FINANCING OPTIONS AND FINANCIAL PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES IN NANYUKI TOWN, KENYA

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A RESEARCH PROJECT SUBMITTED TO THE SCHOOL OF BUSINESS IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF DEGREE OF MASTER OF BUSINESS ADMINISTRATION (FINANCE OPTION) OF KENYATTA UNIVERSITY.

OCTOBER 2018
DECLARATION

Declaration by Student

This research project is my original work and has not been submitted for a degree course or any other award in any other University.

Student’s Sign ____________________ Date ______________________

Emily Ndemi
D53/28735/2014

Declaration by Supervisor

I confirm that this research project has been carried out under my supervision

Dr. John Mungai

Signature ______________________ Date ______________________

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School of Business,
Kenyatta University.
DEDICATION

I dedicate this work to my mother Mrs. Faith Ndemi for her inspiration and financial backing in the course of this undertaking. Dedications also go to my son Alvin Ndemi for his patience as I worked for some inordinately long time on this proposal.
ACKNOWLEDGEMENT

Great appreciation and credit is directed to my supervisor Dr. John Mungai for his insights and commitment in influencing this research work. I further acknowledge Dr. Job Omagwa, lecturer at Kenyatta University for further his guidance and motivation. I acknowledge my university, Kenyatta University for preparing me with the right skills to excel not only in the current task but also in the practical career environment.
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## ABBREVIATIONS AND ACRONYMS

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<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>BIS</td>
<td>Business Innovation and Skills</td>
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<tr>
<td>DWEC</td>
<td>Divisional Women Enterprise Committees</td>
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<tr>
<td>FFS</td>
<td>Formal Financial Sector</td>
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<td>GDP</td>
<td>Gross domestic product</td>
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<tr>
<td>IFS</td>
<td>Informal Financial Sector</td>
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<tr>
<td>MDG</td>
<td>Millennium Development Goal</td>
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<tr>
<td>MFI</td>
<td>Micro Finance Institutions</td>
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<tr>
<td>NGO</td>
<td>Non-Governmental Organization</td>
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<tr>
<td>ROA</td>
<td>Return on assets</td>
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<td>ROE</td>
<td>Return on equity</td>
</tr>
<tr>
<td>ROSCA</td>
<td>Rotating Savings and Credit Associations</td>
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<tr>
<td>SACCO</td>
<td>Savings and Credit Cooperative Organization</td>
</tr>
<tr>
<td>SME</td>
<td>Small medium enterprise</td>
</tr>
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<td>YEDF</td>
<td>Youth Enterprise Development Fund</td>
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# OPERATIONAL DEFINITION OF TERMS

<table>
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<tr>
<th>Term</th>
<th>Definition</th>
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<tr>
<td><strong>Financial Performance</strong></td>
<td>Objective assessment of how prudently a company utilizes the resources of its main method of business to produce revenues. It basically evaluates the basic and in general economic health of the firm with a certain time period.</td>
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<td><strong>Financing Options</strong></td>
<td>This entails the alternative methods or sources of funding business engagements or undertakings and include formal and informal credit sources, personal financing and government funds.</td>
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<td><strong>Formal credit financing</strong></td>
<td>Funding from registered financial institutions such as commercial banks, SACCOs and microfinance institutions.</td>
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<tr>
<td><strong>Formal financial sources</strong></td>
<td>They are those sources of credit, which are registered by the government and have to follow its rules and regulations chief among commercial banks and SACCOs.</td>
</tr>
<tr>
<td><strong>Government funds</strong></td>
<td>These are government funded safety nets and affirmative action funds for which the SMEs qualify for loans and grants.</td>
</tr>
<tr>
<td><strong>Informal financing sources</strong></td>
<td>These are members’ only groupings that loan outside any formalized framework or the control of the government regulations like loan sharks popularly known as shylocks.</td>
</tr>
<tr>
<td><strong>Personal financing</strong></td>
<td>Getting business funds from own savings or from close friends, family members or relatives</td>
</tr>
<tr>
<td><strong>Personal sources</strong></td>
<td>Refers to the funding of business from personal savings or ploughing back profits for the growth of the business or starting of green fields.</td>
</tr>
<tr>
<td><strong>Small and medium enterprise</strong></td>
<td>Refers to the type of business that meet the criterion of being independently managed and not a part of a larger enterprise, handled in a personalized fashion, have an easy</td>
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xi
organization structure, are quite small in size and capitalization like shops, butchery and other stores
ABSTRACT

The role of SME in the economy cannot be gainsaid and whereas it is a key pillar of the economy and sustains many families in Kenya, the sourcing of credit for SMEs has always been problematic and comprehensively studied with an increasing bias towards the constraints the SMEs encounter in accessing funding from commercial banks and other lending institutions. There exist many studies on determinants of performance of SME and aspects influencing financial profitability of SMEs in Kenya. However, hardly any of these studies has addressed the constraints that the SMEs face in accessing financing from different sources and how this is related to their performance. Most of the studies dwell on industry or macro-economic variables in the economy and how they affect the SMEs. The study investigated the effect of financing options on the financial performance of SMEs in Nanyuki Town, Kenya. Specifically, the study assessed the effect of formal financing, personal financing, informal financing and government funds on financial performance of SMEs. Financial performance of SMEs was evaluated from a liquidity and profitability point of view for more objectivity. The study was conducted in Nanyuki town which has a fine mix of thriving SMEs that are the drivers of economic life in the town. The target population was made up of the SMEs and their owners in the town. The study targeted 765 SMEs in Nanyuki town. The sample was picked using stratified sampling technique. A sample of eighty-eight respondents was selected. Information was collected using questionnaires deployed utilizing fall as well as choose technique. Data was examined utilizing regression analysis and descriptive statistics aided by SPSS software version 21. The data was presented using tables, graphs, charts and written discussion. Correlation analysis as well as ordinary least squares regression were employed to determine effectively the effect and nature of associations between the variables. The study found poor liquidity condition for the SMEs with both the current ratio and quick ratios standing 1.47:1 and 0.55:1 respectively which are below the globally accepted standards. The profitability of the SMEs was also relatively low with the return on assets standing at an average of 6.67%. Regression analysis results indicate that financing options had significant effect on financial performance of SMEs. The Pearson correlation analysis findings further specified a positive association between all financing options assessed and financial performance of SMEs. The study concludes that the poor state of financial performance indicated by both profitability and liquidity of SMEs could be attributed to financing options among SMEs. Formal financing moderately enhances the financial performance of SMEs. The study also concluded that informal financing was a key source of SMEs’ finance. A conclusion was further made that consumption of informal finance serves to greatly enhance the financial performance of SMEs. Additionally, the study concluded that personal financing was a very significant facility in financing SMEs’ operations which strongly drives the financial performance of SMEs.
CHAPTER ONE
INTRODUCTION

1.1 Background of the Study
The value of small and medium enterprises (SMEs) in the global economy have increased. SMEs are actually starting to be more and more important in terms of innovation development, employment and wealth creation (Nieman, & Nieuwenhuizen, Hough, 2003). Therefore, many governments, multilateral and bilateral agencies and nongovernmental organizations worldwide have policies set up to help the growth of entrepreneurship (Robertson, & Slater, Medeira, Collins, 2003). Rather than being viewed as just primary driving power of growth in the economy, Garikai (2011) notes that SMEs are also viewed as essential for continual development in nearly all economies. Additionally, SMEs are actually a significant employment source, produce considerable export and domestic earnings, add to the common wellness as well as well-being of economies, and therefore are a vital tool of reducing poverty (Mephokee, 2004). This amazing contribution of SMEs to the economy of nations is actually a worldwide phenomenon with substantial contribution in all indicators of economic development.

For example, SMEs comprise 99 percent and 99.7 percent of all employers in the European Union (EU) and United States (US) respectively. The SMEs industry in Kenya engages 74 percent of the national employment and also contributes more than 18 percent of the GDP of the country (Motilewa, Aka & Ogbari, 2015). In general, SMEs are actually identified by way of sales turnover, value of assets as well as turnover the number of workers employed (Garikai, 2011). The benefits of SME have been captured by statistics that actually call for enhanced funding to the sector (Pretorius, Nieman, & Van Vuuren, 2005).

In furtherance of the growth, sustainability and encouragement of spread of SMEs, their capitalization and financing is critical. Hilton, Maher, and Selto (2008) claim that inadequate funding resources and expertise in fiscal control is presently one of the most serious problems. Ineffective financial and funding could harm SMEs profitability and, as
a result, complicate the progress of SMEs and it is a contributing factor to the constrained and short shelf life of SMEs. A report by World Bank disclosed that 39 percent of Micro and small businesses as well as 37% of medium sized businesses in Nigeria face financial constraints (World Bank report, 2001). This is compounded by the reality that the source financial backing for start up business determines the consequent results of SMEs. Understandably, informal and formal types of financing, have been defined by earlier researchers, practitioners and scholars to have a few in constructed qualities that either foster or constrain the progress of SMEs throughout the world (Suleiman & Aruwa, 2004).

1.1.1 Financing Options
The financing of SME has been proportionately addressed and resolved in the developed world, but it still remains a serious challenge to growth and sustainability of SMEs in Africa and the developing world. The following are the options of financing SMEs in the developing world according to Fatoki (2014) who suggested that SMEs must begin businesses with inside equity before shifting to various other sources of finance. Equity could be largely categorized into external equity and internal equity. Inside equity which may be discussed mainly as retained earnings, contributions from friends and family and owners' contributions is employed a lot more extensively by SMEs (Ou & Haynes, 2006). There has been some significant literature on the use of personal resources to fund SMEs. Proprietors of a new enterprises donate ‘sweat equity’ to the business. It is crucial for the firm proprietor to get a few private assets for the new enterprise, and this usually emanates from individual savings. Additionally, many outside financiers are reluctant to invest in a business that the proprietors have not invested heavily in (Kendall, Mylenko, & Ponce, 2010). Additionally, contribution from friends as well as family is yet another crucial finance source for emerging SMEs. This type of financial input is usually termed "love money" which comprises of loans, outright presents and investments. Mac, Bhaird and Lucey (2010) postulate that internally generated funds provide little cash outflows and hence providing adequate long-term funding for the business.

Some scholars who are categorically opposed to use of credit or borrowing for SMEs aver that SMEs should be funded internally. Ebiringa (2011), for instance, contend that
the usage of inside equity by small enterprises has particular benefits. First, it provides management of SMEs with flexibility. Additionally, SMEs stay away from costs like legal, accounting, and underwriting costs when working with inside funds. Inside equity could additionally help SME proprietors sustain control of their enterprises. A new SME usually requires sourcing outside capital to fund development as inside equity is usually inadequate and limited. The study assessed the proliferation of usage of internal equity in financing SMEs (Scott & Irwin, 2010).

Alternatively, there has been advocacy for the usage of debts to finance SMEs by practitioners as well as scholars. Zhang, Hedges and Wu (2007) for instance describe debt as any outside form of financing that obligates the firm to make periodic or regular payments of interest and principal. Feakins (2004), indicate that commercial banks remain one of the key sources of debt to established businesses and for energizing SMEs. Commercial banking sector offers new enterprises an extensive variety of financial services. These services cover every element of the economic sector like, term loans, trade bill financing, government loan guarantee schemes, factoring, leasing, import and export finance, as well as overdraft facilities (Cosh, Cumming, & Hughes, 2009). This study sought to assess the role of the above-mentioned financing options on the financial performance of SMEs in Nanyuki town.

1.1.2 Financial Performance
Financial performance of a business is actually an objective measure of exactly how effectively a firm is able to utilize its assets in its main economic operations to produce revenues. This particular phrase is likewise used as a broad measure of a firm's general economic health within a certain time period and may be utilized in order to evaluate identical firms across the identical business or maybe to evaluate sectors or industries within the general business environment. Rahim, Taufiq, Annuar, and Zariyawati (2009) argue that if firms do not care about earnings, they cannot endure for an extended period. In addition, in case firms do not pay strict attention to liquidity, they might experience the issue of bankruptcy or insolvency (Eljelly, 2004).
Despite the obvious positive impact and importance of SMEs both to individuals and to the national economy, statistics show that there is only 34% of SMEs that report good financial performance, increasing their chance that they will successfully pass to the next generation and only 13% pass to the third (Ambrecht and Koenig, 2016). In Kenya, IFC (2015) indicated that 75% of SMEs do not survive their first years of operation due to many challenges one of which is poor financial performance.

The importance of ample capitalization which complicates the economic functionality of firms was taken by Padachi (2006) that reported that a firm could be extremely profitable but in case this is not translated into money in exactly the same business cycle, the firm will have to borrow to allow finance its operations through the working capital that it must have. In case materials are actually hindered at the various phases of the supply chain, this will extend the cash operating cycle and constrain firm’s efficiency. Moreover, 60 percent of small enterprises experience liquidity problems which is as a result of cash flow challenges (López-Gracia & Sogorb-Mira, 2008).

