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Financing Options and Financial Growth of Small and Medium Enterprises in Kirinyaga County, Kenya

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Abstract

Small and Medium Enterprises (SMEs) are crucial to Kenya's economy, serving as its foundation and supporting numerous families. However, accessing financing remains a persistent challenge for these enterprises. While extensive research examines factors affecting SME performance and profitability in Kenya, few studies have explored constraints SMEs encounter in securing financing from various sources and how these challenges relate to overall performance. Most studies focus on industry or macroeconomic factors rather than financing options. This study investigated the effect of financing options on the financial growth of SMEs in Kirinyaga County, Kenya. Specific objectives assessed the effects of equity financing, debt financing, and informal financing on SME financial growth. The study's significance lies in its potential to inform SME owners and policymakers about effective financing strategies that enhance financial growth, ultimately contributing to sustainable SME development in Kirinyaga County and fostering a more robust regional economic environment. Theoretical frameworks including Pecking Order Theory, Trade-Off Theory, and Agency Theory guided the analysis, providing comprehensive understanding of how different financing options affect SMEs. The study employed a descriptive research design involving 139 SMEs selected through Yamane sampling strategy from 213 registered SMEs as of December 2023. A pilot test refined the questionnaire, ensuring clarity and relevance. Data collection utilized structured questionnaires, prioritizing ethical considerations including confidentiality and voluntary participation. Operationalization and measurement of variables defined key constructs related to financing options. Diagnostic tests assessed data quality. Data presentation included descriptive statistics (means and standard deviations) and inferential statistics to establish variable relationships, analyzed using SPSS version 23. Equity, debt, and informal financing demonstrated positive significant effects on SME financial growth in Kirinyaga County. The study concludes that equity financing provides essential capital for expanding operations, investing in new technologies, and increasing market reach. Debt financing enables businesses to invest in expansion, improve operations, and enhance market competitiveness. Informal financing provides crucial capital to SMEs struggling to access traditional bank loans due to stringent requirements. The study recommends that the County develop targeted financial literacy programs educating SME owners about equity financing options and effectively presenting business cases to potential investors. The government should create platforms for SMEs to showcase business plans and financial needs to potential investors and lenders, facilitating connections that could lead to better financing opportunities.

Keywords: *Financing Options, Financial Growth, Small and Medium Enterprises, Kirinyaga County, Kenya*

1.0 Background of the Study

Small and medium enterprises (SMEs) play a crucial role in the global economy, contributing significantly to employment, innovation, and economic growth (OECD, 2021). However, these businesses face unique challenges in accessing financing, which impacts their long-term stability and financial growth. One primary challenge is limited access to traditional financing sources, such as bank loans and equity investments, due to lack of collateral, credit history, or perceived risk by financial institutions (Cowling, Baker & Dowell, 2020). Consequently, many SMEs rely on alternative financing options, including trade credit, personal savings, or informal funding sources (Ardic et al., 2022). The emergence of new financing technologies, such as peer-to-peer lending, crowdfunding, and alternative lending platforms, has provided additional capital access options (Lukonga, 2021).

In developed and emerging economies, SME financing presents varied challenges and solutions. In India, traditional bank loans remain inaccessible due to collateral and credit history requirements, prompting government initiatives like MSEFIC and CGTMSE to provide credit guarantees and collateral-free loans (Agrawal & Sharmila, 2021). The United States has implemented programs such as the SBA loan guarantee program and Paycheck Protection Program to support SMEs during economic uncertainty (Ullah et al., 2020). Europe has established the European Investment Fund and European Fund for Strategic Investments to provide credit guarantees and venture capital across the EU (Cowling et al., 2020). Despite these interventions, effectiveness remains debated, with studies suggesting limited impact or uneven distribution across regions and sectors.

In Africa, SMEs face substantial financing obstacles despite their economic significance. Nigerian SMEs contribute over 48% to national GDP and employ over 84% of the workforce, yet face limited access to traditional banking services due to financial sector concentration (Abubakar & Uzairu, 2022). Ghana's SMEs account for over 80% of business activities, with government initiatives like NBSSI and Ghana Venture Capital Trust Fund providing support (Abor & Quartey, 2010). Moroccan SMEs represent over 95% of businesses, with government implementing CCG credit guarantee schemes and Fonds Daraka investment fund (Belarbi & Zouhair, 2020). Digital financial services, including mobile money and crowdfunding platforms, offer promising alternatives, though sustainability concerns regarding high interest rates, regulation gaps, and fraud potential persist (Ozili, 2020).

In Kenya, small and medium-sized enterprises account for over 98% of all businesses, contributing approximately 30% to the country's GDP (Ngugi & Bwisa, 2013). However, financing access remains a significant challenge hindering their financial growth and stability. Limited availability of traditional banking services, particularly in rural and underserved areas, creates substantial financing gaps (Lukonga, 2021). The government has implemented initiatives including the Uwezo Fund, Youth Enterprise Development Fund, and Women Enterprise Fund to provide collateral-free loans and targeted support. Mobile money platforms, particularly M-Pesa, have revolutionized financial inclusion, enabling SMEs to participate in formal financial systems. Despite these interventions, many SMEs still face barriers in obtaining necessary capital, requiring comprehensive policy approaches addressing financing, market access, and regulatory challenges.

