THE EFFECT OF LOAN REPAYMENT FREQUENCY ON THE CASH FLOWS OF SMEs IN KANDUYI CONSTITUENCY OF KENYA

BY

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DECLARATION

This research project is my original work and has not been submitted to any other college, institution, examination body or university other than the University of Nairobi for academic credit. No part of this research should be reproduced without my consent or that of the University of Nairobi.

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DEDICATION

I dedicate this research project to my parents; Rev. Francis Wafula Walusaka & Mrs. Ruphina Nanjala Wafula for taking care of me and inspiring me throughout the entire process. I also dedicate it to my wife Regina, my children Daisy, Japheth & Silverstein and all my siblings.

ABSTRACT

This study sought to investigate the effect of loan repayment frequency on the cash flows of SMEs in Kanduyi constituency in Bungoma County. The objective of the study was to determine how frequency of loan repayment affects the business cash flows of SMEs in Kanduyi constituency, Bungoma County. The research design that was adopted in this study was the quantitative survey design. The study employed regression analysis of data collected in the study. The Statistical Package for Social Sciences (SPSS) was used to analyze data. The study revealed that frequency of loan repayment does not have a significant effect on the cash flows of SMEs. Majority 67.39% indicated that frequency of loan repayment does not affect SMEs' cash flows. Only 32.61% agreed that frequency of loan repayment affects SME's cash flows. The loan amount and business sector does not have a significant effect on the cash flows of SMEs. The study, however, found out that age of business has a significant effect on the cash flows of SMEs. In conclusion, the study found out that SMEs could choose to repay the loans either on weekly basis or monthly. The frequency of loan repayment has no significant effect on the cash flows of SMEs.

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LIST OF ACRONYMS AND ABBREVIATIONS

AMFI: Association of Microfinance Institutions

CBK: Central Bank of Kenya

ICDC: Industrial and Commercial Development Corporation

KIE: Kenya Industrial Estate

LGF: Loan Guarantee Fund

Ltd: Limited

MDGs: Millennium Development Goals

MFIs: Micro-Finance Institutions

SACCO: Savings, Credit and Cooperative Societies

SHGs: Self Help Groups

SMEs: Small and Micro Enterprises

SPSS: Statistical Package for Social Sciences

WEDF: Women Enterprise Development Fund

WWW: World Wide Web

YEDF: Youth Enterprise Development Fund

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The significant positive contribution of *Small* and *Medium Enterprises* (SMEs) to the economies of both developed and developing countries has attracted a lot of attention internationally - in academic, political and socio-economic field of study (Asiedu, as cited by Uwonda, Okello, N., & Okello, N. G, 2013). The field of financing of SMEs is a widely studied topic among scholars and other development agencies. Adequate funding and proper loan scheduling remains one of the biggest challenges for the SMEs sector in Kenya (Kabiru, 2002). This affects the achievement of *Vision* 2030 and *Millennium Development Goal* as SMEs are noted as crucial catalyst for achieving the Vision 2030 (Mwewa, 2013).

SMEs often face some constraints in accessing loans from financial institutions, such as lack of adequate collateral, lack of good financial records, convincing bank statements, short repayment period, and credit history. Information asymmetry makes it difficult to determine the best financial institution offering relatively less expensive loans and friendly conditions.

This study assumed *Microfinance* as the main source of financing for SMEs in Kanduyi constituency, Bungoma County. Microfinance is the provision of financial, micro insurance, training and capacity building, networking and marketing, and socio-economic services to the active economically poor entrepreneurs. Microfinance services include credit aspect, savings component, micro-insurance services, training and capacity building, networking of entrepreneurs, and marketing of innovative products (Ledgerwood, 1999).

1.1.1 The Concept of Loan, Loan Repayment Frequency and Default

According to Dhikhary (2006), a loan is a written or oral agreement for a temporary transfer of property in cash form from its owner (the lender) to a borrower who promises to return it according to agreed terms. Loan repayment is the act of the borrower to return partially or wholly the principal amount advanced to him or her plus a certain percentage of interest loaded on the principal amount in accordance with the predetermined terms in the loan contract. Interest on loan is the cost of funds paid by the borrower to the lender of funds.

Interest rate in this study refers to the nominal rate that is the actual rate of interest charged by the financier and paid by the borrower. The nominal rate consists of the real rate of interest, the risk premium, and the inflation premium. Loan repayment can be scheduled on weekly, monthly or quarterly basis for SMEs. According to Milgo (2013), lending is a risky business because borrowers can either repay their loans or choose to default.

Okurut and Kinyondo (2009) found out that business experience, training time and sanctions have positive and significant effects on loan repayment performance, while transaction costs and group size have negative and significant effects. Milgo (2013) found out that joint liability has a strong positive effect on loan repayment. She concluded that training of borrowers resulted in higher loan repayment rate and less default than those MFIs that do not offer training.

Murray (2011) defines a loan default as failure by the borrower to make required payments or failure to comply with the terms of the loan. Korankye (2014) in a study analyzing causes and control of loan default in microfinance in Ghana found out that high interest rate, inadequate loan sizes, poor appraisal, lack of monitoring and

improper client selection causes default. Berger and De Young (1995) identified inadequacy of collateral security, unrealistic terms and schedule of repayment as some of the causes of default.

Field and Pande (2008) reported that access to future loans is the main incentive for clients to avoid default. Korankye (2014) identified training before and after disbursement, reasonable interest rate, monitoring of clients, and proper loan appraisal as key to controlling default. Nguta and Huka (2010) found out that there is a relationship between the type of business, age of business, business profits and loan repayment default.

1.1.2 The Concept of Cash Flow

Cash flow is defined as the movement of cash into or out of an SME. For a health, financial status an SME's cash inflows should be more than cash outflows at any given time. Net working capital is the difference between the SME's current assets and the SME's current liabilities. According to Mugo (2014), working capital refers to a firm's short-term assets or current assets necessary for the day-to-day smooth running of the firm.

The cash flow of SMEs can be affected by overcapitalization and overtrading. Overcapitalization occurs where the SME has excessive stocks, debtors, and cash balance and very few creditors. Overcapitalization lowers rate of return on investments for SMEs. Overtrading occurs when an SME does much volume of trade too quickly with little long-term capital. Uwonda et. al. (2013), state that cash flow management is concerned with cash payment, collection of management and liquidity management that involves acquisition and disposal of assets in SMEs.

1.1.3 Effect of Frequency of Loan Repayment on SMEs' Cash Flows

SMEs are considered as seedbeds for the growth of new firms and important machinery for poverty alleviation through wealth and job creation, income generation and innovation drivers (Uwonda et. al. 2013). Inadequate cash flow management is the main reason for failure of many SMEs (Uwonda et. al. 2013). Adequate management of cash flow by SMEs is therefore key for the survival of SMEs in any developing economy.

Wang (2013) showed that microfinance loans have a positive significant effect on the level of profit reported by SMEs financed by MFIs. Wang however, notes that the amount of loan advanced to an SME is inversely proportional to profitability. Quainoo (2011) in a study done in Ghana on the impact of loans on SMEs reported that majority of SMEs acknowledge positive contributions of loans towards increasing their returns and sale thus placing them in the competitive arena. Quainoo states that if a firm incurs a major drop in income, employing more debt in the capital structure can be detrimental.

1.1.4 Context of the Study

In Kenya, an enterprise is defined as an undertaking or a business concern whether formal or informal engaged in production of goods or provision of services. Small Enterprises are defined as those enterprises that employ between 10 and 50 employees and whose annual turnover ranges between 500,000 and 5million shillings. Micro enterprise is defined as those enterprises that employ up to ten employees and whose annual turnover does not exceed 500,000 shillings (Micro and Small Enterprises Act, 2012).

The definition differs from one country to another depending on the level of economic development of the specific country (Mwewa, 2013). SMEs can be categorized based on the size of turnover, number of employees, level of operation, type of ownership and management involved (Ackah & Vuvor, 2011). The number of employees is usually lower in developing countries as compared to developed countries.

SMEs play a key role in the development of national economies in both developed and emerging economies (Ackah & Vuvor, 2011). The SME sector is the main driving force behind job creation, poverty reduction, wealth creation, income distribution and reduction in income disparities in a country (Ifeakachukwu & Olasunkanmi, 2013). SMEs create employment opportunities complementing the public sector (Mutuku, 2010). The current constitution recognizes SMEs as important sector for the Kenyan economy. The newly enacted Micro and Small Enterprises Act 2012 (MSE Act, 2012) provides a new window of opportunity for SMEs to explore their full potential.

