FACTORS INFLUENCING CREDIT DELIVERY SYSTEMS TO SMALL-SCALE ENTERPRISES

BY

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DECLARATION

This management project is my original work and has not been presented for a degree in any other University.

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To my loving husband Joseph Muturia, my children Martin and Diana, my parents Nemwel Kerongo and Truphena Migisi, my brother Ken Kerongo, without whose everlasting love, constant efforts and encouragement, I could not have achieved this degree.

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ABSTRACT

This study sought to identify factors that influence credit flow to Small Scale Enterprises (SSE) from the point of view of SSE and commercial banks. The need for this study arose from the fact that a lot of small businesses do not expand their business operations and new start-ups are limited due to lack of financial resources they need. There is lack of identified factors that could indicate accessibility of credit to SSE.

In order to achieve the objectives of this study, primary data was collected from sample of SSE in the Eastlands of Nairobi and commercial banks with a sample size of 30 each. The methods of data collection were "a drop and collect later procedure" of questionnaires to the commercial banks and personally administering the questionnaires to the SSE. Factors 1 and 2 (interest rates, gender) were tested for independence using Chi-Square Statistics for both commercial banks and SSE responses. Factor 3 namely, commercial banks attitudes to credit Guarantee Schemes, was tested using a sign test statistic.

The data analysis revealed that the two factors (interest rates and gender) were independent of credit flow to SSE. In other words, interest rates and gender are not important factors for credit flow to SSE.

The analysis for factor three revealed that there is positive attitude by commercial banks to Credit Guarantee Schemes.

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ABBREVIATIONS

CB	Commercial Banks
CGS	Credit Guarantee Schemes
E	Expected Frequency
FES	Friedrich Ebert Stiftung
MGS	Mutual Guarantee Systems
O	Observed Frequency
SSE	Small Scale Enterprise

1.0 Introduction

1.1 Background

The tremendous potential of the informal sector can only be awakened if Small-Scale Enterprises (SSE) can obtain the financial resources they need to expand their operation. The improvement of the SSE accessibility to credit can increase new business start-ups and expand the already existing operations. The sector will create employment and will provide income for many people who are involved directly or indirectly. This will inturn, contribute to the growth of the economy of the country.

A business can obtain finance for operations and further expansion through contribution of capital by owners, sale of stock or loan obtained from banks and other financial intermediaries. Most of the operators in the SSE sector have very limited financial and property base both at personal and family savings or property-base as viable sources of funds for business operations and expansion for most of SSE. Also the size and legal status of SSE's prevent them from flouting stock. Thus, sale of stock as an option for raising funds is not applicable to SSE. The only option left is borrowing from the banks or financial intermediaries. Two important conditions that have to be satisfied before a loan by a bank is given is security and abiding to pay the interest charges. Whereas many SSE are willing to pay the interest charges, they are often not able to provide tangible collateral to secure the loans. Tangible collateral is therefore, an important factor influencing the flow of credit to SSE's. In addition to collateral, there are other factors that influence the availability of credit to SSEs. These are interest rates, gender, and commercial banks attitudes to credit guarantee schemes (CGS).

1.1.1 Interest Rate

Interest rate is the cost one incurs on funds borrowed from money lending institutions such as banks. Generally, high interest rates discourage prospective borrowers from applying for loans and vice versa. Low interest rates tend to have the opposite effect. However, the findings of a study conducted by Abugrhe (1993) seems to contradict this. Abugre studied the work of the Agency for co-operation and Research in Development (ACORD). ACORD is an NGO which has credit programmes in the Districts of Uganda: Gulu, Nebbi and Mbarara. The involvement of ACORD in these districts resulted from the desire to find out why demand did not respond to interest rates. The common borrower response is that the higher the interest rates the lower the demand for credit. No study was found which has investigated this customer behaviour. Thus, it is not clear whether small business operators are insensitive to the cost of borrowing funds. If this were to be the case then the only major hurdle between them and credit would be tangible collateral.

Small self-selected groups not exceeding 15-30 people were encouraged to form savings and credit groups. These groups were to pool together their cash savings into a common pool from which they would provide themselves with short-term loans at a cost. They loaned to members on a monthly basis at a rate of interest sometimes exceeding 30 percent a month. Inspite of this high cost, the demand for credit remained high. However, it is not clear from the study whether high interest rates discouraged borrowing as it is generally assumed. This is an area which is not yet investigated to establish how interest rate influences credit accessibility to SSE.

1.1.2 Gender

Women commonly have limited access to financial services. Hossain (1988) conducted a study which revealed a very low percentage of women who have access to credit. In his study, Hussain gathered data from 800 randomly selected households in Bangladesh. He found out that about 45 percent of the respondents had access to credit in 1987 but only 2.8 percent of them were women.

One of the reasons why women's access to bank credit is limited is the requirement that women borrowers be guaranteed by their husbands. Yet there are many women who manage their affairs and resources on their own. In addition, there is a growing number of single women many of whom have children. These women are on their own and make their own decisions. Yet according to the current practice by the commercial banks, they would never qualify for a loan since they do not have husbands to guarantee them, notwithstanding the fact that they may have collateral.

Is this just a tradition that commercial banks use to exclude women from credit? Why should Formal Financial Institutions continue to hold on those conditions which seem to have been overtaken by events? The investigation aims at finding out whether commercial banks still require that women borrowers be guaranteed by their husbands.

