THE PERCEPTION OF MICRO FINANCE LOAN BORROWERS ON THE EFFECTS OF LOANS ON THEIR BUSINESSES AND AS A POVERTY ALLEVIATION TOOL: A CASE STUDY OF BORROWERS IN NAIROBI

BY:

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DECLARATION

This Management Research Project is my original work and has not been presented for a degree in any University.

Signed..Date..........................

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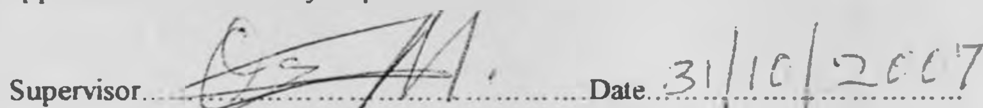
This Management Research Project has been submitted for examination with my approval as the University Supervisor.



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DEDICATION

To my husband: for his encouragement, understanding and support. To my children Mark, George-Smith, and Mwashumbe for letting me use their inheritance. To my dearest late father who without his foundation I would not have been where I am today. To my mother: for her encouragement on paying the price of success "Kudema mdemi na kufunga mkumbo.", to my mother in law for believing in me, and above all to the almighty God for giving me the ability to complete the project.

ABBREVIATIONS

AHF:	African Housing Fund
AMFI:	Association o f Micro Finance Institutions
CGAP:	Consultative Group to Assist the Poor
GDP:	Gross Domestic Product
IMF:	International Monetary Fund
ILO:	International Labour Organisation
KEDP:	Kenya Enterprise Development Programme
K-MAP:	Kenya Management Assistance Programme
K-REP:	Kenya Rural Enterprise Program
KRDP:	Kenya Rural Development Programme
MFIs:	Micro Finance Institutions
MSEs:	Micro and Small Enterprises
NCCK:	National Council Of Churches in Kenya
NGOs:	Non-Governmental Organisations
PRSP	Poverty Reduction Strategy papers
SID:	Society for International Development
SME:	Small and Micro Enterprises
WMS:	Welfare Monitoring Survey

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ABSTRACT

The study sought to establish the perception of Micro Finance Loan Borrowers on the effects of loans on their businesses and as a poverty alleviation tool. It also sought to establish the perceived adverse effects on businesses of interest charge on the loans advanced by MFIs.

The study established that though the loans were perceived to have improved the businesses, the state of businesses before entry into an MFI credit scheme was not bad. The respondents thought their business were not in very bad shape before entry into a credit scheme. This can be explained by the fact that none of the businesses interviewed had received start up capital from an MFI, 93% used own savings and partners'. Further, regarding the perceived effectiveness of Micro Finance Loans as a poverty alleviation Tool, though the respondents perceive their welfare to have improved they did not consider themselves as poor before entry into an MFI credit scheme.

The study also established that the interest charge on MFI loans was perceived to have very little effect on the performance of the businesses.

The study concludes that the loans advanced by MFI are perceived to have a positive effect on the businesses and as a poverty alleviation tool. The interest charge is not perceived to have great adverse effects on the businesses.

CHAPTER ONE

INTRODUCTION

1.1 Background

There is a paradox at the heart of international trade. In the globalised world of the early twenty first century, trade is one of the most powerful forces linking our lives. It is also a source of unprecedented wealth. Yet millions of the world's poorest people are being left behind. Increased prosperity has gone hand in hand with mass poverty and the widening of already obscene inequalities between rich and poor. World trade has the potential to act as a powerful motor for the reduction of poverty, as well as for economic growth, but that potential is being lost. The problem is not that international trade is inherently opposed to the needs and interests of the poor, but that the rules that govern it are rigged in favour of the rich (Oxfam, 2002).

The human costs of unfair trade are immense. If Africa, East Asia, South Asia, and Latin America were each to increase their share of world exports by one per cent, the resulting gains in income could lift 128 million people out of poverty. Reduced poverty would contribute to improvements in other areas, such as child health and education. In their rhetoric, governments of rich countries constantly stress their commitment to poverty reduction. Yet the same governments use their trade policy to conduct what amounts to robbery against the world's poor. When developing countries export to rich country markets, they face tariff barriers that are four times higher than those encountered by rich countries. Those barriers cost them $100bn a year – twice as much as they receive in aid. Poverty Reduction Strategy Papers (PRSPs) provide the IMF and the World Bank with an opportunity to place trade at the centre of their dialogue with governments on poverty. That opportunity is being lost. In a review of twelve PRSPs we found that only four mentioned the possible impact of trade reform on poor people, of which two considered measures to protect the losers (Oxfam, 2002).

The effects of IMF/WB policies on poverty, income distribution, basic social services and employment have been devastating in most African countries. Under privatization policies, there has been an increase in unemployment and job insecurity, workers rights have been weakened, regulatory efforts have been ineffectual and service quality has declined. Public sector reform in the form of retrenchment has not helped things either. The Government

must be bold enough to craft home made or home grown development policies to jump-start the economy. The beaten path can no longer sustain the situation just like the keepers of the past cannot be the leaders of the future and thus the need for home grown development policies. The government of Kenya has over the years designed poverty reduction strategies (PRSPs), but the problem still persists, and has continued to worsen over the years. In its manifesto, NARC argues that its approach to poverty will be through the promotion of an economic growth model based on the private sector as the engine of growth. However, it is important for the Government to note that the model as propagated by IMF and the World Bank will not succeed in the fight against poverty and unemployment (Awiti, 2003).

NGOs and the government have in the past sought to reduce poverty by intermittently providing the poor with needed goods and services. The failure of these programs to address the root of the problem brought the need to confront poverty on a sustained basis. Policymakers and NGOs recognized that both human capital and productive capacity of the poor needed to improve in order to reduce poverty (Khandker, 1998).

Micro-finance is presently promoted as an almost magic solution to poverty. Innovative institutions and programs in Asia and Latin America, some operating as long as 40 years, have demonstrated that providing credit and savings services to the poor can be a powerful and efficient tool for poverty elimination. While micro-finance is not a panacea to eradicate poverty, it is, as Juan Somavía, Chile's Permanent Representative to the United Nations and Director-elect of the ILO stated at the Micro-credit Summit in February 1997 in Washington DC, USA, "a new and already tested tool for discovering new solutions to an old and intractable problem". He added "what I like most about micro-credit is that it builds on age-old human instincts: the need to believe in ourselves and use our imagination, to dare, to take risks, all in pursuit of the most worthwhile of all causes - the advancement of your family, yourself, and your community" (ILO,1998)

One criticism leveled at micro-credit is that in an era of mass market and mass production, self employment is bound to remain small and cannot attain any economies of scale. But home-based production can be as mass-scale as any factory-it is simply not under one roof, nor wage-based. The policy needed for eradication of poverty must be much wider and deeper than the policy for provision of mere employment. Yunus believes that the real eradication of poverty begins when people are able to control their

own fate. Therefore it is not work which saves the poor. but capital linked to work (Yunus with Jolis, 1999)

1.1.1 Definition and State of Poverty in Kenya

Poverty is a cursed thing. People struggle to run away from it and avoid those who are in it. Poverty is a condition of lacking adequate supply of basic necessities of life. These are food, clothing, shelter, health-care and education (Ncebere, 1999).

The Second report on Poverty in Kenya, the Incidence and Depth of Poverty in Kenya (2000) defines the poor as those members of society who are unable to afford basic minimum needs. The report defines poverty in 'Absolute' rather than relative terms, referring to those who cannot meet the universally recommended minimum requirements for human survival. Absolute poverty is evidenced by, low purchasing power, food insecurity and inadequate nutritional levels, unemployment, lack of shelter and access to clean water, health and education. The groups most affected include the urban poor and isolated communities in remote areas, as well as households with land holdings that are too small to meet subsistence requirements. GDP growth rates have barely kept pace with population growth. In Kenya poverty can be classified into Rural and Urban Poverty (Poverty in Kenya, 2000).

Absolute Poverty is defined in terms of the requirements considered adequate to satisfy minimum basic needs; the Absolute Poor have no means to meet these needs. Specification of these minimum requirements is inspired by the universal valuation of human dignity. Those falling below the poverty lines (Food or Overall) derived in this manner are leading inhuman lives according to universal norms of human dignity; facing starvation, lack of shelter, or have the prospect of turning to immoral activities for survival (Poverty in Kenya, 2000).

Another characteristic of absolute poverty is that it has real value over time and space of welfare. What this means is that poverty lines defined in this way guarantees that poverty comparisons made are consistent in the sense that two individuals with the same level of welfare are treated the same (Poverty in Kenya, 2000).

Poverty is perceived differently by different people, some limiting the term to mean a lack of material well being and others arguing that a lack of things like freedom, spiritual

well being, civil rights and nutrition must also contribute to the definition of poverty. According to material well being approach, the poor are defined as those members of society who are unable to afford minimum basic human needs, comprised of food and non-food items (Poverty in Kenya, 2000).

