

**THE EXTENT OF ADOPTION OF FINANCIAL ACCOUNTING
STANDARDS AND ITS EFFECT ON FINANCIAL PERFORMANCE
OF SMALL AND MEDIUM ENTERPRISES IN NAIROBI COUNTY,
KENYA**

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DECLARATION

This research project is my own original work and has never been presented to any other university or institution of higher learning for academic award

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DEDICATION

To Adi Nur Elmi, the man who made me what I am today. Thank you for being there for me always.

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ABBREVIATIONS

GAAP- Generally Accepted Accounting Principles

IAS - International Accounting Standards

ICPAK - Institute of Certified Public Accountants

IFRS - International Financial Reporting Standards

KRA - Kenya Revenue Authority

MDGs- Millennium Development Goals

SACCOs - Savings and Credit Cooperative Societies

SMEs - Small and Medium Enterprises

SSEs - Small Scale Enterprises

ABSTRACT

The study sought to assess the extent of adoption of financial accounting standards and its effect on SMEs financial performance in Nairobi County. This study used a descriptive design and the number of professional SMEs that formed the population of study was 868. The sample size was therefore 86 SMEs, which were sampled using stratified and simple random sampling. The study adopted a questionnaire to collect data and the Cronbach alpha coefficient was employed for testing of reliability. Collated data was analyzed by the use of both descriptive and inferential statistics with the help of statistical package for social studies version 21. The relationship between adoption of financial accounting standards and its effects of financial performance of SMEs was established through a multiple regression model. The results of this study have established an insignificant relationship between adoption of financial accounting standards and financial performance of SMEs. The results also indicate that there is an insignificant negative relationship between adoption of accounting standards and quality of financial reports while size of the SME had an insignificant positive effect on SMEs financial performance. The study concludes that adoption of financial accounting standards has insignificant influence on SMEs financial performance and its adoption negatively affects SMEs financial performance due to additional cost associated with training and consultancy services to meet the laid down standards and procedures associated with international accounting standards. The study also concluded that financial accounting standards enhance relevancy, reliability and improvement in accounting reports of Small and medium enterprises. Finally, the study concluded that extent of financial accounting standards adoption by SMEs in Nairobi County is low and to a little extent. The study recommended that managers and owners of SMEs should train their own staff and develop their own manpower to carry out finance and accounting tasks as this may reduce the cost impacts of financial accounting standard adoption and may improve their SMEs financial performance.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Financial accounting is among effective decision making tools of financial performance of Small and Medium Enterprises (SMEs). Financial accounting presents a methodical way of gathering and organizing information concerning various business transactions that is so crucial to management as far as effective operation of the business is concerned. In simple terms, it aid management in making proper decisions on how to operate a business. It is paramount for a business to keep proper books of accounts (Birya, 1998). Proper books accounts enable the managers of businesses to have accurate information to base their decisions on how to effectively operate a business. Most businesses especially SMEs make a wide range of decisions based on accounting information available to them. This study contends that, closure of some businesses has been due to lack of proper accounting records, hence makes it a vital issue for any business success especially achievement of its objective which in most cases is maximization of shareholders wealth through making more profits. Some studies assert that, SMEs with poor accounting systems are more likely to fail or have failed (Ofonagoro, 1983),

The quality of accounting information used by Small and Medium Enterprise (SME) is perceived to have a positive relationship with the firm's performance as far as finance is concerned as well as the firm's long time survival. A lot of attention has been directed to the significance of financial information for SMEs due to volatility that is usually

associated with their poor accounting systems (Lybaer, 1998). High financial performance reflects the firm's managers' potential to effectively and efficiently make good use of the firm's resources whether finances or assets (Naser & Mokhtar, 2004).

Despite following financial accounting standards, SMEs are still struggling with failure threats. Statistics from previous studies indicates that 3 out of 5 SMEs fail within their first initial months of its operation. Bowen (2009) asserts that to start and operate an SME include a great possibility of failure as well as success. SMEs mostly fail because they are not supposed to make any mistake on financial accounting. A simple mistake on financial accounting is likely to lead to death of an SME thus no opportunity to learn from such past mistakes. Poor management of finance has been the main cause of failure of SMEs (Longeneter et al., 2006). Bowen (2009) confirms existence of a very strong relation between training level of managers on proper keeping of books of accounts and performance of the firm.

In the view of Vision 2030, Kenya will move away from agricultural economy to industrial economy by year 2030 where SMEs will play a major role however after several technological revolutions, the SME sector has gained weight in national production but there is a gap as the SME firm financial performance has not advanced at the same speed, sometimes for lack of financial accounting skills has not matched their economic development. This study aims to conducting comprehensive research including more factors affecting SMEs financial performance. This study will focus on adoption financial accounting by SMEs and the impact financial accounting on financial performance.

1.1.1 Financial Accounting Standards

International Financial Reporting Standards (IFRS) is a reporting standard of firm's finances that has gained a great recognition all over the world and is a more consistent framework of accounting. It has become the main Generally Accepted Accounting Practice (GAAP) worldwide and thus widely used.

In the year 1998, Institute of Certified Public Accountants of Kenya (ICPAK) embraced international accounting standards for financial reporting in Kenya and required all the companies incorporated in Kenya to prepare their financial statements in accordance with IAS and such financial statements to be audited in accordance with international standards on auditing. Since 1999, auditor's opinion in the financial statement states that these statements are to be prepared and be presented in accordance with IAS. One may however ask whether in reality the financial statements fully comply with the requirements of IAS (Chege, 2005).

1.1.2 Financial Performance

Financial performance is an indication of how a firm can utilize its current assets from the firm's main business mode and operations and generate revenues for the business (Baxter, 2007). Financial performance also shows how health a firm is in financial terms over a certain period. Financial performances is applied in weighing up firms from same industry or in comparison to other firms in different industries or sectors with intention to come up with a decision on how to improve on the prevailing situation or sustain a desirable position within the market (Berger, Oliver & Pua, 2007).

Financial performance measurements are essential for accountability and strategic planning. Performance measurement deals with a measure on how well firms are managed in relation to set targets and the generate values to the firm's stakeholders (Illmer, 2011). There exists different ways that SMEs can adapt to in order to improve their financial performance, though all these systems adopted should be considered in aggregation. Items like revenue, income from operations or firm's cash flows, total sale units and so on.

Measures of financial performance includes key business statistics like new orders received by the business, efficiency in cash collection, Return on Investment (ROI), Return on Asset (ROA) that measure the firm's performance in some important areas. Key performance indicators show that, the progress (or lack of it) towards achieving the objectives of the firm is by monitoring those activities that (if not properly done) are likely cause heavy losses or an outright failure of the firm's business. SME are expected to be profitable and there are some checks on profitability such as whether a firm has made a loss or profit on its ordinary or normal activities and by how much this year's loss or profit is higher or lower than the previous year's loss or profit. Profitability measures involves sales margin which is turnover less the cost of sales, earnings per share (EPS) is refers to the profit attributed to each ordinary (equity) share (Illmer, 2011).