Generically, the determinants along with signals of SMEs fiscal functionality or perhaps the firm's economic overall performance on the entire might be grouped into five huge categories: repayment capacity, financial efficiency, profitability, solvency, and liquidity (Crane, 2010). Three widely used monetary ratios to assess solvency are equity-to-asset ratio (sometimes called percent of inside ownership), debt-to-equity ratio (sometimes called the leverage ratio), the along with the debt-to-asset ratio (Saunders and Cornett, 2014).

1.1.3 Financing Options and Financial Performance of SMEs
Access to a variety of financing options is defined as availability of financial services in the different forms of demand deposits, credit, payments, or insurance and from different sources (Donovan, 2012). The availability of such financial services can be constrained by physical access, affordability and eligibility. Barriers such as high transaction cost, distance and minimum balance requirements can exclude firms access to credit and hence
negatively influence their financial performance. In particular, access various financing options is positively associated with financial performance (Ouma & Ramo, 2013).

Beck and Demurguc (2016) also notes that access to a variety of financing options enables SMEs to perform better, grow and be sustainable in the long term. Financial access is the ability of a firm to get and use financial services that are affordable, usable and meet their financial needs (Claessen, 2016). Access to finance has four key dimensions: physical access, affordability, appropriate features that meet the users’ particular needs and appropriate terms that do not effectively exclude any category of potential users. Access to finance services implies an absence to the use of these services, whether that the obstacles are price or non-price barriers to finance (Demirguc-Kunt et al, 2013). Lack of access to finance has been identified as one of the major constraints to small business growth and profitability (Carpenter et al., 2012).

1.1.4 SMEs Sector in Kenya
In the Kenyan context, SMEs are categorised under the popular Jua Kali informal sector. The SME sector provides direct or indirect employment to over 80% of the population (Ayyagari, Beck, & Demirguc-Kunt, 2007). The government pays close attention to the vibrant sector as it is perceived as the answer to the staggering levels of unemployment particularly among the youthful citizens. Over 65% of the population in Kenya is young and jobless. Among the strategies that the Government has implemented to address the need to develop the SME sector are affirmative funds such as the Uwezo Fund, County Enterprise Schemes by County Governments, Youth Enterprise Development Fund, Micro and Small Enterprise Authority and Women Enterprise Fund (Sharu & Guyo, 2015).

As observed by Calice, Chando, & Sekioua (2012), as a matter of fact, both private and public institutions pay close reference to the significance of the Kenya SME sector to economic growth. The banking sector for instance has significantly increased the financing levels to SMEs over the past few years. According to statistics from the Kenya Bankers Association (2014), banks’ SME lending portfolio as at December 2013 was estimated to be KSh 332 billion, accounting to 23.4 per cent of the banks’ total loan
portfolio. This is in contrast to 2009 and 2011, when the total SME portfolio was projected to be KSh 133 and KSh 225 billion, accounting for, 19.5 and 20.9 per cent of total lending. These trends indicate a general growth in SME financing by the financial institutions. The government also provides funding to SMEs through the various revolving funds. Mungai (2015) noted that the repayment by these SMEs was not very good and was influenced by operation procedure of the government revolving funds, socio-micro group functions and the characteristics of the borrowers.

Based on Ayyagari et al. (2007), Kenya's SMEs sector comprises ninety-eight percent of all enterprises in the nation and engages up to fifty per cent of new employment seekers yearly. The SME industry contributes on average forty-five percent to the Gross Domestic Product (GDP). To realize Kenya’s economic blueprint emblazoned as Vision 2030, the SME segment has a substantial part to play. Kenya has in the official development policies of its recognized the SMEs part like an important participant to national development and has put forth a framework to foster the growth of the sector (Ronge, Ndirangu, & Nyangito, 2002). Stakeholders, championed by the national government recognize the importance of having a conducive environment for SMEs by making access to managerial and technical education, job websites, involvement of Jua Kalis in technological innovation as well as construction of an optimistic enabling environment.

1.2 Statement of the Problem

The financial performance of SMEs in Nanyuki town is a tale of mixed fortunes with a few thriving and sustainable business in the midst of many with high failure rate and stagnation. The SMEs in Nanyuki face the tasks of failure to break even before facing a premature closure (Wangari, 2014). This failure to operate for more than one year has been attributed to quick decimation of capital (Garikai, 2011). Another study on SME blamed the oft lack of success of SMEs to constraints in boosting capital away from the owners resources (Aruwa & Suleiman, 2004).

This fluid state was well captured and synonymous with the case in European Union in the last decade where the SMEs operating environment was described as disreputably
unstable and experiencing a high level of business decline and closure (Eriksson & Kuhn, 2006). Just like it is the case in Nanyuki town and elsewhere in the world, most of the SMEs flop to survive beyond start and youth, failing to become key achievement stories, neither generating wealth for their initiators and employment opportunities for the communities they operate in to severe limitation in financing of their businesses (Thornhill, Amit, & others, 2003). This grim situation of the financial situation of SMEs has necessitated a scientific enquiry into the role of financing.

Existing empirical literature has no shortage of causes of business failure and prescriptions. While the factors determining growth and success in large businesses is adequately researched, similar studies regarding SMEs are limited and mostly conducted in the developed nations and hardly in the developing nations (Van Praag, Versloot, et al, 2007; Perks & Struwig, 2005). This condition presents a contextual gap that needs to be addressed. Survival, success and growth of small business has been researched from different perspectives including owner’s skills. Others have cited a plethora and all-inclusive list of aspects that contribute towards failure or success of new enterprises including crowding out in a single market and lack of diversification in the value proposition offered (Baron, 2004). The predominant theme being that the changing aspects of business development remains poorly understood (Dockel & Ligthelm, 2005). Some scholars contend that both external and internal factors that influence success of a business.

There is a scarcity of research assessing the influence of capitalization and individual SME firm level both in Kenya and in Nanyuki which presents a contextual gap on the need for empirical investigation on the subjects in order to inform policy legislation towards boosting growth in the sector. Ntakobajira (2013) studied the factors impacting the overall performance of SME traders at City Park hawkers’ market in Nairobi. This study focused on the various factors affecting performance not just financing. Kibet, Achesa and Omwono (2015) investigated the effects of microfinance on the overall performance of SMEs in Uasin Gichu County. The study discovered that most SMEs borrow investment capital and they apply it for the goal in which they borrowed for,
nearly all of them do not have different sources of financing apart from micro finance institutions and they did not have different types of financing before they began getting financing from microfinance institutions. This study focused on influence of microfinance funding on profitability of small and medium enterprises and did not consider other sources of finance. Mungiru and Njeru (2015) studied the effects of informal financing on the profitability of SMEs in Kiambu County. The study revealed that informal sources of investment funding have a significant effect on the overall performance SMEs. This focused only on informal financial sources and failed to consider other finance sources. There are empirical gaps in that most past studies dealt with sources of financing and never attempted to establish the link with financial performance. Other empirical gaps emerge as most very limited studies have endeavored to address a variety of financing options and have therefore been limited to either informal or formal sources.

As observed in the ongoing discussion, rarely also have past studies focused on different objective dimensions of financial performance of SMEs which represents a critical methodological gap which was filled by assessing both the profitability and liquidity statuses of SMEs. Therefore, this study’s purpose was to fill the contextual, methodological and empirical gaps that existed in understanding how financial performance of SMEs in Nanyuki Town, Kenya is influenced by financing options.

1.3 Objective of the Study
The main objective of the study was to establish the effect of financing options on financial performance of SMEs in Nanyuki Town, Kenya.

1.3.1 Specific Objectives
The study accomplished the following research objectives:

i. To determine the effect of formal credit financing on financial performance of SMEs in Nanyuki Town, Kenya.

ii. To assess the effect of informal financing sources on financial performance of SMEs in Nanyuki Town, Kenya.
iii. To establish the effect of personal financing on financial performance of SMEs in Nanyuki Town, Kenya.

1.4 Research Hypotheses
The following research hypotheses were tested:

\( H_01: \) Formal financing has no significant effect on financial performance of SMEs in Nanyuki Town, Kenya.

\( H_02: \) Informal finance sources have no significant effect on financial performance of SMEs in Nanyuki Town.

\( H_03: \) Personal financing has no significant effect on financial performance of SMEs in Nanyuki Town.

\( H_04: \) Government funds have no significant effect of on financial performance of SMEs in Nanyuki Town.

1.5 Significance of the Study
The study findings and recommendations provide immense benefit to many players. They will benefit the small and medium business owners by giving them the information on the source of funds available to them and the relevant requirement by commercial banks to extend the credit to them. The research gives challenge to the commercial banks in Kenya to modify and restructure their loaning procedures to align with the dynamic structure of the economy as well as the changing consumer demands in order to effectively address the barriers they encounter in the process of financing these small and medium enterprises. To academics who want to understand better the nature and success of relationships between banks and SME clients bringing the gap between the two and their respective credit policy. The study will also be significant to the government as it will shed light on areas that need policy improvements so that commercial banks that offer financial services to SMEs can be incentivized.
1.6 Scope of the study
The research was conducted on various SMEs within Nanyuki Town. Nanyuki town is located some 200 kilometres from the capital city Nairobi. It is the headquarters of Laikipia County. The study targeted the SMEs businesses in the town whose capital stood at less than 500,000 Kenyan shillings. The study focused on SMEs which were licensed and registered. The study objectives limited the examination of financing of SMEs and therefore, the inquiry focused on the sourcing of formal credit institutions, informal groups, personal sourcing and government funds. Other sourcing of financing for SMEs were not addressed by the study. The study considered financial performance for three financial years 2013 to 2016 with a justification that this was the period that a lot of reforms had been introduced for the SME sector including the growth of financial inclusion crusade and establishment of new government affirmative funds such as Uwezo Fund.

1.7 Limitation of the study
The research encountered some challenges, especially in data collection. The study encountered a non-response situation. SMEs traders were busy serving customers with little time for the study. To address this limitation, the study adopted a drop and pick method of collecting data using questionnaires with a follow up visit in between that increased the response rate. There was also reluctance to offer information especially source of capital. To overcome this challenge, the researcher assured respondents of confidentiality and an assurance that data was purely for academic purposes. There were difficulties with accessing the proprietors of SMEs owing to their location. This was addressed by planning resources in advance to ensure that all the targeted SMEs were reached. The study used a letter of introduction from the university and authorities such as National Commission for Science and Technology to boost cooperation. Local based research assistants were further tasked with helping to overcome any possibility of language barrier and help in interpreting the items of the questionnaire in the appropriate language.
1.8 Organization of the Study
The thesis comprises of five chapters. The introductory chapter comprises the study background, statement of the problem, aims of the research, research questions and the study objectives. Moreover, it provides the scope and limitations of the study, the significance of the study, and presents how the whole thesis is actually structured. Chapter two offers an evaluation of theoretical framework, empirical literature on determinants of fiscal performance in addition to financing options. The analysis strategy and profile of the study region are provided in chapter three. This chapter comprises of the research design that was applied to conduct the study, the target population of interest, sampling method in addition to the sample size, the information collecting instrument, information collection procedure, data analysis, ethical considerations and information presentation are in fact outlined. Chapter 4 presents the research results in addition to discussions. It provides the response rate, background info of respondents, descriptive and inferential stats. Chapter 5 offers a summary of the study and also provides policy ideas in addition to justifiable conclusions.
CHAPTER TWO
LITERATURE REVIEW

2.1 Introduction
The chapter encompasses an analysis of pertinent empirical and scholarly literature on the concept of financing options and financial performance of SMEs. The literature was arranged according to the study variables which include formal credit institutions, personal sources, informal sources and government funds. The chapter also encompasses the theoretical framework which is an elucidation of four theories namely the financial intermediation theory, pecking order theory, credit rationing theory and information asymmetry theory. The chapter also provides the research gaps that exists which the current study seeks to bridge and entails a summary of the previous studies conducted by various scholars in the field. Moreover, a conceptual framework is provided which provides the conceptualized association between the dependent and independent variables in the research and how the various variables were measured.

2.2 Theoretical Framework
The research was based the financial intermediation theory, pecking order theory, credit rationing theory and information asymmetry theory which are discussed herein.

2.2.1 Financial Intermediation Theory
Financial intermediation is the role played by financial institutions by creating specific monetary commodities when they discover they are in a position to market them for fees which are anticipated to be over the costs of the development of the commodities, both quick costs in addition to opportunity costs (Scholtens & Van Wensveen, 2003). Monetary intermediaries are available due to business flaws. Financial intermediation theory is based on transaction costs and asymmetric information. It is designed to account for institutions which take deposits or issue insurance policies and channel funds to firms. However, in recent decades there have been significant changes. Although transaction costs and asymmetric information have declined, intermediation has nevertheless increased. This indicates that the financial intermediaries play a critical role in coordinating surplus units with deficit units.
Being a result, in a great market circumstance, with no transaction or maybe information expenses, monetary intermediaries would not exist. A lot of marketplaces are realized by informational differences among clients and sellers. Bulan and Yan (2009) postulate that in financial markets, information asymmetries are particularly noticeable. This is evident since borrowers usually understand their moral integrity, industriousness and collateral than the lender. Moreover, borrowers have in-depth information about the reasons and aspects they require to be financed (Gorton & Winton, 2003). This information asymmetry amongst the borrowers and lenders is a moral hazard that hinders the transmission of information between the two parties and thus affecting flow of capital.

