

FACTORS AFFECTING CHOICE OF RETAIL BANK BY SMEs IN THE
EDUCATION SECTOR IN KENYA

A CASE STUDY OF PRIVATE SCHOOLS IN NAIROBI COUNTY

BY

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of retail bank by smes*



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DEDICATION

This study is dedicated to my son Ian Mwaniki and my wife Jane Nyokabi for their constant encouragement to me and for being patient enough to see me go through my academic struggle thus realizing my long cherished dream.

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ABSTRACT

The financial system in most of Kenya is under-developed and so provides few financial instruments. Studies however show that commercial banks provide the lowest amount of financing to small and Medium-sized Enterprises and where it is provided the credit is rationed (Atieno, 1998). Furthermore, the banks do not know the needs of their clients, which means that they do not have the ability to provide tailor made products for the customers and this is how they lose on potential customers. Meanwhile, none of studies done on Kenyan retail banks have focused on bank preferences by Small and Medium-Sized Enterprises. This research therefore fills this gap by studying the factors that are considered in the choice of a retail bank by Small and Medium-Sized Enterprises and their order of importance. The aim of the study was to establish the factors that affect the choice of a retail bank by Small and Medium-sized Entrepreneurs in educational sector in Kenya. The research used the descriptive research design. The target population of the study was the top management of 300 private schools in Nairobi County. The study used stratified random sampling to come up with the sample of the study. The study used primary data which was collected using semi structured questionnaires.

The study found out that SMEs relied on loans to fund the operation of their institution and therefore the amount of interest rates on loans borrowed and other services influenced the choice of retail bank by the SMEs. The amount of interest rates influenced the choice of retail bank to a great extent. In addition, SMEs preferred their respective bank because they offered interest rate on loan and other services at competitive rates. The researcher

established that through technology had made bank more proximate to SMEs. However this was not the case with all the services since services like borrowing credit from banks could only be accessible over the counter. Thus the proximity of the bank is a determinant of the choice of retail bank as SMEs required banking services regularly. The study revealed that the preferred banks of the SMEs were offering high quality services. The entrepreneurs are satisfied by the services offered by their preferred bank to a great extent. In addition, the quality of customer service influenced SMEs choice of the bank to a great extent. The quality service directly relates to customer satisfaction, retention and loyalty to a great extent. The research also found out that security of deposit is a key consideration made by the SMEs while selecting their choice of retail bank. In addition, the banks were responsible for deficiency in service for lack of security in its premises and loss caused to customer. The study also established that there is a correlation between the factors and the choice of retail bank by the SMEs with quality service having the highest value and country of incorporation having the lowest correlation value.

The research concluded that SMEs relied on loans to fund the operation of their institution and therefore the amount of interest rates on loans borrowed influenced the choice of retail bank by the SMEs. The study concluded that the amount of interest rates influenced the choice of retail bank to a great extent. In addition, SMEs preferred their respective bank because they offer interest rate on loan and services at competitive rates. The researcher concluded that through technology made bank accessible and close to SMEs thus enhancing the proximity of the bank to the business. However some services like borrowing credit from

banks could only be accessible to the entrepreneurs by going to their preferred banks. The proximity of the bank is a determinant of the choice of retail bank as SMEs required banking services regularly. The study concluded that the SMEs considered their preferred banks to be offering high quality services to them thus they were the bank of choice. The entrepreneurs are satisfied by the services offered by their preferred bank to a great extent. In addition, the quality of customer service influenced SMEs choice of the bank to a great extent. The quality service directly relates to customer satisfaction, retention and loyalty to a great extent. The research concludes that security of deposit is a key consideration by the SMEs while selecting their choice of retail bank. In addition, the banks were responsible for deficiency in service for lack of security in its premises and loss caused to customer. The study also concludes that there is a correlation between the factors and the choice of retail bank by the SMEs with quality service having the highest value and country of incorporation having the lowest correlation value.

The study recommends that banks should improve on the quality of service they offer to the SMEs to become the preferred choice of retail bank by the SMEs. Service quality will play an important role in enhancing customer satisfaction, retention and loyalty. The study further recommends that banks should regularly review the amount of interest rates on loans and other services offered to the SMEs, to design interest rates at competitive prices. The study finally recommends that the banking institution should enhance the security of deposit by their clients which is a major determinant of choice of retail bank by the SMEs.

DEFINITION OF TERMS

Small and medium enterprises These are companies that have 50-250 employees and whose headcount or turnover falls below certain limits. The number of employees vary from a country to another. The European Union has started to standardize the concept. Its current definition categorizes companies with fewer than 50 employees as "small", and those with fewer than 250 as "medium". By contrast, in the United States, when small business is defined by the number of employees, it often refers to those with fewer than 100 employees, while medium-sized business often refers to those with fewer than 500 employees.

Private schools; Institutions owned by an individual or supported by a private organization or private individuals rather than by the government.

Interest rates; The percent charged, or paid, for the use of money. It is charged when the money is being borrowed, and paid when it is being loaned. Interest is paid by a bank when money is deposited because the bank uses that money to make loans. The interest rates charged by banks are determined by: interest rate on deposits; cost of liquidity; cost of holding cash; and operational costs. The interest on deposits depends on the bank's cash ratio, its overall financial stability and the type of the bank.

Service Quality involves a comparison of expectations with performance. It is a measure of how well a delivered service matches the customers' expectations. The perceptions of high service quality and high service satisfaction result in a very high level of purchase intentions.

Safety of deposits; This is the assurance that banks offers to its customers on the availability of the cash deposited in their accounts. Bank is responsible for deficiency in service for lack of security in its premises and loss caused to customers.

Proximity to the bank This is the distance that a bank customer covers while seeking banking services. Mainly because with ever advancing technological possibilities distance was losing its influence on trade or banking.

LIST OF ACRONYMS

SMEs Small and medium enterprises

GoK Government of Kenya

CBK Central Bank of Kenya

VAT value-added tax

LSDV Least Square Dummy Variable model

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CHAPTER ONE

INTRODUCTION

1.1 Introduction

This chapter introduces the topic under investigation by highlighting the background of the study. The chapter then presents the problem statement. In addition, the chapter presents the research objectives, scope of the study and the significance of the study. Finally the chapter gives the acronyms used in the study.

1.1.1 Background of the study

Satisfied customers are the best guarantee of stability and growth. As with other service sectors, bank customers deserve the very best products and service a bank can offer. In addition, the reality that retail banking is the new jewel in Kenya's banking industry is slowly sinking in with the banks preparing to expand their branch network to attract the masses. The retail banking sector is currently considered to have handsome dividends causing major banks like Barclays, National Industrial Credit Bank and others to venture into the market. Today it is a common phenomenon for banks to roll out promotional campaigns targeted at retail customers. This has also seen their revenue streams rise, with up to 35% of annual revenue in some banks attributed to it. The segment is also being enticed by personal and micro loans that have enabled the former termed as un-bankable lot access cheap credit (Bonyo, 2008).

In the past banks have not treated customers as the king but rather have preferred to treat them as account numbers, passbooks and even as loan applications (Domingo, 2004). In the current times competition for customers has become very stiff and thus the necessity to shift treating customers as human beings each with their own unique characteristics (Waylaid & Cole, 1997). Kenya has created conditions for private-sector growth but is still held back by an inadequate financial system. Small and Medium-Sized Enterprises are key to the economy but insecurity, corruption and poor infrastructure prevent them being motors of growth. Kenya's private sector consists of mostly informal micro- enterprises, operating alongside large firms. Most companies are small because the private sector is new and because of legal and financial obstacles to capital accumulation.

Between these large and small firms, Small and Medium-Sized Enterprises are very scarce and constitute a "missing middle." Small and Medium-Sized Enterprises are weak in Kenya because of small local markets, undeveloped regional integration and very difficult business conditions, which include official bureaucracy, poor infrastructure, flawed legal systems, inadequate financial systems and unattractive tax regimes. Many firms stagnate and remain informal resorting to the use of primitive technology that cannot give them a competitive advantage. Their small size also protects them from potential lawsuits (since they do not have assets that can be seized in case of bankruptcy)

Large firms have an upper hand because they have the muscle to withstand legal and financial challenges. They are also in a better position to negotiate and also have many credible contacts that can help them to access better resources. They have a better access to

foreign funding, state of the art technology and globalised markets especially if they are subsidiaries of multinationals. They do not have to depend on the wanting public resources since they have the financial muscle to acquire better resources. Kenya's Small and Medium-Sized Enterprises have little access to finance, which acts an impediment to their establishment and eventual growth. Their main sources of capital are ploughed back profits, informal savings and loan associations (tontines), which are unpredictable, insecure and have little room for risk sharing because of their regional or sectarian focus. Access to formal finance is poor because of the high risk of default among Small and Medium-Sized Enterprises.

1.2 Problem Statement

There is a large bulk of both un-banked and under-banked Small and Medium-sized Enterprises (SMEs) as reviewed by a study by Equity Bank in 2006. It has also emerged that most Small and Medium-sized Enterprises' proprietors flock to both microfinance enterprises and informal merry-go-rounds to save their constant income. Despite high percentage of profitability among Kenyan Small and Medium-sized Enterprises in Nairobi, they have been shunned by the formal banking sector and have been looking for escape routes in terms of a place to save the surplus funds. This has greatly benefited the Microfinance institutions which charge exorbitant fees and commissions for services as well as prohibitive interest rates for advances. Small and Medium-sized Enterprises in Kenya can rarely meet the conditions set by financial institutions, which see them as a risk because of poor guarantees and lack of information about their ability to repay loans.

The financial system in most of Kenya is under-developed and so provides few financial instruments. Studies however show that commercial banks provide the lowest amount of financing to small and Medium-sized Enterprises and where it is provided the credit is rationed (Lee, 2003). Furthermore, the banks do not know the needs of their clients, which means that they do not have the ability to provide tailor made products for the customers and this is how they lose on potential customers. In his study, Levesque et al (1996) suggested that customer satisfaction with Canadian retail banks derived from service quality dimensions, service features and pricing issues, as well as problems and its recovery.

Although the statistical base of the small businesses in Kenya is still poor, there can be little doubt about their relative significance. There are more than 800,000 small, medium and micro-enterprises in the country, absorbing about a quarter of the labor force of 30 million people. Small enterprise baseline survey also indicates that there is high rate of failure and stagnation among many start-up businesses. The survey reveals that only 38% of the businesses are expanding while 58% have not added workers (Devlin, 2007). According to the survey, more enterprises are most likely to close in their first three years of operation. This state of affairs has taken place despite the growth in the number of small enterprises as indicated by Devlin, (2007).

According to (Domingo, 2004) finance, manpower and marketing are among the most highly ranked problems facing small enterprises in the manufacturing sector. According to Rukwaro (2001) family size, which is a component of culture, affects the business growth of SMEs. Large families were found to withdraw large sums of money from the business to support

their families on food, clothing, education and other needs leaving little to finance business operations. This is in addition to about 3.5 million people involved in some or other type of survivalist enterprise activities. The small business sector is highly diverse, with structures, problems, growth potential and access to support differing widely between segments. Given the fact that the Small and Medium-sized Enterprises support the bulk of the economy in terms of Gross Domestic Product and the high proportion of the population that it supports, banks should not ignore them. Instead there should be an intensive study detailing what they consider in their banking so as to harness the huge population of small businesses into retail banking and thus grow them to larger and better organizations. The end result will be better small and Medium-sized Enterprises, happier and growing nation and a profitable banking sector (Kangaru, 2008).

Meanwhile, none of these studies have focused on Kenyan retail banks nor do they study retail bank preferences by Small and Medium-Sized Enterprises. This research therefore filled this gap by studying the factors that needs to consider in the choice of a retail bank by Small and Medium-Sized Enterprises and their order of importance.

1.3 Objectives of the Study.

This study aimed at achieving the following objectives:

1.3.1 General objective

To establish the factors that affect the choice of a retail bank by Small and Medium-sized Entrepreneurs

1.3.2 Specific objectives

- i. To establish the influence of interest rate on loan and service on the choice of retail bank by the SMEs.
- ii. To investigate the effect of the proximity to the bank on choice of the retail bank by the SMEs.
- iii. To find out the influence the country of incorporation of the bank on the choice of a retail bank by SMEs.
- iv. To examine the effect of service quality on the choice of a retail bank by the SMEs.
- v. To investigate the influence of safety of deposit on the choice of retail banks by SMEs.

1.5 Research Question

The study was guided by the following research questions;

- i. Do the interest on loan and the charges on other services provided influence the choice of a retail bank by SMEs?
- ii. What is the effect of accessibility to the bank on the choice of retail bank by SMEs?
- iii. What is the effect of country of incorporation of the bank to the choice of a retail bank by SMEs?
- iv. Does the service quality offered by banks affect the choice of a retail bank by SMEs?

- v. Does the safety of deposit determine the choice of retail banks by SMEs?

1.6 Scope of the study

The study was limited to Nairobi County which formed the geographical scope of the study. The study sought to collect information from 300 small and medium sized enterprises. The study also sought to establish the factors affecting choice of retail banks by SMEs.

1.7 Significance of the study

The study may be significant to a number of stakeholders in the banking and other sectors of the Kenyan economy. First of all the study might be of significance to the formal banking sector. Every Kenyan bank, regardless of whether it is fully private or partially private seeks to attain a competitive advantage and provide value for its shareholders and one of the ways this can be done is through expansion of their deposit base and the amount of interest accrued from loans provided to customers.

This study may also help banks in understanding Small and Medium-Sized Enterprises and their needs. It may enable them to tailor their products and services to accommodate the Small and Medium-Sized Enterprises. Since Small and Medium-Sized Enterprises form the greatest part of the Kenyan economy, the banks enhance their competitive advantage by harnessing this unexploited customer segment. It may also help them in their strategic planning activities meant to attract and retain their customers and also expand their customer base.

Secondly, the study may act as a guide to the small and medium sized entrepreneurs in their choice of retail bank. Most Small and Medium-Sized Enterprises are struggling because they cannot get the much needed funding from banks. One major reason that makes them to remain stagnant is their failure to access credit which means that the Small and Medium-Sized Enterprises cannot achieve their strategic objectives.

The proprietors of Small and Medium-Sized Enterprises result to other sources of credit like shylocks, microfinance institutions which provide loans at very prohibitive interest rates hence which compromise their profitability and growth. This study may simplify banking from a Small and Medium-Sized Enterprises perspective. It may also highlight the needs of Small and Medium-Sized Enterprises and outline recommendations that might enable banks to capture the huge Small and Medium-Sized Enterprises customer segment. The end results may be: interest on the loans and other services deposits of Small and Medium-Sized Enterprises, lower interest charged on loans to them and finally phenomenal growth into larger institutions.

In addition, the study may give the Government planners an insight as they plan for the nation. As the backbone of the Kenyan economy, Small and Medium-Sized Enterprises are important for the strategic plans of the Kenyan Government. By looking at the recommendations of this research, the Government might be able to formulate policies that are friendly to Small and Medium-Sized Entrepreneurs thus enable them to be more

profitable. This may see the Government reap more income tax and also help it as it seeks to achieve the Millennium Development Goals and achieve Vision 2030. Finally, the findings of the study might also bridge the knowledge gap and increase the literature hence to be used as reference material by future researchers in this field.

