FACTORS INFLUENCING PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES IN BUNGOMA SOUTH DISTRICT, KENYA

BY

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DECLARATION

This research project is my own original work and has never been submitted for a degree award in any other University.

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DEDICATION

This project is dedicated to my wife Judith Ngeresa, my children Kenneth. Deborah. Kelvin and Desmond for their love, sacrifice and support.

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LIST OF ACRONYMS AND ABBREVIATIONS

ADC	African Development Cooperation
BFSA	Banking and Financial Services Act, 1994
BoZ	Bank of Zambia
BSC	Balanced Score Card
CBS	Central Bureau of Statistics
ERP	Enterprise Resource Planning Systems'
FSDP	Financial Sector Development Plan
KNES	Kenya National Economic Survey
KWFT	Kenya Women Finance Trust
MFIs	Micro Finance Institutions
NBFIs	Non-Bank Financial Institutions
NGOs	Non-Governmental Organization
NGOs	Non-Governmental Organizations
SIDA	Swedish International Development Agency
SMEs	Small and Medium Enterprises
USAID	United States Agency for International Development

ABSTRACT

Small and Medium Enterprises are regarded as a panacea for increased micro-economic growth and reduce poverty among the population. however factors that influence performance of these small and medium enterprise in many parts of Kenya are still not clear . The purpose of this study was to investigate factors influencing performance of small and medium enterprises in Bungoma South District. Kenya. Specifically the objective were to: to investigate how access to credit ; amount of credit influence ; terms of credit repayment and how sources of credit influence performance of the small and medium enterprises in Bungoma South District. This study was conducted through a descriptive survey research design. A two stage simple random sampling method was employed to select one hundred and six from a population of one hundred and forty-five Small and medium enterprises while purposive sampling was done in which managers of the one hundred SMEs were selected as respondents, Structured questionnaires were developed. pre-tested and used for collecting quantitative data for the study from the sampled small and medium entrepreneurs. Descriptive statistics using frequency distribution, percentages and means were used to summarize data. On the source of credit for running SMEs 82% respondents revealed that they borrowed money from financial institutions, On the availability to credit facilities from lending institutions 84% revealed that the loaning process was too slow, 64% responses cited that the amount of credit was not adequate, 71% found borrowing conditions difficult .The study sought to determine the source of capital for running SMEs, 82% respondents revealed that they borrowed money from financial institutions while 18% indicated that they financed their SMEs using their own capital. On the availability to credit facilities from lending institutions, 84% revealed that the processing given was too slow 64% responses cited that the amount was not adequate while 71% indicated that it was difficult to meet all the borrowing conditions .It is recommended that rules on collateral be changed to allow movable and immovable items be used as collateral to ease access to credit, the use of credit rating should be applied so that those with good previous repayments are allowed to negotiate terms of loan repayment finally, lending institutions should ensure adequate training is given to SME managers before disbursing credit to minimise wastage.

CHAPTER ONE

INTRODUCTION

1.1 Background of the study

There has been a growing awareness since the early seventies that small enterprises are important for economic growth (Von Pischke. 1992). They are seen as the engines of employment. alleviating poverty and improving equality. The eighties saw an intensification of this interest and a consequent expansion of policy into the sector of micro-enterprises, following the discovery of widespread entrepreneurial activity in both developed and developing countries (Sebstad and Monique. 2001). In the case of the latter. entrepreneurial activity was particularly salient among the poor. The idea that intuitively followed was that enhancing these small businesses could effectively and rapidly fight poverty.

In Japan. Small and Medium Enterprises (SMEs) are prevalent across the Japanese economy, constituting the lion's share of enterprises SMEs are most numerous in the retail. services and restaurant/lodging industries, the most productive SMEs are those in the manufacturing sector. While many of those in the services sector are wholly reliant on domestic demand, a large proportion of SME manufacturers are essential suppliers to Japan's famous large exporters (von pischke 1992). *Japanese SMEs face particular problems securing* finance. That bank is more reluctant to lend to small companies than big ones this makes them vulnerable. Japanese banks' continue risk-aversion by emphasising reliance on fixed assets for collateral put many SMEs at a disadvantage.

In Bangladesh, SMEs account for about 45% of manufacturing (scully, 2004). They account for about 80%of industrial employment. and about 25% of total labour force. Their total contribution to export earnings varies from 75%-80% based on the Economic Census 2001-2003. The total number of SMEs is estimated at 79754 establishments. of which 93.6% are small and 6.4% are medium. The Bangladesh Bank annual report for fiscal year 2006-07 observed that the SMEs demand for bank loan. especially, medium and long term financing is relatively high; The Banks are however reluctant to extend loans, especially, term loans to SMEs because of perception that the current legal system is unable to protect their interests

Many economies in developed and developing have come to realise the value of small businesses. They are seemed to be characterised by dynamism. witty innovations, efficiency. and their small size allows for faster decision making process. The benefits of SMEs cannot be overemphasized they include: contributions to the economy in terms of output of goods and services, creation of jobs at relatively low capital cost. especially in the fast growing service sector: It's a vehicle for the reduction of income disparities thus developing a pool of skilled or semi-skilled workers as a basis for the future industrial expansion

The small scale sector is an important segment of Uganda's industrial sector, as well as its agricultural sector, in terms of its contribution to employment, value output, and regional

Growth of the SME sector is important as a tool for transition in economic activity. from agricultural sector to the industrial sector. SMEs are estimated to contribute Over 30% of GDP-Over 30% of employment. Therefore the sector is second only to Agriculture in generating employment and contributing to poverty alleviation. A UNESCO funded study noted that majority of SMEs fall in the category of sole proprietorships because they are easy to form. are managed by individuals and decisions are easy to make without consultation.

Small Medium Enterprises (SMEs), which employ between 8-15 people (Barnes. 2011). are reputed to be behind most of the socioeconomic South East Asia play a significant role in Kenya's development process. This is because during the early stages of economic development. these enterprises embodied unique opportunities for creating employment and wealth.

The National Baseline Survey in 1999 revealed the existence of some 550,000 SMEs employing as many as 6 million Kenyans (Central Bureau of Statistics CBS, 1999). The European Commission found that 50% of total net job creation in the SME sector is created by a mere 4% of these firms in Kenya (Manu. 1998). By implication. it would appear that small-enterprises fall into two categories. There is a very large group of them that. for various reasons. will not develop their business beyond a certain (small) scale, and there is a very small group of entrepreneurs who are capable of expanding their business. Other studies have shown that the sector is very dynamic. as evidenced by the rapid rate of investment and enterprise growth (Kimuyu, 1999).

The Government of Kenya policy documents. the Development plan (1997-2001), economic survey (1998) and the Sessional papers No. 2 of (1992), recognize the role SMEs play in economic growth and development and emphasizes plans to support SMEs in the informal sector. The recent SMEs Baseline Survey showed that only six percent of SMEs successfully applied for and used credit (Kenya National Bureau of Statistics. 2010). Therefore these indicate that the SMEs are generally under-capitalized. suggesting major operational difficulties in accessing credit and pursuing corporate goals (Kimuyu. 1997). It is unclear how the remaining 94% meet their working capital and investment needs.

SMEs in the Kenya especially in the rural areas are faced with many problems. One survey report by (Magwanga et.al 2010) indicated that in Eldoret, Bungoma. Busia and Kitale, a total of 7200 SMEs have been started (5111 in Eldoret; 1099 in Bungoma: 322 Busia; and 668 in Kitale) and more than 40% closed after being in operation for between 2-5 years the highest proportion of closures (45%) being reported in Bungoma South District. The problems that were cited as leading to collapse of these small enterprises range from lack of managerial knowledge, registration of businesses, marketing of their products and service and scarcity of financial resources. According to Malonza (2007), more than 70% of the small scale enterprises close due to lack of finance or due to inadequate financing. According to Moyi (2008), factors responsible for development of the SMEs in Kenya include access to finance. conditions of the borrowed capital. institutional challenges and credit characteristics. If these factors are not carefully evaluated then performance of the SMEs may be compromised. It remains unknown how the above factors influence the performance of SMEs in Bungoma South District. It is against this background that this study was conducted.

1.2 Statement of the problem

Small and medium enterprises have enhanced the economic growth of many countries in Asia and their presence is starting to be appreciated in Kenya, however their performance has been poor in many parts of Kenya (Söderbom and Teal, 2010). It has been shown that problems of poor performance occur mostly in the rural based Small and Medium Enterprises in Kenya with a recent survey report indicating that among five areas surveyed in Kenya. Bungoma South District was the most affected with largely poor performance and closures according to (Magwaga *et al*.. 2010). Bungoma south District has numerous micro finance institutions, and banks operating. it is expected that Managers of Small and Medium Enterprise borrow and make these Small and Medium Enterprises vibrant. on the contrary most Small and medium enterprise hardly last for more than three years, Some SMEs that have attempted to borrow from the lending institutions end up defaulting making their assets to be auctioned. This study therefore sought to investigate why SMEs perform poorly despite the apparent numerous sources of credit available locally and on the Kenyan market.

1.3 Purpose of the study

The purpose of the study was to investigate the factors influencing the performance of small and medium enterprises (SMEs) in Bungoma South District, Kenya

1.4 Objectives of the study

The objectives of the study were to:

1. To find out how availability of credit influences the performance of the SMEs in Bungoma South District.
2. To explore how amount of capital borrowed influence performance of the SMEs in Bungoma South District.
3. To determine how terms of repayment influence performance of SMEs in Bungoma South District.
4. To investigate how sources of credit influence performance of SMEs in Bungoma South District.

1.5 Research Questions

The following were the research questions

1. To what extent did availability of credit influence the performance of the SMEs in Bungoma South District?

2 How does the amount of capital borrowed influence the performance of SMEs in Bungoma South District?

3 How do the terms of repayment influence performance of SMEs in Bungoma South District?

4 How do different sources of credit influence performance of SMEs in Bungoma South District?

1.6 Significance of the Study

This study is hoped will contribute in various ways to stakeholders as follows:

Micro finance institutions assisting small and micro enterprises will find the results of this study useful. They will know how to improve on the credit lending by understanding factors that may affect their lend credits to the SMEs.

For purposes of scaling up loans in subsequent loan cycles. implementers need to keep track of the actual uses to which loans under previous loan cycles were put. This is determinant as to whether the loan beneficiaries are able to service subsequently higher loans and also an indicator of the future sustainability of the lending institutions.

Interested academicians especially in entrepreneurship will use the findings to understand the issues raised and use them as reference material and/ or basis for further research. Microfinance who has committed funds to SMEs was interested in finding out how far their objectives of growth are being sustained. which may provide a baseline for further funding

The study will contribute more findings to this debate about the trans-formative capacity of small-scale credit and income generating programs.

Information from this study is hoped will help the SMEs to improve their overall performance through application of the recommendations of the current findings

Finally it is hoped the government will benefit from this study in coming up with policies that will encourage operations of the SMEs.

1.7 Delimitation

The study was confined to Small and Medium Enterprise in Bungoma South District of Bungoma County; Kenya.

1.8 Limitations of the study

The study may be affected by a number of limitations anticipated during the study

Suspicions from some of the respondents viewing the research with fear. this was however dealt with by the research assuring them that the study was meant for academic purpose but not for victimization.

Unfilled questionnaires. this was however corrected by the research getting written consent from all the respondents as per the ethical considerations as stipulated by the National Council of science and Technology.

Inadequate financial resource and time to complete the research within the set period of time, this was however dealt with by the research working within the time frame and the estimated budget for the study.

1.8 Assumptions of the study

The study was based on the assumption that:

There are various sources of credit available to SMEs in Bungoma South District.

Different SMEs in Bungoma South District perform differently.

1.9 Definition of significant terms used in this study.

Access: To obtain amount of money requested by SME from financial institutions

Credit: money borrowed with an aim of repaying with an agreed interest

Entrepreneur: Businessmen/ SMEs.

Loan Utilization: Refers to how the money was used or invested.

Micro institution: Informal sector or small scale is synonymously used in study. To refer to enterprise employing 1-10 persons, has low capital investment, Uses simple technology and local materials and utilizes low skills.

