

EFFECTS OF ACCESS TO CREDIT ON FINANCIAL PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES IN NAIROBI COUNTY

Irene Chepsang¹, Dr. Cyrus Iraya² and Dr. Kennedy Okiro³

ABSTRACT

Purpose: SMEs have been recognized as being great contributors to the Kenyan economy offering both employment and a platform for innovative ideas. They form a larger percentage of the businesses that operate in Kenya as compared to their counterpart, the large companies. They are however faced with many constraints that hinder their performance and consequently their growth. One of the main constraints that have been highlighted over the years is the financial constraint. The need for finance is of paramount importance for the success of any firm, be it big or small. The purpose of this research was to investigate the effect of credit access on financial performance of SMEs in Nairobi County.

Methodology: The literature explored in this research highlight three main factors, namely firm size, loan amounts, access to credit and financial performance. These form the independent variables in the theoretical framework that influence the dependent variable, that is, access to external funding. The analysis involves primary data obtained through questionnaire and interviews and secondary data from journals, books and internet. The data covered a period of five years ranging from the year 2012 to 2016.

Findings: The regression model has an R of 0.724 which indicates a strong positive relationship between the variables. The coefficient of determination, R square indicates how well data fits in the statistical model; how successful the fit is in explaining the variation of the data. In this model, 52.4% of the variations in the dependent variable are explained by the independent variables.

Implications: This report contributes as a wakeup call to the financial system to be more and more SMEs' sensitive and offer financial services that are all inclusive. The financing gap, in the credit market, that exists between large and small companies need to be abridged. This can be achieved by creating an enabling environment for SME, formulating regulatory framework that is SMEs friendly, segmenting NSE for SMEs' listing. SMEs are also called up to keep good financial reports and to form linkages or associations to ease the burden of accessing funds.

Value: This research is motivated by the increasing importance in Kenya's economy of SMEs, and the continuing constraints they face in their activities. The development of SMEs has been identified as one of the strategies in the Kenyan economic blueprint of vision 2030 as one of the pillars for addressing key economic issues for generating industrialization, employment generation and poverty reduction in Kenya and in working towards a sustainable economy that achieves the Millennium Development Goals like solving the problem of unemployment. The government in its goal through Economic Recovery Strategy (ERS) is employing all players to make this dream come true. The research is also resourceful for prospective entrepreneurs wishing to start a small business. It is also a wakeup call on the lending institutions to work up a strategy that would have a wider financial inclusion.

¹ Master of Business Student at the University of Nairobi, School of Business

² Senior Lecturer at the University of Nairobi, School of Business, Department of Finance and Accounting

³ Lecturer at the University of Nairobi, School of Business, Department of Finance and

Introduction

Small and medium sized enterprises (SMEs) are credited with offering about 75% of the general employment and contributing about 18% of GDP in the Kenyan economy. These enterprises cut across all sectors of the economy including general trade (wholesale and retail), services, farm activities and manufacturing (Atieno, 2009). In a state-controlled economic system, though in this millennium is rarely practiced, production is the sole responsibility of the state. However, in free trade or capitalist economic system, production is in the hands of individuals or groups with little government control. A mixed economic system happens when some of the productions are operated by the state while others are left to free enterprises. Kenya practices a mixed economic system but with high capitalist tendencies. It is because of this prevailing economic system that we find a great variety of business organizations that are in the hands of individuals or groups. This variation ranges from size, ownership, products, services offered, advertising capabilities, growth opportunities, financial strengths, among others. This leads to various forms of businesses like sole proprietorship, partnership, private and public limited companies, cooperative societies for the private sector of the economy, and the public corporation for the public sector.

