

Effect of Microfinance Credit on SMEs Financial Performance in Kenya

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Abstract

The Small and Medium Enterprises (SME) sector is important for the growth of the economy in any developing country. Similarly, microfinance credit facilities are crucial to SMEs financial performance as they facilitate growth of the SMEs businesses. In our study, we investigate the effect of microfinance credit factors (credit amount, interest rate, collateral requirement, credit repayment period and entrepreneur orientation) on the SMEs financial performance in Kenya using a sample size of 210 SMEs. Stratified and simple random sampling technique was employed. Cronbach's alpha was used to estimate reliability and alpha of 0.7 was deduced which showed the instruments were reliable. Data collected established that majority of respondents had not received any entrepreneurial training. The effect of interest rate, collateral requirement, and repayment period were found to have negative effect on SMES financial performance, but there was a positive effect on the entrepreneur orientation and credit amount. The study also established that microfinance credit factors affect SMEs financial performance with entrepreneur orientation contributing the most to SMEs financial performance compared to the other factors thus implying that most of the SMEs entrepreneurs are innovative, take risks by venturing into new business activities and are proactive. The study recommends that microfinance institutions consider entrepreneur orientation training while disbursing credit.

Keywords: microfinance credit, financial performance, regression analysis, entrepreneur orientation.

INTRODUCTION

The practice of microcredit dates back to the early 1700 and can be traced to the Irish loan fund system which provided small loans to rural poor with no collateral. Over the years, the concept of microfinance spread to Latin America, then to Asia and later to Africa. Today, use of the expression micro financing has its roots in the 1970s when organizations such as Grameen Bank of Bangladesh with the microfinance Pioneer Mohammed Yunus, were starting and shaping the modern industry of micro financing Mwangi (2011). In the early 1990s with the opening up of the political space and disturbances, the need for the credit by individual, micro, small and medium enterprises increased and this led to the recognition of the microfinance institution in Kenya.

Small and medium enterprises (SMEs) are considered to be the key engine of the economic development (Chittithaworn, Islam & Keawchana, 2011; Ionita, et al, 2009; Deros, Yusof & Salleh, 2006). The relative importance of the SME sector varies greatly across countries, whereby SMEs have been known to make important economic contributions, whether in developed or developing countries. A number of large enterprises

develop from SMEs and some of them even rely on SMEs.

Even though the definitions of 'SMEs' come in variation, the importance of SMEs in the contemporary global economy has demonstrated the shift of emphasis towards SMEs in all countries (Olomi, 2009). This is justified by both the quantitative and qualitative contributions of SME sections to the well-being of a nation's economy. Their effects can be seen in a number of areas, including providing job opportunities for the workers, distributing income, alleviating poverty, providing a training ground for the development and upgrading entrepreneurship skills, and serving as important vehicles for promoting forward and backward linkages in geographically diverse sectors of the economy in many countries (ibid). According to a World Bank report (2016) 600 million jobs are needed across Africa in the next 15 years to absorb a growing global workforce. Most formal jobs in emerging markets are with small and medium enterprises (SMEs), which also create 4 out of 5 new positions and yet more than 50% of SMEs lack access to finance, which hinders their growth (Ref: World Bank - Informal Enterprises in Kenya)

In Kenya, Small and Medium Enterprises (SMEs) is an important sector of the growth of economy like many other developing countries since it employs about 85% of the Kenyan workforce. The current constitutional framework and the new Micro and small Enterprises Act of 2012 (MSE Act 2012) provide a new window of opportunity through which the evolution of SMEs can be realized through the devolution framework. However, the impact of devolution on SMEs development depends on the architecture of regulatory and institutional framework inclined to support SMEs in the economy Ong'olo and Odhiambo (2013). Despite the importance of (SMEs) in the national economy in general, they face many obstacles that hinder their development, one of which is evident in the aspect of financial access.

Several empirical studies have documented the existence of a strong positive link between the functioning of the financial system and economic growth across countries, and that stage of financing increases the probability of performance measures such as investment and employment (Rousseau and Sylla 2003). Several studies conducted in Kenya (e.g. Kibet, Achesa & Gedion, 2015; Rotich, Lagat & Kogei, 2015; Wanambisi, 2013) argue that there is positive relationship between microfinance services and SMEs performance. This includes the favourable initial credit amount, favorable interest amount, achievable collateral and, favourable credit repayment period. Furthermore, the number of the microfinance institutions in developing countries including Kenya is also increasing.

It is generally acknowledged that small businesses can borrow money from formal financial avenues however there is substantial evidence that SMEs face increasingly large number of constraints such as less access to formal sources of external finance, potentially explaining the lack of SME contributions to growth (Olomi, 2009). SMEs' inability to access bank loan can be explained through some well-known reasons such as the collateral required by the banks, high interest rates, and lack of relationships with bankers.

Several studies (e.g. Kibet, Achesa & Gedion, 2015; Rotich, Lagat & Kogei, 2015; Wanambisi, 2015) focused on the effect of microfinance services on SMEs performance; however, they did not consider the effect of entrepreneurial orientation of the SMEs owners or operators.

Despite the contribution of the reviewed literature on SMEs performance and microfinance credit, the literature has indicated that majority of the studies applied a single measure to explain the SMEs

performance. Similarly, the concept of performance cannot be adequately measured by a single item since it is a multi-dimensional factor (Ahmad & Ghani, 2010). Most studies did not consider Entrepreneur Orientation as a variable which is key to SMEs financial performance. This study therefore intends to use multiple variables including the Entrepreneur orientation to examine their effects on SMEs financial performance.