One of the greatest challenges that faced Kenya government at independence was how to reduce widespread poverty. Poverty, ignorance and disease were identified as the major constraints to socio-economic development. Forty-two years after independence the problem of poverty still persists with over 56% of Kenya's population living below the poverty line. Poverty reduction still remains one of the greatest challenges facing the Kenya government today (National Poverty Eradication Plan (1999), Poverty in Kenya (2000), Economic Recovery Strategy for Wealth and Employment Creation (2003) and, Economic Review (2004)). A recent study carried out by SID international and The Ministry of Planning, Kenya; rated Kenya as one of the most uneven societies with the wealthiest 10% controlling 42% of the countries income. This report also found out that, the gap between the rich and the poor is one of the widest in the world and growing (Mogusu, 2004).

1.1.2 Efforts by the Government and NGOs to Alleviate Poverty

Many countries pursued growth oriented development strategies since the late sixties aimed at increasing both employment and productivity through higher economic growth. Issues of distribution and poverty alleviation were considered peripheral, because it was thought that the trickle-down effect would raise living standards among all strata of society, but this did not happen (Khandker, 1998).

Future reductions in poverty in Sub-Saharan Africa will have to come from a significant expansion in the private sector activity and substantial improvements in productivity. The capacity of the sector to bring about such changes will depend importantly on the ability of entrepreneurs to develop more effective business strategies, make profitable investments, and improve technologies in use. Unfortunately, as development literature has so often pointed out, differences in availability of entrepreneurial talent (both technical and managerial) and differences in the motivational mechanisms that drive entrepreneurs have important causes of Africa's relative stagnation, compared with other parts of developing world (Biggs and Shah, 2003)

Governments play a complex role in micro-finance. Until recently. many governments believed that it was their responsibility to provide development finance. including direct lending to the disadvantaged. But decades of experience have shown that when governments engage in retail lending to the poor, they almost always do it badly. Short-term political gain is very tempting for politically controlled lending organizations: they disburse too quickly, and they collect too sporadically because they are unwilling to be tough on defaulters. Furthermore. good micro-finance requires an agile and efficient corporate culture. which can be difficult to maintain in an organization subject to government hiring and firing policies (CGAP. 2003).

More recently, many governments have recognized that they can not do a good job of lending to the poor. yet they still seek to promote such lending by setting up apex facilities that make wholesale funding available to a range of private micro-finance providers. Such apexes can be useful if the country has a critical mass of solid micro-finance institutions. However. they usually have not been effective in developing good institutions where few or none existed before. and they are likely to be subjected to political pressure unless their structure effectively precludes government influence. Although governments are not usually good at lending, they play an important role in setting appropriate policies. The key things that a government can do for micro-finance are to maintain macroeconomic stability and to avoid interest-rate caps that prevent MFIs from covering their costs and operating sustainable (CGAP, 2003).

The government of Kenya in its initial years after independence put a lot of emphasis on training for white color jobs. This led to rural urban migration leaving very few people to produce food to support large populations in cities leading to the current congestion in the cities and food insecurity. It was common belief among Kenyans and it worked for a while that. the only way out of poverty was through education and employment in the public or in the private sector. This orientation is still a stumbling block for Kenya's economy today. It has turned this country into a country of consumers and not producers. Agriculture. which was and has been Kenya's economic back borne was ignored and concentrated in a few pockets which were earlier. the home of the White colonial settlers. In the early 70s when the government realized that the formal job sector was not growing as fast as the job seekers the government started to introduce economic programs aimed

at promoting the informal sector like: KRDP. credit provision from church based organizations and NGOs (AMFI, 2003).

In the Development plan. 1979-1983 the government of Kenya proposed that a credit scheme of Kenya Shillings 50 million be set aside for lending to small enterprise (GOK. 1979). The Sessional paper No 1 of 1986. Economic Management for Renewed Growth. set out to create an enabling environment for SMEs to prosper. The Strategy for Small Enterprise Development which set out mechanisms for the removal of constraints to the development of SME sector was developed (GOK. 1986). A further effort by the government was formation of a policy framework in sessional paper No. 3 of 1992. Small Enterprise and Jua Kali development in Kenya; this paper sought to establish the necessary enabling environment for the development of the sector. The development plan 1989-1993 declared "the Government would speed up the already initiated review of the local authorities. by-laws and regulations that have proved restrictive to the development of SMEs. The provision and delivery of financial services and credit to the sector by the formal financial institutions has been below expectation. One of the outstanding funding agencies of SMEs in many decades has been the Micro Finance Institutions (MFIs) (GOK. 2000).

1.1.3 Evolution of the Micro Finance Industry in Kenya

The Kenyan Micro finance industry is one of the oldest and most established in Africa. Interest in the informal sector in Kenya started as far back as the early 1970's after the seminal ILO report on employment was issued in Kenya in 1972. This report for the first time identified the informal sector as a potentially important contributor to employment and economic growth in Kenya and other developing countries (AMFI, 2003).

The Micro finance Industry has evolved through three distinct phases over the last two decades: The 1960's were marked by targeted credit towards the agricultural sector in recognition of the vital role that this sector played in the economic development of the country. Development finance was not concerned about poor target groups, main thrust was to transfer capital to developing countries in order to fill what was believed to be a structural gap in capital formation (AMFI, 2003).

Multilateral and bi-lateral funding was directed towards large industrial and infrastructural projects in the belief that there would be a "trickle down" effect through which the poor would benefit. However, this approach only fuelled "dualism", migration and poverty. In the 70s- there was a shift in donor orientation - emphasis on target group orientation which required that development effort should be designed and implemented in such a manner that they would directly benefit the poorer segments of the society. This new orientation resulted into the promotion of special development banks for small farmers and business people. Efforts did not create the desired effect. In the 1980's - a new approach gained prominence-consisted of setting up credit programmes largely outside the banking sector as well as outside the Government. Many NGOs as well as Self- Help groups were set up - (NGOs still dominate the micro-finance landscape to date) (AMFI. 2003).

The demand for Microfinance services continues to grow every day. The formal Microfinance Industry serves about 3 million clients through 3 main segments (NGOS. SACCOS and banks). The banking industry only serves about 10% of the population of people who need financial services. The Microfinance industry serves only a third of the remaining 90%. So the unmet demand for financial services is growing by the day. A significant portion of the demand for microfinance services is accounted for by the MSE sector. The 1999 Baseline Survey estimated that there are 1.2 million MSEs in Kenya (This number has increased tremendously as more people are pushed out of formal employment into the informal sector). The role played by MSEs in the Economic Development of this country is well documented. However, most of them still lack access to financial services. In Kenya, micro-finance has been recognized as one of the most important tools of poverty alleviation. About 60% of the population or 15 million are poor and mostly out of the scope of modern banking services. In this connection extension of financial services for poverty alleviation in Kenya is quite significant. According to the National Baseline Survey of 1999, there are close to 1.3 million micro and small Enterprises (MSEs) employing nearly 2.3 million persons or 29% of the country's total employment and contributing to 18% of overall GDP and 25% of non-agricultural GDP. The informal sector; which is defined to cover all semi-organised and regulated activities that are small-scale in terms of employment, has continued to play a big role on employment creation in the country. The ability of this sector to provide employment for the ever-increasing number of entrants in the labour market including those being pushed out of formal employment is widely acknowledged. Given a shrinking public sector employment and a marked slowdown in overall economic activity, which has occasioned massive retrenchments in the private

sector, the informal sector has provided the greatest opportunities for employment. Though micro-credit has spread throughout the world, in Kenya the sector is still unregulated by the government and its services have reached less than one percent of the Kenyan population, yet the demand for these services is overwhelming (AMFI, 2003).

1.2 Research Problem

In the past Kenya depended on donor funds to give handouts to the poor. This method has however been criticized as creating a "bottom less" pit and dependency syndrome. Donors have demanded sustainable ways to poverty alleviation and micro finance has been identified as the best practice (AHF, 2007).

Most of Kenya's people are poor, and the majority of Kenya's poor are women. Most poor people are self-employed or work in micro and small businesses. Growth in formal sector employment is unlikely to change its slow growth pattern over the next ten years. If poverty is to be reduced and if the economic potential of the majority is to be realized the economic activities of poor people need to be financed (AMFI, 2005).

Micro-credit programs are able to reach the poor at affordable costs and can thus help the poor become self-employed (Concern Worldwide, 1999). Views differ on the role of micro-finance and micro-credit programs. Detractors view such programs as a social liability, consuming scarce resources without significantly affecting long-term outcomes. Critics argue that the small enterprises supported by micro-credit programs have limited growth potential and so have no sustained impact on the poor. Instead, they contend, these programs make the poor economically dependent on the program itself (Bouman and Hospes 1994).

Finance Minister David Mwiraria had this to say in his budget speech (2003), "Mr. speaker Sir, these enterprises cut across all sectors of the economy and provide one of the most prolific sources of employment, not to mention the breeding ground for future businesses and employers. During the last decade when the economy faced serious challenges, this sector became the fastest growing. Today these enterprises are found in every corner of the country and have great potential to create a variety of jobs while generating widespread economic benefits. There is little doubt that a well functioning

policy on micro, small and medium scale enterprises is critical to spreading investments into the rural areas" (Kenya Budget speech, 2003).

