DETERMINANTS OF FINANCIAL ACCESSIBILITY BY SMALL AND MEDIUM ENTERPRISES IN ELDAMA RAVINE SUB – COUNTY, KENYA

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A RESEARCH PROJECT SUBMITTED TO THE SCHOOL OF BUSINESS IN PARTIAL FULFILLMENT OF AWARD OF MASTER OF BUSINESS ADMINISTRATION FINANCE OPTION IN THE JOMO KENYATTA UNIVERSITY OF AGRICULTURE AND TECHNOLOGY

SEPTEMBER, 2017

DECLARATION

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

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HD333-C007 -2048/2015

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DEDICATION

To my husband Joshua and daughters Angella, Kate,Valerie and Christabel for their moral support, prayers and cheering me on throughout this study.

To my loving mother Mrs. Angeline Chirchir for her unceasing prayers, encouragement and for setting a strong academic foundation from a very early age.

To my brothers and sisters for what they have done to see me through this challenging education task.

ACKNOWLEDGEMENTS

I am deeply indebted to all those who in their own way contributed to successful completion of this study. First and foremost I thank the almighty God, to whom all knowledge, wisdom and power belong for sustaining me in good health, sound judgment and strength to move on and complete my masters' studies.

Special appreciation goes to my supervisor, Dr. Kimani Maina, for his dedication, guidance, valuable suggestions and ideas throughout the course of this project. Without his enormous support this study would not have been successful.

Thanks to my family who always inspired me in every step to accomplish this study. I am eternally grateful for your love, encouragement and support in all my endeavors.

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ABBREVIATIONS AND ACRONYMS

CBK	Central Bank of Kenya
CMA	Capital Markets Authority
ERIA	Economic Research Institute of Association of Southeast Asian Nations
GDP	Gross Domestic Product
IFC	International Finance Corporation
MFIs	Micro Finance Institutions
MIME	Ministry of Industry, Mines and Energy
MoEF	Ministry of Economy and Finance
MoC	Ministry of Commerce
MSME	Micro, Small and Medium Enterprises
OECD	Organization for Economic Cooperation and Development
PPMC	Pearson's Product Moment Correlation
SEDA	Small Enterprise Development Agency
SME	Small and Medium Enterprises
SMEDC	Small and Medium Enterprises Development Council
SPSS	Statistical Package for Social Sciences
UK	United Kingdom

ABSTRACT

Importance in the role of the SME in the development process continues to be in the forefront of policy debates not only in developing countries but also in developed countries. In spite of the generally fast pace by which access to financial services for SME is being developed, significant segments of the SME sector do not yet benefit from the expansion and deepening of outreach. In attempting to gain access to financial services SME continue to face financial constraints. Thus this research intended to study the determinants of financial accessibility by Small and Medium Enterprises in Eldama Ravine Sub–County in Baringo County, Kenya. Of specific focus was the influence of cost of credit, interest rates, credit rationing and business risk in Eldama Ravine Sub-County, Baringo County. Transaction cost theory, the capital channel model, credit rationing theory and prospect theory guided the study. A cross-sectional survey research design was used. Stratified random sampling technique was adopted to draw a sample of respondents from the accessible population. This study used a self-administered semi-structured questionnaire to collect data. A pre-testing of questionnaires was conducted before carrying out the main study. This study employed the Cronbach alpha coefficient to test the instrument's reliability. Content validity test was used for validity test. The collected data was analyzed with the aid of the Statistical Package for Social Sciences Version 22. Data analysis captured both descriptive and inferential statistics. Descriptive statistics included modes, medians, means, standard deviations and variances. Inferential statistics included Pearson's correlation and regression analysis. The results of the analysis were presented in form of tables, graphs and charts. The significance of the study will be to the financiers of the SMEs who will be interested with this information since they will be able to evaluate SMEs performance, to the firm management team in the capital structure decisions and to the academicians and scholars, the study will form the basis for future research study. From the findings the study concluded that high transaction costs increase the cost of borrowing and also restrict access to external finance for some borrower groups. From the study the researcher further concluded that lending institution consider the size of an enterprise while approving loan application. From the conclusion the study recommended that there is need for the lending institution to simplify loan application process to avoid unnecessary expenses. This will encourage more SMEs to apply for loans. Lending institution should also ensure that loan repayment process is flexible for SMEs. The study further recommended that SMEs should form groups so as to enable them access loans easily, Majority of financial institution would prefer group lending compared to individual. This will have a positive impact on the performance of SMEs.

DEFINITION OF TERMS

Small and Medium Enterprises: The definition varies from country to country. Some of the criteria employed in defining these enterprises include number of workers, value of assets or annual turnover, nature of premises, of status registration and sustainability. In Kenya for example a small enterprise is one which employs 6-10 people while a medium one is expected to have 11-100 employees (CBS et al., 1999).

Cost of Credit: This refers to the amount of money the entrepreneurs pay in process of borrowing money from financial institutions. They include processing fees, negotiation fees, interest rates, personal insurance, legal fees and travelling expenses that the entrepreneurs meet in the process of acquiring credit (Gichuki et al,. 2014).

Interest Rate: This is defined as the return on capital. Interest rates are usually a percentage of the borrowed amount (Saleemi, 2007).

Credit Rationing: A measure employed by lending institutions to limit the availability of capital based on determinations they make about the credit-worthiness of borrowers as well as the lending environment in general. Raising interest rates above current market rates, regardless of the supply and demand equilibrium, is seen as a form of credit rationing (Kung'u, 2011).

Business Risk: Implies uncertainty in profits or danger of loss due to uncertain competitive environment; inadequate accounting systems; more unpredictable operating environment in the developing and emerging markets; assets not properly registered; delayed payments for the products and services rendered; less equipped in terms of both human and financial resources to withstand economic resources (Van Aardt & Fatoki, 2012).

CHAPTER ONE

INTRODUCTION

1.1.1. 1.1 Background of the Study

SMEs are vital for economic growth and development in both industrialized and developing countries because they play a key role in creating new jobs. Financing is necessary to help them set up and expand their operations, develop new products, and invest in new staff or production facilities. Many small businesses start out as an idea from one or two people, who invest their own money and probably turn to family and friends for financial help in return for a share in the business. But if they are successful, there come at times for all developing SMEs when they need new investment to expand or innovate further. That is where they often run into problems, because they find it much harder than larger businesses to obtain financing from banks, capital markets or other suppliers of credit (Mulandi, 2013). According to Aldaba (2012) small and medium enterprises (SMEs) are seen as crucial for a country's economic growth, employment creation and innovation. Their lack of access to financing has often been cited as one of the major constraints affecting their performance and competitiveness. Lack of access to financing implies that a substantial number of SMEs cannot obtain financing from banks and other sources in order to start, innovate, grow and develop their enterprises.

Cost of credit can be classified as; gross interest and net interest. Gross interest is the total amount that the debtor advances to a creditor and the net interest means the part of interest that is for the use of capital only. Kung'u (2011) stated that the segmented and incomplete nature of financial markets increases transaction costs associated with financial services. Those organisations with close relationships are seen to have more access to credit. Relationship with a single bank may reduce risk and hence the cost of credit, i.e. interest rate may be reduced. This is due to reduced incidence of moral hazard and improved knowledge of the firm which ultimately reduces adverse selection (Muguchu, 2013).

High interest rate on credit may discourage SMEs from borrowing therefore reducing the accessibility of credit among them. It is indicated that banks trade on customer deposits, they lend at interest rates high enough to pay their overheads and leave balances to pay interest to customers whose deposits are being loaned (Makena, 2011). The interest rate usually is a percentage of the borrowed amount determined by the amount of interest over duration which may be a year. High interest rate therefore increases the cost of credit (Mutai, 2015). The scenario witnessed in Kenya particularly during the climaxing period of the year 2008 testifies the need for credit among the common and low earning entrepreneurs. Numerous money lenders in the name of Pyramid schemes came up, promising hope among the little investors, that they can make it to the financial freedom through soft borrowing. The rationale behind turning to these schemes among a good number of entrepreneurs is mainly to seek alternatives and soft credit with low interest rates while making profits. Financial constraint remains a major challenge facing SMEs in Kenya (Wanjohi & Mugure, 2008).

The practice of credit rationing by financial institutions using interest rates has locked out most poor individuals as only large scale borrowers who expect higher returns can bear the high cost of borrowing (Stiglitz & Weiss, 1981). Due to the potential for adverse selection resulting from information asymmetry between lenders and borrowers, lenders are often discouraged from using the interest rate as a way to ration credit (Muguchu, 2013). Small firms are more likely to be rationed because they are seen as particularly risky. Although they might be willing to pay more to compensate for the additional risk, the banks will refuse to raise the interest rate sufficiently to equate supply and demand. The bank's credit rationing behavior may theoretically be influenced by a number of factors which include the borrower's observable characteristics (age, gender, wealth, experience, credit history), firm characteristics (business experience, risk profile, earnings), and loan characteristics (amount demanded, loan maturity, collateral offered, interest rate) (Mole & Namusonge, 2016).

Access to formal finance is poor because of the high risk of default among MSEs and due to inadequate financial facilities. Small businesses in Africa can rarely meet the conditions set by financial institutions, which see MSEs as a risk because of poor guarantees and lack of information about their ability to repay loans (Gichuki et al., 2014). Most rural individuals particularly rely on informal credit facility from buyers and sellers of consumer goods like shops and farmers. However, where there is no full information about the level of risk and credit worthiness of the individual, access to credit facility from both formal and informal lenders is constrained. The establishment and launch of the credit reference bureaus is expected to change the credit landscape since information on the credit worthiness is to be made available hence reducing the degree of information asymmetry. However, launch of this body does not suffice since information on most potential borrowers and first timers remain unknown.

1.1.2. Global Perspective of Access to Finance by Small and Medium Enterprises

SMEs are facing many challenges, one of which is access to finance. In the context of Cambodia, according to ERIA Research Project Report (2010) the challenge is a result of the early stage of development of the financial sector. The banking sector is profit-oriented, and banks focus on big business transactions to maximize their profit. The MFIs that tailor-make credit for micro-sized firms usually set small loan sizes, charge high interest rates and allow only short maturity. Moreover, all credit from the formal sector must come with collateral. According to a Ministry of Industry, Mines and Energy (MIME) report on SME statistics in Cambodia in 2007, Cambodia had a total of 31,149 small industrial establishments with fewer than 50 employees. Based on similar data from 1999, this number represents growth in total establishments of approximately 26%. Food, beverage, and tobacco manufacturers comprise the largest number of small industrial establishments. The same report also reveals that according to data from Ministry of Economy and Finance (MoEF) and the Tax Department, there are 55,466 SMEs. However, in 2007, only 14,324 SMEs were formally registered as limited liability companies. It is noteworthy that most enterprises remain unregistered with the Ministry of Commerce (MoC) and instead obtain operating permits from other ministries and departments at the local level i.e. the provincial or municipal level. With so many unregistered SMEs, it is difficult to estimate the number of enterprises in Cambodia, especially the number of very small businesses according to IFC Advisory Services in East Asia and the Pacific (2010).