1.1.3 Effect of Financial Accounting Standards on the Financial Performance

Adoption of financial accounting standards is critical in determination of the financial performance of any business entity. Studies have shown that, the initial step of accounting process in any business starts with record keeping. It also involves classification, analyzing and reporting of business financial information. It involves a couple of items or activities such as organizing and receipts tracking, checks cancellation and so on. Bookkeepers record all transactions in a chronologically way. The information recorded is usually critical for preparation financial statements. Keeping of records is imperative for any profitable firm or the business. Furthermore, many studies that have been done indicates that proper keeping of records and a good business management is crucial for success any firm or business (King & McGrath 1998). In addition, Butler (2009) affirms that any firm or business that doesn't keep accurate and complete records of all their transaction is doomed to fail.

According to Ademola (2012), adoption of record keeping is vital not to individuals alone but also to firms in general since it is a business life wire. According to Maseko and Manyani, (2011), many if not all SMEs owners use accounting records or information to measure the business financial performance. This study reflects they necessity of adoption of financial accounting as the back-bone of financial performance of any SME that is - failure to integrate financial systems of accounting leads to collapse of a financial sector of a business entity.

SME's financial performance can be directed towards both internal and external factors. That is the size of the firm to the environment in which the SME operates in. Endowment of financial resource of an SME plays a great role in determination of the financial performance of an SME. Failure of many entities to meet their financial obligations or demands when they fall due is an outcome of market imperfections that are mostly triggered due to information asymmetry. That is between insiders (entities managers) and external investors or entities. IFRS for SMEs (2009) outlines the basic concepts and principles for preparation and presentation of external financial statements for SMEs. An SME need to identify those principles it considers more vital and applicable to its own needs and the environment it operates in.

1.1.4 SMEs in Nairobi County

In Kenya, an SME is defined as an entity that is not generally accountable to the general public; does not publish its financial statements for general external users and whose equity and debt instruments are not publically traded or even over the counter market or traded in a foreign stock exchange (ICPAK, 2009). SMEs are important to economic growth in Kenya since they play a vital role though they were previously ignored as an important sector to economy before the ILO report on the World Employment program report that laid down great emphasis on possibility of SMEs creating more employment opportunities and generating of income to many Kenyan people. Because of this approach, the SME sector has been given considerable recognition by the Kenya government and the Kenyan people at large.

Most Nairobi's SMEs have adopted financial accounting due to its materiality and tremendous capacity to solve the issue of financial performance hindrances. It has

become common knowledge among managers of SMEs on the in Nairobi on the significance of financial accounting on financial performance of their enterprises. Embracing financial accounting by Nairobi SMEs can be a major headway that SMEs can integrate in their small enterprises in their quest to develop in order to gain full cycle of their corporates in finance and profit sector, this is from the fact that accounting practices enable the firm's managers to access to relevant information that is crucial for meaningful decision making (Alleyne & Marshall, 2011). Uyar (2010) noted that cost accounting was driven by the decrease in profits, increase in operational costs and economic crises since cost accounting was perceived as an important tool to help firms in handling such decrease in profits and increase in operational costs.

Therefore, in any business entity profit is the life-blood of any business entity. As such, the accounting concepts and principles adopted should be able to capture all the required accounting information and report on the same, since such information is relevant to aid in decision making of the firm by the firm's managers. Accounting information ensures reliability in measurement of the firm's financial performance and aid in determination of possible loopholes.

1.2 Research Problem

Financial accounting standards are key to proper book keeping for any business. IFRSs should be fully complied with and more accounting standards that can improve business performance should be adopted. There is also need for increased training so that both the management and the general employees understand the importance of adoption of IFRSs to small and medium enterprises. Absence of financial accounting among most SMEs is

a notable challenge. That is, most SMEs do not keep accurate and complete accounting records or information due to lack of accounting knowledge and these results to failure in financial performance. Best part of the emerging economies and developing economies as well as the developed economies are characterized with small and medium enterprises (Madawaki, 2011). Despite this inclusion of SMEs trade has been impeded by various factors both within their internal and external environment the major one being the absence of financial accounting thus need for its adoption.

In Kenyan context, the challenge with SME is that, most SMEs rarely employ the services of a qualified accountant who may assist in proper keeping of records of accounts. According to Okwena, Okioma and Onsongo (2010), the study affirms that book keeping practice is not adequate for SMEs in Kisii town and this is likely to affect the financial performance of SMEs negatively.

Various studies particularly in Kenya have been carried out on the topic. Kipsang (2006) researched on factors that influence utilization of accounting services by SMEs in Kenya, an indication that there is a serious need for the firm's managers to emphasize on the use of qualified accountants so as to handle some of the challenges for example the competition facing most SMEs. The managers of these SMEs should emphasize on a proper and good book keeping of financial records. This can easily be done if SMEs employ the services of qualified accountants. This has the potential of enhancing growth of SMEs however the study failed to focus on the extent of adoption of financial accounting and its effect on SMEs financial performance.

Kwamboka (2010) carried out a survey on behavioral factors which influence choice of financial accounting methods by SMEs. The survey focused on Ruiru municipality. It was established that financial literacy and educational level significantly influences choice of a financing method to be used by an SME. However, the survey did not address some of the reasons for adoption of a financial accounting standards and its impact on financial performance by Kenyan SMEs.

Aritho (2010) carried out a survey on application of strategic management accounting in firms. The survey focused on Kenya Literature Bureau (KLB). It was found out that adoption of strategic management level of accounting practices were very low. Further, the survey did not consider SMEs adoption of financial accounting and their performance. There is limited information available on the extent of adoption of financial accounting and its effect on SME's financial performance. Hence, the study seeks to address existing research gap. The study will address the following question, to what extent does adoption of financial accounting standards affect SMEs financial performance in Nairobi County.

1.3 Objectives of the Study

To assess the extent of adopting financial accounting standards and its effect on SMEs financial performance in Nairobi County.

1.4 Value of the Study

Proper financial accounting enables the government to realize the total income a particular enterprise generates for easy tax collection. Therefore, this study will benefit

the Kenya revenue authority (KRA) to execute its mandate of tax collection through proper accounting systems being put in place by the SMEs as taxpayers.

The results of the study will contribute to developing small businesses, by generating strategies that will encourage the use of financial accounting by SMEs. Furthermore, the study will inform the small entrepreneurs and make them aware of the need to organize the accounting records properly so as to realize its positive effects on financial performance of SMEs. With proper accounting records, SMEs will be able meet the obligation of providing information that may be required by the government, creditors and even the lenders of finance to SMEs for example the banks usually requires SMEs to provide some financial statements before the bank can offer a loan to an SMEs.

