

**RELATIONSHIP BETWEEN ACCOUNTS  
RECEIVABLE MANAGEMENT PRACTICES AND  
GROWTH OF SMALL AND MEDIUM ENTERPRISES  
IN KAKAMEGA COUNTY, KENYA**

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**2017**

**Relationship between Accounts Receivable Management Practices  
and Growth of Small and Medium Enterprises in Kakamega  
County, Kenya**

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**A Thesis Submitted in Partial Fulfillment for the Degree of Doctor  
of Philosophy in Business Administration (Finance) in the Jomo  
Kenyatta University of Agriculture and Technology**

**2017**

**DECLARATION**

This Thesis is my original work and has not been presented for a degree in any other University.

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## **DEDICATION**

This work is dedicated to my parents Mr and Mrs Jafred Lyani, my husband Festus Sindani Malalu for his financial and moral support, my children Wanakacha, Wambulwa, Namaemba, Tsimbiri, and Malalu. Your love, encouragement and support have enabled me forge ahead even when things seemed difficult. May God bless you all.

## **ACKNOWLEDGEMENT**

First and foremost, I would like to thank Jehovah God almighty who has granted me sufficient Grace and strength to come this far, his knowledge and wisdom has made this research a reality. I wish to sincerely thank my supervisors: Professor G.S. Namusonge and Professor Maurice Sakwa who accepted to tirelessly guide me and mentor me. Their understanding, encouragement and constructive critiques have made me a better researcher, God bless you. Lastly, I wish to acknowledge the support given to me by my nephew Nebat Galo and all my colleagues.

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## ACRONYMS AND ABBREVIATIONS

<b>AMOS</b>	Analysis of Moment Structure
<b>ANOVA</b>	Analysis of Variance
<b>ARAP</b>	Accounts Receivable Analysis Practice
<b>ARCP</b>	Accounts Receivable Collection Practices
<b>AREP</b>	Accounts Receivable Extension Practice
<b>ARFP</b>	Accounts Receivable Financing Practices
<b>ARM</b>	Accounts Receivable Management
<b>ARRAP</b>	Accounts Receivable Risk Assessment Practices
<b>CDF</b>	Constituencies Development Fund
<b>COSO</b>	Committee of Sponsoring - Treadway Commission
<b>GDP</b>	Gross Domestic Product
<b>GOK</b>	Government of Kenya
<b>OECD</b>	Organization for Economic Co-Operation and Development
<b>PACFL</b>	President's Advisory Council on Financial Literacy
<b>PPOA</b>	Public Procurement and Oversight Authority
<b>RM</b>	Receivables Management
<b>SMES</b>	Small and Medium Enterprises
<b>SPSS</b>	Statistical package for the Social Sciences
<b>TIVET</b>	Technical, Industrial, Vocational and Entrepreneurship

## DEFINITION OF TERMS

**Accounts Receivable Analysis Practice:** Kibor and Ngahu (2015) defined Accounts receivable analysis as the practice of analyzing credit data.

**Accounts Receivable Collection Practice:** The accounts receivable collection practice is the collection effort aimed at accelerating collections from slow payers and reducing bad debt losses (Kariuki, 2010)

**Accounts Receivable Extension Practices:** Pandey (2004) asserts that this practice involve setting down agreement under which credit is extended to a customer.

**Accounts Receivable Financing:** is defined as any type of financing which distinctly relies on AR, either as collateral or as eligibility requirement (Mubashir, 2012).

**Accounts Receivable Management:** is the management of credit sales (debtors) (Pandey, 2008).

**Accounts Receivable Risk Assessment Practice:** It is a structured approach to managing uncertainties in the client repayment, (Gakure, Ngugi & Ndwiga 2012),.

**Accounts Receivables:** Represent credit given by firms to their business partners. (Calomiris & Hubbard, 1995).

**Financial Literacy:** is the ability to use knowledge and skills to manage financial resources effectively for a lifetime of financial well-being (PACFL, 2008).

**Growth:** is an organizational outcome resulting from the combination of firm-specific resources, capabilities and routines (Nelson & Winter, 1982).

**Portfolio Strategy:** Michalski (2008) suggests that a portfolio strategy is the act of classifying debtors according to their individual character .that is ability to pay.

## ABSTRACT

The objective of this study was to determine the effect of Account Receivable management practices on growth of SMEs. The practices identified were, accounts receivable analysis, Extension, risk assessment, collection, financing practices, and how the level of financial literacy of Accounts receivable management practices affect growth of SMEs. The target population was 5401 registered SMEs under Single Business Permit Registration. Proportionate stratified random sampling technique was used to select 359 SMEs. The wards were identified as the unit of sampling. The study was premised on the portfolio theory, the pecking order theory and the growth theory. The study adopted a mixed survey research design. Primary data was collected using semi-structured questionnaire .Data was analyzed using statistical Package for Social Sciences (SPSS) .Pearson product moment correlation was computed to assess the relationship between Accounts receivable management practices and growth of SME. Descriptive statistics such as mean, standard deviation and homoscedasticity were used to test for normality of data. Ordinary Least Square method was utilized to establish the cause-effect relationship between variables while hypotheses were tested at 5% significance level. The overall model was statistically significant at  $F=11.298$  and  $p\text{-value} (0.000 < 0.05)$ . The findings revealed that efficient Accounts receivable management practices, when adopted by SMEs lead to growth. The study recommended that owners and managers should be trained and made to understand the various techniques of managing Accounts receivable levels. The findings would form a basis for government and policy makers in management decision making, to formulate Accounts receivable management strategies that would help minimize bad and delinquent debt. The study also forms a basis for further research and adds to the existing body of knowledge.

## **CHAPTER ONE**

### **INTRODUCTION**

#### **1.1 Background of the Study**

Liquidity decision is an important component of financial management that a prudent investor must focus on (Ongore & Kusa, 2013). It is sometimes referred to as working capital decision which looks at working capital as an operating capital that is readily available to a firm (Teruel & Solano 2007). Berk and Demarzo (2016) define net working capital as the “the capital required in the short term to run the business”. It is the difference between current assets and current liabilities and it is recorded on the statement of financial position. An entity’s level of working capital measures its short term financial position. Sound working capital management is crucial to the survival and growth of an organization (Jindal, Jain &Vartika, 2017). The working capital is essential in facilitating daily functions and enables firms achieve their corporate goals (Smith, 1980). Profit is one of those goals which a firm must strive to achieve to grow its worth and survive in the long run (Ongore & Kusa, 2013).

Accounts Receivable is one of the largest and most liquid of corporate assets Kimtai (2006) which are very important in facilitating business transactions. Pike and Neale (1999) consider accounts receivable as both a source and use of finance in that it can be obtained and extended. However, it can be unproductive unless it generates additional business since it ties up scarce financial resources and exposes organizations to risk of default in situations whereby the credit period is lengthy (Pike & Neale, 1999).Huge amounts of accounts receivable is likely to reduce the firm value and as such the need to have best Accounts Receivable best practices. Mbula, Momba and Njeru (2016) assert that Accounts receivable is a current asset and a component of working capital.

##### **1.1.1. Global Perspective of Accounts Receivable Management.**

Salek (2005) posits that an invoice has to be converted into cash in a timely manner; otherwise it becomes meaningless to raise it in the first place, the scholar further

emphasizes that as long as an invoice hasn't been paid there is no sale, and if there is no sale there is no money. Accounts receivable management is the facilitation of the completion of the collection process or better still put the completion of the sale. It is crucial that a firm keeps its current customers and strive to maintain repeat sales through good practices. Accounts Receivables are large investments which appear on a firm's balance sheet, just like capital budgeting projects, they are measured in terms of their net present values (Emery et al., 2004). They are therefore an important component of firm assets. Accounts receivable are monies the customers owe a business, and are comprised of a huge number of invoiced amounts. They are the amounts a firm has the right to collect from their clients for providing them with goods or services on credit.

Summer and Wilson (2001) established from their study that the average ratio of accounts receivable to assets for the sampled firms was 30-40% the researchers further stated that it stands at 35% in the UK. This is an indication of the importance of Accounts receivable as an investment and requires attention on its proper management and financing. They form a part of primary source of incoming cash flow for most businesses, and hence there is need to analyze these invoices in aggregate to ascertain the health of the underlying cash flows. Jindal (2017) established in his empirical study on the commercial vehicle industry in India, done for the period 2009 to 2016 that there was evidence that an increase in the debtors' turnover will increase the profitability of the firm. Thus the efficient management of accounts receivables increases profitability.

Oware, Samanhyia and Ampong (2015), demonstrated that when a firm does not invest well in the collection of account receivable then the probability that a firm will stagnant as a result of very poor account receivables levels and debt accumulation would be high. This is clearly shown on how the operations of Ghana Water Company Ltd (GWCL) were affected. When accounts receivable take a long time to be collected; it becomes impossible investing in production for your next order. Uncollected amounts tie up working capital unreasonably and may lead to long business cycles. It is therefore important for a business to collect all owed amounts in a timely manner to avoid liquidity problems. Accounts receivable is an important



source of funds for both small and medium enterprises around the world (Petersen & Rajan, 1997; Demircuc-Kunt & Maksimovic, 2002). Most firms use Accounts receivable both to finance their input purchases (accounts payable) and offer financing to their clients. Pandey (2010) explains that, a limited capital base and poor cash flow levels as a result of uncollected monies deters growth of an entity. Connolly (2013) observed that many enterprises rarely maintained customer details and credit information; appropriate credit terms and billing cycle which affected timely collection of payments from the customers.

### **1.1.2 Kenyan Perspective of Accounts Receivable Management**

Kimtai (2006) agrees by stating that the failure of most firms whether small, medium or large were as a result of limited finances and management of the available scarce resources. Cash flow is the driving force behind every business operations (Mutwiri, 2007). An analysis of groups of hotels in Kenya show that total debtor's portfolio represents 13% of the balance sheet size of the firm and also indicates that the average value of debtors is 50% of the total borrowing (Gakure, Gekara, & Ngugi, 2017). These are amounts that require serious attention and proper management achieve the desired firms worth. Ngugi *et.al.* (2017), in their findings implied that the hotel management used various accounts receivables tools in reminding their clients. These were letters, phone calls, credit control, sending invoices and sending interest invoices. There was a significant relationship between adoption of the tools and efficiency of accounts receivable management. Bwisa *et al.* (2014) show that most of the Micro Small Business Enterprises in Bungoma District did not practice accounts receivable management which negatively affected business performance. Most scholars in Kenya are in agreement that a firm should manage its accounts receivable for its survival (Adusei, 2017; Ngugi, 2017). In these studies, it is clear that Selling on credit is risky, as there would be idle monies tied up in the accounts receivable. A firm's investment in account receivable depends upon how much it sells on credit and how long it takes to collect receivable. The process of effective utilization and efficient management of Accounts Receivable constitute major challenges for the owners and managers of SMEs. The Kenya Association of Manufacturers had to intervene on behalf of pharmaceutical distributors who were demanding about

Ksh.8billion, from their debtors among them leading supermarkets like Tusksys, Nakumatt and Naivas (Ciuri & Mutegi, 2015). This is a crucial problem that has affected their cash flow.

### **1.1.3 SME Perspective of Accounts Receivable Management.**

World over, various studies have been carried out on the growth of SMEs, illustrating the role SMEs play in the Economy. SMEs are very important economic wheels for growth and development in any country as indicated by recent publication by the 2016 Economic Survey (Kenya), they employees less than 99 workers. Studies indicate that in both developed and emerging economies (Mole & Namusonge, 2017), and contribute 60 percent of total formal employment in the manufacturing sector (Ayyagari et al., 2007). OECD, (2010) states that SMEs play a significant role towards overall enterprise growth, real GDP growth, new job creation and reduction of poverty, however, this units have limited resources due to the inability to have enough cash flows to meet their day to day obligations. SMEs dominate the informal sector in Kenya and they have a potential to grow into large companies that support the Gross Domestic Product (GDP) growth and check unemployment if encouraged by Government policy or public procurement authority, (Njeru, Namusonge & Kihoro, 2012).

Statistics Central Bureau of Statistics, (2004) indicates that there is high rate of failure and stagnation among many SMEs businesses. Millions of MSMEs go bankrupt every year, due to their inability to maintain good cash flow brought about by the uncollected amount on cash sales, which are accounts receivables (Richard 2008). A firm has two options of selling its products to the customers, either by selling on cash basis or selling on credit, the latter is riskless and an advantage since it improves its liquidity position but reduces its profitability. It is imperative that SMEs owners ensure they make liquidity decisions that enhance the market value of the entity.

The Government of Kenya as such recognizes the potential of SMEs in driving an economy and has therefore taken steps in facilitating trade between it and SMEs however one of the largest hitches for SMEs dealing with Government remains the

duration it takes to get paid which is due to beauracracy. SMEs in Kenya are not only operated by illiterate persons but also by well-educated and trained young men and women who have not been able to get jobs. In June 2011, the Public Procurement and Oversight Authority (PPOA) recommended that, the awarding of tenders by government ministries and department valued at 100 million and below be given to local SMEs to encourage unemployed graduates start small businesses and thus enhance job creation. This was indeed a good gesture on the part of the Government. Starting a business may seem an easy thing, however maintaining it by having a balance between attracting customers by providing credit sale and collecting overdue debts is a daunting task. In Kenya, this may be the reason why SMEs are unable take up tenders set aside for them by Government because of their inability to have sufficient funds to facilitate business offers by the government.

#### **1.1.4 Accounts Receivable Management Practices**

The starting point for accounts receivable management practices is to understand the policies and procedures for sales. Two critical questions to answer are, how and when a firm should evaluate a customer for credit, and whether there exist a credit policy. Myers (2003) describes AR management as methods and strategies adopted by a firm to ensure that they maintain the best optimal level of credit and its effective management. It is a component of financial management which involves Accounts Receivable analysis, Accounts Receivable extension, Accounts Receivable collection and Accounts Receivable financing. Some of the other components of Accounts receivable management practices are policies, measurement and outsourcing options.

Scheufler (2002) argues that a credit policy is an important document in an enterprise; it creates a common set of goals and recognizes the credit and collection departments as a key to the enterprise's strategies. According to Scheufler (2002) creating a credit policy involves several steps; Writing of a mission statement, highlighting the goals, defining the credit authority, credit evaluation, accounts receivables monitoring, financing, and actual collection. Mutwiri (2007) agrees that to control credit sales, it is necessary for a firm to specify clear responsibilities for credit department in its credit management policies and function. This function should be instilled with specific

goals and objectives for example, such as to maximize the protection of Accounts Receivables (Knox, 2004). Indeed, this can be done through proper analysis of accounts receivable.

Too, Kubasu and Langat, (2016) argue that money tied in accounts receivable is idle money and is not available for investment in the firm until and unless it is collected. Investment in receivables takes a huge chunk of an organization's assets, these assets are highly susceptible to bad debts and losses. It is therefore necessary to manage accounts receivables appropriately (Kungu, Wanjau, Waititu & Gekara, 2014). Accounts receivable management is an important process which involves putting in place best practices for controlling and collecting payments from customers (Fujo & Ali, 2016; Mukherjee, 2014; Omondi, 2014). It implies planning, organizing, directing and controlling of receivables which should lead to a shortened collection period, low levels of bad debts and a sound credit policy; which improves the businesses financial growth. This essentially is one of the most important corporate finance decision. Mukherjee (2014) noted that an efficient account receivable management practice enables a firm to minimize the amount of tied up funds in accounts receivables and consequently reduces a firm's percentage of bad debts. Hence it is imperative to ensure proper practices are instituted to achieve this. Good Accounts Receivable Management Practices are important in the achievement of firm's sustainability, and growth.

The key practices of accounts receivable management that a firm should try to implement are: Accounts Receivable Analysis Practice, Accounts Receivable Extension Practice, Accounts Receivable Collection Practice, Accounts Receivable Risk Assessment Practice and Accounts Receivable Financing Practice (Njeru et al., 2016).

a) Accounts Receivable Analysis Practice seeks to determine who will receive credit and under what conditions. Sources of such information include; banks, companies, associated competitors, suppliers and individuals applicants. Kakuru (2001) argues that collection of such information is not free but this cost is worthwhile.

b) Accounts Receivable Collection Practice involves all processes and strategies an organization employs to ensure that what has been extended as credit sales is fully collected and on time. The success of companies depends on their ability to collect and prevent default on their accounts, average days in collections gives insight into how efficiently companies are running. A Chinese saying that goes “Cash is King” is so true, it is crucial that collection of payment is in a manner which creates the optimum cash inflow while at the same time ensuring continuity (Kalundaet *al.*, 2012). Nduta (2013) shows that customers are slow payers while some are non-payers and as such the collection effort should be enhanced to accelerate collections from slow payers and reduce bad debt losses (Kariuki, 2010).

c) Accounts Receivable Extension Practice is another variable that needs attention. It is useful to think of the decision to extend credit in terms of carrying costs and opportunity costs. Carrying costs are the costs associated with granting credit and making investment in accounts receivable. It includes the delay in receiving cash, the losses from bad debts and the costs of managing accounts receivable (Omondi,2014).

d) Accounts Receivable Risk Assessment Practice involves identifying potential customers who are likely to be a problem, monitoring and control of accounts receivable in order to maintain optimal cash flow (Gakure, Ngugi & Ndwiga, 2012). Accounts Receivable Risk assessment management can be perceived as a hedging strategy by the firm against bad debts. It can provide certainty of cash flows, which helps with budgeting, encourages management to undertake investment, reduces the possibility of financial collapse (Ali, 2017).A good firm policy on accounts receivable risk assessment and management should be formulated and applied all the time and not only when circumstances dictates, otherwise bad clients would be approved while good ones are turned away without notice. Njagi (2016) analyzed effect of the risk management practices on the performance of hotels in Mombasa. It was observed that majority of hotels did not have a risk management policy which apparently affected their performance. The study concludes that risk management practices have a relationship with performance of hotels. The study further recommends that all hotels should have a risk management policy.

e) An Account Receivable Financing Practice is the act of exchanging Accounts Receivables with money. It is financing which distinctly relies on AR, either as

collateral or as eligibility requirement (Mubashir, 2012) .Receivables finance unlocks the cash that is owed to the small company by selling the invoice that is invoice discounting or through factoring. Cunat (2007) argues that fast growing firms may finance themselves with trade credit when other types of finance are not sufficiently available. Factoring is a financial service where a firm sells its accounts receivables (in the form of invoices) to a factor at a discount in exchange for immediate cash and a range of services including risk management, credit protection, accounts receivable bookkeeping, collection services, and financing (Klapper, 2006; Vasilescu, 2010;Tomusange, 2015)

Financial Literacy is the ability to have better judgments and to take appropriate actions for the management of cash flow (Njoroge, 2013). Financial literacy includes the ability to recognize sound financial choices. For example, whether to sell goods or credit, how much cash discount to give. It is a cornerstone that affects financial decision making. Financial knowledge and skills matters in any business or non-business activities as each and every decision have financial implications (Njoroge, 2013). Lack of basic financial concepts can be linked failure of firms. Sabri (2015) established that financial literacy can lead to better financial management practices. Firms employing staff with financial knowledge and skill are more likely to make decisions that may have positive implications on the liquidity position, account receivable management practices will ensure timely, regular and healthy cash inflow by selecting the right customer, ensuring strict recovery, eliminating poor customers and implementing formal credit policy (Sabri, 2015). Financial knowledge is crucial, a person who has sufficient knowledge is less likely to make expensive mistakes, since every decision undertaken would be guided by principles and policies well stipulated. SMEs lack sufficient funds to attract trained financial managers and analysts most often they employee accountants who only look at the conventional accounting function of recording transactions in the books of accounts. The SMEs manager or accountants should be responsible for providing leadership in all aspects of financial decision making like working capital management, capital budgeting decisions, financing decisions and dividend decisions. It has been noted that the

failure to effectively discharge these broad financial management functions have contributed largely to global financial crisis faced by SMEs (Osisioma, 2010).

#### **1.1.5 Relationship between Accounts Receivables Management Practices and Growth of SMEs**

Several studies have analyzed the effect of Accounts receivable management on performance of firms. For instance, Teruel and Solano (2014) studied a sample of non-financial companies in the UK and established that there existed a relationship between working capital management and corporate performance; the study amplified the fact that there is an existence of an optimal level of investment in working capital which maximizes a firm's value. However accounts receivable was just one of the components of working capital. This study looked at Accounts Receivable management practices as a standalone process. Angahar and Alematu (2014) examined the impact of WCM on profitability of cement companies quoted on the Nigerian Stock Exchange (NSE), one of the independent variable was accounts receivable. The findings showed that Accounts receivable measured by number of days Accounts Receivable outstanding did not impact on the profitability. Sharma and Kumar (2011) undertook a study on 263 non-financial BSE 500 firms listed on the Bombay Stock (BSE) from 2000 to 2008. The study concluded that there is a significant positive relationship between accounts receivable turnover and profitability. When customers pay the amounts they owe promptly then profits increase as these amounts are ploughed back

The study carried out by Lazaridis and Tryfonidis (2006) looked at the association between accounts receivables management and profitability (measured by gross operating profits) for 131 listed companies in the Athens Securities Exchange for the period between the years 2001-2004. The results showed there was a statistically significant relationship between the efficiency of accounts receivable management and profitability and firm value. Gakure *et al.* (2012) studied the association between working capital management and financial performance. His study sample included a sample of 15 companies listed in the NSE. He studied them for the five year period 2006 to 2010. He used multiple regression analysis and the Pearson correlation

analysis between the independent and dependent variables. He concluded that there was a strong negative correlation between ACP and profitability. On the other hand there was a positive association between CCC and profitability. In this study only the ACP was found to be of statistically significant influence. From the above studies most of the studies have focused on WCM and its effect on profitability where most of the findings are contradictory. I aim to study accounts receivables and their specific effects on accounts receivable management practices. Mwangi (2013) in his study of receivable management practices on CDF funded projects in Kenya concluded that the efficiency levels on receivable management practices were average thus indicating that CDF funded projects embraced and implemented efficient receivable management practices in project operations hence the survival of CDF funded projects was eminent.

Karugu and Ntoiti (2015) looked at corporate firms and those listed on the stock exchange markets, the findings indicated that credit risk management measured by credit appraisal practices, credit monitoring practices had a significant influence on profitability of firms. However the study did not address the effect of credit risk management practices on growth in SMEs. And it is for these reasons that this study wishes to establish the effect of Accounts Receivable risk management practices on growth on SMEs.

## **1.2Statement of Problem**

Although scholars are in agreement about the important role played by SMEs in a Country's Economic growth, there is still a fundamental lack of knowledge as to why some of them manage to grow and transition to large firms, while others remain stagnant or fail altogether. The challenges that most SMEs face is striking a balance between liquidity and profitability. This challenge is enormous since SMEs have to wade through stiff competition by attracting and maintaining customers through credit sales and at the same time use aggressive methods of collecting accounts receivables to maintain optimal levels of working capital. Increasing credit sales to improve profitability may end up extending credit to risky customers who will default, such customers will be asked to pay cash as the goods are delivered to them. Inability to



manage accounts receivables, made many SMEs in Kenya to suffer financial distress resulting to their eventual collapse.

SME segment is a very important vehicle for economic development, however, the failure of an SME never attracts the media attention that is usually associated with the collapse of bigger firms such as Enron in the USA, Kicomi and Pan Paper sugar millers in Kenya. The consequences of the failure of smaller firms are certainly a serious matter affecting several stakeholders that require attention, employees want to be assured of job security, government benefit from a constant flow of funds from SMEs in form of taxes, Communities need steady flow of goods and services. For these firms to survive, be self-sustaining and able to create the desirable impact, they have to be liquid. They need to make important financial decisions, among them being the liquidity decision and investment decisions.

Theoretical and empirical studies on effect of firms' accounts receivable management practices on growth are rare. Efficient management of the AR management process is still misconstrued as part of accounting and therefore as a cost center (Salek, 2005). A number of studies have been done on the influence of WCM on profitability of firms in varied countries around the world, most of these studies did focus on non-financial firms across industries and others looked at accounts receivable as proxy. A few of the studies are: Deloof (2003); Padachi (2006); Falope and Ajilore (2009); Gill, Biger and Mathur (2010), Ogundipe, Idowu and Ogundipe (2012); Njeru et al. (2016).

After reviewing various literatures, it was concluded that they mainly dwelt on the methods and tools for effective management of the receivables in all its dimensions. Fewer researches were found in area of accounts receivable management and their influence on financial management decision making and firms' performance. However, little is still known on how SMEs really manage their receivables to enhance growth, what system they have put in place, practices they used in management and collecting of receivables, and methods used to secure the accounts receivables. Studies on whether the manager's knowledge and skills determine how they apply the practices is yet to be established.

Literature reviewed therefore showed need for efficient management of account receivable through proper practices, which provides sufficient cash from operations that guarantee short term survival and growth of business. Small firm needs to manage their working capital in an efficient way as it significantly determines whether a business succeeds or fails. It was evident no research had been conducted on the effects of ARM practices on the growth of SMEs in Kakamega County. This study fills this gap.

