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Abstract

Prior studies on small and medium-sized entreprises (SMEs) have focused on a number of aspects for instance, the challenges affecting SMEs among other aspects. The present study shifted focus and sought to establish the determinants of SMEs' ability in doing business with large corporations in Nairobi County in Kenya. The determinants examined included: financial performance, capacity enhancement, access to finance and corporate governance. The study targeted a stratified sample of 114 SMEs located within Nairobi. Primary data were analysed using factor analysis and OLS regression. The study established that a number of SMEs do business with large corporations, the main source of the interaction being perception of improved business performance. In terms of the determinants, the study established that the key determinants influencing SMEs' engagement with large corporations included capacity enhancement, access to finance and corporate governance. The study established that enabling SMEs to engage in business with large corproations is one of the ways of helping them upscale and transition into medium and even large status.

Key words: Financial Performance, Capacity Enhancement, Access To Finance, Corporate Governance

Introduction

Small and medium-sized enterprises (SMEs) play an important role in the Kenyan Economy (Atieno, 2009). According to the Economic Survey (2016), the SME sector contributed over 50 percent of new jobs created in the year 2015. The Survey shows that SMEs represent more than 90% of the private sector where they employ between 40% to 63% of the private labor force. Despite their significance, past statistics indicate that three out of five SMEs fail within the first few months of operation (Bowen, Morara & Mureithi, 2009). Subsequently, SMEs contribute less than 40% to the Gross National Product (GDP). This is largely because, SMEs are concentrated in less profitable, less capital-intensive and low-tech sectors, and they pay relatively lower wages and the production per employee is lower compared to the large businesses.

Although the SME sector is steadily growing, their ability in doing business with large corporations is constrained as it accounts for only 15 percent of the success in the SMEs sector (Olive, 2010). This phenomenon has presented a real challenge to SMEs in terms of upscaling into large scale enterprises. Prior studies show that when small companies interact with large corporations, there are gains such as improved organizational structures, management practices, and operations (Hallberg, 2010). These changes enable small companies to upgrade their technologies, access finance, improve their governance, and most importantly, become financially stable. As a result, revenue streams grow, and are more consistent, making it possible for the small businesses to create more employment. Further, up scaling into a large corporation opens doors to easier credit and other business opportunities (Schiffer & Weder 2001). Other gains include spillover of new knowledge, innovation and business models (Smallbone & Welter 2001). When a few small businesses improve their systems or business models, other small businesses learn from that and work to remain competitive, boosting the quality of the entire SME sector (McCormick & Pedersen, 2009).

Despite the importance of SMEs contribution to the economy of Kenya, an anlysis of the the determinants of SMEs' ability to engage in business with large corporations has not attracted adequate attention researchwise. This is evident by the dearth of extant literature on this important subject. Most studies have focused on developed economies, while those studies examining the interactions between SMEs and large corporations are quite scanty. Most of these studies focus solely on SMEs or large corporations. Therefore, there exists a gap in literature with respect to what determines an SMEs' ability to do business with large corporation and the perceived benefits. Therefore, the current study sought to explore the determinants of SMEs' ability to do business with large corporations in Nairobi County in Kenya. Nairobi was selected as it has been argued to be a leading financial hub with the East African region. The specific objectives examined in this study included:

- To establish how financial performance affects SMEs ability in doing business with larger corporations.
- To ascertain the contribution of capacity enhancement in SMEs ability in doing business with larger corporations.
- To determine the influence of access to finance on SMEs' ability to do business with larger corporations, and
- To find out the influence of corporate governance on SMEs' ability to do business with larger corporations.

Empirical Literature Review

Financial Performance on SMEs

According to Pandey (2012) getting on top of financial measures of your performance is an important part of running a growing business, especially in the current economic climate. SMEs success depends on developing and implementing sound financial and management systems. Many businesses fail because of poor financial management or planning (Peter, 2010). Shi (2004) shows that small firms consistently report higher growth obstacles than medium-size or large firms. Sakai (2002) show that size, age and ownership are the most reliable predictors of firms financing obstacles. Sakai (2002) found out that older, larger and foreign-owned firms report lower financing obstacles. The relationship is not only statistically but also economically significant.

