

**EFFECT OF MICROFINANCE FUNDING ON THE LIQUIDITY OF MICRO AND  
SMALL ENTERPRISES IN MADARAKA AREA**

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## DECLARATION

I Esther Njoroge declare this project as my own original work and that all the sources have been referenced and acknowledged. This document has not been previously presented for any award at any University to obtain an academic qualification.

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## **DEDICATION**

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## ABBREVIATIONS

AMFI-Association of Microfinance Institutions

ATM-Automated Teller Machine

CBK-Central Bank of Kenya

CBO-Community Based Organization

FBOS- Faith Based organizations

K-REP- Kenya Rural Enterprise Programme

KWFT- Kenya Women Microfinance Bank

MFI-Microfinance Finance Institutions

NGOS-Non Governmental Organizations

SME-Small and Medium Enterprises

## **ABSTRACT**

The title of this research is effect microfinance funding on the liquidity of micro and small business, a case study in Madaraka area. Microfinance is “the provision of financial services to low-income poor and very poor self-employed people”. Most businesses in Madaraka failed due to lack of insufficient capital to help them run their business. The main objective of the study was effect of Microfinance funding on the liquidity of micro and small businesses located in Madaraka area. It helped to understand how variables like loan interest, loan size, loan collateral, loan amount and loan disbursement affects the liquidity of businesses in Madaraka area. The micro and small business help in the creation of employment in the country y and the county in general. The specific objectives of the study include ascertaining the variables, such as loan interest, loan size, loan collateral, loan amount and loan disbursement on the effect of liquidity on small businesses in Madaraka area. The research problem was studied through the use of questionnaires. Out of the 1000 SMEs licensed, according to Nairobi city council records. This study randomly sampled 40 SME“s. The study found that there is a direct relationship of access to credit and financial performance of this enterprises. The study also concludes that the enterprises benefit from loans from microfinance institutions, the enterprises in Madaraka seek financial assistance from the MFIs due to interest rate, easy loan repayment and amount offered. It was recommended, in order to provide an enabling environment for SME“s to grow and thrive, therefore there is a need to develop strategies to enhance increased access to microfinance credit by small and medium enterprises from commercial banks and microfinance institutions.

## CHAPTER 1: INTRODUCTION

### 1.1. Background

In this generation, self-employment is the major impelling cause for economic growth, poverty alleviation and employment in African countries. This small business and/or self-employment have helped in accelerating growth and rapid industrialization. Micro and Small Businesses(MSBs)in Madaraka ward of Nairobi County have acted as a catalyst in the political and socio-economic development. Apart from creating employments and generating revenue, MSBs also help our economy in the creation of products and services and growth of skills. A research of Irene, Charles, & Japheth, (2015)on how the services of Microfinance affects the expansion of SMEs in Kenya found a positive correlation amongst growing MSBs and services offered by microfinance institution. The Kenya Government once committed in helping SMEs to grow and it appeared to be one of their key strategies in their 1980s report. It became a priority in the report for 1989. Vision 2030 had also emphasized the importance of Micro and Small Enterprises in Kenya. MSBs in Madaraka and in other parts of the country are considered of great importance since it will help a great deal in achieving vision 2030. Studies about growth, majority of them have been undertaken based on the law of Gibran's law. Gibran's law says that the size of a business, determines the firm's growing rate. Businesses has there for been categorized by different studies into three; small, medium and large. Other studies on growth have also used assorted ways to gage growth. Dobbs & Hamilton, (2007) laid out a framework of explaining how business grow. These enterprises have continued to act a major role in the economy of this country.

#### 1.1.1. Microfinance Service

Microfinance has been a get through for self-employed person and the SMEs since it offers financial services for individuals who are not able to access banking and related services. Microfinance offers a wide variety of services such as lending money for new businesses, the provision of small loans to poor clients; they help clients to learn how to save; micro insurance; and payment systems. Microfinance services are designed to be accessible and inexpensive for the poor and socially marginalized clients whereas banks their main focus is on big business. Microfinance helps people to secure them own future by ensuring they acquire and secure finances so as to level their expectations. This article researches on the impact of current microcredit

programme on how SMEs are performing in Zambia. It was found that, borrowers who took a second loan, they were a good change in the growth of their business compared to when they took their first loan. Borrowers who only took the first loan, they were a negative change in the performance of their business which made them worse off. Some researchers believed that loans enlarged the prospects and thus plays both fiscal and social roles hence refining the standard of living of the people. These upgrades in brief are there to help businesses grow and to eradicate poverty, and according to this project, it will be seen from the point of the development of small and medium size enterprises SMEs and focusing mostly in Madaraka ward in Nairobi area. Basically, the commercial banks their main target is not to the poor hence the MFIs are better since its target customers is everyone.

### **1.1.2. Liquidity of MSBs**

A firm's is said to be liquid when its able to run their day to day transaction when they fall due or in other words being able to manage their current assets. When Investing in current assets, it affects the business liquidity and profitability. A business is said to be more liquid if it has more current assets. This implies that a business is doing well and can be able to pay its debts. Liquidity is therefore the proportion of a firm's current assets as compared to current liabilities, which give rise to working capital. Liquidity management is being able to run your daily transaction by planning and controlling of cash flow by owner-managers. Most businesses, company's and firms' ability is measured by seeing if the firm is able to run their daily expenses using most of its cash. That is, the ease in which a business can pay its bills and liabilities over the next year. Current ratio and the quick ratio are the two easy way used to measure accounting liquidity. From the global perspective, reports have been carried out on various features of working capital management. Lazarus's & Tryfonidis, (2006) studied on the link between working capital and profitability of listed companies in the Athens Stock exchange and concluded that there is a statistically substantial no relationship between profitability, measured through gross operating profit and cash conversion cycle. Padachi (2006), in Mauritius did a research on the impact on accounts receivable days, accounts payable days, inventory days and cash conversion cycle on return on total assets and found out that a high investment in inventories and receivables is associated with lower profitability. Research into the effects of liquidity of the profitability of SMEs in Kenya has not been widely shepherded. First of all, this study aims to fill that gap in the literature, analyzing what the effect of liquidity on the profitability of Madaraka MSBs would be.

The choice of MSBs in Kenya as the subject of study is important reasons since MSBs in Kenya are relatively small enterprises, and are therefore reliable in dealing with the non-existence of studies about the effects of liquidity on their profitability in this type of service MSB; and ii) MSBs are vital drivers of Kenya's economy and thus the study of their liquidity capability its particularly relevant in order to suggest measures of economic policy to support this type of firms.

### **1.1.3. Loan repayment**

Loan repayment default are different depending on MFIs policy's. According to Pearson, Fund & Bureau, (2006), "loan repayment default is a risk presented to an institution by a borrower by failing to pay at least three instalments within a period of one month". This indicates that the borrower will not be able to pay and eventually fail to repay all the loan. Similarly, Phillips and Vander Hoff, (2004) cited in Woradithee (2011) definitions of loan repayment default as failure to repay the principal amount and/or interest by a borrower when the debt is due. This meant if an individual or a business failed to make an interest payment on loan borrowed at a specified time, then the person or business is at default. From a study, they concluded three dependent variables that were theorized to be of significance in determining loan reimbursement in microcredits. These were, Homogeneity of the borrower, transaction cost incurred by the borrower and threats of sanction by the program. Transaction cost faced by borrowers, for a borrower to access a loan, he or she may incur several types of transactions costs. Borrowers may be unwilling or unmotivated in paying back the loan if they incur a lot of costs when applying a loan or due to inefficiencies of delivery system of the lender, such as missed investment opportunity due to loan disbursement. Homogeneity of the borrower for example," a group of economically deprived individuals form a venture to get loan. The aim of the corporate venture was to help in eradication of poverty and to have access to large loans that makes these people overcome various hitches for cooperation. Thus, "homogeneity of preferences may help the group achieve high repayment rates." Usually an individual or a business at default is likely to lose any property presented as collateral. Loan repayment usually has a devastating effect on both the lender and the borrower. For the lender, he may incur straight losses and financial constraints due to the loan defaults. On the hand, the borrowers may not only lose their properties but also they won't be able to access future loans or borrow again. Business location, years in operation among others entails the characteristics of a business. Prime location leads to increase sales which in turn increases the revenue. Businesses located in prime areas tend to have high loan repayment than the ones not strategically located.