### **1.3 Objectives of the study**

#### **1.3.1 General Objective**

The general objective of this study was to determine the relationship between receivable management practices and growth of Small and Medium Enterprises (SMEs) with a special focus on SMEs in Kakamega County).

#### **1.3.2 Specific Objectives**

The specific objectives were:

1. To assess the effect of Accounts receivable analysis practices on growth of SME in Kakamega County, Kenya
2. To evaluate the effect of Accounts receivable Extension practices growth of SME in Kakamega County, Kenya
3. To establish the influence of Accounts receivable collection practices on growth of SME in Kakamega County, Kenya
4. To determine the effect of Accounts receivable risk assessment practices on growth of SME in Kakamega County, Kenya
5. To evaluate the effect of financing practices Accounts receivable on growth of SME in Kakamega County, Kenya
6. To assess the moderating effect of financial literacy on the relationship between Accounts receivable management practices and growth of SME in Kakamega County, Kenya

#### **1.4. Research Questions**

The study was guided by the following research questions, which were answered through the research instruments:

1. What is the effect of Accounts receivable analysis practice on growth of SME in Kakamega County, Kenya?
2. Does the extension of Accounts receivable practice influence growth of SME in Kakamega County, Kenya?
3. What is the effect of Accounts receivable collection practice on growth of SME in Kakamega County, Kenya?
4. How does the Accounts receivable risk assessment practice influence growth of SMEs in Kakamega County, Kenya?
5. How does financing of accounts receivables practice influences growth of SME in Kakamega County, Kenya?
6. What is the moderating effect of the level of financial literacy on the relationship between RM practices and growth of SMEs in Kakamega County, Kenya?

#### **1.5 Research Hypotheses**

The null hypotheses (H<sub>0</sub>) tested in this study were the following:

1. **H<sub>01</sub>**: There is no significant relationship between Accounts receivable analysis practices and growth of SME in Kakamega County, Kenya
2. **H<sub>02</sub>**: There is no significant relationship between Accounts receivable Extension practices and growth of SME in Kakamega County, Kenya
3. **H<sub>03</sub>**: There is no significant relationship between Accounts receivable collection practices and growth of SME in Kakamega County, Kenya
4. **H<sub>04</sub>**: There is no significant relationship between Accounts receivable risk assessment practices and growth of SME in Kakamega County, Kenya
5. **H<sub>05</sub>**: There is no significant relationship between Accounts receivable financing practices and growth of SME in Kakamega County, Kenya

6. **H<sub>06</sub>**: Financial Literacy does not significantly influence the relationship between Accounts Receivables Management Practices and growth of SME in Kakamega County, Kenya.

## **1.6 Justification of the Study**

This study is very important to SMEs, policy makers and scholars. The following are groups that are likely to benefit from this study in a great way.

### **1.6.1 Investors**

It is extremely important that when goods are sold on credit, a good system should be put in place to manage accounts receivable (Waweru, 2013). Needless to say that, without finances which are often times locked up in the accounts receivable, small and medium enterprises cannot grow to competitively survive in the global markets or network with large firms (Idowu, 2010). The focus of this study was on receivable management practices of the Small to Medium sized firms operating various diverse industrial groups which suffer from Cash flow problems as a result of poor accounts management practices (Aaron & Namoi, 2004). It is therefore expected that the results highlighted in this study is of help to SMEs who hope to wisely mitigate losses by intervening in improving and controlling the levels of accounts receivables by adopting the best Accounts Receivable Management practices. In essence these investors in the growth enterprise market segment will gain from the imminent knowledge from this study.

### **1.6.2 Policy Makers**

This study will help the National and County governments, SME regulators and policy makers in formulating and ensuring the effective implementation of operational guidelines in as far as receivable management is concerned. A growth enterprise sector that is vibrant and self-sustaining contributes enormously to the national growth. This is will materialize the Government's goal of realizing the vision 2030.

### **1.6.3 Research Institutions**

This study will be a source of knowledge on the subject of ARM practices and growth of SMEs and will provide more gaps to be explored in this area in Kenya. There are several factors that affect growth of SMEs and an insight in these factors from varied perspectives is important.

### **1.7 Scope of the Study**

The study examined relationship between Accounts Receivables Management Practices and Growth of SMEs in Kenya. The SMEs studied had been in existence for the last three years and were registered and operated in Kakamega County. The study was inclusive of both manufacturing and service sector SMEs which were the majority in the County. This Central Business Area had the largest number of SMEs and a potential for growth, hence it provided sufficient data for the study. It is also the location that hosts the Headquarter of the entire Kakamega County and can hence be generalized to the entire Country. Both primary was used. The study variables were, growth as a dependent variable and ARM practices comprising of credit analysis, credit extension, credit collection, credit risk assessment, Accounts Receivable financing, as independent variables.

### **1.8 Limitations and Delimitations**

This study was delimited to study the relationship of Accounts receivable management practices and growth SMEs located in Kakamega County whose SME population was considered large enough and sufficient to provide generalization to the entire Country and the sample size was delimited to 359 firms located and operating in Kakamega County. Secondly, the study was delimited to period of three years that is, from 2013–2015, this period was considered sufficient for SMEs growth. Majority were reluctant in providing their actual books and financial data for review. The accuracy of the data was purely dependent on the data of sample units. The study was thus delimited to primary data.

## **CHAPTER TWO**

### **LITERATURE REVIEW**

#### **2.1 Introduction**

The literature review, as presented in this chapter, helped to identify and highlight relevant findings that served as a foundation on which the conceptual model was built. The research study was based on positivist foundational philosophy. This chapter critically reviewed the theories which explored the theoretical foundation that provided rational arguments into new paradigms. The theories were three, the Portfolio theory, the firm growth theory and the pecking order theory.

#### **2.2 Theoretical Framework**

There are many reasons for offering credit including increasing or facilitating sales, meeting terms offered by competitors, attracting new customers or providing general convenience (Megginson & Scott, 2008). Accounts receivable acts as attraction for potential customers and a as a retention strategy for the existing thus weaning them off from the competitors (Megginson *et al.*, 2008). Accounts receivables are assets representing amounts owed to the firm as a result of the sale of goods and services on credit in the ordinary course of business. The main objective of accounts receivables management is to maximize shareholders wealth. Receivables constitute a huge investment in firm's asset, which are, measured in terms of their Net Present Value (NPV), just like capital budgeting projects, (Emery *et al.*, 2004). Selling on credit is one of the firm's approaches in enhancing sales and it has turned out to be an enticement for customers in retaining the business relationship with the firm and in time increase the firm's sales volume and eventually optimizing the farm's profit (Barad, 2010).

### **2.2.1 Theories on Receivables Management Practices and Growth**

A theory represents the coherent set of hypothetical, conceptual and pragmatic principles forming, the general frame for reference for the field of enquiry (Wire, 2015). There are several theories that have been advanced for receivable management and growth of SMEs. These theories explain the practices of receivable management and the growth component, which apply to this study/

#### **a) Portfolio Theory**

Portfolio theory is concerned with risk and return. It is about maximizing the benefits of investments considering risk and return. In the area of accounts receivable management, portfolio theory has influenced areas regarding accounts receivable management practices which are: the analysis and risk assessment of accounts receivable investments. Both areas use Markowitz's studies as reference to evaluate the trade-off between risk and return on investments in accounts receivables. The study looks at accounts receivable as an investment that can be managed as a - portfolio, combining risk and return to maximize the benefits of investing in accounts receivable, these theory helps finance analyze which kind of customers to offer credit and which wants to remove, consequently the theory aid in combining various customers with different levels of risk and return to maximize return.

A portfolio is a set of assets, for example accounts receivable (Jajuga, 2002). Michalski (2008) suggests that a portfolio strategy is the act of categorizing debtors according to their behavior. Portfolio theory by Juja (1994) can be used in making decisions about selecting which customers should be given trade credit. Credit risk assessment is performed through the development of models usually based on a portfolio approach, in order to distinguish potential defaulters from non-defaulters. Generally, portfolio model refers to the assignment of a finite set of objects into predefined classes (Altman, Avery, Eisenbeis & Stinkey1981; Doumpou & Zopounidis, 2002).

Some customers, who previously were rejected because of too great an operational risk, would be accepted back provided they show a possibility of a positive outcome

that increases creation of increased firm value (Michalski, 2008). Extension of trade credit is possible only if the firm categorizes customers from various sectors, branches, regions, status and classes, since various categories of customers may have different levels of default risk. The only way a firm reduces this risk and enhances its success is by performing a portfolio analysis with the result of a varied portfolio of customers with a spectrum of managed levels of operating risk (Michalski, 2008). The portfolio approach to accounts receivable management can be used by utilizing the rate of profit (rate of advantage from assets) as one of the basic criteria that the firm giving the trade credit should encourage to extend credit. Customers who take too long to pay may increase the cost which increase risk, however such customers may be willing and ready to pay more as compensation for the risk (risk premium).

The Portfolio theory predicts that uncertainty in the economic environment affects the investment decisions one is likely to make. The theory suggests that to minimize losses and risk and increase returns then it is important to choose and combine wisely the options/assets that provide less risk and give higher expected return. So factors such as Accounts receivable risk assessment practice and Accounts receivable analysis are more likely to influence the SMEs growth. (Markowitz, 1952)

#### **b) The Theory of the Growth of the Firm**

The firm has to grow because its owners or the entrepreneur always strives to continuously make profits and maintain a better liquidity position to enable him/her meet the daily financial obligations and this is the driving force of all expansions of the firm.(Penrose,1959). Penrose (1959) argues that, when a firm wants to grow, it grows by expanding its stock of knowledge. She argues that automatic increase in knowledge and incentive to search for new knowledge are built into the very nature of the firm. Many ideas of Penrose (1959) are seminal and create a path for researchers' further research into the growth of firms, which has yet to be completed (Martin & Wiklund, 2010).

Greiner (1998) proposed a growth model that explained the growth in business firms as a predetermined series of evolution and revolution. In order to grow a firm is



supposed to pass through a series of identifiable phases or stages of development and crisis. These stages are; growth through creativity, growth through direction, growth through delegation, growth through collaboration and growth through coordination. Howard (2006) explained that firms go through seven stages of growth. The study emphasized that the first three stages are of significant importance and influence on SMEs. The first stage is the infancy stage, when an idea is conceived and a small business just begins with search for markets for products are developed. The second stage is expansion; here the firm struggles to increase its share in the market by increasing its sales. Stage three is professionalization and the desire to formalize the operations of the organization; this stage is closely linked to expansion.

This model suggests how organizations grow, however the processes and means by which firms achieve growth varied. Shimke (2011) suggests that growth and the increase in resource acquisition capabilities provide a positive feedback loop, which continues until the organization matures. A firm will enjoy good profits thus giving positive feedback until limiting factors (e.g an increase in competition, poor cash flow or the depletion of resources within the firm) take effect (Ansoff & McDonald, 2003) Namusonge (2010) identified several strategies used by businesses during the growth process, and further recognized barriers and incidents which facilitate or hinder the growth of Small and Micro Enterprises during the growth process. In this study the means by which a firm may achieve growth is the adoption of good ARM practices.

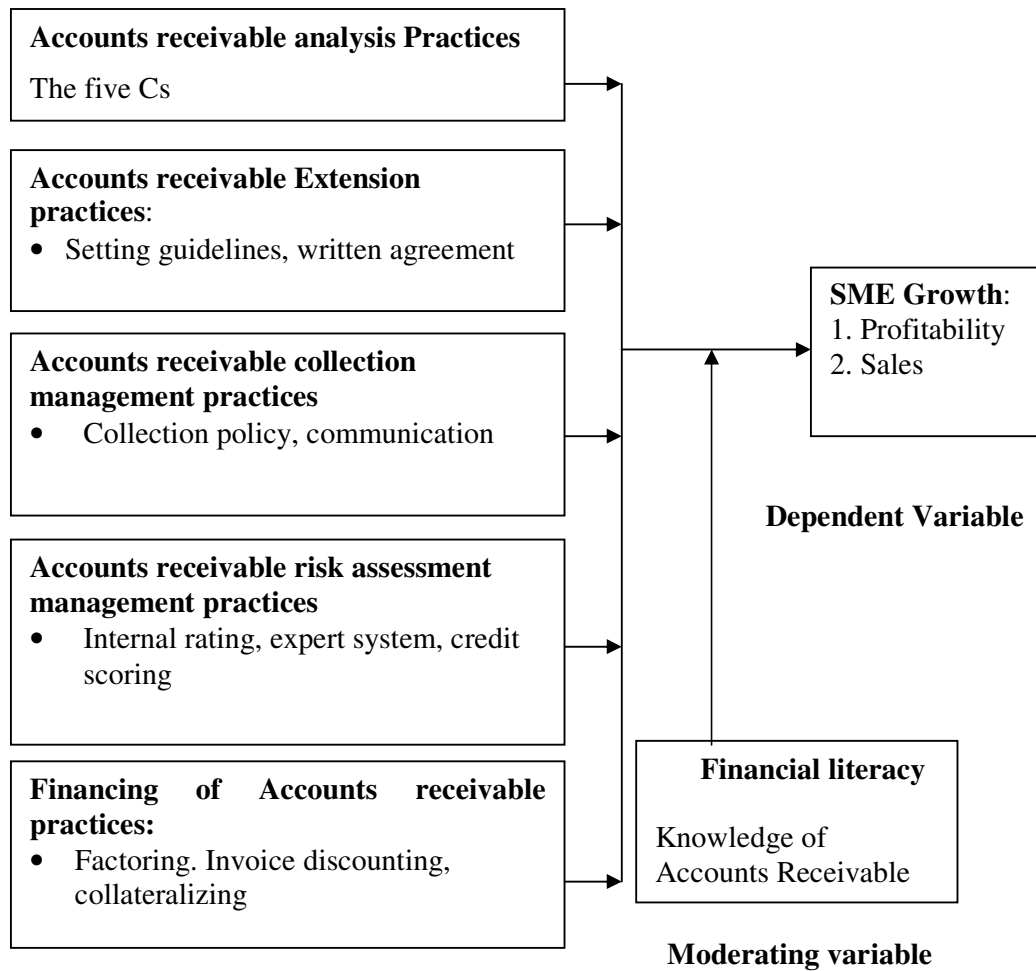
### **c) The Pecking order Theory**

Pecking Order theory addresses an immediate need for funding in a context of asymmetric information. It is based on the existence of a pecking order and provides a rational explanation for choice in corporate finance. Firms would rather focus on internal sources of financing before resorting to external investors. Amounts collected from accounts receivables are funds that would contribute towards profits as internal sources. Financing by internal funds should be encouraged as opposed financing by external funds, according to the following hierarchy: cash flow/debt/issue of shares' (Myers andMajluf1984).Internal financing is cheaper and easier to get than external since most financial institutions are reluctant to lend

money to SME for lack of collateral. The pecking order theory was relevant in this study in that Accounts receivable is an asset which may be effectively used to finance other operations of the firm. Unlocking the funds tied up in AR through factoring, Securitization or Accounts receivable discounting would reduce costs and increase wealth formation.

### **2.3 Conceptual Framework**

The conceptual framework summarizes behaviors and provides explanations and predictions for the majority of empirical observations (Cooper & Schindler, 2008; Mugenda, 2008). The receivable management practices are the independent factors influencing growth of SMEs and growth is the dependent variable as measured in terms of profitability and sales turnover obtained from the SMEs. This is shown in figure 2.1



**Independent Variable**

**Figure 2.1: Conceptual Framework**

## 2.4 Review of Variables

This section focuses on the review of empirical and relevant findings on the study variables which motivated this study. These variables are the components of Accounts receivable Management Practices.

#### **2.4.1 Accounts Receivable Management Practices**

Njeru *et al.* (2016) state that accounts receivable is an element of cash flow and has a direct effect on the growth of a business. Cash flow management refers to the management of movement of funds into and out of business and involves the management of accounts payable, accounts receivables, inventory as well as the cash flow planning (Joshi, 2007). Shapiro (2002) argues that firms grant trade credit to customers, both domestically and internationally because they expect investment in receivables to be profitable either by expanding sales volume or by retaining sales that otherwise would be lost to competitors.

However, Aaron and Namoi (2004) argue that firms suffer from cash flow problems as a result of granting credit and having poor accounts receivable management practices. Companies have traditionally viewed accounts receivable as a basic function. They are beginning to realize, however, that improving the process can lead to significant financial gain for the company. Fewer outstanding account balances mean fewer bad-debt write-offs and enhanced profitability (Salek, 2005). Peel and Wilson (1996), argue that a good receivable management practice is essential to the health and performance of both small and large firms. There are key practices involved: AR analysis, AR collection, AR extension, AR risk assessment, AR financing coupled with high level of financial literacy. These components of receivable management practices, if well adopted would lead to saving on the administration cost related to collection of receivables. Losses as a result of bad debts written off and provisions for bad debts are reflected on the financial statement. This would signal poor management which may lead to poor rating by potential investors. Indeed, mismanagement of accounts receivables is disastrous for a firm and more often leads to liquidity problems to many firms (Waweru, 2013). Waweru (2013) establish that cash-flow problems in manufacturing firms in Thika Municipality were attributed poor control and management of account receivables which adversely affected the day to day business operations .Some firms were even unable to pay the workers

Economic pressures and business practices increases Bankruptcy rates, among several firms which have increased the probability of incurring losses and the inability to pay promptly. Therefore it is a necessity for credit professionals to search for opportunities to implement proven best practices (Mutwiri, 2007). Even large profitable firms can collapse if they fail to manage accounts receivables effectively, (Prere, 2010; Njeru, Mbula & Memba, 2016). It is therefore in order to say that management of AR which is one of the largest tangible assets on a firm's balance sheet receives little or no attention, except when there is a serious problem.

#### **2.4.1.1 Accounts Receivable Analysis Practices**

Kibor and Ngahu (2015) defined credit analysis as the practice of analyzing credit data to establish the degree of risk in selling goods and services on credit. Credit analysts assess the client's financial history and his general ability to pay what he owes (Pandey, 2010). Credit analysis, as argued by Mutwiri (2007) is a basic aspect of credit decision-making and a very fundamental function of credit departments (Mutwiri, 2007). It is the study and analysis of credit information available in assessment of an entity's creditworthiness, this can be done in-house by the credit department or alternatively by engaging services of specialist credit analysts such as Moody's, Standard and Poor's, ratings or from Credit agencies behalf of the firm, (Myers & Brealey, 2003). Credit analysis seeks to determine who will receive credit and under what conditions.

For a continuing customer it is much easier because experience provides considerable information. For new customer credit analysis is obviously a tougher problem (Weaver & Weston, 2008). Portfolio theory may be used in making decisions about selecting which customers should be given trade credit. Weaver and Weston (2008), agree that sources of such information include; banks, companies, associated competitors, supplies and individuals applications and the information comes with a fee. Kakuru (2001) argues that to collect such information comes with a price, which is of course worthwhile when scrutinizing a customer: character, capacity, capital, collateral, condition are important components of Accounts Receivable Management Practices that should be critically evaluated (Njeru *et al.*, 2016).

Capacity is the ability to repay liabilities out of earned income; Capital, is the financial resource available to meet commitments should income not materialize. Condition, states how the current environment may affect the enterprise, whether through competition, economic, industry, or other factors. Character, is the quality of management: Who are they? What experience do they have? Are they well suited to lead the company? Collateral, Security provided, including the pledge of assets, guarantees from third parties, or other risk mitigation. This framework still dominates where information is obtained directly from the client in relationship selling on credit.

Njeru *et al.* (2016) argues that the six C's helps firms to decrease their default rate as they get to know their customers very well. Information on the C's can be obtained from several sources including the firm's prior experience with the customers, that is by tracking the trend of the customers paying history, analyzing the financial statements for previous years, enquiring from credit reporting agencies and even from the customers financial institutions (Kalunda, 2012).The worldwide competitive environment makes it quite necessary that firms grant credit that is if they have to keep abreast with others. Extending credit to customers is a decision based on the credit management and policy of a firm (Gitau, Nyangweno & Mwencha, 2014).

Extension of credit exists to facilitate sales (Njeru *et al.*, 2016). Al-Mwala (2012) suggests that sales are pointless without due payment and therefore the sales and accounts receivable functions must work together to attain the objective of sales maximization within the shortest period of time. Gitau, Nyangweno and Mwencha (2014), asserts that the purpose of credit control is to ensure that trade debts are recovered early enough before they become uncollectible and a loss to the business. Extension of Credit as stated by Gill *et al.* (2010) should only be on the basis of customer creditworthiness in order to minimize the level of default and bad debts. Weston and Copeland (205) state there are six C's of credit which credit managers should consider when extending credit: character, capacity capital, collateral, condition and contribution. They further assert that the six C's helps firms to decrease their default rate as they get to know their customers. Information on the C's can be obtained several sources including the firm's prior experience with the customers,

financial statements for previous years, credit reporting agencies and even the customers financial institutions (Kalunda, 2012).

There is need, therefore for setting timelines and credit limits as situations dictates, this exercise will depend on previous experiences that the firm has had with its existing customers and the information collected from agencies and financial institutions especially for the new customers. In particular, credit applications forms, financial statements and participation in industry credit groups can help a firm develop the information necessary to making a reasonable decision about extending credit to both new and existing customers (Richard, 2008). Sound credit extension policy with optimal credit standards and credit terms will result to higher sales that will lead to improved profitability for the firm and ultimately enhanced growth. Thorough vetting of credit applications before credit is granted will ensure that a firm only extends credit to credit worthy customers Gitau (2014), This will in turn reduce the firms' exposure to risks of delayed payments and a firm's investment in accounts receivable depends on volume of credit sales and collection period.

Giving out credit most often leads to bad debts. Credit sale has three characteristics, which are; it involves an element of risk that should be carefully analyzed; it is also based on economic value. The economic value in goods or services which passes immediately at the time of sale, this value is what the seller expects on equivalent value to be received later on, and lastly, it implies futurity (Njeru *et al.*, 2016). The buyer is expected to make cash payment for goods or services received by him at a future date. (Pandey, 2004) explains that reasons for Granting Credit may include but not limited to: Competition, company's bargaining power, the higher the degree of competition, the more the credit granted by a firm. Company's bargaining power means that the ability for firm to negotiate for better terms, if a company has a higher bargaining power vis-a-vis its buyers, it may grant no or less credit, thirdly, as a marketing tool: Credit is used as a marketing tool, particularly when a new product is launched or which a company wants to push its weak product.

However if the amounts granted are not collected on time the firms suffer losses. Njeru *et al.* (2016) states those longer credit periods are likely to stimulate sales while

at the same time a firm postpones the use of its funds for longer length of time and increases the potential for bad debts and losses. Gitau (2014) states that it is important to set credit terms and payment arrangement. Needless to note that a firm can shorten its credit period if customers default too frequently and bad debts building up.

#### **2.4.1.2 Accounts Receivable Extension Practices**

The global and competitive environment makes it inevitable for firms to grant credit if they have to keep abreast with others. Extending credit to customers is a decision based on the credit management and policy of a firm. Granting credit exists to facilitate sales (Njeru *et al.*, 2016). Al-Mwala (2012) suggests that sales are pointless without due payment and therefore the sales and accounts receivable functions must work together to attain the objective of sales maximization within the shortest period of time. Gitau, Nyangweno and Mwencha (2014), asserts that the purpose of credit control is to ensure that trade debts are recovered early enough before they become uncollectible and a loss to the business. There is need thus for setting timelines and credit limits as situations dictates, this exercise will depend on previous experiences that the firm has had with its existing customers and the information collected from agencies and financial institutions especially for the new customers.

