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Koech, E. J., & Maronge, M.

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INFLUENCE OF INTEREST RATE CAPPING ON GROWTH OF SMALL AND MEDIUM ENTERPRISES NAIROBI COUNTY, KENYA

Koech, E. J.,[*1] & Moronge, M.[2]

[*1] Msc Scholar, Jomo Kenyatta University of Agriculture & Technology [JKUAT], Nairobi, Kenya

[2] PhD., Jomo Kenyatta University of Agriculture & Technology [JKUAT], Nairobi, Kenya

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ABSTRACT

The study sought to investigate the influence of interest rate capping in Small and Medium Enterprises. The research design was descriptive. The target population of interest for the study was from the Nairobi County. The study was based on a target population of 4560 SMEs. Statistical Package for Social Science (SPSS) was used to analyse the data. Based on the study results of the ANOVA Test or F-test in obtained F-count (calculated) value was 33.370. This was greater than the F-critical (table) value (23.418) with significance of 0.000. Since the significance level of 0.001< 0.05 we concluded that the set of independent variables influence the growth of SMEs in the study area.The study revealed that interest rate capping statistically, strongly and significantly correlated to growth of the SMEs as they had a positive relationship with the dependent variable. Therefore, from these quantitative results it was deduced that the study which sought to establish the influence of interest rate capping on growth of SMEs was achieved because it established that it influenced growth of SMEs. The role of credit is basically to bridge the gap between business owner's financial assets and the required financial assets of the business/enterprise. There is need to remove that imbalance between the two hence creating the demand for credit. From the perspective of borrowers, lower rates can increase the potential demand for loans and financial inclusion, while excessive rates can push borrowers into over-indebtedness. The bank credit and bank deposits are very closely related with each other that they represent, roughly speaking, two sides of the same coin, the balance sheets of banks. The lending activity is made possible only if the banks can mobilize enough funds from their customers. The banks face repricing risk if either the average yield on its assets or that on its liabilities is more sensitive to changes in market interest rates. Such a difference in sensitivity could reflect a number of possible mismatches in the characteristics of assets and liabilities. The interest rates ceiling is a key economic aspects that impact the economic growth in the SMEs. The need to regulate the interest charged on credit or any other financial instrument should be founded on the necessity to control economic patterns that has great influence to the SMEs. Controlling and setting of interest rates has huge fiscal implication to the economic development hence the need for rational decision making process within the banking industry to enhance growth of SMES.

Key Words: *Credit Products, Customer Deposits, Bank Interest Risks, Interest Rate Ceiling*

INTRODUCTION

One common form of Government financial control is the use of caps on interests' rate with the major motive of supporting a specific industry or sector where market failure exists or greater concentration of financial resources is required. Thus interest rate caps may be a useful mechanism for providing short-term credit to a strategic industry. (Bekaer, Harvey, and Lundblad 2001).Several countries after the financial crisis of 2008 introduced interest rate controls as a tool for consumer protection with El Salvador (2012), the Kyrgyz Republic (2013), and Zambia (2013) introducing fresh interest rate caps on loans while Japan have imposed more restrictive caps.

Interest rate caps can be further justified as a mechanism to protect consumers from exploitation by guaranteeing access to credit at reasonable interest rates and to facilitate prosecution of exploitative and deceptive lenders. They can also help protect the public interest by ensuring a fair and reasonable interest rate on loans; it may also be a good way to limit access to credit to some impaired and low-income consumers. Others argue that in countries where financial institutions have high market power limiting the price of credit can be justified to protect consumers. In fact, empirical evidence shows that interest caps on loans were successful in the Republic of Korea for the period 1956–94 and that financial liberalization did not significantly help increase financial depth. (Demitriades & Luintel 2001).

Arguments against the use of interest rate caps are that they are an inefficient tool for lowering interest rates, especially in the long run. They also limit access to credit, reduce transparency, and decrease product diversity and competition. In addition, they could undercut the demand for formal credit and affect firms' productivity. Moreover, because interest rate caps distort the market and generate adverse selection, financial entities tend to lend to clients with higher collateral, thereby creating inefficiencies in financial intermediation. Consequently, financial institutions curtail their lending to those who need it most and have little access to alternative sources of credit (Miller 2013).Even though financial institutions can remain profitable in the presence of interest rate caps, such restrictions may reduce investments in new markets. In extreme cases where ceilings are set at unprofitable levels, banks and microfinance institutions may withdraw from certain locales such as rural areas or from expensive market segments because they cannot cover their costs. In some cases, then, low-income borrowers with few options for borrowing in the formal market could turn to unlicensed moneylenders, probably at a higher interest rate.

