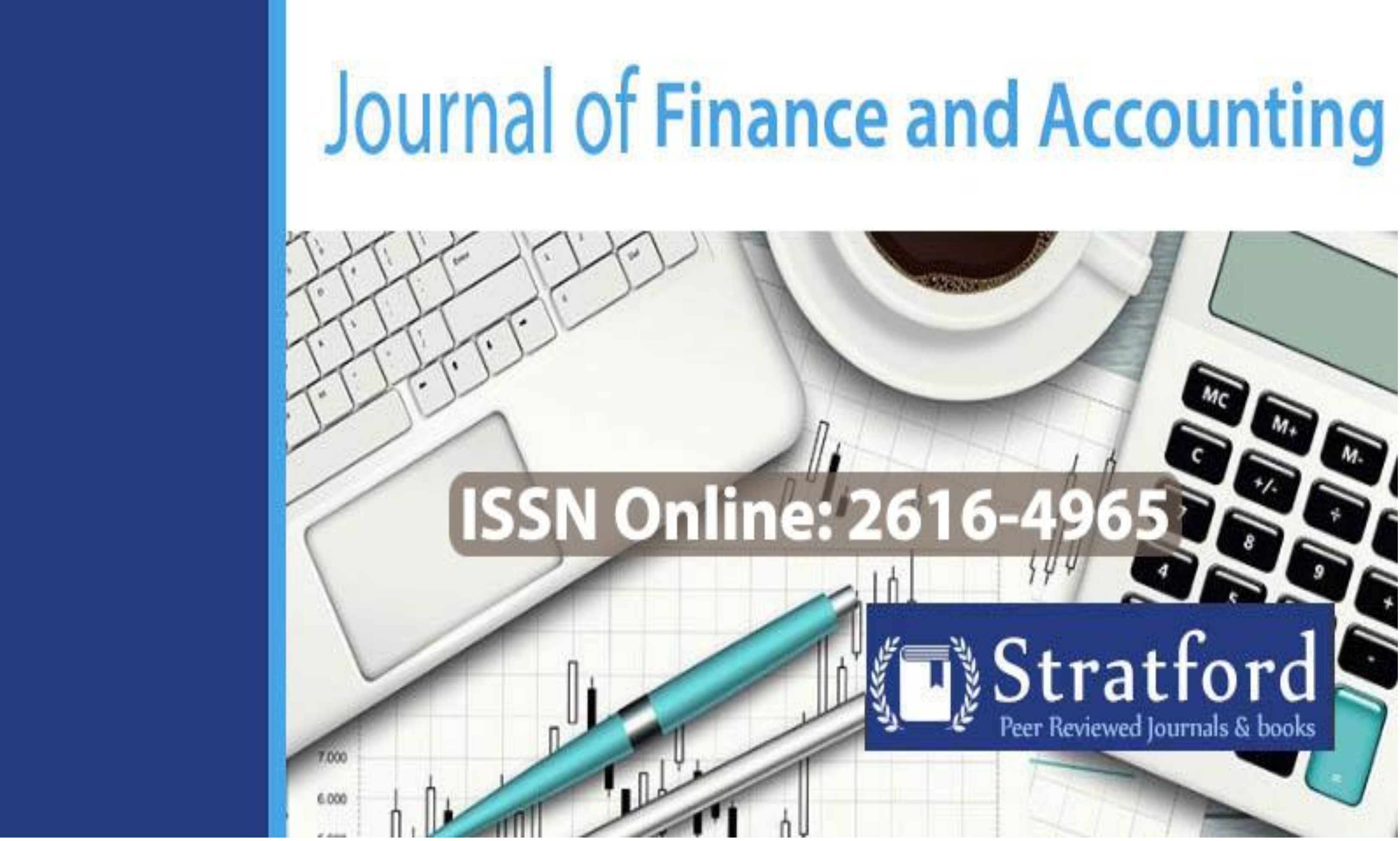


Entrepreneurial Finance and Performance of Small and Medium Sized Enterprises in Kiambu County, Kenya

Irene Wairimu Mwangi, Samson Nyangau &Yusuf Mchelule

ISSN: 2616-8421

Stratford Peer Reviewed Journals and Book Publishing
Journal of Finance and Accounting
Volume 8||Issue 4||Page 1-18 ||April||2024|
Email: info@stratfordjournals.org ISSN: 2616-4965

Entrepreneurial Finance and Performance of Small and Medium Sized Enterprises in Kiambu County, Kenya

***Irene Wairimu Mwangi[1], Samson Nyangau[2] &Yusuf Mchelule[3]**

[1]Student, Jomo Kenyatta University of Agriculture and Technology

[2,3]Department of Economics Accounting and Finance, Jomo Kenyatta University of Agriculture and Technology
***Corresponding authors Email: irenemwas100@gmail.com**

***How to cite this article*: Mwangi I., R., Nyangau S., & Mchelule Y. (2024). Entrepreneurial Finance and Performance of Small and Medium Sized Enterprises in Kiambu County, Kenya. *Journal of Finance and Accounting. Vol* 8(4) pp. 1-18 https://doi.org/10.53819/81018102t2374**

Abstract

Small and Medium Enterprises have contributed greatly to the Kenyan economy. They account for over 90% of all businesses in the country and provide employment opportunities to the majority of the population. Access to finance is a critical determinant to the success and growth of small and medium enterprises. The objective of this study is to assess the effect of access to entrepreneurial finance on the growth of Small and Medium sized Enterprises in Kiambu, Kenya. The target population is the 889 registered Small and Medium sized Enterprises in Kiambu County. The theories looked at in this study are Compensatory Theory of Profits, Traditional Theory of Capital Structures, Pecking Order Theory and Liquidity Preference Theory. The research used the descriptive design and concentrated on registered SMEs in Kiambu County due to their concentration thus a good representation. The target population for this study constitutes of the 889 SMEs in Kiambu County as registered in the Kiambu Business Directory. Using the Yamane sample size formula, a sample size of 276 businesses were selected to represent the target population. Thus, 276 questionnaires were administered out of which 214 were dully filled and returned representing a response rate of 77.5 percent. Data was analyzed using SPSS version 23. It involved both descriptive and inferential statistics and it was presented using pie charts, tables, graphs, and figures. From the analysis results, the correlation between angel financing and performance of SMEs was positive and statistically significant (0.544, 0.000<0.05). The coefficient of angel financing was positive (0.188) and statistically significant (0.001<0.05). The outcomes of correlation between venture capital and performance of SMEs was also positive and significant (0.535, 0.000<0.05). The coefficient of venture capital was positive (0.218) and statistically significant (0.000<0.05). The study concluded that angel financing positively and significantly affects the performance of SMEs. Venture capital is a positive and significant determinant of the performance of SMEs. Own funding by the SMEs also contributes positively and significantly to the performance of SMEs. The study recommended that before the inception of SMEs, the founders ought to look for adequate capital necessary for efficient running of the

operations of the enterprise as well as a capital that enables the purchase of adequate stock. This can be done through conjunction between venture capitalist, SMEs through Micro and Small Enterprises Authority and the ministry of Cooperatives and Micro and Small Enterprise to develop a funding framework for SMEs anchored on venture capital and angel financing.