Performance: Volume of sales, levels of profit. rate of capital. addition of employees, asset level.

Small and Medium Enterprise: Small business enterprise employing between8-15 people

1.10 Organization of the study

The study was organized as follows; Chapter one was the introduction. which contains the background of the study, statement of the problem. purpose of the study, assumption and definition of significant terms. Chapter two comprised of literature review based on the four research objectives, theoretical framework. knowledge gap and conceptual framework. Chapter three comprised of introduction research design target population. sample size, sampling procedure, research instruments, reliability of the instruments, validity of the instrument, data collection procedure and ethical considerations of the study .Chapter four had introduction. questionnaire return rate .profile of respondents, then analysis presentation, discussion and interpretation of the four objectives of the study, finally Chapter five consisted the summary of findings. discussion recommendations and conclusions.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter focuses on what other scholars have written in relation to the topic under investigation: Factors influencing performance of small and medium enterprises (SMEs). The chapter is presented under the sub-titles; Background literature. which includes: Concept and characteristics of SMES. the other part deals with literature in relation to the objectives of the study, the theoretical and conceptual framework.

2.1 Small and Medium Enterprises

The term "Small and Medium Enterprises" (SMEs) has been given different definitions and these definitions vary from one country to another. sector to sector and even one industry to another. But most often. the definitions have however been in terms of either capital employment or number of persons engaged. In Kenya. SMEs have mostly been defined by the number of persons engaged. Steel and Webster (1991) defined Small and Medium Enterprises as productive unit with hired labour that involved enough investment in capital or skills to constitute a barrier to entry but small enough to be managed by one person. This definition indicates the SMEs are usually very small business with simple organizational structures employing very little capital. National Board for Small – Scale Industries (NBSSI) in 1992 also defined SMEs as production units that are engaged primarily in manufacturing. functioning outside the residential premises with an investment in machinery equipment and tools of not less than Kshs.10 million and or which engaged not less than eight people and not more than fifteen people (Steel and Webster, 1991).

International Labor Organization (1970) defines SMEs as a sector whose entry by new enterprises is comparatively easy; enterprises in this sector rely on indigenous resources and family- owned: they operate on a small scale in unregulated and competitive markets and are labor- intensive and use adopted technology. Their workers usually have skills acquired outside the formal schooling system. According to Deakins (1996). Small-Scale Enterprises are in three major criteria these are: the number of employee's definition; turnover definition and the characteristics definition.

The number of employees' definition classifies small firms by some maximum number of employees. However, this will depend on the nature of capital intensity. which varies from one industrial sector to another. Thus, less than 20 employees were considered for manufacturing, whereas less than 15 employees were considered appropriate for construction. Turnover definition maintained that in Bolton Report (1971) Bolton in characteristics definition gave three essential characteristics of the SMEs. It has a small share of the market. it is managed by its owners or part owners, it is operated independently (Musphert, 2009). Considering the above definition, one can deduce that SMEs by their work or operation have acquired certain peculiar characteristics that differentiate them from the large scale productions. The characteristics can be enumerated as follows: low capital base; labour intensity; ease of entry: reliance on indigenous materials and low technology: managed by its owners or part owners and not through the medium of formalized management structures; and workers usually have skills acquired outside the formal systems (that is through apprenticeship).

The small and medium enterprise (SME) sector in Kenya is important for employment generation. wealth creation and welfare improvement. It is a repository for persons either unable to finds jobs in the modern sector or retrenched from formal employment. A 1999 national baseline survey of these enterprises revealed that they contribute 18% of the national gross domestic product (CBS, ICEG. and K-REP. 1999). Studies depict the sector as very dynamic with rapid investment rates and enterprise growth (Kimiyu 1999a).

In Kenya, the SMEs are generally under-capitalised due to operational difficulties in accessing credit (Lundvall *et al*.. 1988). Lack of credit is the second severest problem faced by SMEs, the most important being lack of markets and competition (Kimuyu et al.. 1999a). Only a small proportion is able to successfully apply for and use credit. More than one third of the enterprises die young due to inadequate working capital. Own funds and family resources form the most important sources of initial and additional capital. Considering the very low incomes and savings rate in the country. SMEs fall back on these sources out of desperation. The small proportion that receives some credit receives very modest amounts. reflecting not only low activity levels but also supply ceiling by non-government organizations. (NGOs) and government credit programs that target the sector (Kimuyu, 1997).

Studies in the Kenyan manufacturing sector have shown that enterprises with poor access to credit tend to be less productive and are unable to operate efficiently (Johnson. 1999). Inadequate access to credit means that the potential role of the SME sector in reducing poverty and in Kenya's socio-economic transformation was difficult to realize. To explore this problem of inadequate access to credit by the small enterprise sector. a study by Johnson (1999) was undertaken to find out the types of SMEs that are more likely to successfully seek out credit. examine institutional factors that affect the SMEs credit markets and suggest interventions for increasing such access. Use was made of the 1999 SME baseline survey data supplemented with a follow-up survey. The selection of sample clusters followed a primary stratification that distinguished different households depending on economic and demographic characteristics. Adult members of sampled households were interviewed with the help of a structured questionnaire. The findings indicated that there are a number of factors that affect the growth of SMEs in Kenya key among them was access to credit. characteristics of the credit, amount of credit borrowed and sources of credit. Yet, there has been little follow up study to determine how these factors affect the performance of the SMEs.

2.2 Availability of credit to finance SMEs

Microfinance collectively refers to the supply of loans. savings. and other basic financial services like insurance, to the poor (Hulme and Mosely. 1996). As the poor people cannot avail these financial services from the formal commercial banks (because of the collateral requirements), microfinance tends to provide to them exclusive of these conditions (Carter, McNulty and Verbrugge, 2004). For these financial services. the poor people are willing to pay for because of the added advantage they receive for not collateralizing anything. More broadly, it is a movement that envisions a world in which as many poor and near poor households as possible have permanent access to an appropriate range of high quality financial services, including not just credit but also savings. insurance. and fund transfers (Chen and Snodgrass, 1999). Poor people are not able to get loans from commercial banks due to lack in guarantee and collateral. But there are also many other reasons that commercial banks not willing to provide fund to poor people. such as poor people have less education, no real experience and training. high cost for transactions of small loans and lower profit (Dunford, 2001). Therefore, limited opportunity to access loans leads to people fall into more poverty. This situation resulted in the emerging idea for new market of micro financing to poor people.

The main characteristics of the microfinance are providing small loans to the business. According to the Dunn and Gordon (2001), microfinance has several characteristics that are: Small amounts of loans and savings; short- terms loan (usually up to the term of one year); payment schedules attribute frequent installments (or frequent deposits); installments made up of both principal and interest, which is amortized over the course of time; higher interest rates on credit (higher than commercial bank rates but lower than loan-shark rates). which reflect the labor-intensive work associated with making small loans and allowing the microfinance intermediary to become sustainable over time; easy entrance to the microfinance intermediary saves the time and money of the client and permits the intermediary to have a better idea about the clients financial and social status; application procedures are simple; short processing periods (between the completion of the application and the disbursements of the loan); the clients who pay on time become eligible for repeat loans with higher amounts; the use of tapered interest rates (decreasing interest rates over several loan cycles) as an incentive to repay on time. Larger loans are less costly to the MFI, so some lenders provide large size loans on relatively lower rates; and no collateral is required contrary to formal banking practices. Instead of collateral. microfinance intermediaries use alternative methods, such as the assessments of clients repayment potential by running cash flow analyses, which is based on the stream of cash flows. generated by the activities for which loans are taken.

During the last two decades, micro-credit approach has been increasingly incorporated in the development discourse. Specially the credit is given to the SMEs and the popular belief is that SMEs are benefited and empowered and are being acknowledged for having a productive and active role and thus it is the gateway of gaining freedom for themselves (Liedholm and Mead. 2007). Such NGO Programmes have reversed conventional top down approach by creating livelihood opportunities for the poorest citizen. especially for the SMEs who are about 94 percent of their client (Thente. 2003).

Microcredit is now considered the effective development tool of poor people especially for SMEs. SMEs are become more empowered and play important role in generating income in the rural areas of Kenya (Johnson. 1999). In most developing countries. policies for rural financial development have been based on three erroneous beliefs concerning their target groups: 1. rural micro-entrepreneurs are unable to recognize themselves. 2. they are too poor to save: and 3. they need cheap credit for their income-generating activities or small enterprises (Harper, 2003). However, in Kenya the financial availability of the SMEs appear underestimated by the micro-finance institutions.

2.3 Influence of amount of credit on the performance of SMEs

The credit-seeking decision is a three-stage process. Entrepreneurs first decide on whether or not they need credit. Once that decision is affirmative. a further decision has to be made regarding the appropriate credit source (Maddalla. 1997). An additional decision relates to the level of credit to seek out and how well the entrepreneur was informed about the terms of borrowing and repayments. But even when enterprises feel a need for external credit. they may not borrow if their perceptions on the costs of applying for a loan outweigh the expected receipts (Mei Qiang, 2002). They may also lack enough cash to meet the application costs. Enterprises may also shy away from borrowing due to a poor collateral position and lack of requisite information about the capital borrowed. which requires quite a high level of mentorship from the micro-finance institutions. Collateral requirements imply that there would be enterprises that prefer external funds but are unable to apply for such funds (Mookherjee. 1999).

Studies have shown that most Small scale business enterprises perceive borrowing as necessary for business and the impact of borrowing on business performance as positive (Mwenda. 1993; Rogaly, Fisher and Mayo. 1999: Moyi. 2000). Yet they have weak mentorship in the utilization of the borrowed capital resulting collapses of the loan use. Among the small group of applicants, there are gender. enterprise location. business activity and formality status differences, which must be well factored in during the loan borrowing by the business enterprises. Traders appear more inclined to borrow than entrepreneurs in other activities and the incidence of loan application is greater among female proprietors and urban based enterprises (Scully. 2004). Informal enterprises are dramatically more likely to apply for a loan as do those that are larger and older as well as those owned by older entrepreneurs. if they are provided with novel methods of proper loan utilization. The life expectancy of small scale business enterprises is generally short so that most do not live long enough to build contacts and reputation necessary in seeking out credit (Sebstad and Monique, 2001). Smallness is also a major impediment to effective participation in the credit markets.

Not only is the proportion of small scale business enterprises that borrow, but those who borrow request for small amounts. Amounts borrowed also vary across activities and the gender of the proprietor. Male entrepreneurs borrow substantially more than female entrepreneurs (Chen and Snodgrass, 1999). In other words, although female entrepreneurs are more inclined to borrow. their male counterparts borrow more. The proportion of male entrepreneurs borrowing from commercial banks is more than twice that of small scale business enterprises. On the other hand. a greater proportion of female entrepreneurs borrow from NGOs and non-bank finance institutions. It is not clear why the discrepancy but it is assumed to be due to lack of proper mentorship to the borrowers before they acquire loans. The difference in amounts applied for by formal and informal enterprises is great, the latter borrowing only a fraction of the amounts borrowed by the former (Chen and Snodgrass, 2001). Informality represents low productivity, poor access to infrastructure services and poor property rights over business premises, making credit markets out of reach for most such enterprises (Kimuyu, 1997). Borrowers unable to access credit from commercial banks are therefore unlikely to borrow significant amounts. Urban located and larger enterprises also borrow more. A positive correlation between enterprise size and credit is in order. since demand for working capital increases with enterprise size.

Since most of credit providers are urban located. it has led to lower levels of credit use by rural enterprises hence creating a credit supply constraint (Daniels and Mead, 2010). Membership in a support group increases the level of credit sought for. so that such groups have a strong network side effect. Since education and credit sources are important determinants of the level of credit, the mentorship by the micro finance institutions picks up their impact. Small scale business enterprises enjoy a high success rate regarding positive response and amounts received if they are well mentored by the micro finance institutions (MFI). These high success rates suggest near perfection in the self-selection and application targeting processes. Variations in success rates run across activities, spatially, across the formality/informality divide and credit sources (Dunford, 2001).