The ones located to town centres, they also have high loan repayment than otherwise. (Angaine & Waari 2014 cited in Nawai & Shariff (2017). The age of a business shows how long the business has been into existence and its experience in the market. Previous studies show that, businesses that have been in operation for less than a year are susceptible to low loan repayment compared to the one that have existed for more than a year, In Kenya.

#### **1.1.4. Loan interest**

The outstanding increase of interest rates in the early 1970s pushed many long term market rates on a prime credit. This history provides us with a long view, which shows that recent uttermost returns were far above long term rates provided in the States in 1800. When the banks and Microfinance came into existence, they have been high interest rates recently all over the world. Interest can either be categorized as long term or short term. Traditional finance theory claims that as the loan size grows, and due to increased risks associated with the loan, the lending rate on that loan will increase to adjust the rise of the risk associated with the loan. In spite of this, it was observed that, from the Barbadian banking industry data, the smaller the size of the loan, the more the interest rate was applied, and vice versa. Yet, some fixed data framework, of some research say that borrowers' eligibility for local banks and foreign banks operating characteristics are important in explaining interest rate differentials among size of the loan can be borrower's eligibility. The banks of Uganda, interest rate is a very significant factor. MFIs have been reported for exploiting customers by charging high interest rates. This led the government through the Ministry of Finance passing a Financial Institutions Act with an aim of helping and protecting the SMEs and the individuals involved. The Act levies interest rate ceilings on loan finance. A study published by the central bank shows that interest has led to the decline of accessibility of loans for SMEs. This is due to the Banking Amendment Act that came into plane in 2016 that had set a ceiling lending rate of not less than 4 percent above the central bank base rate. CBK had to effectively intervene due to the interest cap which led to the in the decline of credit to the private sector, a major factor in the performance of the economy. The factors that help MFIs determine the lending rate, are important to the public, the banking industry and to the policy maker. This interest rates have been a sensitive and recurring issue in Kenya, one which needs close examination. Factors such as cost, gender, rules and regulation, lending procedure, inflation and the kind of the organization affects microcredit interest rates. But the main factor that influences

microcredit interest rates is Operating expenses. Some findings show that MFIs tend to subsidize interest rates charged with income from investments not related to their lending.

#### **1.1.5. Loan collateral**

Collateral is a property that a lender takes as security from a borrower in case of loan default. It's a way for obtaining a loan for the borrower. Collateral helps to reduce loss to the lender if the borrower ends up not paying the loan. We have different types of collateral, such as; Cash secured loan –this is when a bank liquidates your accounts in order to recoup the borrowed money. Real estate-this is either one's home or lot parcel and once it's taken it cannot be returned. Invoice collateral- this collateral is mostly used by small business, wherein, invoices that are still unpaid are used as collateral. Blanket lien. –this is when a lender has a legal claim to dispose of the asset of a business that's in default. From a research in Nigeria, it states that depending on the loan size an individual or a small business wants to borrow, the loan size will determine if they are need for collateral or not. Hence they are loans that don't require collateral. The ones that you can borrow without collateral. First, we have unsecured loans, this type of loan does not assure the lender that the loan will be repaid, however they involve small loans. We also have online loans. In this type of loan, the applicant fills a form, and the lender will let the applicant know if it has been approved, the amount approved and how to repay back the loan. Loan collateral disadvantages the MSEs in that, some of the will be scared to take loan due to the fact that may lose whatever they secured to the lender if they dint end up paying. And also, SMEs who are just starting their business, may not have anything to secure for collateral, hence they may not be given a loan

#### **1.2. Statement of the problem**

The liquidity levels of MSBs in Madaraka ward of Nairobi county has been adversely affected by MFI loans and they also face many obstacles that limit their growth, long term survival and development. Being unable to get the loan required from the micro finance banks and these other lending institutions have a standardized way of assessing loan applicants which has been a great hindrance to the business in Madaraka ward, hence the SMEs in Madaraka have been deficient of capital. These MSBs are a presentation of important sectors in our life providing a creative source of self-employment, returns, wages and poverty alleviation. MSBs experience problems in gaining access to credit facilities in Microfinance institutions due to their limited assets.

They have been several research's in Kenya on SMEs and how microfinance institutions influence their liquidity, growth and revenues. (Kisaka & M Mwewa, 2014) did a study on how MFIs impacts SMEs in Kenya and found out that these institutions was on creating employment, helping the country's economy to grow and also helping in eradication of poverty. (Mbugua.) did a study on the impact of micro finance services on financial performance of SMEs in Kenya and discovered that micro finance services help SMEs to be liquid hence enhancing the financial performance financial performances of SMEs. Teo & Cheong, (1994) researched on the difficulties incurred by small enterprises when it comes to financial matter and found that inability to access to loans are the major hindrance to their growth. Kemei (2011) investigated the link between services offered by MFIs and how it affects the financial performance of SMEs. A positive and negative relationships was proven between MFIs loans and SMEs performance. Kimoro (2011) did a research on how the services of microfinance institutions affect women empowerment and the findings was, that, through microfinance women freedom of choice of has expanded. (Koech) did a survey on financial constraints deterring SMEs performance and growth and the findings was that the factors affecting performance and growth was capital market, price, capital access, guarantee requirements, capital management and the fee for registration. Cooper (2010) did a research of SMEs in Nairobi and how it is affected by the services offered by Microfinance institutions and they were a positive relationship between the two. To achieve the research objective, the study was guided by the following research objectives.

### **1.3. Objectives**

#### **1.3.1. General Objective**

The objectives of this study is understand the effect of Microfinance funding on the liquidity of micro and small businesses located in Madaraka area. To study the impact of microfinance on income level of beneficiaries in Madaraka ward.

#### **1.3.2. Specific objectives of the research**

To assess effect of Micro finance service, loan interest rate on liquidity of micro and small business located in Madaraka ward of Nairobi county.

- i. To assess the effect of MFI loan repayment duration on liquidity of micro and small business located in Madaraka ward of Nairobi county.

- ii. To assess effect of MFI loan size on liquidity of medium and small business located in Madaraka ward of Nairobi county.
- iii. To assess effect of MFI Loan collateral requirements on liquidity to of MSBS located in Madaraka ward of Nairobi county.
- iv. To assess effect of MFI loan prompt disbursement duration on liquidity to of MSBs located in Madaraka ward of Nairobi county.