In another study, Feakins (2005) posits that the probability that a small firm lists financing as a major obstacle (as opposed to moderate, minor or no obstacle) is 39% compared to 36% for medium-size firms and 32% for large firms. The higher financing obstacles that small firms report match not only anecdotal evidence from both developed and developing countries, they also confirm theory's predictions (Feakins, 2005). Hellberg (2010) questions whether higher financing obstacles that small firms report actually constrain their growth or the SMEs find ways around the obstacles. Barr (2009) found that the higher obstacles faced by smaller firms indeed translate into slower growth. Small firms thus do not only report facing higher growth obstacles, these higher obstacles are also more constraining for their operation and growth than in the case of medium-size and large firms (Battat & Frank, 2006).

Financial measures of performance can be referred to as the results of a firms' operations in monetary terms (Barrow, 2010). Financial measures of performance are derived from the accounts of a firm or can be found in the firm's profit and loss statement or the balance sheet. Financial measures are also referred to as objective measures because they can be individually measured and verified (Barrow, 2010). Well known financial measures includ:

(i) Return on Assets (ROA): Bhunia (2009) suggests that the return on assets (ROA) is used as a vital measure of profitability. The ROA provides information about how much profits are generated, on average, by each unit of the assets of the firm (Juan & Martinez 2009). In addition, Petersen and Schoeman (2008) note that ROA can be measured suing the equation, ROA = Net Profit after Tax ÷ Total Assets. This suggests that ROA is an indicator of how efficiently a firm is utilising its assets to generate profits.

(ii) Profitability Growth: This is the growth in the profits of a firm over time. Profitability growth can also refer to the continuous increase in the financial profit after all expenses have been paid over a given period on time (Brau & Woller 2004). An increase in the profitability of a firm is an objective measure of performance as it shows that the firm's financial performance is continuously improving.

(iii) Sales growth: This refers to an increase in sales over a specific period of time, usually but not always annually. Cohen (2009) suggests that if there is one measure of SME performance that could be used then it has to be sales growth. Sales growth is a measure of organic growth within the business (Maksimovic, 2005; Beck & Demirguc-Kunt, 2006; North et al., 2008; Torre et al., 2010).

The financial soundness is one of the major weaknesses of SME - large corporation relationship. SMEs face challenges to access external financial resources, which in turn limit their investment in developing new products, upgrading existing production, and capturing emerging business opportunities. This eats into their profits, as a result, the slowed or stagnated financial performance. Governments can reduce financial constraints on SMEs through encouraging supply chain finance, which covers receivables financing, physical asset collateralization, risk-mitigation products, securitization, and guarantee instruments, among others (Vuong, 2008).

Capacity Enhancement on SMEs

Contractual relationships between smaller and larger firms may arise in a number of ways: (i) as a result of a broadening of a supply chain relationship; (ii) as an alternative to acquisition or merger; or, (iii) as a new collaborative alliance. Therefore, the key issue with any capacity building exercise is the resources anticipated to be devoted into it and the likely results of such an investment in skill-building (Mansor & Mat, (2010). This situation is exacerbated where technical, legal and market resources are unevenly distributed or even scare (Villa & Bruno, 2013). Once way of dealing with the moral hazar in capacity enhancement include the adoption of explicit contractual requirements and more implicit or formal agreements (Watkins 2009). This reflects evidence of the importance of trust and continuity of personnel in the broader success of the management of SF-LF relationships in the SME. Other approaches include monitoring the performance or "value-add" of the capacity enhancement exercise (Bayona-Saez, 2011).