Interested parties like finance providers to SMEs will be able to come up with programs to advice and train SMEs in financial accounting practices in order to turn planning into a cause of success rather than for failure.

The study will greatly contribute to researchers and academicians by adding some value to the body of knowledge especially on SMEs financial accounting and financial performance and form a good basis for future and further research.

1.5 Summary of Introduction

In a nutshell, in the introduction, we have discussed the conceptual and contextual framework in detail which includes – a detailed explanation of financial accounting standards, financial performance and SME's in Nairobi County. The research problem has evidenced several research gaps which posed the research question to assess effects of adopting financial accounting standards on SMEs financial performance in Nairobi

County. Lastly, the research will benefit – SME's, the government, financial providers and researchers.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

In this chapter, we examine what previous researchers have done on the study of the of SMEs adoption of the financial accounting standards. Various scholars, authors, international organizations and researchers have developed various perspectives on the importance of Small and medium enterprises adopting financial accounting standards. The chapter aims at reviewing and examining what these institutions and individuals who have developed in terms of aspects and knowledge on importance of SMEs financial accounting standards. This chapter will involve the review of theoretical literature and empirical literature on the impact of application of the financial accounts for the small and medium enterprises.

2.2 Theoretical Literature Review

2.2.1 Balanced Scorecard

Balanced Scorecard (BSC) theory was developed by Kaplan & Norton (1992) with its new concept of organizing financial and non-financial performance measurements. The scorecard is a strategic performance management system which allows firms to manage and evaluate the implementation of their strategy (Mulu, 2010). It translates an organization's strategic plan to order marching for an organization on day to day basis (Kaplan and Norton, 2001). It aligns the organization's mission and vision to requirements of customers and dily work (Rohm, 2008).

It is possible to manage and evaluate business strategy through the use of the balanced scorecard. It also aids in communicating progress to all employees and building organizational capacity through the establishment of operation competence improvements required, (Pearce & Robinson, 2000). It provides a framework which is very comprehensive that is able to translate a firm's strategy and vision into a set of coherent performance measures, and assists managers or planners determine what ought to be done and measured (Kaplan and Norton, 2007).

According to this theory, most SMEs management control systems and operations revolve around financial performance and financial measure. This has little relevance to SME progress as far as achieving its long- term strategic objectives is concerned. Thus, most SMEs put on short-term financial measures that leave a gap between strategy development and its subsequent implementation. SMEs that use the balanced scorecard do not necessarily need to rely more on the short- term financial measures as the only indicator of performance of the SMEs. The scorecard enable the SMEs to introduce four different management processes that are able to contribute whether separately and or in combination to link the long- term strategic objectives with the short- term actions (Kaplan & Norton, 2008).

Kaplan and Norton (2008) describe the four processes as; firstly, translating vision and strategy. This is meant to help in building consensus around the firm's vision and strategy. It also helps members of the firm to recognize the long-term drivers of success described in vision and mission statements. Second process is all about communicating and linking. This is meant to enable the firm's managers to communicate the firm', strategy either up and or down in the firm. This ensures that everyone within the firm at

any level understand the long- term strategy of the firm. The third process which according to Kaplan and Norton business is planning. The process is meant to enable firms to integrate the business plans with its financial plans. The balanced scorecard measures set goals are the basis for resource allocation and setting of priorities. The fourth process of balanced scorecard is to learn and grow. It involves identification of infrastructure that must be established by the firm so as to build a long- term growth and improvement of the firm. Kaplan and Norton observed that, firms may not be able to meet their long- term set goals for their customers and internal processes by the use of current technologies and capabilities.

2.2.2 Contingency Theory

According to Donaldson (1995a, 2001), Contingency theory provide the most important framework for organizational design study. Contingency theory affirms that most effective organizational features or rather characteristics are those that are able to fit contingency variables. For example, in organizational set up, specialization yields a high performance when it fits the organizations size, that is, contingency variable level. Therefore, high performance results from a low level of specialization in a small size organization, whereas for large size organization, high performance results from a high level of specialization.

This theory gives an overview of organization's effectiveness and performance and it states that there exists no optimal method to systematize an organization and its structure (Fiedler, 1964). This theory affirms that the appropriate organization structure is the one

that suits or fits a given operating contingency, like the technology (Woodward, 1965; Perrow, 1970).

All SMEs face quite number of constraints ranging from both internal and external as well as from some environmental incidents that may be specific to an organization that have ability to effect in distinctive levels of environmental uncertainties. There exists no one optimum organization design for every firm since every firm has its own different organizational culture and its own perspective as far as risk is concerned. Structural contingency theory affirms that SMEs in fit yields a high performance than those SMEs in a misfit. However, all these fits yield high performance level.

2.2.3 Resource Based View Theory

According to the resource-based view theory, a firm's competitiveness lies in a firm's ability to well apply a bundle of its valuable resources both tangible and or intangible at its disposal (Mwailu & Mercer, 1983, Wernerfelt, 1984). The theory affirms that a firm's short-run competitive advantage can be transformed to a sustained competitive advantage only if the firm's available are heterogeneous in nature and not perfectly mobile (Peteraf, 1993). This therefore translates to available of valuable resources that are neither substitutable without great effort nor perfectly imitable (Barney, 1991). Incase where these conditions can hold, a bundle of resources can effectively sustain above average returns of the firm.

According to Barney (2007), it was developed to explain how organizations achieve sustainable competitive advantage. He however criticized its lack of clear treatment of the environmental dynamics that guide development of new resources. He came up with

an additional framework (VRIO-value, rarity, inimitability and organization support) to explain the required characteristics of a competitive strategy that can contribute to competitive advantages of firms.

This theory focuses more on idiosyncratic, costly-to-copy resources of the firm, and whose exploitation may give a competitive advantage to a firm. The major assumptions of this theory are resource heterogeneity, which assumes that firms are bundles of products and services with firms possessing different bundles of resources, and resource immobility, which assumes that some resources are either costly to imitate or either inelastic in supply (Barney, 2007). These resources can either be tangible or intangible and they include capabilities, competencies, firm's assets, organization processes, knowledge, information, knowledge that are under the firm's control and can enable a firm to implement strategies that are designed to enhance the firm's effectiveness and efficiency (Pearce & Robinson, 1997; Barney, 2007)

A firm's resources are categorized into either financial, physical, human or organization capital. These resources or internal attributes of firms have been referred to as the core competencies or core capabilities of firms that give them a competitive advantage. To achieve this, the resources must be valuable, rare, costly-to-implement imitability and applied by organized systems of a firm to realize their full potential. The resource-based view and VRIO (value, rarity, imitability, and organization) framework can be used by firms individual to see whether the firm will gain competitive advantage and how such competitive advantage can be sustained. Peteraf (1993) outlined four resources characteristics that can lead to sustainable competitive advantage namely, heterogeneity, ex- post limits to competition, ex- ante limits to competition and mobility imperfection

which have implications on the inelastic supply of such resources (Barney, 2007; Teece, 2010). The resource based view is useful in informing about risks as well as benefits of diversification strategies.