To assess the impact of interest rates on the liquidity level of MSBs in Kenya

#### **1.4. Research Questions**

Following the objectives, I formulated the following research questions;

- i. To which extent does MFI loan repayment influence the level of liquidity of MSBs located in Madaraka ward of Nairobi county?
- ii. To which extent does MFI loan size influence the level of liquidity of MSBs located in Madaraka ward of Nairobi county?
- iii. To which extent does MFI loan collateral duration influence the level liquidity of MSBs located in Madaraka ward of Nairobi county?
- iv. To which extent does MFI loan prompt disbursement influence the level liquidity of MSBs located in Madaraka ward of Nairobi county?

#### **1.5. Significance of the Study**

The reason for this study is to help us understand the impact of microfinance funding on the liquidity of small and medium business located in Madaraka ward in Nairobi county. By evaluating loan administered by MFI and the growth of the SMEs over the last three years. Researchers have considered this as a significant area of study for the improvement of factors that's affecting an individual economic life in African countries and they have a huge contribution to the growing of small and medium size businesses in Kenya. Through Microfinance credit, the urban and rural population have a financial means in their villages to help them improve their basic lives in a viable way in line with the millennium development goals of eradicating poverty in the country. They have been helping in the fight against poverty by growing their businesses since it's the main source of income to the majority of people in Kenya. Hence it will make a way for potential NGOs wishing to aid in the sustainable improvement of SMEs, to also help them in knowing the difficulties they may come across and how they can succeed in their undertakings. This research

can be used by development practitioners to come up with ways of eradicating poverty and promoting small businesses. Well-wishers can use this research to emphasizes on promotion of MFIS. Scholar can benefit from this research by using it as a basis of for future research and it will add it to the body of knowledge. The study of this findings will help in boosting MFI sector of development and investments which is the engine of growth and development.

## CHAPTER 2: LITERATURE REVIEW

### 2.1. Introduction

This chapter reviews the literature surrounding the area of Micro financing and Small and Medium Enterprises. Section 2.2 will review theories. It will also look at MSBs and its situation in Madaraka ward. Section 2.3 looks at Microfinance credit. Section 2.4 reviews about empirical services that was previously done.

### 2.2. Theoretical Review

This study looks into three main theories that try to explain the effect of microfinance funding on SMEs. They include Liquidity theory of interest rate, microfinance credit theory, and poverty reduction technique theory.

#### 2.2.1. Keynes Liquidity Theory of Interest Rate Determination

This theory was presented J M Keynes,(1936 )is the most celebrated of all. Keynes said the rate of interest is a purely monetary phenomenon. It is the payment for parting with liquidity for a specific time horizon. Thus, like the price of a commodity, interest rate is determined by the need for and the supply of money hence it's important to introduce the concepts of demand for money and reserve for money. The supply of money is money in circulation in a country at a specific time and at a specific quantity. It is the total currency (notes and coins) and commercial bank deposits. Central bank of any control and determines the money in circulation hence it remains fixed in the short run.(Paul Samuelson 1938 "Revealed preference theory | economics | Britannica," n.d.). According to Keynes's, interest rate is determined by the demand and supply of money. Demand for money is the desire for people to hold cash. This desire is brought about by three motives explained below.

Transaction demand for money- the public need money for their day to day transactions. People hold cash since they are a gap between the receipt of income and spending. These incomes or wages are earned on an hour basis, weekly or even monthly but people spend their income to facilitate their daily transaction. Since receipt are received monthly or weekly, and spending is throughout the period, Individuals need active balance in form hard money or cash to finance their day to day transactions. People who have liquid money at hand to finance their daily transaction, earn high income.

Precautionary demand for money, is holding money for unknown emergencies. Tomorrow is uncertain, that's why people would like to save some of their cash to meet these unforeseen contingencies like illness, death, accidents and danger of unemployment. This type of money held for such purposes is called "idle balance" and it depends on one's income. People with low income will hold less compared to people with more income.

Speculative money- This is one's desire to hold their assets in cash/liquid form in order to be at upper hand of future changes of bond prices and interest rates. The price of the bond and interest rate are inversely related to each other. If interest rates rise, the price of the bonds is expected to drop and vice versa. The assets held under this motives are used to make speculative gain. Thus, when liquidity preference is high, we have low interest rate and at high interest rate, the securities become attractive. Supply of cash- this is the total amount of cash in the country. The supply curve of money is perfectly inelastic. Determinants of interest rate- the rate of interest rate is depends on the demand/need for money which equals money supply. In a situation the supply of money exceeds the demand for money, people will purchase more securities. Hence interest will fall and price will increase until supply of money equals to the demand for money.

Criticisms of this theory are;

First, this theory is an indeterminate one. It presumed that employment is fixed. Transaction ultimatum for money and speculative ultimatum for money cannot be known without knowing the level of income. Liquidity preference schedule changes as income changes—leading interest rate change. Hence one needs to know the level of income first before determining the rate of interest rate. Hence indeterminacy. Keynes made an error in eliminating real influences as the determinant. Also, in Keynes theory they are a choice between withholding risky bond and riskless cash. In the current world, it is the doubt that prompts an individual to hold both. This gap in this theory was filled up by James. In this theory, it tries explain that the public desire for money is too mainly help them remain liquid to meet their need of day to day transaction. It also explains that "interest" is the price someone pay for borrowing money. Hence, when MSBs in Madaraka area are more liquid, they are able to finance and run their business with ease due to the liquidity they have. But most times, this may not be possible due to the interest rate they have to pay for holding more cash. The interest rates may be too high hence discouraging these enterprises from borrowing cash. And due to this, it slows down the growth of this businesses, economy and profits are reduced.

### 2.2.2. Microfinance Credit Theory

Muhammad Yunus (1983) researched on Microfinance credit theory. Microcredit is the way of very small loans to those in need intended to encourage entrepreneurship. These individuals cannot meet any of the qualification for them to access to traditional credit. They lack collateral, a verifiable credit history and even employment for them to have access to credit. Microcredit is the provision of a variety of financial services to the less fortunate. Microfinance in Kenya is now a full-fledged system. Dondo (2009), Mugori, n.d. studied the history of MFIs in Kenya in the 1950s when ethnic Kenyans with small trading enterprises loans were provided credit with a joint Loan Board Scheme. Microfinance in Kenya is one of the most established in Africa and it has been growing since its inception in the 1970s, (Njeru Warue, 2012). The first specialized microfinances in Kenya were Kenya Rural Enterprise Fund (K-REP) and Kenya Women Trust Finance (KWFT) established in the 1980s. More MFIs like Faulu Kenya, Jamii Bora, Small and Medium Enterprise Programs commonly known as SMEP emerged in the 1990s. Microfinance main innovation is group lending which provides answers to the limitation of imperfect market credit, to the task of prevailing over information asymmetries. Information asymmetry will lead to the distinct phenomena of moral hazard and adverse selection. The lender lacks information on the riskiness of the borrower in adverse selection. Risky borrowers should be charged high interest rate than safe borrowers since they are more likely to default than safe borrower (Rahman 2010) "The shortcomings of interest rate capping in Kenya "Business Daily," n.d.s ). The average way of lending consists of two methods which tries to explain the topic of information asymmetry; peer examining to overcome the danger and screening to deal with adverse selection. Stiligz (1990) and Swain (2008) Wakaba, developed the early models. These models examine how group liability can resolve monitoring problems and moral hazard. Other models that were developed later on were inspired by Stiligz and focused on adverse selection and screening mechanism.

