FINANCIAL LITERACY ON FINANCIAL PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES IN KAJIADO COUNTY, KENYA

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ABSTRACT

The purpose of the study was to examine and determine the efficacy of financial literacy on SMEs in Kajiado town. A descriptive research design was adopted. Specific objectives of the study were to examine budgeting literacy, bookkeeping literacy and savings literacy on financial performance of SMEs in Kajiado county. A business entity may be known to have ascertained growth or declined if its financial performance is known. In determining this, the study focused on business profit and business growth. Using financial literacy theory, transaction cost theory and resource-based theory, the study evaluated the factors that affect different levels of financial literacy and assessing the impact it had on both the long-life and success of the aforementioned businesses. In doing so, it related the previous studies that had identified the phenomenon in developing markets and made a case for the continued improvement of financial literacy as a policy tool to achieve economic growth. The target population was 46,100 registered and licensed SMEs as was indicated in the recent published Kajiado County Integrated Development Plan, 2018 -2022. The study used simple random sampling procedure from a sample size of 399 SMEs which were operating businesses in Kajiado County. The study survey employed primary data source to obtain information, where the main study instrument to collect the data was questionnaire comprising of questions each addressing study objectives. Descriptive analysis was adopted to provide statistics in percentages. The collected data was analyzed and presented in the form of tables and charts. In addition, inferential statistics involved Pearson correlations regression analyses were applied. The study found that financial literacy level is still quite low amongst the SMEs in Kajiado County. The study further found that Budgeting and Bookkeeping were still a major challenge amongst the respondents and savings had insignificant effect on their financial performance.

***Key Words**: Budgeting Literacy, Bookkeeping Literacy, Savings Literacy, Financial Performance*

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INTRODUCTION

According to the World Bank report (2017), SME sector has been considered as the key driver of an economy globally and which has created a range of economic benefits, including innovation and high productivity that are desirable for any society in the world. It is therefore for this reason that many countries around the world have adopted different approaches in finding ways and means of improving financial literacy amongst their citizens, and priority have been to those who have already been in the business and to some extent this has been luring prospective business people as they develop relevant strategies to educate or give financial education to them (Atkinson, 2011).

In Canada, Wise (2013) pointed out that a large group of business ventures have collapsed as a result of lack of or low level of business management skills amongst many people who have gotten into business. In Sri Lanka, Menike (2018), argued that because of inadequate business management skills amongst SMEs, their businesses have performed dismally. Agyapong and Attram (2019), further gave an account of a number of SMEs which have been experiencing diminishing business growth, sales, and eventually collapsed in their early years in business.

In Uganda, Arinda (2019), in his study mentioned that financial performance of SMEs has not been impressive due to lack of proficiency of financial management. In Kenya, Chepngetich (2019), after carrying out a study on business results of SMEs, in Uasin Ghisu county, concluded the business performance was largely influenced by bookkeeping and budgeting literacy. Abongo (2017), had a view that financial performance of most of the SMEs was affected by budgeting process because many of them were neither having knowledge in business forecasting in terms of targeted income results nor had expenditure forecast in place for their businesses. Cherugong (2015), was of the view that the need for financial literacy has continually become a matter of interest in many nations because of ever changing economic environment circumstances.

According to the OECD report (2011), gave the definition of financial literacy as the business skill and knowledge which are deemed to be necessary to help an individual or a firm make good judgement on financial matters. Even though financial literacy does not ultimately guarantee one's success in business engagements, it is considered a contributor for enabling an individual to respond effectively to the changing social and economic situations (Chamwada, 2015). Financial literacy is therefore an essential element in putting an individual at an advantage level to run a successful enterprise or to operate an efficient and effective business venture in the dynamic business environment (Mapepeta, 2018). By acquiring good financial knowledge, a person would have increased confidence in handling business activities to achieve better financial performance as compared to when one has not gained necessary financial skill or having low level of financial literacy.

Statement of the Problem

With the recognition of the role played by SMEs in a number of nations, which has been of necessity not by choice, socio-economic needs in the society around the world (Ibrahim,2017). He further argued that the SME sector adds value in many ways, such as creation of jobs, improvement of income, strengthening purchasing power among others. However, despite the clear importance this sector plays, nearly sixty per cent of these businesses in Kenya are estimated to collapse each year (KNBS, 2017). Wanjohi (2011), and Capital Market Authority report (2010), mentioned that lack of adequate enterprising and business skills has been considered as a setback to the business enhancement in this sector. The Capital Market Authority report (2010), further explained that this is mainly attributed to low levels of financial literacy as a result of lack of adequate financial education.