A report by EIRA Research Project (2010) indicated that, in Vietnam, to promote SMEs' access to finance in the context of economic recession, the Government implemented a flexible monetary policy, adjusting the exchange rate by market signals so as to encourage exports and maintain economic stability, reducing the required reserve ratio of credit institutions and the basic interest rate, and lowering interest rates to increase access to finance for enterprises, including SMEs. Vietnam represents an interesting case because it actually ranks 21th out of 183 countries in terms of getting credit in 2011 (World Bank, 2011). This is an impressive outcome of the banking system. Commercial banks, seeking to boost lending, have begun to see SMEs as a potential market and mapped out plans to tap those corporate customers.

According to Hamilton and Beck (2016) the Republic of Korea's economic development has been the envy of many countries, transitioning from one of the world's poorest nations in the 1960s, to being the 12th largest economy (in GDP). As of 2012, 99.9% of all companies in Korea are SMEs accounting for 87.7% of all employees. The sector is characterized by heavy reliance on bank funding to meet financing needs. The Korean government has long supported SMEs as an engine of growth in the economy. Since 1979, it has supplied public funds to SMEs both directly and through credit guarantee schemes. It has also used moral suasion, for example, in 2009 in the wake of the global financial crisis banks were told to roll over loans to viable SMEs. Support for small companies has increased following the financial crisis, while large business groups have been forced to restructure.

In Malaysia, SMEs generally face difficulties in obtaining finance with lack of collateral and insufficient documents to support loan application. This lack of financial track record is the main constraint faced by Malaysian SMEs in accessing financing (Haron et al., 2013). According to Gunto and Alias (2014) the Malaysian government has given priority to SMEs and has put in place a policy and institutional framework that addresses their developmental needs (UNDP, 2007). To ensure implementation of the policy, the government set up in 2004 a National SME Development Council (SMEDC) chaired by the Prime Minister. Also, in the Third Industrial Master Plan (2006-2020), which is currently under development, is scheduled to commit to a variety of technical and financial assistance policies targeting improved market accessibility for SMEs, the promotion of activities involving technical innovation and information technologies, and the promotion of linkages with key industries. In addition, the SME Development Council has acknowledged the importance of policy-based lending support in facilitating access to capital markets. Moreover, given the fact that the framework of the “Fund for Small and Medium-Scale Industries” is still in place, this project, which aims to develop SMEs via the provision of financial assistance, continues to have relevance. The Government’s programs and initiatives for SME development will be focused on achieving some targets, especially in the areas of developing human capabilities and the necessary enabling infrastructure that will allow for the establishment of high performance and high value-added SMEs.

In Thailand, according to ERIA Research Project Report (2010) there is plenty of evidence that expanding access to SME financing remains an important challenge. Market failures related to information gaps imply that the government has an important role in the creation of a more inclusive financial system. So far, Thai governments have provided a comprehensive range of private and government financing channels that support SMEs. According to the Office of Small and Medium Enterprises Promotion (2013), there were 2.8 million SMEs in Thailand in 2013, constituting 97.2% of total enterprises. Even though SMEs dominated enterprises in Thailand in 2013, their business loans, equal to approximately $72.2 billion, accounted for only 38.7% of total business loans. This problem has been exacerbated by systemic volatility in financial markets in the past, such as the Asian financial crisis in 1997 and the recent global financial crisis. According to OECD (2005), these financial crises have changed the lending behavior of Thai banks (Amornkitvikai & Harvie 2015).

1.1.3. African Perspective of Access to Finance by Small and Medium Enterprises

According to Osano and Languitone (2016) in the context of Mozambique the small enterprises are those with less than ten employees and medium enterprise with employees between 11 and 50. The large enterprises are those which have more than 50 employees. It is observed that 98.6 % of Mozambican firms are composed of

SMEs. They provide more employment, diversification, and stimulus for innovations, mobilize social and economic resources, and provide a greater level of competition. They further indicate that financial institutions have highlighted several constraints encountered by SMEs which limit their provision of finance products. The constraints faced by SMEs are associated with the lack of clear financial plans, the accounting documentation, higher rate of interest, and the lack of collateral requirements. As in other countries in the world, Mozambique focuses on both demand and supply side (Central Bank of Mozambique, 2013). The demand side encourages the commercial banks to provide finance to the small businesses through guarantees and provide more financial assistance through the affordable cost of capital, micro-finance, and innovation fund. On the supply side, this focus is in diminishing the asymmetries of information between the two players (lenders and borrowers). The relevant information between lenders and borrowers should be provided to improve the situation (Central Bank of Mozambique, 2013).

In the Libyan context, as indicated in Tarek et al., (2013) the SMEs are about 46% of the overall number in the North Western of Libya, and about 36% in the North Eastern of the country. The private sector owns approximately 80% of SMEs, while a small corporate owns only 16% and 3% of SMEs are owned by families. Libya’s SMEs in general suffer from some problems which hinder this sector to flourish. Among these problems, easy access to finance is the main one. There are many factors such as social, economic, demographic and political-for the low access to finance. According to Abdesamed and Wahab (2014) although 96% of enterprises in Libya are SMEs, their contributions to the gross domestic product (GDP) growth are little at only 4%. The difficulty of these enterprises in acquiring financial loans is considered one of their main problems. “The 2008 to 2009 report ranked Libya as the last country on financial market sophistication in a survey of 134 countries. In the same survey, Libya ranked 131 on financing through local equity markets and 83 on ease of access to loans. Venture capital availability is almost completely absent in the Libyan financial market. The absence of financial markets forces the banking sectors to shoulder a major responsibility for the Libyan economic development.”

In South Africa, SMEs account for about 91% of the formal business entities, contribute to about 57% of GDP, and provide almost 60% of employment (Kongolo, 2010). The country has introduced a number of SME support frameworks that include both financial and non-financial assistance. For instance, the Small Enterprise Development Agency (SEDA) was set up to oversee the development of small businesses in the country. To underscore the importance of SMEs, the government established a Ministry of Small Business Development in 2014. Evidently, this has in fact helped proliferation of SME in various parts of the country (Waari et al., 2015). According to Mazanai and Fatoki (2012) in South Africa, SMEs face constrained access to both debt and equity financing. Theoretically and in practice a problem of access to finance exist when there is a need for finances from a client with an investment project that warrantees financing, but are impeded access to external financing. This occurs due to the gaps that exist between the suppliers of external financing and the demand for financial resources.

SMEs in Nigeria, according to Taiwo et al., (2016) have not performed creditably well and hence have not played the expected vital and vibrant role in the economic growth and development of Nigeria. However, the role played by SMEs, notwithstanding their development, is everywhere constrained by inadequate funding and poor management. Unfortunately, the SMEs in Nigeria have underperformed despite the fact that the SMEs in Nigeria constitute more than 90% of Nigerian businesses, their contribution to the nation's GDP is below 10%. This very low percentage contribution of the SMEs to Nigeria's GDP could be attributed to amongst others; unfriendly business environment, poor funding, low management skills and lack of assess to modern technology (Gbandi & Amissah, 2014). A World Bank report showed that 39% of small scale firms and 37% of medium scale firms in Nigeria are financially constrained (World Bank report, 2001). Many SMEs in Nigeria lack the capital to continue their business and they are forced to close shop because they are unable to access the required funds (Gbandi & Amissah, 2014).

According to Marwa (2014) Micro, Small and Medium Enterprises in Tanzania play a significant role in income generation, job creation and poverty reduction. However, the sector is facing significant credit rationing from e formal financial institutions. As a result, the sector is highly credit-constrained. The credit rationing by formal financial institutions is explained mainly by the mismatch between the requirements of formal financial institutions' lending process and structural problems in market. In response to this credit market failure, development finance interventions from the government, entrepreneurs and other stakeholders have emerged as alternative financing mechanisms. The most dominant players are microfinance organizations including serving and credit cooperatives, government programs and other non-banking financial institutions. Yet the demand by MSMEs is far outstripping the supply of such finance. Only 5% of the demand is being met by development finance institutions. According to Mutai (2015) in a poor country like Tanzania, it is quite hard to find an average citizen owning valuable land or other property that can be used to secure loans; if they do own one, most average Tanzanians don't find it a merit to have title deeds citing the difficulties of plot valuing and measuring as reasons for not seeking title deeds for their lands (Mutai, 2015).

1.1.4. Kenyan Perspective on Access to Finance Small and Medium Enterprises

The economic contribution of small enterprises in Kenya is widely acknowledged. However, it seems little efforts are made to look at it from the youth perspective. The specific needs of the youth and particularly their entrepreneurial potential as well as their critical contribution to economic and social progress are underestimated (Irene, 2009) quoted in (Mutai, 2015). Small and micro enterprises (SMEs) have become important players in the Kenyan economy, but at the same time they continue to face constraints that limit their development. Lack of access to credit is one of the main constraints, and a number of factors have been identified to explain this problem. These include the segmented and incomplete nature of financial markets, which increases transaction costs associated with financial services. On the supply side, most formal financial institutions consider SMEs uncreditworthy, thus denying them credit. According to CMA Report (2010), it is estimated that there are 7.5 million SMEs in Kenya, providing employment and income generation opportunities to low income sectors of the economy. Due to their characteristics, SMEs in Kenya suffer from constraints that lower their resilience to risk and prevent them from growing and attaining economies of scale.

Access to credit by small and medium enterprises (SMEs') contributes to incremental growth of SME employment and income. SMEs' holders are thereby able to increase their stocks as well as increase on sales made periodically. They are able to take bigger risks due to the financial aid given by the micro finance institutions (Chege, 2014). In Kenya, strong SMEs tend to be located in urban and peri-urban centres and are usually registered. However, they face a number of constraints, which include the difficulty in employing competent people with techniques in financial management because of the salaries such people would demand, financial problems arising from late payments by debtors, and inability to raise own finance and access financial services from formal sources. This category of SME usually looks to the banking sector and other financial Intermediaries for instruments to finance working capital and to provide credit for short-term liquidity management.

1.1.5. 1.2 Statement of the Problem

Accessing credit is considered to be an important factor in increasing the development of SMEs. It is thought that credit augment income levels, increases employment and thereby alleviate poverty. It is believed that access to credit enable poor people to overcome their liquidity constraints and undertake some investments. However the lack of access to credit to start or expand small scale enterprises has often plagued this sector of the economy. Most SMEs tend to rely on the personal resources of their owners, and or loans from friends and relatives to fund the enterprises. Banks remain highly liquid and reluctant to expand credit other than to most credit worthy borrowers which in most cases excludes the SMEs (Muguchu, 2013). Most SMEs have come into many constraints that have seen some collapse, some selling off their assets, some being acquired by others, unemployment and retarded economic growth. Studies have been done and among them Mokogi (2003) studied the economic implication of lending of micro-finance institutions on micro and small enterprises. Mutugi (2006) studied the responses of micro finance institutions in Kenya to the turbulent business environment. Muchiti (2009) studied risk management strategies adapted by commercial banks in lending SMEs. In this study therefore the researcher seeks to fill this gap by carrying out a survey to find out financial factors influencing access to finance by of SMEs in Eldama Ravine Sub-County, Baringo County, Kenya.

1.1.6. 1.3 Objectives of the Study

The general objective of the study was to establish the determinants of financial accessibility by SME's in Eldama Ravine Sub-County in the County Government of Baringo, Kenya.