1.1.3 Attitude of Commercial Banks to Credit Guarantee Schemes (CGS)

Banks in Kenya have a negative attitude towards CGS (Levitsky 1993). The Government of Kenya (GOK) and financial intermediaries such as Non Governmental Organizations (NGOs), mobilize SSE into groups and organize CGS's to be used in the place of tangible collateral to secure loans for small borrowers from commercial banks. Credit Guarantee Funds are established usually with Government financial support to provide lending institutions with money to compensate for the losses sustained when borrowers default on loans. These CGS's have not been successful in Kenya because loans are not 100 percent guaranteed by the Government, unlike the case in France and Japan. Hence, commercial banks in Kenya do not recognize CGS.

In his study, Levitsky, (1993) found that in the past, CGS's in developing countries such as Kenya had not proved very successful. There is usually a major problem in getting banks to participate in guarantee schemes. In addition, the banking sector in Kenya was not sufficiently aware of the potential of the Credit Guarantee arrangements and was not co-operative in the development of such programmes. He concluded that there was lack of understanding and working relationship between commercial banks, the Government and the local development organizations that could allow for the successful development of such CGS's. Yet the GOK is committed to the promotion of SSE as an important strategy for the creation of employment and the overall economic development (GOK Sessional Paper No.2 of 1992). Thus, the major problem lies with the commercial bank attitude towards lending credits to groups with CGS's. This has not been systematically investigated and documented as a factor influencing credit flow to SSE.

The summary of the factors that influence credit flow other than collateral as discussed above are as follows:-

1. Interest rate
2. Gender
3. Attitude of commercial banks to Credit Guarantee Schemes

1.2 DEFINITIONS

1.2.1 Small-Scale Enterprises (SSE)

Ekpenyong (1992) in his definition has stated that there is no generally accepted definition of a small business because the classification of business into large-scale or small-scale is a subjective and quantitative judgement. In countries such as the U.S.A. Britain and Canada, Small Scale (SS) business is defined in terms of annual turnover and the number of paid employees. In Britain SS Business is defined as that industry with an annual turnover of 2 million pounds or less with fewer than 2000 paid employees. In Japan, SS industry is defined according to the type of industry, paid-up capital and number of paid employees. Consequently small and medium size enterprises are defined as those in manufacturing with 100 million Yen paid up capital and 300 employees, those in wholesale trade with 30 million Yen paid-up capital and 100 employees, and those in the retail service trades with 10 million Yen paid-up capital, and 50 employees.

In Nigeria, there is no clear-cut definition for a medium-scale enterprise. The Central Bank of Nigeria in its monetary policy circular No. 22 of 1988, defines SSE, as having an annual turnover not exceeding 500,000 Naira. In the 1990 budget, the federal government of Nigeria defined SSE for purpose of commercial bank loans as those with an annual turnover not exceeding 500,000 Naira, and for merchant bank loans, those enterprises with capital investments not exceeding 2 million Naira (excluding cost of land) or a maximum of 5 million Naira.

Belandress (1987) defines Small-Scale Enterprises as the manufacturing or non manufacturing service enterprise in which the owner-manager is not necessarily actively engaged in production but performs the varied tasks involved in guidance and leadership without the help of a specialized staff. He also defines microenterprises as those enterprises which are mainly family based, unregistered by the government and lack collateral as assets that are bankable.

Kenya Development Plan, 1980-1993, states that a small business is a company with less than 50 employees and has an annual turnover of upto Kshs.5 million. It goes further to state that these small scale businesses are characterised by:

(a) ease of entry and exit
(b) low capital requirement
(c) dependence of local resources and recycled wastes
(d) family ownership
(e) labour intensive production techniques
(f) low cost skill acquisition mainly outside formal school system
(g) ability to operate under high competitive market conditions (Dossajee, 1992).

The Ministry of Technical Training and Applied Technology definition takes a narrower view and includes only those enterprises which are technically based in the popularly called "Jua Kali". They define it as the rural-urban non-farming small enterprise usually comprising of 0-9 employees specializing in general servicing and production of a variety of items using indigenous technology (Maalu, 1990).

For the purpose of this study, a small business is defined as one that employs fewer than 9 employees, is self-initiated, both/or formally and informally financed, managed by the owner and geographically not dispersed. This definition is chosen because the population of this study displays this peculiarity.

1.2.2 Credit

According to the Concise Oxford Dictionary (7th Edition) Credit is defined as "sum at a person's disposal in books of a bank." This dictionary definition is not adequate. In this study, it is defined as money given by a lender, who sets conditions that must be agreed upon by the borrower.

1.3 Statement of the Problem

There are other factors apart from tangible collateral that affect credit accessibility to SSE. These factors have not been empirically investigated and formally documented as influencing the flow of credit to SSE.

The factors identified as influencing credit flow to SSE include:

1. Interest rate
2. Gender
3. Attitude of commercial banks to Credit Guarantee Schemes

1.4 Objectives of the Study

1. To investigate the extent to which interest rate affects credit flow to SSE.

2. To find out why the commercial banks still require that women applicants for bank loans be guaranteed by their husbands.

3. To investigate the attitude of commercial banks towards Credit Guarantee Schemes.

1.5 Hypotheses

H1: Credit accessibility is independent of interest rates.

H2: Credit accessibility is independent of Gender.

H3: Credit accessibility is independent of commercial banks attitude towards Credit Guarantee Schemes.

1.6 Importance of the Study

The result of this study shall, hopefully, be useful to the following parties.

1.6.1 The entrepreneurs:

(i) By creating awareness of where to go for a loan and what the procedures are.