Credit applications forms, financial statements and participation in industry credit groups can help a firm develop the information necessary to making a reasonable decision about extending credit to both new and existing customers (Richard, 2008). Sound credit extension policy with optimal credit standards and credit terms will result to higher sales that will lead to improved profitability for the firm and ultimately enhanced growth. Thorough vetting of credit applications before credit is granted will ensure that a firm only extends credit to credit worthy customers Moti *et al.* (2012). This will in turn reduce the firms' exposure to risks of delayed payments and a firm's investment in accounts receivable depends on volume of credit sales period. Granting of credit most often leads to bad debts. Gitau (2014) posits that a credit sale has three characteristics. It involves an element of risk that should be carefully analyzed; it is also based on economic value. To the buyer, the economic value in goods or services passes immediately at the time of sale, which the seller

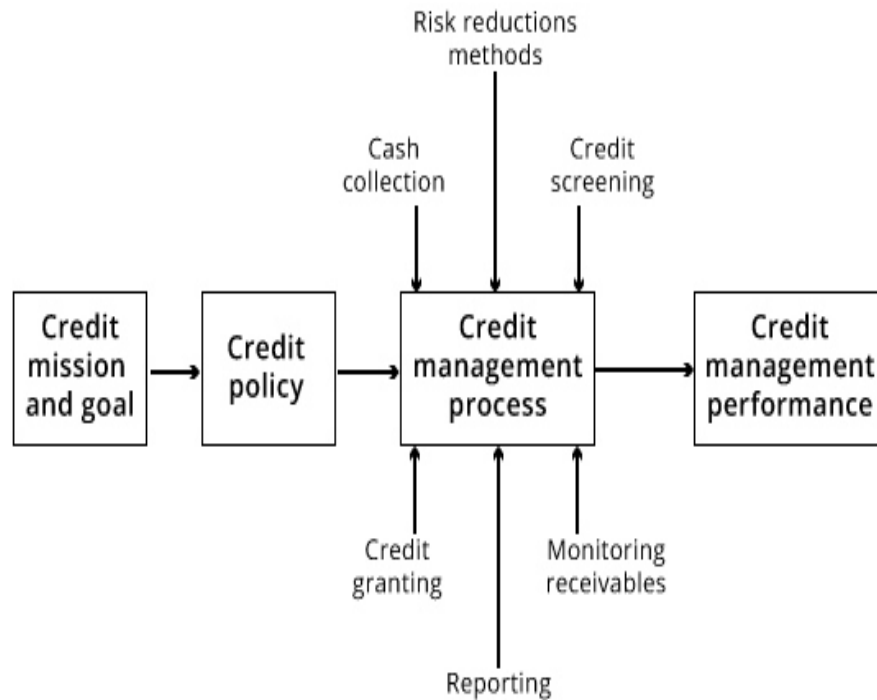


expects on equivalent value to be received later on, and lastly, it implies futurity (Njeru *et al.*, 2016). The buyer is expected to make cash payment for goods or services received by him in a future period. Reasons for Granting Credit may include: Competition, In the business arena the higher the degree of competition, the more the credit granted by a firm.

Secondly, Company's bargaining power if a company has a higher bargaining power vis-a-vis its buyers, it may grant no or less credit, thirdly, Marketing tool: Credit is used as a marketing tool, particularly when a new product is launched or which a company wants to push its weak product. However if the amounts granted are not collected on time the firms suffer losses. Longer credit periods are likely to stimulate sales while at the same time a firm forgoes the use of its funds for longer length of time and increases the potential for bad debts and losses (Njeru, 2016). Gitau (2014) state that it is important to set credit terms and payment arrangement. Moti *et al.* (2012) study on Effectiveness of Credit Management System on Loan Performance: Empirical Evidence from Micro Finance Sector in Kenya found out that Credit terms formulated by the microfinance institutions do affect loan performance; the involvement of credit officers and customers in formulating credit terms affects loan performance.

#### **2.4.1.3 Accounts Receivable Collection Practices**

Basically the collection process is the art of knowing the customer, ideally understanding him/her so that the best approach is used to get monies owed paid without straining the customer-seller relationship. Accounts Receivable collection practices are the procedures and tools used by a company to collect overdue or delinquent accounts receivables (Megginson & Scott, 2008). There are various policies that an organization should put in place to ensure that accounts receivables are managed effectively; one of these policies is a collection policy which is needed because all customers do not pay the firm's bills in time (Nduta, 2011). Some customers are slow payers while some are non-payers. The collection effort should, therefore aim at accelerating collections from slow payers and reducing bad debt losses (Kariuki, 2010).



**Figure 2.2: Credit management Process.** Source: Pike and Neale (1999).

Arnold (2003) agrees with the above idea that good administration of accounts receivable can only be achieved through a clear, concise and well communicated collection policy. He further suggests three principles available to maintaining a good collection policy. The process starts with the customer placing an order and ends at the point where cash is collected. Pike and Neale (1998) stated that businesses are very keen on collecting revenues, however not all organizations take a proactive approach to ensure receivables are collected on a timely basis. Lack of reporting makes it difficult for SMEs to determine which amounts are collectible and which may be in danger of default. When collection policies are not followed to the letter then issues of uncollectible accounts receivables would arise (Maria, 2014).

Dedication of debt collection resources ensures better and timely collection and few instances of bad debts (Njeru *et al.*, 2016). When sales are on credit, a monitoring system is important to avoid the potential build up to excessive levels of accounts receivable which would erode set profits (Maria, 2014). Maria (2014) asserts that dedication of debt collection is related to human factors. She concluded that dedicated

collection resources ensured better collection and fewer instances of bad debts. Padachi (2006) state that a collection resource is a control process which ensures that trade debts are recovered early enough before they become un-collectable and therefore a loss to an organization. Indeed such a process would signal to management that immediate action is required. Owonde (2013) provide that customer relationship officers in most firms act as the link between the firm and customers. They maintain close links which help in monitoring business activities of the customers and raising the red flag for management to take action before a debt can go bad and inhibit profits.

A credit collection policy manual are the procedures used to collect past due accounts including the toughness or laxity used in the process. At one extreme, the firm might write a series of polite letters. Company must determine what its collection policy will be and how it will be implemented (Megginson.et.al, 2008).Penalizing delinquent accounts can be an effective way to ensure timely payments. This can be done by levying interest on overdue balances (Richard, 2008).A credit collection policy that facilitates low average collection period will ensure the firms' healthy cash flows and improved liquidity position (Richard, 2008). Improved liquidity will enable the firm to meet its financial obligations as and when they fall due and also be in a position to seize opportunities that may arise in the market. Kalunda *et al.* (2012) asserts that, the quicker the collection period is, the sooner capital can be freed allowing for reinvestments back into the company. Conversely, the longer the collection period of a particular credit consumer, the higher probability that those receivables will not be collected. Collection policy involves all processes and strategies an organization employs to ensure that what has been extended as credit sales is fully collected and on time.

According to Pike and Neale (1999), a good credit collection policy is one in which procedures are clearly defined, clearly communicated to customers and customers know their rules well. Gitau *et al.* (2014) assert that a creditor should use litigation as a last resort to collect a debt that is bad and when there is a major breakdown in the repayment agreement resulting in undue delays and legal action is required to effect collection. Atrill (2006) asserts that small and medium enterprises often lack the

resources to enable them collect amounts owed by trade debtors (accounts receivable) effectively. He argued that it is not unusual for SMEs to operate without credit control department. SME also lack proper debt collection procedures, such as prompt invoicing and sending out regular statements. There are various policies that an organization should put in place to ensure that credit management is done effectively, one of these policies is a collection policy which is needed because all customers do not pay the firms bills in time (Nduta, 2013) some customers are slow payers while some are non-payers.

The collection effort should, therefore aim at accelerating collections from slow payers and reducing bad debt losses (Kariuki, 2010).Connolly (2013)noted that developing and maintaining receivable schedules and regular review of receivables including customer statements and implement policies to ensure timely and efficient collection of outstanding accounts are necessary SMEs experience volatility in cash flows which affect their liquidity and consequently their growth (Nzyoka, 2011) attributed this to poor financial management, especially the working capital management. Kehinde (2010) noted that most SME's do not care about their working capital position, and that most do not even have standard credit policy. He further emphasized that many do not care about their financial position, as they mainly focus on cash receipt and what their bank account position is which leads to sure collapse.

#### **2.4.1.4Accounts Receivable Risk Assessment Practices**

Risk is the possibility of suffering economic and financial losses or physical material damages, as a result of an inherent uncertainty associated with the action taken. Chapman and Cooper (1983). Credit risk is the oldest of all default risks. Credit risk management is a structured approach to managing uncertainties through risk assessment, developing strategies to manage it, and mitigation of risk using managerial resources (Gakure, Ngugi & Ndwiga 2012). The strategies include transferring to another party, avoiding the risk, reducing the negative effects of the risk, and accepting some or all of the consequences of a particular risk. Mwirigi (2006) stated that credit risk is the probability that counterparty will fail to meet its obligations in accordance to agreed terms. The objective of Accounts Risk

management is to maximize a firm's risk-adjusted rate of return by maintaining credit risk exposure within acceptable parameters required by shareholders. Accounts receivable risk assessment involves identification of problem customers, monitoring and control of accounts receivable in order to maintain optimal cash flow. Most widely used Accounts receivable risk management practices are, setting up risk management teams, credit scoring, expert systems by third party and internal rating. When dealing with difficult customers' accounts are put on hold and future sales are stopped until the account is settled (Kungu *et al.*, 2014).Fabozzi *et al.* (2002), argued that, Accounts receivable risk assessment involves consideration of these factors; default probability, credit exposure and recovery rate. Many organizations give a great deal more attention to retaining customers and snaring new accounts than they do tracking who is paying, who is lagging behind and who might default. However, as the current economic malaise drags on and bankruptcy rates climb, effective credit management becomes an increasingly critical factor in achieving success (Beranek, & Scherer, 1991).

When the debtor does not pay on due date, the seller is exposed to credit risk which may in turn lead to default and bad debts (Nyunja, 2011). Assessment of credit risk, involves trying to find a way of accepting and controlling all businesses including high risk opportunities. There are three basic approaches to credit risk measurement practices. They are: Expert Systems, Credit Rating, and Credit Scoring (Saunders, 1999); Oketch (1995) studied the demand and supply factors to micro small enterprises finance from Kenyan commercial banks to conclude that the credit size offered is determined by its risk assessment. Mwirigi (2006) carried out a study to determine the credit risk management techniques applied by microfinance institutions. He established that, despite having no stringent regulatory framework in relation to credit aspects for microfinance institutions in relative comparison to commercial banks, they all engage in credit management process. Mutwiri (2007) ascertained that both agree that credit management policies form a basic objective for credit risk appraisal.

Accounts Receivable Risk Management extends outside the organization through a process whereby credit control professionals carry out credit risk assessment for their

trade partners (Mutwiri, 2007). It ensures firms remain on track. This is achieved through sourcing organizations' credit history and credit data through for example credit referencing and other data sources like financial statements (Moti, Galo & Sindani, 2012). The Wikipedia describes credit referencing as a method whereby organizations obtain independent credit information from third party sources other than the customers themselves. This is mainly from credit reference agencies who are the custodian of credit information. In Kenya this is mainly done by the Credit Reference Bureau (CRB). Credit bureau collect and collate credit data for organizations which they have a relationship with, they then consolidate and aggregate this data to make it available on request to organizations for purposes of credit assessment and credit scoring (Mutwiri, 2007).

Credit ratings are scoring are available from credit reporting agencies. Internationally recognized credit rating agencies are Dun and Bradstreet (D&B) or Standard and Poor (S&P) (Mutwiri, 2007). This sector is not well developed in Kenya and as such, information is limited. Credit ratings give credit analysts an estimated net worth of a firm. Myers (2003) identifies factors which influence an organization's credit rating as, ability to pay debt (capacity), outstanding amount of credit at any time, savings patterns and spending patterns.

Credit score is a number that reflects how likely an organization is to repay its debts (Horne & Wachowicz, 1998). It is based on an organization's credit report which lists all its debts and their repayment history. The most efficient way to achieve a good score is keeping debts to minimal levels and ensuring their satisfaction to contractual obligations on debt servicing. According to Horne and Wachowicz (1998), a credit scoring system is a quantitative approach to decide whether to grant credit by assigning numerical scores to various firm's characteristics related to creditworthiness. Horne and Wachowicz stress that the credit decision judgment during credit scoring lies with the credit analyst's ability and capability to evaluate available credit information. As credit scores are designed to indicate the likelihood that a debtor will default, a low credit score raises a red flag for an organization to adjust its lending decisions in regard to potential credit risk exposures (Mutwiri, 2007). Rising interest rates and inflation presents a very big burden to organizations towards

their financial obligations irrespective of the industry. According to the CBK Monetary Policy Statement (June, 2006), in the 90s the Kenyan economy was characterized by high inflation and interest rates well above 20% and borrowing was considered a last resort. Credit management was therefore very critical for timely cash collections to meet organizations' obligations.

Internal rating means assessing debtors, through ensuring that difficult customers' accounts are put on hold and future sales stopped till the account is settled (Kungu, Wanjau, Waititu & Gekara, 2014). Internal rating can be done through portfolio strategy where customers are categorized on their behaviour and history of paying. Portfolio theory can be used to determine those risky debtors and ensure that they are communicated to timely or dropped completely. Frequently cited techniques for monitoring the overall quality of accounts receivables are namely: Average-collection period (Days Sales Outstanding), Aging of accounts receivables and payment pattern monitoring. These techniques are discussed below.

**a) Average Collection Period:** The Average Collection Period (ACP) also known as Days Sales Outstanding (DSO) represents the average number of days that credit sales are outstanding. According to Graham, Scott (2010), the Average collection period has two components; first the time from sales until the customer places the payment in the mail and secondly, the time to receive, process and collect payment once it has been mailed by the customer. If it may be assumed that the receipt, processing and collection time is constant, then the Average Collection Period tells the firm how many days (on average) it takes customers to pay their accounts (Graham et al, 2010). Mwangi (2013) on the other hand examined the association between working capital management and financial performance of private hospitals in Kenya. The study used average collection period, average payment period and cash conversion cycle as proxies of working capital management. Return on assets represented profitability

**b) Aging of Accounts Receivable:** This is a method used to monitor accounts receivable where an aging schedule classifies the firms 'receivables by the number of day's outstanding (age of the receivable). It provides useful information about the quality of a firms' accounts receivable.

#### **2.4.1.5 Accounts Receivable Financing Practices**

Access to finance is crucial to the survival and growth of any business enterprise (Ngugi & Bwisa, 2013). Small and Medium Enterprises (SMEs) need financing for two basic reasons: the first being financing the production cycle once it has stabilized (that is, working capital) and secondly financing capital expenditure (World Bank, 2014). Cunat (2007) defines Accounts Receivable financing as any type of financing which distinctly relies on Accounts Receivables, either as collateral or as an eligibility requirement. Receivables finance unlocks the cash that is owed to the small company by selling the invoice for example, invoice discounting or through factoring. Cunat (2007) argues that fast growing firms may finance themselves with trade credit when other types of finance are not sufficiently available. The financing options include: securitization of AR (both on and off balance sheet), factoring of receivables, AR collateralized debt, and general collateralized debt which contains an AR eligibility requirement.

Factoring is a financial service that enables a firm to sell its accounts receivable to a factoring company in exchange for cash. This is a very recent trend that is gaining prominence the world over. Most firms in developed and developing countries are embracing this as a financing tool (Klapper, 2005). Factoring, as a financial service involves purchasing of invoices or receivables. The trade debtors are notified that payments are to be made to the financing agency. In fact, this method minimizes risk to the sellers; the agency generally assumes the credit risks on the receivables. The seller's accounts receivable are considered as the underlying assets for purposes of factoring and are purchased by the factor at a discount. Once the accounts receivables are paid to the factor the remaining balance is paid to the seller, less interest and service fees. Klapper (2005) stated that factoring is a broad financial service that includes credit protection, accounts receivable bookkeeping, collection services and financing. This service is very relevant to small and medium enterprises which operate in financial systems which have weak commercial laws and enforcement. Klapper (2005) further emphasizes that factoring is quite appropriate for financing receivables from large or foreign firms when those accounts receivables are



obligations of buyers who are more financially stable and creditworthy than the firm itself. There is an assurance that the accounts receivables will be paid in due course.

Klapper (2005) suggests that factoring provides small and medium enterprises (SMEs) with working capital financing which is different from the traditional forms of commercial lending. However, unlike traditional forms of working capital financing, factoring involves the outright purchase of the accounts receivable by the factor, rather than using accounts receivables as collateral for a loan (Curat, 2007).

Invoice discounting can be defined as the selling of invoices those payments are not yet been paid. This method has freed SMEs from traditional, financing from banks, helping end the liquidity challenges that so often slow down small businesses' growth plans. The recent financial crunch that most firms experienced, has led to the reluctance of many banks unwillingness to extend credit to firms especially the SMEs. Firms are forced to look for alternative methods of raising finances to run their businesses (Tomusange, 2015). The second method other than factoring is invoice discounting. Invoice discounting is a facility which allows a firm to improve its cash flow by borrowing against invoices that have been raised. The firm is able to access the value of the invoice immediately without having to wait for the normal payment period. In fact, waiting to get paid on their invoices can be very disappointing.

Cash flow affect the business' ability to meet its daily financial obligations. This problem can be worse when the business has a number of orders that it cannot meet as a result of idle cash tied up in unpaid invoices. This is particularly important for both small and large firms who need to finance increasing amounts of debtors. If a company is also using its accounts receivable as collateral for a loan, the lending institution will generally exclude any past due accounts from those used as back up for the credit line (Waweru, 2013). Muschella (2003), in his study of Italian firms, concluded that alternative methods of financing in the business environment are increasing in both developing and developed countries.

#### **2.4.1.6 Financial Literacy**

A moderating variable is defined as a variable that affects the relationship between two other variables; it brings out the interaction effect (Kerry, 2015). It is normally denoted by letter M, and affects the strength of the relationship between a dependent and independent variable. In a correlation, a moderating variable influences the correlation of two variables. In a causal relationship, if x is the predictor variable and y is an outcome variable, then M which would be the moderating variable affects the casual relationship of x and y. Most of the moderating variables determine causal relationship using regression coefficient. The moderating variable, when found to be significant, can cause an amplifying or weakening effect between x and y (Kerry, 2015). In this study Financial Literacy was used as a moderating variable.

Majority of studies have proved that financial literacy has a positive effect on entrepreneurship success. However, there are also cases of illiterate persons running successful enterprises. In Kenya where vast majority of SMEs are in informal sector, many Jua Kali and farming entrepreneurs are financially illiterate and yet they run very successful SMEs. Njoroge, (2013) in his study concludes that there is positive relationship between entrepreneur's success and financial literacy. He noted SMEs that are more successful are run by entrepreneurs who are financial literate and understand key financial concepts that include, risk management, interest rates, time value for money and financial market. However, other scholars contend that lack of financial knowledge of effective receivable management combined with the uncertainty of the business environment leads to poor performance by SMEs (Abor & Biekpe, 2005).

It is important that a firm understands its business position as far as its cash flow is concerned, however this can be done quite effectively when a manager has a certain level of financial literacy. Nunoo et al. (2012) in a study to examine how financial literacy influences SMEs in Ghana found that financial literacy is crucial in stimulating the SME sectors. The stiff competition in the global market that most SMEs face means that the SMEs have to have formal control over their financial decisions than ever. This has placed greater demands on financial directors and

managers to be more financial literate in order to improve decision making. To this end, there has been a rising interest in the financial literacy from academic community, international organizations and governments recently (Olga, 2011). Nyabwanga (2011) studied the effects of working capital management practices on financial performance of small scale enterprises in Kisii, South district. In his study, he established that majority of business operators did not have business management knowledge and further suggested a study to unravel the impact of training on performance of business. Njoroge (2013) on the other hand concludes that there is positive relationship between entrepreneur's success and financial literacy.

Njoroge (2013) observed that SMEs that are more successful are run by entrepreneurs who are financial literate and understand key financial concepts that include, risk management, interest rates, time value for money and financial market. Financial literacy would make an entrepreneur more knowledgeable and better at making informed decisions as to the kind of accounts receivable management practices to adopt. Hartog et al. (2010) used the U.S. National Longitudinal Study of Youth to examine the effects of various personal characteristics among entrepreneurs and employees. They found that verbal abilities appear to be more important for employees, while mathematical, technical and social abilities are more important for entrepreneurs. Financial literacy can facilitate the decision making processes such as payment of bills on time, proper debt management which can improve the credit worthiness of potential borrowers to support firm performance (Adomako, 2014). Being financial literate is a plus to an entrepreneur. Financial literacy enable investors to evaluate and compare financial products, such as bank accounts, saving products, credit and loan options, payment instruments, investments, insurance coverage, so as to make optimal decisions (Miller et al., 2009).

#### **2.4.1.7 Growth**

The main dependent variable is growth. It is regarded as the second most important goal of a firm, the most important being firm survival (Bunyasi et al, 2014). Every firm goes to business to maximize wealth and to be self-sustaining; the SMEs are not an exception. In Kenya various studies have been carried out on growth of SME.

Namusonge (2010) identified several strategies used by businesses during the growth process, and further recognized barriers and incidents which facilitate or hinder the growth of Small and Micro Enterprises during the growth process. \indeed inability to have a suitable level of accounts receivable is a hindrance, leading to low liquidity Namusonge (2012) studied “Determinants of growth oriented SMEs in Nairobi”. He concluded that availability and type of finance are key determinants of the growth performance of SMEs, however these finances should not be tied up in accounts receivables.

In Kenya, various studies have been carried out on the growth of SMEs, illustrating the role SMEs play in the Economy and they are in agreement that Small and medium enterprises (SMEs) make important contributions to the economic and social development of any country (Ouma & Kilonzo, 2015). Most large firms were once small firms which transitioned into large and profitable ones. Kilonzo et al. (2015) argue that the term SMEs covers a wide range of perceptions and measures, varying from country to country and between the sources reporting SME statistics. Sandhar (2013) noted that profitability entails the capacity to make benefits from all the business operations of an organization, firm or company. It portrays the management’s efficiency in converting available resources to profits and is considered a measure of growth (Muya & Gathongo, 2016). Mwangombe (2013) studied factors that influence performance of various youth groups in Taita, and found that leadership, planning and control of funds affect performance. Wanjiru (2013) studied social-cultural factors, education and training skills and established that they affected growth positively.

Mwangi and Wanjau,(2013) found that, firms which rely on credit grow faster as they use the facility as a financing tool, yet these firms get credit from other firms, what happens to the firms that provide goods or services on credit? Do they also grow as fast? Spilling (2001) states that the growth status of a firm may be rather temporary as are the factors that that influence it. The commonly used measures of firm growth are: (employment growth, sales growth, profit, return on equity [ROE], return on assets [ROA]) and entrepreneurs’ perceived growth relative to their competitors in terms of increase in company value (Leona et al., 2010). O’Gorman, (2001) posits that SME

growth can be measured in terms of sales, number of employees, value added, and complexity of the product line, production technology or the number of locations. Bosma et al. (2000) proposed three measures of success of the entrepreneur, such as: profits of the entrepreneur, employment created by the entrepreneur, and the survival period of the firm. In this study, the Key measures of growth were: (Profitability and sales turnover).

#### **2.4.2 Relationship between Receivable Management Practices and Growth**

Njeru et al. (2016) states that accounts receivable as component of cash flow directly affects the growth of a business. Good cash flow levels can be likened to the oil that lubricates the growth engine of a firm and should be well managed. Cash flow management refers to the supervision of movement of funds into and out of business and involves the management of accounts payable, accounts receivables, inventory as well as the cash flow planning (Joshi, 2007). The interest in receivable management emanates from its effect on firms risk and return (Smith, 1980). Small Business (2006), illustrated that there were more than ten thousands of self-employed workers who went bankrupt. In 2010, 99.4% of all firms in Finland were SMEs, while more than 83% were micro enterprises (OECD, 2012). Bad debts can be a major problem to SMEs, especially in the current economic climate where margins may already be squeezed and the high inflation rates may add salt into injury. Firms that provide most or all products or services on credit to more or all of their customers are likely to experience bad debts situation on a large scale.

Having accounts receivables is both good and bad. It is good because it means that the firm would make sales and have customers. It is bad because it is cash that a firm will not have now, and there is always a possibility that firm would not collect leading to bankruptcy. When you offer credit terms to your customers, it is extremely important to have a system in place to manage your accounts receivable (Waweru, 2013). Ojeka (2012), in his study on Nigeria firms concluded that when a firms' credit policy is favorable, liquidity is at a desirable level. Firms which keep an eye on their credit policy, regularly reviewing it and reducing cash discount allowances do better in terms liquidity position and profitability (Ojeka, 2012).

Kalunda et al. (2012) studied the effect of credit risk management practices on pharmaceutical manufacturing companies in Kenya. Using semi structured questionnaire to gather data from finance managers or credit controller, found out that the most important factors considered in establishing a credit policy is the financial stability of the customer and existing credit policy. In a study carried out in Kenya titled “Factors affecting management of accounts receivable among Agro-manufacturing companies in Kenya”, the researchers concluded that although the management of accounts receivable fall under the umbrella of the finance department, it is a complicated field that needs special attention. It affects several departments that is the marketing and the finance departments (Onami, 2008).The inability of SMEs to collect the accounts receivables on good time may lead to further lack of finances to stimulate their growth and this explains why most SME fail within the first few years of their inception.

Mavutha (2010) argued that corporate profitability is achieved through optimal management of working capital. Owele and Makokeyo (2015) opinioned that the firm’s profitability depends on the working capital management approach adopted by such a firm. The researchers further stated that working capital is made up of current assets and current liabilities. In their study on working capital management approaches and financial performance of agricultural firms listed in Nairobi Securities Exchange, Owele and Makokeyo (2015) noted that firms with aggressive approaches were profitable. It noted that firms may register high profits in relation to large asset base but still generate low profitability. This is as a result of larger proportions of assets being idle ie accounts receivables being one of them and therefore affecting profitability (Owele & Makokeyo, 2015). Waithaka (2012) stressed on the importance of efficient management of working capital to improve profitability. He argues that efficient cash management, account receivables and inventory management had direct influence on sales, growth in total assets and increase firm profitability.