This study aims to investigate the effect of microfinance credit factors (credit amount, interest rate, collateral requirement, credit repayment period and entrepreneur orientation) on the SMEs financial performance in Kenya. Recent literature focuses on the effect of micro finance on performance of SMEs using a single variable and without recognizing the impact of entrepreneurial orientation on SMEs performance.

Statement of the Problem

Access to microfinance credit is considered to be an important factor in determining the performance of SMEs. Microfinance credit is one of the financial services that are expected to promote SMEs financial performance. Despite the mushrooming of microfinance institutions that provide microfinance credit in Kenya, majority of SMEs do not perform well. This has been attributed to lack of access to financial services and unfavorable credit facilities such as high interest rates and short repayment period. Despite the contribution of the reviewed literature on SMEs performance and microfinance credit, the literature has indicated that majority of the studies applied a single measure to explain the SMEs performance. Similarly, the concept of performance cannot be adequately measured by a single item since it is a multi-dimensional factor. Most studies did not consider Entrepreneur Orientation as a variable which is key to SMEs financial performance. This study therefore intends to use multiple variables including the Entrepreneur orientation to examine their effects on SMEs financial performance.

Limitations of the Study

The study focused on the effect of microfinance credit factors (credit amount, interest rate, collateral requirement, credit repayment period and entrepreneur orientation) on SMEs financial performance. The key shortcomings while conducting the study included: time limitation as it was conducted within a period of four months, delayed responses and inadequate finances. The target population of the study was limited to 210 SME owners within Nairobi county. This study would have been carried out across the whole country because SMEs are spread throughout the country.

LITERATURE REVIEW

Theoretical Review

Resource based view

The Resources Based View (RBV) is considered to be the key theory that explains the influence of a resource on business performance (Crook *et al*, 2008). This study considered microfinance credit as a financial resource which may have influence on SMEs financial performance and therefore RBV is relevant.

Studies on environmental influence on organization survival have well been documented (Aldrich, 1979, Hannan and Freeman 1977). Research has shown that successful management of internal resources can significantly improve venture performance and the likelihood of survival (Oginni and Adesanyam, 2013). However, for company in general and start-ups in particular, the resource has to be frequently extended and renewed.

According to Barney (1991) firm resources can be classified into three categories: physical capital resources, human capital resources and organizational resources. An entrepreneur is in needs to possess such resources. Organizational resources include informal relations among people within a firm and between the firm and its environment.

Empirical Review

Microfinance credit

Microfinance credit can be considered to be one of the financial sources of SMEs. It plays a crucial role on poverty alleviation due to its contribution in the development of SMEs. For instance, SMEs sector in Kenya is a source of income for over eight million people who present the majority of the Kenyan workforce (World Bank, 2011).

Credit Amount and SMEs Financial Performance

The amount of credit offered by the financial institutions may determine the performance of SMEs in terms of sales, liquidity and even the operating costs. This is supported by several researchers such as Oleka, *et al* (2014 UWFT, 2005; Wanambisi 2013). For example, Oleka, *et al* (2014) argue that the loan size positively influence the growth of SMEs. It was also argued that the business that receive adequate amount of loan frequently perform better than the ones that do not (Wanambisi, 2013) also argues that appropriate loan sizes for clients, matching SMEs needs influence the business sustainability.

Interest Rate and SMEs Financial Performance

A well-developed microcredit system can help SMEs to access affordable credit services (Alhassan &

Hoedoafia, 2016). The microfinance credit can be affordable to SMEs if the interest rate is low. Access to low interest rates has been attributed to a major factor that increases SMEs performance (Mwangi 2011, Kamau and Kalio 2014). Similarly access to low loans increases SMEs risk bearing abilities, improve risk coping strategies and enables consumption smoothing over time.

Collateral Requirement and SMEs Financial Performance

Collateral is defined as security for loans that it can protect the lender if the borrower default (Indersta & Mueller 2007). Studies cite that increase in firm's collateral relax the credit constraints faced by the firm, facilitating the firm to borrow more (Wang, 2004). A well-developed microcredit system can help SMEs to access affordable credit services particularly if the collateral requirement is affordable (Alhassan & Hoedoafia, 2016).

Credit Repayment Period and SMEs Financial Performance

A well-developed microcredit system can help SMEs to access affordable credit services particularly if there are friendly repayment period options to repay the loan (Alhassan & Hoedoafia, 2016). Bragg (2010) stated that "the short time frame reduces the risk of non-repayment to the bank, which can be reasonably certain that the business's fortunes will not decline so far within such a short time period that it cannot repay the loan, while the bank will also be protected from long-term variations in the interest rate".

Entrepreneurial Orientation and SMEs Financial Performance

Entrepreneur orientation (EO) refers to the decision-making styles, practices, processes and behaviours that lead to 'entry' into new or established markets with new or existing goods or services (Lumpkin and Dess 1996; Wiklund and Shepherd 2005). Further EO has been attributed to consisting of dimensions such as innovativeness, risk taking and proactiveness (Frank, Kessler & Fink 2010). EO has been considered as a critical component of the firm's success. A study by (Callagan and Venter, 2011) established association between EO and contextual factors with respect to earnings and continuous satisfaction. A study by Augusto, Moeljadi, Fatchur, & Solimun (2014) on effect of EO on business performance established that EO have an effect on business performance meaning that better EO could improve performance of SMEs and that government policy as a moderating variable did not have direct effect on SMEs performance.