Keywords: *Entrepreneurial Finance, Performance, SMEs, Kiambu County*

1. Introduction

Many countries globally consider small and medium sized enterprises as the backbone of their economies (Ooi & Richardson, 2019). These enterprises are responsible for the industrialization of many economies as they play a leading role in increasing the number of national industries (Lee & Persson, 2016). As a result, many governments have focused on the development of the Micro and small enterprises (SME) sector in order to accelerate economic growth (Pedraza, 2021). Micro and small enterprises (SMEs) are widely recognized as a major source of employment and income in developing countries (OECD, 2017) contributing towards economic growth and poverty reduction.

Small and medium sized enterprises operate in difficult business environments characterized by globalization and internationalization of markets creating the critical need for SMEs to enhance efficiency, effectiveness and competitiveness based on innovation in order to survive (Fadil & St-Pierre, 2021). SMEs have faced many barriers preventing their survival and growth and hindering their potential (Naradda Gamage et al., 2020). One of the greatest challenges identified that largely determine the growth and survival of SMEs is the level of access to various forms of financing and the costs involved in obtaining such funds where available (Berger & Udell, 2016).

Various forms of entrepreneurial finance and their accessibility has stirred the attention of academicians and policy makers worldwide for many decades (Beck et al., 2016). This is because finance is a significant element for determining the growth and survival of SMEs (ACCA, 2019). Access to finance is the most serious barrier to the expansion of SMEs (Eyiah et al., 2018). This study therefore seeks to determine the influence of various forms of entrepreneurial finance on the growth of SMEs in Kiambu County, Kenya.

In the U.S.A, SMEs with fewer than 500 employees are the backbone of U.S. economy. They make up 99 percent of all firms, employ over 50 percent of private sector employees, and generate 65 percent of net new private sector jobs. SMEs account for over half of U.S. non-farm GDP and represent 98 percent of all U.S. exporters and 34 percent of U.S. export revenue (Aseem & Kati, 2015). Indeed, financing is widely found to be the single most robust determinant of firm growth in the U.S.

In the United Kingdom, access to finance for small and medium enterprises (SMEs) is key to the recovery and long-term growth of the UK economy. The principal providers of external finance are the major UK banks. Accordingly, the financial crisis was bound to have an impact on SME finance through the failure and partial nationalization of banks, higher bank funding costs and the subsequent recession (Armstrong, 2013).

In Japan SMEs account for 99.7% of all companies, 70% of all employees, and more than 50% of all added value (manufacturing industry), SMEs form the very basis of the Japanese economy (Ministry of Economy, Trade and Industry, 2022). As SMEs have few assets and weak financial foundations, it is difficult for them to procure capital from the stock market. Accordingly, government-affiliated financial institutions have been established to create a system to provide

Stratford Peer Reviewed Journals and Book Publishing
Journal of Finance and Accounting
Volume 8||Issue 4||Page 1-18 ||April||2024|
Email: info@stratfordjournals.org ISSN: 2616-4965

SMEs with long-term funds at low rates of interest (Ministry of Economy, Trade and Industry, 2013). The average SMEs gets over 50% of their capital in the form of loans from financial institution (Hong et al., 2020). In 2001, firms with less than 20 employees received 66.9% of their capital from loans by financial institutions whereas firms with more than 300 employees received just 24.2% of their capital from such loans. Therefore, SMEs globally heavily relay on bank lending (OECD, 2017).

A crucial problem identified with entrepreneurial financing in African countries including Nigeria by the World Bank (2019) is the low level of financing of entrepreneurial ventures which is on average a miserly 2.3% of the overall total credit disbursed to the private sectors. This trend was repeated in subsequent years and has hampered the level at which the entrepreneurs in Africa have contributed towards employment levels and production which are relatively low in Africa (Quartey et al., 2017). Most African countries such as Nigeria, Ivory Coast, Mali, Uganda, Tanzania, Rwanda Zambia, and South Africa have all experienced this scarcity of funding due to lack of loan collateral security and current macroeconomic anomalies such as galloping inflation rates, high bank interest rates, sky rocketing poverty levels and the high rate of closure of business firms usually within five years of operation as observed by Kauffmann (2005). High interest rates on bank loans advanced to SMEs are a factor of the high risk associated with the survival of SMEs in Africa (Nanziri & Wamalwa, 2021). This high cost of commercial loans and the barriers that exist to access greatly reduce the number small number of small and medium sized enterprises that benefit from this form of financing (Godke et al., 2019).

External financial support received by a firm when it is small and at an early stage immediately after formation is called angel financing while financial support obtained when the firm is more structured and established is called venture capital financing (Wong, Bhatia & Freeman, 2009). In developing African countries which have less market-supportive institutions and have notable formal institutional voids, the concepts of angel investment and venture capital financing is quite distinct because it indigenously borrows from the culture that people are used to (Olarewaju et al., 2023).

In addressing the SME Financing Gap in Kenya, banks have been on the receiving end. A report by Kenya Bankers Association (2016) established that there seems to be two schools of thought surrounding the issue of banks and SME finance. The first school of thought believes that banks have played a big role in providing access to financial services to SMEs. The report indicated that there was a 35% growth of bank lending to SMEs, 95% of banks had at least a product tailored for SMEs and that banks were able to provide lending to SMEs in different sectors of the economy despite the risks involved with some of the sectors. The second school of thought argues that while banks have put an effort to serve SMEs, these efforts are not properly suited for SMEs for various reasons (Kashangaki, 2014).

Kenya has an organization called Kenya Investment Network, which is an angel investment platform where founders can pitch their projects and state their funding requirements in order to find angel investors (Kenya National Bureau of Statistics, 2007). Angel investors in Kenya are wealthy individuals who provide innovative startups with the initial capital to set up the businesses and get involved in the establishment and growth of the startups. Post funding involvement has proved to increase the startups' chances of success as they benefit greatly from the business expertise and business networks of the angel investors (Aseem & Kati, 2015).

Venture capitalists in Kenya provide long-term capital to new and expanding businesses which are usually high risk but offer the potential for above-average returns (Mwasi & Aluoch, 2023). Similar to other parts of the world, venture capitalists pool their resources including managerial abilities to assist new entrepreneurs in the early years of their businesses. In recent years, annual venture capital invested in Kenya has surpassed $1 billion (Mwasi & Aluoch, 2023).