1.8 Limitation of the study

- i. The study could not control the respondents' attitude which could have affect the quality of information given.
- ii. The study was limited by failure of some head teachers and top management personnel in the finance department to disclose critical information on the institutions' financial status owing to the fear that the information could be shared with their competitors.
- iii. The study was also limited to low response rate given that the questionnaires were administered when the respondents were at work and might be too busy to pay attention to the questionnaires.
- iv. The research findings may not be generalizable and applicable to SMEs in other regions in the country owing to the fact that different regions have different factor that affect the choice of retail banks.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter presents a review of literature related to this study. It tries to identify the rationale for the factors affecting choice of a suitable bank by SMEs entrepreneurs. Most economic activities revolve around the small and medium-sized enterprise (SME) sector (Wendel and Harvey, 2006). Yet in many developing countries, SMEs have limited access to formal credit. In sub-Saharan Africa, for example, banking-sector penetration is roughly one percent of the population (Stein, 2001). According to Strategic Business Advisors (Africa) Ltd.–SME Banking Sector Report (2007), there are about 2.2 million micro, small and medium enterprises in Kenya, of which 88 percent are non-registered. Of this non-registered group, only 23 percent have bank accounts, and only 10 percent have ever received credit from any formal source.

2.2 Fragmented Business Systems in Kenya

Business systems do not operate in a vacuum; they operate in an environment of institutions. A theory of business system is derived from this, which acknowledges that business systems differ from country to country because of different historical development of institutions. Four elements are important within an institutional environment. These are financial institutions, Social structure, Market structure and Technological and innovation systems.

2.2.1. Public Sector

In general there are three classes of business sectors in Kenya: the parastatals, characterized by their monopolistic production. Their management is highly indigenized, appointments of top managers, however, are often politically motivated. Parastatal is a term applied, especially in Africa, to an organization established by a government but which, through its constitution and budgetary arrangements, enjoys a great degree of operational freedom and insulation from direct political interference.

2.2.2 Private sector

The private sector, which is dominated by non-indigenous traders, such as multinationals. The non-indigenous traders often occupy a certain sub-system of the economy and form a closed system. The multinationals depend on transfer of knowledge from their corporate headquarters in the west. They are highly dependent on state support for access to the country. In the post independence period the government has tried to break this non-indigenous monopoly, but fears about gaining influence of competing indigenous groups for power prevented it from pursuing it seriously.

2.3 Characteristics of Small and Medium-sized Enterprises in Kenya

In this study, the terms "firm," "establishment," "business," and "enterprise" are used interchangeably. An "enterprise" is defined here as any income-earning activity that is not in primary agriculture or mineral production. There is no generally accepted definition of a

Small and Medium-Sized Enterprises are generally distinguished by the nature of their production and management arrangements, trading relations, financial practices, internal competence, etc. Typically the following features in varying degrees characterize them, Small units, often rural-based and family-owned ,small independent enterprises standing alone and producing for a well-defined market ,specialized firm producing specialized products ,selling to the international and/or local markets, rely on low cost raw materials, low energy costs, low labor costs, low division of labor, flexible and often small production runs, low capital formation and largely labor intensive units with low-level technologies and Small and Medium-Sized Enterprises, especially in high technology industries.

2.4 Types and Features of Small Scale Businesses in Kenya

Survivalist enterprises are activities conducted by people who are unable to find a paid job or get into an economic sector of their choice. Income generated from these activities usually falls far short of even a minimum income standard, with little capital invested, virtually no skills training in the particular field and only limited opportunities for growth into a viable business. Poverty and the attempt to survive are the main characteristics of this category of enterprises. Given the large number of people involved in survivalist activities, this constitutes a vast challenge, which has to be tackled within the broader context. Micro-enterprises are very small businesses, often involving only the owner, some family member(s) and at the most one or two paid employees. They usually lack 'formality' in terms of business licenses, value-added tax (VAT) registration, formal business premises, operating permits and accounting procedures. Most of them have a limited capital base and only

rudimentary technical or business skills among their operators. However, many micro-enterprises advance into viable small businesses. Earning levels of micro-enterprises differ widely, depending on the particular sector, the growth phase of the business and access to relevant support. Small enterprises constitute the bulk of the established businesses, with employment ranging between five and about 50. The enterprises will usually be owner-managed or directly controlled by the owner-community and are mostly family owned. They are likely to operate from business or industrial premises, be tax-registered and meet other formal registration requirements. Classification in terms of assets and turnover is difficult, given the wide differences in various business sectors like retailing, manufacturing, professional services and construction.

Medium enterprises constitute a category difficult to demarcate vis-à-vis the "small" and "big" business categories. It is still viewed as basically owner/manager-controlled, though the shareholding or community control base could be more complex. It is characterized by the employment of more than 200 employees and capital assets of a substantial amount of about Kshs 2 million (excluding property).

2.5 Financial Needs for Small and Medium-Sized Enterprises.

Small and Medium-Sized Enterprises have faced persistent pressure when seeking funds for investment. They cannot easily access funding because they are underdeveloped and also lack a credit history that banks can study before rating their creditworthiness. Secondly, they do not have the business strength that can allow them to bring in equity investors. Owners may also not have a saving history with a financial intermediary that can form the basis of savings led credit. This possibly explains why banks in the fast few years have relocated from rural areas and suburban areas rendering potential customer in these areas to have no access to credit (Coetzee et al, 2000) Small and Medium-Sized Enterprises need credit for investment in business, operational activities and for growth in business.

Invest in business: Small and Medium-Sized Enterprises require funds as start up capital for investing in new ventures that they may come up with. Rukwaro (2000) observes that most Small and Medium-Sized Enterprises obtain fund from own sources, including savings and from friends, citing the fact that very few creditors are willing to lend for start up businesses.

Operational purposes: Small and Medium-Sized Enterprises need funds to purchase raw materials, supplies and carry out activities vital for production. They may make sales on credit and hence need bridging funds as they wait repayment studies have shown that most funds received from credit institutions are used for working capital (Gatune, 2000).

Growth of business: As Small and Medium-Sized Enterprises grow they require funds to finance growth in fixed assets and increase working capital. They therefore require longer-

term credit in ever increasing amounts. Small and Medium-Sized Enterprises obtain such funds from formal institutions as well as own funds since many Micro Finance Institutions lack appropriate programs to finance such growth. Studies indicate that a high drop out rate from Micro Finance Institutions that remain rigid insisting a group methodology and lower amount of loan for customers, who have progressively graduates to higher loan requirements (Rukwaro 2000).

In other purposes promotions of Small and Medium-Sized Enterprises need lump sum funding to finance personal issues so that they can repay the credit using income generated from business. Often loans are diverted to “Providential” or “non-productive” purposes to meet emergency medical or educational expenses.

2.6 Perceptual Barriers

Small businesses do not have the skills to successfully run a business. This perception becomes a barrier for Small and Medium-Sized Enterprises in getting finance” (Alem, 2008). Small and Medium-Sized Enterprises that form the ‘missing middle’ in demand-side financing landscape in African countries are generally perceived by local banks and financial institutions as risky and therefore unprofitable. Small entrepreneurs do not have the skills/capacity to run successful businesses. Differing incentives, expectations and motivations between investors and fund managers with regards to investing in the Small and Medium-Sized Enterprises' sector results in misalignment of financial strategy of fund managers, also becoming a reason of an incorrect perception about the sector’s profitability.

Perception of equity amongst entrepreneurs as giving away stake in their businesses to outsiders hinders them from accessing equity type financing. Enforcing environmental sustainability as a precondition to financing hinders the Small and Medium-Sized Enterprises' chances of accessing affordable finance. In addition the cost of doing business with banks in Africa is high, while the professional attitude is low.

2.7 Factors in Retail Banking

2.7.1 Customer Convenience

Historically, consumers have chosen financial services based largely on availability and location. Unable to have a 24 hour branch on every corner, competitive financial services organizations seek other ways to meet these demands. With advances in technology and innovations in human resource practices, the concept of convenience has extended well beyond availability and location to imply a wide range of products and services available at any time, from any place. Customers might wish to file loan applications over the phone at 3 a.m. on a Saturday, for example, or to use a short telephone call to transfer funds between investment vehicles from a remote site. The development of ATMs, voice response units, computer banking, and the ability to engage in almost any transaction through these channels illustrates the commitment of the industry to provide customers with whatever they want, whenever they want it (Parasuraman, Zeithaml & Berry 1990).

Rapid turnaround time is also increasingly important in financial services. For example, customers expect firms to be capable of moving money instantly across investment products.

Turnaround time on small consumer loans decreased dramatically from weeks to hours in the last few years, a trend that continues across a wider range of products such as home mortgages, re-financing, and second mortgages. Equally important is the amount of time required of the customer in these co-productive processes. Whether it is standing in the teller line, filling out a loan application, or coming to the branch for a loan closing, the demands placed on the customer must be measured and made as mutually beneficial as possible. Banks walk a fine line between the desire to increase contact with the customer to increase sales and the desire to decrease time with the customer in order to increase convenience to the customer (Parasuraman, Zeithaml & Berry 1990).

While clearly important, convenience is difficult to measure in that it is a value *perceived* by the customer which therefore depends upon the make-up of the customer base (Parasuraman, Zeithaml & Berry 1990). There are certain aspects of convenience which will be more or less important to different segments, and the success of an organization depends on how well it identifies and satisfies the appropriate measures of convenience.

2.7.2 Precision

While customers may make many choices based on convenience, they also expect quality in the delivery of financial services and products. Customers are increasingly willing and able to choose from a large number of investment and loan vehicles as banks compete with non-banks for depositors and investors. Quality may suggest a whole host of things to the customer. Examples include error free statements, checks printed correctly, and the

operational soundness of all delivery channels. Banks committed to quality and accuracy will anticipate problems and facilitate a pain free resolution process. In fact banks may require higher levels of precision than their non-bank competitors: one source of advantage over other kinds of organizations lies in the trust consumers place in banks to handle their assets effectively. Mistakes in this process may drive consumers to search for other financial providers. (Roth and velde, 1991).

The competitive environment faced by banks generates two sources of pressure for an error-free operation. First, consumers may be willing to pay a price premium for what they perceive to be responsiveness to their needs: accurate answers to their questions, useful advice about new products, error-free statements, etc. On the other hand, competitors quickly match prices in this market. Thus, even if the bank cannot extract a price premium, precision in operations may be a key contributor to retaining or gaining market share (Porter M.E, 1980). In one study by the Bank Administration Institute (1993), industry leaders in retail banking generally believed that other quality-related factors would be more important contributors to the bank's performance than the ability to exercise price leadership.

In addition to the quality provided to the customer, precision in the delivery of financial services and products enhances the performance of the bank by reducing "rework" in the system and hence, costs. Time spent correcting errors may be better spent generating revenue, thereby encouraging all institutions to be concerned about quality. The ability to make good business decisions also relies on the level of precision in the bank. First, the source information which forms the basis for any decision must be accurate. Second, the

institution must have the tools which enable the interpretation of the source information. For example, making good lending decisions requires accurate information from the consumer, a detailed understanding of the economic environment, and tools such as credit scoring models to facilitate the analysis process (Roth and Velde, 1991). While these decisions may occur without the benefit of sophisticated tools, the ability of the bank to increase precision slightly on an individual credit analysis might translate into systemic improvements.

2.7.3 Efficient Cost Structure

While precision and convenience may differentiate banks, the commodity nature of financial products suggests that any firm unable to manage its cost structure effectively is at a serious disadvantage. Our interviews and pilot survey show that driving down costs by doing more with less is one practice of high-performing banks and thus, banks which fail to seize opportunities to remove costs may be at a disadvantage. Thus, the goal is to maintain the appropriate cost structure relative to the business and revenue mix (Waylaid and Cole 1997).

It is precisely in this area where traditional measures of total factor productivity (Berger and Humphrey, 1992) might be considered. Many retail banks use intricate staffing models to control branch labor costs, and "back office" processing of transactions focuses around taking costs - particularly labor costs - out of these operations. In fact, technology spending in the industry often aims at breaking the link between an increase in business and an increase in costs. If a reduction of costs could occur in a vacuum, then every organization would try to push the traditional productivity levers. However, a comprehensive analysis

should consider the trade-offs between the various value indicators. Efforts to reduce costs might also reduce quality and long-term profitability. For example, if staffing models in bank branches accommodate only the time needed for simple teller transactions, the resulting tight staffing control may inhibit the teller's ability to engage the customer in cross-selling of other financial products. Similarly, if tellers rush as a result of tight staffing, the bank may experience a disastrous decrease in precision. Thus, we must be careful when analyzing costs not to lose sight of the interconnectedness of value indicators and profit implications of choices between these values (Berger, Hancock and Humphrey, 1993).

2.7.4 Adaptability

The first indication of an organization's adaptability is its willingness to meet the changing demands of the customer. This willingness may be evidenced by pricing flexibility. It also surfaces in the mass customization movement making its way through the service industry (Pine, 1993). Many customers have individual needs which are not easily satisfied by standard products and services. Not surprisingly then, the need to customize products and services underlies much of the recent IT investment of bank. In addition to responding to the customer, financial institutions display adaptability in their ability to respond to the marketplace. In competition with non-bank financial institutions, the bank's challenge is to create competitive products and introduce them to market before losing the chance to compete in the larger industry. The introduction of mutual funds is a perfect illustration. Given the opportunity to partake in the investment market, many banks have been slow to bring their funds effectively to the market. As change occurs, whether in the development of new products and services or the introduction of new technology, the institution must respond with changes in the business processes. Organizations and processes should be able to withstand and plan for change, as a lack of flexibility renders a firm unable to respond to changing business conditions (Roth and Velde , 1991).

2.8. Factors Affecting Choice of Retail Bank by Smes

2.8.1 Interest rates

The dynamics of short-term treasury interest rates are central to the pricing of all fixed income instruments and their derivatives. Chan, Karolyi, Longstaff and Sanders (1992), hereafter CKLS compared a variety of single factor continuous-time models of the short-term risk-less rate over the period 1964 through 1989. They found that models that allow the volatility of interest changes to be sensitive to the level of the risk-free rate outperform other models. Longstaff and Schwartz (1992) presented a two-factor general equilibrium model, with the level and conditional volatility of short-term rates as factors. They showed that a two-factor model carries additional information about the term structure and leads to better pricing and hedging performance compared to a single factor model, which only uses the level of the short rate.

The factors that affect short-term interest rates include: the monetary policy, the Government fiscal policy, taxation, inflation, and demand for capital, social values, and political trends. The monetary policy is used by the government to control the supply of money in the economy. When supply of money in the economy is low then the interest rates are expected to be high and vice versa. The volatility in money supply growth may lead to higher interest rates. Under the fiscal policy, the Government is supposed to finance all expenditure for the economy. In cases where expenditure exceeds revenue (budget deficit), the Government is forced to borrow from the local markets. This in turn affects the supply of money in the

economy which in turn affects the trend of interest rates. Inflation on the other hand causes long-term interest rates to rise where investors sell-off their bonds in fear of inflation eroding their capital gains. Demand for capital influences interest rates when the demand/supply of funds is below or above the equilibrium levels. If there are fewer borrowers and the demand for funds is low then the interest rates will be low and vice versa (Long R.H 1988).

