Gender, Institutions, Access to Finance and the Development of Small Scale Enterprises in Kenya: Lessons for the Global Economic Crisis

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Abstract

Small and Micro Enterprises (SMEs) have become an important sector in the Kenyan economy, becoming a major employer for the female labour force in the country. Despite their proliferation, SMEs continue to face a number of constraints, like lack of finance, which limit their development. Due to their characteristics, women-owned SME face more constraints in accessing services, which affect their performance. Literature from the New Institutional Economics (NIE) shows that institutions like linkages and networks provide an important avenue through which enterprises can overcome some of their constraints. Using primary data from a sample of small scale enterprises in Kenya, this paper analyses the institutional networks among women owned SMEs, and with financial institutions and their effect on enterprise performance. It addresses the question of whether institutions can improve the performance of female owned enterprises facing constraints and shocks like the economic crisis. The results show that SMEs have networks among themselves and with financial institutions, which have advantages, reflected in the enterprises' performance. The paper concludes that there is need for policy to strengthen institutional networks among SMEs, to enable them overcome some of their constraints and mitigate the effects of shocks like the economic crisis on their performance.

1. Introduction

1.1 Background

This paper is based on a study motivated by the increasing importance of Small and micro enterprises (SMEs) in the Kenyan economy, while they continue to face a number of constraints in their activities. At the same time, SMEs in Kenya have become a major employer of the female labour force and a source of livelihood for women in the country. The paper applies the New Institutional Economics (NIE) approach to explore the question of whether institutional arrangements among female owned SMEs and between MSEs and financial institutions improve the enterprises' access to financial services and their performance. It attempts to answer the question of whether institutional networks benefit women owned enterprises.

A number of factors make women's participation in the informal sector important. Most of the SMEs are located in the informal sector which has increased its share of employment since the 1980s. Women's share in formal sector employment is proportionately less than that of their male counterparts, while participation of females in wage employment has remained low compared to men's. The share of women in the labour force also shows that they are disproportionately concentrated in community, social and personal services. Although women's share in total wage employment has increased, their share in the traditionally male dominated industries still remains low, while their share in community, social and personal services stands at 42.8% (Republic of Kenya, 1998, 1999, 2007). There are fewer women than men among the regular employees and skilled workers. Women on the other hand outnumber men in the categories of unskilled workers and dominate among unpaid family workers. Regionally, unemployment levels are higher in both rural and urban areas for women than for men.

The characteristics of female owned enterprises are also important. In the informal sector, female owned enterprises have been found to employ fewer workers, and less capital compared to the male owned ones. It is estimated that about 57% of the total informal sector labour force is generated by male owned enterprises while 43% is generated by female owned enterprises ones (CBS, KREP and ICEG 1999). These characteristics of women owned enterprises in the informal sector are also important for employment generation and growth. They start small, grow slowly, and end smaller than the men owned enterprises (McCormick and Mitullah 1995, Atieno 2007). They locate more in the home, rely more on less skilled and unpaid workers, and are less likely to diversify into other activities. In addition, women's activities tend to be less remunerative than the men's. Women face a number of obstacles in entering business, which mostly condemn them to low income occupations.

Despite their increasing importance as a source of employment and incomes for women in the country, SMEs continue to face a number of challenges. Lack of access to financial services is one of the main constraints facing SMEs in Kenya. A number of factors have been identified as explaining the problem of access to financial services by small-scale borrowers like MSEs. Conceptually, the nature of credit markets, which are segmented and incomplete, is one explanation for the limited access to financial services. Due to the risky and inter-temporal nature of credit trade, the information requirements and enforcement problems for lenders are high, resulting in agency costs, which affect the outcome of credit programmes towards SMEs. As a result, firms may prefer funds from external sources but fail to apply due to the high costs of loan application. While financial market involvement by firms may be limited, smaller firms, like the women owned enterprises, have much less involvement than the larger ones (Bigsten et al). On the supply side, most formal financial institutions consider SMEs uncreditworthy, thus denying them credit and other financial services. The slow growth of firms has in turn been attributed by some to lack of access to financial resources (Nkurunziza, 2005).

Literature from the New Institutional Economics (NIE), show that institutions like linkages and associations provide an important avenue through which firms can overcome some of their constraints, and hence enable them achieve goals that they would otherwise not be able to achieve on their own. Networks like associations by cushioning enterprises, enable them to access different forms of services like finance. The question that emerges is therefore how the linkages can contribute to the development of women owned small scale enterprises by improving their access to financial services.

The paper uses primary data collected from a sample of small scale enterprises in two urban centres of Kenya, to analyse the nature of linkages between women owned SMEs and financial institutions as well as the networks among SMEs and their effect on enterprise performance. It address the question of whether institutions can help to improve the performance of female owned enterprises. The data was collected through a survey of sampled enterprises and key informant interviews conducted during the months of October and November 2006. A total of 322 micro and small scale enterprises were interviewed through a structured questionnaire. The paper takes a gender approach in the analysis and disaggregates the data into male and female owned enterprises.

This paper is organised as follows: After this introduction, section 1.2 presents brief overview of the SMEs and female employment in Kenya. Section two presents literature review, focusing on the role of institutions. Section three gives the main enterprise characteristics and discusses the analysis of enterprise linkages and enterprise performance. Section five ends with the summary and conclusions.