Financial growth in SMEs is primarily measured using key financial ratios: Return on Assets (ROA), Return on Equity (ROE), and Profit Margin. Research by Asiedu et al. (2021) shows top-performing Ghanaian SMEs achieved 27% average ROA, while Mensah and Abor (2022) found financially stable SMEs had 37% average ROE. Financing options for SMEs include equity financing, involving capital raising through ownership sales to investors; debt financing, through borrowing from banks or microfinance institutions; and retained earnings, reinvesting profits back into the business (Cowling, Baker & Dowell, 2020). Each option presents distinct advantages and challenges. Equity financing provides capital without debt but may require relinquishing control. Debt financing maintains ownership but strains finances through interest payments. Retained earnings offer sustainable growth but may limit expansion pace.

Kirinyaga County, located in Central Kenya, has a population exceeding 600,000, with an economy largely driven by SMEs contributing significantly to local employment and development (Kenya National Bureau of Statistics, 2022). SMEs account for approximately 80% of employment opportunities, underscoring their importance in enhancing livelihoods. Research by Mwangi et al. (2023) indicates approximately 70% of micro enterprises in Kirinyaga operate in retail and trade sectors. However, financing access remains challenging, with only 30% of SMEs accessing formal credit (Wanjiru & Ndung'u, 2021). Alternative financing options, including microfinance institutions and cooperative societies, have emerged as vital funding sources. Addressing these financing challenges is essential for unlocking SME potential, fostering resilience, and promoting economic prosperity in Kirinyaga County.

1.1 Statement of the Problem

Small and Medium Enterprises (SMEs) are essential for economic development in Africa, comprising about 90% of businesses and generating up to 80% of jobs (Ullah et al., 2020). The International Finance Corporation estimates that formal SMEs in Africa encounter a staggering financing gap of approximately Shs.331 billion, underscoring the urgency of addressing this issue (Dzisi & Ofosu, 2014). In Kirinyaga County specifically, many SMEs struggle to secure funding, limiting their ability to invest in critical areas such as technology, human resources, and market expansion. This financial constraint stifles innovation and hinders potential for increased profitability and job creation within the region. Many SMEs face challenges in attracting equity investment due to fears of losing control over their businesses, while high debt-to-equity ratios often lead to stagnation characterized by lower profitability and liquidity.

Research indicates a complex relationship between financing options and financial growth. Abor and Quartey (2010) found that SMEs with higher equity-to-asset ratios tend to exhibit stronger financial growth, as evidenced by improved ROE, highlighting equity financing's importance in providing essential capital. However, Agwu and Emeti (2014) discovered that SMEs with high debt-to-equity ratios often experience stagnation, as loan repayment burdens strain cash flow and restrict growth opportunities. Conversely, Ullah et al. (2020) argue that strategically managed debt financing can enhance financial growth by providing necessary capital for productive investments. Research by Cowling, Baker, and Dowell (2020) indicates that SMEs with higher proportions of retained earnings typically achieve better financial performance measured by profit margins, though this self-financing approach may limit external capital access and strategic guidance.

Despite existing studies, significant gaps remain in the literature regarding financing options available to SMEs in Kirinyaga County. Current research often overlooks the influence of regional, cultural, and industry-specific factors on financing decisions and financial growth (Abor & Biekpe, 2009; Eniola & Entebang, 2015; Fatoki, 2014). Additionally, many studies utilize cross-sectional methodologies, restricting understanding of long-term effects of financing choices on SME financial growth (Adomako et al., 2016; Quartey et al., 2017; Boateng et al., 2018). Existing research tends to treat African SMEs as a homogeneous group, neglecting diverse characteristics and financing needs of different enterprises (Asah et al., 2015). Addressing these gaps is essential for enhancing understanding of the intricate relationship between financing choices and financial growth among SMEs in Kirinyaga County.

1.2 Objectives of the Study

i. To determine the effect of equity financing on financial growth of small and medium enterprises in Kirinyaga County, Kenya.

ii. To analyze the effect of debt financing on financial growth of small and medium enterprises in Kirinyaga County, Kenya.

iii. To examine the effect of informal financing on financial growth of small and medium enterprises in Kirinyaga County, Kenya.

1.3 Research Hypotheses

H_{o1}. Equity financing has no effect on financial growth of small and medium enterprises in Kirinyaga County, Kenya.

H_{o2}. Debt financing has no effect on financial growth of small and medium enterprises in Kirinyaga County, Kenya.

H_{o3}. Informal financing has no effect on financial growth of small and medium enterprises in Kirinyaga County, Kenya.

2.0 Literature Review

This section discusses the theoretical perspectives on the relationship between financing options and financial growth of small and medium enterprises. It provides an empirical review of the existing literature, summarizing the key findings and highlighting the research gaps. Additionally, the section outlines the conceptual framework used in the study.

2.1 Theoretical Review

This section examines theories that explain how different financing options—equity financing, debt financing, and informal financing—affect the financial growth of small and medium enterprises (SMEs). Theoretical frameworks provide a structured understanding of these relationships, offering insights into how each financing type influences financial performance, business continuity, and resilience. By integrating relevant models, this review establishes a foundation for predicting how these financing options can lead to varying growth outcomes for SMEs, thereby enhancing understanding of their financial dynamics and strategic decision-making. Three key theories are examined: Pecking Order Theory, which explains equity financing preferences; Trade-Off Theory, which addresses debt financing decisions; and Agency Theory, which explores informal financing dynamics. These frameworks collectively provide comprehensive insights into SME financing behavior and growth implications.