In the current study, the aim was to assess how financial performance of SMEs is affected by the following financing options; access government finance, formal sources, informal sources and personal sources. This theory was useful particularly in the evaluation of the barriers and constraints the SMEs face in getting credit from diverse source surplus funds like SACCOs and commercial banks. The theory guided the establishment of how asymmetry, bargaining power and transactional costs and other market imperfections affect the ability SMEs to source for funds and how that influences their performance.

2.2.2 Pecking Order Theory
Myers (1984) developed the pecking order model which he later improved in 2001 (Myers, 2001). According to this particular concept, firms favor inner funding much more than external funding. Merely, in case businesses call for outside financing, they will prefer equity less than debt as equity is actually used as a final measure. The firms adopt cautious approaches with respect to dividends and make use of borrowed funds to enhance the valuation of the business. The principles of the pecking order principle were supported by a selection of academics like (Frank & Goyal, 2007; Bulan & Yan, 2009) which offered evidence of bad choice connected with equity issues. While investigation by Maksimovic and Frank (2005) provided associated evidence on experimental bases concerning firm's financing needs.
Among the components of pecking order principle is the fact that with respect to rewarding firms, they would frequently select internal financing rather than driving up totally different debts or maybe equity. Though, debt is regarded more inexpensive compared to equity within certain proportions. Frank and Goyal (2007) held that big companies have a tendency to accumulate debts to be able to help as well as continue with the payments of dividends while smaller companies have a tendency to behave in reverse conduct principle. Bessler, Drobetz, and Pensà (2008) concluded that non-US firms support pecking order principle.

Although the theory was conceptualized for corporate bodies with choices of debt equity ratios, the theory was useful in guiding the establishment of the preferred financing option for SMEs in Nanyuki and informing reasons for the choices of financing. The theory was used to establish if the SMEs preferred the conservative sources mostly from personal sources or have ventured into liberal financing schemes and loans for SMEs. The effects on financial performance of SMEs by each financing option was also established.

2.2.3 Credit Rationing Theory
Keiding (2015) postulates that financial institutions are primarily private entities which are actually guided by way of the aim of earnings maximization. In comparison to this aim, not all people who seek financing are provided access. Hence the market for credit isn't quite healthy all over the price mechanism. Depending on Wright, Westhead, Stone, Akuetteh, and Robson (2013), borrowers could be denied credit even in cases they're ready to invest arbitrarily high interest rates. Credit marketplace is not like the conventional sector where supply is equivalent to demand as the borrowers that are ready to pay higher interest rates may be problematic in repayments. Tirole (2010) argues that this happens since the high interest rate makes the borrowers unable to effectively repay the loans plus interest.

Credit rationing arises when the expected returns from lending by financial institutions are lower that the expectation of the financial institutions (Ghosh, Mookherjee & Ray,
The non-monotonic link between the anticipated return shipping in addition to interest rates arises due to the following components or maybe reasons: The damaging option effect; occurs as soon as the interest rates are actually not able to filter the ready borrowers from the others. That's the borrowers that are actually in a place to evaluate their projects efficiently and operate inside safer project parameters (Steijvers and Voordeckers, 2009). The borrowers with much more safe tasks are in fact reported to drop out of the business every time the interest rates increase past the expected returns. The financial institution considers the applicants going for increased interest rates far more unsafe. The damaging motivator (moral hazard) effect as supplied by Hellman as well as Stiglitz (2000) posits that a development in interest rate, shifts the choice of the borrowers towards riskier tasks which again places the financial institutions expected returns at risk or maybe perhaps higher likelihood of very poor debts portfolio.

Matthews as well as Thompson (2008) postulated that credit rationing is frequently done deliberately to cushion the financial institutions on immediate risks. In instances that the institutions can't stay in a place to mitigate risks which could develop due to the free market principles being implemented, the institutions could possibly wish to ration credit regardless of the number of borrowers that demand monetary resources are in fact ready to pay higher interest rates. The market imperfection is exemplified when interest rate mechanism is unable to bring equilibrium in the financial market. This provides a link to the information asymmetry, which tends to exist in between the borrower along with the lender. This specific concept tends to explain the financing gap which might exist within the finance industry.

Financing for SMEs is ideally a difficult proposition in the Kenyan markets. The theory was useful in establishing the requirements by funding institutions to the SMEs and how they affect the financial performance of the SMEs. Additionally, the theory was useful in assessing the state of credit advancement to SMEs and how that influenced their survival and financial performance.
2.2.4 Information Asymmetry Theory

This theory was initially conceptualized by Akerlof (1970). The argument was that in most markets, the seller uses several sector statistics to determine the valuation of the items they are promoting. In this particular situation of the credit industry, the customer sees the typical rates of the loans (credit) in the marketplace he is intending to purchase, as the seller has much more personal information of each particular loan product. This places the seller at an advantageous position thus capable to offer items of lower typical market quality at higher prices. In these kinds of conditions, the limitation of the information available to the customer might result in the seller offering less than typical quality of items of the markets which ultimately leads to decrease in size of the marketplace. Information asymmetry theory assumes that a minimum of one party to a transaction has information that is related whereas the other(s) do not.

In a research conducted by Thursby and Jensen (2001) as quoted by Lowe (2001), the authors discovered that a license of a technology or creation often incurs much more price in a bid to transfer technology from the inventor. This arises because of the point that the inventor might retain useful information relevant to the creation but not found in the patent or contract document. Akerlof (1970) argues that information asymmetry provides the seller with an incentive to offer items with quality that is lower than the common market quality. This particular study assessed the effect of information quality and reliability of market information in regard to the financing of SMEs from various sources. This kind of disparities in private and social return can be mitigated by a variety of institutions. Different scholars have contributed to the subject area of information and its role in business financing and different authors have emphasized that the amount of asymmetric information regarding inside operations will be mediated by the firm itself or even by activists (Baron, 2001).

Information asymmetry influences various other elements of firm efficiency from the determination of the cause of financing. Firm development is actually determined not just by the standard attributes of age and size but, additionally by some other aspects specific to the firm like indebtedness, inside financing, upcoming development opportunities,
process and product development as well as business improvements. It is thus crucial that governments have to pay increased attention to MSEs and attempt to produce a business environment which will be advantageous to MSE growth (Anastasov and Mateev, 2010). In response, governments have introduced an assortment of policies like the provision of guidance, in order to facilitate development of new firms as well as to provide help to MSEs to help their survival and foster enhanced rates of growth (Bennett, & Bratton, Robson, 2001). Based on Grimes and Claus (2003), the presence of imperfect, unevenly held information causes frictions of the credit industry. SMEs are especially constrained by gaps of the economic system like higher administrative costs, substantial collateral needs as well as lack of expertise within fiscal intermediaries.

It is the provision of quality, timely and consistency and reliability of information by lending institutions which impact the access of financing to the SMEs across the world. This particular truism is actually corroborated in a report by Dalberg (2011) on assistance to SMEs in developing world cites that Banks have minimal information, abilities as well as regulatory guidance to participate in SME lending. This theory was useful in determining the effect of information availability or lack of it amongst the SMEs and how that affected the financing options and decisions made by SMEs in the Nanyuki market.

2.3 Empirical Literature Review

Empirical literature covers the previous studies on financing options and how they affect the financial performance of diverse organizations and SMES. It is organized and presented as guided by the study variables.

2.3.1 Formal Credit Sources and Financial Performance

The structured capital resources of business financing comprise savings banks, development banks, development banks, merchant banks, and commercial banks. The study by Beck, Demirgüc-Kunt, and Martinez Peria (2008) postulated that formal financial sources relates to the funds from the financial organizations that are legally established with the mandate of providing saving, credit and investment services to other organizations. SAEEED, SME Finance Sub Group 2010 and Financial Inclusion Experts
Group (2009) found that formal finance sources remain dependable sources of funding of SMEs development and also growth and they have contributed meaningfully to the practical use of SMEs in different countries, Kenya inclusive. A report by Otuya, Omoka, Ayako, and Kihimbo (2012) affirmed the significance of having successful funding mechanisms to the small business pursuits. These studies focused on hindrances to credit access by SMEs and did not associate financial performance of the SMEs with financing sources.

The establishment of network of appropriate recognition institutions helps in enhancing lending problems in addition to phrases in favor of tiny scale enterprises will provide an important avenue for facilitating the access of theirs to credit. Empirical evidence by Atieno (2001) on business banks together with other formalized institutions suggested they fall quite short of catering for the credit needs of smallholders, nevertheless, mainly due to their lending terms and conditions. It's often the rules as well as laws of the traditional financial institutions which have created the myth that the really poor are not bankable since they cannot pay for the required collateral, they are believed to be bad credit risks. Kimuyu (2002) assessed the effect of finance on the various other areas of small business operations. Specifically, the study concentrated on the determinants of the most crucial economic choice of SMEs, which include how you can raise capital for the company, distinguishing between the original capital and any follow up capital acquired for restructuring or expansion. The study hence did not assess the funding challenges from the various financing sources but focused on establishing the most suitable financing source for SMEs.

Based on empirical exploration offered by Wagema (2006) as quoted in Jagongo and Kimutai (2013) which sought to figure out crucial factors which affect access to bank credit by SMEs. The study identified entrepreneurial orientation which includes a fast determinant of entry to credit by SMEs. Further, awareness-based methods acquired from maturation (age), finalized start up expertise, knowledge and vicariously through entrepreneurial parents had been discovered to be connected with higher levels of entrepreneurial orientation. Generally, these findings help support the literature which
underscores the primacy of entrepreneurial elements, over operating components in facilitating small enterprises' access to bank credit. Based on the study conducted by Montoriol Garriga and Garcia Appendini (2013) on firms as liquidity providers, they found out that in US, stronger and bigger firms extended more trade funding with the monetary issue while weaker larger received more trade credit. These tests focused on the components which hinder SMES from accessing credit out of correct financial institutions but did not focus on some other financing strategies.

Ntakobajira (2013) interrogated the components impacting the normal performance of SME traders at City Park hawkers’ market in Nairobi. The study revealed that that the sources of capital for SMEs differed ranging from bank loans, donations, private savings & advancements from friends as well as family along with various other sources. On access to finance, the study suggests that the Government of Kenya works out modalities about just how you are able to finance SMEs. Nevertheless, this particular analysis dealt only with sources of energy of capital for SMEs. The current study went further and sought the end result of financing options on financial performance of SMEs.

Kibet, Achesa, and Omwono (2015) investigated the effects of Microfinance on the common performance of SMEs discovered Uasin Gichu County. The study discovered that the vast majority of SMEs borrow investment capital and they as well employ it for the goal in which they borrowed for, just about all of them do not have many sources of energy of financing apart from micro finance institutions and they did not have a variety of types of financing before they began getting financing from microfinance institutions. The analysis means that MFIs should partner with the county governments combined with other stakeholders to create understanding of the task together with the accessibility of accessing micro finance loans. Since MFIs have poverty alleviation as the crucial goal of theirs, they've to think about regarding lending startup capital so that the welfare of the borrower together with the company may be monitored. This particular analysis just assessed the effect of microfinance from SACCOs and banks on SMEs while the present study dealt with all financing sources as well as the effect of its impact on fiscal results.
Muguchu (2013) interrogated the connection between access to economic functionality as well as investment finance of SMEs in Nairobi. The analysis started that funding constraints affect probably the smallest firms most adversely and incremental enhancement of the financial techniques which could help relax these limitations will be excellent for SMEs. The analysis suggested that the national government should come to the aid of SMEs by regulating how economic institutions charge interests to these firms. This particular study was just concerned with expense monetary constraints within SMEs and just centered on official capital sources of investment finance but overlooked informal, personal, and government energy sources of finance.

2.3.2 Personal Sources and Financial Performance

Private contributions also aid the small business to raise extra cash from some other sources. Ekpenyong (2002) explained private savings as the amount left over after subtracting the expense of customer expenditure of the person from the amount of disposable income of a particular period of time shows that almost all of the cash required by SMEs proprietors came from specific savings (96.4 per cent). The experiments by BIS; Department for Skills as well as business Innovation attested that half of SMEs don't make use of formalized funding energy sources of exterior finance, quite they rely on trade credit out of the suppliers of theirs or perhaps retained earnings and those show why the great bulk of the industries have been wallowing in abject poverty with slower business growth and development. This study evaluated the reasons why SMEs prefer personal sources of financing compared to other sources of finance. The study did not establish the link between financing and performance of SMEs.

Agwu, Falohun, and Taiwo (2016) found that SMEs rely largely on individual savings of owners, and quite often company earnings, in case there are any for their monetary requirements. They have little or perhaps no access to formal outside credit. Conventional financial institutions regard SMEs as high risk as well as having substantial probability of default. Consequently, the monetary requirements of SMEs are not considered in the lending policy formulation of banks. Many of them are denied access to economic assistance from conventional financial institutions. Major fiscal commitments made by
proprietors of an enterprise are likely to create a great deal of confidence among possible investors. Vvor and Ackah (2011) found out that individual savings of the owners as well as partners of companies comprise a crucial source of funds, especially in the formative stages of a firm. The study sought to establish the most important financial source of SMEs and did not seek to determine the association between financing and performance of SMEs.