Mattsson & Wallenberg (2003) states that an interesting national initiative to promote contractual network relations among small firms or between small and larger firms is the Italian Business Network Contract Law introduced in 2009. This allows the legal establishment of network relationships between companies based on a common innovation programme, a common project fund and exit and closure rules. Li (2005) states that commentary on the Italian Law, however, suggests that ambiguities in the legislation may be undermining its effectiveness, and some research suggests that contracts are being used simply to formalise existing informal relationships. Use of the statute also seems to be stronger among larger firms perhaps due to the lack of legal resources or expertise in smaller firms. Contracts through larger suppliers tend to be very one sided and require significant negotiation from a legal and a commercial perspective (Atrill, 2008).

Access to Finance on SMEs

All business ventures regardless of size require finances from inception and throughout their life cycles. The amount invested will influence greatly the size of the venture, which in turn determines the early survival of an enterprise if other factors are held constant. The entrepreneur will require seed capital to start the business, to operate and manage the business enterprise. McMahon & Holmes (2008) notes that unavailability or lack of information about alternative sources of finances and inability of SMEs to evaluate financing option were some of the major problems facing the SMEs.

McMahon (2008) singles out lack of access to finances as the main bottleneck facing MSE growth which was similarly echoed by Florida et al. (1996) and Livard Pang (2006) who found that start-up capital is a barrier to entry in most entrepreneurial activities and that lack of capital was cited by 80% of all respondents as the greatest start-up problem. Finding start-up finance for the business is the biggest hurdle that many entrepreneurs go through. Even after getting started, getting sufficient finance to sustain business growth is another problem. Research findings by McCormick et al. (2006), Daniels et al. (2003) Kinyanjui (2006) show how SMEs are constrained by finance. Studies undertaken by Kiiru, Mirero and Masaviro (1988) for Kenya Rural Enterprise Programme (K-Rep) confirm that a major constraint within the small business enterprise sector is financing.

Most studies (e.g., Vuong, 2008; Wanjohi, 2008; Chijoriga & Cassiman, 1997) point to finance as one of the key constraints to small enterprise growth. This is worsened by the absence of financial markets in the developing countries. Small enterprise owners cannot easily access finance to expand business and they are usually faced with problems of collateral, feasibility studies and the unexplained bank charges. This means that they cannot access finance to enable them to grow. Vuong (2008) makes a detailed analysis of finance as a constraining factor and includes collateral, interest rates, extra bank charges, inability to evaluate financial proposals and lack of financial management skills as hindrances to small enterprise success in doing business with large corporations. Therefore this study sought to establish how access to finances influences the ability of SMEs in doing business with large corporations in Nairobi county Kenya.

Corporate Governance on SMEs

Cooley and Pullen (2009) observe that effective SMEs management is of great importance for SMEs in doing business with large corporations and therefore the need for good governance that will steer the business for prosperity and thus avoid strategic failures. The elements that underpin a firm's ability to engage in effective corporate governance, and implement new regulatory changes include leadership, accountablity, culture ,systems and structure. each element relates to the others. For example, organizational culture is shaped by leadership practices. Systems support organizational structure and shape its culture.

Weak governance mechanisms in SMEs have raised concerns about the stewardship and transparency of SMEs managers and the board (Olando, 2013). According to Sile (2009), most SMEs do not comply with the requirement of having their financial statements audited, and they are not always available on a periodic basis. The failure to provide audited annual reports by SMEs on a timely basis curtails transparency and weakens the governance mechanisms of SMEs. Alukwe (2015) found a significant relationship between governance and regulation compliance. The study by Srairi and Douissa (2014) point out thatboard should ensure that the business complies with all relevant laws, regulations, governance practices, accounting and auditing standards. Yeh (2012) asserted that good corporate governance as manifested in the structure of the boardroom and ownership, is effective in improving the quality of reporting. Rouf (2011) established that governance characteristics such as board size, leadership and audit committees had a significant and positive influence on voluntary disclosure. Board transparency has also been found to have a significant influence on disclosure levels, with more transparent boards providing relatively more disclosure. Hence, this study sought to establish how governance influences SMEs ability in doing business with large corporations in Nairobi county Kenya.