CONCEPTUAL FRAMEWORK

In this conceptual framework, it is expected that Microfinance Credit factors (credit amount, interest rate, collateral requirement, credit repayment period and

entrepreneur orientation) have an effect on SMEs Financial Performance.

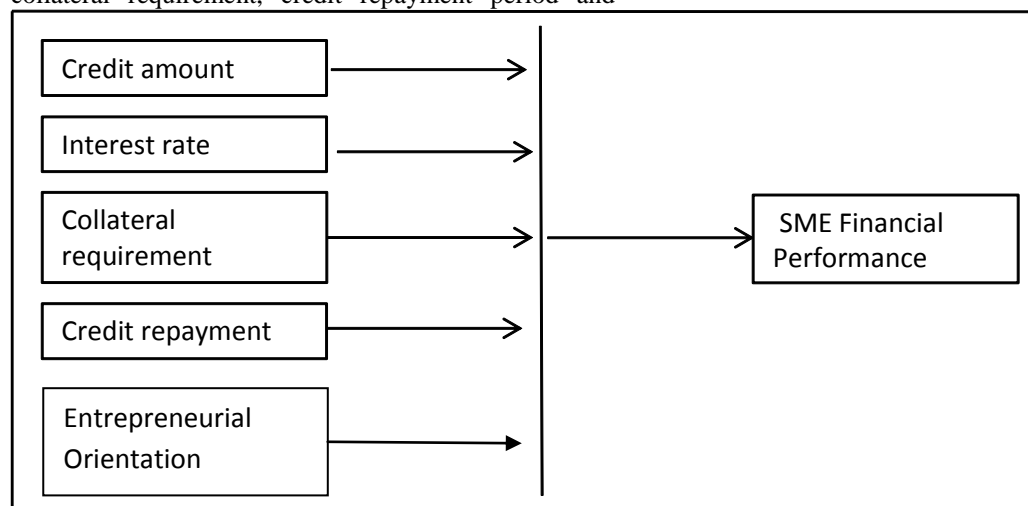


Figure 1: Conceptual framework: Effect of microfinance credit on SMEs financial performance

RESEARCH DESIGN AND METHODOLOGY

Research Design

This study employed descriptive survey and cross sectional design. The descriptive survey design allows the use of quantitative research approach, the designs as purported by (Creswell, 2013; Zikmund, Babin, Carr & Griffin, 2010) allows the researcher to capture quantitative aspects of the study which provides an understanding of a research problem.

Target Population

For this study, the target population included registered SME entrepreneurs in trade, services and manufacturing sectors. The target group was SMEs from Kenyatta Market, Gikomba Market, Toi Market, and Kawangware Market who are traders, manufacturers and those in-service businesses.

Sample and Sampling Procedures

According to Gay, Mills and Airasian (2009), the minimum sample size depends on the type a research involved. For a survey research, a sample of 10% to 30% of population is acceptable. This is concurrent with Lapoite (2013) who had similar observation. For this study the researchers selected 210 SMEs from an estimated target population of 2100 which accounts for 10% of the target population. The study targeted traders, service providers and manufacturers in four markets namely: Kenyatta Market, Gikomba Market, Kawangware and Toi Market.

Table 1: Sampling Techniques

Target SME Sector	Estimated Population	Sampling design	Sample size 10%
Trade	940	Stratified/simple random	94
Services	580	Stratified/simple random	58
Manufacturing	580	Stratified/simple random	58
Total	2100		210

Data Collection Instruments and Procedures

The study used questionnaires to collect relevant information. The use of questionnaires offered objective responses since they gather data in standardized way (Lapoite, 2013). The questionnaires were designed in the Likert scale of five (5) points.

Reliability of the Research Instrument

A measuring instrument is said to be reliable if it provides consistent results (Kothari, 2011). The researchers used Cronbach’s Alpha coefficient which ranges between 0 and 1 (Kipkebut, 2010), to establish the reliability that is to assess the internal consistency of the instrument. The researcher used Cronbach’s alpha because it requires only one testing session. Higher alpha coefficient values mean there is consistency among the items in measuring the concept of interest. As a rule of thumb, acceptable alpha should be at least 0.7 or above (Henson, 2001).

Table 2: Reliability Statistics

Case Processing Summary			N	%
Cases	Valid		30	100.0
	Excluded ^a		0	.0
	Total		30	100.0

a. Listwise deletion based on all variables in the procedure.

From the study an alpha of 0.683 (rounded to 0.7) was established. This shows that the instruments were reliable.

Data Collection Procedures

Two research assistants were trained on how to administer the questionnaires. A piloting test done on 30 SMEs not included in the final study. The questionnaires were self-administered together with the help of research assistants. This enabled collection of firsthand information.

Data Analysis and Presentations

In this research, primary data from questionnaires was used. The primary data played a major role since SMEs do not have reliable financial data. Quantitative data from closed ended questions was coded by assigning numerical values to differentiate the categories. Data was then analyzed using statistical package for social sciences (SPSS). Demographic data obtained was

summarized using descriptive (frequencies and percentages) and the findings were presented using frequency tables. The level of significance was measured using multiple regression model and Pearson Coefficients correlation and to determine the direction and strength of relationship between dependent variable and independent variables.