The Pecking Order Theory, proposed by Myers and Majluf in 1984, is a widely-used framework in studying equity financing and SME financial growth. The theory's central premise is that firms have a preferred hierarchy of financing sources, with internal financing (retained earnings) being most preferred, followed by debt financing, and finally external equity financing as least preferred (Myers, 2001). SMEs face information asymmetries between insiders and external investors, leading to higher external financing costs (Serrasqueiro & Caetano, 2015). Consequently, SMEs rely more on internal financing sources to avoid ownership dilution and control loss associated with equity financing (López-Gracia & Sogorb-Mira, 2008). However, the theory has limitations, failing to fully account for complex and dynamic financing decisions influenced by factors beyond information asymmetries, such as external financing availability, firm growth stage, and entrepreneur's risk preferences.

The Trade-Off Theory, developed by Modigliani and Miller in the 1950s and 1960s, is widely-used in studying debt financing and SME financial growth. The theory's central premise is that firms optimize their capital structure by balancing debt financing benefits and costs (Modigliani & Miller, 1963). Key benefits include tax deductibility of interest payments, which boosts after-tax cash flow and financial performance (Belkhir et al., 2019). Debt financing allows SMEs to maintain control and avoid ownership dilution associated with equity financing (Zachiello et al., 2020). However, the theory recognizes debt costs, such as increased financial distress and bankruptcy risk. Given SMEs' smaller size and limited resources, an optimal debt financing level balances benefits and costs (Bartoli et al., 2018). The theory has been widely tested and supported by empirical research.

Agency theory is instrumental in understanding dynamics between informal financing and SME financial growth. Initially articulated by Jensen and Meckling (1976), the theory highlights inherent conflicts between principals (owners) and agents (managers) within firms. While owners aim to maximize profits and enhance shareholder value, managers may prioritize job security, personal benefits, or non-financial incentives. Informal financing, encompassing financial resources obtained outside traditional banking systems, becomes a focal point due to these divergent objectives. Agency theory posits that goal misalignment results in agency costs—expenses incurred due to conflicts (Eisenhardt, 1988). Managers may hesitate pursuing informal financing for growth initiatives if actions jeopardize job security, stifling long-term financial growth and adversely affecting competitive edge and market adaptability (Colli & Colli, 2017). Recent studies suggest ownership structure plays crucial roles in mitigating conflicts.

2.2 Empirical Review

Equity financing provides SMEs with essential capital for investment and growth without incurring debt obligations. Cumming and Johan (2021) conducted a comprehensive study in Canada using mixed-methods approach including quantitative surveys and qualitative interviews with SME owners, finding that equity financing significantly enhances financial stability and growth prospects for SMEs by reducing financial distress and bankruptcy risk. Bertoni et al. (2020) investigated equity financing effects on Italian SMEs using quantitative methodology, demonstrating that external investors contribute capital and offer critical managerial expertise and strategic guidance, particularly beneficial for high-growth, innovative SMEs. Herciu (2017) identified equity financing as a promising solution to SME challenges, particularly during expansion or economic uncertainty periods. However, Cumming and Johan (2017) highlighted concerns regarding ownership dilution and loss of control, noting many SME owners hesitate relinquishing decision-making authority.

Zhang and Xia (2020) examined equity financing roles in Chinese SMEs using mixed-methods approach, revealing that supportive institutional frameworks, including investor protection and robust venture capital ecosystems, are crucial for successful equity financing in emerging markets. Ayyagari et al. (2018) focused on sub-Saharan African SMEs, employing mixed-methods approach and finding that equity financing success is contingent upon alternative financing options availability and financial market development. They recommended tailored equity financing strategies considering local conditions. Despite advancements, significant gaps remain, particularly concerning emerging and developing economies. Akinola and Ojo (2023) and Silva and Carreira (2022) noted existing literature often focuses on developed markets, leaving voids in knowledge about equity financing impacts in less stable economic environments. Addressing these gaps is essential for developing comprehensive understanding of equity financing dynamics.

Debt financing offers several advantages for SMEs while presenting risks that can undermine long-term stability. Ayyagari et al. (2017) conducted comprehensive study across various developing countries using quantitative approach utilizing SME financial statement data, revealing debt financing significantly enhances SME financial flexibility, enabling growth opportunity investments and operational stabilization. Belkhir et al. (2019) investigated debt financing signaling effects in United States using survey data and financial analysis combination, highlighting that SMEs employing debt financing experienced increased investor and creditor interest, improving reputation and facilitating better future financing terms. Bartoli et al. (2018) explored tax advantages in Italy employing mixed-methods approach including financial data analysis and SME manager interviews, finding SMEs benefiting from tax-deductible interest payments had more reinvestment resources available, contributing to stability and competitive positioning.

Informal financing, encompassing funds obtained outside traditional banking systems, plays vital roles in SME financial management and growth. Bagh and Khan (2020) conducted Pakistani study examining informal financing impact on SME growth utilizing quantitative methodology with SME financial data, finding positive correlation between informal financing and firm stability attributed to critical investment funding ability and financial buffer provision during economic downturns. Papadopoulos et al. (2022) investigated informal financing effects on Greek SMEs employing survey and financial performance data combination, finding informal financing positively influenced smaller and slower-growing SME growth by enabling investments in crucial areas such as research and development and operational improvements. Serrasqueiro and Caetano (2016) conducted Portuguese research utilizing surveys and SME manager interviews, finding reinvesting informal source profits into research, product innovation, and operational improvements contributed to firm competitive advantage and growth.

