FACTORS INFLUENCING ACCESS TO FINANCE BY SMALL AND MEDIUM SIZE ENTERPRISES IN KENYA: A CASE OF SMEs IN MERU COUNTY

BY

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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 - Africa in Nairobi for academic credit.

Signed: ___________________________ Date: __________________________
Wilberforce Mutuma Muriuki (639326)

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

Signed: ___________________________ Date: __________________________
Mr. Kepha Oyaro

Signed: ___________________________ Date: __________________________
Dean, Chandaria School of Business
ABSTRACT

The general objective of the study was to establish the factors influencing access to finance by SMEs in Meru County. The study was guided by the following study objectives that were driven to determining the effect of lending requirements on access to finance by SMEs in Meru County, to assess the influence of financial literacy on access to finance by SMEs in Meru County, and to determine the effect of firms’ characteristics on access to finance by SMEs in Meru County.

This study adopted a descriptive survey research design. The target population constituted of registered SME’s in Meru County in Kenya. The entire target population comprised of 1650 registered SME’s. The sampling frame was obtained from office of economics and statistical data in Meru County. Stratified sampling technique was adopted for this study, since the study was looking at different heterogeneous categories of SMEs within Meru County, stratified sampling was ideal. For this study, Yamane (1967) formula was used to determine the sample size of 92 SMEs. The study utilized a questionnaire as a tool to collect primary data. The Statistical Package for Social Sciences (SPSS) was used to analyze descriptive statistics (percentages and frequencies); and inferential statistics that involved correlation analysis and regression analysis. Analyzed data was presented using tables and figures.

The study showed that entrepreneurs normally did not use title deeds (business or land) in order to access a loan, and their loan security had to cover their loan amount or surpass it for it to be accepted by the bank. The entrepreneurs had used their business loans for their personal and private use although the use of security to pick a business loan, had slightly reduced their chances of misusing loans taken for business growth. The study revealed that the use of security ensured that the entrepreneurs did not invest in high risk projects, and their willingness to pledge security for a loan increased their probability of acquiring a bank loan.

The study revealed that SMEs in Meru County did succeed in accessing financial credit even though strict loan conditions were their major challenge in accessing loans. Most banks believe that small businesses do not have the capacity to repay a loan in case they default, and the SMEs’ owners were in agreement with the decision of banks denying
them a loan when they viewed them to be high risk defaulters. The study showed that SME owners incurred some financial costs in order to receive financial credit from banks or other financial institutions, and there were a lot of costs (transaction costs) that made borrowing very expensive for their businesses. The study revealed that one needs education and skills in order to run a business.

The study showed that the size and age of SME businesses greatly affected their ability to acquire a loan, and that most of the businesses did not struggle to provide required financial information by banks which did not limit their loan accessibility, however, their businesses had fewer assets that could be used as security while accessing bank loans. The study revealed that the number of years that entrepreneurs had been in business did not affect their ability to access bank loans, however, business that had been running for many years indicated they had the ability to withstand tough economic conditions, leading to easy access to loans.

The study concludes that the entrepreneurs did not have poor access to bank loans, because they were more than likely to default on their loan repayment, and that none had failed to secure a business loan because they could not meet the bank’s requirements. It was also concluded that business profitability was not a yardstick used by banks to provide them with loans, and lack of reliable business information had led to businesses accessing loans at high interest rates since banks paid much attention to accounting information when entrepreneurs applied for loans.

The study recommends that business entrepreneurs of SMEs should ensure that they keep an audited financial record for their businesses. The study also recommends that the government policy makers put in place financial regulations that would lower the cost of acquiring loans for SMEs and other organizations in general. The study also recommends that business entrepreneurs of SMEs should ensure that they have reliable information of their business at hand. This would facilitate the ability of SMEs to access and acquire loans from banks and other financial institutions.
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LIST OF ACRONYMS

GDP: Gross Domestic Product
ILO: International Labor Organization
IPO: Initial Public Offering
MFIs: Micro-Finance Institutions
NBFIs: Non-Bank Financial Institutions
NBFs: Non-Bank Financials
NGO-MFIs: Non-Governmental Organizations-Micro-Finance Institutions
OECD: Organization for Economic Co-operation and Development
SACCOs: Savings and Credit Cooperative Organizations
SMEs: Small and Medium Enterprises
SPSS: Statistical Package for Social Studies
SRS: Simple Random Sampling
SSA: Sub-Saharan African
UK: United Kingdom
US: United States of America
USD: US Dollars
USIU-A: United States International University - Africa
VC: Venture Capital
CHAPTER ONE

1.0 INTRODUCTION

1.1 Background of the Study

Financial access is critical for the growth of small and medium-size enterprises (SMEs). It allows entrepreneurs to innovate, improve efficiency, expand to new markets, and provide millions of jobs (Ayyagari, Asli & Vojislav, 2012). Yet, in developing countries, the majority of SMEs are unable to acquire the financing they need to reach their potential. Financing SMEs in the developing world can be risky and expensive for lenders, leading to an estimated financing gap of one trillion US Dollars (USD) (International Finance Corporation, 2011).

In developed countries, financial institutions assess SME loan applicants using information supplied by credit bureaus (Deakins et al., 2008). In emerging markets, however, strong credit bureaus and other financial infrastructure often do not exist. Instead, banks rely on time-consuming methods to obtain credit histories directly from loan applicants (Morck & Yeung, 2010). Incomplete financial records and unverifiable client information further increase the cost of assessing SME loan applications, making banks reluctant or unable to lend to SMEs (Ayyagari, Asli & Vojislav, 2012). However, the SME sector in many developing countries is large and represents a very promising frontier for lenders. To capitalize on this, some banks have begun implementing innovative screening mechanisms to reduce the cost of lending (Deakins et al., 2008; Morck & Yeung, 2010).

Banks traditionally require that clients provide collateral such as land or real estate to secure their loans. However, many creditworthy SMEs do not have the type of collateral required by commercial lenders and therefore have trouble accessing needed financing. To remove this barrier, some governments and financial institutions are relaxing collateral requirements or eliminating them altogether (Osmani, 2009). For instance, the Colombian government, with support from the International Finance Corporation, recently introduced a new Secured Transactions Reform that provides a legal framework for accepting movable collateral such as vehicles, machinery, accounts receivable, and inventory (Deakins et al., 2008). The reform has two main pieces. First, it establishes a unified online registry for all movable assets used as collateral, so that potential creditors can
verify whether assets offered as collateral are subject to other obligations. Second, the law improves enforcement in cases of default. By reducing banks’ risk in accepting alternative forms of collateral, the reform is expected to increase access to credit for SMEs (Villoria, 2009).

In Africa, the major challenges facing SMEs include: lack of a supportive governance framework. SMEs suffer due to lack of legal framework that protects interests, harassment from local authorities’ unsupportive tax regime and exposure to corruption (Kakuru, 2013). The second reason is lack of adequate access to credit. SMEs have little access to finance, which thus prohibit their emergence and eventual growth. This has not been easy for SMEs due to the stringent credit terms offered by financial institutions (Obura & Matuvo, 2011). Most SMEs do not have access to finance due to lack of minimum requirements from commercial banks, and these banks are hesitant in lending to SMEs due to lack of collateral, credit history, financial statement and banking history (Wanjohi, 2010).

The main sources of capital for SMEs in Africa and particularly in Kenya are retained earnings, borrowings from friends, family capital and informal savings, which are unpredictable, not very secure and have little scope for risk sharing. Access to final finance is poor because of the high risk of default among SMEs and due to inadequate financial facilities (Kauffmann, 2010). In a recent study, Atieno (2009) found that although informal finance provides easier access to credit, it is confined to specific activities and at lower levels of income, thus limiting its use.

SMEs have become important players in the Kenyan economy, but at the same time they continue to face constraints that limit their development and financial performance. Lack of access to financial services as observed is one of the main constraints for SMEs, and it is brought about by the segmented and incomplete nature of financial markets (Gatari, 2012). This increases transaction costs associated with financial services. On the supply side, most formal financial institutions consider SMEs un-creditworthy, thus denying them credit. Lack of access to financial resources has been seen as one of the reasons for the slow growth of firms. Difficulties in accessing credit has held back the SME sector in
Kenya as most financial institutions view them as unstable and often place tighter lending requirements before advancing credit (Atieno, 2009).

Access to external resources is needed to ensure flexibility in resource allocation and reduce the impact of cash flow problems. Firms with access to funding are able to build up inventories to avoid stocking out during crises, while the availability of credit increases the growth potential of the surviving firms during periods of macroeconomic instability (Ayyagari, Asli & Vojislav, 2012). Firms without access to bank funding are more vulnerable to external shocks. Credit also enables individuals to smooth out consumption in the face of varying incomes, provides income for investment and improves ability to cope with unexpected expenditure shocks. But lack of collateral and the high possibility of default can prevent individuals and small firms from obtaining credit (Gatari, 2012).

According to Obura and Matuvo (2011), access to finance allows small businesses to undertake productive investments and contribute to the development of the national economy and alleviation of poverty in most of Sub-Saharan African (SSA) countries. External finance for small and medium enterprises is essential for boosting start-up businesses. In addition, without external finance, small and medium enterprises will probably not be able to compete in an international market, to expand the businesses and strike linkages of business with the large firms (Villoria, 2009). Further, access to finance is the most serious barrier to expansion of businesses and start-ups which have been mentioned by existing SMEs and potential operators.

In all economies, developing and developed ones, easy access to credit is a very important factor in accelerating investments, job creation, transforming small businesses into strong enterprises (Morck & Yeung, 2010). For example, despite the United Kingdom (UK) having one of the best banking and financial systems in the world, successive governments have made this possible by working closely with lenders and consumer advisers (Osmani, 2009). This has resulted in a system that gives consumers access to credit at any time of day or night, every day of the year. Consumers can apply for credit over the phone or on the internet and get a decision almost instantly (Merton & Poll, 2008).
Credit constraints operate in variety of ways in Kenya where undeveloped capital market forces SMEs to rely on self-financing or borrowing from friends or relatives. Lack of access to long-term credit for small enterprises forces them to rely on high cost short term finance (Atieno, 2009). These difficulties stem from the more formal lending institutions which tend to rate all SMEs equally as credit unworthy (Konosuke & Minoru, 2003). However, the emergence of less formal institutions like Micro-Finance Institutions (MFIs) and Savings and Credit Cooperative Organizations (SACCOs) do not ease this burden. These micro-credit institutions face limited expansion because of their limited funds. Their mainly short-term finance means they cannot easily turn the savings they collect into medium or long-term loans (Wanjohi 2010).

Improving access to funding for small and medium-sized enterprises is crucial in fostering entrepreneurship, competition, innovation and growth in Kenya. Access to sufficient and adequate capital to grow and further develop their activities is a difficulty faced by many Kenyan SMEs (Gatari, 2012). This situation is compounded by the difficulties in accessing finance as SME financing is considered by many financial providers as a high risk activity that generates high transaction costs and/or low returns on investment. Moreover, SMEs need to meet the challenge of adapting to the changing financial environment and the increasing complexity and extent of financial acquisition (Wanjohi 2009).

1.2 Statement of the Problem
According to Wanjohi, (2010), SME’s are a key component of the economies throughout the world. In Kenya, SME’s have the potential to contribute significantly to economic growth and poverty reduction through increased production and employment. This role has long been recognized by the Government of Kenya. Vision 2030, Kenya’s long-term development plan, places a strong emphasis on the sector (Atieno, 2009). One of the pillars in vision 2030 that was defined to spur growth of SME’s is financial pillar that led the government to set up a youth fund for youthful entrepreneurs, however, the difficulties that SMEs encounter when trying to access financing can be due to a great range of reasons like the firm’s characteristics, financial characteristic and entrepreneurial skills and experience. Other reasons may be due to inadequate financial products and
services, regulatory rigidities or gaps in the legal framework, lack of information on both the bank’s and the SMEs’ side (Gatari, 2012).

There is a myriad of studies that have investigated the relationship between lending terms and access to credit. For instance, Zeller (2014) observed that, collateral value requirements deter SME borrowers from seeking credit. Yehuala (2008) found that loan repayment period negatively influences access to credit as it has a major bearing on the total amount to be repaid. Specifically, longer repayment period increases interest to be paid in the long run. Kakuru (2013) found that when SMEs perceive repayment period as inflexible, they will not apply for the loans. Mutesasira et al. (2011) also found out that short repayment periods do not meet SMEs long term credit needs and as a result, SMEs take any amount of loan that the banks are willing to offer them.

Mounting evidence indicates that the less financially literate are likely to face more challenges with regard to debt management, savings and credit, and are less likely to plan for the future. Miller et al. (2009) indicates that lack of financial literacy is often tied to lack of access to financial products including credit or failure to use them even when they are available. Calvert, Campbell and Sodini (2005) also argue that households with high financial literacy and greater financial sophistication are more likely to participate in risky assets’ markets and invest more efficiently. Other studies (ACCA, 2012; Johnson, 2014; Kidwell & Turrisi, 2014) confirm the view that financial literacy explains variances in access to credit by borrowers. Moreover, Cole, Sampson, and Zia (2009) found that higher financial literacy is significantly associated with greater use of bank services.