Money begets money. When you have money in liquid form you desperately try to make the best use of it, but when you lack money, you try to look for a job at the mercy of others. We can also say, micro credit is a measure of prevention and protection against poverty and helps in increasing a country's revenue. MSBs in Madaraka believe that expanding credit access, is an efficient way to increase their liquidity, promote growth and fight poverty. Microcredit is a type of loan granted to individual who lack steady employment to encourage them to grow on their own. The factors

and discussion on micro lending, argues that micro lending mitigates failure by making accessibility of credit to MSBs in Madaraka and in the country.

### **2.3. Variables**

#### **2.3.1. Theoretical Link between Liquidity Management, Profitability and Growth of Firms (SMEs)**

Managing liquidity is a fundamental component in the safe and sound management of all business enterprises. This is justified by the fact that prudent management of liquidity determines the profitability of the firm and subsequent growth. This relationship is disclosed in the pecking order theory, which states that that maintaining too much liquidity in the firm will constrain profitability and growth and the reverse is true. Too much liquidity in form of cash and cash equivalents constrains investment in long term assets that would generate more earnings hence profitability, part of which would finance the growth and sustainability of the firm (Da Silva, Hall and Hutchison, 2007). On the other hand, the theory asserts that maintaining little liquidity in the firm in form of cash and cash equivalents implies the firm's inability to meet its short-term obligations as they fall due which consequently causes the risk of encroaching on the firm's long -term capital to pay such obligations. This retards the firm's prosperity and growth. According to the theory, there is a need to strike a balance between liquidity and profitability for growth to be attained and financial management theorists recommend a ratio of 1:1(Parsley and Dresden, 2008).

#### **2.3.2. Liquidity**

With respect to the effect of liquidity management on firm's growth, Shin and Soenen (2009) examine a summary efficiency in management of a firm's liquidity. Shin and Soenen's evidence implies that firms that manage their liquidity more efficiently experience higher operating cash flow and potentially more profit, high savings, capital accumulation, more investment in fixed assets, high rates of employment and eventually growth. Bushman et al (2009) however, asserts that inefficiencies in operations may crop up due to difficulties in meeting the daily operational requirements leading to dissatisfied clients and suppliers, reduction in liquidity, profits, saving, investment, retirement of workers hence a firm's failure. This therefore implies a direct relationship between a firm's liquidity management and growth. Nowadays around the globe, it is acknowledged that SMEs are, in general, subject to substantial liquidity constraints which may potentially hinder their full profitability and growth.

### **2.3.3. Repayments Schedule and Delays in Loan Disbursement**

Factors such as repayment schedules and delays in disbursement of loans, they are seen as not being rigid to support microfinance. This has not been often not to be in the consideration of the business environment that customers work in. Most customers in the MFI have been exiting due to the rigidity in loan repayment schedules and loan disbursement. This has been supported by the findings of ("Paul Samuelson, 1938)

### **2.3.4. Return on Assets**

From the name itself, it explains how a business can squeeze its assets into profits. A business with high return on asset it's an indication of good operational performance and liquidity. To determine the ROA of a business, one needs to take the net income of the business divided by the total assets. Through this method, one is able to measure the efficiency of a business in generating returns from its assets.

### **2.3.5. Loan Size**

Hulme et al (1999), in his study pointed out those clients in MFI, withdrew due to the small amounts of loans provided. In addition, Hulme found that, once a customer income flow and profits increased, the customer withdrew from the MFI. Further, the study found that as the loan amount was increased, poorer clients dropped off from MFI's.

## **2.4. Empirical Literature Review**

Ochung (2010 )Did a study on the factors that affected borrowers which caused them to be unable to repay their loan in commercial bank of Kenya. This research was to explore on the issues and factors that's causing loan default amongst customers of commercial Banks in Kenya. The aim of this research was to try and understand the effect of Lender factors, borrower factors and loan factors on loan repayment among customers of Barclays bank. This study showed they was a positive relationship between the firm/group factors, customer borrower factors, and loan factors and the loan repayment among clients of commercial banks in Kenya. The study also concludes that their commercial banks in Kenya.

Wambugu, (2014)did a research on the survey of how the size loan is affected by the lending interest rate in commercial banks. The size of the loan, default risk caused by debt, operating costs and liquidity have a negative impact on the lending interest rate spread of the banks while bad loans, collateral, the size of the bank and performance had weak positive impact on the interest

rate spreads of the commercial banks. This study therefore concluded that loan size does not have a strong impact on interest rate spread of the commercial banks. In order for commercial banks to set a social optimum lending interest rate, it was advised that they examine other issues which can also be affecting the interest rate.

Duarte, (2011) This research was to try to assess the loan disbursement and collection performances of microfinance institutions in Bale zone. Microfinance institutions in Ethiopia has been showing a remarkable improvement on its revenue for a long time now but the MFIs have a strict policy instruments. Although they have displayed good performance in the last 15 years, they have not been able to satisfy the demand for loan and insurance services due to loan disbursement and loan collection. (MFIs) in Ethiopia are considered as one of the crucial policy instruments.

Paul, (2011) This research investigated how using collateral affects the motivations of borrowers, lenders and the relationship between them in loan pricing. The survey of SMEs in the UK, showed that high quality borrowers preferred a contract with low interest and more collateral, suggesting that collateral acts as an encouragement device to adverse problems in default payment. It was found that using personal collateral was more effective in screening models. Microfinance funding and their services go a long way in the development of a business.

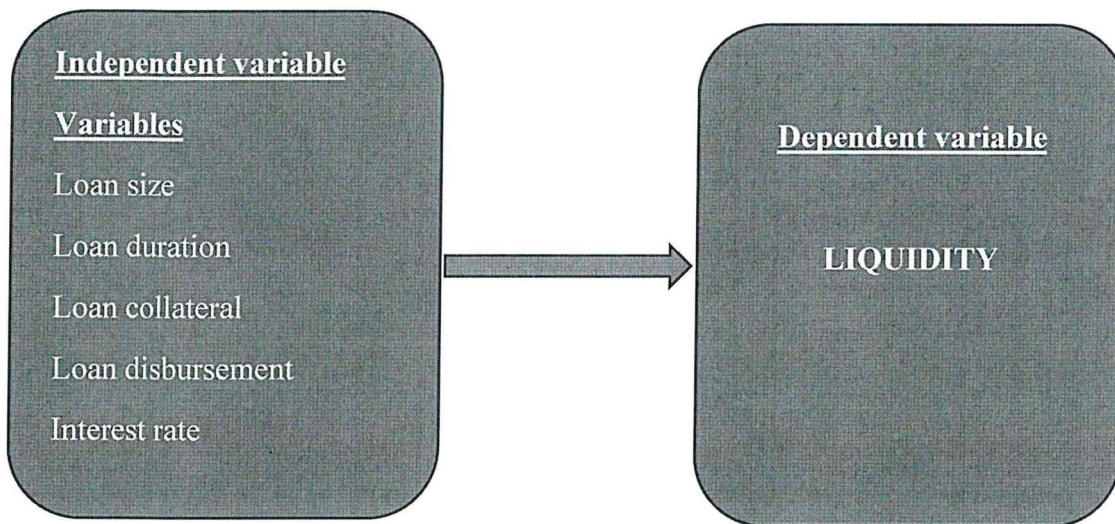
Many businesses post collateral as security for loans. The lender use Collateral as an assurance that the loan will be repaid. However, not all loans require collateral for assurance in case of the borrowers' default. Some research says that loans with collateral are riskier than the ones without. Why is collateral used sometimes, but not others? And why does collateral potentially involve more risk? In this article, considers these questions. He tries to explain why collateral is being used for security and pros and cons of using collateral. Collateral motivates borrowers to work hard to pay for the loans. Collateral increases the cost of borrowing since what the borrower has used to secure for the loan is more expensive or it has more worth than the loan borrowed.

