PERCEIVED IMPACT OF THE 2007-2008 GLOBAL FINANCIAL CRISIS ON SMALL AND MEDIUM SCALE ENTERPRISES CLIENTS IN KENYA

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Declaration

I Francis Kiarie Njogu hereby declare that this research project is my own original work and has never been presented to any other Institution of Higher learning for Examination purposes leading to award of Certificate, Diploma or Degree.

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This research project has been submitted to the University for Examination with my approval as the University Supervisor

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Supervisor: **Date**

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Dedication

This project is dedicated to my parents, Mr J.P.N Kariuki and Mrs Elizabeth Kariuki, and my brothers and sisters whose encouragement and support has greatly inspired my pursuit of education that has culminated to this project.

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Abstract

The onset of 2008 financial crisis can safely be attributed to the collapse of USA and European housing markets. Stimulated by sub-prime mortgage, housing sector enjoyed boom across USA and Europe during 1998 to 2006. Yalmaz (2008) asserts that the worst part of the crisis is already over and the markets are suffering from what can be called ‘the after shocks’. This crisis has thinned foreign exchange of developing countries which sent a ripple effect throughout their economies. Small and Medium scale Entrepreneurs were affected in large and their operations put in jeopardy by the global financial meltdown. This study intended to evaluate some of the impacts of the crisis and ways by which the SMEs in Kenya managed to weather the credit crunch storm.

A Survey study which tends to ask people questions about their behavior, attitudes and opinions was used for this investigation to address the main objective ; *“The impact of the global financial crisis on SMEs in Kenya”*.

The study reveals that SMEs in Kenya were indeed adversely affected by the financial crisis in areas that are critical to their performance. Firstly, the crisis led to a shortage of credit and that which was available was expensive due to a hike in interest rates. Due to a weakened purchasing power of consumers globally, both domestic and offshore demand for goods produced by SME also decreased remarkably thus shrinking the market. Lastly the cost of raw materials also increased especially for the agriculturally based businesses, which was majorly compounded by the drought and the post election violence that gripped Kenya at the time.

SMEs in Kenya came up with strategies to counter the financial crisis and top on the list was workforce downsizing in order to cut down on costs. Many businesses also postponed on investment and actively sought new markets for their products. Old business strategies of operation were also reformed to incorporate new factors introduced by the financial crisis in order to remain afloat.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The term SME covers a wide range of definitions and measures, varying from country to country and between the sources reporting SME statistics, (Kenya Association of Manufacturers, 2008). Although there is no universally agreed definition of SME some of the commonly used criteria are the number of employees, value of assets, value of sales and size of capital as well as turn over. Among them the most common definitional basis used is employees because of the comparatively ease of collecting information and here again there is variation in defining the upper and lower size limit of an SME, (KAM, 2008).

In developing countries the number of employees and size of assets or turnover for SME tend to be much smaller compared to their counterparts in developed countries due to their relative size of business entities and economies, (World Bank, 2007). Types and Features of Small Scale Businesses in Kenya Survivalist enterprises are activities by people unable to find a paid job or get into an economic sector of their choice. Income generated from these activities usually falls far short of even a minimum income standard, with little capital invested, virtually no skills training in the particular field and only limited opportunities for growth into a viable business. Poverty and the attempt to survive are the main characteristics of this category of enterprises.

SMEs usually lack 'formality' in terms of business licenses, value-added tax (VAT) registration, formal business premises, operating permits and accounting procedures. Most of them have a limited capital base and only rudimentary technical or business skills among their operators. However, many micro- enterprises advance into viable small businesses. Earning levels of micro-enterprises differ widely, depending on the particular sector, the growth phase of the business and access to relevant support. Small enterprises

constitute the bulk of the established businesses, with employment ranging between five and about 50. The enterprises will usually be owner-managed or directly controlled by the owner-community and are mostly family owned. They are likely to operate from business or industrial premises, be tax-registered and meet other formal registration requirements. Classification in terms of assets and turnover is difficult, given the wide differences in various business sectors like retailing, manufacturing, professional services and construction – Lack formalities Medium enterprises constitute a category difficult to demarcate vis-à-vis the "small" and "big" business categories. It is still viewed as basically owner/manager-controlled, though the shareholding or community control base could be more complex. It is characterized by the employment of more than 200 employees and capital assets of a substantial amount of about Ksh. 2 million (excluding property). SMEs in Kenya are generally distinguished by the nature of their production and management arrangements, trading relations, financial practices, internal competence, etc.

According to KAM, (2008) SMEs in Kenya typically have the following features in varying degrees; they are small units, often rural-based and family-owned, most of them are mall independent enterprises, standing alone and producing for a well-defined market , some are specialized firms, producing specialized products, selling to the international and /or local markets, they rely on low cost raw materials, low energy costs, low labor costs, and are characterized by low division of labor, flexible and often small production runs, they have low capital formations and finally, they are largely labor intensive units with low-level technologies; but one needs to note the emergence of high skill and technology-intensive SMEs, especially in high technology sectors such as ICT.

During the 20th century, the world experienced two major financial crises. The first global financial crisis was seen during 1929-30, which affected the developed nations, Europe and America. While the second crisis came in 1997 and remained till 1999 and was experienced by emerging economies of Asia Pacific. The recent financial crisis has

taken the attention of the world in current months; it was seen with serious anxiety as it falls outwards from the regions originally affected. Alan Greenspan recently called it a *"once-in-a-century credit tsunami",* born of a collapse deep inside the US housing sector. As it has been seen, the great wave of the financial crisis overtops one economic levee after another. Instability has rushed forward from sector to sector, firstly from housing into banking and other financial markets, and then into all parts of the real economy, Nida et al, (2008).

The 2007-2008 global financial crisis has been felt across both the public and private firms forcing the new heavy demands on the public sector's finances. The crisis has surged across national borders within the developed world, and now there are some alarming reasons that the crisis will swamp other developing countries, affecting the significant economic progress of recent years, Yifu (2008). According to Hyun-Soo, (2008), anxieties have augmented over the global financial crisis, which began from the US sub prime mortgage disaster with the help of the governments of major countries which are coming up with measures such as provision of liquidity and bailout packages for distressed banks, the fear that has gripped financial markets shows little signs of abating. Major stock exchanges are tumultuous while a series of indicators that gauge investors' risk aversion are posting all-time highs.

De Bonis (1999) defines financial crisis to be a wider range of disturbances, such as sharp declines in asset prices, failures of large financial intermediaries, or disruption in foreign exchange markets. Due to the disruption of credit flow, multinational companies have been unable to support their overseas subsidiaries hence resulting in cost cutting measures.

1.2 Problem Statement

In spite of the fact that SMEs are regarded as the bulwark for employment generation and technological development in Kenya, the sector nevertheless has had its own fair share of policy neglect with resultant unsavory impacts on the economy. The problems and challenges that SMEs contend with are enormous no doubt but some SMEs are able to overcome them an indication that there must be some survival strategies, which are not known to many SME businesses. This research thus was intended to explore and unravel some of the key business survival strategies, which have helped a few thriving SMEs to emerge strong from the financial crisis.

Kenya enjoyed a robust economic growth during the Kibaki administration (2002-2007) that strengthened its balance sheets. Sound economic policies like friendly taxation regimes, improved infrastructure, enhanced corporate governance and a strong macro economic environment aimed at containing inflation and maintaining a competitive exchange rate were an important factor, as was the favorable external environment and increased external support in the form of higher inflows from such sources as the Diaspora through remittances and tourism earnings. But the food and fuel price shocks of 2007–08 that preceded the current global financial crisis weakened the external position of net importers of food and fuel, caused inflation to accelerate, and dampened growth prospects by decreasing the purchasing power of consumers. The global financial crisis greatly compounded these challenges on the financial position of SMEs as they try to remain afloat (Central Bank of Kenya, 2009). The SMEs in the developing world (Kenya) – how they have been impacted by the global financial crisis, and what they did to minimize the impact – was therefore the focus of this research.

Understandably, perhaps, until now the focus of policymakers has mostly been on the actions of the governments at the epicenter of the crisis, as well as those of other developed countries like Japan and Korea. SMEs in a country with high unemployment rate of up to 40% (Central Intelligence Agency Fact book, 2001), are one of the most

significant routes to a better life. Therefore these people who live in or on the verge of extreme poverty and given their slim margin for survival, any economic crisis will have its most severe human consequences on them. This was a critical rationale for the concern of this study; the impact of the financial crisis on SMEs in developing countries and specifically Kenya in the face of the financial crisis. This study in addressing the problem aimed to answer two main questions which are; what impact has the global financial crisis had on SMEs in Kenya? What measures did the SMEs take to counter the effects of the financial crisis?

Unlike in the developing countries like Kenya, many countries in the developed world have been able to energize and transform their SME sector to such a vibrant one that they have been able to reduce to the barest minimum their unemployment and poverty level because of the immense contribution of the sub-sector to their economic growth and development. It is expected that the outcome of this research will go a long way in informing Kenya's SME as far as the financial crisis is concerned (Kato 2009).

1.3 Research objectives

General objective

To investigate the impact of the global financial crisis on SMEs in Kenya.

Specific objectives

i. To investigate the impact of the global financial crisis on SMEs in Kenya.
ii. To establish the measures that SMEs employed to counter the effects of the global financial crisis.

