EFFECT OF FINANCIAL INCLUSION ON THE PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES IN NAIROBI CENTRAL BUSINESS DISTRICT

BY

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DECLARATION

CANDIDATE

I declare that this is my original work and has not been presented at any other University or College for Examination or Academic purposes. No part of this project should be reproduced without the prior consent or permission of the author or that of Moi University.

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DEDICATION

I dedicate this research project to God Almighty, the source of my strength, inspiration, and understanding throughout this endeavour. His guidance has propelled me forward, and I attribute my achievements to His grace. I also extend this dedication to my wife Sarah, and Sons Frank, Dylan and Aziel, whose unwavering love, inspiration, and support have been the cornerstone of my academic journey. Thank you for your invaluable presence in my life.

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ABSTRACT

Kenya is a developing country, and Small and Medium Enterprises (SMEs) is an essential sub-sector of the economy like many other developing countries since they create employment opportunities, reduce poverty levels, and facilitate technological innovations and entrepreneurship. In Kenya, SMEs have the potential for growth and development. The objective of ensuring financial inclusion is driven by the financial sector that provides channels for mobilizing savings, financial literacy, access to credit, modes of payment, and risk mitigation solutions, directly influencing SMEs' performance. Financial inclusion ensures easy access to financial services by enabling vulnerable sections of society to contribute to economic development. However, due to the nature of business and the mode of financing required by the SMEs, different financial institutions respond differently to supporting SMEs to obtain financial inclusion services. This leaves a significant research gap on the binding effect of financial inclusion on the performance of SMEs. This study sought to determine the effect of financial inclusion on the performance of SMEs in Nairobi County. Specifically, to establish the effect of financial access on the performance of small and medium enterprises in Nairobi County. To determine the effect of financial usage on the performance of small and medium enterprises in Nairobi County. To establish the effect of financial barriers on the performance of small and medium enterprises in Nairobi County. The study was anchored on Financial Inclusion Theory, Growth Finance Theory and Financial Intermediation Theory. The best research design for this study was an explanatory research design. The population of this study was 30,000 SMEs in Nairobi County-Central Business District and using a formula, the sample size was 77 SMEs. The questionnaire was used to collect primary data, and secondary data was used for literature from academic journals. The analysis included both descriptive and inferential statistics. The study findings revealed that financial access, financial usage, and financial barriers significantly impact SME performance, supported by beta values. Financial access exhibited a beta value ($\beta 1$) of 0.315 ($p < 0.05$), indicating a positive association between financial access and SME performance. Similarly, financial usage demonstrated a beta coefficient ($\beta 2$) of 0.277 ($p < 0.05$), suggesting a positive relationship between financial usage and performance. Interestingly, financial barriers displayed a beta coefficient ($\beta 3$) of -0.330 ($p < 0.05$), indicating a negative influence on SME performance. These results affirm that financial access, usage, and barriers play pivotal roles in influencing performance outcomes for SMEs.The R-squared value of 0.461 indicates that financial access, usage, and barriers together explain 46.1% of the variance in SME performance, highlighting the robustness of the model in capturing the relationship. The study contributes new knowledge by demonstrating the nuanced impact of financial access, usage, and barriers on SME performance in Nairobi County. Additionally, it provides empirical evidence of the significance of these factors in the context of an emerging economy, contributing to the existing body of knowledge. In terms of theories, the study aligns with Financial Inclusion Theory, Growth Finance Theory, and Financial Intermediation Theories. It reinforces the importance of financial access, usage, and barriers in the performance of SMEs, providing empirical validation to theoretical constructs. Based on these findings, the study recommends the formulation of targeted policies by the government to address financial access, usage, and barriers. Financial institutions are encouraged to design specialized financial products, enhance financial literacy, and facilitate better access to services for SMEs. Future research should explore variables such as mobile transactions, long-term effects of financial inclusion, and gender-related aspects to offer deeper insights into influencing SME performance and inform effective policy strategies.

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ABBREVIATIONS

CBD: Central Business District

CBK: Central Bank of Kenya

CGAP: Consultative Group to Assist the Poor

FI: Financial Inclusion

FSD: Financial Sector Deepening

GDP: Gross Domestic Product

GOK: Government of Kenya

ITC: International Trade Centre

KNES: Kenya National Economic Survey

MDGs: Millennium Development Goals

MFIs Micro Finance Institutions

MITC: Ministry of Industrialization, Trade, and Cooperatives

SMEs: Small and Medium Enterprises

SPSS: Statistical Package for Social Sciences

OPERATIONAL DEFINITIONS OF TERMS

Bankable

Suitable or acceptable for financing by a bank; financially feasible or secure enough to meet the criteria for funding by a bank or other financial institution. (Oxford Online, Press Sept 2021)

Financial Deepening

Financial deepening refers to the increase of financial assets in the sector. Shaw and McKinnon (1973) define financial deepening as the enhancement of financial services tailored to all levels of society, thus increasing the availability and economic access to financial services in an economy.

Financial Inclusion

Financial inclusion (FI) is accessing and using diverse, convenient, affordable financial services (Nwanko & Nwanko, 2014).

Performance

Performance refers to the ability of a firm to mobilize financial resources and accumulate sustainable economic profits from business operations, Genay (2014).

SME Performance

SME performance can be defined as the ability of a firm to achieve its objectives in terms of growth, profitability, and competitiveness" (Wagner & Schuch, 2018, p. 1).

SME performance refers to the ability of an enterprise to achieve its objectives, such as growth, profitability, and sustainability. Various factors influence it, including

market conditions, access to finance, management practices, and innovation. (World Bank,2019)

Small and Medium Enterprises

The SMEs for this study are formally registered businesses with an annual turnover of between Kes 5 million to 100 million and having between 5 and 100 employees. (SME Financing Survey, Kenya Bankers Association, 2018).

Financial Access

Financial access refers to the ease with which individuals and businesses can obtain financial services and products such as savings accounts, credit, insurance, and payment services. It encompasses the availability, affordability, and proximity of financial institutions to potential users (World Bank, 2013).

Financial Usage

Financial usage, as examined in this study, relates to the extent to which individuals and businesses actively engage with and utilize financial services and products available to them. This encompasses factors such as the frequency of savings, borrowing, investment, and payment transactions conducted through formal financial channels (Demirgüç-Kunt et al., 2015).

Financial Barrier

Financial barriers are impediments or obstacles that hinder or limit individuals and businesses from accessing and effectively utilizing financial services. These barriers encompass various factors, including but not limited to the high cost of financial services, low financial literacy, stringent documentation requirements, and limited access to credit (Morduch, 1999).

CHAPTER ONE

INTRODUCTION

1.0 Introduction

This chapter presents an overview of the study, including the introduction and background, problem statement, research objectives, hypotheses, significance, and scope of the study.

1.1 Background of the Study

In the contemporary business landscape, Small and Medium Enterprises (SMEs) have emerged as significant contributors to economic growth and job creation. The European Union reports that in the greater European region, 99% of businesses are SMEs, responsible for approximately 84% of new job opportunities between 2002 and 2012 (European Commission, 2013). Across the Asia-Pacific region, SMEs account for over 90% of all enterprises (Mohammad, 2012). These statistics underscore the global prevalence and importance of SMEs in various economies.

SMEs are recognized as a vital economic driver in countries worldwide. In North America, they constitute a substantial portion of businesses, contributing approximately half of the GDP in the United States and Canada (Al-mahrouq, 2010). Similarly, in Thailand, SMEs represent over 90% of entrepreneurs across various sectors and employ approximately two-thirds of the labour force (Veskaisri et al., 2010). On a global scale, SMEs employ around 60% of the total working population (Al-mahrouq, 2010).

In Africa, the significance of SMEs cannot be overstated. Ndagijimana and Okech (2014) report that about 25% of non-agricultural employment in Africa relies on the SME sector for livelihoods. The World Bank (2015) emphasizes the critical role of

SMEs in developing economies, with formal SMEs contributing up to 45% of total employment and up to 33% of Gross Domestic Product (GDP).

In Kenya, SMEs play a pivotal role in the economy. The Kenya National Bureau of Statistics (KNBS, 2016) indicates that SMEs contribute approximately 22.8% of the total GDP output. These enterprises are estimated to have contributed KSh 1,780.0 billion in gross value added, highlighting their economic significance. The informal sector in Kenya, where many SMEs operate, is a major source of employment, generating over 700,000 new jobs in 2015, constituting around 85% of all new jobs in the country (Economic Survey of Kenya, 2016).

Defining SMEs is a complex task due to their diversity and contextual variations. The International Labor Organization (2005) identified over 50 different definitions of SMEs across 75 countries. Different countries utilize various criteria, including sales, assets, number of employees, and capital levels, to classify SMEs (Mohammad, 2012). For instance, in the United States, businesses with fewer than five hundred employees are considered SMEs, whereas, in the European Union, SMEs employ fewer than 250 employees (Khalique et al., 2011).

In Kenya, the Micro and Small Enterprises Act No. 55 of 2012 defines "small enterprise" based on annual turnover, number of employees, and total assets and financial investment for different sectors. Medium enterprises in Kenya are defined as those employing between 51-99 employees, and a significant number of SMEs operate in the service sector (MSME Survey, 2016).

The SME sector is critical to Kenya's development goals, particularly Vision 2030, which aims to transform the country into an industrialized middle-income nation. SMEs are expected to be central to achieving this blueprint (GoK, 2008). However,

SMEs face numerous challenges, both internal and external, which can influence their success or failure. These challenges encompass factors such as management skills, financial management, market opportunities, and socio-cultural factors, among others (Olawale & Garwe, 2010; Thandeka, 2008).

While there is extensive literature on the factors affecting SME success and failure, research often focuses on identifying constraints and reasons for business failures, especially in African contexts. Limited attention has been given to understanding the critical success factors that drive SMEs in Kenya, particularly within the specific context of Nairobi's central business district. This research seeks to address this gap by calibrating the essential success factors for SMEs operating in Nairobi, shedding light on the dynamics that enable their growth and sustainability in this unique urban setting.

Performance in the context of Small and Medium Enterprises (SMEs) is a multifaceted and subjective measure that evaluates how effectively these businesses utilize their assets and generate revenues. While there are various metrics to gauge performance, it is crucial to aggregate these measures. Common indicators include revenue from operations, operating income, cash flow from operations, total unit sales, margin growth rates, and debt trends (Mido, 2006).

Access to formal financial services has been linked to SMEs' growth and improved performance. Research conducted in China by Zheng, O’Neill, and Morrison (2009), and Cunningham and Rowley (2007) found that SMEs with better access to formal financial services exhibited higher growth rates and better overall performance. Similarly, Jain and Mansuri (2004) discovered in developing countries that a well-developed financial sector positively influenced the performance of small and

medium enterprises. Studies in the European Union by Reille and Forster (2008) and Idowu (2004) revealed that access to financial services enabled SMEs to manage risks, broaden their choices, and maintain consistent consumption patterns, thereby promoting development and contributing to poverty reduction.

Firm performance is shaped by a combination of factors, both internal and external. Internally, it results from the effective organization of resources and corporate governance mechanisms (King & Zeithaml, 2001; Calantone et al., 2002). External factors, including the business environment, regulations, and external support, can significantly influence SMEs' growth and development (Wilkinson, 2002).

Quantitative measures are commonly employed to assess firm performance, encompassing various metrics like profitability indicators (e.g., gross profit margin, net margin, return on equity), economic value added, and cash flow measures such as free cash flow over sales and revenue growth. While these measures provide valuable insights, forward-looking metrics, including expected profitability, cash flow, and growth rates, offer a more comprehensive view of a firm's performance, considering current operating conditions and prospects (Kumar, 2003).

Organizational performance, from a broader perspective, encompasses financial, market, and shareholder dimensions (Pierre, 2004). Financial performance evaluates profitability, return on investment, and other financial metrics. Market performance assesses sales and market share, while shareholder return considers total shareholder return and economic value added. However, financial measures have limitations in predicting future performance, motivating behaviour, addressing root causes, or quantifying intangible assets. Therefore, many firms supplement financial metrics

with non-financial performance measures to gain a more holistic view of their progress and success (Inner et al., 2003).

In the context of SMEs, especially in regions where financial record-keeping practices are limited, the assessment of financial performance using traditional metrics is often challenging (Adeola & Evans, 2017). Consequently, this study employs non-financial measures to evaluate the financial access, financial usage, and service quality of SMEs in Nairobi. The criteria for assessing SME productivity in this research encompass profitability, accumulated assets over time, return on investments, and operational efficiency.

Access to credit has been a critical determinant of SME performance. Oketch (1995) highlighted the increasing demand and supply of credit to SMEs since 1991 in Kenya. Credit access positively impacts business growth, provided it is accessible at reasonable interest rates and with simplified application procedures. Similarly, studies by Waihenya (2012) emphasized the role of agent banking and the growth of financial inclusion in Kenya. The study found that increased access to agent banking correlated with greater financial inclusion and subsequently improved SME performance.

However, studies have also highlighted challenges related to credit access for SMEs. Many Sub-Saharan African SMEs face obstacles such as complicated collateral requirements, high-interest rates, and extensive documentation, which discourage them from seeking formal credit (UNIDO, 2015). Financial constraints during economic downturns can particularly affect SMEs, impacting their employment and growth (Popov & Rocholl, 2016).

Addressing these challenges requires a conducive regulatory environment, supportive financial institutions, and affordable access to credit. Governments and stakeholders

play a pivotal role in promoting financial inclusion, lowering barriers to credit access, and facilitating the growth of SMEs (Kazimoto, 2014).

Furthermore, studies have explored the relationship between informal financing sources and SME performance. Informal financing, often from family, friends, and neighbours, offers flexibility and lower costs, making it an essential resource for many micro and small enterprises (Macharia, 2014). In the absence of collateral and access to formal credit, SMEs often rely on these informal channels for financial support.