1.2 Overview of SMEs and Female Employment in Kenya

The informal sector has become increasingly important in the Kenyan economy as a source of employment and income. During the last decade, the growth rate in the sector's employment has remained above that of the formal sector, whose employment growth rate declined, making the sector grow slowly. As the formal sector has The informal sector has seen its share in total employment rise from 16% in 1980, to 63.6% in 1997 and 70% in 2000. Its share in GDP has also recorded increases, rising from 13% in 1993 to 18% in 1999 (Republic of Kenya, 2002). Sectorally, the informal sector is the second largest source of employment after small-scale agriculture (Ministry of Finance and Planning, 2000). The 1999 national survey of small and micro-enterprises (SMEs) found that about 26% of the total households in the country are engaged in some form of SME activity (CBS KREP and ICEG, 1999). The sector is therefore an important source of livelihood for a majority of the country's population. Currently, informal sector's share in total employment stands at 78% (Kenya 2009).

In terms of gender, formal sector employment is male-dominated, with women currently constituting only about 29% of total labour force. Approximately 70% of these women are in the lower income bracket of Ksh.8, 000 to Ksh 25,000 (US $ 103-321) per month. The recent increase in female wage employment has largely been in casual employment. Women are mostly engaged in activities traditionally dominated by females while men are relatively evenly distributed across sectors. Women tend to be concentrated in the informal sector.

Surveys on the labour force participation in both the formal and informal sectors show that women are disproportionately concentrated in certain activities, with limited access to more remunerative enterprises. This is mainly because the choice of occupation depends on factors like education, training, capital requirements, premises and expected earnings. These factors combine to restrict women to trade and other service activities in the informal sector and bar them from other activities. This exclusion from certain activities limits their incomes since male dominated activities are better paid than the female dominated ones. The 1999 ILO report also notes that women's participation in specific sub sectors and activities of the informal sector is quite low (ILO/EAMAT 1999). Household budget surveys as well as empirical studies have shown that female headed households are more vulnerable to falling into poverty than the male headed ones because of women's limited access to productive assets and education (WMS 1997, KIHBS 2007, Atieno 2006).

2. Literature Review

2.1 Institutions and Enterprise Development

Literature on Business Systems and the NIE document the advantages of linkages between firms (McCormick and Atieno 2002), while institutional approaches to business development emphasise the nature and potential costs of interactions between economic units (McCormick and Kimuyu 2004). Linkages between firms are important because they help them achieve goals that they would otherwise not be able to achieve on their own, like access to inputs, goods and specialised services like finance. Institutions, of which linkages are part, have been defined as a set of constraints governing the behavioural relations among individuals and groups (Nabli and Nuggent 1989). They are predictable, understood as either formal or informal ones like labour unions, markets, contracts, as well as cultural rules and codes of conduct as different forms of institutions (Nabli and Nuggent 1989). The importance of institutions derives from the fact that economic actions take place in a social context. Economic actions are embedded in social contexts Grannovetter (1985). Hence an entrepreneur, being a socially embedded individual, will use his/her personal networks for the benefit of the enterprise. The position of the person in the network and the power associated with the position determines the benefits of such networks to the enterprise. Networks of relationships shape the form that market exchange takes. Due to the externalities generated by networks, market entry is easier for members of a specific network than for others (Fafchamps 1999). They contribute by establishing stable structures of interaction.

Linkages are meant to improve resources, but lack of resources will also limit the ability to form linkages. Recent research on business systems (Oketch et al. 2002) show that firms which are limited in resources like small firms may be constrained from joining any networks or contacts due to the costs involved in such associations. This in turn limits the extent to which they can influence the support mechanisms like policies, legislations and infrastructure that affect their businesses. Small firms face a number of constraints, which are institutional in nature, but their weak organisational ability and limited or non existent linkages restrict the extent to which they can address such constraints.

There are a number of forces that influence how individual business activities are organised and operated. These include government business associations and financial institutions. Firms as the basic units of business activity often find it advantageous to join together into associations, which are formed for the joint benefit of the members. Associations help members benefit through collective influence and accessing specific services. Through collective influence, associations lobby for policies that benefit its members, while they also respond to member’s individual needs for services (McCormick and Kimuyu 2004). Since all businesses need capital either for start up or operating capital, financial institutions become an important force for business development. Formal financial institutions normally suffer from problems of loan screening and enforcement of repayments due to information asymmetry. Such imperfections raise the cost of credit, limiting borrowers to such services.

Linkages can be seen either as part of a wider network of social relationships, or narrowly as connections between persons and organisations (see McCormick and Atieno 2002). Linkages can be classified into contracts, collaborations, contacts and associations. This study draws from the different perspectives arising from the discussions on linkages, and focuses on linkages among firms, rather than linkages as part of a wider network of social relations. Although the focus is largely on economic relationships, the non economic aspects of the interactions are also considered in the context of how they affect the firms' activities. Both theoretical and empirical evidence suggest that specific social relations are among the factors that affect economic activities (Grannovetter 1985, Whitley 1992).

Egbert (2004) notes that in many developing countries, entrepreneurs have to deal with instability and unfavourable economic conditions. Under such circumstances, networks can help them overcome constraints they would otherwise not be able to overcome. Networks can be personal or organisational and can be seen as entrepreneurial resources or constraints. When entrepreneurs use their personal networks for the benefit of the enterprises, the personal networks contribute resources for the enterprise. However, personal networks can also be a constraint to the enterprise. The effect of the network, whether positive or negative, depends on how the entrepreneur is able to use the positive effects while avoiding the constraints. The most valuable input for an enterprise generated by networks is information. Other resources are access to capital, inputs, markets, training opportunities and reliability.