SMEs in Kanduyi constituency are spread across all sectors of the economy, which includes, wholesale and retail trade, building and construction, transport and communication, agriculture and forestry, and education. SMEs in Kanduyi are regarded as the force behind the growth of economic development. The SMEs in Kanduyi constituency just like other parts of Kenya faces challenges in exploiting their full potential in achieving financial sustainability and creation of employment opportunities

1.2 Research Problem

It is generally accepted that providing SMEs with financial services and non-financial services, positively influences growth of SMEs (Cooper, 2012). Provision of

affordable loans, business skills, micro-insurance, water and sanitary facilities, and market linkages is a successful poverty reduction and achievement of Millennium Development Goals. The economy of any country is dependent on the success of SMEs that creates employment opportunities, creates demand for the goods produced and supply necessary inputs (Mutuku, 2010).

Some scholars have argued that microfinance loans affect positively the growth of SMEs in terms of profitability, expansion, competitive advantage and entrepreneurial skills (Cooper, 2012; Mutuku 2010; Nguta & Huka, 2013). The issue of most SMEs funded by MFIs defaulting despite the installments being broken down in smaller weekly amounts has raised concern in the sector. This is experienced mainly towards the end of loan repayment term (Morduch, 1999).

Despite the high potential of SMEs in Kanduyi to contribute towards socio-economic development of the Kanduyi constituency, they continue to face challenges inhibiting their economic growth. This scenario seems to suggest that traditional provision of finances by MFIs may not be sufficient and effective panacea to all problems facing SMEs.

Most of the empirical studies that have been done in the field of SMEs and Micro financing by other scholars have focused on MFIs at the expense of SMEs. For instance, Kirera (2009) did a study on factors that influence loan default rate in MFIs. Kanyiri (2009) studied the factors inhibiting innovations in financial intermediaries for SMEs in Kenya. Waweru (2011) studied the relationship between microfinance and financial performance of SMEs. Maingi (2011) studied impact of microfinance on poverty alleviation in Kakamega County, Kenya. Mutua (2011) studied the impact of

microfinance services on women empowerment. Njama (2013) studied effects of venture capital on the growth of SMEs in Kenya.

According to National Micro and Small Enterprise Baseline Survey report (1999), 11,360 businesses were closed between 1995and 1999. The highest number of respondents, 37.2% gave shortage of operating funds as the reason for closure of their enterprises. This revelation that SMEs are closed because of inadequate cash flow of running the business led to my research problem. In my Literature review, I have not come across a research that has been done locally to establish the effect of loan repayment on the cash flows of SMEs.

Based on the above discussion this study sought to investigate the effect of loan repayment on the SMEs cash flows in Kanduyi constituency in Bungoma County. The study targeted to interview a sample of 80 SMEs in Kanduyi constituency. There was no other study done on the effect of loan repayment on the cash flow of SMEs in Kanduyi constituency. This understanding will be of value to policy formulation and program implementation to enhance positive relationship between microfinance and SMEs financing. This study therefore sought to bridge the knowledge gap indentified above.

1.3 General Objective of the Study

The purpose of this study was to carry out an investigation on the effect of loan repayment frequency on the cash flows of SMEs in Kanduyi constituency of Bungoma County in Kenya.

1.3.1 Specific Objectives

The study was guided by the following specific objectives:

i. To establish how the loan amount affects the SMEs' cash flows in Kanduyi constituency, Bungoma County.

ii. To investigate how the age of business affects the business cash flows of SMEs in Kanduyi constituency, Bungoma County.

iii. To determine how frequency of loan repayment affects the business cash flows of SMEs in Kanduyi constituency, Bungoma County.

1.3.2 Research Question

The study was guided by the below research questions:

i. How does the loan amount affect the SMEs' cash flows in Kanduyi constituency, Bungoma County?

iv. How does the age of business affect the business cash flows of SMEs in Kanduyi constituency, Bungoma County?

ii. What are the effects of loan repayment frequency on the business cash flows of SMEs in Kanduyi constituency, Bungoma County?

1.4 Value of the Study

This study contributes to the building of body of knowledge, and helps fill the existing gap in knowledge. The findings provide SMEs in determining frequency of loan repayment that is favorable to the business growth. It provides insights on the factors leading to default to the management of MFIs. It offers insights on good loan design features for the department of Research and Development in financial institutions. The study forms basis for future researchers in the area of Microfinance. The study gives recommendations on the areas that need improvement and innovation to serve SMEs better.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

Literature review is the critical look at the already available research literature relevant to this study. This chapter sought to find out what other researchers have done in the area of SMEs financing, loan repayment and effects on SMEs' cash flow management, and causes of default.

2.2 Theoretical Literature Review

This section reviewed theories that guided the study. It consists of the theories governing the financing options and methodologies of lending by microfinance institutions. The section reviewed the Pecking Order theory of financing, Agency theory and Group lending approach as theories that guided this study.

2.2.1 The Pecking Order Theory of Financing

The pecking order theory of financing states that companies have a preferred hierarchy for financing decisions and maximize value by systematically choosing to finance new investments using the 'cheapest available' source of funds (Myers, 1984). Under the pecking order theory developed in 1984 by Myers (1984) and Myers & Majluf (1984) states that there is a strict ordering or hierarchy of sources of funds for firms. It states that firms will prefer retained earnings to any other source of finance and then choose debt and lastly equity (Njama, 2013).

The pecking order theory of financing argues that adverse selection issues in raising funds from different sources overlook other considerations in the *Trade-off* model resulting in a hierarchy of funds (Mmbaya, 2013). The Trade-off theory assumes that

there are benefits to leverage within a capital structure until the optimal level is reached (Waweru, 2014).

Enterprises will use internal sources of funds first then debt and after exhausting such options, they will resort to using new equity finance (Njama, 2013). Firms have more information about the credit risk facing them than the providers of funds resulting in adverse selection (Kago, 2014). According to this theory, SMEs will prefer internal sources of funds followed by debt and lastly equity finance when internal and debt sources are exhausted (Njama, 2013).

2.2.2 Agency Theory

The proponents of agency theory holds that an agency relationship arises whenever one party (normally the principal) hires another party (an agent) to perform some tasks on the behalf of the principal and delegates decision making authority to agent (Jensen & Meckling, 1976). This relationship gives rise to conflict of interest making it difficult to achieve the goals of the principal. In the context of small and medium enterprises, agency relationship may take the following forms.

Shareholders versus lenders: In this approach, the shareholders (owners) of the SMEs are the agents and lenders (providers of funds) are the principals. Lenders provide SMEs with debt capital to finance the running of the SMEs, but are not involved in the day-to-day running of the enterprises. The lenders expect the SMEs shareholders to manage the funds well by investing in only viable ventures. SMEs owners can have conflict of interest and engage in sale of assets pledged as collateral for the loans, invest in risky business that may fail and cause difficulties in loan repayment or result in default. The owners of SMEs may borrow more debt using the same assets pledged as collateral to other lenders for the new debt. SMEs can also manipulate financial statements and falsify crucial information to creditors.

To resolve this conflict between SMEs owners and funds providers several approaches may be used. The loan contract may have restrictive terms, which may be incorporated into lending agreements to ensure no disposal of assets without creditor's approval. Lenders may charge above normal interest rates to discourage further borrowing from other sources. Sometimes lenders may recall the loans at short notice when the loan funds have been diverted to other uses other than the one specified in the loan contract. Lenders may demand for the transfer of assets from SME to joint ownership between lender and the SME before drawdown.

Owners versus Subordinates: In this approach, the owners of SMEs are the principal while the subordinates are the agents. In many circumstances, the owners delegate power or authority to their subordinates in order to achieve the goals. In this relationship, due to conflict of interest subordinates may engage in activities that make attainment of wealth maximization difficult. Subordinates may exhibit lack of seriousness while performing their duties, use the firm's resources for their personal gains, and may falsify the business records in order to defraud the SMEs' owners. This conflict of interest may result in financial distress that may affect the ability of the SMEs to service the loans according to loan terms.

2.2.3 Group Lending Theory

The approach is based on the premise that social collateral is the most important security that SMEs have in absence of conventional securities like land title deeds and vehicle logbooks. In group-based approach, the MFIs use the group mechanism as a tool to minimize the risk of default. Formation of groups by SMEs owners who know each other reduces the risk of adverse selection by avoiding higher risk profiles based on the previous history (Morduch, 1999, Kago, 2014). The loan officer in charge of

the group offers training on basic business skills, group mechanisms, customer care, and loan management.