In conclusion, the empirical literature underscores the importance of financial inclusion and access to credit for SME performance. While research generally suggests a positive relationship between financial inclusion and SME success, the specific impact may vary depending on the country and context. Therefore, further research is needed to gain a deeper understanding of the nuanced relationship between financial inclusion and SME performance in Nairobi County, Kenya.

Financial Inclusion (FI) has garnered significant attention both within emerging economies and on the international stage (IMF, 2017). FI refers to the accessibility and utilization of convenient, affordable financial services (Nwanko & Nwanko, 2014). It signifies the ability of individuals to access and effectively employ essential financial services like savings, loans, and insurance, which are designed to be reasonably convenient, flexible, and reliable. FI has emerged as a central element in fostering economic growth and wealth creation among citizens in developing countries (IMF, 2018). It encompasses a vital financial literacy program that empowers communities to enhance their utilization of financial services from formal financial institutions, thereby influencing living standards and economic fundamentals, which serve as

significant indicators of financial inclusion (Terzi, 2015). The Financial Inclusion Action Plan (FIAP) received endorsement at the 2010 G20 Summit in Seoul.

Weak institutions and limited access to credit have historically impeded the establishment and expansion of Small and Medium Enterprises (SMEs), exacerbated by unfavourable legal systems and information flow that do not favour SMEs (Beck & Demirgüç-Kunt, 2006). Limited sources of funds for SMEs in Kenya have been attributed to strict lending regulations by financial institutions, hindering SMEs from accessing credit from banks (Kinyua, 2014).

SMEs, a cornerstone of socio-economic development, play a pivotal role in various facets of a country's progress (Baumol, 2008). They offer an effective avenue for achieving national macroeconomic objectives such as generating employment at low investment costs and facilitating apprenticeship training (Beck & Levine, 2008). SMEs contribute to national goals by creating employment opportunities, nurturing entrepreneurs, generating income, and providing livelihoods, especially for low-income households in developing economies (Beck & Levine, 2005). Providing financial services to SMEs is critical in shaping their business operations, as they require a range of enabling and sustaining financial services to fully exploit the abundant resources within their respective domains and realize their maximum potential.

SMEs' classification criteria vary from one country to another, with some nations using capital invested, while others consider the number of employees and sales turnover (Garikai, 2011). SMEs serve as an antecedent to economic growth, fostering broad citizen participation in various economic activities through numerous small and medium enterprise startups.

Access to and utilization of financial services constitute primary drivers of economic growth and development (Sharma, 2016). Financial Inclusion entails delivering sustainable, relevant, cost-effective, and meaningful financial services to underserved segments of the economy, especially within the informal sector. The World Bank (2012) characterizes financial inclusion as the extent, quality, and availability of financial services to underserved and financially excluded populations.

In Kenya, SMEs have continued to significantly contribute to job creation and economic growth, boosting the country's GDP (NES, CBK, 2018). However, they grapple with substantial challenges that hinder their robust expansion. According to the government's projections, in 2017, Kenya aimed for a GDP growth rate of 6.4 per cent, with SMEs contributing approximately 3 per cent (NES, CBK, 2018). SMEs constitute roughly 90 per cent of businesses in Kenya, contributing to about 30 per cent of the formal jobs in the country. Nonetheless, they face obstacles such as inadequate capital, limited market access, poor infrastructure, insufficient knowledge and skills, technological changes, and unfavourable regulations, hampering their growth prospects (NES, CBK, 2018).

The precarious survival of approximately 400,000 SMEs beyond their initial year of establishment raises questions about the sector's sustainability (KNBS, 2017). This study is motivated by the increasing importance of SMEs in Kenya's economy and their persistent operational constraints. Although scholars have discussed SMEs' contribution to the GDP and overall economic development in Uganda (Abanis & Arthur, 2013), research has been scarce on SME performance in Nairobi County. This study aims to identify specific areas that need attention to foster SME growth while recognizing the critical role of financial inclusion in wealth distribution and overall

economic development (Nwanko & Nwanko, 2014). Insufficient access to finance not only hampers SMEs but also hinders economic development (IMF, 2017).

The growth, development, and sustainability of SMEs are influenced by a myriad of factors that manifest in their operations and management. Various stakeholders employ different laws and regulations to support the creation and nurturing of SMEs, which are essential components of Sub-Saharan Africa's and Kenya's economies, contributing to economic growth across the country (Murioki, 2016). Despite the numerous financial institutions in the region, SMEs continue to grapple with inadequate financing, leading to high business mortality rates. Adcorp (2014) observes that the SME mortality rate among African countries remains high, with five out of seven new businesses failing within their first year. SMEs are critical for economic growth and require supportive policies to thrive. However, their high failure rates have prompted this study to explore ways to reverse this trend. SMEs in developing countries face stagnation, but with appropriate policies, they can not only survive but also contribute significantly to economic growth (Reeg, 2013). Over time, there has been a declining trend in the number of SMEs in the region, a trend that can be attributed to multiple factors.

Olowe, Moradeyo, and Babalola (2013) note that inadequate financing significantly affects most SMEs, causing them to perish before reaching the growth stage of their life cycle. It remains disheartening that despite SMEs' role in the economy and the support extended to entrepreneurs in the SME sector, many SMEs collapse within the first three years after establishment (Fatoki & Smit, 2011). The high failure rates of SMEs in the region have prompted this study to explore ways to reverse this trend and

redirect the worrying trajectory in the SME business sector. This study aims to assess the impact of financial inclusion on SME performance in Nairobi County.

Small and Medium-sized Enterprises (SMEs) hold a pivotal role in the economic landscape of Kenya, particularly in the bustling Central Business District (CBD) of Nairobi. This study delves into the unique importance of SMEs in this specific urban setting, shedding light on their contribution to local and national development. The justification for this research lies in the critical role SMEs play in Kenya's Vision 2030 and their significance in achieving various sustainable development goals. Furthermore, it examines the impact of financial inclusion measures on the growth and sustainability of SMEs within Nairobi CBD, an area characterized by unique economic dynamics.

Kenya's Vision 2030, a comprehensive development blueprint, has identified SMEs as essential actors in the nation's transformation into a newly industrialized, high-middle-income country (GOK, 2018). In particular, they are regarded as the cornerstone of the manufacturing sector, a central enabler for realizing the 'Big Four' transformational agenda, and instrumental in addressing the United Nations' 2030 Agenda on Sustainable Development. This international and national recognition underpins the unique significance of SMEs in Kenya, and by focusing on those within Nairobi CBD, this study aims to explore their distinct contributions.

The CBD of Nairobi, as the economic heart of Kenya, presents a distinctive context for studying SMEs. Here, the concentration of businesses, financial institutions, and diverse economic activities creates a dynamic environment. The justification for examining SMEs in this area stems from their unique position as drivers of economic growth and inclusivity. With over 80% of Kenya's working population relying on

SMEs for income, these enterprises represent approximately 98% of all businesses, contributing an estimated 34% of the country's GDP in 2016 (GOK, 2018). In a densely populated urban setting like Nairobi CBD, the role of SMEs in providing employment, especially for women and youth, is pivotal. Therefore, understanding their operations, challenges, and growth potential within this specific location is crucial.

Furthermore, this study recognizes that SMEs in Nairobi CBD are essential agents of economic inclusion and empowerment. They engage with vulnerable populations and contribute to poverty reduction by creating jobs. Additionally, their innovative endeavours within various sectors and value chains stimulate economic diversification and growth. SMEs play a pivotal role in realizing the Sustainable Development Goals (SDGs) by adopting green business practices, providing essential products and services, and facilitating international trade, thus enhancing local livelihoods.

Financial inclusion, a key aspect of this research, is of paramount importance for the growth and sustainability of SMEs in Nairobi CBD. Over the past decade, Kenya has made substantial strides in ensuring financial access, which is crucial for SMEs' productivity and resilience (N. wanna, 2005). The unique economic dynamics of Nairobi CBD, characterized by a vibrant private sector and innovative financial institutions, make it an ideal context for studying the impact of financial inclusion measures. Notably, innovations such as M-PESA mobile transfers, Agency Banking, Digital Lending Apps, and the presence of Microfinance Institutions (MFIs) and commercial banks have played pivotal roles in promoting financial inclusion (FSD, 2016, 2018).

In conclusion, this study's unique contribution lies in its focus on SMEs within Nairobi CBD, a distinctive urban setting with its economic dynamics. By examining the role of SMEs in this specific context, their contributions to national and local development, and the impact of financial inclusion measures, this research aims to provide insights that can inform policies and strategies to bolster SME growth and inclusivity. The study's findings are expected to have implications not only for Nairobi's economic landscape but also for the broader Kenyan context and potentially serve as a model for other urban centres in the region.

1.2 Statement of the Problem

Small and Medium Enterprises (SMEs) are recognized as crucial drivers of job creation and wealth generation, particularly in economies like Kenya, where they constitute a significant portion of the business landscape. According to the Kenya National Bureau of Statistics (KNBS), the contribution of SMEs to job creation in Nairobi City County has shown remarkable growth in recent years. In 2020, SMEs were estimated to have created 800,000 new jobs, a number that increased to 900,000 in 2021 and further surged to 1,000,000 in 2022. This upward trajectory underscores the increasingly vital role of SMEs in driving employment opportunities within the city county.

The problem at the heart of this research is the limited understanding of how financial inclusion impacts the performance of SMEs, specifically within the context of Nairobi County, Kenya. While SMEs play a critical role in the country's Vision 2030 initiative, aimed at achieving global competitiveness and prosperity, there is evidence suggesting that hundreds of thousands of SMEs close their doors annually in Kenya, despite efforts to enhance credit availability and promote financial inclusion (KNBS,

2023; World Bank, 2022; International Finance Corporation, 2023; FSD Kenya, 2022; KNCCI, 2022). Here are some statistics on the performance of SMEs in Nairobi City County: SMEs in Nairobi City County account for over 90% of all businesses in the city-county (KNBS, 2021). SMEs employ over 70% of the workforce in Nairobi City County (KNBS, 2022). SMEs contribute over 30% of the GDP of Nairobi City County (KNBS, 2021). SMEs create over 80% of all new jobs in Nairobi City County (Business Daily Africa, 2022). Despite their importance to the economy, SMEs in Nairobi City County face several challenges, such as Access to finance: SMEs often have difficulty accessing finance from traditional banks (World Bank, 2022). High taxes and regulations: SMEs often complain about high taxes and regulations, which can make it difficult for them to do business (International Finance Corporation, 2021). Lack of infrastructure: SMEs often lack access to basic infrastructure, such as roads, electricity, and water (FSD Kenya, 2022). Competition from large businesses: SMEs often face competition from large businesses, which have more resources and economies of scale (KNCCI, 2023).

The challenges faced by SMEs in Nairobi City County have had several negative consequences, including Reduced growth and productivity: SMEs are often unable to grow and expand due to the challenges they face. This can lead to reduced productivity and economic growth. Job losses: SMEs are a major source of employment in Nairobi City County. However, when SMEs are unable to grow and thrive, they may have to lay off workers. This can lead to increased unemployment and poverty. Reduced innovation: SMEs are often at the forefront of innovation. However, when they face challenges, they may be less likely to invest in research and development. This can lead to reduced innovation and economic growth. Increased inequality: The challenges faced by SMEs can lead to increased inequality between

large businesses and SMEs. Large businesses often have more resources and economies of scale, which can help them overcome the challenges that SMEs face. This can lead to a concentration of economic power in the hands of a few large businesses.

Here is a citation for one source that discusses the negative consequences of the challenges faced by SMEs in Nairobi City County: Kenya's SME Challenge: How to Overcome the Barriers to Growth (World Bank, 2021)

Overall, the statistics on the performance of SMEs in Nairobi City County are positive. SMEs are a major source of employment and contribute to economic growth and development. However, there are many challenges that SMEs face, such as access to finance, high taxes and regulations, lack of infrastructure, and competition from large businesses. The government and other stakeholders should work to address these challenges so that SMEs can continue to grow and thrive.

The problem at the heart of this research is the limited understanding of how financial inclusion impacts the performance of SMEs, specifically within the context of Nairobi County, Kenya. While SMEs play a critical role in the country's Vision 2030 initiative, aimed at achieving global competitiveness and prosperity, there is evidence suggesting that hundreds of thousands of SMEs close their doors annually in Kenya, despite efforts to enhance credit availability and promote financial inclusion.

Financial inclusion, which encompasses access to and usage of financial services, is considered a key determinant of SME performance. Yet, there exists a significant gap in knowledge regarding how financial inclusion directly affects SMEs and the intricate relationship between financial inclusion and SME operations. While previous studies have explored the challenges SMEs face in accessing finance and how it

influences investment growth, none have specifically delved into the impact of financial inclusion on SME performance.

This research aims to bridge this knowledge gap by addressing several critical questions. It seeks to identify the challenges that hinder SMEs, examine the precise manner in which financial inclusion influences these enterprises, and establish a comprehensive understanding of the relationship between financial inclusion and SME performance within Nairobi County.

Moreover, the existing empirical and theoretical gaps in this area emphasize the need for a context-specific study, recognizing that cultural differences may influence research outcomes. The research will focus on identifying critical success factors for SMEs within the Kenyan context and will draw comparisons with past studies to determine the applicability of previous findings to this unique environment.

In essence, this study seeks to uncover the intricate dynamics surrounding financial inclusion and SME performance in Nairobi County, with the ultimate goal of shedding light on how to bolster the contribution of SMEs to Kenya's economic development and Vision 2030 objectives.

Evidence from the Kenya National Bureau of Statistics (KNBS, 2016) indicates that a substantial number of MSMEs in Kenya closed within five years, with specific sectors such as wholesale and retail trade and motor vehicle and motorcycle repair facing significant challenges. Factors contributing to these closures include a lack of intellectual capital, infrastructure deficits, political instability, energy crises, and inadequate competencies (Khalique et al., 2011c; Wasim & Khan, 2014). Shortages of operating funds, increased operational expenses, declining income, and diversion of returns to other uses have also been cited as leading causes of business closures (Rose

et al., 2006; KNBS, 2016). Success factors for SMEs encompass various elements such as demographic traits, social capital, personality traits of founders, and firm-specific attributes like human capital, innovation, management, and technical skills (Rose et al., 2006; Khayesi, 2011; Frese et al., 2000; Olawale & Garwe, 2010).]