Linkages affect firm performance in different ways. Using data from manufacturing firms in Ghana, (Barr 1998) identifies general patterns linking enterprise types and networks as well as structure and effect and concludes that networks affect enterprise performance in different ways and extents, depending on the functions they are built to perform. This is because alternative network structures suit alternative functions. Entrepreneurs with larger enterprises tend to maintain large, diverse and less cohesive innovation networks, which are more suited to providing information about technology and markets. On the other hand, entrepreneurs with smaller enterprises tend to maintain small homogeneous and cohesive networks suited to reducing information asymmetries and hence supporting informal credit and risk sharing arrangements. The paper further concludes that while the smaller solidarity networks may have a marginal effect on enterprise productivity, it is the innovation networks that have a large and significant impact.

2.2 Networks and Uncertainty

Networks of interrelations can enhance the performance of manufacturing enterprises by improving their income generating ability and capacity to compete. In addition, they can also help to reduce the uncertainties faced by enterprises. Networks can affect enterprise performance by providing entrepreneurs with information on various aspects like markets and technology. Information about output markets, their functions and standards, may help enterprises become more competitive, with direct effect on productivity (Barr 1998). A network that reduces uncertainty may increase performance indirectly by encouraging higher levels of investments. It is argued that the relative importance of the two functions to an entrepreneur will determine the kind of networks that an entrepreneur maintains and the effect of such networks on its performance.

In most African countries, much of the uncertainties are caused by poor contract discipline which is due to poverty and unanticipated difficulties, which result from shortage of inputs, delayed payments and transportation problems. Information asymmetry, and the associated high transaction costs however make it difficult for entrepreneurs to identify poor contract enforcement resulting from such difficulties as opposed to those resulting from incompetence. In most African countries therefore, entrepreneurs rely on their networks to reduce information asymmetry by facilitating information flows, providing a basis for credit, trade and insurance. Networks also affect individual access to credit sources (Okten and Osili 2004). Networks can facilitate the flow of information about credit sources, which can lower transaction costs. Individuals with stronger family and community networks will have greater access to credit due to their information advantage.

Despite the importance of credit in most African countries' uncertain environments, its market is among the most affected by poor contract discipline and information asymmetries in these countries. Different institutional environments exist for different types of enterprises, with formal credit available for those with collateral, operating in an environment with well defined property rights, while at the same time, there is informal credit for those with no property rights, but supported by informal networks. In this role, networks therefore can help to substitute for formal market supporting institutions. Although larger informal credit arrangements and risk sharing are more efficient, at certain size the cost of acquiring information may outweigh the benefits. Increasing network diversity also increases the cost of acquiring information. As a result, it is expected that sharing arrangements are likely to be confined to people with broadly similar abilities, character and prospects. Different types of networks perform different functions. An uncertainty reducing network will enhance enterprise performance indirectly, through increased investments, and informal credit overcoming capital constraints.

Fafchamps (1999), argues that the presence of transaction costs leads market participants to enter into long term trading relationships that shape market outcomes. Fafchamps (1999) further identifies two types of institutions that have arisen to minimize the transactions costs are relationships and networks.

2.3 Why Firms Link

Firms link for a number reasons. Firms link in order to attain ends that they cannot meet alone. Linking enables firms to overcome some of the constraints like lack o finance. Other reasons for linking that may also result from access to finance include access to raw materials, or inputs and technology (Oketch et. al,) Hence one of the reasons why firms form linkages and relations is for the purposes of acquiring finance and related services. Small firms are mostly constrained by lack of working and investment capital. Linkage between firms can ease such constraints by reducing the amount of fixed capital required. Vertical linkages between producers and their suppliers may bring credit that reduces working capital requirements. Linkages may also provide access to new sources of capital like being members of group lending schemes. In such schemes, micro enterprises join together to guarantee each others loans. Small firms may also link with large firms as a way of being able to access superior management capability, technology, market information, and finance that are important for firm survival (Meyanathan and Munter 1994). This study considers linkages as relations between individuals or organisations, with firms being the main actors.

Linkages have a number of potential benefits to Firms. They help to improve firm performance by reducing marketing costs, increasing firm flexibility, improving skills and diffusion of skills as well as facilitating information sharing (McCormick and Atieno 2002). They therefore enable firms to achieve goals they would otherwise not achieve on their own. Despite these potential benefits, evidence from the study of business systems show that most small firms, especially those in the informal sector have fewer interactions with firms bigger than them in comparison to large firms. Their associational lives are also limited (Oketch et al. 2002). Limited linkages among SMEs, and with financial services limits their flexibility in taking up emerging entrepreneurial opportunities, and raises the issue of the potential contribution of linking formal and informal financial services. The main line of discussion with respect to linkages pursued in this study is thus identifying the type of linkages existing between firms and the potential benefits behind the formation of the different types of linkages that exist.

Associations are one major form of institutional networks. There are a number of reasons for joining associations. The building of social capital is one reason for joining associations, enabling people to make contacts that they hope to help them in future. In considering the role of associations, their size has been found to be important in determining the benefits to their members. Barr (1998) notes that smaller businesses tend to adhere to smaller networks while larger businesses tend to choose large networks. The small networks, typical of small scale enterprises, are often motivated by the desire to reduce risks while those by large businesses aim at enhancing business performance. The nature and relative importance of private and spillover effects also vary between small and large networks. Small networks tend to generate significant positive spillovers since within themselves it is difficult to exclude individuals from the benefits of the networks. Large networks to which large enterprises belong tend to generate high private returns (Barr 1998).

3. Results and Discussions

3.1 Enterprise characteristics

In this section, we present the main enterprise characteristics like firm history, ownership, size and sources of finance. These characteristics are important in determining the development of firm linkages and their contribution to enterprise performance. They also differ between men and women owned enterprises. The nature of linkages and their benefits by firms for example are likely to differ by firm size[1]. Studies have shown that large firms are more likely to receive more loans, have higher indebtedness, rely less on informal loans, and have more access to credit compared to the small firms, the majority of which get their loans from informal sources of finance (Bigsten et al. 2000). Large and small firms also have different types of linkages, with large firms more likely to have large networks providing information about markets and technology as opposed to the small firms (Barr 1998). In terms of gender, women are more likely to own small enterprises compared to men.