This theory has several limitations namely, unforeseen environmental upheavals or drastic turbulence, managerial influence that is limited, and data challenges based on intra-organization resources. However, it complements other analyses such as Porters five-force model, the generic strategies and opportunity analysis (Barney, 2007; Peteraf, 1993; Porter, 1998).

2.3 Determinants of Financial Performance in SMEs

Financial performance is key to any SME to ensure that the going concern goal is achieved. Various determinants of financial performance have been put across including – accounting skills, quality of financial reports, size of business and external factors.

2.3.1 Accounting Skills

Accounting skills are wide variety of skill that involve record keeping, attention directing, financial performance and reporting skills that are meant to promote effective decision making, evaluation of firm's performance and reporting of business enterprise. Financial accounting skills play a critical role to financial. Accounting skills enables SMEs to make important decision on pricing of products and services issues and production of products whereas reporting skill helps in describing a method and technique on how information pertaining to the business can accurately be reported about the SMEs to its stakeholders.

Accounting skills and procedure are very crucial to any successful entrepreneur and development and growth of an SME. Most SMEs are likely to perform well financially by adopting these vital skills. Failure to adopt such skills many likely lead to financial problems hence collapse of an SME.

2.3.2 Quality of Financial Reports

Financial reports are vital tools for any business since they mainly inform the business stakeholders especially the external providers of capital on how the business is operating or performing. Quality financial reports are defined as so if high standards of financial reporting are adopted and utilized to enable the proper financial performance within SMEs, as they make good use of financial reports to inform both internal and external users about the business position.

Financial ratios are also important to any business since they can be used to measure different aspects of a business more especially the growth aspect which most businesses consider it more important. This is because of a going concern where a business is expected to last for a long period of time.

2.3.3 Size of Business

Business size is measured by a number of its employees and has a positive effect on returns on assets and a significance level. The role of firm's size in explaining performance of a firm has extensively been discussed by various scholars such as Jelic (2001) and Kakani (2001) who stressed more on the role being played by scale

economies and other noted efficiencies in many large firms. On the other hand, structure- conduct performance paradigm explains importance of market concentration and profitability.

According Tarawneh (2006) market share of a firm plays a vital role in explaining the firm's performance than what the firm size can do. Amato and Amato (2004) who carried out a study in US retailing industries found reasonable evidence in support Porter's (1998) conjecture that large and small firms are able to capture niche markets, whereas middle-sized firms are somehow stuck where they are. That is at 'the middle' in the sense that they are less competitive compared to their counterparts in either end of firm size distribution. Organizational size effects have been studied by many scholars. The organizational size benefits may accrue to financial performance of an organization. Big organizations can generate a strong competitive capability as compared to rival small organizations. This is because of big organization's superior access to resources, economies of scale and greater market power (Glen et al, 2003).

2.3.4 External Factors

External factors are the determinants, which contribute to the success or failure of entrepreneurial firms or entrepreneurs 'themselves. Survival and growth of a firm and the likelihood of additional venture start-ups rely on the external environment (Colvin & Slevin, 1989). The external environment has widely been recognized as an important component contributing to a firm's performance. The personality, attitudes and motivation of the entrepreneurs are also dependent on the environment (Gartner, 1985).

In a competitive and turbulent environment, external factors are commonly accepted as the determinants of firm performance and survival. Van deVen (1993) suggested that every research in the field of entrepreneurship should take account of the external circumstances to be able to explain the entrepreneurial process in a more appropriate way. Kuratko and Hodgetts (2004) also argued that entrepreneurial decisions are primarily influenced in direct or indirect ways by external factors and consequently affect performance.

2.4 Empirical Literature Review

Mutai (2014) studied the impact of adopting international financial reporting standards on the quality of financial reporting by firms listed at Nairobi securities exchange (NSE). The study established that accounting is more driven by the economy and political forces, which follow a heightened worldwide integration of politics and markets forces. The aim of the study was to try and established the quality of financial reporting of companies who are adopting the worldwide accepted international financial reporting standards.

Kamwenji (2013) investigated effect of adopting International Financial Reporting Standards on quality of accounting information of deposit taking SACCOS in Nairobi County. The study established that as a result of adoption of IFRSs, majority of the SACCOs were transparent and honest in disclosure and financial statements presentation and that presentation of accounting information was uniform with other institutions which had adopted IFRSs. Further, the financial statements of the SACCOs were comparable with those of other institutions that have adopted IFRSs. Also adoption of

IFRSs in the SACCOs had improved the timely preparation and presentation of financial statements and related disclosures. It had improved the relevance, reliability and understandability of accounting information provided in the financial statements and related disclosures.

Odero (2014) examined the impact of accounting information system quality on financial performance of Small and Medium Enterprises in Nairobi County. The study found that most enterprises had a high linkage of financial performance as measured by the change in ROI being heavily driven by the nature of records and reports, nature of the accounting system adopted the extent of knowledge and usage of accounting information and the extent of regulation in place. In addition, the researcher recommends that development and adoption of user-friendly computerized accounting information systems for all the enterprises in the county for daily operations and reporting is very vital for SMEs. That is there is need to develop affordable, easy and user-friendly training kits to be consumed by majorly players in the SMEs bracket on accounting and financial management. This will majorly be useful in improving skills to boost proper decision-making based on factual realities by management and owners of these enterprises.

Kutsaru (2014) evaluated the accounting practices of Small and Medium Enterprises at Meikles Park in Mutare. The study established that most informal traders use single entry bookkeeping systems and most of it is paper work as few of them have no computers, most of them don't have qualified bookkeepers. Most informal traders do not produce any financial reports neither do they measure their financial performance. Findings on the growth of SMEs reveals that there is still slow and stunted growth, most

of these enterprises have existed between 1-2 years and few of them go above 5 years. The researcher recommends that the current informal business owners or employees to adopt accruals basis of accounting so as to be able to produce a complete picture of the activities of the firm.

Muinde (2013) investigated the relationship that exists between financial reporting and analysis practices and financial performance of SMEs in Kenya. The study found out that there exists a strong positive relationship between financial reporting, financial analysis, financial management and management accounting and financial performance of SMEs. There is need for management of Small and medium enterprise in Kenya to enhance their financial reporting practices, financial analysis practices financial management practices and management accounting practices as it was found that financial reporting and analysis practices affect the SMEs' financial performance.

Okwena (2011) explored effects of proper book keeping practices on financial performance of SMEs in Nairobi County. The aim of the study was to ascertain the main causes of poor financial performance among SMEs. The study established that book keeping practice was one of the challenges facing SMEs in Nairobi County although the greatest challenge affecting them in keeping proper books of accounts was little knowledge of book keeping. The study revealed that most records being prepared are usually inaccurate leading to bad decisions being made concerning the operations of SMEs in Nairobi County.