1.4 Significance of the study

Academic institutions in any country are bestowed with the duty of creating and disseminating knowledge. Findings of this research as regards to the effects of the global financial crisis on SMEs in Kenya and the steps these SMEs undertook to counter the

crisis form a basis from which the teaching fraternity can refer during their day to day activities while at the same time as a reference for further research for those who may want to pursue the subject further. Results of this study also find practical application in SME organizations whose managers are faced with the question of what to do to remain afloat in the face of a global financial crisis. The research results also give the banking sector a glimpse into the effects that the crisis has had on SMEs and this probably will inform their decisions as far as provision of services like credit to SMEs are concerned.

Policy makers and especially the government stand to benefit from the study's recommendations regarding policy measures that could alleviate the effects of the financial crisis and ensure that SMEs do not go under but continue to flourish and thus improve the standards of living of Kenyans by giving them a source of earning through (employment).The research also benefits shareholders of companies in respect to returns on investments expected during financial turmoil.

Credit and risk department in financial institutions stand to understand the expected business cycle in a company and determine lending methodologies that will accommodate such companies. Investors in SME business and especially the equity investors will also benefit from the understanding of how SME businesses are affected by financial crisis and how to cushion themselves from the turmoil while generating maximum returns.

1.5 Scope and Limitations of the study

This research considers the client base of BOA, KCB and Equity bank in the SMEs category. The following are some of the major shortcomings to encountered in the course of the study: The nature of this research in terms of measurability requires a relatively longer period of time to conclusively determine the effects of the financial crisis on SMEs in Kenya because the contagion process is somewhat slow. The time allocated for researching this phenomenon was thus not enough to produce conclusive evidence on its

impact. The short time period allocated for research also impairs the ability to consider larger samples for study since a lot of time is required to collect data.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter covers available and relevant literature on the study phenomena. Its objective was to (from a survey of empirical and theoretical literature); capture existing information pertinent to the impacts of the global financial crisis on SMEs in Kenya. The existing research gaps were also identified and how this study fills these gaps discussed. In summary, the chapter looked at the underlying theories of financial instability and both global and local empirical studies on the impacts of the global financial crisis on SMEs.

2.2 Theoretical Review

2.2.1 Theory of Financial Instability

The financial instability hypothesis has both empirical and theoretical aspects. The readily observed empirical aspect is that, from time to time, capitalist economies exhibit inflations and debt deflations which seem to have the potential to spin out of control. In such processes the economic system's reactions to a movement of the economy amplify the movement--inflation feeds upon inflation and debt-deflation feeds upon debt-deflation, Hyman, (1992). Government interventions aimed to contain the deterioration seem to have been inept in some of the historical crises. These historical episodes are evidence supporting the view that the economy does not always conform to the classic precepts of Smith and Walras: they implied that the economy can best be understood by assuming that it is constantly an equilibrium seeking and sustaining system.

The financial instability hypothesis incorporates the Kalecki, (1965), Levy, (1983) view of profits, in which the structure of aggregate demand determines profits. In the skeletal model, with highly simplified consumption behavior by receivers of profit incomes and wages, in each period aggregate profits equal aggregate investment. In a more complex (though still highly abstract) structure, aggregate profits equal aggregate investment plus

the government deficit. Expectations of profits depend upon investment in the future, and realized profits are determined by investment: thus, whether or not liabilities are validated depends upon investment. Investment takes place now because businessmen and their bankers expect investment to take place in the future.

The financial instability hypothesis, therefore, is a theory of the impact of debt on system behavior and also incorporates the manner in which debt is validated, Hyman, (1992). In contrast to the orthodox Quantity Theory of money, the financial instability hypothesis takes banking seriously as a profit-seeking activity. Like all entrepreneurs in a capitalist economy, bankers are aware that innovation assures profits. Thus, bankers (using the term generically for all intermediaries in finance), whether they be brokers or dealers, are merchants of debt who strive to innovate in the assets they acquire and the liabilities they market. This innovative characteristic of banking and finance invalidates the fundamental presupposition of the orthodox Quantity Theory of money to the effect that there is an unchanging "money" item whose velocity of circulation is sufficiently close to being constant: hence, changes in this money's supply have a linear proportional relation to a well defined price level. According to Hyman, (1992), three distinct income-debt relations for economic units, which are labeled as hedge, speculative, and Ponzi finance, can be identified. Hedge financing units are those which can fulfill all of their contractual payment obligations by their cash flows: the greater the weight of equity financing in the liability structure, the greater the likelihood that the unit is a hedge financing unit. Speculative finance units are units that can meet their payment commitments on "income account" on their liabilities, even as they cannot repay the principle out of income cash flows. Such units need to "roll over" their liabilities: (e.g. issue new debt to meet commitments on maturing debt).

Governments with floating debts, corporations with floating issues of commercial paper, and banks are typically hedge units. For Ponzi units, the cash flows from operations are not sufficient to fulfill either the repayment of principle or the interest due on outstanding

debts by their cash flows from operations. Such units can sell assets or borrow. Borrowing to pay interest or selling assets to pay interest (and even dividends) on common stock lowers the equity of a unit, even as it increases liabilities and the prior commitment of future incomes Hyman, (1992). A unit that Ponzi finances lowers the margin of safety that it offers the holders of its debts. It can be shown that if hedge financing dominates, then the economy may well be an equilibrium seeking and containing system.

In contrast, the greater the weight of speculative and Ponzi finance, the greater the likelihood that the economy is a deviation amplifying system. The first theorem of the financial instability hypothesis is that the economy has financing regimes under which it is stable, and financing regimes in which it is unstable, (Hyman, 1992). The second theorem of the financial instability hypothesis is that over periods of prolonged prosperity, the economy transits from financial relations that make for a stable system to financial relations that make for an unstable system.

In particular, over a protracted period of good times, capitalist economies tend to move from a financial structure dominated by hedge finance units to a structure in which there is large weight to units engaged in speculative and Ponzi finance, (Hyman, 1992). Furthermore, if an economy with a sizeable body of speculative financial units is in an inflationary state, and the authorities attempt to exorcise inflation by monetary constraint, then speculative units will become Ponzi units and the net worth of previously Ponzi units will quickly evaporate. Consequently, units with cash flow shortfalls will be forced to try to make position by selling out position. This is likely to lead to a collapse of asset values. The financial instability hypothesis is a model of a capitalist economy which does not rely upon exogenous shocks to generate business cycles of varying severity. According to Hyman, (1992) the financial instability hypothesis holds that business cycles of history are compounded out of

(i) The internal dynamics of capitalist economies, and

(ii) The system of interventions and regulations that are designed to keep the economy operating within reasonable bounds.

2.2.2 Theories of Financial Intermediation

Understanding of the role or roles played by these intermediaries in the financial sector is found in the many and varied models in the area known as intermediation theory. In the traditional Arrow-Debreu model of resource allocation, firms and households interact through markets and financial intermediaries play no role. When markets are perfect and complete, the allocation of resources is Pareto efficient and there is no scope for intermediaries to improve welfare. Moreover, the Modigliani-Miller theorem applied in this context asserts that financial structure does not matter: households can construct portfolios which offset any position taken by an intermediary and intermediation cannot create value, (Fama (1980).

These theories of intermediation have built on the models of resource allocation based on perfect and complete markets by suggesting that it is frictions such as transaction costs and asymmetric information that are important in understanding intermediation. First, and that which is used in most studies on financial intermediation, is the informational asymmetries argument. These asymmetries can be of an *ex ante* nature, generating adverse selection, they can be interim, generating moral hazard, and they can be of an *ex post* nature, resulting in auditing or costly state verification and enforcement. The informational asymmetries generate market imperfections. Many of these imperfections lead to specific forms of transaction costs. Financial intermediaries appear to overcome these costs, at least partially. For example, Diamond and Dybvig (1983) consider banks as coalitions of depositors that provide households with insurance against idiosyncratic shocks that adversely affect their liquidity position.

Second, is the transaction costs approach which in contrast to the first, this approach does not contradict the assumption of complete markets. It is based on non convexities in transaction technologies. Here, the financial intermediaries act as coalitions of individual

lenders or borrowers who exploit economies of scale or scope in the transaction technology. The notion of transaction costs encompasses not only exchange or monetary transaction costs, Fischer, (1983), but also search costs and monitoring and auditing costs (Benston and Smith, 1976). Here, the role of the financial intermediaries is to transform particular financial claims into other types of claims (so-called qualitative asset transformation). As such, they offer liquidity (Pyle, 1971) and diversification opportunities (Hellwig, 1991). The provision of liquidity is a key function for savers and investors and increasingly for corporate customers, whereas the provision of diversification increasingly is being appreciated in personal and institutional financing.

The third approach to explain the raison d'être of financial intermediaries is based on the regulation of money production and of saving in and financing of the economy (Merton, 1995b). Regulation affects solvency and liquidity with the financial institution. The legal-based view sees regulation as a crucial factor that shapes the financial economy (La Porta et al., 1998). Many view financial regulations as something that is completely exogenous to the financial industry. However, the activities of the intermediaries inherently "ask for regulation". This is because they, the banks in particular, by the way and the art of their activities (i.e. qualitative asset transformation), are inherently insolvent and illiquid (Merton and Bodie, 1993). Furthermore, money and its value, the key raw material of the financial services industry, to a large extent is both defined and determined by the nation state, i.e. by regulating authorities *par excellence*.