Small and Medium Enterprises have contributed greatly to the Kenyan economy. Their influence is felt in all sectors of the economy, and they provide many employment opportunities and generate widespread economic benefits. Although the small Medium and Micro businesses sector in Kenya has experienced been experiencing rapid growth over the last few decades, it has been noted that this rapid growth has not been experienced by the individual enterprises (Muhuhu et al., 2023). This underdevelopment has been attributed to the micro and small enterprises' inability to grow and mature to become medium sized business enterprises. The other factor that hinders this growth are strong barriers to direct entry into the medium-scale business sector.

Records and statistics clearly show that although there is a high business birth rate in Kenya, the stagnation and rapid death of these business enterprises is equally high (Rigito, 2010). While the informal sector contributes over 80% of all employment opportunities in Kenya, it only contribution to the GDP is estimated at 40.2% (Bartocho, 2022). At the global level Small and Medium Enterprises (SMEs) account for 90% of business enterprises and are critical in employment creation, production of output for final consumption and input for further production resulting in economic growth (Omondi, Onono & Barasa, 2022). Despite their critical role in economic growth, millions of SMEs go bankrupt every year (Bunyasi, Bwisa, Namusonge, 2014). This has in turn led to the stagnation in growth of SMEs and therefore most of them do not evolve into medium sized enterprises which are key in the industrialization process and development of national economies (Arzu and Emine, 2018).

Kiambu County is well endowed with SMEs with many of them being unregistered. According to the Kiambu Business Directory, Kiambu County has 889 registered SMEs (2018). Previous studies have shown that apart from the registered ones, the county has probably another 1,400 unregistered SMEs (Mbugua, 2016). For the purpose of this study, we shall focus on the registered SMEs only. Limited access to entrepreneurial finance is a major factor inhibiting entrepreneurship and negatively impacting growth of SMEs and impedes the progress and growth that comes from timely application of resources (Ramukumba, 2014). Based on this, the study sought to;

1. To determine the influence of angel financing in the performance of SMEs in Kiambu County, Kenya
2. To establish the influence of venture capital financing in the performance of SMEs in Kiambu County, Kenya

Angel financing is one of the most common, but least studied methods of financing new business ventures (Edelman et al., 2017). Angel investors are important to entrepreneurs with small and medium sized enterprises because they provide more than money (Samsami et al., 2022). They are hands on investors who in addition to finances contribute their expertise, skills, knowledge, and networks in the businesses they invest in. They are wealthy individuals with great business expertise.

Although Angel investors are exposed to greater uncertainty by investing earlier in the life of a firm compared to venture capital, they do not rely on traditional control mechanisms such as board control, staging, or contractual provisions to protect against expropriation. Instead, Angels reduce expected agency costs by forcing entrepreneurs to hold a larger stake in the firm, thereby aligning the interests of the entrepreneur with the outcome of the business enterprise (Lo, 2016). In addition, angel investors use more informal methods such as investing in close geographical proximity and syndicating investments with fellow angels to mitigate risks (Edelman, 2012).

Financing is a very critical issue for the survival and development of small and medium sized enterprises (SMEs). Angel Investors play a key role in financing small and medium sized enterprises, especially those which are innovative and have a high growth potential (Bonini & Awuni, 2023). SMEs in their development pass through several stages. These stages are Seed stage: This is where the entrepreneur has an idea or concept for potential profitable business, Start-up stage: the idea has now been developed to the level which allows commercialization preparations, Early stage: in this stage production and distribution of a specific product or service takes place, and lastly Later stage where the enterprise matures and becomes profitable (Lo, 2016). Angel investors prefer to invest in business enterprises which are in the start-up or early stages where their money and expertise is needed the most before they exit the market (Scoreboard, 2019).

Much research conducted in the past confirm that angel investors play an important and vital role in entrepreneurship by financing small and medium sized enterprises. The amounts they invest are significant and the expertise and networks they bring to the businesses in post funding involvement makes them more attractive to entrepreneurs as a source of finance in comparison to other sources of capital (Sohl, 2016).

Venture capital is considered to be the most appropriate form of financing for innovative firms in high-tech sectors (Bottazzi, et al., 2016). Venture capital investors have a comparative advantage over traditional financing sources, such as banks and public equity investors, in working in environments characterized by high information asymmetry and high uncertainty (Feng et al., 2020; Panda, 2015). The main reason why venture capital firms exist is their superior ability to reduce the cost of informational asymmetry related to investing in entrepreneurial companies and their ability to display investment strategies that allow them to cope with high uncertainty (Metrick and Yasuda, 2011).

Most venture capital firms are organized as management companies responsible for managing several pools of capital, each representing a legally separate limited partnership. The economic life of most funds is set at 10 years, although provisions are often included to extend the life of the funds with two years (Sammut, 2017). Each new fund typically moves through a number of stages. In the investment period stage, typically from year one to year four, the investment portfolio is formed (Manigart & Sapienza, 2017). First round investments are being made in entrepreneurial companies and intense value adding activities are provided. Second round investment to the earliest deals in the portfolio may also occur during this stage. In the fund maturity stage, typically from year three to year seven, follow-on financing rounds are provided to the portfolio companies in order to further support their growth. Some realizations may already occur at this stage. Finally, in the harvest or liquidation stage, typically from year five to the end of a fund's life, fund managers are fully focused on exiting their investments (Standaert et al., 2022).

The most likely exit routes include the sale to other companies in the industry or the company's own management team in a buyout structure. Another exit mechanism, typically reserved for the most successful portfolio companies, is an Initial Public Offering. Failures also remain very common. Puri and Zarutskie (2015) indeed show that after the length of a typical venture capital investment, almost 40% of US venture capital-backed companies fail, some 34% are acquired and 16% go public. The remaining companies are "living death" companies whose equity stakes are difficult to sell. Corporate venture capital funds are not only interested in financial returns, but also in getting a "window on technology". Hence, they search for investments in sectors relevant to their core activities in order to identify new technologies (Dushnitsky & Yu, 2022). Though it might be hazardous for investors, who put money up, the possibility of above-average profits is an appealing payout. For new firms or projects with a short operational history (less than two years), venture capital is becoming a popular even critical — source of funding, particularly if they lack access to capital markets, bank loans, or other debt instruments. The primary disadvantage is that investors often receive ownership in the firm and hence a vote in corporate decisions (Pan et al., 2020).