In Kenya, the interest rates charged by banks are determined by: interest rate on deposits; cost of liquidity; cost of holding cash; and operational costs. The interest on deposits depends on the bank's cash ratio, its overall financial stability and the type of the bank for example whether it is a corporate bank or a network bank. The cost of liquidity covers both the cash, which is maintained by the banks with Central Bank as required cash ratio, and the cash maintained by the banks as the minimum amounts to meet unexpected demand from the customers. Cost of holding cash is derived from the cash held by the banks in form of liquid form to meet day-to-day customer's needs. The banks have to compare the costs of cash outs and the opportunity costs associated with the cash held in liquid form. Operational costs are mainly meant to cover the costs of running the bank and it includes capital costs, staff costs, and technology costs. The base rate charged by the banks takes into account all these factors. The bank can reduce the base rate by improving efficiency.

2.8.2 Service Quality

Bloemer and Ruyter (1998) suggested that store loyalty resulted from a consumer committed to the store through an explicit and extensive decision-making process. Customer loyalty is frequently operated as a conscious evaluation of the price/quality ratio or the willingness to pay a premium price, or alternatively price indifference (Raju, Srinivasan, & Lal, 1990; Zeithaml, Berry, & Parasuraman, 1996). Supphellen and Nysveen (2001) suggested that corporate brand loyalty affected online shoppers' intentions to revisit the Web site.

Cronin and Taylor (1992) examined the causal relationships among service quality, customer satisfaction, and purchase intention. Each variable was measured by one item. There were 660 usable questionnaires randomly collected from customers of four types of businesses in the southeastern United States: banking, pest control, dry cleaning, and fast food. The results of correlation analysis have suggested that, service quality was an antecedent of consumer satisfaction, service quality had less effect on purchase intentions than did consumer satisfaction, and consumer satisfaction had a significant effect on purchase intentions.

Dabholkar, et al (2000) also found that customer satisfaction strongly mediated the effect of service quality on behavioral intentions. The data used in their study were systematically randomly collected from 397 churches. A test of discriminant validity revealed that the construct of service quality was different from the construct of customer satisfaction. The result of regression analysis in structural equations modeling supported their proposition that

customer satisfaction had a stronger effect on behavioral intentions than service quality did (Dabholkar et al., 2000).

Service quality literature indicated that perceptions of high service quality and high service satisfaction resulted in a very high level of purchase intentions (Boulding, Kalra, Staelin, & Zeithaml, 1993). Coner and Gungor (2002) claimed that customer loyalty was affected by product quality, service quality, and retailer image. They also suggested "quality [of product and service] is directly related to customer satisfaction and lead to the loyalty of the customer" (Coner & Gungor, 2002, p. 195). Customer satisfaction literature showed that the relationship between customer satisfaction and customer loyalty depended on the type of satisfaction. The positive impact of manifest satisfaction on customer loyalty was stronger than that of latent satisfaction on customer loyalty (Bloemer & Kasper, 1995; Bloemer & Ruyter, 1998).

Based on empirical findings in service quality and satisfaction literature, service quality is one of the antecedents of satisfaction (Anderson & Sullivan, 1993; Cronin & Taylor, 1992, 1994; Reidenbach & Sandifer-Smallwood, 1990; Spreng & Mackoy, 1996; Woodside, Frey, & Daly, 1989), and loyalty is one of the consequences of satisfaction (Coner & Gungor, 2002; Cronin & Taylor, 1992, 1994; Dabholkar, Shepherd, & Thorpe, 2000). Luarn and Lin (2004) tested their hypothesized customer loyalty model and found that customer satisfaction, perceived value, and customer loyalty were different constructs. Their findings indicated that not only customer satisfaction and perceived value directly affected customer loyalty, but also indirectly affected customer loyalty through commitment.

2.8.3 Safety of deposits

Bank reserves are required for the safety of depositor's money. Many people have the idea that bank reserves provide for the safety of depositors' money. They don't. The statistics in the study indicate that the amount of demand deposits is several times larger than that of reserves (Nielsen, 1995). Reserves are for control of the money supply. The FDIC provides for safety of deposits by insuring them. Reserves are not principally for depositors' safety. Deposits of cash are necessary to start the process of lending and deposit creation. Many find it difficult to understand that for deposit creation to occur, the banking system needs only to acquire reserves from outside the system or be able to stretch existing reserves further. It may acquire reserves by selling a security to the Fed or by borrowing from the Fed. An individual bank, however, may acquire reserves from another bank. Therefore, to the extent that it has increased its reserves, reserves of another bank have shrunk. Thus, the system has no more reserves after the transaction than it had before and so the system's lending capacity is unchanged.

In their book, Morris and Kuratko, (2002) suggested that bank is responsible for deficiency in service for lack of security in its premises and loss caused to customers accordingly. This is on the ground that ensuring the safety of the money to be deposited and/or withdrawn inside the bank premises is implicitly a part of the service rendered by a bank to a customer. The failure of a bank to honour bank guarantee is a deficiency in service. However, in cases where a demand was made not in accordance with the conditions of the guarantee and therefore, the guarantee was not honoured, it would not amount to deficiency in service.

2.8.4 Proximity to the bank

Distance is a factor that has been heavily discussed in literature. Mainly because with ever advancing technological possibilities distance was losing its influence on trade or banking. Degryse and Ongena (2004) have proven that even though distance has diminished its influence over time it is still an important factor. Petersen and Rajan (2000) and Buch (2001) came to similar conclusions in their studies on the effect of distance on information costs in banking. Portes and Rey (2005) in their study of bilateral cross-border equity flows showed that distance is a big influence on the information cost component of trading costs and therefore could be an impending factor on choice of retail bank by SMEs. Anderson and Wincoop (2004) observed that distance formed a part of the high trade costs which persisted between economies even as highly integrated as those of the European Union. Agarwal and Hauswald (2007) showed that borrower proximity is an advantage for capturing markets. Even though their study was based on domestic competition for borrowers, it could mean that banks close to borders could find a market on the other side because of their proximity. Degryse and Ongena (2004) studied the impact of technology on the geographical scope of banking. Technology enables banks to capture bigger markets and venture abroad via choice of retail bank by SMEs. Others that looked at technology and international banking were for example Singer, Albert and Babu (2008) and Pfeffers and Tuunainen (2002).

Avait and Coerdacier (2007) show in their study that distance has a negative effect on foreign assets and holdings of banks which is in turn mostly due to the positive link between trade and international bank assets. Blank and Buch (2007) show in their work, that cross-border

activities are positively related to foreign trade. This means that countries that are trade partners with high volumes of trade are likely to see high volumes of choice of retail bank by SMEs as well. Bank and Buch (2007) did note here that their model could explain links better between non-banks and banks than between banks.

2.8.5 Country of incorporation of the bank

Tschoegl (2000) found that the presence of foreign banks enhances the competition and innovation in the bank market. This in turn benefits customers and could lead to total banking volumes domestic and internationally. In other words countries with high level of foreign bank penetration could show higher choice of retail bank by SMEs volumes.

Guiso, Sapienza and Zingales (2008) have shown that softer factors are also an important influence on international trade. They found that cultural perceptions are important determinants of economic exchange. From their study they concluded that lower bilateral trust leads to less trade between two countries. The effects are strongest for goods and services that are most trust intrusive. On financial trade similar conclusions were made. Buch, Driscoll and Ostergaard (2005) found that lending increases when countries are culturally more similar have less capital controls in place and improve their risk-conditions. They investigated cross-border assets portfolios of banks using proxies for capital control regulation, country risk and information costs. Ekinçi, Kalemli-Ozcan and Sorensen (2007) investigated the role of institutions, confidence and trust in financial integration. Their study concluded that countries are more integrated with each other where trust levels between the

countries are high. According to these studies countries with higher trust levels and more similar cultures between them, the cross-border trade and cross-border loan and deposit volumes should be higher.

Buch (2000) found that banks rely on the regulatory barriers in place in the country they work in. In her study she shows that the relative importance of this factor differs between countries. Buch states furthermore that: "In addition to regulations, information costs as proxied through distance, the presence of a common language, and a common legal system do have an impact on international investment decisions of banks."(Buch, 2000, Pp25) .With this statement Buch combines a number of factors that influence banks and their markets. Similar combination study was done by Sen (2007) who used a regression model, with variables like size, distance and common language to estimate the determinants of foreign direct investment flows. She found, via a pooled regression as well as random effects estimation, that apart from traditional macro-economic variables also other business environment variables are important determinants for capital flows.

Heuchemer, Kleimeier and Sander (2008) combined all of the above variables and more in a pooled regression model in order to find the best determinants of choice of retail bank by SMEs. They used several gravity models with economic, geographic, cultural and political proxies. These proxies were recalculated using Euklidian Distance, which measured the difference between the value of a customer and bank country. This recalculation was necessary to be increase the comparability. They selected the best regression model from three possible models, namely the Fixed effects model, the Arellano-Bond model and the

Least Square Dummy Variable model (LSDV).. Cultural differences and not belonging to the same legal family were proven to be impeding factors to the choice of retail bank by SMEs volumes. Heuchemer et al. (2008) found furthermore that distance and borders still matter in choice of retail bank by SMEs. The methodology and variables used by Heuchemer et al. (2008) will form the basis for my study. The dataset available for this study is different to the one used by them which will make it a new and innovating exercise.

Indicators of choice of retail banking

Branch of choice

Various business operators tend to have their preferred branch of the bank. This is due to the unique feature in that particular branch which varies with their need. This may include the customized services offered to them, minimal time spent conducting transactions, confidentiality offered to the customers. All these reasons make an entrepreneur prefer a certain branch of a given bank for other even they are near his business premises.

Types of services

There are various services and products offered in a given bank. They include cheques services, trade facilities, mobile banking services, internet banking services, credit/debit card services, current and saving facilities, business clubs, checking business transactions, and ATM services among others. When approaching a given bank, SMEs usually consider the type of service that they need and usually go for the bank offering their desired services. Owing to their specific services requirements, entrepreneurs should be keen to search for their right bank to avoid the need to change the bank which is an expensive.

Size of business

Choosing a corporate bank account is an important financial decision for any SME. Bank accounts for businesses are typically savings accounts used for revenues and checking accounts used for operating expenses, accounts payable and payroll. Before SMEs begin

looking for a corporate bank account, they should determine what they require which may include savings, checking or both. When researching banks for the business account, SMEs should consider the requirements for applying for the account, which range from the size of SME, interest rates, and additional fees. Also, the bank's size, reputation and support for your size of business can be important considerations when selecting the appropriate retail bank account. For SMEs and growing businesses, special programs with incentives for opening accounts can be a very attractive option that some banks offers. One the most important considerations when choosing a corporate bank account may be the requirements for obtaining the account. Requirements typically vary depending upon the size of SMEs, the business locale, but generally include documents for proof of business, proof of identity, an official company seal and corporate resolutions, all of which are the indicator of the SMEs.

Sometimes banks also require a registered government business number. The proof of business for most corporations is the Article of incorporation or Article of Organization if the business is a partnership or proprietorship.

The size of the bank may be important because it can affect the level of customer support and extra services offered by the bank. Smaller banks typically have basic services for their customers and often are not able to provide the support for a SMEs or growing company. Conversely, larger banks with good, solid reputations in the industry generally have more range and flexibility in their financial products and services.

Also, the entrepreneurs consider banks that have special programs for certain types of businesses such as SMEs. To motivate customers to sign-up for or upgrade accounts, banks might give incentives such as higher interest rates for savings accounts or additional fee waivers. These types of deals are typically be made available during special promotional times.

Credit facilities

When SMEs want to expand, they really have no option but to use a bank who provide the with a full range of credit options. Banks have been willing to accommodate the credit needs of SMEs. The entrepreneurs usually evaluate banks on the basis of whether they support their credit needs and on whether it supports their application for credit. Banks need to be flexible in the structure of loans and tailor finance to the needs of the situations of the SMEs. Financing decisions should be made quickly and not drawn out, while collateral requirements need to be realistic and not over the top.

2.9 Conceptual Framework.

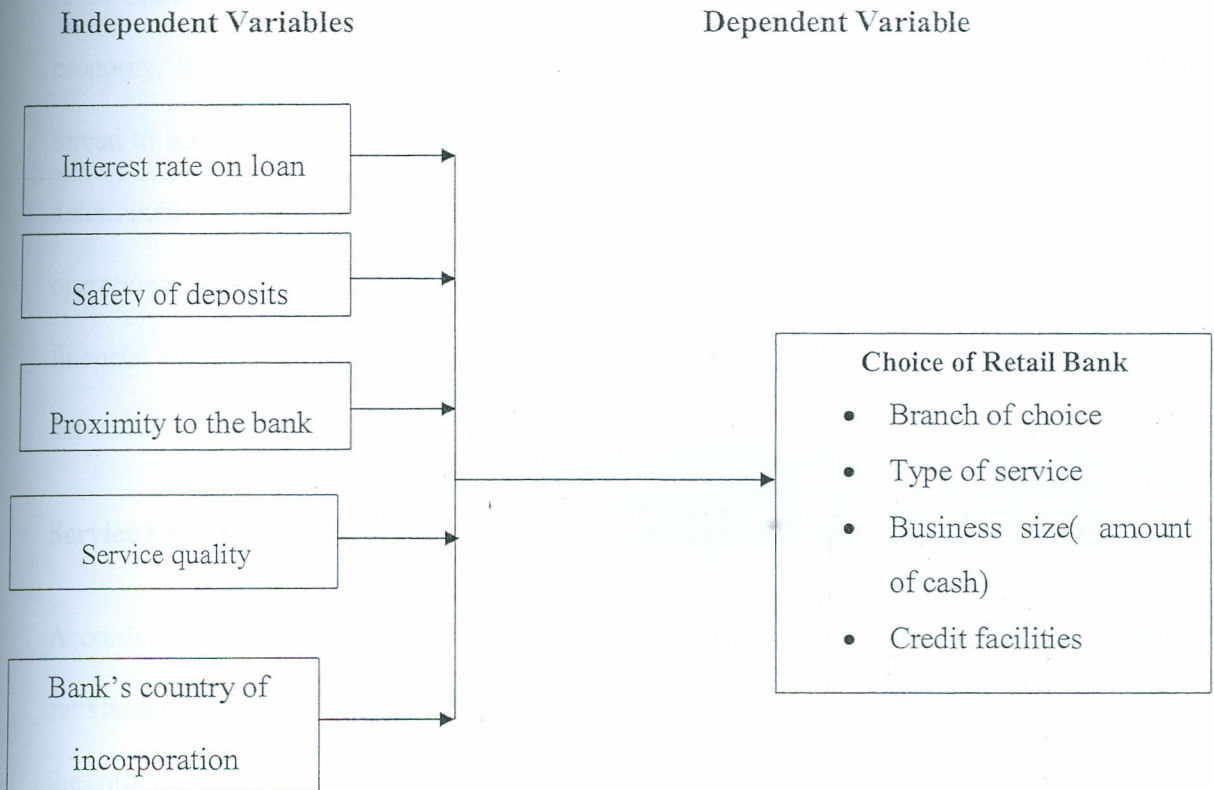


Figure 2.1 Conceptual framework

Source: (Author, 2011)

Interest rates

The factors that affect short-term interest rates include: the monetary policy, the Government fiscal policy, taxation, inflation, and demand for capital, social values, and political trends. The monetary policy is used by the government to control the supply of money in the economy. When supply of money in the economy is low then the interest rates are expected

to be high and vice versa. The volatility in money supply growth may lead to higher interest rates. Under the fiscal policy, the Government is supposed to finance all expenditure for the economy. In cases where expenditure exceeds revenue (budget deficit), the Government is forced to borrow from the local markets. In Kenya, the interest rates charged by banks are determined by: interest rate on deposits; cost of liquidity; cost of holding cash; and operational costs. The interest on deposits depends on the bank's cash ratio, its overall financial stability and the type of the bank for example whether it is a corporate bank or a network bank.

