

**CHALLENGES FACING THE GROWTH AND INNOVATION OF SMEs WHEN
ACCESSING MICROFINANCE CREDIT FACILITIES: CASE STUDY OF NAIROBI
CENTRAL BUSINESS DISTRICT.**

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DECLARATION

I declare that this research project is my original work and has not been earlier on submitted and approved for a degree by this or any other college or university. To the best of my understanding, this project contains no work published or written previously by someone else aside from where there is reference in the project itself.

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ACRONYMS AND ABBREVIATIONS

CBD	Central Business District
CFPR	Challenging the Frontiers of Poverty Reduction
GDP	Gross Domestic Product
KEPSA	Kenya Private Sector Alliance
KNBS	Kenya National Bureau of Statistics
MFI	Microfinance Institution
MSE	Micro and Small Enterprises
MSMEs	Micro Small and Medium Enterprises
SMEs	Small and Medium Enterprises

DEDICATION

I dedicate this project to my family for showing me immense support and love towards my education and throughout this project. May the Lord bless you for believing in me and may he be your rare guard.

ACKNOWLEDGEMENTS

I am grateful to God for his favor and enabling me to conclude my project. I recognize and appreciate the support and counsel of my supervisor, Mr. Albert Ochieng who made time to look at my drafts and giving me corrections and was available whenever I needed to see him. This project would not have been completed without his help.

I would also like to pay tribute to my parents and express my gratitude for their loyalty throughout the course of my education.

ABSTRACT

The objectives of this study were to determine whether SMEs in Nairobi CBD seek credit from microfinance institutions and to find out factors that limit SMEs in Nairobi CBD access to credit from microfinance institutions. This study used a structured questionnaire to collect data from 100 SME owners with businesses in Nairobi CBD who were chosen using purposive sampling. Data was analyzed using Excel and quantitative data was presented in pie charts and bar graphs. In the study it was established that there are various factors that affect access to credit by SMEs which include training, saving, innovation and growth. Challenges that SMEs faced were high interest rates, long duration of loan approvals, lack of space to operate in and market exposure and lack of grace periods accompanied by short repayment periods. It was recommended that microfinance institutions should increase number of savings accounts held by SMEs, financial institutions to act as role models to SMEs, government should encourage innovation and interest rates on credit facilities to be reduced to accommodate SMEs.

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CHAPTER ONE

INTRODUCTION

1.1 Background of Study

Small and medium enterprises are independent businesses that come from diverse industries and are grouped depending on the number of employees they have. They operate mostly in the manufacturing; innovation through changing of product designs to more recyclable and reusable products and use of renewable and cheaper raw materials as described by (Robinson, 2019), goods and service sectors as seen around the world (Ward, 2019). SMEs in Kenya were boosted by the establishment of KEPSA in 2003. In Kenya, Micro-enterprises have maximum number of 10 employees, small enterprises have approximately 10 to 50 employees and medium enterprises have approximately 50 to 100 employees as explained by (Review, 2017). SMEs account for the significant growth of Kenya's GDP, form majority of businesses across many sectors and create employment and wealth in the country. They are mostly considered risky and a large number do not survive five years which leads to a concern on sustainability in the sector KNBS (2017).

A report of the Central Bank of Kenya indicated that almost 98% of businesses constituted of SMEs who created 30% of jobs in the country. Interest rate capping was introduced with the intention of lowering the cost of credit while increasing access for businesses but recently there has been debate on whether it has made economy better or worse. It is hurting low-income earners and restraining their access to finances and minimizing transparency of prices (Ngunjiri, 2018).

Most SMEs have a vision of growth for the future and are very innovative while others seek revenue and market size. According to (Khin, Poorangi, & Kardevani, 2013) SMEs have turned to innovation in order to keep up with the business environment which is faced with tough competition without regard for size of the organisation or scope of operations. Senge and Carstedt (2001) argued that innovation was used to address challenges SMEs face in the competitive environment and sustain growth of organisations.

Schumpeter (1942) explained in his theory that innovation was a way to create wealth by distorting the market structures that existed through introduction of new ways to do things, new products and services that allows movement of resources from existing firms to new firms and therefore development of new firms. However, small businesses will achieve success, growth

and survival when they are innovative. In Kenya, SMEs are hindered from growth by several challenges such as poor infrastructure, inadequate capital, limited capital access, change in technology, corruption all of which can be minimized by adopting innovation as argued by Wanjohi (2009).

Microfinance is a service provided to the low-income earners or group that do not have access to conventional banking or financial services. Robinson (1998) defined microfinance as a means of growth that provides financial products and services like small loans and savings accounts to aid the poor in developing their companies. Microfinance is typically employed in developing countries where there is limited access to financial support. In Kenya, some of the credit providers include microfinance institutions, cooperatives, credit unions and banks, non-governmental organizations and non-banking financial institutions who target self-employed entrepreneurs and low-income earners.

The concept of group lending in microfinance is where many entrepreneurs come together and provide collateral in order to get a loan. This group may be referred to as a solidarity group who urge each other to repay the loan. Their motivation to repay back the loan may depend on peer pressure where other members of the group should make up for the payment if one group member defaults. Therefore, this research seeks to investigate the challenges that hinder growth and innovation of SMEs when accessing microfinance.

The study will be executed in the Central Business District in Nairobi because there so many businesses situated here which are formal and informal and there is a large population of SMEs who drive business in the capital city.

1.2 Problem Statement

Interventions have been done that target the informal economy especially in Kenya in order to solve various challenges being faced. Many formal financial institutions do not consider doing business with SMEs because they are assumed to be high-risk clients (Shane, 2013). In a report by (BioInnovate, 2019), data provided by World Bank Group showed that MSMEs have driven growth in Sub Saharan Africa accounting for up to 90 percent of businesses despite access to credit from financial institutions being one of the main problems hindering SME growth. According to reports by the KNBS, MSMEs account for up to 75% of all ventures in Kenya and create 30% of jobs. The concept of business growth has been an interesting subject in Kenya where the government is intervening to support SMEs in order to provide jobs to the youth.

Various studies have been conducted by researchers relating microfinance to SMEs, however, there exists a gap in these studies that was not taken into consideration. Makorere (2014) did a study on the role of microfinance in benefiting SMEs in Tanzania by SMEs that had received financial credit and it was revealed that problems faced by them were related to macro-economic institutional constraints rather than micro financial. Ruth & Jagongo (2018) organized a study on microfinance and financial performance of SMEs of youth SMEs in Kisumu and revealed that selected microfinance services such as accessibility to credit, role modelling and training on financial skills influenced financial performance of SMEs. Okello (2010) in his study on factors impacting growth of SMEs owned and managed by youth in Rachuonyo, it was revealed that youth who owned small enterprises perform poorly due to challenges of accessing business finance.