Enterprises within finance, insurance and real estate enjoy the highest success rate while those in community and other social services face the lowest success rates (Greenbaum. 2003) because of the knowledge and therefore. this indicate that knowledge base is paramount. Additional differences are observable across credit sources with enterprises seeking credit from non-bank finance institutions showing low success rate and those seeking from co-operative society's high success rates (Harper, 2003). Other studies have shown that small enterprises are particularly disadvantaged with regard to resolution of business related disputes due to high litigation costs and poor contract enforceability (Hulme and Mosely, 1996). The development of long term relationships and good reputation important for trade credit does not take root due to the short life expectancy of enterprises in the sector.

2.4 Influence of Terms of repayment on performance of SMEs

The government of Kenya awareness of the need for credit by SMEs has facilitated several credit programs to assist SMEs in accessing credit. Weidmann (1992). Yet. the terms of payment stipulated by the microfinance institution has also been found to be a crucial factor that affects the acquisition of credits by the SMEs. These programmes change the commercial rate of interest to cover costs and to ensure suitability. These programmes are intended to influence welfare of household. reach directly the poorest of the economically active to make sure that in mixed groups SMEs are not left out.

For many micro finance providers. the reason they focus on SMEs clients is mainly of a practical nature. Repayment rates are typically higher for SMEs than for many enterprises because of the risks of borrowing to the SMEs and the tendancy to have fewer alternative sources of finance (Malonza. 2007). SMEs are also seen as more compliant and reliable. They are perceived to have a higher sense of responsibility and to be more affected by social pressure than men, (Harper.

2003. Simanowitz. 2002). Despite all the efforts channelled towards assisting SMEs. they are faced by diverse challenges as far as repayment of the credits. Despite earning a living. SMEs have little control over the household's finances or even over their own earnings. The men in the family continue to decide on expenditures. As long as SMEs continue to lack social resources such as access to education they will only be able to make limited use of the financial resources they have obtained. As Cheston and Kuhn (2002) observe:

> The ability of a woman to transform her life through access to financial services depends on many factors. some of them linked to her individual situation and abilities and other dependent upon her environment and the status of SMEs as a group.

Repayment of loans a scheduled is not an accurate indicator that funds were used to invest in successful productive activities. Even when a borrower repays a loan in time the source of income is not necessarily from revenues generated by investing the loan in productive activities. (Gallup. 2003) at times repayment is often delivered from general family income rather than the activity for which loan has been provided. Control over loans is by itself not a good indicator of SMEs independence in management of an enterprise. Thirty seven percent of loan retention may already be a significant achievement in a gendered society (Cheston and Kuhn. 2002). Indeed cooperation between SMEs may already be a form of empowerment it can also be considered an improvement if management of such enterprises would previously have taken the decision on business by themselves thus control of the enterprise by SMEs. Such SMEs may find it difficult to make decisions pertaining to their businesses. Several scholars have had a lot of interest on impact of repayment conditions of the micro finance loans on the performance of SMEs. It is evident that many scholars have prescribed microfinance loans as a panacea for all the problems bedevilling SMEs. It is imperative that microfinance loans have had positive impact on the performance of SMES. but whether these loans result into significant business growth is yet to be established. It is not yet known however how SMEs go about making repayment decisions and how to invest the money and the factors that influence such decisions since SMEs entrepreneurs are not independent entities but rather operate as members of households.

Oketch (1991) found in analysis of 126 successful micro enterprise credit recipients in Kenya that 24% of the borrowers diverted portions of their loans to unspecified items not specified on the loan application and therefore it was difficult to repay. The factors into SMEs repayment of loans were also not investigated. Goetz and Sen Gupta (1996) however found out that SMEs do not actually fully control their loans. Their findings cannot however be generalized to the Kenyan situation due to major cultural and religious differences of the 2 countries. Amendariz (2005) in a study of two Grameen replications in the Philippines found that most clients found it difficult to repay their loans. In a survey of clients in repayment arrears and clients who had exited the program (Faulu a local MFI) found that 74% of their clients had diverted their last loan and therefore failed to repay. If credit meant for business development is diverted to consumption needs. the borrowers still have to repay the loans. Consequently the business does not expand and it cannot therefore service subsequently higher loans. Loan repayments may require the borrower to forego the gratification of basic needs or to default. It is important however to find out why loans are diverted leading to non payment.

Lending to large firms, on the other hand, is quite different. since larger firms are more established, and lenders typically can evaluate more precisely the credit risk of the firm by using public information. Some of this is a consequence of large firms' access to national debt and equity markets, for example, arising from credit rating agencies. equity analysts. and filings with the Securities and Exchange Commission (SEC). Furthermore. due to the relative transparency of large firms compared to small ones, these large firms typically can borrow from multiple banks under less restrictive loan contract terms. Thus, financial statement lending to large. relatively transparent firms is unlikely to be a source of economic rents to the lender. Similarly, other transactions-based lending technologies, such as fixed-asset lending, are unlikely to earn the lender substantial rents due to asymmetric information. since the technology for valuing collateral is relatively straightforward. Rather, the benefits accruing to the lender would be related primarily to economies of scale.

Out of the foregoing discussion. it follows that there is scanty empirical data on credit repayment among SMEs entrepreneurs in Kenya. Given the disparities among countries may not readily apply to Kenya. A country's specific study of the kind proposed herein is quite wanting.

2.5 Influence of sources of credit on performance of SMEs

Finance institutions arrange small loans and financial services to the poor people and small business. According to the definition on "Microfinance Gateway" an MFI is the organization that offers financial services to the low-income people (Microfinance gateway. 2008). There is a wide range of micro financial institutions. Mostly when we talk about these, financial NGO`s come into the mind. These financial NGO's provide micro credit and micro finance services too and in most cases these financial NGO's are not allowed to capture saving deposits from general public. Many NGO's provide other financial services along with microfinance and similarly some commercial bank are also providing microfinance along with their routine financial activities so because of these micro finance services which are quite bit part of the whole of the activities of these commercial banks we can call these as a microfinance institutions (Rehman. 2007). There are some other MFI's that can be considered in the business of micro finance. These institutions are the community based financial intermediaries such as credit union: cooperative housing societies and some other are owned and managed by the local entrepreneur and municipalities. This type of institution is varying from country to country (Rehman. 2007).

There are now nearly 70 million poor people who are getting benefits from 2500 micro finance institutions in over 100 countries by microfinance (Sengupta. Aubuchon. 2008). This fact shows how microcredit is important and useful. and how a huge number of people are facilitated by the microfinance institutions. This is the reason is that microfinance is gaining importance as an effective tool of social mobilization and poverty alleviation.

Microfinance has become a major tool of development, and it is fast developing as an international industry, with its own associations, dedicated finance. training and other support organizations. Estimates show that microfinance serves approximately million African households. with aspirations for significant further expansion. Dunn *et al..* (2001), notes that. the upsurge in interest has been accompanied by attention to the sustainability of the microfinance services provided by nongovernmental organizations. through charging commercial rates of interest and using sound business practices. This type of microfinance institution offers smallsized loans and may also provide business development services. health and nutrition education. and other types of services.

Chen and Snodgrass (1999) stated that. most of the clients of micro finance hover around the poverty line, slightly above and below it and that MFIs provide a valuable source of credit for these households. Some programs reach the very poor. but they are not normally the main group accessing the services. Recent impact studies by Sebstad and Cohen (2011).have documented the positive impact of MFI programs, but the impacts have tended to be more modest in scale than often assumed. According to Sebstad and Cohen (2010), microfinance strives to "scale up" to serve as many households as possible. Among the range of possible micro-financial services, micro-credit has predominated, on the assumption that it will deliver higher incomes and increased assets to the poor through micro-enterprises. Indeed injecting capital into existing micro enterprises or creating new ones may enhance that their poor owners face. Thomas *et al.* (2002) argues that, by delivering financial services at a scale, and by mechanisms appropriate to them, micro-credit can reach poor people. By providing the poor people with credit for micro-enterprises it can help them work out their own way and by providing loans rather than grants the micro-credit provider can become sustainable by recycling resources over and over again. However, to Hulme and Mosly (1996) far less attention has been paid to the need to reduce the risk. perhaps the most pressing need especially for the poorest households. They argue that, a proportion of micro-credit clients have become worse off after accessing micro loans. The need to reduce risk is why poor people would prefer regular wage labour than managing their own micro-enterprise, if only such opportunities were available (Ibid).

Micro-credit alone is not enough service to empower the people economically. Rutherford (2000) elucidate that, It is paramount to look beyond micro-credit and frame it in terms of including micro-financial services other than credit for micro enterprises: savings, consumption loans and insurance in particular. A range of those financial services are important to meet the needs of poor people. both protecting them from fluctuating incomes and livelihoods. While microfinance providers emphasize investments of working or fixed capital in micro-enterprises, the reality is that many clients use the credit for consumption, smoothing. especially as most funds are fungible within a household. Such consumption-smoothing can allow households to cope more effectively, but it also runs the risk of pushing them further into debt if they cannot repay the loan out of enhanced income streams. More appropriate financial products for this purpose are savings, insurance and loans to allow poor people to repay the loans and interests. And yet these have received far less attention than micro-credit for micro-enterprises (Rutherford: 2000).

With strong focus on micro-credit for micro-enterprises, it is perhaps surprising that less attention has also been paid to linking poor people to the growing market opportunities and to enhancing control they can exercise over their economic environment. In terms of greater control within the economic environment, the ownership of assets in particular significantly reduces risks to households in the face of fluctuating incomes or expenditure demands. However as individual micro entrepreneurs, most micro-credit clients remain as vulnerable to economic circumstances as they were before taking any micro-loan (Ibid).

The formal segment of Kenya's financial sector is dominated by a few commercial banks. Some of the banks have roots in the colonial period and were historically oriented towards meeting the financial needs of external trade and large-scale commerce. These banks do not therefore have a track record of lending to small enterprises and smallholder agriculture. Perhaps in recognition of this shortfall, the government of Kenya backed initiatives such as the Small Enterprise Finance Company, the Kenya Industrial Estates and other alternatives to formal banks to fill the financing gap. However, these government-backed schemes and development finance initiatives performed unsatisfactorily and in retrospect may have distorted the evolution of financial markets in the country. Studies show that when credit is advocated as the primary remedy for low level productivity or when loans are used to stimulate growth, these strategies often lack mechanisms for excluding risky borrowers (von Pischke, 1992). As a result, many borrowers fail to repay and the credit programmes are left with a progressively drying pool of funds for lending. This phenomenon, referred to as the exit problem of credit programme, has been evident in Kenya. In the 1980s, Savings and Credit Co-operatives (SACCOs) and non-bank finance institutions (NBFIs) expanded rapidly to fill the gap created by commercial banks, but were only useful for salaried employees for whom the lending and borrowing entitlements were clearer.

The continuing gap in the MSE sector attracted the attention of non-governmental organisations (NGOs), including the Kenya Rural Enterprise Programme (K-REP), the Kenya SMEs Finance Trust (KWFT), FAULU and PRIDE Africa. These entire programme attract support from the donor community and are potentially exposed to the exit problem. Kenya also boasts a wide range of informal institutions that extend financial services to different segments of the community. The most widespread are the rotating saving and credit associations (ROSCAs) which are found almost everywhere in the country and act as conduits for converting small regular savings into lump sums, especially among SMEs . These associations are based on trust and close familiarity that is, in turn, based on social institutions such as kinship. Entrepreneurs also rely on friends, relatives, customers and suppliers of materials and provisions as sources of working capital. These divergent credit sources are therefore important components of the financial/credit markets in Kenya.

