ASSET-BASED FINANCE AND FINANCIAL PERFORMANCE OF SMALL AND MEDIUM SIZE MANUFACTURING ENTERPRISES IN NAIROBI CITY COUNTY, KENYA

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ABSTRACT

There has been reduced financial performance witnessed within the manufacturing Small and Medium Enterprises sector despite the effort put in place by the government. Financial performance of manufacturing Small and Medium Enterprises in Kenya has reduced in the last five years leading to decline in the sector's growth. The aim of the research was to establish the effect of asset-based formal finance on financial performance of manufacturing Small and Medium Enterprises in Nairobi City County, Kenya. The study used pecking order. Positivist research philosophy guided the research. Explanatory research design was used with a population of 188 manufacturing Small and Medium Enterprises who registered as new members with Kenya Association of Manufacturers in the year 2021. The sample consisted of 128 managers generated through Yamane sampling formula. Stratified random sampling was adopted to group Small and Medium Enterprises managers in different categories whereas purposive sampling aided the selection of managers. Closed and open-ended questionnaires assisted in data collection. Pilot study was done in Kiambu County with 10% of the sample. Content, internal and external validity were used to determine the instrument's validity while Cronbach's alpha aided in reliability analysis with acceptable cut-off value of 0.7. Descriptive, correlational and multiple regression were the techniques used in data analysis. Normality, homoscedasticity and test of direct effects were done. Findings were presented using tables, pie charts and graphs. Findings revealed that asset-based finance had a significant positive effect on the financial performance of manufacturing Small and Medium Enterprises in Nairobi City County. The research concluded that asset based formal finance is vital to boosting financial performance for Nairobi's manufacturing Small and Medium Enterprises. The study recommended that manufacturing enterprises should consider adopting asset-based finance to enhance their financial performance. Future studies may be done in other geographical locations.

Key words: Asset-based Finance, Financial Performance, Small and Medium Enterprises.

INTRODUCTION

Background of Study

Global manufacturing Small and Medium Size Enterprises (SMEs) sector presents tremendous contribution to national economic growth with 80% of global trade emanating from SME manufactured products (Wall, 2021). The sector drives job growth, fuels GDP, supports industry, meets local demand, fosters innovation, and supplies inputs to larger firms (Adeyeye, 2016). However, manufacturing SMEs continue to face challenges that have stagnated their growth where 80% to 90% of SMEs fail in less than 10 years with majority having less than 5% of return on assets (Cheruiyot, 2019).

The manufacturing Small and Medium Enterprises is critical in Kenya's Vision 2030 contributing 14% of Gross Domestic Product and employment creation. However, its productivity and performance have reduced due to low management capacity and retention of qualified staff (Kering, Kilika, & Njuguna, 2020). Additionally, Cheruiyot (2019) observes how due to poor financial performance evidenced in the Kenyan manufacturing Small and Medium Enterprises, majority of the businesses fail in their first years of operation where only a small number manage to record 20% yearly return on equity. The Kenya Association of Manufacturers (2021) has also revealed a declining trend in financial performance within the sector coming from 9.3% in 2016 to 7.6% in 2020 with reduced employment from 315,100 in the year 2016 coming down to 293,800 in 2020.

Asset Based Finance

Asset-based finance is any borrowing that is related to an organizational asset where the loan is granted to an Small and Medium Enterprise to secure the use of machinery, equipment and other capital assets in exchange for regular payment to the financial institution. Small and Medium Enterprises may also secure asset finance by using existing assets as collateral for loans advanced. However, this depends on the business prospects and credit worthiness of the business (Corporate Finance Institute, 2023).

There is evidence that Small and Medium Enterprises accessing asset formal finance can help capture new opportunities, obtain more income, maintain resiliency and access to markets. It is also noted that Bangladesh women entrepreneurs within the agricultural sector increased their income by 37% through acquisition of cows as assets (Mattern, 2020). Asset finance has further been categorized into;

Purchase order financing which is an instrument provided by financial institution to Small and Medium Enterprises who lack funds to pay their suppliers or where sellers may need capital in advance while at the same time, extending payment to their buyers.

