

**THE EFFECT OF MICRO FINANCIAL INSTITUTIONS ON THE GROWTH
OF SMES IN KITUI COUNTY**

BY


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DECLARATION


This project is my original work and has not been presented in other University or any other institution for an award of degree or any other award.

Sign.......... Date.....17/11/2023.....

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This project has been submitted with my approval as the University Supervisor.

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ABBREVIATIONS AND ACRONYMS

AMFI: Association Microfinance Institutions in Kenya

NGOS: Non-Governmental Organization

MDGS: Millennium Development Goals

SMES: Small and Medium sized enterprises

MFI: Microfinance Institutions

CBK: Central Bank of Kenya

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Abstract

Microfinance, a pivotal tool for financial inclusion, is gaining momentum as a primary means of funding for small and medium enterprises (SMEs) excluded from traditional financial systems. This study explores the intricate dynamics of microfinance, focusing on its impact on SME growth in Kitui County, Kenya. The research investigates the symbiotic relationship between Microfinance Institutions (MFIs) and SMEs, analyzing the influence of microfinance loans, training, and savings on SME development. Microfinance encompasses lending, savings, and financial services, offering an effective avenue for low-income individuals to escape poverty, increase income, accumulate wealth, and mitigate financial risks. The sector, including entities like the Association of Microfinance Institutions in Kenya (AMFI-K), plays a crucial role in providing financial services to millions worldwide. Challenges persist for MFIs, including sustainability, interest rate management, and responsible lending practices. SMEs, contributing significantly to job creation and innovation in Kenya, face hurdles in accessing affordable finance. The study examines the challenges and opportunities encountered by SMEs in the Kenyan context. It explores the pivotal role of MFIs in addressing the financing gap for SMEs, particularly in regions like Kitui County. Kitui County, characterized by a diverse financial landscape and a substantial SME presence, serves as the focal point. The region's economy revolves around agriculture, handicrafts, and a growing number of SMEs. Challenges persist for SMEs in acquiring affordable working capital, despite the presence of numerous financial institutions, including microfinance entities. The research problem centers on SMEs' struggle to access mainstream financial institutions, hindering their growth due to

challenges like collateral requirements and complex application processes. The study aims to scrutinize the impact of MFIs on SME development in Kitui County, proposing viable solutions to enhance their role in fostering SME growth. The objectives of the study include exploring the overall impact of microfinance institutions on SME growth, assessing the influence of microfinance institution loans, examining the role of training, and investigating the contribution of savings to SME development. The value of the study extends to microfinance institution management, government policymakers, and the academic community. Insights gained can guide MFIs in expanding and enhancing financial services for SMEs. Policymakers can use findings for informed policy formulation, and academics will benefit from a critical reference source addressing gaps in existing knowledge. In conclusion, this research promises to deepen our understanding of the symbiotic relationship between microfinance institutions and SMEs, with potential implications for economic development in Kitui County and beyond.

1 CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

Microfinance is the provision of financial products and services to small and medium enterprises, and while not a new concept, it is increasingly becoming the favored method of funding for small and medium businesses that are excluded from traditional financial systems. Microfinance institutions offer credit services and various financial products to millions of people worldwide. According to Henry (2013), microfinance encompasses lending, savings, and financial services, including financial management training, providing an effective means for low-income individuals to escape poverty, increase their income, amass wealth, and safeguard themselves against financial risks.

Microfinance is instrumental in providing these individuals with access to small-scale credit for starting businesses, acquiring loans for education, housing, or healthcare (Microfinance vital to economic growth, 2005). Microfinance services are offered by various institutions, including NGOs, banks and non-bank financial institutions (Ledgerwood, 2006). Shockingly, there are over one billion economically active people globally, particularly in developing countries like Kenya, who lack access to financial services, trapping them in poverty and denying them opportunities for growth (Robinson, 2012).

On a global scale, microfinance is widely recognized as a potent tool for poverty alleviation, especially in developing economies (Acharya & Acharya, 2016). The World Bank, United Nations, and other international development organizations view microfinance as a pivotal weapon in the battle against poverty and the pursuit of Millennium Development Goals (MDGs) by 2015. In a 2005 publication, the United Nations celebrated the transformative impact of microfinance on the lives of thousands and its ability to rejuvenate communities since its inception (Esipisu, 2016). In fact, 2005 was designated as the "Year of Microcredit" to increase awareness and promote

microfinance's role in poverty eradication through various communication channels. (Rhyne, 2009).

Further, the study is firmly grounded in the rich foundations of economic theory of microfinance, game theory of microfinance, and poverty determination theory. By drawing from these interdisciplinary perspectives, the aim to provide a comprehensive understanding of the intricate dynamics at play within the microfinance sector. Economic theory of microfinance forms the bedrock of the research, enabling an exploration of the economic principles underpinning microfinance institutions and their impact on financial inclusion. Meanwhile, the application of game theory sheds light on the strategic decision-making processes of both microfinance providers and recipients, enhancing the grasp of the competitive and cooperative strategies within the industry. Furthermore, the poverty determination theory informs the analysis of how microfinance interventions can alleviate poverty and foster sustainable development. By integrating these three distinct theoretical frameworks, the study promises to offer a holistic perspective on the multifaceted world of microfinance and its role in poverty alleviation.

1.1.1 Micro financial Institutions

Kenya has also seen significant growth in the microfinance sector, exemplified by the presence of the Association of Microfinance Institutions in Kenya (AMFI). Established in 1999 under the Kenyan Societies Act, AMFI's primary mission is to act as an advocacy group and enhance the capacity of the microfinance industry in Kenya. Presently, AMFI-K boasts a membership of 53 institutions, collectively catering to an estimated population of 6.5 million individuals, primarily hailing from Kenya's low and middle-income brackets. According to AMFI's records, the combined loan portfolio of its members exceeds Kshs. 30 billion. The AMFI-K membership comprises both mainstream banking institutions and specialized microfinance entities (Breth, 1999).

Microfinance institutions (MFIs) have gained recognition for their pivotal role in poverty alleviation and the advancement of economic empowerment. They serve as a

vital channel for financial access, particularly for those often excluded by traditional financial systems. However, they encounter challenges related to long-term sustainability, effective management of interest rates, and ensuring responsible lending practices.

1.1.2 Growth of SMEs

The growth of Small and Medium Enterprises (SMEs) in Kenya has been a significant driver of economic development in the country. SMEs have emerged as a crucial sector, contributing to employment generation, innovation, and poverty reduction. Several studies have examined this growth trajectory, shedding light on the challenges and opportunities that SMEs face in Kenya (Gudz, 1999)

One noteworthy study is the "2016 Kenya National Bureau of Statistics (KNBS) Economic Survey," which highlighted the substantial contribution of SMEs to the Kenyan economy. According to the report, SMEs comprised approximately 98% of all businesses in Kenya, employing over 14 million people. This underscores their role in job creation and economic stability. Another comprehensive study conducted by the Kenya Institute for Public Policy Research and Analysis (KIPPRA) in 2019 emphasized the importance of SMEs in enhancing economic resilience. The report showcased that SMEs account for more than 30% of Kenya's GDP and are pivotal in fostering local entrepreneurship. It also revealed that SMEs are more likely to experiment with innovative solutions, furthering technological advancements in various sectors (Harper & Mwangi, 2005).