Extant literature associate firm characteristics like firm size to the ability of firms to access finance. For example, Honhyan (2009) found that larger firms tend to be more diversified and fail less often, so size can be an inverse proxy for the probability of bankruptcy. Cassar (2004) argues that it may be relatively more costly for smaller firms to resolve information asymmetries with debt providers. Consequently, smaller firms may be offered less debt capital. In addition, transaction costs are typically a function of scale and may be higher for smaller firms. It is also possible that small firms have fewer opportunities to raise capital because capital markets are out of reach due to their size. More recently, Dun and Girma (2012) using firm level data from China spanning the
period 1998-2005 found that bigger firms source capital from the bank while smaller firms use self-raised finance.

As observed, there are many studies that have been conducted on determinants of financial inclusion of SMEs, but they are wide and varied from region to region. The results do not offer a conclusive results of how the various factors (lending requirements, financial literacy, and firm characteristics) influence the SMEs access to credit. This suggests that there exists a financing gap when it comes to SMEs’ funding, and therefore it was the purpose of this study to determine factors influencing access to finance by SMEs.

1.3 General Objective
The general objective of the study was to establish the factors influencing access to finance by SMEs in Meru County.

1.4 Specific Objectives
1.4.1 To determine the effect of lending requirements on access to finance by SMEs in Meru County.
1.4.2 To assess the influence of financial literacy on access to finance by SMEs in Meru County.
1.4.3 To determine the effect of firms characteristics on access to finance by SMEs in Meru County.

1.5 Significance of the Study
The research was expected to benefit various groups of stakeholders as follows:

1.5.1 SMEs
The loans advanced to small scale traders come with costs. That is, the interests charged on the principal sum. Therefore the traders are under the obligation to pay the principal sum pus the interest, at the end of the agreed duration. In some cases, the traders are unable to pay in time leading to foreclosure on their businesses. The study may therefore be significant to the SMES since it establishes whether the loan facilities available for
SMEs are worth the risk of losing their businesses, through liquidation by financiers in case of default.

1.5.2 Financial Institutions
The research has generated vital information that may assist financial institutions to develop solutions to narrow the SME financial needs gap and better serve their stakeholders. Managers of financial institutions may have an in depth understanding of how their policies affect SMEs’ access to finance, and thus, they may review these policies and make them inclusive for SMEs.

1.5.3 Policy Makers
The research generates vital information that may assist policy makers in government and those involved in improving SMEs in the country to develop solutions to narrow the SME financial needs gap and better serve their stakeholders. Policy makers may gain a profound understanding of SMEs’ challenges with regards to access to finance, and therefore provide solutions through better policy formulation.

1.5.4 Meru County Government
The research generates vital information for Meru County Government. It will enable the county to understand the challenges faced by its SME businesses. This information, may assist the county and its policy makers in developing better policies that may increase SME’s access to finance and this improve their performance.

1.5.5 Academicians and Researchers
The study forms a profound base of the study topic on SMEs and access to finance. The results provide an in depth review of the case in Meru County, and this may act as a source of reference material for future academic research on other related topics or expansion of knowledge on the same in other counties. The study provides research gaps that it did not fill, and thus future scholars may pursue the same.

1.6 Scope of the Study
This study focused on SMEs in Meru County in Kenya. The study focused on factors influencing SMEs’ access to financing, but limited to collateral requirements, lending
procedures, and measures taken to enhance access to SME financing. The study took place between January and April 2018. The study population were all registered SMEs in Meru, out of which a number of SMEs was selected for the purpose of this research. The study faced constraints in terms of collecting data. To overcome this, the researcher ensured to use language that was easily understandable to the entrepreneurs. The researcher also ensured that a formal letter addressing the purpose of the study accompanied the questionnaire to facilitate data collection.

1.7 Definition of Terms

1.7.1 Access to Finance
Access to finance is defined as the formal channels through which SMEs can be able to get finances for their business start-ups and operations at affordable rates or cost (Niskanen, 2010). Access has four key dimensions: physical access, affordability, appropriate features that meet the users’ particular needs and appropriate terms that do not effectively exclude any category of potential user.

1.7.2 Collateral Requirements
Collateral refers to the extent to which assets are committed by borrowers to a lender as security for debt payment (Gitman, 2003). The security assets should be used to recover the principal in case of default. SMEs in particular provide security in form of properties (houses, the businesses, the car, and anything that could actually bring back the principal) in case of default on loans.

1.7.3 Financial Literacy
Financial literacy refers to the ability of an individual to understand how money works—how it is earned, managed and invested (Andoh & Nunoo, 2011). It can also be defined as the ability to make informed judgments and to take effective decisions regarding the use and management of money (Beal & Delpachitra, 2003).

1.7.4 Firms Characteristics
Firm characteristics refer to the business characters of the firm that encourage debt and equity financial providers to invest in such business (Esperanca et al., 2013).
1.7.5 Lending Requirements
Lending requirements have been understood to mean collateral, repayment periods and lending interest rate (Atieno, 2011).

1.7.6 Micro-Financing
Micro-financing is the provision of financial services to low income clients who include customers and self-employed individuals that traditionally lack access to banking and related services (Mwarari 2013).

1.7.7 SME
According to Garrett (2009), a small medium enterprise is considered to be that consisting of 10-99 employees, a turnover of less than Kshs 0.5 million annually and an asset base of Kshs 100,000 or less.

1.8 Chapter Summary
This chapter discusses the background of the study problem as well as given a brief history of SMEs. The chapter has also covered the research problem which examines the factors influencing access to finance by SMEs. The chapter has highlighted the objectives of the study and has come up with specific objectives that guided the study. The chapter ends with study’s significance, scope, and the definition of key terms. Chapter two discusses the literature review of the study. Chapter three discusses the research methodology used in the study. Chapter four presents the study results and findings. Chapter five offers the study discussions, conclusions and recommendations.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction
This chapter presents literature review based on the study specific objectives. Literature review on lending requirements for SMEs, followed by financial literacy, and finally literature review on influence of firm’s characteristics on access to finance by SMEs.

2.2 Lending Requirements and Access to Finance by SMEs
Lending is one of the major activities from which commercial banks make their profit and a greater proportion of the profit of commercial banks comes from lending (Aghion & Bolton, 2012). Banks, the world over, thrive on their ability to generate income through their lending activities. The lending activity is made possible only if the banks can mobilize enough funds from their customers as long as they meet the required terms (Roodman, 2011). Lending requirements have been understood to mean collateral, repayment periods and lending interest rate (Atieno, 2011).

Bank lending is the most common source of external finance for many SMEs and entrepreneurs, which are often heavily reliant on traditional debt to fulfill their start-up, cash flow and investment needs. While it is commonly used by small businesses, however, traditional bank finance poses challenges to SMEs, in particular to newer, innovative and fast growing companies, with a higher risk-return profile (OECD, 2017). Despite the fact that financial institutions have identified the SME sector as a fast growing sector in the country, there are several constraints serving as bottlenecks to SMEs in accessing finance from financial institutions (Kwaning et al., 2015). However, according to IFC (2011), SMEs often have great difficulty accessing financial services in many emerging markets.

When lending to small businesses, the major task of lenders in reducing or avoiding credit risk is to overcome the problem of asymmetric information (Agyapong et al., 2011). Banks that finance SMEs usually face lack of accurate and reliable information on the financial condition and performance of small firms. Thus, in order to extend credit to SMEs, banks’ lending decision is based on the strength of income statements, strength of the balance sheet, long histories, quality of accounts receivable and inventory, history of
the principal owner and transparency of firms through provision of certified financial statements (Vuvor & Ackah, 2011) most of which SMEs do not have.

2.2.1 Collateral Requirements

Mbonyane and Ladzani (2011) state that, collateral requirements refers to the extent to which assets are committed by borrowers to a lender as security for debt payment. The assets pledged should be used to recover the principal in case of default. SMEs in particular provide security in form of fixed assets (houses, the car, and anything that could actually bring back the principal) in the event of default on loans (Aghion & Bolton, 2012). Security for loans must actually be capable of being sold under the normal conditions of the market, at a fair market value and also with reasonable promptness. However, in most banks, in order to finance SMEs and to accept loan projects, the collateral must cover 100% or more, equal to the amount of credit extended or financial product (Mbonyane & Ladzani, 2011).

Sometimes the borrowers divert the funds provided by the lenders for their own personal and private use (Kihimbo et al., 2012). Therefore, the collateral requirements when in place can reduce negative consequences that can arise from improper utilization of the funds by SMEs (Roodman, 2011). It is evident that most SMEs are denied and discriminated by the lenders in providing financing. This is because of the high risk associated with them lacking adequate resources to pledge as collateral (Kihimbo et al., 2012).

Matavire and Duflo (2013), contend that collateral is an important prerequisite for SMEs in order to access bank finance. Collateral reduces the riskiness of a loan by giving the financial institution a claim on the tangible asset without diminishing its claim on the outstanding debt. Rambo (2013), points out that collateral is the lender’s second line of defense. Collateral can solve problems derived from asymmetries in valuation of projects, uncertainty about the quality of projects and the riskiness of borrowers, and problems related to the cost of monitoring or supervising borrowers’ behavior.

Collateral requirements serve as an incentive mechanism because higher collateral enforces a selection of less risky projects (Wanjohi, 2010). This is due to the fact that a
lower-risk borrower has a greater incentive to pledge collateral than a high-risk borrower, because of his lower probability of failure and loss of collateral. The willingness of the entrepreneur to pledge collateral positively influences the quality of credit request as perceived by the bank. Borrowers signal the real value and belief in the quality of the project to the bank (Matavire & Duflo, 2013). Thus, low risk borrowers can signal their status through the provision of collateral, even though literature identifies collateral as a key, contracting tool employed by lenders to reduce the problem associated with asymmetrical information (Kihimbo et al., 2012).

According to Aghion and Bolton (2012), collateral acts as an indicator of the borrower’s creditworthiness. The bank screens firms by offering both loan contracts with higher collateral value with lower interest rates and loan contracts with lower collateral with higher interest rates. Vuvor and Ackah (2011) state that, although risk factors may not be readily observable, lower risk borrowers will nonetheless pledge more and better collateral value than riskier borrowers because this pledge is less costly for borrowers who have lower likelihoods of losing the pledged collateral. Matavire and Duflo (2013) note that, the probability of losing collateral acts as a disciplinary tool for the borrower. Thus, the pledge of collateral leads to a higher level of effort to satisfy loan conditions and meeting loans obligations, reducing a borrower’s default probability. Collateral therefore serves as a tool for resolving moral hazard problems.

Gangata and Matavire, (2013) in their study on challenges facing SMEs in accessing finance from financial institutions, found out that very few SMEs succeed in accessing funding from financial institutions, the main reason being failure to meet lending requirements, chief among them being provision of collateral security. A study was done on challenges faced by SMEs in obtaining credit in Ghana. Based on the responses received through the questionnaires circulated, it became evident that SMEs in Ghana like most SMEs in other countries are faced with major challenges in accessing credit. These challenges were revealed by the study to include, the inability of SMEs to provide collateral and other information needed by banks such as audited financial statement coupled with the high cost of loan in terms of high interest rates making it extremely difficult to access bank loans (Vuvor & Ackah, 2011).
2.2.2 Tangible Assets Availability

Previous researchers (Kihimbo et al., 2012; Aghion & Bolton, 2012; Wanjohi, 2010) suggest that bank financing will depend on whether the lending can be secured by collateral. When other factors are held constant, firms with more intangible assets have limited access to financing, compared to firms with more tangible assets (Aghion & Bolton, 2012). SMEs have fewer collateralizable assets than large firms. This may partly relate to the stage of growth the firm is in (Obwori, 2012). In the earlier stages of the firm, it may have lower retained profits which may hinder it from purchasing fixed assets compared to the larger firms which have a longer history (Mbonyane & Ladzani, 2011). Another reason why small firms have a smaller proportion of fixed assets is the capital constraints faced by them. Because of the need to raise large amounts of capital, it becomes difficult for them to acquire substantial fixed assets (Obwori, 2012).

Access to formal finance is also poor because of the high risk of default among SMEs due to inadequate financial facilities. Matavire et al., (2013), in their study on challenges facing SMEs in accessing finance from financial institutions; A case of Belaway, Zimbabwe found out that SMEs fail to secure loans because of restrictive requirements of the financial institutions, top among them being lack of collateral. Among their recommendations was that the government should play its role of enabling SMEs to access finance from financial institutions. Makena, et al., (2014), in their study on challenges facing women entrepreneurs in accessing business finance in Kenya: A case of Ruiru Township, Kiambu County, and lack of fixed assets was one of the objectives. However, the study found out that lack of tangible collaterals like land was a greater hindrance to credit accessibility by women entrepreneurs. Among their recommendations was that the government should play its role of enabling SMEs to obtain finance from financial institutions.

2.2.3 Group Guarantees Availability

As indicated by Roodman (2011), small business in Africa can once in a while meet the conditions set by money related organizations, which see SMEs as an unsafe in view of poor certifications and absence of satisfactory data about their capacity to reimburse advances. According to Lydiah (2012), the money related markets in the greater part of Africa are immature nonetheless thus gives less monetary instruments. Capital markets are in their early stages, shareholding is uncommon and no long-haul financing is
accessible for SMEs. Non-bank monetary mediators, for example, Micro Finance Institutions, which could have been of a major help in loaning cash to the little SMEs do not have the assets to catch up their clients when they extend.