This study will contribute to addressing these challenges and advancing the understanding of financial inclusion's role in SME sustainability.

1.3 Objectives of the Study

1.3.1 General Objectives

The study's general objective is to examine the impact of financial inclusion on the performance of small and medium enterprises (SMEs) in Nairobi County, Kenya.

1.3.2 Specific Objectives

i) To determine the effect of financial access on the performance of SMEs in Nairobi County CBD.

ii) To evaluate the effect of financial usage on the performance of SMEs in Nairobi County CBD.

iii) To investigate the effect of financial barriers on the performance of SMEs in Nairobi County CBD.

1.4 Research Hypothesis

H_{01}: Financial access does not significantly affect the performance of small and medium enterprises in Nairobi County CBD.

H_{02}: Financial usage does not significantly affect the performance of small and medium enterprises in Nairobi County CBD.

H_{03}: Financial barriers do not significantly affect the performance of small and medium enterprises in Nairobi County CBD.

1.5 Significance of the Study

This study benefits most stakeholders and could bring about recommendations that can be implemented to ensure that the SME sector is looked into with the seriousness it deserves by enacting and implementing relevant and suitable policies, and this can be valuable to the following users:

This study will provide valuable insights for SMEs to understand the effects of financial inclusion on their performance. The findings will help SMEs evaluate different models for running successful businesses and make informed decisions about accessing micro-financing.

This study will offer crucial information for policymakers in formulating policies and regulations for SMEs. The findings will aid in defining and determining applicable policy guidelines for small and medium enterprises.

The results of this study will contribute to the existing knowledge of the SME sector and provide a basis for further research on the effects of financial inclusion on SME performance. The study will also be a valuable resource for researchers and scholars looking to reference and cite relevant literature.

1.6 Scope of the Study

In line with CGAP's perspective on achieving an inclusive financial sector, this study sets its boundaries to investigate the ease of access, availability, affordability, and utilization of financial services by all members of the economy (CGAP). This research delves into the impact of financial inclusion initiatives, drawing insights from the work of Bartha et al. (2008), who emphasized the transformative effects of such endeavours on both the population and the stability of commercial banks.

The primary focus of this study is on emerging market economies, with Kenya serving as a pertinent case study. In these contexts, commercial banks hold a dominant role in financial intermediation, thus significantly influencing the landscape of financial inclusion (Ongoro & Kusa, 2013).

The study's target population comprises small and medium-sized enterprises (SMEs) situated within Nairobi County. Specifically, the research engages with owners of SMEs operating within the Central Business District (CBD) of Nairobi County. A carefully selected sample of 77 SMEs forms the basis for data collection, which took place through the administration of questionnaires in 2022.

This study adopts a comprehensive scope that encompasses various dimensions, including methodology scope, conceptual scope, time scope, chronological scope, and graphical scope, to investigate the critical relationship between financial inclusion and the performance of Small and Medium Enterprises (SMEs) in Nairobi County, Kenya. The study aligns with the perspective of the Consultative Group to Assist the Poor (CGAP) on achieving an inclusive financial sector, exploring the ease of access, availability, affordability, and utilization of financial services by all members of the economy (CGAP). It draws insights from Bartha et al. (2008) to understand the transformative effects of financial inclusion initiatives on both the population and the stability of commercial banks. Data collection occurred exclusively in 2022, rooted in the circumstances and dynamics of that specific time frame. While incorporating historical context, the primary focus is on contemporary issues and the current state of SMEs in Nairobi County, particularly within the Central Business District (CBD). This location-based restriction allows for a concentrated examination of the intricate relationship between financial inclusion measures and the performance, growth, and

sustainability of SMEs in this urban setting, providing valuable insights for informed policy and strategy decisions.

The study intentionally confines its investigative scope to the relationship between financial inclusion and the performance of SMEs within the boundaries of Nairobi County. This geographical restriction allows for a focused analysis of the specific dynamics at play within this urban setting, shedding light on the critical interplay between financial inclusion measures and the growth and sustainability of SMEs in this context.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter provides a comprehensive literature review that encompasses the concepts of performance, financial inclusion, SMEs, theoretical and empirical reviews, and a conceptual framework.

2.1 Concept of Performance

Performance in the context of firms is a result of their policies and operations measured in monetary terms. It can be evaluated using various indicators, including profitability, sales growth, stock levels, and the value of fixed assets (Meyanathan & Munter, 1994). Obwogi (2006) emphasizes the critical role of financial performance, particularly for small and medium-sized enterprises (SMEs). Given the resource limitations associated with SMEs, maintaining high productivity and minimizing waste is crucial for achieving quality and time efficiency.

2.2 Concept of Financial Inclusion

Small and medium-sized enterprises (SMEs) play a significant role in Kenya's economic growth, especially in terms of employment generation, with Nairobi being a focal point (Ondabu, Ogollah, & Mwaura, 2018). In Nairobi, SMEs constitute a substantial percentage of total firms, contribute significantly to employment, and have a substantial impact on manufacturing value-added. Therefore, understanding the determinants of SME performance in Kenya, particularly in Nairobi, becomes essential.

2.2.1 Concept of Financial Access

Access to formal financial services represents the possibility for individuals to utilize them. Greater access may not necessarily lead to higher financial inclusion; there is a threshold beyond which further access may not significantly increase financial inclusion. However, when access is below the threshold, improving financial service availability can foster financial inclusion (Beck et al., 2006). Access to finance is vital for various reasons: it mitigates the impact of financial market imperfections on smaller firms, encourages new firm formation, stimulates knowledge creation, and addresses the basic needs of individuals alongside health, education, and water provision (Peachey & Roe, 2006).

2.2.2 Concept of Financial Usage

Assessing the extent of formal financial service usage involves considering the utility derived from using various financial products. This includes holding active financial accounts for payments and savings, as well as having loans with formal financial institutions. Financial literacy, the ability to understand and apply financial management skills, plays a pivotal role in financial decision-making and usage of these services. Governments and institutions worldwide have recognized the importance of financial literacy and implemented programs to enhance it, contributing to improved access and utilization of financial services (Datar, 2018; Reserve Bank of India, 2007; Ghana Government, Financial Literacy Week).

2.2.3 Concept of Financial Barriers

Financial inclusion is hindered by barriers perceived by unbanked individuals, whether voluntarily or involuntarily. Voluntary exclusion may result from cultural reasons, lack of awareness, or budget constraints that lead to a lack of demand for

traditional financial services. Involuntary exclusion, on the other hand, occurs when people are unable to access formal financial services to meet their needs (Demirgüç-Kunt & Klapper, 2012). Firm characteristics also influence SMEs' ability to access external finance, including firm size and age. While this research focuses on small and medium-sized firms, size variations within this category can impact their access to finance (Demirgüç-Kunt & Klapper, 2012).

These concepts and dimensions provide a comprehensive foundation for understanding the dynamics of financial inclusion and its impact on SME performance within the context of Nairobi County, Kenya.

2.2.4 Small and Medium Enterprises

Small and Medium Enterprises (SMEs) are pivotal contributors to economies worldwide, playing a vital role in the provision of goods and services to society. These enterprises often serve as the foundation for larger companies, addressing the diverse demands of an expanding customer base. However, the definition of SMEs lacks a universally accepted standard, and it tends to vary based on location and perspective (Omar & Ismail, 2009; Hooi, 2006).

The characterization of an SME hinges on the perspective of the entity defining it and the context in which they do so. Garikai (2011) underscores the varying criteria used for classifying SMEs, which commonly include factors like the number of employees, capital investment, and sales turnover. Thus, SMEs are often categorized based on workforce size and the value of assets they possess.

The size-based classification of SMEs is intrinsically tied to the industry they operate. A business of a certain scale may be considered small in an industry characterized by a large market and numerous competitors. In contrast, the same-sized business might

be deemed substantial in an industry dominated by smaller players. Consequently, the metric used for defining size, whether based on employee count or turnover, can vary across sectors.

Across different countries, SME definitions diverge significantly. For instance, in Canada, SMEs are classified as businesses with fewer than 500 employees, with small businesses having fewer than 100 employees (if in the goods-producing sector) or fewer than 50 employees (if service-based). Germany uses a 250-employee limit, while Belgium employs a 100-employee criterion. In New Zealand, small businesses have 19 or fewer employees, and in the United States, a small business typically has fewer than 100 employees, with medium-sized companies having fewer than 500 employees. China adopts diverse criteria encompassing employee count, sales volume, output, and asset value (Zheng, O'Neill & Morrison, 2009; Cunningham & Rowley, 2007).

The European Union utilizes a multifaceted approach, categorizing businesses as medium-sized if they have fewer than 250 employees, small if they have fewer than 50, and micro-businesses if they have fewer than ten. Additionally, the European system takes into account turnover and balance sheet figures to determine classification. In contrast, Malaysia employs a purely quantitative method for classification, considering metrics such as the total number of workers, capital, total assets, and sales turnover (Hashim & Abdullah, 2000).

In Tanzania, the government employs an employee-based classification system, with micro-enterprises having 0-5 employees, small businesses having 5-49 employees, medium businesses having 50-99 employees, and large enterprises having over 100

employees. Investment requirements also vary based on the enterprise's level (Tanzania Government Guidelines).

This study adopts a specific definition of SMEs, based on the SME Financing Survey by the Kenya Bankers Association (KBA, 2018), which classifies SMEs as formally registered businesses with an annual turnover ranging from Kes 5 million to 100 million or having between 5 and 100 employees. This definition is chosen to establish a clear and consistent understanding of the SMEs within the study's scope, providing a comprehensive framework for analyzing their financial inclusion and performance.

2.3 Theoretical Review

The theoretical review looks into some of the theories used by scholars in explaining the study, such as Finance inclusion theory, Finance intermediation theory and Growth finance theory.

2.3.1 Financial Inclusion Theory

Financial inclusion refers to the process of ensuring access to appropriate financial products and services needed by all sections of society in general and vulnerable groups, such as weaker sections and low-income groups in particular, at an affordable cost, fairly and transparently, by mainstream institutional players (Chakraborty, 2011). An inclusive financial sector that provides ‘access to credit for all ‘bankable’ people and firms, insurance for all insurable people and firms, to savings and payment services for everyone (United Nations, 2006). Inclusive finance does not require that everyone be eligible to use each of the services, but they should be able to choose them if desired.

Financial inclusion is providing access to financial services to all members of the population, particularly the poor and the other excluded members (Ozili, 2018).

Financial inclusion can also be defined as delivering banking services at an affordable cost to the vast sections of disadvantaged and low-income groups (Dev, 2006). Financial inclusion is also defined as using and accessing formal financial services (Sahay et al., 2015). These definitions have one thing in common: they emphasize that each member of the population should have access to available financial services.

Muhammad Yunus (1983), Who founded Grameen Bank in Bangladesh in 1983. Yunus believed that access to financial services was essential for poor people to improve their economic condition. He pioneered the concept of microfinance, which provides small loans to individuals who would not otherwise have access to credit.

Financial exclusion is most prevalent amongst those on low incomes. Unemployed people living on social security payments from the state are, therefore, especially vulnerable, as are low-income households from ethnic minority communities who may also have relatively low levels of engagement with the financial services industry. Kempson *et al*. (2004), supported by evidence from the Family Resources Survey 2002-2005, report that uptake of financial products and services is lowest amongst African-Caribbean, Black, Pakistani and Bangladeshi households in the UK. However, religious beliefs may partially explain this apparent exclusion for some members of these groups.

World Bank (2008) has classified financial access barriers into four main categories; physical barriers, lack of documentation barriers, affordability barriers and lack of appropriate products and services. For geographic access, branches have been the traditional bank outlets. Hence the geographic distance to the nearest branch or the destiny of branches relative to the population can provide a crude indication of geographic access or lack of physical barriers to access Beck, demiurgic-Kunt and

Martinez (2007). In this study, this theory provided the critical essential for business economic growth through access to resources needed for financial consumption and investment.

2.3.2 Growth Finance Theory

Theories on the finance growth nexus advocate that financial development creates a productive environment for growth through the ‘supply leading’ or ‘demand following effect. Theories also perceive the lack of access to finance as a critical factor responsible for persistent income inequality and slower growth. According to Serrao et al. (2012), access to a secure, convenient, and cost-effective funding source is crucial for promoting economic growth, reducing income inequality and poverty, and providing equal opportunities. This access allows socially and economically excluded individuals to integrate more effectively into the economy, participate actively in development, and safeguard themselves against economic shocks.

Hughes (1986) published a seminal article titled "Finance and Economic Growth: Some Further Evidence" in the Journal of Development Economics. In this article, Hughes argued that developing financial markets could stimulate economic growth by promoting savings, investment, and efficient resource allocation.

Levine (1997) is also prominent in developing the Finance-Growth Nexus theory. In his influential article titled "Financial Development and Economic Growth: Views and Agenda," published in the Journal of Economic Literature, Levine argued that financial development was a critical determinant of economic growth, and he provided evidence to support this claim.

Furthermore, theory and evidence imply that better-developed financial systems ease external financing constraints facing firms, which illuminates one mechanism through which financial development influences economic growth. (Ross Levin)

Theoretical disagreements do exist about the role of financial systems in economic growth. Some economists see the role as minor or negligible, while others see it as significant. The origin of the finance-led growth hypothesis can be traced back to Bagehot (1873). Those who favour finance-led growth (the hypothesis argues that the existence of an energetic financial sector has growth-enhancing effects). Schumpeter, in 1911 posited that banks enable an economy to grow by providing efficient markets for funds. Goldsmith (1969), McKinnon (1973), Levine and Zervos (1996), and others also emphasized the positive role of financial systems in economic growth, as cited by Ndebbio (2004). The main argument of proponents of the supply-leading theory is that financial markets evolve in response to increased demands for financial services from an already budding economy. Therefore, the development of financial markets reflects growth in other sectors of the economy.