1.1.7. 1.3.1 Specific Objectives

The specific objectives of the study was to:

i. To assess the effect of cost of credit on financial accessibility by SME's in Eldama Ravine Sub-County in Baringo County, Kenya.

ii. To investigate how interest rate affect financial accessibility by SME's in Eldama Ravine Sub-County in Baringo County, Kenya.

iii. To examine the effect of credit rationing on financial accessibility by SME's in Eldama Ravine Sub-County in Baringo County, Kenya.

iv. To analyze the effect of business risk on financial accessibility by SMEs in Eldama Ravine Sub-County in Baringo County, Kenya.

1.1.8. 1.4 Research Hypothesis

H_{01}: The relationship between cost of credit and financial accessibility by SME's in Eldama Ravine Sub-County in Baringo County, Kenya is not statistically significant.

H_{02}: The relationship between interest rate and financial accessibility by SME's in Eldama Ravine Sub-County in Baringo County, Kenya is not statistically significant.

H_{03}: The relationship between credit rationing and financial accessibility by SME's in Eldama Ravine Sub-County in Baringo County, Kenya is not statistically significant.

H_{04}: The relationship between risk and financial accessibility by SME's in Eldama Ravine Sub-County in Baringo County, Kenya is not statistically significant.

1.1.9. 1.5 Scope of the Study

The study was carried out between September, 2016 and June, 2017. The scope of this research was limited to SMEs which are registered in Eldama Ravine Sub-County, Single Registration Licences (2016). The study laid emphasis on determinants of financial accessibility by SME's in Eldama Ravine Sub-County in Baringo County, Kenya. The number of SMEs have continued to increase and thus resulting to vibrant growth. The study was undertaken within the effect of cost of credit, interest rate, credit rationing and business risk on how they influence access to finance by SMEs operating in Eldama Ravine Sub-County in Baringo County.

1.1.10. 1.6 Significance of the Study

The financiers of the SMEs will be interested with this information since they will be able to evaluate SMEs performance, this will enable them to determine the rate of interest to charge on the amount given as a debt. Financiers are keen on the performance of company so as to get the assurance of adequate returns and timely repayment of the debts. To the firm management team, the capital structure decisions impact on firm performance and as a result the management will be interested to know how the current choices affect the company financial performance, how any change in the capital structure will affect the performance. They will also be enlightened on investment decisions that increase the value of the firm, long term project financing, dividend policy to adopt, financing for possible mergers among other decisions undertaken. To the academicians and scholars, the study will form the basis for future research study. This study will add value to the body of knowledge in areas of capital structure determinant and it effect on financial performance of the SMEs in Kenya.

1.7 Limitations of the Study

The study faced a couple of challenges. Some employees working with SMEs in Eldama Ravine Sub County were not willing to participate in the study for fear of probable reprisals from their bosses. The researcher addressed this challenge by assuring them that the study was for academic purposes and that the data collected were to remain confidential. More so, some managers/owners of the SMEs were skeptical in allowing the research to be carried out in their respective businesses. The researcher informed them that the findings of the study were likely to benefit their businesses and that there was willingness to share the findings with them and any other interested parties.

CHAPTER TWO

LITERATURE REVIEW

1.1.11. 2.1 Introduction

This chapter reviews existing literature on the subject of this study. It discusses the theoretical and conceptual frameworks, empirical review, summary of reviewed literature and research gaps.

1.1.12. 2.2 Theoretical Reviews

This section explores the various theories related to access to credit by SMEs

2.1.1 Transaction Cost Theory

The Transaction Cost Theory was developed by Ferris in 1981. This theory postulates that trade credit use brings down exchange costs. The transaction motive rests on the simplification of payment induced by trade credit. The purpose here is not financing but reducing transaction costs. This theory holds that when transactions between sellers and buyers are frequent both parties may reduce transaction costs by agreeing to a periodical payment schedule This work so long as saving in transaction costs remains more than the cost of holding receivables. Mian and Smith (1992) found that when supply of goods and credit are made from one point there is an overall reduction in costs and increase in efficiency as both the monitoring of supplies and the credit could be done from the same point. Sellers in general, but more particularly those having large inventory can save on warehousing and related costs by effecting sales with attractive credit terms. This is possible when marginal cost of holding inventory is greater than the cost of holding receivables. Firms whose product suffers from high demand fluctuations may resort to trade credit, which is found to be the least cost solution, the others being adjustment of production schedule or effecting price reduction.

The seller could relax credit terms when the demand is slackening and tighten them when demand shows an upswing. This hypothesis of Emery (1987) found support in the empirical findings of Long, Malitz and Ravid (1993) who concluded that firms with high variable demand extend more credit than firms enjoying demand stability. Some writers suggest that by offering trade credit suppliers can defer tax payment or benefit from tax shields in the short run (Mian & Smith, 1992). When buyers and sellers are in different tax brackets, cost of financing is also different, other things remaining constant. A firm in high tax bracket has lower net interest cost than a firm in low tax bracket. Hence, the former has an incentive to offer trade credit to save on marginal tax (Brick & Fung, 1984).

2.2.2 The Capital Channel Model

The bank capital channel model was developed by Chami and Cosimamo in 2001. It is a model in which banks maximize present value of future profits subject to a minimum capital- asset ratio. In anticipating that the capital constraint may bind the future, banks choose and optimal level of dividend payouts each period to minimize this possibility. According to Obamuyi (2007), the bank capital channel views a change in interest rate as affecting lending through bank's capital, particularly when banks' lending is constrained by a capital adequacy requirement. The "bank capital channel" works in the following way. After an increase in market interest rates, a lower fraction of loans can be renegotiated with respect to deposits (loans are mainly long-term, while deposits are typically short-term): banks therefore bear a cost due to the maturity transformation performed that reduce profits and then capital. If equity is sufficiently low (and it is too costly to issue new shares), banks reduce lending because prudential regulations establish that capital has to be at least a minimum percentage of loans (Bolton and Freixas, 2001; Van den Heuvel, 2001).

The bank capital channel model considers the lending behaviors of bank to SMES to be affected by a capital adequacy requirement. Thus, an increase in interest rates will raise the cost of banks' external funding, but reduce banks' profits and capital. The tendency is for the banks to reduce their supply of loans if the capital constraint becomes binding. However, banks could also become more willing to lend during certain periods because of an improvement in their underlying financial condition. This condition as purported by this model, is seen clearly in the relationship between banks and SMEs as the SMEs suffers through a lack of financial assistance as a result of this situation.

2.2.3 Credit Rationing Theory

One of the most important theories that focused on financing gap analysis is the Credit Rationing Theory by Stiglitz and Weiss (1981). In their formulation, Stiglitz and Weiss (1981) argued that agency problems (a conflict of interest between management (agents) and the shareholders (owners) of the organization) and information asymmetries are the major reason why SMEs have constrained access to finance. They argued that only SMEs know their real financial structure, the real strength of the investment project and the effective intention to repay the debt, that is, firms have superior private information (asymmetric information). Hence, the bank manager makes decisions under asymmetric information, and operates under a moral hazard and adverse selection risk.

Stiglitz and Weiss (1981) explained the choice among different financing sources under conditions of asymmetric information and credit rationing. Constrained access to finance derived from financial institutions' credit rationing behavior might not be efficient because managers work under conditions of asymmetric information. This may result in less profitable investments getting financed while more profitable investments are being left out and thus resulting in adverse selection and moral hazard risks. Therefore, asymmetric information can explain asymmetric of credit among firms with identical characteristics, the lenders not being aware of the exact bankruptcy likelihood for the firms, know only that this likelihood is positive and therefore choose to increase debts' cost.

Start-up small firms are more likely to be affected by information asymmetry problems. There are some categories of SMEs that will face additional problems due to lack of security, such as young entrepreneurs or those from deprived areas. In addition, there may be asymmetries arising from location as well as sector. For example, owners of MSEs in rural environments may face difficulties with access to bank finance. Small firms are more likely to be rationed because they are seen as particularly risky. Although they might be willing to pay more to compensate for the additional risk, the banks will refuse to raise the interest rate sufficiently to equate supply and demand.

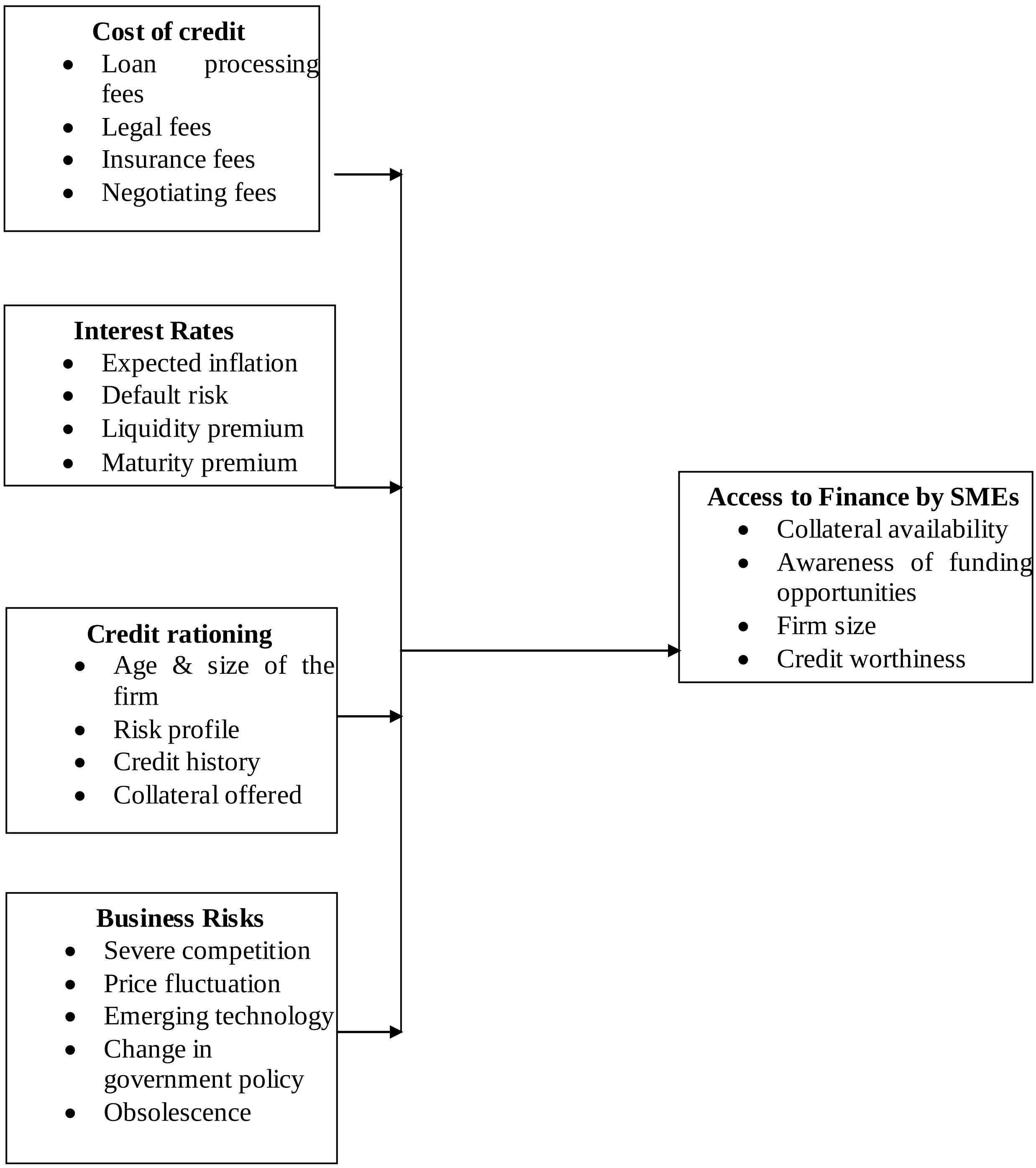
2.2.4 Prospect Theory

Prospect theory was developed by Kahneman and Tversky (1979). In its original form, it is concerned with behavior of decision makers who face a choice between two alternatives. Decision making under risk can be viewed as a choice between prospects or gambles. Decisions subject to risk are deemed to signify a choice between alternative actions, which are associated with particular probabilities or gambles. The theory states that we have an irrational tendency to be less willing to gamble with profits than with losses. Prospect theory is based on the idea that people evaluate gains or losses from some neutral or status quo point, an assumption consistent with the adaptation level findings that occur not just in perception but in virtually all experience. That is, we adapt to a constant level of virtually any psychological dimension and find it to be neutral.