The results show that on average, most enterprises were started by single individuals, with the highest number of owners being three. The enterprises also vary in their age from those less than one year to those as old as 34 years. The mean age was found to be 8.6 years. The data further shows that about 71% of the enterprises in the sample were started after 1994, and are therefore not more than 11 years old. This is an important outcome, conforming to the observation that the informal sector in Kenya experienced its most rapid growth in the 1990s. This is the period that experienced major decline in the

[1] The definition of firm size used in this study is based on the GEMINI definition which considers firms with 1-10 employees as small, those with 11-49 as medium, and those with over 50 as large. See also McCormick and Atieno (2002).

formal sector, resulting from the implementation of economic reforms as well as economic stagnation.

The sample is almost equally distributed in terms of the gender of those who started the enterprises, with 50.3% of those who started being females, and 49.7% males. The national survey of MSEs (CBS, KREP, ICEG 1999) showed that men own 52% of the enterprises, while women own 48% of the enterprises.

The education level of those who started the enterprises ranges from those with no education to those with university education. Most however had secondary level of education with training. They are concentrated between those having primary education with training, and those having secondary education with training. Looking at the level of education by gender shows that most of the women entrepreneurs have their education concentrated at the level of secondary with training (table 1).

Table 1: Education level for those who started the enterprises

Level of education	**Total Sample**		**Female**	
	Frequency	**%**	**Frequency**	**%**
None	9	2.8	5	3.1
Primary	33	10.2	14	8.6
Primary with training	79	24.5	37	22.8
Secondary	95	29.5	50	30.9
Secondary with training	103	32	54	33.3
University	2	0.6	1	0.6
Adult Education	1	0.3	1	0.6
Total	**322**	**100**	**162**	**100**

Sources of finance for enterprise startup ranged from own savings at home to retirement benefits and gifts from relatives. Majority (56.8%) however started with capital from savings at home, while none started with bank loan. It is also noteworthy that only two enterprises started with supplier's credit. This conforms to the results from other studies which show that small firms used less trade credit among Kenya's manufacturing firms, compared to large firms, most of which obtained trade credit (Issakson and Wilhborg 2002). Bigsten et.al, (2000) also find that more large firms have bank overdrafts compared to small firms in Kenya's manufacturing sector. The SMEs therefore appear not to have support services especially from the financial sector. Looking at the source of finance by gender, we find that most (53.7%) of women entrepreneurs started with savings at home. While about 20% used gift from families and another 24.8% used loan from family.

Enterprise Ownership and Size

Enterprise ownership and size are important characteristics in determining its linkages and the access to services like finance as well as the performance. Enterprise ownership has been associated with the firms' ability to mobilise financial resources (Ikiara et al, 2002). Bigsten et al. (2000) in their study of manufacturing firms in Africa observe that, although general financial market involvement in the form of borrowing is limited, there are differences across firm sizes, with large firms receiving more loans and having higher indebtedness than small firms. Manufacturing firms in Africa have been found to have different levels of productivity, depending on the size (Soderbom 2000). We find that 59% of the firms had no employees. Enterprise ownership also determines the type of linkages they can have.

Enterprise size is an important characteristic that is likely to influence performance. Among other things, firm size determines access to services like finance and is likely to influence the type of linkages that an enterprise develops. The results show that despite most enterprises being sole proprietorships (owned by one persons), some also employed workers, although the majority did not have any employees. The highest level of employment was for the temporary male employees, where about 32% of the firms had between one and ten temporary male employees. This category is followed by temporary female employees. It therefore appears that those enterprises that employ prefer temporary employees.

3.2. Inter firm Linkages Among Enterprises

The data collected from the survey contained information on the linkages among the SMEs including the environment within which they operate as well as enterprise networks. The questions on networks included the number and nature of contacts they maintained with the different types of the enterprises. These related to linkages with enterprises of different sizes and activity, linkages with other enterprises in the same line of business, or different lines of business, with smaller or larger enterprises, linkages with financial institutions as well as membership to networks of informal groupings. This information is used to capture the networking activity of the enterprises.

Information on the institutional environment within which the enterprises operate was taken in terms of whether they use formal sources of credit and other financial services or not. The indicator of potential market diversity used here relates to market outlets for the enterprises and users of their products, with small scale enterprises more likely to supply their products to end users only. Enterprises were also asked how they sell their products, whether directly to consumers, as wholesalers or through brokers.

We argue like Barr (1998) that in production, small enterprises employ relatively labour-intensive technologies and their labour is significantly less educated and experienced. With such indicators, small enterprises have less to gain and more to loose from maintaining large, diverse networks. They are instead likely to build the type of networks that can substitute for formal market-supporting institutions and help them cope with potential information asymmetries. These are relatively small, homogeneous and cohesive solidarity networks. On the other hand, larger enterprises have reasonable access to formal institutions and may have more to gain from large, diverse innovation networks. The enterprise linkages by gender of the owners are presented in table 2.