Kumar ,(2011 ) Investigated on how big the impact of collateral measures on accessibility of credit for small business in Kisii Town in order to understand and determine how management skills impact credit financing of small business in Kisii Town. A descriptive research design was used for the study and they also adopted questionnaire for data collection from 160 MSB in Kisii town. Out of 560 MSB, the researcher sampled one hundred and sixty MSB using simple stratified method. From there research, it was found out that the businesses lacked adequate capital. Hence

the businesses were festered in their financial status mainly due to corruption in the municipality. Furthermore, the businesses lacked sufficient capital due to the processes that were tedious for them in acquiring funds from financial institutions. Hence the financial status of an enterprise is always affected one way or another.

Onyango, (2010) This research ought to explain the relationship between loan duration and lending interest rate in Commercial Banks in Kenya. This research studied commercial banks in Kenya on a period from 2009 to. It was found out that they are a positive relationship between the lending interest rate and average loan duration. This shows that when average loan duration decreases, lending interest rates is high and vice versa. Regulatory framework tends to have an effect on loan duration. Due to this framework, it enhances liquidity and reserve ratios offered by commercial banks hence leading to a better loan duration period. The study found that an increase in lending risk results to an increase in commercial banks' average loan duration.

#### 2.4.1. Conceptual Framework



The variables study will be measured using a 5 Likert scale.

Figure 2.1 Conceptual Framework

## **2.5. Summary of the Literature Review**

From the literature review, it is evident that microfinance funding of MSBs has a significant impact on the liquidity of MSBs. Microfinance funding is a credible and effective instrument for the growth and performance of SMEs. Financing of this small business is essential for creating employment and alleviating poverty. The literature review discussed above has shown that microfinance funding is important for growth and development of SMEs. It is important to note that restrictive credit requirements and guidelines in regulatory systems inhibit access to microfinance credit by borrowers. This is a constraint to the liquidity of SMEs. This study is geared to determine the effects of microfinance funding on liquidity and financial performance of SMEs.

## **2.6. Research Gap**

The area of Microfinance institutions on how liquidity has impacted the SMEs, have widely been studied. All the same, a gap still remains in understanding how MSBs liquidity impact their growth and performance in Madaraka ward. In the pursue of understanding how some variables such as interest rates, loan collateral, loan size, loan disbursement and loan repayment period of how they relate with SMEs liquidity, researchers have seen the challenges faced by SMEs, the working model for MFIs and range of services that provide solution to SME problems. However, they are great deal of evidence which helps us understand the relationship between liquidity of SMEs and the loan provided by the MFIs. This study therefore sought to fill in the gap by examining the effect of microfinance funding on the liquidity of micro and small business located in Madaraka area.

## CHAPTER 3: RESEARCH METHODOLOGY

### 3.1. Introduction

On this chapter, we will discuss research strategy to be employed in establishing the effect of liquidity determinants on MSBs in Madaraka ward. In this chapter we present research methodology with the following subheadings; research design, target population, sample size, sampling procedure, research instruments, reliability and validity, data analysis procedures and test of significance.

### 3.2. Research Design

Muhammad Yousef, (2018) Research design is a method that helps to obtain answers in an orderly way. The researcher uses this to help him be able to answer questions accurately, objectively and economically. One of the major functions of research design, is to help the researcher be organized and detailed in their work and the tasks they'll be performing. Through this, the readers are able to understand your work in detail. The researcher will employ an explanatory research design, due to expected causality in the independent and dependent variables.

#### 3.2.1. Population

Linear, (2017) We can define population as the total number of people, animals, events or objects that have a common characteristic. In Madaraka ward, we have a lot of MSBs in various sectors. Sectors such as, Salon business, Selling fast foods, Play station/movie shop business, Hotel business and Hostel business. The population size of MSBs in Madaraka is not known since it falls under Nairobi west ward. This study will focus on the owners of those SMEs.

#### 3.2.2. Sample

A sample is a representative of a whole group or population. This study applied stratified random sampling technique. Secondary data was used from Madaraka area in order to achieve the intended objective of the study. To determine my sample size, I will use the following formula  $n = \frac{4pq}{d \times d}$ , where n is the sample size p is proportion of the population, q is 1-p and d is precision.  $2 \times 0.5 \times 0.5 / 0.05 \times 0.05 = 200$ . Hence 50 will be my minimum sample size. (Parker Kadam, 2010)

### **3.2.3. Data Collection**

Debose,(2010)Data collection is the process of collecting facts, statistics and measuring information which help answer the research questions, test hypothesis and evaluate outcomes. Both primary and secondary sources of data have been used in this study. Primary data was obtained through administering structured questionnaires. The questionnaires will be distributed using drop and pick method and the respondents to fill, are either the owners or managers of the MSB. We are also going to use cross sectional approach and collect data from many MSBs over a single period.

### **3.2.4. Questionnaires**

The most essential information collection technique is structured questionnaire. Questionnaires is an affordable way of gathering quantitative data and also helps to reduce biasness since the researcher's opinion does not influence the respondents answers unlike face to face interviews which may make the respondent answer to please the researcher. The questionnaire will be short and structured with multiple choices to encourage participation and uniformity of answers I will inquire the respondents to fill the survey and to feel free when giving their own views, as all data gotten is to be taken care of with at most confidentiality. The survey will contain open and closed ended questionnaire. The format of collection moreover helped the researcher to be able to inquire and collect information on delicate data and complex questions

### **3.2.5. Descriptive design**

Descriptive research aims to accurately and systematically describe a population, situation or phenomenon. It can answer what, when, where, when and how questions, but not why questions. (Mccombes, 2019)

### **3.3. Data Validity and Reliability**

Mugenda and Mugenda (2003), defined validity as the degree to which theory and evidence conform the truth and establish knowledge entailed by use of tests. In other words, validity, its simply an instrument which ought to measure what its suppose to measure. It therefore refers to the extent to which an instrument asks the right questions in terms of accuracy. The content validity of the instrument was determined in two ways. First, it was determined through piloting, where the responses of the respondents will be plaid against the research objectives. Content selected and included in the questionnaire must always be relevant to the variables being studied for a research

instrument in order to be considered valid. The researcher performed a pilot test with a randomly selected sample of five SMEs. The instruments were modified as per results of the pilot test.

Reliability of an instrument is the measure of the degree to which a research instrument yields consistent results or data after repeated trials. In order to test the reliability of the instrument to be used in the study a pilot study was carried out and a reliability coefficient computed. A pilot study is an important step in research process because it uncovers unclear instructions and vague questions in the instruments. This helps in conforming whether the questionnaire produces the same response every time its administered. (Peter Kivunzi, 2019)his study will adopt the method of Cronbach alpha since it's a measure of scale reliability, i.e.