It is evident that there is a gap in research after looking at the studies above. The researcher therefore, came to an understanding that there is a need to find out the challenges that face SMEs in Kenya as there are limited studies that look into those challenges. This study looks to examine the research gap when it comes to microfinance and specifically the challenges that mostly affect the growth and innovation of SMEs and possibly some solutions.

1.3 Research Objectives

- 1) To determine whether SMEs in Nairobi CBD seek credit from microfinance institutions.
- 2) To find out factors that limit SMEs in Nairobi CBD access to credit from microfinance institutions.

1.4 Research Questions

- 1) Do SMEs in Nairobi CBD seek credit from microfinance institutions?
- 2) What are the factors that limit SMEs in Nairobi CBD access to credit from microfinance institutions?

1.5 Significance of the Study

This study will be used to increase the depth of knowledge on the challenges that face growth and innovation of SMEs when accessing microfinance. It is supposed to shed more light on the microfinance credit in relation to growth and innovation of SMEs.

1.5.1 Microfinance institutions

It would also provide insight to microfinance institutions on the degree to which their credit affects small and medium businesses. For microfinance institutions, it will help them come up with more business ideas, embrace technological improvement while also improving their service delivery.

1.5.2 Small and Medium Enterprises

For SMEs, it will help highlight on various forms of credit not known to them and how it can be of use to them and provide a framework that will help investors make sound decisions in their decision making process in the respective sectors.

1.5.3 Researchers

It would provide a basis of reference upon which further studies can be carried out on matters microcredit financing. It would be important to other researchers who may find it useful in providing information on SME microcredit financing.

1.5.4 Government

This study would also be useful in helping policy-making by the government on matters financing SMEs through microfinance institutions.

1.6 Scope of the Study

This study will focus mainly on the challenges facing growth and innovation of SMEs when accessing microfinance credit facilities. This study will be based on a sample that will be representative of the population of SMEs in the Central Business District in Nairobi. The information will be gotten from owners or managers of the businesses. The time frame for data to be collected will be between the months of August and October 2019 after which analysis will be done through November 2019.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter will focus on the literature review of the topic above. The chapter entails section 2.2 which describes the theoretical foundation, section 2.3 which entails the empirical literature review, section 2.4 which explains the research gap and section 2.5 which details the summary of the chapter.

In looking at the theoretical foundation of microfinance, the researcher searched for the theories which would explain why SMEs go for microfinance institutions in search of credit. He used various search engines and databases while searching for several theories that may interrelate microfinances and SMEs. He decided to use Google scholar as his main search engine for looking into the theories. The researcher was limited to studies done and published in the past decade; that is from 2010 to 2018. With this, the researcher was able to get information on the theories from various journal articles written in the recent past not exceeding ten years. The researcher then went ahead and identified the key theories that were used by the researchers and the criticisms associated with the theories.

2.2 Theoretical Foundation

2.2.1 Pecking Order Theory

This theory was first brought up and suggested in 1961 by Donaldson. It was then modified and made known to many by Myers and Majluf in (1984) who explained that companies will often look at various priorities when financing their company in order to bring profit. They explained that companies will often prefer internal financing before looking at external financing opportunities. Businesses will often go with internal funding as the first choice of financing then when it is not enough, they will look at financing through issuing of debt then equity as the third and final choice. Looking at previous research articles, in table 2.1 below, that have been done, the researcher opted to use this theory because it has been employed several times by other authors.

This theory is criticized by (Khan & Butt, 2013) who explain that it does not include effects of tax, agency costs or the financial problem of an investment opportunity. They also critic this theory explaining that it misses out on the decision making problems of financial managers who slack in their financial duties and are sheltered by market discipline.

2.2.2 Poverty Alleviation Theory

Abject poverty as described by the United Nations (1995) is where individuals and households suffer due to extreme deprivation of basic needs and services. As recently as last year it was estimated that half of the world's nations have destitution rates under 3% but the levels of poverty are still very high as stated by (Bank, 2018).

According to (Alvarez & Jay, 2013), they explain that opportunities that are available to the poor with certain kinds of financial and human capital as well as rights to property are not those kinds of opportunities that may prompt development in the economy and creation of jobs, which has led to entrepreneurship failing to alleviate poverty. The researcher used this theory because as identified in the table 2.1 below, several authors in their previous research articles used it to explain why SME owners' use microfinance services.

Alvarez and Jay (2013) also explain that entrepreneurs in poor settings can benefit when they understand that not all opportunities have same potential of creating wealth.

2.3 Empirical Literature review

Many researches have been conducted in regards to the role of MFI on the growth of SMEs. These researches have been conducted locally and internationally with varied results and outcomes.

2.3.1 Global Empirical review

There have been a couple of global studies done on this topic.

A study was conducted by (Mahmuda, Baskaran, & Jatin, 2014) to look at financing social innovation for poverty reduction in Bangladesh. They employed use of interviews and surveys to collect data from beneficiaries and households respectively. They noted that there was poverty reduction and improved quality of life for those who showed interest in their enterprises, motivated and had demonstrated proper planning while those who demonstrated lack of training, hard work, motivation and proper planning failed to curb poverty effectively than others.

They all recommended that the unsuccessful members should not be excluded but provided with focused training and more motivation that would help them build their self-confidence and capabilities that would help them understand their shortcomings. They iterated that if an integrated approach was applied to the CFPR programme when they are implemented, it would

help foster grassroots innovations that would solve local problems and help overcome lack of financial and available to grassroots innovators.

Taiwo (2016) did a study on the degree to which small enterprise have gained from credit form microfinance institutions while looking at the role of MFI and banks on SMEs. The researcher conducted interviews to gain primary data from small businesses across Lagos and analysed them in tables. (Taiwo, 2016) noted that both financial and non-monetary services given by microfinance institutions and banks has incredibly aided SMEs in Nigeria and has amplified the spread of business skills and brainstorming of innovative ideas while reducing the resource gap for these enterprises. The researcher recommended that training on credit maximisation should be accorded by MFIs to support the customers while the government should encourage microfinance banks to support SMEs.

2.3.2 Regional Empirical Review

Azeref and Gelagil (2018) conducted a study to examine the role of financial institutions on the growth of SMEs in Ethiopia. They employed a questionnaire to obtain first-hand data while using both quantitative and qualitative methods to gather and analyse the data collected. (Azeref & Gelagil, 2018) identified that there was a notable influence and effective relationship of lower borrowing cost, saving account and size of the loan on the growth of SMEs. It was also revealed that loan duration, criteria simplicity, follow ups and supervision had positive relationship but relative insignificance on the growth of SMEs. They recommended that financial institutions lower the borrowing cost of credit facilities, government make credit available and economical to SMEs and training mechanisms be set up for SMEs before and after the loan.