Numerous studies have been carried out in this field but they have all focused on different issues. Wanjiru (2000) and Agala-Mulwa (2002) have focused on issues affecting staff productivity and job satisfaction in Micro Finance Institutions. Rukwaro (2001) carried out a survey on credit rationing by Micro Finance Institutions and its influence on the operations of small and micro enterprises. Studies by Kimandi (2002) Mutonyi, (2003) and, Lengewa, (2003) focused on segmentation practices, strategic planning and competitive strategies used by NGO Micro finance institutions. Magiri (2002) studied the relationship between credit models used by Micro Finance Institutions in Kenya and attainment of outreach and Mwindi, (2002) looked at the relationship between interest rates charged by Micro Finance Institutions and performance of Micro and small enterprises in Nairobi. Mokogi (2003) looked at the economic implications of lending of Micro Finance Institutions on MSES. Mudiri (2003) studied credit management techniques applied by financial institutions offering micro credit in Kenya,) and Ndulu, (2003) did a survey of the causes of information systems failure among Micro Finance Institutions in Kenya. Ringeera (2003) studied the implications of commercialization of Micro Finance Institutions on their client outreach in Kenya. The study carried out by Mokogi (2003), Economic implications of lending of Micro Finance Institutions on MSES established that the MSES experienced tremendous growth in their businesses in terms of sales, fixed assets, net income, savings, number of employees and space occupied by the businesses. Though this study established that the living conditions of the respondents had improved, the study concentrated on MSES growth and did not use any parameters to measure the improvement in the standard of living, which would translate to alleviation of poverty. An impact Assessment of the WEDCO Enterprise Development Project, carried out by Maalu et al (1999) gave inconclusive evidence thus creating the need for further research following some of their recommendations. No study to the researchers' knowledge has been carried out in Kenya regarding this problem. This study will be carried out to establish how the micro-finance loan recipients perceive the effect of the loans on their businesses and as a poverty alleviation tool.

1.3 Objectives of the study

To establish:

i) ,The perceived effects of the micro-finance loans by the recipients on their businesses

ii) The perceived effectiveness of micro-finance loans by the recipients as a poverty alleviation tool

iii) How micro-finance loan recipients perceive the effect of interest charges on their businesses.

1.4 The importance of this study

i) The government can use the study to come up with practical poverty reduction strategies. As the Micro Finance sector grows the government has to come up with regulatory frame- work that will safeguard the interests of all the stakeholders.

ii) Development practitioners can use this research to come up with future programmes for the alleviation of poverty and promotion of businesses.

iii) Players in the industry can benefit from this study by justifying their demand for subsidies.

iv) Donors can use the research to justify their stand on sustainability of projects and emphasis on promotion of MFIs.

v) Scholars can use it as a basis for future research and. it will add to the body of knowledge.

CHAPTER TWO

LITERATURE REVIEW

2.1 The Role of Micro-Finance in Poverty Alleviation

Micro finance institutions are set up in order to finance small and micro-enterprises, which are excluded from traditional banking practices. Micro finance is the provision of financial services to low income poor and very poor self-employed individuals. The main objective of MFI's is to alleviate poverty by providing these groups of people with credit facilities that are not available to them through conventional banking institutions (Dondo, 1999).

Micro finance (described here as small scale financial services to clients that are economically active in various urban and rural areas) has been proven to be effective in fighting poverty by providing entrepreneurs with the necessary capital to start and expand their entrepreneurial activities. According to Concern Worldwide Micro-finance Policy (1999), Micro-finance is about providing financial services to the poor who are not served by the conventional formal financial institutions - it is about extending the frontiers of financial service provision. There are two main features of micro-finance that distinguish it from formal financial products - first, the smallness of loans advanced and/or savings collected and second, the absence of asset-based collateral.

The provision of such financial services requires innovative delivery channels and methodologies. Micro-finance is also associated with a positive impact on social and human development. For example, impact assessments have found positive changes in micro-enterprise output, assets, employment and income. In addition to these effects on the entrepreneurial activity of the poor, micro-finance is being attributed with positive effects on issues such as household income, savings, children's education, health and nutrition, and women's empowerment, (Sebstad and Gregory, 1996).

In a phase in the international development endeavour in which ideology is out of fashion, the search is on for practical, workable solutions to the deep-seated challenges of poverty. Micro-credit seems to provide just such a solution. By delivering financial services at a scale, and by mechanisms, appropriate to poor people, micro-credit can reach them. By providing poor people with credit for micro-enterprise it can help them work their own way

out of poverty. And by providing loans rather than grants the micro-credit provider can become sustainable by recycling resources over and over again. In other words micro-credit appears to deliver the 'holy trinity' of outreach, impact and sustainability. No wonder the development sector has become so excited. International debate has been dominated by two schools of thought, which we call the finance school and the poverty school. Sometimes these schools have been in conflict with each other. The former celebrates the mainstreaming of micro-credit as a financial service (BancoSol, a micro-finance bank in Bolivia, has sold certificates of deposit on Wall Street), the latter emphasises the need to reach poor people and may be suspicious of financial sustainability; believing it is likely to lead a micro-finance provider away from its focus on poorer clients. The micro-credit industry has sought to resolve the tensions between a focus on poverty and a commitment to sustainability by integrating them within a matrix defined by two axes, of outreach (or access) and financial sustainability (Mahajan and Ramola, 1996).

In Kenya the poorest of the poor people are caught in an environment and situation from which many of them work hard to escape. Some of them get themselves out of their poverty, but the majority, are still poor, while a large number of others become impoverished. Poverty is constantly being generated and regenerated. The key challenge to the efforts aimed at poverty alleviation is to strengthen the abilities of poor people to build resistance and resilience and facilitate opportunities for escape. Boosting poor people's assets reduces their vulnerability and builds their resilience against poverty. Working towards creating self-sustenance among poor communities through empowering them to, take control of their lives and livelihoods (AHF, Micro-Finance proposal, 1997).

By providing sustainable access to financial services for the working poor, a group which has been previously excluded from affordable sources of credit and savings facilities that are secure, convenient and liquid, micro-finance programmes demonstrate that the poor are creditworthy (ILO, 2000)

The appropriateness of micro-credit as a tool for reducing poverty depends on the local circumstances. Poverty is often the result of low economic growth, high population growth, and extremely unequal distribution of resources. The proximate determinants of poverty are unemployment and the low productivity of the poor. When poverty results from unemployment, reducing poverty requires creating jobs, when poverty results from

low productivity and low income. reducing poverty requires investing in human and physical capital to increase workers' productivity (Khandker, 1998).

The major stumbling block that keeps the rest of the world from benefiting from capitalism is its inability to produce capital. Capital is the force that raises the productivity of labour and creates the wealth of nations. It is the lifeblood of the capitalist system. the foundation of progress. and the one thing that the poor countries of the world cannot seem to produce for themselves, no matter how eagerly their people engage in all the other activities that characterize a capitalist economy (De Soto, 2000). A research carried out by him and his team in Asia, Africa. the Middle East and Latin America. has shown that most of the poor already possess the assets they need to make a success of capitalism. Even in the poorest countries, the poor save. The value of savings among the poor is. in fact. immense: forty times all the foreign aid received throughout the world since 1945. In Egypt, for instance, the wealth that the poor have accumulated is worth fifty-five times as much as the sum of all direct foreign investment ever recorded there. including the Suez Canal and the Aswan Dam (De Soto, 2000).

Proponents of micro-credit consider increasing the poors' access to institutional credit an important means of ending poverty (Yunus. 1983). They argue that by virtue of their design such programs can reach the poor and overcome problems of credit market imperfections. In their view improved access to credit smoothes consumption and eases constraints in production. raising the incomes and productivity of the poor (Khandker R. Shahidur, 1998). Empirical studies support this view to some extent: credit market interventions improve both the consumption and production of the poor who otherwise lack access to credit (Feder and others 1988: Foster 1995: Rosenzweig and Wolpin 1993).

In many countries. such as Kenya. poverty is caused by lack of both physical and human capital. Consequently, the best way to reduce poverty is to deal with both problems: increasing productivity by creating and providing credit seems to be a way to generate self-employment opportunities for the poor. But because the poor lack physical collateral. they have almost no access to institutional credit. Informal lenders play an important role in many low-income countries. but they often charge high interest rates, inhibiting poor rural households from investing in productive income-increasing activities. (Adams and Fitchett 1992; Ghate 1992). Moreover, although informal groups,

such as rotating savings and credit associations can meet the occasional financial needs of rural and urban poor households in many societies, they are not reliable sources of finance for income-generating activities (Webster and Fidler, 1995).

2.1.1 Business Enterprise

The term business means different things to different people. Kibera (2000) says business refers to an economic activity which is primarily organized and directed to manufacture or produce goods and services at a profit.

Business is any economic activity that does not include employment. Such activities are carried out with a view to making financial gain or a profit. The activity must generate some goods or services, which are offered to the society for a gain. You are in business if what you are doing is aimed at making financial gain and that if such gain was missing, you would not continue with the activity (Ncebere, 1999).