Table 2: Enterprise network characteristics by gender of enterprise owners

Network Description	Total Sample		Female Owned Enterprises	
	Percentage of Respondents	**Standard deviation**	**Percentage of Respondents**	**Standard deviation**
Institutional Environment				
Enterprises having applied for bank loan or overdraft	34.8	.47702	36.4	.4827
Enterprises having interactions with formal financial institutions	41.6	.49369	45.1	.4991
Enterprises having savings with formal financial institutions	78	.41523	76.5	.4250
Market diversity				
Enterprises supplying end users (final consumers) only	83.5	.68844	85.2	.6851
Networks				
Contacts with other enterprises	73.0	.44475	74.7	.43613
Membership to associations with enterprises in same kind of activity	23.6	.42530	24.1	42886
Membership to associations with enterprises in different kinds of activity	33.2	.47177	35.2	.47903
Membership to informal groupings	53.7	.49939	58	.49505
Number of enterprises	***322***		***162***	

From the results, we see that most (over 75%) female owned enterprises sell their products directly to final consumers, have savings with financial institutions and contacts with other enterprises. Over half also belonged to informal groupings.

3.3. Types of Linkages Among SMEs

Groupings and Interactions Among Enterprises

The key informant interviews revealed that the enterprises have different forms of linkages among themselves. These linkages mainly take the form of associations, welfare groups and SACCOs among the entrepreneurs as well as informal groupings. The main form of linkage that the SMEs were found to have is membership to business groupings. In such groupings, the members make regular contributions to a common fund. The contributions are either used as security to obtain loan from MFIs or to lend to group members on a *'merry-go-round'* basis. People join groups to make contacts that may not be of immediate benefits but which may become useful later, through either formal or informal networks (McCormick et al 2003). The main form of interaction that the SMEs belonged to were found to be business groupings or associations. A total of 73% of the enterprises had relationships with other enterprises either in the same line of business or in different lines of business, while 27% did not have any relationship. Most enterprises therefore interacted with each other. Among the female owned enterprises, 75% had relationships with enterprises either in their line of business or in different business.

Subcontracting

Subcontracting arrangements belong to a broader category of contractual linkages. The typical motives for subcontracting include the lowering of labour costs, reducing risks through lowering of fixed costs, the need to produce specialized products that would be difficult to produce in house, as well as keeping the business small.

Enterprises can either receive or give out subcontracts. More than half of the enterprises did not receive any subcontracts, with only 45.3% of the enterprises receiving any subcontracts. Fear of inability to meet the subcontract targets, inadequate capacity to take subcontracts, inadequate finances to handle subcontracts, difficulty in getting subcontracts, being new in the business, and not being interested in subcontracts were the reasons given for not receiving any subcontracts. Among those which received subcontracts, most received them from firms of the same size in the same business (table 3). They received the least subcontracts from firms of the same size but in different lines of business. Of the female owned enterprises, 43 % received subcontracts. Most female enterprises received subcontracts from same size firms in the same line of business.

Table 3: Characteristics of Sources of Subcontracts by Gender of Enterprise Owner

	Total Sample		Women Owned Enterprises	
Source of Subcontracts	***Frequency***	***Percentage***	***Frequency***	***Percentage***
Same Size same business line	83	25.8	37	22.8
Large firms same business line	20	6.2	9	5.6
Large firms different business line	14	4.3	7	4.3
Smaller firms different business line	13	4	5	3.1
Smaller firms same business line	12	3.7	6	3.7
Same Size different business line	4	1.2	.3	1.9
No subcontract	176	54.7	95	58.6
Total	***322***	***100***	***162***	***100***

Source: computed from survey data

The subcontracts can be categorised into specialised subcontracts, seasonal subcontracts, and subcontracts arising from inadequate capacity. Most firms (18%) received specialized subcontracting, followed by seasonal subcontracting (15.5%), while subcontracts due to inadequate capacity were received by 11.8% of the enterprises.

Most enterprises also did not give subcontracts, with only 47.5% of the enterprises giving out subcontracts. Having adequate capacity was the most common reason (24.2%) for not giving out subcontracts. Others included of not being interested, the need to be independent, and the fear of failure by the subcontracted firms to meet their obligations. For those which gave subcontracts, most of them gave to firms of the same size in the same line of business (table 4). Most enterprises (25.2%) gave out subcontracting due to inadequate capacity. Of those who gave out subcontracts, 30 % gave to those in their line of activity with the same size. 28% of women owned enterprises gave out subcontracts to the same size enterprises in the same line of activity.

The entrepreneurs therefore seem to interact more with firms in the same line of activity and size. This may be a factor limiting the amount of resources that they can pool together if they are resource-constrained. It has been argued that the concentration of African entrepreneurs in the range of SMEs is due to their inability to mobilize financial resources that can enable them to move out of the SME activities (Ikiara et.al, 2002). Of the female owned enterprises, 45% gave out subcontracts.

Table 4: Characteristics of Enterprises Given Subcontracts by Firm Size

	Total Sample		***Women Owned enterprises***	
Firms receiving Subcontracts	***Frequency***	***Percentage***	***Frequency***	***Percentage***
Large firms same business line	6	1.9	5	3.1
Large firms different business line	4	1.2	2	1.2
Same size same business line	98	30.4	46	28.4
Same size different business line	42	13	16	9.9
Smaller firms same business line	3	0.9	3	1.9
Smaller firms different business line	0	0	1	0.6
Not giving out a subcontract	169	52.5	89	54.9
Total	***322***	***100***	***162***	***100***

Source: Computed from survey data

Associations

Business associations have been defined as collective bodies that are intermediaries between individual business action and state action. They are therefore a kind of organisation that may influence the development of individual businesses. Associations perform facilitating roles for the development of networks among SMEs (Bennet 1998). Associations are established for various reasons which affect their effectiveness. While some focus specifically on the business activities of their members, others do not have business as their primary focus (McCormick et al 2003). Although associations provide different types of benefits to their members, from the sample, only 23.6% of the enterprises belonged to any association with enterprises in their line of activity, while 33.2% belonged to associations with enterprises not in the same line of business. Inability to meet the financial requirements by the associations was among the reasons for not belonging to any association. Among the female owned enterprises, 24% belonged to associations with enterprises in their line of activity while 35% belonged to associations with enterprises not in the same line of activity.