DATA ANALYSIS AND PRESENTATION OF RESEARCH FINDINGS

This section of the research study discusses the findings and results of the study based on the collected primary data and information from questionnaires. The aim of this study was to find out the effect of microfinance credit on SMEs financial performance.

Response Rate

The study targeted 210 SMEs respondents from Nairobi County. In total there were 210 duly completed questionnaires: (Kenyatta Market = 56, Gikomba Market = 86, Toy market = 68). Of the respondents, 94 were in trade, 58 in service and another 58 in manufacturing sectors.

Demographic Characteristics of the Respondents

The demographics of concern by the researcher included the following; the gender respondents, marital status and level of education.

Table 3: Demographic Characteristics of SMEs respondents

Gender		
	Frequency	Percent
Female	86	41.0
Male	124	59.0
Total	210	100.0
Marital status of people engaged in SMEs		
Single	59	28.1
Married	65	31.0
Divorced	35	16.7
Widowed	51	24.3
Total	210	100.0
Level of Education		
Primary	35	16.7
Secondary(KCSE)	40	19.0
Vocational training	37	17.6
A level	30	14.3
Certificate/Diploma	29	13.8
Degree/Advanced Diploma	20	9.5
Postgraduate/At least diploma	19	9.0
Total	210	100.0

On gender the study findings indicate that majority of the SMEs respondents were male (59%) while 41% of were female. This shows that there is higher percentage of male SMEs than female SMEs who were involved in this study. On the marital status of SME entrepreneurs’

28.1% were single, 31% married, 16.7% divorced and 24.3% widowed. This means there is almost an equal percentage of those who are single and those who are married are involved in SMEs activities. In this study (19%) were KCSE certificate holders, 17.67% had

vocational/technical training, 16.7% were primary certificate holders, 14.3% had 'A' levels, 13.8% certificate/ Diploma, 9.5% Degree/ Advanced Diploma and the least 9% were postgraduate. There is unequal distribution between those who had attained high level, from KCSE and above (66.6%), and those who low level of education; vocational training and below (34.2%).

Entrepreneurial Training

Base on the study, the results indicate that the majority 59% had not received any Entrepreneurial training whereas 41% had received training. This implies majority of SMEs are untrained and rely on their own skills.

Entrepreneurial Characteristics

Table 4: Enterprise ownership and Business Activities Respondents

Ownership			Business activities		
	Frequency	Percent		Frequency	Percent
Sole proprietor	145	69.0	Trade	94	44.8
Partnership	65	31.0	Services	58	27.6
Total	210	100.0	Manufacturing	58	27.6
			Total	210	100.0

The findings indicate that the majority of SMEs 69% are sole proprietors while 31% are in partnership. Those in trade business activities comprise 44.8% services and manufacturing were 27.6% each. The findings reveal that majority of SMEs activities concentrate on service provision and manufacturing (55%) and 45% on trading.

A total of 40% had received the first loan 2-3 years ago whereas 31% had received the first loan between 5-9 years ago. Those who had received a loan over 9 years ago comprised 19.5% while those who had received loans less than a year ago comprised 9.5%.

Table 5: Acquisition of microfinance credit

	Has Businesses acquired credit from microfinance institution?		Has Business more than one loan?	
	Frequency	Percent	Frequency	Percent
Yes	161	76.7	54	25.7
No	49	23.3	125	59.5
None of the above	210	100.0	31	14.8
Total	161	76.7	210	100.0

The respondents were asked to indicate their level of agreement as to whether the initial credit amount had influence on SMEs financial performance. The results are as indicated in the tables below.

A total of 76.7% responded that the business had acquired credit from microfinance institutions (MFI) whereas 23.8% had not received credit from MFI. In addition, majority of the respondents 59.5% had received only one loan while 25.7% had received more than one credit.

Table 7: The Initial Microfinance credit amount

Table 6: Period when first credit was acquired
When did the business acquired the first loan from microfinance institution

	Frequency	Percent
Less than a year	20	9.5
2 – 3 years	84	40.0
5 – 9 years	65	31.0
more than 9 years	41	19.5
Total	210	100.0

Statement	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
The credit amounts offered by the microfinance institutions are adequate to implement the business ideas	21(10%)	42(20%)	12(5.7%)	93(44.3%)	42(20%)
The credit amount is not limited by the collateral value	25(11.9%)	87(41.4%)	1(5%)	63(30%)	34(16.2%)
The credit amount is adequate to promote business growth	26(12.4%)	74(35.2%)	0(0%)	110(52.4%)	0(0%)
The credit amount given tallies with the loan application submitted to the microfinance institutions	23(11.0%)	55(26.2%)	0(0%)	109(51.9%)	23(11.0%)

According to the results 64.3% of respondents agreed that the initial credit amount offered by the microfinance institution is adequate to implement the business ideas whereas 30% disagreed. The remaining 5.7% were neutral. On the other hand 53.3% of respondents disagreed that the credit amount is not limited by the collateral requirement, while 46.2% agreed, and 5% were neutral. This means credit amount is limited by the collateral requirement. A total

of 52.4% agreed that the credit amount is adequate to promote business growth while 47.6% respondents disagreed. This implies credit amount received by SMEs is adequate in promoting business growth. A total of 62.9% of the respondents agreed that the credit amount tallies with the loan application submitted to the microfinance institution while 37.2% disagreed.