Makorere (2014) undertook a study to look at the role of microfinance in promoting small and medium enterprises in Tanzania. He utilized a questionnaire to gather primary data while employing secondary data to back up the primary data. It was also revealed by (Makorere, 2014) that an increase in employment of labour, business profits, sales volumes and outlets were impacted by adequate access to microfinance. However, there was no direct connection between increased capital structure and access to microfinance. It was also noted that SME entrepreneurs who received fair interest rate, business training, tax exemption and fair repayment periods functioned better than those who didn't. It was recommended that an integrative methodology should be taken to manage credit by giving close attention to macroeconomic, microcredit and constraining factors.

2.3.3 Local Empirical Review

Munene (2014) administered a study to examine the role of MFIs on growth of MSE in Thika. Both primary and secondary sources were utilized to collect data through use of questionnaires and interviews and was later analysed by use of descriptive statistics. In his study, (Munene, 2014) found out that microfinance institutions' services had contributed to rapid growth of MSEs over the years and people preferred to save for future expansion and business growth. There were challenges such as high default rate while people preferred microfinance institutions as the second financing option. Recommendations were that government need to set essential policies that improve loan amounts and repayment periods.

Omondi and Jagongo (2018) sought to examine the influence of microfinance services on the financial performance of SMEs in Kisumu. Structured questionnaire was utilized in the collection of first hand data while using descriptive statistics to analyse the data. They both established that some services offered by microfinances influenced monetary performance of SMEs while there was credit access by SMEs which helped them get financial skills training and saving s mobilizations. It was recommended that microfinance institutions need to create awareness for services they offer and how it can help them succeed. Microfinance institutions also need to train SME entrepreneurs on management skills before giving them any more credit support.

Table 2.1. Summary of Articles used in Theoretical Foundation and Empirical Review that relate Microfinance to SMEs.

AUTHOR AND YEAR	TITLE OF ARTICLE AND YEAR	THEORY(S) USED	METHODS OF DATA COLLECTION	FINDINGS
Jayati Ghosh (2013)	Microfinance and the Challenge of Financial Inclusion for development	Poverty Reduction	Observation Interviews	Profit-driven microfinance institutions are difficult must be regulated and subsidised.
Susanna Khavul (2010)	Microfinance: Creating Opportunities for the Poor?	Women Empowerment Poverty Reduction	In-person Survey Interviews In-depth case comparisons Observation	Microfinance is an instrument for eliminating poverty and it has the appeal to bring financial power to those who need it.
Joyce Sidimu Atsede Woldie John Mwita (2012)	Challenges of Microfinance Accessibility by SMEs n Tanzania	Capital Constraint Model Lending Behaviour Model Bank Capital Channel Model	Semi-structured questionnaires Focus groups	The economic sector has failed to properly expand microfinance services to SMEs because high transaction costs, absence of collaterals, insufficient ability to creating and managing profitable projects.

Robert Makorere (2014)	The role of microfinancing in promoting small and medium enterprises(SMEs) in Tanzania: empirical evidence from SMEs holder who have received microcredit	Pecking order theory Tax shield Trade- off theory Signalling Model	Structured questionnaire	An increase in employment of labour, business profits, sales volumes and outlets were impacted by adequate access to microfinance.
Paul Munene (2014)	The Role of Microfinance Institutions to the Growth of Micro and Small Enterprises (MSE) in Thika, Kenya (Empirical Review of NonFinancial Factors)	Labour Surplus Theory Schumpeterian Growth Theory	Structured questionnaires	Microfinance institutions' services had contributed to rapid growth of MSEs over the years and people preferred to save for future expansion and business growth.
Ruth Omondi Dr. Jagongo (2018)	Micro-Finance Services and Financial Performance of Small and Medium Enterprises of Youth SMEs in Kisumu County, Kenya	Women Empowerment Theory Game Theory	Structured questionnaires	Some services offered by microfinances influenced monetary performance of SMEs while other credit facilities helped them get financial skills training and savings mobilizations.

		Financial Sustainability Theory Poverty Reduction		
George Anane Patrick Cobbinah Job Kwame (2013)	Sustainability of small and medium scale enterprises in Rural Ghana: The role of microfinance institutions	Financial Sustainability Poverty Reduction Women Empowerment	Surveys Interviews	Microfinance recipients are better off than those without microfinance facilities in regards to enhancing the SME operations, boosting yield and ensuring careful management of finances.
Ismat Mahmuda Angathevar Baskaran Jatin Pancholi (2014)	Financing Social innovation for poverty reduction: A case study of microfinancing and micro-enterprise development in Bangladesh	Women Empowerment Poverty Reduction	Triangulation method Direct observations Interviews Surveys	There was poverty reduction and improved quality of life for those who showed interest in their enterprises, motivated and had demonstrated proper planning while those who demonstrated lack of training, hard work, motivation and proper planning failed to curb poverty effectively than others.

Isaac Quaye Eugene Abrokwah Alfred Sarbah Joseph Osei (2014)	Bridging SME Financing Gap in Ghana: The Role of Microfinance Institution	Poverty Reduction	Questionnaires Field Surveys	There is SME financing gap and operations of MFI have positive impact on SMEs. MFIs have risk mitigation tools when granting loans including provision of collateral security.
Benjamin Otoo (2012)	<u>Micro-credit for micro-enterprise: A study of women “petty” traders in central region, Ghana</u>	Women Empowerment Poverty Reduction	In-depth questionnaires Questionnaires	Internal, socio-cultural and politically motivated constraints are the crucial moderating impacts on the capacity of women traders to obtain credit.
Abu Noruwa Emeka Ezike (2012)	The Role and Sustainability of Microfinance Banks in Reducing Poverty and Development of entrepreneurship in Urban and Rural areas in Nigeria	Poverty alleviation	Structured questionnaires	There were high loan non-remittance rates among SMEs which posed consequences for MF banks. Challenges facing microfinance banks were false data, credit applicant’s identity and documentation of credit process

Taiwo JN Onasanya Yewande Edwin Agwu Benson KN (2016)	The Role of Microfinance Institutions in Financing Small Businesses	Pecking Theory Bank Channel Model	Order Capital	Interview	Both financial and non-monetary services provided by microfinance institutions and banks has greatly assisted SMEs in Nigeria and has amplified the spread of business competence and sharing of creative ideas while reducing the resource gap for these enterprises.
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2.4 Research Gap

This study appreciates the scholarly efforts put in other studies that had been undertaken previously related to the role and influence of microfinance institutions on the development of SMEs. However, it was noted that there was some missing information in these studies that will be addressed in this study. Most of the studies done in the articles mentioned in the table above have looked at the influence of MFIs on SMEs by (Omondi & Jagongo, 2018), (Munene, 2014; Makorere, 2014; Azeref and Gelagil, 2018) on the role of MFIs on growth of SMEs, (Mahmuda, Baskaran & Jatin, 2014) on financing of social innovation for poverty alleviation and factors influencing growth SMEs by Okello (2010), but have not looked at what are the actual challenges facing these SMEs in the Nairobi CBD from innovation and growth as also shown in the problem statement. This study therefore intends to look at this gap in research in view together with the problem statement explained above.