Purchase order financing is widely used among manufacturing Small and Medium Enterprises with high sales growth. The instrument allows the businesses to access capital which may not be available through other lending instruments due to lack of information.

Trade credit is a critical asset based formal finance which has been used by manufactuing Small and Medium Enterprises in the developed and developing countries to finance business operations. Through trade credit, manufacturing Small and Medium Enterprises may access supplies needed to meet their customer demands, achieve reduced transaction costs as well as promote Small and Medium Enterprises growth where 74% of small and medium businesses agreed that trade credit promotes their growth while 60% indicates how trade credit enhances sales growth and hence financial performance (Jepkorir & Gichure, 2019).

Financial Perormance

Financial performance is the measurement of how well manufacturing Small and Medium Enterprises are taking advantage of primary assets to generate revenue (Mwangi, 2016). Financial performance demonstrates an organization's financial condition in a given period of time evidenced in how the organization is collecting and using its funds (Fatihudin, Jusni, & Mochklas, 2018).

Financial performance is a detailed analysis and evaluation of the financial health of an Small and Medium Enterprise (Podhorska & Siekelova, 2020) and the determination of an organization's achievement in a given time period with an aim of obtaining information concerning the movement of fund, how it was used, its efficiency and effectiveness. The feedback may be used by the management in decision making regarding growth and expansion of the business (Batching, 2017). In the last five years, the manufacturing sector performance has not been impressive evidenced in slow growth rate and reduced number of employment. This has been attributed to Covid 19 effects, inefficiency in production, reduced access to credit facilities, obsolete technology and counterfeit products ((Kingi & Opiyo, 2021). The reduced performance in Gross Domestic Product and employment have impacts on the manufacturing financial performance where a total of 34 manufacturing SMEs have closed their operations (Prosper, 2020). Table 1. presented the trend in the sector's growth rate and employment between 2016 to 2020 (Okeyo, 2022).

Table 1.Manufacturing SMEs Five Year Performance

Item	2016	2017	2018	2019	2020
GDP	9.3	8.7	8.4	7.9	7.6
Employment	300.9	343.9	347.9	353.3	316.9

Source: Okeyo (2022)

From Table 1, manufacturing SMEs' GDP has been declining from 2016 registering 9.3% and coming down to 7.6% in 2020. There has also been unsteady growth in employment seen in 2016 where employment was 300.9, increasing upto 353.3 and coming down to 316.9 in 2020.

Small & Medium Size Manufacturing Enterprises in Nairobi City County

Manufacturing Small and Medium Enterprises in Kenya are categorized by their small size, limited resources, and over reliance on manual labor. They operate in various sub-sectors such as food processing, textiles, chemicals, machinery, and electronics. Manufacturing Small and Medium Enterprises in Kenya carry out vital obligation in the expansion of the economy of Kenya through creation of employment opportunities, wealth generation, poverty eradication and utilization of resources. The overall manufacturing sector in Kenya has an estimate of 1.5 million people employed in the industry (Kenya National Bureau of Statistics, 2018) with 7.5% GDP contribution (Kenya Association of Manufacturers, 2020). In the year 2020, the sector employed a total of 3 million by 2020 (Prosper Africa, 2020).

According to the Kenya National Bureau of Statistics (2020), the food and beverages sub-sector which include processing of fruits, vegetables, dairy products, beverages, and other food items accounted for the largest share of manufacturing sales in 2019, contributing approximately Ksh 1.2 trillion. The textiles and apparel sub-sector taking part in textile production, garment manufacturing, and associated accessories generated sales worth Ksh 85 billion. The chemical manufacturers which include the production of pharmaceuticals, fertilizers, paints, soaps, detergents, and other chemical-based products recorded sales of Ksh 200 billion in 2019 (Kenya National Bureau of Statistics, 2020). Despite their performance, manufacturing companies in Kenya, are reportedly experiencing financial constraints.