Service Quality

According to Dabholkar, et al (2000), service quality is an antecedent of consumer satisfaction and it had less effect on purchase intentions than did consumer satisfaction. On the other hand, consumer satisfaction had a significant effect on purchase intentions. Customer satisfaction strongly mediated the effect of service quality on behavioral intentions. The data used in their study were systematically randomly collected from 397 churches. A test of discriminant validity revealed that the construct of service quality was different from the construct of customer satisfaction. Based on empirical findings in service quality and satisfaction literature, service quality is one of the antecedents of satisfaction, loyalty is one of the consequences of satisfaction. Customer loyalty model found that customer satisfaction, perceived value, and customer loyalty were different constructs. Their findings indicated that not only customer satisfaction and perceived value directly affected customer loyalty, but also indirectly affected customer loyalty through commitment.

Safety of deposits

Bank reserves are required for the safety of depositor's money. Many people have the idea that bank reserves provide for the safety of depositors' money. Study indicates that the amount of demand deposits is several times larger than that of reserves. Reserves are for control of the money supply. Deposits of cash are necessary to start the process of lending and deposit creation. Many find it difficult to understand that for deposit creation to occur, the banking system needs only to acquire reserves from outside the system or be able to stretch existing reserves further. Banks are responsible for deficiency in service for lack of security in its premises and loss caused to customers accordingly. This is on the ground that ensuring the safety of the money to be deposited and/or withdrawn inside the bank premises is implicitly a part of the service rendered by a bank to a customer. The failure of a bank to honour bank guarantee is a deficiency in service. However, in cases where a demand was made not in accordance with the conditions of the guarantee and therefore, the guarantee was not honoured, it would not amount to deficiency in service (Morris and Kuratko, 2002).

Proximity to the bank

Distance is a factor that has been heavily discussed in literature. Mainly because with ever advancing technological possibilities distance was losing its influence on trade or banking. In a study of bilateral cross-border equity flows showed that distance is a big influence on the information cost component of trading costs and therefore could be an impending factor on choice of retail bank by SMEs (Portes and Rey 2005).

Country of incorporation of the bank

Presence of foreign banks enhances the competition and innovation in the bank market. This in turn benefits customers and could lead to total banking volumes domestic and internationally. In other words countries with high level of foreign bank penetration could show higher choice of retail bank by SMEs volumes (Tschoegl, 2000). Banks rely on the regulatory barriers in place in the country they work in. The relative importance of this factor differs between countries. In addition to regulations, information costs as proxied through distance, the presence of a common language, and a common legal system do have an impact on international investment decisions of banks (Buch, 2000).

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter describes the methodology that was adopted for the study. It describes the research design, the population, sampling design, data collection method and data analysis methods. Bless and Achola (1988), defines research methodology as a tool that guides the researcher in collecting, analyzing and interpreting observed facts. There are several research designs ranging from exploratory studies, descriptive studies, explanatory studies within each of this design are strategies that can be applied such as survey and case study. Descriptive research portrays an accurate profile of persons; events or situations surveys allow the collection of large amount of data from a sizeable population in highly economical way. It allows one to collect quantitative data which can be analyzed quantitatively using descriptive and inferential statistics (Barbie, 1995). Surveys are concerned with describing recording, analyzing and interpreting conditions that either exist or existed. In the research methodology the following aspects of acquiring and presenting data are to be considered; the research design, population and sample size, sampling techniques, data collection instruments, data analysis, and data analysis. It also shows the method of data presentation and the scope of the data.

3.2 Research Design

According to McMillan and Schumacher (2001) a research design is a plan for selecting subjects, research sites and data collection procedures to answer the research questions. A research design is the arrangement of conditions for collection and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure, (Seltiz, 1963). It is the conceptual structure within which research is conducted; it constitutes the blueprint for the collection and data analysis. All these do assist the investigator in answering the research questions formulated (M'Mwari, 1999). The design shows which individuals will be studied, when and where and under which circumstances they will be studied. In this research paper, qualitative and qualitative approach was adopted. It is viewed that this method is tenable as the study focused on assessing the factors considered by the SMEs entrepreneur in the choice of a suitable retail bank.

3.3 Target Population

Population refers to an entire group of individuals which are the concern for the study within the area of the study (Mugenda and Mugenda, 1999). According to Somer, (1986), "sample" refers to the students and teachers selected for the study. This is because it is seldom necessary to obtain data from all people within a population frame (Charles, 1988). Target population in statistics is also the specific population about which information is desired. According to Ngechu (2004), a population is a well defined or set of people, services, elements, events, group of things or households that are being investigated. This definition

ensures that population of interest is homogeneous. And by population the researcher means complete census of the sampling frames. Population studies also called census are more representative because everyone has equal chance to be included in the final sample that is drawn according to Mugenda and Mugenda (1999). The target population of this study was all the private schools in Nairobi County. The population frame constituted of 300 private schools in different constituencies that comprise of whole of Nairobi County.

Table 3.1 Population frame

Constituency	No. of schools	Sample size
Makadara	56	17
Kasarani	44	13
Westlands	51	15
Kamukunji	49	15
Embakasi	48	15
Dagoreti	52	15
Total	300	180

Source: PEO Nairobi Province

3.4 Sampling techniques and Sample Size

The research used purposive sampling to identify the private schools in Nairobi. From the above population of three hundred schools, a sample of 30% was considered for the study

which comprised 90 schools. The study only considered two respondents from each institution. This included one top management personnel working in the finance departments and the school principal owing to their knowledge on the schools' operation. The study area was stratified in to the six respective constituencies which includes Makadara, Embakasi, Kasarani, Kamukunji, Dagoreti and Westlands.

Table 3.2 sampling frame

Constituency	No. of schools	No. of respondents	Sample size
Makadara	17	2	34
Kasarani	13	2	26
Westlands	15	2	30
Kamukunji	15	2	30
Embakasi	15	2	30
Dagoreti	15	2	30
Total	90		180

Source: Researcher, 2011

3.4.1 Sample Techniques

The sampling plan describes how the sampling unit, sampling frame, sampling procedures and the sample size for the study. The sampling frame describes the list of all population units from which the sample was selected (Cooper and Schindler, 2003). The study gave

every element in the target population equal opportunity to become a respondent. This technique ensured that bias was not introduced regarding who is included in the census (Kothari, 2005). The study sampled 90 private schools in Nairobi County.

3.5 Data collection method

Data was collected from primary sources through a semi-structured questionnaire, administered to the respondents who are the top management personnel from various Small and Medium-Sized Enterprises in the Nairobi Region, Kenya. The questionnaire consisted of both closed and open questions. The researcher enhanced response to the questionnaires by conducting direct interviews. Secondary data was obtained to reinforce the primary data. The questionnaires were issued first on a pilot project basis. Modifications to the questionnaire document were then effected and then the document issued out to the respondents. The respondents filled the questionnaire under the guidance of the researcher/or research assistant.

3.6 Data Collection Instruments

Instruments are developed to collect the necessary information (Mugenda and Mugenda, 1999). In this case, the instruments considered for the study are: questionnaires, interview schedules, library research and observation. Questionnaire is one of the major research instruments for the study. Questionnaires contain printed questions to which informants reply in writing (Charles, 1988), The research involves the collection of constructs. These are non observable inferences from observed behaviour. The counseling skills, core values

conditions, views involve in counseling and therapeutic climate are all constructs. Rating scales, quite suitable for measuring the constructs (Kothari, 2001). Documents relevant to the research were examined and these include books, magazines and periodicals as well as published and unpublished research work from Kenyatta University, the University of Nairobi library, other learning institutions and other published excerpts. This was useful in order to provide secondary data that supported the primary data.

3.7 Data analysis

The data was summarized and presented using descriptive statistics of mean and standard deviation. Factor analysis was used to extract the set of factors that affect the choice of banks according to responses from the respondents. Correlation analysis was used to show the relationship among the extracted variables.

CHAPTER FOUR

DATA ANALYSIS, INTERPRETATION AND PRESENTATION

4.1 Introduction

This chapter presents analysis and findings of the study as set out in the research methodology. The results were presented on the factors affecting choice of retail bank by SMEs in the education sector in Kenya with special reference to private schools in Nairobi County. The study targeted a total of 180 respondents out of which 150 responded and returned their questionnaires contributing to 83.3% response rate. This response rate was excellent and representative and conforms to Mugenda and Mugenda (1999) stipulation that a response rate of 50% is adequate for analysis and reporting; a rate of 60% is good and a response rate of 70% and over is excellent. This commendable response rate was due to extra efforts that were made via personal calls and visits to remind the respondent to fill-in and return the questionnaires. The chapter covers the demographic information, and the findings are based on the objectives.

4.2 Demographic Information

4.2.1 Gender composition

The study sought to establish the respondents' gender. From the findings, the study established that the majority of respondents were males as shown by 52.7%, while females

were 47.3%. This means that the choice of retail bank is affected by demographic characteristics like gender as the study had both male and female respondents.

Table 4.3 Gender of the respondents

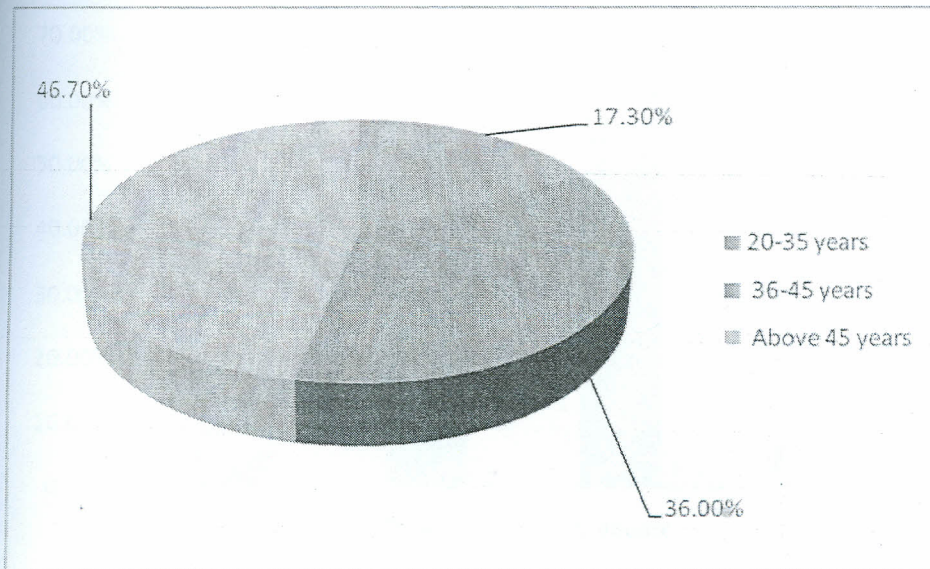
	Frequency	Percent
Male	79	52.7
Female	71	47.3
Total	150	100.0

Source: Research Data

4.2.2 Age of the Respondents

The respondents were also asked to state their age bracket. On the age of the respondents, the study found that most of the respondents (46.7%) were between above 45 years, 36.0% were aged between 36-45 years while a small proportion of respondents as indicated by 17.3% were between 20-35 years old. This shows that the respondents were well distributed in terms of age and could therefore give reliable information on factors affecting the choice of retail bank by SMEs as different generations are affected by the various factors differently.

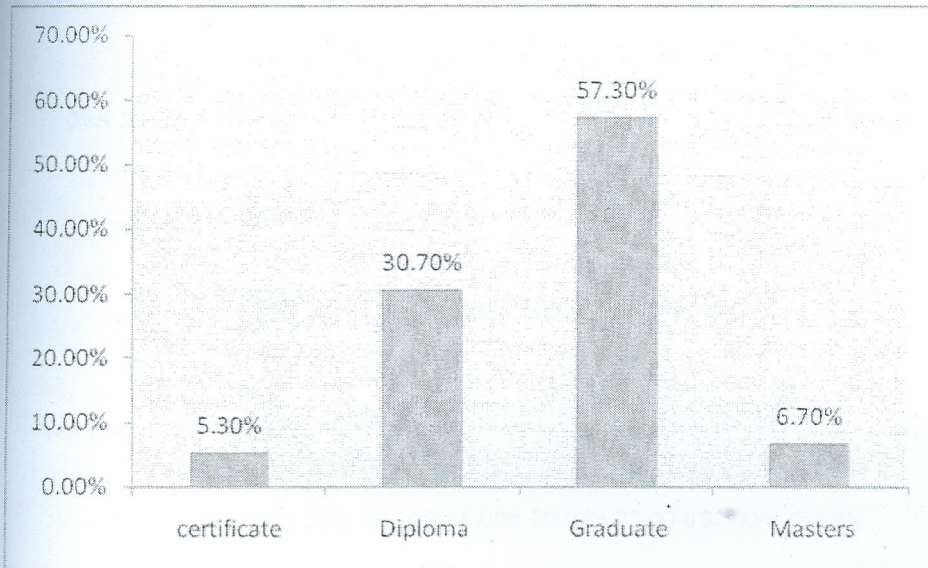
Figure 4.2: Age bracket of the respondents



4.2.3 Level of Education

The study also sought to establish the highest level of education of the respondents. According to the findings, the majority of respondents were graduates as shown by 57.3% of the respondents, 30.7% had a diploma education, 6.7% had masters while a small proportion of respondents as indicated by 5.3% had a certificate as their highest level of education. This information shows that the respondents were knowledgeable enough and could give valid and reliable information based on their high level of understanding of various financial issues.

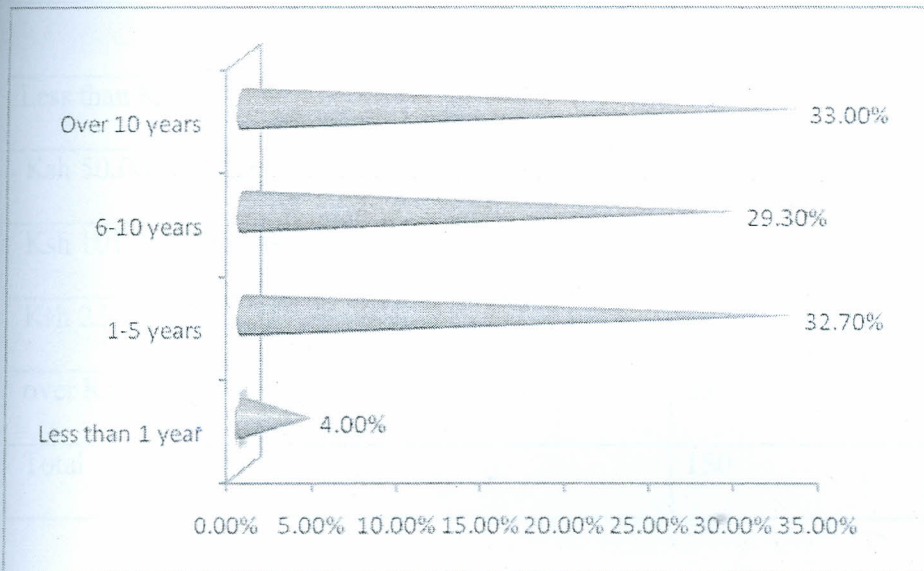
Figure 4.3: Highest level of education



4.2.4 Number of years the respondent had operated the business

The respondents were asked to state the duration years they had operated the business. The response tabulated below show that most of the respondents (33%) had operated the business for over 10 years, 32.7% for 1-5 years, 29.3% for 6-10 years, while 4.0% had operated it for less than 1 year. This shows that majority of the respondents had enough experience with the management of schools' financial resources to give credible information with regard to factors affecting choice of retail banks by the institution.