(ii) To strengthen co-ordination among credit schemes and between these schemes and other programmes.

1.6.2. The Government policy makers.

(i) To assist in proper assessment of beneficiaries so as to appropriately target the credits.

(ii) To strengthen coordination among Credit Schemes and between these schemes and other programmes.

1.6.3 The Small business consultants.

(i) The study forms a good basis for giving their clients useful advice on where to go for a loan and what the procedures are.

1.6.4. Academics

(i) The study forms a sound basis for further research into improvement of credit delivery systems to small scale businesses and Jua Kali sector.

1.7 PLAN AND ORGANIZATION OF THE RESEARCH REPORT

This research report is presented in 5 chapters. Chapter one gives the introduction, background of the study, definitions of Small Scale Enterprise; Credit, The Statement of the Problem, Objectives of the Study, Hypotheses and Importance of the Study.

Chapter two deals with literature review. Emphasis is given on the factors influencing credit flow to SSE a part from tangible collateral. Empirical studies that have been carried out on credit delivery systems on small scale businesses in Kenya and other parts of the world are also reviewed.

The third chapter deals at length with the research method, a detailed discussion of the population of study, sample frame, sample size, sample selection techniques, data collection techniques, data analysis techniques is presented.

The fourth chapter covers research findings and discussions, SSE responses, commercial banks responses.

Chapter five and last chapter gives the summary of the findings, conclusions, recommendations, and the limitations of the study and suggestions for further research.

CHAPTER TWO

2.0 Literature Review

2.1 Introduction

The volume of literature on SSE in Kenya and the world at large has been growing fast. However, empirical literature on factors influencing credit accessibility to SSE per se is scarce or none at all. The available studies have tended to concentrate on business success, management aspects, development banks and SSE, the role of NGOs in creating enabling environment, credit guarantee systems, among others.

This literature review will focus on the studies that have been conducted on factors affecting credit availability to SSEs. It outlined the areas that have already been covered by other researchers, gaps in knowledge and areas of misunderstanding and uncertainty.

2.2 A SURVEY OF EMPIRICAL AND THEORETICAL LITERATURE

2.2.1 Attitudes of commercial banks to Credit Guarantee funds and Mutual Guarantee Systems (CGS and MGS)

Levitsky, (1993) contends that one of the major problems depriving small enterprises of access to finance from institutions is the perception by the lenders that giving credit to

SSEs is a high-risk undertaking. This is primarily because these enterprises cannot provide sufficient tangible collateral or material securities in the form that banks are accustomed to obtain from borrowers. To overcome this, schemes have been set up to offer to the lending institutions a guarantee to cover some or all of the losses incurred when borrowers default on loans. The most frequent form of such schemes is for credit guarantee funds to be set up, usually with government financial support, to provide the money to compensate the financial institutions for the losses sustained when the borrowers fail to repay the loan.

2.2.2 Commercial Banks Attitude to Credit Guarantee Schemes

The general experience of setting up government-funded credit Guarantee Schemes (CGS) in developing countries has been very mixed (Levitsky, 1993). In most cases the schemes were embarked upon without sufficient preparation or concern for viability, and for the potential demand by the borrowers and the banks, and without establishing suitable arrangements and administration for the approval of guarantee and the processing of claims. In several cases, there has been a reluctance by guarantee organisations to pay out claims because it has not been clearly spelt out under what conditions a claim will be settled. This has further contributed to a lack of confidence (and interest) by lending banks in the schemes.

Levitsky (1993) conducted a study on one of the donor organizations that has made special efforts to help establish guarantee schemes in developing countries, Friedrich Ebert Stiftung (FES), a German Foundation working in developing countries with the aid funds from the German Government. The FES believed that credit guarantee schemes could be a suitable instrument, together with revolving funds, for helping SSE obtain greater access to finance from commercial banks. It has to an extent attempted to reproduce in developing countries the experiences and success achieved with credit guarantee systems in German (FES, 1991).

The FES believed primarily in the use of CGA, which can put pressure on the individual members to repay their loans, so as not to require the other members to make repayment on their behalf. However, the FES reported that it had encountered special difficulties in introducing the CGS or MGS approach. FES attempted this approach in Kenya in the year 1983-7, among other developing countries. In 1983, the Development Finance Corporation of Kenya (DFCK) established a subsidiary company, Small Enterprise Finance Company (SEFCO) aimed at providing finance for small and medium-scale industries with the help of FES. It was agreed with SEFCO that the share capital contributed by FES would be used for establishing a credit guarantee fund. No separate legal entity was created, so SEFCO issued guarantees at least to the amount of capital deposited by FES.

In early 1983, a meeting was held to set up a CGS in a region north of Nairobi with 70 artisans taking part. After several meetings a CGA was constituted with 16 members and the first loans were approved in May 1984. Limits for guarantee were set according to members' contributions. Of the 12 contributing members who agreed to be part of the fund, 5 contributed the equivalent of DM.100 and 7 DM.200 each, making a total contribution of DM.1900 (the exchange rate at that time, 1993, was DM.2.5 to the pound).

FES made a matching contribution of the same amount so that the CGA guarantee fund amounted to DM.3800. It was agreed that this could guarantee the equivalent of DM.1900 of loans with the assumption that the projected default in the worst scenario might be 20 percent. However, because of the difference in contributions, the guarantee level for five (5) members was set at DM 1000 and those of 7 that had contributed more were allowed loan guarantees of up to DM 2000.