Mwangi (2011) evaluated accounting systems in small and medium enterprises in Kenya. The study established that those SMEs that extensively populate informal sector

are likely to be more profitable just like those enterprises in formal business sector. The study also noted that absence of accounting records in informal sector makes it more difficult to carry out a financial ratio analysis.

Kamyabi and Devi (2011) asserted that the degree of competition is positively and significantly associated with outsourcing the accounting functions. The finding were similar to other previous studies carried on by Chen hall (2003) which established that competition intensity is positively associated with employment of formal controls, Guilding & McManus (2002) found out that the degree of competition is closely related to accounting usage of the client.

Akande (2011) studied impact of accounting skills on the performance of an entrepreneur for the success of an SME in Nigeria. The study established that most SME entrepreneurs did not see the importance of preparing financial statements. They argued that preparation of financial statements is just a waste of time since they were not under any obligation to prepare such statements. Neither were such financial statements a control tool since they were the sole stakeholders of their businesses. This may be incorrect since other stakeholders may as well exist such as the banks, creditors and so on depending on the type of the business an entrepreneur is operating.

Ismaila (2011) explored financial measures that most Small and Medium Enterprises in Pretoria employ in measuring of their financial performance. The study established that SMEs in manufacturing sector employed financial ratios as a measure of their financial performance, though to a very low extent. The study concluded that in measuring the performance of any firm, financial measure alone cannot give a realistic and a true

performance picture of a firm in a more convincing way since there exists a number of non- financial performance matters and measures that play a great role in an overall performance of a firm.

Katwei (2009) investigated the constraints that small- scale enterprises face when accessing formal financing. The study established that education levels, poor recording keeping and general awareness of formal financing products was a hindrance towards accessing formal finance. Lack of collateral and ability to pay also proved a challenge to accessing formal finance.

Muchiti (2009) explored the risk management strategies adopted by commercial banks while lending to SMEs. The author concluded that banks used effective credit policies based on the 5 C s of lending. Specifically, the banks managed lending through ensure that loans were covered by adequate security. The banks also effectively enforced the ability to 19-pay policy. To enhance sustainability of the borrower, the banks invested in training borrowers in financial literacy and book keeping. According to some banks, training lenders (for instance, SMEs) is a long-term risk management strategy.

Mosalakae (2007) explored the performance measurements of top firms in South Africa. The study established that, most of top firms in South Africa do not use the available measurement tools (that is, the bankruptcy prediction models and the financial analysis ratios) for measuring financial performance of their firms.

Nyagari (1997) explored the inflation accounting and current firm's financial reporting in Kenya, the study revealed that the firms using inflation accounting practices positively influenced their financial performance. The study further established that, all

the firms that employ good accounting practices and systems are able to generate and make good use of accounting information in their financial analysis thereby influencing their firm's overall financial performance.

2.5 Conceptual Framework

This study seeks to assess the effect of adopting financial accounting standards on financial performance of SMEs in Nairobi County. The independent variable was accounting standards, while quality of financial report and size of the SMEs formed the control variables and the dependent variable was financial performance. Figure 2.1 below shows the conceptual framework.

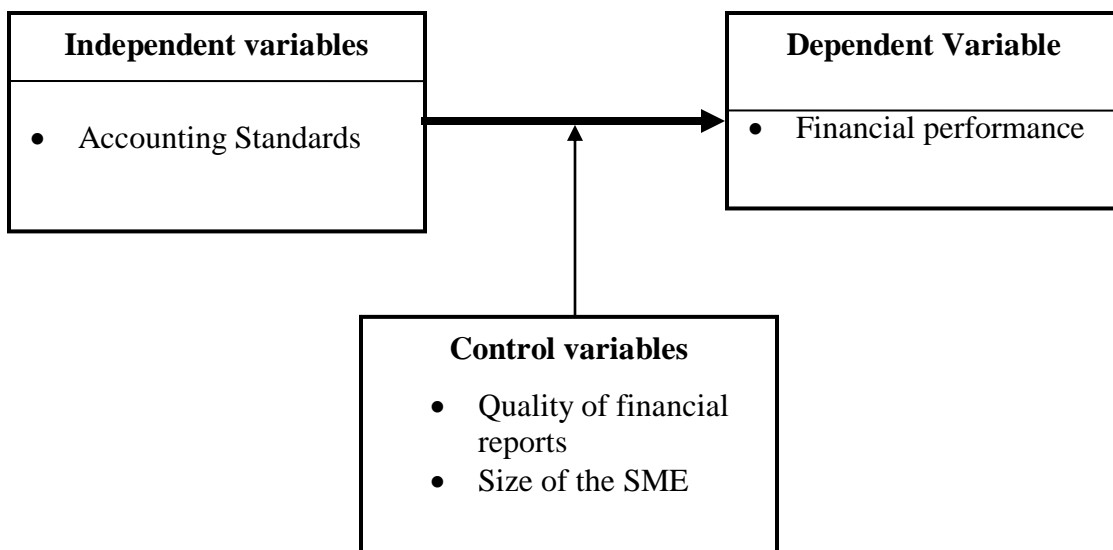


Figure 2.1 Conceptual Framework

2.5 Summary of the Literature Review

SME Financial performance can only be achieved through adoption of financial accounting. Through financial accounting Small and medium enterprises are able to realize the amounts a business owns and what the business owes to other stakeholders,

the amount of profits the business has made within a given period of time or the losses made within a given period of time, what properties the business has in its possess and the current value of such properties, the growth on profits or an increase in losses, and the capital amounts employed in a business and business financing deficit. Okwena, (2011) affirms that it will not be possible for any business to give an accurate net profit if the proper records of accounts are not kept by the business managers, similarly Williams, Susan, Haila, (2008) emphasizes on the importance of keeping proper books of records by any business entity more especially for SMEs. They argue that, in keeping proper records on a daily basis, the entrepreneur is likely to have an easy time when framing the future business plans for his or her entities. They further stresses that better business policies are usually made if the business has good records of its operations. They also argue that without proper records, it will be difficult to dispose of a business and get a true value for that business. It is therefore paramount for any business entity to keep proper records of its activities or operations.

Ademola, (2012) gives several disadvantages of informal records. Without proper formal records, an entrepreneur will not be able to recognize when there are some movements in business sales or when the costs or running the business rises to a higher level that is not acceptable. High operational costs can easily lead to collapse of a business entity if not well monitored and controlled. This monitoring and control can only be done if a business entity has proper records of its activities and operations. Corrective measures may not be undertaken at the right time when proper records are not kept. As such, the business survive may hang in a balance without proper being kept. Poor business decisions are also likely to be made without proper records. Such decision

may also be costly to a business entity. Future planning may not be possible without good records. Mwangi, (2011) urge SMEs to adopt the IFRS for SMEs which were meant to help SMEs to mostly formalize their operations and financial reporting processes, this formalize was also meant to enable SMEs access to financing and other related benefits.