Wangui and Tirimba (2014), led a review on SME exhibitions in country regions in focal Kenya and discovered that absence of underwriters by smallholders is ordinarily observed as one of the requirements constraining them to profits by credit offices. In any case, much of the time the get to issue, particularly among formal monetary establishments, is one made by the foundations for the most part through their loaning approaches. This is shown as endorsed least advance sums, entangled application methods and confinements on layaway for particular purposes.

2.2.4 Repayment Modes Flexibility

For small scale ventures, solid access to fleeting and little measures of credit is more important, and underlining it might be more suitable in credit programs went for such undertakings (Roodman, 2011). Lydiah (2012), contend that the kind of money related organization and its approach will frequently decide the get to issue. Where credit length, terms of instalment, required security and the arrangement of supplementary administrations do not fit the necessities of the objective gathering, potential borrowers won't make a difference for credit even where it exists and when they do, they will be denied get to. Wangui and Tirimba (2014) encounter demonstrates that the vast majority of the conditions forced by formal credit organizations like guarantee prerequisites ought to not really restrain smallholders and the poor in acquiring credit.

The poor can utilize the advances and compensate if compelling strategies for payment, supervision and reimbursement have been set up. Accessing contingency funding in form of credit from formal financial institution is not easy and especially within short notice in case of an emergency (Lydiah, 2012). According to a survey conducted by Central Bank of Kenya (CBK, 2012), the interest rate charged on a loan is only one part of the cost of the loan. A complete list of charges may include commitment / facility arrangement fees, processing fees, negotiation fees, valuation fee, insurance, appraisal fee and legal fee (CBK, 2012).
2.3 Financial Literacy and Access to Finance by SMEs

Financial literacy refers to the ability of an individual to understand how money works—how it is earned, managed and invested. It is very important for any business entrepreneur to have knowledge on how to manage the business so that they can oversee its growth (Andoh & Nunoo, 2011). A literate entrepreneur understands on the best time to make certain investment decisions such as when to borrow and from whom to borrow and at what cost. Van AardtSmit and Olawale (2012) observed that, financial literacy remains an interesting issue in both developed and developing economies, and has elicited much interest in the recent past with the rapid change in the finance landscape. Mounting evidence indicates that the less financially literate are likely to face more challenges with regard to debt management, savings and credit, and are less likely to plan for the future (Lyons et al., 2012; Bert et al., 2015). Such evidence suggests that there is a certain relationship between financial literacy and access to formal credit.

Literature indicates that individuals who are not educated or knowledgeable enough will not be able to make effective financial choices and this will limit their credit accessibility. Thus considerable efforts in education to improve financial literacy abound as experts agree that financial knowledge directly correlates with self-beneficial financial behavior (Hilgert et al., 2013). Hence even though questions exist concerning the effectiveness of financial education in improving financial literacy (Lyons et al., 2012), there are consistent findings of a positive relationship between financial knowledge and access to credit. Having knowledge of the different sources from which one can borrow increases the chances of success in borrowing (Hilgert et al., 2013).

2.3.1 Stringent Loan Conditions

Stringent loan conditions are a major inhibitor for SMEs access to finance. A study conducted by Kiraithe (2015) revealed the existence of a strong relationship between stringent loan conditions and access to finance. The study revealed that stringent loan conditions had inhibited SMEs access to financing particularly from the banking sector and major financial institutions. According to Wangui et al., (2014) many SMEs are not able to access loans from financial institutions due to the stringent conditions that loanees have to fulfil. Thus, financial institutions hold back from lending to SMEs since most of them do not have acceptable levels of collateral. Collateral is defined as a form of assets that is offered as security to financial institutions, and it is deemed important in this case.
by banks since most banks do not trust that SMEs have the capacity to repay should they go into default (Mbonyane & Ladzani, 2011). Consequentially, without adequate collateral, banks have limited mechanisms to protect the loan assets, and in this regard, the stringent collateral conditions are imposed to cushion and mitigate risks associated with SME loans (Kiraithe, 2015).

According to Wanjohi (2010), in so much as SMEs complain difficulties in access to credit from banks and financial institutions, financial institutions have to protect their bottom lines. If a bank feels that a given SME offers high risk of default, they are obligated to deny them financing. This is not just a wise idea, but one that is also geared at protecting banks and financial institutions bottom lines (Bert et al., 2015).

### 2.3.2 Cost of Credit

Cost of credit is defined as the financial burden that one has to incur to access a given financial credit from a bank or other financial institution (Gitari, 2012). On the other hand, Niskanen (2010) argues that cost of credit refers to the amount of money the entrepreneur has to pay in the process of accessing or borrowing a loan from a bank or financial institution. Vuvor and Ackah (2011) posits that key indicators for cost of credit include loan processing fees, interest rates, loan negotiation fees, loan insurance fees, legal fees and traveling fees that an entrepreneur has to incur to acquire a loan. The other significant area singled out by Obura and Matuvo (2011) is the fixed cost associated with acquisition of information concerning the SME by the lending bank. Any cost incurred by the financial institution in doing credit appraisal is transferred as cost of credit to the borrower, thus, making borrowing expensive for SMEs.

In essence, high transaction costs do not only increase the cost of borrowing, but restrict access to external borrowing by SMEs (Van AardtSmit & Olawale, 2012). While it is the case that high transaction costs are restraining for all borrowers, there are also arguments that high costs impact SMEs negatively, adversely affecting their ventures. In this regard, unlike other credit categories such as mortgage lending or customer credit, SMEs are still high cost products that are prohibitive in access, and unfriendly in repayment terms (Vuvor & Ackah, 2011).
According to Aabii (2014), banks have often been criticized for considering their super normal profits more than the plight of SMEs seeking financing. Banks usually argue that high cost credit is beyond their control as the base interest rates are set by central banks, however, in reality, the interest rates that banks offer to SMEs are far higher compared to the base rate offered central banks (Charbonneau & Menon, 2013). For instance, in Kenya, over the last five years, the central bank base rate has been 8%, however, banks have been charging SMEs up to 24% to access credit facilities. This is 16 points above the base rate (Wanjohi, 2010). Whichever way one looks at it, the exploitative nature of banks towards SMEs seeking loans pushes costs of credit high, and thus, unaffordable for most SMEs.

A study by Mwangi and Bwisa (2013) on challenges SMEs face in access to credit in Makuyu Kenya, found that a significant relationship between access to loan facilities by SMEs and high cost of credit. The findings revealed that high loan processing fees, high legal fees make loans accessibility expensive for local SMEs. The study recommended that financial institutions should look at mechanisms for enhancing credit products for SMEs as a way of attracting new clients, and in the process enhancing credit accessibility.

Cheluget (2013) argues for the need to have banks and financial institutions lower interest rates as a way of enhancing access to financial credit. Lower cost of credit does enable SMEs particularly startups ventures which need more financial input when pivoting new business ideas (Rambo, 2013).

2.3.3 Training and Education

Lack of knowledge of the rights that women have and how to enforce them is a challenge (Aabii, 2014). Women may not be aware of the legal issues that they need to address to start a business, and they can find it difficult to navigate the complex array of laws and regulations (McGrath, 2002). Education equips women with the knowledge and skills they need to more effectively manage and succeed in their businesses (Aabii, 2014). Research (ILO, 2010; Falkena, 2011; Amanda, 2012; Aabii, 2014) shows that the level of formal entrepreneurial activity among women increases as their education rises, and there a major jump in business ownership among those who go beyond secondary education.
Education and skills are needed to run a business. Majority of people carrying out SME’s in Kenya are not quite well informed in terms of education and skills (Aabii, 2014). According to King and McGrath (2002), those with more education and training are more likely to be successful in the sector. The literacy level was reflected in their ability to carry out managerial routines - the routine includes making decisions on financial investment and management - and this influences the decision on the external funding of his enterprise (Falkena, 2011).

According to International Labor Organization (ILO) (2010) most of the entrepreneurs have low literacy levels as majority of them drop from the primary level or they have acquired primary level. This makes an entrance to the jua-kali sector increasingly the last resort for the disadvantaged students with relatively low levels of education. ILO (2010) observed that an entrepreneur’s level of education is directly correlated with his ability to make financial decisions of his business.

ILO (2010) noted that declining level of education had negative influence on entrepreneur’s ability awareness on how and where to get loans to improve their businesses. With low ability to read and write, therefore an entrepreneur is at a disadvantage in the loans market. Information on availability of loans, and the rate of interests charged, is communicated through newspapers, in which a good level of literacy is required to read and interpret.

Falkena (2011), noted that; complete, accurate and precise information is necessary for financial decisions including obtaining business loans. The literacy level is again observed in the ability to have appropriate book keeping skills. The banks often demand cash flows and other financial records as a prerequisite for approving of credit. Due to low literacy levels most SME traders are unable to differentiate the loan products offered by the financial institutions. Amanda (2012) also observes that, since most of the services are offered in banking jargons, most traders are discouraged from applying for the loans. Further inadequacy in financial management skills and strategic planning put the SME’s in a disadvantaged position in competing with a large firms which are run by well-educated professional managers.
Most lenders advertise their services on the print media. Since the literacy levels among the small scale traders are low they may not access the information (Aabii, 2014). Others may have general literacy but are not well informed, on the effect of credit facilities on business growth, and therefore may fail to ask for the services (McGrath, 2002). The literacy level may therefore be a constraining factor in the access to, among traders (Falkena, 2011; Aabii, 2014). Lower education levels put Kenyan women entrepreneurs at a disadvantage compared to men. While the gender gap in primary education in Kenya has decreased in recent years, the gap remains high at secondary and tertiary education levels (ILO, 2010). Women are much less likely to enroll in public universities, national polytechnics, and technical institutes, and accounting for only about 39 percent of those enrolled in tertiary education (Amanda, 2012).

2.4 Firms Characteristics and Access to Finance by SMEs

Firm characteristics refer to the business characters of the firm that encourage debt and equity financial providers to invest in such business (Esperanca et al., 2013). To encourage financial providers to provide funds to SMEs, the owner/manager of the business has to prove the ability of the firm to repay loans through its financial leverage ratio and the size of the business (Berger & Udell, 1998).

There is a relationship between the financial leverage (the amount of debt that a firm uses to finance its assets) and access to finance. In other words, the higher the financial leverage (debt more than equity) of the firm, the higher the bankruptcy risk and the less attractive the firm is as an investment for finance providers (Beal & Goyen, 2015; Cassar & Holmes, 2013). Other studies consider firm characteristics that influence ease of access to the current financial services provided by banks, such as availability of a business plan, business size, business growth and profit, and business type (Kushnir, 2010).

According to Kira (2012), firm characteristics affect SMEs’ ability to access external finance. The size and age of the firm were identified as important variables under this category. Firm size is one of the most important variables in literature related to access to credit. This was true for both developed as well as developing countries. As this research focused on small and medium sized firms, it did not seem logical to consider size as a
determinant of access to finance. However, even among the SMEs’ category, there is still a large variation in the size of the firms.

Kakuru (2013), argues that numerous studies have discussed that small and medium-sized enterprises are financially more constrained than large firms. Firstly, the small firms are faced with information opacity such as inability to provide financial information. When the firm is small, most of the time it is owned and operated by the entrepreneur himself and there is no such legal requirement to regularly report financial information and many firms do not maintain audited financial accounts. Second, smaller firms have fewer assets to offer as collateral (Kakuru, 2013). In order to reduce the anticipated risk and moral hazard associated with lending, the banks use collateral as one of the instrument (Mbonyane & Ladzani, 2011).

Gitari (2012), states that that it may be relatively more costly for smaller firms to resolve information asymmetries with debt providers. Consequently, smaller firms may be offered less debt capital. In addition, transaction costs are typically a function of scale and may be higher for smaller firms. It is also possible that small firms have fewer opportunities to raise capital because capital markets are out of reach due to their size. Esperanca et al. (2013) state that, in the presence of non-trivial fixed costs of raising external funds large firms have cheaper access to outside financing per dollar borrowed. Cassar and Holmes (2013) observe that, size may also proxy for the volatility of firm assets, for small firms are more likely to be growing firms in rapidly developing and thus intrinsically volatile industries. Yet another explanation is the extent of the wedge in the degree of information asymmetry between insiders and the capital markets which may be lower for larger firms, for example because they face more scrutiny by ever-suspicious investors (Dun & Girma, 2012; Esperanca et al., 2013).

Mbonyane and Ladzani (2011), offers an alternative explanation for the relationship between firm size and profitability, arguing that the greater profits of large firms have little or nothing to do with conventional scale economies. Rather large firms are inherently more efficient than small firms due to superior management. Consequently, overtime, the more efficient firms are rewarded with both growth and elevated profit. Again profitable firms have higher access to finance given the assurance it gives to the
lenders on financial sustainability. More recently, Dun and Girma (2012) using firm level data from China spanning the period 1998-2005 found that bigger firms source capital from the bank while smaller firms use self-raised finance.

