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LEVEL OF ACCESS TO FINANCIAL PRODUCTS AND SERVICES FOR SMALL AND MEDIUM ENTERPRISES IN KENYA.

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Abstract

Purpose: The purpose of this study was to highlight the level of access to financial products and services for small and medium enterprises in Kenya

Methodology:The research design was descriptive survey study. The target population was 46 commercial banks .The sampling frame was the list of commercial banks given at the Central bank of Kenya Website. A sample of 17 banks was selected using random sampling. The second stage of sampling involved the selection of the respondents using a stratified sampling approach. The strata were the various departments that interact with SMEs in a bank. The respondents were the head of departments of the respective departments that form the strata. Both qualitative and quantitative data was collected using a questionnaire that consisted of both open ended and close ended questions. Data was analysed using Statistical Package for Social Sciences (SPSS.

Results: The study objectives were to establish the level of access to financial products and services offered by the banks to SMEs. Results from the bank manager's perspective indicated that the level of access to finance was high, but the bank clients indicated otherwise, that it was low. The other objective of the study was to determine the factors that hinder the SMEs from accessing the financial products offered by banks. Results indicated that several factors influence access of SMEs to finance. These factors include gender, level of education, size of the business, age of the entrepreneur, collateral, and level of income for the entrepreneurs. All the factors had a negative effect on the access of finances from the banks by SMEs and hence indicate SMEs low access to financial products. Results also indicated that there are tools and systems put in place by banks to improve accessibility to financial products offered to small and medium enterprises.

Unique contribution to theory, practice and policy:The study recommended that training be emphasized to SME entrepreneurs on financial matters, all gender to be treated equally, the banks to introduce financial education programs for SMEs to improve their access to credit, banks to further make use of a credit scoring system to assess the credit worthiness of small businesses and to introduce the use of new credit bureau regulations to increase SME finances.

Keywords:*financial products,small and medium enterprise*

1.0 INTRODUCTION

1.1 Background to the Problem

Previous research, on access to financial products and services for SMEs has identified various challenges that SMES face in accessing finance (Kapilla, 2006; OECD, 2004; IFC Kenya Country Study, 2005). These challenges stem from the perception that financial institutions have of SMEs. SMEs are perceived to be financially more risky, as reflected in their relatively high debt equity ratio and in their higher failure rates (Cressy & Christer, 1997).

The Kenya Government's Economic Recovery Strategy (ERS) has identified access to financial services as one means of creating employment, promoting growth and reducing poverty in the country (Government of the Republic of Kenya, 2008). Overall policy responsibility for supporting SMEs vests with the Ministry of Labour and Human Resource Development and in particular, the Department of Micro and Small Enterprise Development (DMSED). DMSED segments the following business population by employment size: Micro sized business – Up to 5 employees; Small sized business – 5 to 50 employees; Medium sized business – 50 to 150 employees and large business – More than 150 employees (Atterton, 2008).

The IFC Kenya Country Study (2005) estimated approximately 87% of SMEs have debt financing for up to 50% of the total capital employed, with owners being the highest contributors of both debt and equity capital. The study estimates that 66% of all SMEs have applied for a loan facility with banks. Most of the loan applications are in the form of the overdrafts, term loans and for purchase of motor vehicles. Of the SMEs that applied for the loan facilities, 87% had their loan requests granted with only 13% having their requests declined and the vast majority of the rejection being due to lack of sufficient collateral.

Whereas 66% of the SMEs have attempted to borrow, 82% of the SMEs need additional finance but are reluctant to do so because of the current interest rates and the cost of finance. Costs notwithstanding, a large number (over 80%) of SMEs would like financing of up to KShs 20 million for working capital and investment purposes (Mantle Ltd, 2005). The IFC study also identified significant potential demand for providing working capital and asset based financing to expand operations. Kenyan banks need to become more innovative and aggressive in the formal SME market as opportunities to generate returns from securities and consumer lending.

Forty percent of the Kenyan respondents have (or have had in the past) experience of formal or informal credit or loan services (not including borrowings from family and friends) and 20.6% of the respondents were self-employed in the business sector. Of those that currently had credit (31.7%) the majority used informal arrangements with shops or suppliers (74.2%). The proportion accessing formal personal or business loans from a bank was only 5.7% (FSD Kenya, 2007).