Cronbach alpha	Internal Consistency
$0.9 \leq \alpha$	Excellent
$0.8 \leq \alpha < 0.9$	Very good
$0.7 \leq \alpha < 0.8$	Good
$0.6 \leq \alpha < 0.7$	Acceptable
$0.5 \leq \alpha < 0.6$	Unacceptable
$\alpha < 0.5$	Poor

*Table 3.1 Cronbach alpha*

Validity is the extent to which the scores from a measure represent the variable they are intended to. We have already considered one factor that they take into account—reliability. When a measure has good test-retest reliability and internal consistency, researchers should be more confident that the scores represent what they are supposed to. There has to be more to it, however, because a measure can be extremely reliable but have no validity whatsoever. Although this measure would have extremely good test-retest reliability, it would have absolutely no validity. (Roberta Heale, 2015.) In this study, data was analyzed using Cronbach alpha to test the internal consistency and reliability on the effect of Microfinance funding on the liquidity of SMEs in Madaraka area. The research used Microsoft excel to enter, run and compute the measurements of Cronbach alpha.

### 3.4. Data analysis

The completed questionnaires were reviewed and edited for accuracy, consistency and completeness. The study will adopt factor analysis and ordinal regression analysis. Ordinal Regression and correlation analysis was applied to show the relationship between variables. The dependent variable being the loan interest and loan amount of MSBs in Madaraka ward, will be measured using amortization and compound interest. The value for most SMEs is measured in terms of financial records after access to credit hence the independent variable will be measured by checking the loan book records from MSBs. The data will be analyzed and presented in charts and tables. The inferential statistic was used to show the nature and magnitude of relationships established between the independent, intervening and dependent variable using regression analysis.

### 3.5. Analytical model

The study used the following model:

$$Y = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4 + \beta_5X_5 + \epsilon$$

Y = Liquidity level measured by current ratio

Liquidity Ratio = loans (current assets)

X1= Loan size (Loan Ratio)

X2 = Loan amount

X3 = Loan repayment duration

X4 = Interest rates

X5 = Loan prompt Disbursement

$\beta_0$  = Represents the factor affecting liquidity when credit policy is zero.

$\epsilon$  = Random error term

$\beta_{1,2}$  = Coefficients of the variables

### **3.6. Test of significance**

True representation of the study population and subject to scrutiny is as a result of research outcomes from data analysis. Reliability can be defined as the accuracy of the instruments used in the study (Mugenda and Mugenda, 2003). The research was reliable since the data sources are regarded credible, reliable and consistent because the selected SMEs have had operated for at least five years consecutively.

## CHAPTER 4: DATA ANALYSIS AND PRESENTATIONS

### 4.1. INTRODUCTION

This chapter presents the research findings to establish the effect of Microfinance funding on the liquidity of SMEs in Madaraka. The study was conducted through administering questionnaire which was used in the analysis. The data targeted a sample of 50 SMEs from which 30 respondents were interviewed (filled in and returned the questionnaires) making the response rate of 60%. This response rate was overwhelming and conforms to Mugenda and Mugenda (1999) statement that a response rate of 50% is adequate for analysis and reporting; a rate of 60% is good and response rate of 70% and over is excellent. This section presents the research findings; it presents the study findings from the regression analysis, correlation and Cronbach alpha.

### 4.2. Table 4.1: Distribution of respondents by Gender

The table below, shows a representation of both genders that participated in the data collection. 40% being female and 60% being male.

Gender	Frequency	Percentage
Male	18	60%
Female	12	40%

### 4.3. Table 4.2: Analysis of each variable

Variables of the study	Very Satisfactory	Satisfactory	Neutral	Not Satisfactory	Completely unsatisfactory
Loan size	26	4	0	0	0
Loan interest	13	10	7	0	0

Loan collateral	0	3	10	10	7
Loan repayment	7	15	8	0	0
Loan disbursement	3	13	14	0	0
Mean	9.8	9	7.8	2	1.4
Standard deviation	9.20	4.77	4.58	4	2.8

Mean is the most common measure of central tendency and refers to the average value of a group of numbers standard deviation provides insight into how much variation there is within a group of values. It measures the deviation (difference) from the group's mean (average) (Gani and Vally, 2016). A large standard deviation means that more numbers are spread out while a small standard deviation means that more of the data is clustered between the mean. In the column for not satisfactory and completely unsatisfactory, the standard deviation is higher than the mean which simply means the data were not distributed evenly. In the column for very satisfactory, satisfactory and neutral, have high means which means most of the independent variables have an impact on the dependent variable (Parker 2013.)

#### 4.4. Table 4.2: Provision of microfinance services

The respondents who used MFIs were asked a question whereby they were asked to state the services they receive from MFIs. The respondents stated the services listed in table below

Services received from MFI	Frequency
Loans	13
Saving	9
Training	14
Micro insurance	0
Mean	9
Standard deviation	5.52

From the table above, it shows only 14 respondents admitted borrowing and using microfinance services as a way to finance their businesses. The mean and standard deviation is above average hence we can say that the independent variables have an effect on the dependent variables. 14 of the respondents indicated that their major source was through loans from MFIs, this clearly shows that liquidity of SMEs is influenced by independent variables such as loan amount.

**4.4.1. Table 4.3; Distribution of respondents in respect to reasons for using MFIs services.**

Reason for borrowing loan	Frequency
Liquidity	14
Profits	5
Investments	13
Emergencies	6
Medical expenses	7
Social security	3
Mean	8
Standard deviation	4.08

The mean and standard deviation are average, which shows that most people used MFIs for one reason or another. This shows that people borrowed loans from microfinance institutions for whatsoever reason hence it would affect their level of liquidity.

**4.5. Table 4.4: Reasons as to why the enterprises obtained loans from MFI's**

Reasons	Frequency
Easy loan repayment	4
Loan size	4
Interest rates	6
Total	14
Mean	7
Standard deviation	4.29

The mean (7) is high which clearly justifies why people would take a loan from microfinance institutions, thus affecting their liquidity level. The standard deviation (4.29) shows that the numbers are evenly distributed.

#### 4.6. Table 4.5: Whether the Enterprises benefit from Loans from Microfinance Institutions

Response	Frequency
Yes	16
No	14
Total	30
Mean	15
Standard deviation	7.12

From the responses and the mean, it clearly shows Respondents who borrowed loans from MFIs said that their businesses and enterprises benefited from loans from microfinance institutions, while the ones who had other indicated otherwise.

#### 4.7. Table 4.6: As to whether they required loan security before disbursing the loan borrowed

Response	Frequency
Yes	2
No	12
Total	14
Mean	7
Standard deviation	4.37

Since the mean and the standard deviation are both average, it helps us explain the fact that these microfinance institutions did not necessarily need security depending on the loan amount borrowed.

#### 4.8. Regression analysis

In order to establish the relationship between independent and dependent variables, a multiple regression was conducted. The research study aimed at evaluating the relationship between microfinance liquidity and financial performance of SMEs in Madaraka area. The study also revealed that 87.3% of financial performance in the SMEs could be explained by the variables under study. From this study it is evident that at 95% confidence level, the variables produce statistically significant values and can be relied on to explain financial performance in the SMEs sector in Kenya.

**4.8.1. Table 4.7 The Effect of Independent variables on the Liquidity of MSBs in Madaraka area.**

To test the effect of loan size, interest rate, loan amount, loan repayment duration and loan prompt disbursement on the liquidity of small and medium enterprises in Madaraka area a multiple linear regression was conducted. The results are discussed in the following sections.

Model	R	R square	Adj R square	Std err of the estimate
1	.706a	.419	.490	.15241
a. Predictors: (Constant), Loan size, loan amount, Duration, Interest rates, loan prompt disbursement				

The above table shows a R value of 0.706 which shows that the correlation between the dependent variable and the combined variables was positive and strong ( $r=0.706$ ). Changes in the loan amount, loan duration, collateral amount and interest rates causes 41.9% of the variation in the dependent variable liquidity while 58.1% are explained by factors outside the study.