2.4.1 Firm Age
Firm age appears in several studies in the empirical finance literature as control variable especially in corporate strategy research. However, the age of the firm has implications on financial access (Beal & Goyen, 2015). The relation between age of the firm and growth or profitability has been given attention in the industrial organization literature. Age of the firm can affect performance by inducing organizational inertia and by impairing firms’ ability to perceive valuable signals (Kushnir, 2010). According to this hypothesis, the problem is the tendency of firms to codify their success with organizational measures, rules of conduct, and processes, thus, the organizational inertia restricts them from recognizing, accepting, and implementing change (Vera & Onji 2010).

Another perspective is given by Rambo (2013) that the longer a firm exists; the more it signals that it can weather tough economic conditions. Furthermore, by staying in business, a firm can signal that it does not adopt opportunistic behavior. It also signifies that the firm and in particular the owners or managers are mature enough to deal with business challenges. Beal and Goyen (2015) state that, older firms provide a resume in which lenders can use to gauge their credit worthiness. It is often difficult and expensive for young SMEs to access bank financing, due in large part to information asymmetry between the banks and firms.

2.4.2 Ownership Structure of Firm
There are several types of firm ownership. For example sole proprietorship, partnership and companies. Makena and Njati (2014), demonstrate that incorporated firms under limited liability, have higher growth than unincorporated firms. Several factors could explain the association between incorporated firms and growth. First, corporations have the ability to issue stock and their stockholders have the freedom to resell their stock. This ability facilitates the process of accessing finance for expansion.
Roodman (2011), observed that lenders may perceive incorporation as a sign of credibility and formality of operations. The form of ownership could affect the debt-equity decisions of SMEs. Thus, corporations and limited liability companies may be more likely to finance their projects with equity, while sole proprietors are more likely to employ debt financing. Coleman and Cohn (2010) also find evidence suggesting a positive relationship between leverage and incorporation. Thus one can state that, ownership structure has a positive effect on firms’ access to finance such that incorporated firms are likely to have more access to finance.

2.4.3 Business Type
The industry in which a firm operates does determine its capital structure albeit indirectly via the nature and composition of the firm’s assets. Wanjohi (2010), argue that the relationship between industry classification and financial leverage is based on the assumption that industry classification is a proxy for business risk. Firms in the same industry face the similar environmental and economic conditions and, thus, tend to cluster with respect to variance of earnings and sales. Wangui (2011), found that SMEs in the agricultural sector exhibit the highest capital structure and asset structure or collateral value, while the wholesale and retail trade industry has the lowest debt ratio and asset structure.

Raphael and Jogsoon (2012) states that barriers to entry and other structural features of industries create significant differences in firm performance. Because of differences in sunk and fixed-cost requirements by industry, firm performance may differ significantly by industry regardless of country affiliation. Thus, even among firms with different affiliations by country, important differences may arise in performance by industry. Roodman (2011) observes that, some industries are characterized by higher risk and thus because lenders assess risk levels of the industry, risk exposed sectors may not access as much finance as compared to other less risky sectors. In the same vein, Dun and Girma (2012) note that, some sectors are less profitable than others, and since profitability is a yardstick used by lenders, then it means that some sectors may be disadvantaged in access to finance.
2.4.4 Financial Characteristics

Wangui and Tirimba (2014), explain that financial characteristics have been categorized into three variables namely, having audited financial statements, asset tangibility, and firm performance. Lack of reliable information leads to comparably high interest rates even if a long term relationship between borrower and bank exists. In a situation like this, having audited financial statements play a major role. Audited financial statements are very useful in accessing credit from financial institutions because they present a picture of the financial performance of a firm.

Obwori (2012), found that lenders in the UK pay much attention to accounting information in order to deal with the loan applications of small firms. Given the reduced information risk arising from audited financial statements, potential lending institutions may offer low interest rates as well. In other words, audited financial statements improve borrower’s credibility and therefore reduce risk for lenders. However, Wangui and Tirimba (2014) note that, most of the SMEs in Kenya have difficulty in getting credit from the formal financial institutions because they lack proper financial records. Most of the businesses often keep multiple sets of books and do not have audited financial statements based on reliable accounting standards. On the other hand, Wanjohi (2010) found that, these firms end up getting loans at higher interest rates because banks considered them as high risk borrowers. Asymmetric information problems may be more pronounced for small firms (Obwori, 2012). Monitoring SMEs is more difficult and expensive as information on them is less easily available, they have less credit history, are subject to less rigorous reporting requirements and the quality of their financial statements may vary (Mbonyane & Ladzani, 2011; Beal & Goyen, 2015). All these elements result in SMEs often facing difficulties in signaling their creditworthiness.

2.5 Chapter Summary

This chapter has presented literature review based on specific objectives of the study. The literature review on available lending institutions is presented first, followed by lending requirements, followed by financial literacy, and finally literature review on influence of firm’s characteristics on access to finance by SMEs. The next chapter presents the research methodology adopted for the study.
CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction
This chapter presents the study methodology that was adopted for this study. This chapter covers the study research design that was used to carry out the research. The study population and sampling design has also been presented followed by the data collection methodology, data analysis, and research procedures.

3.2 Research Design
This study adopted a descriptive survey research design. According to Mugenda and Mugenda (2011) a research design provides a study framework for streamlining the scope of the scope and mechanics through which the study objectives are achieved. The research design also provides the researcher a plan to control how the study will be guided, control, without interfering or influencing the study environment. The research design is the researcher’s overall plan for obtaining answers to the research questions. Descriptive design was ideal for this study since the aim of the researcher was to describe the nature of respondents, nature of results and findings in a manner that answered the research objectives. For this study the aim was to identify influencing factors (independent variables) for SMEs’ access to finance (dependent variable) in Meru County.

3.3 Population and Sampling Design
3.3.1 Population
Mugenda and Mugenda (2011) define population as the total entities or elements from which a researcher wish to draw a sample for the study. Population forms the subject of the study. For the purpose of this study, the target population constituted of registered SME’s in Meru County in Kenya. The entire target population comprised of 1650 registered SME’s (Meru County, 2014). The population distribution was as highlighted in Table 3.1
Table 3.1 Population Distribution

<table>
<thead>
<tr>
<th>SME Sector</th>
<th>Population</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>General merchants &amp; kiosks</td>
<td>540</td>
<td>33</td>
</tr>
<tr>
<td>Medium &amp; small retails</td>
<td>320</td>
<td>19</td>
</tr>
<tr>
<td>Informal traders</td>
<td>360</td>
<td>22</td>
</tr>
<tr>
<td>Agricultural producers &amp; processors</td>
<td>280</td>
<td>17</td>
</tr>
<tr>
<td>Lodging hotels &amp; restaurants</td>
<td>150</td>
<td>9</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1650</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Source: Meru County Office of Economics and Statistical Data (2017)

3.3.2 Sampling Design

3.3.2.1 Sampling Frame

The sample frame is defined as a list containing all the population elements a researcher relied on to draw a sample size (Cooper & Schindler, 2012). The sampling frame is important in that it ensures that a researcher is only dealing with a population that is current and credible. For this study, the sampling frame was obtained from the office of economics and statistical data in Meru County.

3.3.2.2 Sampling Technique

According to Cooper and Schindler (2012), a sampling technique is defined as the method that a researcher employs to pick a sample size from the entire population. Stratified sampling technique was adopted for this study. According to Mugenda and Mugenda (2011) stratified sampling is ideal for a study that is heterogeneous. Since this study was looking at different heterogeneous categories of SMEs within Meru County, stratified sampling was ideal.

After stratification of the population, the researcher used Simple Random Sampling (SRS) to select the study respondents. SRS is a probability sampling technique that gives population elements an equal chance (probability) of being selected (Babbie, 2014). SRS was selected for this study because of its advantages which include its ease of use and its accurate representation of the larger population, and the fact that it offered all elements of the population an equal chance of being selected.
3.3.2.3 Sample Size

A sample size is defined as the element of a study that represents the actual population, or that elements to be examined within a study, from which, inference was made to the entire population (Babbie, 2010). For this study, Yamane (1967) formula was used to determine the sample size of 92 SMEs as follows and distribution is as shown in Table 3.2:

\[
n = \frac{N}{1 + N(e)^2}
\]

Where \( n \) is the sample size, \( N \) is the population size and \( e \) is the margin of error (Yamane, 1967).

\[
n = \frac{1,650}{1 + 1,650 (0.1)^2}
\]

\( n = 92 \)

<table>
<thead>
<tr>
<th>SME Sector</th>
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<th>Sample Size</th>
<th>Percentage Distribution</th>
</tr>
</thead>
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<tr>
<td>Large, medium &amp; small retails</td>
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<td>19</td>
</tr>
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<td>17</td>
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<td>9</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1650</strong></td>
<td><strong>92</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

3.4 Data Collection Methods

Copper and Schindler (2012) define data collection methods as mechanisms a researcher employs to collect data from respondents of the study so as to answer the research questions. This study utilized a questionnaire as a tool to collect primary data. A
questionnaire tool in research is used to collect data where a researcher wants structured responses (Cox & Hassard, 2010).

The researcher adopted a questionnaire tool with a five level Likert scale ranging from strongly disagree, disagree, neutral, agree and strongly agree. Section I of the questionnaire dealt with the demographic data of the respondents, section II dealt with collateral requirements; section III dealt with lending procedures; section IV dealt with firms characteristics.

3.5 Research Procedures
According to Cox and Hassard (2010) research procedures are the step by step processes that guide a researcher on how to conduct the study, or how to collect data for the study. Prior to data collection, an introduction letter authorizing data collection was obtained from the Chandaria School of Business at United States International University – Africa (USIU-A) and submitted to county offices of Meru for relevant approvals. After being granted with approvals, the researcher pilot tested the questionnaire using SMEs in Kiambu County, to ensure the study validity and reliability.

The feedback from the pilot was used to adjust the questionnaire too. After this was done, some questionnaires were administered by use of drop and pick approach to SMEs Owners/Managers where respondents were given 1-2 hours to fill in the questionnaire. The remaining questionnaires were administered through face-to-face approach; whereby some Owners/ Managers completed the questionnaire. The respondents were given a chance to ask for clarifications, while those that were literally challenged, the data collectors translated the questionnaires from English into appropriate language for the respondents to understand. All questionnaires were collected by the data collectors and checked for completeness or missing data before submitting them to the researcher.

3.6 Data Analysis Methods
Copper and Schindler (2012) defined data analysis as the process through which raw data is converted and summarized in a way that makes sense and meaning to the user of the data or the research report. The Statistical Package for Social Sciences (SPSS) was used to analyze descriptive statistics (percentages, and frequencies); and inferential statistics
(correlations, and regressions). According to Babbie (2014) quantitative analysis is the numerical representation and manipulation of observations for the purpose of describing and explaining the phenomena that those observations reflect. The collected data was used to explain how the access to finance affects the financial performance of SMEs in Meru County. Analyzed data was presented using tables and figures.

3.7 Chapter Summary
This chapter has presented the research methodology the researcher adopted to carry out the study. First, the descriptive survey research design has been presented, followed by population and sampling design which has articulated how data was sampled from the population. The sample size has also been presented, followed by data collection methods, research procedures and data analysis and presentation methods. The next chapter presents the study’s results and findings.
CHAPTER FOUR

4.0 RESULTS AND FINDINGS

4.1 Introduction
The general objective of the study was to establish the factors influencing access to finance by SMEs in Meru County. This chapter presents results and findings based on the data analyzed for lending requirements and access to finance by SMEs, financial literacy and access to finance by SMEs, and firms characteristics and access to finance by SMEs in Meru County.

4.2 Response Rate and Demographics

4.2.1 Response Rate
Based on the collection method employed by the researcher and his assistants, the study managed to collect data from the 92 targeted respondents. The method of checking for completeness of the questionnaire before collection, ensured that all 92 questionnaires were completely filled and thus valid for the study results, giving the study a response rate of 100%.

4.2.2 Gender
Figure 4.1 shows that 58.7% of the respondents were male and 41.3% were female, showing that both genders were entrepreneurs in Meru County, and thus the results could be applied consistently to both genders.

Figure 4.1 Gender
4.2.3 Level of Education

Figure 4.2 indicates that 35.9% of the respondents had undergraduate degrees, 32.6% had college certificates, 16.3% had secondary certificates, and 15.2% had Master’s degrees, showing that entrepreneurs in Meru County had basic to interim education, meaning they would be able to understand the research questions.

![Figure 4.2 Level of Education](image)

4.2.4 Years in Business

Figure 4.3 shows that 32.6% had been in business for 1-3 years, 18.5% had equally been in business for 7-9 years and 10 years and above respectively, 16.3% had been in business for less than 12 months, and 14.1% had been in business for 4-6 years. This indicates that majority of the respondents had been in business for more than 3 years, meaning they were well versed with the challenges of financial access, making them valid for the study.

![Figure 4.3 Years in Business](image)
4.2.5 Business Monthly Income

Figure 4.4 shows that 35.9% of the businesses had a monthly income of between 10,001 and 20,000 Kenya shillings, 34.8% of the businesses had a monthly income of between 20,001 and 30,000 Kenya shillings, 17.4% of the businesses had a monthly income of between 30,001 and 40,000 Kenya shillings, 7.6% of the businesses had a monthly income of less than 10,000 Kenya shillings, and 4.3% of the businesses had a monthly income of 40,001 Kenya shillings and above.