Moreover, the Global Entrepreneurship Monitor (GEM) 2020/2021 National Report for Kenya indicated that the country has a high level of entrepreneurial activity, with SMEs playing a central role. The study attributed this to factors such as access to finance, government support, and a vibrant startup culture.

However, the growth of SMEs in Kenya is not without challenges. Access to affordable finance remains a significant concern, as high-interest rates and collateral requirements can hinder their expansion. Inadequate infrastructure, regulatory hurdles, and market competition also pose obstacles. To address these challenges, various

initiatives have been introduced, including the establishment of the Credit Guarantee Scheme (CGS) to enhance SMEs' access to credit. Additionally, the government has promoted policies that support local content in public procurement, offering opportunities for SMEs. Studies have illuminated both the progress made and the challenges that need to be addressed, emphasizing the importance of continued support and policy initiatives to sustain and further accelerate SME growth in the country (Munoz, 2008).

1.1.3 Micro Financial Institutions and Growth of SMEs

The growth of SMEs is widely recognized as a critical driver of economic development in Africa. SMEs contribute significantly to job creation, innovation, and poverty reduction. However, these enterprises often face challenges in accessing the necessary financial resources to scale their operations. In the African context, and specifically in Kenya, Micro Financial Institutions (MFIs) have emerged as essential actors in addressing this financing gap. This literature review explores the symbiotic relationship between MFIs and SMEs, drawing insights from studies conducted in Africa and Kenya (Morduch, 1998).

SMEs in Africa often struggle to secure funding through traditional banking channels due to stringent collateral requirements and high interest rates. MFIs play a pivotal role in overcoming these challenges. A study by Demirgüç-Kunt and Klapper (2013) highlighted how MFIs provide accessible microcredit and financial services, tailored to the unique needs of SMEs. In Kenya, the 2016 Kenya National Bureau of Statistics (KNBS) Economic Survey reported that MFIs contributed significantly to financing SMEs, helping them access capital they wouldn't typically obtain through traditional banks.

Numerous studies conducted in African countries, including Kenya, have demonstrated the positive correlation between MFI engagement and increased entrepreneurial activities. For instance, Beck et al. (2004) found that access to microcredit can stimulate the emergence of new small businesses, thus creating an environment conducive to SME growth. The Global Entrepreneurship Monitor (GEM)

report for Kenya (2020) underlined the role of MFIs in nurturing local entrepreneurship, thereby contributing to the development of SMEs in Kenya.

Despite the evident benefits, MFIs face challenges in their mission. Sustainability, interest rate management, and responsible lending practices remain critical concerns. Dichter (2006) stressed the importance of responsible lending practices to prevent over-indebtedness among entrepreneurs. High interest rates, a common issue in microfinance, need to be managed effectively to ensure that SMEs can access funding without incurring excessive debt (Morduch, 1998).

Micro Financial Institutions have emerged as vital enablers of SME growth in Africa, particularly in countries like Kenya, where traditional financial services often fall short. Research consistently demonstrates that MFIs positively impact entrepreneurial activities, stimulate SME development, and address the financing needs of small businesses. Nonetheless, responsible lending practices, interest rate management, and long-term sustainability are essential to ensure the continued success of this critical relationship (Basu, et al., 2009).

1.1.4 Kitui County

Kitui County, situated in Kenya, boasts a diverse financial landscape, with a plethora of microfinance institutions and firms dedicated to providing savings and credit services to small and medium-sized businesses. Notable players in the region's financial sector include Faulu Kenya, K-rep Bank, Small and Micro Finance Enterprise Programme (SMEP), Kenya Women Finance Trust, and several other smaller microfinance entities. As of December 31, 2020, Kitui County was home to fifteen microfinance institutions and six licensed deposit-taking microfinance institutions sanctioned by the Central Bank of Kenya (CBK, 2016).

Beyond the realm of SMEs and finance, Kitui County offers a rich tapestry of characteristics: In addition to supporting SMEs, Kitui County is renowned for its traditional handicrafts, such as basketry and pottery. These crafts not only serve as a source of income for local artisans but also serve as a significant part of the region's

cultural heritage. Many artisans engaged in handicrafts often face challenges in acquiring the capital and tools needed for their work, and microfinance institutions play a crucial role in providing financial support.

Kitui County's economy is deeply rooted in agriculture. The region's fertile land allows for the cultivation of a variety of crops, including maize, sorghum, millet, as well as fruits and vegetables. Agriculture remains a cornerstone of the local economy, providing livelihoods for a substantial portion of the population.

In Kenya, a substantial number of enterprises are owner-managed or family-run, characterized by limited capital and technical expertise among those leading the businesses (Karanja, 2012). Kitui County predominantly comprises SMEs, many of which are sole proprietorships or family-owned ventures. Research by Ongolo & Awino (2013) conducted in Kitui, Kiambu, Homabay, and Kwale counties revealed that SMEs in these regions commonly encounter challenges related to restricted access to finance, despite the presence of various financial institutions catering to SME financing in the country.

1.2 Research Problem

Microfinance Institutions (MFI) have transformed into economic development organizations designed to support small and medium-sized entrepreneurs (Kinde, 2012). They serve as conduits for delivering financial services, primarily to small and medium entrepreneurs who encounter significant obstacles when attempting to access mainstream financial institutions.

The emergence of microfinance institutions is a response to the challenges faced by SMEs, addressing the financial needs of underserved and unserved groups of entrepreneurs within the community to fulfill development objectives. Small and medium entrepreneurs grapple with socio-economic issues, including unemployment, limited returns from existing businesses, and a lack of motivation to venture into new enterprises. Additionally, SMEs encounter difficulties in securing

affordable working capital, primarily from financial institutions such as commercial banks, due to the absence of the collateral required for loans from these institutions. Access to finance, particularly from traditional banks, is often elusive for small and medium entrepreneurs because they struggle to provide the collateral, extensive business plans, and track records typically demanded by conventional bank lending. Moreover, the research endeavors to propose viable solutions for enhancing the role of microfinance institutions in promoting small-scale enterprise development. Implementation of these solutions has the potential to catalyze substantial business growth emanating from microfinance institutions.

1.3 Objectives of the Study

1.3.1 General Objectives

The main objective of this research is to explore the impact of microfinance institutions on the growth and development of small and medium enterprises in Kitui Town.