Despite the fact that financial institutions have identified the SME sector as a fast-growing sector in the country, several constraints exist to SMEs access to finance from financial institutions (Kwaning et al.., 2015). According to the IFC (2015) SMEs globally experience difficulties in accessing bank finance but especially SMEs in emerging markets. When lending to small businesses, the major challenge of lenders is to reduce the risk posed to them by overcoming the problem of information asymmetry (Agyapong, 2017). Banks when financing SMEs usually lack accurate and reliable information on the financial condition and performance of small firms. Banks base their decision to extend credit on the strength of income statements, balance sheets, debtors and creditors lists and their aging analysis, amongst other financial reports (Shikum & Mirie, 2020).

When it comes to financing, entrepreneurs are frequently confronted with a slew of difficult problems. Entrepreneurs face numerous questions such as "how much money do we need," "when should we raise the money," "who would we receive the money from," "what would the payment conditions be," "what are the valuation charges for a startup," and so on (Beck, 2013). It is critical to understand who to approach for funding. While many people fund their new businesses with their own money or by borrowing from family or friends, there are alternative solutions. However, business entrepreneurs must realize that getting startup capital is never straightforward and always takes longer than expected (Liu et al., 2022).

The alternative to debt and equity financing for an entrepreneur is the use of their own funds to finance the startup process and activities of the business enterprise. Use of own funds also known as bootstrapping is a situation whereby the entrepreneur starts a business with available funds as capital instead of relying on external investments (Afolabi, 2013). Entrepreneurs can bootstrap by personally financing the business operations, finding ways to cut costs to the bare minimum and cutting back on operations. Most of the times, when the entrepreneur is bootstrapping to fund his business, the business is started with little or no assets (Harash et al., 2014). This is in contrast to starting a company by first raising capital through other means such as angel investors or venture firms.

Compared to using equity financing such as venture capital or angel financing, using own funds can be beneficial to the entrepreneur who is then able to maintain control over all decisions and the direction the company takes (Manigart & Sapienza, 2017). However, this form of business financing may place unnecessary financial risk on the entrepreneur and may not provide enough investment for the company to grow at a reasonable rate (Kato, 2021). Before bootstrapping their start-up business, entrepreneurs must first assess whether bootstrapping makes sense for their operations. It may not be financially feasible to use own funds for a business that requires high amounts of capital to form or one that has a slower turnaround on inventory thereby cash may be tied up for long periods of time (Afolabi, 2013). The business owner must keep in mind that there are costs associated with the enterprise that are required to be met by the founders. Hence, the business must at all times generate enough money to sustain itself while compensating the costs of the founders (Kato & Tsoka, 2020).

2. Theoretical Review

This paper was anchored on Traditional Theory of Capital Structure and Pecking Order Theory. The Traditional Theory of Capital Structures was advanced by Ezta Solomon and Fred Weston (2002). It states that there is an optimal ratio between debt and equity where the overall cost of capital is at the minimum and at the same time the firm's market value is at the maximum. This Traditional Theory of Capital structure is used to aid organizations in determining an optimal capital structure and its overall effect on the value of the firm. When deciding their debt-to-equity ratio which is usually informed by the amount of debt necessary to obtain the required capital, SMEs find it necessary to control their appetite for borrowing as debt capital definitely increases the overall cost of capital. Whenever an optimal balance is obtained for the capital structure, the cost of funds is reduced. This theory is instrumental in guiding SMEs on the optimal amounts of commercial loans to start and run their businesses.

This theory was advanced by Donaldson in 1961 and it was modified and made popular by Stewart Myers and Nicolas Majluf (1984). According to this theory, firms follow a hierarchy when considering sources of financing. The pecking order theory states that managers display the following preference of financing sources to fund investment opportunities: first, retained earnings from the company's profits, followed by debt, and equity financing is considered as a last resort. The pecking order theory arises from the concept of asymmetric information, also known as information failure, and this occurs when one party possesses more information than the other party in a transaction resulting in an imbalance in transaction power.

Business owners and managers usually possess more information concerning the company's performance, future prospects and risks than external parties such as creditors and investors. To compensate for this information asymmetry, external parties demand a higher return to counter their risk. Therefore, due to information asymmetry, external sources of finance always demand a higher rate of return to compensate for higher risk.

3. Empirical Review

Results of previous studies on entrepreneurial finance have focused on the different options of financing available to the entrepreneur (Zachary, 2020). Sabana (2014) studied Entrepreneurial Finance, Financial access, and performance of micro business in Nairobi. The determinants of the study were employment, market share, and profit. The study concluded that entrepreneurs need to invest in improving their financial literacy in order to improve the growth of their microenterprises. The study also found that key areas of improvement in financial management include financial planning, budgeting, cash flow management and preparation of financial statements. This study did not highlight the specific measures of growth. In 2016, Financial Sector Deepening (FSD) in conjunction with Growth Cap did a study on 'Understanding How Kenyan Entrepreneurs Grow and Finance Their Businesses'. The study focused on why banks are challenged in serving SMEs appropriately and gave a list of recommendations on how entrepreneurs would improve their chances of obtaining credit. However, the study only focused on credit from commercial banks and did not explore other forms of entrepreneurial finance.

The empirical evidence clearly reveals the importance of entrepreneurial finance to SME growth and points towards a positive relationship between growth and internal finance in different economies namely Germany, United States of America, Portugal and Spain (Bunyasi, Bwisa & Namusonge, 2014).

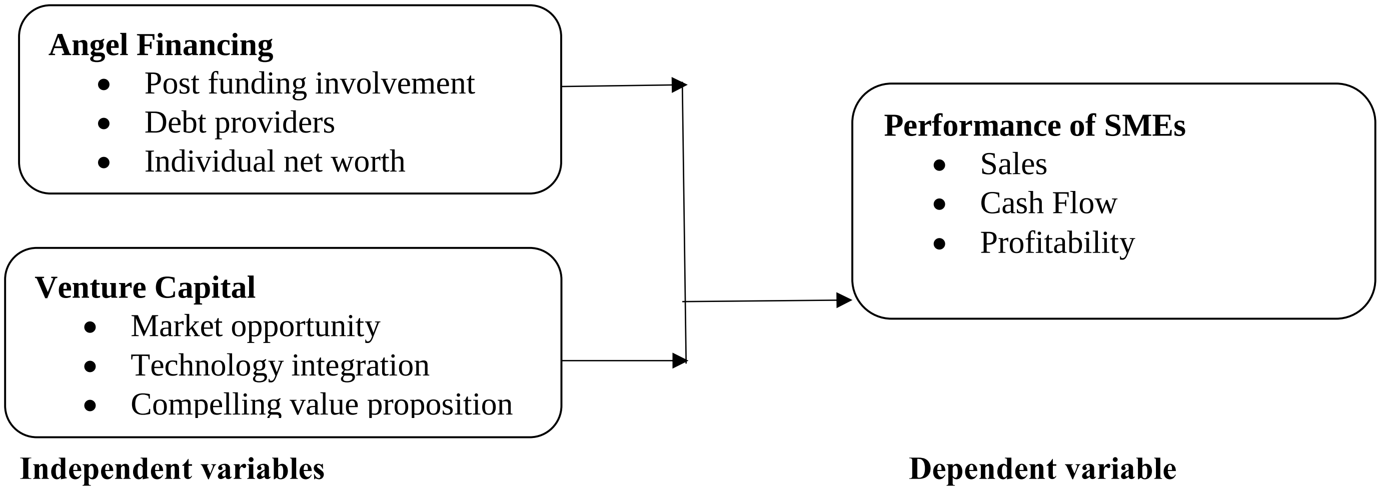
Most financial institutions like banks are very conservative and risk averse and therefore avoid SMEs that are considered risky and with no collateral or dependable track records (Wonglimpiyarat, 2015; Li, 2015). Most of those SMEs that are able to secure start up finance find the cost of capital too high (Rwigema & Venter, 2014). Financial constraints remain a major challenge facing SMEs in Kenya (Bunyasi et al 2014) and this is the situation in Kiambu as well. The study therefore determined how access to finance influences growth of SMEs in Kiambu County, Kenya.