Group lending approach requires members to save regularly through a joint group account. The savings are commonly known as Loan Guarantee Fund (LGF). The LGF contributed by the individual forms part of the security when one applies for the loan. The total amount contributed by the group is jointly considered to form security for the aggregate loans advanced to group members.

The group lending methodology requires members to co-guarantee one another for repayment of the loans advanced, hence providing social security in complementary of conventional security (Okurut & Kinyondo, 2009). The loans issued to members are jointly guaranteed and future loan acquisition is based on the previous group reputation. The whole group is responsible for repayment of the outstanding loan balance of the defaulting member. The group applies peer pressure to ensure good repayment from the members (Nguta & Huka, 2013).

Ghatak and Guinnane (as cited in Okurut & Kinyondo, 2009) identified four main advantages of group lending. They assert that group based lending techniques mitigate the information asymmetry problems of determining the risk of default by borrowers. They posit that group based approach enhances productive use of loans advanced to members because of the close monitoring of each other. They argue that groups provides a form of insurance to loans advanced in case of loan default by a member and also sanction each other in case of default at a considerable low cost.

2.3 The Determinants of Cash Flows in SMEs

In this section, the determinants of cash flows in SMEs are discussed below. The determinants discussed in this section are cash collection policy, accounts receivables

management policy, age of business, accounts payable policy, cash balance policy model used by SME, and cash idle policy.

2.3.1 Cash Collection Policy

An SME's cash collection policy affects its cash flow in terms of length of time when payment is initiated by a debtor sending a cheque and the time when funds are actually available for use by the SME in the SME's bank account (Mugo, 2014). An SME can have a cash collection policy that requires the use of standing orders or direct debits for regular payments from debtors. Another approach is personal collection of cheques by messengers from customers whose accounts are due.

2.3.2 Accounts Receivables Management Policy

Accounts receivables are amounts of money owed to a firm by customers who buy on credit. The SMEs can control the accounts receivables through the establishment of good credit policy, and collection policy. The SMEs can use the five Cs of credit (Character, capacity, capital, collateral and conditions) to determine credit worthiness of prospective credit customers (Kirera, 2009). Increased cash discount has a negative effect of decreased profit margin per unit as more people take the discount and pay reduced price. Increased cash discount period has both positive and negative effects on the cash flow.

If the period is increased, more customers want to take the cash discounts thereby reducing the average accounts collection period. On the negative side customers who were taking the cash discount will be able to take cash discount and pay later thus slowing down collection period. Accounts Receivables policy affects the level of default and bad debts, sales volume and contributions margin, and accounts receivable collection expenses (Ackah & Vuvor, 2011). This in turn affects cash flows of the SMEs.

2.3.3 Age of the SME

Investments of SMEs tend to be more dependent on the cash flow during start-up period and face liquidity restrictions that diminish as the firms get older. Berger & Udell (1998) found out that older companies have better access to external financing and better terms, which means investment in working capital s less expensive.

2.3.4 Accounts Payable Policy

The accounts payable policy affects the cash flow of the business in terms of availability of funds to creditors once the payments have been dispatched by the SME. SMEs may play the float by issuing cheques that are postdated to increase time between the receipt of cheque and actual withdrawal of funds from the SME's account. Payment for services and goods on accruals also help the SMEs in retaining funds for sometime in the firm.

2.3.5 Cash Balance Model Used by the SME

The working cash balance is the amount of cash held by the SME for transaction purposes. The optimal working cash balance occurs when total costs are at a minimum. The levels of cash and marketable securities held by SMEs are determined by the motives of holding them. These motives are transaction motive, speculative motive, safety motive and precautionary motive. One approach of determining optimal working cash balance is the use the Baumol model (Baumol, 1952).

The Baumol model of cash balance has three inputs; total cash outflows over the period, transactions costs of replenishing cash balance by borrowing or selling securities and the interest rate that can be earned per year. The Baumol model assumes that the firm uses cash at a steady predictable rate, the cash outflows from operations also occurs at a steady rate and the cash net outflows also occurs at a steady rate (Mugo, 2014).

Another approach of determining the optimal working cash balance is the use of Miller-Orr model (Modiglian & Miller, 1963). This model provides for cost-efficient cash balances between determining an upper limit and the return point of cash in an SME. The Miller-Orr model is based on the assumption that receipts and disbursements are completely random. The Miller-Orr model requires the determination of an upper limit, lower limit and return point (Mugo, 2014). In setting the return point and upper limit the SME needs to consider conversion costs, daily opportunity costs of funds, and the variance of daily net cash flows.

2.3.6 Cash Idle Investment Policy

An SME may finds itself holding cash in excess of its requirements with time. This results from increase of transaction balances due to seasonal business and increase in precautionary balances needed for emergencies or profitable opportunities. An SME should have a good investment policy to guide it in investing in short-term debt instruments considering default risk, maturity period and asset marketability.

2.4 Empirical Review

This section of the study looked at both the global and local empirical literature available relevant to the study investigating the effects of loan repayment frequency on the cash flows of SMEs in Kanduyi constituency in Bungoma County. The findings of this study are compared to the earlier findings in other related studies done by other researchers.

2.4.1 Global Empirical Review

A number of studies have been done globally on the SMEs in areas such as factors affecting their growth, factors affecting SMEs access to finances, effect of devolution on SMEs growth, causes of loan default, and contribution of micro financing to poverty alleviation. For instance, Berger & De Young (1995) identified inadequacy of

collateral security, unrealistic terms and schedule of repayment as some of the causes of default. Barnes (2001) in a study to assess the impact of microfinance program in Zimbabwe found that all the respondents were able to sign their own signatures while applying for loans from MFIs.

Jain and Mansuri (2003) argue that the need to raise funds for weekly repayment makes clients take informal sector loans. They argue that MFI benefits from these informal lenders because of their effective collection methods and therefore prefers a repayment schedule that makes it more likely that a client will also take credit from moneylenders to service the loan.

Field and Pande (2008) found out that there is no significance effect of type of repayment schedule on delinquency or default. The study suggests that a more flexible schedule can significantly lower transaction costs without increasing client default. Field and Pande identified weekly collection of repayment installments as a key feature of MFI that is believed to reduce default risk in the absence of collateral and thus make lending to the poor viable. They also identified weekly collection as a key feature that increases MFI's transaction costs, thereby limiting the set of loan sizes and client types that are profitable under weekly repayment schedule. Field and Pande reported that access to future loans is the main incentive for clients to avoid default.

Murray (2011) defines a loan default as failure by the borrower to make required payments or failure to comply with the terms of the loan. Feigenberg, Field and Pande (2011) show that clients who meet weekly instead of monthly are three and half times less likely to default on their subsequent loans. They linked this to increased interactions among group members through weekly meetings that enhanced social

interactions. Sheila (2011) showed that illiteracy and inadequate skills contributes to loan default in Uganda because it inhibits business diversification.

Quainoo (2011) in a study done in Ghana on the impact of loans on SMEs reported that majority of SMEs acknowledge positive contributions of loans towards increasing their returns and sales thus placing them in the competitive arena. Quainoo states that if a firm incurs a major drop in income, employing more debt in the capital structure can be detrimental, as the firm will not be able to cover the cost interest.

Uwonda et. al. (2013) noted that SMEs are considered as seedbeds for the growth of new firms and important machinery for poverty alleviation through wealth and job creation, income generation and innovation drivers. Inadequate cash flow management was identified as the main reason for failure of many SMEs. Adequate management of cash flow by SMEs is therefore key for the survival of SMEs in any developing economy.

Wang (2013) did a study on the impact of microfinance on the development of small and medium enterprises in China, the study showed that microfinance loans has a positive significant effect on the level of profit reported by SMEs financed by MFIs. He however, notes that the amount of loan advanced to an SME is inversely proportional to profitability.

Korankye (2014) in a study analyzing causes and control of loan default in microfinance in Ghana found out that high interest rate, inadequate loan sizes, poor appraisal, lack of monitoring and improper client selection causes default. Korankye (2014) identified training before and after disbursement, reasonable interest rate, monitoring of clients, and proper loan appraisal as key to controlling default.