2.5 Summary of the Chapter

This chapter has looked at the theoretical foundations of the research study including the pecking order theory, women empowerment and poverty alleviation while also looking at the empirical review of existing research on the relationships between microfinance institutions and SMEs.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter will look at how the study will be undertaken with the main purpose being to get an understanding of the challenges facing SMEs in order to predict a solution for them. It highlights section 3.2 which describes research design, section 3.3 which details population of study, section 3.4 which details the sampling design, section 3.5 which describes the sample size, section 3.6 which describes data collection method, section 3.7 which describes data analysis and section 3.8 which details ethical considerations.

3.2 Research Design

A research design conforming to Bryman and Bell (2015), is a framework on how data is collected and analysed. A descriptive study as illustrated by (Cooper & Schindler, 2011) is concerned with looking at the relationship between variables or determining frequency with which something occurs. In this study, the researcher chose to apply descriptive research design so as to determine the challenges that SMEs in Nairobi CBD encounter when accessing microfinance services. This design will be aided by using the survey method where questionnaires and interviews (if necessary) will be used to get data. The use of questionnaires in this study by the researcher as the main tool of data collection is because it is free of interviewer bias, easy to analyse, fast results, inexpensive and anonymity of the respondent.

3.3 Population

In consonance with Cooper and Schindler (2011), a population is total sum of individuals or elements and from which inferences are made. The study's target population is the over 103,000 registered and licensed SMEs who operate in Nairobi County as at 2017 and illustrated in Appendix III.

3.4 Sampling Design

It involves selecting elements from a population that represents a sample of the population as described by Cooper and Schindler (2014). The researcher decided to focus on SMEs in Nairobi County Central Business District that had been registered by the county. This study employed purposive sampling where the researcher targeted people believed to be reliable for the study, could provide information necessary and conform to the researcher's criteria. The merits of purposive sampling are that it provides justification to make a general statement from the sample, it can help save time and cost as it is adaptive and flexible while also looking at the

niche demographics therefore involving everyone in the population of study. However, it also has its demerits such as its proneness to researcher bias as it relies on researcher's judgement, respondents can manipulate the data being collected and it can be ineffective on a large population. Since availability will be based on convenience, it will be less costly and less time consuming.

3.5 Sample Size

A sample size is a small group which is gotten from a population for research purposes. The sample size to be reviewed in this research, in order to acquire a wider blueprint and broad knowledge, is a representative sample of 100 respondents of the SMEs in the informal sector, general trade, wholesale, retail, stores and transport services which amounts to over 15,000 SMEs being targeted in the Central Business District as sourced from Nairobi City Licensing Department (2017). This sample size was calculated using Yamane (1967) method illustrated as: $n = \frac{N}{1+N(e^2)}$; with n being the sample size, e being the error margin and N being the population. Therefore, $n = \frac{15000}{1+15000(0.1^2)}$; with 10% margin of error, n= 100 respondents.

Table 3.1 SME Categories, Number in Central Business District

Category of SME	Population in CBD
General Trade, Wholesale, Retails, Stores	11,353
Agriculture and Natural Resources	1,025
Catering and Accommodation	1,750
Informal Sector	254
Transport, Storage and Communication	1,200
Industrial Plants, Factories and Workshops	1,342
Professional Services	3,242
Private Education and Entertainment	934
TOTAL	21,100

Origin: Nairobi County, Licensing Department (2017)

3.6 Data Collection

According to Robson (2011), he states that this process commences with descriptive observation where the researcher focuses on observing the physical surrounding, expounding on the key sources, particular events and their sequences then later writing down a narrative account Saunders (2015). The researcher chose to employ a questionnaire as the focal means

of primary data collection that would be self-administered to respondents. This questionnaire will employ both open and closed-ended questions to gain detailed answers and quantitative data relevant for the study. The questionnaire will be used in order to accomplish internal validity which refers to the questionnaire's capacity to gauge what researchers want to measure as explained by Saunders (2015). Open ended questionnaires help provide many possible answers as they have no limits, help collect more details on complex issues and helps in understanding respondents' point of view. This then helps get detailed answers. Closed ended questionnaires are easy to analyse as the answers are assigned values for statistical interpretation, they are more specific and take less time for the researcher and respondent thus higher response rate and it is easier to compare with other respondents. This therefore will help in getting quantitative data as there are specific values with answers that is required. This way of administering the questionnaire may help get a higher response rate. The cons using questionnaires include dishonesty of the respondents, unanswered questions, it is hard to convey respondent feelings, survey fatigue of the respondents as they participate in too many researches.

3.7 Data Analysis

According to (Gay, 1992) it was explained that analysis of data entails justifying and translating data so as to make meaning of respondent's interpretation of the setting while jotting down categories, regularities and patterns. Questionnaires from the field will be screened, grouped and numbered according to the respondent's sector of work. The questionnaires were checked for errors or omissions in data. The first research question was analysed by summing up the number of respondents and grouping them depending on their answers in order to calculate their percentages of the total responses in a tabular format. The second research question was analysed by looking at each factor that affected the SMEs individually from the questionnaire and used tabular format to present percentage of respondents that were affected as well as pie charts and graphs to look at general information of the respondents.

3.8 Ethical Consideration

Ethics are behaviour standards that guide a researcher's conduct which relates to the rights of participants and the accompanying norms as narrated by Saunders (2012). The ethical principles were explained in the book by Bryman and Bell (2011) and group into harm to participants, invasion of privacy, lack of informed consent and deception. In that respect, the researcher decided to adhere to them accordingly as laid out. The researcher will ensure that integrity will be enhanced in his research and that the research is independent and impartial to

any other. The researcher will be transparent and communicate on the purpose of the study with no hidden agendas, deception or misleading information to the participant. The researcher will request for consent and ensure that the participants in the research only participate voluntarily in the research process. Therefore, the researcher will respect and protect the privacy and confidentiality of the respondents during the research and avoid any harm towards them as per their wishes if they do not want to participate in the research study.

CHAPTER 4

DATA ANALYSIS AND INTERPRETATION

4.1 Introduction

This chapter will focus on analysis of data and presentation. It highlights section 4.2 describes the response rate, section 4.3 describes general information, section 4.4 details access to credit, section 4.5 details growth, section 4.6 describes business innovation, section 4.7 describes on training, section 4.8 describes saving culture and section 4.9 describes challenges facing SMEs.