The survival and growth of small and medium-sized companies is a complex but relevant subject which generates major interest in different stakeholders. These stakeholders include business owners, angel investors and venture capitalists who want returns on their investment, and financial institutions such as banks, savings societies and micro-finance organizations who need the credit they have advanced these business enterprises to be repaid with interest in the agreed manner. The societies where the business is established see the firms as vessels for jobs and job creation. Despite the amount of research conducted on SMEs survival and growth and factors associated with both, there is no coherent body of knowledge, and the rate of survival and growth is not increasing. This research focuses on various forms of entrepreneurial financing and how they influences the growth of small and medium sized enterprises in Kiambu County, Kenya. The purpose is to investigate the effect of angel financing and venture capital on growth in SMEs in Kiambu County, Kenya.

4. Conceptual Framework

A conceptual framework summarizes behaviors and provides explanations and predictions for the majority number of empirical observations (Cooper & Schindler, 2008).

Figure 1
Conceptual Framework Diagram



5. Methodology

This study used descriptive research design which is created by gathering, analyzing, and presenting the collected data. This allows the researcher to provide insight into the why and how of the research. The target population for this study constitutes of the 889 SMEs in Kiambu County as registered in the Kiambu Business Directory. The respondents were business owners or their managers. The target population is shown in Table 1.

Table 1

Target Population

Category of SMEs	Population
Manufacturing	169
General Trade Services	401
Services	319
Total	889

Source: Kiambu Business Directory 2023

Yamane, (1967) simplified formula used to obtain a sample size of 276 SMEs owners/ operators. The Stratified sampling method was used whereby the population was divided into different strata each strata containing elements with similar characteristics. The strata into which the population were divided are Manufacturing SMEs, Trading SMEs, and Service SMEs.

This study relied on primary data. The primary data was collected through a semi-structured questionnaire to obtain both quantitative and qualitative data for the research. Both closed and open types of questions were used to obtain qualitative and quantitative data to obtain information. Open questions were used to obtain qualitative data while closed questions were used to get quantitative data. Data was analyzed using SPSS version 23. It involved both descriptive and inferential statistics. Descriptive tests comprised mean, frequencies and standard deviations. On the other hand, inferential statistics entailed the correlation and multivariate regression model. Pearson's product-moment correlation coefficient (r) was used to examine the extent of correlation between the variables of study and to show the strength of the linear associations between the variables in the regression ranges between ±1. Where r= +0.7 and above it indicates a very strong correlation; r=+0.5 to below 0.7 is a strong correlation; r=0.3-0.49 is a moderate correlation while r=0.29 and below indicates a weak correlation. Where r=0 it indicates that there is no association (Dănăcică, 2017). The results were presented using tables. The multivariate regression model was:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \varepsilon$$

Y = Performance of SMEs, β_0 = Constant

X_1 = Angel financing, and X_2 = venture capital financing and ε = error term

6. Results

The study distributed 276 questionnaires to the respondents out of which 214 were dully filled and returned. This represented a response rate of 77.5% and this was adequate for analysis as outlined in Table 3. According to Mugenda and Mugenda (2003) a response rate of above 50% is considered adequate for analysis and the study response rate was above this threshold and therefore adequate for analysis.

Descriptive Statistics

Descriptive statistics entailed the study means, standard deviation as well as percentages. A Likert scale was used to collect responses from closed ended questions. The values of the scale ranged from 1 to 5 with 1 representing Strongly Disagree, 2 for Disagree, 3 for Neutral, 4 for Agree and 5 for Strongly Agree. In the interpretation of these responses, the study calculated the mean response of each of the statements. A mean of 1 implied that the responses were largely in strong disagreement, mean of 2 implying that the responses were largely in disagreement, mean of 3, responses were neither in agreement or disagreement, mean of 4, the responses were largely in agreement and finally mean of 5 implying that the responses were largely in strong agreement.

Table 2

Descriptive Findings

Variable	Mean	Standard deviation
Angel Financing	3.59	1.2
Venture Capital	3.6	1.15

As per the findings, the majority respondents were in agreement that angel financing and venture capital were crucial socials for entrepreneurial financing. Venture capital was ranked high as form of entrepreneurial financing followed by angel financing.

Correlation Analysis

Pearson correlation analysis was conducted to determine the strength and direction of relationships between variables of the study. The correlation results are outlined in Table 3.

Table 3
Correlation Results

		Performance	Angel Financing	Venture Capital
Performance	Pearson Correlation	1		
	Sig. (2-tailed)			
Angel Financing	Pearson Correlation	.544**	1	
	Sig. (2-tailed)	0.000		
Venture Capital	Pearson Correlation	.535**	.473**	1
	Sig. (2-tailed)	0.000	0.000	
	N	214	214	214
	Sig. (2-tailed)	0.000	0.000	0.000

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

Stratford Peer Reviewed Journals and Book Publishing
Journal of Finance and Accounting
Volume 8||Issue 4||Page 1-18 ||April||2024|
Email: info@stratfordjournals.org ISSN: 2616-4965

From the outcomes, the correlation between angel financing and performance of SMEs was positive and statistically significant (0.544, 0.000<0.05). Furthermore, the outcomes of correlation between venture capital and performance of SMEs was also positive and significant (0.535, 0.000<0.05).