In the recent years, according to a report by Kenya Association of Manufacturers (2020), many manufacturing companies have closed down their businesses with others relocating to other countries. The surviving manufacturers have also tried to cut on operational cost by reducing the number of employees and minimizing their manufacturing capacity. The industry is faced with several major challenges which limit their financial performance; high cost of production such as raw materials, energy and labor (Institute of Economic Affairs, 2018). According to the Kenya National Bureau of Statistics, the cost of energy alone accounts for approximately 25% of total production costs. Other challenges are related with financial limitation where banks and other financial institutions require collateral and other forms of security before providing loans to the manufacturers. This becomes an obstacle for SMEs that lack necessary assets to secure funding and therefore limiting their performance (Nyakundi, 2021).

Statement of the Problem

The manufacturing Small and Medium Enterprises is recognized in the government's Vision 2030 and its Big Four Agenda as an enabler of Kenya's industrialization and development of the country (Kenya Association of Manufacturers, 2022). Its financial performance is therefore key for the realization of the government's objectives. However, the sector's financial performance has been dwindling evidenced in the analysis of a five-year trend between 2016 to 2020 where GDP growth and employment have been on a decline trend coming from 9.3% to 7.6% in 2020 with

employment reduction leading to closure of 34 manufacturing Small and Medium Enterprises (Okeyo, 2022).

Previous studies showed that manufacturing Small and Medium Enterprises were failing due to lack of capital and the government advocated for the provision of formal finance to the Manufacturing Small and Medium Enterprises for sustainable financial performance and growth. However as more and more manufacturing Small and Medium Enterprises access asset-based formal finance, they do not live beyond three years. This research sought to establish the effect of asset-based formal finance on financial performance of small and medium manufacturing enterprises in Nairobi City County, Kenya.

Objectives of the Study

The study aimed to establish the effect of asset-based formal finance on financial performance of small and medium size manufacturing enterprises in Nairobi City County, Kenya.

Research Hypotheses

H_{01}: Asset-based formal finance has no significant effect on the financial performance of small and medium size manufacturing enterprises in Nairobi City County, Kenya.

Theoretical Review

Pecking Order Theory

Myers and Majluf (1984) proposed pecking order theory to explain how firms prefer internal financing to external based on reduced cost in financing. It is one of the most recognized theories within corporate finance suggesting that firms do not finance their deficit given the current level of debt but rather preference to internal funding more than external. This means that due to information asymmetry, manufacturing Small and Medium Enterprises do not have a pre-determined preference for debt over equity but are conservative when it comes to dividend payment where debt can be used for maximization of firm value (Jibran et al., 2012).

Due to information asymmetry, the managers have more information about financial status of the firm as compared to investors, thereby following a certain order when looking for alternative sources of finance such as financing of projects with retained earnings, profit from internal finance, short term securities, debt, preferred stock, common stocks and equity. Myers and Majluf (1984) add that manufacturing Small and Medium Enterprises preference will be internal finance even though they may adjust their dividend payout to match with the investment opportunities. Should a firm seek external financing because of dynamics in profitability, advantageous dividend policies, or any other investment opportunities, manufacturing Small and Medium Enterprises may seek instruments that are secure, go for hybrid solutions such as convertible bonds or choose equity as the last option. This indicates that manufacturing Small and Medium Enterprises will go for external financing due to experienced shortage with internal financing (Gunarsih, 2011).

Pecking order theory has proved that firms will first use their internal financing before sourcing for external funding. However, the order has been disapproved by Mina and Lahr (2018) study on the investigation of pecking order of innovation finance that looked at high growth firms arguing that innovation reduces information asymmetry due to uncertainty that surrounds innovation outcome. Additionally, should projects fail, it becomes difficult to sell intellectual property and skills as well as there is no guarantee on sales returns of new product developed (Hall, 2010). In this situation, it becomes difficult to evaluate R&D, hence the information gap which hinders supply of external capital. This means that there is no standard pecking order theory among high growth manufacturing Small and Medium Enterprises as there is more preference to external equity financing over internal financing (Mina & Lahr, 2018). Pecking order theory was to analyse the asset-based formal finance to determine the order of preference by manufacturing SMEs according to financial needs.