Associations among these enterprises were formed to serve various interests of enterprises and therefore existed for different purposes, like the provision of credit to members, helping with welfare matters and business development. Some enterprise owners were found to belong to more than one association where one association did not serve all their needs. The multiplicity of membership to associations can be explained by objectives of forming associations. Associations are mostly formed among members with similar characteristics like, traders in a specific commodity, or even people from the same clan. Such criteria mean that one person can belong to more than one association to satisfy the different needs.

Enterprises were also asked if they belonged to any informal groupings. A total of 53.7% belonged to informal groupings. The types of these groupings included merry go rounds (33.2%), welfare groupings (14%), business groupings as well as church groups and security groups. Such groupings brought different types of benefits to the members like improved business security, sharing of advice, and provision of loans. Key informant interviews revealed that belonging to many associations had both advantages and disadvantages for the enterprises. Among the female owned enterprises, 58% belonged to informal groupings.

3.4 Linkages between MSEs and Financial Institutions

In this section, we present results on linkages between clothing enterprises and financial institutions. One of the constraints often identified with SMEs is lack of finance. Over half (58%) of the respondents indicated that they had no interaction with financial institutions for reasons including high transaction costs associated with services from such institutions, the repayment procedures, and the recovery methods employed by the institutions in case of default. There are different types of linkages between clothing enterprises and financial institutions.

Linkages with Commercial Banks

The main form of interaction between SMEs and commercial banks was found to be through savings by the enterprises. Most traders hold savings accounts with commercial banks. Group savings were also mostly saved with commercial banks. In addition to savings, borrowing is the other main service from financial institutions used by the enterprises. However, only 34.8% reported having ever directly applied for credit. In contrast to the low number that had borrowed any credit, the majority (78%) saved part of their earnings with financial institutions, with 55% saving with commercial banks while others saved with self-help groups, Micro-Finance Institutions (MFIs) and Rotating Savings and Credit Associations (ROSCAs). Small-scale enterprises mobilise savings through commercial banks, but such savings may not come back to them in the form of credit. Only 36% of the female owned enterprises had applied for credit from financial institutions while 76% had savings with the bank.

When the application for credit is considered by membership to networks of association or informal groupings, we notice that most of those entrepreneurs who were members of associations had applied for credit while most of those who were not members to any association did not apply for any credit. Table 5 presents the results.

Table 5: Application for credit by network memberships by gender of Enterprise owners

	Total Sample		Female Owned enterprises	
	Ever applied for loan before	**Never applied for loan before**	**Ever applied for loan before**	**Never applied for loan before**
Belongs to association	55.3	44.7	53.8	46.2
Does not belong to association	28.5	71.5	30.9	69.1
Belong to informal grouping	36.4	63.6	37.2	62.8
Does not belong to informal grouping	32.9	67.1	35.3	64.7
Total	34.8	65.2	36	64

Linkages with MFIs

Microfinance refers to the practice of providing financial services, such as micro-credit, micro-savings or micro-insurance to poor people, by helping them to accumulate larger sums of money, thus expanding their choices and reducing the risks they face. Institutions providing these services are referred to as Micro-Finance Institutions (MFIs). Linkages with MFIs form the major means by which SMEs access financial services. The MFIs have different backgrounds which appear to be related to the nature of services they provide to their clients. These backgrounds are reflected in the reasons for starting their activities. MFIs gave different reasons for starting up, which included addressing the problem of poverty among a specific social categories of traders like widows, or single parents, helping small traders finance their business as a way of alleviating poverty, contribute to managerial, technical, and financial development of the region by enabling people to take advantage of the opportunities in the region. These reasons influence the type of services they provide and therefore their relationship with SMEs. Among the services the offer are the provision of savings and loans to the SMEs through groups, cheque clearance services, offering of training for clients on business management and income generating activities, insurance services and the provision of assets like Heifers.

SMEs interact with MFIs mainly through loans, which are provided mainly through groups. Some SMEs also have relationships with more than one financial institution especially the MFIs. This happens when people belong to different groups and use their membership to access loans from the different MFIs. This has been associated with default problems among the members, and in some cases, collapse of businesses.

Enterprises, which had interactions with financial institutions benefited in various ways. Those who had interacted with financial institutions saw accessing credit for their businesses as one major benefit of such interactions. Other benefits also included business training, secure and accessible savings facility, and cash transfer services.

In addition to direct relationships with financial institutions, some enterprises (61%) also belonged to groups that enabled them access financial resources for their enterprises. These groups include ROSCAs, merry go-rounds, women groups and welfare associations. These kind of groups provide not just financial services, but also other services like health insurance for members, training and assists in welfare matters which might affect their business like deaths. These services indirectly help in the business by enabling entrepreneurs not divert resources from the business. Another notable observation was that some SMEs are pulling out of their relationships with MFIs due to reasons like high transaction costs, short repayment periods, and lack of training.

3.5 Institutional Arrangements and Enterprise Performance

One of the main reasons why firms form linkages is to ultimately improve their performance. Firm performance can be measured using different indicators, like profitability, growth in employment, production level, or even sales. In addition, firms also have their own indicators of measuring their performance (Meyanathan and Munter 1994; McCormick and Atieno 2002; Oketch et al, 2002). All these indicators however have their advantages and disadvantages. Profitability, for example, has the problem that most of the small firms do not keep records, and do not easily share income information. On the other hand, some firms may not grow, but may diversify into other activities as a strategy to minimise their risks. In this study, we use firm performance based on specific indicators, which incorporate both the enterprises' own measures of performance as well as the conventional measures of performance. Following from the literature it is hypothesised that the different forms of linkages have a positive effect on firm performance. Firms involved in more linkages would therefore be expected to experience a better performance than those not involved in any linkages.