**4.9. Table 4.8 ANOVA**

Model		Sum of squares	Df	Mean square	F	Sig
1	Regression	.578	4	.145	6.221	.001
	Residual	.581	25	.023		
	Total	1.159	29			
a. Dependent Variable: Current ratio						
b. Predictors: (Constant), Loan size, loan amount, Duration, Interest rates, Collateral amount						

Analysis of Variance test (ANOVA) is used to test the significance of the model and thus the goodness of fit of the model. In this case, the ANOVA test findings indicates a p-value of 0.01 which is lower than 0.05 at 95% level of significance which implies that the independent variables are jointly significant in influencing the dependent variable

#### 4.10. Coefficients

Mode	Unstandardized Coefficients		Standard coefficient(Beta)	t	Sig
	B	Std. Error			
(Constant)	1.689	0.219		7.717	0.000
Loan amount	0.001	0.001	12.895	1.117	0.274
Loan duration	0.105	0.098	0.162	1.070	0.295
Collateral amount	-0.002	0.001	-13.477	-1.168	0.254
Interest rates	1.429	0.877	-0.252	-1.630	0.116
a. Dependent Variable: current ratio					

Table 4.9 shows the results of the regression test coefficients. The coefficients findings as per the p-value or sig, the value column indicates that no independent variable has a significant effect on the dependent variables since all the p-values are greater than 0.05 at 95% level of significance

#### 4.11. Discussion of the Research Findings

According to Joachim (2007) to remain in business operations effectively a microfinance institution should be able to make withdrawals to members instantly and also be able to offer loans to members upon receipt of such applications. It is important that liquidity levels of these MFIs remain checked and at appropriate levels because financial goals can be sudden especially due to the unforeseen demands of their customers. This study focused on how microfinance lending affects the liquidity of small and medium enterprises. The main variables of concern for this study was the effect loan size, loan amount, loan repayment period, interest rate and loan prompt disbursement on the liquidity of small businesses. A correlation test shows that there exists significant positive correlation between liquidity and credit policy. This means that these enterprises with improved credit policies had more liquidity compared to the ones which had weak credit policies. The results were confirmed by the multiple linear regressions which tested the effects of several variables on the liquidity of the small and medium enterprises. From the results, microfinance funding was found to significantly affect the liquidity level of this MSBs. Similar notion was held by Heider, Saidi, & Schepens (2014) who argued that poorly structured policy could affect liquidity by posing a risk of lending out money and being unable to recover outstanding debt in good time. Also Ayodele, Thomas and Raphael (2014)

noted that credit policy affects the amount of capital, quality of asset, management quality, earnings and liquidity position of a financial institutions either positively or negatively depending on how the management implement the policies. A, S, O, Alex, & Felicia, (2019) observed that that favorable credit policy affect liquidity favorably and suggested that businesses needed to regularly review their credit policy to maintain liquidity at favorable levels. The study results agree with the previous studies that loans affect the liquidity of firms. This shows that depending on the MFIs lending policies, how they are formulated and the strength of the policy affect the liquidity of businesses which in turn affects the ability of such firms to meet short term financial obligations and goals. A correlation test shows a positive and significant correlation between capital adequacy and the liquidity of Microfinance institution. Similarly, a regression test shows that the level of loan affects the liquidity of the MFI. McMahon and Stanger (2005) also argued that shortage of working capital was a common problem for small firms. Similar results were justified by David, Willy and Mboya (2015) who held that adequate capital helps cushion depositors and act as a protection of the depositors' funds hence improving the liquidity of the financial institutions. Joachim (2007) emphasized that the primary role of a financial institutions is to absorb risk using its equity capital. This underlines the fact that capital of the firms should be adequate enough to guard against any threats or potential loss of liquidity.

## CHAPTER 5: INTRODUCTION

This chapter discussed the summary of the findings and the conclusion that was reached. It also gives recommendation to the readers as well as give the limitations or weaknesses within the study. From the collected data and analysis, the following assumptions, conclusion and recommendations were made. The responses were based on the objectives of the study. The researcher was motivated and focused to clearly establish to what extend the effect of microfinance funding has on the liquidity of micro and small businesses located in Madaraka area.

### 5.1. Summary

The core objective of the study was to determine the effect of microfinance funding on the liquidity of micro and small businesses located in Madaraka area and the study developed that there is a relationship between the above mentioned variables. My Primary data was collected from different and diverse both small and medium enterprises within the proximity of Madaraka ward. Secondary data was used from different internet sources. Cronbach alpha was used in the data analysis. From the findings of the Cronbach's analysis, it was found out that there was a variation of 90.8% give or take 0.1% on financial performance Madaraka SMEs could be accounted to changes in current ratio, operating cash flow ratio and capital structure. This is an indication that 90.8% changes in financial performance of these small firms is due to current ratio and operating cash flow ratio. The study objective further revealed that there was strong positive correlation between current ratio and operating cash flow ratio and the performance of these SMEs in Madaraka area, shown by strong positive correlation coefficient. From the finding on analysis of variance, the study found that the overall item had a significance value of 0.9% which shows that the data is ideal for making a conclusion on the population's parameter. It then

further outlined that current ratio, operating cash flow ratio and current debt significantly affects the performance of SMEs.

## **5.2. Conclusion**

The study established that current ratio positively affects the financial performance of SMEs, thus the study concludes that liquidity positively affect the performance of SMEs in Madaraka area. The study also revealed that an increase in operating cash flow ratio positively affect the financial performance of SMEs in Madaraka ward, thus the study concludes operating cash flow ratio positively affect the financial performance of all SMEs. The study revealed that an increase in loan borrowing/ debt to equity positively affects the financial performance of firms, thus the study concludes that debt to equity ratio positively affects the financial performance.

From the findings and conclusion, the study recommends that there is need for non-financial companies listed at the Nairobi Securities Exchange to increase their current assets so as to increase their liquidity as it was found that an increase in current ratio positively affect the financial performance. The study further recommends that there is need for non-financial companies listed on the Nairobi Securities Exchange to increase their operating cash flow, through reduction of their credit repayment period in order to positively influence their financial performance. There is need for the non-financial companies listed at the NSE to increase them debt to equity ratio as it was found that capital structure positively affects the financial performance of non-financial companies listed at the Nairobi Securities Exchange.

## **Recommendations of the Study**

The study found that the microfinance lending influence the liquidity of this small businesses operating within Madaraka area which in turn affects the operational efficiency of MSBs. This implies that good credit policies need to be designed and enforced to ensure that liquidity of the

MFIs is sustained at appropriate levels. It is thus recommended that, business strategists and strategic managers as well as the credit department personnel invest in market research and benchmark studies to ensure they develop good credit policies which positively influence the liquidity of small and big firms. To effectively maintain the levels of liquidity of the MFIs, it is recommended that MFIs focus on having adequate capital and assets. This can be achieved by increasing the members and assets so as to cushion any loss or threats against their liquidity levels. Collection policies on loans and the duration of the loans need to be well designed and implemented so that it is cost effective and productive for small firms.