Empirical Review

Oluwabunmi and Abiola (2021) investigated how trade credit affected financial performance of Small and Medium Enterprises in Nigeria targeting 300 businesses in Ekiti state. The study adopted multistage sampling to identify and group respondents from rural and urban areas. It was found that cost of trade credit affected manufacturing Small and Medium Enterprises' performance even though there was no significant effect. It was concluded that Nigerian manufacturing SMEs do not rely on asset-based formal finance through trade credit. The research was conducted in both rural and urban regions of Nigeria. This research was conducted in a distinct geographical location. Sindani (2018) used mixed method research design targeting 5401 Small and Medium Enterprises in Kakamega to determine the influence of accounts receivable and Small and Medium Enterprise growth. The study distributed the participants into 12 strata according to the wards in Kakamega County. Krijcie and Morgan (1970) sample selection technique was used to derive 359 Small and Medium Enterprises. Purposive sampling was used to identify participants while Likert scale with 5-point rating was used in questionnaire development. The study found that 38.1% of Small and Medium Enterprises used invoice discounting while 58% indicated that they were using accounts receivables as security for the loan. It was established that 57.5% of manufacturing SMEs were using formal finance for invoice factoring accounts receivable. The study adopted purposive sampling to identify respondents which could lead to biasness. The current study considered random sampling that reduced biasness.

Warunyua (2018) did a study on the effect of asset-based formal finance and loan portfolio performance in commercial banks in Kenya examining the period between 2012 and 2016. Working with quantitative correlational study design, the study targeted 43 commercial banks using secondary data from Central Bank of Kenya to determine total loans offered and their values. Descriptive analysis was used with presentation in mean, mode, range and standard deviation. The results showed a moderate link between firm size and loan performance, with asset-based finance explaining 22.7% of its variation. The study's limitation was the use of secondary data only as it

did not incorporate primary data to validate the findings. The study as well, did not incorporate demographic studies of the participants as well as not indicating who the participants from 43 commercial banks were. The current study employed the use of primary data that improved the quality of the findings. Demographic data was analysed to understand the distribution of study population thereby enriching the findings.

Kimathi (2017) investigated the influence of asset-based formal finance solutions on the growth of manufacturing Small and Medium Enterprises in Nairobi. A causal research design was employed to determine the cause-effect relationship using a target population of 4120 manufacturing SMEs. The population was grouped into strata; Agro-based, chemical and mining, engineering and construction where two staged sampling was used that involved stratification of sampling and systematic random sampling leading to a final sample of 92. The findings indicated that manufacturing Small and Medium Enterprises could not access purchase order formal finance as they were not affordable to enhance their financial performance. It was also found that LPO influenced Small and Medium Enterprise growth due to technology adoption that enhanced access of formal finance. Cheque discounting was found to be accessible to Small and Medium Enterprises especially by engineering and construction manufacturers. The study used growth as the outcome variable while financial performance was used in the present research as the outcome variable.

RESEARCH METHODOLOGY

The research was guided by a positivism research paradigm using quantitative method. The philosophy guided the researcher to be objective based on the belief that there are facts which were found through observing participants and collecting primary and secondary data to confirm the truth.

The study used explanatory research design to investigate cause and effect relationship between the study variables (Miller and Ross, 2020). The design was chosen due to its flexibility and incorporation of other research methods.

The study targeted 188 manufacturing Small and Medium Enterprise managers affiliated with the Kenya Manufacturers Association. The report provided a list comprising of ten different sectors of manufacturing; food and beverage, textile and apparel, leather and footwear, agro processing, metal and allied, motor vehicle and accessories, paper and paperboard, plastics and rubber, timber, wood and furniture, pharmaceutical and medical equipment (Kenya Association of Manufacturers, 2023).

Probability sampling was chosen to incorporate all the members in the study and to minimize sampling error and biasness (Adwok, 2015).

The study applied multiple linear regression to determine how asset-based formal finance connects with SME financial performance in Nairobi. The study modified the model to fit the current study as indicated in the following equation:

$Y=a + B_1X_1 + \varepsilon$

Y= Financial performance

X_1= asset-based finance

e= error term

a= Constant variable

The researcher collected primary data using questionnaires Likert scale question format was used to capture respondent's attitude where the scale was 5 for very high rating and 1 for very low rating. The questions were made simple and easy to understand to increase participation rate of respondents. All questions were arranged sequentially to allow smooth flow and interactivity.