Table 8: Interest Rate on Microfinance credit

Statement	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
The interest rate on microfinance credit is low	15(7.1%)	70(33.3%)	2(1.0%)	109(51.9%)	14 (6.7%)
The interest rate is fair and affordable	25(11.9%)	75(35.7%)	0(0%)	110(52.4%)	0(0%)
The interest rate on loan does not significantly increase the business financial costs	8 (3.8%)	40(19.0%)	2(1.0%)	149 (71.0%)	11(5.2%)
The interest rate on loan does not significantly decrease the business cash flows	0(0%)	104(49.5%)	2(1.0%)	104(49.5%)	0(0%)

The table shows that 58.6% agreed that interest rate on microfinance credit is low while 40.4% respondents disagreed and the least 1% were neutral, this means the interest rate on microfinance credit is favourable. Most

of the SMEs 52.4% agreed that the interest rate is fair and affordable, while 47.6% disagree. This implies that the interest rate is fair and affordable.

Table 9: Collateral Requirements

Statement	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
The collateral value is affordable	16(7.6%)	63(30.0%)	0(0%)	120(57.1%)	11(5.2%)
There is fair evaluation of the collateral value	13(6.2%)	74(35.2%)	4(1.9%)	119(56.7%)	0(0%)
The collateral value is not the key requirement for the business to qualify for microfinance credit	21(10.0%)	117(55.7%)	10(4.8%)	62(29.5%)	0(0%)
The legal requirements to justify the ownership of the collateral are affordable	9(4.3%)	53(25.2%)	52(24.8%)	96(45.7%)	0(0%)

Respondents 62.3% agree that collateral value is affordable while 37.6% disagree. A total of 56.7 agree that there is fair evaluation of collateral while 41.4% disagree and 1.9% were neutral. Most of the respondents 65.7% disagree that the collateral value is not a key requirement for the business to qualify for the microfinance credit, whereas 29.5% agree, and the least 4.8% were neutral. This implies collateral value is a key

requirement for the business to qualify for microfinance credit. The result indicates 29.5% of the respondents disagree that the legal requirement to justify the ownership of the collateral are affordable, whereas 47.5% agree and 24.8% of the respondents were neutral. This implies that the legal requirement to justify the ownership of the collateral is affordable.

Table 10: Credit Repayment period

Statement	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
The credit repayment period is favorable to the business	22 (10.5%)	90(42.9%)	3(1.4%)	88(41.9%)	7(3.3%)
The duration of loan repayment is flexible	30(14.3%)	31(14.8%)	9(4.3%)	113(53.8)	27(12.9%)
The time given to repay the loan does not negatively influence the business cash flow	9(4.3%)	96(45.7%)	0(0%)	85(40.5%)	20(9.5%)
The time given to repay the loan allows the business to accumulate the required amount of cash	9(4.3%)	62(29.5%)	2(1.0%)	98(46.7%)	39(18.6%)

The majority of respondents 53.4% disagree that the credit repayment period is favorable to the business whereas 45.2% agreed and 1.4% were neutral. Majority 66.7% of the respondents agree that the duration of loan repayment is flexible, whereas 29.1% disagree and 4.3% were neutral. This implies that repayment period is

flexible. There is an equal response of 50% each of the respondents who agree and disagree that the time given to repay the loan does not negatively influence the business cash flow. This implies that the time to repay the loan is inconclusive.

Table 11: Entrepreneurial Orientation

Statement	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
I have been doing the same business the since its establishment	33(15.7%)	40(19.0%)	0(0%)	105(50.0%)	32(15.2%)
I usually develop new business strategies in order to compete in the market	0(0%)	11(5.2%)	0(0%)	155(73.8%)	44(21.0%)
I have a vision to invest into new unknown markets	0(0%)	15(7.1%)	7(3.3%)	132(62.9%)	56(26.7%)
I can invest the business money into the selling of newly introduced products to the market	0(0%)	5(2.4%)	0(0%)	142(67.6%)	63(30.0%)
I have plans on how to tap new business opportunities	0(0%)	5(2.4%)	0(0%)	170(81.0%)	35(16.7%)

Majority 65.2% of the respondents agree that they have been doing the same business since establishment whereas 34.7% disagree. This implies that most of SMEs have been consistent in their businesses.

least 3.3% were neutral. This implies that majority of the SMEs have vision to invest into unknown markets.

A total of 94.8% respondents agree that they usually develop new business strategies in order to compete in the market, while 5.2% disagree. This means majority of SMEs usually develop new business strategies in order to compete in a new market. Majority 89.6% agree that they have a vision to invest into new unknown markets, while 7.1% disagree and the

Almost all respondents 97.6% agree that they can invest the business money into the selling of newly introduced products to the market, while the remaining 2.4% disagree. This implies that majority of SMEs are of the opinion that they can diversify their products. Almost all 97.7% of respondents agree that they have plans on how to tap new business opportunities while 2.4% disagree.

Table 12: Business Financial Growth

Statement	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
Sales have increased	12(5.7%)	22(10.5%)	6(2.9%)	161(76.7%)	9(4.3%)
The number of employees have increased	0(0%)	53(25.2%)	0(0%)	157(74.8%)	0(0%)
The volume of inventory purchased from suppliers on cash basis have increased	10(4.8%)	13(6.2%)	0(0%)	187(89.0%)	0(0%)
The size of business transactions has decreased	0(0%)	99(47.1%)	22(10.5%)	58(27.6%)	31(14.8%)
The number of customers have increased	0(0%)	10(4.8%)	0(0%)	180(85.7%)	20(9.5%)

A total of 81% of the respondents agree that Sales have increased, whereas 16.2% disagree and 2.9% were neutral. Majority 74.8% of the respondents agree that the number of employees have increased, whereas 25.2% disagree.

disagree that the size of business transactions has decreased, while 42.4% agree and 10.5% were neutral. Majority 95.2% agree that the number of customers have increased, whereas 4.8% disagree.