In conclusion, most theories have established a positive link between financial development and economic growth through the growth of all sectors of the economy. Therefore, growth finance theory asserts that access to resources leads to increased production of goods and services, thus resulting in performance growth.

2.3.3 Financial Intermediation Theory

Financial intermediation is a fundamental concept within the field of finance, elucidating the degree to which financial institutions facilitate the convergence of entities with surplus funds and those with deficits (Ndebbio, 2004). At its core, this theory strives to answer a pivotal question: why do investors, rather than lending

directly, first entrust their resources to financial institutions, which subsequently allocate these funds to borrowers? An argument often presented in response posits that banks are adept at monitoring borrowers, effectively serving as delegates for monitoring activities (Diamond, 1984). Diamond's seminal work highlights the reduction in monitoring costs as a primary source of this comparative advantage. He posits that intermediaries, such as banks, deliver valuable services by issuing secondary financial assets to procure direct financial support. Crucially, Diamond contends that intermediaries must provide tangible benefits; otherwise, investors who acquire secondary securities from intermediaries might as well directly purchase the primary securities, bypassing the intermediary's associated costs.

Colin Mayer (1990) defines financial systems as pivotal components responsible for mobilizing funds from savers and channelling them toward productive investment opportunities. These systems serve as the lifeblood of modern economies, furnishing the necessary infrastructure for businesses to access capital and individuals to engage in saving and investment. Encompassing a myriad of institutions and instruments, including banks, financial markets, insurance companies, and pension funds, financial systems are the conduits through which economic activity is fueled. Mayer's conceptualization underscores the profound significance of well-functioning financial systems in underpinning economic development. He particularly accentuates the role of financial intermediaries in fostering investment and managing risk. Financial intermediaries, exemplified by banks and other financial entities, offer a secure repository for savers to deposit their funds and then transmute these short-term deposits into long-term loans for borrowers. This transformative process empowers individuals and enterprises to access the capital needed for investment and expansion, thereby making a substantial contribution to economic development.

Notably, financial market frictions wield considerable influence over the persistence of income inequality and the emergence of poverty traps. These market imperfections, typified by information asymmetry and transaction costs, significantly shape the accumulation of critical human and physical capital, as well as individual choices about occupations. Demirgüç-Kunt, Beck, Honohan, and Asli (2008) elucidate that in theories emphasizing capital accumulation, financial market imperfections dictate the extent to which individuals with limited means can borrow capital for investments in education or physical assets. In theories spotlighting entrepreneurship, these imperfections determine the avenues through which talented yet financially constrained individuals can secure external funding to initiate entrepreneurial ventures. Consequently, the trajectory of financial development, economic growth, and intergenerational income dynamics are intrinsically interwoven. Finance exerts a profound influence over the efficiency of resource allocation within an economy and the relative economic opportunities available to individuals hailing from affluent or impoverished households.

Demirguc Kunt and Levine (2007) put forth a compelling argument positing that mitigating financial market imperfections to expand individual opportunities engenders positive incentive effects. These models advance the notion that the lack of access to finance can serve as a pivotal mechanism driving persistent income inequality, the entrenchment of poverty traps, and hindered economic growth.

In summation, the theoretical frameworks expounded upon above underscore five prominent roles that financial intermediaries fulfil: information acquisition concerning borrowers, provision of risk-mitigation agreements, capital accumulation, enhancement of corporate governance, and streamlining of transaction processes.

These facets collectively elucidate the multifaceted nature of financial intermediation and its far-reaching implications for economic dynamics and development.

2.4 Empirical Review

In recent years, there has been a growing interest in understanding the impact of financial inclusion on the performance of small and medium enterprises (SMEs). Several studies have been conducted in different countries to examine this relationship.

2.4.1 Financial Access and performance

Financial inclusion is geared towards enhancing access to financial administrations for the unbanked, low-pay earners and the rural population located in areas away from financial reach (Musah, Gakpetor & Pomaa, 2018). With reduced distances to access a point where an individual can get financial services, individuals spend less money and time while gaining more time to take care of their business operations. Commercial banks and Microfinance institutions have developed several products and platforms that enable consumers to save, deposit and withdraw their finances without being physically present in the banking hall or travelling to urban centres to transact businesses (Maksimov, Wang & Luo, 2017).

Financial access was much more difficult for Kenyan SMEs for the past decade as the financial sector was underdeveloped (Muneer, Ahmad & Ali, 2017). Small business owners were disadvantaged compared to big businesses in accessing finances; their inability to repay made it attractive for financial service providers to extend financial services to their reach. With the advent of technology, many avenues are now available that make it easy to participate in the financial sector. However, many still find it challenging to makesound financial decisions (Acosta,

Crespo & Agudo, 2018). For example, mobile loan apps have improved the credit uptake by small-scale business owners or individuals who have defaulted and are thus blocked by regulatory agencies.

To measure financial access, the study designed financial access review information to appraise the conveyance paces of store account proprietorship and admittance to credit inside Nairobi County. We created the sums for store accounts and the breakdown by every area from the filled-in gauges. We then, at that point, used family reviews to appraise the average number of records per account holder, which permitted the study to assess the quantity of banked and unbanked people in the SME sector

2.4.2 Financial Usage and performance

Most SME owners rely on personal finances as a source of start-up capital (Ezeagba, 2017). Personal savings and contributions from friends are generally used to meet the initial cost. Additional finances sort to either meet more expenses or expand the business after a period of operations. According to Fried V.H & Hisrich, RD (1995), this has worked to the advantage of those enterprises small scale trade while it has given negative consequences to individuals who under-estimated the financial requirement of the business (Maziriri, Mapuranga & Madinga, 2018). Insufficiency of starting capital has led to the loss of savings as companies fail to start. It has likewise been seen that numerous SMEs access financial administrations from commercial banks, microfinance institutions and SACCOs, but most of them fail to fully utilize and grow their businesses (Abdulaali, Alnoor & Eneizan, 2019). The biggest problem many individuals have failed to manage effectively is the separation of finances meant for their business and money needed for their financial needs. This leads to the misappropriation of

funds. As a result, they fail to meet all the business requirements that, need to default in repaying the loans and earning penalties or auctioning their properties to recover debts (Majama & Magang, 2017).

To address this problem and other related issues that small business owners face, financial institutions offer financial training to individuals and groups so that they can equip them with the necessary skills that help them manage their businesses more effectively. Economic use was assessed by tracking the financial decisions made by individual SME owners in allocatingthe finances obtained with a focus on the percentage allocated to the businesses versus the amount used for personal needs.

2.4.3 Financial Barrier and performance

Financial barriers are one of the most significant barriers to growth in small businesses. The saying goes to make money, companies should be willing to spend money, and this may be particularly challenging for small businesses as they may not have the capital spent on Research and Development to grow (Hisrich et al., 2019). Financial barriers which affect SMEs include high collateral, high bank charges, lack of outside equity and venture capital and high cost of credit (Bartlett & Bukvić, 2021). Banks usually assist larger businesses with good credit histories and high collateral and loan payment guarantees. Also, entrepreneurs may be reluctant to seek outside help from venture capitalists or fear losing their company's autonomy (Bartlett & Bukvić, 2019).

Numerous studies have discussed that small and medium-sized enterprises are financially more constrained than large firms (Carpenter and Petersen, 2002). Firstly, small firms face information opacity, such as the inability to provide financial

information. When the firm is small, it is mainly owned and operated by the entrepreneur. There is no legal requirement to report financial information regularly; many firms do not maintain audited financial accounts. Second, smaller firms have fewer assets to offer as collateral. To reduce the anticipated risk and moral hazard associated with lending, the banks use collateral as one of the instruments. Berger and Udell (1998) found smaller and younger firms are more likely to face a higher cost of financing, and at the same time, they are required to offer collateral.

High risk is involved because small firms have a higher failure rate than large firms. For example, Schiffer and Weder (2001) sampled firms across several countries and found a negative relationship between the size of a business and the risk it might pose for a lender. Firm size is a critical variable in the analysis of financial restrictions (Beck et al., 2005). Thus, in general, large and small firms do not have equal opportunities to access external sources of finance. So, while the presence of both large and small firms is essential for market competition and, hence, for economic growth, to ensure industrial dynamics, firms must have access to financial markets

The firms that are typically most severely affected by the imperfections of the financial market are small firms, as their internal information can be somewhat opaque or, at least, not as public as it is in the case of their larger counterparts. Small firms seeking small loans face higher transaction costs and risk premiums since they are opaque and have less collateral to offer (Beck et al. 2006). Becket has found similar results (2005, and Schiffer and Weder (2011). Schiffer and Weder (2011) confirm that small firms have to confront higher barriers to their financing and growth.

2.4.4 Financial Inclusion and Small and Medium Enterprises

Access to suitable financial services is often a bottleneck for small businesses, constraining their ability to leverage credit facilities effectively. These challenges frequently stem from lending policies instituted by formal financial institutions, which manifest as stipulated minimum loan amounts, convoluted application processes, and limitations on credit usage for specific purposes. Furthermore, small businesses grapple with limited access to capital and money markets, aggravated by investors' reluctance to engage with proprietorships, partnerships, or unlisted companies due to heightened risk perceptions. Additionally, the cost of capital remains high, and institutional credit, when available, often necessitates collateral, posing significant obstacles to securing financing (Kamweru, 2011).

Research has convincingly demonstrated that a robustly developed financial sector can substantially enhance the performance of small and medium enterprises. The availability and utilization of financial services enable firms to manage risk effectively and expand their operations, benefiting from a comprehensive range of financial offerings. This not only fosters business development but also contributes to overall societal upliftment. Access to financial services serves as a vital instrument for directly enhancing firms' performance and catalyzing productive capacity through investment financing (Nwanna, 1995). Several factors contribute to improved access, including financial innovations such as the integration of microfinance units within mainstream financial institutions, technological advancements, rising living standards, and relaxed banking sector regulations. Nonetheless, it is noteworthy that these innovations within the formal financial sector do not necessarily diminish reliance on the informal and semi-formal economic sectors within an economy (Udell, 1992).

Financial inclusion (FI) signifies a shift in the economic agent's mindset concerning money and profit. Its objective is to eradicate barriers to accessing and utilizing financial services, and the existing infrastructure is instrumental in advancing this goal. Alarmingly, more than half of the world's economically challenged adults lack bank accounts, rendering them susceptible to exploitation and theft, leading to substantial losses (World Bank, 2012). Promoting FI on a global scale holds the potential to broaden economic inclusion, subsequently enhancing the financial well-being of financially marginalized SMEs (Khan, 2011). Facilitating efficient financial inclusion can potentially improve the efficiency of SMEs by bridging the gap between savings and investments (Aduda & Kalunda, 2012). While underutilized capital remains a growth impediment for SMEs, it plays a pivotal role in shaping the investment landscape and contributing to the financial inclusion of citizens (Aldaba, 2011).

SMEs commonly grapple with financial constraints, and easing credit constraints or enhancing financial access for SMEs compared to larger corporations is likely to stimulate employment and enhance labour productivity, consequently fostering economic growth and development (Ayyagari, Demirguc-Kunt, & Maksimovic, 2016). Establishing and nurturing SMEs not only spurs employment and labour productivity across the nation but also facilitates access to formal finance. The World Bank (2018) underscores that implementing policy reforms aimed at stimulating SME growth through initiatives like establishing credit bureaus nationwide can substantially enhance the financial inclusion of citizens. Beck and Cull (2014) further emphasize that financial inclusivity plays a pivotal role in driving SME growth across Sub-Saharan Africa, holding significant promise for the region's economic development.

2.5 Conceptual Framework

The conceptual framework for this study aims to systematically integrate the various dimensions of financial inclusion to explain its impact on Small and Medium Enterprises (SMEs) performance (Brown, Renwick, & Raphael, 1995). It comprises three key dimensions: financial access, financial usage, and financial barriers. Financial access assesses the availability and ease of SMEs obtaining financial services, while financial usage examines how these services are utilized. Financial barriers encompass the challenges faced by SMEs in accessing and using financial services. Additionally, the framework incorporates SME performance indicators like investment growth, sales growth, and profitability to assess the influence of financial inclusion. This structured approach helps to understand the relationship between financial inclusion and SME performance in Nairobi County, Kenya (Kamweru, 2011; Aldaba, 2011).

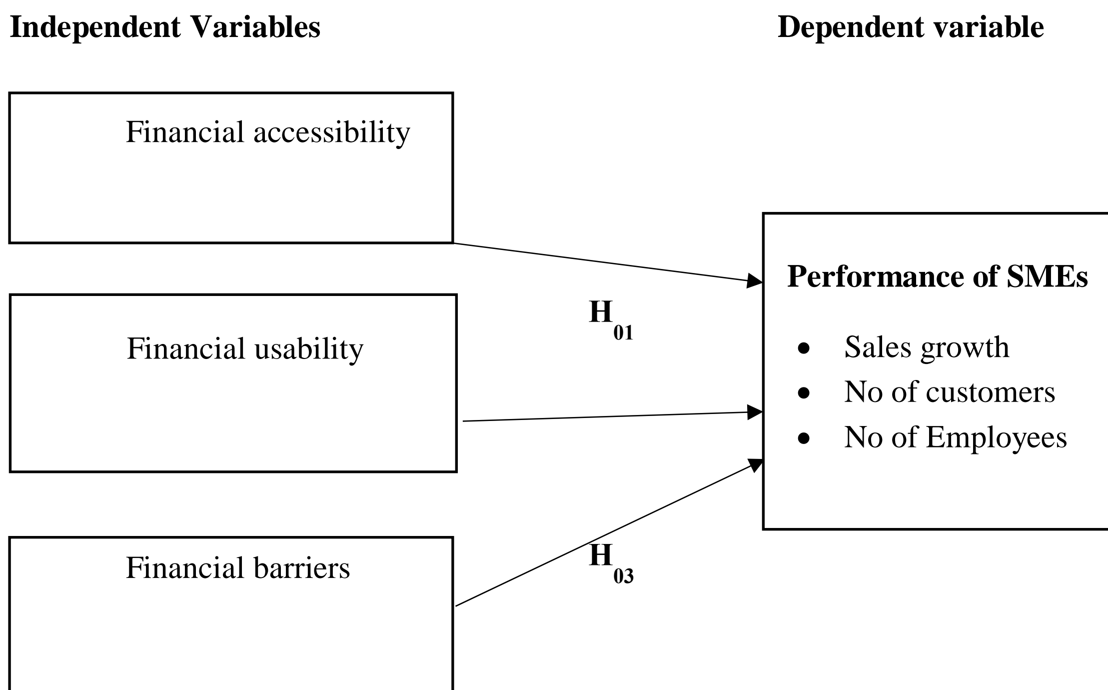

Figure 2.1: Conceptual Framework
Source: Researcher 2023.