Results And Discussions

SME engagement with Large Corporations

The study established that 46% of the SMEs have not engaged with large corporations while 54% had engaged businesses with large corporations in the past 1 year. The study revealed that 19.3% of the SMEs had dealt with government, 37.3% with private and local large corporations, 13.3% private and international large corporations, 19.3% with multinationals, and 10.8% with NGOs.

The study revealed that 19% of the SMEs had dealt with less than 3 large corporations since establishment, 13% with 4-6 large corporations, 28% with 7-9 corporations and 40% with over 40 corporations. The findings of the study indicated that 4.8% of the respondents developed relationship with large corporations through networks, existing customers and good reputations respectively; 13.3% through perceived financial gains, 12% through relationship management; 10.8% through tender; 12%

through supply chain and subcontractor respectively; 8.4 % as suppliers, customers and consultant respectively.

Financial Performance on SMEs

The study revealed that 19.3% of the SMEs had less 1 million Kenya Shillings (Kshs) as sales volume in a year, 6% had Kshs. 1-5 million, 30.1% had Kshs. 5-10 million and 44.6% had more than Kshs. 10 million. The findings of the indicated that 15.7% of the SMEs generated less than Kshs. 1 million in net profit annually, 2.4% generated Kshs. 1-5 million, 32.5% generated Kshs. 5-10 million and 49.4% generated more than Kshs. 10 million in net profits every year. The study revealed that 45% of the SMEs were not profitable while 55% were profitable.

The findings of the study on sales revenue of the business, the mean was 2.6506 with a standard deviation of 1.2919. On customer base/number of customers; the mean was 2.5301 with standard deviation of 1.1825. On the number of employees in the business; the mean was 2.1566 with a standard devaiton of 1.1943. On the uniqueness of the product/service provided; the mean was 1.6988 with a standard deviation of 0.92043. On high quality products/services; the mean was 2.3976 with a standard deviation of 1.4728. On Profitability of the business the mean was 4.3735 with standard deviation of 0.99647. On the value of the assets/ investments owned by the business; the mean was 4.3614 with standard deviation of 1.0190.

Capacity Enhancement on SMEs

The study revealed that 16.9% of the respondents had submitted less than 1 proposal, 2-5 proposals and 6-10 proposals per quarter of a year respectively; 9.6% had submitted 6-10 proposals, 15.7% had submitted 11-15 proposals while 12% had submitted 16-20 and over 20 proposals respectively. The study further established that 10.8% of the SMEs had certificate of registration and PIN Certificate respectively; 20.5% had tax compliance certificate and credit reference bureau clearance respectively, 19.3% had CR12 check which indicates the company directors and shareholders while 18.1% had certificate of good conduct (for owners/directors)

The study established that on handling large contracts; the mean was 2.6506 with a standard deviation of 1.29194. On licensing agreements; the mean was 2.5301 with standard deviation of 1.18257. On too many forms required to be filled for bidding purposes; the mean was 2.1566 with standard deviation of 1.19432. On lack of know how to run some of the business affairs; the mean was 1.6988 with standard deviation of 0.92043. Regarding the lack of external assistance of plans for entrepreneurs; the mean was 2.3976 with standard deviation of 1.47284. On perception that the job opportunity at hand is not meant for you, since it is difficult ; the mean was 4.3735 with standard deviation of 0.99647. On lack of access from new firm to new research and technology as large firm; the mean was 2.5301 with standard deviation of 1.18257.

Access to Finance Capabilities on SMEs

Majority of the respondents indicated that intial capital was tricky to raise although loans from SACCOs and other finacial institutions helped in driving the start up. It was also established that friends gave out donations besides the owners themselves chipping in in terms of owners' equity. The study found out that 47% of the respondents had not applied for loans from financial institutions while 53% had applied for loans. The study established that 19.3% of the respondents fund their investments through bank loans, 6 % through personal funds, 30.1% through friends and 44.6% through family and relatives. This implies that SMEs have wider range of sources of funds for driving their investments.