Regression Results

A regression analysis was conducted to determine the linear relationship between the variables of the study. The independent variables in the study were angel financing and venture capital. The dependent variable of the study was the performance of SMEs. From the results of regression, analysis the model estimated explains 47.9% of the total changes in performance of SMEs as evidenced by the value of R Square in the model of 0.479. This means that the variables angel financing and venture capital explain performance of SMEs. The model summary results are tabulated table 4.

Table 4
Model Summary

R	R Square	Adjusted R Square	Std. Error of the Estimate
.692a	0.479	0.469	0.31429

Predictors: (constant) venture capital, angel financing

The model estimated was significant statistically. This is provided by the estimated p-value of 0.000<0.05. Furthermore, these results can be confirmed by the estimated value of F (48.082) which is far greater than the F critical value (F 4, 209) in the F tables. Thus, the identified study variables are significant in giving explanations on performance of SMEs. The ANOVA results are outlined in Table 5.

Table 5
ANOVA Results

	Sum of Squares	df	Mean Square	F	Sig.
Regression	18.998	4	4.75	48.082	.000b
Residual	20.645	209	0.099		
Total	39.643	213			

Dependent Variable: Performance of SMEs
Predictors: (Constant), venture capital, angel financing

The estimated model's constant exhibited a positive value on Table 5 based on the regression coefficient outcomes. The coefficient of angel financing was positive (0.188) and statistically significant (0.001<0.05). Thus, improving angel-financing services by a unit results in a significant 0.188 units improvement in the performance of SMEs. Hence, angel-financing services is a significant determinant of performance of SMEs. The coefficient of venture capital was positive (0.218) and statistically significant (0.000<0.05). Enhancing venture capital of the SMEs by unit results in a significant 0.218 units significant improvement in the performance of SMEs. Thus, venture capital is a significant determinant of performance of SMEs.

Table 6

Regression Coefficients

	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	1.054	0.194		5.448	0.000
Angel Financing	0.188	0.056	0.215	3.385	0.001
Venture Capital	0.218	0.055	0.238	3.949	0.000

Dependent variable: Performance of SMEs

From the regression model, the coefficient of Angel Financing was positive (0.188) and statistically significant (0.001<0.05). This means that, improving angel-financing services by a unit result in a significant 0.188 units improvement in the performance of SMEs. Hence, angel-financing services are a significant determinant of performance of SMEs. Angel Financing entails the external financing support received by a firm when it is small and at an early stage immediately after formation (Wong, Bhatia & Freeman, 2009).

Much research conducted in the past confirm that angel investors play an important and vital role in entrepreneurship by financing small and medium sized enterprises. The amounts they invest are significant and the expertise and networks they bring to the businesses in post funding involvement makes them more attractive to entrepreneurs as a source of finance in comparison to other sources of capital (Sohl, 2019). Financing is a very critical issue for the survival and development of small and medium sized enterprises (SMEs). Angel Investors play a key role in financing small and medium sized enterprises, especially those which are innovative and have a high growth potential (Preston, 2014). SMEs in their development pass through several stages. Angel investors prefer to invest in business enterprises, which are in the start-up, or early stages where their money and expertise is needed the most before they exit the market (Harrison & Mason, 2018).

Angel investors are important to entrepreneurs with small and medium sized enterprises because they provide more than money. They are hands on investors who in addition to finances contribute their expertise, skills, knowledge, and networks in the businesses they invest in. They are wealthy individuals with great business expertise (Ramadani, 2016). Although Angel investors are exposed to greater uncertainty by investing earlier in the life of a firm compared to venture capital, they do not rely on traditional control mechanisms such as board control, staging, or contractual provisions to protect against expropriation. Instead, Angels reduce expected agency costs by forcing entrepreneurs to hold a larger stake in the firm, thereby aligning the interests of the entrepreneur with the outcome of the business enterprise (Wong, 2016). In addition, angel investors use more informal methods such as investing in close geographical proximity and syndicating investments with fellow angels to mitigate risks (Edelman, 2012).

Furthermore, the coefficient of venture capital was positive (0.218) and statistically significant (0.000<0.05). This implies that enhancing venture capital of the SMEs by unit results in a significant 0.218 units' significant improvement in the performance of SMEs. Thus, venture capital is a significant determinant of performance of SMEs. Venture capital entails the financial support obtained when the firm is more structured and established (Wong, Bhatia & Freeman, 2009). The results of this analysis are in tandem with the findings of Mboya et al. (2020) who indicated that venture capitalists in Kenya provide long-term capital to new and expanding

Stratford Peer Reviewed Journals and Book Publishing
Journal of Finance and Accounting
Volume 8||Issue 4||Page 1-18 ||April||2024|
Email: info@stratfordjournals.org ISSN: 2616-4965

businesses, which are usually high risk, but offer the potential for above-average returns. Capitalists pool their resources including managerial abilities to assist new entrepreneurs in the early years of their businesses. In recent years, annual venture capital invested in Kenya has surpassed $1 billion.

The findings of Bottazi and Laura (2015) further pointed out that venture capital is considered to be the most appropriate form of financing for innovative firms in high-tech sectors. Amit et al. (2008); Chan, (2013) also indicated that venture capital investors have a comparative advantage over traditional financing sources, such as banks and public equity investors, in working in environments characterized by high information asymmetry and high uncertainty. The essence of the existence of venture capital firms is their superior ability to reduce the cost of informational asymmetry related to investing in entrepreneurial companies and their ability to display investment strategies that allow them to cope with high uncertainty (Metrick & Yasuda, 2011). For new firms or projects with a short operational history (less than two years), venture capital is becoming a popular — even critical — source of funding, particularly if they lack access to capital markets, bank loans, or other debt instruments (Chen, 2020).

Most venture capital firms are organized as management companies responsible for managing several pools of capital, each representing a legally separate limited partnership. The economic life of most funds is set at 10 years, although provisions are often included to extend the life of the funds with two years (Sammut, 2017). Each new fund typically moves through a number of stages (Sammut, 2017). In the investment period stage, typically from year one to year four, the investment portfolio is formed. First round investments are being made in entrepreneurial companies and intense value adding activities are provided. Second round investment to the earliest deals in the portfolio may also occur during this stage. In the fund maturity stage, typically from year three to year seven, follow-on financing rounds are provided to the portfolio companies in order to further support their growth. Some realizations may already occur at this stage. Finally, in the harvest or liquidation stage, typically from year five to the end of a fund's life, fund managers are fully focused on exiting their investments (Manigart & Wright, 2018).

7. Conclusions

Drawing inference from the research results, it can be concluded that angel financing positively and significantly affects the performance of SMEs in Kiambu County. The amounts the angel investors invest are significant and the expertise and networks they bring to the businesses in post funding involvement makes them more attractive to entrepreneurs as a source of finance in comparison to other sources of capital. Angel Investors play a key role in financing small and medium sized enterprises, especially those that are innovative and have a high growth potential. Angel investors prefer to invest in business enterprises, which are in the start-up, or early stages where their money and expertise is needed the most before they exit the market.