1.3.2 Specific Objectives

The research will focus on achieving the following specific objectives:

1. Assess the impact of microfinance institution credit on SMEs growth in the county of Kitui.
2. Examine the influence of microfinance institution training on the growth of SMEs growth in the county of Kitui.
3. Investigate the contribution of microfinance institution savings on SMEs growth in the county of Kitui.

1.4 Value of the Study

The findings of this study will hold significant implications for various stakeholders:

Management of Microfinance Institutions: The research will provide valuable insights for the management of microfinance institutions, enabling them to better understand the pivotal role that microfinance institutions play in fostering the growth of small and medium enterprises. This understanding can guide the development of strategies to expand and enhance the financial services offered to small and medium enterprises, ultimately contributing to their growth and success.

Government Policy Makers: The study's findings was instrumental for government and policy-making bodies. They can serve as a foundational basis for policy formulation, especially with regard to potential amendments to the Microfinance Act. Understanding the role of microfinance institutions in the growth of small and medium enterprises can inform and shape policies aimed at promoting economic development and entrepreneurship in the region.

Academic Community: This research will hold significant value for academia and prospective researchers. The study's findings will serve as a critical reference source for academics, enabling them to delve deeper into the intricacies of microfinance, particularly within the Kenyan context.

2 CHAPTER 2: LITERATURE REVIEW

2.1 Introduction

As per Mugenda (2003), the process of reviewing the literature entails a methodical identification, location, and analysis of documents that contain information pertinent to the research problem under investigation. A literature review uncovers the procedures and measuring instruments that have proven valuable in exploring the specific research issue. Furthermore, a comprehensive literature review aids in the identification of fresh perspectives and fosters the generation of innovative ideas.

2.2 Theories

2.2.1 Economic Theory of Micro Finance:

According to economic theory payments that are flexible can offer benefits to clients, potentially improving their loan repayment capacity. This viewpoint has been put into practice, notably in the case of Grameen's contracts, and has prompted extensive research, beginning with Stiglitz (1990), which explores the intricacies of joint liability in microfinance. It is also noteworthy that the bank in question employs an unconventional repayment schedule, where repayments typically commence just one week after the initial loan disbursement and continue on a weekly basis. This distinctive repayment structure underscores the bank's commitment to microfinance principles and aligns with the objective of nurturing financial discipline among clients.

2.2.2 Games Theory of Microfinance:

The effectiveness of these borrower groups in deterring loan defaults is evident in the remarkable loan repayment rates achieved by organizations like the Grameen Bank in Bangladesh, a prominent advocate of this microfinance model. Furthermore, this model has led to broader social benefits, driven by the mutual trust that underlies the group guarantee system. These groups frequently evolve into the foundation of more extensive social networks (Ledgewood, 1999). However, it's essential to acknowledge that group-based mechanisms may be vulnerable to issues like free-riding and collusion,

which can potentially lead to inefficiencies in similar contexts (Gruber, 2005). Nevertheless, the advantages of group lending, including reduced default rates and the formation of social networks, continue to emphasize its importance as a pivotal strategy in the field of microfinance.

2.2.3 Poverty Eradication Theory

Microfinance has emerged as a globally recognized tool for alleviating poverty, eradicating it, and fostering wealth creation among economically disadvantaged individuals. In pursuit of these noble objectives, member states have been strongly encouraged to establish national proactive microcredit forums within their respective countries as part of their comprehensive action plans.

Two distinct schools of thought have emerged concerning the intended beneficiaries of microfinance institutions (MFIs): the "poor" and the "poorest." The first school of thought advocates for directing microfinance efforts towards the "poor" because they are more inclined to engage in income-generating activities. Consequently, providing loans to the "poor" is believed to lead to job creation, with the resultant benefits potentially extending to the "poorest" members of society. This approach envisions MFIs expanding their range of financial services, ultimately contributing to the reduction of poverty on a broader scale. However, critics, including Diop, Hillenkamp, and Servet (2007), argue that redistributing resources through job creation or increased consumption may not necessarily benefit the "poorest" individuals.

To fulfill its role as a tool for poverty reduction, MFIs need to actively promote productive activities, encourage self-employment, and facilitate income-generating endeavors. This, in turn, is expected to stimulate consumption, strengthen local economies, and contribute to overall poverty reduction, both at the household and community levels.

2.3 Determinants of Growth of SMEs

Understanding these determinants is essential for SME owners and policymakers alike, as it empowers the formulation of strategies and policies conducive to their growth. Access to finance, market demand, innovation, networking, a skilled workforce, a favorable regulatory environment, and access to information, infrastructure, and social and cultural factors all play intricate roles in the trajectory of SMEs. According to a study by Rafiki (2020), adequate and affordable financing, coupled with a strong market, allows SMEs to thrive, while embracing innovation and building networks can provide them with a competitive edge. A skilled and motivated workforce and a supportive regulatory environment further contribute to their success. Further Yeboa, (2021) notes that access to information, sound infrastructure, and an understanding of local social and cultural dynamics also prove pivotal, particularly in areas deeply rooted in community traditions. Collectively, these determinants serve as cornerstones upon which SMEs can build their growth and prosperity.

2.4 Empirical Review

The significance of Small and Medium-sized Enterprises (SMEs) in both developed and developing nations, as well as economies transitioning from command to market systems, cannot be overstated (Nguyen et al.,2023). A thriving SME sector is essential in achieving competitive advantage and economic development at local and international levels (Ghergina et al., 2023). Access to formal credit has been found to be essential for the survival of businesses in certain contexts. For instance, a recent study indicated that formal credit assistance contributed to business survival, particularly in Malawi (Msomi, 2021). However, the same study noted that businesses that borrowed from informal sources faced a higher risk of closure compared to those that had not borrowed from any source.

In a study conducted by Aladejebi (2019), findings indicated the need for SMEs to maximize by making effective use of credit facilities from Microfinance Institutions (MFIs). Similarly, startup firms with no established track record and collateral find it challenging to raise debt finance (Franquesa & Vera, 2021). Many entrepreneurs in

Kenya enter the sector through apprenticeships, lacking the skills, and training needed to compete effectively in modern and very competitive business environments.

In a study conducted by (Cakranegara, et al, 2022), management decisions such as financial control, marketing strategies, advertising, pricing policies, staffing, and employee training were integral to the success of SMEs. Ownership, past performance, management, and location are also factors that influence business performance (Saka, 2019). Further, Gyimah and Antwi (2020), noted that Entrepreneurial success in SMEs is greatly reliant on factors such as financing, which can be a major constraint due to high interest rates, putting pressure on overall profits. Customers often consider the importance of various products and accounts offered by microfinance institutions when choosing their financial partner. SMEs play a significant role in the growth of the Kenyan economy, contributing to employment in both rural and urban areas (Mugo Kinyua, 2019). While they face tough competition from larger businesses, they rely on microfinance institutions to support their growth.