According to majority 89% the volume of inventory purchased from suppliers on cash basis have increased, while 11% disagree. A total of 47.1% of respondents

Hypothesis Testing

The study sought to establish the effect of Microfinance Credit Factors (credit amount, interest rate, collateral requirement, credit repayment period and entrepreneur

orientation) on SMEs Financial Performance. The various variables were computed using a multiple regression model and Pearson Coefficients correlation and the results are as discussed in the tables below.

Null Hypothesis

H₀: There is no significant effect of Microfinance Credit factors (credit amount, interest rate, collateral requirement, credit repayment period and entrepreneur orientation) on SMEs Financial Performance.

In order to test this hypothesis regression analysis was conducted and the results are shown below.

Table 13: Model Summary on effect of Microfinance factors on SMEs financial performance

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.719 ^a	.518	.506	.34663

a. Predictors: (Constant), entrepreneur orientation, credit amount, credit repayment period, interest rate, collateral

The table represents results of regression analysis carried on effect of Microfinance factors on SMEs financial performance. The findings show that the coefficient of determination, R²=0.518, meaning that the generated model can account for 52% of the observed values.

Table 14: Regression Coefficients on effect of Microfinance factors on SMEs financial performance Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.115	.315		-.367	.714
	credit amount	.095	.028	.168	3.380	.001
	interest rate	.207	.028	.363	7.270	.000
	Collateral requirement	.147	.034	.223	4.372	.000
	credit repayment period	-.056	.031	-.088	-1.799	.073
	entrepreneur orientation	.591	.075	.402	7.879	.000

a. Dependent Variable: microfinance growth

- CA - credit amount
- IR - Interest rate
- CR - collateral requirement
- CRP - Credit repayment period
- EO - entrepreneur orientation

The results indicated the regression equation model as:

$$\text{SMEs financial performance} = -0.115 + 0.168 (CA) + 0.363 (IR) + 0.223 (CR) - 0.088 (CRP) + 0.402 (EO)$$

From the above equation, the results indicate that credit amount contributes 16.8% of the SME performance; interest rates 36.3%; collateral requirement 22.3%; credit repayment period 8.8% and entrepreneur orientation 40.2%.

For credit amount, interest rate, collateral and entrepreneur orientation had statistical significant effect to SMEs financial performance as indicated by the p-values 0.001, 0.000, 0.000, and 0.000 respectively which are less than alpha 0.05. The credit repayment period p-value 0.073 is greater than alpha 0.05 meaning that it has no statistical significant effect on SMEs financial performance. This would imply the credit repayment period negatively affected the SMEs financial performance by causing a decrease of 8.8%. Of the factors that have significant effect to SMEs performance entrepreneur orientation was found to have the greatest effect meaning the entrepreneurs have been

innovative, risk taking by venturing into new businesses/services and proactive.

Table 15: Correlations on effect of Microfinance factors on SMEs financial performance

		SME financial growth
credit amount	Pearson Correlation Sig. (2-tailed) N	.243** .000 210
Interest rate	Pearson Correlation Sig. (2-tailed) N	.482** .000 210
Collateral requirement	Pearson Correlation Sig. (2-tailed) N	.341** .000 210
Credit repayment period	Pearson Correlation Sig. (2-tailed) N	-.102 .140 210
Entrepreneur orientation	Pearson Correlation Sig. (2-tailed) N	.539** .000 210

It was noted that: There is weak positive correlation between **Credit amount** and SMEs finance performance since the r = 0.243 and the p-value 0.000 is less than alpha 0.05. This means the credit amount has significant statistical effect on SME financial performance.

There is moderate positive correlation between **Interest rate** and SMEs finance performance since the $r = 0.482$ (which is approximately 0.5). The p-value is 0.000 is less than alpha 0.05. This means the Interest rate has significant statistical effect on SME financial performance.

There is weak positive correlation between **collateral requirement** and SMEs finance performance since the $r = 0.341$. The p-value is 0.000 is less than alpha 0.05. This means the **collateral requirement** has statistical significant effect on SME financial performance.

There is weak negative correlation between **Credit repayment period** and SMEs finance performance since the $r = -0.102$. The p-value is 0.140 is greater than alpha 0.05. This means the **Credit repayment period** has no statistical significant effect on SME financial performance. This implies the time given to repay the loan negatively influences the business cash flow and is not favourable to the SMEs.

There is moderate positive correlation between **entrepreneur orientation** and SMEs finance performance since the $r = 0.539$. The p-value is 0.000 is less than alpha 0.05. This means the **entrepreneur orientation** has statistical significant effect on SME financial performance. This implies that most of the entrepreneurs are innovative, take risks by venturing into new business activities and are proactive.