The capital needs of small and medium-size enterprises (SMEs) can be either satisfied by its own internal funds or by debt capital. The lack of access to credit remains a major constraint for the entrepreneurs in African countries. Unlike larger firms, SMEs rarely have access to public equity markets in most countries, therefore, they do not have access to the public debt (Demirguc-Kunt et al 2002). Instead, they turn to banks and the credit market (trade credit, money lenders, informal lending from family/friends, and rural finance) for both short- and long-term credit. Access to external resources is needed to ensure flexibility in resource allocation and reduce the impact of cash flow problems (Bigsten et al. 2000). Firms with access to funding's are able to build up inventories to avoid stocking outs during crises, also the availability of credit increases the growth potential of the surviving firms during periods of macroeconomic instability. Firms without access to bank funding are more vulnerable to external shocks (Nkurunziza, 2005). Credit also enables individuals to smooth out consumption in the face of varying incomes, provide income for investment and improve the ability to cope with unexpected expenditure shocks. A lack of collateral and the high possibility of default can prevent individuals and small firms from obtaining credit.

Lack of access to financial services is one of the main constraints that limit the development and financial performance of SMEs and a number of factors have been identified to explain this problem. This includes the segmented and incomplete nature of financial markets, which increases transaction costs associated with financial services. On the supply side, most formal financial institutions consider SMEs un-creditworthy, thus denying them credit. Difficulties in accessing credit has held back the micro and small enterprise sector in Kenya as most financial institutions view them as unstable and often place tighter lending requirements before advancing credit (Atieno, 2009).

Access to Credit

Credit constraints operate in variety of ways in Kenya, where undeveloped capital market forces SMEs to rely on self-financing or borrowing from friends and relatives. Lack of access to long-term credit for small enterprises forces them to rely on high cost short term finance. These difficulties stem from the more formal lending institutions which tend to rate all SMEs equally as un-credit worthy. However, the emergence of less formal institutions like MFIs and SACCOs do not ease this burden. These micro-credit institutions face limited expansion because of their limited funds. Their short-term finance means they cannot easily turn the savings they collect into medium or long-term loans. They are also up against the cost of refinancing through the formal banking sector and have no access to refinancing either by the central bank (Wanjohi 2009).

Longer term relationships with a commercial bank or other financial institutions may indicate that a firm has a “formal” relationship in financial markets, which some have argued is important to help in gaining access to credit markets. A firm’s credit history is an important determinant of whether a firm can obtain credit. Since owner and firm finances are often co-mingled and somewhat indistinguishable for some smaller businesses, the credit history of the owner may be just as important as the credit history of the firm (Baas and Schrooten, 2005).

Financial Performance

Firm financial performance is used to describe the state of affairs of a firm. In analyzing a firm’s financial performance, emphasis should be made in formulating an adequate description of the concept of a firm’s financial performance which uncovers the different dimensions upon which firm’s financial performance should be evaluated. In terms of measurement, Demstz and Lehn (2001) measured firm financial performance as accounting

profit rate. Uadiale (2010) measured firm performance by return on equity (ROE) as the proportion of profit after tax to issued share capital and return on capital employed (ROCE) as the proportion of profit after tax to issued share capital plus reserves.

Kechi (2011) measured firm financial performance by return on asset (ROA) and profit margin (PM). Fazlzadeh et.al. (2011) measured firm financial performance as the net income to total assets and ordinary income to total assets. Uwaloma and Olamide (2012) measured firm financial performance as return on asset (ROA). For the purpose of this study, firm financial performance is defined as return on equity measured by the proportion of profit after tax to total shareholders' equity at book value.

Access to Credit and Financial Performance

Among the major factors of production that any organization requires capital is the most important one since it enables the organization to operate. Access to finance boosts SMEs productivity and hence become sustainability by utilizing the economies of scale (Kira and He, 2012). Entrepreneurial activities such as access to new markets, expansion of business, reduction of risks, innovation and creativity enhancement all require finances. A study by Rahaman (2011) revealed that an increase of 10% in bank credit to a firm would lead to an increase of 18.14% in firm growth. On the other hand, lack of credit negatively affected profit margins of the business than any other challenges (Khandker et al, 2013). They also established that firms that borrow money from informal lenders to start businesses have lower profits compared to other sources.

Credit access challenges occur when small businesses fail to obtain credit from lenders despite their ability to use the finances productively (OECD, 2006). When funding difficulties leads to collapsing economically viable projects innovation; growth and economic development is negatively affected.