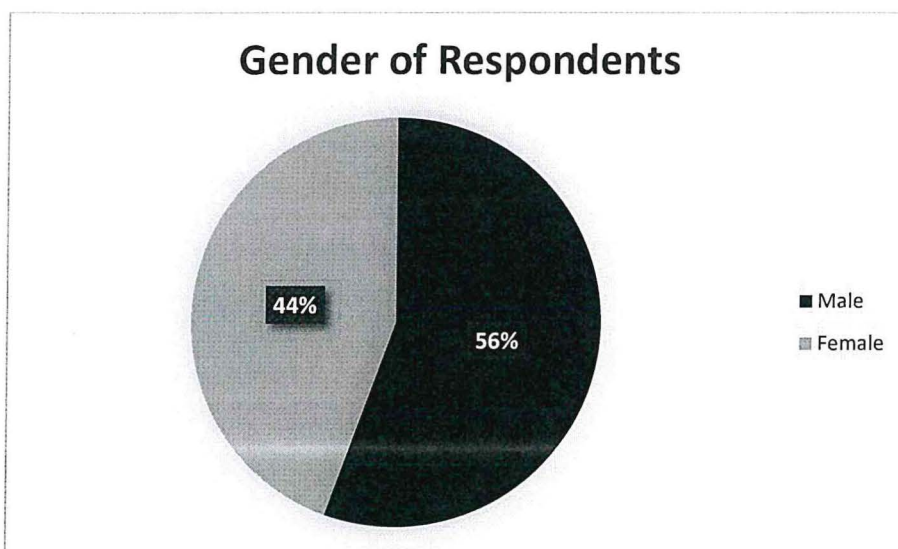
4.2 Response Rate

This research study focused on a sample size of 100 SMEs operating in the Nairobi CBD. The number of questionnaires that were distributed in the field were 100 with only 63 being returned back. This shows that there was a 63% response rate. This response rate is supported because whatever the response rate whether high or low, it does not provide unbiased estimates of the population but having more responses can sway results massively as explained by (Fosnacht, Howe, Sarraf, & Peck, 2017). Researchers should therefore focus on evaluating data they collect rather than fretting about having high response rates.

4.3 General Information

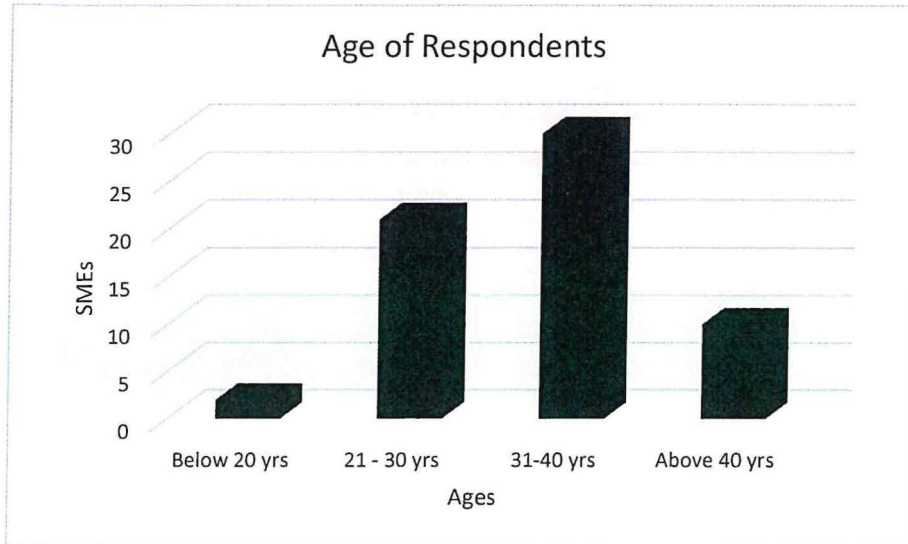
4.3.1 Gender

Data collected from the field indicated that most of the respondents were male at 56% with females being 44% as shown in figure 4.1 below. The female respondents were 28 while males were 35 respondents.



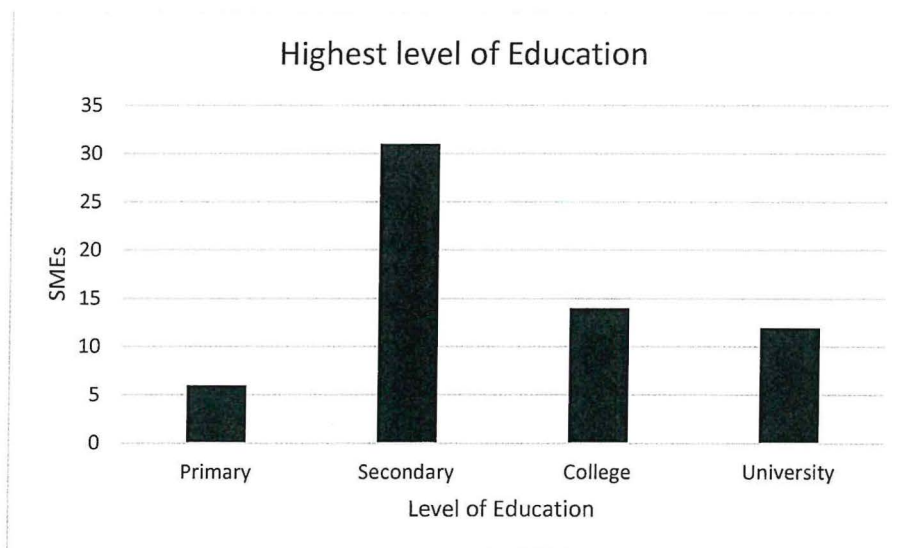
4.3.2 Age of respondents

The study conducted found out that majority of SMEs operating in the CBD were middle aged between 31-40 years. Two respondents were below 20 years, 21 were aged between 21-30, 30 were aged between 31-40 and 10 were aged above 40 years as shown in the graph below.



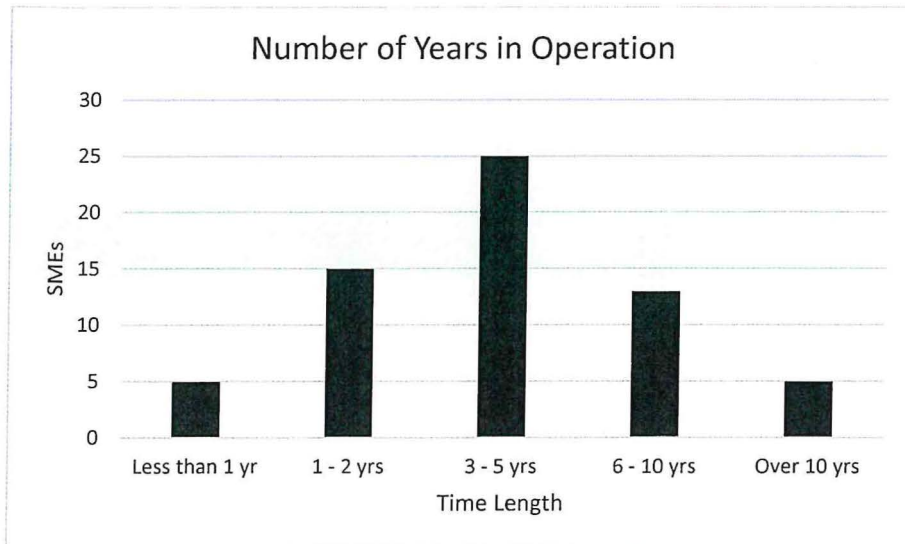
4.3.3 Level of Education

The study undertaken came to unravel that most of the SME owners who responded had completed up to secondary education with very few completing university level. 9.5% completed primary education, 49.2% completed secondary education, 22.22% completed college and 19.05% completed university education.