During the mid-1980s, the government's stated policy was to get markets to determine interest rates. There was therefore a shift toward positive real interest rate. The gap between interest rates applied by commercial banks and non-bank financial institutions narrowed but the gap between minimum deposit rates and maximum lending rates widened (Johnson, 1999). The interest rates were fully liberalised in 1991. This did not increase SMEs access to credit because in addition to broader market imperfections, withholding taxes increased the administrative costs of small accounts. Treasury Bills enjoying tax exemption status were also introduced and reduced the incentive to hold savings in the formal financial institutions. There was also no improvement in the efficiency of the financial sector as evidenced by a widening of the interest rate spread. More significantly, the Government of Kenya became a dominant borrower in the domestic market, mopping out existing financial resources from the market and in the process crowding out the productive sectors. Since credit does not ordinarily flow to the MSE sector, excessive domestic government borrowing further reduced financial resources that were trickling down to the sector. The recent period has also been marked by a banking instability resulting from lax licensing of financial institutions, poor enforcement of prudential regulations, and bad debts. Liberalisation reduced some of the entry barriers and opened new opportunities for extending financial services to the business community. But the financial health of many local banks has remained weak. Kenya's banking sector is characterised by an ever-looming crisis. The Central Bank has been addressing the problem by pushing banks to close loss-making branches and improve loan recovery. Banks have also been allowed to set minimum balances, limiting the access of small clients to banking services and reducing the potential for mobilising savings. Concerns about depositor protection have led to conservative liquidity and cash ratios and increased the reserve requirements. These measures are likely to increase the cost of funds and further distance the SMEs from the banking sector.

"Indeed, the concept of microfinance is not new in Kenya. There has always been the tradition of people saving and/ or taking small loans from individuals and groups within the context of self – help to start business. For example, available evidence suggests that the first credit in Africa was established in northern Kenya in 1955 by Canadian catholic missionaries. However, Susu, which is one of the microfinance schemes in Kenya, is thought to have originated from Nigeria and spread to Kenya in the early twentieth century. Over the years, the microfinance sector has thrived and evolved into its current state thanks to various financial sector policies and programmes undertaken by different governments give independence. Among these are:

Provision of subsidized credit in the 1950s. Establishment of the Agricultural Development Bank in 1965 specifically to address the financial needs of the fisheries and agriculture sector,the establishment of rural and community bank (RCBS), and the introduction of regulations such as commercial banks being requested to set aside 20% of total portfolio, to promote lending to agriculture and small scale industries in the 1970s and early 1980s. Shifting from a restrictive financial sector regime to a liberalized regime in 1986; Promulgation of PNDC law 328 in 1991 to allow the establishment of different categories of non-bank financial institutions, including savings and loans companies, and credit unions.

These policies have led to the emergence of three broad categories of microfinance institutions. These are: Formal suppliers such as savings and loan companies, rural and community banks, as well as some development and commercial banks.

Semi-formal suppliers such as credit unions, financial non-governmental organizations (FNGOs), and co-operatives.

Informal suppliers such as susu collectors and clubs, rotating and accumulating savings and credit association (ROSCAs and ASCAs), traders, moneylenders and other individuals".

Dadson.1997,EconomicsWebInstitute

(www.economicswebinstitute.org/essays/microfinanceKenya .htm).

2.6 Knowledge gap

In the report of a group of SMEs researchers in the informal sector and agro industries (1991) the researchers after their research in seven African countries reported that SMEs in the informal sector experience common constraints. Up on the list is the lack of access to credit lending institutions due to lack of collateral and property ownership. Lack of information and technical knowhow, poor conditions under which SMEs operate and location of financing institutions. Studies by Kinyanjui. Munguti. Rono and Ogoma (1998) showed that food processing and garment making at the micro enterprise level was a small scale domain. The study noted that SMEs have the skills and they have engaged in non-traditional activities like printing. Small and medium enterprises have enhanced the economic growth of many countries in Asia and their presence is starting to be appreciated in Kenya. however their performance has been poor in many parts of Kenya (Söderbom and Teal, 2010). The current study sought to determine extent to which credit availability affect the performance of SMEs despite the apparent numerous sources of credit available on the Kenyan market.

Musinga (1994) in a study on impact of loans in SMEs in Kenya showed that men owned enterprises increased employment at a significantly faster rate than those owned by SMEs. He states that SMEs owned enterprises tend to grow slower. On credit. Kinyanjui (1998). reports that credit is given based on the entrepreneurs ability to repay and the security that one has. These studies also revealed that majority of entrepreneurs were not aware of government of Kenya policies on credit. despite the above findings most lending institutions provide entrepreneurship training programmes to their clients therefore the current study sought to find out the factors that influence the performance of SMEs in Bungoma South District.

SMEs have a high potential of succeeding as entrepreneurs (Kibas. 1997). This would be possible through economic empowerment. Kibas also notes that. micro enterprises owned and ran by SMEs remains small because of failure to reinvest business profit. Nassiuma, (2003) in a study on the impact of Uasin–Gishu Trade Development Joint Board Interventions on micro and small enterprise revealed that, financial support extended to clients was not adequate to enable them to realize substantial growth in their businesses. He noted some improvement in the SMEs after introduction of the loan in most variables, except on profits and employment growth. These studies have identified presence of many obstacles and challenges that may affect growth of SMEs. The present study will focus on the extent of credit availability on the performance of the SMEs; effects of capital borrowed on performance of the SMEs; how terms of payment influence the performance of SMEs and the effects of sources of credit on the performance of SMEs.

Ogolla (2005) revealed in his study on the impact of micro credit in poverty reduction that all micro finance institutions from which the samples were drawn lent clients through groups and relied on the group solidarity model. The study however discovered that whereas most clients did not object to that approach, most of them preferred individual loaning system. He also noted that household expenditures and payment of school fees presented formidable sources of failure for the SMEs. Tubey, (2001)'s study on Non-governmental organization's interventions and the growth of SMEs owned micro and small enterprises concluded that there was a gradual but statistically significant improvement in all performance parameters over the intervention period. She looked at several interventions e.g. training, counselling, and credit. Makhanu, (2006) in his study on the impact of credit financing on the performance of SMES in Kimilili concluded that credit financing had a significant role on the performance of SMEs in terms of growth, information seeking behaviour and attainments of a customer value and satisfaction as indicators of SMEs performance indicators. Imbaya (2004) investigated factors influencing SMEs performance in micro and small-scale enterprises and revealed that SMEs are performing poorly because of lack of access to credit. She further noted that majority of the SMEs did not reinvest their profit in the business but rather used the money to meet their domestic needs. These studies have identified presence of many obstacles and challenges that may affect growth of SMEs. The present study will focus on the extent of credit availability on the performance of the SMEs; effects of capital borrowed on performance of the SMEs; how terms of payment influence the performance of SMEs and the effects of sources of credit on the performance of SMEs.

2.7 Theoretical framework

This study relied on the balanced scorecard theory of Kaplan and Norton (1996). The balanced scorecard is a performance planning and measurement framework. with similar principles as management by objectives. The balanced score card (BSC) began as a concept for measuring whether the smaller scale operational activities of a company are aligned with its larger-scale objectives in terms of vision and strategy by focusing not only on financial outcomes, but also on the human issues, the balanced score card helps provide a more comprehensive view of a business. which in turn helps organizations act in their best long term interests. The strategic management system helps managers focus on performance metrics while balancing financial objectives with customers. process and employee perspectives. measures are often indicators of future performance.

Balanced score card is a tool to execute and monitor the organizational strategy by using a combination of financial and non-financial measures. It is designed to translate vision and strategy into objectives and measures across four balanced perspectives. It gives a framework ensuring that the strategy is translated into a coherent set of performance measures.

Balanced score card theory is based on .Financial perspective, Customer perspective,

Internal process perspective, Learning and growth perspective

This theory is relevant to the present study because the four factors are crucial to determining the performance of small scale business enterprises. The correct use of the four perspectives will increase business assets stock of the business, which will result in increased sales, customers. profits etc. This will trickle down to increased customer satisfaction and the smooth running of the business which eventually will lead to growth of the business.

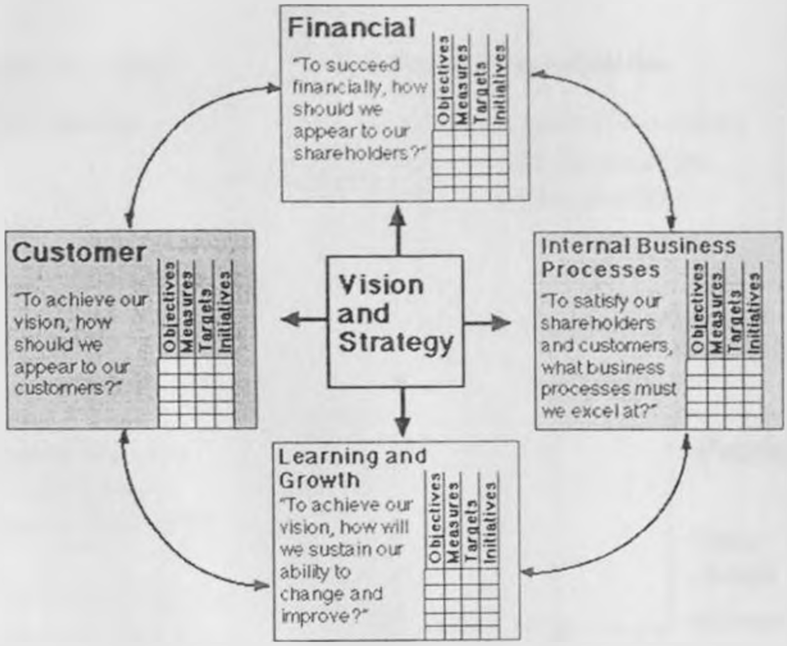

Figure 2.1: Balanced Score Card Diagram. Source: Kaplan and Norton (1996).

This diagram shows a classification of Balanced Scorecard designs based upon the intended method of use within an organization. They describe how the Balanced Scorecard can be used to support three distinct management activities, the first two being management control and strategic control. They assert that due to differences in the performance data requirements of these applications, planned use should influence the type of BSC design adopted.

2.8 Conceptual framework

The conceptual framework for this study was researcher based framework depicted in Figure 1. In the framework the researcher intended to determine how access to finance. influence of loan characteristics, institutional facts and sources of credit determined the growth of SMEs

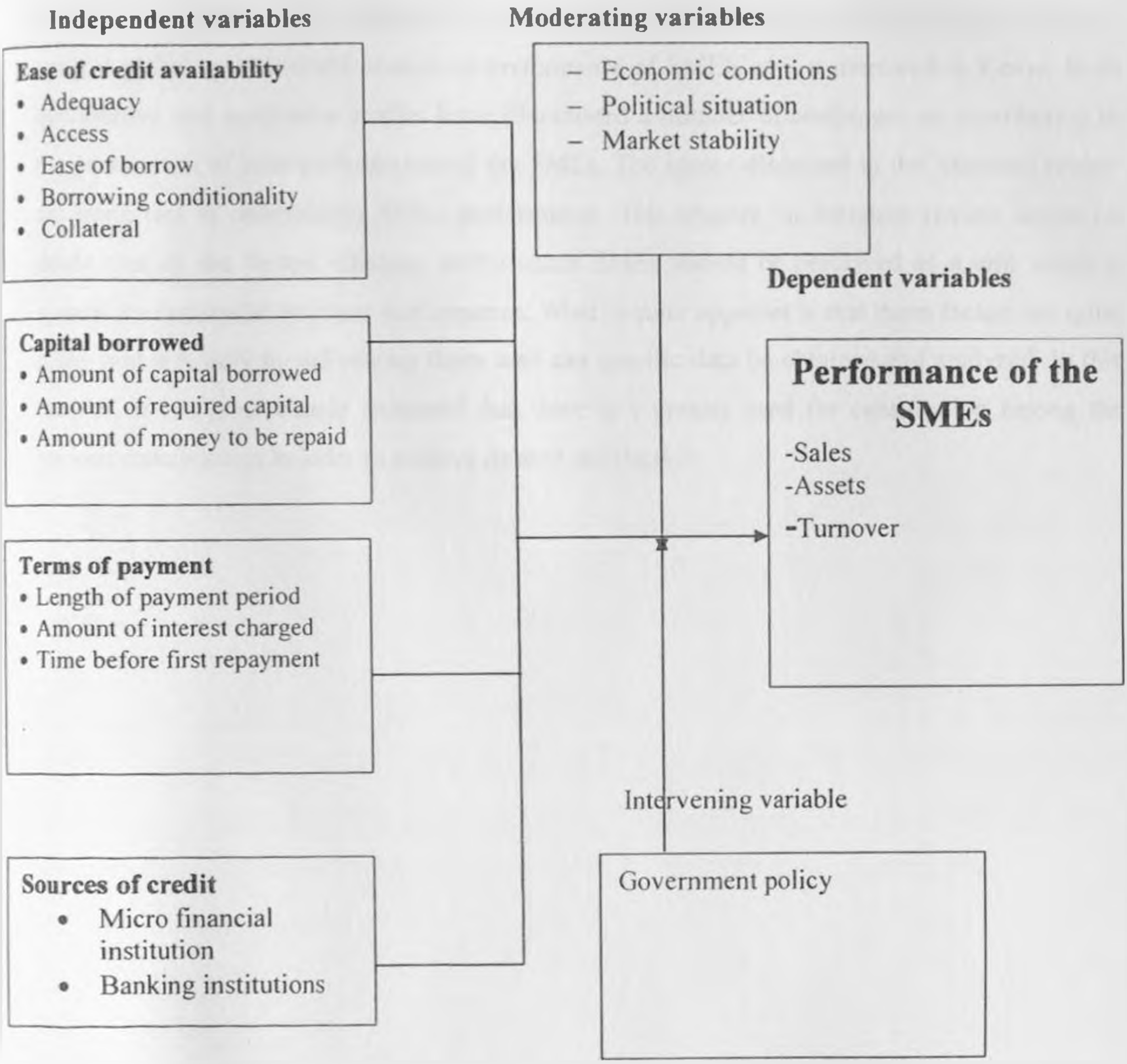

Figure 2.2: Conceptual framework for the study.