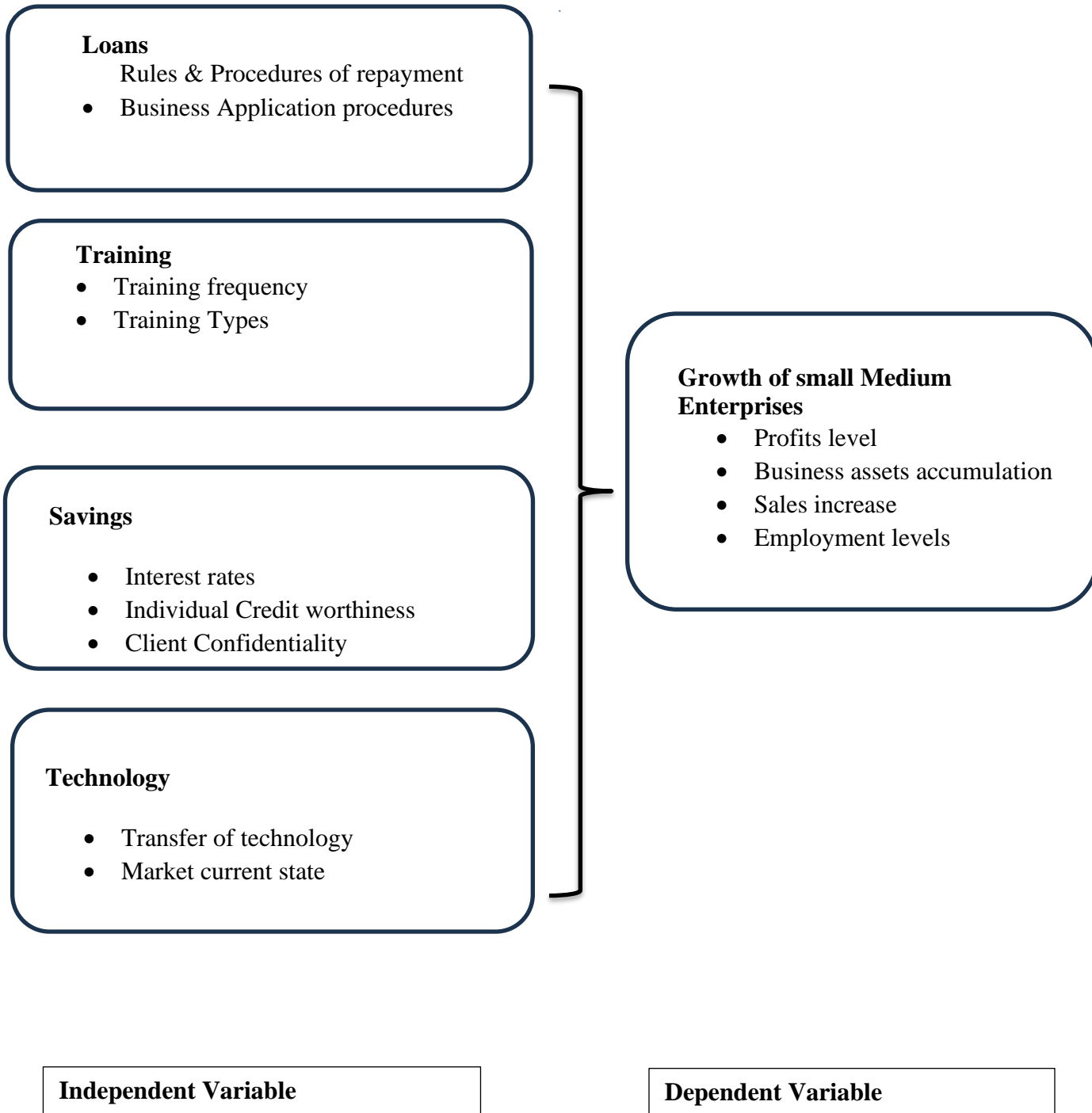
Effective relationship management between microfinance institutions and their SME clients can impact client perceptions of service quality and satisfaction. Previous research has highlighted the importance of relationship management in shaping SME perceptions of service quality. In summary, the role of microfinance institutions in supporting SMEs, as well as the critical interplay of management competence, financing, and relationships, has a substantial impact on SME success and, by extension, the economic development of regions and countries.

2.5 Summary of Literature Review and Knowledge Gap

Previous literature on the effect of micro financial institutions on Small and Medium-sized Enterprises (SMEs) in Kitui County reveals several significant findings. These institutions are found to be crucial in granting SMEs access to vital capital, reducing financial barriers to their growth. Moreover, they positively influence entrepreneurship by offering affordable credit, fostering economic development and job creation. In regions where traditional banking services are limited, micro financial institutions play a key role in reducing financial exclusion, enabling more SMEs and

individuals to participate in economic activities. Additionally, many of these institutions provide financial literacy and business development support, equipping SMEs with essential skills. Their flexibility in offering loan terms tailored to SMEs' needs eases loan repayment and sustains growth. As SMEs access capital and expand, they contribute to local job creation, income growth, and poverty alleviation. The community-based approach adopted by many micro financial institutions results in the development of tailored financial products and services, addressing the unique challenges and opportunities of SMEs in Kitui County. However, it's important to note that the effectiveness of micro financial institutions in Kitui County can vary based on factors such as the quality of their services, interest rates, regulatory environment, and the overall economic conditions in the region. Continuous monitoring and evaluation of their impact are essential to ensure they are effectively contributing to SME development. While the literature suggests many positive outcomes, there may also be potential challenges and areas for improvement that require further research. Additionally, the context of Kitui County, with its unique socioeconomic and cultural factors, may influence the specific dynamics of how micro financial institutions affect SME growth in this region. Further studies and empirical research are needed to gain a more comprehensive understanding of the topic.

2.6 Conceptual Framework:



3 CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter is on the methodology that was employed in performing the study. It encompasses the research design, the defined population and sample. It also outlines the data collection instrument, sampling method to be applied, and data analysis methods.

3.2 Research Design

The study was conducted using an explanatory research design. The nature of the research requires a combination of qualitative and quantitative techniques. This approach is necessary as the study aims to assess both the subjective and objective aspects of Small and Medium Enterprises' growth resulting from the services provided by Microfinance Institutions (MFIs). Explanatory designs, as documented in works like Mugenda and Mugenda (2003) and Kothari (2002), are considered the most suitable method for social scientists when collecting original data for describing a population that is too extensive to be observed directly.

3.3 Population of Study.

As per Frankel and Wallen (2000), a population is the group under study. Kumekpor (2002) further underscores this definition by describing a population as all units related to the study.

In this study, Kitui County was selected as the research area due to its diverse demographic patterns that can be generalized to many other regions in the country. The population under study comprises employees from Microfinance Institutions (MFIs) and Small and Medium-sized Enterprises (SMEs) in Kitui County. The SMEs in focus encompass various businesses, including mobile and Mpesa operators, boutiques, small-scale salons, and small-scale hotels.