More often than not, businesses are established with the aim of maximizing their profits which eventually ending up in improving their returns to equity invested into the business. It would therefore be unbiased to believe that the intention of every small and medium-sized businesses exist with the purpose of growing in their net-worths. Despite this notion, a number of factors may play key in influencing business financial performance, and this includes financial literacy. In a business point of view, financial literacy might be looked at from different ways, but this study will be focusing on a mix of financial budgeting, financial records keeping, and savings amongst other factors that an individual or a firm could use to improve a business financial performance.

Many academic researchers have highlighted the essence of acquiring business skills in view business performances of SME sector but have not exhaustively brought out clearly that lack of financial literacy could be a hindrance to business growth and may cause collapse of a number of SMEs (Niwaha, *et al,* 2016). Arinda (2019), in examining the business results of SMEs in Ntungamo municipality, and the outcome was that business skills and saving practice were yet to be studied. In addition, Osinde, *et al* (2013), pointed out that the owner-managers were mainly focused on training.

Objective of the Study

The general objective of the study was to examine effect of financial literacy on financial performance of SMEs in Kajiado county. The specific objectives were;

- To determine effect of budgeting literacy on financial performance of SMEs in Kajiado county.
- To examine effect of financial records keeping literacy on financial performance of SMEs in Kajiado county.
- To determine effect of savings literacy on financial performance of SMEs in Kajiado county.

The study sought to answer the following research questions**:**

- Was there effect of budgeting literacy on financial performance of SMEs in Kajiado county?
- Was there effect of bookkeeping literacy on financial performance of SMEs in Kajiado county?
- Was there effect of savings literacy on financial performance of SMEs in Kajiado county?

LIETRATURE REVIEW

Theoretical Framework

SMEs are majorly considered to be playing a critical role in an economy, and because of their importance, a large number of researchers have been inspired to carry out studies to contribute greater knowledge of the financial literacy on financial performance in the sector of SMEs businesses. Due to this fact, many theories have emerged from different authors or have been written by different scholars in an attempt to explain any relationship which could exist in view of financial literacy and financial performance of a business. The research study will be introducing various theories relevant to the study in an effort to support this relationship. The study will look at financial literacy theory, transaction cost theory, and resource-based theory.

Financial Literacy Theory

The financial literacy theory explains that a decision an individual or firm will be making on financial management, will be playing a key role to the future performance of the firm. The theory further gives a view point that behavior is either driven by what one feels to be true even without conscious reasoning (Evans 2008).

Financial literacy empowers individuals doing business or one who intends to do business with useful financial knowledge that matters for making sound financial decisions that best fulfills an individual's personal or business goals. This theory will therefore be helpful in assessing how the business operators do come up with the decisions they do make in terms of business activities forecast, and also understanding what drives them to make those decisions in their business operations.

Transaction Cost Theory

This theory was written by Williamson (1981), which explains that business financial transactions involve costs, which in essence, reflect the cost of the business entity incurred within or outside the enterprise. The author is forwarding an argument that a transaction cost will automatically reflect the

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cost of a business activity regardless of whether it is within or outside of the business. Rindfleisch (2020), argued that it is through a transaction cost that an enterprise can measure how efficient its business operations has been in comparison to its planned business activities. Therefore, in order for a firm to manage the transaction costs effectively, one needs to acquire financial management skill.

Using this theory, lack of or low financial skills may cause an avoidable increase in transactions costs, which in turn could influence financial performance negatively. It is the needed financial management skills which would enable the business operator or the firm to identify transactions that are likely to improve or decrease financial performance of the firm. Getting acquainted with the theory, an individual or business operator is tasked with the responsibility of managing a business will strive to avoid unproductive activities, and also to be keeping proper books of accounts, through which accurate business affairs in the final analysis could be ascertained (Rindfleisch, 2020).

Resource-Based Theory

The theory was written and presented by Barney (1995), and it suggests that an enterprise is compromised of assets and resources, which when utilized in an efficient manner will strengthen its capability of keeping the enterprise in a going concern. What the theory is advocating is that, if a business entity acquires financial resources and manages them efficiently, it is highly likely that the firm is going to gain competitive advantage over others in similar business or will be achieving high financial perforamnce (Barney, 1991). The author of the theory further gave reasons why there occurs successful and struglling firms, by saying that the difference happens as a result of how they deploy and utilize their resources in the business.

Empirical Review

Financial Budgeting and Financial Performance

Asakania (2016) presented outcome of the study on budgeting and record keeping skills on business performance. The result of the study was that there existed relationship between financial literacy and financial performance of the business entities studied. The study recommended that both governmental agencies and NGOs should be exploring ways on how they could be facilitating training for the SMEs operators with the aim of equipping them with appropriate and relevant financial management skills to improve their efficiency in managing their business activities.