In this section, we analyse the performance of the enterprises in relation to the different kinds of linkages that the enterprises have, based on the hypothesis that linkages improve firm performance. We compare selected indicators for enterprises with different types of linkages, against those without.

3.5.1 What has changed

It was noted that while most firms can be said to have expanded in terms of their production and sales, they have not split into different business. Most of those that have grown have mainly specialized in producing products targeting specific customers.

This study used the same indicators used by the entrepreneurs to examine their performance. Looking at changes between start and current, we find that at start, the number of enterprises without temporary employees was 264 (82%), but currently, only 191 (59.3%) had no temporary employees. For permanent employment, whereas 91.6% of the enterprises had o permanent employees at start, 86.6 % have no permanent employees currently. Enterprises also considered the number of branches they had as an indication of their performance. Only 10% of the enterprises reported having one branch at start, but 18% of the sample reported having between one and three branches currently. Most enterprises (98%), covered only one town at start, but currently, this has dropped to 88% covering only one town. This means that only 2% of the traders covered more than one town at start, but 12% cover more than one town currently.

We tested the significance of the differences between the indicators at start and currently. Tables 6 and 7 give a comparison of means for selected performance indicators between start and current period.

Table 6: Comparison of means for performance indicators at start and current period

Indicator	**Mean Values**			**t-values**
	Now	**At start**	**Mean Difference**	
Production volume (units per ay)	88.16 (134.627)	63.62 (85.302)	24.536	3.426***
Temporary employment	2.53 (23.458)	0.366 (1.027)	2.1677	1.659*
Permanent employment	0.28 (.928)	0.15 (.577)	0.127	3.070***
Sales volume (Kshs)	9203 (20524)	3476 (8288)	5726	5.659***
Profit level (Kshs)	2711 (6663)	1232 (2727)	1479	4.444***
Number of branches	0.21 (.464)	0.1 (.304)	0.106	5.787***
Number of towns covered	1.26 (.786)	1.02 (.222)	0.239	5.785***

Note: Figures in parentheses are standard deviations
*** significant at 1%; * significant at 10%

Table 7: Comparison of means for performance indicators at start and current period for women owned enterprises

Indicator	Mean Values			t-values
	Now	At start	Mean Difference	
Production volume (units per ay)	71.8 (95.866)	37.2 (105.662)	14.571	1.544
Temporary employment	3.79 (32.969)	.388 (1.1325)	3.4012	1.312
Permanent employment	.28 (.832)	.12 (.527)	.167	3.352***
Sales volume (Kshs)	9704.6 (22278)	4097.44 (10775)	5607	3.860***
Profit level (Kshs)	2837 (8435.117)	1232 (3079.825)	1592	2.680**
Number of branches	.21 (.435)	.09 (.282)	.099	4.200***
Number of towns covered	1.28 (.552)	1.28 (.248)	.259	4.084***

Note: Figures in parentheses are standard deviations
*** significant at 1%; * significant at 10%

The results from the comparison of the means show that except for temporary employment, there are significant differences in the values of the indicators between start and current period. This can be taken to imply that on average, there has been an improvement in these indicators between the time the enterprises started and the time when the interviews were conducted. On average, enterprises have experienced positive change in most of their indicators. For the women owned enterprises however, production volume and temporary employment have not experienced any change between the time of start and current. The important question is whether these improvements can be linked to the linkages that entrepreneurs have. In the next section, we explore this question.

3.5.2. Linkages and Performance

In this section, an attempt is made to analyse firm performance of women owned enterprises against the different kinds of linkages that the enterprises have. We compare the various indicators of those with different types of linkages, against those without. Table 8 presents the results of differences in the indicators for those having any relationships with enterprises in same line of business versus those without. We see that there is significant difference in current production volume between those who had relationships with other firms and those who did not. The difference between the other indicators were not significant. Membership to associations seems to matter. The difference in the indicators between those that belong to associations and those who do not is significant (Table 9).

From table 10, we see that only differences in current production volume, temporary employment at start and current profit levels are significant between those enterprises which interact with others. For those saving with financial institutions, the difference with those not saving was significant for production volume and profit level.

Table 8: Comparison of selected indicators for women owned enterprises with and without relationships with enterprise in same line

Indicator	Mean Value		t-value
	With relationship (n=121)	Without relationship (n=41)	
Production volume now	94.2	71.83	1.930**
Production volume at start	58.83	76.55	1.660*
Temporary employment now	3	1	1.150
Temporary employment at start	0.5	0	1.643
Sales volume now	9739.91	7753	0.909
Sales volume at start	3296	3963	0.651
Profit level now	2891	2225	1.061
Profit level at start	1190	1345	0.479

** Significant at 5% ; * significant at 10%

Table 9: Comparison of Selected indicators for women owned enterprises belonging to Associations and those not

Indicator	Mean Value		t-value
	In association (n=39)	Not in association (n=123)	
Production volume now	166.58	63.93	3.691***
Production volume at start	87.46	56.25	2.818***
Temporary employment now	8	1	2.375**
Temporary employment at start	1	0	3.127***
Sales volume now	16172.14	7050.35	3.443***
Sales volume at start	4983.00	3010.98	1.819*
Profit level now	5164.87	1953.89	3.746***
Profit level at start	2039.50	983.28	2.987***

*** significant at 1%; ** Significant at 5% ; * significant at 10%

Table 10: Comparison of selected indicators for women owned enterprises interacting with Financial Institutions