## **2.5 Research Gaps**

The main objectives of any firm is to grow and to be able to sustain itself, however this is not so for many SMEs in Kenya. Koech (2011) identified the factors hindering

growth of SMEs as capital access, cost, capital market, collateral requirements, information access, capital management and cost of registration. Njagi (2016) analyzed effect of the risk management practices on the performance of hotels in Mombasa. It was observed that majority of hotels did not have a risk management policy which apparently affected their performance. However, the study looked at only one component of accounts receivable management practices. Oware, Samanhyia and Ampong (2015), demonstrated that when a firm does not invest well in the collection of account receivable then the probability that a firm will stagnant as a result of very poor account receivables levels and debt accumulation would be high. The study concentrated a state firm offering utility service. This study looks at a cross section of all types of businesses.

Mwangi (2013) in his study of receivable management practices on CDF funded projects in Kenya concluded that the efficiency levels on receivable management practices were average thus indicating that CDF funded projects embraced and implemented efficient receivable management practices in project operations hence the survival of CDF funded projects was eminent. Murara and Mureithi (2009) in their study of receivable management challenges among SMEs in Kenya conclude that indeed most SMEs were suffering from bad debts.

Nganda, Wanyonyi and Kitili, (2014) conducted a study on the determinants of growth of SMEs in Kakamega Central sub-county and established that income taxes and collection of revenues slowed down growth of SMEs. Bunyasi, Bwisa and Namusonge( 2014) studied the effect of entrepreneur finance on growth of SMEs, suggesting that there is a positive influence on growth, however the study did not exhaust all other dimensions of growth factor such management of accounts receivable as a source of finance. Effective management of accounts receivable presents important opportunities for firms to achieve competitive edge and to grow.

Mairura, Namusonge and Karanja (2013) conducted a study on the role of financial intermediation on the growth of SMEs in Kenya. The study established that SMEs largely depend on financial intermediation for growth. Ngugi and Bwisa (2013) studied on factors influencing growth of group owned MSEs. The study variables

were technology, access to finance and market. Several studies have been advanced on the effects of accounts receivable management practices on the impairment of receivables (Mwangi, 2013; Lazaridis & Dimitros, 2009; Bowen, Murara & Mureithi, 2009). Bowen, Murara and Mureithi (2009) in their study of receivable management challenges among SMEs in Kenya conclude that indeed most SMEs were suffering from bad debts. Other studies have analyzed receivable management from the working capital stand point; mostly as a proxy of working capital management. Mathuva (2010); Bougheas et al. (2009), for example, talks about the reaction of accounts receivable to fluctuations in the cost of inventories, profitability, risk and liquidity.

Several of the authors have given recommendations on how to achieve optimal receivables management. None has looked at receivable management practices that may lead to wealth maximization, signified by growth in this study. Nyaga (2011).studied the relationship of Accounts Receivable management and performance of Learning institutions (TIVET),he posits that there is a positive relationship between collection policy and monitoring practices adopted and organization performance, he also asserts that these institutions use formal practices, however these are non-profit making organization, this study will want to compare this with the profit making firms. Nyabwanga (2012) looked at working capital management practices on financial performance of small scale enterprises in Kisii, Kenya, the study concentrated on credit guidelines and how they affect performance of firms, however good financial performance may not necessarily translate to growth. It is against this background that this research sought to fill the gap by establishing the effect of accounts receivable management practices on the growth of SMEs.

From the above literature review, it was evident no research had been conducted on the effects of Account receivable management practices on the growth of SMEs. . It was quite interesting to relate practices with growth. This study investigated the effects of ARM practices on the growth of SMEs in Kakamega County. Many studies have mainly dwelt on importance of financial literacy and its effects on household or personal financial behavior (Cherugong,2015).Financial literacy facilitates the decision making processes such as payment of bills on time, proper debt management



(Mutegi &Phelister, 2015). There has been little or no theoretical and empirical study on how financial literacy may influence the adoption of Accounts Receivable Management Practices on growth of SME in Kakamega County. This study sought to establish this effect.

Very few studies have looked at all the components of receivable management practices on SMEs and those that have been done either looked at determinants of receivable management or narrowed their study to just one sector or looked at working capital. However present literature relating to SMEs in Kenya has not related receivables management to the net profit and hence growth, while the focus in previous researches was on financial management broadly, this research narrows on receivable management practices.

## **2.6 Summary**

Growth is a very important pointer to the well-being and sustainability of a firm and ultimately the general economy as illustrated by the literature reviewed in this chapter. This study however identified several theories, the portfolio theory, the life cycle theory, and the organization growth theory. Growth is the dependent variable and accounts receivable management practices as the independent variable with the following practices reviewed; credit analysis, credit extension practices, credit collection practices; credit risk assessment practices and Accounts receivable management practices. Financial literacy was another independent variable reviewed. Having gone through various researches it can be seen that there was urgent need to undertake a study on receivable management practices and its relationship to growth of the firms.

The research problem depended upon two important aspects of receivables management. One was to determine the receivables management practices used by SMEs and how they affect the business profit and sale turnover, the other aspect was to analyze how financial literacy level of Accounts receivable management practices affects growth and sustainability of SMEs. Many studies have mainly dwelt on importance of financial literacy and its effects on household or personal financial

behavior with little or no theoretical and empirical study its effect on growth of SMEs in Kakamega County. Lastly, the study assessed the adequacy and effectiveness of these practices in reducing amount of account receivable on the balance sheet.

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1 Introduction**

The aim of this chapter was to describe the methods that were used to carry out the study. It covers study area, study population; sample size and data collection methods, data management, data analysis, quality and reliability of data. The research study was based on the foundational philosophy called positivist.

#### **3.2 Research Design**

Mixed research design study was undertaken in order to ascertain reliability of data collected which made it possible to describe the characteristics of the study's variables and answer the research questions in chapter one. Best and Khan (2009) posit that descriptive survey research is aimed at describing the characteristics of variables in a situation and is concerned with conditions or relationships that exist, opinion that are held, processes that are going on, effects that are evident or trends that are developing. Cooper and Schindler (2010) further recommend descriptive survey design for its ability to produce statistical information about aspects of education that interest policy makers and researchers. A sample survey method was used to collect data from SME operators in Kakamega County.

#### **3.3 Target Population**

Orodho (2003) posits that a population refers to an entire group of individuals, events or objects having a common observable characteristic. The Population of this study was 5401 SMEs in (Kakamega County, which had been in operation as at 22<sup>nd</sup> April 2015 as per the Kakamega County Revenue Department Register. The finance officers in the SMEs were interviewed. The SMEs included all with six to ninety employees or with annual turnover revenue below Kshs 50 million

### 3.4 Sampling and Sample Size

This study used the geographical location (ward) as the key unit for sampling to categorize firms into twelve strata. Firms in other Counties were not included in the study. Mugenda and Mugenda (2003) and Kothari (2004) define the term sampling frame as a list that contains the names of all the elements in a universe. Sampling frame comprised 5401 small and medium enterprise which operated in Kakamega Central County.

**Table 3.1: Sampling Frame and Sample Size**

<b>Ward</b>	<b>Population</b>	<b>Sample size(<math>X/5401 \times 359</math>)</b>
Amalemba,	223	15
Bukhulunya,	102	7
Central	4017	267
Mahiakalo	274	18
Matende	130	9
Milimani	154	10
Musaa	52	3
Shibirir	120	8
Shieywe	25	2
Shirere	10	1
Shichirai	284	19
<b>Total</b>	<b>5401</b>	<b>359</b>

**Source: Kakamega County Revenue Department (2015)**

Kombo and Tromp (2009) and Kothari (2004) also describe a sample as a collection of units chosen from the universe to represent it. The SMEs were first of all stratified according to the geographical location then samples were selected from each stratum using proportionate random sampling to ensure equal representation from every stratum. Therefore, the entire population under consideration in this study was 5401. This population was chosen as they were deemed to be in a position to provide reliable information for the study purposes. A sample of 359 SMEs was selected.

Krijcie and Morgan (1970) prescribes a model for a sample size determination of 359 subjects for a population of 5401. Purposive sampling for data collection was used to target financial officer from every SME dealing with accounts receivables. Wards were used as the unit of sampling.

### **3.5 Data Collection Method**

In this study, the researcher used primary in order to perform a good research. Primary data are the data gathered and assembled specifically for the research project at hand. Questionnaires were employed as the main instrument for the data collection. Kothari (2007), states that a questionnaire is the most suitable instrument due to its ability to collect a large amount of information in the shortest time possible. It guarantees confidentiality of the source of information through anonymity while ensuring standardization (Churchill, 1991). Schwab (2005) further defines questionnaires as measuring instruments that ask individuals to answer a set of questions or respondent to a set of statement Dawson (2002) suggests that there are three basic types of questionnaires; closed ended, open-ended or a combination of both. Closed-ended questionnaires are used to generate statistics in quantitative research. The above justifies the reason why questionnaire were used as an appropriate instrument for this study. Questionnaires with an introductory letter assuring participants their confidentiality were randomly administered to finance officers of each of the 359 SMEs. Questionnaire with 5 point Likert scale showed the respondents' level of agreement towards the statement in the questionnaire.

Primary data was collected using semi-structured questionnaire administered to the finance officers or owners. The drop-and-pick later approach was used in this study as it is considered an appropriate method because it gave the respondents' time to complete the questionnaire and also gave the researcher an opportunity to review the questionnaire before picking to ensure completeness of the responses. Where necessary, personal interviews and documentary analysis was conducted to enhance validity. Limited secondary data was obtained from financial statements maintained by the firms. Manual processing involved collecting and tabulating the information from the returned questionnaires. The data was coded to point out relevant and

understandable category of answers. Coding was done to close-ended questions by assigning codes to various variables. Data collected and coded was then analyzed using SPSS (Statistical Package for Social Scientists) version 21. Research findings were presented using both descriptive and qualitative methods. Opinions were supported by frequency distribution tables constructed from the results of the study.

### **3.6 Pilot Study**

Cooper and Schindler (2010) showed that a pilot study is conducted to identify faults in design and instrumentation and to provide proxy data for selection of a probability sample. Pilot test is an activity that assists the researcher in determining if there are faults and weaknesses within the interview design and allows for amendments prior to the implementation of the study (Kvale, 2007) A pilot test was carried out twice with two different groups of participants, as suggested by (Malhotra et al., 2006).

#### **3.6.1 Content Validity**

Content validity was employed by this study as a measure of the degree to which data collected using a particular instrument represents a specific domain or content of a particular concept. Mugenda and Mugenda (2003) suggest that the usual procedure in assessing the content validity of a measure is to use a professional expert in a particular field. The experts and supervisors determined the content validity of the instrument through their advice. A pilot test with the experts was used to confirm content validity of the measurements used in the questionnaire.

#### **3.6.2 Reliability**

Reliability is a measure of the degree to which a research instrument yields consistent results or data after repeated trials (Borg, Gall & Gall, 2003).it refers to the consistency of measurement and is enhanced through a pilot study before the actual study took place In the second group, a pilot study was undertaken on 20 SMEs in Bungoma County (within the Town). Finance officers/owners were used to test the reliability and validity of the questionnaire. The rule of thumb is that 5%-10% of the sample should constitute the pilot test (Cooper & Schilder, 2011; Creswell, 2003). The

proposed pilot test was within the recommendation for instance 20 owners/finance officers of SMEs in the Bungoma County. This group was chosen as suggested by Hair et al. (2010), who said that when the scales used in the research are based on previous studies, a pilot test with respondents similar to those from the population to be studied is recommended to screen items for appropriateness. The researcher conducted reliability tests for every measureable variable in this study. The Cronbach's Alpha coefficients helped to identify the consistency of items in the independent and dependent variables. The following is the Cronbach's coefficient alpha formula which was used:

$$\alpha = \frac{N \cdot \bar{c}}{\bar{v} + (N - 1) \cdot \bar{c}}$$

Here N is equal to the number of items, c-bar is the average inter-item covariance among the items and v-bar equals the average variance. After ascertaining that the instrument is giving consistent results, it was adopted as the main tool to be used for data collection. The Cronbach's Alpha values from the first test established the need to revise the instrument. During the first pilot study, the respondent had difficulties in answering the questions with the words accounts receivables. To correct this researcher added the word debtors. Secondly, questions that seemed ambiguous were removed, and more appropriate ones were added and then retest was carried out. The Cronbach's coefficient alphas were obtained from the SPSS to determine the internal consistency of the questionnaire in measuring: Credit Analysis practice, Credit Extension practice, Credit collection practices, Credit risk assessment practices, Accounts receivable financing practices, financial literacy and growth performance. The obtained Cronbach's alphas for variables are listed in chapter 4. The alpha values were acceptable as they exceeded the 0.7 threshold as recommended by Gliem and Gliem (2003).

### **3. 7 Data Analysis and Presentation**

The study employed both descriptive as well as inferential statistics for data analysis. Descriptive statistics was used to test for normality of data; Homoskedascity was used to determine whether the variance of the error term is constant and same for all observations. Hypotheses were tested at 5% level of significance using t-test, and F-test. Ordinary least square method was used to determine the cause-effect relationship among the variables. Multiple linear regressions was used to determine the degree and magnitude of the relationship that existed between variables. (Hair et al. 2010),

#### **3.7.1 Descriptive Analysis**

A descriptive analysis was carried out on receivable management practices to determine their influence on the growth of SMEs. The mean and standard deviation were used to show how the respondents strongly agree, agree, or are neutral according to the Likert scale of 1-5. The frequencies procedure provides statistics and graphical displays that are useful for describing many types of variables in this study. Frequencies distributions were used to interpret the respondent profile data and information (demographics). The researcher arranged the displayed frequencies in chart such as bar.

#### **3.7.2 Inferential Analysis.**

Data analysis was guided by the objectives of the study. Various statistical techniques were used to analyze data. This included statistical analysis of variables, correlations among variables; A Pearson product moment correlation was computed to assess the relationship between accounts receivable management practices and growth of SMEs. Hypotheses were tested at 5% level of significance using inferential statistics. Ordinary Least squares method was used to determine the cause and effect relationship among the variables. Regression analysis is a statistical tool that examines the relationship between the variables by analyzing coefficients for the equation in a straight line (Faraway, 2002).



In answering the research questions and objectives, multiple regression analysis was used to test the identified hypotheses. Regression consists of R Square, which was used to test the overall significance of the model (Malholtra, 2007).

SMEs growth was proxied by: sales growth and profitability rate that fundamentally is dependent on Receivable management practices adopted. Survey respondents were asked to self-assess their overall financial knowledge based on a five-point scale with a rating of one being very low and a rating of five being very high. This affective item provided insights into how respondents perceive their level of financial literacy, their understanding and adoption of the ARM practices, i.e. Credit analysis, credit extension, credit risk assessment, credit collection and financing of receivables.

### **3.7.3 Variable Definition and Measurement**

Each of these five measures was developed from previous studies. Each of the measures examined items associated with a distinct aspect of Accounts receivable management practices in SMEs. Although these items were developed from existing research, they were being examined in a single study unlike previously:

**a) Accounts Receivable Analysis Practice** has items used to measure the importance of various forms of information in determining whether a customer receives authorization to purchase on credit. In his research, Perry (1995) examined the following items that were used by credit managers to determine whether customer buys on credit. (Capacity, cashflows, collateral. Amount of credit). Questions related to each of these were included in the instrument for the current research.

**b) Accounts Receivable Extension Practices:** There are many different measures that could be used to assess a debtor's qualifies to have his credit extended .For example: the length of time they have been in business, bank or trade references, and third party reference, credit checking and credit information to granting of credit extension is important, credit extension agreement.

**c) Accounts Receivable Collection Practices:** Pike *et al.* (1998) acknowledged that small businesses feel that the management of debtor days is the most important

measurement of the effectiveness of their credit management processes (82 per cent of participants) followed by their achievement of cash collection targets. Less than half of the participants reported that reducing bad debts and bad debt to sales ratio a being an important measure of credit performance within the firm. In this study questions related to collection targets were included in the instrument .measured by follow up, collection policy, average collection period, aging of accounts receivable.

**d) Accounts Receivable Risk Assessment Practices:** There are many different measures that could be used to assess and reduce the chances of an accounts receivable turning into a bad debt their account. Internal rating systems, credit scoring model, assessment staff.

**e) Accounts Receivable Financing Practices:** The measures here included the use of factoring, invoice discounting and collateralized debt, therefore questions related to this were asked.

**f) Financial Literacy:** Just as there is no standard definition of financial literacy, there is no standardization in the measures that are used in research studies. In this study questions related to accounts receivables management were asked to test the level of understanding of the entrepreneur.

**g) SME Growth:** The commonly used measures of firm growth: (employment growth, sales growth, profit, return on equity [ROE], return on assets [ROA]) and entrepreneurs' perceived growth relative to their competitors in terms of increase in company value (Leona *et al.*,2010). However in this study growth will be measured by profitability and sales turnover.

#### **3.7.4 Research Model**

Linear multiple regressions was used to establish and explain the relationship between Accounts receivable management practices and growth for three years. Based on Aiken and West (1991), the relationship between ARMP and SMEs growth was developed into linear regression model as follows:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \varepsilon'$$

Where:

Y=the dependent variable. Referring to SMEs growth (proxied by sales growth and profitability)

$\beta_0$  Regression constant. It is the value of Y when  $X_1=X_2=X_3=X_4=X_5=0$

$\beta_1$  Change in Y with respect to a unit change in  $X_1$

$\beta_2$  Change in Y with respect to a unit change in  $X_2$

$\beta_3$  Change in Y with respect to a unit change in  $X_3$

$\beta_4$  Change in Y with respect to a unit change in  $X_4$

$\beta_5$  Change in Y with respect to a unit change in  $X_5$

$\beta_6$  Change in Y with respect to a unit change in  $X_6$

X1- Accounts receivable analysis practices (measured by the creditworthiness and level of cashflow of customers)

X2- Accounts receivable extension practice (measured by tracking of customer records and third party references, security or guarantee)

X3-Accounts Receivable collection Practice (measured by collection timelines (aging schedules, collection period, the discounts used)

X4- Accounts Receivable risk assessment Practice (measured by internal rating system, training employees and debtor education, credit scoring mode.

X5- Accounts Receivable financing Practice (measured by the number of invoices discounted, collateralized or factored)

X6-Financial literacy of ARMP (measured by the knowledge and skill acquired on practice accounts receivable management practices as a moderating factor.

$\beta_i$  ( $i = 0, 1, 2, 3, 4$ ) are the coefficients

$\varepsilon$  is the error term. The inclusion of a random error,  $\varepsilon$ , is necessary because other unidentified variables may also affect SMEs growth.

The multiple regression is based on the assumption that for any specific value of the independent variable, the value of the Y variable are normally distributed (normality assumption) and that the variances for the Y variables are the same for each of the independent variable (equal –variance assumption).Based on the model above the researcher hypothesizes that;

**H0:** $\beta_1 = 0$  ( $X_i$  is not significantly related to Y)

**H1:** $\beta_1 \neq 0$  ( $X_i$  is significantly related to Y)

The study applied six hypotheses generated from the model as follows;

**H<sub>01</sub>:** An Accounts receivable analysis practice has no significant effect on growth of Small and Medium Enterprises in Kakamega County in Kenya. Growth of SMEs =  $f$  (Accounts receivable analysis practices, random error)

$$Y = \beta_0 + \beta_1 X_1 + \varepsilon$$

**H<sub>02</sub>:** Accounts receivable extension practice has no significant effect on growth of Small and Medium Enterprises in Kakamega County in Kenya. Growth of SMEs =  $f$  (Accounts receivable analysis practices, random error)

$$Y = \beta_0 + \beta_2 X_2 + \varepsilon$$

**H<sub>03</sub>:** Accounts Receivable collection Practice has no significant effect on growth of Small and Medium Enterprises in Kakamega County in Kenya. Growth of SMEs =  $f$  (Accounts receivable analysis practices, random error)

$$Y = \beta_0 + \beta_3 X_3 + \varepsilon$$

**H<sub>04</sub>:** Accounts Receivable risk assessment Practice has no significant effect on growth of Small and Medium Enterprises in Kakamega County in Kenya. Growth of SMEs =  $f$  (Accounts receivable analysis practices, random error)

$$Y = \beta_0 + \beta_4 X_4 + \varepsilon$$

**H<sub>05</sub>:** Accounts Receivable financing Practice has no significant effect on growth of Small and Medium Enterprises in Kakamega County in Kenya. Growth of SMEs =  $f$  (Accounts receivable analysis practices, random error)

$$Y = \beta_0 + \beta_5 X_5 + \varepsilon$$

Model summary with Financial Literacy as a Moderator Variable was based on (Kerry, 2015) model.

$$Y = \beta_0 + \beta_1 X_1 \cdot M + \beta_2 X_2 \cdot M + \beta_3 X_3 \cdot M + \beta_4 X_4 \cdot M + \beta_5 X_5 \cdot M + \varepsilon$$

M=Financial Literacy

## CHAPTER FOUR

### RESEARCH FINDINGS AND DISCUSSIONS

#### 4.1 Introduction

The results of data analysis on the relationship between accounts receivable management practices and growth of SMEs in Kakamega, Kenya are presented and discussed in this chapter. The data obtained from the respondents was analyzed using SPSS version 21. The analyzed data was arranged under themes that reflect the research objectives. All the hypotheses were tested at 0.05 significant levels

#### 4.2 Response Rate

The number of questionnaires that were administered was 359. A total of 276 questionnaires were properly filled and returned. This represented an overall successful response rate of 77% as shown in Table 4.1. According to Gall, Borg, and Gall (1996) response rate of 80 % is considered excellent in quantitative research in social sciences, and according to Fincham (2008), a response rate of 60% is considered appropriate in research, while according to Mangione (1995) a response rate of over 85% is considered excellent for self-filled questionnaires. The response rate was considered appropriate for further analysis since it was 77%.

**Table 4.1: Response Rate**

<b>Response</b>	<b>Frequency</b>	<b>Percent</b>
Returned	276	77
Unreturned	83	33
<b>Total</b>	<b>359</b>	<b>100</b>

Source: Field data, 2016

### 4.3 Reliability Results

Reliability is a measure that indicates the extent to which there is no biasness, therefore it ensures consistent measurement across the various items in the instrument. In this study reliability study was done on all the items. The Cronbach's Alpha is a reliability measure which shows how well the items in the instrument are correlated to each other (Sekaran, 2006). Reliability of this instrument was evaluated through Cronbach Alpha which measures the internal consistency.

**Table 4.2: Reliability Coefficient**

<b>Variables</b>	<b>Cronbach's Alpha</b>	<b>Comment</b>
Credit Analysis Practice	0.823	Accepted
Credit Extension Practice	0.754	Accepted
Credit Collection Practice	0.875	Accepted
Credit Risk Assessment Practice	0.824	Accepted
Financing Practice	0.820	Accepted
Financial Literacy	0.820	Accepted
SME growth	0.822	Accepted
Average Cronbach Alpha for all the variables	0.820	Accepted

Source: Field Data, 2016

Cronbach Alpha value is widely used to verify the reliability of the construct. The findings in table 4.2 indicated that Accounts Receivable analysis practice had a coefficient of 0.823, Accounts Receivable extension practice had a coefficient of 0.754, Accounts Receivable Collection Practice had a coefficient of 0.875, Accounts Receivable Risk Assessment Practice had a coefficient of 0.824, Accounts Receivable financing practices had a coefficient of 0.820, and financial literacy had a coefficient of 0.820 while SME growth had a coefficient of 0.822. The average cronbach alpha for all the variables was 0.820 which is above the recommended threshold. All variables depicted that the value of Cronbach's Alpha are above value of 0.7 thus the data collection instrument was reliable (Castillio, 2009). This represented high level of reliability and on this basis; it was supposed that scales used in this study is reliable to

capture the variables. Of 0.7 thus the data collection instrument was reliable (Castillio, 2009). This represented high level of reliability and on this basis; it was supposed that scales used in this study is reliable to capture the variables

#### **4.4 Entrepreneurs Background Information**

This section analyzes the background information of the respondents. This section presents the descriptions of the respondents in terms of their gender, level of education, number of years in current firm. Results are as presented in Table 4.3, 4.4, 4.5 respective

**Table 4.3: Showing Respondents' Gender**

<b>Gender</b>	<b>Frequency</b>	<b>Percentage</b>
Female	117	57.6
Male	159	42.4
<b>Total</b>	<b>276</b>	<b>100</b>

**Source: Field data, 2016**

Results in table 4.3 reveal that 57.6% of the respondents were male while 42.4% of the respondents were female. It is observed that most entrepreneurs who operate SMEs are male. This can be attributed to the culture dynamics of the residents of Kakamega who have for a long time viewed men as providers while women stay at home to take care of the children. However the small margin can be seen as a good indicator of changes in the culture and thus a representation of the study population.