Economic profit is the difference between total revenue and total economic cost. Total revenue is measured as sales receipts of a firm, that is, price times quantity sold. The economic activity may be thought as the highest valued alternative opportunity that is forgone. To attract economic resources to some activity, the firm must pay a price for these factors: labour, capital and natural resources that is sufficient to convince the owners of these resources to sacrifice other alternatives and commit the resources to this use (McGuigan, Moyer and Harris, 2002).

Profit itself is the difference between sales revenue and or income (receipts) received after selling goods and services and the costs (expenditure) incurred in producing and selling goods and services. In order to continue making profit a firm must satisfy its varied stakeholders including customers, employees, owners, government and the general public or society (Kibera, 1996). Michael Porter in his (1990) publication argues that national prosperity is created and not inherited. This is true for the nation as it is for a business. The firm secures capital it needs and employs it in activities, which generate returns on invested capital. A business firm thus is an entity that engages in activities to perform the functions of finance, production and marketing (Pandey, 1993)

2.1.2 The Role of Small and Micro-Enterprises (SMEs)

The important roles that small and micro enterprises (SMEs) play in the development of Kenyas' economy has been recognised and documented in a number of studies. A detailed review of the development of SMEs in Kenya is found in King (1996a and b) who identifies and discusses the critical turning points in the history of the sector. SMEs contributions to Kenya's economy have been studied by ILO (1972). McCormick (1988). Parker and Torres (1994). Danieis et al. (1995) and King (1996). Parker and Torres (1994) estimated that out of the roughly 13.000.000 Kenyans of working age in 1993. SMEs provided employment for 16% of the labour force. Daniels et al. (1995) estimated that SMEs created jobs for 100.000 workers in 1994 and 130.000 in the first half of 1995. SMEs provide direct and indirect employment as well as part-time and full-time employment to households in rural and urban areas in Kenya. According to a study by Maalu J. et el 1999: the informal sector provided 64.5% of employment, while the formal sector provided 35.5 % of employment in 1997. The figure for the informal sector has been rising while that of the formal sector has continued to decrease. The informal sector created 458.800 new jobs constituting 94.3 percent of all new jobs created outside small-scale agriculture in 2003. Employment in the modern sector grew by 1.6 percent compared with the growth of 1.3 percent in 2002 (Economic Survey, 2004).

With moderate recovery of the economy, employment outside small-scale farming and pastoralists activities reached 7.338.600 in 2003 from 6.851.600 in 2002. The informal sector created 458.800 new jobs constituting 94.3 percent of all new jobs created outside small-scale agriculture. Self employment and unpaid family workers within modern sector accounted for 0.9 per cent of all jobs. Wage employment in the modern sector grew by 1.6 percent compared with the growth of 1.3 percent in 2002 (Economic Survey. 2004).

There is a lot of emphasis being put on Micro-finance as a tool for poverty alleviation more so because of its ability to recognize dead capital which the poor posses in large quantities (De Soto. 2000).

2.1.3 Measurement of Standard of Living

The concept of 'standard of living' is widely but loosely used by the general public. The most obvious measure is real income per head, total 'real' income divided by the number of population. This tells us the value of goods and services received by the 'average man'. Such figures are published annually by the United Nations. statisticians for all countries

(Columbia Encyclopedia, 2004). Income per head as index of economic welfare: Real income per head is only an index of economic welfare or material well-being. By this we mean if income per head increases, material welfare will increase; but we cannot say by how much it has increased, and certainly that it has increased in proportion. We cannot, in other words measure material welfare of arithmetic scale in the same way as we can measure real income per head (Livingstone and Ord, 1980).

Standard of living has traditionally been measured in terms of a person's ability to attain certain universally recommended basic needs for survival such as food, clothing, health, education and shelter. For example, the human body requires a minimum food-energy intake to maintain bodily functions at rest. In addition, different people require different levels of food energy-intake depending on the types of work they do, or their geographical location. However, food-energy intake alone cannot be a valid welfare indicator because there are some essential non-food goods and services that even the poorest person cannot do without. For example health is essential for most activities, and being healthy requires spending on clothing, shelter and health care (Livingstone and Ord, 1980).

GDP per capita is the total output divided by the total population. Growth in GDP per capita is attained only when the growth of output exceeds population growth (Bradley, 1999).

Total consumption of both food and non-food is therefore considered a better welfare indicator than food-energy intake. Efforts to determine people's well being have therefore concentrated on estimating the aggregate value of all goods and services considered necessary to satisfy an individual's basic needs. The WMS series collects information mainly on household consumption expenditures, which is then analyzed to assess the welfare of households. Although the above approach is widely used as the measure of well being, it should however be noted that it may ignore some peoples' perception (subjective view) of welfare. In an attempt to include the ordinary person's view of who is poor, the government of Kenya has carried out Participatory Poverty Assessments (PPAs) in some districts, which have been used to complement the statistical information from the WMS series (Poverty in Kenya, 2000).

The method adopted by the WMSIII is called the Food Energy Intake (FEI) method. which aims at finding monetary value at which basic needs are met. Such a poverty line only represents the minimum levels of basic needs. below which a decent material lifestyle is not possible series (Poverty in Kenya. 2000). Food poverty line. the FEI method sets the minimum food requirement by finding the consumption expenditure level at which food energy intake is just sufficient to meet pre-determined average food energy requirements for normal bodily functions. The pre-determined food energy requirements recommended by FAO and WHO is; 2,250 calories, per day. per adult person. The Overall poor are defined as those whose expenditure on both food and non food items do not meet the recommended minimum. The Hardcore poor are those who could not afford the minimum recommended food energy requirements even if they devoted their entire incomes to food (Poverty in Kenya, 2000).

The food poverty line for rural areas was estimated at Kshs. 927 per adult equivalent while the line for urban areas was drawn at Kshs. 1.254 per month. The mean non food expenditure for rural areas was estimated at Kshs. 312 per adult equivalent and, that for urban areas at Kshs. 1,394 per month. This resulted in an Overall Poverty Line of Kshs. 1.239 for rural areas and Kshs. 2.348 per month for urban areas. The Hardcore Poverty Line was Kshs. 927 for rural areas and Kshs. 1.254 month for urban areas (Poverty in Kenya. 2000)

Since the WMS series started in 1992. attempts have been made to widen the coverage of the food items consumed by various communities in Kenya. Thus, WMS III gathered more information on food items consumed than did WMSII. Emphasis has been placed on collecting more information about the various non-purchased food items (own-food) consumed by households. It should however be admitted that some own-consumption food items have been left out because of the difficulty of finding their market value. Some Kenyan communities. for example; rely heavily on wild fruits. roots and even fresh blood for food. yet these items have no known market values. These food items could however be providing these communities with the minimum food-energy requirements. While the proportion of communities with these dietary patterns is small. (mainly nomadic communities) there is still need for research into this area to establish the nutritional values of these food items. Food items gathered in WMSIII were grouped into

the following food categories that formed the food basket (Poverty in Kenya. 2000). The breakdown of these grouped food items is contained below:

1. Bread	7. Maize	13. Cereals
2. Meat	8. Fish	14. Milk
3. Eggs	9. Oils and fats	15. Fruits
4. Vegetables	10. Beans	16. Roots
5. Sugar	11. Tea and Coffee	17. Beverages
6. Baby food	12. Other foods	

Composition of Non-Food

The basic non-food items included in the analysis are grouped as follows:

1. Health	5. Non-durables	9. Personal care	13. Clothing
2. Footwear	6. Tobacco	10. Entertainment	14. Transport
3. Transfer	7. Insurance	11. Education	15. House rent
4. Durables	8.Water	12. Fuel	

Monetary Dimensions of Poverty

According to Coudouel et al (2000) the following methods can be used to establish the different dimensions of poverty. When estimating monetary measures of poverty, one may have a choice between using income or consumption as the indicator of well-being. Most analysts argue that provided the information on consumption obtained from a household survey is detailed enough, consumption will be a better indicator for poverty measurement than income for the following reasons: Consumption is a better outcome indicator than income: Actual consumption is more closely related to a person's well-being in the sense of having enough to meet current basic needs. Income is only one of the elements which will allow consumption of goods (others include questions of access, availability, etc.). Consumption may be better measured than income: In poor agrarian economies and in urban economies with large informal sectors, income flows may be erratic and fluctuate during the year. For farmers, one added difficulty in estimating income consists in excluding the inputs purchased for agricultural production from the farmer's revenues. Finally, large shares of income are not monetized if households consume their own production or exchange it for some other goods, and it might be difficult to price these. Estimating consumption has its own difficulties, but it may be more reliable if the

consumption module in the household survey has been well designed (Coulouel et al. 2002).

Consumption may better reflect a household's ability to meet basic needs: Consumption expenditures reflect not only the goods and services that a household can command based on its current income, but also whether that household can access credit markets or household savings at times when current income is low or even negative, due perhaps to seasonal variation or harvest failure. Consumption can therefore provide a better picture of actual standards of living than current income, especially when income fluctuates a lot designed. One should not be dogmatic about the use of consumption data for poverty measurement, however. Using income may have its own advantages, for example, by allowing to; distinguish by income sources when analyzing poverty. When this is available, income can also be compared more easily to data from other sources, such as wages, which provides a check for the quality of the data in the household survey. Finally, in some surveys, consumption or expenditure might simply not be collected (Coulouel et al. 2002).