Small and Medium Enterprises in Nairobi County

There is no single definition for SMEs because of the diversity of businesses. What SME means exactly is dependent on the number of employees and business' turnover and assets. A small business is regarded as one whose scale of operation is less than the industry average. The term 'SME' is used in this research to mean those firms with less than 100 employees. In Nairobi county, small businesses lack access to capital and money markets. Investors are unwilling to invest in sole proprietorships, partnerships or unlisted companies as the risk

perception is high, and so is the cost of capital and institution credit which requires collateral when available, which in turn makes the business even more vulnerable to foreclosure. Despite efforts by financial institutions and public sector bodies to close funding gaps, SMEs continue to experience difficulty in obtaining capital. These funding gaps relate to firm size, risk, knowledge and flexibility (Ross, 2007).

SMEs are regarded by many as the backbone of every country's economy. Most of the large corporations of today were developed from SMEs. Small and Medium Enterprises also support the larger corporations in form of sub-contractors, suppliers of manufacturing materials or customers. In Kenya, SMEs have played a major role in the reduction of poverty from 51.7% in 1999 to 39.5% in 2015 and also reducing extreme poverty from 36.4% to 27% over the same period (UNDP Action plan, 2016). Despite the tremendous contributions to the economy, SMEs in Kenya and in Nairobi county have a lot of difficulties when accessing funds from financial institutions.

Determinants of Financial Performance

Interest Rates

SMEs have to pay a higher rate of interest and comply with more restrictive requirements on institutional credit obtained by them, compared to those imposed on their large-scale counterparts (Berger, 2004). Moreover, upwards of four-fifths of SME applicants are required to provide suitable collateral and the preferred security of fixed real estate assets has imposed a difficult requirement on smaller enterprises.

Inflation

Low interest rates stimulate the economy, but could lead to inflation. When interest rates are high, people do not want to borrow from the bank because it is more difficult to pay back the loans, and the number of real assets purchase goes down. While the effects of a lower interest rate on the economy are very beneficial for the consumers, they are not beneficial for lenders, who are seeing a lesser return on their assets than in times of high interest rates. The problem of high interest rates is one that is generally associated with Sub-Saharan African financial markets. This is seen as reflecting the absence of competition in the markets. The clearest indicator of the absence of competition in Sub-Saharan African financial markets is the continuing wide spread in interest rates. In general, between 1990 and 2004, the spread which

is the difference between lending and deposit rates for many Sub-Saharan African countries was in excess of 12 percentage points and appeared to be widening (Aryeetey, 2005).

Tangible Assets Availability

Previous researchers suggest that bank financing will depend on whether the lending can be secured by collateral (Berger and Udell, 1998). When other factors are held constant, firms with more intangible assets have limited access to financing, compared to firms with more tangible assets. SMEs have fewer collateralizable assets than large firms. This may partly relate to the stage of growth the firm is in. In the earlier stages of the firm, it may have lower retained profits which may hinder it from purchasing fixed assets compared to the larger firms which have a longer history.

Group Guarantees Availability

As indicated by Ono (2005), small business in Africa can once in a while meet the conditions set up by lending organizations, which view SMEs as an unsafe, in view of poor certifications and absence of satisfactory data about their capacity to reimburse advances. The money markets in the greater part of Africa are immature, thus, they give less monetary instruments. Capital markets are in their early stages, shareholding is uncommon and no long-haul financing is accessible for SMEs. Non-bank monetary mediators, for example, Micro Finance Institutions, which could have of greater help in loaning cash to the little SMEs don't have the assets to catch up their clients when they extend (Hempel, 2007).

Leverage

This is the term used to describe the converse of gearing, which is the proportion of total assets financed by equity and may be called equity to assets ratio. The study focused on total debt as a percentage of equity or total assets. There are however, some studies on the relative proportions of different types of debt held by small and large enterprises.

Research Problem

To establish how credit accessibility affects financial performance of SMEs in Nairobi county.