DISCUSSION OF FINDINGS

The findings based on gender indicate that there was almost equal distribution between female and male in SMEs involvement. Similarly, the findings also reveal that there is almost equal distribution of SME entrepreneurs' in terms of marital status of 28.1% were single, 31% married. There is unequal distribution between those who had attained high level, from KCSE and above (66.6%), and those who low level of education; vocational training and below (34.2%). In terms of entrepreneur training the majority 59% had not received any entrepreneurial training whereas 41% had received training. This implies majority of SMEs were untrained and rely on their own skills which can have a negative impact on SMEs performance.

The findings reveal that majority of SMEs 69% are sole proprietors while 31% are in partnership most of the SME activities concentrate on service provision and manufacturing (55%) and 45% on trading.

The microfinance Credit factors comprise: credit amount; microfinance credit interest rate; collateral

requirement; credit repayment period; and entrepreneur orientation on SMEs Financial Performance.

A total of 76.7% respondents had acquired credit from microfinance institutions indicating that most of the SMEs are being supported by Microfinance Institutions. According to the results 64.3% of respondents agreed that the initial credit amount offered by the microfinance institution is adequate to implement the business ideas. A total of 52.4% agreed that the credit amount is adequate to promote business growth. This implies credit amount received by SMEs is adequate in promoting business growth. The findings revealed weak positive correlation between **Credit amount** and SMEs finance performance since the $r = 0.243$ and the p-value 0.000 is less than alpha 0.05. However, the regression analysis indicated the credit amount contributes 16.8% of the SME performance which was found to have statistical significant effect to SMEs financial performance. This concurs with Oleka, *et al* (2014) who argued that the loan size positively influence the growth of SMEs.

The findings from correlations revealed there is moderate positive correlation between **Interest rate** and SMEs finance performance since the $r = 0.482$ (which is approximately 0.5). The p-value is 0.000 is less than alpha 0.05. The results from the regression analysis indicate interest rate contributes 36.3% which was found to have statistical significant effect to SMEs financial performance. Similar views were observed by Heidhues (2005) who found out that access to credit allows SMEs to enhance their performance. However, from the descriptive analysis our study revealed an equal divide between respondents who agreed and those who disagreed that interest rate on loans does not significantly decrease the business cash flows and business financial costs which concurs with Accion, (2011) who pointed out that low interest rates lending by microfinance institutions may not be significant in SMEs financial performance. This means there is inconclusive findings on the effect of interest rates on SMEs financial performance.

The findings show that 62.3% agree that collateral value is key requirement for the business to qualify for the microfinance credit. The study established weak positive correlation between **collateral requirement** and SMEs finance performance since the $r = 0.341$. The p-value is 0.000 is less than alpha 0.05. This means the **collateral requirement** has statistical significant effect on SME financial performance. In addition, the results from the regression analysis indicate collateral requirement contributes 22.3% which was found to have statistical significant effect to SMEs financial

performance. This means the magnitude of the effect does not have a great impact on SMEs financial performance. This concurs with Ono & Uesuge (2005) who found that collateral have little impact on SMEs financial performance.

The majority of respondents 53.4% disagree that the credit repayment period is favorable to the business. Time for repayment of loans is inconclusive since there was an equal response of 50% each of the respondents who agreed and disagreed that the time given to repay the loan does not negatively influence the business cash flow.

There is weak negative correlation between **Credit repayment period** and SMEs finance performance since the $r = -0.102$. The p-value is 0.140 is greater than alpha 0.05. This means the **Credit repayment period** has no statistical significant effect on SME financial performance. From the regression analysis, the credit repayment period contributes -0.088 (8.8%) to SMEs financial performance. These results indicated that **Credit repayment period** had no statistical significant effect on SMEs financial performance since the p-value 0.073 is greater than alpha 0.05. This would imply the credit repayment period negatively affected the SMEs financial performance by causing a decrease of 8.8%.

A total of 94.8% respondents agree that they usually develop new business strategies in order to compete in the market. The study established that 89.6% have a vision to invest into new unknown markets meaning they are ready to take risks and are therefore innovative. The results from the correlations established moderate positive correlation between **entrepreneur orientation** and SMEs finance performance, since the $r = 0.539$ and p-value is 0.000 is less than alpha 0.05. Similarly regression analysis results indicate orientation entrepreneurship contributes 40.2% of the SMEs financial performance which was found to have statistical significant effect since the p-value 0.000 is less than alpha 0.05. This implies that most of the SMEs entrepreneurs are innovative, take risks by venturing into new business activities and are proactive which is also supported by the descriptive statistics.

CONCLUSIONS AND RECOMMENDATIONS

The findings based on gender indicate that there was almost equal distribution between female and male in SMEs involvement. The study also established unequal distribution between those who had attained high level, from KCSE and above (66.6%), and those who low level of education; vocational training and below (34.2%). In terms of entrepreneur training the majority 59% had not received any entrepreneurial training

whereas 41% had received training. This implies majority of SMEs were untrained and rely on their own skills which has a negative impact on SMEs performance. In addition, the findings reveal majority of SMEs 69% are sole proprietors while 31% are in partnership.

The microfinance Credit factors comprise: credit amount; microfinance credit interest rate; collateral requirement; credit repayment period; and entrepreneur orientation on SMEs Financial Performance.

The study established that credit amount received by SMEs is adequate in promoting business growth and has statistical significant effect to SMEs financial performance.