**Table 4.4: Showing Respondents' Level of Education**

<b>Qualification</b>	<b>Frequency</b>	<b>Percentage</b>
Primary	29	10.5
Secondary	118	42.8
Graduate	122	44.2
Postgraduate	7	2.5
<b>Total</b>	<b>176</b>	<b>100</b>

**Source: Field data, 2016**

Further, results in Table 4.4 show that 44.2% of the respondents were graduates, 42.8% of the respondents had acquired education up to the secondary level while 10.5% of the respondents had acquired education up to primary level. Only 2.5% of the respondents had acquired education up to post graduate level. This is an indicator that most of the respondents were educated implying that they were better positioned to learn and apply ARM practices in their firms with an aim of experiencing growth this could also imply that most of the educated were trying their hands on entrepreneurship either as a result of not getting jobs or as an incentive from the government from the youth funds and women funds. Indeed this can also be attributed to Government's initiative of providing free and affordable education to all.

The responses on the job titles included; owner, data entry clerk, manager, accountant, business lady, salesman, underwriter, cyber attendant, salonist, trader, shopkeeper, supervisor, sales woman, farmer barber, sales agent, relationship manager, finance manager, engineer, driver, financial analyst, M-pesa attendant, mechanic, assistant manager, hotelia, co-owner, massager, trader, retailer, clerk, hawker, waiter, bodaboda operator, wholesaler, revenue officer, clinical officer and pharmacist. This is an implication that the data collection process was diversified. This is of importance as the results will represent people from different professions.

**Table 4.5: Showing Respondents' Number of Years in the Business**

<b>Number of years worked</b>	<b>Frequency</b>	<b>Percentage</b>
1-5 Years	193	69.9
6-10 Years	68	24.6
11-15 Years	10	3.6
More than 15Years	5	1.8
<b>Total</b>	<b>276</b>	<b>100</b>

**Source: Field data, 2016**

Results in table 4.5 also revealed that 69.9% of the respondents had worked in the firm for a period of 1 – 5 years while 24.6% of the respondents had worked in the firm for 6 – 10 years. Another 3.6% of the respondents had worked in the firm for 11 – 15 years while a paltry 1.8% of the respondents had worked in the firm for more than 15 years. Since all the characteristic classifications were represented with the majority of the respondents having worked or dealt with SMEs for a period more than 3 years the information obtained was believed to be reliable. This is an indicator that most of the respondents had not worked in the firm for a long period of time and thus did not have much experience on how to run the firm's operations. Hence, it could be of great significance that they acquire information on Account Receivable Management (ARM) practices. This would go a long way in ensuring that they experience growth. However, an experience of 1 – 5 years is good enough to give reasonable information on which this study based its results.

#### **4.5 Business Demographics**

This section outlines the sector of the businesses, the type of business ownership and the period the business has been in operation. Results are presented in Table 4.6.

**Table 4.6: Sector of Business**

<b>Sector</b>	<b>Frequency</b>	<b>Percentage</b>
Retail	90	32.6
Health and Beauty	12	4.3
Construction	6	2.2
Agriculture	19	6.9
Manufacturing	33	12
Hospitality	39	14.1
Transport	31	11.2
Service	46	16.7
<b>Total</b>	<b>276</b>	<b>100</b>

**Source: Field data, 2016**

Results revealed that 32.6% of the respondents operated firms in the retail sector, 16.7% of the respondents indicated that they operated firms in the service sector, 14.1% operated firms in the hospitality sector, 12% operated firms in the manufacturing sector, and 11.2% operated firms in the transport sector while 6.9% were in the agricultural sector. Results also revealed that 4.3% operated firms in the health and beauty sector while a paltry 2.2% operated firms in the construction sector. This indicates that the study looked at diverse sectors.

**Table 4.7: Showing Respondents in Business**

Type of Business	Frequency	Percentage
<b>Sole trader</b>	<b>152</b>	<b>55.1</b>
<b>Partnership</b>	<b>70</b>	<b>25.4</b>
<b>Family trust</b>	<b>39</b>	<b>14.1</b>
<b>Public Enterprises</b>	<b>15</b>	<b>5.4</b>
Total	276	100

**Source: Field data, 2016**

Results in Table 4.7 revealed that 55.1% of the respondents were sole traders, 25.4% of the respondents had partnerships while 14.1% of the respondents indicated that they operated family trust firms. Another 5.4% of the respondents had public enterprises. Majority of SMEs are either sole traders or partnership. The low percentage of public enterprises could be attributed to the high capital outlay required to start and the long procedures involved.

#### **4.6. Descriptive Analysis**

Descriptive statistics were used to test for normality of data. Normality test was used to determine the normal distribution of the sampled data in order to make accurate and reliable conclusions. The mean which is a measure of central tendency was used in generalization of findings while standard deviation was used as a measure of dispersion from the mean. The summary of descriptive statistics is shown in Table 4.8

**Table 4.8 Descriptive Analysis**

	<b>Mean</b>	<b>Std dev.</b>
Growth	43.762	6.993
1. Accounts Receivable analysis practices	3.32	1.159
2. Accounts receivable extension practices	3.94	1.033
3. Accounts receivable collection practices	3.41	1.168
4. Accounts receivable risk assessment practices	3.04	1.234
5. Accounts receivable financing practices	3.00	1.154
6. Financial literacy level on Accounts receivable management	3.30	1.031

**Source: Field data, 2016**

The standard deviation is a summary measure of the differences of each observation from the mean while the mean is the average for all the variables, growth had a mean of was 43.762 which represent the mean amount of growth originated by all SMEs in Kakamega Kenya. Use of Accounts receivable analysis practices had a mean of 3.32 which represents the average changes in use of AR analysis practices in the period under study. Use of Accounts receivable extension practices had a mean of 3.94 which indicates the mean changes in use of Accounts receivable extension practices for the period under study for all SMEs. Accounts receivable collection practices had a mean of 3.41 which indicates the average changes in the use of Accounts receivable collection practices for the period under study. Accounts receivable risk assessment practices had a mean of 3.04 which indicates the mean changes in use of Accounts receivable risk assessment practices for the period under study for all SMEs. Accounts receivable financing practices had a mean of 3.00 which indicates the average changes in the use of Accounts receivable financing practices for the period under study. Financial literacy level on Accounts receivable management had a mean of 3.30 which indicates the average changes in the use of financial level on Accounts receivable management for the period under study. The standard deviation for Accounts Receivable analysis practices was 1.159, Accounts

receivable extension practices had 1.033, Accounts receivable collection practices had 1.168, Accounts receivable risk assessment practices had 1.234, Accounts receivable financing practices had 1.154, and lastly the standard deviation of financial level on Accounts receivable management was 1.031.

Accounts receivable risk assessment practices had the highest deviation from its mean; this could imply that it would have a higher effect on the dependent variable. The standard deviation for Accounts Receivable risk assessment practices was 1.234, Accounts receivable extension practices had 1.232 and financial literacy levels on Accounts receivable had the lowest, 1.033. The standard deviations for the variables are closer to zero which implies that the values are concentrated around the mean.

#### **4.7 Accounts Receivable Analysis Practice**

The study sought to establish the influence of Accounts receivable analysis practices on growth of SMEs in Kakamega, County Kenya. The study specifically investigated the following elements of AR analysis practices; customers' paying history, contacting third parties for references, scrutinizing of customers' account, customers cash flows financial statement and collateral issued as indicated in table 4.9

**Table 4.9: Accounts Receivable Analysis**

<b>Statement</b>	<b>Never</b>	<b>Annually</b>	<b>Semi- annually</b>	<b>Monthly</b>	<b>Always</b>	<b>Mean</b>
1. How often do you analyze customers' paying history to determine capacity to pay	4.30%	19.20%	9.40%	44.20%	22.80%	3.62
2. How often do you contact third parties for references(creditworthines s)	7.60%	24.30%	26.80%	28.30%	13.00%	3.15
3. How often do you scrutinizes customers' account to determine his capital base	10.50%	30.10%	14.10%	36.20%	9.10%	3.03
4 How often do you analyze and determine Customers cash flows financial statement.	8.70%	19.60%	18.80%	40.60%	12.30%	3.28
5. How often do make a follow up on collateral issued	6.50%	13.80%	18.10%	44.90%	16.70%	3.51
<b>Average</b>						<b>3.32</b>

**Source: Field Data, 2016****4.7.1 Customers' Paying History**

The study sought to determine whether SMEs analyze customers' paying history to determine capacity to pay. Results in Table 4.9 reveal that 67% of the respondents occasionally t they analyze customers' paying history to determine capacity to pay while 23.5% of the respondents disagreed that they analyze customers' paying history to determine capacity to pay. Another 9.4% of the respondents said they analyzed monthly. In line with the findings of Anthony (2006), this study found significant

relationship between evaluations of clients paying history to determine his/her capacity pay. The findings implied that the SMEs under study analyze customers' paying history to determine capacity to pay. Moti et al. (2012) concurs arguing that capacity to repay is critical in client appraisal and hence credit analysis, this further implies that analyzing a customer ability to pay may assist the SMEs owners to avoid bad debts. This further indicated that the SMEs in Kakamega County have put in place effective customer analysis practices which may have an implication on the growth of the SMEs.

#### **4.7.2 Contacting Third Parties for References**

The study sought to determine whether SMEs contact third parties for references. Results in Table 4.9 reveal that 41.3% of the respondents occasionally contact third parties for references (creditworthiness) while 31.9% of the respondents that once in a year that they contact third parties for references (creditworthiness). Another 26.8% of the respondents said twice. Wanjiru (2013) indicates that third party reference is important as it facilitates prudent decision making as to which customer should be granted credit. Anderson, (2007) further asserted that with Credit Reference Bureaus a culture of financial discipline will be instilled since consumers know that they will be monitored and black listed. The findings implied that the SMEs under study analyze contact third parties for references a bid to establish the creditworthiness of their customers. Contacting third parties for will enable the SMEs owners to acquire full information about the creditworthiness of their customers which in return will help them evade the risk of bad debts. This further indicated that the SMEs in Kakamega County have put in place effective customer analysis practices which may have an implication on the growth of the SMEs.

#### **4.7.3 Scrutinizing of Customers' Account**

The study sought to determine whether SMEs scrutinize customers' account to determine their capital base. Results in Table 4.9 reveal that 45.3% of the respondents occasionally scrutinize customers' account to determine their capital base while 40.6% of the respondents did not that they scrutinize the customer's account. Another



14.1% of the respondents did it just twice. Connolly (2013), posits that many firms hardly maintained customer details and credit information, hence they do not practice proper billing which adversely affected timely collection of payments from the customers. The findings implied that the SMEs under study scrutinize customers' account to determine their capital base. Scrutinizing customers' account to determine their capital base is of great significance to the SMEs owners as they will avoid advancing credit to customers' before determining their ability to pay. This further indicated that the SMEs in Kakamega County have put in place effective customer analysis practices which may have an implication on the growth of the SMEs.

#### **4.7.4 Customers Cash Flows Financial Statement**

The study sought to determine whether SMEs analyze and determine customers' cash flows financial statement. Results in Table 4.9 reveal that 52.9% of the respondents occasionally analyze and determine customers' cash flows financial statement while 28.3% of the respondents rarely analyze and determine customers' cash flows financial statement. Another 18.8% of the respondents twice a year. Contrary to this findings, Moti et al. failed to establish any significant importance of evaluating the cashflow statement when appraising customers for credit, however the study concurred with that of Abedi (2000) who recommends that cashflow statements be evaluated when appraising clients. The variance in the findings could be as a result of the various strategies used in investing and financing. The findings implied that the SMEs under study analyze and determine customers' cash flows financial statement. The practice of analyzing and determining customers' cash flows financial statement may help the SMEs owners to establish the speed at which a customer is able to pay back their debt and thus enable them to make prudent decisions. This further indicated that the SMEs in Kakamega County have put in place effective customer analysis practices which may have an implication on the growth of the SMEs.

#### **4.7.5 Collateral Issued**

The study sought to determine whether SMEs evaluate collateral issued. Results in Table 4.9 reveal that 61.6% of the respondents agreed that they evaluate collateral

issued while 20.3% of the respondents disagreed that they evaluate collateral issued. Another 18.1% of the respondents were undecided. This finding is consistent with the findings of Moti et al. (2012 since the study found a significant relationship between collateral attached as security and growth .The findings implied that the SMEs under study evaluate collateral issued. Evaluating the collateral issued will enable the SMEs owners to advance credit that does not exceed the value of the collateral issued. This further indicated that the SMEs in Kakamega County have put in place effective customer analysis practices which may have an implication on the growth of the SMEs. SMEs should therefore evaluate the collateral used as security when appraising the clients; this is so that in case a customer defaults the collateral can be used to settle the debt.

#### **4.7.6 Bivariate Regression Showing Relationship between Accounts Receivable Management Practices and Growth**

Regression analysis was used to find out if there was a relationship between customer analysis practices and SMEs growth by evaluating the contribution of the customer analysis practices in explaining SMEs growth, when the other variables are controlled; the R Square value was obtained in this case.

From the results in Table 4.9, customer analysis practices were found to have an R Square value of 0.289 or to contribute to 28.9% SME growth. The R square value is an important indicator of the predictive accuracy of the equation. The remaining 71.1% can be explained by other factors. The implication of these finding is that customer analysis practices plays a significant role in enhancing SME growth.

**Table 4.10: Model Fitness**

	<b>R</b>	<b>Adjusted R</b>	<b>Std. Error of</b>
<b>R</b>	<b>Square</b>	<b>Square</b>	<b>the Estimate</b>
0.540	0.292	0.289	0.50474

Table 4.11 provides the results on the analysis of the variance (ANOVA). The results indicate that the overall model was statistically significant. Further, the results imply that customer analysis practices are good predictors of SMEs growth. This was supported by an F statistic of 112.798 and the reported p value (0.000) which was less than the conventional probability of 0.05 significance level.

**Table 4.11: Analysis of Variance**

Indicator	Sum of Squares	df	Mean Square	F	Sig.
Regression	28.737	1	28.737	112.798	0.000
Residual	69.805	274	0.255		
Total	98.541	275			

Regression of coefficients results in Table 4.12 shows that there is a positive and significant relationship between customer analysis practices and SMEs growth as supported by a p value of 0.000 and a beta coefficient of 0.278. This was also supported by the t values whereby  $t_{cal}=31.232 > t_{critical}=12.706$  at 95 percent confidence level which depicts that we reject the null hypothesis and accept the alternative.

The findings concurred with those in Iku (2015) who identified that the strongest independent variable in his study was credit analysis. This implies that an increase in customer analysis practices by 1 unit would result to increase in SMEs growth by 0.278 units.

**Table 4.12: Regression of Coefficients**

Variable	B	Std. Error	t	Sig.
(Constant)	2.734	0.088	31.232	0.000
Accounts Receivable Analysis Practices	0.278	0.026	10.621	0.000

$$\text{SMEs Growth} = 2.734 + 0.278 \text{ Customer Analysis Practices}$$

#### 4.8 Accounts Receivable Extension Practices

The study sought to establish the influence of credit extension practices on growth of SMEs in Kakamega County Kenya. The study specifically investigated the following elements of credit extension practices; development of a written plan, use of formalized credit processes, and use of third party provided intelligence, extension to regular customers with good records and use of portfolio strategy as shown in table 4.13

**Table 4.13 Showing Relationship between AR Extension Practices and Growth**

<b>Statement</b>	<b>Never</b>	<b>Annually</b>	<b>Semi-A</b>	<b>Monthl</b>	<b>Always</b>	<b>Mean</b>
				<b>y</b>		
1. How often do you review written plan(showing credit terms)	3.60%	8.70%	9.80%	46.70%	31.20%	<b>3.93</b>
2 How often do you Use formalized credit processes(documentation of agreement)	7.60%	11.20%	11.60%	41.30%	28.30%	<b>3.71</b>
3. How often do you use third party provided intelligence.	5.50%	17.90%	24.50%	36.50%	15.70%	<b>3.39</b>
4. How often do you review data of regular customers who have had good record?	3.40%	10.50%	8.20%	54.30%	23.60%	<b>3.84</b>
5. How often do use portfolio strategy to segment categories of customers	4.40%	4.40%	13.10%	53.30%	24.80%	<b>3.90</b>
<b>Average</b>						<b>3.67</b>

**Source: Field Data (2016)**

78.1% of the respondents agreed that they extended credit to regular customers who have had good records while 47.1% of the respondents agreed that they used portfolio strategy to segment categories of customers. The results show good practice of the credit extension practices. This can be supported by the mean of the responses (3.67) which means that majority of the respondents were agreeing to the statements in the questionnaire.

#### **4.8.1 Development of a Written Plan Showing Credit Terms**

Results in Table 4.13 show that 77.9% of the respondents have developed a written plan (showing credit terms), 69.6% of the respondents also agreed that they use formalized credit processes (documentation of agreement). Table 4.13 demonstrates 3.6% percent of respondents never a written plan showing credit terms, while 8.9% reviewed the written plan once a year, 9.8% were semiannually and 46% monthly while 31.30% never review their written plan. This finding suggests that having a written plan was strongly practiced by SMEs in Kakamega County. Majority of the SMEs studied about (78%) agreed that they use written plan (credit policy manuals) and reason could be that majority have formal education and are enlightened. This is indeed good move because a written plan is the blueprint used by any firm in making its decision as whether to extend credit to customers or not . The major objective of a written plan is to ensure that credit is not extended to customers who are unable to pay their accounts.

Result on written plan agree with Wanjiku (2013), however it contradicts the findings by Kalunda et al. and that by Kwame (2008) which showed that small businesses always do not have written plans. The finding is also consistent with Grover (2002) who states a credit policy must be written with an ample room for change and must be reviewed regularly to be updated in regards to any environmental changes. The findings implied that the SMEs under study have developed a written plan showing credit terms. The existence of a written plan showing credit terms creates a good platform for the SMEs owners to follow up on the customers' in-case of default. This further indicated that the SMEs in Kakamega County have put in place effective credit extension practices which may have an implication on the growth of the SMEs.

#### **4.8.2 Use of Formalized Credit Processes**

The findings concurred with those in Tomusange. (2015) who state that credit procedures are the criteria used by a firm to decide on the type of customers to whom sales can be made on credit. The findings implied that the SMEs under study use formalized credit processes in the documentation of agreements. The practice of using formalized credit processes in the documentation of agreements provides a clear procedure, according to the law, which ought to be followed by the two parties (SME owner and the customer). This helps to curb the challenge of credit default and bad debts. This further indicated that the SMEs in Kakamega County have put in place effective credit extension practices which may have an implication on the growth of the SMEs.

#### **4.8.3 Use of Third Party Intelligence**

Table 4.13 further illustrates that 52.2% of the respondents agreed that they used third party provided intelligence. Wanjiru (2013) concurs with the study findings that indicate third party reference is important as it facilitates prudent decision making as to which customer should be granted credit. Anderson, (2007) further indicated that with Credit Reference Bureaus a culture of financial discipline will be instilled since consumers know that they will be monitored and black listed. The findings implied that the SMEs under study use third party provided intelligence. The use of third party provided intelligence by SMEs owners will help them in making wise decisions when advancing credit to their customers. This further indicated that the SMEs in Kakamega County have put in place effective credit extension practices which may have an implication on the growth of the SMEs.

#### **4.8.4 Extension to Regular Customers with Good Records**

Results also revealed that 77.9% of the respondents agreed that they extend credit only to customers who have good records, Table 4.13 demonstrates 5.5 % percent of respondents never review records while giving credit while 17.9 % percent review annually, 9.8%, 24.5% semiannually review before they extend and 36.5% monthly while 15.7% always. This finding suggests that on average about 50% SMEs

practiced in Kakamega County about (50%) agreed that they allow credit (Accounts receivable), for amounts guaranteed. These results agree with. (Fafchamps1997.).Table 4.13 demonstrates that4.4% percent of respondents strongly disagree to reviewing past customer records, while 4.40 % percent disagree 9.8%, 13.1 % neutral as to whether they review or not and 53.3 % agreed while 24.8 % strongly agree. These finding suggests that Majority of SMEs (79%) carried out this practice in Kakamega County. Kalunda (2012), findings also concur. She argues that the six C's helps firms to decrease their default rate as they get to know their customers.

Information on the C's can be obtained several sources including the firm's prior experience with the customers, by tracking the trend of the customers paying history, analyzing the financial statements for previous years, enquiring from credit reporting agencies and even the customers financial institutions. The study determined that SMEs extend credit to regular customers who have had good records. (Ndonye, 2015) argues that controlling of receivables involves following up on debtors records and paying behavior. The findings implied that the SMEs under study extend credit to regular customers who have had good records. This practice acts as a reward to the customers for their good records and also helps the SMEs owners retain the customers. This can also assist them to increase their customer base as the regular customers will market them for their good practice. This further indicated that the SMEs in Kakamega County have put in place effective credit extension practices which may have an implication on the growth of the SMEs.

#### **4.8.5 Use of Portfolio Strategy**

The study showed that SMEs use portfolio strategy to segment categories of customers. Gekara et al. (2014) concurred with the results; the results ascertained that firms at times use portfolio strategy to segment customers according to their payment behavior. The findings implied that the SMEs under study use portfolio strategy to segment categories of customers. Use of portfolio strategy helps the SMEs to hedge against risk as they have been able to segment their customers according to their riskiness. This further indicated that the SMEs in Kakamega County have put in place

effective credit extension practices which may have an implication on the growth of the SMEs. Having a record of who pays and how they pay may form the basis of the portfolio.

#### **4.8.6 Bivariate Regression Showing Relationship between Accounts Receivable Extension Management Practices and Growth**

Regression analysis was used to find out if there is a relationship between credit extension practices and SMEs growth by evaluating the contribution of the Accounts Receivable Extension Practices in explaining SMEs growth, when the other variables are controlled; the R Square value was obtained in this case.

From the results in Table 4.14 credit extension practices were found to have an R Square value of 0.395 or to contribute to 39.5% SME growth. The R square value is an important indicator of the predictive accuracy of the equation. The remaining 60.5% can be explained by other factors. The implication of these finding is that credit extension practices plays a significant role enhancing SME growth.

**Table 4.14: Model Fitness**

<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Std. Error of the Estimate</b>
0.631	0.398	0.395	0.46544

Table 4.15 provides the results on the analysis of the variance (ANOVA). The results indicate that the overall model was statistically significant. Further, the results imply that credit extension practices are good predictors of SMEs growth. This was supported by an F statistic of 180.873 and the reported p value (0.000) which was less than the conventional probability of 0.05 significance level.



**Table 4.15: Analysis of Variance**

Indicator	Sum of Squares	df	Mean Square	F	Sig.
Regression	39.183	1	39.183	180.873	0.000
Residual	59.358	274	0.217		
Total	98.541	275			

Regression of coefficients results in Table 4.16 shows that there is a positive and significant relationship between credit extension practices and SMEs growth as supported by a p value of 0.000 and a beta coefficient of 0.519. This was also supported by the t values whereby  $t_{cal}=13.097 > t_{critical} = 12.706$  at a 95 percent confidence level which depicts that we reject the null hypothesis and accept the alternative. The findings concurred with those in Ndonye (2015); Njeru et al. (2016), who agree that credit extension practices are important in determining tradeoff between increase in sales and loss from uncollected debts. This implies that an increase in credit extension practices by 1 unit would result to increase in SMEs growth by 0.519 units.

**Table 4.16: Regression of Coefficients**

Variable	B	Std. Error	t	Sig.
(Constant)	1.798	0.137	13.097	0.000
Credit Extension Practices	0.519	0.039	13.449	0.000

$$\text{SMEs Growth} = 1.798 + 0.519 \text{ Credit Extension Practices}$$

#### **4.9 Accounts Receivable Collection Practices**

The study sought to establish the influence of customer collection practices on growth of SMEs in Kakamega County, Kenya. The study specifically investigated the following elements of customer collection practices; credit collection policy, prompt invoice and regular sending of statements, contact overdue accounts, use of ageing sheet, keeping accurate and timely records, use of collection agencies and use of average collection period technique.