Methodology

The descriptive research design was used in the study because the variables were analyzed in terms of means and standard deviation. A correlation research design determines whether two

variables are related, it was considered adequate and appropriate because it can describe the statistical relationship between independent variables of the study (access to credit) and the dependent variable (return on assets). The target population comprises of 1,570 SMEs, that is according to the City Council of Nairobi human resource department, 2016. This research employed a simple random sampling technique. The sample frame was based on the population of owners and employees in SMEs firms within Nairobi County therefore a sample of 157 was selected. Secondary data were used in this research for gathering information that was obtained from the annual reports and accounts of the companies listed at NSE. The data covered a period of five years ranging from the year 2012 to 2016. The primary data was obtained by use of questionnaire which contained both closed and a few open-ended questions. The questionnaires were administered using drop and pick method. Quantitative data analysis was undertaken by use of the statistical package for social science (SPSS version 21). Percentages, means and frequency distribution tables were run to present the results. Relationships between the independent and the dependent variables were established using multiple regression analysis.

Analytical Model

The study used multiple regression model as recommended by Hair et al. (2006).

The model specification is as presented herein under.

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

Where:

Y = Return on Assets

X₁ = Loan Amounts (Ln Loan Amounts)

X₂ = Access to Credit

X₃ = Total Assets (control variable)

The multiple regression models were used to predict the values of α_0 and β_i , which explains the association between the independent variables and dependent variable.

The regression analysis was used. The ANOVA test was done to determine firstly, the impact of independent variables on the dependent variable in the regression analysis and secondly, test the mean score differences and then use T – statistic test to establish the likelihood that there is a link between ownership and performance which are the main data variables. A significance level of 5% was used.

Results and Discussion

Response Rate

Information was collected for 110 registered SMEs, with available and complete set of data for a period of 5 years from 2012 to 2016. Data on loan amounts, total assets and performance of the SMEs was gotten from financial reports. Questionnaire completion rates is the proportion of the sample that participated as intended in all the research procedures. In this study 157 questionnaires administered, 110 (70%) filled in and returned, this return rate was deemed as adequate for the study.

Reliability Test

The study used Cronbach statistics to test for reliability. In Cronbach, any alpha of more than 0.7 shows that data was reliable. The findings show Cronbach alpha of 0.798 which is more than 0.7 indicating that data was reliable.

Descriptive Statistics

Descriptive statistics including the mean, standard deviation, coefficient of variation, skewedness and kurtosis. Table 1 below shows the descriptive statistics for each of the independent variables; Data on fund size, current assets, current liabilities, liquidity as well as the dependent variable performance as measured by the ROA is shown in Table 1 below.

Table 1: Descriptive Statistics

	N	Minimum	Maximum	Mean	Std Deviation
ROA	110	-.63	.42	.0481	.17774
Size	110	12.90	23.96	16.4414	2.11387
Loan	110	9.20	19.60	13.9564	2.46865
Access	110	1.00	5.00	3.2655	1.53177
Valid N (listwise)	110				

Source: Authors (2017)

The mean for the ROA was an indication that there was a big variation of performance as measured by ROA with a standard deviation of .17774. The mean was an indication that there was a big variation on the size of SMEs in Nairobi County with a standard deviation of 2.11387. The variables have positive skewness meaning that the distribution has a longer tail on the higher-return side of the curve meaning the data is asymmetrical. A negative kurtosis is also observed, which implies a platykurtic distribution and indicates a higher probability

than a normally distributed variable of values near the mean and a lower probability than a normally distributed variable of extreme values (Cooper & Schindler, 2003).

Questionnaire Response Rate.

In this study, 157 questionnaires were administered, 110 (70%) were filled in and returned, this return rate was deemed adequate for the study.