Prospect theory deals with the way we frame decisions, the different ways we label outcomes, and how they affect our attitude towards risk. It helps explain how loss aversion, and an inability to ignore sunk costs, leads people to take actions that are not in their best interest. The sting of losing money, for example, often leads investors to pull money out of the stock market unwisely when prices decline. Prospect theory assumes that investors' utility functions depend on changes in the value of their portfolios rather than the value of the portfolio.

2.3 Conceptual Framework

A conceptual framework is a product of qualitative process of theorization which interlinks concept that together provides a comprehensive understanding of a phenomenon or phenomena (Jabareen, 2009). The concepts that constitute a conceptual framework support one another, articulate their respective phenomena, and establish a framework-specific philosophy that defines relationships. The conceptual framework of this study relates to independent variables; cost of credit, interest rates, credit rationing, business risks and the dependent variable; Access to credit facilities by small and medium enterprises in Eldama Ravine Sub-County in the County Government of Baringo, Kenya.



Independent Variables **Dependent Variable**

Table 2.1: Conceptual Framework of Factors Influencing Access to Finance by SMEs

2.3.1. **Cost of Credit**

The cost of credit accessibility refers to the amount of money the entrepreneurs pay in process of borrowing money from financial institutions. The key indicators of cost in this respect are loan processing fees, negotiation fees, personal insurance and legal fees (Gichuki et al,. 2014). Berger and Udell, (2006) cited in Gichuki et al., (2014) argued that high transaction costs do therefore not only increase the cost of borrowing, but can also restrict access to external finance for some borrower groups. While transaction costs are restraining for all borrowers, there are arguments that they are even more constraining for small and micro enterprises. Their diverse characteristics and their relative opaqueness increases assessment and monitoring costs. Unlike other credit categories, such as consumer credit or mortgage lending, SME lending is still considered a high-cost lending product. More specifically, unlike other lending products that can be reduced to simple transactions, SME lending often still depends heavily on relationships between borrowers and lenders.

Every business needs financing, even though at first glance it might appear that funding is unnecessary (Gichuki et al,. 2014) . Banks have often been criticized for having high interest rates charged on loans. But sometimes, there are factors beyond their control. For example, the amount of interest payable on loans depend on interest rates charged, which is driven by the base lending rate of interest set by the Central Bank of Kenya (CBK). The amount of interest rate charged is sometimes, intertwined with the security of the loan, and the use for which it is to be used, or the nature of the business. That is, the more secure loans are charged low interest rates due to, their low risks involved. This leads MSEs to the Micro Finance Institutions (MFIs), who lend unsustainable interests short term loans (Mutai, 2015).

2.3.2. **Interest Rates**

Saleemi (2007) defined interest rate as the return on capital. Cost of credit can be classified as gross and net interest. Interest rates are usually a percentage of the borrowed amount. High interest rates on credit may discourage SMEs from borrowing reducing the accessibility of credit among them. Banks have often been criticized for having high interest rates charged on loans. But sometimes, there are factors beyond their control. For example the amount of interest payable on loans depend on interest rates charged, which is driven by the base lending rate of interest set by the Central Bank of Kenya (Mole & Namusonge, 2016). The amount of interest rate charged is affected by expected inflation, default risk, liquidity premium and maturity premium. This leads the SME's to the micro finance institution, who lend unsustainable interests short term loans. The high interest rates, discourages the entrepreneurs in this sector from borrowing. It's because the interest payment come out of profit and can be reduced by the borrowing business if profit and trading conditions are unfavorable (Thuranira, 2009). Another contributing factor discouraging interest rates, is the structural weakness inherent in Kenyan banks. They do not have stable source of funding they can only lend on short term basis. Apart from becoming a problem to SME's who seek funding over a number of years, the lending rate is high since the banks may lack stable financial source. All these contribute to the rate being a constraining factor in accessibility to credit among the SME's (Thuranira, 2009).

As a factor affecting accessibility of credit the interest rate charged, on loans ranks high. It also affects the rate of repayment of the loans leading to high rate of default on loans. Banks have been criticized for overcharging their clients by setting high interest rates. Most of these interest rate range from 18-20%. With poor business performance worsened by the global economic depression, most businesses are not only unable to repay their current loans but are discouraged from accessing more credit (Thuranira, 2009). Close monitoring of the lending institution by the central bank is required to avoid escalation of interest rates which discourages growth of the sector by reducing the accessibility of credit. The government should also increase competition in the lending sector by creating a fund exclusively for the micro finance institutions. And create a microfinance department within the central bank, instead of being lent by the commercial banks. This will enable them to borrow at competitive rates. It will enable them to; end at lower interest rates and increase available of loans as they pass the benefits to their clients (Thuranira, 2009).

2.3.3. **Credit Rationing**

The bank's credit rationing behavior may theoretically be influenced by a number of factors which include credit history, age and size of the firm, risk profile and collateral offered (Mole & Namusonge, 2016). Lapar and Graham (1988) argued that the bank's credit rationing behavior against the firm's loan demand can be categorized into three stages: the screening stage, the evaluation stage, and the quantity rationing stage. At the screening stage, the bank manager interviews the potential borrower to determine their eligibility for credit (in terms of their creditworthiness, loan requirements and the terms desired). The manager then decides whether the applicant is sufficiently qualified to apply for a loan or not. At the evaluation stage, the loan officer undertakes a detailed analysis of the viability of proposed investment project (including detailed investigations of the credit history, the type and value of proposed collateral, management of the firm, probability of repayment). Based on this information, the loan officer (and/or the loan committee) makes a decision as to whether it will be profitable for the bank to grant a loan or not (Mole & Namusonge, 2016).

The borrowers deemed to be not creditworthy will be denied loans completely (credit rationed). At the quantity-rationing stage, the bank determines the optimal loan size for a borrower at a given interest rate. The optimal loan size will be determined by the bank taking into account the bank's evaluation of the probability of repayment, the marginal cost of granting the loan, and the value of collateral offered. Quantity rationing refers to a scenario where some borrowers are granted loan amounts that are less than what they had applied for. It is at quantity-rationing stage that the bank fine tunes the loan contract to reflect the bank's subjective evaluation of the riskiness of the loan and of the borrower and the impact of these risks on expected profit (Lapar & Graham ,1988) quoted in (Mole & Namosonge, 2016). Firms for which the repayment of the loan is more uncertain are more risky for the bank, and hence are more likely to be credit rationed. The risk for the bank implies the default risk, being the risk that the firm can't fulfill its obligations to the bank. The degree of risk of the firm may be inferred from the credit history of the borrower, the expected returns of the project, business experience of the firm.

2.3.4. **Business Risks**

Risk factor is another aspect that explains the access to credit facilities by SMEs. Financial risks occur when a firm makes use of debt. In such instances, the firm takes on additional responsibility of financing the debt which is paying interest payments on time (Gichuki et al., 2014). The inability of the firm to pay the interest payments or repay the principal will result in a default that might lead to bankruptcy. As the amount of debt used by the firm increases, the chances of it defaulting will also go up due to constraints on its cash flows as a result of the interest payments. SMEs rely more on external financing, thus the financial risk in the SME sector is most likely to be very high (Gichuki et al., 2014).

The difficulties faced by SMEs in accessing credit facilities are attributed to their perceived higher risk profile. Lending institutions regard SMEs as riskier enterprises for a number of reasons which include severe competition environment, price fluctuation, emerging technology in government policy, obsolescence, inadequate accounting systems, more unpredictable operating environment in the developing and emerging markets, assets not properly registered, delayed payments for the products and services rendered, less equipped in terms of both human and financial resources to withstand economic resources (Van Aardt & Fatoki, 2012). Green (2003) as cited in Gichuki et al., (2014) argued that commercial banks tend to impute a high risk to small enterprises and are therefore reluctant to extend credit to them. Due to their small size and inherent vulnerability to market fluctuations, the mortality rates of small enterprises are relatively high. These firms are, by their very nature, often relatively young and consequently lack a financial history and a track-record of profitable projects. In addition, organization and administrative deficiencies, lower quality management and a lack of appropriate accounting systems may compromise the accessibility and reliability of information from small firms on their repayment capacity.

2.3.5. **Access to Finance**

Lack of access to finance is almost universally indicated as a key problem for SMEs. Credit constraints operate in variety of ways in Kenya where undeveloped capital market forces entrepreneurs to rely on self-financing or borrowing from friends or relatives which is not enough to enable SMEs undertake their business activities optimally. Lack of access to long-term credit for small enterprises forces them to rely on high cost short term finance. There are various financial challenges that face small enterprises. They include the high cost of credit, high bank charges and fees (Kamunge et al., 2014). There is no structured institutional mechanism in Kenya to facilitate the flow of financial resources from the formal sector through micro finance institutions to such enterprises. Generally, such enterprises operate on tight budgets, often financed through owner's own contribution, loans from friends and relatives and some bank credit. They are often unable to procure adequate financial resources for the purchase of machinery, equipment and raw materials as well as for meeting day-to-day expenses (Gichuki et al., 2014).

Interest in access to finance has increased significantly in recent years, as growing evidence suggests that lack of access to credit prevents low-income household and small firms from financing high return investment projects, having an adverse effect on growth and poverty alleviation (Gichuki et al., 2014). Nalwelishe (2003) as cited in Ondieki, Nashappi, and Moraa (2013) carried out a research on sources of finance available to small scale enterprises in Nairobi. The objectives of the study were to identify which types of credit are easily obtainable by SMEs and to evaluate the credit policies of SMEs. On access to credit, majority of entrepreneurs relied on limited own and family savings for start-up and additional capital. They hardly rely on external sources of finance. Therefore, these enterprises have poor access to credit. Concerning supply of credit; urban-located enterprises were noted to have achieved a higher success rate than the rural ones.

1.1.13. 2.4 Empirical Literature

This section puts into perspective review of past empirical studies on determinants of financial accessibility by small and medium enterprises in Kenya.