There are approximately 130 micro-credit organizations recorded by the Central Bureau of Statistics, 4000 Savings and Credit Co-operative Societies (SACCOs) across the country and

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perhaps, as many as one million Rotating and Accumulating Savings and Credit Associations (ROSCAs and ASCAs). Primarily, these organizations provide goods or capital to their members for starting or enhancing businesses. They face major hurdles in their operations including: Lack of capacity to track and recover loans; a lack of coordination; a lack of commitment from the borrowers; the use of counterfeit documentation as collateral; and the lack of supportive judicial system and effective documentation of property rights (OECD, 2004).Therefore, they are unlikely to become a vehicle for unlocking the intrinsic economic potential of Kenya's SME sector.

1.2 Statement of the Problem

Small businesses are the backbone of most developing and developed economies. They outnumber large companies and they employ the majority of the working population in Kenya. SMEs need finance in order to grow (Kapilla 2006).However; small businesses in developing countries such as Kenya seem to be off the mainstream financial radar screens. The financing gap for the middle segment is often called the "Missing Middle" (Sanders and Wegener, 2006).SME finance is referred to as the "missing middle" because SME financial requirements are too great for most MFIs and SMEs have been viewed as too small, risky, or costly for traditional commercial banks (International Finance Corporation, 2009). Studies such as Kumar and Francisco (2006), Levine (2004), Pandula (2011) have pointed out that SMES face constraints when accessing credit.

In addition, studies have shown that there exist various factors that affect SME access to credit. For instance, Storey (2004) conducted a study on racial and gender discrimination in the micro firm's credit market and demonstrated evidence from Trinidad and Tobago. The study was built upon human capital theory and specifically looked at education, age, work experience and social background of the owner when accessing credit from banks. Traditional sources of corporate business development are not available to small and medium businesses. Therefore, small and medium enterprises are financed by imperfect markets which include segments of debt and equity markets. These imperfections in the financial markets are as result of (1) financial and regulatory entry barriers to some traditional corporate financial markets and (2) size and economic characteristics of the demandants for business financing (Walker, 1989). Another study by Whincop (2001) attempted to assess how the entrepreneurial financial gap can be bridged and therefore investigated the firm characteristics such as size, age of the business, legal status and financial characteristics such as profit, fixed assets base. This indicates that the proper conceptualization of the factors affecting the use or access of bank credit by SMEs should at least take into consideration three types of characteristics namely; entrepreneur characteristics, firm characteristics and financial characteristics.

Studies have also indicated that the access to credit by women and the performance of women SMEs significantly differs from that of men. McComick (2001) noted that there is a difference in performances of women vs. men in enterprise. He especially noted that women enterprises area smaller, less profitable and begins with less capital than those owned by men. The author concludes that gendered patterns of business operations are supported by five institutions -the incorporation of the wife into the husband's family, the division of labour within the household, the division of asset ownership (the tradition that vests ownership of land in males remains strong, even though women now can purchase and inherit land), the sharing of household expenditures, and the allocation of educational opportunities. Flestcner and Kenney (2011) also assert that context-specific legal rights, social norms, family responsibilities and women's access to and control over other resources shape their need for capital and their ability to obtain it.

A more comprehensive conceptualization of factors that affect SME access to finance was therefore necessary because earlier studies (Whincop (2001), Pandula (2011), Levine (2004), Kumar and Fransico (2006), Storey (2004) have tended to concentrate on a three factor frame work (entrepreneurial factors, firm factors and financial factors). Previous studies used either the three factor frame work or the gender factor in the investigation of factors that affect the SME financial access. Consequently this study sought to address the three factors and an additional fourth factor which relates to gender mainstreaming of financial access for establishing the factors that affect the access of finance by SMEs(McComick (2001),Flestcner and Kenney (2011).

1.3 Research Questions

1.3.1: What is the level of access to appropriate financial products and services offered by banks to SMEs?
1.3.2: What factors hinder the SMEs from accessing the financial products offered by banks?
1.3.3: What tools or systems are required to improve accessibility to financial products offered by banks to small and medium enterprises?

2.0 LITERATURE REVIEW

2.1 Level of Access to Financial Products and Services

Providing access to a broad range of financial products and services for SMEs has gained prominence in the past few years as a policy objective for national policymakers, multilateral institutions, and others in the development field (Beck et al, 2007). Financial institutions offer four types of financial products which include deposit products, transaction and other products, financing products and lastly advisory products.