The demographic information

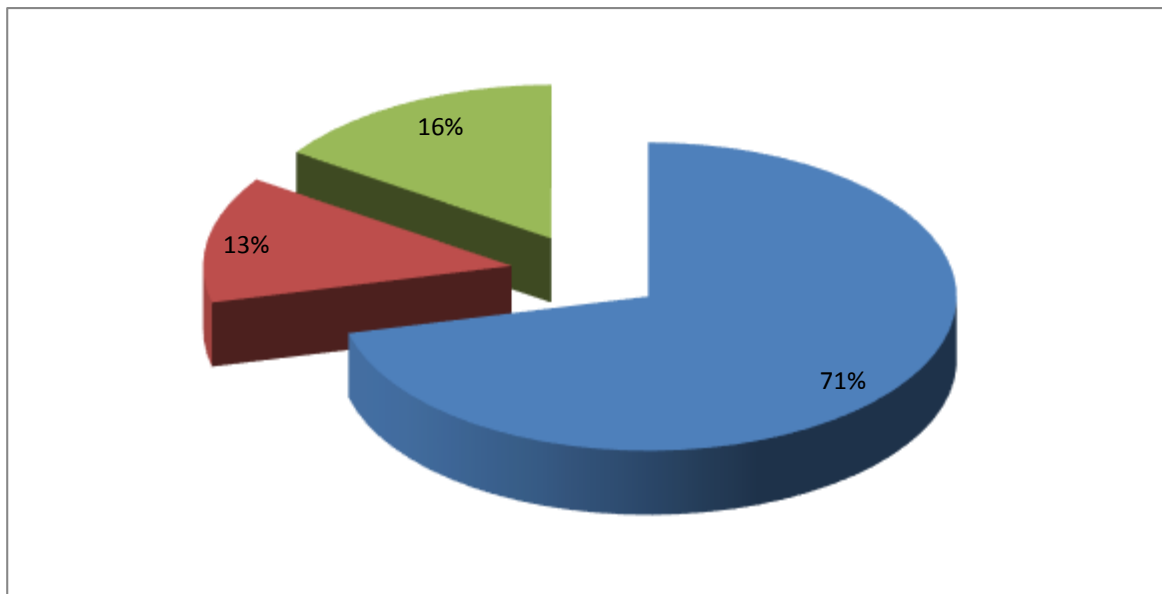
Table 2: Sex

Factor	Frequency	Percentage
Male	96	0.87
Female	14	0.13
Total	110	1.00

Source: Authors (2017)

The study implied a large number of the respondents were male.

Figure 1: Designation



Source: Authors (2017)

When they were asked about their designation the response was as follows 32 (71%) indicated administration, 7 (16%) indicated finance and 6 (13%) indicated customer service. The researcher concluded that most of the respondents were administrators.

Table 3: Age

Factor	Frequency	Percentage
19 – 24 years	34	31
25 – 29 years	20	18
30 – 34 years	24	22
35 – 39 years	14	13
40 – 44 years	12	11
45 – 49 years	4	4
Over 50 years	1	1
Total	110	100

Source: Authors (2017)

Therefore, from the table above there is a strong indication that a majority of the employees are between the ages of 19 to 24 years among the SMEs in Nairobi County.

Figure 2: Educational Level

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Source: Authors (2017)

On the educational level the majority of the respondents attained high school level of education.

Table 4: Working Years

Factor	Frequency	Percentage
1 – 4 years	27	24.4
5 – 9 years	17	15.6
10 – 14 years	17	15.6
15 – 19 years	12	11.1
20 – 24 years	17	15.6
25 – 29 years	20	17.8
Over 30 years	0	0
Total	110	100

Source: Authors (2017)

As per the working years in the SMEs the responses indicated that most of the workers have worked for between 1 – 4 years in the SMEs.

Correlation Coefficients of Pension Funds

Pearson Correlation was used to determine the degrees of association between the independent variables (performance, size, loan amounts and credit access) and dependent variable.

Table 5: Correlation Coefficients

		ROA	Size	Loan	Access
ROA	Pearson Correlation	1	.438**	.362**	.713**
	Sig. (2-tailed)		.000	.000	.000
	N	110	110	110	110
Size	Pearson Correlation	.438**	1	.881**	.540**
	Sig. (2-tailed)	.000		.000	.000
	N	110	110	110	110
Loan	Pearson Correlation	.362**	.881**	1	.517**
	Sig. (2-tailed)	.000	.000		.000
	N	110	110	110	110
Access	Pearson Correlation	.713**	.540**	.517**	1
	Sig. (2-tailed)	.000	.000	.000	
	N	110	110	110	110

** . Correlation is significant at the 0.01 level (2-tailed).

Source: Authors (2017)

The correlation matrix shows that there is a strong positive relationship between credit access and performance with an association of positive .713. The relation between the size and performance was also positive at .438 while the relation between performance and loan amounts was a positive .362 which was not very strong. All the relations were significant with p values being less .05.