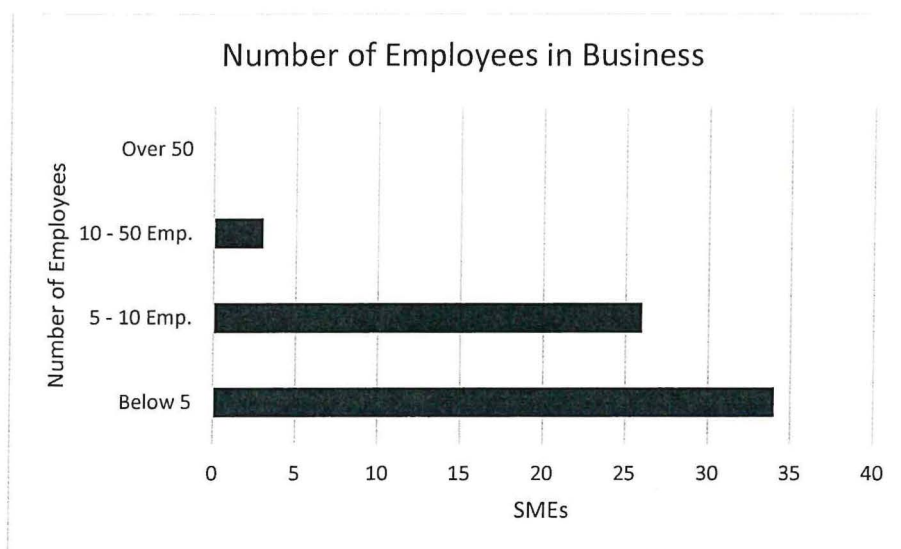
4.3.4 Number of Years in Operation

According to the study undertaken, majority of the businesses owned by SMEs had been established for 3-5 yrs. Out of the 63 enterprises being operated in the CBD, 5 businesses had operated for less than a year, 15 businesses for 1-2 years, 25 businesses for 3-5 years, 13 businesses for 13 years and 5 businesses for over 10 yrs. This showed most business were able to pass the initial stage of the business cycle.



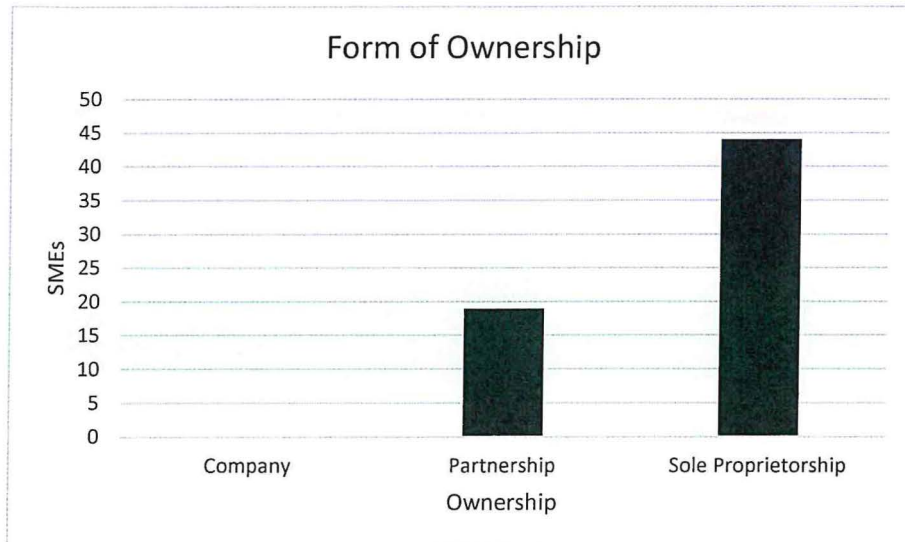
4.3.5 Number of Employees

According to the 63 businesses studied, 53.97% of them had less than 5 employees, 41.27% had 5-10 employees, 4.76% had 10-50 employees and none of them had over 50 employees. This indicated that majority of SMEs in Nairobi CBD had less than 5 employees.



4.3.6 Form of Ownership

Most of the businesses which participated in this study were found to be solely owned by the SME owners with 69.84 % being sole proprietorship, 30.16% being partnership and none of them were companies.



4.4 Access to Credit

SME Owners who borrow from MFIs

One of the main questions this study sought answers for was whether SMEs borrow from MFIs and it was revealed that all except for one SME had borrowed. This is shown in table 4.1 below. This indicates that majority of the enterprises in Nairobi CBD have sought credit facilities from MFIs. This has been because many MFIs have come up in the last 5 years and have offered opportunities for SME owners to access credit facilities

Have you ever borrowed from MFI?	Responses	Percentage
Yes	62	98.41%
No	1	1.59%

Table 4.1

Credit Secured in Full

According to responses from the field, 59 businesses secured loans that they asked for with only for SMEs not securing the loans. This indicated that majority of SMEs receive their credit in full. This shown in table 4.2 below.

Did you secure loan you asked for?	Responses	Percentage
Yes	59	93.65%
No	4	6.35

Table 4.2

Of all the SMEs who secured the loans they asked for, 2 SMEs did not receive the loans full amount they asked for because of reasons such as not having an ability to pay as explained to them by MFI agents. Ability to pay is where the gross profit of an SME owner's business will be able to facilitate the credit being asked for.

4.5 Growth

Business Financing

Financing of an enterprise can be done in many ways and this study was conducted to look at how SME owners finance their businesses. This study examined for 4 ways in which businesses are financed be it Personal Income, Business Income, Family and Friends or MFIs. It was revealed that majority of the businesses were financed using business income. Most of the SME owners preferred to employ a mix of ways to finance the business such as using Family and Friends and Personal Income or Business and Personal Income.

Growth of the Business

In looking at whether the business had accomplished growth in terms of Sales, Labour or Size, the study revealed that 88.89% of the businesses had grown with 11.11% having not grown at all. This is represented in the table 4.3 below.