When both income and consumption are available, the analyst might want to compute poverty measures with both indicators and compare the results. Whether one chooses income or consumption, it is typically necessary to aggregate information provided at the household or individual level for many sources of income or consumption in the survey (Coulouel et al, 2002).

Non-Monetary Dimensions of Poverty

Poverty is associated not only to insufficient income or consumption, but also to insufficient outcomes with respect to health, nutrition and literacy, to deficient social relations, to insecurity, and to low self-confidence and powerlessness. In some cases, it is feasible to apply the tools developed for monetary poverty measurement to non-monetary indicators of well-being. The requirement for being able to apply the tools of poverty measurement to non-monetary indicators is that it must be feasible to compare the value of the non-monetary indicator for a given individual or household to a threshold or "poverty line" under which it can be said that the individual or household is not able to meet its basic needs. A few examples of dimensions of well-being for which the techniques could be used include: Health and nutrition poverty: One could focus on the nutritional status of children as a measure of outcome, as well as on the incidence of specific diseases (diarrhea, malaria,

and respiratory diseases) or life expectancy for different groups within the population. Education poverty: One could use the level of literacy as the defining characteristic, and some level judged as the threshold for illiteracy as the "poverty line". In countries where literacy is close to universal, one might opt for specific test scores in schools or for years of education as the relevant indicators. Composite indices of wealth: An alternative to using a single dimension of poverty could be to combine the information on different aspects of poverty. One might want to create a measure which takes income, health, assets and education into account. It is important to note that a major limitation of composite indices is that it is not possible to define a 'poverty line'. Analysis by quintile or other percentile remains possible, though, and can provide important insights in the profile of poverty (Coulouel et al, 2002).

Subjective perceptions: Such measures of poverty are based on questions to households about one; their perceived situation, such as 'do you have enough?', 'do you consider your income to be very low, rather low, sufficient, rather high, or high?', second: a judgment about minimum standards and needs, such as 'what is the minimum amount necessary for a family of two adults and three children to get by?' or 'what is the minimum necessary for your family?', or third; poverty rankings in the community, such as 'which groups are most vulnerable in the village?'. On the basis of the answers, one can also derive poverty lines. Self-reported measures have important limitations, however. They might reproduce existing discrimination or exclusion patterns, if these patterns are perceived as 'normal' in the society. More generally, the observed perceptions of poverty need not provide a good basis to establish priority public actions. This may be the case if policy makers have a different time horizon and/or a different focus than the population (Coulouel et al, 2002).

2.1.4 Previous Studies on Impact Analysis

Various studies both quantitative and qualitative, document increases in income and assets and decreases in vulnerability of micro finance clients. According to Rhyne (1992) most evaluations of credit programs are based on the old view of causality. They are centered on the presumption of direct line causation between receipt of credit by individual borrowing and a particular desired response for example, changed borrowers' income resulting directly from receipt of a particular loan (Mokogi, 2003).

The impact on credit can be economic, sociopolitical or cultural and personal or psychological. A number of studies have been carried out to ascertain the impact of credit programs on SMEs. Some of the variables that have been investigated are indicators of change on the enterprise are improved or increased production, fixed assets, working capital, inventory, credit availability and its use, level of purchases and sales, net profit, organization of the work place, locale improvement, additions to work place that enhance productive capacity (Otero, 1991).

Impact assessment studies done in Honduras (Tegucigalpa and Choleteca) revealed that 60% and 50% of the recipients had their sales and incomes increase respectively one year after receipt of credit for working capital. The study further revealed that for every enterprise assisted with working capital loan of US$ 820, 0.75 full time jobs were created (CGAP, 2003). The second study in Cholteca-South Honduras revealed that 82% of those surveyed experienced an average sales doubling while 86% recorded an increase in income. The greatest changes were in those who had received six to seven loans, 92% considered that they lived better due to their participation in the program. 50% used the additional income for food, health, education and home improvement (CGAP, 2003).

Mosley (2000) asserted that micro finance makes a considerable contribution to the reduction of poverty. He finds significant increases in incomes and assets of micro finance clients relative to their non-borrowing counterparts. Micro finance allows poor people to protect, diversify, and increase their sources of income; the essential path out poverty and hunger. The ability to borrow a small amount of money to take advantage of a business opportunity, to pay school fees, or to bridge a cash-flow gap can be a first step in breaking the cycle of poverty. Similarly a poor household will use a safe, convenient savings account to accumulate enough cash to buy assets such as; inventory for a small business enterprises, to fix a leaky roof, to pay for health care and to send their children to school (CGAP, 2003). Micro finance also helps safeguard poor households against extreme vulnerability that characterizes their everyday existence. Loans, savings, and insurance help smooth out income fluctuations and maintain consumption levels even during lean periods. The availability of financial services acts as a buffer for sudden emergencies, business risks, seasonal slumps, or events such as a flood or a death in the family that can push a poor family into destitution (CGAP, 2003)

A study of SHARE clients in India documented that three-fourths of clients who participated in the program for longer periods saw significant improvements in their economic well-being (based on sources of income, ownership of productive assets, housing conditions and household dependency ratio) and that half the clients graduated out of poverty. There were marked shift in employment patterns of clients from irregular, low paid daily labour to diversified sources of earnings, increased employment of family members, and a strong reliance on small business. Over half of SHARE clients indicated that they had used their micro enterprise profits to pay for major social events rather than go into debt to meet such obligations (Yunus, 2001).

A study of Grameen Bank also found statistical evidence of economic welfare. The incomes of Grameen Bank members were 43 percent higher than incomes of control groups in non-program villages and 28 percent higher than non-members in Grameen villages. Grameen members were also able to rely more on savings and their own funds to cope with crises rather than borrow from moneylenders. Wage rates in program villages increased (CGAP, 2003).

A comprehensive study on the impact of micro finance conducted by world bank in the early 1990 on three of the largest programs in Bangladesh-Grameen, BRAC and RD-12 found that female clients increased household consumption by 18 Takas borrowed, and 5 percent of clients graduated out of poverty each year by borrowing and participating in micro finance programs. Households were able to sustain these gains over time. There was also spill over effects in the village economy. Average rural household incomes in program, villages increased even for non program households. One of the programs even influenced village wage rates. Increases in self employment and subsequent withdrawals from informal labour pools led to 21 percent increase in wages in the program villages (Abed, 2000).

An impact assessment of WEDCO by Maalu et al (1999) found out from the clients during group discussions that the loans they received were used to increase their stocks and remain in business, earning some income, some of which was spent on household needs such as education, medical care and food. The impact of credit on incomes, profits and employment growth was not significant. The impact of credit on decision making revealed that though a higher proportion of loan 2 and above clients make the final decision with respect to new business activities, borrowing of money, household savings and use of family planning

methods, the differences noted were statistically significant with respect to only decision making on household savings.

A Research carried out by Graham, Deborah, Germina and Leonard on, Vulnerability, Risks, Assets And Empowerment – The Impact Of Microfinance On Poverty Alleviation a case of Uganda Women's Finance Trust, concluded that, "Financial services reduce the vulnerability of poor individuals and households by providing access to "chunks" of money to protect against risk and cope with shocks". Financial services (in the broadest sense of the term to recognise UWFT clients' use of additional formal and informal sector savings systems) help to protect against risk by: providing chunks of money to build assets (financial, physical, human and social assets), providing chunks of money to better manage cash flow and assets, increasing the diversification and development of household assets, offering a place to safely store savings and, increasing women clients' control over assets. In addition, financial services help poor clients cope with shocks by: providing savings or emergency loans to draw upon and building assets that can be sold. it was also reasonably concluded that "Social intermediation combined with financial services contributed to reduced vulnerability and increased empowerment for women clients". This is achieved by: building women's human assets (self esteem, bargaining power, control over decisions, and to a limited extent, skills and knowledge, usually relating to planning and financial management, but sometimes also to business-related information); and increasing women's social assets (social networks, membership of [functionally-useful] groups, relationships of trust, and access to wider institutions of society).

A study by Mokogi (2003) on The Economic Implications Of Lending Of Microfinance Institutions on Micro and Small Enterprises In Kenya established that MSEs that participated in MFI loan schemes achieved tremendous impact. The results showed that the MSEs which participated in these schemes longer and took more loans experienced higher impact in sales, net income, fixed assets, number of employees and space occupied by businesses.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Research Design

Survey method was employed in this study. This method was important for getting information from a broad category of borrowers within Nairobi regarding the effects of loans on their businesses, as a poverty alleviation tool and the adverse effects of interest charged.

3.2 Population

The population frame for the study was all SMEs in Nairobi who had been in any MFI credit scheme for at least 4 years. According to K-REP (1997) most MFIs are concentrated in Nairobi, this factor in addition to time, finances and logistic problems limited the study population within Nairobi. The directory of MFIs produced by K-REP in 1997 lists 61 organisations giving various types of services ranging from credit training to issuance of loans. Kenya Management Assistance Program (K-MAP) lists two more providers of loans to micro small and medium scale enterprises that are not in the list of K-REP. The register of AMFI consists of 11 MFIs, three of which are not on the K-REP list.