2.4.2 Local Empirical Review

Mutua (2011) carried out a study to determine the impact of microfinance services on women empowerment focusing on Mwingi District. Mutua found out that microfinance services empower women entrepreneurs to start businesses that enhance their income generation and acquisition of assets. The study suggested that through empowerment of women, most of their children acquired education and improved health care (Mutua, 2011). The findings in Mutua's study cannot be generalized to male entrepreneurs and hence need to carry out a research that covers both men and women entrepreneurs. Other factors could have played a role in the economic empowerment of these women entrepreneurs in Mwingi district such as additional income contributed by the male spouses, and changes in micro economic environment.

Maingi (2011) carried out a study on the impact of microfinance on poverty alleviation in Kakamega County and found out that microfinance services led to the improved financial management, increased savings, increased literacy level, and better health for the clients. Maingi also found out that microfinance services led to empowerment of beneficiaries, accumulation of wealth and created employment opportunities.

Silikhani (2012) found out that the level of education of women entrepreneurs affected the running of businesses and managing customers. She notes majority of the women entrepreneurs in Sirisia division had received secondary education therefore able to run their businesses. Silikhani also indicated that most of the respondents could not calculate interest on loans independently without being assisted by the loan officers. The level of education plays a significant role in enabling the client to determine the loan size appropriately depending on the loan installment to repay.

Njama (2013) did a study on the effect of venture capital financing on the growth of small and medium sized enterprises in Kenya. The study found out that there was a positive and significant relationship between growth of SMEs and Venture capital financing. Njama concluded venture capital financing improves credit rating, marketing and distribution networks, improves technical expertise, which in turn enhances growth of SMEs. Njama recommended SMEs' need to recognize the potential advantages of seeking external equity finance from corporate sources.

Mwewa (2013) did a study on the effects of microfinance services on the growth of SMEs in Machakos County. A quantitative descriptive design was used to study eight types of business categories in Machakos County. In her study, she sampled 100 businesses from a population list of 5311 in Machakos County. She used a moderate regression analysis to analyze her data. Mwewa found out that there is a positive relationship between microfinance services such as micro credit and training and the SMEs growth in Machakos County. She identified micro insurance a service affecting growth of SMEs negatively. Since the study focused on MFI services on the growth of SMEs in Machakos County, there is, need to carry out another study in other Counties.

Mugo (2014) argues that optimal working capital differs from one company to another. This is due to difference in operations in different industries. Mugo argues that a company can adopt any of three distinct working capital policies. These are an aggressive policy, moderate policy and a conservative policy. Mugo concludes that an effective management of working capital has a positive effect on the liquidity of firms.

2.5 Summary of Literature Review

From the literature reviewed above MFIs generally, adopt weekly repayment schedules when providing loan facilities to clients to reduce transaction cost and enhance good repayment behavior. Few MFIs allow their clients to choose the frequency of payment based on their cash flow. There exist a cash flow disconnect when SMEs are required to pay on weekly basis yet the businesses performs better only during specific weeks of the month.

Weekly repayment funds are sometimes raised through sale of productive assets, under stocking, or reduced consumption and this affects the growth of business. A monthly repayment schedule could assist MFI clients manage their cash flows better, repay their loans on time and have sufficient working capital. Weekly repayment schedule may limit the amount of loan a client can borrow, increases workload for the loan officers, and may lead to exit of lucrative clients. Client retention may be affected by the frequency of repayment because clients could leave the program to join another MFI offering monthly repayment schedule.

Majority of studies done in Kenya in the field of SMEs' financing have focused on MFIs with few studies being done to evaluate the impact of loan on SMEs financial performance. No study had been done in Kanduyi Constituency on the effect of weekly loan repayment on the business cash flow of SMEs. There was need to investigate the effect of loan repayment on the cash flows of SMEs in Kanduyi constituency, Bungoma County.

2.6 Conceptual Framework

A business research model is a pictorial representation of a system that is constructed to study some aspects of that system or the system as a whole (Cooper & Schindler,

2006). The conceptual framework in figure 2.1 shows the relationship between the independent variables, the intervening variables and the dependent variable.

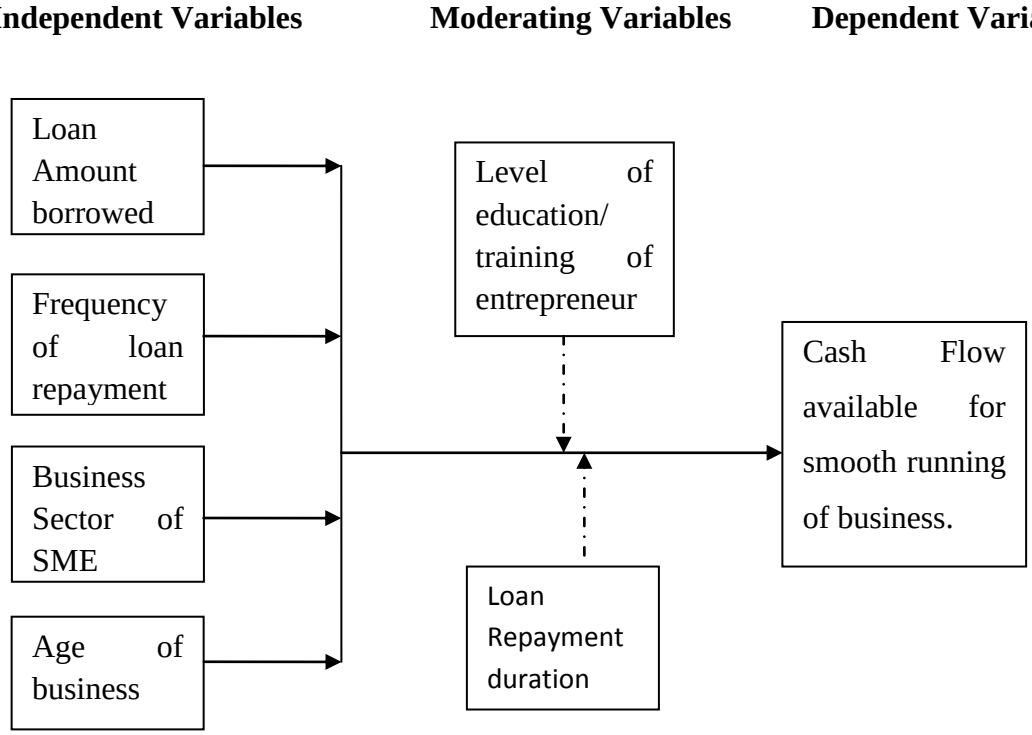

Figure 2.1 Conceptual Framework

2.7 Research Hypothesis

The research study was guided by the following hypothesis in finding out the effect of loan repayment frequency on the SMEs cash flow.

H1: The loan repayment frequency positively affects business cash flows of SMEs.

H2: Loan amount positively affects business cash flows of SMEs.

H3: The business cash flow of SMEs is positively related to the business sector.

H4: The age of business positively affects the business cash flow of SMEs.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents the methodology of the study. It gives the information on specific research design that was adopted, population target for the study, sample selection method used, data collection method, and data analysis procedures.

3.2 Research Design

The research design is the blue print for the collection, measurement, and analysis of data for fulfilling objectives and answering the questions (Cooper & Schindler, 2006). The research design that was adopted in this study is the quantitative survey design. A survey is a measurement process used to collect information from participants and recording their responses for analysis. Survey design is a report of study that requires the collection of quantifiable information from sample to allow generalization to whole population. Quantitative survey design was chosen because the study was concerned with finding out who, what, where, when, and how much. It is also quick to administer, relatively inexpensive to carry out, efficient, achieves greater accuracy of results than other methods and flexible.

3.3 Target Population

A population refers to the entire group of elements about which we wish to make an inference (Cooper & Schindler, 2006). The target population of the study consisted of SMEs operating businesses such as retail shops, chemists, carpentry, hair salons, groceries, cereal stores, hotels, and animal selling in Kanduyi constituency, Bungoma County.

3.4 Sample Design & Sample Size

This study used simple random sampling technique to obtain a sample size of 80 respondents. The study used simple random sampling because it is simple, less expensive and convenient. Simple random technique was chosen because each population element has a known and equal chance of selection.

3.5 Data Collection Method

The study used a questionnaire to collect primary data for analysis. The questions included both closed and open-ended questions. The questionnaire was divided into three sections (A, B & C). Section **'A**', contained general information questions that dealt with issues touching on gender, age, dependants and level of education. Section **'B',** contained credit related investigative questions. Section **'C',** contained business related investigative questions. In this study, reliability was achieved through pretesting of the questionnaire on 20 randomly selected SMEs.