The relationship between informal financing and SME financial growth varies based on several factors. Serrasqueiro and Caetano (2016) found more intricate relationships in Portuguese SMEs, observing informal financing impacts on growth were influenced by company growth stages and strategic goals, with mature, slow-growing SMEs benefiting more than younger, high-growth firms. Al-Najjar and Naser (2023) investigated Jordanian SMEs, revealing while informal financing contributed positively to firm stability, benefits were moderated by external economic conditions and alternative financing option availability. Despite growing literature, significant knowledge gaps remain regarding informal financing impacts on developing economy SMEs. Most existing research focuses on developed countries, with developing markets facing unique challenges including weaker regulatory environments, limited external financing access, and volatile economic conditions. Further research is essential understanding how informal financing affects SME health and growth in diverse settings, aiding effective strategy crafting for policymakers, lenders, and SME owners.

2.3 Conceptual framework

Figure 1 presents the conceptual framework

Independent variables

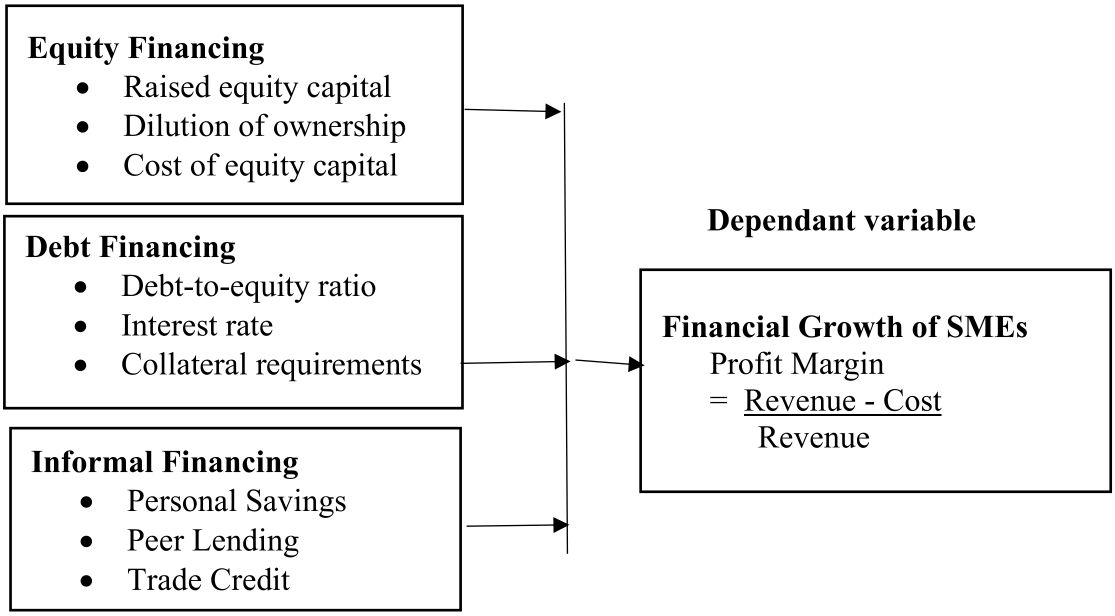

Figure 1: Conceptual Framework

3.0 Research Methodology

This chapter covers methods employed to structure the research process in gathering and analyzing information to address research objectives. Cooper and Schindler (2018) define research design as the configuration of parameters for data collection and analysis with the goal of balancing procedural economy and relevance to the study goal. This research used a descriptive research approach to determine variables influencing SME expansion in Kenya. According to Mugenda and Mugenda (2019), a population refers to an entire group of individuals sharing common observable characteristics. The target population consisted of 213 SME managers or owners in Kirinyaga County. The sampling design utilized purposive sampling, with sample size determined using Yamane formula. For 213 SMEs and 0.05 margin of error, calculated sample size was approximately 139. Questionnaires were utilized to collect primary data from participants (Creswell & Creswell, 2018).

Prior to data collection, research instruments were pilot tested with five SMEs to improve validity and reliability. Reliability test results achieved correlation coefficient of 0.759, indicating instrument reliability. Questionnaires were distributed using Drop and Pick method, where researchers left questionnaires at specified SME locations and returned later to retrieve them (Kothari, 2022). The selected data analysis method was quantitative approach utilizing descriptive statistics. Collected data was carefully reviewed for completeness and clarity, then summarized, edited, classified, coded, and entered for analysis. Diagnostic tests included normality test using Shapiro-Wilk, multicollinearity test using Variance Inflation Factor, and heteroscedasticity test using Breusch-Pagan. Ethical considerations prioritized informed consent, data confidentiality, and voluntary participation to safeguard participants' rights, maintaining cultural sensitivity and preventing harm or exploitation (Yin, 2018; Smith, 2021).

4.0 Research Findings and Discussions

This chapter discusses the study results in subsections according to the research objectives. These sections comprise the response rate, demographic data of participants, results of descriptive analysis, and findings from inferential statistics.

4.1 Response Rate

A total of 139 questionnaires were distributed to all the respondents. Table 1 demonstrates the results.