Although there exist some challenges for SMEs in trying to formalize their activities and operations, the benefits of such formalization outweigh the challenges. The current study notes that the reviewed studies failed to address the extent of adoption of financial accounting by SMEs and its influence on SMEs financial performance in Kenya fail to use accountant's services. This study therefore seeks to establish whether adoption of financial accounting standards has any crucial impact on SMEs financial performances in Nairobi County, Kenya.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter focuses on the research design, population of the study, sample design, data collection and techniques of analysis.

3.2 Research Design

The study used a descriptive design. Descriptive research involves a survey and fact-finding enquiries. The main purpose of descriptive research is to describe the state of affairs as it currently exists (Mugenda & Mugenda, 2003). According to Kothari (2004), descriptive research aims at identifying and recording a phenomenon, processor system and may be conducted using surveys.

3.3 Population of the Study

Kumar (2005) defines population as a set of all kind of units of analysis in a problem area. That is, the specific problematic area that the study intends or need to address. Population included the entire professional registered SMEs in the SME Directory 2015. The number of professional SMEs that formed the population of study was 868. The characteristics of the target population are as indicated in the table in appendices.

3.4 Sample

According to Cooper and Schidler (2011), a sample is a selected subset within entire population that reflects or represents the features or characteristics of that population. According to Mugenda & Mugenda (2003), a sample size of 10% or more is sufficient

for a survey study. The study used a sample size of 86 SMEs, which were sampled using stratified and simple random sampling. Stratified sampling was used to group SME's into different strata or categories while simple random was employed in selection of respondents from each stratum.

3.5 Data Collection

This study adopted a questionnaire in data collection. Questionnaires was dropped to the sampled owners and employees of the SMEs and picked after two days. On the other hand secondary data was collected from journals, magazines and the internet.

3.6 Validity and Reliability

Validity shows whether the instrument measures what they are designed to measure (Borg and Gall, 1989). A pilot test was done to test for validity of questionnaires. In addition, pilot test was used to correct any inefficiencies and mistakes in the instruments. Reliability ensures accuracy or the consistency of the instrument, that is, the extent to which the results remain similar over different forms of the same instruments (McMillan & Schumacher, 1993). The Cronbach alpha coefficient was employed to test for reliability of instruments. According to Mugenda & Mugenda (2003), a coefficient of 0.7 or more is a clear indication of reliability.

3.7 Data Analysis

The data collected was analysed using descriptive and inferential statistics with help of statistical package for social studies version 21. Descriptive statistics involved the use of measures of the central tendency such as mean, standard deviation and percentages. Inferential statistics was used to draw conclusions.

3.7.1 Analytical Model

The relationship between adoption of financial accounting standards and its effects of financial performance of SMEs was established through a multiple regression model of the form shown below.

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \mu$$

Where

Y – Financial performance by SME’s ROA (Dependent variable)

α - is the constant

X_1 – Accounting Standards (Independent variable)

X_2 – Quality of financial reports (Control variable)

X_3 – Size of the enterprise (Control Variable)

β_1, β_2 & β_3 - Coefficients of the regression equation

μ – Error term

3.7.2 Test of Significance

The t-test was employed to test statistical significance of independent variables, while F-test was employed to test significance of dependent variable at 5% level of significance. In addition, the coefficient of determination (R^2) was employed to explain both explained and unexplained variation of the model.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND INTERPRETATION

4.1 Introduction

This chapter presents results of the collected data and the interpretation of research findings based on the objectives of this study.

4.2 Response Rate

This study used a sample of 86 small and medium enterprises in Nairobi County but only obtained data from 69 SMEs, which represented 80.23% response rate. The 80.23% response rate was considered representative enough since it is more than 50% as recommended by Mugenda & Mugenda (2003) that a sample of more than 50% is sufficient. Table 4.1 shows the obtained results.

Table 4.1 Response Rate

	Frequency	Percent
Questionnaires responded to	69	80.2
Questionnaires responded not to	17	19.8
Total	86	100.0

Source: Research Findings

4.3 Data Reliability

The study used the Cronbach Alpha coefficient to establish the variables whose data was collected using questionnaires. Table 4.2 shows the results obtained

Table 4.2 Reliability Analysis

Variable	Cronbach's Alpha	N of Items
Accounting Standards	.746	4
Quality of financial reports	.721	4
Overall	.763	8

Source: Research Findings

Table 4.2 shows that accounting standards and quality of financial reports yield a Cronbach alpha coefficient of 0.746 and 0.721 respectively. The overall Cronbach alpha coefficient was 0.763, which indicates that the questionnaire was reliable since all the alpha values were above the recommended alpha value of 0.7.

4.4 Descriptive Statistics

4.4.1 Respondents Profile

This section focused on the gender of the respondents, the years the SMEs had been operation and the different lines of business of the SMEs. Table 4.3 shows the obtained results

Table 4.3 Respondents Profile

		Frequency	Percent
Gender	Male	39	56.5
	Female	30	43.5
Years in operation	Up to 1 year	10	14.5
	1-5 years	20	29.0
	6-10 years	18	26.1
	Over 11 years	21	30.4
Line of Business	ICT SMEs	13	18.8
	Human resource training SMEs	11	15.9
	Medical SMEs	10	14.5
	Educational SMEs	11	15.9
	Insurance SMEs	10	14.5
	Finance/forex bureaus	14	20.3

Source: Research Findings

The results on table 4.3 show that 56.5% of respondents were male whereas 43.5 were female respondents. Results also show that most of the SMEs had been in operation for more than 1 year. The results also show that data was obtained from different SMEs like

ICT SMEs, human resource training SMEs, Medical SMEs, Educational, and Insurance and Forex/financial services SMEs.

4.4.2 Accounting Standards

This section examined various statements on accounting standards. Table 4.4 shows results that were obtained.

Table 4.4 Accounting Standards

	N	Mean	Std. Deviation
Is financial accounting standards necessary	69	3.72	1.211
Adoption of financial accounting standards affect financial performance	69	3.64	1.124
Accounting skills and quality of financial reports affect financial performance	69	3.71	1.099
Size of business and external factors influence financial performance	69	3.77	1.126

Source: Research findings

The results on table 4.4 show that the highest mean value is 3.77 followed by 3.72, 3.71 and the lowest mean value is 3.64. All the scale value on the scale value of 3 which indicates that the respondents neither agree or disagree that financial accounting standards necessary, adoption of financial accounting standards affect financial performance, accounting skills and quality of financial reports affect financial performance and size of business and external factors influence financial performance of SMEs. This result indicates that the respondents are indifferent on whether accounting standards influence the SMEs financial performance in Nairobi County, Kenya.