**Table 4.17: Showing Relationship between Accounts AR Practices and Growth**

Statement	Never	Annual	Semi-An	Monthly	Always	mean
1. How often do you refer to a defined credit collection policy?.	6.90%	19.30%	15.70%	42.00%	6.10%	3.41
2. How often do you Invoice and send statement?	8.00%	24.60%	24.30%	31.90%	11.20%	3.14
3. Do you Contact overdue accounts holders?	7.40%	4.70%	16.20%	42.30%	19.50%	3.52
4. How often do you review collection timelines?	5.10%	10.30%	9.20%	58.50%	16.90%	3.72
5. How often do you use ageing sheet and make constant follow up?	6.60%	17.60%	27.20%	38.20%	10.30%	3.28
6. How often do you call customers prior to due date?	5.80%	21.90%	13.50%	43.40%	15.30%	3.41
7. How often do you use collection agencies?	4.80%	6.70%	9.60%	34.40%	44.40%	4.07
8. How often do you use collection agencies?.	13.10%	32.80%	18.20%	26.60%	9.10%	2.86
9. Do you use average collection period technique	5.50%	24.40%	25.80%	33.50%	10.90%	3.20
<b>Average</b>						<b>3.29</b>

Source: Field data 2016

Results in Table 4.17 show that 58.1% of the respondents indicated that there is a defined credit collection policy, 43.1% of the respondents also agreed that they invoice promptly and send statement regularly while 61.8% of the respondents agreed that they contact overdue accounts more frequently. Results also revealed that 75.4% of the respondents agreed that they review set collection timelines and penalize those who pay late, 48.5% of the respondents agreed that they used ageing sheet and make constant follow up 58.7% of the respondents agreed that they call customers prior to

due date while 78.8% of the respondents agreed that they review and kept timely records.

Further, results in Table 4.17 reveal disagreed that they used collection agencies while 44.4% of the respondents agreed that they used average collection period technique. The results show good practice of the AR collection practices. This can be supported by the mean of the responses (3.29) which means that majority of the respondents were agreeing to the statements in the questionnaire. Table 4.17 demonstrates 5.10 % percent of respondents never review set collection timelines, while 10.30 % do it annually.9.20% semiannually while58.50 % monthly while 16.90% always carried out the practice. Table 4.17 demonstrates 6.60 % percent of respondents never use ageing sheets showing, while 17.60 % only once a year 27.20 % twice a year. 38.20 % use them monthly while 10.30% always. This finding suggests that having an ageing sheet is not often practiced by SMEs in Kakamega County, only about 48% of SMEs studied had ageing sheet. Many seem not to have information about ageing sheet.

#### **4.9.1 Debt Collection Policy**

The study determined that SMEs have a defined debt collection policy. The findings concurred with those in Gitau (2014) who explains that it is important to set credit terms and payment arrangement, the period of repayments. The findings implied that the SMEs under study have a defined credit collection policy. The existence of a defined credit collection policy creates a good platform for the SMEs owners to follow up on the customers' in-case of default. This further indicated that the SMEs in Kakamega County have put in place effective credit collection practices which may have an implication on the growth of the SMEs.

#### **4.9.2 Prompt Invoice and Regular Sending of Statements**

The study showed that not all SMEs invoice promptly and sends statement regularly. Results in Table 4.17 reveal that less than 43.1% of the respondents agreed that they invoice promptly and send statement regularly while 32.6% of the respondents

disagreed that they invoice promptly and send statement regularly. Another 24.3% of the respondents were sent only twice a year.

The findings agreed with Connolly (2013), who found out many firms do not practice proper billing which adversely affected timely collection of payments from the customers. The findings implied that less than half of SMEs under study invoice their customers promptly and send statement regularly. Invoicing their customers promptly and sending statement regularly alerts the customer's on when to pay back the credit which is of advantage to the SMEs owners as this may reduce the default rate. This further indicated that not all the SMEs in Kakamega County have put in place effective credit collection practices which may have an implication on the growth of the SMEs.

#### **4.9.3 Contact Overdue Accounts**

The study indicated that most of the SMEs contact overdue accounts more frequently. The findings concurred with those in Mutwiri (2007) who ascertained that customers with overdue accounts were contacted and late payment charges made on these overdue accounts. The findings implied that the SMEs under study contact overdue accounts more frequently. Contacting overdue accounts more frequently helps to minimize the default rate as constant reminder yields good result ultimately. This further indicated that the SMEs in Kakamega County have put in place effective credit collection practices which may have an implication on the growth of the SMEs.

#### **4.9.4 Use of Ageing Sheet**

The table showed that only 48.5% of the SMEs use ageing sheet and make constant follow up 27.2% of the respondents do not. The findings concurred with those in Mukhoma (2014) who agrees that the aging of accounts receivables enables the management appraise its credit and collection policies and this hence minimizes possible problems. The findings implied that at least there are SMEs that use ageing sheet and make constant follow up. Use ageing sheet and making constant follow up helps the SMEs owners to ensure that they remind all the customers who have debts which in return increases the credit repayment rate. This further indicated that a

reasonable number of SMEs in Kakamega County have put in place effective credit collection practices which may have an implication on the growth of the SMEs.

#### **4.9.5 Accurate and Timely Records**

The study sought to determine whether SMEs keep accurate and timely records. Results in Table 4.17 reveal that 78.8% of the respondents agreed that they review and keep accurate and timely records while 11.5% of the respondents do not review and keep accurate and timely records. Another 9.6% of the respondents were undecided. The findings implied that the SMEs under study keep accurate and timely records. The practice of keeping accurate and timely records helps the SMEs owners to avoid errors which could result to losses. This further indicated that the SMEs in Kakamega County have put in place effective credit collection practices which may have an implication on the growth of the SMEs.

#### **4.9.6 Use of Collection Agencies**

The findings disagreed with those in Mutwiri (2007) that demonstrated that firms use collection agencies (73.7%). The findings implied that only a few SMEs under study use collection agencies. Use of collection agencies helps the SMEs owners to follow up on customers who have declined to pay back their debts even after reminding them constantly and giving them ample time to repay back even after their credit is long overdue.

#### **4.9.7 Use of Average Collection Period Technique**

The study sought to determine whether SMEs use average collection period technique. Results in Table 4.17 reveal that 44.4% of the respondents agreed that they use average collection period technique while 29.9% of the respondents disagreed that they use average collection period technique. Another 25.8% of the respondents were undecided.

The findings concurred with those in Graham et al, (2010) who agrees that use of average collection period aids a firm to determine how long it takes a customer to pay

his/her dues. The findings implied that less than half of the SMEs under study use average collection period technique. The practice of using average collection period technique gives the customers enough time and flexibility to repay their loans which in-turn helps to reduce on default rates. This is an indicator that not very many SMEs in Kakamega County have put in place effective credit collection practices which may have an implication on the growth of the SMEs.

#### **4.9.8 Bivariate Regression Showing Relationship between Accounts Receivable Collection Practices and Growth**

Regression analysis was used to find out if there is a relationship between credit collection practices and SMEs growth by evaluating the contribution of the credit collection practices in explaining SMEs growth, when the other variables are controlled; the R Square value was obtained in this case. From the results in Table 4.18, credit collection practices were found to have an R Square value of 0.578 or to contribute to 57.8% SME growth. The R square value is an important indicator of the predictive accuracy of the equation. The remaining 42.2% can be explained by other factors. The implication of these finding is that credit collection practices plays a significant role enhancing SME growth.

**Table 4.18: Model Fitness**

<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Std. Error of the Estimate</b>
0.761	0.579	0.578	0.38889

Table 4.19 provides the results on the analysis of the variance (ANOVA). The results indicate that the overall model was statistically significant. Further, the results imply that credit collection practices are good predictors of SMEs growth. This was supported by an F statistic of 377.581 and the reported p value (0.000) which was less than the conventional probability of 0.05 significance level.

**Table 4.19: Analysis of Variance**

<b>Indicator</b>	<b>Sum of Squares</b>	<b>df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
Regression	57.103	1	57.103	377.581	0.000
Residual	41.438	274	0.151		
Total	98.541	275			

Regression of coefficients results in Table 4.20 shows that there is a positive and significant relationship between credit collection practices and SMEs growth as supported by a p value of 0.000 and a beta coefficient of 0.296. This was also supported by the t values whereby  $t_{cal}=50.75 > t_{critical}=12.706$  at a 95 percent confidence level which depicts that we reject the null hypothesis and accept the alternative. The findings concurred with those of Pandey (2008), an indication that collection practice adopted influences growth of SMEs. This implies that an increase in credit collection practices by 1 unit would result to increase in SMEs growth by 0.296 units. However contrary to the study findings, Wanyama (2014) in their study on Effects of bookkeeping Management Practices show that most of the MSBES in Bungoma District did not practice accounts receivable management which negatively affect business performance. This results concur with Oware, Samanhyia and Ampong

(2015), who demonstrated that when a firm does not invest well in the collection of account receivable then the debt accumulation will decrease profits.

**Table 4.20: Regression of Coefficients**

<b>Variable</b>	<b>B</b>	<b>Std. Error</b>	<b>t</b>	<b>Sig.</b>
(Constant)	2.684	0.053	50.75	0.000
Accounts Receivable Collection Practices	0.296	0.015	19.431	0.000

$$\text{SMEs Growth} = 2.684 + 0.296 \text{ Credit Collection Practices}$$

#### **4.10 Accounts Receivable Risk Assessment Practices**

The study sought to establish the influence of customer risk assessment practices on growth of SMEs in Kakamega County, Kenya. The study specifically investigated the following elements of Accounts Receivable Risk Assessment Practices; use of expert systems, use of credit scoring models, and internal rating system as shown in table 4.21

**Table 4.21: Accounts Receivable Risk Assessment Practices**

<b>Statement</b>	<b>very low</b>	<b>low</b>	<b>Average</b>	<b>high</b>	<b>Very high</b>	<b>Mean</b>
1. How often do you make use of Expert Systems?	11.30%	28.10%	16.40%	32.80%	11.30%	3.05
2. How often do you make use of Credit Scoring Models?	13.40%	23.20%	30.40%	24.30%	8.70%	2.92
3. How often do you make use of Internal Rating Systems?	7.00%	21.90%	14.80%	44.10%	12.20%	3.33
<b>Average</b>						<b>3.58</b>

Source: Field Data 2016



The study sought to determine the influence of Accounts Receivable Risk Assessment Practices on Growth of SMEs. Results in Table 4.21 show that 44.1% of the respondents indicated that they used expert systems, 36.6% of the respondents also rarely used credit scoring models while 56.3% of the respondents agreed that they used internal rating systems. Table 4.21 demonstrates over 50% of respondents rarely use credit scoring models, This finding suggests that use of credit scoring models are not practiced by SMEs in Kakamega County very few agreed to using credit scoring model and reason could be that majority have no knowledge on this practice and it is a new idea. The major objective of credit scoring model is to ensure that only good clients are retained.

Table 4.21 demonstrates over 55% percent of respondents rarely use of Expert system, while only 11.30% occasionally use it. This finding suggests that use of expert systems is moderately practiced by majority of the SMEs in Kakamega County. On average(54%) agreed to using expert systems, reason could be that there are SME owner who have formal education and are enlightened on this practice. This is indeed good move because expert system is good as it helps a firm make informed decisions as whether to extend credit to customers or not .

#### **4.10.1 Use of Credit Scoring Models**

The findings disagreed with Moti et.al. (2012) who found a significant relationship between credit rating and performance of a firm. The findings implied that only few SMEs under study use credit scoring models. This implies that most of the SMEs in Kakamega County use other methods to determine the credit worthiness of their customers other than credit scoring.

#### **4.10.2 Internal Rating System**

The findings concurred with those in Ikuu (2015) who said there is a significant relationship between internal credit rating and performance of a firm. The findings implied that the SMEs under study have internal rating systems. Use of these systems helps the SMEs owners to avoid the moral hazard problem. This further indicated that

the SMEs in Kakamega County have put in place effective credit risk assessment practices which may have an implication on the growth of the SMEs.

#### **4.10.3 Bivariate Regression Showing Relationship between Accounts Receivable Risk Assessment Practices and Growth**

Regression analysis was used to find out if there is a relationship between Accounts Receivable Risk Assessment Practices and SMEs growth by evaluating the contribution of the Account risk assessment practices in explaining SMEs growth, when the other variables are controlled; the R Square value was obtained in this case. From the results in Table 4.22, ARRAP were found to have an R Square value of 0.528 or to contribute to 52.8% SME growth. The R square value is an important indicator of the predictive accuracy of the equation. The remaining 47.2% can be explained by other factors. The implication of these finding is that Accounts Receivable Risk Assessment Practices plays a significant role enhancing SME growth.

**Table 4.22: Model Fitness**

<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Std. Error of the Estimate</b>
0.726	0.528	0.526	0.4122

Table 4.23 provides the results on the analysis of the variance (ANOVA). The results indicate that the overall model was statistically significant. Further, the results imply that credit risk assessment practices are good predictors of SMEs growth. This was supported by an F statistic of 305.985 and the reported p value (0.000) which was less than the conventional probability of 0.05 significance level.

**Table 4.23: Analysis of Variance**

<b>Indicator</b>	<b>Sum of Squares</b>	<b>df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
Regression	51.985	1	51.985	305.954	0.000
Residual	46.556	274	0.17		
Total	98.541	275			

Regression of coefficients results in Table 4.24 shows that there is a positive and significant relationship between credit risk assessment practices and SMEs growth as supported by a p value of 0.000 and a beta coefficient of 0.277. This was also supported by the t values whereby  $t_{cal}=49.249 > t_{critical}=12.706$  at a 95 percent confidence level which depicts that we reject the null hypothesis and accept the alternative. The findings concurred with those in Owonde (2013) posits that maintaining close links with their customers activities either through expert systems, internal rating or credit scoring help in monitoring business activities of the customers and this may raise the red flag for management to take action before a debt can go bad and inhibit profits. Maria (2014) concurs that when sales are on credit, a monitoring system is important to avoid the potential build of excessive levels of accounts receivable which would erode set profits. The study equally agree with Njagi (2016) who analyzed effect of the risk management practices on the performance of hotels in Mombasa. It was observed that majority of hotels did not have a risk management policy which apparently affected their performance.

**Table 4.24: Regression of Coefficients**

<b>Variable</b>	<b>B</b>	<b>Std. Error</b>	<b>t</b>	<b>Sig.</b>
(Constant)	2.736	0.056	49.249	0.000
Acc. R Risk Assessment Practice	0.277	0.016	17.492	0.000

$$\text{SMEs Growth} = 2.736 + 0.277 \text{ Credit Risk Assessment Practice}$$

This implies that an increase in credit risk assessment practices by 1 unit would results to increase in SMEs growth by 0.277 units.

#### **4.11 Accounts Receivable Financing Practices**

The study sought to assess the influence of financing practices on growth of SMEs. The study specifically investigated the following elements of financing practices; regular discount/sale of overdue invoices, use of accounts receivable as collateral for a loan, securitization of accounts receivables and factoring accounts receivables.

**Table 4.25: Showing Accounts Receivable Financing Practices**

<b>Statement</b>	<b>never</b>	<b>Annual</b>	<b>Semi Ann</b>	<b>Monthly</b>	<b>Always</b>	<b>Mean</b>
1. do you discount/sell overdue invoices	12.30%	22.10%	27.50%	30.10%	8.00%	2.99
2. Use of account receivable as collateral for a loan.	8.30%	19.20%	14.50%	47.50%	10.50%	3.33
3. Factoring accounts Receivables.	10.10%	18.80%	19.60%	38.80%	12.70%	3.25
<b>Average</b>						<b>3.23</b>

Source: Field data 2016

The study sought to assess the influence of financing practices on growth of SMEs. Results in Table 4.25 show that 38.1% of the respondents indicated that they discounted/sold overdue invoices regularly while 58% of the respondents agreed that they used accounts receivable as collateral for a loan. Results also revealed that 56.7% of the respondents agreed that they securitized accounts receivables while 51.5% of the respondents agreed that they factored accounts receivables. The results show good financing practices as confirmed by the mean of the responses (3.23) which means that majority of the respondents were agreeing to the statements in the questionnaire.

Table 4.25 demonstrates 9.5 % percent of respondents never discount overdue invoices, while 16.4 percent discount annually 17.5 % discount twice a year and 42.90% monthly while 13.80% always when they are in need of cash. This finding suggests that discounting overdue invoices is commonly practiced by SMEs in Kakamega County majority of the SMEs studied about (56 %) agreed to discounting invoices .and reason could be that majority have formal education and are enlightened. The major objective of discounting invoices is to ensure that that money is not tied up in invoices or remain idle for a long time. Table 4.25 demonstrates 3.6% percent of respondents strongly disagree to using accounts receivable as collateral,

while 8.3% percent disagree 19.2% were undecided as to whether they use or not and 47.5% agreed while 10.5% strongly agree This finding suggests that having a use of accounts receivable as collateral for loans is strongly practiced by SMEs in Kakamega County. Majority of the SMEs studied about (58%) agreed to use AR as collateral,)

Table 4.25 This finding suggests that Factoring accounts receivable is not a common practice among SMEs in Kakamega County. Majority of the SMEs studied about (78.1 %) rarely use factoring and reason could be that majority have do not have sufficient level of financial literacy in this area. This is meant majority do not understand factoring.

#### **4.11.1 Discounting overdue invoices**

The study sought to determine whether SMEs regularly discount/sell overdue invoices. Results in Table 4.25 reveal that majority of the respondents regularly discount/sell overdue invoices the findings implied that the SMEs under study do regularly discount/sell overdue invoices. Failure to regularly discount/sell overdue invoices may result to an increase in the volume of bad debts which in return dampens the SMEs growth. This study agree with (Waweru, 2013)

#### **4.11.2 Use of Accounts Receivable as Collateral for a Loan**

The study sought to determine whether SMEs use accounts receivable as collateral for a loan. Results in Table 4.25 reveal that 58% of the respondents agreed that they use accounts receivable as collateral for a loan while 27.5% of the respondents disagreed that they use accounts receivable as collateral for a loan. Further 14.5% of the respondents occasionally or even do not use. The findings concurred with those in Njeru et al. (2016). The findings implied that the SMEs under study use accounts receivable as collateral for a loan. When Banks allow customers to use accounts receivable as collateral for a loan helps the SMEs to increase their performance as more customers as able to access loans to grow their businesses. This is also an indicator that the SMEs in Kakamega County have put in place effective financing practices which may have an implication on the growth of the SMEs. If a company is also using its accounts receivable as collateral for a loan, the lending institution will

generally exclude any past due accounts from those used as back up for the credit line (Waweru, 2013)

#### **4.11.3 Securitization of Accounts Receivables**

The study sought to determine whether SMEs securitize accounts receivables. Results in Table 4.25 reveal that 56.7% of the respondents agreed that they securitize accounts receivables while 25.9% of the respondents disagreed that they securitize accounts receivables. Further 17.5% of the respondents were undecided. The findings concurred with those in Palia and Sopranzetti. (2004) who argued that securitization is becoming a more acceptable way of financing SMEs which are starved of external financing. The findings implied that most of the SMEs under study securitize accounts receivables. This helps to convert its accounts receivable into cash or an investment instrument which increases the SMEs capital base. An increase in the capital base may result to increased productivity and thus improved SME growth.

#### **4.11.4 Factoring Accounts Receivables**

The study sought to determine whether SMEs factor accounts receivables. Results in Table 4.25 reveal that 51.5% of the respondents agreed that they factor accounts receivables while 28.9% of the respondents disagreed that they factor accounts receivables. Further 19.6% of the respondents were undecided. The findings concurred with those in Blayney (2006); Mutwiri, (2007) they agree with the study that most SMEs are now using factoring. The findings implied that the SMEs under study factor accounts receivables. This is of great significance to the SMEs owners as they are able to access their cash more quickly than it would by waiting for many days for a customer payment. This is an indicator that the SMEs in Kakamega County have put in place effective financing practices which may have an implication on the growth of the SMEs. This supports Asselbergh (2002) who described Factoring as an alternative mean of finance.

### 4.11.3 Bivariate Regression Showing Relationship between Accounts Receivable Financing Practices and Growth

Regression analysis was used to find out if there is a relationship between financing practices and SMEs growth by evaluating the contribution of the financing practices in explaining SMEs growth, when the other variables are controlled; the R Square value was obtained in this case. From the results in Table 4.26, financing practices were found to have an R Square value of 0.1 or to contribute to 1% SME growth. The R square value is an important indicator of the predictive accuracy of the equation. The remaining 99% can be explained by other factors. The implication of these finding is that financing practices do not play a significant role enhancing SME growth.

**Table 4.26: Model Fitness**

<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Std. Error of the Estimate</b>
0.322	0.104	0.1	0.56776

Table 4.27 provides the results on the analysis of the variance (ANOVA). The results indicate that the overall model was statistically significant. Further, the results imply that financing practices are good predictors of SMEs growth. This was supported by an F statistic of 31.692 and the reported p value (0.000) which was less than the conventional probability of 0.05 significance level.

**Table 4.27: Analysis of Variance**

<b>Indicator</b>	<b>Sum of Squares</b>	<b>df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
Regression	10.216	1	10.216	31.692	0.000
Residual	88.325	274	0.322		
Total	98.541	275			

Regression of coefficients results in Table 4.28 shows that there is a positive and significant relationship between financing practices and SMEs growth as supported by a p value of 0.000 and a beta coefficient of 0.04. This was also supported by the t values whereby  $t_{cal}=24.134 > t_{critical} =12.706$  at a 95 percent confidence level which depicts that we reject the null hypothesis and accept the alternative. The findings concurred with those in Mutwiri (2007) who illustrated that respondents agreed that they engaged in invoice discounting and factoring use of accounts receivables as collateral due to provision of finance, this implies that an increase in financing practices by 1 unit would result to increase in SMEs growth by 0.204 units.

**Table 4.28: Regression of Coefficients**

<b>Variable</b>	<b>B</b>	<b>Std. Error</b>	<b>t</b>	<b>Sig.</b>
(Constant)	2.946	0.122	24.134	0.000
Financing Practices	0.204	0.036	5.63	0.000

$$\text{SMEs Growth} = 2.946 + 0.204 \text{ Accounts Receivable Risk Assessment Practice}$$

#### **4.12 Moderating effect of Financial Literacy on Accounts Receivable Management Practices**

The study sought to assess the financial literacy of the respondents. The study specifically investigated the following elements of financial literacy; financing of receivable options available, credit monitoring methods, computation of discounts, computation of financial ratios, credit analysis methods and credit collection methods.



**Table 4.29: Showing moderating effect of Financial Literacy**

<b>Statement</b>	<b>Very low</b>	<b>Low</b>	<b>Average</b>	<b>high</b>	<b>Very High</b>	<b>Mean</b>
1. Financing of receivable options available.	6.50%	20.30%	50.00%	18.50%	4.70%	2.95
2. Credit monitoring methods.	6.50%	12.30%	36.60%	33.70%	10.90%	3.30
3. Computations of discounts.	12.70%	16.70%	34.80%	25.70%	10.10%	3.04
4. Computation of financial ratios.	15.30%	22.90%	36.70%	20.40%	4.70%	2.76
5. AR analysis methods.	9.50%	27.50%	35.90%	17.60%	9.50%	2.90
6. AR collection methods.	1.80%	12.30%	41.70%	29.70%	14.50%	3.43
<b>Average</b>						<b>3.06</b>

Source: Field data 2016

The study sought to assess the financial literacy of the respondents. The study specifically investigated the following elements of financial literacy; financing of receivable options available, credit monitoring methods, computation of discounts, computation of financial ratios, credit analysis methods and credit collection methods.

#### **4.12.1 Options for Financing Receivables**

The study sought to determine whether SMEs have the knowledge on options of financing receivables available. Results in Table 4.29 reveal that 50% of the respondents have sufficient knowledge. The results also revealed that about 26.8% of the respondent's very low level of financial literacy on options of financing receivables available. The findings implied that the SMEs under study do not have the options of financing receivables. Lack of this form of financial literacy limits by the SMEs owners limits their customers from accessing credit more than what is available. This would dampen their growth as they would not make to meet all needs of their customers.

#### **4.12.2 AR Monitoring Methods**

The study sought to determine whether SMEs have information on credit monitoring methods. Results in Table 4.29 reveal that 44.6% of the respondents agreed that they have knowledge on credit monitoring methods while 18.8% of the respondents have low level of financial literacy on credit monitoring methods. The results also revealed that 36.6% of the respondents were Average. The findings implied that the SMEs under study used credit monitoring methods. Use of credit monitoring methods would help the SMEs to identify customers' who have the ability to pay back credit and thus avoid the risk of advancing credit to risky customers.

#### **4.12.3 Computations of Discounts**

The study sought to determine whether SMEs compute discounts. Results in Table 4.29 reveal that 35.8% of the respondents agreed that they know how to compute discounts while 29.4% of the respondents occasionally compute discounts. The results also revealed that 34.8% of the respondents rarely. The findings implied that the some of the SMEs under study compute discounts. Computation of discount is a practice which would enable the SMEs owners retain their customers as well as attract new customers. Use of this knowledge can help SMEs improve their growth.

#### **4.12.4 Computation of Financial Ratios**

The study sought to determine whether SMEs compute financial ratios. Results in Table 4.29 reveal that 38.2% of the respondents disagreed that they compute financial ratios while 36.7% of the respondents were undecided. The results also revealed that 25.1% of the respondents disagreed that they compute financial ratios. The findings implied that the most of the SMEs under study do not compute financial ratios. Failure to compute financial rations is risky as the SMEs owners are not informed of their status in-terms of profitability. Lack of knowledge on the importance of computing financial ratios can result to poor decision making which could dampen the growth of the SMEs

#### **4.12.5 AR Analysis Methods**

The study sought to determine whether SMEs use credit analysis methods. Results in Table 4.29 reveal that over 60% of the respondents have knowledge on credit analysis methods while 35.9% of the respondents don't. The results also revealed that 27.1% of the respondents have minimum know how on credit analysis methods. The findings implied that the most of the SMEs under study do not use credit analysis methods. This further indicated that the SMEs owners in Kakamega County are not financial literate which may have a negative impact on the growth of the SMEs.