The collection instrument adequately covered the topics that were considered as the relevant dimensions of the study to enable it have good content validity. The content validity of a measuring instrument is the extent to which it provides adequate coverage of the investigative questions guiding the study (Cooper & Schindler, 2006).

3.6 Data Validity and Reliability

In this study, the content validity and the criterion validity were considered. The questionnaire adequately covered the topics that were considered as the relevant dimensions of the study to enable it have good content validity. A careful approach was used to come up with a relevant criterion that predicted the scores. A questionnaire used was free from bias to enable each respondent to score well on the

criterion. The questionnaire used was stable and reproducible in another study. The information specified by the criterion being sought is available.

In this study, reliability was achieved through pretesting of the questionnaire on 20 randomly selected SMEs. The retest was repeated after two weeks to ascertain reliability of the questionnaire. Reliability of an instrument is the degree to which a measure is able to supply consistent results (Cooper & Schindler, 2006). Reliability is concerned with estimates of the degree to which measurement is free of random or unstable error. This ensured that the questionnaire is a valid measurement tool to measure what it was supposed to measure or predict accurately the effect of frequency of loan repayment on the business cash flow of SMEs in Kanduyi constituency, Bungoma County.

3.7 Data Analysis Methods

The study employed regression analysis on data collected in the study investigating the relationship between the frequency of loan repayment and business cash flow of small and medium enterprises. The Statistical Package for Social Sciences (SPSS) was used to analyze data. Data is represented in frequency tables and analysis results presented in tables.

The regression model used in the study was in the form below.

$$Y= \beta_0+\beta_1X_1+\beta_2X_2+\beta_3X_3+\beta_4X_4+e$$

Where:

Y= Weekly cash flow of the business

X_1= frequency of loan repayment (weekly or monthly)

X_2= Current loan amount being serviced

X_3= Business sector

X_4= Age of business

β_1- β_4 = Coefficients of the independent variables.

β_0= Constant

e=Error term, takes care of other factors that affect cash flow not in the model.

3.8 Test of Significance

The study used 95% confidence level and 5% significance level to test the relationship between loan repayment frequency and cash flow of SMEs. This was in line with requirements for research projects using quantitative survey designs. The coefficients of determination, R^2 and the Adjusted R^2 were used to determine how much variation in the dependent variable is explained by variation in the independent variables.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSION

4.1 Introduction

This chapter presents the data analysis, results and discussion of the study findings. The objective of the study was to find out the effect of loan repayment frequency on the cash flows of SMEs in Kanduyi constituency. The study used a questionnaire to gather the data needed to achieve the research objectives. The research used regression analysis to analyze data collected in which weekly cash flow was the dependent variable. For the purposes of summarizing the relationship among the variables, the data is presented in the form of tables showing frequencies and percentages.

4.2 Questionnaire Return Rate

Table 4.1 Response on Questionnaire Return Rate

Name of Ward	**Number distributed**	**Frequency of returned**	**Correctly filled**	**Valid percent**	**Cumulative percent**
Bukembe East	10	8	7	15	**15**
Bukembe West	10	7	6	13	**28**
East Sang'alo	8	5	4	9	**37**
Khalaba	10	8	6	13	**50**
Marakaru/Tuuti	9	7	4	9	**59**
Musikoma	8	6	5	11	**70**
Township	15	10	8	17	**87**
West Sang'alo	10	7	6	13	**100**
TOTAL	**80**	**58**	**46**	**100**	

Source: Author, 2015

Self-administered 80 questionnaires were distributed to the randomly selected SMEs during the study. Table 4.1 contains the rate at which the questionnaires were returned from various wards.

Fifty-eight of the dispatched questionnaires were collected from 58 respondents. According to the questionnaires distributed, 73% was realized giving 58 questionnaires. Out of the 58 questionnaires returned, 79% was correctly filled, giving 46 questionnaires. According to Mugenda and Mugenda (2003), a response rate of 50% is adequate for analysis and research findings reported. Mugenda and Mugenda showed that a response rate of 60% is good, 70% and over is excellent for descriptive studies. In this study, 57.5% was realized; this was above the recommended percentage by Mugenda and Mugenda. The study therefore considered 46 questionnaires as 100% of the sampled population.

The valid number of questionnaires considered was 46 in total. The distribution of correctly filled questionnaires per ward: Bukembe East, 15%, Bukembe West, 13%, East Bukusu, 9%, Khalaba 13%, Marakaru/Tuuti, 9%, Musikoma, 11%, Township, 17% and West Sang'alo, 13%. Twenty-two questionnaires, constituting 23% of the respondents, were not returned in good time. Therefore, those returned in good time were considered adequate for analysis.

4.3 General Characteristics of Respondents

This section contains presentation of findings arising from the data analysis that investigated general characteristics of the respondents of SMEs in Kanduyi constituency, Bungoma County. The findings are tabulated in the tables

4.3.1 Gender of Respondents

This study sort to determine gender distributions of respondents represented in the study.

Table 4.2 Gender Distribution of Respondents

Gender	Frequency	Percent	Cumulative Percent
Female	26	56.52	**56.52**
Male	20	43.48	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

According to table 4.2 above, majority of respondents, 56.52% were female and 43.48% were male respondents. The majority of SMEs that use loans from microfinance are women because of being preferred by the MFIs.

4.3.2 Age of Respondents

This section presents the findings relating to the age of the SMEs' owners. Age of the respondent was a general characteristic sought to determine demographic distribution. The results are shown in table 4.3 below.

Table 4.3 Age Distribution of Respondents

Age bracket	Frequency	Percent	Cumulative Percent
18-35	27	58.70	**58.70**
36-55	16	34.78	**93.48**
56 and Above	3	6.52	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

According to table 4.3, the study revealed the following: Majority of the respondents, 58.70%, was aged between 18 and 35 years old. This means that majority of those operating SMEs and used microfinance loans were youths. Those between 36 and 55 years old formed 34.78%, while those above 55 years old only formed 6.52% of the respondents.

4.3.3 Number of Dependants

This section presents the findings relating to number of dependants of the SMEs' owners. Number of dependants of the respondent was a general characteristic sought to determine if it had any relationship on SMEs' cash flows. The results are shown in table 4.4 below.

Table 4.4 Dependants Distribution of Respondents

Number of dependants	Frequency	Percent	Cumulative Percent
0	4	8.70	**8.70**
1-5	33	71.74	**80.44**
6-10	9	19.56	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

From table 4.4 above, majority of respondents, 71.74% had dependants between one and five dependants. Respondents who had between six to 10, formed 19.56%, and those who had no dependants were only 8.7%.

4.3.4 Education Levels Distribution of Respondents

Table 4.5 Education Levels Distribution of Respondents

Level of education	Frequency	Percent	Cumulative Percent
Primary	7	15.22	**15.22**
Secondary	26	56.52	**71.74**
College	13	28.26	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

According to table 4.5 above, the study revealed that majority of respondents, 56.52% had attained secondary education, and 28.26% had attained college education, while 15.22 had only attained primary education. Considering the results shown in Table 4.3 where 58.70% were aged between 18 and 35 years old, 15.22% with only primary education indicates that there is a high dropout rate in Kanduyi constituency.

4.4 Regression Analysis

In order to establish the relationship between independent and depended variables, a multiple regression was carried out. The analysis of data was done using the Statistical Package for Social Sciences (SPSS). The findings are presented in the succeeding sections.

4.4.1 Model Summary

The model summary was used to summarize the relationship between cash flow and frequency of loan repayment by determining the correlation and coefficients of determination of the regression model as shown below in table 4.6.

Table 4.6 Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.405[a]	.164	.076	3691.69

a. Predictors: (Constant); frequency of loan repayment, current loan amount, business sector, and age of business.

b. Depended variable: Weekly Cash flow

Results in table 4.6 indicates that the r squared for the model was 0.164, meaning that the four independent variable that were studied, explain 16.4% variance of cash flow of SMEs as represented by $R^{2.}$ This therefore means that other factors related to cash

flow of SMEs not studied in this study account for 83.6% of the variance in the dependent variable. The four variables have a weak relationship with cash flow variance.

4.4.2 Analysis of Variance

Analysis of Variance (ANOVA) is a statistical method that was used to test differences between cash flow and frequency of payment of SMEs in Kanduyi constituency. The findings are tabulated in table 4.7 below.