It is hypothesized that the independent variable factors with it is components ease of credit available. capital borrowed. terms of payments and sources of credit directly influence the dependent variable performance of SMEs with it is components more sales. more assets and turnover. However this may be accelerated or delayed by the moderating and intervening variables.

2.9 Summary of Literature Review

This Chapter reviewed the literature on performance of SMEs. The review proceeded from the general global and historical context of performance of SMES until it narrowed to Kenya. Both quantitative and qualitative studies have illuminated a number of challenges as contributing to the persistence of poor performance of the SMEs. The issues discussed in the literature review are important in determining SMEs performance. This chapter on literature review leaves no doubt that all the factors affecting performance SMEs should be perceived as a unit within a system for successful business performance. What is quite apparent is that these factors are quite many and it is only by delineating them well can specific data be obtained and analyzed. In this chapter, it has been clearly indicated that there is a greater need for consultation among the various stakeholders in order to achieve needed satisfaction

CHAPTER THREE;

RESEARCH METHODOLOGY

3.1 Introduction

Methodology refers to the application of the principles of data collection methods and procedures in any field of knowledge. This section describes research design. target population, sampling design and sample size. data collection methods. validity and reliability of research instruments and data analysis technique.

3.2 Research Design

The study used descriptive research designs. According to Kerlinger(1973), a descriptive study is not restricted to fact finding. but may often result in the formulation of important principles of knowledge and solutions to significant problems. This design involved the measurement, classification, analysis, comparisons and interpretation of data.

3.3 Target Population

The respondents were the Managers of Small and Medium Enterprises (SMEs) . These owners of the SMEs were selected from across the various sectors namely manufacturing, commerce, trading and service among others. The target population was 145 managers of the SMEs

Table 3.1 Target population

Type of SMEs	Total
Manufacturing	05
Commerce	20
Trade	60
Service	60
Total	145

3.4 Sample size selection

To determine the sample size. the Yamane (1967) formula was used thus:

$n = \frac{N}{1 + Ne^2}$. Where n = required responses

N = Population

e^2 = error limit

Placing the formula for yielded a sample size of:

$$\text{Sample size (n)} = \frac{145}{1 + 145 * 0.05^2} = 106.$$

Therefore a random sample of 106 SMEs was selected and from each Small and Medium Enterprise. 1 manager was selected to provide the requisite information

Table 3.2 Sample population

Type of SMEs	Total
Manufacturing	05
Commerce	10
Trade	41
Service	50
Total	106

3.4 Sampling procedure

A sample is a subset of the population to which the researcher intends to generalize the results. To do this, the researcher wants the sample, or the individuals actually involved in the research. to be representative of the larger population.

The population represents any group of individuals, to whom the researcher (s) wishes to generalize his/her research. Best and Kahn (1998: 12) state that a population is any group of individuals who has one or more characteristics in common those are of interest to the researcher.

Research point out that quantitative studies typically use larger samples selected through probability sampling techniques. while qualitative studies typically use smaller samples selected through non-probability (e.g. purposive) techniques (Fink. 2006; Wiersma & Jurs, 2005; Tashakkori & Teddlie, 2003; Nardi, 2003). For instance. Wiersma and Jurs (2005: 220) affirms that quantitative data often involve random sampling. so that each individual has an equal probability of being selected and the sample can be generalized to the larger population. In contrast. purposeful sampling is often used in qualitative data collection so that individuals are selected because they have experience of the central phenomenon providing the most information for the questions under study. In the current study the sample size of the study comprised of 106.

3.5 Data collection instruments

The main instrument for data collection was the questionnaire for Managers and Document analysis.

3.5.1 Questionnaires

Bourke (2005) simply states that questionnaires are used to obtain different types of information, such as age, gender. it is a convenient way of obtaining information especially where there are large numbers of subject to be handled. Oppenheim (1996) affirms that the questionnaires are one way of obtaining a measure of attitude. The attitudes have two components: beliefs (cognitive) and feelings (emotional or affective). Responses to questionnaire items are what respondents say their belief or say they would do. which are taken as indicators of their beliefs, attitudes and likely behaviour.

3.5.2 Document analysis

Document analysis involved reviewing the contents of target financial documents kept by the SMEs and financial institutions with the aim of adducing some relevant secondary data (Oso and Onen, 2005). In terms of secondary data there was a desk-research done to review the sources relevant to the topic. The sources included materials from the few microfinance institutions in the District and finally the quarterly report on the activities of SMEs from the District helped the researcher in data collection. This technique was used to derive data on performance of the SMEs

3.6 Piloting of the instruments

The pilot study was conducted in eight SMEs to test the reliability of the instruments used in collecting data. Eight Managers from Eight SMEs were purposively selected to fill the questionnaires(Babbie2003) says that the instruments may be pre-tested on a sample of at least ten respondents who do not have to be representative. The information received was used to improve the reliability of the questionnaires

3.7 Validity of Research Instruments

The Principal Component Analysis (PCA) is a type of Factor Analysis which is used to explore the possibility of a factor structure underlying the variables (Brace, Kemp. & Snelgar. 2006). Manning and Munro (2006: 159) explain the usefulness of PCA to measure the validity of variables. In the context of quantitative research, validity is simply defined as "the degree to which it measures what it claims to measure" (Manning & Munro, 2006; Wiersma & Jurs. 2005; Pallant. 2005: Best & Kahn. 1998).

On the basis of the Principal Component Analysis (PCA), the results of pilot study demonstrate that the factor loadings ranged from .732 to .787. The Kaiser-Meyer-Olkin (KMO) Measure of Sampling Adequacy was .640 with the Barlett's Test of Sphericity was significant at less than .05. indicating an acceptable factorability.

However. after the revision of item variables. the results of factorability in the main study were higher. The results of data analysis demonstrate that the factor loadings ranged from .779 to .883. The Kaiser-Meyer-Olkin (KMO) of Sampling Adequacy was .682 with Barlett's Test of Sphericity $p = .000$, indicating a good factorability (Brace. Kemp. & Snelgar, 2006: 318).

Dane (1990) defines validity as the extent to which a measure actually measures what it ought to measure. To ascertain the validity of the research instruments. the research consulted the supervisor and lecturers in the department who are experts in terms of item analysis and research methodology.

3.8. Reliability of Research Instrument

Reliability is defined as the consistency of the methods. conditions. and results (Manning & Munro. 2006: Wiersma & Kurs. 2005; Pallant. 2005; Best & Kahn. 1998). There are three common ways of testing reliability in quantitative research. namely. test-retest reliability. split-half reliability, and coefficient (Munning & Munro. 2006: Pallant, 2005). The test-retest approach is applied when a researcher tests the same set of people on two different occasions and the scores from the first test is correlated with the scores from the second test. In the split-half reliability. a researcher administers questionnaires only once and split the items used to create composite variable into two equivalent halves, followed by creating two composite variables from these two sets and correlate them.

For the purpose of this study, the coefficient alpha (also known as Cronbach's alpha) was applied. The coefficient alpha ranges in values from 0 (no reliability) to 1 (perfect reliability). Gregory (2000, cited in Manning & Munro, 2006: 25) claims:

Coefficient alpha is an index of the internal consistency of the items, that is, their tendency to correlate with one another. Insofar as a test or scale with high internal consistency will also tend to show stability of scores in a test-retest approach. coefficient alpha is therefore a useful estimate of reliability.

They then state that the values of coefficient alpha above .70 are considered to represent "acceptable" reliability, above .80 "good reliability". and above .90 to represent "excellent" reliability. However, Pallant (2005: 90) asserts that with short scales (e.g. scales with fewer than ten items); it is common to find quite low Cronbach values, for example. .50. In this study, the values of coefficient alpha ranged from .75 to .84. indicating an acceptable and good reliability (Gregory cited in Manning & Munro, 2006)

3.9 Data Analysis Techniques

Some researchers report that there are two broad categories of statistical approaches in quantitative research, namely, descriptive (Creswell, 2005; Spatz, 2005; Salkind, 2004; McMillan & Schumacher, 2001). Descriptive statistics are used to summarize, organize, and describe the characteristics of a data collection. Descriptive statistics is the most fundamental way to summarize data and it is a prerequisite for interpreting the results of quantitative research, while inferential statistics are commonly used in reporting results (McMillan & Schumacher, 2001). Similarly. in the context of analyzing quantitative data using statistical techniques. Creswell (2005) explains that descriptive statistics summarize a single variable in a data set or compare how one score relates to all others, while inferential statistical tests are used to assess the differences. relationships, and correlations among variables in the data set. The following section provides a detailed description of the descriptive statistics. which have been used in the study.

The raw data was analyzed using descriptive statistics such as the mode, the mean and standard deviations. Data was presented using APA tables.

Table 3.3 Summary of Data Analysis

Independent Variable	**Dependent Variable**	**Statistical Technique**
1. Extent of credit availability for the SMEs	performance of SMEs	• Frequencies • Percentages
2. Effects of capital borrowed for the SMEs	performance of SMEs	• Frequencies • Percentages
3. Terms of loan repayment	performance of SMEs	• Frequencies • Percentages
4. Sources of credit for the SMEs	performance of SMEs	• Frequencies • Percentages

3.10 Operational definition of variables

There were two variables that were considered in this study. the independent and Dependent variables, the independent variables were credit availability. amount Borrowed, terms of repayment and sources of credit while the dependent variable was Performance of SMEs

Table 3.4 operationalisation of the variables of the study

objectives	Independent variable	indicators	Measuring scale	Tools of measurement
Determining how access to credit influence performance of SMES	Availability of credit	Adequacy Access collateral borrowing conditions	ordinal scale ordinal nominal	questionnaire document analysis Document analysis
To find out how amount of credit influence performance of SMEs	amount borrowed	Amount required Amount given Amount to be repaid	Scale scale	Document Analysis questionnaire
To determine how terms of repayment influence performance of SMEs	Terms of payment	Length of payment period Amount of interest time before first repayment	scale scale scale	Questionnaire Document analysis questionnaire

To find out how sources of credit influence performance of SMEs in Bungoma south District	Sources of credit	Micro financial institutions Banking institutions	nominal ordinal	questionnaire questionnaire

3.11 Ethical consideration of the study

Permission to carry out the study was sought after presentation of study proposal to the supervisors at the University of Nairobi. The nature and purpose of the study will be explained to the respondents by the researcher. The researcher treated all the information given by the respondents with a lot of confidentiality to safeguard the respondent's personal integrity in regard to University's ethical considerations.

In line with human ethics procedures established by the University of Nairobi. the researcher submitted the questionnaire. which was constructed in English to the National Council for Science and Technology (NCST). It was aimed at seeking approval and ensuring the ethical acceptability of the research involving human participants. Accordingly. the pre-testing and pilot study was conducted after obtaining the approval of the NCST.