Levistsky (1993) findings were: Of the 16 members, 2 left early on and, of the remaining 14, only 4 made full use of the credit facilities. Three members refused to meet their obligations and 7 were dismissed from CGA after defaulting on loans. It was FES's view that this first attempt showed that there was an inadequate understanding of the limitations and obligations of CGA, and there were unrealistic expectations on both sides.

Later, 11 more CGAs with 170 members were organized in three other regions of Kenya. By 1990 a decision was made to expand existing CGS to at least 15 members in the belief that this was the most effective number for the functioning of a CGA, but few reached this level. The original idea of a second-tier reinsurance of the CGA by the Government also never materialized.

Levitsky concluded that there existed a basic problem in the target groups in the passive attitudes they adopted, their unrealistic expectations and their reluctance to be involved in self help and mutual support activities. Furthermore in the Kenyan context, it was considered that the banking sector was not sufficiently aware of the potential of the credit guarantee arrangements and was not co-operative in the development of such programmes. Minimum bank co-operation and some form of suitable relationship with the Government and with a local development organization were indispensable for the successful development of such a credit guarantee scheme.

2.2.3 Effects of Interest Rates on Credit Flow to SSE

Abugre, (1993) carried out a study of identical rural credit programme initiated by the Agency for cooperation and Research in Development (ACORD) in three districts of Uganda; Gulu, Nebbi and Mbarara. In each of these areas, ACORD carved out areas with active adult populations of less than 20,000 people. The missing link to development in these areas was thought to be capital, but as an advance over previous practice, emphasis was placed on mobilizing savings. It was thought that given the years of military conflict from which Uganda was just emerging, traditional structures were unlikely to be available or strong enough to be the basis for building trust and confidence, a basic prerequisite for providing loans. Therefore, small self-selected groups not exceeding 15-30 people each (depending on the specific area) were encouraged to form savings and credit groups. These groups were to pool together their cash savings into a common pool from which they would provide themselves with short-term loans at a cost. Groups set up Revolving Savings and Credit Association (RESCA's) and loaned to members on a monthly basis at rates of interest sometimes exceeding 30 percent a month (360 percent per annum). Despite this high cost, the demand for credit remained high. The interest payments were usually capitalized into the group fund and divided among members as dividends only at the end of each year. Rural development workers were employed to help these groups to build cohesion, and to record their financial transactions. They taught simple book-keeping, interest rate policy, and simple ways of analyzing the viability of small projects.

In two years, the total savings mobilized by more than 200 RESCAS in one of the programme areas amounted to about £25,000, an amount which was larger than the capital funds of the commercial banks in the area. This proved that there was more potential for the mobilization of savings than is usually acknowledged. ACORD supplemented these funds through the establishment of a parallel independent credit scheme, with a whopping £50,000, followed by another £20,000 the following year. The justification for this supplement was that the excessive interest rate charged by RESCAs to their members for loans indicated large deficit in the supply of credit.

Abugre (1993) concluded that the reluctance to charge market rates for services, on the basis that the poor cannot afford these rates, does not seem to have been borne out by empirical evidence. In most of ACORD's experiences there has been no evidence that interest rates per se discourage borrowing or affect repayment. What discourages borrowing is the unreliability of markets for produce and of the weather, and difficulties of the general environment. When the poor fails to pay it is either because of uncontrollable factors or that the loan was inappropriately given in the first place.

With liberalization of trade in financial institutions in Kenya, banks are not restricted in interest rates they charge. High interest rates are charged on small loans because of high transaction costs, which is brought about by the high unit costs of administering small loans to SSE, and increased risks that arise because SSE lack collateral and formal credit history.

The way high interest rates influence credit flow is not well understood. It lacks empirical verification (Abugre 1993). My aim is to investigate and establish the influence of interest rate on credit flow to SSE.

If interest rate does not discourage SSE from borrowing, banks will charge competitive interest rates on small loans with adequate margin to cover the relatively high cost of administering such loans with a profit. Recent moves by the Government to deregulate interest rates in the commercial banking sector are expected to provide the necessary freedom to banks in this regard. This will encourage banks to make credit accessible to SSE.

2.2.4 Gender

2.2.4.1 Limited Access to Financial Services for Women

Women have limited access to credit. Hossain and Afsar (1988) gathered data from 800 randomly selected households in Bangladesh. The data revealed that about 45 percent of respondents had access to credit in 1987 but only 2.8 percent of them were women. An in-depth study of credit flows by gender in two bank branches in Andhra Pradesh found that disbursements to women ranged between 6 percent and 12 percent but dropped to zero from Agricultural loans (World Bank 1989a: 134). These trends are not limited to South Asia. In the loan program of the Banco Industrial de Peru, directed at Small and Microbusinesses in the Shanty towns of Lima, only 14 percent of its borrowers were women despite specific instructions to target women (Arias 1989). In Zaire, only 1.5 percent of all commercial bank loans were allocated to women in 1984 (World Bank, 1990).

Hossain (1988) found in his study that the factors that limit credit flow to women entrepreneurs are: Limited education and familiarity with loan procedures, social and cultural barriers and the nature of women businesses.

2.2.4.2 Education and Familiarity with Loan Procedures

Women's relatively low levels of literacy and numeracy make it difficult for them to overcome even the procedural barriers of taking out formal loans. In many countries, women have less education than men, which puts them at a further disadvantage in applying for credit. Women's educational attainment averages 58 percent in Africa, 56 percent Middle East, and only 47 percent in South Asia (Blumberg 1989). Girl's school enrolment and literacy rates have increased greatly in Latin America, but literacy rates are still low for older women, who tend to work in the informal sector.