3.3 Sampling Design

The sampling frame was developed from the entire population MFIs and all the small and medium enterprises in Nairobi that are funded by them. A sample of 100 loan borrowers was selected from MFI loans beneficiaries who had been in any MFI for a minimum of 4 years. The units of study were selected using systematic random sampling. It was not easy to find respondents who had been in one MFI for four or more years hence the researcher had to visit Micro Finance offices where she was advised where to find the respondents who met the research criteria.

3.4 Data Collection Methods

The study employed primary and secondary data. The primary data was collected through the use of semi-structured and structured questionnaires (see appendix-C). The

drop and pick methods were employed in addition to attending group meetings and requesting those who met our research criteria to fill the questionnaire. Secondary data was used to guide the researcher to the respondents. The secondary data was obtained from relevant literature and the respective MFIs offices

Data Analysis

Data has been presented using tables. Comparative analysis was carried out between the perception of the borrowers before they joined the scheme and four years after joining. A five point scale where 1 was very low and 5 the highest was used. Descriptive statistics enabled the researcher to describe the distribution of the various variables in the study. Mean score and standard deviations were used for comparative analysis. The data has been analysed using descriptive statistics (mode, mean, frequencies and percentages).

CHAPTER FOUR

DATA ANALYSIS AND INTERPRETATIONS

This chapter presents data on the perception of the micro finance loan borrowers on the effects of the loans on their businesses. as a poverty alleviation tool and the adverse effects of interest charged on loans on their businesses. The objectives of the study were to determine the perceived effects of the micro-finance loans by the recipients on their businesses, as a poverty alleviation tool and how micro-finance loan recipients perceive the effects of interest charged on their businesses. Data was collected from the field and was presented. analysed and interpreted under data collection and response rate; Section A: background (general information) of respondents. Section B: Business Enterprise Level. general information and the perception of the effects of loans on their businesses, Section C household level; the perceived effects of the loans as a poverty alleviation tool. Section D the perceived negative effects on their businesses of the interest charged on loans.

4.1 Data Collection and Response Rate

Of the 100 SMEs selected 83 responded but only 77 were analysed; the six rejected did not meet the criteria because they had not been in an MFI credit scheme for over 4 years and 17 did not return the forms. This represented a response rate of 77% which was considered adequate as a basis for deriving conclusions on the study. The reasons for non response included suspicion for theft of business ideas, lack of time and inability to fill the forms due to illiteracy. 100 questionnaires were administered to 100 loan borrowers at their businesses or during their weekly group meetings. The findings and conclusions were based on the 77% response rate.

Table 1: Response Rate of Respondents

	Number	Percentage
Rejected	6	6
Forms not returned	17	17
Received/Accepted	77	77
Total	100	100

Source: Research data

4.2 Background of the micro finance loan borrowers

The background information included the gender, marital status, level of education, training, main occupation and who influenced them into becoming business people or entrepreneurs. The terms entrepreneur and business person are used interchangeably in this research. Out of 77 loan recipients, 48% were men and 52% percent were women. There were more women in business than men but the difference is not significant.

Table 2: Gender and Marital Status

Marital status	Women	Men	Total	Percentage
Married	31	37	68	88
Single	7	0	7	9
Widowed	1	0	1	1
Divorced	1	0	1	1
Total	40	37	77	100

Source: Research data

All male respondents were married. 88% of the respondents were married only 9% were unmarried and these were all women and 1% were widowed and divorced respectively.

Table 3: Level Of Education

Level Attained	Number	Percentage
Ordinary Level	47	61
Standard 7 and 8	16	21
Intermediate College	1	1
University	1	1
High School dropout	7	9
Primary dropout	5	6
	77	100

Source: Research data

Of the respondents interviewed 61% were form four graduates (ordinary level), 16 percent were standard 7 and 8 graduates. 1 percent College and University graduates.

Only 1 out of 77 respondents was a University graduate. If one combines primary and ordinary level graduates they form 82 percent of the total number of those in business.

Table 4: Level of Training

Training	Number	Percentage
Technical	7	9
Craft	6	8
Business certificate	16	21
Diploma	1	1
Degree	1	1
None	30	39
Artisan	16	21
	77	100

Source: Research data

The respondents who did not receive any form of training were 39%, 21% received business certificate training and 21% received artisan training. Those who received training related to the businesses undertaken formed 42% of the population. The diploma and degree courses were in fields not related to the businesses undertaken.

4.2.1 Main Occupation

Most SMEs owners managed their businesses; 96 percent, only 4 percent were employed elsewhere and had employed people to manage their businesses.

Table 5: Main Occupation

Occupation	Number	Percentage
Business	74	96
Employed	3	4
Total	77	100

Source: Research data

When asked if their parents were entrepreneurs 49 percent said yes and 51 percent said no, making the difference not significant, the information is presented in Table 6.

Table 6: Whether Parents/Relatives are Entrepreneurs

Who	Yes	No	Total
Parents	49	51	100
Relatives	81	19	100

n=77

Source: Research data

When asked if any of their relatives were entrepreneurs 81% responded yes and 19 percent responded no, this information is presented in Table 6 above. The results show a significant relationship between relatives being entrepreneurs and the respondents becoming entrepreneurs.

4.2.2 Influence into Business

When asked who influenced them into becoming business people 25 percent said their parents, 10 percent spouses and 16 percent said their relatives as depicted in Table 8. If you consider parents, spouses and relatives to be regarded as relatives then they form 51 percent of the total, which is significant. Only 1% said was influenced by an MFI into becoming an entrepreneur, this is insignificant. Other people who can not be classified as having any relationship with the respondents only accounted for 5% influence which is also not significant.

Table 7: Influence to Business

Who influenced you	Number	Percentage
Spouse	8	10
Self	17	22
Parents	19	25
Relative	12	16
Other	4	5
Friend	16	21
MFI	1	1
Total	77	100

Source: Research data

4.3 Business Enterprise level impact

Data was collected and analysed on the background of the business which included location of business. the name of MFI which has given the business loans, age of the business, location of business, who manages the business and where they got their start up capital, and the perceived state of business before accessing finance from an MFI and 4 years into receiving loans from an MFI. The businesses analysed were those that had been in business for 4 years or more. Businesses are located in different parts of Nairobi 95% of the respondents' businesses are located near where the owners reside only 5% are located elsewhere. Most respondents had received loans from more than one MFI, some were members of more than one MFI.

4.3.1 Source of Start up capital

None of the respondents received start up capital from an MFI or a bank, 93 percent used their own savings and partners. This is can be attributed to the fact that MFI do not lend to startups, they lend to established businesses. Table 8 below shows the main sources of start up capital.

Table 8: The Main Source of starting capital

Source of Capital	Number	Percentage
Own Savings	65	84
Own Savings and partners	7	9
Gift from spouse	2	3
Loan from friend	2	3
Relative	1	1
Loan from MFI/NGO	0	0
Loan from bank	0	0
Others		0
Total	77	100

Source: Research data

4.3.2 Number of loans received

The respondents were also asked to state the number of loans that they had received from an MFI, 78 percent had received more than 4 loans and only, 6 percent had received between one and two loans, 94 percent had received more than 2 loans. The results are presented in Table 9.

Table 9: The Number of loans taken to date

Number of loans taken	Number	Percentage
1 -2	5	6
3-4	12	16
5-6	32	42
7 and above	28	36
Total	**77**	**100**

Source: Research data

4.3.3 Perceived State of business before and 4 years in an MFI scheme

Data was collected and anlaysed to establish the perceived state of business before the loan and 4 years after being in an MFI credit scheme. The respondents were asked to describe their business before they took a loan from an MFI and after. A five point scale where 1 equals very bad and 5 equals very good was used to arrive at the results presented in Table 10. Results have indicated an improvement on average of 19 percent on the 12 business aspects analysed. The highest increase was in the working capital. from a mean score of 3.01 to a mean score of 3.81 after four years in the MFI loan scheme; this represents a change of 27% followed by a change in fixed assets from a mean of 2.83 to a mean of 3.48 representing a change of 23%. The lowest changes were noted in location of business which had 10% change from a mean of 3.04 to a mean of 3.35. Technology also registered a small change of 14%; from a mean of 2.96 to a mean of 3.35.

4.4 Household Level Impact. The effectiveness of Micro Finance Loans a poverty alleviation tool.

The respondents were asked to describe their incomes using a five point scale where 1=very low, 2=rather low. 3=sufficient. 4=high and 5=very high; Reference is made to Table 11 where the results are tabulated. The mean score before the loan was 2.87 and 3.27 after being in the credit scheme for 4 years. This shows an improvement in income after loans of 13.94%. The number of people in the very low and rather low income categories reduced by 100 and 80 percent which appear as -100 and -80 in Table 11 respectively. Respondents in the sufficient and high incomes categories increased by 80 and 25 percent respectively. four years into the credit scheme and no change was registered in

the very high income category.