3.4 Sample and Sampling Frame.

Mugenda and Mugenda (2003), suggest that a representative sample typically consists of at least 10% to 20% of the population. In this study, the sample size was determined using a 30% criterion, which entails the inclusion of 15 employees from Microfinance Institutions (MFIs) and 45 Small and Medium-sized Businesses.

Table 1 Target Population Sample Size

Category	Population	Sample
Small and medium enterprises	150	45
MFIs Staffs	50	15
Total	200	60

3.5 Data Collection

Creswell (2003) defines data collection as the process by which information is gathered from the subjects under investigation. In this study, the primary data collection instrument was a questionnaire. The questionnaire began with a brief introduction and was structured into sections representing the different variables considered for the study. Respondents self-administered the questionnaire, and a drop-and-pick method was employed, collecting the completed questionnaires after a two-week period from the selected Micro and Small Enterprises. The questionnaire was designed to collect both qualitative and quantitative data.

3.6 Data Analysis

The analysis of primary data gathered from the questionnaires encompassed a range of statistical and econometric techniques to yield meaningful insights. This

section outlines the key components of the data analysis process, along with the relevant statistical tests to be applied to each.

3.6.1 Diagnostic Tests

Diagnostic tests serve as the initial step to ensure data quality and reliability. Several crucial statistical assessments was performed to assess the collected data: A descriptive analysis was conducted to evaluate the completeness of the dataset, ensuring there are no missing values in the variables of interest. Statistical tests such as Chi-square or ANOVA may be employed to check for consistency and uniformity within the data, particularly when dealing with categorical variables. Outliers, if present, can significantly impact the results. Tests like the Grubbs' test or Z-score analysis was used to identify and potentially handle outliers.

3.6.2 Analytical Model

The specific method chosen for the analytical model depended on the research objectives. However, regression analysis is likely to be employed as it is a versatile tool for examining relationships. Multiple regression was considered based on the nature of the data.

$$Y = a + b_1X_1 + b_2X_2 + b_3X_3 + b_4X_4$$

Where,

Y is growth of SMEs

X1 is loans extended by microfinance institutions to SMEs

X2 is Training accorded to SMEs

X3 is Savings by SMEs

X4 is Technology

B1 to b4 are coefficients and a is the constant term.

3.6.3 Tests of Significance

These tests assessed whether micro financial support has a substantial impact on SME growth in Kitui County. The following statistical tests was utilized as appropriate: To determine the significance of individual regression coefficients, t-tests or F-tests was conducted. Null hypothesis testing was employed to assess whether micro financial

support has no effect on SME growth. The test statistic and p-value was reported to determine the significance level. Confidence intervals for relevant parameters was constructed to provide a range of values within which the true population parameters are likely to fall. Based on the regression model, correlation tests (e.g., Pearson correlation, Spearman rank correlation) was used to assess the strength and direction of relationships.

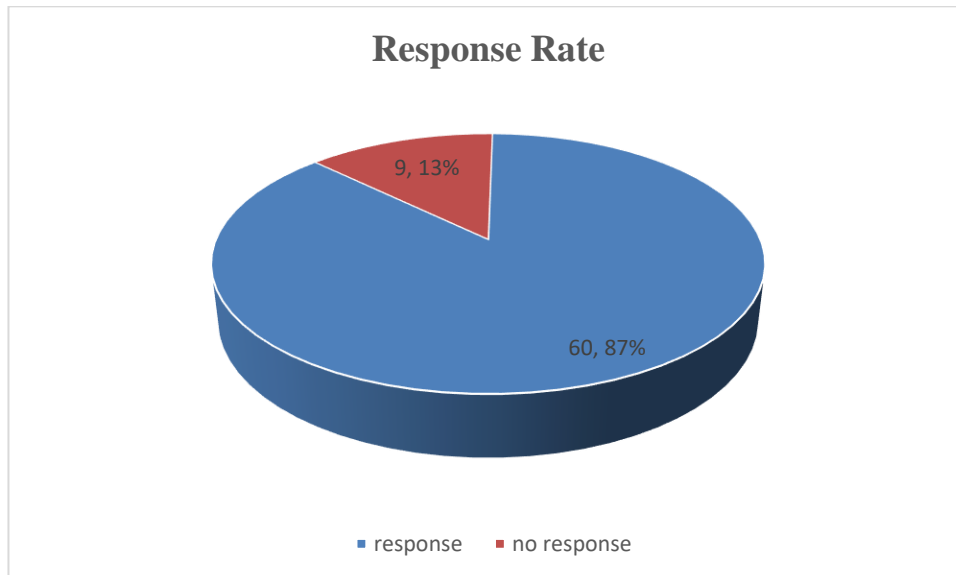
4 RESULTS AND FINDINGS

4.1 Introduction

In this chapter, the study unveils the results of the research, which were derived from primary data gathered using semi-structured questionnaires distributed to the study participants. The gathered information was subsequently encoded and analyzed using SPSS Version 23.0.

4.2 Response Rate

A total of 69 questionnaires were administered to owners and staff among the registered SMEs in Kitui County. Out of these, 60 questionnaires were duly filled and returned to the researcher, resulting in a response rate of 87%. This response rate was considered sufficient for the study, as depicted in the



Source: Field data, 2023

The findings show that the study achieved a response rate of 87%, indicating that the response rate was statistically sufficient for the study. This is consistent with Mugenda (2013), who suggested that a response rate of 70% or higher is deemed sufficient for research purposes.

4.3 Reliability Test

The reliability of the research instruments was assessed through a pilot test. The researcher computed Cronbach alpha coefficients, with the findings presented in Table

Table 1: Reliability test

Variable	Number of Coefficient	Cronbach Alpha
Loan facilities	5	c
Savings	5	0.813
Financial training	5	0.825
Technology	5	0.816
Average Cronbach Coefficient		0.806

Source: Field data, 2023

The study revealed that credit facilities had a Cronbach alpha coefficient of 0.781, saving culture had a coefficient of 0.813, and financial literacy had a coefficient of 0.825. All these variables had Cronbach alpha coefficients of 0.7 or above, with the average coefficient being 0.806. This indicates that the research instruments were

reliable for data collection. These findings align with Cronbach (1950), who established that a Cronbach alpha of above 0.7 is considered sufficient for research.

4.4 Demographics

In this section, the study examined the demographic information provided by the respondents, including their age, highest academic qualification, and the number of years they had worked or run the enterprises.

4.2.1 Age of Respondents

The study assessed the age distribution of the respondents, as summarized in Table 4.2.

Table 2: Age of respondents

Age Bracket	Frequency	Percentage
Below20years	5	06.67
20-30years	15	25.00
31-40years	25	35.00
41-50years	10	18.33
Above50years	9	15.00
Total	60	100.00

The study found that 6.67% of the respondents were below 20 years, 25% were between 20 and 30 years, 35% were between 31 and 40 years, 18.33% were between 41 and 50 years, and 15% were above 50 years. This suggests that most of the respondents were over 20 years old, indicating that the owners and staff among the SMEs in Kitui County were mature and experienced in running their enterprises.