In Guatemala and Honduras, literacy rates for women 35 years and older are only 30 and 37 percent, respectively (Lycette and White 1989). As a result, many women have trouble completing the complicated application forms and financial statements that banks require. And their limited experience with formal credit institutions adds to the problem.

2.2.4.3 Social and Cultural Barriers

Social and cultural barriers also restrict women's demand for, and access to credit. In many areas it is considered inappropriate for a woman to travel a long distance between her rural home and a bank in a town, or to offer the occasionally necessary bribe to a male official in charge of credit applications (Lycette and White, 1989). More important, women are commonly excluded from local organisations, such as agricultural cooperatives or social groups, that provide information or may even extend credit. In Malawi for example, credit is usually administered only to members of farmers' clubs. By custom, women may not belong to these clubs, and membership is often on the recommendation of agricultural extension agents, whose contacts are mainly with men (Morna, 1989).

In Kenya, banks require, that women borrowers be guaranteed by their husbands.

2.2.4.4. The Nature of Women's Businesses

The type of business women engage in also affect their access to credit. First, because women have limited access to physical and human resources, their businesses tend to be among the smallest, even within the category of microenterprises (five employees or fewer); and have low profit margins. Most women's businesses have only one worker - the business owner herself. Women-owned businesses borrowing from a microenterprise program in Ecuador, for example averaged only one employee, compared with two for men's businesses (Berger, 1989). Their concentration in smaller, lower-profit activities makes women bigger credit risks for commercial lenders.

Secondly, women tend to keep their businesses close to home to minimize conflict between their many roles as wage earners, mother, homemaker, and so on (Berger, 1989). These multiple responsibilities restrict the time and mobility of many women in developing countries (Hossain and Afsar, 1989, Otero and Downing, 1989). A crossregional study of women in the informal sector in Zimbabwe found that about 64 percent of women run their businesses from other homes (ENDA, 1990). Similarly, a study of a sample of women marketers in the Kutus region of Kenya showed that for the most part, women were limited to small-scale retail trade, unable to pursue long-distance wholesale trade because of constraints on both their time and mobility (Downing and Santer, 1989).

Does the requirement by Commercial banks that women borrowers be guaranteed by their husbands still work? Times have changed. Women manage their own resources, a good number of them have no husbands and among them are single mothers. They head families and make independent decisions. The investigation aims at finding out whether this condition hold these days. If it does not hold, then women borrowers are accessible to credit. On the other hand, if it does hold, then women borrowers are limited in terms of access to credit.

CHAPTER 3

3.0 Research Method

3.1 Population of Study

The population of interest are the small-scale enterprises employing 0-9 workers with an annual turnover not exceeding Kshs.5 million. In addition, the other set of population is all commercial banks with their branches, licensed with the Central Bank of Kenya to operate as commercial banks.

3.2 Sample

3.2.1 Sampling Frame

The sampling frame consisted of both locally and foreign-owned banks -government and private national and multinational (see Appendix IV).

Small Scale Enterprises (SSE)

The SSE are in great numbers, thus the cost of constructing a sample frame are far greater than the resources available to the researcher. In addition, the population of

SSE keeps on changing by new start-ups and others drop out of business. Due to the said practical problems, I used stratified sampling in the Eastlands of Nairobi. The area lies in the East of Nairobi City Centre, and it is an area of small business concentration. There are numerous small businesses of various natures. The area was divided, using judgement sampling, into three main areas of concentration which had the highest concentration of the small enterprises. The three areas are: Kariobangi, Dandora and Gikomba. The enterprises compose of three main categories: manufacturing, service and trading. The proportion of sampling will be equal.

3.2.2 Sample Size

All the 38 Commercial Banks which appear on the sample frame were visited and interviewed by the researcher and her assistants and out of these, 30 responses were considered usable. On the other hand, a sample of 30 small scale enterprises were randomly selected from the three regions under study (Kariobangi, Dandora and Gikomba) on equal basis and were personally administered by the researcher and her assistants. Convenient sampling was used because it was difficult to construct a sample frame at SSE.

3.2.3 Sample Selection Technique

Random sampling technique was used on Commercial Banks because the sample frame was easily constructed, since Commercial Banks are only 38. Stratified sampling technique was used on SSE because it was difficult to construct a sample frame. Stratified sampling was used in the three areas of concentration of SSE; Kariobangi, Dandora and Gikomba in equal proportions.

3.2.4 Data Collection Techniques

Primary data was used for the purpose of this study. A questionnaire was used to collect the data as detailed in the appendix (i) and (ii). This questionnaire was administered through interviews conducted by the researcher and her assistants over a period of one and a half months in both Commercial Banks and SSE in the Eastlands of Nairobi (Kariobangi, Dandora and Gikomba). Essentially the main purpose of the questionnaire was to get information leading to the factors influencing credit delivery to SSE. In order to achieve this primary objective, the researcher divided the questionnaire into two sections.

Section A which contains 7 questions was administered to SSE by the researcher personally and her assistants through interviews. Questions 1-4 were general questions to SSE which served as introduction and questions 5-7 were meant to capture the factors influencing credit flow to SSE. It was necessary to conduct interviews because some of the respondents were found to be illiterate in which case other methods of administration such as self administration could not be possible.

Section B which contains six (6|) questions was administered to the commercial banks. As far as Commercial Banks were concerned, the researcher adopted a drop and collected later procedure to get the required information. The Bankers are literate people and hence it was not necessary for the researcher to administer the questionnaire personally.