Mensah (2004) found out that contributions from family as well as friends form an alternate source of finance for SME operators. Collins and Low (2010) found that financing from friends as well as families is actually a crucial occurrence. Furthermore, it is crucial for small and medium enterprises (SMEs), a segment which comprises a lot of worldwide economic formations. Sarbah and Quaye (2014) noted that financial institutions have yet to take advantage of a potential global market for SME financing worth approximately five trillion dollars. Aside from owners' cost savings, informal financial sources come from friends and distant relatives. Atieno (2001) examined that actually in the informal sector, the various segments screen various amounts of accessibility. From their findings, they suggested that family sources are the most prevailing application of fiscal source utilized for each working and original capital. For start up capital, it was followed by loans from parents, close relatives as well as selling of formality. The study demonstrated that for start up as well as operating capital; private savings at home, friends & relatives offered in excess of 50% of the loans from the informal sector. The study sought the most vital source of start-up finance and did not focus on growth capital.

Odinga (2012) studied the problems facing progress of small and medium enterprises owned by women in Kakamega municipality. The study results revealed that access to finance and credit facilities impacted heavily on the progress of women owned SMEs in the municipality. Lack of or perhaps inadequate capital for development led to collapse of countless companies. Commercial banks along with other micro finance institutions must think of an appealing financing bundle for women that are involve in business ventures. This must have friendlier terms, repayment period as well as interest rates. This study
dealt with the women who are in SMEs. Moreover, the study assessed the financial challenges facing these firms but did not link the financial challenges to financial performance of the SMEs.

2.3.3 Informal Sources on Financial Performance

Mungiru and Njeru (2015) found out that shylock companies have been legalized in particular parts of the planet and appropriately, formally instituted policies have been put in place to regulate the operations of theirs and consequently are normal in the semi urbanized locations. It calls for the provision of third party or maybe security as to stay away from defaults in repayment. Ugwuanyi and Agbo (2012) observed that the borrower is usually necessary to create a guarantor, pledge the land of theirs or possibly both to perform as collateral before the extension of the loan facilities. Recognition from these moneylenders is ordinarily the priciest credit available; hence the demand for this usually comes from persons not having another choice. Aryeetey (2008) concluded which credit remains nevertheless the single source of informal credit which doesn't have borrowers to satisfy certain membership obligations. The study focused on establishing the which informal source of finance required no collateral and was very accessible. The study did not focus on other financing sources apart from informal sources.

Riding (2006) found out sources beneath informal that provides economic help with or perhaps without demanding severe collateral security from SMEs' owners; instead, it might base it on words of mouth or even with basic agreement. A report carried out by Amissah and Gbandi (2014) established that informal finance sector (IFS) provides greater than seventy percent of the money to the SMEs, consequently, advocated the government must find out those elements which necessitate for this and include these kinds of aspects to their policy for enhancing SMEs access to finance. This particular type of funding is generally according to an equity contract, usually common stock. This study only focused on the role of informal sources of finance for SMEs but failed to consider other sources.
Empirical investigation provided by Udell, Berger as well as Klapper (2001), shows that company angels are in fact a informal tool for internet business finance. Madill, Haines and Riding (2005) found out that angels are in fact extremely discerning wealthy individuals with comprehensive internet business expertise which spend directly in growth SMEs that is high with which they've had no prior connection. Fadiga et al. (2004) conducted a report on collective activity and informal fiscal institutions: An empirical analysis of rotating and savings credit associations (ROSCAs) in Senegal. This specific analysis modelled cooperation among participants together with the financial performance in addition to sustainability of associations with info collected from region research conducted in Dakar, Senegal in 2001. The results suggest that things as homogeneity of individuals within an association, just how long the association has existed, just how defaults are in fact covered, and rules concerning residency requirements, individual contributions, and rotation order are in fact to various extents important to the economic performance in addition to sustainability of ROSCAs and additionally to the fostering of cohesiveness with members of the associations. This study investigated the role of ROSCAs and other informal sources of finance in enabling financial deepening for SMEs but did not link the accessibility of finance to financial performance of the SMEs.

Njeru and Mungiru (2015) investigated the consequences of informal financing on the profitability of SMEs found Kiambu County. The study revealed that informal energy sources of investment funding have a significant effect on the overall performance SMEs. Self assistance staff finance, family along with friends' finance; trade investment funding has a great effect on the general functionality of SMEs while shylock finance sources like an adverse impact on the overall performance of SMEs. The research suggested that SMEs have to put a lot more focus on informal finance resources including trade credit, finance from friends as well as self help team finance and family, because the informal sources of financial rely on relationships in addition to character implying that info asymmetries between informal borrowers & lenders are far less acute, the loan application system lighter, along with the collateral requirement easier to satisfy. This
study only assessed the influence of informal financial sources and did not focus on other financing sources.

2.3.4 Government Funds and Financial Performance

Empirical evidence presented by Makubo (2015) indicated that most companies in the private sector have been not able to develop as well as realize their full potential largely because of, along with other things, the high-cost of finance and lack of collateral required by financial institutions. The study indicates that government funding for small enterprises enhances performance. They are empirical studies and authoritative reports hailing the role of government and donor aided funds in supporting SMEs. The study only focused on the role of government funding in enhancing financial performance of SMEs.

Mensah (2004) presented empirical evidence to indicate that authorized official schemes are actually those launched by government possibly by itself or perhaps with the assistance of donor agencies to boost the flow of financing to SMEs. It has been argued that these kinds of programs and schemes have the ability to enhance the access of more credit to SMEs. Nevertheless, Madill, Riding, and Haines (2007) found that government schemes aimed at helping SMEs to access finance could be useful only if they operate within well specified factors. Additionally, SMEs are actually subjected to credit rationing due to their small size as well as information asymmetry. Ventura and Zecchini (2009) discovered that for them to be successful, the national government has to aim at reducing the amount of discrimination against SMEs borrowers in terms of lending costs as well as unmet need for funding. This study focused on government financing and did not consider other sources of financing.

Irungu and Kamau (2015) investigated the influence of Youth Enterprise Development Fund on Development of new ventures in Kenya. The study was a survey of certain Youth ventures in Mathioya District. The study targeted a total of 40 youth enterprises funded by the fund. The study established that Youth Enterprise Development Fund played a critical role to the development of new enterprises in Kenya. As such,
government financing contributes to business growth and performance. This study investigated the role of government funding on SME performance but failed to consider other vital sources of financing.

Kamunge, Njeru and Tirimba (2014) investigated the aspects impacting functionality of SMEs situated in Limuru market Kiambu. The research revealed that access to funding exposes enterprises to better chances to grow and thrive while additionally, it leads to enhanced SME performance to a tremendous degree. The study even found out that access to funding for enterprises is quite complicated to a high degree. Generally, access to finance impacts the overall performance of business to a high degree. The study found out that nearly all SMEs liked using contributions and private savings and savings from relatives since they experience challenges when they try to access financing from commercial banks because of tight requirements such as collateral and substantial repayment expenses. The research thus recommends that banks along with other credit providing financial institutions must come up with innovative policies that are simple and well suited for the SMEs to access financing. This study was mainly concerned with start capital for SMEs traders and did not focus on growth capital for the SMEs.
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<td>Kamunge, Njeru, and Tirimba (2014)</td>
<td>Aspects impacting functionality of SMEs situated in Limuru market Kiambu</td>
<td>The research revealed that access to funding exposes companies to better chances to grow and thrive while additionally, it leads to enhanced company performance to a tremendous degree. The study even found out that access to funding for enterprises is quite complicated to a high degree. Generally, access to finance impacts the overall performance of business to a high degree.</td>
<td>The study found out that nearly all SMEs liked using contributions and private savings and savings from relatives since they experience challenges when they try to access financing from commercial banks because of tight requirements such as collateral, and substantial repayment expenses. The research thus recommends that banks along with other credit providing financial institutions must come up with innovative policies that are simple and well suited for the SMEs to access financing.</td>
<td>This study was mainly concerned with start capital for SMEs traders.</td>
<td>This study assessed the various sources of capital for SMEs</td>
</tr>
</tbody>
</table>

Source: Various Literature Reviewed (2018)
2.4 Conceptual Framework

The independent variables included the various financial options that SMEs assess in their pursuit of financial performance. They include the formal credit institutions, personal sources, sources, informal sources and government funding. The dependent variable was financial performance assessed from a liquidity and profitability point of view.

**Dependent Variables**

- **Formal Financing**
  - Access to Information
  - Availability of collateral
  - Previous experience
  - Punitive rates

- **Informal Financing**
  - Prevalence self-help groups
  - Prevalence of shylock
  - Experience of round table
  - Assets Availability

- **Personal Financing**
  - Use of owners’ seed capital
  - Using profits to start other ventures
  - Apathy of borrowing

- **Government Funds**
  - Accessibility of government funds
  - Mode of allocation
  - Efficiency of disbursement
  - Interest rates

**FINANCIAL PERFORMANCE**

- **Liquidity**
  - Quick ratio
- **Profitability of SMEs**
  - Return on Assets
  - Net Profit Margin

*Figure 2.1: Conceptual Framework*

*Source: Researcher (2018)*
CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction
This chapter details the research strategy utilized in the study. It specifies in detail the
research design, target population, sample size, sampling process, data collection
instruments, reliability and validity of data gathering instruments, analysis and
presentation of data. This section also covers ethical considerations that the researcher
observed to ensure confidentiality was adhered to. The chapter was critical in providing a
framework for data analysis useful in testing the research hypothesis and providing
conclusions based on empirical evidence.

3.2 Research Design
Research design refers to the general approach that one could select to incorporate the
various parts of the study logically and coherently. This is accomplished to ascertain that
the researcher formally tackles the aspect under investigation (Kothari, 2004). The
researcher used a descriptive survey design technique to establish the association between
financing options and financial performance of the small and medium enterprises.
According to Saunders, Lewis, Thornhill and Wilson (2009), a descriptive survey
research design is actually affordable and also enables one to obtain great amount of
information, allow for standardized details, for ease of comparison and analysis.

3.3 Target Population
Target population is defined by Orodho (2005) as a set of all cases and elements in the
universe that hold the information required by the researcher. For purposes of this study,
the targeted population was made up of seven hundred and sixty-five SMEs operating
within Nanyuki town (County government of Laikipia licensing department, 2015). According to the licensing department of the county there were seven hundred and sixty-five (765) registered SMEs within Nanyuki town (County government of Lakipia licensing department, 2015). The target respondents were the proprietors of the SMEs in Nanyuki Town.
3.4 Sampling Techniques and Sample size

The study used stratified sampling to select the SMEs for the study whereby the different classification of business were the strata as shown in Table 3.1. The sampling technique ensured comprehensiveness and control of bias in sample selection. A stratified random sampling procedure is a population sampling procedure that requires the population to be divided into smaller groups, called strata (Mugenda & Mugenda, 2003). Stratified sampling certifies that the different clusters are represented, even proportionately, in the sample(s) by picking individuals from each of the strata list (Kothari, 2004). The use of simple random sampling from each stratum strengthened the sample and enabled collection of comprehensive data on all the study variables. The study purposively selected the proprietors of the enterprise as the respondents as they were the ones ideally equipped with the information sought.

The sample size of SMEs to be studied was determined using a formula developed by Trek (2015) to determine a statistically representative sample from a known population. Using the formula

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

Where: N-Population Size
n- Sample Size
\( e \)- Level of Precision at 95 percent confidence level.

This formula was engaged, and the sample size was computed as indicated below.

\[ n = \frac{765}{1+765(0.05)^2} = 88.44 \text{ respondents} \]

The sample was therefore composed of 88 potential participants selected from the target population of 765.
3.5 Data Collection Instrument

Questionnaires as well as secondary info compilation sheets have been used as the crucial resources for info compilation. The researcher, to a significant degree, utilized structured questionnaires if the main instrument for information compilation. Kothari (2004) postulates that utilization of the questionnaire as the main data collection instrument permits the researcher to get big quantity of information in a moderately short span of time and assures confidentiality as they are in a position to ensure anonymity while certifying standardization.

3.5.1 Validity and Reliability

3.5.1.1 Validity

The validity of an assessment instrument is actually the extent to which the instrument methods what's created to measure. In this specific scenario, the validity is really an equivalent to accuracy (Mugenda & Mugenda, 2003). It's frequently recognized that the idea of scientific validity relates to the dynamics of accuracy as well as fact. Validity is important because it is in a position to assist the researcher to determine what types of tests to make use of, in addition to helping in making sure that researchers are actually using solutions which are not merely honest, and cost effective, but also are strategies that actually assess the construct or maybe idea in question (Kothari, 2004). To be able to make sure validity of the information collection instruments, content validity as well as face validity of the analysis instruments was conducted by validation by an examination and the boss of the research instruments by a specialist. Pre-testing of the data collection instrument was conducted using a selected group of workers in the SMEs which further certified that the information collection instruments collected the intended and reliable information envisaged by the researcher. A total of 10 questionnaires had been distributed to 10 randomly selected SMEs for pre-testing uses.