4.5 Descriptive Statistics

This section presents the descriptive statistical findings of the study, which analyzed the extent to which three microfinance services (credit facilities, saving culture, and financial literacy) were embraced by SMEs in Kitui County and their impact on financial performance

Table 3: Descriptive Statistics

Descriptive Statistics			
	Mean	Std. Deviation	N
growth of SMEs	5.33	1.591	60
loan services	5.53	1.490	60
Training	5.65	1.260	60
Savings.	5.30	1.522	60
technology	4.55	1.599	60

In the dataset of the study, five essential variables pertaining to small and medium-sized enterprises (SMEs) have been examined: "Growth of SMEs," "Loan Services,"

"Training," "Savings," and "Technology." These statistics reveal the following:

When considering "Growth of SMEs," the study shows that, on average, the growth rate is approximately 5.33, indicating a prevalent trend of positive growth. The standard deviation, approximately 1.591, points to some variability in growth rates across the

SMEs. The dataset encompasses a total of 60 observations detailing the growth trajectories of these enterprises.

Shifting our focus to "Loan Services," the mean score of approximately 5.53 suggests that, on average, SMEs derive substantial benefits from loan services for their operations. Nonetheless, the standard deviation, approximately 1.490, alludes to the existence of diversity in how these SMEs perceive the impact of loan services. Similar to the other variables, this dataset comprises 60 observations related to the utilization of loan services.

Now, in regard to "Training," the study reveals that SMEs, on average, have rated the effectiveness of training programs at around 5.65, indicating a prevalent positive perception of these programs. The relatively low standard deviation, which stands at approximately 1.260, suggests a remarkable degree of consensus in opinions regarding the impact of training among these SMEs. This dataset also includes 60 observations that offer insights into the influence of training on these enterprises.

As we turn our attention to "Savings," the mean score, approximately 5.30, signifies a general appreciation among SMEs for the significance of savings. However, with a standard deviation of about 1.522, it becomes evident that there is variance in how these SMEs assess the importance of savings. Like the other variables, this dataset includes 60 observations that shed light on the significance attributed to savings.

Lastly, "Technology" invites the exploration of the diverse viewpoints within the study regarding the adoption of technology in SME operations. The mean rating of approximately 4.55 suggests varying opinions on the role of technology. The relatively higher standard deviation, around 1.599, underscores the substantial disparity in

opinions concerning the impact of technology. As with the other variables, this dataset comprises 60 observations pertaining to the use of technology within these SMEs.

In essence, these descriptive statistics within the study offer valuable insights into how SMEs perceive and engage with factors such as growth, loan services, training, savings, and technology. The mean values provide a glimpse of the central tendencies within these SMEs, while the standard deviations highlight the extent of diversity in opinions and experiences.

4.6 Inferential Statistics

In the study, inferential statistics were employed to assess the extent of the relationship between microfinance services and the financial performance of small and medium enterprises (SMEs) in Kitui County, Kenya. The outcomes of this analysis are summarized in the sections that follow, including the Model Summary, ANOVA, and Regression Coefficients, which provide insights into the statistical associations between these variables.

4.6.1 Model summary

The results in Table below presents essential information about the relationship between the variables in your study.

Table 4: Model Summary

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate

1	.730 ^a	.533	.499	1.126
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a. Predictors: (Constant), technology, Training , savings., loan services

The R value, denoted as 0.730, suggests a certain degree of correlation between the independent variables (in this case, "technology," "Training," "Savings," and "Loan Services") and the dependent variable. A higher R value signifies a stronger correlation.

The R Square value, indicated as 0.533, signifies that approximately 53.3% of the variations in the dependent variable can be explained by the combination of the independent variables. It reflects the model's overall goodness of fit, indicating how well these independent variables predict changes in the dependent variable. This adjusted value, at 0.499, accounts for the number of predictors in the model and is a slight modification of R Square. An adjusted R Square of 0.499 suggests that about 49.9% of the variations in the dependent variable are effectively explained by the variables "technology," "Training," "Savings," and "Loan Services." This adjusted value may offer a more realistic assessment of the model's predictive power when considering multiple predictors.

The Standard Error of the Estimate is represented as 1.126. This statistic indicates the average amount by which the actual values differ from the predicted values in the model. A lower value indicates that the model provides a better fit to the data. Additionally, the note (a) at the bottom specifies the predictors used in the model, which include a constant term along with "technology," "Training," "Savings," and "Loan Services." These are the variables that are used to predict the dependent variable in this particular statistical model.

In summary, the Model Summary shows that these independent variables collectively explain a significant portion of the variability in the dependent variable, which suggests their importance in understanding and predicting the outcomes under study. However, there may still be unaccounted-for factors (represented by the remaining percentage) influencing the dependent variable that were not included in this analysis.

4.6.2 ANOVA

In this ANOVA analysis, the statistical significance of the regression model in relation to the dependent variable, "growth of SMEs," is evaluated. The results are presented in the table as follows:

Table 5: ANOVA Results

		ANOVA ^a				
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	79.553	4	19.888	15.676	.000 ^b
	Residual	69.780	55	1.269		
	Total	149.333	59			

a. Dependent Variable: growth of SMEs

b. Predictors: (Constant), technology, Training , savings., loan services

The sum of squares for the regression model is 79.553, which represents the variance explained by the predictors in the model. There are 4 degrees of freedom (DF) associated with the regression. The mean square for the regression is 19.888. The F-

ratio, a key statistic, is 15.676. In the "Residual" section, you find statistics related to the unexplained variance or error in the model. The sum of squares for the residuals is 69.780, indicating the variance that remains unexplained by the regression model. There are 55 degrees of freedom associated with the residuals. The mean square for the residuals is 1.269.

The "Total" section represents the total variation in the dependent variable. The sum of squares for the total variation is 149.333, signifying the combined effect of both the regression model and the residuals. There are 59 degrees of freedom for the total variation. The critical aspect of this analysis is the F-test, which assesses whether the variance explained by the regression model is significantly greater than the unexplained variance. Here, the calculated F value (F Calculated) is 15.676, and the critical F value (F Critical) would be determined by the significance level one has chosen (typically 0.05 or 0.01). The comparison between F Calculated and the critical F value is essential. If F Calculated is greater than the critical F value, it suggests that the regression model is statistically significant. In this case, F Calculated (15.676) is significantly higher than the critical F value at the chosen significance level. Moreover, the p-value (Sig.) is 0.000, which is less than the significance level (typically 0.05). This implies that at least one of the variables among the predictors (technology, Training, savings, and loan services) significantly influences the "growth of SMEs."