3.2.5 Data Analysis

Different statistical tools were applied to different factors as follows:

Banks

Factor 1 and 2: Interest rates, Gender

Based on the data summary which was summarised in a contingent table, the preferable relevant statistical analysis was chi-square dependence test. The researcher has adopted chi-square dependence test by borrowing from similar studies done in other fields. For example, Maalu (1990) used chi-square in his study on "Factors Influencing

Record Keeping in the Small Scale Enterprises: A Case of the Microenterprises in the Eastlands of Nairobi."

Factor 3: Commercial Banks' Attitudes to CGS

Due to the categorical nature of the data on this factor, the researcher decided to use sign test. Hulme (1993) used the same test in his study of "Attitudes of SSE to Grameen Bank Model."

CHAPTER FOUR

4.0 Data Analysis and Findings

4.1 Introduction

The objectives of this study were to establish the factors influencing credit deliveries to SSE. The first part of the chapter, presents the empirical findings on credit aspects to the SSEs. It outlined the areas that have already been covered by other researchers, gaps in knowledge and areas of misunderstanding and uncertainty was highlighted.

All 38 banks on the sample frame were visited and interviewed by the researcher and her assistants but 30 responses were considered usable. A sample of 30 SSEs was drawn from the three regions of SSE concentration (Kariobangi, Dandora and Gikomba) in equal proportions hence analysis is based on 30 bank responses and 30 SSE responses.

4.2 Banks Responses

4.2.1 Factor 1: Interest Rates

Numerical data is summarized from the questionnaires as follows:

Credit Flow (Applicants) \ Interest Rates	High	Low	Total
High	10 / 9	8 / 9	18
Low	5 / 6	7 / 6	12
Total	15	15	30

Based on the data summarized in table 1, the relevant statistical analysis is chi-square (^{2}) test of dependence.

The following hypothesis was tested:

H_o: Credit accessibility is independent of interest rates.

H_A: Credit accessibility is dependent of interest rates.

$$\text{Sample} = \frac{(O - E)^2}{E}$$

Where;

O = Observed Frequency

E = Expected Frequency

$$E = \frac{\text{Row total} * \text{Column total}}{\text{Grand total}}$$

$$\chi^2 \text{ sample} = \frac{(10-9)^2}{9} + \frac{(8-9)^2}{9} + \frac{(5-6)^2}{6} + \frac{(7-6)^2}{6}$$

χ^2 sample = 0.11 + 0.11 + 0.16 + 0.16 = 0.54

χ^2 sample = 0.54

χ^2 critical = 3.841

χ^2 sample = 0.54 < χ^2 critical (3.84), P 0.05

As χ^2 sample (0.54) is less than χ^2 critical (3.84), Null hypothesis cannot be rejected. That is, the result is not significant at the 0.05 level and it is concluded that credit accessibility is independent of interest rates.

4.2.2 Factor 2: Gender

Table 2: Effect of Gender on Credit Flow to SSE for both Observed (O) and Expected (E) Frequencies

Gender / Credit flow (Applicants)	High	Low	Total
High	7 6.93	9 9	16
Low	6 6	8 7.93	14
Total	13	17	30

On the basis of data summarized in table 2, chi-square (^{2}) dependence test of independence is used to test the hypothesis as stated below.

The factor was tested for statistical significance using this statistics as follows:

H_o: Credit accessibility is independent of gender.

H_A: Credit accessibility is dependent of gender.

$$x^2 \text{ Sample} = \frac{(O-E)^2}{E}$$

$$x^2 \text{ Sample} = \frac{(7-6.93)^2}{6.93} + \frac{(9-9)^2}{9} + \frac{(6-6)^2}{6} + \frac{(8-7.93)^2}{7.93}$$

$$x^2 \text{ Sample} = (0.0007 + 0 + 0.00062)$$

$$x^2 \text{ Sample} = 0.0013$$

$$x^2 \text{ Sample} = 0.0013 < x^2 \text{ critical} \quad (3.841),\ P \leq .05$$

As x^2 sample (0.0013) is less than x^2 critical (3.841), accept the H_o. The result is not significant at the 0.05 level, hence it is concluded that credit delivery is independent of gender.

4.2.3 Factor 3: Commercial Banks attitudes to CGS

The question was intended to capture information on the attitude of commercial banks to CGS. It was measured on a three point scale, that is large extent, moderate and small extent.

Data summarized as follows:

Large Extent	10
Moderate	8
Small	12
	30

This was analyzed using the sign test as follows:

Large extent	10
Moderate (equivalent of ties in sign test)	8
Small	12
	30

H_o: There is negative attitude for any credit system offered by Commercial Banks to CGS.

H_A: There is positive attitude for credit lending by Commercial Banks to CGS.

In numerical terms, using the sign test statistics, the above hypothesis can be stated as follows:

H_o: $P = 0.50$

H_A: $P \neq 0.50$

Taking $\alpha = 0.05$

Z critical value $= \pm 1.96$

Z sample $= \dfrac{\bar{P} - P}{\sigma P}$

$$\sigma \bar{p} = \frac{pq}{n} = \frac{(0.50)(0.50)}{30-8}$$

$$\sigma \bar{p} = 0.01$$

$$\bar{p} = \frac{22}{22} = 1$$

$$Z \text{ sample} = \frac{1 - 0.50}{0.01}$$

Z sample = 50

Since Z sample (50) > Z critical (1.96)

reject the H_o. The result is significant at the 0.05 level.