The study employed both quantitative and qualitative data analysis where descriptive, correlation, multiple regression and content analysis were used (Flick, 2013).

The researcher performed the normality test, homoscedasticity test and test for direct effect.

Descriptive Statistics

Asset Based Formal Finance and Financial Performance

Asset-based formal finance was the first objective of the research used to ascertain its influence on financial performance. Asset based formal finance is a debt that is covered by collaterals such as inventory, property or payment receivables. Manufacturing Small and Medium Enterprises qualify for formal finance based on their assets. These assets are used to meet immediate cash flow needs for short term periods; payment of wages, running costs and expansion (San, 2019). Asset-based formal finance was assessed using trade credit, invoice factoring, and purchase order finance, with results shown in Table 2.

Table 2. Asset Based Formal Finance

Asset based finance	N	Min	Max	Mean	Std. D
Purchase order finance is convenient for my business due to its affordability.	105	2	5	3.61	0.84
Purchase order finance has enhanced my SMEs borrowing capacity to acquire needed capital.	105	2	5	3.53	0.93
Trade credit finance has given my business opportunity to fulfill order requirements.	105	1	5	3.46	1.23
Trade credit has enhanced the supply of raw materials I need for my business.	105	2	5	3.51	0.89
Invoice factoring has enhanced my SME cash flow.	105	2	5	3.63	1.06

Asset based finance has enhanced my SME financial performance.	105	1	5	3.13	1.23
Total	**105**			**3.48**	**1.03**

Source: Research (2024)

As shown in Table 2, respondents rated purchase order finance as affordable and convenient, averaging 3.61 (SD = 0.84). This shows that some respondents agreed while others did not agree with the statement. However, asset based formal finance was considered affordable in supporting manufacturing Small and Medium Enterprises meet their daily business operations that improved financial performance. Equally, it was found that purchase order finance was enhancing Small and Medium Enterprises borrowing capacity to acquire needed capital with a mean of 3.53, variation of 0.93. This demonstrated that manufacturing Small and Medium Enterprises had more opportunity through their existing assets to acquire capital they needed for their business operation thereby realizing financial performance.

Additionally, it was established that trade credit finance had given Small and Medium Enterprises the opportunity to fulfill order requirements with mean rating of 3.46, variation of 1.23. The results demonstrated that trade credit had enhanced the supply of raw materials that Small and Medium Enterprises needed in running the business with a mean score of 3.51 and a variation of 0.89. The revelation indicates that manufacturing Small and Medium Enterprises could use trade credit to fulfill order requirements while sourcing for needed raw materials to boost their business through asset-based formal finance and hence improved financial performance.

The findings indicated that invoice factoring had enhanced Small and Medium Enterprises' cash flow with a rating of 3.63 mean and standard deviation of 1.06 which shows that high number of respondents agreed as compared to those who disagreed to the statement. Respondents reported that asset-based finance improved Small and Medium Enterprise performance, averaging 3.13 with a 1.23 deviation. The results showed that purchase order finance and trade credit were preferred as it helped Small and Medium Enterprises to meet capital requirements, and the supply of raw materials thus enhanced their financial performance. Overall mean score for asset based formal finance was 3.48, variation of 1.03 which suggested that respondents took a neutral perspective on whether asset based formal finance enhanced financial performance of manufacturing Small and Medium Enterprises in Nairobi City County.

Financial Performance

Financial performance consists of benefits derived from business activities (Muhammad, 2014) which shows how well and effective the business is in generating wealth from investments made (Benard, 2014). The study measured financial performance as the dependent variable using; changes in sales and profits as exhibited in Table 3.