Table 4.7 ANOVA Test

Model		Sum of Squares	df	Mean Square	F	Sig
	Regression	101412085.187	4	25353021.297	1.860	.138[b]
1	Residual	517885821.790	38	13628574.258		
	Total	619297906.977	42			

a. Dependent Variable: Weekly Cash Flow

b. Predictors: (Constant), frequency of loan repayment, current loan amount, business sector and age of business.

From table 4.7 shown above, the F-ratio in the ANOVA table F (4, 38) is 1.860 and P is 0.138. This is greater than 0.05 significant at 95% confidence interval. This means that the four independent variables studied in this study do not significantly explain the variations in cash flow about its mean.

4.4.3 Multiple Regression Analysis

Table 4.8 Multiple Regression Analysis

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	2718.247	1367.581		1.988	.054
	current loan size	-.002	.004	-.087	-.515	.609
	how often do you make payments	2190.223	1308.912	.287	1.673	.102
	business sector	-100.024	507.985	-.030	-.197	.845
	how long have you been in the business	246.865	100.621	.432	2.453	.019

a. Dependent Variable: weekly cash flow

b. Explanatory variables: Frequency of loan repayment (X_1), Loan amount (X_2), Business sector (X_3) and Age of business (X_4).

From the regression findings, the substitution of the equation

$$Y= \beta_0+\beta_1X_1+\beta_2X_2+\beta_3X_3+\beta_4X_4+e$$

Became:

$$Y = 2718.247 - 2190.223X_1 - 0.002X_2 - 100.024X_3 + 246.865X_4$$

Where:

Y was the dependent variable representing weekly cash flow.

Independent Variables were:

X1: Frequency of loan repayment

X2: Current loan amount

X3: Business sector

X4: Age of Business

$\beta_{0:}$ 2718.247

$\beta_{1:}$ - 2190.223

β_{2}: - 0.002

$\beta_{3:}$ - 100.024

$\beta_{4:}$ 246.865

e: 3691.690

According to table 4.8 above, only age of business is significant p=0.19 (this is less than 0.05 at 95% confidence interval). This means that age of business is the only independent variable that has a statistical effect on cash flows. This could be due to the SME having loyal customers therefore contributing positively to the cash flow variation. The other explanation could be due to experience gained in the running of the business that results to good management skills. Other explanatory variables do not have a statistically significant effect on cash flows as p>0.05.

4.5 Credit Related Characteristics

This section presents the results of the study about the credit related responses collected from the SMEs. This was considered important to find out if it had any relationship with other main investigative questions.

Table 4.9 Duration of usage of MFI loans Distribution of Respondents

Duration of MFI loans usage	Frequency	Percent	Cumulative Percent
1-3 years	33	71.74	**71.74**
4-7years	9	19.57	**91.31**
Above 7	4	8.69	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

In relation to the table 4.9 above, the study revealed that majority of respondents, 71.74% had only used MFI loans to fund their business between one and three years. Those who had used MFI loans in their businesses between four to seven years formed 19.57% of the respondents. Only 8.69 had used MFI loans for a period longer than seven years. This indicates that there is a higher rate of drop out from the program.

Table 4.10 Weekly Cash Flow Distributions

Weekly cash flow (Ksh.)	Frequency	Percent	Cumulative Percent
1-1000	5	10.87	**10.87**
1001-5000	27	58.69	**69.56**
5001-10000	12	26.09	**95.65**
10001 and above	2	4.35	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

With reference to table 4.10 above, 58.69% of the respondents had a weekly cash flow of between Ksh. 1,000 and Ksh. 5,000. This was more than two times of the respondents who had between Ksh. 5,001 and Ksh. 10,000 that formed 26.09%. Respondents, who had between Ksh. 1 and Ksh. 1,000, comprised of 10.8%, while those who had 10,001 and above were 4.35%. The results show that 69.56% had cash flows between Ksh. 1 and Ksh. 5,000. This shows that majority of SMEs studied had very low amounts of cash flows. This could be due to lack of proper record keeping that resulted in estimation of weekly cash flows.

Table 4.11 Current Loan Amount Distribution

Current loan amount (Ksh.)	Frequency	Percent	Cumulative Percent
5,000-20,000	13	28.26	**28.26**
20,001-50,000	16	34.78	**63.04**
50,001-100,000	11	23.91	**86.95**
100,001 and above	6	13.05	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

According to table 4.11 above, majority of the respondents, 34.78% had borrowed between Ksh. 20,001 and Ksh. 50,000. This was closely followed by those who had borrowed between Ksh. 5,000 and Ksh. 20,000 that formed 28.26%. Those who had borrowed between Ksh. 50, 001 and Ksh. 100,000 formed 23.91%, while 13.05% had loan amount above Ksh. 100,000.

Table 4.12 Effect of Loan Installment on Cash Flow

Effect of loan Installment on cash flow	Frequency	Percent	Cumulative Percent
Yes	27	58.70	**58.70**
No	19	41.30	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

From table 4.12 above, the study revealed that 58.70% of the respondents indicated that loan installment affects cash flow of the business. The study revealed that 74% of those that indicated loan installment affects cash flow had current loans averaging above Ksh. 30,000. This means that the higher the installment amount the greater the

effect felt on cash flow. However, 41.30% indicated that the loan installment amount does not affect the cash flow of the business.

Table 4.13 Loan Repayment Duration Distribution

Period for loan repayment (Months)	Frequency	Percent	Cumulative Percent
6 – 12	37	80.43	**80.43**
18 -24	9	19.57	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

From table 4.13 above, 80.43% had loans repayable within 12 months, and only 19.57% had loan repayable beyond 12 months. Those that had been advanced loans above Ksh. 100, 000 were allowed to repay their loans within 18 months or 24 months. The study revealed that the loan repayment period was pegged on the loan size of the respondents. Those repaying loans for a longer period had on average higher weekly cash flows as compared to those repaying within a year. This could be due to reduced weekly installment because of number of weeks the respondents are given to repay the loan.

4.5.1 Frequency of Loan Repayment

This section presents the findings in relation to the frequency of loan repayment. This helped to investigate its effect on cash flows of SMEs in Kanduyi constituency, Bungoma County. The table 4.14 below shows the findings of the study.

Table 4.14 Frequency of Loan Repayment

Frequency of loan repayment	Frequency	Percent	Cumulative Percent
Weekly	26	56.52	**56.52**
Monthly	20	43.48	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

According to table 4.14 above, the study revealed that majority of respondents, 56.52% repaid their loans on weekly basis, while 43.48% repaid their loans on monthly basis.

4.5.2 Effect of Frequency of Loan Repayment on Cash Flow

Table 4.15 Statistics

N	Valid	46
	Missing	0
Mean		.65
Std. Deviation		.482

Table 4.16 Effect of Frequency of Loan Repayment on Cash Flow

Frequency affects cash flow	Frequency	Percent	Cumulative Percent
Yes	15	32.61	**32.61**
No	31	67.39	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

From table 4.16 above, the study showed that majority of the respondents, 67.39% said the frequency of loan repayment does not affect the SMEs' cash flow. Only

minority, 32.61% said that frequency of loan repayment affected their cash flows. This shows that the cash flow is not significantly affected by the frequency of loan repayment.

Table 4.17 Number of employee's distribution

Number of employees	Frequency	Percent	Cumulative Percent
1	15	32.61	**32.61**
2	18	39.13	**71.74**
3	6	13.04	**84.78**
4	4	8.70	**93.48**
6	2	4.35	**97.83**
10	1	2.17	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

From table 4.17 above, 32.61% had only one employee, 39.13% had two employees, 13.04% had three employees, 8.70% had four employees, 4.35% had six employees and only 2.17% had 10 employees.

Table 4.18 Business Sector Distribution

Business sector	Frequency	Percent	Cumulative Percent
Trading	18	39.13	**39.13**
Farming	13	28.26	**67.39**
Manufacturing	5	10.87	**78.26**
Service	10	21.74	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

In relation to table 4.18 above, majority of respondents, 39.13% were trading business sector, 28.26% practicing farming business, 10.87% were in manufacturing and 21.74% were doing service business.

Table 4.19 Age of Business

Age of business (Years)	Frequency	Percent	Cumulative Percent
1-5	28	60.87	**60.87**
6-10	10	21.74	**82.61**
More than 10	8	17.39	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

From table 4.19 above, the study revealed that majority of respondents, 60.87% had operated business between one and five years, 21.74% had operated business between 6 and 10 years. Those that had operated business for more than 10 years formed 17.39% of the respondents.