Indicator	Mean Value		t-value
	In association (n=73)	Not in association (n=89)	
Production volume now	110.67	72.11	2.556**
Production volume at start	66.87	61.30	0.577
Temporary employment now	5	1	1.538
Temporary employment at start	1	0	1.679*
Sales volume now	10727.65	8116.84	1.126
Sales volume at start	3509.44	3452.90	0.063
Profit level now	3482.65	2162.29	1.758*
Profit level at start	1231.71	1233.19	0.050

** Significant at 5% ; * significant at 10%

Table 11: Comparison of Selected Indicators for women enterprises saving with financial institutions

Indicator	Mean Value		t-value
	Those Saving (n=124)	Those not Saving (n=38)	
Production volume now	96.3	59.4	3.388***
Production volume at start	63.2	65.1	.206
Temporary employment now	3	1	1.558
Temporary employment at start	1	1	1.062
Sales volume now	10,004.6	6,370.7	1.470
Sales volume at start	3,099.4	4,809.2	1.098
Profit level now	3,180.3	1,055.3	4.008***
Profit level at start	1,166.8	1,465.1	.586

*** Significant at 1%; ** Significant at 5%; * Significant at 10%

From the results, we can observe that while some linkages may lead to better performance of the women owned enterprises, some do not. However, the nature of the linkages is also important. Associations seem to matter. As observed in this paper, associations have different objectives. The objectives of associations were to provide credit, help members with welfare issues, and help in business development. Interaction with financial institutions also implies access to external sources of finance. Such linkages are therefore likely to improve enterprise performance than other relationships. Firms with better performance are also more likely to relate to each other or with other firms, than those with poor performance. Membership to associations and interaction with financial institutions in the form of savings are significant in enterprise performance. Associations are formed for different objectives, like the mobilisation of financial resources and the provision of credit to members as well as addressing social welfare issues that affect members' business. This indirectly ensures that financial resources are not diverted from the enterprises, which might affect its performance. Interactions with firms in the same line of business also appear to be more important than those with enterprises in different lines of business.

Interaction with financial institutions implies access to external sources of finance, which increases firm flexibility in resource allocation and the ability to take up emerging investment opportunities as well as to reduce cash flow problems. Entrepreneurs form groups to either directly facilitate access to credit for their business or to address non-business problems that affect their businesses. Most MFIs provide credit to enterprises only through associations or groupings. Such linkages are likely to improve financial flexibility of the enterprises.

The importance of associations as a vehicle for improving SME performance is illustrated by cases where enterprise owners have pulled out of their relationships with MFIs and formed their own their own associations where they collect savings and lend to each other.

4. Summary and Conclusions

This paper was motivated by the increasing importance of the SMEs as a source of employment and income for women, while at the same time facing serious constraints that impede its development. Literature from the NIE show that linkages have the potential to help firms overcome some of their constraints. The paper aimed at analysing the nature of linkages between SMEs and financial institutions and the effect of these linkages on enterprise performance. Primary data, collected through key informant interviews and questionnaire survey in two urban centers of Kenya was used.

The results show that although limited, women owned small scale enterprises have different forms of linkages both among themselves, and with financial institutions. Such linkages include linkages among SMEs, which also help to mobilise and allocate financial resources among the members, subcontracting arrangements, and associations as well as informal groupings. Linkages with financial institutions were mainly with MFIs, while interaction with commercial banks was limited to banking services mainly savings. The results also show that women owned enterprises with membership to associations and those interacting with financial institutions had better performance than those without such networks.

Results from the paper may lead to the conclusion that although the linkages are limited, some linkages have advantages to the enterprises. Enterprises belonging to associations, have better performance indicators than those, which do not. Although the direction of causality between associations and performance is not clear, evidence from other studies (Oketch et al. 2002; Ikiara et al. 20002) may help to support the conclusion here that firms with associations have better performance than those without. This is because associations help their members to access certain services which help them improve their performance, like information, finance and support on social issues that may affect their business performance.

Some conclusions can be drawn from these results. The SME sector is a vibrant sector providing employment both directly to those involved in it, and indirectly trough the creation of other enterprises, which provide them with support services. It is a major employer of the female labour force in the country. Most of such support services are also dominated by women. Addressing the problems that impede the development of SMEs is necessary to ensure the sustainability of the sector. Given the nature of their activity, SMEs may be increasing in numbers, but not improving in performance. Under such circumstances, they are also likely to be vulnerable to shocks like economic crisis, which further affect their potential for employment generation. From the results in this paper, supporting institutions like associations that enable women in the SMEs to overcome some of their constraints is important. Linkages among the enterprises themselves and between them and financial institutions enable them access financial services. Such financial services either contribute to business development directly by injecting external financial resources to the enterprises or by addressing social problems that may affect their financial stability and therefore performance.

Institutions like associations that support SMEs to access financial services that either go to the businesses directly or indirectly are an important avenue for strengthening them. The Sessional Paper Number Two of 2005 on the Development of Micro and Small Scale Enterprises for Wealth and Employment Creation for Poverty Reduction, recognises the need for incentives for investments that enhance the development of linkages between SMEs and large enterprises. This should be moved to the level of implementation. The proposed establishment of the Micro Finance Trust Fund from which MFIs can withdraw for on lending to the SEs is an important way of increasing their capacity, while at the same time providing a regulatory framework which can guide MFI activities. The enactment of the microfinance bill is important in this regard.

The results from this study have shown that although limited, the small scale enterprises have different forms of networks among themselves and linkages with financial institutions. Some of these linkages have advantages, which are reflected in the firms' performance. One policy recommendation that can be drawn here is that there is need for the government to strengthen the institutional networks among SMEs, which enable them access resources as a way of overcoming some of their constraints.

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