#### **4.12.6 AR Collection Methods**

The study sought to determine whether SMEs use credit collection methods. Results in Table 4.29 reveal that over 44.2% of the respondents have knowledge on credit collection methods while less 41.7% of the respondents had low financial literacy level. The findings implied that the most of the SMEs under study use credit collection methods to some extent. Financial literacy on the use of credit collection methods can help the SMEs owners avoid uncollectible debts which would impact their growth positively.

#### **4.13 Small and Medium Enterprises (SMEs) Growth**

The study sought to access the growth of SMEs. The study specifically investigated the following elements of SMEs growth; increased sales, decrease in total current asset, the business percentage of bad and delinquent debts, profits for the last three years, fees paid to collection agencies.

**Table 4.30: Showing SMEs Growth**

<b>Statement</b>	<b>S.D</b>	<b>D</b>	<b>U</b>	<b>A</b>	<b>S.A</b>	<b>M</b>
1. Sales have increased over the last three years.	0.80%	4.60%	9.50 %	64.10%	21.00%	4.00
2. The total current asset represented by accounts receivable has gone down.	4.80%	34.70%	18.50%	29.20%	12.90%	3.11
3. The business percentage of bad and delinquent debts is less than 10% of sales.	4.00%	19.30%	32.00%	33.80%	10.90%	3.28
4. The business has been able to generate profits for the last three years.	1.80%	3.60%	7.20%	58.00%	29.30%	4.09
5. Fees paid to collection agencies have reduced.	15.80%	27.60%	15.10%	28.30%	13.20%	2.95
<b>Average</b>						<b>2.95</b>

S.D-Strongly Disagree, D- Disagree, U- Undecided, A- Agree, A.A- Strongly Agree, M- Mean

Source: Field data 2016

#### **4.12.1 Increased Sales**

The study sought to determine whether SMEs in Kakamega County have experienced increase sales. Results in Table 4.30 reveal that 85.1% of the respondents agreed that they have experienced increase sales while 9.5% of the respondents were undecided. The results also revealed that 5.4% of the respondents disagreed that they have experienced increase sales. The findings reveal that most of the SMEs under study have experienced increase sales. This is an indicator that SMEs in Kakamega County

are experiencing growth which is an implication that use of account receivable management practices improves the growth of the SMEs in Kakamega County.

#### **4.12.2 Decrease in Total Current Asset**

The study sought to determine whether SMEs in Kakamega County have experienced a decrease in total current assets. Results in Table 4.30 reveal that 42.1% of the respondents agreed that they have experienced a decrease in total current assets while 38.5% of the respondents disagreed that they have experienced a decrease in total current assets. The results also revealed that 18.5% of the respondents were undecided. The findings implied that the most of the SMEs under study have experienced a decrease in total current assets. This is an indicator that use of account receivable management practices improves the growth of the SMEs in Kakamega County.

#### **4.12.3 Business Percentage of Bad and Delinquent Debts**

The study sought to determine whether the business percentage of bad and delinquent debts for SMEs in Kakamega County is less than 10% of sales. Results in Table 4.30 reveal that 44.7% of the respondents agreed that their business percentage of bad and delinquent debts is less than 10% of sales while 32% of the respondents were undecided. The results also revealed that 23.3% of the respondents disagreed that their business percentage of bad and delinquent debts is less than 10% of sales. The findings implied that the business percentage of bad and delinquent debts for most of the SMEs in Kakamega County is less than 10% of sales. The low percentage of bad and delinquent debts is an indicator that use of account receivable management practices improves the growth of the SMEs in Kakamega County.

#### **4.12.4 Profits for the Last Three Years**

The study sought to determine whether the business for SMEs in Kakamega County has been able to generate profits for the last three years. Results in Table 4.30 reveal that 87.3% of the respondents agreed that their business has been able to generate profits for the last three years while 72% of the respondents were undecided. The

results also revealed that 5.4% of the respondents disagreed that their business has been able to generate profits for the last three years. The findings implied that the business for most SMEs in Kakamega County has been able to generate profits for the last three years. Continuous profitability is an indicator that SMEs in Kakamega County are experiencing growth.

#### **4.12.5 Fees Paid to Collection Agencies**

The study sought to determine whether the fees paid to collection agencies for SMEs in Kakamega County has reduced. Results in Table 4.30 reveal that 43.4% of the respondents disagreed that the fees paid to collection agencies has reduced while 41.5% of the respondents agreed that the fees paid to collection agencies has reduced. The results also revealed that 15.1% of the respondents were undecided. The findings implied that the fees paid to collection agencies for most SMEs in Kakamega County have not reduced. This is an indicator that the default rate is still high which calls for the extreme action of using collection agents. Existence of a fees paid to collection agencies by SMEs in Kakamega County could be dampening their growth.

#### **4.13 Knowledge of ARM Practice**

The study found out that 46.1% of the respondents were aware and practiced the ARM practices in their businesses. The study also found out that 35.4% of the respondents were aware but did not practice ARM in their businesses. Further, results revealed that 18.5% of the respondents were not aware and so did not practice as shown in table 4.31.

**Table 4. 31: Knowledge of ARM Practice**

	<b>Knowledge of ARM Practices</b>	<b>Frequency</b>	<b>Percent</b>
1.	Know and practice	112	46.1
2.	Know but do not practice	86	35.4
3.	No knowledge	45	18.5
	<b>Total</b>	<b>243</b>	<b>100</b>

**Source: Field data, 2016**

In a study to investigate the effect of business development services on the performance of Small Scale enterprises in Kisii Town Osinde *et al.* (2013) found out that entrepreneur who attended the training services recorded an improvement in their businesses in terms of growth in sales and profits with 83.3% of the respondents who always attended training reporting to have good growth in profits as opposed to only 41.2% of those who never attended training. The implication of the results is that most of the SMEs owners are aware and practice ARM in their businesses. This can be attributed to improved SME growth and secondly that most of the SMEs owners have formal education.

#### **4.14 Correlations**

Pearson correlation coefficient ( $r$ ) was used to determine the degree or strength of linear relationship among the variables. Linearity increases the predictive power of the model and the validity of the estimated coefficients. A correlation of  $r > \pm 0.7$  implies that the variables are strongly related either positively or negatively. The study sought to determine the correlation between the variables in order to determine the strength of the relationship at 5% significance level. A summary of the correlation coefficients and significance level for all the variables is shown in Table 4.32

**Table 4.32 Correlation**

<b>Growth</b>	<b>ARAP</b>	<b>AREP</b>	<b>ARCP</b>	<b>ARRAP</b>	<b>ARFP</b>	<b>ARFL</b>
<b>Growth</b>	1.000					
<b>ARAP</b>	0.247*	1.000				
<b>AREP</b>	0.222*	0.604*	1.000			
<b>ARCP</b>	0.255*	0.575*	0.592*	1.000		
<b>ARRAP</b>	0.348*	0.521*	0.470*	0.677*	1.000	
<b>ARFP</b>	0.271*	0.522*	0.253*	0.559*	0.575*	1.000

*\*correlations significant at 0.05 level of sig*

#### **4.14.1. Correlation between Accounts Receivable Analysis Practice and Growth**

Pearson correlation was used to determine the relationship between Accounts receivable analysis and SME growth. The correlation coefficient was 0.247 with p-value (0.000) which was found to be significant at 5% significance level suggesting the existence of a moderate positive relationship between Accounts receivable analysis and SME growth, implying that the more often the practice is used the higher would be the growth.

#### **4.14.2 Correlation between Accounts Receivable Extension Practice and Growth**

Pearson correlation was used to determine the relationship between Accounts receivable analysis and SME growth. The correlation coefficient was 0.222 with p-value (0.000) which was found to be significant at 5% significance level suggesting the existence of a positive relationship between Accounts receivable extension and SME growth, implying that the frequent use of this practice the higher would be the growth.

#### **4.14.3 Correlation between Accounts Receivable Collection Practice and Growth**

Pearson correlation was used to determine the relationship between Accounts receivable analysis and SME growth. The correlation coefficient was 0.255 with p-value (0.000) which was found to be significant at 5% significance level suggesting



the existence of a positive relationship between Accounts receivable collection and SME growth, implying that the frequent use of this practice the higher would be the growth

#### **4.14.4. Correlation between Accounts Receivable Risk Assessment Practice and Growth**

Pearson correlation was used to determine the relationship between Accounts receivable analysis and SME growth. The correlation coefficient was 0.348 with p-value (0.000) which was found to be significant at 5% significance level suggesting the existence of a positive relationship between Accounts receivable extension and SME growth, implying that the frequent use of this practice the higher would be the growth

#### **4.14.5. Correlation between Growth Receivable Financing Practice and Growth**

Pearson correlation was used to determine the relationship between Accounts receivable analysis and SME growth. The correlation coefficient was 0.271 with p-value (0.000) which was found to be significant at 5% significance level suggesting the existence of a positive relationship between Accounts receivable extension and SME growth, implying that the frequent use of this practice the higher would be the growth.

### **4.15 Homoscedasticity**

The assumption of homoscedasticity is essential to linear regression models. Homoscedasticity explains a situation where the error term is the same across all of the independent variables' values. On the other hand, heteroscedasticity appears when the size of the error term is different across all of the independent variables' values. The effect of violating the assumption of homoscedasticity is a matter of degree, increasing as heteroscedasticity increases (Andreas, 2007). In regression analysis, heteroscedasticity means a condition in which the variance of dependent variable varies across the data. On the other hand homoscedasticity means a situation which the variance of the dependent variable is the same for all the data. According to

Deloof (2009), homoscedasticity describes the consistency of variance of the error term ( $e$ , residual) at different levels of the predictor variable. Smith (2010) explains homoscedasticity in terms of the standard error estimate (of the regression line). The standard error of estimate is an index of the variance of measured values around each predicted value. The homoscedasticity assumption more formally stated as  $VAR(e_j) = c$  that is, the variance of the error of residual term of each point  $j$  is equal to the variance for all residuals. The Gauss-Markov theorem states that when all the methodological assumptions are met, the least squares estimator regression parameters are unbiased and efficient, that is, the least square estimators said to be BUE: Best linear Unbiased Estimators (Horne & Wachowicz, 2010).

#### **4.16 Multicollinearity**

Multi-collinearity was used to test correlation between the independent variables. The presence of multicollinearity makes it difficult to isolate the impact of each independent variable on the dependent variable and also standard errors for each independent variable become inflated (Landau & Everett, 2004). Multicollinearity can be corrected by excluding one or more of the corrected by excluding one or more of the correlated independent variable from the regression model (Lind, Marchal, & Wathen, 2008). To check for multicollinearity Variance inflation Factor and Tolerance level were used. A VIF of less than 10 or a tolerance level of greater than 0.1 is acceptable. A summary of multicollinearity statistics is shown in Table 4.33.

**Table 4.33: Collinearity Diagnostics**

<b>Independent variable</b>	<b>Tolerance</b>	<b>VIF</b>
Accounts Receivable analysis practice	0.799	1.252
Accounts receivable extension practice	0.735	1.361
Accounts receivable collection practices	0.658	1.519
Accounts receivable risk assessment practice	0.630	1.587
Accounts receivable financing practice	0.815	1.226

Source: Field data, 2016

Accounts receivable risk assessment practices had the lowest tolerance level of 0.630. The tolerance level for all the independent variables was greater than 0.1 which suggests the absence of multi-collinearity problem. Accounts receivable risk assessment had the highest VIF of 1.587 and accounts receivable financing had the lowest VIF of 1.226, the VIF for all the variables was less than 10 hence this suggests there is no multi-collinearity among the independent variables. The rule of thumb was applied in the interpretation of the variance inflation factor. From table 4.33, the VIF for all the estimated parameters was found to be less than 4 which indicate the absence of multi-Collinearity among the independent factors. This implies that the variation contributed by each of the independent factors was significant independently and all the factors should be included in the prediction model.

#### **4.17 Moderating effect of Financial Literacy**

The sixth objective of the study was the moderating effect of financial literacy on the relationship between Accounts receivable management practices and growth. The moderation effect was tested using Ongore and Khisa (2013) approach. Each variable was interacted with the moderator and the model took the following estimation equation;

$$Y = \beta_0 + \beta_1 X_1 * M + \beta_2 X_2 * M + \beta_3 X_3 * M + \beta_4 X_4 * M + \beta_5 X_5 * M + \varepsilon$$

**Table 4.34: Multi-Linear Regression after Moderating.**

<b>Variable</b>	<b>B</b>	<b>Std. Error</b>	<b>t</b>	<b>Sig.</b>
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(Constant)	35.758	1.195	29.93	0.001
Account Receivable analysis and Financial literacy( $X_{1*} \cdot M$ )	0.001	0.006	2.123	0.009
Account Receivable Extension and Financial literacy( $X_{2*} \cdot M$ )	0.008	0.007	2.166	0.024
Account Receivable Collection and Financial literacy( $X_{3*} \cdot M$ )	0.003	0.005	3.586	0.005
Account Receivable risk assessment and Financial literacy( $X_{4*} \cdot M$ )	0.01	0.005	2.159	0.032
Account Receivable Financing Practices and Financial literacy( $X_{5*} \cdot M$ )	0.003	0.008	3.323	0.007
R square	=69.23			
F statistic,(p value)	=11.298(0.000)			

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$$Y = 35.758 + 0.001X_{1*} \cdot M + 0.008X_{2*} \cdot M + 0.003X_{3*} \cdot M + 0.01X_{4*} \cdot M + 0.003X_{5*} \cdot M$$

$R^2$  improved to 69.23% after moderation. Further the interaction terms of all the variables were significance since the calculated P values were less than the critical p value (0.05). Therefore the study concluded that financial literacy has a moderating effect on the relationship between Accounts receivable management practices and growth.

#### 4.18 Multi-Linear Regression Equation

Regression of coefficients results in Table 4.34 shows that there is a positive and significant relationship between Accounts Receivable Analysis Practices, Accounts Receivable Extension Practices, Accounts Receivable Collection Practices, and Accounts Receivable Risk Assessment Practices and SMEs growth. This was supported by a p value of 0.001, 0.009, 0.024, 0.005, 0.032 and 0.007 respectively. This was also supported by beta coefficients of 0.001, 0.008, 0.003, 0.01, and 0.003 respectively.

### Regression Equation

Ordinary least square regression equation was

$$Y = \beta_0 + \beta_1 X_{1*.M} + \beta_2 X_{2*.M} + \beta_3 X_{3*.M} + \beta_4 X_{4*.M} + \beta_5 X_{5*.M} + \epsilon$$

$$Y = 35.758 + 0.001 X_{1*.M} + 0.008 X_{2*.M} + 0.003 X_{3*.M} + 0.01 X_{4*.M} + 0.003 X_{5*.M}$$

From the above regression equation while moderating by financial literacy, it was revealed that holding accounts analysis practice, Accounts receivable extension practices, Accounts receivable collection practices, Accounts receivable risk assessment practices, Accounts receivable financing practices to a constant zero, SME growth would be 35.758, a unit increase in ARAP would lead to increase in SME growth in Kakamega County by a factor of 0.001, a unit increase in AREP would lead to increase SME growth in Kakamega County by a factor of 0.008, unit increase in ARCP would lead to increase in SME growth by a factor of 0.003, unit increase in ARRAP would lead to increase in SME growth by a factor of 0.003, and lastly unit increase in ARFP would lead to increase in SME growth by a factor of 0.01 and unit increase in Financial literacy level on ARMP would lead to an increase in growth by a factor of 0.003. The study also found that all the p-values were less than 0.05, an indication that all the variables were statistically significant in influencing SME growth when financial literacy is used as a moderating variable in Kakamega County.

**Table 4.35: Model Fitness**

<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Std. Error of the Estimate</b>
0.714	0.692	0.581	0.433

Regression analysis was used to find out if there is a relationship between ARM practices and SMEs growth by evaluating the contribution of the ARM practices in explaining SMEs growth, when the other variables are controlled; the R Square value

was obtained in this case. Adjusted R squared is coefficient of determination which tells us the variation in the dependent variables due to change in the independent variables. R is the correlation coefficient which shows the relationship between the study variables when financial literacy comes in as an interactive variable. From the findings shown in table 4.35 there was a strongly positive relationship between the study variables as shown by 0.714. From the results in Table 4.35, ARM practices were found to have an R Square value of 0.692 or to contribute to 69.2% SME growth.

The R square value is an important indicator of the predictive accuracy of the equation. The remaining 30.2% can be explained by other factors. The implication of these finding is that ARM practices plays a significant role enhancing SME growth. The results differ with that of Oluoch (2014) who postulated that ARM practices have no impact on SMEs success, Mathuva (2010) study of 30 firms listed in the Nairobi stock Exchange for the period 1993 to 2008 also found a negative relation of accounts receivable on profitability. Padachi (2006) found that high investment in inventories and receivables is associated with lower profitability, however the study agrees with (Mwangi, 2013). In his study of receivable management practices in CDF funded projects in Kenya, he concluded that the successful CDF funded projects embraced and implemented efficient receivable management practices and so their survival was eminent. The variations in the findings were expected as accounts receivable management varies from one context to the next and also the size of the firm. For the SMEs with different setting, such as, in Kakamega County that Accounts Receivable Management Practices may have a considerable effect on their growth and may lead to their closures. The study further concurs with Sabri (2015) indicating financial literacy level of the respondents affects performance of a firm.

#### **4.19. Test of Significance of Regression Coefficients**

In determining the cause effect relationship between the dependent variable and the explanatory variables the regression coefficients were tested at the 5% level of significance using t-test. The regression is presented in Table 4.36.

**Table 4.36: Regression of Coefficients**

<b>Variable</b>	<b>B</b>	<b>Std. Error</b>	<b>t</b>	<b>Sig.</b>
(Constant)	35.758	1.195	29.93	0.001
Account Receivable analysis and Financial literacy(X <sub>1</sub> *.M)	0.0127	0.006	2.123	0.009
Account Receivable Extension and Financial literacy(X <sub>2</sub> *.M)	0.0151	0.007	2.166	0.024
Account Receivable Collection and Financial literacy(X <sub>3</sub> *.M)	0.0179	0.005	3.586	0.005
Account Receivable risk assessment and Financial literacy(X <sub>4</sub> *.M)	0.0212	0.005	2.159	0.032
Account Receivable Financing Practices and Financial literacy(X <sub>5</sub> *.M)	0.0266	0.008	3.323	0.007

Source: Field data 2016

#### **4.19.1. The Effect of Accounts Receivable Analysis Practice on Growth**

The study sought to find out the effect of Accounts receivable analysis practice on growth of SMEs. In Table 4.36, the coefficient obtained from regression was 0.0127 with (p-value  $0.009 < 0.05$ ) thus the null hypothesis that use of Accounts receivable analysis practice has no significant effect on growth was rejected which leads to the conclusion that there is a statistically significant relationship between use of Accounts receivable analysis practice and SME growth. In this case ARAP has a positive effect on growth such that a unit increase in use of ARAP will result to a significant increase in profits by 0.0127 or 1%. This may be attributed to the fact that scrutiny of clients would mean owners selling on credit to only creditworthy customers. The study agrees with Rosemary Nduta (2011) on credit management of MFIs. Her study established that majority of the respondents agreed that Client

appraisal is a viable strategy for credit management as shown by a mean of 1.70, which is in agreement with (Kungu et al., 2016)

#### **4.19.2. The Effect of Accounts Receivable Extension Practice on Growth**

The study sought to find out the effect of Accounts receivable extension practices growth of SMEs. In Table 4.36, the coefficient obtained from regression was 0.0151 with (p-value  $0.024 < 0.05$ ) thus the null hypothesis that use of Accounts receivable extension practices has no significant effect on growth was rejected which leads to the conclusion that there is a statistically significant relationship between use of Accounts receivable extension practices and SME growth. In this case use accounts receivable extension practice has an effect on growth such that a unit increase in use of AREP will result to an increase in growth by 1.5%. These results agree with Waniku (2013), however it contradicts the findings by Kalunda et al. and that by Kwame (2008) which showed that small businesses always do not have written plans.

#### **4.19.3 The Effect of Accounts Receivable Collection Practice on Growth**

The study sought to find out the effect of Accounts receivable collection practices on growth of SMEs. In Table 4.36 the coefficient obtained was 0.0179 with (p-value  $0.005 < 0.05$ ) thus the null hypothesis that use of Accounts receivable collection practices has no significant effect on SME growth was rejected which leads to the conclusion that there is a statistically significant relationship between use of use Accounts receivable collection practices and SME growth. In this case use ARCP has positive effect on growth such that a unit increase in use of ARCP will result to an increase in growth by 2%. The implication of these finding is that credit collection practices plays a significant role enhancing SME growth which negates Uremadu *et al.* (2012) study that established a distorted and non-significant relationship of debtors collection period with the level of corporate profitability among quoted companies in Nigeria This, however agrees with the study carried out by Nyaga (2011).studied the relationship of AR management and performance of Learning institutions (TIVET), he concluded that there is a positive relationship between



collection policy and monitoring practices adopted and organization performance. This study is consistent with another study carried out by Kilonzo, Memba and Njeru (2016) who posits that dedication of debt collection resources ensure better and timely collection and few instances of bad debts.

#### **4.19.4. The Effect of Accounts Receivable Risk Assessment Practice on Growth**

The study sought to find out the effect of Accounts receivable risk assessment practice on growth of SMEs. In Table 4.36 the coefficient obtained was 0.0212 with (p-value  $0.032 < 0.05$ ) thus the null hypothesis that use of ARRAP has no significant effect on growth was rejected which leads to the conclusion that there is a statistically significant relationship between use of use of ARRAP and SME growth. In this case use Accounts receivable risk assessment practices have a positive effect on SME growth such that a unit increase in use of Accounts receivable assessment practice will result to an increase in growth by 2.1%. This may be attributed to the increase in the tracking methods to owners selling on credit to only creditworthy customers. This study agrees with Mutungi (2010) who established that there was a significant positive relationship between monitoring and control of accounts receivables and performance of a firm.

#### **4.19.5 The Effect of Accounts Receivable Financing Practice on SME Growth**

The study sought to find out the effect of internal rating on growth of SMEs. In Table 4.36, the coefficient obtained was 0.0266 with (p-value  $0.933 > 0.007$ ) thus the null hypothesis that use of Accounts receivable financing practice has no significant effect on growth was accepted which leads to the conclusion that there is no statistically significant relationship between Accounts receivable financing practices and SME growth. In this case use Accounts receivable financing practices have an effect on growth such that a unit increase in use of Accounts receivable financing practices will result to an increase in growth by about 3%. This may be attributed to the increase awareness of the entrepreneurs about other forms of financing other than financial loans from financial institutions which are not readily available due to insufficient collateral. This finding is differ with the study by Afza and Nazir (2009), who in his

regression results found a negative relationship between the profitability of firms and the degree of aggressiveness of receivables investment and financing policies.

#### **4.19.6. The Moderating Effect of Financial Literacy on the relationship between Accounts Receivable Management and Growth**

The study sought to find out the moderating effect of financial literacy levels on the relationship between Accounts receivable management practices and growth of SMEs. In Table 4.36. The significant level for all is less than 0.05 indicating that there is a significant impact of financial literacy on the relationship between Accounts Receivable and Management Practices and growth of SMEs. This may be attributed to the fact that knowledge of Accounts receivable management practices leads to their use by the owners. This study differs with the one of Nyabwanga (2011), who studied the effects of working capital management practices on financial performance of small scale enterprises in Kisii South district. In his study, he established that majority of business operators did not have business management knowledge. However, the findings concur with Njoroge (2013), in his study concludes that there is positive relationship between entrepreneur's success and financial literacy. He noted SMEs that are more successful are run by entrepreneurs who are financial literate and understand key financial concepts that include, risk management, interest rates, time value for money and financial market. The study agrees with the study of Sabri (2015) who posits that there is positive relationship between ARM practices and Growth.

#### **4.20 Hypothesis Testing and Discussion**

This section presents the hypothesis testing of the study variables. The rule of thumb was to reject the hypothesis if the independent variable had significant with the dependent variable. The significance was tested at a critical P value of 0.05.

**H<sub>01</sub>:** Revealed that an Accounts receivable analysis practice has no significant effect on the SME growth in Kakamega County. However, research findings showed that Accounts receivable analysis practice had coefficients of estimate which was significant basing on  $\beta_1 = 0.0127$  (p-value = 0.009 which is less than  $\alpha = 0.05$ ) implying

that we reject the null hypothesis stating that Accounts analysis practice has no significant effect on the growth of SMEs in Kakamega County. This indicates that for each unit increase in practice there is 0.089 units increase in the growth of SMEs in Kakamega County. Furthermore, the effect of Accounts Analysis was stated by the t-test value = 2.123 which implies that the effect of Accounts receivable analysis surpasses that of the error by over 2times.