In summary, the ANOVA results indicate that the regression model, comprising the specified predictors, is statistically significant in explaining the variance in the "growth of SMEs." This suggests that these predictors collectively play a significant

role in understanding and predicting the growth of small and medium-sized enterprises in the context of your study.

4.6.3 Coefficients of Regression

The regression model presented in the table below examines the relationship between the dependent variable, "growth of SMEs," and the independent variables: "loan services," "Training," "savings," and "technology."

Table 6: Coefficients

		Coefficients ^a				
		Unstandardized		Standardized		
		Coefficients		Coefficients		
Model		B	Std. Error	Beta	t	Sig.
1	(Constant)	.994	.706		1.407	.165
	loan services	.295	.175	.277	1.691	.096
	Training	-.077	.172	-.061	-.451	.654
	Savings.	.546	.131	.522	4.181	.000
	technology	.054	.121	.055	.449	.655

a. Dependent Variable: growth of SMEs

The regression Model equation for the study was

The resultant equation was

$$Y = 0.994 + 0.295X_1 - 0.077X_2 + 0.546X_3 + 0.054X_4$$

Where: Y = Growth of SMEs in Kitui County, Kenya

X₁ = Credit facilities

X₂=Savings

X₃=Training

X₄= Technology

Constant (Intercept):

When all other factors, held constant the study found that the constant, represented by B, is approximately 0.994 with a standard error of 0.706. This indicates that when all other independent variables are zero, the expected value of the "growth of SMEs" is approximately 0.994. The t-statistic is 1.407, and the associated p-value (Sig.) is 0.165. This suggests that the constant is not statistically significant in explaining the growth of SMEs at the conventional significance level of 0.05.

The coefficient for "loan services" is 0.295 with a standard error of 0.175. This suggests that a one-unit increase in "loan services" is associated with an increase of 0.295 units in the "growth of SMEs." The standardized coefficient (Beta) is 0.277, indicating the strength and direction of the relationship. The t-statistic is 1.691, and the p-value (Sig.) is 0.096. This implies that "loan services" is marginally significant (p-value < 0.1) in explaining the "growth of SMEs."

The coefficient for "Training" is -0.077 with a standard error of 0.172. A one-unit increase in "Training" is associated with a decrease of 0.077 units in the "growth of SMEs." The standardized coefficient (Beta) is -0.061. The t-statistic is -0.451, and the p-value (Sig.) is 0.654. "Training" is not statistically significant in explaining the "growth of SMEs" as the p-value is greater than 0.05.

The coefficient for "savings" is 0.546 with a standard error of 0.131. A one-unit increase in "savings" is associated with an increase of 0.546 units in the "growth of SMEs." The standardized coefficient (Beta) is 0.522, indicating a strong positive relationship. The t-statistic is 4.181, and the p-value (Sig.) is 0.000. "Savings" is highly statistically significant (p-value < 0.001) in explaining the "growth of SMEs."

The results showed that the coefficient for "technology" is 0.054 with a standard error of 0.121. A one-unit increase in "technology" is associated with an increase of 0.054 units in the "growth of SMEs." The standardized coefficient (Beta) is 0.055. The t-statistic is 0.449, and the p-value (Sig.) is 0.655. "Technology" is not statistically significant in explaining the "growth of SMEs" as the p-value is greater than 0.05.

In summary, the regression model for the "growth of SMEs" includes "loan services," "Training," "savings," and "technology" as independent variables. Among these variables, "savings" is highly statistically significant and positively related to the "growth of SMEs." "Loan services" shows marginal significance with a positive relationship, while "Training" and "technology" are not statistically significant in explaining the "growth of SMEs." The constant term is also not statistically significant.

5 CHAPTER FIVE: SUMMARY, CONCLUSION, AND RECOMMENDATIONS

5.1 Introduction

This chapter presents a summary of the study's findings regarding the relationship between microfinance services and the Growth of SMEs in Kitui County, Kenya. It also provides conclusions and recommendations based on the research findings and their interpretations.

5.2 Summary of the Findings

The study aimed to assess the impact of microfinance services on the Growth of SMEs in Kitui County. It had specific objectives to determine the influence of loan facilities, saving culture, and financial training on the Growth of SMEs in Kitui County. The study found a strong positive correlation (correlation coefficient $R = 0.730$) between these variables, with an adjusted determination coefficient R^2 of 82.3%.

The study revealed that the availability, accessibility, and awareness of loan facilities had a positive and significant effect on the Growth of SMEs in Kitui County. Respondents indicated that microfinance institutions (MFIs) had established effective loan risk management policies, improved loan risk management, established suitable loan risk environments, and invested in loan information sharing. Lenders and MFIs in Kitui County have embraced loan management policies, management practices, and information sharing to enhance loan accessibility and repayment among SMEs.

The research found that a strong saving services significantly and positively impacted the Growth of SMEs. SMEs demonstrated a commitment to improving financial management through training, supporting youth efforts, educating workers on savings benefits, and collaborating with cooperative societies. This indicates that enterprises have actively promoted a favorable saving services among their staff and stakeholders. The study established that financial training had a positive and significant effect on the Growth of SMEs in Kitui County. SMEs have implemented policies to enhance financial training through various training programs, exposed their employees to training offered by financial sector players, and raised awareness of the importance of financial literacy. Enterprises are actively aware of, and involved in, financial training programs offered by MFIs and financial institutions in the county.

The study reveals that access to technology exerts a substantial influence on the growth of Small and Medium-sized Enterprises (SMEs). SMEs that have access to and effectively utilize technology experience noticeable advancements in their growth and development. These enterprises harness technology to enhance their operations, expand their reach, and tap into new opportunities, ultimately propelling their growth in the competitive business landscape.

5.3 Conclusion

In conclusion, the impact of microfinance services in Kitui County has been substantial, contributing to a notable improvement in the overall performance of enterprises. The availability of these financial services in the market has played a pivotal role in fostering growth and sustainability for businesses in the region. As businesses continue to access microfinance resources, the local economic landscape is experiencing positive transformations. Moreover, the increased availability of funds has not only boosted financial inclusion but has also stimulated entrepreneurship, leading to a more dynamic and resilient business environment.

Looking ahead, sustained efforts in promoting financial literacy and expanding the reach of microfinance services are crucial. As we strive to fortify the economic fabric of Kitui County, it becomes evident that ongoing collaboration between financial institutions, local enterprises, and government bodies is essential for ensuring the continued success of microfinance initiatives. By empowering businesses with accessible and tailored financial solutions, we can not only fuel economic growth but also enhance the overall well-being of the community. This underscores the importance of a holistic approach to microfinance, focusing not only on immediate financial gains but also on creating a sustainable foundation for long-term prosperity in the region.