Table 1: Response Rate

Status of questionnaires	Frequency	Percentage
Returned	121	87.1
Not returned	18	12.9
	139	**100**

Source: Survey Data, 2025

Table 1 results indicate that a response rate of 87.1% was attained, as out of 139 questionnaires distributed, 121 were returned fully completed. The non-response rate stood at 12.9%, representing 18 questionnaires that were not submitted. Orodho (2005) stated that a response rate of no less than 70% can validate the analysis. Therefore, following that guidance, this research proceeded with data analysis to reach conclusions and formulate insights.

4.2 Descriptive Statistics Results

Descriptive statistics on the variables under particular objectives is covered. A 5-point likert scale rated the responses and results displayed using standard deviations and mean. The findings are presented as follows.

4.2.1 Equity Financing

To determine the effect of equity financing on financial growth of small and medium enterprises in Kirinyaga County, Kenya the respondents were required to rate 4 statements according to their level of agreement. The findings obtained are presented in Table 2.

Table 2: Equity Financing

Statements	Mean	Standard Deviation
To what extent has raising equity capital improved the financial growth of your SME?	4.15	0.849
To what extent has the dilution of ownership affected the decision-making power within your SME?	4.62	0.379
To what extent does the cost of equity capital influence the financial stability of your SME?	3.86	1.158
To what extent has the timing of your equity financing affected your SME's stability?	4.53	0.470
Aggregate score	**4.29**	**0.714**

Source: Survey Data, 2025

The results in Table 2 shows that the respondents strongly agreed that the dilution of ownership affected the decision-making power within their SME businesses (M=4.62, SD=0.379) and the timing of your equity financing affected your SME's stability (M=4.53, SD=0.740). These results highlight the importance of understanding the relationship between ownership structure and financial strategies in maintaining effective governance and operational stability in SMEs. The finding agree with Herciu (2017) research observation that equity financing, which entails offering ownership stakes to external investors, has emerged as a promising solution to these challenges. The respondents agreed that raising equity capital improved the financial growth of your SME (M=4.15, SD=0.849) and cost of equity capital influenced the financial stability of your SME (M=3.86, SD=1.158). This finding suggests that both the increase in equity capital and the management of its associated costs are vital for fostering financial health and sustainability in SMEs. The finding is in line with Cumming and Johan (2021) research observation that equity financing significantly enhances financial stability and growth prospects for SMEs.

On average, the respondents agreed that equity financing on financial growth of small and medium enterprises in Kirinyaga County, Kenya as shown by aggregate mean and standard deviation score of 4.29 and 0.714 respectively. The results suggest that there is a strong agreement among the participants regarding the positive impact of equity financing on the financial development of SMEs in the region. The finding is consistent with Bertoni et al. (2020) research results that external investors not only contribute capital but also offer critical managerial expertise and strategic guidance, which are particularly beneficial for high-growth, innovative SMEs.

4.2.2 Debt Financing

To analyze the determine the effect of debt financing on financial growth of small and medium enterprises in Kirinyaga County, Kenya the respondents were required to rate 4 statements according to their level of agreement. The findings obtained are presented in Table 3.

Table 3: Debt Financing

Statements	Mean	Standard Deviation
To what extent does the debt-to-equity ratio of your SME influence its financial growth?	4.05	0.958
To what extent do the interest rates on debt financing impact the financial growth of your SME?	3.87	1.130
To what extent do the collateral requirements for debt financing affect your SME's financial growth?	4.16	0.840
To what extent does the ease of access to credit influence the financial growth of your SME?	3.99	1.089
Aggregate score	**4.02**	**1.004**

Source: Survey Data, 2025

The results in Table 3 show that the respondents agreed that; the debt-to-equity ratio of your SME influence its financial growth (M=4.05, SD=0.958), the interest rates on debt financing impact the financial growth of your SME (M=3.87, SD=1.130), the collateral requirements for debt financing affect your SME's financial growth (M=4.16, SD=0.840) and the ease of access to credit influence the financial growth of your SME (M=3.99, SD=1.089). These findings suggest that all these elements are interconnected and play a vital role in shaping the financial trajectory of SMEs. The finding agrees with Belkhir et al. (2019) who investigated this signaling effect in the United States, utilizing a combination of survey data and financial analysis. Their research highlighted that SMEs employing debt financing experienced increased interest from investors and creditors, thus improving their reputation and facilitating better financing terms in the future.

On average, the respondents agreed that debt financing on financial growth of small and medium enterprises in Kirinyaga County, Kenya as shown by aggregate mean and standard deviation score of 4.02 and 1.004 respectively. The relatively low standard deviation reflects that the opinions of the participants were closely aligned, reinforcing the idea that debt financing is perceived as a vital factor for financial growth among these enterprises. The finding is in line Ayyagari et al. (2017) who conducted a comprehensive study across various developing countries, employing a quantitative approach that utilized data from SME financial statements and their findings revealed that debt financing significantly enhances the financial flexibility of SMEs, enabling them to invest in growth opportunities and stabilize operations.

4.2.3 Informal Financing

To analyze the determine the effect of inflormal financing on financial growth of small and medium enterprises in Kirinyaga County, Kenya the respondents were required to rate 4 statements according to their level of agreement. The findings obtained are presented in Table 4.