2.4.1 Cost of Credit

Gichuki et al., (2014) in their study on challenges facing MSEs in accessing credit facilities in Kangemi Harambee Market in Kenya, found out that access to credit facilities by micro and small enterprises is highly limited by high repayment cost of credit given. The study therefore recommended that the management of credit giving institutions should consider lowering their interest rates as a way of encouraging MSEs to borrow from them. Gitari, (2012) in her study on factors affecting women entrepreneurs' financial performance in Kenya: a case of Ngara Market found out that lack of information on who is offering what and the cost of obtaining such services limit them and that high inventory costing are some of the major drawbacks for success in women entrepreneurship. The high cost of running the entrepreneurs is a big threat to the women development due to lack of adequate capital and on the other hand lack of information on how to access funds to boost the business also is a major threat.

2.4.2 Interest Rates

Bowen et al., (2009) in their study on Management of Business Challenges Among Small and Micro Enterprises in Nairobi Kenya found out that SMEs face the following challenges; competition among themselves and from large firms, lack of access to credit, cheap imports, insecurity, high interest rates and debt collection. Amonoo et al., (2003) on their study The Impact of Interest Rates on Demand for Credit and Loan Repayment by the Poor and SMEs in Ghana, found that demand for credit among firms in Ghana is also influenced by interest rate charged as well as the owners' equity and firm's annual profit. There is a negative relationship between interest rate (defined as the lending rate at which SMEs borrow from lending institutions) and SMEs' demand for credit and loan repayment at both bank and non-bank financial institutions.

2.4.3 Credit Rationing

Maziku (2012) in the study credit rationing for SMEs for commercial bank loan market in Tanzania, revealed that long term loan is more rationed compared to short term loan. Furthermore, findings from both SMEs owner and credit officers revealed that credit rationing in Tanzania appears to be driven primarily by business and entrepreneur characteristics , managerial competence of owner, quality of business information and poor quality accounting practices , borrower understanding of banks requirements for obtaining credit, inadequacy of collateral, poor relationship with banks and lack of credit history and supply side conditions - inflexible loan eligibility criteria, cumbersome analysis of loan applications, unfavorable credit terms and conditions such as higher interest rate and commissions charged by banks and excessive collateral requirements in comparison to loan value, higher monitoring costs and corruption of bank officials.

2.4.4 Business Risks

Waari (2015) in the study factors influencing access to finance by MSMEs in Meru County established that 47.6% of the MSME‟s have high credit risk exposure due to them operating more than two loans. This raises their credit risk profile which the lenders may not be aware of. The research is consistent with the literature review that established that MSME‟s have poor credit risk mitigation measures. Makena (2011) in the study Challenges faced by SMEs in access to finance in Kiambu town, clearly demonstrated that SME are usually more credit constrained than other segments of the economy because of financial sector policy distortions, lack of collateral, information asymmetries, lack of sufficient collateral as well as high risks inherent in lending to SMEs.

2.5 Summary of Reviewed Literature

Transaction cost theory can be employed to address the issue of high transaction cost of lending to SMES. Studies have established that when transactions between sellers and buyers are frequent both parties may reduce transaction costs by agreeing to a periodical payment schedule. Sellers in general, but more particularly those having large inventory can save on warehousing and related costs by effecting sales with attractive credit terms. This is possible when marginal cost of holding inventory is greater than the cost of holding receivables. Unlike other lending products that can be reduced to simple transactions, SME lending often still depends heavily on relationships between borrowers and lenders.

The bank capital channel model can be employed to address the issue of high interest rates on bank loans. High interest rates on credit may discourage SMEs from borrowing reducing the accessibility of credit among them. After an increase in market interest rates, a lower fraction of loans can be renegotiated with respect to deposits. Loans are mainly long-term, while deposits are typically short-term. Banks therefore bear costs due to the maturity transformation performed that reduce profits and then capital. Lower interest rates will encourage SMEs to access more credit and also reduce the rate of default on loans.

The credit rationing theory is relevant to SMEs as it is argued that only SMEs know their real financial structure, the real strength of the investment project and the effective intention to repay the debt, that is, firms have superior private information (asymmetric information). Hence, the bank manager makes decisions under asymmetric information, and operates under a moral hazard and adverse selection risk. Bank credit rationing has usually been influenced by observable characteristics e.g age, firm characteristics e.g business experience and loan characteristics e.g amount demanded. Small firms are more likely to be rationed because they are seen as particularly risky although they might be willing to pay more to compensate for the additional risk.

Prospect theory is relevant to SMEs because it is concerned with behavior of decision makers who face a choice between two alternatives. It deals with the way we frame decisions, the different ways we label outcomes and how they affect our attitude towards risk. The degree of risk of the firm has been inferred from its credit history, expected returns and business experience of the firm. The more risky the product, the lower is the expected value of the purchase. This will address the risk factor in lending to SMEs.

2.6 Research Gaps

Wangai and Omboi (2011) did a study on factors influencing demand for credit among small scale investors. Their study limited itself to the individual characteristics of the borrower and their influence towards access to credit facilities as opposed to financial factors. Gichuki, Njeru and Tirimba (2014) also did a study on challenges facing micro and small enterprises in accessing credit facilities in Kangemi Harambee Market in Nairobi City County. Their study failed to include medium enterprises and concentrated on general factors as opposed to financial factors influencing access to finance.

Waari and Mwangi, (2015) did a study on factors influencing access to finance by micro, small and medium enterprises in Meru County. The study also concentrated on general factors as opposed to financial factors influencing access to finance by MSMEs. Makena, (2011) did a study on challenges faced by small and medium enterprises accessing finance in Kiambu town. The study limited itself to the individual characteristics of the borrower and their influence towards access to credit facilities as opposed to financial factors. Therefore, the present study will seek to bridge these gaps by examining the financial factors influencing access to finance by SMEs in Kenya.

CHAPTER THREE

RESEARCH METHODOLOGY

1.1.14. 3.1 Introduction

This chapter discusses the research design adopted in carrying out the study. It also states and discusses the population of the study, sampling technique and sample size, research instrument, pre-testing of research instruments, data collection procedure and data processing and analysis. It further states how the study results were presented.

1.1.15. 3.2 Research Design

Research design is the arrangement of conditions for collection and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure (Kothari, 2004). In respect to this study, a cross-sectional survey research design was adopted. Cross-sectional surveys are part of descriptive studies and sought to put into perspective the views of respondents participating in a study over a specific point in time or over a given period of time (Kothari, 2008). These attributes justify the choice of cross-sectional research design for this study.

1.1.16. 3.3 Target Population

The target population is that population to which the researcher wants to generalize the results of the study (Mugenda & Mugenda, 2003). The target population for this study were all proprietors of the SMEs in Kenya. Accessible population refers to that population which is part of the target population and from which the sample is obtained (Kothari, 2008). Accessible population were 286 proprietors of SMEs in Eldama Ravine Sub-County in the County Government of Baringo.

1.1.17. 3.4 Sampling Technique and Sample Size

A sample is a subset of the accessible population. In this respect, all the 286 proprietors of SMEs in Eldama Ravine Sub-County in the County Government of Baringo constituted the accessible population. In view of this, a representative sample was calculated from the accessible population using Nassiuma's (2000) formula as hereby illustrated.

$$n = \frac{NC^2}{C^2 + (N-1)e^2}$$ Where:

n = Sample Size

N = Population Size

C = coefficient of variation (21% ≤ C ≤ 30%)

e = error margin (2% ≤ e ≤ 5%)

Substituting the equation:

$$n = \frac{286\,(0.21)^2}{0.21^2 + (286-1)0.025^2}$$

n =56.8

n = 57 respondents

This implies that the sample population constituted 57 proprietors of SMEs in Eldama Ravine Sub-County, Baringo County. Simple random sampling was used to obtain 16 respondents from proprietors of small enterprises and 41 from those of medium enterprises as shown in Table 3.1. This sampling method is necessitated by the fact that it ensures that there is fair and equitable selection of respondents from each of the groups of SMEs in Eldama Ravine Sub-County in the County Government of Baringo.

Table 3. 1: Sampling Distribution

Group	Proprietors	Sampling size	Percentage (%)
1. Small Enterprises	80	16	28
2. Medium Enterprises	206	41	72
Total	**286**	**57**	**100**

1.1.18. 3.5 Research Instrument

This study used a self-administered semi-structured questionnaire to collect data. Questionnaires are the most appropriate tools for collecting data in survey studies since it is possible to administer them on a relatively large number of respondents. The instrument was structured in a way that enabled collection of data that would objectively address all study variables. Secondary data was collected using data collection sheet.

1.1.19. 3.6 Pre-Testing of Research Instruments

A pre-testing of questionnaires was conducted before carrying out the main study. The pilot study involved 10% the size of the sample (Kothari, 2004). This equaled to 6 respondents who were randomly drawn from Eldama Ravine Sub-County in the County Government of Baringo. The participants in the pre-testing were not involved in the final study. The main aim of pre- testing the research instrument is to ensure that it is both valid and reliable for data collection.

1.1.20. 3.6.1 Validity Testing

Validity test seeks to determine whether the instrument is able to serve the purpose of collecting the purported data. A valid instrument must meet the reliability threshold (Kimberlin & Winterstein, 2008). This study used on content validity which was determined through expert opinion of university supervisor.

1.1.21. 3.6.2 Reliability Testing

Reliability is described as a measure of internal consistency of a research instrument or data collection tool. This study employed the Cronbach alpha coefficient which is the most widely used and recommended test of reliability. Using the Cronbach alpha coefficient, reliability ranges from 0 to 1 with higher values indicating greater reliability. The reliability threshold is alpha coefficient 0.7 for each study construct (Kimberlin & Winterstein, 2008).

1.1.22. 3.7 Data Collection Procedure

Before collecting data, consent of the University and that of the proprietors of the SMEs in Eldama Ravine Sub-County in the County Government of Baringo was sought. The questionnaires were issued to the respondents by the researcher in person. The entire period of data collection was anticipated to be about fourteen days.

1.1.23. 3.8 Data Processing and Analysis

The data collected was analyzed with the help of the Statistical Package for Social Sciences (SPSS) version 21 software. The analysis constituted both descriptive statistics and inferential statistics. Descriptive statistics included frequency, median, mean standard deviation and variances. Inferential statistics included Pearson's Product Moment Correlation (PPMC) and multiple regression analysis. The study results were presented in form of statistical tables.

The following multiple regression function was used.

$$\mathbf{Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon}$$

Where:

Y represents Access to Finance

$\boldsymbol{\beta_0}$ represents Constant

$\mathbf{X_1}$ represents Cost of Credit

$\mathbf{X_2}$ represents Interest Rates

$\mathbf{X_3}$ represents Credit Rationing

$\mathbf{X_4}$ represents Business Risks

$\boldsymbol{\varepsilon}$ represents Error Term

$\boldsymbol{\beta_1, \beta_2, \beta_3, \beta_4}$ represents Regression Coefficients for Independent variables.

CHAPTER FOUR

RESEARCH FINDINGS AND DISCUSSIONS

4.1 Introduction

This chapter presents results arising from the analysis of data collected using questionnaires. The data collected was analyzed using descriptive and inferential statistic for each variable and the findings were presented in tables, charts and graphs.

4.2 Response Rate

Response rate equals the number of people with whom semi-structured questionnaires were properly completed divided by the total number of people in the entire sample (Fowler, 2004). The study had a sample size of 57 respondents. Out of 57 respondents, 48 responses were obtained giving a response rate of 84%. According to Kothari (2004) any response of 50% and above is adequate for analysis thus 84% was excellent. The results of response rate are presented in Table 4.1.