Table 3. Financial Performance

Financial Performance	N	Min	Max	Mean	Std. Dev
My business has increased sales in the last three years.	105	1	5	3.01	1.37
There is increased sales due to new products the business has developed.	105	1	5	3.50	1.36
There is increased sales in the last three years due to new markets.	105	1	5	3.02	1.49
My business is highly profitable hence able to meet immediate operational needs.	105	1	5	2.84	1.42
My business has maintained profitability in the last three years.	105	1	5	3.02	1.43
There is improved business performance in the last three years.	105	1	5	2.72	1.31
Total	**105**			**3.02**	**1.39**

Source: Research (2024)

The results indicated a neutral agreement from respondents that Small and Medium Enterprise business had increased sales in the past three years with a mean of 3.01, variation of 1.37. This showed that Small and Medium Enterprises have not been able to increase their sales in the last three years. It was found that respondents agreed that there were increased sales due to new products the business had developed with a mean of 3.5, variation of 1.36. The results showed that there was agreement among respondents that manufacturing Small and Medium Enterprises had introduced new products which enhanced their financial performance.

There was a mean rating of 3.02, a variation of 1.49 to the statement that there are increased sales in the last three years because of new markets. The findings demonstrate that manufacturing businesses have not enhanced their sales from new markets in the last three years. Respondents agreed that the business was highly profitable hence were able to meet immediate operational needs with a mean of 3.84, and a variation of 1.42. This showed that despite reduced sales in the last three years, respondents were able to achieve high profits that could enable them to access asset-based formal finance they needed to improve their financial performance. Respondents remained neutral that the business had maintained profitability in the past three years with a mean of 3.02, variation of 1.43. The revelation indicates that despite achieving profitability, maintaining it for three years was proving challenging to the sector, hence having impacts on financial performance. It was established that respondents disagreed that there was improved business performance in the past three years with a mean of 2.72, variation of 1.31. The aggregate mean score was 3.02, variation of 1.39 which suggested that respondents were neutral that there was

financial performance among manufacturing Small and Medium Enterprises in Nairobi City County.

Normality Test

The researcher employed Shapiro-Wilk test to determine normality as indicated in Table 4.

Table 4. Normality Test

Variables	Shapiro-Wilk statistic	df	Sig
Asset Based Finance	0.931	105	0.280
Financial Performance	0.936	105	0.329

Source: Research (2024)

From Table 4, the results demonstrate that all the variables had Shapiro Wilk statistics that had p values above 0.05. The study upheld the null hypothesis since both variables met normality, with p-values below 0.05. The results allowed the researcher to use linear regression model as there was no violation in the assumption.

Homoscedasticity Test

homoscedasticity is a regression analysis problem which may have impact on test procedures and estimation. The study used Breusch-Pagan test to detect heteroscedasticity (Abdul-Hamed & Matani, 2021). The null hypothesis was rejected when the p values was <0.05 which indicated presence of homoscedasticity (Martin, 2023). The findings were exhibited in Table 5.

Table 5. Homoscedasticity Test

Variable	Chi-Square	df	P-Value
Asset Based Formal Finance	3.13	1	0.077
Financial Performance	1.69	1	0.194

Source: Research (2024)

From the Breush-Pagan test, the null hypothesis was homoscedasticity while alternative hypothesis was presence of heteroscedasticity. From the results, all the variables had p values >0.05 hence rejection of the null hypothesis as there was homoscedasticity.

Test for Direct Effect

The study analysed how the asset-based affected financial performance. Asset-based formal finance is a specific asset, a line of credit, loan or conditional sales contract (Powell, 2020). It is a form of lending backed by inventories, land, payment receivables or facilities which are used as collaterals to the borrower's obligation of payment during the period of the contract (San, 2019). Table 6 shows how asset-based formal finance was assessed for its impact on financial performance among Nairobi's manufacturing Small and Medium Enterprises.

Table 6. Effect of Asset Based Formal Finance on Financial Performance

	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	6.419	3.179		2.019	0.046
Asset based	0.579	0.160	0.335	3.613	0.000
R-Square	0.112				
F-Statistic	13.056				
P-value	.000				

Source: Research (2024)

From the results in Table 6, asset based formal finance R Square was 0.112 which showed that asset based accounted for 11.2% of the changes of financial performance of manufacturing Small and Medium Enterprises in Nairobi City County. The findings further showed that F-statistics was 13.056 p value 0.000 which signified that there was a difference in the mean of asset based in predicting financial performance. The coefficient value showed that under constant circumstances, financial performance would go up by 6.419. However, the introduction of asset based formal finance would lead to rise in financial performance 0.579 significantly (p=0.000).