3.5.1.2 Reliability

Reliability depicts the uniformity of a research instrument in collecting related details. What this means is the fact that if the assessment is actually repeated with precisely the same measuring techniques; the conclusions will be precisely the same. Golafshani
(2003) equally posits that reliability validates that the functioning of an instrument such as the data collection instrument would be repeated with similar outcome. In order to ensure reliability of the data gathering instrument, the study utilized the Cronbach Alpha reliability coefficient created using SPSS application for analysis.

3.6 Data Collection Procedure
The questionnaire was the appropriate instrument for collecting data as suggested by Orodho (2009) who posited that a questionnaire is an instrument used to collect information, allowing a measurement in support of or contradicting a specific viewpoint. Questionnaires are actually not hard to administer, provides the respondent enough time to provide a nicely thought-out response and therefore are hence checks against the investigator’s partiality. Administration of the questionnaire was conducted through the drop-and-pick-later technique. The study also employed secondary data collection checklist to obtain information about the profitability and liquidity of the SMEs. The questionnaires were administered to the target respondents and collected after five working days to provide respondents enough time to respond to all of the questions therein.

3.7 Data Analysis and Presentation
William (2003) defines information analysis as the entire process that begins right after collection of data and ends once the outcomes are actually interpreted. It provides coding, classifying, analyzing along with editing gathered info to guarantee completeness as well as accuracy. Quantitative technique to data analysis was. The key data collected through the questionnaire were entered into Statistical Package for Social Sciences (SPSS) edition 20 after coding. Information was examined using both descriptive analysis (percentages, standard deviation, means and inferential statistics) (Pearson correlation analysis and multiple linear regression analysis).

Pearson correlation was utilized to recognize the nature, power and power of interactions between specific financial funding options as well as financial performance of SMEs.
Values of r which represents the correlation coefficient would be interpreted on a scale of -1 to one. Being a result, values of $r = 1.0$ indicated relationship that is ideal. In addition, values of $r = 0$ to $+1$ implied that the two variables had been more likely to increase or perhaps reduce jointly (Orodho, 2009).

Additional analysis was done using ordinary least squares regression analysis which helped the assessment of the particular magnitude of the association amongst the variables under study. The ordinary least squares regression model that was applied was of the form;

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \epsilon$$

Where,

$Y$ = Financial performance

$\beta_0$ = Constant

$X_1$ = Formal financing

$X_2$ = Informal financing

$X_3$ = Personal financing

$X_4$ = Government funds

$\beta_{1-4}$ = Regression coefficients

$\epsilon$ = Error term

The ordinary least squares regression analysis was applied to ascertain the funding options that are the predicators of profitability of SME’s in Nanyuki town. The model above would ascertain the actual effect of each of the funding options on the financial profitability of SMEs in Nanyuki town. Before running the regression analysis, the diagnostic tests were conducted to ascertain that the data collected met the basic assumptions for regression analysis. The diagnostic assessments conducted included test of normality which utilized the Shapiro Wilk test, test for multicollinearity and Test
Glejser for heteroskedasticity utilizing regression diagnostics on SPSS. Information was provided in charts, tables, graphs and other relevant presentation techniques. This formed a good ground for arriving at vital findings and conclusions.

3.8 Ethical Considerations
Ethics refers to the standards for behavior which distinguish between unacceptable and acceptable behavior. It is perspective, procedure, or a method for determining how you can act and for examining complicated issues and problems (Crandall and Diener, 1978). For the goal of this particular study, a permit to conduct the study in Nanyuki Town was provided by NACOSTI (National Council of Science and Technology). Moreover, a consent was pursued from Kenyatta University. The researcher clarified the intent behind the analysis to the target participants and assured them of concealment of their identities, participation status and responses. The researcher also ensured that those who participated did that voluntarily. The appropriate permission was received from the respondents before administration of questionnaires. Lastly, literary materials quoted from previous academicians and scholars have been appropriately recognized through formal citations.
CHAPTER FOUR
DATA ANALYSIS AND PRESENTATION

4.1 Introduction
Presented in this chapter are the research findings and discussions. In the chapter, the researcher presents the study results that emanated from the data analysis. It covers both descriptive and inferential statistics. The findings are compared with foundations of theory as well as past empirical results. The comparison acts as the premise for justifiable conclusions.

4.2 Response rate
This section covers an analysis of the successful responses secured by the study. The analysis is imperative to ensure the threshold set is achieved for worthy conclusions. Table 4.1 offers statistics on the achieved response rate. A justification is also provided as to why the responses attained were considered sufficient for study purposes.

<table>
<thead>
<tr>
<th>Targeted participants</th>
<th>Successful Responses</th>
<th>Percent response</th>
</tr>
</thead>
<tbody>
<tr>
<td>88</td>
<td>65</td>
<td>73.86%</td>
</tr>
</tbody>
</table>

Source: Survey data (2018)

The study targeted 88 potential respondents who were administered with the questionnaire. Out of these, 65 questionnaires were successfully submitted back. This represented a response rate of 73.86%. As indicated by Mugenda and Mugenda (2003), a response rate which is above 50% would be considered satisfactory, 60% good and above 70% as very good for study purposes.

4.2 Reliability Test
The reliability of the questionnaire items was tested. A score of above 0.7 indicated that the questionnaire was reliable and adequate for the study (Table 4.2).
Table 4.2: Reliability of the Items

<table>
<thead>
<tr>
<th>Cronbach's Alpha</th>
<th>Standardized Cronbach's Alpha</th>
<th>No of Items</th>
</tr>
</thead>
<tbody>
<tr>
<td>.775</td>
<td>.788</td>
<td>8</td>
</tr>
</tbody>
</table>

Source: *Survey data (2018)*

The computed Cronbach alpha for the eight questionnaire items was 0.788 which depicted acceptable reliability. A Cronbach’s alpha internal consistency coefficient of 0.7 or above would be seen as appropriate in social science research scenarios (Gliem & Gliem, 2003).

4.3 Descriptive Analysis

This part covers the descriptive statistics that were derived from the analysed data. The statistics give us a picture of the conditions as they are regarding the various aspects of small business financing options in Nanyuki town. The results are captured with the framework of the objectives in mind.

4.4.1 Financial Performance

This section provides descriptive statistics relating to financial performance of SMEs in Nanyuki town, Kenya. The dimensions of financial performance captured include liquidity and profitability performance. Table 4.3 presents statistics on the liquidity performance of the SMEs. This is indicated by the current ratio and quick ratio.

Table 4.3: Liquidity Performance of SMEs

<table>
<thead>
<tr>
<th></th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current ratio of SME</td>
<td>65</td>
<td>.76</td>
<td>2.10</td>
<td>1.4602</td>
<td>.41695</td>
</tr>
<tr>
<td>Quick Ratio of SME</td>
<td>65</td>
<td>.44</td>
<td>1.10</td>
<td>.5555</td>
<td>.16332</td>
</tr>
<tr>
<td>Valid N (listwise)</td>
<td>65</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: *Survey data (2018)*
The average liquidity position of the SMEs in Nanyuki town Kenya stood at 1.47: 1 (Current Ratio) and 0.55: 1 (Quick Ratio). This illustrates poor state of liquidity for SMEs since both ratios are below the universally accepted and recommended threshold of 1:1 and 2:1 and for quick ratio and current ratio respectively. The results are in agreement with past findings by Nyabwanga, Ojera, Simeyo, and Nyanyuki (2013) who also reported the liquidity of SMEs to be below the globally accepted norms.

Table 4.4 presents statistics on the SMEs profitability. This is indicated by the return on assets ratio. The ratio indicates the efficiency with which the resources (assets) of the business are utilised to generate income for the business organisation.

**Table 4.4: Profitability Performance of SMEs**

<table>
<thead>
<tr>
<th></th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Return on Assets</td>
<td>65</td>
<td>1.03</td>
<td>23.76</td>
<td>6.6642</td>
<td>4.22424</td>
</tr>
<tr>
<td>Valid N (listwise)</td>
<td>65</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Source:** Survey data (2018)

The profitability of the SMEs in Nanyuki town, Kenya as indicated by return on assets stood at an average of 6.67% which is relatively low. There is however wide variation in profitability of SMEs with the highest performer reporting a profit of 23.76% with the lowest indicating a mere 1.03% profit. The profitability of SMEs therefore stood low which supports earlier indications by Orinda and Otieno (2014) in an analysis on financial challenges facing SMEs.

### 4.4.2 Formal Financing

This section covers statistics on formal financing options for SMEs. Table 4.5 presents study findings regarding the extent to which the SME consumes formal sources of credit financing to meet day to day demands.
Table 4.5: Consumption of Formal Finance

<table>
<thead>
<tr>
<th>Extent to which the SME consumes formal sources of credit financing to meet day to day demands</th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Valid N (listwise)</td>
<td>65</td>
<td>1.00</td>
<td>5.00</td>
<td>2.7692</td>
<td>1.16952</td>
</tr>
</tbody>
</table>

**Source:** Survey data (2018)

The mean of 2.76 indicates that the respondents showed that consumption of formal finance sources by SMEs to meet day to day demands was only to a moderate extent. The low standard deviation of (1.17) further affirms the validity of this condition indicating that the responses were closely distributed around the mean. The study findings agree with past indications by Kauffmann (2005) and Kimaiyo (2016) who observed that SMEs were rarely able to meet formal finance conditions.

Figure 4.1 presents statistics on the most commonly utilised formal sources of finance by Small scale business enterprises. Majority, representing close to half of all SMEs got formal finance from Micro Finance Institutions. This was followed by SACCOS (38.46%) with the least utilised source being commercial banks (12.31%). The results support earlier results by Chimucheka and Rungani (2013) and Gichuki, Njeru, and Tirimba (2014) who also indicated difficulties in accessing commercial banks finance by SMEs.
Figure 4.2 presents statistics on the most common limiting factors for utilisation of formal sources of finance by the SMEs in Nanyuki town, Kenya. Majority, representing close to half (46.15%) of respondents listed collateral requirements as the main drawback for access to formal lending by SMEs. This was followed by lending conditions and previous experience at 21.54% and 18.46% respectively. Access to information was listed as the least hindrance to formal funding as it was cited by only 13.85% of respondents. The findings are in agreement with past indications by Babu (2017) and Nikaido, Pais, and Sarma (2015) who also highlighted collateral and lending conditions as among principal hindrances for formal financing.
Figure 4.2: Limiting Factors for Formal Finance

Source: Survey data (2018)

4.4.3 Informal Finance

This section covers descriptive statistics regarding informal sources of credit by SMEs in Nanyuki town, Kenya. Table 4.6 presents study results regarding the extent to which the SMEs relied on informal sources of funding business operations.

<table>
<thead>
<tr>
<th>Table 4.6: Use of Informal Sources of Finance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extent of reliance on informal funding options for SMEs</td>
</tr>
<tr>
<td>--------------------------------------------------------</td>
</tr>
<tr>
<td>Extent of reliance on informal funding options for SMEs</td>
</tr>
<tr>
<td>Valid N (listwise)</td>
</tr>
</tbody>
</table>

Source: Survey data (2018)

The mean of 3.96 shows that the SMEs greatly relied on informal sources of finance for their operations. The low standard deviation of (1.24) illustrates proximity of observations around the mean. The results agree with past findings by Mungiru and Njeru, (2015) and Aryeetey (2008) who also established high usage of informal financing for SMEs.
Figure 4.3 provides statistics on the most commonly utilised source of informal funding for SMEs in Nanyuki town, Kenya. The most significant source of informal funding for SMEs was cited as round table or table banking arrangements as held by close to half of respondents (47.69%). Other notable informal sources commonly cited included membership advances, donations from friends and shylock lending as cited by 30.77%, 12.30%, and 9.23% of respondents respectively. The results support past results by Asetto (2014) who found table banking to be the most significant source of informal finance by small business entities.

![Graph: Most Common Source of Informal Funding](image)

**Figure 4.3: Most Common Source of Informal Funding**

**Source:** Survey data (2018)

Figure 4.4 presents statistics on the main factor highlighted as driving preference for informal financing over other available options by SMEs. Low risk associated with informal groups and less collateral requirements were cited as the main reasons driving preference for informal funding while lack of knowledge of other sources was the least cited factor. The results follow past indications by Mungiru and Njeru, (2015) who also indicated less risk and collateral as principal reasons for preference of informal sources.
4.4.4 Personal Finance

This part provides descriptive statistics on personal finance and how it was utilised by the SMEs. Table 4.7 shows the extent to which personal sources of finance were utilised by the SMEs.

Table 4.7: Use of Personal Sources of Finance

<table>
<thead>
<tr>
<th>Extent of reliance on personal financing in funding the SME</th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value</td>
<td>65</td>
<td>2.00</td>
<td>5.00</td>
<td>4.2923</td>
<td>.93078</td>
</tr>
</tbody>
</table>

Source: Survey data (2018)

As shown by the mean of 4.29, personal finance was relied upon to a great extent as a key source of funding for SMEs. The low standard deviation of 0.93 further affirms this condition as it demonstrates closeness of the observations to the mean. The results support earlier results by Taiwo, Falohun, and Agwu (2016), Ackah and Vvor (2011)
and Mensah (2004) who found personal finance as significantly utilised for SMEs operations.