Figure 4.4 Number of years the respondent had operated the business



4.2.5 Average sales turnover of the organization

The study also sought to establish the financial performance of the institution by inquiring on their average sales turnover. From the findings 24.0% of the respondents indicated that their organization's average sales turnover was Ksh 50,000 -100,000, 22% rated it to be over Ksh 500,000, while 20.7% said that it was Ksh 250,001-500,000. This illustrates that majority of the institutions had a sound financial base which dictated the choice of retail bank.

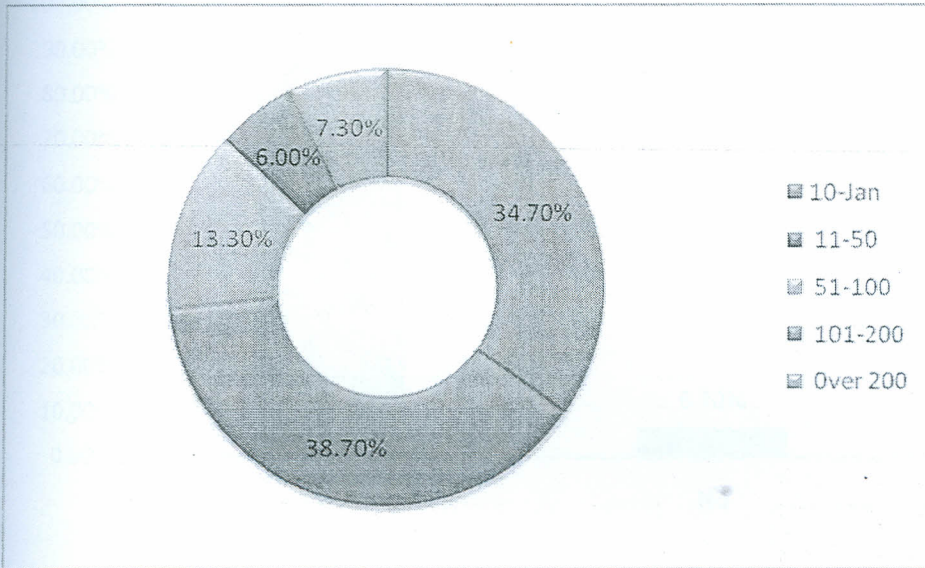
Table 4.4 Average sales turnover of the organization

	Frequency	Percent
Less than Ksh 50,000	24	16.0%
Ksh 50,000 -100,000	36	24.0%
Ksh 101,001-250,000	26	17.3%
Ksh 250,001-500,000	31	20.7%
over Ksh 500,000	33	22.0%
Total	150	100.0%

4.2.6 Number of employees

The respondents were asked to indicate the number of employees that their school had. From the study findings, 38.7% of the SMEs had 11-50 employees, 34.7% had 1-10 employees, 13.3% had 51-100 while 7.3% had Over 200 employees.

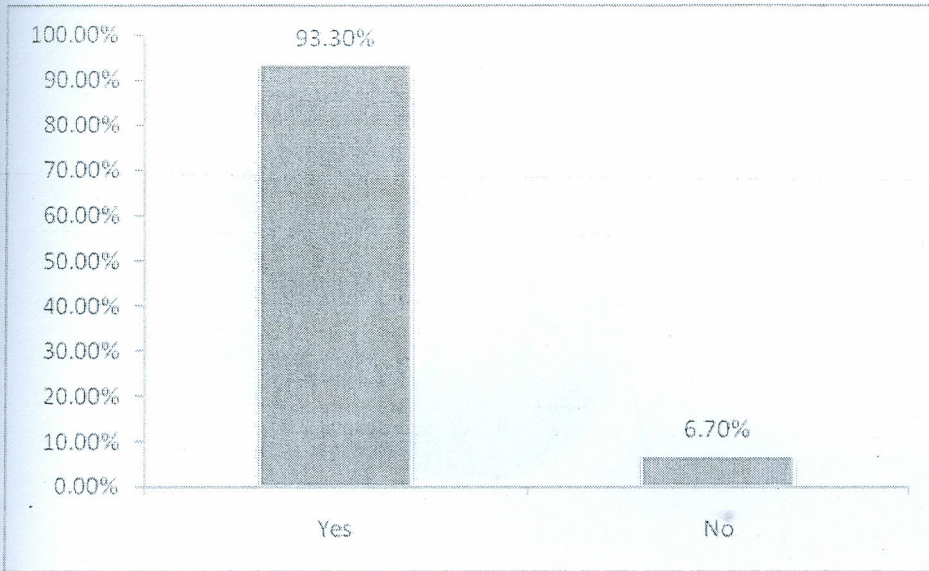
Figure 4.5 Number of employees



4.2.7 Whether the school operates a bank account/(s)

The respondents were also requested to indicate whether their respective institutions had a bank account with one of the retail banks. From the results of the study, the majority of the respondents 93.3% had a bank account while only 6.7% did not have a bank account. This depicts that majority of then SMEs in Kenya rely on banks to fulfill their financial needs.

Figure 4.6 Whether the school operates a bank account/(s)

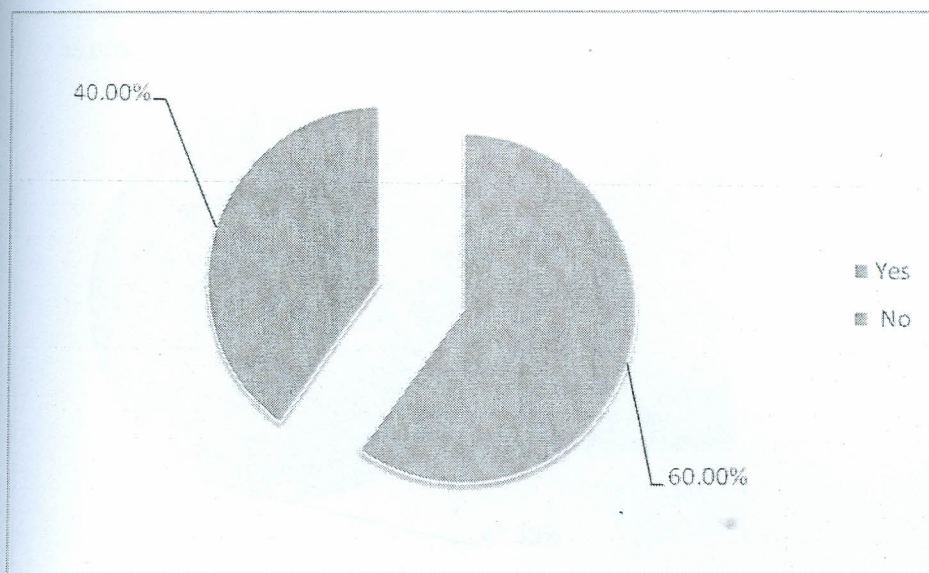


4.3 Influence of Interest rate charged on loan and service on choice of retail bank

4.3.1 Whether the school has taken a business loan

The study also wanted to establish whether the institutions took loans from their preferred banks to finance their operations. From the study findings, majority of the respondents (60%) reported that their organizations had taken a business loan to fund the school operations while 40% of the organizations had not taken a loan. This point to the fact that SMEs depend on banks to finance their operations through borrowing credit thus interest rate on loan is a key determinant of the choice of retail bank by the SMEs.

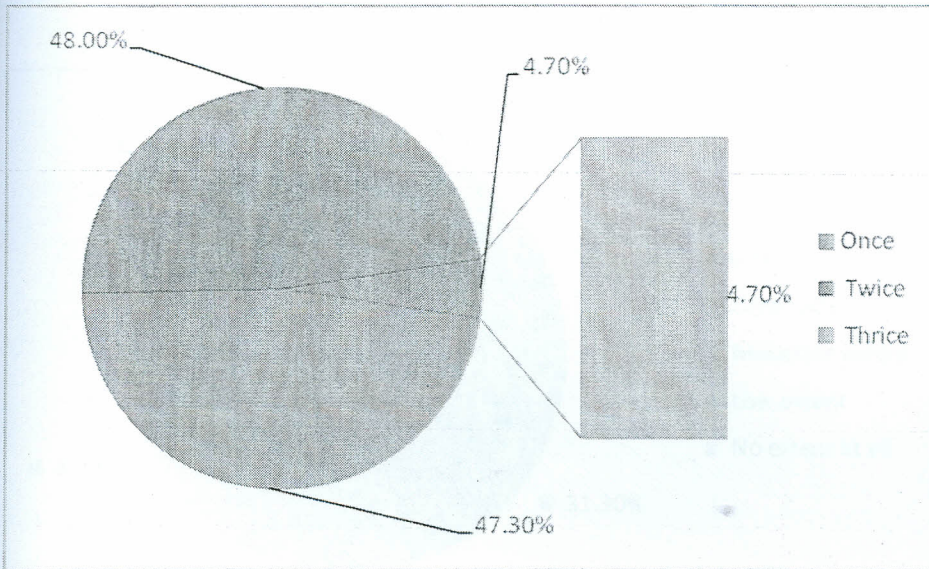
Figure 4.7 Whether the school has taken a business loan



4.3.2 Number of times the school has taken a loan

The study also required the respondents to indicate the number of times that the school had taken a loan to fund its operation. According to the responses given, most of the respondents (48%) reported that they had borrowed a loan twice, 47.3% for once while only 4.7% had borrowed loan three times.

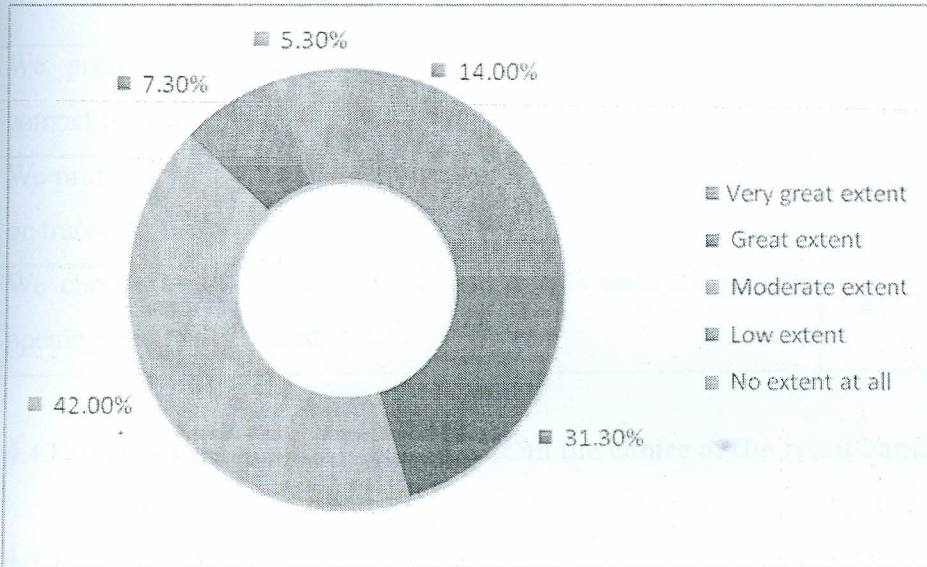
Figure 4.8 Number of times the school has taken a loan



4.3.3 Extent to which interest rates on loans influence the choice of the lending bank

The study also wanted to establish the extent to which the interest on loan influenced the choice of the lending bank by the SMEs. According to the study, most of the respondents (42%) were of the opinion that the interest on loan influenced the choice of the lending bank to a moderate extent, 31.3% to great extent, 14% to a very great extent while 7.3% indicated that the interest on loan influenced the choice of the lending bank to a low extent. This depicts that interest on loan is a major factor that influence the choice of retail bank as different banks offers different interest rates on loans to their clients.

Figure 4.9 Extent to which interest rates on loans influence the choice of the lending bank



4.3.4 Influence of the interest rate on the choice of retail bank

The study sought to establish the influence of the interest rate on the choice of retail bank by the SMEs. According to the findings, customers preferred their respective bank because it offers competitive interest rate level as shown by a mean of 3.54. Other reasons were that they choose their bank because it offers them incentives when opening business account as shown by a mean score of 3.45. The least significant reason for their choice of banks was that they preferred their bank because it does not charge additional costs on transactions made as shown by mean of 2.71.

Table 4.5 Influence of the interest rate on the choice of retail bank

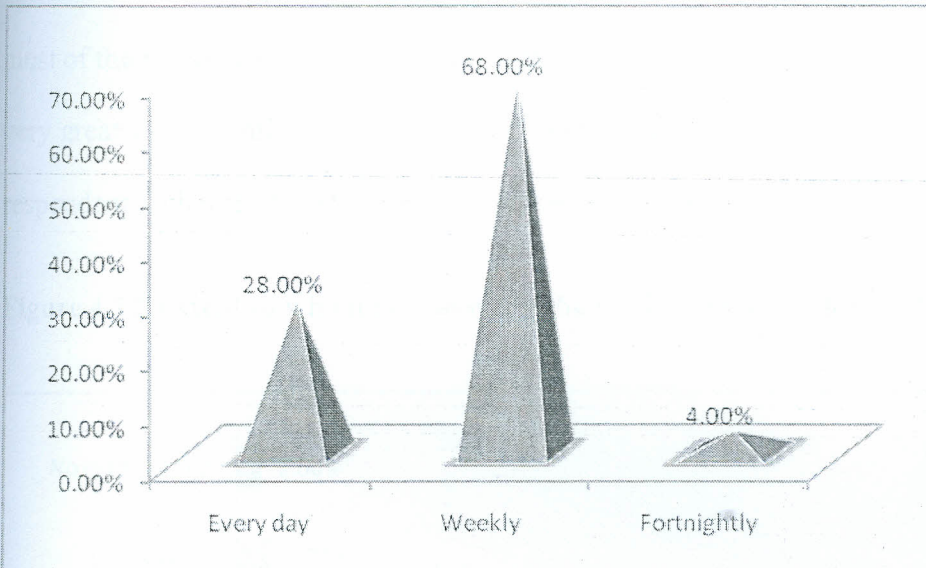
	Mean	Std. Deviation
We prefer this bank because it offers interest rates at competitive rates	3.5400	0.72009
We prefer this bank because it does not charge additional costs on transactions made	2.7133	0.96472
We choose this bank because it offers us incentives when opening business account	3.4467	0.95212

4.4 Effect of the proximity to the bank on the choice of the retail bank by the SMEs

4.4.1 Visit to the preferred bank

The study also inquired on the number of times that the respondents visited their preferred bank. From the results of the study, the majority of respondents as shown by 68% visited their banks weekly, 28% daily while 4% visited their preferred banks fortnightly. Owing to the numerous times that the majority of the respondents sought the services of banks, the proximity of the bank is thus a determinant of the choice of retail bank.