A traditional criticism of these standard market-based theories is that a large number of securities are needed for it to hold except in special cases. However, the development of continuous time techniques for option pricing models and the extension of these ideas to general equilibrium theory have negated this criticism. Dynamic trading strategies allow markets to be effectively complete even though a limited number of securities exist.

Such an extreme view - that financial markets allow an efficient allocation and intermediaries have no role to play- is clearly at odds with what is observed in practice. Historically, banks and insurance companies have played a central role. This appears to be true in virtually all economies except emerging economies which are at a very early stage. Even here, however, the development of intermediaries tends to lead the development of financial markets themselves, McKinnon (1973).

2.2.3 Kitchin's Theory

Kitchin, (1923) identified 3-5-year economic cycles mainly linked to company inventories - which cause fluctuations in economic performance. This research was based on statistical data published by the financial institutions of the USA and the United Kingdom between 1890 and 1922.

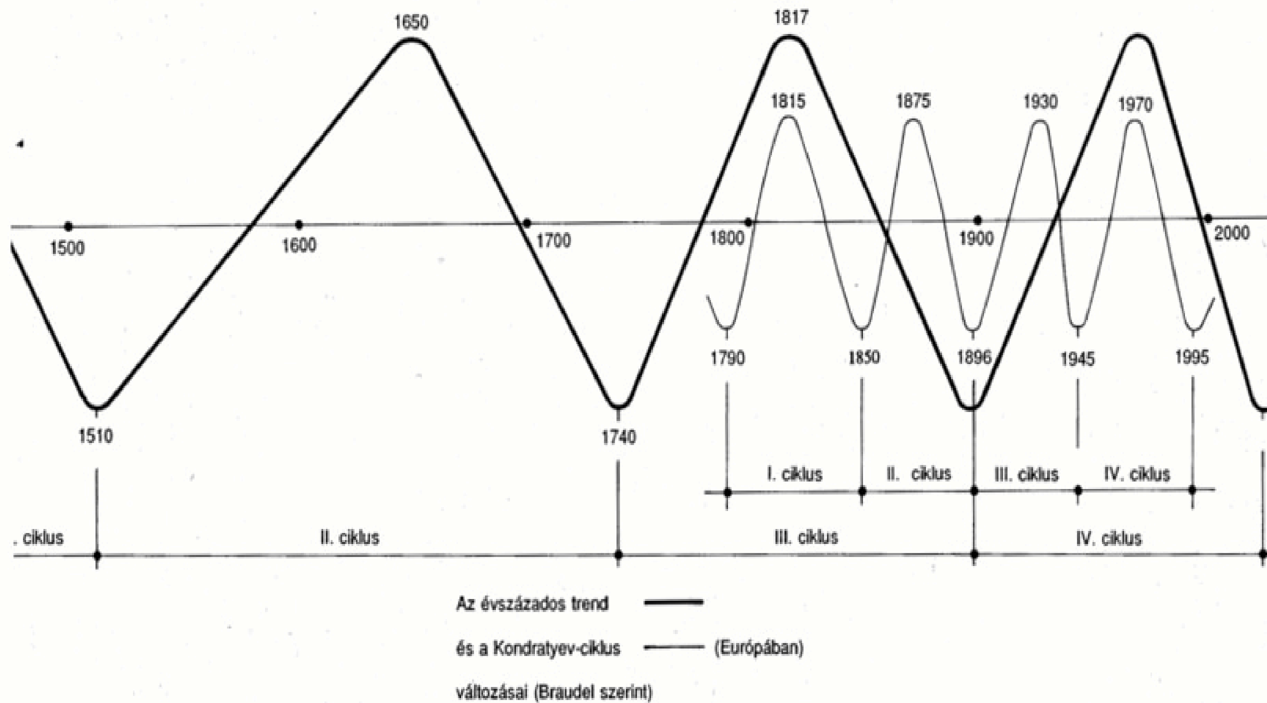
2.2.4 Juglar's Theory

The research by Juglar focuses our attention on longer periods. The theory, which mainly refers to sectors and is based on fixed investment cycles, defines 7-11 year periods in which the trough between waves is shown by overproduction and financial market crises. The periodicity of this cycle can be seen clearly in connection with the current collapse of stock market prices and also, for example, in similar movements during the earlier Russian financial crisis. Since the reappearance of major infrastructural investment by companies is visible within such periods.

2.2.5 Kondratiev Long Wave Cycles Theory

One of the most popular theories is that of the Kondratiev Long Wave Cycles. The Kondratiev theory, formalized in 1920 but neglected until the 1929 world crisis, identifies 45-60 year-long periods (see figure 1). Both the up-slopes and down-slopes of the wave have their different repetitive characteristics. Before the up-slopes begin, significant changes can be observed in economic conditions: methods of production and exchange change radically, the use of technical innovation accelerates and new money transmission methods are introduced. At the improvement stage, the social shocks, wars and tensions

increase in frequency. During down-slopes the price-gap between agricultural and industrial products increases and a prolonged agricultural depression appears.



Source: Kehl, D., Sipos, B. (2009).

Figure 1: Constructive and destructive interference of the Kondratiev cycles and the secular trend

The secular trend cycle span an even longer periods of time than does the Kondratiev cycle. These cycles, of varying lengths, can enhance or attenuate each other's effects – as can the wavelike motions known from physics – depending on whether the direction of the waves as they meet is the same or the opposite (see figure 1). Kondratiev established in his original work that the medium-term cycles (Juglar) conform to the long-term. During the down-slope, periods of long and deep depression are seen in the Juglar cycles, whereas, in the up-slopes of the K-waves, an increasing proportion of the Juglar cycle shows both longer and stronger development.

2.3 Empirical Studies on the Financial Crisis

As Nikolson, (2008), recognized that financial crisis which initiated in United States has now become a global phenomenon. At present, not only in United States but across Asia and Europe, stock exchanges crashed; collective losses of the London, Paris and Frankfurt markets alone amounted to more than 350 billion Dollars. Stock Exchange 100 index closed more than 323 points down in January 2008, Times online, (2008). This crisis apart from affecting the capitalist economies has distressed the Socialist economy like Russia as well; in May 2008 Russian stock market was fallen by 50% and the Russian central bank had to buy rouble in massive amount to prevent the severe falling against US Dollar and Euro, Erkkilä, (2008). As regards the cause of the current crisis Bartlett, (2008) said that the crisis was started with the downfall of US sub-prime mortgage industry, the intensity of this collapse was significant. Mark-to-market losses on mortgage backed securities, collateralized debt obligations, and related assets through March 2008 were approximately $945 billion, Bartlett, (2008). He further stated that it is the largest financial loss in history, as compared to Japan's banking crisis in 1990 about $780 billion, losses stemming from the Asian crisis of 1997-98 approx. $420 billion and the $380 billion savings and loan crisis of U.S itself in 1986-95.

Yılmaz, (2008) charged U.S subprime mortgage industry to be the major reason of current global financial crisis, he also stated that the total loses estimated initially up to $300 to $600 billion are now considered to be around $1 trillion. While enlightening the factors as to why this US sub-prime mortgage crisis turn into global banking crisis, Khatiwada and McGirr (2008) stated that many of these sub-prime mortgages actually never made it on the balance sheets of the lending institutions that originated them; and they were made attractive to foreign banks by high investment grading. When sub-prime borrowers failed to repay their mortgages, the originating institution needed to finance the foreclosure with their own money, bringing the asset back on its balance sheet. This left many banks in a financially unviable situation, in a rather short, unmanageable timeframe.

However Hyun-Soo (2008) argues that it was the "Trust Crisis" which caused this global predicament. DeBoer (2008) believes that it was a series of events which caused the crisis; it begins with the collapse of currencies in East Asia in 1997 and became edgy due to the financial crisis of Russia in 1998. Next, in USA was the "dot-com" stock collapse in 2001, and the final stroke was again in USA, when after a swift decline in housing prices and "rapid contraction in credit, it fell into recession. Rasmus (2008) has the same thoughts; he, while discussing the reasons of economic recession of U.S said that the 'real' ailments afflicting the US economy for more than a quarter-century now include sharply rising income inequality, a decades-long real pay freeze for 91 million non-supervisory workers, the accelerating collapse of the US postwar retirement and healthcare systems, the export of the US economy's manufacturing base, the near-demise of its labor unions, the lack of full time permanent employment for 40 per cent of the workforce, the diversion of massive amounts of tax revenues to offshore shelters, the growing ineffectiveness of traditional monetary and fiscal policy, and the progressive decline of the US dollar in international markets.

2.4 Local Empirical Studies on Impact of the Financial Crisis on Business

It has been argued that African banks are insulated from foreign finance, as they rely on domestic deposits and lending and do not have derivatives or asset-based securities among their portfolios, Mwega, (2008). According to Shanta Devarajan, Chief Economist of the Africa region at the World Bank (2008), 'African banks retain loans they originate on their balance sheets, the interbank market is small, and the market for securitized or derivative instruments is either small or nonexistent'. Even though some banks have significant foreign ownership, their parent banks are typically not in the US and the foreign ownership share is less than 5%, compared with an average of 40% in other developing countries.