The findings of the study on the level of external financing; the mean was 4.2735 with standard deviation of 0.99647 and this implies that respondents agreed on the statement. On regulatory factors; the mean was 4.3614 with standard deviation of 1.01907 and this means that respondents agreed on the statement. Regarding the compliance of the business with regulatory requirements; the mean was 3.6024 with standard deviation of 1.49748 and this means that respondents agreed on the statement. On registration status of the business – whether registered or not; the mean was 2.6386 with standard deviation of 1.30270. On lack of cheap funding to finance potential projects; the mean was 2.5542 with standard deviation of 1.10711 and this means that respondents were not sure on the statement. On the inability to obtain short-term financial capital (working capital finance); the mean was 2.3735 with standard deviation of 1.25631.

Corporate Governance on SMEs

The findings of the study indicated that 51.8% of the SMEs had board of directors while 48.2% did not have board of directors. Majority of the respondents also indicated that their boards consist of 5-8 members and this is convenient. The study revealed that 20.5% of the businesses were in a start up, 36.1% were doingly poorly, 13.3% were doing well, 19.3% were doing very well and 10.8% were winding up.The findings of the study on embezzlement of funds by those charged with governance/owners; the mean was 4.3614 with standard deviation of 1.01907 which implies that respondents agreed on the statement. On mismanagement of the business; the mean was 3.6024 with standard deviation of 1.49748 and this means that rspendents agreed on the statement. On the lack of integrity by board members; the mean was 2.6386 with standard deviation of 1.30270 which implies that respondents were not sure on the statement. On domination of the business by a few individuals; the 2.5542 with standard deviation of 1.10711. On family wrangles; the mean was 2.3735 with a mean of 1.25631. On wrangles within the management and the board, the mean was 2.1446 with standard deviation 1.17008. On lack of transparency in the business; the mean was 2.6506 with standard deviation of 1.29194. On unethical business conduct the mean was 2.5301 with standard deviation of 1.18257. On lack of board/key owner's ability/acumen to win business opportunities; the mean was 2.1566 with standard devition of 1.19432. Regarding the choice of business opportunities that have proved costly or not viable/profitable; the mean was 1.6988 with standard deviation of 0.92043. On lack of information by key owners of available business opportunities; the mean was 2.3976 with standard deviation of 1.47284. The study also established that only 57% of the SMEs had audited books of accounts.

Regression Analysis

The researcher conducted a multiple regression analysis to determine the determinants of SMEs in doing business with large corporations in Nairobi County, Kenya. From Regression analysis, the p-values of capacity enhancement, access to finances and corporate governance are 0.049, 0.007 and 0.001 respectively which are all less than 0.05 and therefore they were statistically significant.

Table 1: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
	0.3441[a]	0.1184	0.0731	3.0626

From the Model Summary in Table 1 the value of R is 0.3441, R square is 0.1184 while adjusted R square is 0.0731. This implies that 11.84% of the variations in determinants of SMEs are explained by their ability to do businesses with large corporations.

Table 2: ANOVA

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	98.270	4	24.5675	2.6191	.011[b]
Residual	731.609	78	9.380		
Total	829.879	82			

From the ANOVA statistics of the processed data at 0.05 level of significance, the value of F calculated is 2.6191 while F critical (from F-tables) is 2.48888596. Since the value of F calculated is greater than F critical at 0.05 level of signficant, this implies that the overal regression model was significant.