San (2019) recognizes how asset-based formal finance is less costly, easier and faster and may be used by organizations to meet short-term objectives. The current results demonstrate that asse-based formal finance significantly enhances financial performance of manufacturing Small and Medium Enterprises in Nairobi City County as it is easier to access in comparison to other formal finance. Ndung'u et al., (2020) found that asset-based securities influenced Kenyan commercial bank's financial performance which agrees with the current findings. Pavlovna et al. (2023) added that Russian SMEs were using asset-based formal finance to procure goods with conclusion that it could help in developing objective market condition which ultimately enhances organization's profitability.

This study established that manufacturing SMEs are using purchase order finance due to its affordability. Additionally, Small and Medium Enterprises are using invoice factoring and trade credits as asset-based formal finance which enhance financial performance. Wilcky et al. (2022) found that asset-backed formal finance positively influenced financial performance among Ugandan Small and Medium Enterprises. From previous studies, there is an agreement from different organizations and geographical location that asset-based formal finance enhances financial performance despite the different target population.

Hypothesis Testing

The hypothesis was tested using regression method. The decision on hypothesis was made as presented in Table 7.

Table 7. Hypothesis Testing

Hypothesis	Statement	Decision Reject H_0, Fail to Reject H_0
H_{01}	Asset based formal finance has no significant effect on the financial performance of small and medium size manufacturing enterprises in Nairobi City County.	Reject H_0

Source: Research (2024)

Conclusion and Recommendation

Conclusion

The objective of the study was to determine the effect of asset-based formal finance on the financial performance of small and medium size manufacturing enterprises in Nairobi City County, Kenya. The study concluded that Small and Medium Enterprises use purchase order finance due to its affordability. It is concluded that purchase order finance is used by manufacturing Small and Medium Enterprises to expand their borrowing capacity hence convenient in the acquisition of finance needed to expand their business for more financial performance. The study concluded that invoice factoring has enhanced cash flow of manufacturing Small and Medium Enterprises. It is concluded that trade credit enables Small and Medium Enterprises to meet supply demand for enhanced financial performance. The study concluded that asset-based formal finance has a weak yet positive link to financial performance, and still plays a meaningful role in supporting Nairobi's manufacturing Small and Medium Enterprises.

Recommendation for Policy

The study generates knowledge on the challenges Small and Medium Enterprises experience in accessing asset based formal finance due to documentation requirement for NSE. Policy makers may need to consider engaging with manufacturing stakeholders to develop friendly policies to allow more Small and Medium Enterprises manufacturing get registered with NSE and access asset-based formal finance. Policy makers may also consider creating an environment that will allow free market as well as a make a stable fiscal policy to enhance financial performance of the sector.

The study recommends that Small and Medium Enterprises should work with the Association of Kenya Manufacturing to engage more with the government to identify possible areas for policy improvement. This will enhance a stable environment as well as enable the development of policies that contribute to enhanced financial performance of the sector.

Recommendations for Practice

The managers should explore potential opportunities that come with initial public offers and venture capital to enable more access to affordable capital for enhancement of financial performance.

Pecking order theory demonstrates the different options organizations have and the decisions made according to Small and Medium Enterprise's needs. The study contributes to the understanding of

short-term alternatives such purchase order, trade credit and invoice factoring as formal finance solutions that may be adopted by the Small and Medium Enterprise manufacturing sector to enhance financial performance. The study provides knowledge on the status of Small and Medium Enterprises manufacturing within the venture capital which is an avenue that may be adopted to secure equity for purposes of enhancing financial performance. The study has contributed in gaining knowledge on how innovation may help Small and Medium Enterprise manufacturing sector to tap into new opportunities to enhance their financial performance. Future scholars may use the findings to advance research topics within finance.

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