Arinda (2019), studied the relationship between financial literacy and financial performance of SMEs in Ntungamo municipality in Uganda. The study focused on three objectives namely effect of debt management, bookkeeping and budgeting. The outcome from the study mentioned there was a positive correlation between bookkeeping and debt management and therefore highly predicting results of their businesses.

Bookkeeping and Financial Performance

Mwaniki (2019) studied financial literacy on the expansion Small and Medium Enterprises in Nyeri County, focusing on examining on the effect bookkeeping and budgeting skills on the business expansion or growth of small and medium enterprises in the area. The survey study mentioned that bookkeeping skill had remarkable effect on the expansion or growth of these businesses. The study further presented that bookkeeping had made it easier for the business operators to know when their business obligations were due.

Mapepeta (2018), investigated bookkeeping literacy amongst the SMEs and how this could be applicable in measuring profitability of these busnesses. The result of the research study mentioned that even though these businesses were viably operating businesses, there weren't sufficient or proper financial records keeping to measure their profitability. The study further mentioned that there were other market players who sometime take advantage of the absence of financial record keeping to dwarf their business growth aspirations. The study in its conclusion stated that if financial literacy could be acquired and good business activities records are kept, the measurement of financial performance would be beneficial to key stakeholders of this business information. For example, governmental regulatory agencies would use financial information available from the business operators to use in their forecast on revenues attainable from the sector.

Savings and Financial Performance

Mutiso and Muigai (2018), gave an account from their study on financial literacy and performance of the business groups which received financial grants or were given money for their businesses in Kirinyaga County. Using financial literacy theory, the study randomly selected eighty-eight businesses to find out the financial literacy level and its effect on the business performance of the small and medium enterprises in the county. The result of the survey was that there was a positive correlation between financial literacy and the financial performance amongst these businesses. The study outcome mentioned that the business proprietors had good business skills and knowledge of business operations in terms of savings and bookkeeping because of the skills they had acquired from the previous trainings from the local government initiatives, thus showing good business performance.

Chepkemoi, *et al*. (2017) studied the effect of the acquisition of business skill with aim of understanding business profitability, in Kwale County, Kenya. The sampled population included those business people who had attended business skills training in the previous sessions offered by the World Bank through the initiative of county strategic development plan. The findings showed that the previous training conducted to improve business skills had some good impact on financial performance of small and medium enterprises which immensely contributed to their businesses profitability.

Conceptual framework

Conceptual framework is a pictorial expression that shows an interaction between the study variables in a diagrammatic manner. Dependent variable in the study was financial performance focused on profit of small and medium enterprises, and the independent variable was financial literacy which focused on financial budgeting, bookkeeping and savings.

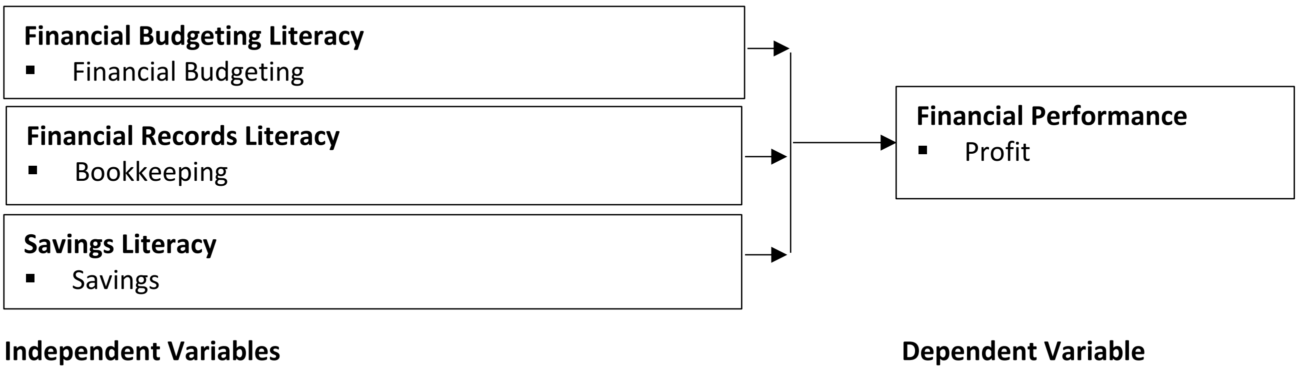

Figure 1: Conceptual Framework

METHODOLOGY

A descriptive research design was adopted**.** The target population in this study consisted of 46,100 licensed traders as indicated in the latest published strategic development plan of Kajiado County for the highlighted period between 2018 and 2022. The study will adopt simple random sampling procedure. A sample size of 397 SMEs was to be considered for the survey study and the sample size was going to be split between small and medium-sized businesses operating within Kajiado county. The study used questionnaires to collect data. Before embarking on analyzing the responses collected, the completed questionnaires was reviewed to make sure that they're all complete and accurate. Simple linear regression was applied to analyze the data to establish the relationship of the variables. Descriptive analysis was employed to come up with