It is concluded that there is preference in lending to CGS by commercial banks.

4.3 SSE Responses

4.3.1 Factor 1: Interest rate

Table 3: Effect of Interest Rates on Credit Flow to SSE for both Observed (O) and Expected (E)

Credit Flow (Applicants) \ Interest rates	High	Low	Total
High	7 / 9	11 / 9	18
Low	5 / 6	7 / 6	12
Total	15	15	30

H_o: Credit accessibility is independent of interest rates.

H_A: Credit accessibility is dependent of interest rates.

$\alpha = 0.05$

$r = 1$

$$\chi^2 \text{ sample} = \frac{(0-E)^2}{E}$$

$$\chi^2 \text{ Sample} = \frac{(7-9)^2}{9} + \frac{(11-9)^2}{9} + \frac{(5-6)^2}{6} + \frac{(7-6)^2}{6}$$

χ^2 Sample = 0.44 + 0.44 + 0.17 + 0.17 = 1.22

χ^2 Sample = 1.22

χ^2 critical = 3.841

χ^2 sample (0.098) $< \chi^2$ critical (3.84), $P < 0.5$

As χ^2 sample (0.098) $< \chi^2$ critical (3.841), Null hypothesis cannot be rejected. The result is not significant at the 0.05 level, hence, it is concluded that credit flow to SSE is independent of interest rates.

4.3.2 Factor 2: Gender

Table 4: Effect of Gender on Credit Flow to SSE for both Observed (O) and Expected Frequencies

Gender / Credit flow (Applicants)	High	Low	Total
High	14 12.67	5 6.3	19
Low	6 7.3	5 3.67	11
Total	20	10	30

On the basis of data summarized on table 4, chi-square (^{2}) of independence is used to test the hypothesis as stated below:

H_o: Credit accessibility is independent of Gender.

H_A: Credit accessibility is dependent of Gender.

$$\chi^2 \text{ Sample} = \frac{(O-E)^2}{E}$$

$$\chi^2 \text{ Sample} = \frac{(14-12.67)^2}{12.67} + \frac{(5-6.3)^2}{6.3} + \frac{(6-73)^2}{7.3} + \frac{(5-3.67)^2}{3.67}$$

$$= 0.14 + 0.27 + 0.23 + 0.48 = 1.12$$

$$= 1.12$$

χ^2 Critical = 3.841

χ^2 Sample (1.12) < χ^2 critical (3.84), $P \leq 0.05$

The result is not significant at the 0.05 level and it is concluded that credit accessibility is independent of (Gender). In other words, Gender does not affect credit accessibility to SSE.

In this case ^{2} sample (1.12) is less than ^{2} critical (3.84), Null hypothesis cannot be rejected. The result is not significant at 0.05 level, thus, it is concluded that credit flow to SSE is independent of Gender.

CHAPTER FIVE

5.0 Discussion, Conclusions and Recommendations/Suggestions

5.1 Discussion and Conclusion

The findings from the analysis of the factors that influence credit flow to SSE showed that the two factors were not significantly important, the two factors were interest rate and Gender. In addition, the analysis of factor three which was the attitude of Commercial Banks to CGS showed that there was positive attitudes in lending to CGS by commercial banks. Credit Guarantee Schemes serve as security which is a better alternative in the absence of tangible collateral.

One of the findings is that the interest rates do not appear to affect the credit flow to SSE. As a collary, this also means that low interest rates do not necessarily attract greater flow of credit to SSE. This is contrary to the general belief that high interest rates limit credit to SSE. However, the finding is in line with what was found in Mbarara area of Uganda in Chapter two of the literature review. (Abugre 1993) in his study found out that despite high cost of borrowing (360 percent per annum) the demand for credit remained high.

The reason why interest rates have no effect on credit flow to SSE as has been given by respondents (CB, SSE) is that there are other factors that go with interest rates. Such factors are for example availability of a market for the products/services. With availability of a market, the costs of borrowing may be passed to the customer by charging higher prices for the products/service, hence the profitability of the producer is not affected. Another reason being that once a business owner has committed him/herself to business, it would be expensive to just abandon the business due to high interest rates. It means then that high interest rates will not hinder the SSE from applying for the loan.

According to the findings, gender does not seem to have effect on credit flow to SSE. This is contrary to what is in the literature that women are discriminated against in credit flow by commercial banks. Respondents from SSE and commercial banks state that women are not discriminated against. This is because women manage their resources. Some of these women are single and hence the condition of women being guaranteed by husbands does not arise.

Under the test of attitude of commercial banks to CGS as tested by sign test statistics, data indicates that there is favourable attitude in lending to CGS by commercial banks. This is because Banks feel that their money is secure. They can recover the money easily from the contributions of members of CGS in case of default. Thus, the popular belief that commercial banks have negative attitude to CGS is not true. This is contrary to what is in the literature that Commercial Banks have a negative attitude to CGS. Levitsky (1993) in his study in Kenya found out that commercial banks had a negative attitude in lending to CGS. It appears that this negative attitude of commercial banks to CGS in loan deliveries to SSE has changed over time since 1993.

5.2 Recommendations/Suggestions

There is need to educate the public on the bank's requirements because from the findings it seems to be a misconception, what the public believes in, that interest rates affect low credit flow to SSE and women are discriminated against in credit flow by commercial banks.