Regression Analysis

Regression analysis of the model provided the results summarized in Table 6 below.

Table 6: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.724a	.524	.511	.12435

a. Predictors: (Constant), access, loan, size

Source: Authors (2017)

The model has a coefficient of correlation, R of 0.724 which indicates a strong positive relationship between the variables. The coefficient of determination, R square indicates that 52.4% of the variations in the dependent variable are explained by the independent variables. The predictors are viewed as statistically significant compared to all the other variables that affect returns of pension funds. The standard error of .12435 indicates variability in the model estimates.

Table 7: Regression results

Model	Unstandardized Coefficients		Standardized Coefficients		t	Sig.
	B	Std. Error	Beta			
1 (Constant)	-.360	.100			-3.578	.001
Size	.023	.012	.272		1.872	.044
Loan	.116	.010	-.226		-1.577	.018
Access	.079	.009	.683		8.504	.000

a. Dependent Variable: ROA

Source: Authors (2017)

The regression coefficient value of size was .023 with a p-value of less than .05. The regression coefficient value of loan amounts was .116 with a significance level of 0.018 while regression coefficient value of credit access 0.079 and the p value were significant.

$$Y = -0.360 + 0.023X_1 + 0.116X_2 + 0.079X_3 + \epsilon$$

Taking all other factors as zero, the return on fund will be -0.360. However, this is not a reasonable interpretation due to the fact that the performance and credit access can never be zero. The coefficient of 0.023 indicates the difference in predicted value of Y for each one-

unit difference in size, all other factors held constant. From Table 7 above, it is evident that loan amounts and credit access have a significant relationship with performance ($p < 0.05$).

Table 8: Analysis of Variance (ANOVA^b)

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	1.803	3	.601	38.823	.000 ^a
Residual	1.641	106	.015		
Total	3.444	109			

a. Predictors: (Constant), access, loan, size

b. Dependent Variable: ROA

Source: Authors (2017)

The overall model was statistically significant ($P < 0.05$) as illustrated in the Analysis of Variance Table 8 above, indicating that all the variables have a significant relationship with the performance of SMEs in Nairobi County. Under the null hypothesis, the statistic has an F-distribution with 38.823 and 109 degrees of freedom at 5% level of significance and 95% confidence interval. The null hypothesis that credit access and financial performance of SMEs in Nairobi County are related was therefore accepted.

Findings

From the findings obtained, the regression equation further implied that there was a direct relationship between access to credit and financial performance of SMEs in Nairobi County. The analysis was undertaken at 5% significance level. Therefore, from the above analysis access to credit was significant in the model as its corresponding predictor variables were less than 5%. This shows that the model is a good predictor which is well explained by the coefficient of determination $R^2 = 52.4\%$. The granting of loans or credit to SMEs is still a major problem as many of SMEs are unable to access such funds. Also, there is the problem of information between the loan provider and loan receiver as to the availability and cost. The study revealed that most borrowers could only borrow a small amount of money from the financial institutions since they were eligible to only access such amounts given the criteria set by the institutions and also because they were reluctant to take out large amounts that they may not be able to repay. Such small amounts can only have so little impact on the financial performance.

The financial institutions have severally refused giving credit facilities to various SMEs due to different reasons. Some of the reasons given by the financial institutions include: inability

to meet all needed requirements, the credibility of the entrepreneur, unrealistic proposals, general economic conditions, unfavorable turnover, weak balance sheet and others. Most of the attention was given to the turnover of the enterprise requesting for the loan. This was followed by the credibility of the entrepreneur. This includes a background check on the ability of the entrepreneur to pay back the loans or if there are any outstanding loan in their name. Little priority was given to the SMEs fulfilling all needed requirements and the general economic condition in the country. This is similar to Hiedhues (1995) who stated that accessing credit is considered to be an important factor in increasing the development of SMEs.