CHAPTER FOUR

DATA ANALYSIS, PRESENTATION INTERPRETATION AND ANALYSIS

4.1 Introduction

This chapter presents an analysis of the data that was gathered using the tools of research discussed in chapter three. The first part presents the questionnaire response rate. Secondly the researcher presents data on the background information of the respondents and for the business. Section 4.3 presents information on extent of credit availability on the performance of the SMEs in Bungoma South District. Section 4.4 provide and discusses the influence of capital borrowed on the performance of SMEs in Bungoma South District. Section 4.5 provides results and analysis of the how terms of repayment influence performance of SMEs in Bungoma South District. The final section 4.6 presents information on Influence of sources of credit on performance of the SMEs in Bungoma South District. Tables and figures have been used to summarize and illustrate the findings of the study.

4.2 Questionnaire return rate

The study used questionnaires as a tool for data collection. The sample size for this study was 106 SMEs in Bungoma South, Each of the SME managers was given the appropriate questionnaire to answer. The entire respondent returned the questionnaires. From the 106 questionnaires. 106 were filled and returned to the researcher and to the research assistant. This represented a response rate of 100%. The response rate was good when compared to the recommended response rates to verify consistency of measurements required for analysis (for example over 60%, based on Kothari, 2005).

4.3 Influence of credit availability on performance of SMEs in Bungoma South District.

The study sought to find out the influence of credit availability on the performance of SMEs in Bungoma south district and the following findings were revealed.

Capital from financial institutions

The study sought to determine the source of capital for running SMEs and the study enlisted the following findings. 82% (87) respondents revealed that they borrowed money from financial institutions while 18%(19) indicated that they financed their SMEs using the owners capital. The table shows the study findings.

Table 4.1 source of capital for SMEs

Category	Frequency	Percentage
Owner's capital	19	18
From financial institutions	87	82
Others	0	0
Total	106	100

From table 4.1. the findings shows that majority of the respondents revealed that they get their capital from financial institutions with 82% respondents. This finding is supported by previous studies by Johnson who asserted that microcredit is now considered the effective development tool of poor people especially for SMEs. SMEs are become more empowered and play important role in generating income in the rural areas of Kenya (Johnson, 1999).

Access to credit facilities

The study sought to determine access to credit facilities from lending institutions and study enlisted the following findings,84% (89) revealed that the loaning process was too slow. 10%(11) revealed that it was easy, while 6% (6) cited that they do not know. The table below shows the study findings.

Table 4.2 Accessibility to credit facilities

Category	Frequency	Percentage
Loan process too slow	89	84
Loan process easy	11	10
Do not know	6	6
Total	106	100

From table 4.2, the findings majority of the respondents revealed that the loan processing period is too long with 84%. These findings are in line with previous research by Daniel who cited that since most of credit providers are urban located; it has led to lower levels of credit use by rural enterprises hence creating a credit supply constraint (Daniels and Mead. 2010). Membership in a support group increases the level of credit sought for. so that such groups have a strong network side effect. Variations in success rates run across activities. spatially. across the formality/informality divide and credit sources (Dunford. 2001).

Adequacy of the amount borrowed.

The study sought to determine the adequacy of funds borrowed by the SMEs and the findings revealed that 64% (67) responses cited that the amount was not adequate. 26% (28) indicated that it was barely adequate while 10% (11) indicated that it was adequate. The table below shows the study findings.

Table 4.3 Adequacy of the amount borrowed

Category	Frequency	Percentage
Adequate	11	10
Barely adequate	28	26
Inadequate	67	64
Total	106	100

From table 4.3. the findings shows that majority of the respondents revealed that the borrowed amount was inadequate with 64% responses. These findings are also supported by the previous findings by lundvall who asserted that in Kenya. the SMEs are generally under-capitalized due to operational difficulties in accessing credit (Lundvall *et al.*. 1988). Lack of credit is the second severest problem faced by SMEs, the most important being lack of markets and competition (Kimuyu et al., 1999a). Only a small proportion is able to successfully apply for and use credit. More than one third of the enterprises die young due to inadequate working capital. Own funds and family resources form the most important sources of initial and additional capital. Considering the very low incomes and savings rate in the country. SMEs fall back on these sources out of desperation. The small proportion that receives some credit receives very modest amounts. reflecting not only low activity levels but also supply ceiling by non-government organizations. (NGOs) and government credit programs that target the sector (Kimuyu. 1997).

Conditions for borrowing the capital

The study sought to find out the conditions to be fulfilled before SMEs access the loaning facilities and the findings revealed that 71% (75) respondents indicated that it was difficult to meet all the borrowing conditions. 22% (23) cited that it was easy to meet the borrowing conditions while 7% (8) were not sure. The table below shows the study findings.

Table 4.4 collaterals to obtain the capital

Category	Frequency	Percentage
Easy to meet	23	22
Difficult to meet	75	71
Not sure	8	7
Total	106	100

From table 4.4. the findings shows that majority of the respondents revealed that the loaning conditions were difficult to meet with 71% responses. The findings are in line with the previous findings by maddala and mei Qiang, who asserted that credit-seeking decision is a three-stage process. Entrepreneurs first decide on whether or not they need credit. Once that decision is affirmative, a further decision has to be made regarding the appropriate credit source (Maddalla, 1997). An additional decision relates to the level of credit to seek out and how well the entrepreneur was informed about the terms of borrowing and repayments. But even when enterprises have a need for external credit. they may not borrow if their perceptions on the costs of applying for a loan outweigh the expected receipts (Mei Qiang, 2002). They may also lack enough cash to meet the application costs. Enterprises may also shy away from borrowing due to a poor collateral position and lack of requisite information about the capital borrowed. which requires quite a high level of mentorship from the micro-finance institutions. Collateral requirements imply that there would be enterprises that prefer external funds but are unable to apply for such funds (Mookherjee, 1999).

4.4 Influence of the amount of credit borrowed visa via performance of SMEs in Bungoma South District.

The study sought to investigate the influence of the borrowed amount of credit visa a vis performance of SMEs.

Credit borrowed in relation to the business operations

The study sought to find out if the credit borrowed was enough for the operations of SMEs and the findings revealed that 68% (73) respondents indicated that the items were more expensive than expected. 22% (22) cited that it was too little while 10% (11) indicated that they had too many things to purchase. The table below shows the study findings.

Table 4.5 Credit borrowed in relation to business operations

Category	Frequency	Percentage
Too little	22	22
Items more expensive than expected	73	68
Too many things to purchase	11	10
Total	106	100

From table 4.5. the findings shows that majority of the respondents revealed that the credit borrowed was not adequate for business operations indicating that the items were more expensive than expected with 68% responses. The findings are in line with other studies that have shown that most Small scale business enterprises perceive borrowing as necessary for business and the impact of borrowing on business performance as positive (Mwenda. 1993: Rogaly. Fisher and Mayo, 1999; Moyi, 2000). Yet they have weak mentorship in the utilization of the borrowed capital resulting collapses of the loan use. Among the small group of applicants, there are gender. enterprise location. business activity and formality status differences. which must be well factored in during the loan borrowing by the business enterprises. Traders appear more inclined to borrow than entrepreneurs in other activities and the incidence of loan application is greater among female proprietors and urban based enterprises (Scully. 2004). Informal enterprises are dramatically more likely to apply for a loan as do those that are larger and older as well as those owned by older entrepreneurs. if they are provided with novel methods of proper loan utilization. The life expectancy of small scale business enterprises is generally short so that most do not live long enough to build contacts and reputation necessary in seeking out credit (Sebstad and Monique. 2001). Smallness is also a major impediment to effective participation in the credit markets

Mode of Investment

The study sought to find out how the SMEs invested their capital and the findings revealed that 52% (55) they bought items for trade. 21% (22) cited that they bought raw materials, 17% (18) revealed that they bought working equipments while 10% (11) revealed that they paid rent for the premises. The table below shows the study findings.

Table 4.6 Mode of investment

Category	Frequency	Percentage
Bought items for sale	55	52
Bought raw materials	22	21
Bought working equipments	18	17
Paid rent for premises	11	10
Total	**106**	**100**

From table 4.6, the findings shows that majority of the respondents invested their borrowed credit in the purchase of items for trade with 52% responses. The findings are supported by recent impact studies by Sebstad and Cohen (2011). Whose research documented the positive impact of MFI programs, but the impacts have tended to be more modest in scale than often assumed. According to Sebstad and Cohen (2010), microfinance strives to "scale up" to serve as many households as possible. Among the range of possible micro-financial services, micro-credit has predominated. on the assumption that it will deliver higher incomes and increased assets to the poor through micro-enterprises. Thomas *et al*. (2002) argues that. by delivering financial services at a scale. and by mechanisms appropriate to them. micro-credit can reach poor people. By providing the poor people with credit for micro-enterprises it can help them work out their own way and by providing loans rather than grants the micro-credit provider can become sustainable through recycling resources over and over again.

Approximate value of business assets

The study also sought to determine the approximate value of SMEs in Bungoma South District and the findings revealed that most businesses were valued between 10.000-20.000 Ksh.20% (21) citing that their business were valued between 20.000-50.000Kshs. While 7% (8) indicating that their businesses were valued above 100,000Kshs.The table below shows the study findings

Table 4.7Approximate value of business Assets

Category	Frequency	Percentage
Value between 1001-5000	0	0
Valued between 5001-10,001	0	0
Value between 10.001- 20.001	77	73
Valued between 20.000-50,000	21	20
Value above 100.000	8	7
Total	106	100

From table 4.7 the findings shows that majority of the respondents have their business assets valued between 10,000-20.000 Kshs. with 73% responses. These findings are supported by Von pischke who asserted that despite government-backed schemes and development finance initiatives SMEs performed unsatisfactorily and in retrospect may have distorted the evolution of financial markets in the country. Studies show that when credit is advocated as the primary remedy for low level productivity or when loans are used to stimulate growth. these strategies often lack mechanisms for excluding risky borrowers (von Pischke. 1992). As a result. many borrowers fail to repay and the credit programmes are left with a progressively drying pool of funds for lending. This phenomenon. referred to as the exit problem of credit programme, has been evident in Kenya. In the 1980s, Savings and Credit Co-operatives (SACCOs) and non-bank finance institutions (NBFIs) expanded rapidly to fill the gap created by commercial banks. but were only useful for salaried employees for whom the lending and borrowing entitlements were clearer.

Business performance indicators before and after borrowing the credit from microfinance institution

The study sought to be find out the performance indicators of the SMES before and after borrowing credit from microfinance institution and the following findings were revealed.81% (86) indicated there is no significant change in the performance of SMES in the last six years while 19% (20) citing that most SMES have closed down in the last six years. The table shows the study findings.

Table 4.8 Trends in the performance of SMEs before and after getting credit

Category	Frequency	percentage
Significant improvement	0	0
Significant	0	0
Not significant	86	81
Closed down	20	19
Total	106	100

From table 4.8, the finding revealed that majority of SMEs did not make any significant improvement before and after getting credit with 86% responses. The findings are support by Greenbaum and Harper when they asserted that eenterprises' within finance, insurance and real estate enjoy the highest success rate while those in community and other social services face the lowest success rates (Greenbaum, 2003) because of lack basic skills. this indicate that knowledge base is paramount. Additional differences are observable across credit sources with enterprises seeking credit from non-bank finance institutions showing low success rate and those seeking from co-operative society's high success rates (Harper, 2003). Other studies have shown that small enterprises are particularly disadvantaged with regard to resolution of business related disputes due to high litigation costs and poor contract enforceability (Hulme and Mosely. 1996).

4.5 Terms of loan repayment by SMEs in Bungoma South District

The study sought to find out the terms of loan repayment and its effects on performance of SMEs in Bungoma South District and the study enlisted the following findings.

Source of money for repayments visa via performance of SMEs

The study sought to determine whether the repayment terms affect the performance of SMEs and the findings revealed that 84% (89) respondents felt that repayment terms adequately interfered with the performance of SMEs, while 16% (17) indicating that it do not interfere at all with the performance of SMEs. The table below shows the study finding.