### **5.3. Limitation of the study**

The study adopted a multiple regression model with five variables: four independent variables (loan amount, loan duration, collateral amount and interest rate other independent variables are held constant) and one dependent variable (liquidity). As noticed apart from the four independent variables mentioned above, other variables are held constant in this study which might weigh as much if not more than the ones chosen for this research purpose. This colossally can make the research hypothesis less authentic. As if that is not enough just because this model has more than one independent variable doesn't make it 100% unbiased especially if done with limited resources like time, manpower and a small sample size of the entire population like in this study. As absurd as this may sound one independent variables depending on the randomly chosen respondents might receive more positive causal effect in the study in relation to the dependent variable making the findings based more on these particular independent variables when reviewing liquidity of SMEs. This study was therefore carried out within a limited time frame and resources which constrained the scope and depth of the study. This necessitated the adoption of a sample design with small sampling size of the superset hence these findings cannot be used to make generalizations on the effect of microfinance funding on the liquidity of SMEs found in Madaraka area.

#### **5.4. Areas For Further Research**

Further research should be carried out in all the 47 Counties of Kenya and also other variables that were held constant in this research should be simulated since this study only and only focused on SMEs in Madaraka area and therefore its findings if used to represent Kenya in its entirety will be considered biased and therefore cannot be generalized to apply to all the SMEs in the 47 Counties in Kenya. Further research should be conducted on SMEs countrywide to investigate on the effects of microfinance funding on the liquidity of SMEs to find out whether there are similarities or unique factors. For the small and micro enterprises sector to grow, small businesses need to link with the rest of the economy even plausibly with the whole world via e-commerce. Most of these businesses are so small that creating a link seems almost impossible.

Further research should also be done specifically in this area to establish the most accommodating way to link small and micro businesses with large companies even multinational corporations in the economy. Most multinational corporations started out as either small or micro businesses on inception. With the right management and a good diversification of portfolio to minimize risks on returns and simultaneously maximize returns on investment managed to increase revenues exponentially.

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## APPENDIX 1

Dear Sir/Madam,

### **Re: Administration of Questionnaires**

I am a 4<sup>th</sup> year student at Strathmore University Business School Pursuing Bachelor of Commerce. I am conducting a research on the effects of microfinance funding on the liquidity of micro and small businesses located in Madaraka area.

I am requesting to administer some questionnaires in your locality for the above-mentioned research. All the information collected is purely for academic purpose and will be confidential.

Your support and participation will be appreciated.

Kind Regards,

Esther Njoroge,

094647.

Strathmore University.

## APPENDIX 2

### SURVEY OF MICRO AND SMALL BUSINESSES IN MADARAKA WARD

Dear sir/Madam

I Wangui Esther Njoroge, Research student Department of Commerce, Strathmore University, undertaking this research on “Microfinance Funding on the Liquidity of Micro and Small Businesses in Madaraka ward”, as a partial requirement for fulfilment of my degree request you to fill this questionnaire and return the same. Your support in terms of investing time with us to respond this questionnaire would be a great contribution to accomplish the study. Thanks you.

Please follow the instructions:

Tick or mark X on one box ONLY below your answer for each question.

Do not write your personal answer unless specified.

1. To what extend do you think loan repayment duration affects the business in Madaraka area?

To no extent	To a low extent	To a moderate extent	To high extent	To a very high extent

2. To what extend do you think loan size affects interest rate?

To no extent	To a low extent	To a moderate extent	To high extent	To a very high extent

3. To what extent do you think loan collateral has affected your business here in Madaraka?

To no extent	To a low extent	To a moderate extent	To high extent	To a very high extent

4. To which extent do you think loan prompt disbursement has affected the liquidity of MSBs in Madaraka area?

To no extent	To a low extent	To a moderate extent	To high extent	To a very high extent

5. To what extent is Microfinance services being helpful to your business?

Very satisfactory	Satisfactory	Neutral	Not Satisfactory	Completely unsatisfactory

6. To what extent are the microfinance services reliable?

Very satisfactory	Satisfactory	Neutral	Not satisfactory	Completely unsatisfactory

7. To what extent do you agree that the services of Microfinance-specifically loans are fair to all members?

Strongly agree	Agree	Neutral	Disagree	Strongly disagree

8. To what extent would you want to take a loan for your business?

	Strongly agree	Agree	Neither	Disagree	Strongly disagree
Liquidity					
For profits					
Investments					
Emergencies					
Medical expenses					
Social security					

9. To what extent were you Satisfied with the loan amount that was approved to you by the Microfinance institution?

Very satisfactory	Satisfactory	Neutral	Not Satisfactory	Completely unsatisfactory

10. To what extent was the requirement of being given a loan easy?

Very satisfactory	Satisfactory	Neutral	Not Satisfactory	Completely unsatisfactory

11. To what extent are Microfinance finance giving back to the community in this area?

Very satisfactory	Satisfactory	Neutral	Not Satisfactory	Completely unsatisfactory

12. To what extent has Microfinance assisted your business growth?

Very satisfactory	Satisfactory	Neutral	Not Satisfactory	Completely unsatisfactory

13. To what extent do feel that the Microfinance interest on loans are compared to let say banks?

Very satisfactory	Satisfactory	Neutral	Not satisfactory	Completely unsatisfactory

14. To what extent would you say the loan you were given has helped you financially?

Very satisfactory	Satisfactory	Neutral	Not satisfactory	Completely unsatisfactory

15. To what extent would say the saving to loan rate are? i.e. you can request loan up to three times your saving limit.

Very satisfactory	Satisfactory	Neutral	Not satisfactory	Completely unsatisfactory

16. To what extent would you recommend your friends, family and colleagues to sign up to any Microfinance institution?

Very satisfactory	Satisfactory	Neutral	Not satisfactory	Completely unsatisfactory



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In this generation, self-employment is the major impelling cause for economic growth, poverty alleviation and employment in African countries. This small business and/or self-employment have helped in accelerating growth and rapid industrialization. Micro and Small Businesses (MSBs) in Madaraka ward of Nairobi County have acted as a catalyst in the political and socio-economic development. Apart from creating employments and generating revenue, MSBs also help our economy in the creation of products and services and growth of skills. A research of Irene, Charles, & Japheth, (2015) on how the services of Microfinance affects the expansion of SMEs in Kenya found a positive correlation amongst growing MSBs and services offered by microfinance institution. The Kenya Government once committed in helping SMEs to grow and it appeared to be one of their key strategies in their 1980s report. It became a priority in the report for 1989. Vision 2030 had also emphasized the importance of Micro and Small Enterprises in Kenya. MSBs in Madaraka and in other parts of the country are considered of great importance since it will help a great deal in achieving vision 2030. Studies about growth, majority of them have been undertaken based on the law of Gibran's law. Gibran's law says that the size of a business, determines the firm's growing rate. Businesses has there for been categorized by different studies into three: small, medium and large. Other studies on growth have also used assorted ways to gauge growth. Dobbs & Hamilton, (2007) laid out a framework of explaining how business grow. These enterprises have continued to act a major role in the economy of this country.

#### Microfinance Service

Microfinance has been a get through for self-employed person and the SMEs since it offers financial services for individuals who are not able to access banking and related services. Microfinance offers a wide variety of services such as lending money for new businesses, the provision of small loans to poor clients; they help clients to learn how to save. Microfinance services are designed to be accessible and inexpensive for the poor and socially marginalized clients whereas banks their main focus is on big business. Microfinance helps people to secure their own future by ensuring they acquire and secure finances so as to level their expectations. This article researches on the impact of current microcredit programme on how SMEs are performing in Zambia. It was found that, borrowers who took a second loan, they were a good change in the growth of their business compared to when they took their first loan. Borrowers who only took the first loan, they were a negative change in the performance of their business which made them worse off. Some researchers believed that loans enlarged the prospect and thus plays

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