There is urgent need to improve access and increase the volume of loanable funds to the SSE sector by:

Commercial banks are advised to relax the collateral requirements to some reasonable degree by insuring the loans with insurance firms. Banks would recover their money from insurance firms in case of default.

5.3 Limitations of the Study

The limitations of this study were as follows:

The first limitation of the study is that the sample may not be representative of the SSE due to the absence of the sampling frame.

The other limitation is that the findings of this research may not be generalized beyond the sample elements because of the risk of a large sampling error.

The nature of the respondents largely illiterate, required some of the questions or all of the questions in other cases, had to be explained in Kiswahili. In the process, some of the original meanings could have been distorted.

Due to time constraints this sample size for both banks and SSE were only 30 each. A larger sample of SSE could have made the study results more generalizable.

5.4 Suggestions for Further Research

From the findings of this study, there is need for further research in the following areas: First, a larger sample incorporating small business operations in both urban and rural areas countrywide could be carried out to consolidate what they consider as factors influencing credit flow to SSE.

Second, a study could be carried out on Grameen Bank Model of Bangladesh and its applicability to other developing countries like Kenya.

APPENDIX I

Dear Respondent,

I am a postgraduate student at the University of Nairobi. I am undertaking a survey on some aspects of credit delivery to SSE as a requirement for the course I am taking.

Your enterprise/Bank has been selected to form part of the study. Please respond to the attached questionnaire. The information you provide will be treated in strict confidence. The name of your firm or your own name will not be mentioned anywhere in the report.

A copy of the report will be made available to you upon request.

Thank you for your continued cooperation.

Yours faithfully

Muturia Jemimah

Department of Business Administration

Faculty of Commerce

University of Nairobi.

APPENDIX II

THE QUESTIONNAIRE

SECTION A

Tick in the box provided for the most appropriate response.

1. What is the main type of Business you are engaged in?

   (i) Manufacture

   (ii) Service

   (iii) Trading

   (iv) Others (Please specify)

2. What is the nature of ownership of your business?

   (i) Individually owned

(ii) Family Partnership

(iii) Corporation/Company

(iv) Others (Please specify)

3. How long have you been in this business?

.... months/years

4. What has been your major source of finance?

(i) Informal (self, family, friends etc)

(ii) Formal (banks etc)

5. In these days do you think it is necessary for women borrowers to be guaranteed by their husbands even when they meet the banks' condition for providing loans?

(i) Yes

(ii) No

6. Give reasons for your answer in number 1 above.

....

....

7. To what extent does the interest rate affect your borrowing?

(i) Large extent

(ii) Moderate extent

(iii) Small extent

APPENDIX III

THE QUESTIONNAIRE

SECTION B

1. To what extent do you provide loans to Credit Guarantee Schemes?

    (i) Large extent

    (ii) Moderate extent

    (iii) Small extent

2. Give reasons for your rating in number 1 above.

    ....

    ....

    ....

3. To what extent do you require that women borrowers be guaranteed by their husbands even when they meet the banks' condition for providing loans?

    (i) Large extent

(ii) Moderate extent

(iii) Small extent

APPENDIX IV

COMMERCIAL BANKS OPERATING IN KENYA AS AT DECEMBER 1995

1.	ABN-AMRO BANK	13-5-81
2.	AFRICAN BANKING CORP. LTD	1-5-84
3.	AFRICAN MERCANTILE BANKING CO. LTD.	13-9-89
4.	BANK OF BARODA	1-7-53
5.	BANK OF INDIA	5-6-53
6.	BANK OF INDOSUEZ	1-7-60
7.	BARCLAYS BANK OF KENYA LTD.	1-7-26
8.	BIASHARA BANK OF KENYA LTD.	1-7-84
9.	BULLION BANK LTD.	1-1-91
10.	CITIBANK N.A.	1-7-74
11.	COMMERCIAL BANK OF AFRICA LTD.	13-2-67
12.	CONSOLIDATED BANK OF KENYA LTD.	8-12-89
13.	CO-OPERATIVE BANK OF KENYA LTD.	1-7-68
14.	CREDIT BANKING CORPORATION	1-9-92
15.	CREDIT BANK LTD.	14-5-86
16.	DAIMA BANK LTD.	1-9-92
17.	DELPHIS BANK LTD.	30.8-91
18.	EURO BANK LTD.	17-12-92

19.	EXPORT BANK OF AFRICA LTD.	18-12-92
20.	FIRST AMERICAN BANK OF KENYA	1-6-74
21.	GIRO BANK LTD.	17-12-92
22.	GUILDERS INTERNATIONAL BANK LTD.	1-4-91
23.	HABIB BANK A.G. ZURICH	1-7-78
24.	HABIB BANK LTD.	2-3-56
25.	KCB	1-2-70
26.	KENYA FINANCE BANK LTD.	1-3-78
27.	MASHREQ BANK P.S.C.	11-9-81
28.	MERIDIAN BIAO BANK LTD.	2-1-92
29.	MIDDLE EAST BANK (K) LTD.	15-12-80
30.	NATIONAL BANK OF KENYA LTD.	1-1-68
31.	PRIME BANK LTD.	13-1-92
32.	RELIANCE BANK LTD.	1-4-88
33.	STANBIC BANK KENYA LTD.	9-8-70
34.	STANDARD CHARTERED BANK (K) LTD.	1-10-10
35.	TRANS NATIONAL BANK LTD.	1-8-85
36.	TRUST BANK LTD.	23-11-86
37.	UNITED BANK LTD.	1-4-91
38.	ALGEMENE BANK NEDERLANDS	3-5-92

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