4.4.3 Quality of Accounting Reports

4.4.3.1 Preparation and Maintenance of books of Accounts

This was aimed at establishing the parties who are involved in the preparation and maintenance of SMEs books of accounts. Table 4.5 shows obtained results.

Table 4.5 Preparation and Maintenance of books of Accounts

	Frequency	Percent
Owner	11	15.9
Manager	19	27.5
Full Time Accounting Officer	13	18.8
Consultant	26	37.7
Total	69	100.0

Source: Research Findings

Table 4.5 shows that most SMEs (37.7%) use consultants or external parties to prepare and maintain their books of accounts whereas 27.5%, 18.8% and 15.9% of the SMEs statements are prepared by managers, full time accounting officers and the owners respectively. This finding shows that SMEs rely on consultants to prepare and maintain their books of account.

4.4.3.2 Accounting Records and Reports

This sought to establish the various accounting reports and records maintained and prepared by SMEs. Tables 4.6 shows the results that were obtained from the study.

Table 4.6 Accounting Records and Reports

	Frequency	Percent
Management Accounts Reports	34	49.3
Financial Accounts	32	46.4
None	3	4.3
Total	69	100.0

Source: Research Findings

The result on table 4.6 shows that 49.3% maintain management accounts reports for internal use.

On the other hand, 46.4% indicated the maintained financial accounts to establish the financial performance of their enterprises while 4.3% did not maintained any accounting reports.

4.4.3.4 Usage Level of Accounting Information and Statements

This aimed at determining the usage level of various accounting information and statements by SMEs. Table 4.7 results that were obtained from the study.

Table 4.7 Usage level of accounting Information

	N	Mean	Std. Deviation
Cash flow Projections/budgeting	69	2.14	1.517
Financial statements (income statement, Balance sheet etc)	69	2.09	1.551
Ratio Analysis	69	2.10	1.554
Product/Service costing	69	2.99	1.586

Source: Research Findings

Table 4.7 shows that the highest mean value was 2.99 followed by 2.14, 2.10 and 2.09, which corresponds to the scale value of 2 hence an indication that SMEs rarely use cash flow projections/budgeting, financial statements, ration analysis and service or products costing.

4.5 Correlation Analysis

Correlation analysis was undertaken to establish correlation between the variables of the research. Table 4.8 results that were obtained from the study

Table 4.8 Correlation Analysis

		ROA
ROA	Pearson Correlation	1
Accounting Standards	Pearson Correlation	-.087
	Sig. (2-tailed)	.476
Quality of financial reports	Pearson Correlation	-.053
	Sig. (2-tailed)	.663
Size	Pearson Correlation	.145
	Sig. (2-tailed)	.234

Table 4.8 shows that there is a negative and insignificant correlation between SMEs financial performance measured using ROA and accounting standards and also the quality of financial reports. The study also shows that size has an insignificant positive correlation with performance of SMEs in Nairobi County, Kenya.

4.6 Regression Analysis

Regression analysis was undertaken to establish a relationship between variable of the study. The results obtained are shown by table 4.9

Table 4.9 Regression Results

Model 1: OLS, using observations 1-69

Dependent variable: ROA

	Coefficient	Std. Error	t-ratio	p-value
const	0.111883	0.413363	0.2707	0.78751
Accounting Standards	-0.0322335	0.0503829	- 0.6398	0.52457
Quality of financial reports	-0.0268166	0.0457257	- 0.5865	0.55959
Size	0.0245613	0.0236784	1.0373	0.30344
Mean dependent var	0.260460	S.D. dependent var 0.186487		
Sum squared resid	2.285663	S.E. of regression 0.187521		
R-squared	0.334890	Adjusted R-squared 0.112150		
F(3, 65)	0.556626	P-value(F) 0.45557		
Log- likelihood	19.65028	Akaike criterion 31.30057		
Schwarz criterion	22.36414	Hannan-Quinn 27.75519		

Source: Research Findings

The regression results on table 4.9 shows that adoption of accounting standards and the quality of financial reports had an insignificant negative relationship with SMEs financial performance. The results also show that size has a positive but insignificant effect on the SMEs financial performance in Nairobi County. The study also shows that R squared value is 0.33489, which indicates that the independent variables explain 33.49% of the variation in the dependent variables. The F statistics value $F(3,65)$ is also insignificant at 95% significance level since the P-value(F) $0.45557 > 0.05$ which indicates that there exists no significant relationship between the adopting financial accounting standards and SMEs financial performance.

4.7 Interpretation of the Findings

This sector presents all results on hypothesized research variables. The finding established that most of respondents neither agreed or disagreed that financial accounting standards necessary, adoption of financial accounting standards affect financial performance, accounting skills and quality of financial reports affect financial performance hence an indication that SME entrepreneurs were indifferent on the on whether accounting standards influence SMEs financial performance. The study also revealed that most SMEs use the services of consultants or external parties to prepare and maintain their books of accounts. Thus, indications that the quality of their financial statements was good to a large extent since consultants are well trained to produce such reports though it's an additional cost to SMEs which may reduce their financial performance.

The study findings also established that most SMEs rarely various accounting statements information like cash flow projections/budgeting, financial statements, ration analysis and service or products costing. The study also found an insignificant correlation between financial performance of SMEs and accounting standards, the quality of financial reports and size hence an indication that accounting standards, the quality of financial reports and size of the enterprise have no correlation with SMEs financial performance. The study further revealed that accounting standards and the quality of financial reports had an insignificant negative relationship with financial performance of SME while size has a positive but insignificant effect on SMEs financial performance in Nairobi County. This indicates that the employment of accounting standards and preparation of quality financial statements adversely affect SMEs performance.

The above findings concur with that of Kutsaru (2014) who revealed that most of the informal traders employ traditional bookkeeping systems and most of them don't have qualified bookkeepers. Kipsang (2012) also found that the usage level of accounting service by SMEs was low. Senik (2012) further established that most SMEs managers lack adequate skills and qualifications required to use accounting information to better their firms operations. Okwena (2011) also established that one of challenges facing SMEs in their operations is the ability to keep proper records and therefore in most cases, they end up preparing inaccurate financial statements hence leading bad decision making for SMEs.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

Chapter five presents the summary of findings of this research, conclusions and recommendations based on research findings, the limitations of the study and suggestion of areas which may require further consideration as far as future research is concerned.

5.2 Summary

The study explored the extent of adoption of financial accounting standards and its effect on SMEs financial performance in Nairobi County in Kenya. The dependent variable was SMEs Financial performance and the independent variable was accounting standards, while quality of financial reports and size of the SMEs formed the control variables. The study obtained data from 69 SMEs from a sample of 86 SMEs in Nairobi County, which represented 80.23% response rate. Data for the study was obtained from different SMEs like ICT SMEs, human resource training SMEs, Medical SMEs, Educational, and Insurance and Forex/financial services SMEs. The reliability of the questionnaire was adequate with an overall Cronbach alpha coefficient of 0.763 respectively.