Table 4.1: **Response Rate**

Target No. of respondents	No. of Questionnaires Returned	Response Rate (%)
57	48	84

1.1.24. 4.3 Background Information

The study collected information pertaining the gender, level of education, duration of business existence, type of business, number of employees and business license and document among SME's in Eldama Ravine Sub-County, Kenya.

4.3.1 Distribution of Respondents by Gender

The respondents were requested to indicate their gender. The results were as shown in Figure 4.1.

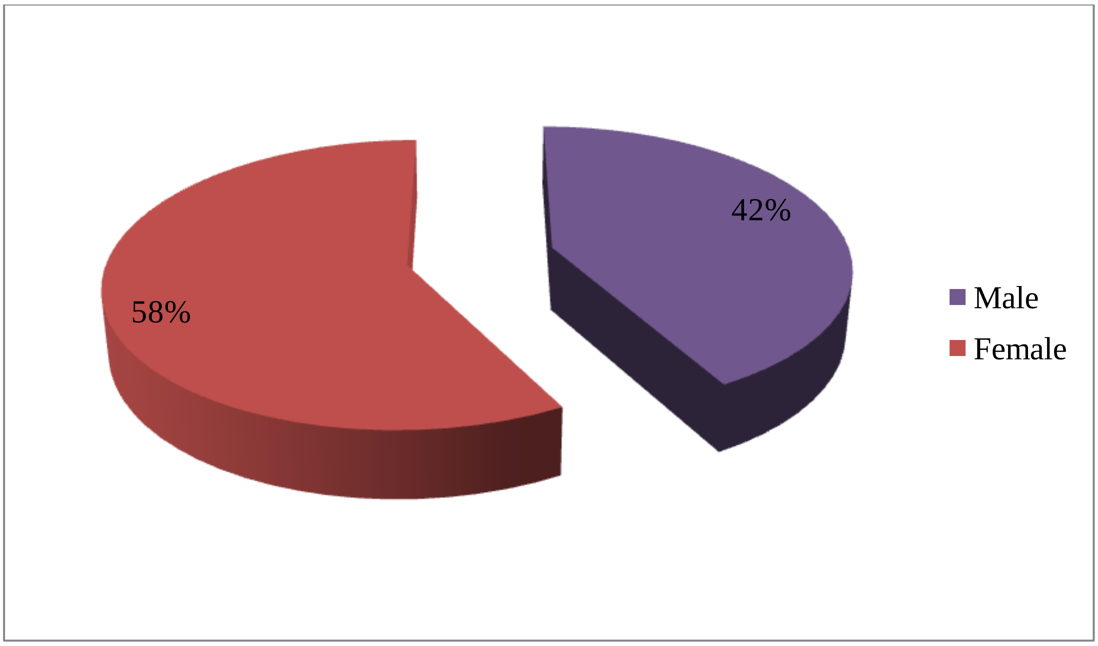


Figure 4.1: Distribution of Respondents by Gender

According to the findings, 58% of the respondents were female while 42% of the respondents were male. This implies that majority of proprietors of SMEs in Eldama Ravine Sub-County were female. Gender has an influence on the type of business.

4.3.2 Distribution of Respondents by Academic Qualifications

The respondents were asked to indicate their highest level of education. The findings were as shown in Table 4.2.

Table 4.2: Distribution of Respondents by Academic Qualifications

	Frequency	Percentage
Primary	2	4%
Secondary	2	4%
College	35	73%
University	9	19%
Total	**48**	**100**

From the findings, 73% of the respondents indicated they had attained a college education, 19% stated they had attained university degree while 4% of the respondents indicated that they had attained primary and secondary education each. This shows that majority of the respondents had attained college education.

1.1.25. 4.3.3 Duration of Business Existence

The respondents were asked to indicate the duration their businesses have been in operation. The findings were as presented in Table 4.3.

Table 4.3: Duration of Business Existence

Years	Frequency	Percentage
Less than 1 Years	2	4%
1-5 Years	19	40%
6-10 Years	13	27%
More than 10 Years	14	29%
Total	**48**	**100**

According to the findings, 40% stated they had been operational for 1-5 years, 29% stated they had been operational for more than 10 years, 27% stated they had been operational for 6-10 years while 4% of the respondents indicated their businesses had been operational for less than 1 year. This shows that majority of the businesses had been operational for 1-5 years.

4.3.4 Type of Business

The respondents were requested to indicate the type of businesses they operate. The results were as shown in Figure 4.2.

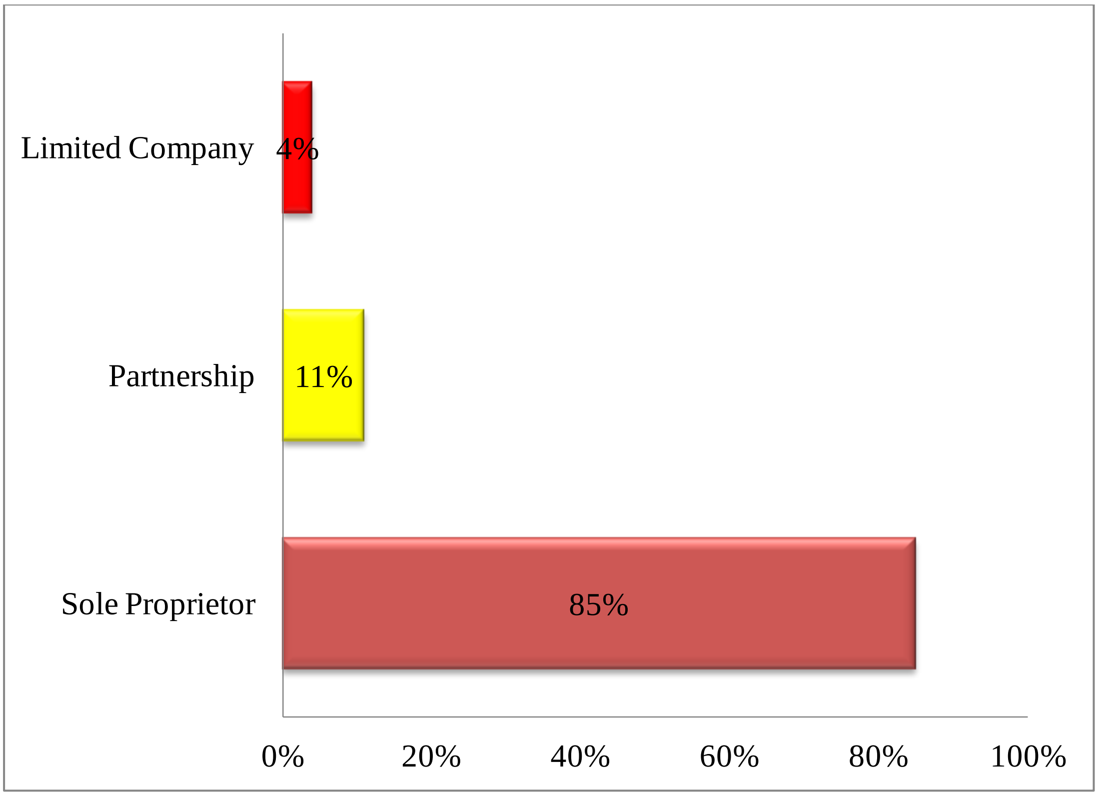


Figure 4.2: Type of Business

According to the findings, 85% of the business in Eldama Ravine Sub-County are sole proprietorships, 11% are partnerships while 4% are limited companies. This implies that majority of the businesses in Eldama Ravine Sub-County are sole proprietorships.

4.3.5 Number of Employees

The respondents were requested to indicate the number employees they have. The results were as shown in Figure 4.3.

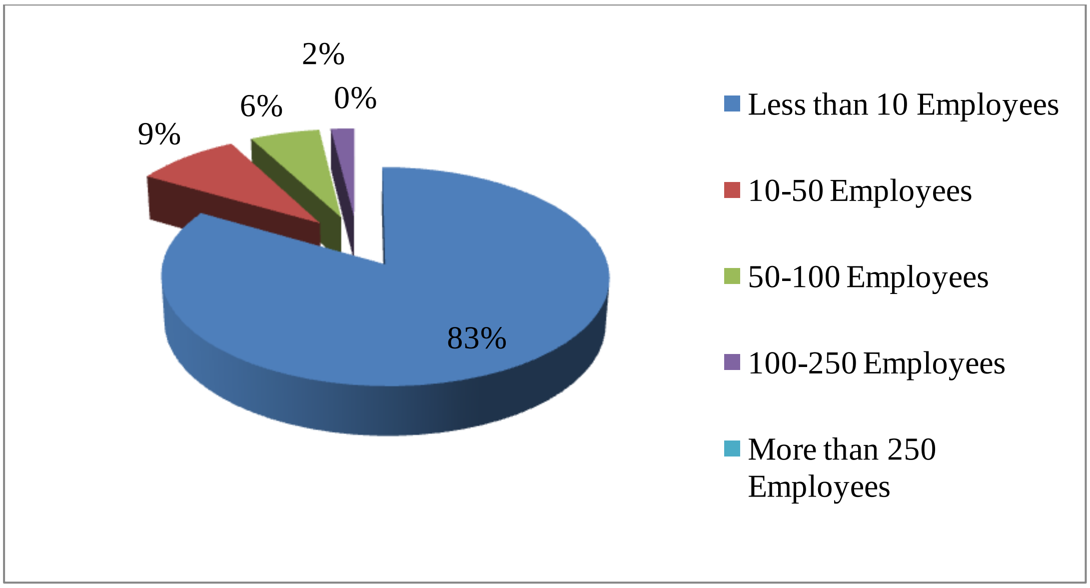


Figure 4. 3: Number of Employees

According to the findings, 83% of the respondents stated they had employed less than 10 employees, 9% of the respondents stated they had employed 10-50 employees, 6% of the respondents stated they had employed 50-100 employees while 2% stated that had employed 100-250 employees. This implies that majority of businesses in Ravine town had less than 10 employees.

4.3.6 Business Licences and Documents

The respondents were requested to indicate the various business licence they have. The results were as shown in Table 4.4

Table 4.4: Business Licences and Documents

Business Licences and Documents	Frequency	Percentage
VAT Registration Certificate, County Council Single Permit, PIN Certificate, Tax Compliance Certificate, Annual Tax Returns and Monthly VAT Returns	32	41
VAT Registration Certificate, County Council Single Permit and PIN Certificate	33	43
County Council Single Permit	12	16

From the findings, 43% stated they only have VAT Registration Certificate, County Council Single Permit and PIN Certificate, 41% of the businesses under study have all the licences and documentation (VAT Registration Certificate, County Council Single Permit, PIN Certificate, Tax Compliance Certificate, Annual Tax Returns and Monthly VAT Returns) needed to operate a business, while 16% of the respondents stated they only have County Council Single Permit. This implies that majority of businesses operating in Eldama Ravine Sub-County have all the licences and documents needed to operate a business.

1.1.26. 4.4 Descriptive Findings and Discussions

The study requested respondents to give opinions in regard to cost of credit, interest rate, credit rationing and business risk on financial accessibility among SMEs in Eldama Ravine Sub-County in the County Government of Baringo. The responses were on a scale of five points where 5, 4, 3, 2, and 1 represented strongly agree, agree, not sure, disagree, and strongly disagree respectively.