Has the firm accomplished growth in terms of sales, labour or size?	Response	Percentage
Yes	56	88.89%
No	7	11.11%

Table 4.3

Success of the Business

There are many factors that can lead to the success of any business. In this study, respondents were quick to state that they achieved success due to a combination of factors. The factors being used in this study were technology, innovation of new products, diversification to new markets, access to loans and reinvesting of profits. Very few SME owners accredited their success to reinvesting of profits because most of their profits gotten are used for personal consumption. Majority of the respondents explained that technology, diversification and innovation were the main factors that lead to their businesses succeeding.

Effective use of Profits

Since most SMEs are start-ups that grow to become established, this study was done to see how the SMEs use their profits. They study looked at whether SMEs use their profits for saving, personal consumption, business expansion or working capital purposes. Majority of the SMEs used their profits on working capital for their business as well as personal consumption. Very few SMEs used their profit for expanding their business because they saw it as a huge risk because of fear of collapsing of their business in the future and since most of the operate in the informal sector, they explained that it would be difficult for them to recover.

4.6 Innovation

Businesses That Are Innovative

Introducing new ways to do things or rolling out new products or services in the market to create wealth explains innovation as described by Schumpeter (1942). This study looked to answer whether businesses are innovative and it was revealed that 71.43% of the businesses were innovative while 28.57% were not innovative. This is shown in table 4.4 below.

Is your Business Innovative?	Responses	Percentage
Yes	45	71.43%
No	18	28.57%

Table 4.4

Credit and Innovation

In answering whether borrowing of credit facilities encouraged innovation, the study showed that it was not a clear cut decision and the SME owners were split on whether credit was good

or bad for innovation with only one response breaking the tie in favour of credit facilities encouraging innovation. This was illustrated in table 4.5 below. Those against credit encouraging innovation cited some challenges which will be addressed later on.

Has credit encouraged innovation	Responses	Percentage
Yes	32	50.79%
No	31	49.21%

Table 4.5

4.7 Training on Management of Finances

Training of SME Owners

Another factor that this study examined was training and whether SME owners had undergone training on managing of finances. It was revealed that majority of the respondents had not undergone any sought of training whatsoever. This represented 73.02% of the respondents with only 26.98% have undergone some type of training as shown in table 4.6 below. This unfortunately, indicates that most SME owners are not trained on financial management skills.

Have you undergone training?	Responses	Percentage
Yes	17	26.98%
No	46	73.02%

Table 4.6

Payment of Training Services

The study looked to see whether individuals paid for training services. 10 of the respondents who had received training did not pay for their training while 7 of them paid for their training. This is illustrated in table 4.7 below. It was discovered that training had been offered as an initiative by other MFIs, banks, private individuals or schools.

Did you pay for training exercise?	Responses	Percentage
Yes	7	11.11%
No	56	88.89%

Table 4.7

Effect of Training On Growth of the Business

It was discovered in the study that of all those who had been trained, 15 of them believed that the training had helped their business grow while 2 of the respondents believed that it did not

help them at all. This indicates that being trained about financial management helped in business growth.

4.8 Saving Culture

Businesses with Savings Account

The study looked to discover whether businesses had savings account and it was found that 98.41% of businesses had savings account with only 1.59% not having savings accounts. This indicated that saving is critical for all SMEs in Nairobi CBD. Those who did not have explained that they did not have enough money to save.

Importance of Savings on Growth of Business

The study looked to see whether businesses had saved in the past year and whether it had helped the business and it was discovered that all 42 businesses that had saved in the year that passed had benefited from saving since uncertainties that came about later on were able to be tackled.

4.9 Challenges facing SMEs

Besides the four main factors that had been dealt with in the study, SME owners listed some challenges they faced when accessing microfinance credit facilities. Main challenge was high interest rates. They exclaimed that with time, they came to see that the interest they are paying for credit was increasing without regulation which reduced their gross profits significantly and therefore were not able to further some of their goals.

They faced was the long duration for loan approval and short loan repayment. The SME owners exclaimed that some of the loans they requested took too long (more than 24 hours) to be approved and later on did not serve a purpose when it arrives and therefore they would use it for personal consumption which would be difficult to pay later on instead of using it in the business to help bring in more money. They also exclaimed that they were being given too little time to pay back huge loans yet their businesses would take long to bring in profits that pay the loans. Most of the businesses were expected to pay back huge loans in 1 month yet they would only be able to pay it back in 2-3 months.

They also lack of space to run the business and exposure to the market. They explained that the government had allocated to them small areas to operate in yet they were crowded and many which made marketing their goods difficult and getting credit facilities difficult because they didn't have a stationary place to work.

They were not also able to achieve desired goal with loans they got. This is a challenge to them because some of them mismanaged funds and used them for other purposes rather than fund the business. Some of them diverted funds from their intended use in the business to other personal uses.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATION

5.1 Introduction

This chapter will look at an overview of research study. It highlights: 5.2: Summary and Discussion of Findings, 5.3: Conclusion, 5.4: Recommendations and lastly 5.5: Suggestions for further research.

5.2 Summary

The study discovered that when it comes to credit, most of the SMEs prefer microfinance institutions to banks and credit unions when borrowing credit facilities. This is because they are able to secure the loans they requested and in full amount.

The study discovered that when it comes to growth of the business, they finance their businesses using mostly personal income and family and friends support as start-ups but then employ use of business income much more as they grow. According to the findings, businesses credit their success to technology, innovation of new products and diversifying to new markets. The findings also show that businesses use their profits mostly on working capital and personal use.

The findings of the study show that more than 70% of the businesses are innovative even though business owners are divided on whether credit encourages businesses to become more enough with the additional financial resource.

The findings also established that majority of the businesses had not undergone any financial management training and therefore the owners would be prone to making mistakes when making financial decisions. It also showed that majority of those who received training did not pay but the training helped in growing their businesses.

The findings showed that having a savings account and using it helped businesses grow in the future with majority having saved in the year that passed with helped their businesses onwards.

5.3 Conclusion

It is evident that SMEs drive the economy for developing countries whether in the formal or informal sector. Success of these SMEs will improve the economic status of the country. Studies illustrated in the empirical review showed a gap in knowledge that formed the basis for this research. The study assessed SME owners in the Nairobi CBD who access credit facilities from MFIs. The findings showed that most of the challenges they face are related to MFIs and

not the macro environment. The research objectives were achieved and research questions answered accordingly. It was seen that over 98% of the respondents seek credit from microfinance institutions. The factors that limit SMEs from access to credit include lack of proper training on financial management, lack of having a culture of saving, lack of innovation to grow the business. Challenges the SMEs face include short repayment period, long duration of loan approval, high interest rates, lack of space to operate the business and inability to achieve desired goal of a loan.