Study participants were also requested to show the category of personal finance mostly utilised for SME funding. Figure 4.5 presents statistics on the most utilised source of personal finance in the organisation. Ploughing back profits and personal savings were highlighted as main categories of personal finance utilised for day to day operations.

**Figure 4.5: Most Common Source of Personal Finance**

*Source: Survey data (2018)*

Figure 4.7 highlights results on the main factor driving use of personal finance as cited by the proprietors. Need to maintain control and high risk associated with other sources were cited as the main factor behind use of personal finance. Dislike for debt was listed as the least factor. The results agree with Mensah (2004) and Taiwo, Falohun, and Agwu (2016) who also highlighted need to maintain control as principal reason for personal funding.
4.4.5 Government Financing

This section provides study results regarding government financing as a key variable to the current study. Table 4.8 provides study findings on the extent to which government affirmative funds were relied upon as a source of SME funding.

Table 4.8: Reliance on Government Finance

<table>
<thead>
<tr>
<th></th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extent to which the SME relies on Government Affirmative Funds in funding operations</td>
<td>65</td>
<td>1.00</td>
<td>5.00</td>
<td>2.8769</td>
<td>1.17935</td>
</tr>
<tr>
<td>Valid N (listwise)</td>
<td>65</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Survey data (2018)

As indicated by the mean of (2.88), SMEs in Nanyuki town, Kenya utilised or relied upon Government Affirmative Funds in funding operations only to a moderate extent. This is further affirmed by the small standard deviation of (1.18) which indicates that observations were closely held about the mean. The results agree with Irungu and Kamau (2015) who found utilization of affirmative action funds by SMEs to be moderate.
Figure 4.7 shows the government affirmative funds that respondents indicated to have benefited from. As demonstrated, majority, representing more than 2 thirds of SMEs in Nanyuki were yet to benefit from government affirmative funds. This supports past results presented by Simiyu (2016) and Kamau (2013) on low penetration of the funds.

Figure 4.7: SMEs’ Benefit from Affirmative Funds

Source: Survey Data (2018)

Table 4.9 provides study results regarding the extent to which study participants felt there was fairness in funding SMEs by the government.

Table 4.9: Fairness in Government Funding for SMEs

<table>
<thead>
<tr>
<th>Extent</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not at All</td>
<td>14</td>
<td>21</td>
</tr>
<tr>
<td>Little Extent</td>
<td>20</td>
<td>31</td>
</tr>
<tr>
<td>Moderate Extent</td>
<td>17</td>
<td>26</td>
</tr>
<tr>
<td>Great Extent</td>
<td>9</td>
<td>14</td>
</tr>
<tr>
<td>Very Great Extent</td>
<td>5</td>
<td>8</td>
</tr>
<tr>
<td>Grand Total</td>
<td>65</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Survey data (2018)
Respondents were generally of the opinion that government affirmative funds lacked fairness in proving funds to SMEs. More than three quarters of the respondents indicated that the level of fairness was either moderate, little or no fairness at all. The findings support earlier positions reported by Kamau (2013) and Irungu and Kamau (2015).

Figure 4.8 provides study findings regarding the extent that the study participants felt that the government affirmative funds were efficient in disbursement of funds to SMEs. Majority, representing more than two thirds of respondents indicated either moderate, little or no efficiency at all in disbursement of government funds to SMEs as earlier held by Kamau (2013).

Table 4.10 provides study results regarding the extent to which study participants felt that the funds provided by the government affirmative funds are sufficient or enough for SME’s undertakings.

Figure 4.8: Efficiency of Disbursement of Government Funds

Source: Survey data (2018)
Table 4.10: Sufficiency of Government Funding for SMEs

<table>
<thead>
<tr>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not at All</td>
<td>16</td>
</tr>
<tr>
<td>Little Extent</td>
<td>19</td>
</tr>
<tr>
<td>Moderate Extent</td>
<td>17</td>
</tr>
<tr>
<td>Great Extent</td>
<td>9</td>
</tr>
<tr>
<td>Very Great Extent</td>
<td>4</td>
</tr>
<tr>
<td>Total</td>
<td>65</td>
</tr>
</tbody>
</table>

**Source:** Survey data (2018)

Majority of respondents (more than two thirds) indicated that the funds were either insufficient, little or just moderate. Only less than a quarter of respondents indicated that the funds were sufficient. The findings support earlier indications by Kamau (2013) in an analysis of funding at Youth Enterprise Development Fund.

Figure 4.9 provides study findings on the extent to which study participants agreed with the statement that the repayment rates for affirmative funds was attractive. Majority, representing more than three quarters of respondents indicated that the affirmative action funds by the SMEs provided attractive repayment rates for funding extended to SMEs as also observed earlier by Simiyu (2016).

![Figure 4.9: Affirmative Funds Repayment Rates](image)

**Source:** Survey data (2018)
4.5 Inferential Analysis

This part provides inferential statistics which help in making generalisations to the entire population. The inferential statistics include Pearson correlation analysis ordinary least squares regression analysis. The study findings are then discussed in relation to theoretical orientations and past empirical results and justifiable conclusions made.

4.5.1 Diagnostic tests

Thorough data screening by way of diagnostic tests was done to ensure that the data sets followed assumptions of major analytical procedures sought such as regression analysis. The diagnostics provided the test for auto-correlation with the Durbin Watson test as well as test for heteroscedasticity by using Test Glejser. Others incorporated test for normality utilizing Shapiro Wilk test as well as test for multicollinearity using VIF and Tolerance regression diagnostics.

Normality test

The study conducted the test of normality in the information set. A total of sixty-five responses was achieved. Shapiro Wilk test was applied since the number of observations were less than 2000. The null hypothesis of the Shapiro Wilk test is that the observed distribution is normally distributed.

The study findings in Table 4.11 indicate that the null hypothesis was not rejected (p > 0.05) and hence a conclusion reached that the observations were normally distributed (Razali & Wah, 2011; Shapiro & Wilk, 1965).

Table 4.11: Normality Test

<table>
<thead>
<tr>
<th></th>
<th>Shapiro-Wilk</th>
<th>Kolmogorov-Smirnov</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Statistic</td>
<td>df</td>
</tr>
<tr>
<td>Financial Performance</td>
<td>.546</td>
<td>65</td>
</tr>
</tbody>
</table>

Source: Survey data (2018)
Test of Multicollinearity

The study was also concerned about the multicollinearity position of the data set. Table 4.12 provides the study results for the multicollinearity test on SPSS.

Table 4.12: Multicollinearity Test

<table>
<thead>
<tr>
<th>Variables</th>
<th>Collinearity Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Tolerance</td>
</tr>
<tr>
<td>(Constant)</td>
<td></td>
</tr>
<tr>
<td>Formal Financing</td>
<td>.456</td>
</tr>
<tr>
<td>Informal Financing</td>
<td>.365</td>
</tr>
<tr>
<td>Personal Financing</td>
<td>.235</td>
</tr>
<tr>
<td>Government Financing</td>
<td>.432</td>
</tr>
</tbody>
</table>

Source: Survey data (2018)

Liu, Hou, Gong, and Kuang, (2003) postulate that variance inflation factors (VIF) of above 10 could warrant further investigation. The study results indicate that VIF for the study variables were 2.192, 2.739, 4.255 and 2.315 for formal financing, informal financing, private financing as well as government financing respectively. All of the values are beneath the maximum or even cut off point of ten. As a result, the multicollinearity issue was absent from the information set.

Heteroscedasticity test

Test for Heteroskedacity was additionally performed using Test Glejser. Extended and Ervin (2000) postulate that Heteroskedacity examination evaluates the chance of there being unequal variance in the error term. Study findings in Table 4.13 indicate that there was no heteroscedasticity as all the p values for all the variables were above 0.05 (Glejser, 1969). The P values for formal financing, informal financing, private financing as well as government financing were 0.071, 0.080, 0.061 as well as 0.089 respectively.
Table 4.13: Heteroscedasticity Test

<table>
<thead>
<tr>
<th>Variables</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
</tr>
<tr>
<td>(Constant)</td>
<td>.011</td>
<td>.003</td>
</tr>
<tr>
<td>Formal Financing</td>
<td>.600</td>
<td>.004</td>
</tr>
<tr>
<td>Informal Financing</td>
<td>.670</td>
<td>.002</td>
</tr>
<tr>
<td>Personal Financing</td>
<td>.075</td>
<td>.003</td>
</tr>
<tr>
<td>Government Financing</td>
<td>.021</td>
<td>.003</td>
</tr>
</tbody>
</table>

Source: Survey data (2018)

4.5.2 Correlation Analysis

Correlation analysis was conducted to establish principally the relationships between the variables of interests to the study. Pearson correlation was utilised for this purpose. It sought to demystify the direction and strength of relationships between financing options and financial performance of SMEs. Table 4.14 provides the study results from the analysis.

Table 4.14: Relationship Between the Study Variables

<table>
<thead>
<tr>
<th>Variables</th>
<th>Financial Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Pearson Correlation coefficient</td>
</tr>
<tr>
<td>Formal Financing</td>
<td>.306**</td>
</tr>
<tr>
<td>Informal Financing</td>
<td>.786**</td>
</tr>
<tr>
<td>Personal Financing</td>
<td>.783**</td>
</tr>
<tr>
<td>Government Financing</td>
<td>.507**</td>
</tr>
</tbody>
</table>

Source: Survey data (2018)
The results show a positive association between financial performance and formal financing of SMEs. The association is actually considered average as the Pearson Correlation Coefficient of 0.306 is actually under 0.5 beyond which the connection will have been mirrored as powerful. The relationship was significant as the p value (0.012) is below 0.05. The study results support earlier empirical foundations by Otuya, Omoka, Ayako, and Kihimbo (2012), Atieno (2001), Kimuyu (2002) and Montoriol Garriga and Garcia-Appendini (2013) that suggested that formal financing would serve to improve the economic functionality of firms.

The Pearson Correlation analysis results also demonstrate a really powerful and significant relationship between financial performance of SMEs and informal financing of SMEs p < 0.01). The relationship is recognized as strong as the Pearson correlation coefficient of 0.786 is actually above 0.7. The outcomes agree with previous studies like Njeru and Mungiru, (2015), Agbo and Ugwuanyi (2012), as well as Fadiga, et al. (2004) that also developed performance enhancing consequences of informal financing.

The results show a strong, positive and significant relationship between financial performance and personal financing of SMEs (p < 0.05). The association is recognized as strong as the Pearson Correlation Coefficient of 0.783 is actually in excess of 0.7. The results support previous studies by Vuvor and Ackah (2011), Mensah (2004) Atieno and), (2001) that additionally suggested that individual financing enhances economic results.

The results show a strong, positive also significant relationship between financial performance and government financing of SMEs found Nanyuki town, Kenya. The strength of relationship is regarded as strong since the Pearson Correlation Co efficient of 0.507 lies between five as well as seven beyond which it will be strong and beneath which it will be seen as average. The relationship is statistically considerable because the significance of 0.012 is actually under five percent level of significance. The outcomes agree with previous outcomes by Makubo (2015), Mensah (2004), Ventura and Zecchini (2009) and Kamau and Irungu (2015) that started that government funding enhances efficiency.
4.5.3 Hypothesis Testing

The results from multiple regression analysis were applied as crucial evidence towards reliably testing the study hypothesis and creating justifiable inferences. This is since inferential statistics permit generalizations on the population. A five percent significant level ($\alpha = 0.05$) was applied. The hypothesis to be tested were captured as:

$H_01$: Formal financing has no significant effect of on the financial performance of SMEs in Nanyuki Town, Kenya.

$H_02$: Informal finance sources has no statistically significant effect on the financial performance of SMEs in Nanyuki Town.

$H_03$: Personal financing has no statistically significant effect on the financial performance of SMEs in Nanyuki Town.

$H_04$: Government funds have no significant effect on the financial performance of SMEs in Nanyuki Town.

The ordinary least squares regression model was considered key in determining the direction and strength of effect, if any, of the financing variables on SMEs’ financial performance.

Table 4.15 presents the summary of the regression model. The study results are essential in deciding the practical use of the suggested type in predicting economic performance of SMEs.

**Table 4.15: Summary of the Regression Model**

<table>
<thead>
<tr>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Durbin-Watson</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.875a</td>
<td>0.7656</td>
<td>0.7706</td>
<td>.00281</td>
<td>2.065</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Formal Financing, Informal Financing, Personal Financing, Government Financing

b. Dependent Variable: Financial Performance

**Source:** *Survey data (2018)*
The R squared is 0.7656. The significance is the fact that 76.56% of variation in financial performance is actually explained by variability in the financing options (formal financing, informal financing, private financing as well as government financing). The results agree with earlier findings by Ugwuanyi and Agbo (2012), Makubo (2015) and Mensah (2004) who observed that financing options have a significant effect on financial performance.

Table 4.16 presents regression model results on analysis of variance.