Table 10 : Perceived effect on the Business after loan from MFI

No	Business Aspect	Mean Score Before	Mean Score After	Difference	Percentage Change
1	Location	3.04	3.35	0.31	10
2	Fixed Assets	2.83	3.48	0.65	23
3	Sales	3.13	3.69	0.56	18
4	Profit	3.01	3.62	0.61	20
5	Employees	2.86	3.25	0.39	14
6	Stock	2.99	3.66	0.67	22
7	Working Capital	3.01	3.81	0.80	27
8	Space Occupied	2.97	3.62	0.65	22
9	Savings	3.04	3.64	0.60	20
10	Technology	2.96	3.35	0.39	13
11	Marketing	3.01	3.68	0.67	22
12	Growth	3.08	3.74	0.66	21
Average		2.99	3.57	0.58	19

n=77

Source: Research data

4.4.2 Economic Class

The respondents were asked to choose an economic class which they belonged to before joining a credit scheme and 4 years of being in an MFI credit scheme. Using a scale where classes 1 was equal to very poor, 2 was equal to poor, 3 was equal to middle class, 4 was equal to high class and 5 was equal to rich; The results presented in Table 12 show that, the mean before the loan was 2.75 and after being in an MFI credit scheme it was 3.09 showing an improvement in the economic class. There was no change in the economic class very poor, respondents in the poor economic class reduced by 85% whereas those in the middle, high and rich classes increased by 20.37 and 300 both respectively.

Table 11: Perceived Income before and after 4 years in a credit scheme

Income	Number Before	Number After	Percentage change
Very low	5	5	-100.00
Rather low	30	6	-80.00
Sufficient	25	45	80.00
High	20	25	25.00
Very high	1	1	0.00
Total	77	77	
Mean before	2.87		
Mean after	3.27		

Source: Research data

Table 12: Economic Class of Respondent before entry into an MFI credit scheme and 4 years after entry

Class	Number Before	Number After	Percentage change
Very poor	1.00	1.00	0.00
Poor	20.00	3.00	-85.00
Middle class	54.00	65.00	20.37
High class	1.00	4.00	300.00
Rich	1.00	4.00	300.00
Total	77.00	77.00	
Mean before	2.75		
Mean after	3.09		

Source: Research data

4.4.3 Changes in Savings

The respondents were asked how their savings had changed compared to four years ago; Table 13 shows changes in savings after 4 years of entry into an MFI credit scheme. 87% percent said their savings had increased. 5 percent said their savings had decreased and

8 percent said there was no change. This shows that the majority (87%) of the respondents thought their savings had increased.

Table 13: Change in Savings

Change	Number	Percentage
Increased	67	87
Decreased	4	5
No Change	6	8
Total	77	100

Source: Research data

4.4.4 State of Overall life

The respondents were also asked, taking into consideration all aspects of their lives how they would describe their lives after the loan. Table 15 shows that 81 percent of the respondents thought their lives had become better. 9 percent thought their lives had become worse after the loan and 6 percent said there was no change while 4 percent were not sure.

Table 14: State of overall Life

No	Change	Number	Percentage
1	Better	62	81
2	Worse	7	9
3	No Change	5	6
4	Not sure	3	4
5	Others	0	0
	Total	77	100

Source: Research data

4.4.5 Perceived State of welfare before and 4 years into an MFI Credit Scheme

The respondents were asked to describe how they perceived their welfare before they took a loan from the MFI and after. Data was collected and analysed and presented in Table 15. Different parameters were used to describe the different aspects which are widely used in the measurement of poverty. The largest positive change was seen in

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leisure goods with a mean difference of 0.86 which represents a percentage increase of 29% followed by schools for dependants and entertainment with an increase of 0.84 and 0.83 which represents an increase of 28% each respectively. The lowest changes were witnessed under health and decision making both with a mean of .49 and 0.51 which represents a percentage change of 15% for both.

Table 15 : Perceived Welfare Aspect before and after 4 years into an MFI Credit Scheme

No	Welfare Aspect	Mean Score Before	Mean Score After	Difference	Percentage Change
1	Diet	3.08	3.79	0.71	23
2	Clothing	3.17	3.91	0.74	23
3	Schools for dependants	3.00	3.84	0.84	28
4	Housing	3.13	3.86	0.73	23
5	Water and sanitation	3.10	3.82	0.72	23
6	Home Furniture	3.14	3.78	0.64	20
7	Friends	3.16	3.82	0.66	21
8	Health	3.30	3.79	0.49	15
9	Marital life	3.27	3.91	0.64	20
10	Relationship with others	3.16	3.74	0.58	18
11	Leisure goods	2.92	3.78	0.86	29
12	Entertainment	3.01	3.84	0.83	28
13	Social Status	3.18	3.95	0.77	24
14	Decision making	3.32	3.83	0.51	15
	Average	3.14	3.83	0.69	22

n=77
Source: Research data

4.5 The Perceived adverse effects by the borrowers on their businesses' of interest charged on MFI loans

The respondents were asked if the interest charged on the loans had any adverse effects on the different business parameters. Data was collected and analysed and the results show that the effect is not significant as evidenced by the mean and standard deviation depicted in Table 16. The highest mean scores were in growth at 2.58, savings at 2.55 and working capital at 2.53 and standard deviations of 0.0492, 0.0456

and 0.0433 which means that the adverse effects of interest charged are greatest on the three parameters. The lowest means were seen in location 2.21 and fixed assets 2.34 which had the lowest standard deviations of 0.0059 and 0.0211 respectively..

Table 16: The perceived adverse effect on Business of interest charged on loans

No	Business Aspect	Mean Score	Standard Deviation
1	Location	2.21	0.0059
2	Fixed Assets	2.34	0.0211
3	Sales	2.49	0.0386
4	Profit	2.51	0.0410
5	Employees	2.44	0.0328
6	Stock	2.48	0.0375
7	Working Capital	2.53	0.0433
8	Space Occupied	2.49	0.0386
9	Savings	2.55	0.0456
10	Technology	2.47	0.0363
11	Marketing	2.45	0.0339
12	Growth	2.58	0.0492
Average		2.16	0.0000

n=73

Source: Research data

CHAPTER FIVE

CONCLUSION

5.1 Summary, Discussions and Conclusions

The study sought to determine; one, the perceived effects of MFI loans on the borrowers businesses, two, the perceived effectiveness of MFI loans as a poverty alleviation tool and three, to establish the adverse effects of interest charged on loans on the borrowers businesses.

The study established that only one out of the 77 respondents was a University graduate, the rest were either form four graduates, standard seven or eight graduates or some had not been to school. In the past the informal sector has been the preserve of the less educated. Those who went to school sought white color jobs (formal employment). This notion is fast changing due to a paradigm shift which has been necessitated by the dwindling formal job market leading to the expansion of the informal sector. More and more people are venturing into the informal sector, both educated and uneducated.

Regarding the perceived effects of MFI loans on the respondents businesses, the study established that though the borrowers perceive the loans to have improved their businesses, they did not perceive their businesses to have been in a bad state before getting loans from an MFI. The mean of all parameters examined before entry into a credit scheme was 2.99 out of a total of 5 and the mean after entry was 3.57 out of the same total; an increase of 0.58 which translates to a 19% increase after being in the credit scheme for 4 years. Though there is a perceived improvement in the state of business after entry into an MFI credit scheme, the study established that out of the 77 respondents, none had received any money from an MFI to set up their businesses. 84% used their personal savings, while 9% got from their partners and 3% from either spouse or friend. The conclusion therefore is that MFI lend to already existing businesses and not start-ups, though the loans do improve the businesses in all the aspects examined.

On the perceived effectiveness of MFI loans as a poverty alleviation tool; the study established that there was an improvement in welfare, though majority of the borrowers did not regard themselves as poor before taking Micro Finance Loans. The fact that the respondents were not poor is depicted by a mean of 2.75 when asked to place themselves in economic classes using a five point scale where 1 was equal to very poor and 5 was equal to rich. The same explanation can be drawn from the results of a question on income; when asked how they perceived their incomes before taking an MFI loan using five point scale where 1 was equal to very low and 5 was equal to very high, a mean of 2.87 was realized. The results show that the respondents' incomes were neither very low nor very high; they had more than sufficient income and hence past the middle class. 78 percent used their savings to set up their businesses, further proving the fact that the MFI borrowers were indeed not poor given the different definitions of poverty. The study established that the borrowers perceived their general welfare to have improved as a result of loans received from MFI. The study concludes that the loans advanced help in improving the businesses, increasing savings and improving the welfare of the borrower in the borrowers' perspective.

The study also sought to establish whether interest charged on the loans advanced by MFIs had adverse effects on the respondents businesses. The study established that the interest charged on MFI loans was not perceived to have significant adverse effects on the businesses. The study further concludes that though Micro Finance loans improved the welfare and state of business according to the perception of the borrowers, there is need to come up with stratified products that would address the needs of different social classes because the people served by MFI are not poor. MFI lend to people who have saved and have existing businesses, the claim that they are alleviating poverty does not hold water.

5.2 Limitations of the Study

It was difficult to get MFI borrowers who had been in one MFI for 4 or more years. Most borrowers had moved from one MFI to another for one reason or another and, some were even in more than one MFI. The level of literacy of most borrowers was low thus making it necessary to translate the questionnaires to languages most preferred by the respondents. The respondents being business people were very time

pressed making data collection difficult and in some cases expensive. Due to lack of time some respondents were unable to return the questionnaires and due to limited education some respondents were very suspicious that their business secrets would be stolen. making it necessary for those administering the questionnaires to explain at length the objectives of the study.