1.1.27. 4.4.1 Cost of Credit

The study analysed the views of respondents in respect of cost of credit on financial accessibility by SME's. The results of the analysis are as shown in Table 4.5

Table 4.5: Descriptive Statistics for Cost of Credit

Cost of Credit	N	Min	Max	Mean	Std. Deviation
SMEs incur huge costs on loan processing fees.	48	1	5	3.92	.679
Legal fees incurred by SMEs while borrowing funds has reduced in the recent past.	48	1	4	1.92	1.069
Insurance fees have drastically reduced as a result of financial institutions partnering with insurance companies.	48	1	5	3.73	.917
Negotiation fees with financial institutions have reduced in the recent past.	48	1	4	2.10	1.171

According to the findings, the respondents agreed that SMEs incur huge costs on loan processing fees (mean ≈ 3.92; std dev = 0.679). They also agreed that insurance fees have drastically reduced as a result of financial institutions partnering with insurance companies (mean ≈ 3.73; std dev = 0.917). However they disagreed that the negotiation fees with financial institutions have not reduced in the recent past (mean ≈ 2.10; std dev = 1.171) and legal fees incurred by SMEs while borrowing funds have not reduced in the recent past (mean ≈ 1.92; std dev = 1.069). The study is in agreement with Gichuki et al., (2014) who argued that high transaction costs increase the cost of borrowing and also restrict access to external finance for some borrower groups.

1.1.28. 4.4.2 Interest Rate

The study put into perspective the opinions of respondents regarding the influence of interest rate on financial accessibility by SME's**.** The results are as shown in Table 4.6

Table 4. 6: Descriptive Statistics for Interest Rates

	N	Min	Max	Mean	Std. Deviation
High expected inflation rate in the country has led to rise in interest rates.	48	1	5	4.12	.767
SMEs are deemed to have high default risk by lending institutions hence high interest rates are applied when they borrow.	48	1	5	3.98	1.285
A less liquid security attracts high interest rate.	48	1	5	2.48	1.255
Interests on loans vary depending on length of time to maturity an obligation bond takes.	48	1	4	4.00	.923

According to the findings, the respondents agreed that high expected inflation rate in the country has led to rise in interest rates (mean = 4.12; std dev = 0.767). The respondents also agreed that interests on loans vary depending on length of time to maturity an obligation bond takes (mean =4.00; std dev = 0.923).The respondents also admitted that SMEs are deemed to have high default risk by lending institutions hence high interest rates are applied when they borrow (mean =3.98; std dev = 1.285). Moreover, it was disagreed (mean = 2.48; std dev = 1.255) that less liquid security attracts high interest rate. These findings concurred with the observations of an earlier study by Namusonge, (2016) that the amount of interest rate charged is affected by expected inflation, default risk, liquidity premium and maturity premium.

1.1.29. 4.4.3 Credit Rationing

The study sought to establish the effect of credit rationing on financial accessibility. The respondents were asked to indicate the aspect of credit rationing on financial accessibility by SMES. The results were as shown in table 4.7

Table 4.7: Descriptive Statistics for Credit Rationing

	N	Min	Max	Mean	Std. Deviation
Older and large enterprises are not denied loans (credit rationed).	48	1	5	3.60	1.162
Firms with good credit history are not denied loans.	48	1	5	4.06	.998
Risky ventures are credit rationed by banks in most cases.	48	1	5	3.50	.945
Firms that offer highly valued collaterals are not credit rationed.	48	1	5	3.52	1.131

From the findings, the respondents agreed that firms with good credit history are not denied loans (mean = 4.06; std dev = 0.998). They also agreed that older and large enterprises are not denied loans (credit rationed) (mean = 3.60; std dev = 1.162). They further agreed that risky ventures are credit rationed by banks in most cases (mean =

3.50; std dev = 0.945). The respondents also agreed that firms that offer highly valued collaterals are not credit rationed (mean = 3.52; std dev = 1.131). The findings of the study tallied with Namusonge, (2016) who states that borrowers deemed to be not creditworthy are denied loans completely (credit rationed).

4.4.4 Business Risks

The study sought to establish influence of business risk on financial accessibility. The respondents were asked to indicate the effect of business risk on financial accessibility by SMEs. The results were as shown in Table 4.6

Table 4.8: Descriptive Statistics for Business Risks

	N	Min	Max	Mean	Std. Deviation
SMEs face severe competition.	48	1	5	3.54	.898
Price fluctuations of commodities negatively affect profitability of SMEs in most cases.	48	1	5	4.21	.798
Emerging technology in government policy has negatively affected most SMEs operations.	48	1	5	3.12	1.347
Assets of most SMEs face the risk of obsolescence therefore may not be offered as collateral.	48	1	5	3.95	.978

The study revealed that the respondents concurred that price fluctuations of commodities negatively affect profitability of SMEs in most cases (mean = 4.21; std dev = 0.798). The respondents also agreed that the assets of most SMEs face the risk of obsolescence therefore may not be offered as collateral (mean = 3.95; std dev = 0.978). SMEs face severe competition (mean = 3.54; std dev = 0.898). They also agreed that emerging technology in government policy has negatively affected most SMEs operations (mean = 3.12; std dev = 1.347). The findings supported earlier findings in a study conducted by Gichuki et al., (2014) who argued that commercial banks tend to impute a high risk to small enterprises and are therefore reluctant to extend credit to them.

4.4.5 Financial Accessibility

Lastly, the study sought to establish financial accessibility by SMEs. The results were as shown in table 4.9

Table 4.9: Descriptive Statistics for Financial Accessibility

	N	Min	Max	Mean	Std. Deviation
Lack of collateral has led to poor access of credit by SMEs.	48	1	4	4.02	.729
Lack of awareness on funding opportunities has led to poor access to credit by SMEs.	48	1	4	4.10	.973
Large enterprises are likely to access credit easily compared to medium and small enterprises	48	1	5	4.15	1.031
Borrowers deemed to be not credit worthy are denied loans completely.	48	1	5	3.81	.938

Respondents admitted that large enterprises are likely to access credit easily compared to medium and small enterprises (mean = 4.15; std dev = 1.031). In addition, the respondents concurred that lack of awareness on funding opportunities has led to poor access to credit by SMEs (mean = 4.10; std dev = 0.973). It was also agreed that lack of collateral has led to poor access of credit by SMEs (mean = 4.02; std dev = 0.729). Finally, the respondents agreed that borrowers deemed to be not credit worthy are denied loans completely (mean = 3.81; std dev = 0.938). The study agreed with Kamunge et al. (2014) who indicated that there are various financial challenges that face small enterprises which include the high cost of credit, high bank charges and fees among others.

1.1.30.

1.1.31.

1.1.32. 4.5 Inferential Findings and Discussions

This section puts into perspective the relationship between the independent variables and the dependent variable and also the influence of the independent variable on the dependent variable. Therefore, the section outlines the results of both correlation and multiple regression analysis.

1.1.33. 4.5.1 Relationship between Cost of Credit and Financial Accessibility

The study examined the relationship between cost of credit and financial accessibility by SME's in Eldama Ravine Sub-County. Table 4.10 shows the results of correlation analysis.

Table 4.10: Correlation between Cost of Credit and Financial Accessibility

		Financial Accessibility
Cost of Credit	Pearson Correlation	-0.948**
	Sig. (2-tailed)	.000
	N	48

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

According to the findings the relationship between cost of credit and financial accessibility by SME's in Eldama Ravine Sub-County is negative, strong and significant ($r = -0.948$; $p < 0.01$). The results implied that as cost of credit increase financial accessibility reduce and the reverse was true As such in order to ensure financial accessibility is enhanced financial institutions should reduce the cost of credit.

1.1.34. 4.5.2 Relationship between Interest Rate and Financial Accessibility

The study determined the relationship between interest rate and financial accessibility by SME's in Eldama Ravine Sub-County. The results of correlation analysis are as shown in Table 4.11.

Table 4.11: Correlation between Interest Rates and Financial Accessibility

		Financial Accessibility
Interest Rates	Pearson Correlation	-0.562**
	Sig. (2-tailed)	.001
	N	48

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

As indicated in Table 4.11 the relationship between interest rate and financial accessibility by SME's in Eldama Ravine Sub-County is negative, moderately strong and significant ($r = -0.562$; $p < 0.01$). The results implied that as interest rates increase financial accessibility reduces and the reverse was true. As such in order to ensure financial accessibility is enhanced financial institutions should reduce the interest rates.

1.1.35. 4.5.3 Relationship between Credit Rationing and Financial Accessibility

The study determined the relationship between credit rationing and financial accessibility by SME's in Eldama Ravine Sub-County. The results of correlation analysis are as shown in Table 4.12.

Table 4.12: Correlation between Credit Rationing and Financial Accessibility

		Financial Accessibility
Credit Rationing	Pearson Correlation	-0.566**
	Sig. (2-tailed)	.007
	N	48

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

As indicated in Table 4.12 the relationship between credit rationing and financial accessibility by SME's in Eldama Ravine Sub-County is negative, moderately strong and significant ($r = -0.566$; $p < 0.01$). The results implied that as credit rationing increase financial accessibility reduces and the reverse was true. As such in order to ensure financial accessibility is enhanced financial institutions should reduce the credit rationing.

1.1.36. 4.5.4 Relationship between Business Risk and Financial Accessibility

In addition the study analyzed the relationship between business risk and financial accessibility by SMEs in Eldama Ravine Sub-County. The relevant findings are illustrated in Table 4.13.

Table 4.13: Correlation between Business Risk and Financial Accessibility

		Financial accessibility
Business Risk	Pearson Correlation	-0.948**
	Sig. (2-tailed)	.017
	N	48

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

The results of correlation analysis (Table 4.13) indicated that the relationship between business risk and financial accessibility by SME's in Eldama Ravine Sub-County is negative, strong and significant ($r = -0.948$; $p < 0.01$). The results implied that as business risk increase financial accessibility reduces and the reverse was true. As such in order to ensure financial accessibility it is important that SMEs reduce the risks of their businesses.

1.1.37. 4.5.5 Influence of Financial Factors on Financial Accessibility

The study evaluated the effect of financial factors (cost of credit, interest rate, credit rationing and business risk) on financial accessibility by SME's in Eldama Ravine Sub-County in the County Government of Baringo. The foregoing was achieved through multiple regression analysis. The pertinent results are as shown in Tables 4.14, 4.15 and 4.16.

Table 4.14: Model Summary

B	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.726[a]	.527	.246	.50555

a. Predictors: (Constant), Cost of Credit, Interest Rate, Credit Rationing, Business Risk

As illustrated in Table 4.14, the relationship between financial factors under investigation and financial accessibility was positive and strong. The R-Squared is the proportion of variance in the dependent variable which can be explained by the independent variables. The R-squared in this study was 0.527, which shows that the four independent variables (cost of credit, interest rate, credit rationing and business risk) can explain 52.7% of financial accessibility by SME's while other factors explain 47.3.