**Table 4.16: Analysis of Variance**

<table>
<thead>
<tr>
<th>Source of variance</th>
<th>Sum of Squares</th>
<th>Df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>4.876</td>
<td>4</td>
<td>1.219</td>
<td>.360</td>
<td>.033a</td>
</tr>
<tr>
<td>Residual</td>
<td>287.598</td>
<td>61</td>
<td>4.425</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>278.685</td>
<td>65</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Formal Financing, Informal Financing, Personal Financing, Government Financing

b. Dependent Variable: Financial Performance

Source: Survey data (2018)

The p value of 0.033 is less that 5% or 0.05 indicating that the financing sources were significant predictors of financial performance of SMEs. The results therefore support earlier empirical foundations by Ugwuanyi and Agbo (2012), Atieno, (2001), Makubo (2015) and Mensah (2004) who observed that financing options affect financial performance.

Table 4.17 provides the output of the regression model coefficients as generated through SPSS. The regression model was the main tool in explaining the influence of financing options on financial performance of SMEs.
Table 4.17: Coefficients of the Regression Model

<table>
<thead>
<tr>
<th>Independent variable</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>T</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>(Constant)</td>
<td>5.345</td>
<td>.693</td>
<td>2.345</td>
<td>.007</td>
</tr>
<tr>
<td>Informal Financing</td>
<td>.767</td>
<td>.393</td>
<td>.743</td>
<td>3.234</td>
</tr>
<tr>
<td>Personal Financing</td>
<td>.701</td>
<td>.467</td>
<td>.521</td>
<td>.904</td>
</tr>
<tr>
<td>Government Financing</td>
<td>.489</td>
<td>.284</td>
<td>.344</td>
<td>.218</td>
</tr>
</tbody>
</table>

a. Dependent Variable: Financial Performance

Source: Survey data (2018)

The multiple regression analysis provides proof to demonstrate this all of the independent variables; specialized financing, informal financing, private financing as well as government financing are helpful predictors of fiscal performance since the P Values of were under five percent degree of significance. The coefficient for formal financing (0.202) is significantly different from zero since its p value of 0.002 is smaller than the five percent significance level used. As a result, a unit increase in usage of formal financing options would result in a 0.202 device improvement in fiscal results. The null hypothesis was thus rejected, along with a conclusion made that formal financing has a significant effect on financial performance of SMEs. The results support earlier empirical findings by Kihimbo, Ayako, Omoka, and Otuya (2012), Atieno (2001), Kimuyu (2002) and Montoriol Garriga and Garcia-Appendini (2013) that suggested that formal financing would serve to improve the economic performance of firms.

The coefficient for informal financing (0.767) is statistically significant and different from zero. This is because its p value is 0.020 which is below the 5% degree of significance. Thus, a unit increase in informal financing for the SMEs will result in a 0.767 improvement in financial performance. Thus, the null hypothesis was rejected, and a finding made that informal financing has a statistically significant impact on financial performance of SMEs. The outcomes agree with previous studies like Njeru and

The regression coefficient for personal financing (0.701) is statistically and strongly distinct from zero. This is because its p value of 0.011 is under five percent significance level. As a result, a unit increase in usage of personal financing would result in a 0.701 increase in financial performance of the SME. As a result, the null hypothesis was rejected, along with a finding made that personal financing has a significant positive effect on financial performance of SMEs. The results support previous findings by Vuvor and Ackah (2011), Mensah (2004) and Atieno (2001) that additionally suggested that personal financing enhances financial performance.

Lastly, the coefficient for government financing (0.489) is statistically drastically distinct from zero. This's since the p Value of its of 0.017 is under five % or maybe 0.05 degree of significance. As a result, a device increase of usage of government financing would result in a 0.489 device increase in financial performance of SMEs. The null hypothesis was thus rejected, along with a conclusion made that government financing has performance enhancing impact on financial performance of SMEs. The outcomes agree with previous outcomes by Makubo (2015), Mensah (2004), Ventura and Zecchini (2009) and Kamau and Irungu (2015) that started that government funding enhances efficiency. The regression model was developed as follows:

\[
\text{Financial Performance} = 5.345 + 0.202 \text{ (Formal Financing)} + 0.767 \text{ (Informal Financing)} + 0.701 \text{ (Personal Financing)} + 0.489 \text{ (Government Financing)}.
\]

4.5.4 Study Discussion
The study established that there was a statistically significant effect of formal financing on the financial performance of SMEs in Nanyuki Town, Kenya. The study results also show a moderate, positive, and statistically significant relationship between formal financing and financial performance of SMEs. The results support earlier empirical foundations by Kihimbo, Ayako, Omoka, and Otuya (2012), Atieno (2001), Kimuyu
(2002) and Garcia-Appendini and Montoriol-Garriga (2013) who indicated that formal financing would serve to enhance the financial performance of firms. The findings imply that establishment of network of formal credit institutions helps in improving lending conditions as well as terms in favour of small-scale enterprises hence offering a crucial avenue for facilitating their access to credit. The study results also support the findings by Atieno (2001). However, Atieno (2001) established that commercial banks along with other formal institutions fell short of catering for the credit requirements of smallholders, nonetheless, primarily due to their lending terms and conditions.

The study also established that there is statistically significant effect of informal finance sources on the financial performance of SMEs in Nanyuki Town. Moreover, correlation statistics illustrated that there was a very strong, positive, and statistically significant relationship between informal financing and financial performance of SMEs. The results agree with past studies such as Ugwuanyi and Agbo (2012), and Fadiga, et al. (2004) which also established performance enhancing effects of informal financing. The study results also concur with findings by Mungiru and Njeru (2015) that informal sources of investment funding have a major impact on the performance SMEs. Self help team finance, family along with friends’ finance; trade investment funding has a good impact on the overall performance of SMEs while shylock finance sources enjoy an adverse effect on the performance of SMEs. The research suggests that SMEs have to place much more focus on informal finance sources such as trade credit, finance from friends and family and self-help team finance, because the informal sources of finance depend on relationships as well as character implying that information asymmetries between informal borrowers and lenders are much less acute, the loan program process lighter, as well as the collateral requirement easier to satisfy.

Additionally, the study results indicated that there is statistically significant effect of personal financing on the financial performance of SMEs in Nanyuki Town. The results also demonstrate a very strong, positive, and statistically significant relationship between personal financing and financial performance of SMEs. The results support past studies by Ackah and Vvor (2011), Mensah (2004) and Atieno, (2001) who also indicated that
personal financing enhances financial performance. The study results also agree with findings by Agwu et al. (2016) that SMEs rely largely on individual savings of owners, and quite often company earnings, in case there are any for their monetary requirements. This is because they have little or perhaps no access to formal outside credit. Conventional financial institutions regard SMEs as high risk as well as having substantial probability of default. Consequently, the monetary requirements of SMEs are not considered in the lending policy formulation of banks. Many of them are denied access to economic assistance from conventional financial institutions and hence relying heavily on personal sources of finance.

Lastly, the study findings imply that there is statistically significant effect of government funds on the financial performance of SMEs in Nanyuki Town. Similarly, the study results demonstrate a strong, positive and statistically significant positive relationship between government financing and financial performance of SMEs in Nanyuki town, Kenya. The results agree with past results by Makubo (2015), Mensah (2004), Zecchini and Ventura (2009) and Irungu and Kamau (2015) who established that government funding enhances performance. The findings also support the results by Kamunge et al. (2014) that access to government funding exposes enterprises to better chances to grow and thrive while additionally, it leads to enhanced SME performance to a tremendous degree. Generally, access to finance impacts the overall performance of business to a high degree.
CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction
This chapter clarifies on how the research objectives were handled and effectively accomplished. The study provides a summary of the study and its findings. It also reflects on conclusions and provides policy recommendations to guide various stakeholders. Recommendations for further research are also provided based on an analysis of gaps that could not be addressed.

5.2 Summary of Findings
The study investigated the influence of financing options on the financial performance of SMEs in Nanyuki Town, Kenya. The study specifically examined the influence of formal financing, informal financing, personal financing and government financing on the financial performance of SMEs. The Pearson correlation analysis and the multiple regression analysis were the main analytical procedures sought to inform the conclusions.

Regarding financial performance, the study established a poor state of both profitability and liquidity of SMEs. On liquidity, the indicators demonstrated that liquidity of SMEs was way below the universally accepted and recommended thresholds. Specifically, both the current ratio and quick ratio were below the globally accepted norms. The profitability of the SMEs in Nanyuki town, Kenya as indicated by return on assets was established to be relatively low. The profitability among the individual small businesses also demonstrated wide variations.

The findings on formal financing show moderate usage of formal finance sources among SMEs in Nanyuki town. In addition, most SMEs benefiting from formal finance got the facilities from mainly Micro Finance Institutions and SACCOS and rarely from banks.

Collateral requirements and lending conditions were listed as the main hindrances for SMEs access to formal finance. The results of the Pearson correlation analysis indicated a
moderate, positive, and statistically significant relationship between formal financing and financial performance of SMEs. Regression analysis results also demonstrated that formal financing has a significant effect on financial performance of SMEs.

Regarding informal finance, the study established that the facilities were consumed to a great extent in financing SMEs’ operations. The round table or table banking arrangements was the most utilised informal financing facility by the SMEs. The study established that the main factor highlighted as driving preference for informal financing over other available options was the low risk associated with informal groups and less collateral requirements. The Pearson Correlation analysis results demonstrated a very strong, positive, and statistically significant relationship between informal financing and financial performance of SMEs. Multiple regression results established that financial performance of SMEs was significantly and positively affected by informal financing.

The study results show that the SMEs relied on the personal financing sources to a great extent in financing operations. The category of personal finance mostly utilised for SME funding involved ploughing back profits and personal savings. The main factors driving use of personal finance was highlighted as the need to maintain control and high risk associated with other finance sources. The Pearson correlation analysis results demonstrated a very strong, positive, and statistically significant relationship between personal financing and financial performance of SMEs. The multiple regression analysis demonstrated that financial performance of SMEs was significantly and positively affected by personal financing.

The findings on government financing indicated that SMEs only moderately used Government Affirmative Funds in funding their operations. The visibility of the government affirmative action funds was wanting as most SMEs were yet to benefit from government affirmative funds. It was the view of the majority that government affirmative funds lacked fairness in proving funds to SMEs and lacked efficiency in disbursements. Results further indicated that government funding for SMEs was largely insufficient although the repayment rates for affirmative funds was attractive. The Pearson correlation analysis results signposted a strong, positive and statistically
significant positive relationship between government financing and financial performance of SMEs in Nanyuki town, Kenya. Results of the multiple regression analysis indicated that government financing has a significant effect on financial performance of SMEs.

5.3 Conclusion
On financial performance, the study made a conclusion that the poor state of financial performance indicated by both profitability and liquidity of SMEs could be attributed to financing options among SMEs. SMEs had poor access to different financing sources.

Regarding formal financing, the study concluded that formal financing facilities moderately enhanced the financial performance of SMEs. Though SMEs had low access to these sources of financing, the conclusion was that SMEs could perform better financially if access to formal financing is enhanced.

The study concluded that informal sources of finance were the key source of SMEs’ finance. A conclusion was further made that utilisation of informal finance serves to greatly enhance the financial performance of SMEs.

The study further concluded that personal financing was a very significant facility in financing SMEs’ operations. A further conclusion was made that personal financing strongly drives the financial performance of SMEs.

Regarding government financing, it was concluded that the Government Affirmative Funds were yet to gain visibility among SMEs. The study concluded however that government funding influences the financial performance of SMEs.

5.4 Recommendations of the Study
On financial performance, recommendations are made for SMEs to work towards measures to enhance their liquidity and profitability informed by poor performance reported. SMEs are encouraged to revaluate their financing structures to ensure optimal finance mix to boost liquidity and profitability. The stakeholders and especially the
government should devise measures to assist SMEs boost their ability to access alternative funds from formal institutions.

The formal finance institutions should be encouraged to set SMEs friendly lending conditions to enhance accessibility of credit to SMEs. To this regard, the government should consider incentives to formal financial players who establish special facilities targeting SMEs. The government should also consider measures towards improving the visibility and relevance of affirmative funds in boosting SMEs’ activities due to their significance to the economy. The fiscal allocations to affirmative funds should be enhanced and measures established to enhance accountability. The affirmative funds should also be encouraged to pursue alternative disbursement channels to ensure efficient disbursement to SMEs.

Lastly, the study recommends SMEs to formalize their operations, financial management and legal status to enable them enhance access to formal financing sources. Proprietors and managers of the SMES should also ensure that they observe prudent management, accounting and ethical business practices so that to have a good reputation which can help them access funds from different sources.

5.5 Contribution to Knowledge
This study provides empirical evidence on the effect of financing sources on financial performance of SMEs in Nanyuki Town, Kenya. Most of the studies had been conducted in major towns in Kenya and hence this study has provided evidence on access to financing by SMES and how it affects financial performance of SMEs in a small town. Most previous studies treated access to financing as a single variable. Rather than focusing on access to finance as a single variable, the study was able to separate the different financing sources and interrogate the accessibility to the different sources by SMEs. Most previous studies only focussed on access to finance as a single variable failing to capture the disparity that can be observed in accessing the different financing sources such as formal, personal, informal and government affirmative funds. The study hence isolated the different financing sources and established that SMEs were
significantly challenges in assessing government and formal finding sources. These findings hence provide evidence that can be used in reframing the financing access policy by government and other NGOS that focus on financial deepening to SMEs.