In the year 2008, Kenyan Banks' profitability has substantially declined substantially Mwega, (2008). In the capital market, by March 2009 the Nairobi Stock Exchange (NSE)

20-Share Index had fallen to a near seven-year low. It improved between March and June 2009, slumped in July-September of the same year and increased marginally by about 5% between end-September and December 2009 (0.8% in October, 4.1% in November and -0.1% in December 2009) as investors focused their portfolio on the bond market. Data on foreign direct investment (FDI) show a substantial decline in 2008 to a more normal level ($50 million) following an upsurge in 2007**.**

From a major decline in 2008, the tourism sector experienced some recovery in 2009. According to some estimates, by November 2009 tourism arrivals and earnings were up 90% from 2008. Tea exports, on the other hand, increased by 5.4% and earnings by 36.2% in 2008. Despite a production shortfall in 2009, earnings from tea exports increased by 17% in the first half of 2009 as a result of increased tea prices Mwega, (2008).. Horticultural exports increased by 4.5% and earnings by 24.6% in 2008. Between January and August 2009, however, output declined, attributed mainly to a decline in flower production, which dropped 30% by October 2009, with exports moving in the same direction. The volume of coffee exports declined by 24.5% in 2008, with coffee earnings roughly unchanged. Coffee production peaked at 130,000 metric tonnes in the 1988/89 crop year, systematically declining since then. Less than 54,000 metric tonnes of coffee exports were expected in 2009.

Remittances from the Kenyan diaspora increased by 6.6% in 2008. In the first 10 months of 2009 they declined slightly, to $504.6 million, compared with $527.1 million in the same period in 2008 but more than $476.7 million in 2007. The database of the Organization for Economic Development's Development Assistance Committee (OECD-DAC) shows a substantial increase in foreign aid to the country in 2008. Kenya received $1523 million in 2008 (compared with $1345 million in 2007), with committed funds fully disbursed in 2009 compared with only 53% in 2008, reflecting the urgency of the situation. With the global financial crisis and other crises, current account and budget deficits have widened. The current account deficit rose from $2.12 billion in 2008 to $2.388 billion in the year to August 2009, affecting the exchange rate and foreign

exchange reserves. Implementation of the 2008/09 budget also faced numerous challenges, which included inability to achieve revenue targets and additional drought-related expenditures. In the 2009/10 fiscal year, the government adopted an expansionary fiscal stance. A budget deficit of KSh109 billion (about 6% of gross domestic product (GDP)) is envisaged, with concerns that heavy borrowing will crowd out lending to the private sector Mwega, (2008).

According to an April 2009 IMF forecast, sub-Saharan African growth is projected at 1.5% in 2009 before recovering to just fewer than 4% in 2010, which is still below the pre-crisis level Kang'aru, (2009). According to the African Development Bank (AfDB)/Organisation for Economic Co-operation and Development (OECD), African economic growth will fall to 2.8% in 2009, less than half the rate forecast before the onset of the global slowdown (Reuters, 2009). The ratio of NPLs to assets is an indicator of banks' lack of asset quality and financial soundness. In the case of the current financial turmoil, a high ratio may indicate that banks are not healthy, since they have significant exposure to the origins of the problem. In Kenya, the NPL/assets ratio decreased from a high of 23.27% in 2000 to a low of 4.02% in 2008, an indication that the banking system's asset quality had improved. This may be attributed to the requirements for bad loans provisions and increased core capital mandated by CBK. According to CBK, net NPLs as a share of total loans declined from 2.9% in March 2008 to 2.2% in November 2008. This was accompanied by increased provisions for bad loans in 2005 and 2006, with a decline thereafter in 2007 and 2008. However, there is some evidence that the ratio increased slightly in 2009. According to CBK's September 2009 Monthly Economic Review, the ratio of net NPL to gross loans increased from 3.4% in August 2008 to 3.7% in August 2009. CBK has accused commercial banks of fuelling loans defaults by charging borrowers high interest rates (Kang'aru, 2009b).

2.5 Conclusion

From the reviewed literature, much has been said and written about past global financial crises but the 2008/2009 financial crisis has attracted the most global attention presumably due to its adverse effects and global reach despite its origin having been in the United States as noted by (Nikolson, 2008). Different scholars have tried to argue the origin of the crisis but the most notable one being Yılmaz, (2008) who argues that when sub-prime borrowers failed to repay their mortgages, the institution of origin needed to finance the foreclosure with their own money, bringing the asset back on its balance sheet. This left many banks in a financially unviable situation, in a rather short, unmanageable timeframe. The negative effects of the financial crisis on the local scene was felt in various sectors of the economy which was seen through a fall in export earnings for the tourism and agricultural sector Mwega, (2008), decreased credit /money occasioned by a drop in Diaspora remittances, (OECD-DAC, 2008), and current account and government budget deficits widened.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter describes the research design, population and sampling design, the data collection techniques, the research procedures and data analysis methods that were used in the study. This section also indicates the research tool that was used to collect data, the data collection and analysis procedures.

3.2 Research Design

This study used a descriptive research design to describe the impact of the financial crisis and the measures which SMEs adopted to emerge out of the crisis. A descriptive study is concerned with finding out who, what, where or how much, (Cooper and Schindler, 2001). They further state that a descriptive study is used when one needs to determine characteristics associated with a subject population which this study was actually concerned with for example the background information on SMEs in Kenya such as annual turnover, number of employees and so on.

Descriptive research designs help in gathering information from large groups of people and also allow us to assess a wider variety of behaviors. Ngechu, (2002) states that a descriptive study brings about several advantages. These are; it helps give testable hypotheses, it also educates conjecture, brings out correlation relationships e.g. young machinists (under 35 years of age) are less productive than those who are 35 years of age or older. It also brings out an explanation based on cause and effect i.e. meaning roughly to "help make happen" independent variable being the causal agent on dependent variable e.g. an increase in family income leads to an increase on the percentage of income saved.

3.3 The Study Population

Target population in statistics is the specific population about which information is desired. According to Ngechu (2004), a population is a well defined set of people, services, elements, and events, group of things or households that are being investigated. This definition suggests that the population of interest is homogeneous. The population in research means complete census of the sampling frames. In most cases since it is not possible to study the entire population, a sample (subset of the population) is selected and studied in detail either for purposes of generalization or simply for better understanding the phenomena under investigation. In a case study, a sample is selected to provide a basis of studying a phenomenon in detail. The study population of the study was made up of all the SME customers of BOA, KCB and Equity bank. A sample size of 60 respondents was used in this study of a possible population size of 10,000 SME customers.

3.4 Sampling Technique

The target respondents were selected using a simple random sampling method. With this sampling method, respondents had an equal chance of being selected to participate in the study. Copper et al (2001) assert that the basic idea of sampling is that by selecting some of the elements in a population, conclusions may be drawn about the entire population. They identify that there are several advantages of sampling as opposed to a census. These are lower costs, greater accuracy in results, greater speed of data collection and the availability of population elements is higher. Based on the above assertions, used purposive sampling technique. Copper et al (2001) also propose that the ultimate test to a sample design is how well it represents the characteristics of the population it purports to represent. The sample must be valid. The validity of a sample depends on two considerations: accuracy and precision. The purposive sampling design is aimed at ensuring high accuracy and precision.

3.5 Data Collection Method

The study utilized a quantitative data collection technique. The data collection tool was a questionnaire which by definition is a group of structured questions with each item in the questionnaire developed to address a specific objective, research question or hypothesis of the study (Olive and Mugenda, 2003).This tool of data collection was chosen due to the ease with which it can be administered. It has been widely asserted that a self administered questionnaire is the most efficient and cost effective method used to collect data pertaining to the various aspects of public behaviour (Yoo et al, 2000); (Washban and Plank, 2000). In this study the questionnaire had 2 distinct parts: The first part collected background information from respondents. The second part was the main questionnaire intended to determine impacts of the global financial crisis on SMEs in Kenya. The questionnaire had closed and open ended questions measured on a 5. Likert scale where 1 = No 2 = to a small extent, 3 = to a medium extent 4= to a large extent, 5= to a very large extent. There were also numerous open- ended questions that sought further explanations from the respondents.

3.6 Data Analysis Method

The collected data was edited centrally, Coppers and Schindller (2000) to detect errors and omission, ensure data was accurate, uniformly entered, complete, consistent with intent of the question and other information in the survey and arranged to simplify coding and tabulation. Alpha numeric data coding was carried out to assign numbers and other symbols to the questions, which Coopers and Schindler (2000) explain is done in order to group the respondents to a limited number of classes or categories that facilitate efficient analysis.

Coded data was then tabulated in Statistical Package for Social Science (SPSS version 16.0). Descriptive statistics (frequencies and percentages) were then used to evaluate the responses. The results of analysis were presented in a tabulated format and charts used to present the information.

3.7 Analysis of Questionnaire Reliability

Before the study was carried out, a sample of 20 responses were collected for testing the reliability of the survey instrument. The method for testing reliability was Cronbach's Alpha reliability coefficient test. The decision to accept Likert scales of measurement in the instrument were arrived at using the guide of (George and Mallery 2003). The guide is as follows;

C > .9 – Excellent,

C > .8 – Good

C > .7 – Acceptable

C > .6 – Questionable

C > .5 – Poor, and

C < .5 – Unacceptable

Where C is the value of Chronbach's Alpha Coefficient.

Cronbach's alpha reliability coefficient normally ranges between 0 and 1. However, there is actually no lower limit to the coefficient. The closer Cronbach's alpha coefficient is to one, the greater the internal consistency of the items in the scale. Cronbach's Alpha for this study's data collection instrument was approximately 0.8.