**Ho<sub>2</sub>**: Stated that Receivable management has no significant effect on the growth of SMEs in Kakamega. Findings showed that Accounts receivable extension practices had coefficients of estimate which was significant basing on  $\beta_2 = 0.0151$  (p-value = 0.000 which is less than  $\alpha = 0.05$ ) hence we reject the null hypothesis, and conclude that Accounts Receivable extension practices has significant effect on the growth of SMEs in Kakamega. This implies that for each unit increase in Accounts receivable extension practice, there is up to 0.2 unit increase in growth of SMEs in Kakamega County. Also the effect of Accounts receivable extension practice is shown by the t-test value of 2.166 which implies that the effect of AREP is more than of the error by over 2 times.

**Ho<sub>3</sub>**: Stated that Accounts receivable collection practice has no significant effect on the growth of SMEs in Kakamega County. However, study findings showed that Accounts receivable collection practices had coefficients of estimate which was significant basing on  $\beta_3 = 0.0179$  (p-value = 0.005 which is less than  $\alpha = 0.05$ ) hence the research failed to accept the hypothesis and concluded that Accounts receivable collection practices has a significant effect on growth, there is up to 0.0179 units increase in the growth of SMEs in Kakamega County. The effect of Accounts receivable collection practices is stated by the t-test value = 3.568 which clearly demonstrates that the effect of Accounts receivable collection practices is over 4 times that of the error associated with it.

**Ho<sub>4</sub>**: Stated that Accounts receivable risk assessment practice has no significant effect on the growth of SMEs in Kakamega. However, study findings showed that Accounts receivable risk assessment practice had coefficients of estimate which was significant basing on  $\beta_4 = 0.021$  (p-value = 0.000 which is less than  $\alpha = 0.05$ ) hence research

failed to accept the hypothesis and concluded that Accounts Receivable Risk Assessment Practice has a significant effect on the growth of SMEs in Kakamega. This indicates that for each unit increase in Accounts receivable risk assessment practices, there is up to 0.021 units increase in the growth of SMEs in Kenya. The effect of Accounts receivable risk management practices is stated by the t-test value = 2.159 which point out that the effect of Accounts receivable risk assessment practice is over 2 times that of the error associated with it

**H<sub>05</sub>**: Stated that Accounts receivable financing practice has no significant effect on the growth of SMEs in Kakamega. However, study findings showed that Accounts receivable financing practice had coefficients of estimate which was significant basing on  $\beta_5 = 0.0266$  (p-value = 0.007 which is less than  $\alpha = 0.05$ ) hence research rejected the hypothesis and concluded that Accounts receivable financing practice has significant effect on the growth of SMEs in Kakamega. This indicates that for each unit increase in Accounts receivable financing practices, there is up to 0.03 units increase in the growth of SMEs in Kakamega. The effect of Accounts receivable financing practices is stated by the t-test value = 3.323 which point out that the positive effect on growth of SMEs.

## **CHAPTER FIVE**

### **SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS**

#### **5.1 Introduction**

The chapter has presented the summary of the findings, the conclusion and the recommendation that can help enhance SMEs growth in Kakamega County. Finally, the suggestion for further research has been given in order to shed light on the key areas which need more research to be conducted. The purpose of the study was to establish the relationship between Accounts Receivable Management Practices (ARM practices) on growth of SMEs in Kakamega County (Central Sub County), Kenya. The study sought to establish the relationship between Accounts Receivable analysis practices, Accounts receivable extension practices, Accounts Receivable collection practices, Accounts Receivable Risk Assessment Practices, Accounts Receivable Financing Practices and SMEs growth. Financial literacy was the moderating variable.

#### **5.2 Summary of Findings**

This section summarizes the findings obtained in chapter four in line with the study objectives.

##### **5.2.1 Accounts Receivable Analysis Practices**

The first objective of the study was to determine the influence of customer analysis practices on growth of SMEs in Kakamega County, Kenya. Results revealed that the SME owners practice various Accounts Receivable Analysis Practices. These include; analyzing customers' paying history to determine capacity to pay, frequently analyzing debtors ledger accounts, contacting third parties for references (creditworthiness), scrutinizing customers' account to determine his capital base, analyzing and determine customers' cash flows financial statement and evaluating collateral issued.

The bivariate regression results revealed that there is a positive and significant relationship between Accounts Receivable Analysis Practices and SMEs growth as indicated by beta coefficient and so the null hypothesis was rejected and the alternative was accepted. This implies that an increase in ARAP would results to increase in SMEs growth.

The multivariate regression analysis revealed that there is a positive and significant relationship between customer analysis practices and SMEs growth.

### **5.2.2 Accounts Receivable Extension Practices**

The second objective of the study was to establish the influence of Accounts Receivable Extensions Practice son growth of SMEsin Kakamega County; Kenya.Results revealed that the SME owners practice various ARAP. These practices include; developed a written plan(showing credit terms), formalizing credit processes (documentation of agreement), use third party provided intelligence, granting credit only when amount is guaranteed, extending credit to regular customers who have had good records and using portfolio strategy to segment categories of customers.

The bivariate regression results revealed that there is a positive and significant relationship between Accounts Receivable Extensions Practices and SMEs growth which depicts that we reject the null hypothesis and accept the alternative. This implies that an increase in Accounts Receivable extension practices would results to increase in SMEs growth

The multivariate regression analysis revealed that there is a positive and significant relationship between Accounts Receivable Extensions Practices and SMEs Hence, an increase in Accounts Receivable Extension Practices would results to increase in SMEs growth.

### **5.2.3 Accounts Receivable Collection Practices**

The third objective of the study was toexamine the influence of credit collection practices on growth of SMEsin Kakamega County, Kenya.Results revealed that the

SME owners practice various AR collection practices. These practices include; defining the credit collection policy, invoicing promptly and sending statements regularly, contacting overdue accounts more frequently, setting collection timelines, using ageing sheet and making constant follow up, calling customers prior to due date, keeping accurate and timely records and using average collection period technique. Results also revealed that the SME owners did not visit their customer as well as use collection agencies.

The bivariate regression results revealed that there is a positive and significant relationship between AR collection practices and SMEs growth depicts that we reject the null hypothesis and accept the alternative. This implies that an increase in AR collection would results to increase in SMEs growth.

The multivariate regression analysis revealed that is a positive and significant relationship between AR collection practices and SMEs growth. Thus, an increase in Accounts Receivable Collection Practices would results to increase in SMEs growth

#### **5.2.4 Accounts Receivable Risk Assessment Practices**

The fourth objective of the study was to assess the influence of Accounts Receivable Risk Assessment Practices on growth of SMEs in Kakamega County, Kenya. Results revealed that the SME owners practice various Accounts Receivable Risk Assessment Practices. These practices include; using internal rating systems, expert system, credit scoring models Results also revealed that the SME owners did not use expert systems as well as credit scoring models.

The bivariate regression results revealed that that there is a positive and significant relationship between credit risk assessment practices and SMEs depicts that we reject the null hypothesis and accept the alternative. This implies that an increase in Accounts Receivable risk assessment practices would results to increase in SMEs growth by 0.277 units.

The multivariate regression analysis revealed that there is a positive and significant relationship between credit risk assessment practices and SMEs growth. This implies

that an increase in Accounts Receivable risk assessment practices would result to increase in SMEs growth.

### **5.2.5 Financing of Accounts Receivable Practices**

The fifth objective of the study was to determine the influence of financing practices on growth of SMEs in Kakamega County, Kenya. Results revealed that the SME owners practice various financing practices. These practices include; discounting/selling overdue invoices regularly, using accounts receivable as collateral for a loan, securitizing accounts receivables and factoring accounts receivables.

The bivariate regression results revealed that there is a positive and significant relationship between financing practices and SMEs growth which depicts that we reject the null hypothesis and accept the alternative. This implies that an increase in financing practices would result to increase in SMEs growth. The multivariate regression analysis revealed that financing practices had positive relationship with SMEs growth. This implies that financing practices did have effect on the overall growth of SMEs as funds tied up are unlocked through these practices.

### **5.2.6 Financial Literacy**

The sixth objective of the study was to establish the moderating effect of financial literacy on the relationship between ARM practices and growth of SMEs in Kakamega County, Kenya. Results revealed that the SME owners were informed about various aspects of finances such as using credit monitoring methods, computing discounts and using credit collection methods. However, results revealed that the SME owners who were more financially literate were able to manage their accounts receivables.

## **5.3 Conclusion**

### **5.3.1 Accounts Receivable Analysis Practices**

Based on the findings the study concluded that Accounts Receivable analysis practices influence the growth of SMEs in Kakamega County, Kenya. This can be



explained by the bivariate and multivariate regression results which revealed that the influence was positive and significant.

### **5.3.2 Accounts Receivable Extension Practices**

The study concluded that Accounts Receivable Extension Practices influence the growth of SMEs in Kakamega County, Kenya. This can be explained by the bivariate and multivariate regression results which revealed that the influence was positive and significant.

### **5.3.3 AR Collection Practices**

The study concluded that Accounts Receivable Collection Practices influence the growth of SMEs in Kakamega County, Kenya. This can be explained by the bivariate and multivariate regression results which revealed that the influence was positive and significant.

### **5.3.4 Accounts Receivable Risk Assessment Practices**

The study concluded that Accounts Receivable Risk Assessment Practices influence the growth of SMEs in Kakamega County, Kenya. This can be explained by the bivariate and multivariate regression results which revealed that the influence was positive and significant.

### **5.3.5 Accounts Receivable Financing Practices**

The study concluded that Accounts Receivable Financing Practices influence the growth of SMEs in Kakamega County, Kenya individually without inclusion of other factors. This can be explained by the bivariate regression which revealed that the influence was positive and significant.

### **5.3.6 Moderating effect of Financial Literacy**

Based on the study results, the study concluded that financial literacy moderates the relationship between ARM practices and growth of SMEs in Kakamega County,

Kenya. This can be supported by the regression results which revealed a positive and significant moderating effect. The magnitude of the effect was significant and illustrated that the interactive factor increased the way Accounts Receivable management Practices affected growth of SMEs. It can be concluded that when SMEs empower their employees with more knowledge in ARMP the SMEs would be successful.

## **5.4 Recommendations**

The study recommendations are in line with the objectives, findings and conclusions of the study.

### **5.4.1 Accounts Receivable Analysis Practices**

As evidenced by the study findings, customer analysis practices play a key role in the growth of SMEs in Kakamega County, Kenya. Thus, it is imperative that SMEs owners should continue in the practice of customer analysis practice for consistent growth. Additionally, the SMEs owners should endeavour to use other AR analysis practices that are not outlined in this study.

### **5.4.2 Accounts Receivable Extension Practices**

Based on the study findings, credit extension practices play a key role in the growth of SMEs in Kakamega County, Kenya. The study therefore recommends that SMEs owners should continue in the practice of AR extension practice for consistent growth. Additionally, the SMEs owners should endeavour to use other AR extension practices that are not outlined in this study.

### **5.4.3 Accounts Receivable Collection Practices**

As evidenced by the study findings, credit collection practices play a key role in the growth of SMEs in Kakamega County, Kenya. Thus, it is imperative that SMEs owners should continue in the practice of Accounts Receivable Collection Practice for consistent growth. Additionally, the SMEs owners should endeavour to use other credit collection practices that are not outlined in this study.

#### **5.4.4 Accounts Receivable Risk Assessment Practices**

The study findings reveal that Accounts Receivable Risk Assessment Practices play a key role in the growth of SMEs in Kakamega County, Kenya. The study therefore recommends that SMEs owners should continue in the practice of AR Risk Assessment Practice for consistent growth. Additionally, the SMEs owners should endeavour to use other Accounts Receivable Risk Assessment Practices that are not outlined in this study.

#### **5.4.5 Accounts Receivable Financing Practices**

The study findings reveal that AR financing practices play a key role in the growth of SMEs in Kakamega County, Kenya. The study therefore recommends that SMEs owners should continue in the practice of AR financing practice for consistent growth. Additionally, the SMEs owners should endeavour to use financing practices to unlock the tied funds in Accounts Receivables.

#### **5.4.6 Financial Literacy**

Accruing form the study findings, financial literacy moderates the relationship between ARM practices and growth of SMEsin Kakamega County, Kenya. The study recommends that financial institutions within Kakamega County should endeavor to educate SME owners about the ARM practices. This would result to economic growth within the county which would also impact them positively. The study also recommends that SMEs owners should take the initiative to be financial literate. This would help to speed the growth of their businesses. Government should encourage entrepreneurs to learn about Accounts Receivable Management Practices, SMEs growth translates to economic growth for the entire Nation which will mean reduction in poverty levels. SMEs would be able to sustain themselves.

#### **5.5 Areas of Further Research**

The study recommends that a similar study should be conducted in the mid-sized enterprises within Kakamega County for comparison purposes. The study also

recommends that a study seeking to establish other ARM practices that affect SMEs growth should be conducted. This would help to give insight to SMEs and other organizations on other kinds of ARM practices they can use in their businesses. As a result, this would translate to better performance. The study also recommends that a similar study should be conducted in a different County. This would assist to establish whether SMEs across different counties use the same ARM practices and whether the impact of these practices is different. Further, the study recommends that a study seeking to establish the direct effect of financial literacy should be conducted. This would help to determine whether the direct effect differs from the moderating effect.

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## APPENDICES

### Appendix 1: Researcher's Letter of Introduction

Dear Participant/Respondent,

I am a post graduate student in Jomo Kenyatta University pursuing Doctor of Philosophy degree in Business Administration. I wish to request you to participate in my study. The title of my research is **“Relationship between Accounts Receivable Management Practices on growth of SMEs in Kakamega County (Central Sub County), Kenya** The purpose of this study is to establish whether receivable management practices affect growth of SMEs. The results of the study will help SMEs formulate ways of enabling SMEs increase their finance and growth prospects.

You are requested to provide honest and accurate responses to the Questionnaires and interview schedule. You are free to participate/not to participate or seek for any clarification during the study. Thank you very much for accepting to participate in this study

Researchers name.....

Student number.....

Contact phone numbers .....

Signature.....

**Appendix 2: Interview Schedule**

1. Does credit analysis practice affect growth of SME in Kenya?

Yes[ ] No[ ] please, Explain

.....

2. Does the extension of credit practice on trade receivables influence growth of SMEs in Kenya? Yes [ ] No [ ] Explain

.....

.....

3. Does Credit collection practice affect growth of SMEs in Kenya?

Yes[ ] No[ ] please, Explain

.....

.....

4. Does the credit risk assessment practice used affect growth of SMEs in Kenya?

Yes[ ] No[ ] please, Explain

.....

.....

5. Does financing of accounts receivables practice influences growth of SMEs?

Yes [ ] No[ ] please, Explain your

.....

.....

6. Does the level of financial literacy on the affect the relationship between RM practices and growth of SMEs? Yes[ ] No[ ] please, Explain your

.....

**Appendix3: Questionnaire**

Questionnaire to illicit views on the receivable management practices and growth of SMEs within Kakamega Central Sub-County

**Part A: Business Demographics**

**Part A: Entrepreneurs' background Information**

1. Gender of the respondent:

Male  Female

2. How many years have you worked in this firm-----

3. Highest level of education attained:

4. None  Primary  Secondary  Graduate  Post Graduate

others (specify) \_\_\_\_\_

5. What is your job title? \_\_\_\_\_

6. Which sector does your organization fall?

Retail  Health and Beauty

Construction  Agriculture

Manufacturing  Hospitality

Transport  Service

Others, specify \_\_\_\_\_

7. Business Ownership: Sole trader  Partnership  Family trust  public

Enterprise  other specify.....

8. How long has the business been in operation since inception.....

**PART B: RECEIVABLE MANAGEMENT PRACTICES**

9. To what extent do you agree that the following Credit analysis practices and approval practices are adopted by your firm? (Tick as appropriate)

<b>AR analysis practices that are adopted by the SME</b>	<b>Never</b>	<b>Annually</b>	<b>Semi-annually</b>	<b>Monthly</b>	<b>Always</b>
How often do you analyze customers' paying history to determine capacity to pay					
How often do analyze debtors ledger accounts					
How often do you contact third parties for references(creditworthiness)					
How often do you scrutinizes customers' account to determine his capital base					
How often do you analyze and determine Customers cash flows financial statement.					
How often do make a follow up on collateral issued					

10. To what extent do you agree that the following credit extension/granting practices has your firm adopted? (Tick as appropriate)

<b>AR extension practices that are adopted by theSME</b>	<b>Never</b>	<b>Annually</b>	<b>Semi-annually</b>	<b>Monthly</b>	<b>Always</b>
How often do you review written plan(showing credit terms)					
How often do you Use formalized credit processes(documentation of agreement)					
How often do you use third party provided intelligence					
How often do you review data of regular customers who have had good records?					
How often do use portfolio strategy to segment categories of customers					

11. To what extent do you agree that your firm adopts the following Accounts Receivable Collection practices?

<b>AR collection practices that are adopted by the SME</b>	<b>Never</b>	<b>Annually</b>	<b>Semi-annually</b>	<b>Monthly</b>	<b>Always</b>
How often do you refer to a defined credit collection policy?					
How often do you Invoice and send statement?					
Do you Contact overdue accounts holders?					
How often do you review collection timelines?					
How often do you use ageing sheet and make constant follow up?					
How often do you call customers prior to due date?					
How often do you use collection agencies?					
Do you use average collection period technique					

12. To what extent do you agree that your firm adopts the following credit risk assessment practices?

<b>AR risk assessment practices that are adopted by the SME</b>	<b>Never</b>	<b>Annually</b>	<b>Semi-annually</b>	<b>Monthly</b>	<b>Always</b>
How often do you make use of Expert Systems?					
How often do you make use of Credit Scoring Models?					
How often do you make use of Internal Rating Systems?					

13. To what extent do you agree that your firm adopts the following Accounts receivable financing practices?

<b>Accounts receivable financing practices that are adopted by the SME</b>	<b>Never</b>	<b>Annually</b>	<b>Semi-annually</b>	<b>Monthly</b>	<b>Always</b>
How often do you Discounting/selling overdue invoices?					
Do you often use of accounts receivable as collateral for a loan ?					
Do you Securitize accounts receivables					
How often do contact Factoring firms to factor accounts receivables					



**PART D: Financial Literacy**

14. On a scale of 1 to 5 rate your overall understanding of the subject matter and how comfortable are you making decisions about these items

<b>Level of financial literacy</b>	<b>Very low</b>	<b>Low</b>	<b>Average</b>	<b>High</b>	<b>Very High</b>
1. Financing of receivable options available					
2. Credit monitoring methods					
3. Computations of discounts					
4. computation of financial ratios					
5. AR analysis methods					
6. AR collection methods					

**PART E: GROWTH MEASURE**

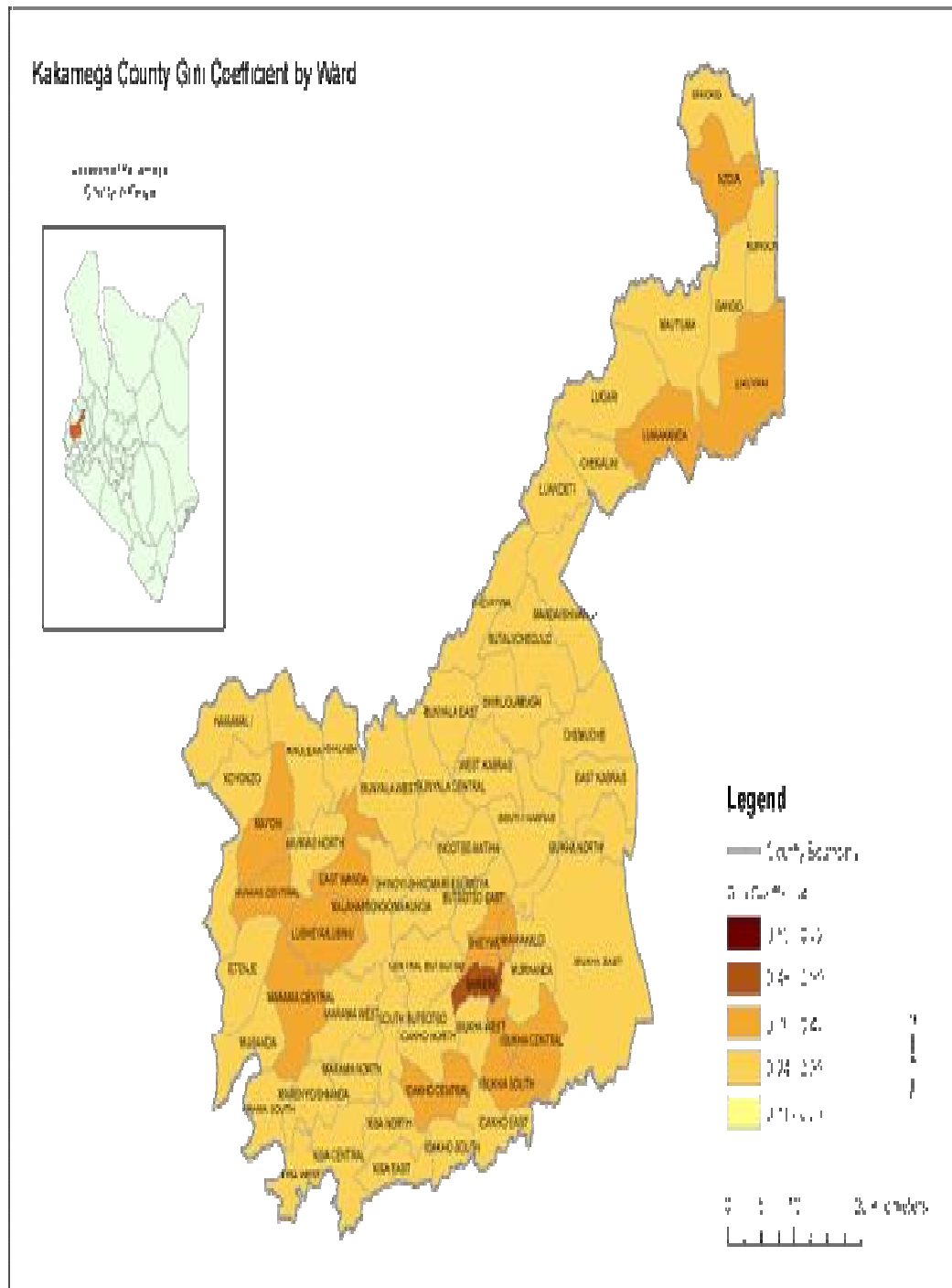
15. What is your opinion on the following statements on how Accounts receivable management practices have affected profitability growth?

<b>Statement</b>	<b>Strongly disagree</b>	<b>Disagree</b>	<b>Undecided</b>	<b>Agree</b>	<b>Strongly agree</b>
Sales have increased over the last three years					
The total current asset represented by accounts receivable has gone down					
The business percentage of bad and delinquent debts is less than 10% of sales					
The business has been able to generate profits for the last three years					
The total current asset represented by accounts receivable has gone down					
Fees paid to collection agencies has reduced					

17 How would you rate your level of knowledge of the ARM PRACTICES?

- a Know and practice
- b Know but do not practice
- c No knowledge

## Appendix 4: Map of Kakamega



**Appendix 5: Research Permit**

**ORIGINAL** National Commission for Science, Technology and Innovation National Commission for Science, Technology and Innovation  
**OFFICIAL RECEIPT** National Commission for Science, Technology and Innovation National Commission for Science, Technology and Innovation  
**Station:** Neobio **Date:** 29/11/15  
**RECEIVED FROM:** Mary Nelima Lyani  
**Shillings:** Two Thousand only  
**ON ACCOUNT OF:** Research fee  
**Head:** R. J. P.  
**Signature of Officer receiving remittance:** [Signature]

**THIS IS TO CERTIFY THAT:** **Permit No : NACOSTI/P/15/38752/8946**  
**MS. MARY NELIMA LYANI(SINDANI)** **Date Of Issue : 4th December,2015**  
**of JOMO KENYATTA UNIVERSITY OF** **Fee Received : Ksh 2000**  
**SCIENCE AND TECHNOLOGY, 0-50103**  
**MALAVA, has been permitted to conduct**  
**research in Kakamega County**  
**on the topic: RELATIONSHIP BETWEEN**  
**ACCOUNTS RECEIVABLE MANAGEMENT**  
**PRACTICES AND GROWTH OF SMALL**  
**AND MEDIUM ENTERPRISES IN**  
**KAKAMEGA COUNTY, KENYA**  
**for the period ending:**  
**30th November,2016**  
**Applicant's Signature** **Director General**  
**National Commission for Science, Technology & Innovation**