5.6 Suggestions for further research
Contextually, because of constraints on research resources, the current study’s scope was restricted to SMEs in Nanyuki Town, Kenya. A further study targeting a wider population should therefore be conducted to give more evidence and enhance generalization. A further study should be conducted on the challenges that SMEs face in accessing government affirmative funds. The current research has highlighted hitches in visibility of government affirmative funds to SMEs despite their significance to the economy. The efficiency of the affirmative funds has also been questioned through the current study. A further study should be carried out on assessment of the efficiency of the affirmative funds. Setbacks were also highlighted on SMEs’ access to formal financing. A further study should be conducted to determine how SMEs’ access to formal finance could be enhanced.
REFERENCES


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Appendices

Appendix I: Introduction Letter

RE: OWNERS OF SMEs IN NANYUKI TOWN

I am a Master of Business Administration (Finance option) at Kenyatta University. I am conducting a study titled ‘Financing options and financial performance of small and medium enterprises in Nanyuki town, Kenya’. The study is aimed at satisfying the requirements for the award of the degree. I hereby request you to provide the required information to enable me to achieve my objectives.

Data provided will only be used for academic purpose only and will be held confidentially. The results of the analysis will eventually help boost the overall performance of this particular business and particularly the usefulness of introducing as well as using funding mechanisms.

Appreciation is provided as you assist in the development of new understanding to help both the business as well as the sector.

Regards,

..................

Emily Gakatha Ndemi
D53/NYI/PT/ 28735/2014
Researcher
Appendix II: Questionnaire to SMEs

SECTION A: BACKGROUND INFORMATION
1. SME’s Name (Optional)

2. Gender of Respondent
   Male ( )
   Female ( )

3. Please indicate the number of years that the SME has been in operation?
   2 years and below [ ] 3 to 4 years [ ]
   Above 5 years [ ]

SECTION B: FINANCING OPTIONS
I: FORMAL FINANCING
4. To what extent does the SME consume formal sources of credit financing to meet day to day demands? Tick appropriately
   1. Not at All ( ) 2. Little Extent ( )
   3. Moderate Extent ( ) 4. Great Extent ( )
   5. Very Great Extent ( )

5. Which of the following formal sources of credit financing does the SME utilise most in financing business undertakings?
   SACCOs ( ) Commercial Banks ( )
   Micro Finance Institutions ( ) {Others state…………………} ( )

6. Which of the following factors mostly limit your ability to access formal sources of funds from the above institutions?

<table>
<thead>
<tr>
<th>Factor</th>
<th>Tick against one factor</th>
</tr>
</thead>
<tbody>
<tr>
<td>Access to Information</td>
<td></td>
</tr>
<tr>
<td>Availability of collateral</td>
<td></td>
</tr>
<tr>
<td>Previous experience</td>
<td></td>
</tr>
</tbody>
</table>
II: INFORMAL FINANCING

7. To what extent do you rely on informal funding options as a source of the SME funding?

1. Not at All ( )  2. Little Extent ( )
3. Moderate Extent ( )  4. Great Extent ( )
5. Very Great Extent ( )

8. Which of the following is the most commonly consumed informal lending option for SME funding?

<table>
<thead>
<tr>
<th>Option</th>
<th>Tick against one option</th>
</tr>
</thead>
<tbody>
<tr>
<td>Membership advances from Self-help groups</td>
<td></td>
</tr>
<tr>
<td>Informal advances from shylocks</td>
<td></td>
</tr>
<tr>
<td>Round table or Table banking arrangements</td>
<td></td>
</tr>
<tr>
<td>Donations from friends</td>
<td></td>
</tr>
</tbody>
</table>

9. What is the main reason or factor that makes you prefer informal sources of business financing over other options available? Tick one option

   Little or no collateral requirement by informal groups. ( )
   Lack of knowledge about other sources of financing. ( )
   Low risk associated with informal groups. ( )
   Inhibitive Conditions of other sources. ( )

III: PERSONAL FINANCING

10. To what extent do you rely on personal financing in funding your SME?

1. Not at All ( )  2. Little Extent ( )
3. Moderate Extent ( )  4. Great Extent ( )
5. Very Great Extent ( )
11. Which among the following is the most commonly utilised source of personal financing by the SME?

<table>
<thead>
<tr>
<th>Source</th>
<th>Tick against one option</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal Savings</td>
<td></td>
</tr>
<tr>
<td>Ploughing back profits into the company</td>
<td></td>
</tr>
<tr>
<td>Proprietors seed capital</td>
<td></td>
</tr>
</tbody>
</table>

12. What is the main factors informing the decision to finance the business using personal sources? Tick one

- Need to keep control of the business
- Dislike for debt
- High Risks involved with other sources
- Tough conditions in accessing other sources of funds
- Small amounts of capital needed

IV: GOVERNMENT FINANCING/FUNDS

13. To what extent do you rely on Government Affirmative Funds in funding your SME?

1. Not at All ( )
2. LittleExtent ( )
3. Moderate Extent ( )
4. Great Extent ( )
5. Very Great Extent ( )

14. Which of the following affirmative (SME) funds have you benefited from in your business undertakings? Tick appropriately

- Uwezo Fund ( )
- Youth Enterprise Development Fund ( )
- Women Enterprise Development Fund ( )
- Micro and Small Enterprise Authority ( )
- County (Government) Enterprise Funds ( )
- Others (Please state)………………………………… ( )
- None of the above ( )

15. Indicate the extent you agree with the listed statements concerning the administration of government funds to SMEs? Tick appropriately.

1. Not at All ( )
2. Little Extent ( )
3. Moderate Extent ( )
4. Great Extent ( )
5. Very Great Extent ( )

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>a) There is farness in funding SMEs by government funds</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>b) The government affirmative funds are efficient in disbursing funds to SMEs</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>c) The government funds disburse enough cash to finance SMEs undertaking and business plans</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>d) The repayment rates for government funds are very attractive</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

SECTION C: FINANCIAL PERFORMANCE OF SMEs

I: LIQUIDITY

16. Provide the following information on current assets and liabilities of the business.

A: CURRENT RATIO

<table>
<thead>
<tr>
<th>YEAR</th>
<th>Current liabilities</th>
<th>Current assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2014</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

3 YEARS AVERAGE CURRENT RATIO

B: QUICK RATIO OR ACID TEST RATIO

<table>
<thead>
<tr>
<th>FINANCIAL YEAR</th>
<th>Inventory</th>
<th>Current liabilities</th>
<th>Prepayments</th>
<th>Current assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2014</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

3 YEARS AVERAGE QUICK RATIO
II: PROFITABILITY

17. Provide information on the past profitability of the business.

<table>
<thead>
<tr>
<th>FINANCIAL YEAR</th>
<th>Earnings After Tax</th>
<th>Total Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2014</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3 YEARS AVERAGE ROA</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

B: NET PROFIT MARGIN

<table>
<thead>
<tr>
<th>FINANCIAL YEAR</th>
<th>Net profit</th>
<th>Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2014</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3 years average Net Profit Margin</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Thank you for your input into the Questionnaire
## Appendix III: Sampling Frame and Sample Size

<table>
<thead>
<tr>
<th>No</th>
<th>Type of business</th>
<th>Population (N)</th>
<th>Nh = (Nh/N) Xn</th>
<th>Sample size</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Chemist</td>
<td>42</td>
<td>4.83</td>
<td>5</td>
</tr>
<tr>
<td>2</td>
<td>Butchery</td>
<td>64</td>
<td>7.36</td>
<td>7</td>
</tr>
<tr>
<td>3</td>
<td>Salons/ barbers</td>
<td>57</td>
<td>6.55</td>
<td>7</td>
</tr>
<tr>
<td>4</td>
<td>Shops/Supermarkets</td>
<td>52</td>
<td>5.98</td>
<td>6</td>
</tr>
<tr>
<td>5</td>
<td>Garages</td>
<td>12</td>
<td>1.38</td>
<td>1</td>
</tr>
<tr>
<td>6</td>
<td>Restaurants</td>
<td>40</td>
<td>4.6</td>
<td>5</td>
</tr>
<tr>
<td>7</td>
<td>Hardwares</td>
<td>32</td>
<td>3.68</td>
<td>4</td>
</tr>
<tr>
<td>8</td>
<td>Fuelling stations</td>
<td>33</td>
<td>3.79</td>
<td>4</td>
</tr>
<tr>
<td>9</td>
<td>Boutiques</td>
<td>35</td>
<td>4.02</td>
<td>4</td>
</tr>
<tr>
<td>10</td>
<td>Tailors/ drycleaners</td>
<td>47</td>
<td>5.41</td>
<td>5</td>
</tr>
<tr>
<td>11</td>
<td>Electronics shops</td>
<td>50</td>
<td>5.75</td>
<td>6</td>
</tr>
<tr>
<td>12</td>
<td>Money transfer agents</td>
<td>52</td>
<td>5.98</td>
<td>6</td>
</tr>
<tr>
<td>13</td>
<td>Workshops</td>
<td>63</td>
<td>7.24</td>
<td>7</td>
</tr>
<tr>
<td>14</td>
<td>Beauty shops</td>
<td>37</td>
<td>4.25</td>
<td>4</td>
</tr>
<tr>
<td>15</td>
<td>Bars</td>
<td>71</td>
<td>8.16</td>
<td>8</td>
</tr>
<tr>
<td>16</td>
<td>Clinics</td>
<td>14</td>
<td>1.6</td>
<td>2</td>
</tr>
<tr>
<td>17</td>
<td>Consultants</td>
<td>40</td>
<td>4.6</td>
<td>5</td>
</tr>
<tr>
<td>18</td>
<td>College services</td>
<td>24</td>
<td>2.76</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong></td>
<td><strong>765</strong></td>
<td><strong>88.94</strong></td>
<td><strong>88</strong></td>
</tr>
</tbody>
</table>

*Source: NCCI, Laikipia County (2018)*
Appendix IV: Kenyatta University Authorization Letter

KENYATTA UNIVERSITY
GRADUATE SCHOOL

E-mail: dean-graduate@ku.ac.ke
Website: www.ku.ac.ke

P.O. Box 43844, 00100
NAIROBI, KENYA
Tel. 810901 Ext. 4150

Internal Memo

FROM: Dean, Graduate School
TO: Emily Gakatha Ndemi
     C/o Accounting & Finance Dept.

DATE: 25th September, 2017
REF: D55/ NYI/FT/28735/2014

SUBJECT: APPROVAL OF RESEARCH PROPOSAL

We acknowledge receipt of your revised Research Proposal as per our recommendations raised by the Graduate School Board of 29th March, 2017 entitled “Effects of financing options on financial performance of Small and Medium Enterprises in Nanyuki Town, Kenya”.

You may now proceed with your Data Collection, Subject to Clearance with Director General, National Commission for Science, Technology and Innovation.

As you embark on your data collection, please note that you will be required to submit to Graduate School completed Supervision Tracking Forms per semester. The form has been developed to replace the Progress Report Forms. The Supervision Tracking Forms are available at the University’s Website under Graduate School webpage downloads.

Thank you.

ANNELI MWANIKI
FOR: DEAN, GRADUATE SCHOOL

C.c. Chairman, Department of Accounting & Finance

Supervisors:

1. Dr. John Mungai
   C/o Management Science Department
   Kenyatta University
Appendix V: NACOSTI Research Permit

NATIONAL COMMISSION FOR SCIENCE, TECHNOLOGY AND INNOVATION

Ref. No. NACOSTI/P/17/32099/19639

Date: 2nd November, 2017

Ndeemi Gakatha Emily
Kenyatta University
P.O. Box 43844-00100
NAIROBI

RE: RESEARCH AUTHORIZATION

Following your application for authority to carry out research on “Effects of financing options on financial performance of Small and Medium Enterprises in Nanyuki Town Kenya” I am pleased to inform you that you have been authorized to undertake research in Laikipia County for the period ending 30th October, 2018.

You are advised to report to the County Commissioner and the County Director of Education, Laikipia County before embarking on the research project.

Kindly note that, as an applicant who has been licensed under the Science, Technology and Innovation Act, 2013 to conduct research in Kenya, you shall deposit a copy of the final research report to the Commission within one year of completion. The soft copy of the same should be submitted through the Online Research Information System.

GODFREY P. KALERWA MSc., MBA, MKIM
FOR: DIRECTOR-GENERAL/CEO

Copy to:

The County Commissioner
Laikipia County.

The County Director of Education
Laikipia County.
THIS IS TO CERTIFY THAT:
MS. NDEMI GAKATHA EMILY
of KENYATTA UNIVERSITY, 0-10101
KARATINA, has been permitted to
counter research in Laikipia County

on the topic: EFFECTS OF FINANCING
OPTIONS ON FINANCIAL PERFORMANCE
OF SMALL AND MEDIUM ENTERPRISES
IN NANYUKI TOWN KENYA

for the period ending:
30th October, 2018

Applicant's Signature

 Permit No : NACOSTI/P/17/32099/19639
 Date Of Issue : 2nd November, 2017
 Fee Received : Ksh. 1000

Director General
National Commission for Science,
Technology & Innovation