ROLE OF CREDIT RATIONING ON FINANCIAL ACCESSIBILITY BY SMALL AND MEDIUM ENTERPRISES IN ELDAMA RAVINE SUB – COUNTY, KENYA

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ABSTRACT
The micro, small and medium enterprises continue to play a critical role in the development process in developing economies. Therefore they continue 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. Risk based lending continues to gain momentum in Kenya and as a result credit rationing for SMEs is imminent. In attempting to gain access to financial services SME continue to face constraints. Thus this research intended to study the role played by credit rationing on financial accessibility by Small and Medium Enterprises in Eldama Ravine Sub–County in Baringo County, Kenya. 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. Data analysis captured both descriptive and inferential statistics. Descriptive statistics included modes, medians, means, standard deviations and variances. The results of the analysis were presented in form of tables, graphs and charts. From the findings the study concluded 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. Majority of financial institution would prefer group lending compared to individual. This will have a positive impact on the performance of SMEs.

Key Words: *Credit Rationing, Financial Accessibility, Small and Medium Enterprises*

1.0 INTRODUCTION

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 Problem Statement

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.

1.2 Objective of the Study
To examine the effect of credit rationing on financial accessibility by SME's in Eldama Ravine Sub-County in Baringo County, Kenya.
1.3 Hypothesis
The relationship between credit rationing and financial accessibility by SME's in Eldama Ravine Sub-County in Baringo County, Kenya is not statistically significant.
1.4 Scope
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.

2.0 LITERATURE REVIEW
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.
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.

3.0 METHODOLOGY

3.1 Research Design
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.

3.2 Target Population
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.

3.3 Sampling Technique and Sample Size
In this study, 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 ($21\% \leq C \leq 30\%$)
e = error margin ($2\% \leq e \leq 5\%$)
Substituting the equation:
n $\quad = \quad \dfrac{286\,(0.21)^2}{0.21^2 + (286\text{-}1)0.025^2}$

n $\quad$ =56.8
n $\quad$ = 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 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 1: Sampling Distribution

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

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. 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. Content validity was determined through expert opinion. Cronbach alpha coefficient was used to test for the reliability.

3.7 Data and Analysis

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. The data collected was analyzed using descriptive statistics and further relationship between credit rationing and access analaysed using Pearson correlation analaysis.

4.0 FINDINGS, DISCUSSIONS AND CONCLUSIONS
4.1 Background Information of Respondents and their Businesses

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. 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.

4.2 Academic Qualifications of SME owner Managers

The respondents were asked to indicate their highest level of education. The findings were as shown in Table 2.

Table 2: 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.

4.3 Experience in Business

The respondents were asked to indicate the duration their businesses have been in operation. The findings were as presented in Table 3.

Table 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.

4.4 Nature of Business Operated

The respondents were requested to indicate the type of businesses they operate. The results were as shown in Figure 1.
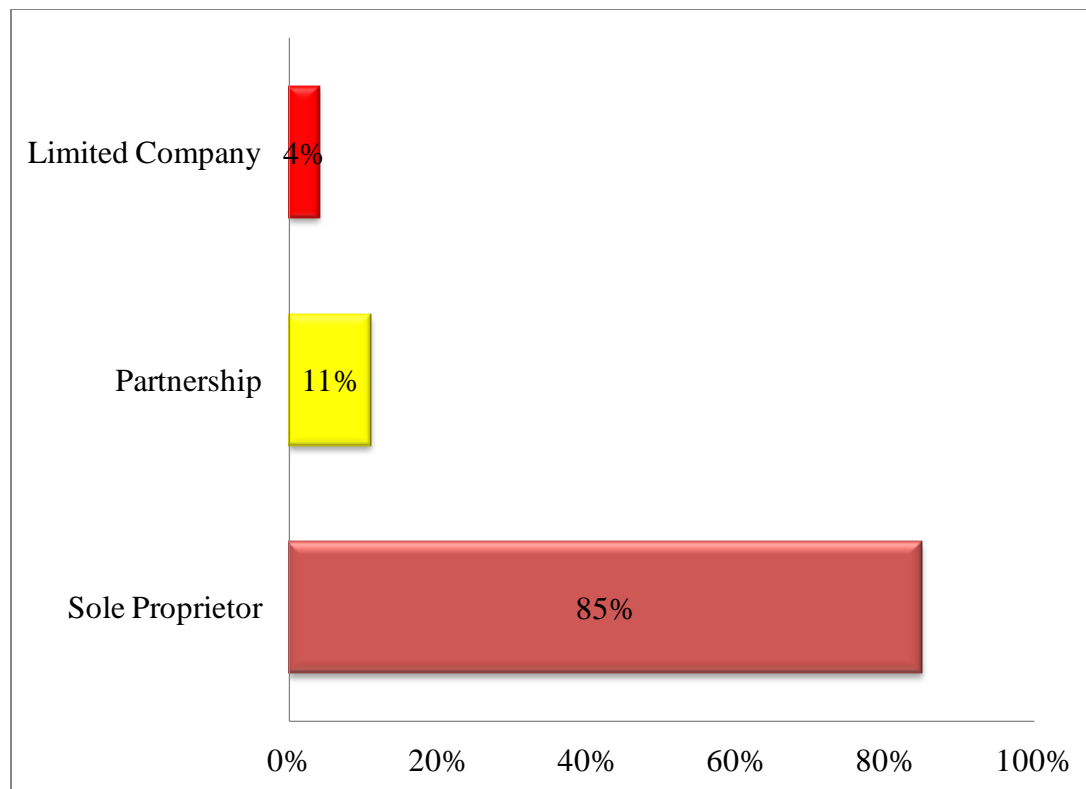
Figure 1: Nature of Business

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.

4.5 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.

4.6 Business Licences and Documents

The respondents were requested to indicate the various business licence they have. The results were as shown in Table 4

Table 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.

4.7 Credit Rationing
The study requested respondents to give opinions in regard to credit rationing and 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. The results were as shown in table 5.

Table 5: 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).

4.8 Financial Accessibility
The study also sought to establish financial accessibility by SMEs. The results were as shown in table 6.

Table 6: 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.

4.9 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 by computing the pearson correlation analysis between the two variables as shown in Table 7.

Table 7: 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.

4.10 Conclusion

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.

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.

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