CHAPTER FOUR

DATA ANALYSIS AND INTERPRETATION

4.1 Introduction

This chapter discusses findings of the data analyzed together with their interpretations. The data was analyzed using the Windows based Statistical Package for Social Science version 16.0.The output was then processed thematically and organized into subtopics that reflect the different questions that were posed to respondents in the questionnaires. This chapter begins by outlining characteristics of the Small and Medium Scale enterprises in Kenya followed by results of the impact of the financial crisis on SMEs in Kenya. Finally the chapter discusses some of the measures undertaken by the firms surveyed to counter the effect of the financial crisis.

4.2 Factor Analysis

Table 1: Total Variance Explained for impact of financial crisis on SMEs

Component	Initial Eigen values			Extraction Sums of Squared Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	2.975	59.495	59.495	2.975	59.495	59.495
2	.759	15.175	74.670			
3	.563	11.266	85.936			
4	.440	8.804	94.741			
5	.263	5.259	100.000			

From the table above there is only one factor that has an Eigen value greater than one. These means that only one variable has enough contribution to explain the variances of the variables. Given this there is no need to carry out a rotation comparative matrix because there is not more than one factor to carry out detailed analysis.

Principal components analysis method of extraction was used to explore the correlation between the defined variables in the questionnaire that measured the impact of the financial crisis on SMEs and the steps these SMEs undertook to counter the crisis.

Table 2: Total Variance Explained

Component	Initial Eigen values			Extraction Sums of Squared Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	4.582	50.915	50.915	4.582	50.915	50.915
2	1.517	16.855	67.770	1.517	16.855	67.770
3	1.223	13.586	81.356	1.223	13.586	81.356
4	.658	7.310	88.666			
5	.412	4.575	93.242			
6	.301	3.350	96.592			
7	.130	1.440	98.031			
8	.099	1.101	99.132			
9	.078	.868	100.000			

Table 2 shows that there are three factors derived from the Eigen values that are greater than one. It also means that out of the 9 variables only 3 contribute significantly to the explanation of variance in the variables, 81.4% to be exact. The first variable alone contributes 50.9% cumulative percent.

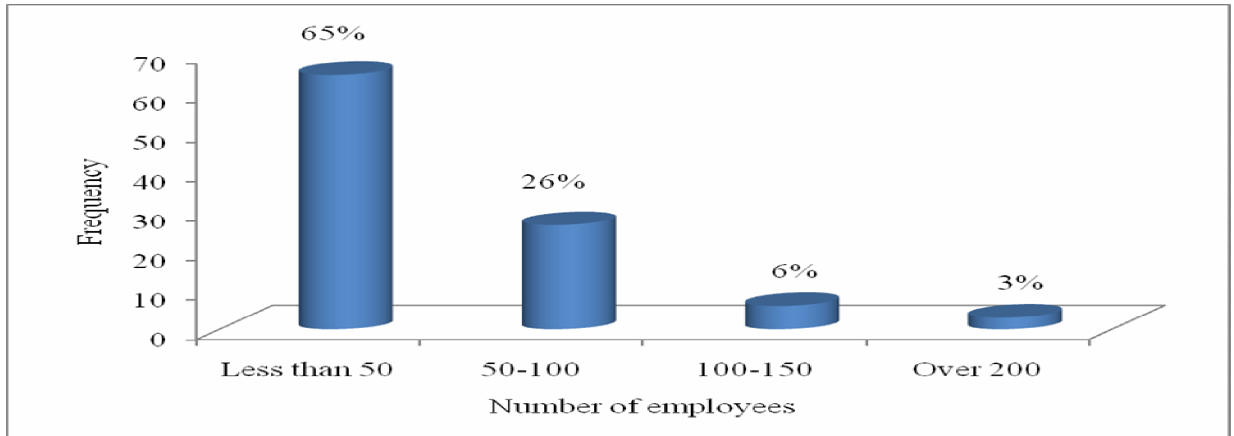
Table 3 component matrix on solution to financial crisis

	Component		
	1	2	3
Do nothing	.216	-.184	**.872**
Workforce downsizing	**.780**	.371	-.126
Postpone investment	**.749**	.528	-.142
Reduce organizational costs	**.446**	**.593**	.488
Freezing of wages	**.896**	.018	.209
Increasing marketing budgets	-.606	-.305	**.349**
Search for new markets	-.817	**.423**	.054
Reformation of old business strategies	-.800	**.500**	.025
Increase organizational effectiveness	-.830	**.439**	.137

Factor one, cost reduction; consists of workforce downsizing, postponing investment, reduce organizational costs and freezing of wages. Factor 2, strategic includes searching for new markets, reforming old strategies and increasing effectiveness the final factor, status quo includes doing nothing and increasing marketing budgets, though increasing marketing budget contributes a very low percentage (34.9%).

4.3 Characteristics of SMEs Surveyed

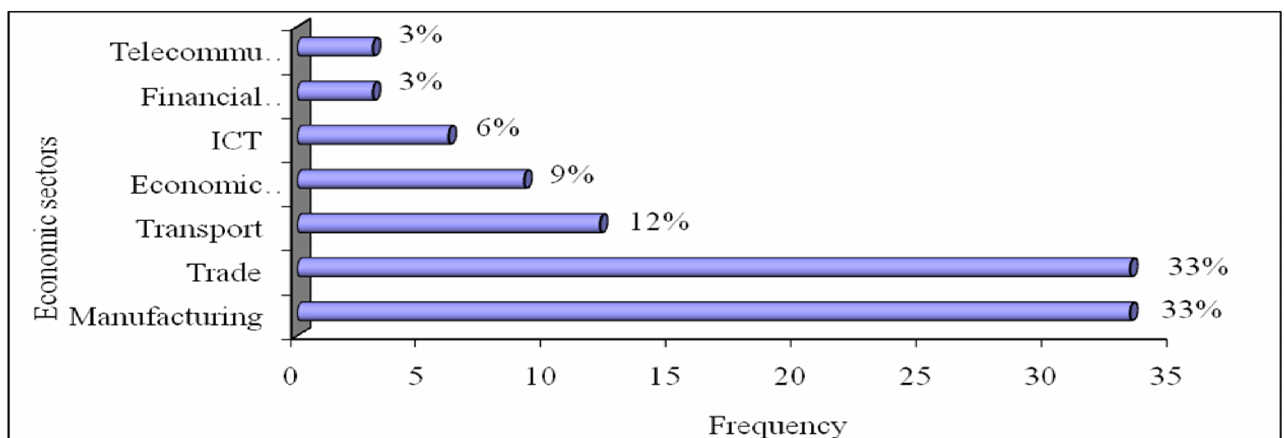
4.3.1 Number of employees



Source: primary data 2010

The great majority (65%) of the respondents have fewer than 50 employees. This is followed by those with 50-100 employees at 26%. The proportion of those with more than 200 is only 3%. On the other hand, those with 100-150 employees are were 6% of the sample.

4.3.2 Economic sectors of respondents surveyed

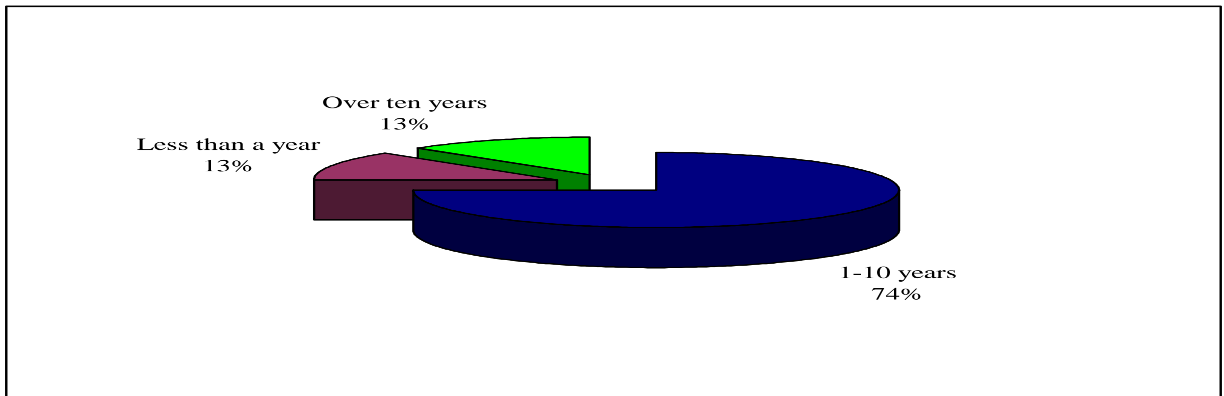


Source: primary data 2010

The Trade and Manufacturing sectors represented the highest number of sample members with both scoring a frequency of 33% (66% if combined). The transport sector came in second with 12% of the total respondents. The economic services sector had 9% of

respondents while ICT stood at 6%. Telecommunications and the financial sector contributed the least number of sample members both of which were 3%.