![Figure 4.4 Business Monthly Income](image)

4.2.6 Source of Business Loan

Figure 4.5 indicates that 41.3% of the entrepreneurs sourced their loans from family members, 34.8% acquired their loans from Saccos, 17.4% acquired their loans from banks, and 6.5% acquired their loans from friends. This shows that most of the entrepreneurs acquired their loans from family members and Saccos.

![Figure 4.5 Source of Business Loan](image)
4.2.7 Ability to Acquire Loans
Figure 4.6 shows that 53.3% of the entrepreneurs indicated that their business’ ability to access loans was somewhat difficult, 21.7% stated it was difficult, 16.3% stated it was easy, 5.4% stated it was very difficult, and 3.3% stated it was very easy. This shows that most SMEs in Meru found it somewhat difficult to access business loans.

![Figure 4.6 Ability to Acquire Loans](image)

4.3 Lending Requirements and Access to Finance by SMEs
4.3.1 Grading of Lending Requirements and Access to Finance by SMEs
Table 4.1 shows that entrepreneurs normally did not use title deeds (business or land) in order to access a loan as disagreed to by 45.6% of the respondents, 30.4% were neutral, and 23.9% agreed with a corresponding mean and standard deviation of (2.78; 1.282). My loan security must cover my loan amount or surpass it for it to be accepted by the bank as agreed to by 76.1% of the respondents, 20.7% were neutral, and 3.3% disagreed with a corresponding mean and standard deviation of (4.12; 0.888). As a businessman, I have used my business loan for my own personal and private use as agreed to by 78.2% of the respondents, 18.5% were neutral, and 3.3% disagreed with a corresponding mean and standard deviation of (4.24; 0.869). The use of security to pick a business loan, has reduced my chances of misusing loans I take for my business growth as agreed to by 77.2% of the respondents, and 22.8% were neutral with a corresponding mean and standard deviation of (4.27; 0.813).
Table 4.1 Grading of Lending Requirements and Access to Finance by SMEs

<table>
<thead>
<tr>
<th></th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Dev</th>
</tr>
</thead>
<tbody>
<tr>
<td>I normally use title deeds (business or land) in order to access a loan</td>
<td>16.3</td>
<td>29.3</td>
<td>30.4</td>
<td>7.6</td>
<td>16.3</td>
<td>2.78</td>
<td>1.282</td>
</tr>
<tr>
<td>My loan security must cover my loan amount or surpass it for it to be accepted by the bank</td>
<td>1.1</td>
<td>2.2</td>
<td>20.7</td>
<td>35.9</td>
<td>40.2</td>
<td>4.12</td>
<td>.888</td>
</tr>
<tr>
<td>As a businessman, I have used my business loan for my own personal and private use</td>
<td>0</td>
<td>3.3</td>
<td>18.5</td>
<td>29.3</td>
<td>48.9</td>
<td>4.24</td>
<td>.869</td>
</tr>
<tr>
<td>The use of security to pick a business loan, has reduced my chances of misusing loans I take for my business growth</td>
<td>0</td>
<td>0</td>
<td>22.8</td>
<td>27.2</td>
<td>50</td>
<td>4.27</td>
<td>.813</td>
</tr>
<tr>
<td>The use of security ensures that I do not invest in high risk projects</td>
<td>10.9</td>
<td>18.5</td>
<td>21.7</td>
<td>7.6</td>
<td>41.3</td>
<td>3.50</td>
<td>1.456</td>
</tr>
<tr>
<td>My willingness to pledge security for a loan increases my probability of acquiring a bank loan</td>
<td>0</td>
<td>1.1</td>
<td>20.7</td>
<td>40.2</td>
<td>38</td>
<td>4.15</td>
<td>.784</td>
</tr>
<tr>
<td>My loan security acts as an indicator to the bank that I am a creditworthy individual</td>
<td>0</td>
<td>9.8</td>
<td>19.6</td>
<td>34.8</td>
<td>35.9</td>
<td>3.97</td>
<td>.977</td>
</tr>
<tr>
<td>I have missed out on a bank loan because my business does not have audited financial records</td>
<td>14.1</td>
<td>12</td>
<td>22.8</td>
<td>17.4</td>
<td>33.7</td>
<td>3.45</td>
<td>1.425</td>
</tr>
<tr>
<td>I have poor access to bank loans, because I am more than likely to default on my loan repayment</td>
<td>14.1</td>
<td>31.5</td>
<td>30.4</td>
<td>14.1</td>
<td>9.8</td>
<td>2.74</td>
<td>1.166</td>
</tr>
<tr>
<td>I have failed to secure a business loan because I could not meet the bank’s requirements</td>
<td>40.2</td>
<td>25</td>
<td>20.7</td>
<td>9.8</td>
<td>4.3</td>
<td>2.13</td>
<td>1.179</td>
</tr>
</tbody>
</table>
The use of security ensures that I do not invest in high risk projects as agreed to by 48.9% of the respondents, 18.5% were neutral, and 29.4% disagreed with a corresponding mean and standard deviation of (3.50; 1.456). My willingness to pledge security for a loan increases my probability of acquiring a bank loan as agreed to by 78.2% of the respondents, 20.7% were neutral, and 1.1% disagreed with a corresponding mean and standard deviation of (4.15; 0.784). My loan security acts as an indicator to the bank that I am a creditworthy individual as agreed to by 70.7% of the respondents, 19.6% were neutral, and 9.8% disagreed with a corresponding mean and standard deviation of (3.97; 0.977).

Entrepreneurs have missed out on a bank loan because my business does not have audited financial records as agreed to by 51.1% of the respondents, 26.1% disagreed, and 22.8% were neutral with a corresponding mean and standard deviation of (3.45; 1.425). Entrepreneurs did not have poor access to bank loans, because they were more than likely to default on their loan repayment as disagreed to by 45.6% of the respondents, 30.4% were neutral, and 23.9% agreed with a corresponding mean and standard deviation of (2.74; 1.166). Entrepreneurs had not failed to secure a business loan because they could not meet the bank’s requirements as disagreed to by 65.2% of the respondents, 20.7% were neutral, and 14.1% agreed with a corresponding mean and standard deviation of (2.13; 1.179).

4.3.2 Correlation Analysis of Lending Requirements and Access to Finance by SMEs

Table 4.2 provides a correlation analysis for lending requirement factors and their significance to SMEs’ access to finance, and it indicates that collateral requirements were significant to SMEs’ access to finance (r=0.411, p<0.1). Tangible assets availability were significant to SMEs’ access to finance (r=0.241, p<0.5). Group guarantees availability were insignificant to SMEs’ access to finance (r=0.003, p>0.5). Repayment mode flexibility was insignificant to SMEs’ access to finance (r=0.195, p>0.1).
Table 4.2 Correlations for Lending Requirements and Access to Finance by SMEs

<table>
<thead>
<tr>
<th></th>
<th>SMEs Access to Finance</th>
<th>Collateral Requirements</th>
<th>Tangible Assets</th>
<th>Group Guarantees</th>
<th>Repayment Mode Flexibility</th>
</tr>
</thead>
<tbody>
<tr>
<td>SMEs Access to Finance</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Collateral Requirements</td>
<td>.411**</td>
<td>.000</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tangible Assets</td>
<td>.241*</td>
<td>.680**</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Group Guarantees</td>
<td>.003</td>
<td>.552**</td>
<td>.608**</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Repayment Mode Flexibility</td>
<td>.195</td>
<td>.065</td>
<td>.221*</td>
<td>.317**</td>
<td>1</td>
</tr>
</tbody>
</table>

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

4.3.3 Regression Analysis of Lending Requirements and Access to Finance by SMEs

Table 4.3 shows the regression analysis for significant factors of lending requirements and their relation to SMEs’ access to finance, and the adjusted R square of 0.153 means that collateral requirements and tangible assets influence SMEs’ ability to access finance by 15.3%.

Table 4.3 Regression Model Summary of Lending Requirements and Access to Finance by SMEs

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. of Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.415</td>
<td>.172</td>
<td>.153</td>
<td>.31113</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Collateral Requirements, and Tangible Assets
Table 4.4 presents the regression analysis of variance for the significant factors of lending requirements and their relation to SMEs’ access to finance, and the value of $F(2,89) = 9.249$, $p<0.1$ shows that there was a significant difference between collateral requirements and tangible assets availability and SMEs’ access to finance, indicating that the analysis provided a great fit for the study.

Table 4.4 Regression ANOVA of Lending Requirements and Access to Finance by SMEs

<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>1.791</td>
<td>2</td>
<td>.895</td>
<td>9.249</td>
<td>.000</td>
</tr>
<tr>
<td>Residual</td>
<td>8.616</td>
<td>89</td>
<td>.097</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>10.406</td>
<td>91</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Collateral Requirements, and Tangible Assets
b. Dependent Variable: SMEs’ Access to Finance

Table 4.5 indicates the regression coefficients for the significant factors of lending requirements and their relation to SMEs’ access to finance, and it shows that collateral requirements were significant to SMEs’ access to finance since their p value was <0.1 and the B value of 0.214 shows that every increase in collateral requirements would increase SMEs’ access to finance by 21.4%. The table also shows that, tangible assets availability was insignificant to SMEs’ access to finance since its p value was >0.5 and the B value of -0.029 shows that every increase in tangible assets availability would decrease SMEs’ access to finance by 2.9% because the two variables were inversely correlated.

Table 4.5 Regression Coefficients for Lending Requirements and Access to Finance by SMEs

<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 (Constant)</td>
<td>2.818</td>
<td>.196</td>
<td>.460</td>
<td></td>
</tr>
<tr>
<td>Collateral</td>
<td>.214</td>
<td>.061</td>
<td>.588</td>
<td></td>
</tr>
<tr>
<td>Requirements</td>
<td>-.029</td>
<td>.054</td>
<td>-.543</td>
<td>.588</td>
</tr>
</tbody>
</table>

a. Dependent Variable: SMEs’ Access to Finance
4.4 Financial Literacy and Access to Finance by SMEs

4.4.1 Grading of Financial Literacy and Access to Finance by SMEs

Table 4.6 shows that the businesses did succeed in accessing financial credit as disagreed to by 92.4% of the respondents, and 7.6% were neutral with a corresponding mean and standard deviation of (1.46; 0.636). Strict loan conditions are my major challenge in accessing loans as agreed to by 79.3% of the respondents, and 20.7% were neutral with a corresponding mean and standard deviation of (4.21; 0.764). Most banks believe as a small business, I do not have the capacity to repay a loan in case I default as agreed to by 85.9% of the respondents, and 14.1% were neutral with a corresponding mean and standard deviation of (4.53; 0.733). As a businessman, I am in agreement with the decision of banks denying me a loan when they see me as a high risk defaulter as disagreed to by 44.5% of the respondents, 28.3% were neutral, and 27.2% agreed with a corresponding mean and standard deviation of (2.70; 1.420).

As a business person, I incur some financial costs in order to receive financial credit from a bank or other financial institution as agreed to by 50% of the respondents, 37% were neutral, and 13% disagreed with a corresponding mean and standard deviation of (3.68; 1.058). There are a lot of costs (transaction costs) that make borrowing very expensive for my business as agreed to by 58.7% of the respondents, and 41.3% were neutral with a corresponding mean and standard deviation of (3.88; 0.837). One needs education and skills in order to run a business as agreed to by 65.2% of the respondents, 29.3% were neutral, and 5.4% disagreed with a corresponding mean and standard deviation of (4.00; 0.961).