Table 4.20 Training Related to Business

Training related to business	Frequency	Percent	Cumulative Percent
Yes	29	63.04	**63.04**
No	17	36.96	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

The above table 4.20 revealed that 63.04% of the respondents were running businesses that were related to the respondents training. However, 36.96% were operating businesses that they had no any training related to the business.

Table 4.21 Effect of Loan on Business

Effect of loan on business	Frequency	Percent	Cumulative Percent
Increased stock	20	43.48	**43.48**
Decreased stock	1	2.17	**45.65**
Increased profits	22	47.83	**93.48**
Decreased profits	2	4.35	**97.83**
No change observed	1	2.17	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

In table 4.21 above, majority of the respondents, 47.83% reported increased profits after funding the business with the loans. This was closely followed by 43.48% that reported increase in stock after funding business with the loan obtained. Those that reported decreased stock and no change observed formed 2.17% each.

Table 4.22 Challenges faced by SMEs

Challenges faced	Frequency	Percent	Cumulative Percent
Lack of enough cash to run the business	16	34.78	**34.78**
Lack of market for produce	11	23.91	**58.69**
Lack of good management skills	9	19.57	**78.26**
Lack of collateral	10	21.74	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

With reference to table 4.22 above, the study revealed that majority respondents, 34.78% identified lack of enough cash to run the business as their main challenge. This was followed by 23.91% that identified lack of market for products as their main challenge. Those that identified lack of collateral as their main challenge formed 21.7 4%, while those that identified lack good management skills were 19.57%.

Table 4.23 Multiple Borrowing from Different MFIs Distribution

Borrowing from different MFIs at the same time	**Frequency**	**Percent**	**Cumulative Percent**
Yes	9	19.57	**19.57**
No	37	80.43	**100**
TOTAL	**46**	**100**	

Source: Author, 2015

According to table 4.23 above, only 19.57% of respondents affirmed borrowing from multiple MFIs at the same time. Majority, 80.43% indicated they do not borrow from different MFIs at the same time. All that indicated they borrow from different MFIs at the same time argued that multiple borrowing increases funds available to run the business and therefore responded positively to the question investigating whether multiple borrowing affects SME's cash flow.

4.6 Discussion of Research Findings

From the research findings, 56.52% of respondents paid their loans on weekly basis. This was in agreement with the findings of a research done by Jain and Mansuri, (2003) that showed most MFIs use weekly payment schedules to collect loans from clients. Paying on weekly basis had both positive and negative effects according to respondents. On the positive side, the research showed that it allows respondents to

pay in four small equal installments every week. This reduced the probability of clients falling into arrears as compared to paying a single installment at the end of the month. Majority of respondents, 75.25 % paying on weekly basis indicated they have never fallen into arrears.

On the negative side, research findings showed that respondents who pay on weekly basis reported lower amounts of weekly cash flows as compared to the respondents paying on monthly basis. Weekly loan repayment reduces the amount invested in stock that may lead to low stocking of products by the SMEs. Quainoo (2011) noted that 25% SMEs sampled in Ghana, indicated inadequate re-investment in business as negative impact of loan repayment on SMEs' performance. Quainoo showed that 18% chose prioritizing inflows to settle debt as a disadvantage of taking a business loan (second highest after High cost of capital). Paying on monthly basis enables the SMEs to turn over cash more times through stock than weekly payment.

SMEs do not have constant income streams throughout the four weeks of the month, this leads to cash flow disconnect. The study showed that clients would give priority to paying of loans rather than stocking when faced with cash constraints, just to avoid falling into arrears. This concurred with results of Jain and Mansuri (2003) that showed MFI clients would resort to informal borrowing moneylenders to finance regular repayment installments. The research findings showed that respondents paying on monthly basis had on average higher weekly cash flows than those paying on weekly basis. Respondents however, said the options for frequency of loan repayment are determined by the MFIs.

The research findings show that 67.39% of respondents indicated that loan repayment frequency did not affect SMEs cash flows. Only 32.61% showed that loan repayment

frequency affects cash flows. Respondents that showed that frequency of loan repayment affects cash flows argued that weekly loan repayment reduces amount of cash invested in the business stock. They attributed low profits to weekly loan repayments. This was in line with the findings of Quainoo (2011) that noted that 25% SMEs sampled in Ghana, indicated inadequate re-investment in business as negative impact of loan repayment on SMEs' performance.

The research has showed that cumulatively, 91.31% realized either increase in stock or increase in profits. Cumulatively only 8.69% had, either realized no effect or decreased stock. These findings are in line with the findings of Quainoo (2011) that showed 85.19% had increased profit in a study done Ghana examining the impact of loans on SMEs in Ghana.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Introduction

The objective of the study was to find out the effect of loan repayment frequency on the cash flows of SMEs in Kanduyi constituency, Bungoma County in Kenya. The study issued questionnaires to 80 SMEs in Kanduyi constituency. Questionnaires that were returned were 58, this formed 73% of distributed questionnaires. Respondents that correctly filled and returned questionnaires were 46. This formed 57.5% of distributed questionnaires. This number was considered adequate for analysis and reporting of the study findings.

5.2 Summary of findings

The study was guided by the following specific objectives:

i. To establish how the loan amount affects the SMEs' cash flows in Kanduyi constituency, Bungoma County.
ii. To investigate how the age of business affects the business cash flows of SMEs in Kanduyi constituency, Bungoma County.
iii. To determine how frequency of loan repayment affects the business cash flows of SMEs in Kanduyi constituency, Bungoma County.

The study aimed at establishing the effect of frequency of loan repayment on the weekly cash flows of the SMEs in Kanduyi constituency. The research findings indicated that there is no significant effect between the loan repayment frequency and the cash flows of SMEs. From table 4.19 presented earlier, 67.39% of respondents showed that frequency of loan repayment does not affect the business cash flows. Only 32.61% of respondents showed that cash flow is affected by frequency of loan

repayment. This may be a result of poor record keeping, making it difficult to ascertain changes.

The study found out that the current loan amount in the in the study does not significantly affect the cash flows of SMEs. These results could be due to the investment of loan amounts in the SMEs' business stock hence generating more income to the SMEs but the same increase in income used to service the loan. This cancels out the effect making the current loan amount insignificant in relation to SMEs' cash flow. Another possible reason could be the longer period allowed for repayment of loans above Ksh. 100, 000 neutralizes the effect of increased loan installment amount.

The study found out that there is no significant relationship between the type of business sector and cash flow of SMEs. However, the study showed that those in the Farming Sector had on average the highest level of cash flows compared to other sectors. The second highest average cash flow was reported in the Trading Sector. Manufacturing sector had the lowest level of average cash flows of the SMEs. This could be due to those in the farming sector selling their produce from their farms thus minimizing expenses. The study also revealed that majority of SMEs is in trading sector, forming 39.13%. This was followed by farming sector that formed 28.26% of respondents.

This study revealed that the age of business has a significant relationship with the cash flows of the SMEs. The SMEs that had been in operation for more than three years had on average higher cash flows as compared to those that had been operation for less than three years. This therefore shows that with increased number of years of operation there is a positive increase in cash flow. This could be due to increased

number of loyal customers buying from established SMEs. The experience also in managing business cash flow could have contributed to the increased amounts of cash flow as reported by the study.

The study found out that 19.57% of SMEs borrow from multiple financial institutions at the same time. It also noted that 66.67% of respondents who had multiple borrowing agreed that the loan installment affects cash flows. Though the respondents indicated that multiple borrowing increased working capital and leading quick expansion, 80.43% when probed said that multiple borrowing affects business cash flows and could easily lead to default. This should be a warning sign to MFIs that have not started using the service of Credit Reference Bureaus. Multi-borrowing loans that are repaid on weekly basis could be affecting the growth of these SMEs as evidenced with low amounts weekly cash flows observed in the study.

5.3 Conclusion

In conclusion, the study revealed that the frequency of loan repayment, loan amount and business sector has insignificant relationship with the variations of cash flows of SMEs. Frequency of loan repayment was found to have no significant effect on the cash flows empirically. This shows that SMEs can choose to repay loans on weekly or monthly basis. The loan amount was also statistically found not to be having any significant effect on the cash flows of SMEs. The type of business operated by the SME was found to have insignificant effect on the cash flows f SMEs. However, the age of business significant effect on the cash flows of SMEs.