Table 3: Regression Coefficients

Dependent variable:	***SMEs ability to do business with large corporations (1,0)***				
Model	**Unstandardized Coefficients**		**Standardized Coefficients**	**t-statistic**	**Sig.**
	B	**Std. Error**	**Beta**		
(Constant)	17.624***	2.510		7.021	0.000
Financial Performance	0.042	0.366	0.046	0.114	0.909
Capacity Enhancement	-0.128**	0.281	-0.148	-0.457	0.049
Access to Finances	-0.259***	0.094	-0.299	-2.754	0.007
Corporate Governance	0.045***	0.148	0.075	0.305	0.001

***, **, and *, significant at the 1%, 5% and 10% levels respectively.

From the regression coefficient Table, the following regression model is developed:

$Y = 17.624 + 0.042X_1 - 0.128X_2 - 0.259X_3 + 0.045X_4$

Where Y = SMEs' ability in doing business with large corporations

X_1= Financial performance; X_2 = Capacity Enhancement; X_3 = Access to finance; X_4 = Corporate Governance and e = Error

This means that when all the variables are held constant, SMEs doing business with large corporations would be at 17.624. A unit increase in financial performance of SMEs holding other variables constant would increase their ability to do business with large corporations by 0.042; a unit decrease in capacity enhancement holding other variable constant would affect the ability of SMEs to do business with large corporations by 0.128; a unit decrease in access to finances would affect the ability of SMEs to do business with large corporations by 0.259 and a unit increase in corporate governance would increase the ability of SMEs to do business with large corporations by 0.045. The p values of capacity enhancement, access to finances and corporate governance are 0.049, 0.007 and 0.001 respectively which are all less than 0.05 and therefore they were statistically significant.

This implied that capacity enhancement, access to finances and corporate governance affects SMEs in doing business with large corporations to a great extent. Limited capacity capabilities makes SMEs less aware of opportunities in the market. The findings concurred with Mattsson & Wallenberg (2003) who found that SMEs face difficulties accessing markets due to limited market information, poor marketing capacity and poor market research leading to a discrepancy between the supply and demand . From the regression results in Table 4.19 access to finances, the study found that limited finances significantly affected SMEs ability in doing business with large corporations ($r= -.259$, $p=0.007<0.05$). the findings concurred with McMahon (2008) singled out lack of access to finances as the main bottleneck facing SMEs growth. This clearly indicated that inaccessibility of funds, unimproved capacity capabilities and poor corporate governence constrained the small and medium enterprises in doing business with large corporations.

Conclusion

This study sought to investigate what determines an SME's ability to engage in business with large corporations. The study found that majority of the SMEs in Kenya conduct businesses with large corporations mostly the private and local large corporations and have dealt with over 10 large corporations. The study also found that SMEs mostly develop relationships with large corporations through perceived financial gains. The studies further found that majority of SMEs were not profitable enough despite generation of large sales revenue and profitability. The uniqueness of the product/service provided by SMEs is an important financial factor that large corporations consider when carrying out business with SMEs, followed by number of employees in the business and then high quality products/services. The study established that most of the SMEs were compliant to legal requirements especially tax payment. The study revealed that the perception that the job opportunity at hand is not meant for the SME is an important factor that large corporations consider when transacting with SMEs, followed by the ability of SMEs to handle large contracts, licensing agreements and lack of access from new firm to new research and technology as large firm. The regression analyses revealed that there was a statistically significant association between capacity enhancement, access to finances, and corporate governance in relation to the ability of SMEs to do business with large corporations in Kenya.

Recommendations for the Study

The study recommends that all SMEs in Kenya should work on developing good working relationships with large corporations which shall enable them to do businesses. The study also recommends that SMEs in Kenya should strive to enhance their profitability by increasing their cash flow streams. There is also a need to for SMEs to offer unique product/service; increase their employee numbers and offer high quality products to their customers. The study further recommends that SMEs in Kenya should be involved in tendering businesses to grow their profits. SMEs need to be compliant to laws and regulations. SMEs should also increase their ability to handle large contracts, licensing agreements and their accessibilty to new research and technology. The study recommends that SMEs should actively take up loans from financial institutions to fund their operations. SMEs should increase their level of external financing and the compliance of the business with regulatory requirements so as to enhance the level of their undertaking of business with large corporations. The study recommends that all SMEs in Kenya should put in boards of directors to oversee their operations and make important decisions. There is need to for SMEs to train their employees and the staff on ethical values to avoid embezzlement of funds. Finally, SMEs should employ qualified external auditors to examine their books of accounts.

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