADA) increasing the reluctance of banks to provide loans required by SMEs. Otherwise, the problem of information asymmetry reflects a risk imbalance in disfavor of the firms. This problem is linked to the inadequate business experience and financial illiteracy of SMEs promoters as well as insufficient risk-based credit assessment of the credit application. Banks often increase interest on loans so as to compensate for this issue. They can however not increase the interest rate beyond a certain level for fear of attracting bad borrowers with unsound projects. Banks are therefore forced to focus on alternative criteria like heavy screening and asking for high collateral in order to select profitable and reliable clients.

The findings revealed that SMEs struggle to access finance from banks due to stringent collateral requirements (Mean=4.48, SD=1.334). Azende (2012) on a study in Nigeria notes that SMEs struggle to access finance from banks due to stringent collateral requirements and inefficient guarantees schemes. Young SMEs have little tangible assets to give as collaterals. SMEs in west Africa were also found incapable of providing audited financial statements and accounting reports required by banks. In the even accounts were provided, a lack of competent and credible accounting practices interfere with the quality of the information provided thereby increasing reluctance of the banks to provide loans. Banks inturn make it harder for SME’s by further increasing interest as a way of compensating (Ghimire, & Abo 2013

5.4 Conclusion

5.4.1 To assess the effect of credit accessibility on the sustainability of SME’s

Most SMEs have relied on rotating savings and credit association or chamas and MFI credit financing for the business this has been beneficial in expanding this business. In order to be able to approach the MFIs, quality of service of financial institution’s staff was important. Other factors that affect credit accessibility for SMEs include interest rate/cost of borrowing as well as the repayment period. Collateral has also played a role in the credibility.
5.4.2 Debt Rating and Performance of SME’s

Micro-finance institutions play a big role in the growth of SME’s, in addition, depending on the size of the firm large institutions have comparative advantages in transactions lending’s than small SME’s. At the same time the good rating is crucial to SMEs as they facilitate access to funds at cheaper rates and better terms. This has also resulted in the rating facilitates which prompts credit decisions from Banks on proposals of SMEs. There was a positive and significant correlation between debt rating and performance of SME’s,

5.4.3 Favourability of MFI Credit Terms In Comparison To Traditional Banking

Reasons such as ethnicity or sex play no role in the determination of SMEs being awarded loans. Despite this the main areas of concern hindering SME’s from accessing credits is management. On the other hand, banks have played a role in the evaluation of SMEs creditworthiness, this is because they demand high collateral in order to select profitable and reliable clients, another challenge that face this institutions include issue of information asymmetry and collateral requirements (Mean=4.30, SD=1.249).

5.5 Recommendations

5.5.1 Recommendation for Improvement

5.5.1.1 Effect Of Credit Accessibility On The Sustainability Of SME’s

MFI need to review the requirement needed for SMES credit financing. To boost this, the quality of service offered by financial institution’s staff should be good enough to attract more SMEs. There is also a need to review the cost of borrowing as well as set up convenient repayment period in order to guarantee MFI sustainability. Similarly, SMES need to invest more on immovable property as this is considered as collateral and thus increase their chances of getting credit accessibility.

5.5.1.2 Debt rating and performance of SME’s

There is a need of educating the SMEs about what they need to do in order to have good rating and be able to access to funds at cheaper rates and better terms. Person correlation test was reveal a positive relationship between debt rating and performance, thus imply the need to push for good debt ratings. More SMEs need to push for rating by independent, trusted third party in order to increase their credit worthiness. They should also be encouraged to undertake the rating to ascertain the strengths and weaknesses of
their existing operations and take corrective measures to enhance their organizational strength.

5.5.1.3 Favorability of MFI Credit Terms In Comparison To Traditional Banking

Borrowers should be encouraged to seek alternative funding if need be in order to avoid the bureaucratic systems. Management also require training to better handle the financial aspects of the business. The loan providers need to give the SMEs a chance to grow by ensuring that they gain their confidence. The SMEs also need to offer the necessary data to avoid information asymmetry challenges arising from poor or non-existent financial records which diminish creditworthiness.

5.5.2 Recommendation for Further Studies

While the model applied for this study examined relevant to SME performance by reviewing credit accessibility, debt rating and favourability of MFI credit terms to those of traditional banking institutions in Nairobi. A similar study need to be done in other counties so as to generalize the findings. In addition, variables such as entrepreneurs characteristics, SME characteristics of SMEs and management as well as customers and markets intelligence need to be studied to establish how they influence SMEs performance.
REFERENCES


QUESTIONNAIRE

Section A. SOCIAL DEMOGRAPHIC INFORMATION

1. What is your gender?
   - Male
   - Female

2. How old are you? (Years)
   - Less than 30:
   - 31-40:
   - 41-50:
   - Above 50:

3. What is your level of education?
   - Primary
   - Secondary
   - College
   - University

4. How long has the business been in operation?
   - less than 1 year
   - 2 to 5 years
   - 6 to 10 years
   - more than 10 years