Table 4: Informal Financing

Statements	Mean	Standard Deviation
How significant is the role of your personal savings in covering unexpected expenses for your business?	4.52	0.480
To what extent do you believe peer lending has positively impacted your business growth?	3.68	1.320
How significant is trade credit in enabling you to invest in inventory or other business necessities?	4.11	0.889
To what extent do you receive financial assistance from family members to help grow your business?	3.94	1.060
Aggregate score	**4.06**	**0.937**

Source: Survey Data, 2025

The results in Table 4 show that the respondents strongly agreed that: the role of their personal savings in covering unexpected expenses for your business (M=4.52, SD=0.480). The finding is in line Bagh and Khan (2020) who conducted a study in Pakistan examining the impact of informal financing on SME growth and found a positive correlation between informal financing and firm stability. This stability was attributed to the ability of informal financing to fund critical investments and provide a financial buffer during economic downturns. The respondents agreed that; they believe peer lending had positively impacted their business growth (M=3.68, SD=1.320), trade credit in enabling them to invest in inventory or other business necessities (M=4.11, SD=0.889), they received financial assistance from family members to help grow their business (M=3.94, SD=1.060). The finding concur Papadopoulos et al. (2022) who investigated the effects of informal financing on SMEs in Greece. Their findings indicated that informal financing positively influenced the growth of smaller and slower-growing SMEs by enabling them to invest in crucial areas such as research and development and operational improvements. On average, the respondents agreed that informal financing on financial growth of small and medium enterprises in Kirinyaga County, Kenya as shown by aggregate mean and standard deviation score of 4.06 and 0.937 respectively. The finding agrees with Serrasqueiro and Caetano (2016) who conducted research in Portugal, utilizing surveys and interviews with SME managers and found that reinvesting profits from informal sources into research, product innovation, and operational improvements contributed to a firm's competitive advantage and growth.

4.2.4 Financial Growth of SMEs

The study analysed the financial growth of small and medium enterprises in Kirinyaga County, Kenya. The respondents were asked to indicate their average monthly revenue for the years 2019, 2020, 2021, 2022 and 2023. The results are presented in Figure 2.

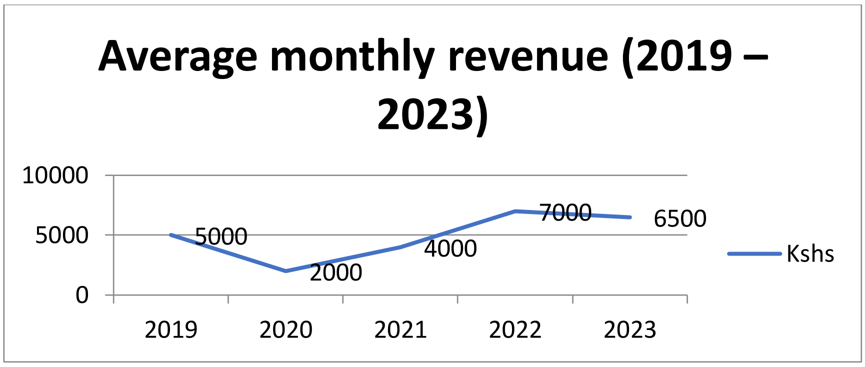

Figure 2: Average monthly revenue (2019 – 2023)

The research findings reveal that the average monthly revenue generated by small and medium-sized enterprises (SMEs) was 5000 Kshs in 2019. This figure saw a decline in 2020, dropping to 2000 Kshs. However, in 2021, there was a recovery, with the average monthly revenue increasing to 4000 Kshs. The upward trend continued in 2022, where the average revenue rose significantly to 7000 Kshs. In 2023, the average monthly revenue slightly decreased to 6500 Kshs. These results suggest a fluctuating yet generally improving financial performance for SMEs over the observed years. The respondents were asked to indicate their primary sources of revenue. The results are presented in Figure 3.

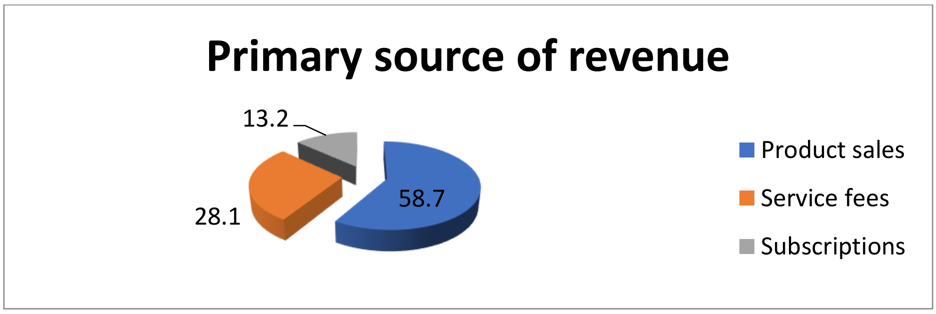

Figure 3: Primary Source of Revenue

Source: Survey Data, 2025

The results indicate that majority 71(58.7%) of the respondents had their primary source of revenue as product sales, 34(28.1%) service fees and 16(13.2%) subscriptions. This distribution of revenue sources suggests that product sales play a dominant role in the financial landscape of the surveyed group, highlighting a potential area for further exploration and emphasis in business strategies.The respondents were asked to indicate how the revenue had changed over the past year. The results are presented in Table 5.