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statistical information to use in making conclusions and recommendations. The reason for carrying outa pilot study was to identify any errors that could be noticed in the questionnaire and correct them before embarking on the full exercise of collecting data.

RESULTS

Gender of Respondents

The respondents were asked to indicate their gender, and the findings were that 244 (61.16%) of the respondents were male and the remaining were 155 (38.84%) were female. The findings above to a great extent indicated small and medium enterprises existing in this field study area were dominated by male compared to female. However, there is no clear reason as to why such discrepancy exists because the study was mainly focused on financial literacy in relation to financial performance for these types of businesses. The response was got by the interviewers ticking the gender on the questionnaire if either male or female when doing the interview.

Table 1: Period in Business of the SMEs

Period in Business of the SMEs	Frequency	Percentage
Less than 2 years	178	44.62%
1 – 4 years	127	31.83%
5 years and above	94	23.55%
	399	100%

The study wanted to establish how long the SMEs had been in operation since their establishment. The responses from the study found out that 178 SMEs (44.62%) had been in operation less than 2 years, 127 SMEs (31.83%) had been in business between 2 and 4 years, and 94 SMEs (23.55%) had been in business for 5 years and above. This implies that majority of the SMEs were in the early of their businesses but as they remain in the business longer fewer were in businesses. This may be attributed to experiencing difficulty in business operations.

Number of Employees in the SMEs

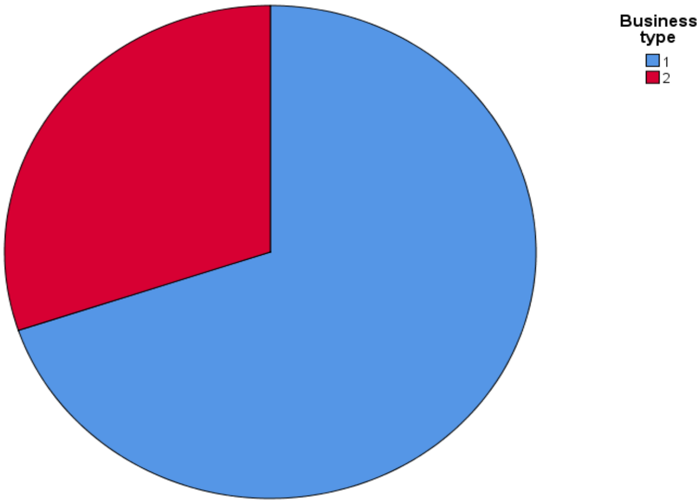
The study findings as shown by table 2. indicates that 161 (40.35%) SMEs had less than 5 employees, 118 (29.57%) SMEs had between 6 and 10 employees, and 120 (30.08%) SMEs had 11 employees and above. This implies that the majority of the respondents in the field study area were small-sized enterprises as shown the figure 2 below.

Table 2: Number of Employees in the SMEs

Number of Employees	Frequency	Percentage
Below 5 employees	161	40.35%
6 – 10 employees	118	29.57%
11 and above employees	120	30.08%
Total	399	100%

Business Types – Small and Medium Enterprises

Figure 2: Business Types – Small and Medium Enterprises



1. **Small-sized enterprises**
2. **Medium-sized enterprises**

The data in the figure 2. above shows that small businesses that operate in Kajiado county have a higher number compared to medium businesses. The study findings indicated by figure 2, 69.92% of them were small enterprises while 30.08% represented medium enterprises. A sample size of 399 SMEs was surveyed in the study and the respondents were randomly selected from the target population between small and medium-sized businesses operating within Kajiado county. The study intended to sample the respondents from the two different types of businesses equally, that is, small and medium enterprises picked on equal basis at random. That meant the small-sized businesses was account for 198 and the medium-sized businesses were to be equally the same number, but in reality the small-sized businesses took a larger portion due to the fact they were the larger number of the enterprises in the studied field area.

Respondents Financial Literacy

Many of the respondents, 257 (64.42%) had a score of between 1-3 and 142 (35.58%) of the respondents had a score of between 3 – 5. This implied that a large number of the respondents had low financial literacy.