5. Please indicate the number of employees working for your organization
   - 1-5:
   - 6-10:
   - 11-50
   - Over 50:

Section B: Effect of Credit Accessibility on the Sustainability of SME’s

6. Have you borrowed money from a rotating saving and credit association/Chama in the last three years?
   - Yes
   - No
b. If yes, to the above questions, how much in total have you borrowed from the association in the last three years. Tick appropriately Year

<table>
<thead>
<tr>
<th>Amount</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 100,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>100,001-150,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>150,001-200,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Above 200,000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

7. State your level of agreement on the following statements related to MFI Credit Accessibility where 5 strongly agree, 1 strongly disagree

<table>
<thead>
<tr>
<th>MFI Credit Accessibility</th>
<th>5</th>
<th>4</th>
<th>3</th>
<th>2</th>
<th>1</th>
</tr>
</thead>
<tbody>
<tr>
<td>We rely on MFI credit financing for our business</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MFI credit has been beneficial in expanding this business</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>MFI credit is easy to access</td>
<td></td>
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<td></td>
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<tr>
<td>MFI credit attracts reasonable interest rates</td>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

8. Kindly rate the importance of the following factors when getting a loan from a micro financial institution (Rate from 1 to 5, with 1 being least important and 5 very important):

<table>
<thead>
<tr>
<th>Statement</th>
<th>5</th>
<th>4</th>
<th>3</th>
<th>2</th>
<th>1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Convenient location of financial institution</td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>MFI have assisted us in disbursement of loan (quick processing of loan application)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Quality of service of financial institution’s staff</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Low interest rate/cost of borrowing</td>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Convenient repayment period</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Absence of requirement for immovable property as collateral
Availability of other financial services from same financial institution

Section C: Debt rating and performance of SME’s
10. State your level of agreement on the following statements related to MFI Credit rating, where 5 strongly agree, 1 strongly disagree

<table>
<thead>
<tr>
<th>Statement</th>
<th>5</th>
<th>4</th>
<th>3</th>
<th>2</th>
<th>1</th>
</tr>
</thead>
<tbody>
<tr>
<td>micro-finance institutions are particularly important for startups; high growth and innovative SME’s</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Large institutions have comparative advantages in transactions lending’s than small SME’s)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>One of the problems that hinder SME’s from accessing credits is management</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Low productivity is a barrier in SME’s accessing funds</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Benefits of Rating</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rating by independent, trusted third party has led into increased credit worthiness of SMES</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rating enables SMEs to ascertain the strengths and weaknesses of their existing operations and take corrective measures to enhance their organizational strength</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Good rating enables SMEs to access to funds at cheaper rates and better terms</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Rating facilitates prompter credit decisions from Banks on proposals of SMEs

Good rating enhances the acceptability of the SMEs with their customers and buyers.

Section D: Favorability of MFI credit terms in comparison to those of the banks

12. State your level of agreement on the following statements related to financing in microfinance and traditional banking (where 5 strongly agree, 1 strongly disagree)

<table>
<thead>
<tr>
<th>Statement</th>
<th>5</th>
<th>4</th>
<th>3</th>
<th>2</th>
<th>1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Due to repeated effects many SMEs borrowers have been denied loans for various unacceptable reasons like ethnicity or sex</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Borrowers have shielded away from applying for external funding to avoid the stringent due bureaucratic systems</td>
<td></td>
<td></td>
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<td>One of the problems that hinder SME’s from accessing credits is management</td>
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<td>Low productivity is a barrier in SME’s accessing funds</td>
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<td>We do not apply for loans from micro finance and banks due to fear of being rejected</td>
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<td>SMES have been granted full amount of credit applied for by microfinance organizations over the years</td>
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<td>SMES have sought credit from traditional banking institutions compared to micro finance institutions</td>
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<td>Information asymmetry challenges arising from poor</td>
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</table>
or non-existent financial records by an SME limits the borrower’s creditworthiness

Evaluation makes it impossible for banks to acquire loans from banks

Banks are to blame for poor and difficult evaluation of SMEs creditworthiness

Compared to MFIs banks ask for high collateral in order to select profitable and reliable clients.

SMEs struggle to access finance from banks due to stringent collateral requirements

It is difficult for new firms to obtain bank financing due to the issue of information asymmetry and collateral requirements

**SECTION E: Performance of SMEs**

13. State your level of agreement on the following statements related to performance of SMEs (where 5 strongly agree, 1 strongly disagree)

<table>
<thead>
<tr>
<th>Statement</th>
<th>5</th>
<th>4</th>
<th>3</th>
<th>2</th>
<th>1</th>
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</thead>
<tbody>
<tr>
<td>Effective entrepreneurship has led to growth of SMEs in the country</td>
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<td>Appropriate human resource is vital for increased profitability in SMEs</td>
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<td>SMEs has used marketing information to improve profitability</td>
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<td>Use of Information Technology plays a major role in SME effectiveness</td>
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