Table 4.9 repayment terms vis a vis performance of SMEs

Category	Frequency	Percentage
Adequately interfere	89	84
Don't interfere at all	17	16
Total	**106**	**100**

From table 4.9. the finding revealed that majority of SMEs were interfered with by loan repayment terms with 84% responses. The findings are supported by previous research findings by Cheston and Kuhn that despite all the efforts channelled towards assisting SMEs. they are faced by diverse challenges as far as repayment of the credits is concerned. Despite earning a living. SMEs have little control over the household's finances or even over their own earnings. The men in the family continue to decide on expenditures. As long as SMEs continue to lack social resources such as access to education which make them unable to prudently use limited financial resources they obtain.

Default in loan repayment Vis a vis performance of SMEs in Bungoma South District

The study sought to find out if default in loan repayment had any effect on the performance of SMEs, 82% (87) indicated that it has led to total closure of SMEs while 18% (19) indicated that it had little effect to the performance of SMEs in the study District. The table below shows the study findings.

Table 4.10 Default in loan repayment

Category	Frequency	Percentage
Total closure	**87**	**82**
Little effects	**19**	**18**
Total	**106**	**100**

From table 4.10, the finding revealed that majority of SMEs in Bungoma South District faced total closure in case of default in loan repayment with 82% responses. These findings are supported by Amendariz (2005) in a study of two Grameen replications in the Philippines it was found that most clients have difficulty repaying their loans and hence leading to closure of their premises. In a survey of clients in repayment arrears and clients who had exited the program (Faulu a local MFI) found that 74% of their clients had diverted their last loan and therefore failed to repay. If credit meant for business development is diverted to consumption needs, the borrowers still have to repay the loans. Consequently the business does not expand and it cannot therefore service subsequently higher loans. Loan repayments may require the borrower to forego the gratification of basic needs or to default.

4.6 Sources of credit to the SMEs in Bungoma South District.

The study sought to find out the sources of credit to the SMEs in Bungoma South District and the study enlisted the following findings.

Source of the initial capital for SMEs

The study sought to find out the initial source of capital for the SMEs in Bungoma South District and the study findings revealed that 84%(89) of respondents indicated that they borrowed the initial capital from family and friends.10%(11) citied that they borrowed from formal leading institutions while 6%(6) revealed that own savings. The table below shows the study findings.

Table 4.11 Sources of the initial capital for SMEs

Category	Frequency	Percentage
Loan from employer	0	0
Own savings	6	6
Borrowed from formal institutions	11	10
Borrowed from family and friends	89	84
Total	106	100

From table 4.11, the findings , majority of the respondents revealed that they got there initial capital from family and friends with 84% responses. These findings are in line with the previous findings by Rutherford. who asserted that Micro-credit alone is not enough service to empower the people economically. Rutherford (2000) elucidate that, It is paramount to look beyond micro-credit and frame it in terms of including micro-financial services other than credit for micro enterprises: savings, consumption loans and insurance in particular. A range of those financial services are important to meet the needs of poor people, both protecting them from fluctuating incomes and livelihoods. While microfinance providers emphasize investments of working or fixed capital in micro-enterprises, the reality is that many clients use the credit for consumption.and meeting there basic needs within the household. Such consumption makes households to run into debt. More appropriate financial products for this purpose are savings. insurance and loans which will allow poor people to repay the loans and interests, yet these have received far less attention than micro-credit for micro-enterprises (Rutherford: 2000).

Influence of different sources of credit on the performance of SMEs in Bungoma South District

The study sought to determine the influence of different sources of credit on the performance of SMEs in Bungoma South District and the findings revealed that different sources of credit do not have a positive influence on the performance of SMEs with 64% (67) responses, while 26% (28) indicated that it had a positive influence to the performance of SMEs and 10% (11) indicated that it barely influence performance of SMEs in Bungoma South District. The table below shows the study findings

Table 4.12 influence of different sources of credit on performance of SMEs in Bungoma South District

Category	Frequency	Percentage
Positive influence	28	26
No influence	67	64
Barely influence	11	10
Negatively influence	0	0
Total	**106**	**100**

From table 4.12, From the findings majority of the respondents(64%) revealed that sources of credit have no positive influence on performance. The findings are in line with other previous research findings by Hulme and Mosly (1996) who asserted that far less attention has been paid to the need to reduce the risk, perhaps the most pressing need especially for the poorest households. They argue that, a proportion of micro-credit clients have become worse off after accessing micro loans. The need to reduce risk is why poor people would prefer regular wage labour than managing their own micro-enterprise, if only such opportunities were available (Ibid).

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATION

5.1 Introduction

This chapter provides a summary of major findings as deduced by the study, it also presents Conclusions. Recommendations and areas of further research.

5.2 Summary of findings.

The study sought to determine the source of capital for running SMEs and study enlisted the following findings, 82% (87) respondents revealed that they borrowed money from financial institutions while 18%(19) indicated that they financed their SMEs using the owners capital.

On the availability to credit facilities from lending institutions the study enlisted the following findings. 84% (89) revealed that the loaning process was too slow. while10 %(11) revealed that it was easy. while 6% (6) citing that they do not know.

The findings also revealed that 64% (67) responses cited that the amount was not adequate, 26% (28) indicating that it was barely adequate while 10% (11) indicating that it was adequate. The findings shows that 71% (75) respondents indicated that it was difficult to meet all the borrowing conditions. 22% (23) citing that was easier to meet the meet the borrowing conditions while 7% (8) were not sure.

The findings revealed that 68% (73) respondents indicated that the items were more expensive than expected. 22% (22) citing that it was too little while 10% (11) indicating that they had too many things to purchase. The findings revealed that 52% (55) respondents revealed that they bought items for trade. 21% (22) citing that they bought raw materials, 17% (18) revealed that they bought working equipments while 10% (11) revealed that they paid rent for the premises.

The study also sought to determine the approximate value of SMEs business .The findings revealed that their businesses were valued between 10,000-20,000 Ksh20% (21) citing that their business were valued between 20.000-50.000Kshs while 7% (8) indicating that their business were valued above 100.000Kshs. The findings also that 81% (86) indicated there is no significant charge in the performance of SMES in the last six years while 19% (20) citing that most SMES has closed down in six years.

The study sought to determine whether the repayment terms affect the performance of SMEs and the findings revealed that 84% (89) respondents felt that repayment terms adequately interfered with the performance of SMEs, while 16% (17) indicating that it do not interfere at all with the performance of SMEs. The findings shows that 82% (87) indicated that it has led to total closure of businesses while 18% (19) indicating that it had little effects to performance of SMEs in the study District..

The study sought to find the initial source of capital for the SMEs in Bungoma South District and the study findings revealed that 84%(89) of respondents indicated that borrowed the initial capital from the family and friends,10%(11) citing that they borrowed from formal leading institutions while 6%(6) revealed that own savings. The findings revealed that different sources of credit do not have a positive influence on the performance of SMEs with 64% (67) responses, while 26% (28) indicating that it had positive influence to the performance of SMEs and 10% (11) indicated that it barely influence pperformances of SMEs in Bungoma South District.

5.3 Discussion of the study findings.

Concerning the Influence of credit availability on performance of SMEs in Bungoma South District the findings shows that majority of the respondents revealed that they get their capital from financial institutions with 82% respondents. This finding is supported by previous studies by Johnson who asserted that microcredit is now considered the effective development tool of poor people especially for SMEs. SMEs are become more empowered and play important role in generating income in the rural areas of Kenya (Johnson. 1999). The findings also shows that majority of the respondents revealed that the loan processing period is too slow with 84%. These findings are in line with previous research by Daniel who cited that since most of credit providers are urban located; it has led to lower levels of credit use by rural enterprises hence creating a credit supply constraint (Daniels and Mead, 2010). Membership in a support group increases the level of credit sought for, so that such groups have a strong network side effect. Since education and credit sources are important determinants of the level of credit. the mentorship by the micro finance institutions picks up their impact. Small scale business enterprises enjoy a high success rate regarding positive response and amounts received if they are well mentored by the micro finance institutions (MFI). These high success rates suggest near perfection in the self-selection and application targeting processes. Variations in success rates run across activities, spatially, across the formality/informality divide and credit sources (Dunford, 2001).

Concerning the influence of the amount of credit borrowed vis a vis performance of SMEs in Bungoma South District the findings shows that majority of the respondents revealed that the borrowed amount was inadequate with 64% responses. These findings are also supported by the previous findings by lundvall who asserted that in Kenya, the SMEs are generally under-capitalized due to operational difficulties in accessing credit (Lundvall *et al.*, 1988). Lack of credit is the second severest problem faced by SMEs, the most important being lack of markets and competition (Kimuyu et al., 1999a). Only a small proportion is able to successfully apply for and use credit. More than one third of the enterprises die young due to inadequate working capital. Own funds and family resources form the most important sources of initial and additional capital. Considering the very low incomes and savings rate in the country, SMEs fall back on these sources out of desperation. The small proportion that receives some credit receives very modest amounts, reflecting not only low activity levels but also supply ceiling by non-government organizations. (NGOs) and government credit programs that target the sector (Kimuyu, 1997). The findings also shows that majority of the respondents revealed that the loaning conditions were difficult to meet with 71% responses. The findings are in line with the previous findings by maddala and mei qiang, when they asserted that credit-seeking decision is a three-stage process. Entrepreneurs first decide on whether or not they need credit. Once that decision is affirmative, a further decision has to be made regarding the appropriate credit source (Maddalla, 1997). An additional decision relates to the level of credit to seek out and how well the entrepreneur was informed about the terms of borrowing and repayments. But even when enterprises feel a need for external credit, they may not borrow if their perceptions on the costs of applying for a loan outweigh the expected receipts (Mei Qiang, 2002). They may also lack enough cash to meet the application costs. Enterprises may also shy away from borrowing due to a poor collateral position and lack of requisite information about the capital borrowed, which requires quite a high level of mentorship from the micro-finance institutions. Collateral requirements imply that there would be enterprises that prefer external funds but are unable to apply for such funds (Mookherjee. 1999). The findings shows that majority of the respondents revealed that majority of respondents found that the credit borrowed was not adequate for business operations indicating that the items were more expensive than expected with 68% responses.

The findings are in line with other sstudies that have shown that most Small scale business enterprises perceive borrowing as necessary for business and the impact of borrowing on business performance as positive (Mwenda, 1993; Rogaly, Fisher and Mayo. 1999: Moyi. 2000). Yet they have weak mentorship in the utilization of the borrowed capital resulting collapses of the loan use. Among the small group of applicants. there are gender. enterprise location. business activity and formality status differences, which must be well factored in during the loan borrowing by the business enterprises. Traders appear more inclined to borrow than entrepreneurs in other activities and the incidence of loan application is greater among female proprietors and urban based enterprises (Scully, 2004). Informal enterprises are dramatically more likely to apply for a loan as do those that are larger and older as well as those owned by older entrepreneurs. if they are provided with novel methods of proper loan utilization. The life expectancy of small scale business enterprises is generally short so that most do not live long enough to build contacts and reputation necessary in seeking out credit (Sebstad and Monique. 2001). Smallness is also a major impediment to effective participation in the credit markets. The findings shows that majority of the respondents revealed the bulk of SMEs have invested their borrowed credit in the purchase of items for trade with 52% responses. The findings are supported by recent impact studies by Sebstad and Cohen (2011).have documented the positive impact of MFI programs, but the impacts have tended to be more modest in scale than often assumed. According to Sebstad and Cohen (2010), microfinance strives to "scale up" to serve as many households as possible. Among the range of possible micro-financial services. micro-credit has predominated. on the assumption that it will deliver higher incomes and increased assets to the poor through micro-enterprises. Indeed injecting capital into existing micro enterprises or creating new ones may enhance that their poor owners face. Thomas *et al.* (2002) argues that. by delivering financial services at a scale. and by mechanisms appropriate to them. micro-credit can reach poor people. By providing the poor people with credit for micro-enterprises it can help them work out their own way and by providing loans rather than grants the micro-credit provider can become sustainable by recycling resources over and over again. The findings shows that majority of the respondents have their business assets valued between 10.000-20,000 Kshs with 73% responses. These findings are supported by Von pischke who asserted that despite government-backed schemes and development finance initiatives performed unsatisfactorily and in retrospect may have distorted the evolution of financial markets in the country. Studies show that when credit is advocated as the primary remedy for low level productivity or when loans are used to stimulate growth. these strategies often lack mechanisms for excluding risky borrowers (von Pischke, 1992). As a result. many borrowers fail to repay and the credit programmes are left with a progressively drying pool of funds for lending. This phenomenon. referred to as the exit problem of credit programme, has been evident in Kenya. In the 1980s, Savings and Credit Co-operatives (SACCOs) and non-bank finance institutions (NBFIs) expanded rapidly to fill the gap created by commercial banks, but were only useful for salaried employees for whom the lending and borrowing entitlements were clearer.