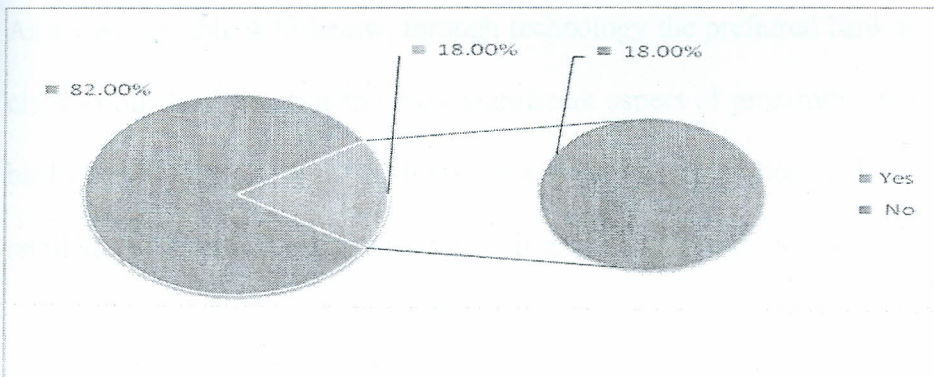
Figure 4.10 Visit to the preferred bank



4.4.2 Whether the preferred bank(s) is near the location of the business

According to the findings in the below, the majority of respondents (82%) indicated that their preferred bank(s) was near the location of their business. This reaffirmed that the proximity of the bank is a major factor influencing the choice of retail bank by the SMEs.

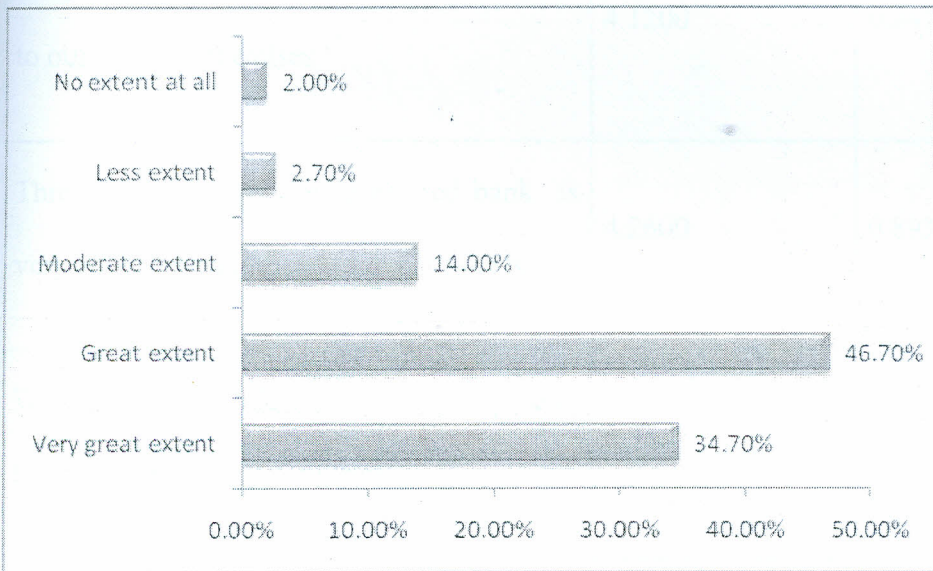
Figure 4.11 Whether the preferred bank(s) is near the location of the business



4.4.3 Extent to which proximity to the bank influence choice of a retail bank

On the extent that the proximity to the bank influenced respondents' choice of a retail bank, most of the respondents (46.7%) reported that it influenced them to a great extent, 34.7% to a very great extent while 14.0% of the respondents said that proximity to the bank influenced respondents' choice of a retail bank to a moderate extent.

Figure 4.12 Extent to which proximity to the bank influences choice of a retail bank



4.4.4 Influence of proximity to the bank on choice of the retail bank

As shown in table 4.13 below, through technology the preferred bank is very accessible and close to our business was the most significant aspect of proximity of bank to the choice of banks by the entrepreneurs as shown by a mean of 4.26. Others included that they prefer the retail bank because it is close to our business premises and that they preferred local banks to

foreign ones due to their proximity to the enterprise as shown by means of 4.12 and 3.39 respectively.

Figure 4.13 Influence of proximity to the bank on choice of the retail bank

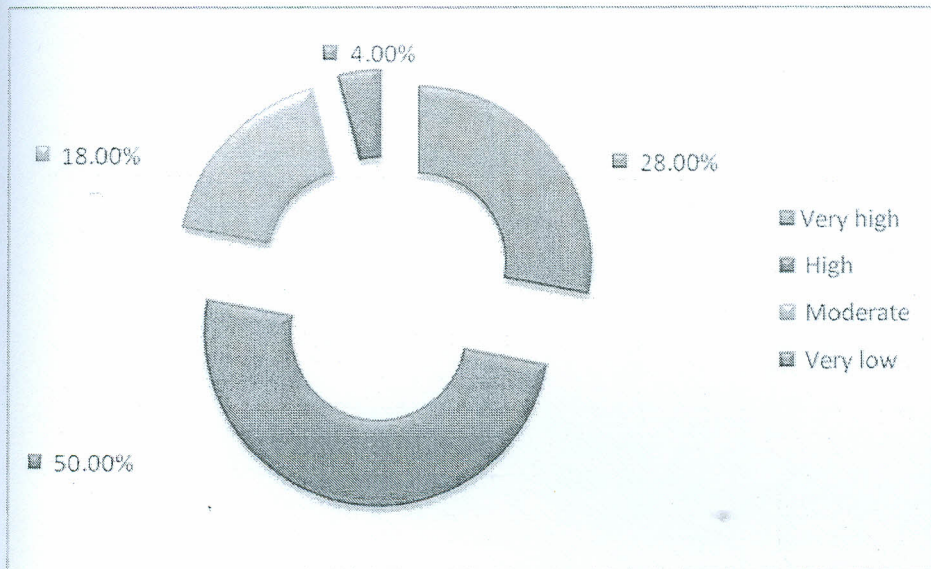
	Mean	Std. Deviation
We prefer this retail bank because it is close to our business premises	4.1200	0.94776
Through technology the preferred bank is very accessible and close to our business	4.2600	0.89315
We prefer local banks to foreign ones due to their proximity to our enterprise.	3.3867	1.20283

4.5 Effect of service quality on the choice of a retail bank

4.5.1 Rating of service quality in the preferred bank

The researcher sought to establish the service quality offered in banks. As shown in figure 4.14 majority of the respondents rated the service quality offered in their preferred banks as high, 28% as very high while 18% rated it as moderate.

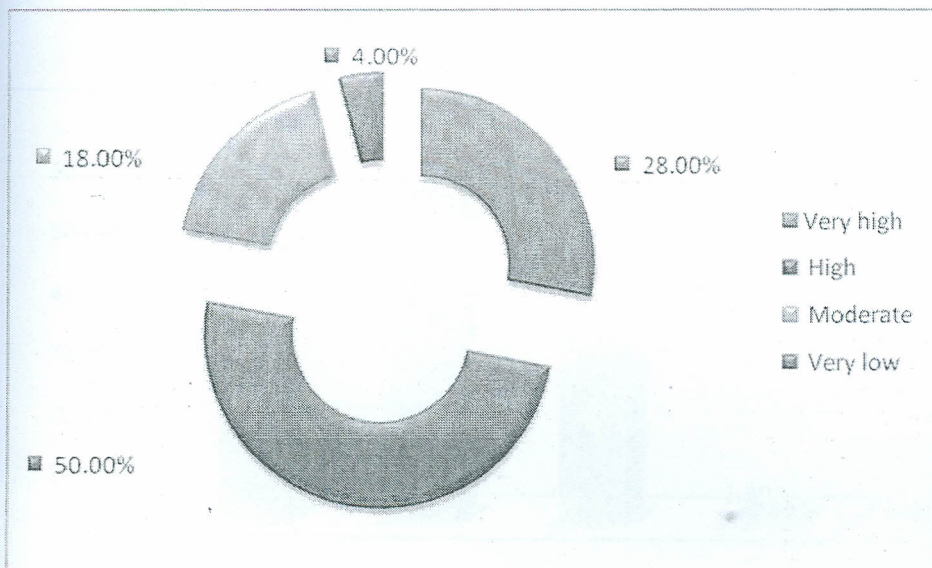
Figure 4.14 Rating of service quality in the preferred bank



4.5.2 Extent of satisfaction with the services offered by customer care representatives in the preferred bank

As shown in figure 4.15 majority of the respondents (53.3%) indicated that they were satisfied by the services offered by customer care representatives in their preferred bank to a great extent, 26% to a moderate extent while 19.3% were satisfied to a very great extent.

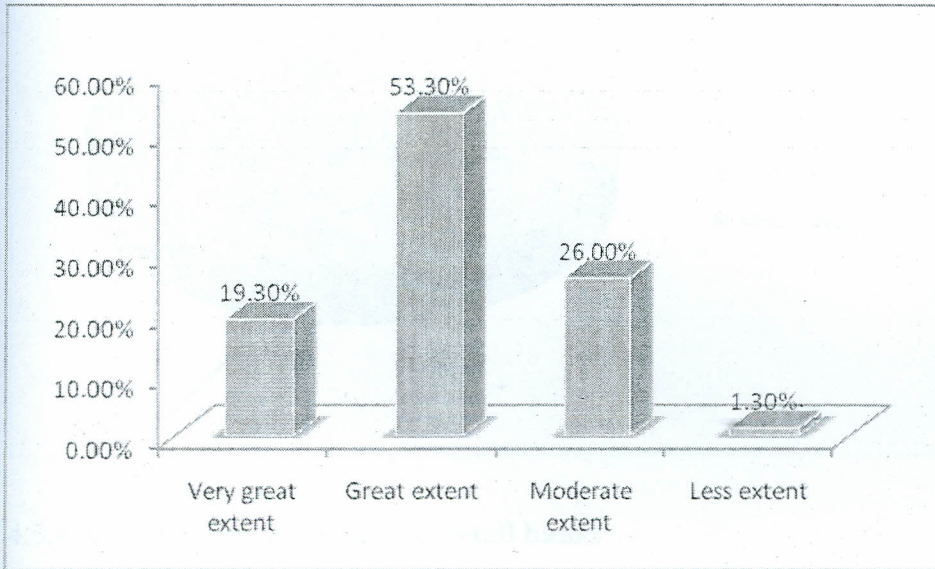
Figure 4.14 Rating of service quality in the preferred bank



4.5.2 Extent of satisfaction with the services offered by customer care representatives in the preferred bank

As shown in figure 4.15 majority of the respondents (53.3%) indicated that they were satisfied by the services offered by customer care representatives in their preferred bank to a great extent, 26% to a moderate extent while 19.3% were satisfied to a very great extent.

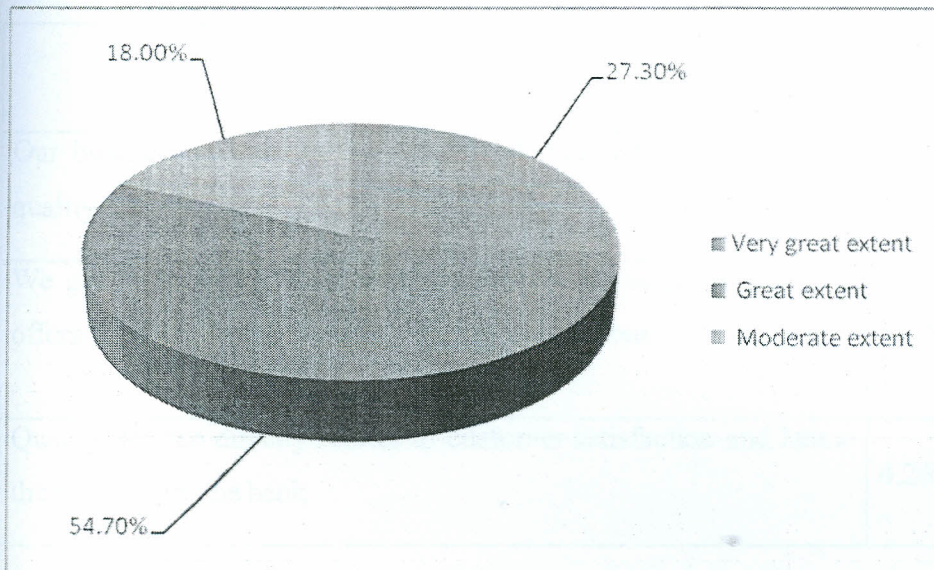
Figure 4.15 Extent of satisfaction with the services offered by customer care representatives in the preferred bank



4.5.3 Extent to which quality of customer service influence choice of the bank

The study sought to find out the extent to which the quality of customer service influenced SMEs choice of the bank. The researcher revealed that the quality of customer service influenced SMEs choice of the bank to a great extent as indicated by the majority of the respondents (54.7%). On the other hand 27.3% indicated that the quality of customer service influenced SMEs choice of the bank to a very great extent while only 18% of the respondents agreed to a moderate extent.

Figure 4.16 Extent to which quality of customer service influences choice of the bank



4.5.4 Aspect of service quality in retail banks

The researcher further sought to find out how various aspects of service quality affected the choice of retail bank by the SMEs. According to the findings, quality service directly relates to customer satisfaction and hence their loyalty to the bank to a great extent as shown by a mean of 4.26. Other aspects were that the clients get high level of customer satisfaction as their preferred bank offers them high service quality during transactions and that the entrepreneurs are loyal to the retail bank because they offer high quality services as shown by means of 4.04 and 4.03 respectively.