In view of the research results, inference can be made that venture capital is a positive and significant determinant of the performance of SMEs in Kiambu County Kenya. Venture capital entails the financial support obtained when the firm is more structured and established. Venture capitalists in Kenya provide long-term capital to new and expanding businesses, which are usually high risk, but offer the potential for above-average returns. The essence of the existence of venture capital firms is their superior ability to reduce the cost of informational asymmetry related to investing in entrepreneurial companies and their ability to display investment strategies that allow them to cope with high uncertainty.

8. Recommendations

The study recommends that before the inception of SMEs, the founders ought to look for adequate capital necessary for efficient running of the operations of the company as well as capital that enables the purchase of adequate stock. This is necessary as it ensures the sustainability as well as the financial performance of the SMEs.

Furthermore, the SMEs after their establishment ought to look for more sources of capital to enable the expansion of these businesses as well as enhancing their sustainability. As the business expands, there is a likelihood of the improvement in the customer base thus necessitating the need for more stocks as well as the diversification of the stocks available to enhance customer satisfaction.

The study recommended that before the inception of SMEs, the founders ought to look for adequate capital necessary for efficient running of the operations of the enterprise as well as a capital that enables the purchase of adequate stock. This can be done through conjunction between venture capitalist, SMEs through Micro and Small Enterprises Authority and the ministry of Cooperatives and Micro and Small Enterprise to develop a funding framework for SMEs anchored on venture capital and angel financing.

9. References

Afolabi, M. O. (2013). Growth effect of small and medium enterprises (SMEs) financing in Nigeria. *Journal of African Macroeconomic Review*, *3*(1).

Agyapong, D., (2019). Effect of owner-manager's financial literacy on the performance of SMEs in the Cape Coast Metropolis in Ghana. *Journal of Global Entrepreneurship Research*, *9*(1), 67.

Aseem, G., & Kati, S. (2015). State of SME Finance in the United States. *White paper*.

Bartocho, E. J. (2022). Enhancing Women Entrepreneurs, Entrepreneurial Innovations and Sustainability of Small Enterprises in Kenya. *World*, *2579*, 0544.

Beck, T. (2013). Bank financing for SMEs–lessons from the literature. *National institute economic review*, *225*(1), R23-R38.

Beck, T., Demirgüç-Kunt, A., & Singer, D. (2016). *Is small beautiful? Financial structure, size and access to finance*. World Development, 52, 19-33.

Berger, A. N., Frame, W. S., & Miller, N. H. (2005). *Credit scoring and the availability, price, and risk of small business credit*. Journal of money, credit and banking, 191222.

Bonini, S., & Awuni, M. (2023). Business Angel Syndicates. In *The Palgrave Encyclopedia of Private Equity* (pp. 1-7). Cham: Springer International Publishing.

Bottazzi, L., Da Rin, M., & Hellmann, T. (2016). The importance of trust for investment: Evidence from venture capital. *The Review of Financial Studies*, *29*(9), 2283-2318.

Bunyasi, G. N. W., Bwisa, H., & Namusonge, G. (2014). Effect of Access to Business Information on the Growth of Small and Medium Enterprises in Kenya. *International Journal of Business and Social Science* 5 (10), 121–128.

Cooper, D., & Schindler, P. (2014). *EBOOK: Business research methods*. McGraw Hill.

Cooper, D.R., & Schindler P.S. (2008). *Business Research Methods. (10th ed).* Singapore: McGraw-Hill.

Dushnitsky, G., & Yu, L. (2022). Why do incumbents fund startups? A study of the antecedents of corporate venture capital in China. *Research Policy*, *51*(3), 104463.

Edelman, L. F., Manolova, T. S., & Brush, C. G. (2017). Angel investing: A literature review. *Foundations and Trends® in Entrepreneurship*, *13*(4-5), 265-439.

Eyiah, K. A., Kheni, N. A., & Acquah, R. (2018). SME financing constraints: evidence from the survey of construction firms in Ghana. *Int J Small Medium Enterp Bus Sustain*, *3*(2), 23-47.

Fadil, N., & St-Pierre, J. (2021). Growing SMEs and internal financing: the role of business practices. *Journal of Small Business and Enterprise Development*, *28*(7), 973-994.

Feng, X., Chan, K. C., & Lo, Y. L. (2020). Are venture capitalist-backed IPOs more innovative? Evidence from an emerging market. *The North American Journal of Economics and Finance*, *51*, 100839.

Godke Veiga, M., & McCahery, J. A. (2019). The financing of small and medium-sized enterprises: an analysis of the financing gap in Brazil. *European Business Organization Law Review*, *20*(4), 633-664.

Harash, E., Al-Timimi, S., & Alsaadi, J. (2014). Effects of financing on performance of small and medium enterprises (SMEs). *International Journal of management*, *2*(10), 1-9.

Hong, G. H., Ito, A., Saito, Y., & Nguyen, T. N. A. (2020). Structural Changes in Japanese SMEs: Business Dynamism in Aging Society and Inter-Firm Transaction Network. *Policy Discussion Papers. Research Institute of Economy, Trade and Industry (RIETI)*.

Kashangaki, J. (2014). Transforming SME finance.

Kato, A. (2021). A literature review of venture capital financing and growth of smes in emerging economies and an agenda for future research. *Academy of Entrepreneurship Journal*, *27*(1), 1-17.

Kato, A. I., & Tsoka, G. E. (2020). Impact of venture capital financing on small-and medium-sized enterprises' performance in Uganda. *The Southern African Journal of Entrepreneurship and Small Business Management*, *12*(1), 11.

Kauffmann, C. (2005). Financing small and medium enterprises in Africa. *INSIDE THIS ISSUE*, *3*(2), 3.

Kenya Bankers Association (2016). Financing Small and Medium Enterprise: The Reconciliation of Borrower-lender Expectations. chrome-extension://efaidnbmnnnibpcajpcglclefindmkaj/https://www.kba.co.ke/wp-content/uploads/2022/05/SME-Financing-Survey.pdf

Kenya National Bureau of Statistics (2007). Connecting Kenyan Entrepreneurs and Angel Investors. https://www.angelinvestmentnetwork.co.ke/

Kiambu Business Directory (2018). Registered SMEs. https://carijournals.org/journals/index.php/IJF/article/view/1261

Kwaning, C. O., Nyantakyi, K., & Kyereh, B. (2015). The challenges behind SMEs' access to debts financing in the Ghanaian financial market. *International Journal of Small Business and Entrepreneurship Research*, *3*(2), 16-30.