A total of 76.7% respondents had acquired credit from microfinance institutions indicating that most of the SMEs are being supported by Microfinance Institutions. According to the results 64.3% of respondents agreed that the initial credit amount offered by the microfinance institution is adequate to implement the business ideas. A total of 52.4% agreed that the credit amount is adequate to promote business growth

The findings revealed weak positive correlation between **Credit amount** and SMEs finance performance since the $r = 0.243$ and the p-value 0.000 is less than alpha 0.05. However, the regression analysis indicated the credit amount contributes 16.8% of the SME performance which was found to.

Based on interest rates, there was an equal response between respondents who agreed and those who disagreed that interest rate on loans does not significantly decrease the business cash flows and business financial costs. The findings are therefore inconclusive. However, from correlations there was moderate positive correlation between **Interest rate** and SMEs finance performance since the $r = 0.482$ (which is approximately 0.5). The p-value is 0.000 is less than alpha 0.05. The results from the regression analysis indicate interest rate contributes 36.3% which was found to have statistical significant effect to SMEs financial performance.

The study further established that **collateral requirement** had statistical significant effect on SME financial performance. Majority of the respondents 62.3% agree that collateral value is key requirement for the business to qualify for the microfinance credit. The study established weak positive correlation between **collateral requirement** and SMEs finance performance since the $r = 0.341$. The p-value is 0.000 is less than

alpha 0.05. Similarly, the findings from hypothesis test using regression indicate collateral requirement contributes 22.3% which was found to have statistical significant effect to SMEs financial performance.

The study established that the credit repayment period did not have statistical significant effect and had contributed negatively to SME financial performance. This is supported by majority of respondents 53.4% who disagreed that the credit repayment period is favorable to the business. Time for repayment of loans was inconclusive since there was an equal response of 50% each of the respondents who agreed and disagreed that the time given to repay the loan does not negatively influence the business cash flow. In addition, the study established weak negative correlation between **Credit repayment period** and SMEs financial performance since the $r = -0.102$. The p-value is 0.140 is greater than alpha 0.05. This means the **Credit repayment period** has no statistical significant effect on SME financial performance. From the regression analysis the credit repayment period contributes -0.088 (8.8%) to SMEs financial performance. This would imply the credit repayment period negatively affected the SMEs financial performance by causing a decrease of 8.8%. However the p-value 0.073 is greater than alpha 0.05 which indicates that **Credit repayment period** had no statistical significant effect on SMEs financial performance.

The study established that entrepreneurial orientation had positive effect on SMEs financial performance. A total of 94.8% respondents agree that they usually develop new business strategies in order to compete in the market. The study findings also established that 89.6% have a vision to invest into new unknown markets meaning they are ready to take risks and are therefore innovative. The results from the correlations established moderate positive correlation between **entrepreneur orientation** and SMEs financial performance, since the $r = 0.539$ and p-value is 0.000 is less than alpha 0.05. Similarly, regression analysis results indicate orientation entrepreneurship contributes 40.2% of the SMEs financial performance which was found to have statistical significant effect since the p-value 0.000 is less than alpha 0.05. This implies that most of the SMEs entrepreneurs are innovative, take risks by venturing into new business activities and are proactive which is also supported by the descriptive statistics. This concurs with Augusto et al, (2014) who observed that EO improved performance of SMEs.

CONCLUSION

The study reveals that microfinance credit factors namely: credit amount; interest rate; collateral requirement; and entrepreneur orientation had a positive effect on SMEs financial performance. However, the credit repayment period factor was established to have negatively affected the SMEs financial performance. The hypothesis testing showed the regression analysis test having p-values of 0.000 each for credit amount, interest rate, collateral requirement, and entrepreneur orientation indicating that they significantly influenced SMEs financial performance. The p-value of 0.073 for the credit repayment period showed non-statistical significant effect on SMEs financial performance.

The study also concludes that microfinance credit factors affect SMEs financial performance with entrepreneur orientation contributing the most (40.2%) to SMEs financial performance compared to the other factors. This implies that most of the SMEs entrepreneurs are innovative, take risks by venturing into new business activities and are proactive.

There were inconclusive findings on whether the time given to repay the loan influences the business cash flow and also on whether interest rates on loans significantly decrease the business cash flows and business financial costs. Further studies would need to be carried out to establish this as they are important factors in the financial performance of SMEs.

RECOMMENDATIONS

Based on the conclusions, the study recommends the following: The microfinance institutions consider entrepreneur orientation training while disbursing credit. The trainings should target SME entrepreneurs who do not have entrepreneurial skills and should help the SMEs not only in the process of setting up new businesses, but also acquaint them with skills to identify new marketing possibilities including familiarizing them on the various statutory requirements such as Income Tax, VAT etc.

The study focused on the effect of microfinance credit factors (credit amount, interest rate, collateral requirement, credit repayment period and entrepreneur orientation) on SMEs financial performance. The key shortcomings while conducting the study was time limitation, delayed responses and inadequate finances. The target population of the study was limited to SME owners within Nairobi county. This study would have been carried across the whole country because SMEs are spread throughout the country.

The study recommended the following areas for further research given their inconclusive findings namely: Effect of credit repayment period on SMEs financial performance; and Effect of credit interest rates on business cash flows and business financial costs. The study also recommends the need to conduct further studies countrywide to establish commonalities and differences in the effect of microfinance credit on SMEs financial performance in order to generalize the findings. The findings cannot be generalized using Nairobi only. In addition, the study recommends that further similar studies among larger enterprises be conducted in order to find out the effect of credit on performance of these businesses. This would contribute to the body of knowledge since that knowledge is missing.

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