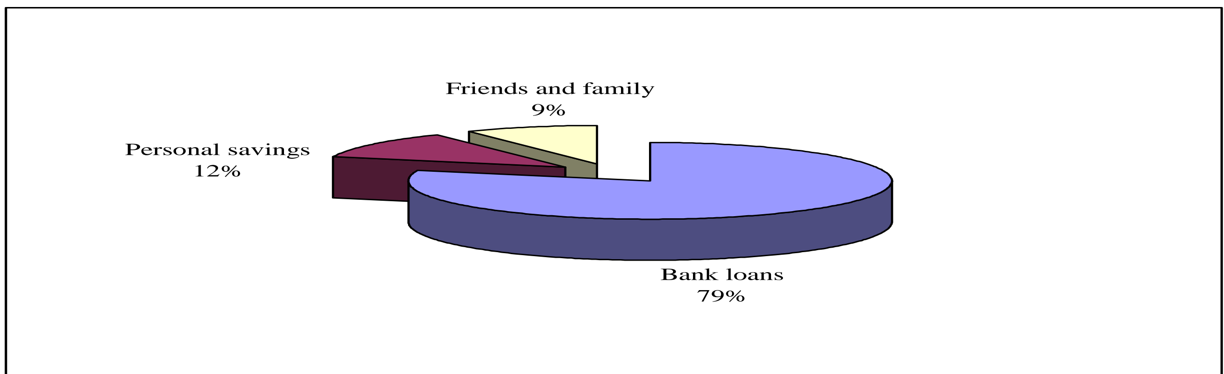
4.3.3 Years of operation of the firms studied



Source: primary data 2010

This research sought to establish the number of years the firms under study had been in operation and the majority (74%) claimed to have been operating for less than 10 years. Those that had been in operation for over ten years were 13% of the sample which is equivalent to those that had operated for less than a year at the time this research was carried out.

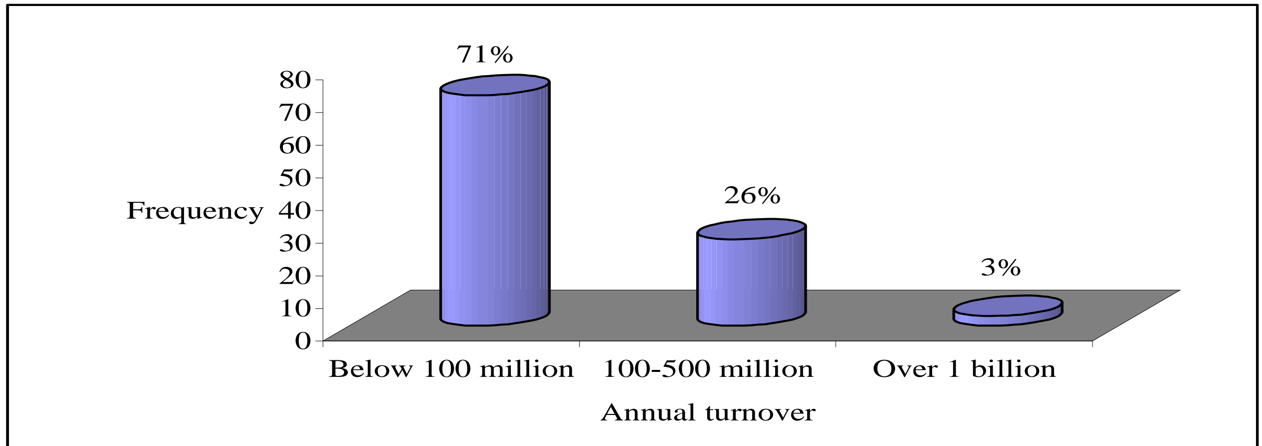
4.3.4 Sources of funding for SMEs surveyed.



Source: primary data 2010

An overwhelming majority (79%) of firms surveyed fund their businesses through bank loans. Just a handful (12%) and (9%) fund their operations through personal savings and friends and family respectively.

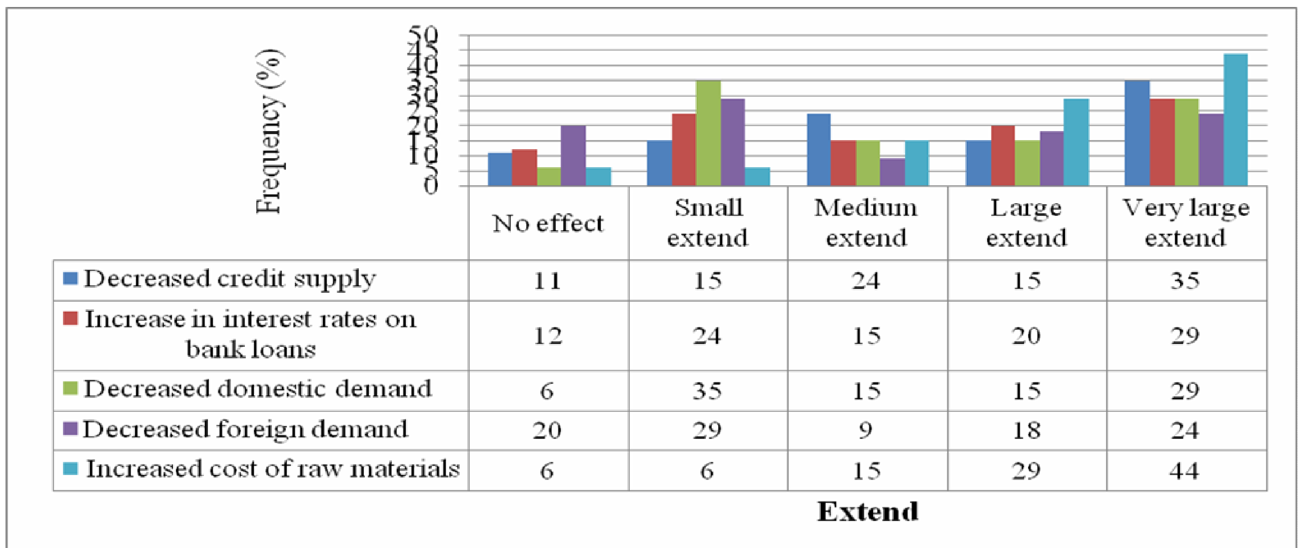
4.3.5 Annual turnover



Source: primary data 2010

Most of the firms in the study have an annual turnover of below 100 million Kenya shillings. Those with annual turnover of between 100 and 500 million were 26%. The minority (3%) had over 1 billion Kenya shillings in annual turn over.

4.4 Impact of the financial crisis on SMEs



	No effect	Small extend	Medium extend	Large extend	Very large extend
Decreased credit supply	11	15	24	15	35
Increase in interest rates on bank loans	12	24	15	20	29
Decreased domestic demand	6	35	15	15	29
Decreased foreign demand	20	29	9	18	24
Increased cost of raw materials	6	6	15	29	44

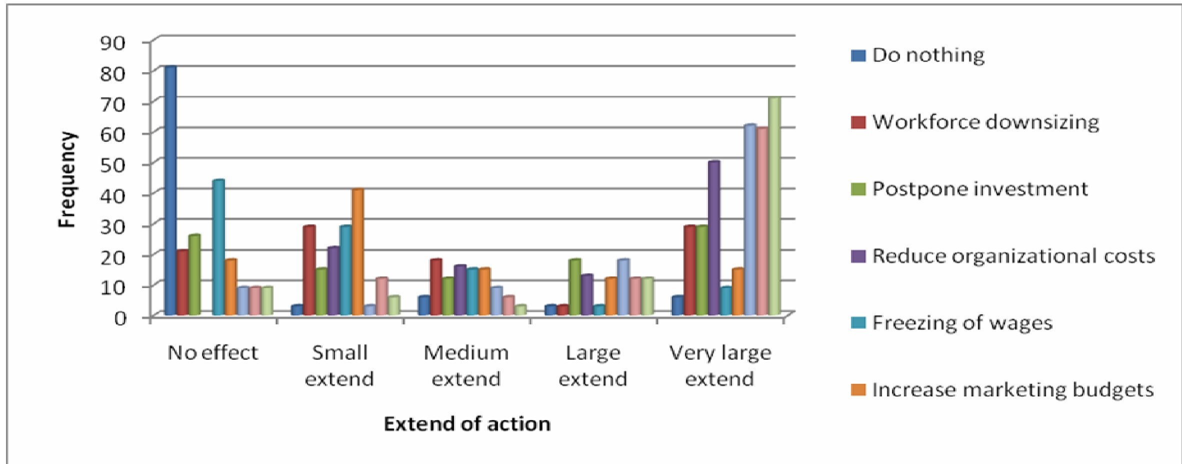
As has been shown by results of this study, majority of respondents (79%) rely on bank loans in financing their operations and a decrease in credit supply that was occasioned by the financial melt down was of negative impact to their businesses to a very large extend according to 35% or respondents. For another 15% of them shortage in credit supply had

a negative impact to a large extend while those who felt that it was to a medium extend were 24%. There were those who still felt that the extend of the negative effect of credit supply shortage was only small and they formed 15% of the total sample. 12% did not feel any impact of the credit supply shortage and these are the SMEs that rely on personal savings and friends and families to finance their businesses and as can be been they are only a handful as far as this study is concerned. Likewise, it is plausible to claim that the global financial crisis had an impact to at least 89% of the SMEs surveyed by causing a shortage in credit supply.

It is also notable that the financial crises led to an increase in lending rates by banks according to at least 88% of respondents a proportion which this study shows rely on bank loans to finance their operations. This increase in interest rates was perhaps a strategy aimed in discouraging borrowing to avoid loan defaults which was synonymous with the financial crisis of 2008-2009. This increased interest rates impacted 29%, 21% 15% and 24% to a very large extent, to a large extend, to a medium extend and to a small extend respectively. Some 29% of respondents indicated that a decrease in domestic demand by consumers as a result of their decreased purchasing power owing to the financial crisis impacted their businesses to a very large extend. Those that were affected to a medium and large extend comprised 30% of the sample and 35% were only affected to a small extend. This brings it to 94% of the total SMEs that were affected by the decreased domestic demand during the financial crisis.