Lee, S., & Persson, P. (2016). *Financing from family and friends*. The Review of Financial Studies, 29(9).

Li, Y. (2015). SMEs and Entrepreneurial Finance in OECD Countries. *Journal of Law and Governance*, *10*(2), 31-36.

Liu, Y., Dilanchiev, A., Xu, K., & Hajiyeva, A. M. (2022). Financing SMEs and business development as new post Covid-19 economic recovery determinants. *Economic Analysis and Policy*, *76*, 554-567.

Lo, J. Y. (Ed.). (2016). *Angel financing in Asia Pacific: A guidebook for investors and entrepreneurs*. Emerald Group Publishing Limited.

Manigart, S., & Sapienza, H. (2017). Venture capital and growth. *The Blackwell handbook of entrepreneurship*, 240-258.

Metrick, A., & Yasuda, A. (2011). Venture capital and other private equity: a survey. *European Financial Management*, *17*(4), 619-654.

Ministry of Economy, Trade and Industry (2022). Japan Finance Corporation Guide to the Operations of the Small and Medium Enterprise (SME) Unit. chrome-extension://efaidnbmnnnibpcajpcglclefindmkaj/https://www.jfc.go.jp/n/english/sme/pdf/jfc2022e-sme_web.pdf

Muhuhu, M. W., Ngali, R., & Wepukhulu, J. M. (2023). Venture Capital and Growth of Small and Medium-Sized Enterprises in Kiambu County, Kenya. *International Journal of Finance*, *8*(2), 65-89.

Mwasi, L. L., & Aluoch, M. O. (2023). Venture capital financing and financial performance of technology start-up firms in Kenya. *International Academic Journal of Economics and Finance*, *3*(10), 1-25.

Myers, S. C., & Majluf, N. S. (1984). When firms have information that investors. *Journal of Financial Economics*, *13*, 187-221.

Nanziri, L. E., & Wamalwa, P. S. (2021). Finance for SMEs and its effect on growth and inequality: evidence from South Africa. *Transnational Corporations Review*, *13*(4), 450-466.

Naradda Gamage, S. K., Ekanayake, E. M. S., Abeyrathne, G. A. K. N. J., Prasanna, R. P. I. R., Jayasundara, J. M. S. B., & Rajapakshe, P. S. K. (2020). A review of global challenges and survival strategies of small and medium enterprises (SMEs). *Economies*, *8*(4), 79.

OECD, P. (2017). Enhancing the contributions of SMEs in a global and digitalised economy. *Paris. Retrieved Feb*, *25*, 2019.

Olarewaju, A. D., Adebisi, S. A., George, O. J., & Gonzalez-Tamayo, L. A. (2023). Institutions and internationalization of SMEs in an emerging African economy: the moderating role of sustainable entrepreneurship. In *A Research Agenda for International Entrepreneurship* (pp. 289-318). Edward Elgar Publishing.

Omondi, F., Onono, P., A. & Barasa, S. (2022). A gendered analysis of institutional and government Small and Medium Enterprises-related policies in Kenya. https://kenya.oxfam.org/latest/publications/gendered-analysis-institutional-and-government-small-and-medium-enterprises#:~:text=Small%20and%20Medium%20Enterprises%20(SMEs,production%20resulting%20to%20economic%20growth.

Ooi, S. M., & Richardson, C. (2019). The internationalisation of service-sector SMEs in an emerging market: Insights from business training and consultancy firms in Malaysia. *Review of International Business and Strategy*, *29*(1), 44-60.

Pan, L., Li, X., Chen, J., & Chen, T. (2020). Sounds novel or familiar? Entrepreneurs' framing strategy in the venture capital market. *Journal of Business Venturing*, *35*(2), 105930.

Panda, S. (2015). Factors affecting capital structure of Indian venture capital-backed growth firms. *Entrepreneurial Ecosystem: Perspectives from Emerging Economies*, 133-156.

Pedraza, J. M. (2021). The micro, small, and medium-sized enterprises and its role in the economic development of a country. *Business and Management Research*, *10*(1), 33.

Puri, M. & R. Zarutskie (2015). "On the Life Cycle Dynamics of Venture-Capital- and NonVenture-Capital-Financed Firms". The Journal of Finance 67(6), 2247–2293.

Quartey, P., Turkson, E., Abor, J. Y., & Iddrisu, A. M. (2017). Financing the growth of SMEs in Africa: What are the contraints to SME financing within ECOWAS?. *Review of development finance*, *7*(1), 18-28.

Ragozzino, R., & Blevins, D. P. (2016). Venture–backed firms: how does venture capital involvement affect their likelihood of going public or being acquired?. *Entrepreneurship Theory and Practice*, *40*(5), 991-1016.

Ramukumba, T. (2014). Overcoming SMEs challenges through critical success factors: A case of SMEs in the Western Cape Province, South Africa. *Economic and business review*, *16*(1), 2.

Rogito, D. O. (2010). *Influence of monitoring and evaluation on project's performance: case of Youth Enterprise Development Fund in Marani district, Kenya* (Doctoral dissertation, University of Nairobi, Kenya).

Sammut, S. (2017). Venture capital and entrepreneurial management. *Philadelphia. PA: The University of Pennsylvania*, *The Wharton School*.

Samsami, M., El Kolaly, H., & Schøtt, T. (2022). Business angels ties with entrepreneurs. In *Developments in Entrepreneurial Finance and Technology* (pp. 182-198). Edward Elgar Publishing.

Scoreboard, A. O. (2019). Financing SMEs and Entrepreneurs 2019.

Shikumo, D. H., & Mirie, M. (2020). Determinants of lending to small and medium enterprises by commercial banks in Kenya. *arXiv preprint arXiv:2010.12550*.

Sohl, J. (2019). The Angel investor market in 2018: More angels investing in more deals at lower valuations. *Center for Venture Research*, 1-2.

Standaert, T., Knockaert, M., & Manigart, S. (2022). Venture capital winners: A configurational approach to high Venture capital-backed firm growth. *British Journal of Management*, *33*(1), 211-230.

Wong, A., Bhatia, M., & Freeman, Z. (2009). Angel finance: The other venture capital. Strategic Change, 18(7-8), 221-230.

Wonglimpiyarat, J. (2015). Challenges of SMEs innovation and entrepreneurial financing. *World Journal of Entrepreneurship, Management and Sustainable Development*, *11*(4), 295-311.

World Bank (2019). Small and Medium Enterprises (SMEs) Finance. Available at https://www.worldbank.org/en/topic/smefinance.

Zachary, L. N., (2020). Technology and government regulation: A conceptual perspective of entrepreneurial orientation on creditworthiness of micro-enterprises. *African Journal of Business Management*, *14*(3), 93-100.