2.6 Summary and Gaps

The Literature Review provides a comprehensive overview of the foundational concepts and theories that underpin this study. It navigates through the intricate landscape of financial inclusion, SMEs, and financial intermediation, setting the stage for the research's focus on their interplay.

The concept of financial inclusion is fundamental to understanding the economic landscape. Financial inclusion encompasses various dimensions, including access to financial services, financial usage, financial barriers, and financial literacy (Ondabu, Ogollah, & Mwaura, 2018). It serves as a crucial driver of economic development, especially in emerging economies like Kenya.

Small and Medium Enterprises (SMEs) constitute a cornerstone of the economy, contributing significantly to employment generation and economic growth (Economic Survey, 2016 KNBS). However, SMEs face numerous challenges, including limited access to financial resources. The existing literature emphasizes the importance of SMEs but lacks a granular understanding of how financial inclusion initiatives directly impact their performance (Kenya National Bureau of Statistics [KNBS], 2016).

The Financial Intermediation Theory, as articulated by Diamond (1984), sheds light on why investors often choose to channel their resources through financial institutions rather than lending directly. It highlights the role of financial intermediaries, such as banks, in reducing monitoring costs and providing risk-reduced agreements (Diamond, 1984).

This study aims to address critical gaps in the existing literature. Firstly, it seeks to examine the precise mechanisms through which financial inclusion initiatives impact SMEs' performance in Nairobi County, Kenya, thereby providing a deeper understanding of this relationship. Secondly, the study focuses on the unique challenges and opportunities faced by SMEs in the Kenyan landscape, offering region-specific insights that are often missing in the global literature. Thirdly, it aims to apply the Financial Intermediation Theory to the Kenyan SME context, elucidating the specific roles played by financial intermediaries in facilitating SME growth. Finally, the study intends to provide concrete policy recommendations tailored to the Kenyan context, helping policymakers and stakeholders devise strategies to enhance SME performance through improved financial inclusion. In summary, this study strives to contribute to the existing body of knowledge by addressing these gaps and providing valuable insights into the intricate relationship between financial inclusion, financial intermediation, and SME performance, with a specific focus on the unique Kenyan context (Kamweru, 2011; Aldaba, 2011).

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 Introduction

This chapter presents the research methodology used in this study. It encompasses the research design, target population, sample size, data collection method, data analysis, reliability and validity testing, and data presentation. The details of each component are discussed below.

3.1 Research Design

A research design is a crucial aspect of any research study, as it outlines the systematic approach to collecting, analyzing, interpreting, and reporting data (Creswell & Plano Clark, 2007). It serves as a blueprint for conducting research, specifying the methods and procedures for obtaining and analyzing the necessary information (Mugenda & Mugenda, 2005). Additionally, it encompasses critical elements such as the sampling method, sample size determination, and data measurement and analysis processes (Akhtar, 2016; Silva, 2017). A well-structured research design provides a clear plan for data collection, measurement, and analysis, ultimately facilitating the study's ability to address research questions (Akhtar, 2016). In this study, an explanatory research design was employed, which aligns with the research's primary objective of examining the impact of financial inclusion on the performance of small and medium enterprises (SMEs) in Nairobi County, Kenya. Explanatory research designs, as described by Saunders et al. (2007), are particularly suited for exploring the characteristics of variables and simultaneously investigating causal relationships between these variables. Given the complexity of the relationship between financial inclusion and SME performance, an explanatory research design allows for a comprehensive examination of the subject matter, helping to clarify the

underlying causal mechanisms and factors contributing to SME performance within the context of financial inclusion. Thus, the choice of an explanatory research design is well-suited to fulfil the study's objectives and address the research questions effectively.

3.2 Target Population

A Population can be defined as a set of individuals, objects, or data from where a statistical sample can be drawn and analyzed (Sunders et al., 2009). The population is the entire group of individuals, events or objects having common observable characteristics (Copper and Schindler, 2000). Cooper and Schindler (2003) added that a population is the total sum of collected units from which the researcher concludes a study. The population consists of the study's subjects, individuals, groups, organizations, humans, products, events, or the conditions they are exposed to (Welmanet et al., 2005). The units of analysis were the members or elements of the population. The population for the study comprised the 30,000 SMEs in Nairobi County-Central Business District. (Nairobi County Licensing Office, 2022).

Table 3.1: Target Population

Sector	Population	Percentage%
Shops and Retail stores	10,236	34.12
M-Pesa services	7,167	23.89
Hardware	2,196	7.32
General Merchants	3,408	11.36
Small Restaurants and hotels	4,809	16.03
Small Consulting Services	2,184	7.28
Total	30,000	100

Source, NRB County (2022)

3.3 Sampling Methods and Techniques

A sample can be defined as a set of respondents (people or organizations) selected from a larger population for a study, and sampling is the act, process, or technique of selecting a suitable sample or a representative part of a population to determine parameters or characteristics of the whole population (Mugo, 2011). Sampling aims to conclude populations from samples with a population's characteristics by directly observing only a portion (or sample), which is cheaper than observing the whole population. From the target population, 77 SMEs were used as the study sample.

3.3.1 Sample Frame

A sampling frame is the list of individuals or events, source material or devices from which a sample is drawn (Mugenda&Mugenda, 2005). It comprises a list of all those within a population who can be sampled and may include individuals, households, organizations or institutions (Saunders et al., 2009). The frame of this study comprised all the SMEs within the Nairobi-CBD.

Table 3.2: Sample size

Sector	Population	Percentage%
Shops and Retail stores	26	33.80
M-Pesa services	18	23.40
Hardware	6	7.80
General Merchants	10	12.98
Small Restaurants and hotels	12	15.58
Small Consulting Services	5	6.44
Total	**77**	**100**

Source, Field Data (2022)

3.3.2 Sampling design

A sample refers to a small group obtained from the accessible population (Mugenda and Mugenda, 2003). A research sampling design is that part of the research plan that indicates how cases or events are selected for observation. The design, therefore,

maps out the procedure followed to draw 77 study samples. According to Cooper and Schindler (2011), a good example should be a representative of the population. This study utilized a random sampling design to select the sample population. The sampling technique explains the method deemed relevant for the study in which the researcher wants to investigate whether the characteristics of a specific phenomenon cut across the units of observation with maximum variation. (Mugenda&Mugenda, 2005). The parameters regulate the sampling process in the population in line with the study's specific objectives (Cooper and Schindler, 2011).

3.3.3 Sample Size Determination

A sample is a smaller group of individuals or units selected from a larger group called the population. According to Kothari (2008), a population usually consists of more than 10,000 units. To determine the appropriate sample size, the Cochran equation is commonly used.

The equation is as follows:

$$n = \frac{z^2 p\,(1-p)}{e^2}$$

Where:

n = sample size

z = level of confidence

p = estimated proportion of the population with a particular characteristic

e = margin of error

Therefore, the sample size was derived as follows;

n = sample size

z = the standard deviation value for the level of confidence, for instance, a 95% level of confidence = 1.96

e = margin of error (level of precision set at 0.112% in the study is justifiable due to size, quality of data and study design, (Jack & Suri, 2011) and such enables confident inferences about the population under study. (Wafula at al, 2019).

p = Since the proportion of the population with the characteristic is unknown, 50% was used. P=0.5.

$$n = \frac{1.96^2\ x\ 0.5\ x\ (1 - 0.5)}{0.112^2} = 77$$

3.4 Study Area

This research covered the scope of identifying the binding effect of the ability of small and medium enterprises to access financial inclusion on their performance in Nairobi County. The key focus was identifying positive and negative impacts to recommend a suitable economic model for SMEs. We interviewed SMEs from Nairobi County-CBD as the focal point of the research. Nairobi County was selected since the region has many SMEs and a high concentration of banking services, which are well distributed to enable the area to provide a good data source for the study.

3.5 Data Collection

The sources of data in this study were based on primary data. Primary sources of data and information are collected during the questionnaire filled with the respondents during the survey. The questionnaire was structured with close-ended questions and was hand-delivered to the respondents to reach a broader base of respondents effectively.

3.5.1 Data Collection Methodology

Data collection is gathering and measuring information on variables of interest to answer the research question, test the hypothesis and evaluate outcomes.

The data collection method used for the study is administering questionnaires. In this study, structured questionnaires were distributed and used to collect the required data from the respondents. The respondents for this study were the SME owner or the business manager. This ensures the credibility and validity of the information gathered. Questionnaires refer to a collection of information about the population (Mugenda&Mugenda, 2003). Structured questionnaires are inexpensive to collect data from respondents with tight schedules. The study's steps to develop the structured questionnaires include defining the survey's objectives, determining the sampling group, constructing the instrument and administering the instrument to respondents.

Questionnaires also reduce bias since the researchers' opinions would not influence the respondents to answer questions in a particular manner, unlike a telephone or face-to-face survey. The questionnaire was short and structured, with mostly multiple-choice selections on a Likert scale to ensure uniformity in response and encourage participation.

3.6 Operationalization of Variables

Operationalization is the process of strictly defining variables into measurable factors. The method explains fuzzy concepts and allows them to be measured empirically and quantitatively. Operationalization also sets down exact definitions of each variable, increasing the results' quality and improving the design's robustness. McGregor, (2006). Table 3.3 outlines the process of operationalizing the variables and analysis for this research.

Financial inclusion: this variable was operationalized as the level of access to formal financial services by small and medium enterprises in Nairobi County. This was measured using a combination of closed-ended and open-ended questions in the survey, asking about the types of financial services SMEs have access to, the conditions under which they access these services, and the perceived impact of financial inclusion on the performance of their businesses.

Financial access: this variable was operationalized as the level of access to financial services, such as credit and savings, by small and medium enterprises in Nairobi County. This was measured using closed-ended questions in the survey, asking about the types of financial services SMEs have access to, the conditions under which they access these services, and the perceived impact of financial access on the performance of their businesses.

Financial usage: this variable was operationalized as the extent to which small and medium enterprises in Nairobi County utilize financial services, such as credit and savings. This was measured using closed-ended questions in the survey, asking about the types of financial services that SMEs use, the conditions under which they use these services, and the perceived impact of monetary usage on the performance of their businesses.

Financial barriers: this variable was operationalized as the obstacles and challenges that small and medium enterprises in Nairobi County face in accessing and utilizing financial services. This was measured using open-ended questions in the survey, asking about the specific barriers that SMEs face, such as lack of collateral or lack of financial literacy, and the perceived impact of these barriers on the performance of their businesses.

Performance: this variable was operationalized as the overall success and growth of small and medium enterprises in Nairobi County CBD. This was measured using a combination of closed-ended and open-ended questions in the survey, asking about the financial performance of the businesses, such as profitability and sales growth, as well as the perceived impact of financial inclusion on the overall performance of the companies.

Table 3.3: Operationalization of Variables

Type	Variable	Operationalization	Types of Analysis	Measure
Independent	Financial Inclusion	Access to Financial Services	Descriptive and inferential statistics	Frequencies, Percentages and multiple linear regression (Likert Scale)
		Usage of Financial Services	Descriptive and inferential statistics	Frequencies, Percentages and multiple linear regression (Likert Scale)
		Barriers to Financial Services	Descriptive and inferential statistics	Frequencies, Percentages and multiple linear regression (Likert Scale)
Dependent	SMEs Performance	Sales growth, No of customers and No of employees	Descriptive and inferential statistics	Frequencies, Percentages and multiple linear regression (Likert Scale)

3.7 Validity and Reliability

In this section, we delve into the critical aspects of validity and reliability, essential components that underpin the trustworthiness and accuracy of the data collected in this research (Trochim & Donnelly, 2008). Validity pertains to the extent to which our data collection methods accurately measure what they are intended to measure. On the other hand, reliability concerns the consistency and dependability of our data collection instruments. To ensure the integrity of our findings, we systematically address these aspects by detailing the steps taken to establish content validity and reliability through a pilot study and statistical analysis.

3.7.1 Validity

In the pursuit of ensuring the validity of the data collection process, the researcher took several essential steps. Firstly, necessary permissions were obtained from relevant authorities, which is a crucial aspect of ensuring the data's credibility and the respondents' trustworthiness (Smith, 2010). This step helped establish the legitimacy of the research and fostered cooperation from the SMEs participating in the study.

Secondly, the content validity of the questionnaire was meticulously addressed. Each question within the questionnaire was scrutinized to verify its validity and ensure that it effectively captured the intended information. This process involved a comprehensive review to guarantee that the questions were relevant, comprehensive, and comprehensible to the participants (Bryman & Bell, 2015). Ensuring content validity enhances the accuracy of data collection by confirming that the questions accurately measure the constructs under investigation.

3.7.2 Reliability

To ensure the reliability of the questionnaire and data collection instrument, a pilot study was conducted before the main research phase (Masibo, 2005). In this pilot study, seven SMEs were engaged to pre-test the questionnaire. The purpose of this pre-testing process was to evaluate the feasibility of the proposed data collection procedures and to identify any potential issues, ambiguities, or shortcomings in the instrument (DeVellis, 2016).