5.3 Suggestions for further Research

A study should be carried out where all respondents have no savings or businesses before joining an MFI credit scheme. The study should take baseline data on the different parameters that would measure poverty levels and business growth before entry and 4 years into the scheme. The businesses should also be monitored from start to 4 years into the business. A study should also be carried out to study the effects of interest charged on loans advanced by MFI; comparative analysis should be carried out, where a control group that is not charged any interest on loan advanced or a much lower interest and one that is charged the normal interest charged by MFIs are monitored on the different business growth parameters over a period of time in order to compare the progress.

5.4 Recommendations for Policy and Practice

The study recommends that any MFIs which has alleviation of poverty as its vision. lends to startups so that the welfare of the borrower and business can be monitored; before and after loans over a successive period of time; 4years and over. Though the interest charged is not perceived to have significant adverse effects on the businesses MFI's should consider lowering the interest charged and instead look for ways of operating efficiently and effectively. The government should work with MFI in financing the poor members of the society by providing the savings needed by the MFI in order to enable MFI give loans and training to the poor to start businesses without compromising the existence of MFIs.

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APPENDICES

Appendix A: List of Micro Finance Institutions Offering Credit

1. Kenya Rural Enterprise Programmes- (K-REP)
2. Kenya Women Finance Trust
3. Faulu Kenya
4. Pride Africa
5. Young Women Christian Association (YWCA)
6. Jitegemee Trust
7. Hope Africa
8. Sunlink Micro Finance
9. The Cooperative Bank of Kenya
10. Post Bank
11. Ecumenical Church Loan Fund (ECLOF)
12. Small and Micro-Enterprise Programmes (SMEP)
13. Action Aid
14. Dandora Catholic Church-Welfare Advisory Services
15. Archdioceses of Nairobi
16. ADRA Kenya
17. Vintage Management Consultants
18. Kenya Commercial Bank-Special Loans Unit
19. United Disabled Persons of Kenya (UDPK)
20. Kenya Small Traders and Enterprise Society
21. Private Sector Development Unit
22. St. Johns Community Centre
23. Undugu Society of Kenya
24. Family Finance
25. Trio Caire
26. Small Enterprises Credit Association
27. World Vision
28. Daraja Trust
29. Christian Health Association of Kenya
30. Skills Across Kenya

31. Care International
32. Smallholder Irrigation Scheme Development Organisation (SISDO)
33. KADET
34. Dan Church Aid
35. Equity Building Society
36. WEDCO
37. Ghetto Child Programme
38. Jamii Bora
39. AREP

Appendix B: Introductory Letter

Flora M. Maghanga-Mtuweta.
C/O MBA Office.
Faculty of Commerce,
University Of Nairobi.
P.O Box 30197
NAIROBI
October 2005

Head of Micro Finance,

Dear Sir/Madam.

RE: MANAGEMENT RESEARCH PROJECT

I am a postgraduate student in the faculty of Commerce. University of Nairobi. pursuing a Masters in Business Administration degree. I am undertaking a Management Research Project in the Micro Finance Sector titled: "The Perception of Micro Finance Loan Borrowers in Nairobi on the effects of loans on their Businesses and as a Poverty Alleviation Tool". Your clients have been selected in the study.

I am therefore kindly requesting you to grant me permission to interview your clients. The information will be treated with utmost confidentiality and will be used only for academic purposes. The final copy of this study will be presented to you.

For any clarification you can contact my supervisor. Dr. Martin Ogutu. who is the Chairman Business Management Department. Kabete. Your assistance and consideration will be greatly appreciated. Thank you.

Yours sincerely,

Flora M. Maghanga-Mtuweta
MBA Student-UON

Appendix C: Questionnaire

A. Personal Details of Respondent

1. Full Name:...
2. Sex 1. Male (   ) 2. Female (   )
3. Marital Status 1. .Married (   ) 2. Single (   ) 3. Divorced (   ) 4. Widowed (   )
4. Position in the household 1. Head (   ) 2. Spouse (   ) 3. Other household member (   )
5. Your age in complete years ________________
6. Highest level of Education ________________
7. Spouse's highest level of education___________
8. Training completed (Tick appropriately)

   Technical 1. Artisan (   ) 2. Craft (   ) 3. Technician (   )

   Business Certificate (   ), Diploma (   ), Degree (   )

   None (   )

9. Main occupation of the respondent..
10. Spouse's main occupation..
11. Number of children..
12. Number of regular dependant..
13. If married, does spouse reside within? 1. Yes (   ) 2. No (   )
14. Were your parents entrepreneurs/or Business people 1.Yes (   ) 2.No (   )
15. Were any of your relatives entrepreneurs/or Business people 1.Yes (   ) 2.No (   )
16. Who influenced you in becoming an entrepreneur/or Business person..................

B Enterprise Level Impact

1) Name of MFI……………………………………………………..

2) Location of the enterprise…………………………………………

3) Name of loan group………………………………………………

4) When did you join the loan group?………………………………

5) Age of the main business………………………………………..

1. Less than 4yrs ( )
2. Over 4yrs ( )

6) Who manages the business/enterprise

a. Self ( ) b. Spouse ( ) c. Paid worker ( ) d. Others ( )

7) What was your main source of starting capital tick in as appropriate

1. Own savings ( ) 2. Savings and partners ( ) 3. Gift from spouse ( ) 4.Loan from friend( )
5. Relative ( ) 6.Loan from NGO/MFI ( ) 6.Loan from bank( )
7. Others (specify)

8) How would you describe your business before you took a loan from an MFI.

Use a 5 point scale where 1 equals not bad and 5 Very Good

1=very bad

2=bad

3=okay

4=good

5=very good

Item

iv. Profit ( )

v. Employees ( )

vi. Stock ( )

vii. Working capital ( )

viii. Space occupied by business ( )

ix. Savings ( )

x. Technology used ( )

xi. Marketing ( )

xii. Growth ( )

9) How would you describe your business 4 years after you took a loan from an MFI. Use a 5 point scale where 1 equals not bad and 5 Very Good

1=very bad

2=bad

3=okay

4=good

5=very good

Item

iv. Profit ( )

v. Employees ( )

vi. Stock ( )

vii. Working capital ( )

viii. Space occupied by business ( )

ix. Savings ( )

x. Technology used ( )

xi. Marketing

xii. Growth

C Household Level Impact

1) How would you describe your income before you took the loan

1) Very low ( )
2) Rather Low ( )
3) Sufficient ( )
4) High ( )

2. How would you describe your income after you took the loan

1) Very low ( )
2) Rather Low ( )
3) Sufficient ( )
4) High ( )

3. In which class below would you place yourself before you took your loan from the MFI

1) Poor ( )
2) Middle income ( )
3) High income ( )
4) Rich ( )

4. In which class below would you place yourself after you took your loan from the MFI

1) Poor ( )
2) Middle income ( )
3) High income ( )
4) Rich ( )

5. How have yours savings changed compared to five years ago? Tick where appropriate

1. Increased ( ) 2. Decreased ( ) 3. No Change ( )

6. Overall (taking into consideration income, free time, health, diet and housing and all the parameters mentioned below) how has your life been?

Tick where applicable.
1. Better ( ) 2. Worse ( ) 3. No change ( ) 4. Not sure ( ) 5. Others ( )
Specify............

7. How would you describe your welfare in the different aspects below before you took a loan from an MFI.

1=very bad

2=bad

3=okay

4=good

5=very good

Item	**Scale**
i. Diet	( )
ii. Clothing	( )
iii. Schools for dependants	( )
iv. Housing	( )
v. Water and sanitation	( )
vi. Home furniture	( )
vii. Friends	( )
viii. Health	( )
ix. Marital life	( )
x. Relationship with others	( )
xi. Entertainment	( )
xii. Leisure goods	( )
xiii. Social status	( )
xiv. Decision making	( )

8. How would you describe your welfare in the different aspects below 4 years after you took the loan

1=very bad

2=bad

3=okay

4=good

5=very good

Item	Scale
i. Diet	( )
ii. Clothing	( )
iii. Schools for dependants	( )
iv. Housing	( )
v. Water and sanitation	( )
vi. Home furniture	( )
vii. Friends	( )
viii. Health	( )
ix. Marital life	( )
x. Relationship with others	( )
xi. Entertainment	( )
xii. Leisure goods	( )
xiii. Social status	( )
xiv. Decision making	( )

D Effect of Interest Charge

1. To What extent do you consider the interest charged to have affected negatively the different aspects of your business.

1=not at all
2=to a small extent
3= to some extent
4=to a great extent
5=very great extent

Item	Scale
i. Location of business	( )
ii. Fixed assets	( )
iii. Sales	( )
iv. Profit	( )
v. Employees	( )
vi. Stock	( )
vii. Working capital	( )
viii. Space occupied by business	( )
ix. Savings	( )
x. Technology used	( )
xi. Marketing	( )
xii. Growth	( )