I am well educated and I am informed on how to run a business as agreed to by 73.9% of the respondents, 17.4% were neutral, and 8.7% disagreed with a corresponding mean and standard deviation of (4.08; 0.975). I have the ability to carry out managerial routines in my business as agreed to by 83.7% of the respondents, and 16.3% were neutral with a corresponding mean and standard deviation of (4.27; 0.728). I have the ability to keep proper business records (bookkeeping) that are often demanded by banks as agreed to by 81.5% of the respondents, 16.3% were neutral, and 2.2% disagreed with a corresponding mean and standard deviation of (4.30; 0.822).
Table 4.6 Grading of Financial Literacy and Access to Finance by SMEs

<table>
<thead>
<tr>
<th></th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Dev</th>
</tr>
</thead>
<tbody>
<tr>
<td>My business rarely succeeds in accessing financial credit</td>
<td>62</td>
<td>30.4</td>
<td>7.6</td>
<td>0</td>
<td>0</td>
<td>1.46</td>
<td>.636</td>
</tr>
<tr>
<td>Strict loan conditions are my major challenge in accessing loans</td>
<td>0</td>
<td>0</td>
<td>20.7</td>
<td>38</td>
<td>41.3</td>
<td>4.21</td>
<td>.764</td>
</tr>
<tr>
<td>Most banks believe as a small business, I do not have the capacity to repay a loan</td>
<td>0</td>
<td>0</td>
<td>14.1</td>
<td>18.5</td>
<td>67.4</td>
<td>4.53</td>
<td>.733</td>
</tr>
<tr>
<td>As a businessman, I am in agreement with the decision of banks denying me a loan when</td>
<td>29.3</td>
<td>15.2</td>
<td>28.3</td>
<td>10.9</td>
<td>16.3</td>
<td>2.70</td>
<td>1.420</td>
</tr>
<tr>
<td>As a business person, I incur some financial costs in order to receive financial credit</td>
<td>0</td>
<td>13</td>
<td>37</td>
<td>18.5</td>
<td>31.5</td>
<td>3.68</td>
<td>1.058</td>
</tr>
<tr>
<td>There are a lot of costs (transaction costs) that make borrowing very expensive for</td>
<td>0</td>
<td>0</td>
<td>41.3</td>
<td>29.3</td>
<td>29.3</td>
<td>3.88</td>
<td>.837</td>
</tr>
<tr>
<td>One needs education and skills in order to run a business</td>
<td>0</td>
<td>5.4</td>
<td>29.3</td>
<td>25</td>
<td>40.2</td>
<td>4.00</td>
<td>.961</td>
</tr>
<tr>
<td>I am well educated and I am informed on how to run a business</td>
<td>0</td>
<td>8.7</td>
<td>17.4</td>
<td>31.5</td>
<td>42.4</td>
<td>4.08</td>
<td>.975</td>
</tr>
<tr>
<td>I have the ability to carry out managerial routines in my business</td>
<td>0</td>
<td>0</td>
<td>16.3</td>
<td>40.2</td>
<td>43.5</td>
<td>4.27</td>
<td>.728</td>
</tr>
<tr>
<td>I have the ability to keep proper business records (bookkeeping) that are often</td>
<td>0</td>
<td>2.2</td>
<td>16.3</td>
<td>30.4</td>
<td>51.1</td>
<td>4.30</td>
<td>.822</td>
</tr>
</tbody>
</table>
4.4.2 Correlation Analysis of Financial Literacy and Access to Finance by SMEs

Table 4.7 provides a correlation analysis for financial literacy factors and their significance to SMEs’ access to finance, and it indicates that stringent loan conditions were significant to SMEs’ access to finance (r=0.424, p<0.1). Cost of credit was insignificant to SMEs’ access to finance (r=0.036, p>0.5). Training and education was significant to SMEs’ access to finance (r=0.439, p<0.1).

Table 4.7 Correlation Analysis of Financial Literacy and Access to Finance by SMEs

<table>
<thead>
<tr>
<th></th>
<th>SMEs Access to Finance</th>
<th>Stringent Loan Conditions</th>
<th>Cost of Credit</th>
<th>Training and Education</th>
</tr>
</thead>
<tbody>
<tr>
<td>SMEs Access to Finance</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stringent Loan</td>
<td>.424**</td>
<td>1</td>
<td>.372**</td>
<td>.060</td>
</tr>
<tr>
<td>Conditions</td>
<td>.000</td>
<td></td>
<td>.000</td>
<td>1</td>
</tr>
<tr>
<td>Cost of Credit</td>
<td>.036</td>
<td>.734</td>
<td></td>
<td>.060</td>
</tr>
<tr>
<td>Training and Education</td>
<td>.439**</td>
<td>.362**</td>
<td>.567</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td></td>
</tr>
</tbody>
</table>

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

4.4.3 Regression Analysis of Financial Literacy and Access to Finance by SMEs

Table 4.8 shows the regression analysis for significant factors of financial literacy and their relation to SMEs’ access to finance, and the adjusted R square of 0.258 means that stringent loan conditions and training and education influence SMEs’ ability to access finance by 25.8%.

Table 4.8 Regression Model Summary of Financial Literacy and Access to Finance by SMEs

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. of Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.523</td>
<td>.274</td>
<td>.258</td>
<td>.29138</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Stringent Loan Conditions, and Training and Education
Table 4.9 presents the regression analysis of variance for the significant factors of financial literacy and their relation to SMEs’ access to finance, and the value of F(2,89) = 16.782, p<0.1 shows that there was a significant difference between stringent loan conditions, and training and education and SMEs’ access to finance, indicating that the analysis provided a great fit for the study.

Table 4.9 Regression ANOVA of Financial Literacy and Access to Finance by SMEs

<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>1</td>
<td>Regression</td>
<td>2</td>
<td>1.425</td>
<td>16.782</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>Residual</td>
<td>89</td>
<td>.085</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>91</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Stringent Loan Conditions, and Training and Education
b. Dependent Variable: SMEs’ Access to Finance

Table 4.10 indicates the regression coefficients for the significant factors of financial literacy and their relation to SMEs’ access to finance, and it shows that stringent loan conditions were significant to SMEs’ access to finance since their p value was <0.1 and the B value of 0.120 shows that every increase in stringent loan conditions would increase SMEs’ access to finance by 12%. The table also shows that, training and education was significant to SMEs’ access to finance since its p value was <0.1 and the B value of 0.183 shows that every increase in, training and education would increase SMEs’ access to finance by 18.3%.

Table 4.10 Regression Coefficients for Financial Literacy and Access to Finance by SMEs

<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>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>2.420</td>
<td>.223</td>
<td>10.872</td>
<td>.000</td>
</tr>
<tr>
<td>Stringent Loan Condition</td>
<td>.120</td>
<td>.038</td>
<td>.306</td>
<td>3.155</td>
</tr>
<tr>
<td>Training and Education</td>
<td>.183</td>
<td>.054</td>
<td>.328</td>
<td>3.390</td>
</tr>
</tbody>
</table>

a. Dependent Variable: SMEs’ Access to Finance
4.5 Firms Characteristics and Access to Finance by SMEs

4.5.1 Grading of Firms Characteristics and Access to Finance by SMEs

Table 4.11 indicates that, the size and age of my business greatly affects my ability to acquire a loan as agreed to by 83.7% of the respondents, 13% were neutral, and 3.3% disagreed with a corresponding mean and standard deviation of (4.39; 0.838). My business does not struggle to provide required financial information by banks, limiting my loan accessibility as disagreed to by 45.6% of the respondents, 37% were neutral, and 17.4% agreed with a corresponding mean and standard deviation of (2.55; 1.123). My business has fewer assets that can be used as security while accessing a bank loan as agreed to by 82.6% of the respondents, and 17.4% were neutral with a corresponding mean and standard deviation of (4.25; 0.736). The number of years that I have been in business does not affect my ability to access a bank loan as shown by 46.7% of the respondents who were neutral, 36.9% disagreed, and 16.3% agreed with a corresponding mean and standard deviation of (2.64; 1.125).

Business that have been running for many years indicate they have the ability to withstand tough economic conditions, leading to easy access to loans as agreed to by 51.1% of the respondents, 31.5% were neutral, and 17.4% disagreed with a corresponding mean and standard deviation of (3.66; 1.112). Businesses that are composed of partnerships have easy access to finance for expansion as agreed to by 59.8% of the respondents, 33.7% were neutral, and 6.5% disagreed with a corresponding mean and standard deviation of (3.72; 0.843). Ownership structure has a positive effect on a business’ ability to access bank loans as agreed to by 56.5% of the respondents, 30.4% were neutral, and 13% disagreed with a corresponding mean and standard deviation of (3.84; 1.102).

My business profitability is not a yardstick used by banks to provide me with a loan as disagreed to by 73.9% of the respondents, and 26.1% were neutral with a corresponding mean and standard deviation of (1.93; 0.768). Lack of reliable business information has led to my access to loans at a high interest rate as agreed to by 55.4% of the respondents, 38% were neutral, and 6.5% disagreed with a corresponding mean and standard deviation of (3.75; 0.921). Banks pay much attention to accounting information when I apply for a
loan as agreed to by 48.9% of the respondents, 31.5% were neutral, and 19.6% disagreed with a corresponding mean and standard deviation of (3.57; 1.092).

Table 4.11 Grading of Firms Characteristics and Access to Finance by SMEs

<table>
<thead>
<tr>
<th>Description</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Dev</th>
</tr>
</thead>
<tbody>
<tr>
<td>The size and age of my business greatly affects my ability to acquire a loan</td>
<td>0</td>
<td>3.3</td>
<td>13</td>
<td>25</td>
<td>58.7</td>
<td>4.39</td>
<td>.838</td>
</tr>
<tr>
<td>My business struggles to provide required financial information by banks, limiting my loan accessibility</td>
<td>21.7</td>
<td>23.9</td>
<td>37</td>
<td>12</td>
<td>5.4</td>
<td>2.55</td>
<td>1.123</td>
</tr>
<tr>
<td>My business has fewer assets that can be used as security while accessing a bank loan</td>
<td>0</td>
<td>0</td>
<td>17.4</td>
<td>40.2</td>
<td>42.4</td>
<td>4.25</td>
<td>.736</td>
</tr>
<tr>
<td>The number of years that I have been in business affect my ability to access a bank loan</td>
<td>21.7</td>
<td>15.2</td>
<td>46.7</td>
<td>9.8</td>
<td>6.5</td>
<td>2.64</td>
<td>1.125</td>
</tr>
<tr>
<td>Business that have been running for many years indicate they have the ability to withstand tough economic conditions, leading to easy access to loans</td>
<td>0</td>
<td>17.4</td>
<td>31.5</td>
<td>18.5</td>
<td>32.6</td>
<td>3.66</td>
<td>1.112</td>
</tr>
<tr>
<td>Businesses that are composed of partnerships have easy access to finance for expansion</td>
<td>0</td>
<td>6.5</td>
<td>33.7</td>
<td>41.3</td>
<td>18.5</td>
<td>3.72</td>
<td>.843</td>
</tr>
<tr>
<td>Ownership structure has a positive effect on a business’ ability to access bank loans</td>
<td>0</td>
<td>13</td>
<td>30.4</td>
<td>16.3</td>
<td>40.2</td>
<td>3.84</td>
<td>1.102</td>
</tr>
<tr>
<td>My business profitability is a yardstick used by banks to provide me with a loan</td>
<td>32.6</td>
<td>41.3</td>
<td>26.1</td>
<td>0</td>
<td>0</td>
<td>1.93</td>
<td>.768</td>
</tr>
<tr>
<td>Lack of reliable business information has led to my access to loans at a high interest rate</td>
<td>0</td>
<td>6.5</td>
<td>38</td>
<td>29.3</td>
<td>26.1</td>
<td>3.75</td>
<td>.921</td>
</tr>
<tr>
<td>Banks pay much attention to accounting information when I apply for a loan</td>
<td>0</td>
<td>19.6</td>
<td>31.5</td>
<td>21.7</td>
<td>27.2</td>
<td>3.57</td>
<td>1.092</td>
</tr>
</tbody>
</table>
4.6.2 Correlation Analysis of Firms Characteristics and Access to Finance by SMEs

Table 4.12 provides a correlation analysis for firms characteristic factors and their significance to SMEs’ access to finance, and it indicates that firm age was insignificant to SMEs’ access to finance (r=0.160, p>0.5). Ownership structure of the firm was insignificant to SMEs’ access to finance (r=0.110, p>0.5). Business type was significant to SMEs’ access to finance (r=0.423, p<0.1). Financial characteristics were insignificant to SMEs’ access to finance (r=0.070, p>0.5).

Table 4.12 Correlation Analysis of Firms Characteristics and Access to Finance by SMEs

<table>
<thead>
<tr>
<th></th>
<th>SMEs Access to Finance</th>
<th>Firm Age</th>
<th>Ownership Structure of the Firm</th>
<th>Business Type</th>
<th>Financial Characteristics</th>
</tr>
</thead>
<tbody>
<tr>
<td>SMEs Access to Finance</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firm Age</td>
<td>.160</td>
<td>.128</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ownership Structure of the Firm</td>
<td>.110</td>
<td>.296</td>
<td>.018</td>
<td>.864</td>
<td>1</td>
</tr>
<tr>
<td>Business Type</td>
<td>.423**</td>
<td>.028</td>
<td>.537**</td>
<td>.000</td>
<td>1</td>
</tr>
<tr>
<td>Financial Characteristics</td>
<td>.070</td>
<td>.945</td>
<td>.200</td>
<td>.056</td>
<td>.703</td>
</tr>
</tbody>
</table>

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

4.6.3 Regression Analysis of Firms Characteristics and Access to Finance by SMEs

Table 4.13 shows the regression analysis for significant factors of firm’s characteristics and their relation to SMEs’ access to finance, and the adjusted R square of 0.170 means that business type influences SMEs’ ability to access finance by 17%.
Table 4.13 Regression Model Summary of Firms Characteristics and Access to Finance by SMEs

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. of Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.423</td>
<td>.179</td>
<td>.170</td>
<td>.30813</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Business Type

Table 4.14 presents the regression analysis of variance for the significant factors of firm’s characteristics and their relation to SMEs’ access to finance, and the value of F(1,90) = 19.602, p<0.1 shows that there was a significant difference between business type and SMEs’ access to finance, indicating that the analysis provided a great fit for the study.