The assessment of reliability was carried out through the application of Cronbach's alpha test, a widely recognized measure of internal consistency (Tavakol & Dennick, 2011). This statistical analysis helped determine the degree to which the items within the questionnaire were consistent in measuring the same underlying construct. The high Cronbach's alpha coefficients obtained during the pilot study demonstrated a high level of reliability in the instrument, indicating that the questions were internally consistent and could be depended upon for subsequent data collection in the main study (George & Mallery, 2003).

3.8 Regression Model

The questionnaires, upon completion, underwent a thorough review and editing process to ensure data accuracy, consistency, and completeness following established research practices (Researcher, 2023). Subsequently, regression and correlation analyses were employed to examine the relationships between variables, particularly focusing on the measurement of SMEs' value in terms of financial records post-access to credit (Researcher, 2023).

The data underwent comprehensive analysis, with the results presented in the form of charts and tables. To investigate the nature and magnitude of relationships between

the independent and dependent variables, inferential statistics, specifically regression analysis, was utilized (Researcher, 2023). The multiple linear regression model was employed to represent these relationships using the equation:

$$Y = \beta0 + \beta1X1 + \beta2X2 - \beta3X3 + \varepsilon$$

Where:

Y = performance

β_0- β_3 = regression coefficient of independent variables

X_1 = Financial access

X_2 = Financial usage

X_3 = Financial barriers

ε = error term

It is important to note that this modelling approach assumes several key assumptions, including linearity, independence of errors, homoscedasticity (constant variance of errors), and normality of errors, which are critical for the interpretation and generalizability of the regression results (Hair et al., 2019). These assumptions ensure that the estimated coefficients accurately reflect the relationships between variables and that the model's predictions are reliable.

3.9 Pilot Testing

The pilot study conducted in a controlled setting with a distinct subset of participants played a pivotal role in assessing the reliability of key variables critical to the research. Its primary objective was to establish the consistency and dependability of these variables before embarking on the full-scale investigation involving SMEs in Nairobi County, Kenya (Researcher, 2023). During the pilot study, the reliability of

various variables was thoroughly examined. The results demonstrated robust reliability coefficients: financial access displayed a reliability coefficient of 0.851, indicating a high level of consistency among responses related to this variable. Similarly, financial usage exhibited strong reliability, boasting a Cronbach's alpha of 0.957, signifying a high degree of internal consistency among responses about this aspect. The variable of financial barriers exhibited exceptional reliability, recording an impressive Cronbach's alpha coefficient of 0.982, which indicated a high level of stability in responses concerning this variable. Finally, the variable of performance, a critical aspect of the study, displayed a reliability coefficient of 0.797, indicating a reasonable level of internal consistency among responses related to performance. These results provided strong validation for the reliability of the research instruments and variables. All variables surpassed the recommended threshold of 0.70 for Cronbach's alpha, confirming their reliability for subsequent use in the main study. In essence, the pilot study's outcomes ensured that the research instruments were dependable and prepared for implementation in the comprehensive research involving SMEs in Nairobi County, Kenya.

3.10 Diagnostic Tests

This section deals with diagnostic tests which include normality, multicollinearity and homogeneity tests.

3.10.1 Normality test

A normality test determines whether a sample data has been drawn from a normally distributed population. It is generally performed to verify whether the data involved in the research have a normal distribution. The Shapiro-Wilk test is used to test normality. If the p-value of the Shapiro-Wilk test is greater than 0.05, the data is

normal. If it is below 0.05, the data significantly deviates from a normal distribution (Saunders, Lewis & Thornhill, 2012).

3.10.2 Multicollinearity test

Multicollinearity occurs when independent variables in a regression model are correlated. This correlation is a problem because independent variables should be independent. The variance inflation factor (VIF) identifies a correlation between independent variables and the strength of that correlation. When VIF is higher than 10 or tolerance is lower than 0.1, there is significant multicollinearity that needs to be corrected (Hair, et. al., 2006).

3.10.3 Heteroscedasticity Test

Heteroscedasticity tests examine whether the variance of errors in a regression model is constant across different levels of the independent variable(s). The most widely used test is the Breusch-Pagan test (Breusch & Pagan, 1979), which evaluates the null hypothesis of homoscedasticity. Heteroscedasticity violates the assumption of ordinary least squares regression and may require appropriate model modifications. Using the Breusch Pagan test a p-value >0.05 indicates that the constancy of the error term is met, and p<0.05 indicates that the assumption has been violated.

3.10.4 Autocorrelation tests

Autocorrelation tests examine whether there is a correlation between error terms in a time series or panel data analysis. The Durbin-Watson test (Durbin & Watson, 1951) is frequently used to detect autocorrelation. It tests the null hypothesis that there is no first-order autocorrelation. Autocorrelation violates the assumption of independent observations and may necessitate adjustments to the model specification. A Durim

Watson statistic between 1.5 and 2.0 indicated no presence of autocorrelation a number less than 1.5 or more than 2.0 indicates a violation of the assumption.

3.11 Ethical Issues

3.11.1 Privacy and Confidentiality

The participants had highlighted concerns about privacy and confidentiality due to the sensitive nature of the topics and the small sample size that may have compromised confidentiality. To address these concerns, the researcher ensured that a high level of professionalism was exercised during the research.

3.11.2 Respondent-Related Issues

The participants may have felt that the inquiry in the qualitative research could lead to psychological disturbance, loss of income for daily wagers due to the lengthy duration of interviews, and challenges in research with vulnerable groups. To minimize these issues, the researcher utilized brief questionnaires that were distributed electronically to avoid any delays on the part of the respondent.

3.11.3 Interviewer-Related Issues

The interviewer's experience in qualitative research was crucial to avoiding the wrong framing of questions and disturbing probing. There was also a risk of misinterpretation of information. Participants emphasized the need for professional competence among the researchers utilizing qualitative research methods.

As a researcher, this addressed the ethical issues by prioritizing the privacy and confidentiality of the participants. I did this by maintaining high professionalism throughout the research process. I used brief questionnaires distributed electronically

to minimize any potential psychological disturbance or loss of income for daily wagers. Additionally, I exercised professional competence in conducting qualitative research to avoid wrong questions or misinterpreting information.

CHAPTER FOUR

DATA ANALYSIS, PRESENTATION, INTERPRETATION AND DISCUSSION

4.0 Introduction

This chapter presents the findings of the study, which are based on the feedback provided by the respondents and are linked to the research objectives. The chapter discusses the company profile and the descriptive and inferential statistics used to analyze the respondents' views on financial access, financial usage, and financial barriers to performance.

4.1 Response Rate

The sample size of 77 questionnaires was distributed among SMEs in CBD Nairobi. Table 4.1 below shows the response rate.

Table 4.1: Response Rate

Response	Number	Percentage
Not respondent	19	25
Returned and filled questionnaire	58	75
Total	**77**	**100**

Source: Research Data (2022)

77 questionnaires were distributed to the respondents, and 58 questionnaires were filled and returned, representing 75%, while (25%) did not respond. “The response rate of 75% was considered adequate for data analysis. This could be supported by Kothari (2014), who stated that the 60% and above response rate is good, while over 70% was perfect. Based on these assertions, this implies that the response rate for this study was adequate, thus fulfilling the study's main goal. Figure 4.1 illustrates the level of response rate.”

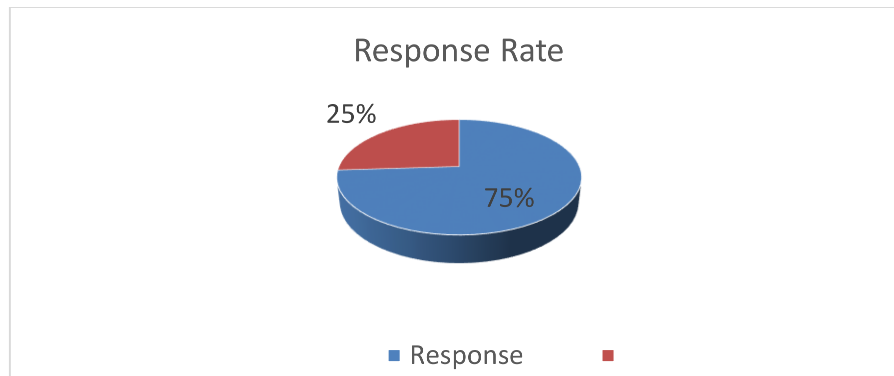

Figure 4.1: Response Rate

Source: Research Data (2022)

4.2 Results of the Reliability Test

The pilot study served as an initial assessment of the reliability of key variables utilized in the research, aiming to establish their consistency and dependability before proceeding with the full-scale investigation. Conducted in a controlled setting with a smaller subset of participants, distinct from the primary research sample, the pilot study evaluated the reliability of various variables. Results of the pilot study revealed robust reliability coefficients for the examined variables: financial access exhibited a reliability coefficient of 0.851, indicating strong consistency; financial usage demonstrated high reliability with a Cronbach's alpha of 0.957; financial barriers displayed exceptional reliability, scoring 0.982; and the critical variable of performance achieved a reasonable level of reliability at 0.797. All variables surpassed the recommended threshold of 0.70 for Cronbach's alpha, affirming their reliability for use in the subsequent full-scale research. Consequently, the pilot study played a pivotal role in ensuring the reliability and consistency of research instruments and variables, preparing for the main study involving SMEs in Nairobi County, Kenya (Researcher, 2023).

Table 4.2: Reliability Results

Variables	Alpha value	Number of conclusions
Financial access	0.851	6 reliable
Financial usage	0.957	6 reliable
Financial barriers	0.982	7 reliable
Performance	0.797	3 reliable

Source: Research Data (2022)

4.3 Demographic Characteristics

This section provides information that posits the essential characteristics such as gender, years in operation, level of education, number of employees and annual turnover of respondents.

4.3.1 Firm Profile

Table 4.3 shows that 39.7% were male respondents and 60.3% were female respondents. On the years of operations, 13.7% operated between 2-4 years, 37.9% operated between 5-7years, 20.7% performed between 8-10years and 27.5% of businesses operated above 10 years.

While in matters of education level, 8.6% had education up to certificate level, 48.2% had a diploma, 27.6% had a bachelor's degree, and 15.5% had a post-graduate degree. Regarding the number of employees in the business, 12.1% had below 5 employees, 32.1% had 5-10 employees, and 18.9% had 15-20 employees. 22.4% had above 20 employees.

Lastly, on annual turnover, 50% had below 5milion, 39.6% had a yearly turnover of 5 million- 50 million and 10.3% had an annual turnover above 50 million.

Table 4.3: Profile

Characteristics		Percent (%)
Gender	Male	39.7
	Female	60.3
	Total	**100**
Years in operations		
2-4yrs	13.7	
5-7yrs	37.9	
8-10yrs	20.7	
Above 10yrs	27.5	
Total	**100**	
Education		
Certificate	8.6	
Diploma	48.2	
Degree	27.6	
Post-graduate	15.5	
Total	**100**	
Number of employees		
Below 5yrs	12.1	
5-10	32.1	
10-15	18.9	
15-20	13.8	
Above 20yrs	22.4	
Total	**100**	
Annual Turnover		
5Million	50	
5-50M	39.6	
Above 50M	10.3	
Total	**100**	

Source: Research Collected Data, 2022

4.4 Statistical Assumptions

Statistical tests rely upon certain assumptions about the variables used in the analysis. Osborne and Waters (2014) opine that when these assumptions have not been met, the results may not be valid. They further argue that this may result in type I or II error, over or under-estimating significance or effect size(s). It is, therefore, important to pre-test these assumptions for the validity of their results. Osborne, Christensen, and Gunter (2001) observed that few articles report testing hypotheses of the statistical tests they rely on for conclusions.

According to Osborne and Waters (2014), not pretesting for these assumptions has led to a situation where there is a rich literature in education and social science. However, questions about the validity of many of these results, conclusions, and assertions still exist. Testing for assumptions is beneficial as it ensures that an analysis meets the associated assumptions and helps avoid type I and II errors (Osborne and Waters, 2014; Owino, 2014). Before data analysis, assumptions for normality and multicollinearity were checked.

4.4.1 Normality Test

The normality of data was tested using the Shapiro-Wilk test. Thus, on the one hand, if the p-value is less than the chosen alpha level, then the null hypothesis is rejected, and there is evidence that the data tested are not normally distributed. On the other hand, if the p-value is more significant than the chosen alpha level, then the null hypothesis that the data came from a normally distributed population cannot be rejected. The null hypothesis of this test is that the population is normally distributed. The results of the normality test are presented in Table 4.4. The normality results showed that financial access had a p-value of .084>0.05; hence the data is normally distributed. It was also established that the p-value for financial usage was .061>0.05, and financial barriers had a p-value of .073>0.05. In comparison, the performance had a p-value of .068>0.05. The normality test results revealed that the data were normally distributed, so further analysis was conducted.

Table 4.4: Tests of Normality

	Shapiro-Wilk	
	Statistic	**Sig.**
Financial access	0.975	.084
Financial usage	0.896	.061
Financial barriers	0.978	.073
Performance	0.840	.068

4.4.2 Multicollinearity Test

Multicollinearity exists when two or more predictors in a regression model are moderately or highly correlated, thereby limiting the research conclusions. According to Zainodin, Noraini, and Yap (2011), multicollinearity refers to correlations between the predictor variables. In severe cases of perfect correlations between predictor variables, multicollinearity can imply that a unique least squares solution to a regression analysis cannot be computed (Field, 2009). According to Field (2009), VIF values over 10 indicate the presence of Multicollinearity. Multicollinearity inflates the standard errors and confidence intervals, leading to unstable estimates of the coefficients for individual predictors. Multicollinearity was assessed in this study using the Variance Inflation Factor (VIF), as shown in Table 4.5.

Results are presented in Table 4.5. A variance inflation factor test was conducted to test for the multicollinearity of the predictors. A value less than 10 is acceptable financial access with a V.I.F value of 1.641, which is less than 10, implying no multicollinearity. Financial usage with a V.I.F value of 1.936 means no multicollinearity since VIF is less than 10. The results indicated that Financial barriers had a V.I.F value of 1.586, implying no multicollinearity since VIF is less than 10.