5.3.1 Limitations of the Study

It was discovered that age, level of education and length of business being in operation were the most critical factors that SMEs were keen on when collecting data in the field. Most of the SMEs were very rude and did not entertain people using their information for research. Questionnaires that were not recovered was because of carelessness of the potential respondents and care free attitude of SMEs who were not keen on the importance of the research. It took a lot of time and energy to get answers from them as they would waste your time on purpose or out of suspicion. Availability of money to print more questionnaires after most of them were lost was difficult for the researcher to acquire. Most SMEs evade talking about money problems but are quick to talk about challenges they face when accessing it if you are able to help them overcome he challenge.

5.4 Recommendations

It was discovered that access to credit facilities was marred by high repayment cost by SMEs. It was therefore recommended that institutions that provide credit facilities should consider lowering their interest rates in order to encourage more borrowing by SMEs.

It was also discovered that majority of the SMEs were not trained on how to manage credit and finances. The researcher therefore recommended that the government and other financial institutions should support SMEs by allocating places that offer training services.

The researcher also recommended that microfinance institutions increase the number of saving accounts being held by SMEs because it has been seen that having a savings account acts as collateral for the business in the future.

The researcher would also like to recommend that financial institutions that offer credit facilities to act as role models who guide SMEs to succeed in their businesses.

The researcher also recommends that the Government should provide an environment that allows innovation to be implemented by SMEs for them to grow.

5.5 Suggestions for Further Research

The researcher suggests that further research be done to better understand whether there is a relation between education and success of the business.

The researcher also suggests that further research to be done to establish who SMEs prefer between banks and MFIs.

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APPENDICES

APPENDIX I: INTRODUCTORY LETTER

Dear Respondent,

RE: APPEAL FOR YOUR COOPERATION

I am a student studying Bachelor of Commerce, Finance specialisation at Strathmore University. So as to fulfil my degree requirements, I am taking on a research project on “Challenges Facing the Growth and Innovation of SMEs when accessing microfinance services: A Study of Nairobi Central Business District.”

You have been selected to be a part of this project and I am requesting for your participation. Please note that no answer is wrong and that report you provide will be useful for academic knowledge. Your response will be anonymous.

Thank you in advance.

Yours sincerely,

Isaac Kirimi.

APPENDIX II: QUESTIONNAIRE

Section A: Background Information

1. What is your gender

Male () Female ()

2. How old are you?

Below 20 yrs () 21-30 yrs () 31-40 yrs () Above 40 yrs ()

3. What is your highest education level?

a) Primary ()

b) Secondary ()

c) College ()

d) University ()

4. How long has your business been in operation?

a) Less than one year ()

b) 1-2 yrs ()

c) 3-5 yrs ()

d) 6-10 yrs ()

e) Over 10 yrs ()

5. How many employees are there in your business?

a) Below 5 ()

b) 5- 10 ()

c) 10-50 ()

d) Over 50 ()

6. What is the form of ownership of the business?

a) Company ()

b) Partnership ()

c) Sole proprietorship ()

d) Other (specify)

.....

Section B: Access to Credit

1. Have you ever borrowed a loan or credit facility from a microfinance institution?

Yes () No ()

2. If no, where have you borrowed from?

.....

3. Please indicate your opinion on the following statements relating to credit. **1= Strongly Disagree, 2= Disagree, 3= Neutral, 4= Agree, 5= Strongly Agree**

Statement	1	2	3	4	5
It is easy to access credit from micro-financial institutions					
My business relies on credit from microfinance institutions					
Credit financing has been beneficial to my business					

4. Did you secure the loan you asked for?

Yes () No ()

5. If yes, were you given the full amount? If no, explain why?

Yes ()

No ().....

6. In your opinion, what do you think should be done to overcome the challenges?

Section C: Growth

1. How do you finance your business?

- a) Personal Income () b) Business Income ()
- a) Microfinance loans () c) Friends and Family ()

2. Has your firm accomplished boost in term of sales, labour or size?

Yes () No ()

3. What accredited to the success?

- a) Technology ()
- b) Diversification to new markets ()
- c) Innovation of new products ()

- d) Access to loans ()
 - e) Re-investing profits ()
 - f) Other (specify)
-

4. How do you use your profits?

- a) Savings ()
 - b) Personal Consumption ()
 - c) Expansion of the business ()
 - d) Working capital ()
 - e) Other (specify)
-

Section D: Innovation

1. Is your business innovative?

Yes () No ()

2. Has credit encouraged innovation in your business?

Yes () No ()

Section E: Training

1. Have you undergone training?

Yes () No ()

2. Did you pay for training exercise?

Yes () No ()

3. Was the training helpful?

Yes () No ()

Section F: Saving Culture

1. Do you have a savings account?

Yes () No ()

2. Have you saved in the past year?

Yes () No ()

3. Has the savings helped your business?

Yes () No ()

APPENDIX III: LIST OF SME SECTORS IN NAIROBI

Category	No. of SMEs
Medium Trader Shop or Retail	16,804
Small Trader Shop or Retail	55,194
Small Transport Company	2,844
Petrol Filling	895
Storage Facility	945
Communications Company.	175
Small agric. Producer/Processor/Dealer	2,452
Medium Lodging with Bar or Restaurant	274
Small Lodging with Bar or Restaurant	236
Medium Lodging House	328
Small Lodging House Standard	415
Small Restaurant with Bar	956
Large Eating House Snack Bar; Tea House	612
Medium Eating House; Snack Bar; Tea House	1,054
Medium professional services business	508
Small professional services business	5,235
Medium financial services	512
Small financial services	478
Small private health centre	65
Doctor or Dentist	912
Small Entertainment Centre	75
Small Industrial Plant	704
Medium Workshop, Repair Service Contractor	3,124
Small Workshop, Repair Service Contractor	9,124
TOTAL	103,921

Origin: Nairobi County, Trade and Licensing Department

APPENDIX IV: SME CATEGORIES AND NUMBER IN CBD

Category of SME	Population in CBD
General Trade, Wholesale, Retails, Stores	11,353
Agriculture and Natural Resources	1,025
Catering and Accommodation	1,750
Informal Sector	254
Transport, Storage and Communication	1,200
Industrial Plants, Factories and Workshops	1,342
Professional Services	3,242
Private Education and Entertainment	934
TOTAL	21,100

Origin: Nairobi County, Licensing Department (2017)



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CHALLENGES FACING THE GROWTH AND INNOVATION OF SMEs WHEN
ACCESSING MICROFINANCE CREDIT FACILITIES: CASE STUDY OF NAIROBI
CENTRAL BUSINESS DISTRICT.

ALARIC ISAAC KIRIMI
ADMISSION NO. 095234

A Management Research Project Submitted to Strathmore University Business School
In Partial Fulfillment of the Requirements for the award of Degree of Bachelor of
Commerce of Strathmore University

DECEMBER, 2019