Decreased foreign demand seems to have had a relatively minimal impact on SMEs surveyed (79)% were impacted) as compared to (94%) in the case of domestic demand. This is probably due to the fact that most of the SMEs rely on domestic demand for their products. A majority of respondents (44%) were affected to a very large extend by the increased cost of raw materials while 29% were affected to a large extend. Only 6% of the entire sample were not affected at all by rising costs of raw materials.

4.5 Steps taken by SMEs to counter effects of the Global financial crisis



Source: Primary data 2010

Majority of respondents 81% agreed that action needed to be taken to avoid the negative impacts of the crisis and that it was not enough to continue to run the business in the same manner as before the financial crisis. Our questions can be grouped into two categories: The first (1-5) comprise a group of reactive, defensive steps, involving traditional, belt-tightening activities which basically aim to counter the effects of the crisis from a cost-cutting perspective. The second category refers to possible proactive, offensive options. The answers here see solutions in finding a new approach, albeit adapting to change, by capturing new areas and markets through increasing marketing budgets and searching for new markets. It seems obvious that reducing costs has a clear priority for the SMEs, but opinions differ on the way this has to be done. Whilst the need to postpone investment is unequivocal, the companies proved more cautious in connection with redundancy. Just 50% of respondents stated that it was vital to take this step. This proves that despite the hard times during the financial crisis SMEs were still optimistic that this was not the end and therefore their retaining employees would still be beneficial in the long run.

Postponing future investment as a reactionary strategy was supported by 73% of respondents. Reducing organizational costs as another way to tackle the financial crisis

was popular among (74%) of respondents while freezing of employee wages was supported by a relatively smaller proportion of the sample (56%) as compared to other strategies which scored above 70% among respondents. Search for new markets and increasing market budgets were agreeable among 91% and 82% of respondents respectively. Reformation of old business strategies and increasing organizational effectiveness both scored 91% as favorable strategies for alleviating the impact of the financial crisis.

4.6 Summary of findings and interpretation

Most of the firms surveyed had a great majority of respondents of fewer than 50 employees with trade and manufacturing sector representing the highest number of sample members with both scoring a frequency of 66%.The research also established that majority of the firms under the study had been operating for less than 10years(74%),with majority having turnover below 100mio(71%) and their major source of financing being bank loans

From the study, 89% of the SME surveyed claim that the financial crisis had an impact on their businesses by causing a shortage in credit supply.It is also notable that the financial crisis led to an increase in lending rates by banks with 29% of the respondents having been impacted to a large extend. A majority of the respondents (44%) were affected to a very large extend by the increased cost of raw material as a result of the global financial crisis.

Principal components analysis method of extraction was used to explore the correlation between the defined variables in the questionnaire that measured the impact of the financial crisis on SMEs and the steps these SMEs undertook to counter the crisis. The communalities tables for both table one and table two variables show the variance explained for in our factor solution. Decreased foreign demand doesn’t seem to fit into

this factor solution due to its small communality value (0.460). All the variables in table two did fit in the factor analysis solution given the high communality values i.e. above 0.581. In terms of correlation, variables in first table regarding the impact of the financial crisis showed significant correlations with each other as indicated in the component matrix table one i.e above 0.678. On the other hand, variables in table two showed statistically insignificant correlation with each other as indicated by the component matrix table two above.

CHAPTER FIVE

CONCLUSIONS AND RECOMMENDATIONS

5.1 Conclusions

It would be unreasonable to examine SMEs behaviour in the face of the crisis merely from a knowledge-management point of view, and it is clear that social interactions and emotions have a strong influence on decision-making. However, it cannot be deduced from the answers given that companies shy away from lay-offs on these grounds alone.

During the 2008-2009 global financial crisis SMEs in Kenya applied different methods to ride out the storm. Their main underlying reason was to achieve short-term survival and avoid the overhanging threat of bankruptcy. However, they put their future at risk in several ways by lay-offs and postponing investments. By losing human capital they jeopardized the innovativeness which ensures flexibility and lost the driving force of growth: their intangible assets. The comprehensive, strategic-level management of knowledge leads to faster growth and to recovery. Earlier crisis management solutions work with little success in the present changed economic environment. However, this survey revealed that SMEs still tend to prefer some of those old solutions which are mostly reactionary and cost-cutting in nature.

5.2 Recommendations

SMEs must avoid short-term survival strategies like employee layoffs in tackling a crisis like the 2008-2009 global financial crisis and should instead focus on strategic-level management of knowledge which leads to faster growth and to recovery in addition to being sustainable in the long-run. SMEs in Kenya should diversify their sources of funding other than borrowing from banks to avoid shortage of funds like was the case when credit supply declined during the global financial crisis. It is important for SMEs to diversify their markets to include foreign ones in order to cushion them against negative impacts of financial melt down which does not affect all regions of the word equality.

5.3 Suggestion for further research

This study was limited in scope and surveyed SMEs in three banks only: Equity bank, Kenya Commercial bank and Bank of Africa. For a better insight on the impact of the Global financial crisis, a similar study should be undertaken on a large scale taking into account SME clients of all banks in Kenya. Further to this, future studies should seek to establish exactly the direct effects that the financial crisis had on financial performance of SMEs which this study did not consider.

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Appendix: The questionnaire

Preamble

Dear respondent,

You are hereby requested to participate in giving your opinions on questions posed herein in regard to the impact of the global financial crisis on access to finance by the Small and Medium Enterprises in Kenya. The information given will be kept secret and used only for the purpose of this study and no personal identity information is required.

Thank you so much for your time.

SECTION A: Background information

Q1 (a) Name of the company

…………………………………………………………………

(b) Approximate number of employees **(Tick as appropriate)**

☐ 1-50 employees ☐ 50-100 employees ☐ 100-150 employees

☐ 150-200 employees ☐ Over 200 employees

Area of Business

Sector	**Frequency (%)**
1.	
2. Financial sector	
3. Trade	
4. ICT	
5. Telecommunications	
6. Transport	
7. Energy	
8. Economic services	
Total	

(d) Number of years in operation (**Tick as appropriate**)

☐ New (less than one year) ☐ 1-10 years ☐ Over ten years

(e) The major source of funding for the business/company

☐ Bank loans ☐ Friends and Family

☐ Personal savings ☐ Donor funding

(d) What is your company's approximate annual turnover in Kenya shillings?

☐ Below 100 million ☐ 100-500 million 500-1billion ☐ over 1 billion

SECTION B: RESEARCH QUESTIONS

Q1. On a Likert scale of 1-5 where 1 = No effect 2 = To a small extent 3 = To a medium extend 4 = To a large extent and 5 = To a very large extend, please indicate how your business/company has been affected by the global financial crisis. Indicate by ticking your option in the table below:

IMPACTS OF THE FINANCIAL CRISIS ON SMEs	**EXTEND OF IMPACT**				
	No effect	To a small extent	To a medium extent	To a large extent	To a very large extent
Decreased credit supply					
Increase in interest rates on bank loans					
Decreasing domestic demand					
Decrease of foreign demand					
Increased cost of raw materials					

Q2. On a Likert scale of 1-5 where 1 = Nothing 2 = To a small extent 3 = To a medium extend 4 = To a large extent and 5 = To a very large extend, please show how your business/company plans to deal with the effects of the global financial crisis. Indicate this by ticking your option in the table below:

PLANNED SOLUTIONS TO MITIGATE EFFECTS OF THE FINANCIAL CRISIS BY SMEs	**EXTENT OF ACTION**				
	Nothing	**To a small extent**	**To a medium extent**	**To a large extent**	**To a very large extent**
1) We need to do nothing					
2) Workforce downsizing					
3) Postpone investment					
4) Reduction in organizational costs					
5) Freezing of wages					
6) Increase marketing costs					
7) Search for new markets					
8) Reformation of old business strategies					
9) Increase organizational effectiveness					

Appendix 2: Sampling guide

	Sample size			Sample size	
Population size	**+5%**	**10%**	**Population size**	**5%**	**10%**
10	10		275	163	74
15	14		300	172	76
20	19		325	180	77
25	24		350	187	78
30	28		375	194	80
35	32		400	201	81
40	36		425	207	82
45	40		450	212	82
50	44		475	218	83
55	48		500	222	83
60	52		1,000	286	91
65	56		2,000	333	95
70	59		3,000	353	97
75	63		4,000	364	98
80	66		5,000	370	98
85	70		6,000	375	98
90	73		7,000	378	99
95	76		8,000	381	99
100	81	51	9,000	383	99
125	96	56	10,000	385	99
150	110	61	15,000	390	99
175	122	64	20,000	392	100
200	134	67	25,000	394	100
225	144	70	50,000	397	100
250	154	72	100,000	398	100

Source: Isaac and Michael, 1981; Smith, MF, 1983

Appendix 3

Reliability

R E L I A B I L I T Y   A N A L Y S I S - S C A L E (A L P H A)

1.	CREDIT	Decreased credit supply
2.	INTEREST	Increase in interest rates on bank loans
3.	DEMAND	Decreased domestic demand
4.	FOREIGN	Decreased foreign demand
5.	RAMATS	Increased cost of raw materials
6.	Q1	Do nothing
7.	Q2	Workforce downsizing
8.	Q3	Postpone investment
9.	Q4	Reduce organizational costs
10.	Q5	Freezing of wages
11.	Q6	Increasing marketing budgets
12.	Q7	Search for new markets
13.	Q8	Reformation of old business strategies
14.	Q9	Increase organizational effectiveness

Reliability Coefficients

N of Cases = 34.0   N of Items = 5

Alpha = .8248

Appendix 4: Factor Analysis

Factor Analysis table one results

Communalities table one

	Initial	Extraction
Decreased credit supply	1.000	.558
Increase in interest rates on bank loans	1.000	.692
Decreased domestic demand	1.000	.703
Decreased foreign demand	1.000	.460
Increased cost of raw materials	1.000	.561

Extraction Method: Principal Component Analysis.