Regression could thus be conducted to the effect of financial inclusion on the performance of small and medium enterprises in Nairobi Central Business District

Table 4.5: Multicollinearity Test

	Collinearity Statistics	
Variable	**Tolerance**	**VIF**
Financial access	0.708	1.641
financial usage	0.889	1.936
Financial barriers	0.832	1.586

4.4.3 Homoscedasticity test

Lani, (2011) defines homoscedasticity of errors in linear regression as the constant nature of their spread from the regression line. This implies that a regression error represents the deviation between a data point and the standard regression line.

The even distribution of residual or error term across the graph is a crucial assumption for this method. If this assumption is not met and the variance of errors from the regression line is not constant, (Paper, 2016) the results of the analysis may be biased, causing distorted statistical conclusions. This phenomenon is known as heteroscedastic dispersion. Table 4.6 shows a p-value of 0.432>0.05 therefore the assumption of homoscedasticity was not violated.

Table 4.6: Homoscedasticity test

Prob > chi2	= 0.432

Survey Data (2023)

4.4.4 Autocorrelation test

Gujarati, (2003) explains that one of the assumptions that must be met in linear regression modelling is the independence of error components. However, when

dealing with data that follows a relevant temporal sequence, such as weekly sales data, this assumption may be violated if each error term is related to its immediate predecessor (i-1). This phenomenon is known as first-order autocorrelation.

To detect serial correlation using the Durbin-Watson test. They note that the Durbin-Watson statistic should be between 1.5 and 2.5. Table 4.7 shows a Durbin-Watson statistic of 1.845, indicating that there was no autocorrelation in the data.

Table 4.7: Autocorrelation test

Durbin- Watson statistic	1.845

Survey Data (2023)

4.5 Descriptive Statistics

4.5.1 Financial access

Table 4.8 illustrates the respondents' results demonstrating that the bank is credible with a (mean=4.06, standard deviation= 0.785). The location of my bank is convenient with a (mean=4.47, standard deviation= 0.587). I use alternative sources of finance with a (mean=3.85, and standard deviation= 0.748). Making remittances with a (mean=4.00, and standard deviation= 0.635) is easy. No hidden charges affect business (mean=3.62, standard deviation= 0.750). I can quickly secure a loan from my bank with a (mean=3.96, standard deviation= 0. 771).

Table 4.8: Table 4.2: Access

5 = Strongly Agree **4** = Agree **3** = Neutral **2** = Disagree **1**= Strongly Disagree

	Mean	Std. Dev	Skewness	Kurtosis
My bank is credible	4.06	0.785	-0.597	-0.076
The location of my bank is convenient	4.47	.587	-0.581	-0.598
I make use of alternative sources of finance	3.85	0.748	-.205	-0.291
It is easy to make remittances	4.00	0.635	0. 000	-0.471
There are no hidden charges that affect the business	3.62	0.750	0.298	-0.537
I can quickly secure a loan from my bank	3.96	0.771	-0.160	-0.648
Financial access				

4.5.2 Financial usage

Table 4.9 illustrates the results from respondents demonstrating that It is easy to make payments to my service providers with a (mean=4.51, standard deviation= 0. 587). Operating a bank account with a (mean=3.13, and a standard deviation= 1.190) is cheap. My bank offers training on financial literacy with a (mean=3.60, standard deviation= 1.362). It's easy to make deposits with my bank (mean= 3.23, standard deviation=1.279). I can access mobile/internet banking (mean=4.48, standard deviation= 0.546). It is affordable to use a mobile banking platform (mean=3.70, standard deviation= 0.711). It is easy to get tailored services for your business had a mean of (mean=4.38, standard deviation= 0.613)

Table 4.9: Financial usage

5= Strongly Agree **4 =** Agree **3** = Neutral **2** = Disagree **1**= Strongly Disagree

	Mean	**Std. Dev**	**Skewness**	**Kurtosis**
It is easy to make payments to my service providers	4.51	0.587	-0.064	-2.129
It is cheap to operate a bank account	3.13	1.190	0.785	0.046
My bank offers training on financial literacy	3.60	1.362	0.322	-1.895
It's easy to make deposits with my bank	3.23	1.279	0.425	-0.584
I can access and use mobile/internet banking easily	4.48	0.546	-0.020	-0.841
It is affordable to use a mobile banking platform	3.70	0.711	0. 349	-0.581
It is easy to get tailored services for your business	4.38	0.613	-0.178	-0.428
Financial usage				

4.5.3 Financial barriers

Table 4.10 illustrates the findings from Do You Operate a Bank Account with a mean of (mean=4.18, standard deviation= .720). The distance between you and the bank is near with a (mean=3.19, standard deviation= 0.705). Do you have multiple sources of income (mean=3.32, standard deviation= 0.739)? Making payments is less tedious with a (mean=4.12, standard deviation= 0.747). In contrast, there is a high cost of doing business which had a (mean=3.10, standard deviation= 1.041). Raising expansion capital is easy (mean=4.08, standard deviation= 0.682).

Table 4.10: Financial barriers

5= Strongly Agree **4 =** Agree **3** = Neutral **2** = Disagree **1**= Strongly Disagree

	Mean	**Std. Dev**	**Skewness**	**Kurtosis**
Do you operate a bank account	4.18	0.720	-0.279	-0.874
The distance between you and the bank is near	3.19	0.705	0.113	-0.288
Do you have multiple sources of income?	3.32	0.739	0.222	-0.134
Making payments is less tedious	4.12	0.747	-0.318	0.786
There is a high cost of doing business	3.10	1.041	0.132	-0.710
I find it easy to raise expansion capital	4.08	0.682	-0. 107	-0.828
Financial barriers				

4.5.4 Performance

Table 4.11 illustrates that respondents' results demonstrate that Our business emphasizes employees' education and training to enhance performance with a(mean=3.88, standard deviation= 0.728). Improvement of the firm net profit growth over the last 5 years (mean, standard deviation= 0.956). Reduction of customer complaints in service delivery in the previous 5 years (mean = 3.77, standard deviation= 0.710).

Table 4.11: Performance

5 = Strongly Agree **4 =** Agree **3** = Neutral **2** = Disagree **1**= Strongly Disagree

	Mean	**Std. Dev**	**Skewness**	**Kurtosis**
Our business emphasizes employees' education and training as a way of enhancing performance	3.88	0.728	0.081	-0.877
Improvement of the firm net profit growth over the last 5 years	3.03	0.956	-0.062	-0.521
Reduction of customer complaints in service delivery over the last 5 years	3.77	0.710	0.102	-0.546
Performance				

4.6 Inferential Statistics

The study used correlation and regression analysis to make necessary deductions and inferences. The findings of the analysis are presented in subsequent sections.

4.7 Correlation Analysis

A correlation coefficient enables the researcher to quantify the strength of the linear relationship between two ranked or numerical variables (Smith, 2010). Table 4.12 indicates that access is positively correlated with performance (r= 0.226), and Financial usage is positively correlated with performance (r= 0.359). Lastly, financial barriers are positively correlated with performance (r= 0.201)

Table 4.12: Correlation Results

		Performance	Financial access	Financial usage	Financial barriers
Performance	Pearson Correlation	1			
Financial access	Pearson Correlation	.226**	1		
Financial usage	Pearson Correlation	.359**	.228**	1	
Financial barriers	Pearson Correlation	.201**	.247**	.370**	1

Correlation is significant at the 0.05 level (2-tailed).

4.7.1 Regression Results

Regression analysis was used to establish the effect of financial inclusion on performance. The findings of the Model Summary are shown in Table 4.8.

Model Summary

The results in Table 4.13 indicated that financial Access, Financial usage and Financial barriers positively correlated with performance up to 67.9% or (R= 0.679). The results reveal that Access, Financial usage and Financial barriers caused a variation of 46.1% or (R^2=0.461 and adjusted R^2 =0.456) in performance. This implies that the remaining 53.9 % of the change was caused by other factors not included in the model.

Table 4.13: Effect of Access, Financial usage and Financial barriers on performance

Model Summary				
Model	R	R Square	Adjusted R Square	Std. The error in the Estimate
1	.679[a]	.461	.456	.62731

Dependent Variable: Performance
Predictors: (Constant), financial Access, Financial usage and Financial barriers

4.7.2 Analysis of Variance

Further ANOVA tests were conducted to determine whether the model explains the relationship among variables as postulated in the conceptual model. The findings show an F value of 5.885 with a significance level of 0.000 which is far lower than the confidence level of 0.05, hence establishing the model is statistically significant. The implication is that each independent variable contributes significantly to changes in the dependent variable performance.

Table 4.14: ANOVAa

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	4.123	4	1.030	5.885	0.000
	Residual	9.456	54	.175		
	Total	13.579	58			

a. Dependent Variable: Performance
b. Predictors: (Constant), financial Access, Financial usage and Financial barriers

4.7.3 Hypothesis Testing

Regression was carried out to determine the combined influence of Financial access, financial usage and Financial barriers on Performance

Table 4.15: Overall Effect of Financial access, financial usage and Financial barriers on Performance

	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
(Constant)	.292	.088		3.318	.000
Financial access	.315	.051	.376	6.176	.002
Financial usage	.277	.047	.240	5.893	.000
Financial barriers	.330	.086	.287	3.837	.000

Dependent Variable: Performance

b Independent Variables: (Access, Financial usage and Financial barriers)

Regression Equation

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

Where:

γ Represents performance

$\boldsymbol{\beta}_0$ Is the constant

$\boldsymbol{\beta}_1$, $\boldsymbol{\beta}_2$ **and** $\boldsymbol{\beta}_3$ The regression coefficients

$\mathbf{X_1}$ =Financial access

$\mathbf{X_2}$ =Financial usage

$\mathbf{X_3}$ = Financial barriers

$\boldsymbol{\varepsilon}$ = The error term or residuals

Régression Equation

$Y = 0.292 + .315\mathbf{X_1} + .277\mathbf{X_2} - .330\mathbf{X_3}$

The regression equation shows that the independent and dependent variables were statistically significant. In comparison, a unit change in Financial access increases

performance by 0.315. A unit change in Financial usage decreases performance by 0.277. Lastly, A unit change in Financial barriers impacts performance by 0.330.

4.7.4 Test of Hypotheses

The first hypothesis **H_{01}:** Financial access does not significantly affect the performance of small and medium enterprises in Nairobi County. Financial access has a positive relationship effect. The finding in Table 4.15 showed a positive and significant relationship with the performance of small and medium enterprises. The p-value was less than 0.05, ρ=0.002, which implies that the relationship was statistically substantial; therefore, the hypothesis was rejected.

The second hypothesis **H_{02}**: Financial usage does not significantly affect the performance of small and medium enterprises in Nairobi County. Financial use has a positive relationship affect performance. The finding in Table 4.15 showed a positive and significant relationship with the performance of small and medium enterprises. The p-value was less than 0.05, ρ=0.000, which implies that the relationship was statistically substantial; therefore, the hypothesis was rejected.

The third hypothesis **H_{03}**: Financial barriers do not significantly affect the performance of small and medium enterprises in Nairobi County. Financial barriers have a positive relationship effect on performance. The finding in Table 4.15 showed a positive and significant relationship with the performance of small and medium enterprises. The p-value was less than 0.05, ρ=0.000, which implies that the relationship was statistically substantial; therefore, the hypothesis was rejected.

Table 4.16: Summary of Hypothesis Testing

Hypothesis	P-value	Conclusion
H_{01}: Financial access does not significantly affect the performance of small and medium enterprises in Nairobi County.	0.002	Reject H_{01}
H_{02}: Financial usage does not significantly affect the performance of small and medium enterprises in Nairobi County	0.000	Reject H_{02}
H_{03}: Financial barriers do not significantly affect the performance of small and medium enterprises in Nairobi County	0.000	Reject H_{03}

Source: Research, 2023

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.0 Introduction

This chapter presents and summarizes the study's findings, conclusions, and recommendations. The content is arranged clearly and concisely, providing a brief overview of the preliminary results of the research. The chapter includes a summary of the conclusions that can be drawn from the study's findings and highlights areas for future research.

5.1 Summary of Findings

The main objective of this study was to investigate the effect of financial inclusion on the performance of small and medium enterprises in Nairobi County. The study applied an explanatory research design, and the primary data method was used to gather data for this research. Preliminary data was collected using a self-administered predetermined questionnaire to achieve the study's objectives. The questionnaire of the survey included closed-ended questions with five-point Likert scale-type statements. The study had three specific goals; To establish the effect of financial access on the performance of small and medium enterprises in Nairobi County. To determine the impact of financial usage on the performance of small and medium enterprises in Nairobi County. To establish the effect of financial barriers on the performance of small and medium enterprises in Nairobi County.

5.1.1 Specific Objective One: Effect of Financial Access on Performance

The primary objective of this study was to investigate the impact of financial access on the performance of small and medium enterprises (SMEs) within Nairobi County. The results of the analysis demonstrated a statistically significant and positive

association between financial access and SME performance, with a correlation analysis revealing a positive relationship. Specifically, the regression analysis indicated a significant positive relationship between financial access and SME performance, as evidenced by a $\beta 1$ coefficient of 0.315 and a p-value of 0.002, which is less than the conventional threshold of 0.05.

Consistent with these findings, previous research conducted by Kazimoto (2014) has also emphasized the importance of governments and other stakeholders in providing SMEs with access to financial resources at reasonable interest rates, as well as leveraging modern information and communication technologies in business operations and marketing strategies. To address challenges faced by SMEs in Africa, including issues related to financial inclusion, unfavourable legal and regulatory frameworks, and inadequate infrastructure, Lega (2015) has emphasized the need for improved support systems and training initiatives.

In summary, this study's findings underscore the significance of financial access in influencing the performance of SMEs, supporting the argument that enhancing financial inclusion, coupled with supportive policies and infrastructure, can contribute significantly to SME growth and development (Kazimoto, 2014; Lega, 2015).