3.0 RESEARCH METHODOLOGY

The research design was descriptive survey study. The target population was 46 commercial banks .The sampling frame was the list of commercial banks given at the Central bank of Kenya Website. A sample of 17 banks was selected using random sampling. The second stage of sampling involved the selection of the respondents using a stratified sampling approach. The strata were the various departments that interact with SMEs in a bank. The respondents were the head of departments of the respective departments that form the strata. Both qualitative and quantitative data was collected using a questionnaire that consisted of both open ended and close ended questions. Data was analyzed using Statistical Package for Social Sciences (SPSS.

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4.0 RESULTS AND DISCUSSIONS

4.1: Level of Access to Financial Products and Services.

4.1.1 Products Availed

The respondents were asked if the organization provides deposit products such as current accounts and savings accounts to SMES. A majority (46%) strongly agreed while another 44% agreed bringing to a total of (90%) of those who agreed. Ten per cent were neutral and none agreed and strongly agreed. The results are presented in table 1.

Table 1: Level of Access to Credit

Scale	Distribution	
	frequency	Per cent
Strongly Disagree	0	0%
Disagree	0	0%
Neither agree nor disagree	7	10%
Agree	30	44%
Strongly Agree	31	46%
Total	68	100%

4.1.2 Trade finance Products

The respondents were asked whether the organization provided trade finance products such as letter of credits to SMEs. A majority (84%) agreed while another 16% strongly agreed bringing to a total of 100% of those who agreed. The results are presented in table 2

Table 2: Trade Finance Products

Scale	Distribution	
	frequency	Per cent
Strongly Disagree	0	0%
Disagree	0	0%
Neither agree nor disagree	0	0%
Agree	57	84%
Strongly Agree	11	16%
Total	68	100%

4.2 Factors hindering Small Medium Enterprises Access to financial products and Services.

4.2.1 Lack of Credit Worthiness Information

The respondents were asked whether the lack of credit worthiness information about SMES is a factor that limits most types of lending. A majority (50%) agreed while another 41% strongly agreed bringing to a total of 91% of those who agreed. However, only 9% respondents who were neutral. The results are presented in table 3

Table 3: Factors Hindering Access to Credit

Scale	Distribution	
	frequency	Per cent
Strongly Disagree	0	0%
Disagree	0	0%
Neither agree nor disagree	6	9%
Agree	34	50%
Strongly Agree	28	41%
Total	68	100%

4.2.2 Lack of Business Information

The respondents were asked whether the lack of credit worthiness information about SMES is a factor that limits most types of lending. A majority (50%) agreed while another 41% strongly agreed bringing to a total of 91% of those who agreed. However, only 9% respondents who were neutral. The results are presented in table 3.

Table 4: Lack of Business Information

Scale	Distribution	
	frequency	Per cent
Strongly Disagree	0	0%
Disagree	8	12%
Neither agree nor disagree	9	13%
Agree	26	38%
Strongly Agree	25	37%
Total	68	100%

4.3 Tools or Systems that Improve Small Medium Enterprise Finance

4.3.1 Credit Bureau Regulations

When the respondents were asked if the organization views the new credit bureau regulations as a positive step in increasing SME finance, a majority 63% agreed while 37% strongly agreed bringing to a total of 100% of those who agreed. Table 5 indicates these results.

Table 5; Credit bureau Regulations

Scale	Distribution	
	frequency	Per cent
Strongly Disagree	0	0%

Scale	Distribution	
	frequency	Per cent
Disagree	0	0%
Neither agree nor disagree	0	0%
Agree	43	63%
Strongly Agree	25	37%
Total	68	100%

4.3.2 Credit Scoring System

When the respondents were asked if the use of a credit scoring system is a positive step to assess the credit worthiness of small businesses, a majority 69% agreed while 24% strongly agreed bringing to a total of 93% of those who agreed. However, 6% were neutral and only 1% respondents disagreed with the statement. Table 6 indicates these results.

Table 6: Credit Scoring System

Scale	Distribution	
	frequency	Per cent
Strongly Disagree	0	0%
Disagree	1	1%
Neither agree nor disagree	4	6%
Agree	47	69%
Strongly Agree	16	24%
Total	68	100%

5.0 DISCUSSION CONCLUSIONS AND RECOMMENDATIONS

5.1: Summary of Findings

The general objective of this study was to investigate the factors affecting access to finance and establish tools or systems required to improve accessibility to financial products offered by banks to small and medium enterprises in Kenya. The specific objectives of this study were to establish the level of access to financial products and services, to determine factors hindering SMEs access to financial products offered by banks, and to establish tools or systems required to improve accessibility to financial products offered by banks to small and medium enterprises.