Table 4.14 Regression ANOVA of Firm’s Characteristics and Access to Finance by SMEs

<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>1 Regression</td>
<td>1.861</td>
<td>1</td>
<td>1.861</td>
<td>19.602</td>
<td>.000</td>
</tr>
<tr>
<td>Residual</td>
<td>8.545</td>
<td>90</td>
<td>.095</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>10.406</td>
<td>91</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Business Type

b. Dependent Variable: SMEs’ Access to Finance

Table 4.15 indicates the regression coefficients for the significant factors of firm’s characteristics and their relation to SMEs’ access to finance, and it shows that business type was significant to SMEs’ access to finance since its p value was <0.1 and the B value of 0.209 shows that every increase in business type would increase SMEs’ access to finance by 20.9%.

Table 4.15 Regression Coefficients for Firm’s Characteristics and Access to Finance by SMEs

<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>3.011</td>
<td>.140</td>
<td>.209</td>
</tr>
<tr>
<td>Business Type</td>
<td>3.011</td>
<td>.140</td>
<td>.209</td>
<td>.047</td>
</tr>
</tbody>
</table>

a. Dependent Variable: SMEs’ Access to Finance
4.6.4 Correlation Analysis for Factors Influencing Access to Finance by SMEs

Table 4.16 provides a correlation analysis for factors influencing SMEs’ access to finance, and it indicates that lending requirements were significant to SMEs’ access to finance (r=0.401, p>0.1). Financial literacy was significant to SMEs’ access to finance (r=0.623, p>0.1). Firm’s characteristics were significant to SMEs’ access to finance (r=0.460, p>0.1).

<table>
<thead>
<tr>
<th>SMEs Access to Finance</th>
<th>Lending Requirements</th>
<th>Financial Literacy</th>
<th>Firm Characteristics</th>
</tr>
</thead>
<tbody>
<tr>
<td>SMEs Access to Finance</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lending Requirements</td>
<td>.401**</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td></td>
<td>.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial Literacy</td>
<td>.623**</td>
<td>.259*</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>.000</td>
<td>.013</td>
<td></td>
</tr>
<tr>
<td>Firm Characteristics</td>
<td>.460**</td>
<td>.055</td>
<td>.123</td>
</tr>
<tr>
<td></td>
<td>.000</td>
<td>.602</td>
<td>.243</td>
</tr>
</tbody>
</table>

** Correlation is significant at the 0.01 level (2-tailed)
* Correlation is significant at the 0.05 level (2-tailed)

4.6.5 Regression Analysis of Factors Influencing Access to Finance by SMEs

Table 4.17 shows the regression analysis for significant factors influencing SMEs’ access to finance, and the adjusted R square of 0.885 means that lending requirements, financial literacy, and firm characteristics impact SMEs’ ability to access finance by 88.5%.

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. of Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.943</td>
<td>.888</td>
<td>.885</td>
<td>.11492</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Lending Requirements, Financial Literacy, and Firm Characteristics
Table 4.18 presents the regression analysis of variance for factors influencing SMEs’ access to finance, and the value of $F(3,88) = 233.330$, $p<0.1$ shows that there was a significant difference between lending requirements, financial literacy, and firm characteristics and SMEs’ access to finance, indicating that the analysis provided a great fit for the study.

**Table 4.18 Regression ANOVA of Factors Influencing Access to Finance by SMEs**

<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>9.244</td>
<td>3</td>
<td>3.081</td>
<td>233.330</td>
<td>.000</td>
</tr>
<tr>
<td>Residual</td>
<td>1.162</td>
<td>88</td>
<td>.013</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>10.406</td>
<td>91</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Lending Requirements, Financial Literacy, and Firm Characteristics

b. Dependent Variable: SMEs’ Access to Finance

Table 4.19 indicates the regression coefficients for factors influencing SMEs’ access to finance, and it shows that lending requirements were significant to SMEs’ access to finance since their $p$ value was $<0.1$ and the $B$ value of 0.222 shows that every increase in lending requirements would increase SMEs’ access to finance by 22.2%. Financial literacy was significant to SMEs’ access to finance since its $p$ value was $<0.1$ and the $B$ value of 0.479 shows that every increase in financial literacy would increase SMEs’ access to finance by 47.9%. Firms characteristics requirements were significant to SMEs’ access to finance since their $p$ value was $<0.1$ and the $B$ value of 0.190 shows that every increase in firms characteristics would increase SMEs’ access to finance by 19%.

**Table 4.19 Regression Coefficients for Factors Influencing Access to Finance by SMEs**

<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 (Constant)</td>
<td>.561</td>
<td>.116</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lending Requirements</td>
<td>.222</td>
<td>.013</td>
<td>.613</td>
<td>4.832</td>
</tr>
<tr>
<td>Financial Literacy</td>
<td>.479</td>
<td>.024</td>
<td>.732</td>
<td>16.617</td>
</tr>
<tr>
<td>Firm Characteristics</td>
<td>.190</td>
<td>.017</td>
<td>.404</td>
<td>11.256</td>
</tr>
</tbody>
</table>

a. Dependent Variable: SMEs’ Access to Finance
4.6 Chapter Summary

This chapter has presented results and findings based on the data analyzed for lending requirements and access to finance by SMEs, financial literacy and access to finance by SMEs, and firms characteristics and access to finance by SMEs in Meru County. The next chapter concludes the study by providing the study’s discussions, conclusions, and recommendations.
CHAPTER FIVE

5.0 DISCUSSIONS, CONCLUSIONS, AND RECOMMENDATIONS

5.1 Introduction
The general objective of the study was to establish the factors influencing access to finance by SMEs in Meru County. This chapter concludes the study by presenting the study’s summary, discussions, conclusions, and recommendations based on the objectives that were set to determine how lending requirements, financial literacy, and firm’s characteristics influence SMEs’ access to finance in Meru County.

5.2 Summary
The general objective of the study was to establish the factors influencing access to finance by SMEs in Meru County. The study was focused in determining the effect of lending requirements on access to finance by SMEs in Meru County, to assess the influence of financial literacy on access to finance by SMEs in Meru County, and to determine the effect of firms’ characteristics on access to finance by SMEs in Meru County.

This study adopted a descriptive survey research design. The target population constituted of registered SME’s in Meru County in Kenya. The entire target population comprised of 1650 registered SME’s. The sampling frame was obtained from office of economics and statistical data in Meru County. Stratified sampling technique was adopted for this study, since the study was looking at different heterogeneous categories of SMEs within Meru County, stratified sampling was ideal. For this study, Yamane (1967) formula was used to determine the sample size of 92 SMEs. The study utilized a questionnaire as a tool to collect primary data. The researcher pilot tested the questionnaire using SMEs in Kiambu County, to ensure the study’s validity and reliability. Questionnaires were administered by use of drop and pick approach to SMEs owners/managers where respondents were given 1-2 hours to fill in the questionnaire. The remaining questionnaires were administered through face-to-face approach; whereby some owners/ managers completed the questionnaires. SPSS was used to analyze descriptive statistics (percentages, and frequencies); and inferential statistics (correlations, and regressions). Analyzed data was presented using tables and figures.
The study showed that entrepreneurs normally did not use title deeds (business or land) in order to access a loan, and their loan security had to cover their loan amount or surpass it for it to be accepted by the bank. The entrepreneurs had used their business loans for their personal and private use although the use of security to pick a business loan, had slightly reduced their chances of misusing loans taken for business growth. The study revealed that the use of security ensured that the entrepreneurs did not invest in high risk projects, and their willingness to pledge security for a loan increased their probability of acquiring a bank loan. The study indicated that loan security acted as an indicator to the bank that the business men and women were creditworthy individuals.

The study revealed that SMEs in Meru County did succeed in accessing financial credit even though strict loan conditions were their major challenge in accessing loans. Most banks believe that small businesses do not have the capacity to repay a loan in case they default, and the SMEs’ owners were in agreement with the decision of banks denying them a loan when they viewed them to be high risk defaulters. The study showed that SME owners incurred some financial costs in order to receive financial credit from banks or other financial institutions, and there were a lot of costs (transaction costs) that made borrowing very expensive for their businesses. The study revealed that one needs education and skills in order to run a business, and that most of the SME owners in Meru County were well educated and informed on how to run a business.

The study showed that the size and age of SME businesses greatly affected their ability to acquire a loan, and that most of the businesses did not struggle to provide required financial information by banks which did not limit their loan accessibility, however, their businesses had fewer assets that could be used as security while accessing bank loans. The study revealed that the number of years that entrepreneurs had been in business did not affect their ability to access bank loans, however, business that had been running for many years indicated they had the ability to withstand tough economic conditions, leading to easy access to loans. Businesses that were composed of partnerships had easy access to finance for expansion, meaning ownership structure had a positive effect on a businesses’ ability to access bank loans.
5.3 Discussions

5.3.1 Lending Requirements and Access to Finance by SMEs

Entrepreneurs normally did not use title deeds (business or land) in order to access a loan. This results differ from those of Aghion and Bolton (2012) who state that, SMEs in particular provide security in form of fixed assets (houses, the car, and anything that could actually bring back the principal) in the event of default on loans. The SMEs’ loan security provided by the entrepreneurs must cover the loan amount or surpass it for it to be accepted by the bank. This results are agree with the findings of Mbonyane and Ladzani (2011) that, in most banks, in order to finance SMEs and to accept loan projects, the collateral must cover 100% or more, equal to the amount of credit extended or financial product.

The study revealed that the businessmen in Meru County had used their business loan for their own personal and private use. This results are agree with the findings of Kihimbo et al. (2012) that, sometimes the borrowers divert the funds provided by the lenders for their own personal and private use. The use of security to pick a business loan by the entrepreneurs, has reduced their chances of misusing loans they had taken for their business growth. This results concur with those of Roodman (2011) who noted that, the collateral requirements when in place can reduce negative consequences that can arise from improper utilization of the funds by SMEs.

The use of security provided by the SME entrepreneurs ensures that they do not invest in high risk projects. This results are similar to observations made by Wanjohi (2010), that, collateral requirements serve as an incentive mechanism because higher collateral enforces a selection of less risky projects. The entrepreneurs’ willingness to pledge security for a loan increases their probability of acquiring a bank loan. This results agree with the findings of Matavire and Duflo (2013) that, the willingness of the entrepreneur to pledge collateral positively influences the quality of credit request as perceived by the bank.

The entrepreneurs’ loan security acts as an indicator to the bank that they are creditworthy individuals. This results concur with Aghion and Bolton (2012) who state that, collateral acts as an indicator of the borrower’s creditworthiness. The bank screens firms by
offering both loan contracts with higher collateral value with lower interest rates and loan contracts with lower collateral with higher interest rates. Entrepreneurs have missed out on a bank loan because their business does not have audited financial records. This results correspond to the findings of Vuvor and Ackah’s (2011) study, that the challenges faced by SMEs in Ghana include, the inability of SMEs to provide collateral and other information needed by banks such as audited financial statement coupled with the high cost of loan in terms of high interest rates making it extremely difficult to access bank loans.

Entrepreneurs did not have poor access to bank loans, because they were more than likely to default on their loan repayment. This results are similar to those of Obwori (2012) who states that, SMEs have fewer collateralizable assets than large firms, and this partly relates to the stage of growth the firm is in, and also SMEs have a smaller proportion of fixed assets is the capital constraints faced by them. Entrepreneurs had not failed to secure a business loan because they could not meet the bank’s requirements. The study results are confirmed by Roodman (2011) who observed that, small business in Africa can once in a while meet the conditions set by money related organizations, which see SMEs as an unsafe in view of poor certifications and absence of satisfactory data about their capacity to reimburse advances.

5.3.2 Financial Literacy and Access to Finance by SMEs
The entrepreneurs’ businesses in Meru County did succeed in accessing financial credit. This results differ from those conducted by Kiraithe (2015) that revealed that stringent loan conditions had inhibited SMEs access to financing particularly from the banking sector and major financial institutions. Strict loan conditions are the entrepreneurs’ major challenge in accessing loans. This results concur with those of Wangui et al. (2014) who notes that, many SMEs are not able to access loans from financial institutions due to the stringent conditions that loanees have to fulfil.

Most banks believe that as a small business, the entrepreneurs do not have the capacity to repay a loan in case they default. This results concur with Mbonyane and Ladzani (2011) who state that, collateral is deemed important in the case by banks since most banks do not trust that SMEs have the capacity to repay should they go into default. As
businessmen, the entrepreneurs are in agreement with the decision of banks denying them a loan when they were deemed as high risk defaulters. This results concur with Bert et al. (2015) who states that, if a bank feels that a given SME offers high risk of default, they are obligated to deny them financing. This is not just a wise idea, but one that is also geared at protecting banks and financial institutions bottom lines.

As business persons, the entrepreneurs incur some financial costs in order to receive financial credit from a bank or other financial institution. These results are in agreement with Gitari (2012) who states that, the cost of credit is defined as the financial burden that one has to incur to access a given financial credit from a bank or other financial institution. There are a lot of costs (transaction costs) that make borrowing very expensive for the entrepreneurs’ business. This results concur with those of Van AardtSmit and Olawale (2012) who states that, in essence, high transaction costs do not only increase the cost of borrowing, but restrict access to external borrowing by SMEs.

One needs education and skills in order to run a business. This results agree with those of Aabii (2014) who observed that, education and skills are needed to run a business, and that, majority of people carrying out SME’s in Kenya are not quite well informed in terms of education and skills. The entrepreneurs in Meru County are well educated and are informed on how to run a business. This results differ with observations made by ILO (2010) that most of the entrepreneurs have low literacy levels as majority of them drop from the primary level or they have acquired primary level.