This concurs with Navajas et al, (2000) that the main objective of microcredit is to improve the welfare of the poor as a result of better access to small loans that are not offered by the formal financial institutions. Diagne and Zeller (2001) also argue that insufficient access to credit by the poor just below or just above the poverty line may have negative consequences for SMEs and overall welfare. Access to credit further increases SMEs risk-bearing abilities; improve risk-copying strategies and enables consumption smoothing overtime. With these arguments, microfinance is assumed to improve the welfare of the poor.

The study found that there was a strong positive relationship between savings and the financial sustainability of SMEs. This comes to an agreement with Guichandut (2006) that more MFIs are becoming interested in the potential of savings, thanks partly to the global financial crisis which has become a big boost to the SMEs. The study further found that the SMEs do not have a long history of saving culture. The savings have an influence on the financial sustainability of the enterprises amounts, most microfinance institutions offer savings services and savings influences financial sustainability. This corresponds with Cheston and Kuhn (2001) findings that in an emergency, richer people might choose between dipping into their savings and borrowing. The choice for the great mass of the unbanked in the developing world is limited to whom to borrow from, often at great cost.

Conclusions

Lack of access to financial capital has been frequently stressed as a major (if not the main) impediment to firm growth in developing countries. The problem is further compounded by stringent requirements that lock out potential borrowers such as high interest rates and collateral required. Micro and Small Enterprises typically lack sufficient collateral or personal guarantors to pledge against formal loans, or they are unfamiliar with the

bureaucratic procedures of accessing credit. Financial capital is the catalyst for firm expansion. Hence, insufficient access to it is evidently harmful to the overall economic growth. Financial constraints slow down capital accumulation, impede productivity improvements and increase the time it takes for entrepreneurs to reach their potential objective's.

The literature that was explored in this research highlighted three main factors that contribute to accessibility to funding for SMEs. These factors guided the course of this research throughout. These are total assets, loan amounts and profitability. The SMEs contacted were of the view that financial constraints do exist in the SME sector. This was attributed to a financing gap that exists between larger and the smaller companies' accessibility to funding. Lack of access to equity financing coupled with the lenders shying off from SMEs' funding, this only tends to augment the difficulty. Under the firm characteristics, size and age of the firm were investigated to determine whether they influence SME's access to funding. It was found that the smaller the business, the greater the difficulty of accessing funds. The size was found to be directly correlated to the financial performance of the SMEs. It was evident from the findings that 52.4% generally agreed that establishing relationship with the lending institutions would ease the burden of borrowing.

Recommendations

Recommendations that can be made are; financial institutions should consider revising their policies on interest rate charged, credit policies and appraisal techniques and limitation on the amount of credit granted to SMEs. Another recommendation is that financial institutions should consider reducing or waiving associated costs of borrowing, so as to increase SMEs accessibility to credit and stimulate financial deepening. The study also recommended that to increase SMEs accessibility to credit, loan limit policies should be reconsidered or harmonized to accommodate the needs of SMEs. Finally, the study recommended that all stakeholders in the different sectors should intervene to ensure that SMEs have access to financial services to enable them to contribute to development.

The Government can play an important role in supporting the SME sector particularly in cases of market failures and incomplete markets that inhibit the provision of adequate financing or financing on terms suitable for the stage of SME development. This would help in creating an enabling environment for the SME sector, entrepreneurship and innovation; an

enabling environment that provides, among other things, political stability and security. This boosts the investors' confidence. Government measures to promote SMEs should be carefully focused, aiming at making markets work efficiently and at providing incentives for the private sector to assume an active role in SME finance. It should also reduce the transaction costs that the SMEs incur in order to access government grants.

Public policy should improve awareness among entrepreneurs, on the range of financing options available from official programs, MFIs, private investors and banks. Lack of proper knowledge on the available financial services has locked many entrepreneurs from advancing. At the same time these entrepreneurs need to establish linkages with their partners in the business and with the lending institutions that could help them build their knowledge on the available financial services, management of funds and other business skills. Such associations could prove important for the SMEs in accessing fund where one SME could even act as a guarantor for another.

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