The study findings established that most of SME owners and employees were indifferent on whether accounting standards influence the financial performance of their businesses. Additionally, the study findings also established that SMEs rely on consultants to prepare and maintain their books of account hence an indication that the quality of their

financial reports was good though it was an addition cost to them. The findings also established that SMEs mostly maintain management accounts reports for internal use and financial accounts to determine their financial performance. However, the study revealed that SMEs rarely use the accounting statements information like cash flow projections/budgeting, financial statements, ration analysis and service or products costing.

The results of correlation analysis found that financial performance of SMEs proxied using Return on assets (RoA) had an insignificant correlation with accounting standards, the quality of financial reports and size of the SME. The study of the regression results found an insignificant negative relationship between adoption of accounting standards and quality of financial reports while size of SME had an insignificant and positive effect on SMEs financial performance in Nairobi County. The study further found that accounting standards, the quality of financial reports and size only explained 33.49% of the variation in SMEs financial performance and the F test generated the P-value ($0.45557 > 0.05$) an indicates that there is an insignificant relationship between the adopting financial accounting standards and SMEs financial performance.

5.3 Conclusions

The study results have established an insignificant relationship between the adopting financial accounting standards and financial performance of SMEs. The results also indicate that there is an insignificant negative relationship between adoption of accounting standards and quality of financial reports. Based on this finding, the study concludes that the adoption of financial accounting standards has insignificant influence

on SMEs financial performance and its adoption negatively affects SMEs financial performance due additional cost associated with training and consultancy services to met the laid down standards and procedures associated with international accounting standards. However, the study concludes that financial accounting standards enhance relevancy, reliability and improvement in accounting reports of Small and medium enterprises. The study also established that SMEs rarely use the accounting statements information to project cash flows projections, for budgeting and for ratio analysis therefore the conclusion that extent of financial accounting standards adoption by SMEs in Nairobi County is low and to a little extent.

5.4 Recommendations for Policy and Practice

This study concluded that financial accounting standards enhance relevancy, reliability and improvement in accounting reports of SME. The study therefore recommends that manager and owners of SMEs should adopt financial accounting standards despite the associated costs to improve the relevance of their financial reports, transparency and for internal auditing services.

The study also concluded that adoption of financial accounting standards by SMEs in Nairobi County is way too low. In light of this, the study recommends that policy making entities and the county and national governments should generate strategic and effective policy mechanisms to ensure that they encourage SMEs to adopt financial accounting standards as this would enhance the quality of their accounting and financial reports.

Finally, the study found that SMEs mostly employ the services of consultants to prepare and maintaining the books of accounts and records. Based on this finding, the study recommends that managers and owners of SMEs should train their own staff and develop their own manpower to carry out such task as this may reduce the cost impacts of financial accounting standard adoption and may improve their SMEs performance financially.

5.5 Limitations of the study

The study was undertaken among SMEs in Nairobi County thus its findings may be applied to SMEs within the County. This is due to the fact that entrepreneurs in Nairobi County have adequate access of financial and consultancy services compared to other counties in Kenya.

The study combined primary and secondary data from all the SMEs involved. Collection of primary data was done by the use of questionnaires while the secondary data on financial performance was obtained directly from SMEs. However, the study established that some of SMEs did not have accurate records hence the data obtained could not be 100% validated with accuracy.

5.6 Suggestions for Further Research

The study focus was mainly on SMEs in Nairobi County, data collected was collected from different SMEs within the county, and its findings generalized to all the SMEs despite the nature of their business. The study therefore suggests additional studies on effects of adopting financial accounting standards on specific SMEs financial

performance like manufacturing SMEs, clothing SMEs, restaurants SMEs and other SME sectors.

The study also focused on financial performance measured using return on assets (ROA), however, the performance of SMEs can be measured using non-financial measures like service delivery, improvement in service delivery and others. Therefore, the study recommends additional research on effect of adoption of financial accounting standards on non-financial measures of small and medium enterprises. Additional studies, can also be carried out in SMEs in other counties in Kenya

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APPENDICES

APPENDIX I: Questionnaire

My name is **Abdille Omar Bare**, a student pursuing Masters in Finance at the University of Nairobi carrying out a research on **the extent of adoption of financial accounting standards and its effect on financial performance of SMEs in Nairobi County**. The research is purely academic in nature and any information obtained will be kept confidential to the later. Your cooperation and support will be highly regarded.

SECTION I:

A. Background information

- | | | |
|--------------------------------|------------------------------|--------------------------|
| 1. Gender | Male | <input type="checkbox"/> |
| | Female | <input type="checkbox"/> |
| 2. Number of years in business | Up to 1yr | <input type="checkbox"/> |
| | 1 – 5 yrs. | <input type="checkbox"/> |
| | 6 – 10 yrs. | <input type="checkbox"/> |
| | 11 + years | <input type="checkbox"/> |
| 3. Line of retail business | ICT SMEs | <input type="checkbox"/> |
| | Human resource training SMEs | <input type="checkbox"/> |
| | Medical SMEs/SMEs | <input type="checkbox"/> |

Educational SMEs

Insurance SMEs

Finance/forex bureaus

Others

SECTION II:

B. Accounting Standards

4. In relation to your everyday experience of management, rate the following by ticking the most appropriate response choice to the statement made in the table below;

Statement	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
Is financial accounting standards necessary					
Adoption of financial accounting standards					

affect financial performance					
Accounting skills and quality of financial reports affect financial performance					
Size of business and external factors influence financial performance					

C. Quality of Accounting Reports

5. Who maintains and prepares the books of accounts and the Financial Statement of the business entity? Tick () Where appropriate.

(a) Owner (b) Manager (c) Full Time Accounting Officer

(d) Consultant

6. Which Accounting records and reports are mainly generated and consumed by the Entity?

(a) Management Accounts Reports (b) Audited Financial Accounts

7. Please indicate your usage level of the following 4 accounting Information aspects in your enterprise based on a 5 point scale where (1=Do not use, 2 = Rarely used, 3= Neutral 4 = Often used 5=extensively used).

	1	2	3	4	5
Cash flow					
Projections/budgeting					
Financial statements (income statement, Balance sheet etc.)					
Ratio Analysis					
Product/Service costing					

D. Financial performance of the firm

Kindly provide the details of the firm's financial performance for the financial period/
year ends in Kenya shillings as below:

YEAR	Net Income	Total Assets
2014		
2015		

Thank you for your cooperation

Appendix II: Population

Category of SME	Population frequency	Percentage
Legal SMEs	182	21%
ICT SMEs	61	7%
Tours and travel/hospitality SMEs	160	19%

Human resource training SMEs	50	6%
Medical SMEs/SMEs	101	12%
Educational SMEs	52	6%
Insurance SMEs	104	12%
Finance/forex bureaus	53	6%
Others	105	12%
Total	868	100%

Source: SME Directory 2014