Table 4.6 Aspect of service quality in retail banks

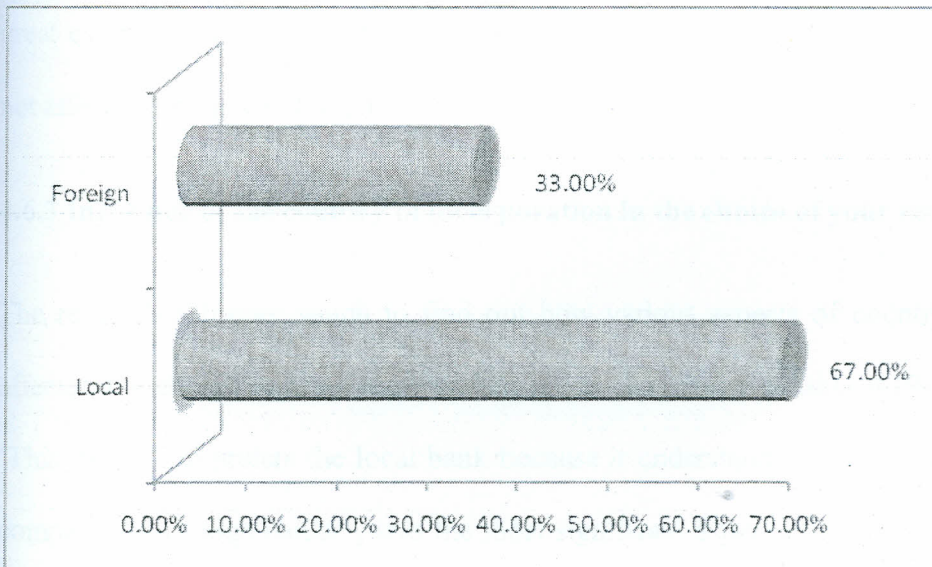
	Mean	Std. Deviation
Our business is loyal to the retail bank because they offer high quality services	4.0333	0.78933
We get high level of customer satisfaction as our preferred bank offers to us high service quality during transactions	4.0400	0.79326
Quality service directly relates to customer satisfaction and hence their loyalty to the bank	4.2600	0.91542

4.6 Effect of Country of Incorporation on the choice of retail bank by the SMEs

4.6.1 Country of Incorporation of the Banks

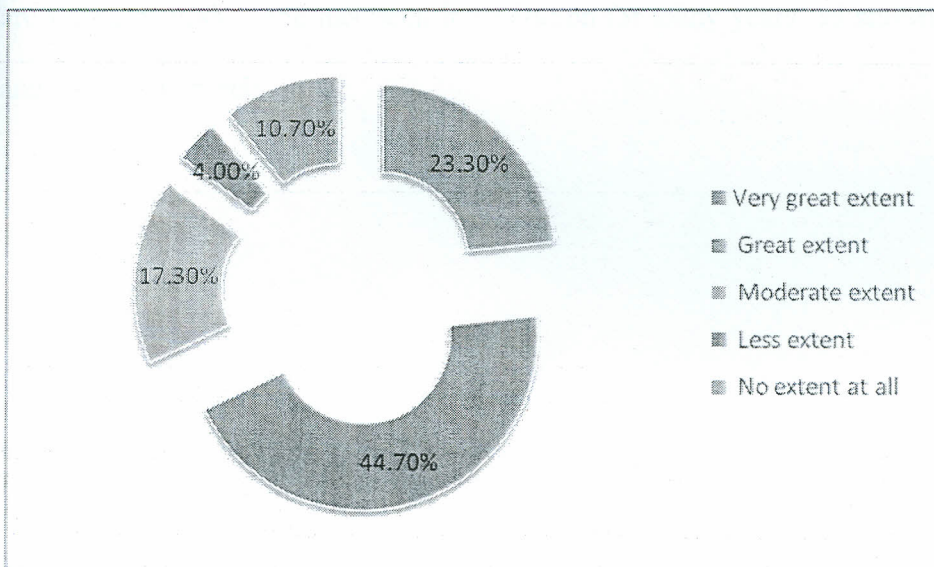
To evaluate the effect of country of incorporation on the choice of bank by SMEs, the study requested the respondents to state the nature of their preferred bank. As shown in figure 4.17, majority of the respondents (66%) posited that they banked with local financial institutions while 40% banked with foreign banks. As disclosed by the respondents, this is owing to the fact that local banks had a better understanding on the needs of the SMEs and helped growth of the local economy as compared to foreign banks whose profits benefits their mother countries.

Figure 4.17 Country of Incorporation of the Banks



4.6.2 Extent to which country of incorporation of the bank affect the choice of the bank

Figure 4.18 Extent to which banks' country of incorporation of affect the choice of bank



According to the findings, most of the respondents (44.7%) concurred that the country of incorporation of the bank affected the choice of the bank to a great extent, 234.3% to a very great extent, 17.3% to a moderate extent while 10.7% said the country of incorporation did not affect their choice of retail bank.

4.6.3 Influence of the country of incorporation in the choice of your retail bank

The researcher further sought to find out how various aspects of country of incorporation affected the choice of retail bank by the SMEs. As shown in table 4.19, the statement that 'This institution prefers the local bank because it understands the needs of its customers as compared to foreign banks', was the most significant aspect of country of incorporation as shown by a mean of 3.40. Other statements on how the country of incorporation affected the choice of retail bank by the SMEs were 'We prefer foreign banks because they enhance competition and innovation in the bank market' and 'We prefer foreign bank because they are well established and has been in operation for many years' as shown by means of 3.30 and 3.26 respectively.

Table 4.7 Influence of the country of incorporation in the choice of your retail bank

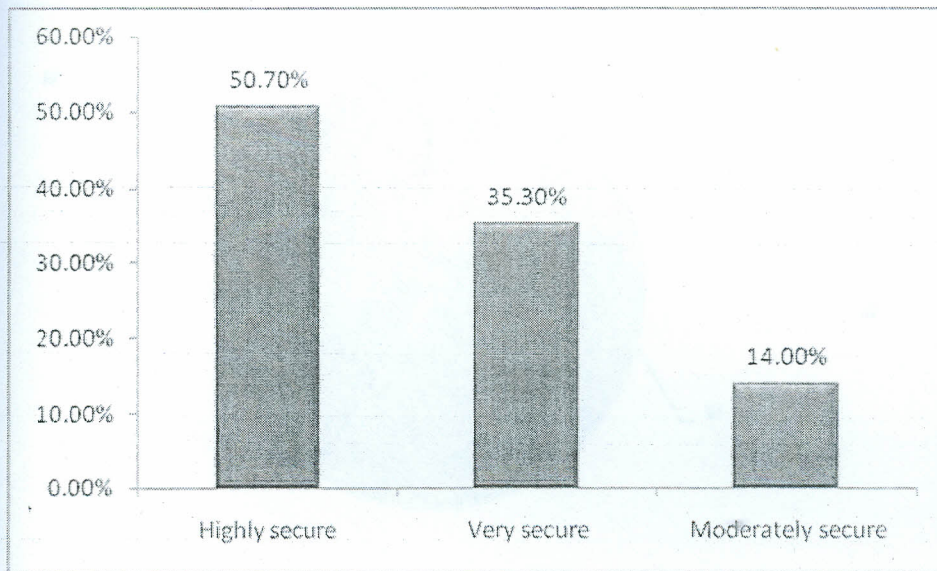
	Mean	Std. Deviation
We prefer foreign banks because they enhance competition and innovation in the bank market	3.3000	1.23566
This institution prefers the local bank because it understands the needs of its customers as compared to foreign banks	3.4067	1.10579
We prefer foreign bank because they are well established and has been in operation for many years	3.2600	1.14358

4.7 Influence of Security of Deposit on the choice of retail bank

4.7.1 Rating of the security of the bank

The respondents were required by the study to rate the security of deposit in the bank in which they deposited their money. According to the findings, majority of the respondents (50.7%) rated their banks' as highly secure, 35.3% as very secure while 14% rated them as moderately secure. This illustrates that security of the bank as perceived by the clients is a key consideration by the customers while selecting their choice of bank.

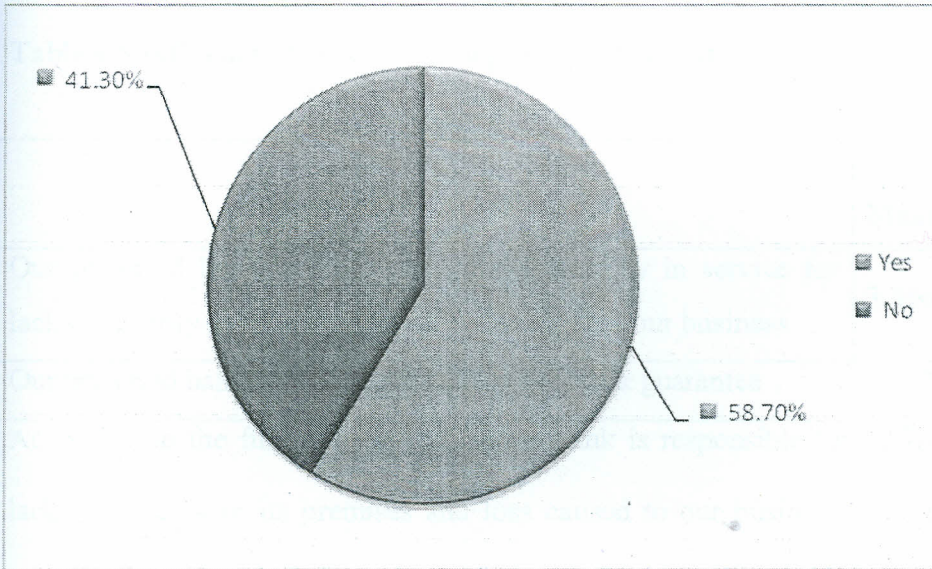
Figure 4.19 Rating of the security of the bank



4.7.2 Whether the bank is responsible for deficiency in service for lack of security

The researcher sought to establish whether the bank were responsible for deficiency in service for lack of security in its premises and loss caused to customer. As shown in the figure 4.20, majority of the respondents (58.7) indicated that bank were responsible for deficiency in service for lack of security in its premises and loss caused to customer. On the other hand, 41.3% of the respondents posited that bank were not responsible for deficiency in service for lack of security in its premises and loss caused to customer. This depicts that the security of deposits offered by the bank influences the choice of retail banks by the SMEs.

Figure 4.20 Whether the bank is responsible for deficiency in service for lack of security



4.7.3 Influence of security of deposit on choice of your preferred retail bank

Table 4.8 Influence of security of deposit on choice of your preferred retail bank

	Mean	Std. Deviation
Our preferred bank is responsible for deficiency in service for lack of security in its premises and loss caused to our business	3.4667	1.44551
Our preferred bank sometimes fails to honor bank guarantee	3.4333	1.20634

According to the findings, 'our preferred bank is responsible for deficiency in service for lack of security in its premises and loss caused to our business' was the most significant aspect of the influence of deposit on security on choice of bank. This is as shown by a mean of 3.46. Other aspect of security of deposit were that 'the preferred bank sometimes fails to honor bank guarantee' as shown by its mean of 3.43.

4.8 Choice of Retail Bank

4.8.1 Reasons for the choice of Retail Bank

The researcher sought to establish the various reasons that had made the respondents to stay with their current banks. As shown in table 4.11, confidentiality and good rapport between bank employees and the customers were the most significant reasons that had made the respondents to stay with their current bank as shown by means of 4.19 and 4.03 respectively.

The other reasons that made the respondents to stay with their current banks were that the bank offers customized services; the bank offers services very promptly, convenience and availability of credit facilities as shown by mean of 3.97, 3.86, 3.74 and 3.26 respectively.

Table 4.9 Reasons for the choice of Retail Bank

	Mean	Std. Dev
We have chosen to stay with the bank because it offers to us types of services we need	3.9667	0.90053
We have been banking with this bank because it is convenient to our size of business	3.7400	0.74573
This school has chosen to stay in this bank because it is possible to obtain credit facilities	3.2667	1.00112
This school prefer this retail branch because it offers services very promptly	3.8600	0.81948
We have chosen this retail bank because its staff have good rapport with us	4.0333	0.64938

We have chosen to stay with this retail bank because it gives high confidentiality to our transactions	4.1933	1.06624
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4.9 Inferential Statistics

Pearson's product moment correlation analysis was used to assess the relationship between the variables while multiple regressions were used to determine the predictive power of the factors affecting choice of retail banks by the SMEs.

4.9.1 Correlation Analysis

The data presented before on interest rates on loan, proximity to the bank, service quality, country of incorporation and security of deposit were computed into single variables per factor by obtaining the averages of each factor. Pearson's correlations analysis was then conducted at 95% confidence interval and 5% confidence level 2-tailed. The table below indicates the correlation matrix between the factors (interest rates on loan, proximity to the bank, service quality, country of incorporation and security of deposit) and choice of retail banks. According to the table, there is a positive relationship between choice of retail bank and service quality, security of deposit, interest on loan proximity to the bank and country of incorporation of magnitude 0.894, 0.493, 0.661, 0.402 and 0.308 respectively. The positive relationship indicates that there is a correlation between the factors and the choice of retail bank with service quality having the highest value and country of incorporation having the lowest correlation value.

This notwithstanding, all the factors had a significant p-value ($p < 0.05$) at 95% confidence level. The significance values for relationship between choice of retail bank and interest rates on loan, proximity to the bank, service quality, country of incorporation and security of deposit were 0.018, 0.031, 0.024, 0.046 and 0.48 respectively. This implies that service quality was the most significant factor, followed by interest on loan then security of deposit while country of incorporation was the least significant.

Table 4.10 Correlation Matrix

	Choice of retail banks	Service quality	Security of deposit	Interest on loan	Proximity to the bank	Country of incorporation
Choice of retail banks (r) (p) Sig. (2 tailed)	1.000					
Service quality (r) (p) (2 tailed)	0.894 0.018	1.000				
Security of deposit (r) (p) Sig. (2 tailed)	0.493 0.031	0.316 0.047	1.000			
Interest on loan (r) (p) Sig. (2 tailed)	0.661 0.024	0.163 0.019	0.216 0.047	1.000		
Proximity to the bank (r) (p) Sig. (2 tailed)	0.402 0.046	0.161 0.029	0.233 0.0464	0.462 0.014	1.000	
Country of incorporation (r) (p) Sig. (2 tailed)	0.308 0.048	0.159 0.035	0.243 0.442	0.454 0.011	0.543 0.341	1.000

4.9.2 Regression Analysis

In addition, the researcher conducted a multiple regression analysis so as to test relationship among variables (independent) on the choice of retail banks. The researcher applied the statistical package for social sciences (SPSS V 17.0) to code, enter and compute the measurements of the multiple regressions for the study.

Coefficient of determination explains the extent to which changes in the dependent variable can be explained by the change in the independent variables or the percentage of variation in the dependent variable (choice of retail bank) that is explained by all the five independent variables (interest rates on loan, proximity to the bank, service quality, country of incorporation and security of deposit).

4.8.2.1 Model Summary

The five independent variables that were studied, explain only 84.5% of the choice of retail bank as represented by the R^2 . This therefore means that other factors not studied in this research contribute 15.5% of the choice of retail bank. Therefore, further research should be conducted to investigate the other factors (15.5%) that affect choice of retail bank in Kenya by the SMEs.

Table 4.11: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.919	0.845	0.789	0.6273

Source: Research, 2011

4.8.2.2 ANOVA Results

The significance value is 0.0179 which is less than 0.05 thus the model is statistically significant in predicting how interest rates on loan, proximity to the bank, service quality, country of incorporation and security of deposit affect the choice of retail bank by SMES in the education sector in Kenya. The F critical at 5% level of significance was 3.23. Since F calculated is greater than the F critical (value = 9.475), this shows that the overall model was significant.