The entrepreneurs in Meru County have the ability to carry out managerial routines in their businesses. This results are in agreement with those of Falkena (2011) that, literacy level was reflected in their ability to carry out managerial routines - the routine includes making decisions on financial investment and management - and this influences the decision on the external funding of his enterprise. The entrepreneurs in Meru County have the ability to keep proper business records (bookkeeping) that are often demanded by banks. The results are in agreement with Falkena (2011) who noted that; complete, accurate and precise information is necessary for financial decisions including obtaining business loans. The literacy level is again observed in the ability to have appropriate book keeping skills.
5.3.3 Firms Characteristics and Access to Finance by SMEs

Size and age of an entrepreneurs’ business greatly affects my ability to acquire a loan. This results are in agreement with observations made by Kira (2012) that, firm characteristics affect SMEs’ ability to access external finance. The size and age of the firm were identified as important variables under this category. Beal and Goyen (2015) that, the age of the firm has implications on financial access.

The entrepreneurs’ business did not struggle to provide required financial information by banks, thus did not limit their loan accessibility. This results differ with those of Kakuru (2013) who argues that, SMEs are faced with information opacity such as inability to provide financial information, since most are owned and operated by the entrepreneurs themselves which means they have no legal requirement to regularly report financial information. The entrepreneurs’ businesses have fewer assets that can be used as security while accessing a bank loan. This results are in agreement with those of Kakuru (2013) who states that SMEs have fewer assets to offer as collateral, and Mbonyane and Ladzani (2011) observe that, in order to reduce the anticipated risk and moral hazard associated with lending, the banks use collateral as one of the instrument.

The number of years that entrepreneurs’ business have been in business does not affect their ability to access a bank loan. This results differ with Beal and Goyen (2015) who state that, the age of the firm has implications on financial access, and Kushnir (2010) who observed that, the age of the firm can affect performance by inducing organizational inertia and by impairing firms’ ability to perceive valuable signals. Business that have been running for many years indicate they have the ability to withstand tough economic conditions, leading to easy access to loans. This results coincide with the perspective offered by Rambo (2013) that, the longer a firm exists; the more it signals that it can weather tough economic conditions, and furthermore, by staying in business, a firm can signal that it does not adopt opportunistic behavior.

Businesses that are composed of partnerships have easy access to finance for expansion. This results agree with Roodman (2011) who observed that lenders may perceive incorporation as a sign of credibility and formality of operations, and thus, the form of ownership could affect the debt-equity decisions of SMEs. Ownership structure has a positive effect on a business’ ability to access bank loans. This results are in tandem with
observations made by Coleman and Cohn (2010) who found evidence suggesting a positive relationship between leverage and incorporation, thus, one can state that, ownership structure has a positive effect on firms’ access to finance such that incorporated firms are likely to have more access to finance.

The entrepreneurs’ business profitability is not a yardstick used by banks to provide them with a loan. This results differ with those of Dun and Girma (2012) who note that, some sectors are less profitable than others, and since profitability is a yardstick used by lenders, then it means that some sectors may be disadvantaged in access to finance. Lack of reliable business information has led to the entrepreneurs accessing loans at a high interest rate. This results coincide with those of Wangui and Tirimbina (2014) who state that, lack of reliable information leads to comparably high interest rates even if a long term relationship between borrower and bank exists.

Banks pay much attention to accounting information when the entrepreneurs apply for a loan. This results go hand-in-hand with those of Obwori (2012) who, found that lenders in the UK pay much attention to accounting information in order to deal with the loan applications of small firms, since asymmetric information problems may be more pronounced for small firms.

5.4 Conclusions

5.4.1 Lending Requirements and Access to Finance by SMEs

The study concludes that entrepreneurs normally did not use title deeds (business or land) in order to access a loan, and their loan security had to cover their loan amount or surpass it for it to be accepted by the bank. The entrepreneurs had used their business loans for their personal and private use although the use of security to pick a business loan, had slightly reduced their chances of misusing loans taken for business growth. The study concludes that the use of security ensured that the entrepreneurs did not invest in high risk projects, and their willingness to pledge security for a loan increased their probability of acquiring a bank loan. The study concludes that loan security acted as an indicator to the bank that the business men and women were creditworthy individuals, and some of the entrepreneurs had missed out on bank loans because their business did not have audited financial records. The study concludes that the entrepreneurs did not have poor access to
bank loans, because they were more than likely to default on their loan repayment, and that none had failed to secure a business loan because they could not meet the bank’s requirements.

5.4.2 Financial Literacy and Access to Finance by SMEs
The study concludes that SMEs in Meru County did succeed in accessing financial credit even though strict loan conditions were their major challenge in accessing loans. Most banks believe that small businesses do not have the capacity to repay a loan in case they default, and the SMEs’ owners were in agreement with the decision of banks denying them a loan when they viewed them to be high risk defaulters. The study concludes that SME owners incurred some financial costs in order to receive financial credit from banks or other financial institutions, and there were a lot of costs (transaction costs) that made borrowing very expensive for their businesses. The study concludes that one needs education and skills in order to run a business, and that most of the SME owners in Meru County were well educated and informed on how to run a business. They had the ability to carry out managerial routines in their businesses, as well as the ability to keep proper business records (bookkeeping) that were often demanded by banks.

5.4.3 Firms Characteristics and Access to Finance by SMEs
The study concludes that the size and age of SME businesses greatly affected their ability to acquire a loan, and that most of the businesses did not struggle to provide required financial information by banks which did not limit their loan accessibility, however, their businesses had fewer assets that could be used as security while accessing bank loans. The study concludes that the number of years that entrepreneurs had been in business did not affect their ability to access bank loans, however, business that had been running for many years indicated they had the ability to withstand tough economic conditions, leading to easy access to loans. Businesses that were composed of partnerships had easy access to finance for expansion, meaning ownership structure had a positive effect on a businesses’ ability to access bank loans. The study concludes that business profitability was not a yardstick used by banks to provide them with loans, and lack of reliable business information had led to businesses accessing loans at high interest rates since banks paid much attention to accounting information when entrepreneurs applied for loans.
5.5 Recommendations

5.5.1 Recommendations for Improvement

5.5.1.1 Lending Requirements and Access to Finance by SMEs
The study recommends the business entrepreneurs of SMEs to ensure that they keep an audited financial record for their businesses. This would ensure that they make strategic plans for their businesses based on the business performance, as well as facilitate their ability to access and acquire loans from banks and other financial institutions.

5.5.1.2 Financial Literacy and Access to Finance by SMEs
The study recommends that the government policy makers put in place financial regulations that would lower the cost of acquiring loans for SMEs and other organizations in general. This would greatly increase the financial performance of SMEs and financial institutions in the country leading to a great business performance in general.

5.5.1.3 Firms Characteristics and Access to Finance by SMEs
The study recommends the business entrepreneurs of SMEs to ensure that they have reliable information of their business at hand. This will facilitate their ability to expand their businesses based on proper information, and they can use this information to attract investors who would be willing to engage with them, as well as facilitate their boundaries in accessing business loans.

5.5.2 Recommendations for Further Studies
This study focused on SMEs in Meru County in Kenya. The study focused on factors influencing SMEs’ access to financing, but limited to collateral requirements, lending procedures, and measures taken to enhance access to SME financing. Further studies need to be conducted in other counties within Kenya, to examine the full extent of the discussed items, and other studies should be conducted on SMEs in Meru County and focus on other factors other than those discussed in this study.
REFERENCES


This study examines the “Determinants of Financial Inclusion (Access to Finance) of Small and Medium Size Enterprises in Kenya with a focus on Meru County”. This questionnaire will facilitate the researcher to have a conclusive results for the above study. Your responses will be used for academic purposes only. Kindly take your time and fill the questionnaire appropriately.

Part A: Personal Information

1. Gender

   Male ☐

   Female ☐

2. What is your level of education?

   Secondary ☐

   College ☐

   Undergraduate Degree ☐

   Master’s Degree ☐

   Other ☐ ________

3. How many years have you been in business?

   Less than 12 Months ☐

   1-3 Years ☐

   4-6 Years ☐

   7-9 Years ☐

   10 Years and Above ☐
4. What is your monthly income bracket?
   - Less than 10,000 Ksh
   - 10,001 – 20,000 Ksh
   - 20,001 – 30,000 Ksh
   - 30,001 – 40,000 Ksh
   - 40,000 Ksh and Above

5. Where do you get your business loan from?
   - Friends
   - Family
   - Sacco
   - Bank
   - Other

6. How would you rate your business’ ability to acquire a loan?
   - Very Easy
   - Easy
   - Somewhat Difficult
   - Difficult
   - Very Difficult
Part B: Lending Requirements and Access to Finance by SMEs

7. Kindly rate the following statement based on your experience on lending requirements and access to finance by your business using the scale 1 - Strongly Disagree, 2 – Disagree, 3 – Not Sure, 4 – Agree, and 5 – Strongly Agree.

<table>
<thead>
<tr>
<th>No:</th>
<th>Statement</th>
<th>1</th>
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<tbody>
<tr>
<td>a.</td>
<td>I normally use title deeds (business or land) in order to access a loan</td>
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<td>b.</td>
<td>My loan security must cover my loan amount or surpass it for it to be accepted by the bank</td>
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<td>c.</td>
<td>As a businessman, I have used my business loan for my own personal and private use</td>
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<td>d.</td>
<td>The use of security to pick a business loan, has reduced my chances of misusing loans I take for my business growth</td>
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<td>e.</td>
<td>The use of security ensures that I do not invest in high risk projects</td>
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<td>f.</td>
<td>My willingness to pledge security for a loan increases my probability of acquiring a bank loan</td>
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<td>g.</td>
<td>My loan security acts as an indicator to the bank that I am a creditworthy individual</td>
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<td>h.</td>
<td>I have missed out on a bank loan because my business does not have audited financial records</td>
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<tr>
<td>i.</td>
<td>I have poor access to bank loans, because I am more than likely to default on my loan repayment</td>
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<td>j.</td>
<td>I have failed to secure a business loan because I could not meet the bank’s requirements</td>
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</tbody>
</table>
Part C: Financial Literacy and Access to Finance by SMEs

8. Kindly rate the following statement based on your level of financial literacy and access to finance by your business using the scale 1 - Strongly Disagree, 2 – Disagree, 3 – Not Sure, 4 – Agree, and 5 – Strongly Agree.

<table>
<thead>
<tr>
<th>No:</th>
<th>Statement</th>
<th>1</th>
<th>2</th>
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<tbody>
<tr>
<td>a.</td>
<td>My business rarely succeeds in accessing financial credit</td>
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<tr>
<td>b.</td>
<td>Strict loan conditions are my major challenge in accessing loans</td>
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<td>c.</td>
<td>Most banks believe as a small business, I do not have the capacity to repay a loan in case I default</td>
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<td>d.</td>
<td>As a businessman, I am in agreement with the decision of banks denying me a loan when they see me as a high risk defaulter</td>
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<td>e.</td>
<td>As a business person, I incur some financial costs in order to receive financial credit from a bank or other financial institution</td>
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<td>f.</td>
<td>There are a lot of costs (transaction costs) that make borrowing very expensive for my business</td>
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<td>g.</td>
<td>One needs education and skills in order to run a business</td>
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<td>h.</td>
<td>I am well educated and I am informed on how to run a business</td>
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<tr>
<td>i.</td>
<td>I have the ability to carry out managerial routines in my business</td>
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<td>j.</td>
<td>I have the ability to keep proper business records (bookkeeping) that are often demanded by banks</td>
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</tbody>
</table>
Part D: Firms Characteristics and Access to Finance by SMEs

9. Kindly rate the following statement based on your firm characteristics and access to finance by your business using the scale 1 - Strongly Disagree, 2 – Disagree, 3 – Not Sure, 4 – Agree, and 5 – Strongly Agree.

<table>
<thead>
<tr>
<th>No:</th>
<th>Statement</th>
<th>1</th>
<th>2</th>
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</thead>
<tbody>
<tr>
<td>a.</td>
<td>The size and age of my business greatly affects my ability to acquire a loan</td>
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<tr>
<td>b.</td>
<td>My business struggles to provide required financial information by banks, limiting my loan accessibility</td>
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<td>c.</td>
<td>My business has fewer assets that can be used as security while accessing a bank loan</td>
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<td>d.</td>
<td>The number of years that I have been in business affect my ability to access a bank loan</td>
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<tr>
<td>e.</td>
<td>Business that have been running for many years indicate they have the ability to withstand tough economic conditions, leading to easy access to loans</td>
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<td>f.</td>
<td>Businesses that are composed of partnerships have easy access to finance for expansion</td>
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<td>g.</td>
<td>Ownership structure has a positive effect on a business’ ability to access bank loans</td>
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<td>h.</td>
<td>My business profitability is a yardstick used by banks to provide me with a loan</td>
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<tr>
<td>i.</td>
<td>Lack of reliable business information has led to my access to loans at a high interest rate</td>
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<tr>
<td>j.</td>
<td>Banks pay much attention to accounting information when I apply for a loan</td>
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</tr>
</tbody>
</table>

THANK YOU