Table 5: Change of Revenue over Time

Change	Frequency	Percentage
Increased significantly	19	15.7
Increased slightly	31	25.6
No change	7	5.8
Decreased slightly	31	25.6
Decreased significantly	33	27.3
	121	**100**

Source: Survey Data, 2025

The results indicate that majority 64(52.9%) of the respondents indicated a decrease in change in revenue over time, 7(5.8%) indicated no change and 50(41.3%) indicated that had increased. However, most of the respondents indicated that there was an increase in change in revenue over time. These findings suggest a clear trend in the data, highlighting the varying experiences of revenue changes among the respondents. The respondents were asked to indicate their average monthly expenses from the year 2019 to 2023. The results are presented in Figure 4

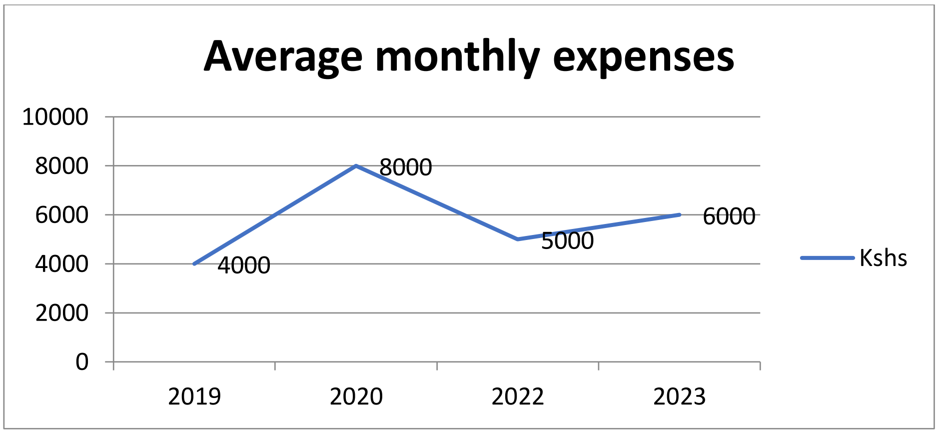

Figure 4: Average Monthly Expenses

Source: Survey Data, 2025

The results regarding the average monthly expenses indicate that in the year 2019 it was 4000 Kshs as indicated by the respondents, 8000 Kshs in the year 2020, 5000 Kshs in the year 2022 and 6000 Kshs in the year 2023. In addition, most of the respondents indicated that Salaries and Wages, Rent/Mortgage, Marketing/Advertising were the most monthly expense These trends suggest that there may be fluctuations in consumer spending habits over the years, possibly influenced by economic conditions or changes in personal financial situations.

4.3 Diagnostic Test Results

The diagnostic test carried out included the normality test, multicollinearity test and heteroscedasticity test.

4.3.1 Normality Test

The normality of the data was confirmed by using the Shapiro-Wilk one sample test. The results are presented in Table 6

Table 6: Normality Test

Variable	Statistic	Sig.
Equity financing	0.594	0.214
Debt financing	0.701	0.152
Informal financing	0.699	0.106
Financial growth	0.723	0.113
Aggregate score	**0.679**	**0.146**

Source: Survey Data, 2025

https://doi.org/10.53819/81018102t5411

The results indicate that the study had an aggregate statistic value of 0.679 and significance value of 0.146. Therefore, it was concluded that there was a normal distribution of data since the significance values were above 0.05.

4.3.2 Multicollinearity Test

The multicollinearity was determined by using Variance Inflation Factor (VIF), as illustrated below. The results are presented in Table 7

Table 7: Multicollinearity Test

	Collinearity Test	
Variable	**Tolerance**	**VIF**
Equity financing	0.442	2.264
Debt financing	0.333	3.001
Informal financing	0.379	2.634
Aggregate score	**0.385**	**2.633**

Source: Survey Data, 2025

The multicollinearity test indicates that the aggregate tolerance value is 0.385 and the aggragate VIF value is 2.633. Therefore, the study concluded that none of the independent variable could suffer from multicollinearity test since every individual variable had a VIF value below 5.

4.3.3 Heteroscedasticity Test

The study used the Breusch-Pagan (1980) test for detecting heteroscedasticity in the data. The results are presented in Table 8.

Table 8: Heteroscedasticity Test

Test	**Statistic**	**Prob.**
Breusch-Pagan LM	211.502	0.003

Source: Survey Data, 2025

The results indicate that the statistics value of 211.502 and significance value of 0.003 which is less than 0.05 justify that the null hypothesis could be rejected.

4.4 Multiple Regression Analysis Results

A regression model was established to provide a clear and interpretable equation that represents the relationship between variables. The model summary, Analysis of Variance (ANOVA) and coefficient results are provided in Table 9, 10 and 11.

Table 9: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.859	0.738	0.702	1.0054

Source: Survey Data, 2025

The results in Table 9 indicate that the coefficient of determination represented by adjusted R-value was 0.702 which means that there was 70.2% proportion of variance in financial growth of small and medium enterprises in Kirinyaga County, Kenya that was due to the effect of equity financing, debt financing and informal financing in the model. Therefore, other variables not included are represented by the remaining percentage (29.8%).

Table 10: Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	201.236	3	67.079	74.642	0.003
	Residual	105.145	117	0.899		
	Total	306.381	120			

Source: Survey Data, 2025

The results in Table 10 indicate that the model meets the following two criteria; Firstly, the statistics F was 74.642 greater than the statistical mean square value (67.079). Secondly, the level of significance is below 0.05 at 0.003. This result indicates the goodness of fit of the study model.