Table 4.15: ANOVA[b]

Model		Sum of Squares	Df	Mean Square	F	Sig.
	Regression	37.061	5	7.403	31.097	.000[b]
1	Residual	17.379	72	.238		
	Total	54.395	78			

a. Dependent Variable: Financial Accessibility

b. Predictors: (Constant), Cost of Credit, Interest Rate, Credit Rationing, Business Risk

The findings indicated in Table 4.15 show that the association between the financial factors and financial accessibility was positive and statistically significant ($F=31.097$; $p < 0.05$). Therefore the financial factors investigated were fundamental in financial accessibility by SMEs in Eldama Ravine Sub County. The results also indicate that the model was statistically significant.

Table 4.16: Regression Coefficients[a]

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	1.207	.443		2.724	.000
Cost of credit	-.083	.177	-.085	-.472	.000
Interest rate	-.070	.157	-.082	-.444	.019
Credit rationing	-.610	.180	-.749	-.393	.001
Business risk	-.204	.155	-.222	-.314	.000

a. Dependent Variable: Financial Accessibility

Table 4.16 shows the overall significant test results for the hypothesized research model.

The interpretations of the findings indicated follow the following regression model.

$$\mathbf{Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon}$$

Therefore,

$$\mathbf{Y = 1.207 - 0.083X_1 - 0.070X_2 - 0.610\, X_3 - 0.204\, X_4}$$

The findings indicated that in order for financial accessibility to be enhanced by 1 unit, cost of credit, interest rate, credit rationing and business risk were supposed to be reduced by 0.083 unit, 0.070 unit, 0.610 unit and 0.204 unit respectively. This ought to have held 1.207 constant. The findings indicated that interest rate was the most fundamental factor that ought to have been considered by SMEs during financial accessibility. The findings also indicated that cost of credit ($t = -0.472$; $p > 0.05$), interest rate ($t = -0.444$; $p > 0.05$), credit rationing ($t = -0.393$; $p > 0.05$) and business risk ($t = -0.314$ $p > 0.05$) did not have significant effect on financial accessibility. In general, the four factors had a significant effect on financial accessibility ($t = 2.724$; $p > 0.05$).

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter focuses on the summary of major findings of the study; both descriptive and inferential. This is followed by a presentation of the conclusions inferred from the findings. The relevant recommendations are then suggested. Finally, the chapter outlines the areas suggested for further research.

5.2 Summary

The major study findings are summarized in this section. It outlines the summary of the findings in line with the objectives of the study.

5.2.1 Cost of Credit and Financial Accessibility

Regarding the effect of cost of credit on financial accessibility, it emerged from the results that SMEs incur huge costs on loan processing fees. It also emerged that insurance fees have drastically reduced as a result of financial institutions partnering with insurance companies. However the negotiation fees with financial institutions and legal fees incurred by SMEs while borrowing funds have not reduced in the recent past. The cost of credit should therefore be reduced to ensure financial accessibility with proper management of loan processing fees, negotiation fees and insurance fees. Financial institutions in Eldama Ravine Sub-County should find a relationship that works for benefit of SME's and their growth in lending to their customers.

5.2.2 Interest Rate and Financial Accessibility

The results on how interest rate influences financial accessibility revealed that high expected inflation rate in the country has led to rise in interest rates. It also revealed that interests on loans vary depending on length of time to maturity an obligation bond takes. SMEs are deemed to have high default risk by lending institutions hence high interest rates are applied when they borrow. Moreover, it was disagreed that less liquid security attracts high interest rate. Financial institutions should ensure interest rates are capped to manageable levels so that SME's can access more financial facilities being offered.

5.2.3 Credit Rationing and Financial Accessibility.

Regarding the effect of credit rationing on financial accessibility the study revealed that firms with good credit history, older and large enterprises are not denied loans. The respondents further agreed that risky ventures are credit rationed by banks. In most cases firms that offer highly valued collaterals are not credit rationed. The results indicated with reduced credit rationing, financial institutions will ensure financial services are accessible to SME's. This should therefore mean that credit facilities being offered should not only be tied to firm's good history but also ability to service these credits.

5.2.4 Business Risk and Financial Accessibility

The findings on the effect of business risk on financial accessibility revealed that price fluctuations of commodities negatively affect profitability of SMEs in most cases. It also revealed that assets of most SMEs face the risk of obsolescence therefore may not be offered as collateral. It was further agreed that SMEs face severe competition. Emerging technology in government policy has negatively affected most SMEs operations. It is important that SME's reduce risks in their businesses to ensure increase in financial accessibility.

5.2.5 Financial Accessibility

It was admitted that large enterprises are likely to access credit easily compared to medium and small enterprises. The respondents also concurred that lack of awareness on funding opportunities has led to poor access to credit by SMEs. It was agreed that lack of collateral has led to poor access of credit by SMEs. Respondents also agreed that borrowers deemed to be not credit worthy are denied loans completely. Finally, the financial factors of cost of credit, interest rate, credit rationing, business risk were fundamental in financial accessibilities by SME's in Eldama Ravine Sub County.

5.3 Conclusions

From the findings the study concluded that high transaction costs increase the cost of borrowing and also restrict access to external finance for some borrower groups. The researcher also concluded that insurance fees have drastically reduced as a result of financial institutions partnering with insurance companies. Legal fees incurred by SMEs while borrowing funds has reduced in the recent past.

The study concluded that the amount of interest rate charged is affected by expected inflation, default risk, liquidity premium and maturity premium. It also conferred that a less liquid security attracts high interest rate. Interests on loans vary depending on length of time to maturity an obligation bond takes.

The study concluded that borrowers deemed to be not creditworthy are denied loans completely (credit rationed). Risky ventures are credit rationed by banks in most cases. From the findings the study further concluded that lending institutions consider the size of an enterprise while approving loan application.

The study further concluded that lending institutions tend to impute a high risk to small enterprises and are therefore reluctant to extend credit to them. Assets of most SMEs face the risk of obsolescence therefore may not be offered as collateral. The emerging technology in government policy has negatively affected most SMEs operations

5.4 Recommendations

In the light of the foregoing findings, the study recommends that;

SME lending often depends heavily on relationships between borrowers and lenders, and therefore there is need for the lending institutions to simplify loan application process to avoid unnecessary expenses. This will encourage more SMEs to apply for loans. Lending institutions should also ensure that loan repayment process is flexible for SMEs.

The high interest rates is one of the greatest hindrance of financial accessibility by SMEs. Interest in access to finance has increased significantly in recent years Therefore the government through the ministry of finance should ensure that the set interest rates are adhered to. This will ensure that SMEs are not exploited and are able to access loans.

The study also recommended that SMEs should form groups so as to enable them access loans easily, Majority of financial institutions would prefer group lending compared to individual. This will have a positive impact on the performance of SMEs.

SME are usually more credit constrained than other segments of the economy because of financial sector policy distortions, lack of collateral, information asymmetries, and lack of sufficient collateral as well as high risks inherent in lending to SMEs. Therefore financial institutions should design loan packages for SMEs. They should also train SMEs on proper financial management.

1.1.38. 5.5 Suggestions for Further Studies

The study suggests that a replication of the above study should be carried out in another county in order to establish whether similar findings will be obtained. In addition further research should be carried out to assess the factors affecting loan repayment by SMEs. A study should also be carried out to determine effects of group lending model on loan repayment among SMEs.

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APPENDIX I: LETTER OF INTRODUCTION

Dear Respondent,

REF: <u>REQUEST FOR</u> <u>INFORMATION</u>

I am a Master of Business Administration (MBA) student at Jomo Kenyatta University of Agriculture and Technology (JKUAT). As part of my MBA, I am required to carry out a research project. In tandem, I am collecting requisite data for the project titled: **Financial factors influencing access to finance by Small and Medium Enterprises (SMEs)**. Eldama Ravine Sub County is the focus of the study and you have been selected to participate in the study.

Kindly provide the required data by filling in the questionnaire accompanying this letter. Your participation will be highly valued and appreciated.

Thank you.

Yours faithfully,	University Supervisor
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Stella Chirchir	**Dr. Kimani Maina**

APPENDIX II: RESEARCH QUESTIONNAIRE

Please answer freely the questions below. The information provided will be treated with the highest degree of confidence. When the questionnaire is completed, it should be submitted to the researcher.

Section A: Background Information

1. Gender

a) Male ( )

b) Female ( )

2. Level of education

a) Informal Education ( )

b) Primary ( )

c) Secondary ( )

d) College ( )

e) University ( )

3. Name of your business ---

4. What position do you hold in the organization (optional) -----------------------------

5. When did your firm start business ---?

6. What type of business organization is your firm? Tick where appropriate

Sole Proprietorship { } Partnership { } Limited Company { }

7. How many employees do you have in the business? (Full time and Part time basis including directors and owners)

< 10 10-50 50-100 100-250 >250

8. Which of the following does your organization have? (Please tick all that apply)

a) VAT Registration Certificate ( )

b) County Council Single Business Permit ( )

c) PIN Certificate ( )

d) Tax Compliance Certificate ( )

e) Annual Tax Returns ( )

f) Monthly VAT Returns ( )

Section B: Factors influencing access to finance by SMEs

You are requested to show your level of agreement with the statements under each construct. Kindly use the following scale to indicate your level of agreement. 1 = Strongly Disagree; 2 = Disagree; 3= Not Sure; 4 = Agree; and 5 = Strongly Agree.

Section I: Cost of Credit

	5 Strongly Agree	**4 Agree**	**3 Not sure**	**2 Disagree**	**1 Strongly Disagree**
1. SMEs incur huge costs on loan processing fees.					
2. Legal fees incurred by SMEs while borrowing funds has reduced in the recent past.					
3. Insurance fees have drastically reduced as a result of financial institutions partnering with insurance companies.					
4. Negotiation fees with financial institutions have reduced in the recent past.					

Section II: Interest Rates

	5 Strongly Agree	4 Agree	3 Not sure	2 Disagree	1 Strongly Disagree
1. High expected inflation rate in the country has led to rise in interest rates.					
2. SMEs are deemed to have high default risk by lending institutions hence high interest rates are applied when they borrow.					
3. A less liquid security attracts high interest rate.					
4. Interests on loans vary depending on length of time to maturity an obligation bond takes.					

Section III: Credit Rationing

	5 Strongly Agree	4 Agree	3 Not sure	2 Disagree	1 Strongly Disagree
1. Older and large enterprises are not denied loans (credit rationed).					
2. Firms with good credit history are not denied loans.					
3. Risky ventures are credit rationed by banks in most cases.					
4. Firms that offer highly valued collaterals are not credit rationed.					

Section IV: Business Risks

	5 Strongly Agree	4 Agree	3 Not Sure	2 Disagree	1 Strongly Disagree
1. SMEs face severe competition.					
2. Price fluctuations of commodities negatively affect profitability of SMEs in most cases.					
3. Emerging technology in government policy has negatively affected most SMEs operations.					
4. Assets of most SMEs face the risk of obsolescence therefore may not be offered as collateral.					

Section V: Access to Finance

	5 Strongly Agree	4 Agree	3 Not sure	2 Disagree	1 Strongly Disagree
1. Lack of collateral has led to poor access of credit by SMEs.					
2. Lack of awareness on funding opportunities has led to poor access to credit by SMEs.					
3. Large enterprises are likely to access credit easily compared to medium and small enterprises.					
4. Borrowers deemed to be not credit worthy are denied loans completely.					

Thank you for your time and cooperation.