Total Variance Explained table one

Component	Initial Eigen values			Extraction Sums of Squared Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	2.975	59.495	59.495	2.975	59.495	59.495
2	.759	15.175	74.670			
3	.563	11.266	85.936			
4	.440	8.804	94.741			
5	.263	5.259	100.000			

Extraction Method: Principal Component Analysis.

Component Matrix one

	Component
	1
Decreased credit supply	.747
Increase in interest rates on bank loans	.832
Decreased domestic demand	.838
Decreased foreign demand	.678
Increased cost of raw materials	.749

Extraction Method: Principal Component Analysis.
a 1 components extracted

Factor Analysis table two results

Communalities table two

	Initial	Extraction
Do nothing	1.000	.842
Workforce downsizing	1.000	.762
Postpone investment	1.000	.861
Reduce organizational costs	1.000	.788
Freezing of wages	1.000	.846
Increasing marketing budgets	1.000	.581
Search for new markets	1.000	.849
Reformation of old business strategies	1.000	.892
Increase organizational effectiveness	1.000	.901

Extraction Method: Principal Component Analysis.

Total Variance Explained table two

Component	Initial Eigenvalues			Extraction Sums of Squared Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	4.582	50.915	50.915	4.582	50.915	50.915
2	1.517	16.855	67.770	1.517	16.855	67.770
3	1.223	13.586	81.356	1.223	13.586	81.356
4	.658	7.310	88.666			
5	.412	4.575	93.242			
6	.301	3.350	96.592			
7	.130	1.440	98.031			
8	.099	1.101	99.132			
9	.078	.868	100.000			

Extraction Method: Principal Component Analysis.

Component Matrix two

	Component		
	1	2	3
Do nothing	.216	-.184	.872
Workforce downsizing	.780	.371	-.126
Postpone investment	.749	.528	-.142
Reduce organizational costs	.446	.593	.488
Freezing of wages	.896	.018	.209
Increasing marketing budgets	-.606	-.305	.349
Search for new markets	-.817	.423	.054
Reformation of old business strategies	-.800	.500	.025
Increase organizational effectiveness	-.830	.439	.137

Extraction Method: Principal Component Analysis.
a 3 components extracted.

Appendix 5: Workings

Approximate number of Employees

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 1-150	22	64.7	64.7	64.7
50-100	9	26.5	26.5	91.2
100-150	2	5.9	5.9	97.1
Over 200	1	2.9	2.9	100
Total	34	100.0	100.0	

Area of Business

	Frequency	Percent	Valid Percentage	Cumulative Percent
Industry	11	32.4	33.3	33.3
Financial Sector	1	2.9	3.0	36.4
Trade	11	32.4	33.3	69.7
ICT	2	5.9	6.1	75.8
Telecommunication	1	2.9	3.0	78.8
Transport	4	11.8	12.1	90.9
Economic Services	3	8.8	9.1	100.0

Missing	1	2.9	100	
Total	34	100		

Number of years in operation

	Frequency	Percent	Valid percent	Cumulative Percent
Less than a year	4	11.8	12.5	12.5
1-10 years	24	70.6	75.0	87.5
Over ten years	4	11.8	12.5	100.0
Total	32	94.1	100.0	
Missing system	2	5.9		
Total	34	100.0		

The major source of funding for the business

	Frequency	Percent	Valid percent	Cumulative percent
Bank loans	27	79.4	79.4	79.4
Friends and family	3	8.8	8.8	88.2
Personal savings	4	11.8	11.8	100
Total	34	100	100.0	

Approximate annual turnover

	Frequency	Percent	Valid percent	Cumulative percent
Below 100	24	70.6	70.6	70.6

million	9	26.5	26.5	97.1
100-500 million	1	2.9	2.9	100.0
Over 1 billion	34	100.0		
Total				

Decreased credit supply

	Frequency	Percent	Valid percent	Cumulative percent
No effect	4	11.8	11.8	11.8
Small extend	5	14.7	14.7	26.5
Medium extend	8	23.5	23.5	50.0
Large extend	5	14.7	14.7	14.7
Very large extend	12	35.3	35.3	100.0
Total	34	100.0	100.0	

Increase in interest rates on bank loans

	Frequency	Percent	Valid percent	Cumulative percent
No effect	4	11.8	11.8	11.8
Small extend	8	23.5	23.5	35.3
Medium extend	5	14.7	14.7	50.0
Large extend	7	20.6	20.6	70.6
Very large extend	10	29.4	29.4	100.0
	34	100.0	100.0	

Decreased domestic demand

	Frequency	Percent	Valid percent	Cumulative percent
No effect	2	5.9	5.9	5.9
Small extend	12	35.3	35.3	41.2
Medium extend	5	14.7	14.7	55.9

Large extend	5	14.7	14.7	70.6
Very large extend	10	29.4	29.4	100.0
Total	34	100.0	100.0	

Decreased foreign demand

	Frequency	Percent	Valid percent	Cumulative percent
No effect	7	20.6	20.6	20.6
Small extend	10	29.4	29.4	50.0
Medium extend	3	8.8	8.8	58.8
Large extend	6	17.6	17.6	76.5
Very large extend	8	23.5	23.5	100.0
Total	34	100.0	100.0	

Increased cost of raw material

	Frequency	Percent	Valid percent	Cumulative percent
No effect	2	5.9	5.9	5.9
Small extend	12	35.3	35.3	41.2
Medium extend	5	14.7	14.7	55.9
Large extend	5	14.7	14.7	70.6
Very large extend	10	29.4	29.4	100.0
Total	34	100.0	100.0	

Do nothing

	Frequency	Percent	Valid percent	Cumulative percent
No effect	26	76.5	81.3	81.3
Small extend	1	2.9	3.1	84.4

Medium extend	2	5.9	6.3	90.6
Large extend	1	2.9	3.1	93.8
Very large extend	2	5.9	6.3	100.0
Total	32	94.1	100.0	
Missing system	2	5.9		
Total	34	100.0		

Workforce downsizing

	Frequency	Percent	Valid percent	Cumulative percent
No effect	4	11.8	11.8	11.8
Small extend	8	23.5	23.5	35.3
Medium extend	5	14.7	14.7	50.0
Large extend	7	20.6	20.6	70.6
Very large extend	10	29.4	29.4	100.0
Total	34	100.0	100.0	

Postpone downsizing

	Frequency	Percent	Valid percent	Cumulative percent
No effect	9	26.5	26.5	26.5
Small extend	5	14.7	14.7	41.2
Medium extend	4	11.8	11.8	52.9
Large extend	6	17.6	17.6	70.6
Very large extend	10	29.4	29.4	100.0
Total	34	100.0	100.0	

Reduce organization costs

	Frequency	Percent	Valid percent	Cumulative percent
No effect	4	11.8	11.8	11.8
Small extend	5	14.7	14.7	26.5
Medium extend	8	23.5	23.5	50.0
Large extend	5	14.7	14.7	14.7
Very large extend	12	35.3	35.3	100.0
Total	34	100.0	100.0	

Freezing of wages

	Frequency	Percent	Valid percent	Cumulative percent
No effect	15	44.1	44.1	44.1
Small extend	10	29.4	29.4	73.5
Medium extend	5	14.7	14.7	88.2
Large extend	1	2.9	2.9	91.2
Very large extend	3	8.8	8.8	100.0
Total	34	100.0	100.0	

Increasing market budgets

	Frequency	Percent	Valid percent	Cumulative percent
No effect	4	11.8	11.8	11.8
Small extend	8	23.5	23.5	35.3
Medium extend	5	14.7	14.7	50.0
Large extend	7	20.6	20.6	70.6
Very large extend	10	29.4	29.4	100.0
Total	34	100.0	100.0	

Search for new markets

	Frequency	Percent	Valid percent	Cumulative

				percent
No effect	3	8.8	8.8	8.8
Small extend	1	2.9	2.9	11.8
Medium extend	3	8.8	8.8	20.6
Large extend	6	17.6	17.6	38.2
Very large extend	21	61.8	61.8	100.0
Total	34	100.0	100.0	

Reformation of old business strategies

	Frequency	Percent	Valid percent	Cumulative percent
No effect	15	44.1	44.1	44.1
Small extend	10	29.4	29.4	73.5
Medium extend	5	14.7	14.7	88.2
Large extend	1	2.9	2.9	91.2
Very large extend	3	8.8	8.8	100.0
Total	34	100.0	100.0	

Increase organization effectiveness

	Frequency	Percent	Valid percent	Cumulative percent
No effect	3	8.8	8.8	8.8
Small extend	2	5.9	5.9	14.7
Medium extend	1	2.9	2.9	17.6
Large extend	4	11.8	11.8	29.4
Very large extend	24	70.6	70.6	100.0
Total	34	100.0	100.0	