Table 11: Coefficients Analysis

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	0.602	0.301		2	0.003
	Equity financing	0.754	0.185	0.0214	4.076	0.002
	Debt financing	0.779	0.224	0.0165	3.478	0.001
	Informal financing	0.701	0.119	0.0441	5.891	0.004

Source: Survey Data, 2025

The results in Table 11 indicate that the constant value of 0.602 indicate the level of dependent variable by keeping independent variables constant. The results indicates that as you increase equity financing, debt financing and informal financing by one unit respectively, the financial growth of small and medium enterprises in Kirinyaga County, Kenya would increase by 0.754 (75.4%), 0.779(77.9%) and 0.701(70.1) respectively. Hence the final regression equation is expressed as follows;

Financial growth = 0.602 + 0.754(equity financing) + 0.779(debt financing) + 0.701(informal financing)

4.5 Test of Hypotheses

This section shows the results of the hypotheses that were tested.

4.5.1 Equity Financing

$H0_1$. Equity financing has no effect on financial growth of small and medium enterprises in Kirinyaga County, Kenya.

The study found that equity financing had a positive significant influence on the financial growth of small and medium enterprises in Kirinyaga County, Kenya as indicated by (β=0.0214, p=0.002). Therefore, the null hypothesis was rejected. The finding concur with

Cumming and Johan (2021) study which concluded that equity financing positively influences survival rates and financial performance, primarily by providing access to capital and external expertise.

4.5.2 Debt Financing

$H0_2$. Debt financing has no effect on financial growth of small and medium enterprises in Kirinyaga County, Kenya.

The study revealed that debt financing had a positive significant influence on the financial growth of small and medium enterprises in Kirinyaga County, Kenya as indicated by ($\beta=0.0165$, $p=0.001$). This led to the rejection of null hypothesis. The finding is in line with Belkhir et al. (2019) who investigated this signaling effect in the United States, utilizing a combination of survey data and financial analysis. Their research highlighted that SMEs employing debt financing experienced increased interest from investors and creditors, thus improving their reputation and facilitating better financing terms in the future.

4.5.3 Informal Financing

$H0_3$. Informal financing has no effect on financial growth of small and medium enterprises in Kirinyaga County, Kenya

The study established that informal financing had a positive significant influence on the financial growth of small and medium enterprises in Kirinyaga County, Kenya as indicated by ($\beta=0.0441$, $p=0.004$). Therefore, the null hypothesis was rejected. The finding agree with Serrasqueiro and Caetano (2016) who conducted research in Portugal, utilizing surveys and interviews with SME managers and found that reinvesting profits from informal sources into research, product innovation, and operational improvements contributed to a firm's competitive advantage and growth.

5.0 Conclusion of the Study

The study concludes that equity financing provides these businesses with essential capital that can be used for various purposes, such as expanding operations, investing in new technologies, and increasing their market reach. Equity financing allows SMEs to access funds without incurring debt, which can be particularly beneficial in a region where traditional bank loans may be difficult to obtain due to stringent requirements. Furthermore, equity investors often bring valuable expertise and networks that can help SMEs navigate challenges and seize opportunities in the competitive market. The study also concludes that debt financing enables these businesses to invest in expansion, improve their operations, and enhance their competitiveness in the market. The availability of loans and credit facilities allows SMEs to acquire new technologies, hire additional staff, and increase their production capacity, which can lead to higher revenues and profitability. Furthermore, effective management of debt can improve the creditworthiness of these enterprises, making it easier for them to secure future financing. Moreover, the study concludes that informal financing play a crucial role in providing capital to SMEs that struggle to access traditional bank loans due to stringent requirements. Informal financing enhances the liquidity of these businesses, enabling them to invest in growth opportunities, purchase inventory, and cover operational costs. Informal financing can be a lifeline, allowing entrepreneurs to innovate and expand their operations despite limited access to formal financial services.

6.0 Recommendations of the Study

The study recommends that there is need to increased education on the benefits and processes of equity financing to empower entrepreneurs to make informed decisions. Offer training programs that can develop business acumen so as to help entrepreneurs effectively pitch their businesses to potential investors. Focus on establishing networks of investors interested in local SMEs to create a more conducive environment for equity financing opportunities. In addition, the study recommends that there is need to foster environments that simplify access to debt financing for SMEs which may include offering financial literacy programs to help entrepreneurs understand loan agreements and financial management, developing favorable lending terms tailored to the unique challenges faced by small businesses and encouraging partnerships between financial institutions and SMEs to reduce perceived risks. The SMEs should promote the use of technology in the financing process, such as online lending platforms, to streamline applications and approvals, making it easier for SMEs to access funds quickly and efficiently.

The study also recommends that there is need for the County to establish a platform should be for small and medium-sized enterprises (SMEs) to present their business plans and financial requirements to prospective investors and lenders, thereby fostering connections that may result in enhanced financing opportunities. The County ought to offer guarantees or subsidies for loans acquired by SMEs, which would mitigate the risk for lenders and simplify the process for businesses to obtain financing. Additionally, the County should introduce financial literacy initiatives designed to educate SME owners regarding debt financing, assisting them in comprehending the consequences of borrowing and how to proficiently manage their finances to enhance their creditworthiness.

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