Table 4.12: ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2.534	2	1.267	9.475	.0179 ^a
	Residual	9.307	40	2.327		
	Total	3.465	42			

4.8.2.3 Coefficient of determination

Multiple regression analysis was conducted as to determine the relationship between choice of retail bank and the five variables. As per the SPSS generated table below, the equation ($Y = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4 + \beta_5X_5 + \varepsilon$) becomes:

$$Y = 1.147 + 0.752X_1 + 0.487X_2 + 0.545X_3 + 0.439X_4 + 0.416X_5$$

According to the regression equation established, taking all factors into account (service quality, security of deposit, interest on loan, proximity to the bank and country of incorporation) constant at zero, choice of retail bank will be 1.147. The data findings analyzed also shows that taking all other independent variables at zero, a unit increase in service quality will lead to a 0.752 increase in choice of retail bank; a unit increase in security of deposit will lead to a 0.487 increase in choice of retail bank, a unit increase in interest on loan will lead to a 0.545 increase in choice of retail bank, a unit increase in proximity to the bank will lead to a 0.439 increase in choice of retail bank while a unit increase in country of incorporation will lead to a 0.416 increase in choice of retail bank. This infers that service quality contribute most to the choice of retail bank followed by

interest on loan. At 5% level of significance and 95% level of confidence, service quality had a 0.0192 level of significance, security of deposit showed a 0.0269 level of significance, interest on loan showed a 0.0251 level of significance, proximity to the bank showed a 0.0454 level of significance and country of incorporation showed a 0.0494 level of significance, hence the most significant factor is service quality.

Model	Sum of Squares	df	Mean Square	F	Sig.
1	0.419	5	0.0837	0.163	0.984
2	0.415	10	0.0415	0.079	0.994

Table 4.13: Coefficient of determination

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.147	1.2235		1.615	0.367
	Service quality	0.752	0.1032	0.152	4.223	.0192
	Security of deposit	0.487	0.3425	0.054	3.724	.0269
	Interest on loan	0.545	0.2178	0.116	3.936	.0251
	Proximity to the bank	0.439	0.1937	0.263	3.247	.0454
	Country of incorporation	0.416	0.139	0.279	3.056	.0494

Source: Research, (2011)

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMENDATIONS

5.1 Introduction

This chapter gives a summary of the research findings, conclusion and recommendations. In this chapter, the researcher gives a summary of the factors affecting choice of retail bank by SMEs in the education sector in Kenya.

5.2 Summary of the Study

The aim of this study was to find out the factors affecting choice of retail bank by SMEs in the education sector in Kenya. The specific objectives of the study included to find out the influence of interest rate charged on loan and service to the SMEs entrepreneurs; to investigate the influence of proximity to the bank on choice of the retail bank; to find out the influence of bank country of incorporation on the choice of a retail bank by SMEs; to examine the effect of service quality on the choice of a retail bank by the SMEs and to investigate the effect of safety of deposit on the choice of retail banks by SMEs. The questionnaires were designed in line with the specific objectives of the study. The questionnaires were used to collect quantitative data. To enhance the quality of data obtained, structured type questions were included whereby respondents indicated the extent to which the variables were practiced. Frequency distribution tables were used to present data while percentages are used to discuss the findings.

5.3 Discussion of the Findings

5.3.1 Influence of Interest rate charged on loan and service on choice of retail bank

The research established that SMEs relied on loans to fund the operation of their institution which they had borrowed for two or more times and therefore the amount of interest rates on loans borrowed influenced the choice of retail bank by the SMEs. The study found out that the amount of interest rates influenced the choice of retail bank to a great extent. In addition, SMEs preferred their respective bank because they offer interest rate on loan and services at competitive rates. Other reasons were that SMEs choose their bank because it offers them incentives when opening business account and because the bank does not charge additional costs on transactions made.

5.3.2 Effect of the proximity to the bank on choice of the retail bank by the SMEs.

The research found out that the entrepreneurs visited their banks weekly and on daily basis thus proximity of the bank is a determinant of the choice of retail bank. It was reported that the proximity of the bank influenced the choice of retail bank to a great extent by most of the respondents.

The researcher established that through technology the preferred bank is very accessible and close to our business was the most significant aspect of proximity of bank to the choice of banks by the entrepreneurs. This point to the effect of technology on increasing accessibility of banking services to the SMEs. However the entrepreneurs further pointed out that

technology could not help them access some services like loans and they had to walk to the bank to ask for them.

5.3.3 Effect of service quality on the choice of a retail bank

The study found out that the services the banks offered high quality services to their customers which were the reason the customers preferred them for others. The entrepreneurs were satisfied by the services offered by customer care representatives in their preferred bank to a great extent. In addition, the quality of customer service influenced SMEs choice of the bank to a great extent. The quality service directly relates to customer satisfaction and hence their loyalty to the bank to a great extent.

5.3.4 Influence the country of incorporation of the bank on the choice of a retail bank by SMEs

The research established that SMEs prefer local banks as compare to their foreign counterparts. This is owing to the fact that local banks had a better understanding on the needs of the SMEs and helped growth of the local economy as compared to foreign banks whose profits benefits their mother countries. The country of incorporation of the bank affected the choice of the bank to a great extent.

5.3.5 Influence of safety of deposit on the choice of retail banks by SMEs

The study revealed that the banks are highly secure and offered enough security of the customers' deposits. This illustrates that security of the bank as perceived by the clients is a

key consideration by the customers while selecting their choice of bank. In addition, banks were responsible for deficiency in service for lack of security in its premises and loss caused to customer. However the preferred bank sometimes fails to honor bank guarantee to the entrepreneurs.

The research further established that confidentiality and good rapport between bank employees and the customers were the most significant reasons that had made the respondents to stay with their current bank. The other reasons that made the respondents to stay with their current banks were that the bank offers customized services; the bank offers services very promptly, convenience and availability of credit facilities respectively.

The study also established that there is a correlation between the factors and the choice of retail bank by the SMEs with quality service having the highest value and country of incorporation having the lowest correlation value. From the regression analysis the following regression equation was formulated; $Y = 1.147 + 0.752X_1 + 0.487X_2 + 0.545X_3 + 0.439X_4$

From the above regression equation, it can be deduced that quality service contributes most to the choice of retail banks by the SMEs in Kenya followed by interest on loans and other services. At 5% level of significance and 95% level of confidence, the most significant factor is quality of service.

The five independent variables that were studied, explain only 84.5% of the choice of retail bank as represented by the R^2 . According to the regression equation established, taking all factors into account (service quality, security of deposit, interest on loan, proximity to the

bank and country of incorporation) constant at zero, choice of retail bank will be 1.147. The data findings analyzed also shows that taking all other independent variables at zero, a unit increase in service quality will lead to a 0.752 increase in choice of retail bank; a unit increase in security of deposit will lead to a 0.487 increase in choice of retail bank, a unit increase in interest on loan will lead to a 0.545 increase in choice of retail bank, a unit increase in proximity to the bank will lead to a 0.439 increase in choice of retail bank while a unit increase in country of incorporation will lead to a 0.439 increase in choice of retail bank. This infers that service quality contribute most to the choice of retail bank followed by interest on loan. At 5% level of significance and 95% level of confidence, service quality had a 0.0192 level of significance, security of deposit showed a 0.0269 level of significance, interest on loan showed a 0.0251 level of significance, proximity to the bank showed a 0.0454 level of significance and country of incorporation showed a 0.0494 level of significance, hence the most significant factor is service quality.

5.4 Conclusion

The research concluded that SMEs relied on loans to fund the operation of their institution and therefore the amount of interest rates on loans borrowed influenced the choice of retail bank by the SMEs. The study concluded that the amount of interest rates influenced the choice of retail bank to a great extent. In addition, SMEs preferred their respective bank because they offer interest rate on loan and services at competitive rates.

The researcher concluded that through technology made bank accessible and close to SMEs thus enhancing the proximity of the bank to the business. However some services like borrowing credit from banks could only be accessible to the entrepreneurs by going to their preferred banks. The proximity of the bank is a determinant of the choice of retail bank as SMEs required banking services regularly.

The study concluded that the SMEs considered their preferred banks to be offering high quality services to them thus they were the bank of choice. The entrepreneurs are satisfied by the services offered by their preferred bank to a great extent. In addition, the quality of customer service influenced SMEs choice of the bank to a great extent. The quality service directly relates to customer satisfaction, retention and loyalty to a great extent.

The research concludes that security of deposit is a key consideration by the SMEs while selecting their choice of retail bank. In addition, the banks were responsible for deficiency in service for lack of security in its premises and loss caused to customer.

The study also concludes that there is a correlation between the factors and the choice of retail bank by the SMEs with quality service having the highest value and country of incorporation having the lowest correlation value. The study finally concludes that service quality contribute most to the choice of retail bank followed by interest on loan.

5.5 Recommendations

The study recommends that banks should improve on the quality of service they offer to the

SMEs to become the preferred choice of retail bank by the SMEs. Service quality will play an important role in enhancing customer satisfaction, retention and loyalty.

The study further recommends that banks should regularly review the amount of interest rates on loans and other services offered to the SMEs, to design interest rates at competitive prices with respect to changing economic times.

The study finally recommends that the banking institution should enhance the security of deposit by their clients which is a major determinant of choice of retail bank by the SMEs.

5.6 Suggestions for further studies

Since this study explored the factors affecting choice of retail bank by SMEs in the education sector in Kenya, the study recommends that;

- i. Similar study should be done in SMEs based in other sectors of economy in Kenya for comparison purposes and to allow for generalization of findings on the factors affecting choice of retail bank by SMEs.

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APPENDIX 1 INTRODUCTION LETTER

Kenyatta University,

DEPARTMENT OF

P.O Box,

Date.....

Dear Sir/Madam/Student,

RE: LETTER OF INTRODUCCION

I am a student at the Kenyatta University taking a Master's in Business Administration. As a requirement for the fulfillment of the Masters degree, I intend to carry out research on **“FACTORS AFFECTING CHOICE OF RETAIL BANK BY SMEs IN THE EDUCATION SECTOR IN KENYA.”**

The questionnaire attached here with is meant to gather information for this study from you. It will be treated with utmost confidentiality and will only be used on purposes of academic research. I am kindly requesting you to assist me by filling in the questionnaire.

Yours faithfully

Daniel Kamakia Mwaniki

APPENDIX 2 QUESTIONNAIRE

Instructions: *(Please read the instructions given and answer the questions as appropriately as possible).* It is advisable that you answer or fill in each section as provided. Make an attempt to answer every question fully and correctly.

PART A: Demographic Information

1. What is the name of the school? (Optional)
2. What is your gender? Male Female
3. Which is your age bracket?
 - a) 20-35 years b) 36-45 years
 - c) Above 45 years
4. What is your highest level of education?
Secondary School certificate Diploma Graduate
Masters PhD
5. For how many years have you operated this business?
 - a) Less than 1 year b) 1-5 years c) 6-10 years
 - d. Over 10 years

6. On average, what is the sales turn over?

- a. Less than Ksh 50,000 [] b) Ksh 50,000 -100,000 []
c) Ksh 101,001-250,000 [] d) Ksh 250,001-500,000 []
d. over Ksh 500,000 []

7. How many employees does your school have?

- a) 1-10 b) 11-50 c) 51-100 d) 101-200 e) Over 200

8. Does the school operate a bank account/(s)? a) Yes [] b) No []

9. Which is /are the schools' preferred retail bank(s)?

PART B: Influence of Interest rate charged on loan and service to the SMEs entrepreneurs

10. Have you ever taken a business loan to fund the school operations?

- a) Yes [] b) No []

11. If yes, over a period of 5 years, how many times have you taken a loan?

- a) Once [] b) Twice [] c) Thrice [] d) Four times []

12. To what extent did the interest rates charged by the banks on loans influence the choice of the lending bank?

- a) Very great extent [] b) Great extent [] c) Moderate extent []
d) Less extent [] e) No extent at all []

13. To what extent do you agree with the following statements on the influence the interest rate on the choice of retail bank?

	Strongly agree	Agree	Moderately disagree	Disagree	Strongly disagree
We prefer this bank because it offers low interest rate level					
We prefer this bank because it does not charge additional costs on transactions made					
We choose this bank because it offers us incentives when opening business account					

PART C: Proximity to the Bank

14. How often do you visit your preferred bank?

- a) Every day [] b) Weekly [] c) Fortnightly []

Others specify

15. Is/are your preferred bank(s) near the location of your business?

- a) Yes [] b) No []

16. To what extent does the proximity to the bank influence your choice of a retail bank?

- a) Very great extent [] b) Great extent [] c) Moderate extent []
 d) Less extent [] e) No extent at all []

17. To what extent do you agree with the following statement on how proximity to the bank has influenced your choice of the retail bank?

	Strongly agree	Agree	Moderately agree	Disagree	Strongly disagree
We prefer this retail bank because it is close to our business premises					
Through technology the preferred bank is very accessible and close to our business					
We prefer local banks to foreign ones due to their proximity to our enterprise.					

PART D: Effect of service quality on the choice of a retail bank

18. How would you rate service quality in your preferred bank?

- Very high [] High []
 Moderate [] Low []
 Very low []

19. To what extent are you satisfied with the services offered by customer care representatives in your preferred bank?

- a) Very great extent b) Great extent c) Moderate extent
d) Less extent e) No extent at all

20. To what extent does the quality of customer service influence your choice of the bank?

- a) Very great extent b) Great extent c) Moderate extent
d) Less extent e) No extent at all

21. To what extent do you agree with the following aspect of service quality of your retail bank?

	Strongly agree	Agree	Moderately	Disagree	Strongly disagree
Our business is loyal to the retail bank because they offer high quality services					
We get high level of customer satisfaction as our preferred bank offers to us high service quality during transactions					
Quality service directly relates to customer satisfaction and hence their loyalty to the bank					

PART E: EFFECT OF COUNTRY OF INCORPORATION

22. Which is the nature of your preferred bank?

Local [] Foreign []

23. To what extent does the country of incorporation of the bank affect the choice of the bank?

- a) Very great extent [] b) Great extent [] c) Moderate extent []
 d) Less extent [] e) No extent at all []

24. To what extent do you agree with the following aspect when looking at the influence of the country of incorporation in the choice of your retail bank ?

	Strongly agree	Agree	Moderately	Disagree	Strongly disagree
We prefer foreign banks because they enhance competition and innovation in the bank market					
This institution prefers the local bank because it understands the needs of its customers as compared to foreign banks.					
We prefer foreign bank because they are well established and has been in operation for many years					

SECTION F : Security of Deposit

25. How would you rate the security of the bank in which you deposit you money?

- a) Highly secure
- b) Very secure
- c) Moderately secure
- d) Not secure
- e) Very insecure

26. Is your bank responsible for deficiency in service for lack of security in its premises and loss caused to customer?

- a) Yes []
- b) No []

27. To what extent do you agree with the following statement on the influence of security of deposit on choice of your preferred retail bank?

	Strongly agree	Agree	Moderately agree	Disagree	Strongly disagree
Our preferred bank is responsible for deficiency in service for lack of security in its premises and loss caused to our business					
Our preferred bank sometimes fails to honor bank guarantee					

SECTION G: CHOICE OF RETAIL BANK

In the past 5 years, this school may have changed or continued with the same bank. The following statements relate to the decision to stay or change. For each statement indicate how you agree or disagree.

	Strongly agree	Agree	Moderately agree	Disagree	Strongly disagree
We have chosen to stay with the bank because it offers to us types of services we need					
We have been banking with this bank because it is convenient to our size of business					
This school has chosen to stay in this bank because it is possible to obtain credit facilities					
This school prefer this retail branch because it offers services very promptly					
This school has chosen to stay with this retail bank					
We have chosen this retail bank because its staff have good rapport with us					
We have chosen to stay with this retail bank because it gives high confidentiality to our transactions					

THANK YOU FOR YOUR TIME AND PARTICIPATION