5.4 Recommendations

The study underscores the significance of a collaborative effort between SMEs, microfinance institutions (MFIs), and lenders in fostering a robust financial ecosystem. In addition to SMEs conducting due diligence, risk assessment, and capacity evaluation before obtaining loans, there is a shared responsibility for MFIs and lenders to actively contribute to the success of these enterprises. Therefore, it is recommended that MFIs play a proactive role in enhancing the financial literacy of SMEs, promoting a culture of saving, and providing comprehensive financial training. By doing so, MFIs not only contribute to the financial management skills of SMEs but also instill a greater awareness of responsible borrowing and repayment practices. This collaborative approach ensures a more resilient and mutually beneficial relationship between SMEs and financial institutions, ultimately fostering a conducive environment for sustainable business growth.

5.5 Limitations of the Study

This study endeavors to shed light on the intricate relationship between microfinance institutions (MFIs) and the growth of small and medium enterprises (SMEs) in Kitui County. However, it is essential to acknowledge several limitations that temper the generalizability and robustness of the findings.

Firstly, the regional specificity of the study is a notable constraint. Focused solely on Kitui County, the findings may not seamlessly extrapolate to other regions within Kenya or beyond. Varied economic, social, and cultural contexts across regions could influence the dynamics between MFIs and SMEs differently.

Secondly, the study's reliance on data up to December 31, 2020, introduces a temporal limitation. The dynamic nature of the financial landscape and economic conditions implies that recent changes or developments in the microfinance sector may not be adequately captured, potentially impacting the study's relevance

Furthermore, the absence of longitudinal data restricts the ability to track the enduring impact of microfinance interventions on SMEs. A more comprehensive understanding of the evolving relationship between MFIs and SMEs over time necessitates longitudinal data, which this study lacks.

Lastly, potential bias in the study cannot be overlooked. Depending heavily on existing literature, surveys, and reports introduces inherent biases from these sources. Additionally, self-reported data from SMEs and MFIs may be susceptible to response bias, influencing the accuracy of the information.

Despite these limitations, this study provides an initial exploration of the relationship between microfinance institutions and SMEs in Kitui County. Subsequent research efforts should strive to address these limitations and extend the inquiry to assess the broader application of results.

5.6 Suggestions for Further Studies

Expanding the scope of this study to include small and medium-sized enterprises (SMEs) in other countries holds significant promise for advancing our understanding of the nuanced effects of microfinance services on financial performance. Cultural, economic, and regulatory differences among nations may introduce variations or

convergences in the outcomes observed, offering valuable insights into the adaptability and universality of microfinance interventions. Comparative analyses across diverse contexts could unveil patterns that may have been overlooked in a single-country study, contributing to a more comprehensive and globally applicable knowledge base.

The study's residual, constituting 17.7%, signals the presence of unexplored factors that transcend the current research focus. To unravel these mysteries, future investigations should delve into these residual elements, conducting in-depth analyses to identify and understand the underlying dynamics influencing financial performance. This pursuit may involve exploring broader economic trends, socio-political factors, or industry-specific variables that were not considered in the initial study.

Moreover, there is a clear call for further research to assess the impact of additional microfinance services within the financial services sector. As the landscape of financial services evolves, examining the effects of diverse microfinance offerings can elucidate their individual and collective contributions to the overall financial well-being of businesses. This avenue of research is essential for shaping targeted policies and strategies that leverage the full spectrum of microfinance services to foster sustainable economic development. In conclusion, extending this study's reach to new geographies and probing the unexplained residual will enrich our understanding of microfinance's multifaceted impact, guiding future efforts to optimize financial services for diverse enterprises worldwide.

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7 APPENDIX QUESTIONNAIRE

1. How is your business financed in order to grow?

- a) MFI {Loan} { }
- b) Borrowing from friends { }
- c) Personal saving { }
- d) Commercial bank { }
- e) Loan from sacco { }

2. How would you rate MFIS loan services received when accessing loan for the growth on your business?

- a) Excellent { }
- b) Very good { }
- c) Good { }
- d) Poor { }
- e) Very poor { }

3. How would you rate the effect of MFIS loan on growth of business?

- a) Very high { }
- b) High { }
- c) Neutral { }
- d) Low { }
- e) Very low { }

4. How can you rate the challenges of accessing the MFIS loan on the growth on SMES?

- a) Most challenging { }
- b) Very challenging { }
- c) Challenging { }
- d) Less challenging { }
- e) Not challenging { }

5. How can you rate the challenges of accessing the MFIS loan on the growth on SMES?

- a) Most challenging { }
- b) Very challenging { }
- c) Challenging { }
- d) Less challenging { }
- e) Not challenging { }

Section 3: Role of MFIS training on growth of SMES

6. How various training programmes offered by MFIS would facilitates on the growth of business?

- a) Most effective { }
- b) Effective { }
- c) Less effective { }
- d) Not effectives { }

7. How would management skills received from financial institutions affect the growth of business?

- a) Very high { }
- b) High { }
- c) Neutral { }
- d) Low { }
- e) Very low { }

Section 4: Role of MFIS advisory service on growth of SMES

8. How would you rate the advisory services offered by MFIS on the growth?

- a) Excellent { }
- b) Very good { }
- c) Good { }
- d) Poor { }
- e) Very poor { }

9. How would you rate savings account with MFIS on the growth of business?

- a) Very strong { }
- b) Strong { }
- c) Not strong { }
- d) Not influential { }

10. How would you rate effect of advises of savings from micro financial institutions on growth of business?

- a) Most effective { }
- b) Very effective { }
- c) Effective { }
- d) Less effective { }
- e) Not effectives { }

Section 5 Role of technology on growth of SMEs

11. To what extent has the adoption of technology positively impacted your SME's operational efficiency and productivity?

- a) Strongly Improved

- b) Moderately Improved
- c) No Significant Change
- d) Moderately Declined
- e) Strongly Declined

12. Have you integrated e-commerce or online platforms for sales and marketing in your SME?

- a) Highly Effective
- b) Somewhat Effective
- c) Neutral
- d) Not Very Effective
- e) Ineffective

13. How do you perceive the role of technology in enhancing customer engagement and satisfaction in your SME?

- a) Greatly Improved
- b) Moderately Improved
- c) No Significant Impact
- d) Moderately Decreased
- e) Greatly Decreased

Section 6 of performance or what you are calling growth of SMEs

14. To what extent has access to affordable loan positively influenced the growth and expansion of your SME in the past year?

- a) Strongly Disagree

- b) Disagree
- c) Neutral
- d) Agree
- e) Strongly Agree

15. In your opinion, what are the main obstacles or challenges that have hindered the growth and development of SMEs in your industry or region?

- a) Not a Challenge
- b) Slight Challenge
- c) Moderate Challenge
- d) Significant Challenge
- e) Major Challenge

16. Have you utilized government support programs or incentives aimed at promoting SME growth, and if so, to what extent have these initiatives contributed to your business's expansion and success?

- a) Not at all Contributory
- b) Slightly Contributory
- c) Moderately Contributory
- d) Significantly Contributory
- e) Extremely Contributory