Concerning the Terms of loan repayment by SMEs in Bungoma South District the finding revealed that majority of SMEs were adequately interfered with by loan repayment terms with 84% responses. The findings are supported by previous research findings by Cheston and Kuhn that despite all the efforts channelled towards assisting SMEs, they are faced by diverse challenges as far as repayment of the credits. Despite earning a living, SMEs have little control over the household's finances or even over their own earnings. The men in the family continue to decide on expenditures. As long as SMEs continue to lack social resources such as access to education they will only be able to make limited use of the financial resources they have obtained, Cheston and Kuhn (2002). The finding also revealed that majority of SMEs in Bungoma South District face total closure in case of default in loan repayment with 82% responses. These findings are supported by Amendariz (2005) in a study of two Grameen replications in the Philippines found that most clients found it difficult to repay their loans and hance leading to closure. In a survey of clients in repayment arrears and clients who had exited the program (Faulu a local MFI) found that 74% of their clients had diverted their last loan and therefore failed to repay. If credit meant for business development is diverted to consumption needs, the borrowers still have to repay the loans. Consequently the business does not expand

and it cannot therefore service subsequently higher loans. Loan repayments may require the borrower to forego the gratification of basic needs or to default.

Concerning the Sources of credit to the SMEs in Bungoma South District the findings shows that majority of the respondents revealed the bulk of SMEs in Bungoma South District got their initial capital from family and friends with 84% responses. These findings are in line with the previous findings by Rutherford, who asserted Micro-credit alone is not enough service to empower the people economically. Rutherford (2000) elucidate that. It is paramount to look beyond micro-credit and frame it in terms of including micro-financial services other than credit for micro enterprises: savings. consumption loans and insurance in particular. A range of those financial services are important to meet the needs of poor people. both protecting them from fluctuating incomes and livelihoods. While microfinance providers emphasize investments of working or fixed capital in micro-enterprises. the reality is that many clients use the credit for consumption. smoothing. especially as most funds are fungible within a household. Such consumption-smoothing can allow households to cope more effectively, but it also runs the risk of pushing them further into debt if they cannot repay the loan out of enhanced income streams. More appropriate financial products for this purpose are savings. insurance and loans to allow poor people to repay the loans and interests. And yet these have received far less attention than micro-credit for micro-enterprises (Rutherford: 2000). the findings shows that majority of the respondents revealed the bulk of SMEs in Bungoma South District have no positive influence to performance by different sources of credit by 64% responses. The findings are in line with other previous research findings by Hulme and Mosly (1996) far less attention has been paid to the need to reduce the risk. perhaps the most pressing need especially for the poorest households. They argue that. a proportion of micro-credit clients have become worse off after accessing micro loans. The need to reduce risk is why poor people would prefer regular wage labour than managing their own micro-enterprise. if only such opportunities were available (Ibid).

5.4 Conclusions.

The study sought to investigate the factors influencing the performance of small and medium enterprises (SMEs) in Bungoma South District, Kenya. The findings shows that majority of the respondents revealed that they get their capital from financial institutions, majority of the respondents revealed that the loan processing period is too long. majority of the respondents revealed that the borrowed amount was inadequate and lastly the findings show loaning conditions were difficult to meet.

credit borrowed was not adequate for business operations indicating that the items were more expensive than expected. the findings revealed that a bulk of SMEs have invested their borrowed credit in the purchase of items for trade. majority of the respondents have their business assets valued between 10,000-20,000 K.shs. majority of SMEs did not make any significant improvement before and after getting credit.

The finding revealed that majority of SMEs were interfered with by loan repayment terms, the finding also revealed that majority of SMEs in Bungoma South District faced total closure in case of default in loan repayment.

The findings shows that majority of the respondents revealed that the bulk of SMEs in Bungoma South District got their initial capital from family and friends and lastly the findings shows that majority of the respondents revealed that the bulk of SMEs in Bungoma South District have no positive influence to performance by different sources of credit.

5.5 Recommendations of the Study

On the basis of the findings and conclusions above, the following section presents the recommendations of the study

Regulations require loans to be collateralized while limiting the types of acceptable collateral. At the same time the laws and registries on collateral (especially for movables such as equipment) need to be updated to promote their use in raising capital

A well-functioning and competitive credit information system that incorporates positive and negative information and covers all sectors of the economy (not just financial institutions) is imperative for credit to continue to develop in Kenya. Without access to reliable information on the financial condition of a debtor. and his willingness to pay as evidenced by historical payment patterns. creditors tend to limit the amount of credit by relying only on the value of security (collateral) available

Unsuccessful past attempts to promote the SME sector could lead authorities (and sceptical banks) to resist new SME policies due to a perceived high risk of failure. Past attempts to promote the sector. have not lived up to expectations. The private sector could build on this experience to focus on proven "debt-plus" mezzanine funding mechanisms to promote greater SME financing. Debt-plus financing for SMEs consists of hybrid loans that allow the company to repay the loan on the basis of its cash flow instead of a pre-determined amortization table. In exchange. the lender has the right to share in the company profits or receive an equity interest in the company that can be sold back to the principals at a premium.

Rapid growth at the top and bottom ends of the market could distract both the public and private sectors from the missing SME middle. Banks are rapidly expanding at the top end of market and are also expanding regionally and internationally. At the micro credit level. MFBs are growing and professionalizing. However. too little is being done to promote growth of the missing middle in SME finance. and policy makers and funders should refocus efforts on this vital sector. they should review and where necessary reform legislation and regulation on collateral. Legislation and regulations should be reformed to incorporate the realities of the Kenyan SME market, broaden the definition of acceptable guarantees. and improve use of debtor credit history.

5.6 Suggestions for further research

To bring more light into the issue investigated in this study, it was suggested that:

1. A similar study may be carried out in other counties to compare the findings.
2. Evaluation of SMEs in relation to access to Banking institutions.
3. Adequacy of Financial assistance to SMEs in relation to performance.

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APPENDICES

Appendix I: Introduction letter

University of Nairobi

Department of Project Planning and Management

Dear Respondent.

Re: "Factors influencing performance of small and Medium Enterprises (SMEs) in Bungoma South District, Kenya".

I am a Masters student in Department of Project Planning and Management. University of Nairobi undertaking a research on **"Factors influencing performance of small and Medium Enterprises (SMEs) in Bungoma South District Kenya"**

I am requesting for your assistance by filling in the questionnaires that will enable me accomplish my research objectives. All responses will be treated with total confidentiality. Do not therefore write your name anywhere on the questionnaire. Please kindly respond to all items (questions).

Thank you

Yours sincerely,

Chrispinus Juma Ndombi

(L50/66749/10)

Appendix II: Questionnaires for the SMEs

Part I: Personal and business back ground

1. Age of respondent:

< 18 [ ] 18-25 [ ] 26-35 [ ] 36-50 [ ] > 50 [ ]

2. Marital status

Married [ ] Single [ ] Separated [ ] Divorced [ ]

Windowed [ ]

3. What is your highest level of education: None [ ] Primary [ ] Secondary [ ]

Tertiary [ ] University [ ] University [ ]

4. Occupation before you started the business?

Unemployed [ ] Employed [ ] Operating another type of business [ ]

Farmer [ ] Others (Specify)____________________

5. What is the nature of your business?

Trade and Commerce [ ] Manufacturing [ ] Service [ ]

6. Why did you choose to start this business?

Skilled in the activity [ ]

Family has been engaged in this type of business [ ]

Its High turnover [ ]

7. Who manages the business on a day today basis?

Self [ ] Wife [ ] Husband [ ] Employees [ ]

Son [ ] Relative [ ]

Part III: Access to business credits

1 For how long has the current SMEs business been in existence?

< 6 months [ ] 6-12 months [ ] 13-24 months [ ] 25-36 months

37-60 months [ ] Over 60 months

2 Did you borrow the money you are using from a financial institution?

Yes [ ] No [ ]

3. Did you find access to credit easy? Yes [ ] No [ ]

b. If yes. what problems did you experience? e.g. Loan process too slow

....

....

....

....

4. Did you find the amount of capital you wanted to be adequate?

Yes [ ] No [ ]

5. Did you present a lot of collaterals to obtain the credit?

Yes [ ] No [ ]

7. Can you describe the conditions for borrowing the capital?

Easy [ ] Difficult [ ] Not sure [ ]

8. Did you experience any problems? Yes [ ] No [ ]

Part IV: Amount of credit borrowing

1. What was your initial capital? KSh.......................................

2. How much of the capital had you initially applied for.................

3. Was the credit borrowed enough for the business operation?

b. If no, why?

Too little [ ]

Items were more expensive than expected [ ]

Too many things to purchase [ ]

Other specify................................

4. How did you invest the capital?

Paid rent the premises [ ] Bought raw materials [ ]

Bought working equipment [ ] Used to employ workers [ ]

Bought items for trade [ ] Other specify.......................

5 What is the approximate value of your business assets?

Amount in Kshs	Before	After
Valued < 1,000		

Valued between 1,001-5.000
Valued between 5,001-10,000
Valued between 10.001-20.000
Valued between 20.001-50.000
Valued > 100.000

5. Indicate in the table below how the business has been performing both before and after the loan?

		After the loan					
Item	Before The Loan (KShs)	Year 1 KShs	Year 2 KShs	Year 3KShs	Year 4 KShs	Year 5 KShs	Year 6 KShs
Sales							
Cost							
Income							
Expenses							
Profits							
Stock							
Total assets							
Total Liabilities							
Other (Specify)							

Part V: Terms of loan repayments

1. Who decided on how the loan would be utilized?

Self [ ] Spouse [ ]

Friends [ ] Other (specify)........................

2. What is the frequency of the loan repayment?

Daily [ ] Weekly [ ] Fortnight [ ]

Monthly [ ] Yearly [ ]

3. What was the source of money used to repay the loan?

Sales from the business [ ] Borrowed money [ ]

Own savings [ ] Other specify............................

4. Have you defaulted in Loan repayment at anyone time? Yes [ ] No [ ]

b. If yes, what was the cause for the default?

Shortage of funds [ ] Did not make profits [ ]

Did not sell anything [ ] Spend the money doing other things [ ]

Did not give it a priority [ ]

5. Were you penalised? Kshs .... yes No N/a

6. How much was the penalty? Kshs ....

7. How did you utilize the loan?

Invested in other businesses [ ] Invested I this business [ ]

Used it in other family responsibilities [ ]

Other specify....................................

Part VI: Sources of credit to the SMEs

1. What were the sources of the initial capital?

Loan from employer [ ] Borrowed from formal institutions [ ]

Own savings [ ] Funds borrowed from family or friends [ ]

Others (Specify)...............................

2. Have you received any loan from any other source? Yes [ ] No [ ]

b. If Yes, Why did you look for a loan from another organization other than the present Micro Credit Scheme?

....

....

....

....

....

3. How did you come to know about the Micro Credit Scheme you borrowed from?

A member Chief's Baraza News papers

Other specify................................

Part VII: Influence of loan on SMEs

1. What type of operational technology have you used in your business

Type of technology	Before the loan	After the loan
Manual Labour		
Simple hand tools		
Combination of manual and machines		
Others (Specify)		

2. Indicate your employment status before and after the loan

	No. Employees	
Type of employee	Before the loan	After the loan
Part time		
Full-time		

3. What future plans do you have for your business?

Build own premises

Expand in other areas

Build own premises to accommodate the business

Become a wholesaler

Increasing stock

Other (Specify) ....

THANK YOU VERY MUCH FOR YOUR CO-OPERATION