5.4 Recommendation

The study recommends that MFIs adopt weekly loan repayment schedules that allow the SMEs borrow and pay every week to ease burden of loan installment. The study

recommends that SMEs should be tasked by financial institutions to keep proper records of their transactions. SMEs should have proper record keeping to enable them monitor their cash flows on a daily basis. Majority of the SMEs could not provide very accurate information of the cash flow movements due to lack of proper record keeping. Cash flows are the basis of loan approvals and therefore if the records are scanty, it could lead to MFIs giving bad loans hence strangling the SMEs with unaffordable loan repayments.

Based on the findings in this study, the study recommends that there is need to address the high rate of pupils dropping out school at primary level as revealed by the study. Quite a significant 15.22% of respondents had no secondary education despites the fact that 58.70% were aged below 35 years. This undermines the attainment of vision 2030 and the Millennium Development Goals (MDGs).

The study recommends that MFIs adopt the use Credit Reference Bureau services in advancing the loans to curb the loan delinquencies occasioned by multiple borrowing that starves the businesses to the point where it can no longer service all debts. Training of SMEs' owners should put emphasis on the effects of servicing many debts at the same time on the cash flow.

5.5 Limitations of the Study

The main constraint of the study was the time to complete the study. This study therefore sought to study a few SMEs in Kanduyi constituency. Time could not allow a greater number of SMEs to be sampled as this could not have been possible within the short period. Cost was also a limiting factor, in that studying a large number of samples could not have been feasible. The other limitation of this study was the unwillingness of respondents to participate in the study. The sampled SMEs claimed

to be busy and not able to find time to respond to questionnaires. This was minimized by leaving the questionnaires behind to be filled and collected later by those who said were busy when approached.

Some clients based on their perceptions of MFIs were unwilling to participate after they were randomly picked as samples from the population. This was overcome by convincing the participants to believe the experience would be pleasant and satisfying, and have the participants think answering the questions was an important and worthwhile use of their time. The other limitation of the study was the unwillingness of some respondents to give the correct information desired in the study. Some respondents did not give information sort in the questionnaires leaving the questions blank. This resulted in reduction of the number sampled because only those questionnaires that were correctly filled were considered as samples.

5.6 Suggestions for Further Studies

Future research should be carried out based on the above limitations that this study faced while carrying out the research. There is need to replicate the study in future with higher number of samples. A study should be done on the effect of lack of management skills on the performance of SMEs.

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APPENDIX 1: AUTHORIZATION LETTER

UNIVERSITY OF NAIROBI
SCHOOL OF BUSINESS
MBA PROGRAMME

Telephone: 020-2059162
Telegrams: "Varsity", Nairobi
Telex: 22095 Varsity

P.O. Box 30197
Nairobi, Kenya

DATE 12/08/2015

TO WHOM IT MAY CONCERN

The bearer of this letter NOAH SIMIYU KALUSIAKA WAFULA

Registration No. D.61/8973/2006

is a bona fide continuing student in the Master of Business Administration (MBA) degree program in this University.

He/she is required to submit as part of his/her coursework assessment a research project report on a management problem. We would like the students to do their projects on real problems affecting firms in Kenya. We would, therefore, appreciate your assistance to enable him/her collect data in your organization.

The results of the report will be used solely for academic purposes and a copy of the same will be availed to the interviewed organizations on request.

Thank you.

PATRICK NYABUTO
MBA ADMINISTRATOR
SCHOOL OF BUSINESS

UNIVERSITY OF NAIROBI
SCHOOL OF BUSINESS
12 AUG 2015
P.O. Box 30197 – 00100, NAIROBI

APPENDIX 2: COVER LETTER

University of Nairobi,

School of Business,

P.O BOX 30197-00100

NAIROBI, KENYA

13th AUGUST 2015

Dear Sir/Madam,

RE: MBA RESEARCH PROJECT STUDY

I am Noah Simiyu Walusaka Wafula, a Master of Business Administration (MBA) student at the University of Nairobi, registration number D61/8973/2006. I am conducting a study to investigate the effect of loan repayment frequency on the business cash flows of SMEs in Kanduyi constituency, Bungoma County.

For the success of this study, you have been randomly chosen to participate in this study. Attached is a questionnaire for collection of information. Please provide the information by selection of the most appropriate answer by putting a mark against and put remarks where there are spaces for you to give your comments.

The purpose of this study is to fulfill requirements for my MBA in Accounting at the University of Nairobi. Any information obtained will be treated with utmost confidence, and will only be used solely for the purpose of this study.

Thank you for taking time to participate in this noble exercise.

Yours faithfully,

Noah Simiyu Walusaka Wafula,

D61/8973/2006

Email: noahwalusaka@yahoo.com

APPENDIX 3: QUESTIONNAIRE

A QUESTIONNAIRE INVESTIGATING THE EEFECT OF LOAN REPAYMENT FREQUENCY ON THE CASH FLOWS OF SMES IN KANDUYI CONSTITUENCY OF KENYA

You have been randomly chosen to participate in this study. Please provide the information by selecting the most appropriate answer by putting a mark against it and remarks where there are spaces for you to give your comments. Any information obtained will be treated with utmost confidence, and will only be used for the purpose of this study.

Section A: General Information

1. What is your gender? a) Male ☐ b) Female ☐
2. What is your age? (in years)_____
3. How many dependants do you have?_____
4. What is your highest level of education attained?
   a) Primary ☐ b) Secondary ☐ c) Post secondary ☐

Section B: Credit Related Information

5. How long have you been using the microfinance? (in years)_____
6. Did you receive training from the microfinance institution before being advanced first loan? a) Yes ☐ b) No ☐
7. How often do you meet for group meetings? a) Weekly ☐ b) Monthly ☐
8. What is the weekly cash flow of the business? (The difference between money coming in and money going out of the business). KSH_____
9. What is your loan cycle?
   a) First loan ☐ b) Second loan ☐ c) Third loan ☐ d) Above third cycle ☐

10. How much is your current loan size? (Ksh.)_____

11. Does the loan installment amount affect your business cash flow?

a) Yes ☐ b) No ☐

12. After how long are you expected to repay the loan? (Months/years)_____

13. What security did you pledge or give for the loan?

a) Household items ☐ b) Motor cycle/Vehicle logbook ☐

c) Title Deed ☐ d) Animals ☐

14. How often do you make or submit payments for your loan to microfinance institution? (weekly/monthly)_____

15. How many times have you fallen into arrears?

a) Once ☐ b) Twice ☐ c)Thrice ☐ d) Many times ☐ e) Not at all ☐

16. A. Does the frequency of loan repayment affect your business cash flow?

a) Yes ☐ b) No ☐

B. If yes please explain how the business cash flow is affected

_____

17. How would you rate your ability to read and understand a loan application form? a) Poor ☐ b) Fair ☐ c) Good ☐ d) Very Good ☐

18. Are you able to calculate the loan interest and installment payable?

a) Yes ☐ b) No ☐

19. Do you borrow loans from different Microfinance Institutions or Banks at the same time? a) Yes ☐ b) No ☐

20. A. If yes in Question 19 above, does it affect in any way the availability of funds to run the business? (Skip if you answered No above)

a) Yes ☐ b) No ☐

(B). Explain your answer in part A above

Section C: Business Related

21. How many employees do you have in your business?_____

22. What is the sector of your business funded by Microfinance Institution?

    a) Trading (e.g. General retail shop, cereals, hardware)

    b) Farming (e.g. Dairy, Poultry farming)

    c) Manufacturing and processing (e.g. yogurt production)

    d) Service (e.g. Kinyozi, salon, transport)

23. How long have you been in this business? (months/years)_____

24. A. Do you have any training related to your business? a) Yes ☐ b) No ☐

    B. If yes above, how does it help in business management?

    _____

    C. If no, above how does it affect your business management?

    _____

25. Do you mainly sell on cash basis or credit basis? A) Cash ☐ b) Credit ☐

26. How has your business changed since you obtained the loan?

    a) Stock has increased ☐ b) Stock has decreased ☐

    c) Profit has increased ☐ d) Profit has decreased ☐

    e) Nothing has changed ☐

27. What is the main problem that you experience in your business?

    a. Lack of enough cash to run the business ☐

    b. Lack of market for products ☐

    c. Lack of good business management skills ☐

    d. Lack of collateral/security ☐

28. Would you recommend to your friends to join microfinance groups?

    a. Yes ☐ b. No ☐

If No above please give reasons

_____

_____

_____

_____

Thank you for participating in this study.