Table 3: Respondents Financial Literacy

Financial Literacy Score	Frequency	Percentage
1 - 3	257	64.42%
3 - 5	142	35.58%
	399	100%

Respondents Financial Performance

Several factors can determine the profit of a business gained from its business activities. From the respondents of 399 in the study, SMEs financial performance was measured by the business profit, comparing previous year profit with current year profit. Table 4 below shows many of the respondents, 205 (51.38%), had a reported profit of between 1% and 5%, a number of respondents mentioned that they were not sure whether they made a profit or not 141 (35.34%), 53 (13.28%) of the respondents made a profit of above 5%. This implies that the majority of the respondents either had no skill on financial literacy or the respondents did not understand why the need calculate their financial performance.

Table 4: SMEs Financial Performance

Financial Performance (Profit)	Frequency	Percent
Not Sure	141	35.34%
Between 1% and 5%	205	51.38%
Above 5%	53	13.28%
Total	399	100%

Financial Literacy and Financial Performance

A simple linear regression analysis was done on the dependent and independent variables to determine correlation coefficient between financial literacy: budgeting, bookkeeping and savings, and financial performance: profit. The table 5: below shows correlation coefficient of 0.7818 indicating a strong positive relationship between financial literacy and financial performance which implies that it is highly likely any variation in independent variables, either by increasing or decreasing, explain up to correlation coefficient of 0.7818 or 78.18% of variations in the financial performance of these businesses.

Table 5: Model Summary: Financial Literacy and Financial Performance

R	R Square
0.8842	**0.7818**

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

Summary

Budgeting on Financial Performance**,** from the findings, the study found out that budgeting was important to many business people in the county with 45.11% agreed to be aware of it its importance but had low knowledge of budgeting process. The study also established that among the business people interviewed agreed to be aware that there is process for budgeting but admitted they had no training.

Bookkeeping on Financial Performance, from the study findings, it was found that majority of the respondents (43.9%) had strongly agreed that keeping of proper financial records is important but they had no bookkeeping skill to maintain their business financial transactions records. This indicates that many of the respondents were not keeping their business financial records and not sure on how their businesses had performed.

Savings on Financial Performance, findings from the study, a large number of the respondents, 47.62%, agreed to have knowledge to the reasons why they need to save part of business profit but were not saving all their business surplus and the smallest percentage of 2.51% who did not know they should do so.

Conclusions

The study showed that financial performance has myriads factors contributed to its achievement but having good knowledge of budgeting, proper keeping of financial records skill and having knowledge why one should be saving part of the business surplus will be a milestone in enhancing business financial performance. While many business operators may view acquiring these skills as a second-thought in the business operation, these are universally recognizable a strategic step for a business to continue operating and to a greater extent become a strategic action for any business venture to counter any threat to business going concern.

The study therefore concluded that there is a strong relationship between financial literacy and financial performance of small and medium enterprises. Gaining business skills in bookkeeping, good knowledge of budgeting and also having understanding of the benefits of savings enhances greater chance of achieving high financial performance.

Recommendations

Budgeting is a business skill of knowing how to forecast for income and expenditure of the business operational activities. It is a skill helpful in understanding where funds for running a business are coming from. Therefore, the research study recommends that the business owners or operators should strive to acquire basic skill on budgeting so as to avoid failing to get sufficient income to keep an enterprise on a going concern. Further still, the study recommends that the county government needs to get more involved in empowering both potential and the existing business operators through trainings in business skills or organizing forums or workshops for creating awareness of the importance of such skills within their local regions for the purpose of improving the management of the business activities in a sustainable manner which in return will generate more revenues for the growth of the overall economy.

The study recommended that relevant department in the county government in charge of building capacities of the existing business operators be involved in rolling out training to empower or equip them so as to improve their business' performance capabilities in terms of understanding the benefits of bookkeeping functions. Additionally, creating a learning and development environment for business people will boost or promotes high level of self-reliance of the economy of the country.

The study recommends that business people need to be educated on why they need to save and where to save the extra money they get from the business operations and also know the benefits it brings to business continuity.

Implication of the Research Study on Financial Literacy

The analysis done on the variables under the study have clearly indicated that consideration needs to be taken in order to achieve good financial performance. This is indicative of the business owners or managers putting more efforts in the development of skills in financial literacy in terms of budgeting literacy, bookkeeping literacy and savings in order to enhance confidence of the business operators in this field and improve their financial performance.

Recommendations for Further Studies

The study recommends another study should be conducted find out the reason why there is high discrepancy of the percentage between the number of male and female who are involved in these businesses in the county.

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