The research used a total population of sixty eight bank managers and sixty eight bank clients as the sample size for the study. For purposes of collecting primary data, the use of a questionnaire developed by the researcher was used and their results analysed using various statistical methods such as graphs, charts and with the aid of Microsoft Excel.

Study findings indicated that most of the bank managers (69%) of the respondents were male and (31%) were female. A majority (60%) of respondents were aged between 31-50 years, followed by (21%) respondents who aged between 18 to 30 years. Majority (41%) of the respondents were university graduates. The finding implies that the respondents of the study were mature and probably ready to retire in the next decade. A majority 62% of the respondents indicated they were trained on financial matters.

Results indicated that banks offered different types of financial products such as deposit products, trade finance products, and advisory services to their clients. This is evidenced by the majority of respondents who indicated they strongly agree and agreed. Results also indicated that several factors hindered SMEs from accessing financial products such as lack of collateral, lack of borrower's honesty and trustworthiness. This is evidenced by the majority of respondents who indicated that they strongly agreed and agreed it was not easy for SMEs to access credit from banks. In addition, the bank implemented tools or systems that would improve SMEs access to finance since the majority of the respondents indicated that the systems would give entrepreneurs financial education program to improve their access.

Study findings further indicated that most of the bank clients (66%) of the respondents were male and (34%) were female. A majority (44%) of respondents were aged between 31-50 years, followed by (35%) respondents who aged between 18 to 30 years. A majority (59%) of the respondents was single and 41% were married. Majority (35%) of the respondents were university graduates and a further same percentage indicated they had secondary certificates. The finding implies that the respondents of the study were mature and probably ready to retire in the next decade. A majority 71% of the respondents indicated they were not trained on financial matters. Forty four per cent of the respondents indicated that their businesses were in existence for less than one year. Majority 50% of the respondents indicated that they had no employees.

Results indicated that gender was one of the factors that influence access to credit. This is evidenced by the majority of respondents who indicated they strongly disagreed and disagreed with the statements that stated they had access and control over the household assets and resources such as land, they had adequate access to information about financial and investment opportunities.

Results also indicated that SMEs had a low access to financial products as it was evidenced by the majority of respondents who indicated that they disagreed they were always willing to approach a bank for financing, their application rarely got rejected, they were always awarded loan which was adequate for their businesses.

5.2 Conclusion.

5.2.1 Level of Access to Financial Products and services

It was possible to infer from this study that there was low access to credit from banks by SMEs. In particular, the bank managers indicated that their organization provides deposit products such as current accounts and savings accounts to SMES, their organization provides trade finance products such as letter of credits to SMES. The findings agree with those in international Finance Corporation, (2009) who asserted that financial institutions offer four types of financial products which include deposit products, transaction and other products, financing products and advisory products.

It is also possible to conclude that the banks provided finance products such as overdraft, credit cards, leasing, cheque discounting to SMEs. The findings are in line with those in Beck, Demirguc-Kunt, Martinez Peria, (2007) who asserted that financing products include loans of various types, lines of credit, overdraft, credit cards, leasing, cheque discounting, foreign trade financing, various insurance products, letters of credit and factoring.

From the study findings of the managers, it was possible to conclude that their organization provided advisory services to SMES such as training on how to produce reliable financial statements and development of good business plans and offered advices to SMES on how to select appropriate financing products.

5.3 Recommendations

5.3.1 Recommendations for Improvement.

Level of Access to Financial Products and services

Following study results, it is recommended that training be emphasized to SMEs entrepreneurs on financial matters as it influences access to finance. Therefore the banks are urged to introduce financial advisory services such as training on how to produce reliable financial statements and development of good business plans, offer advice to SMEs on how to select appropriate financing products.

5.4 Recommendations for Further Studies

The study recommends further studies on the access of informal credit by SMEs. Such as study should focus on the factors that influence the access of small firms from microfinance institutions, merry go rounds and SACCOs. Future studies should also focus on the financial management practices of small firms. This is because the proper working capital management may influence the growth, profitability and the consequent ability to access finance from all sources.

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