5.1.2 Specific Objective Two: Effect of Financial Usage on Performance

The second specific objective of this study was to assess the impact of financial usage on the performance of small and medium enterprises (SMEs) in Nairobi County. The results of the analysis indicated a statistically significant and positive relationship between financial usage and SME performance, with both correlation and regression analyses confirming this association. The correlation analysis revealed a positive and significant relationship between financial usage and performance, while the regression

analysis demonstrated a significant positive relationship, represented by a β1 coefficient of 0.277 and a p-value of 0.000, which is less than the conventional threshold of 0.05.

In line with these findings, previous research conducted by Otiato (2016) has also explored the determinants of financial inclusion and performance among SMEs in Nairobi City, Kenya. Otiato's study employed an explanatory research design, encompassing a population of 236 SMEs and a sample of 30 participants. The study collected primary data through questionnaires and employed SPSS for data analysis. Otiato's research highlighted various factors as determinants of financial inclusion, including the quality and utilization of financial services, product/service costs, trade volume levels, profit margins, human resource capacity, and efficiency levels, all of which serve as proxies for measuring SME performance.

In summary, the findings of this study emphasize the significant role of financial usage in influencing the performance of SMEs, aligning with previous research that has explored the determinants of financial inclusion and performance within the Kenyan context (Otiato, 2016). These results underscore the importance of optimizing financial service utilization as a strategy for enhancing SME performance and financial inclusion.

5.1.3 Specific Objective Three: Effect of Financial Barriers on Performance

The third specific objective of this study aimed to investigate the impact of financial barriers on the performance of small and medium enterprises (SMEs) in Nairobi County. The analysis conducted in this study indicated a statistically significant and positive relationship between financial barriers and SME performance, as corroborated by both correlation and regression analyses. The correlation analysis

exhibited a positive and significant association between financial barriers and performance, while the regression analysis provided further evidence of this significant positive relationship, represented by a $\beta 1$ coefficient of -0.330 and a p-value of 0.000, which falls below the conventional significance threshold of 0.05.

These findings align with previous research conducted by Berger and Udell (1998), who found that smaller and younger firms often encounter higher financing costs and are typically required to provide collateral. Additionally, Schiffer and Weder (2001) confirmed that small enterprises frequently face more significant obstacles to securing financing and achieving growth. In summary, the results of this study emphasize the substantial influence of financial barriers on SME performance, echoing prior research findings that underscore the challenges faced by small businesses in accessing financial resources and the consequent impact on their performance.

5.2 Conclusions

In summary, this study has provided valuable insights into the relationship between financial inclusion and the performance of small and medium enterprises (SMEs) in Nairobi County, Kenya. The research findings support the hypotheses formulated, highlighting the significant impact of financial access, financial usage, and financial barriers on SME performance.

Firstly, the study has established that financial access plays a crucial role in enhancing SME performance. SMEs with easy access to financial services, such as remittances and loans, reported improved performance outcomes. This finding aligns with the existing literature, emphasizing the importance of financial inclusion in supporting SME growth (Kazimoto, 2014).

Secondly, the research findings confirm that financial usage positively affects SMEs in Nairobi County. SMEs that can easily make payments and utilize mobile/internet banking services exhibit enhanced performance. This underscores the significance of efficient financial service utilization for SME success (Otiato, 2016).

Lastly, the study highlights the positive influence of overcoming financial barriers on SME performance. SMEs that find it less tedious to make payments and access expansion capital experience improved performance outcomes. This result resonates with previous research emphasizing the challenges faced by SMEs in accessing financial resources and the subsequent impact on their performance (Berger & Udell, 1998; Schiffer & Weder, 2001).

Overall, the study underscores the critical role of financial inclusion in bolstering SME performance, emphasizing the need for policymakers and stakeholders to focus on facilitating financial access, and usage, and overcoming barriers to promote SME growth and contribute to economic development in Nairobi County.

5.3 Recommendations

5.3.1 Policy Implication

Drawing from the insights of the study and the existing literature, policymakers, including the government and the Central Bank of Kenya (CBK), should prioritize the development of comprehensive policies that address financial access, usage, and barriers faced by small and medium enterprises (SMEs) in Nairobi County. The study aligns with previous research, such as the work of Khan (2011), emphasizing the critical role of financial inclusion in SME development. It underscores the need for tailored policies to enhance SME access to financial resources, thereby facilitating their growth and economic contributions.

Policy measures should encompass initiatives to streamline access to credit, reduce bureaucratic hurdles, and provide incentives for SMEs to adopt digital financial services, consistent with findings by Kamweru (2011) and Aldaba (2011). Additionally, the government and regulatory bodies can consider measures to encourage financial institutions to offer affordable and SME-friendly financial products, in line with recommendations from Udell (1992) and Demirguc-Kunt et al. (2008).

These policies should reflect the local context, address the unique challenges faced by SMEs, and promote financial inclusion as a driver of economic development within Nairobi County.

5.3.2 Practice and Management

Effective practice and management are paramount for the sustainable growth and success of SMEs in Nairobi County. Building on the research findings, several recommendations can help SMEs in enhancing their practice and management strategies.

Firstly, SMEs should prioritize efficient financial management practices. This includes maintaining accurate financial records, budgeting, and monitoring cash flow. The research has shown that financial access, usage, and overcoming barriers positively impact performance. Therefore, SMEs should actively seek funding options, including traditional banks, microfinance institutions, and government-sponsored programs, to improve their financial stability. Digitalization is another critical aspect of practice and management. Embracing modern technologies can significantly improve SME operations, customer engagement, and overall

performance. This includes adopting digital payment systems, e-commerce platforms, and data analytics tools to make informed decisions and expand market reach.

Furthermore, SMEs should collaborate and network with industry peers and relevant stakeholders. Partnerships with other businesses, associations, and government agencies can provide valuable support, knowledge sharing, and access to resources. Mentorship programs and business incubators should also be explored to gain insights and guidance from experienced entrepreneurs. Continuous learning is crucial for staying competitive. SME owners and managers should invest in their education and skills development. Participating in training programs, workshops, and seminars can equip them with the latest business trends and best practices. Market research is essential for understanding customer needs and preferences. SMEs should regularly conduct market research to identify opportunities, assess competition, and tailor their products or services accordingly.

SMEs can also benefit from implementing sustainable practices. This includes adopting environmentally friendly processes and socially responsible initiatives, which can not only improve their image but also attract a wider customer base.

Lastly, SMEs should develop robust risk management strategies. This involves identifying potential risks, such as economic downturns or supply chain disruptions, and developing contingency plans to mitigate these threats.

5.3.3 Theoretical Implication

This study contributes significantly to the existing literature by reinforcing the relevance of several financial theories, including the Financial Inclusion Theory, Growth Finance Theory, and Financial Intermediation Theories. To further advance

scholarly understanding, it is recommended that researchers delve deeper into the intricacies of these theories within the SME context.

Future research should focus on refining and extending these theoretical frameworks, exploring how specific aspects of financial inclusion, such as mobile banking and digital payments, influence SME performance. Scholars should also investigate how contextual factors, such as regulatory environments and economic conditions, mediate the relationship between financial inclusion and SME outcomes.

Moreover, comparative studies across different regions and countries would enrich theory development by revealing variations in the impact of financial inclusion on SMEs in diverse settings. Researchers can employ rigorous methodologies, including longitudinal analyses and case studies, to unravel the causal mechanisms and nuanced dynamics involved.

By advancing theoretical foundations, this research area can provide policymakers, practitioners, and scholars with deeper insights into how financial inclusion can be harnessed as a tool for fostering SME growth and economic development.

5.4 Limitations of the Study

Due to the sensitivity of the information, the respondent may have an imaginary fear of giving the information to competitors. This limitation was countered by assuring the respondents that the data was purely for academic purposes and would be treated with confidentiality. Another limitation of this research pertains to the potential for response bias. Respondents' answers to survey questions may have been influenced by their desire to portray their businesses in a favourable light or to align with socially desirable responses. Such bias could impact the accuracy and reliability of the data collected (Tourangeau, Rips, & Rasinski, 2000). While efforts were made to ensure

confidentiality and encourage candid responses, the inherent challenge of obtaining completely unbiased data remains a limitation in survey-based research. Researchers should be cognizant of the possibility of response bias and consider additional methods or triangulation of data sources to address this limitation in future studies.

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APPENDICES

Appendix I: Questionnaire

INSTRUCTIONS

This questionnaire sought to collect information on the effect of financial inclusion on the performance of the 77 Small and Medium Enterprises in Nairobi Kenya-CBD. Please provide information in the spaces provided unless indicated as optional and tick or circle the appropriate boxes. All the information received was confidential and for academic purposes only.

Section A: General Information

1. Kindly indicate your gender.

a. Male ☐

b. Female ☐

2. How long has the business been in operation?

a. 2-4years ☐

b. 5-7 years ☐

c. 8-10 years ☐

d. Over 10 years ☐

3. Indicate the level of education

a. Certificate ☐

b. Diploma ☐

c. Degree ☐

d. Post- Graduate ☐

4. How many employees are there in your business

a. Below 5 employees ☐

b. 5 – 10 employees ☐

a. 10 – 15 employees ☐

b. 15 – 20 employees ☐

c. Above 20 employees ☐

5. What is your current annual revenue range

a. Below 5million☐

d. Between 5-50million☐

e. Above 50 million☐

SECTION B: ACCESS

To what extent do you agree with the following statements about the relationship of financial inclusion with the business? Use: 1- Strongly Disagree, 2- Disagree, 3- Neutral, 4- Agree and 5- Strongly Agree

	1	**2**	**3**	**4**	**5**
My bank is credible					
The location of my bank is convenient					
I make use of alternative sources of finance					
It is easy to make remittances					
There are no hidden charges that affect the					
I can quickly secure a loan from my bank					

SECTION C: FINANCIAL BARRIER

To what extent do you agree with the following statements about financial barriers to financial services and SMEs? Use: 1- Strongly Disagree, 2- Disagree, 3- Neutral, 4- Agree and 5- Strongly Agree

	1	**2**	**3**	**4**	**5**
Do you operate a bank account?					
The distance between you and the bank is near					
Do you have multiple sources of income?					
Making payments is less tedious					
There is a high cost of doing business					
I find it easy to raise expansion capital					

SECTION D: FINANCIAL USAGE:

To what extent do you agree with the following statements about using financial services and how it affects your business? Use: 1- Strongly Disagree, 2- Disagree, 3- Neutral, 4- Agree and 5- Strongly Agree

	1	**2**	**3**	**4**	**5**
It is easy to make payments to my service					
It is cheap to operate a bank account					
My bank offers training on financial literacy					
It’s easy to make deposits with my bank					
I can access and use mobile/internet banking					
It is affordable to use a mobile banking platform					
It is easy to get tailored services for your business					

SECTION E: PERFORMANCE

To what extent do you agree with the following statements about the performance and how it affects your business? Use: 1- Strongly Disagree, 2- Disagree, 3- Neutral, 4- Agree and 5- Strongly Agree

	1	**2**	**3**	**4**	**5**
Our business emphasizes employees' education and training as a way of enhancing performance					
Improvement of the firm net profit growth over the last 5 years					
Reduction of customer complaints in service delivery over the last 5 years					

"Thank you for sparing time to answer this questionnaire."

Appendix II: List of small and medium enterprises in Nairobi Central Business District

1. Njuguna Peter Kinyagia	26. Fredrick Ng'ang'a Karanja	51. Richard Musyimi Mbalya
2. Meena Lalit Gajjar	27. Joseph Njenga Kirunyu	52. Annah Wakio
3. Arjun Singh Bhachu	28. Susan Nakhanu	53. Klassics Wears
4. E P Kibuci Maringa Mucungu	29. Margaret Njoki Kariuki	54. Geospace Invest
5. Davies Gakinya Kimani	30. Jagjit Singh Ahluwalia	55. Outdoor Invents
6. Danson Ndirangu Gatimu	31. Fredrick Njeru Nduku	56. Pints Decor
7. Vincent Komu Kibiro	32. Mwangi Irungu Weru	57. Poonam Mukesh Gohil
8. Amit Mohan Shah	33. Wariz Zuri Palour	58. Joseph Wathua Kigwe
9. Benson Ngari Kamau	34. Abdullahi Mohamed Hanchi	59. Kamaldeep Singh Phull
10. Nurdin Gulamhussein Ajania	35. Samuel Njehia Gitau	60. Nasim Akhtar Rasul
11. Raphael Wamiti Gachoka	36. Boniface Kilonzi Kisilu	61. Professor Francis Ndungu Kibera
12. Charles Kamau Mungai	37. John Karuga	62. Rupal Shah
13. Wilfred Githua Mwethera	38. Peter Njoroge Kagwima	63. Abdul Rahman
14. Thomas Maara Gichuhi	39. Kariaria Holdings	64. Drill Masters
15. Joseph Njenga Kirunyu	40. Moses Kimang'a Mwangi	65. Africana Restaurants
16. Peter Kibiro Komu	41. Kalyan Shivji Patel	66. Wairimu Richards
17. Kamal Kishore Thakore	42. Boniface Kihiu Kamau	67. Pauline Cleaners
18. Peter Ndungu Kanari	43. Joseph Njenga Kirunyu	68. Smart Dry Cleaners
19. Jemimah Jane Wacheke Kimari	44. Margaret Ruguru Macharia	69. Posh Palours
20. Pavlos Pavlidis	45. Pushpa Keshavlal Punja Shah	70. Blend Dishes
21. James Kariuki Thuo	46. James Chege Njoroge	71. Rhoda Akinyi
22. Ruth Wanjiru	47. Varsha Ramniklal Shah	72. Bee Clean Services
23. George Wellington Kopondo	48. Weston Wambugu Kamau	73. Beat Ventures
24. Robert Gikura Njoroge	49. Weston Wambugu Kamau	74. Coral Print Ventures
25. John Chrispus Mwaura Njuguna	50. John Ngaruro Mugo	75. CoolErants Limited
		76. Bestwise Limited
		77. Peter Njuguna Mwangi