Finally, according to some evidence, interest rate caps on loans discourage microfinance nongovernmental organizations (NGOs) and other sources of finance for the poor from converting into licensed financial institutions (Helms and Reille 2004). Caps that are set too low and caps that are set too high are both problematic. In countries where the caps do not cover fees and commissions and when the definition of interest rate is not clear, for example, financial institutions may give the impression of compliance with the ceiling but charge fees and commissions that are not considered part of the cost of the loan. Some also argue that in the opposite case, when caps are not set too low, interest rates will still tend to rise toward the caps (Helms and Reille 2004; Miller 2013; and OFT 2010) In light of all the above arguments for and against interest rate caps, this project paper seeks to examine the influence of Interest rate capping on growth of SMEs in Kenya- a case of Nairobi County.

In Japan, France and Germany, caps on interest rates saw financial institutions avoid lending to high-risk borrowers such as people in low-income areas. This in effect reversed the main aim of helping more people have access to credit. It also opened the door for informal lending avenues which in most cases exploit consumers. This is likely to affect job seekers, who would wish to get into business, as they are considered high-risk borrowers due to their limited sources of income. In some cases, banks and financial institutions withdrew from low-income areas and this further curtailed access to credit facilities. The main argument was that the interest rates became too low and this made operations in low-income areas unsustainable. Banks and other financial institutions also avoided investing in areas considered unprofitable

Government borrowing remains substantially high in Kenya further exacerbating the high inter-est rate problem. In an auction conducted recently for the 10 year bond, the government accepted 70% of the bids at an average rate of 15.267%. This implies how desperate the government is for financing. Would it then not be only sensible to conclude that banks will revert to lending to the government which is desperately in need of cash, and avoid the risky private sector as much as possible? According to 2015 stats, government domestic debt accelerated 156.5% y/y to KES 524.1B, accounting for 18.8% of total credit while private sector credit grew 18.0% to KES 2.2T to account for 79.6% of total credit. Of course as banks divert most of their assets to government securities, the government will be spoilt for choice which may see rates decline like they did in the first half of the year.

In the Kenyan economy, most of small-scale enterprises are operated within the informal sector which covers all semi-organized and unregulated economic activities that are small scale in terms of employment. It's economic contribution is more than double that of medium and large enterprise sectors that stands at 7% of the country's GDP (CBS-GoK, 2013). The sector therefore is a major source of demand for credit, employment and income to many households in Kenya.

There are various definitions of an SME. According to Sessional Paper No. 2 (2005) an SME is defined as an enterprise with between 1 to 50 employees, the World Bank defines an SME as one that fits to either of the following criteria that is to say: (1) A formally registered business (2) with an annual turnover of between Kenya Shillings 8 to 100 million (3) an asset base of at least Kenya Shillings 4 million and (5) employing between 5 to 150 employees. The MSME Bill 2011 has used 2 criteria to define SMEs in general that is: (a) the number of people/employees and (b) the company's annual turnover. For enterprises in the manufacturing sector, the definition takes into account the investment in plant and machinery as well as the registered capital.

Statement of the Problem

Mcloughlin (2013) states that for some time, policymakers have been concerned about the effects of the seemingly high interest rates typically charged by financial institutions lending money to SMEs Available data indicates that interest rates typically fall between 20 per cent and 50 per cent per year in places where inflation runs no higher than 10 per cent per year). It has been argued that such interest rates can erode surpluses generated by SMEs, leaving them with little net gain. There is also concern that high rates reduce the demand for and uptake of financial services. As Dehejia, Montgomery and Morduch (2012) point out, where these effects are seen, high interest rates can undermine the original intention of the push for growth of SMEs

Whilst there exist a number of studies on interest rate capping (Karlan and Champion 2012), the researcher notes that there are still knowledge gaps that need to be addressed. First, the studies have mainly established the effect of interest rate capping on the consumer behavior of individual consumers and not access to credit among small and medium enterprises. Cooper (2012), in his study indicated that SMEs in Nairobi depend on financing for growth. Muthoka (2012) also found that SMEs benefit from loans from microfinance institutions, and they seek financial assistance from the MFIs due to ease of access, easy loan repayment and amount offered. Munene (2009) found out credit bureaus enabled the lenders assess credit worthiness, ability to pay back a loan, and this affects the interest rate and other terms of a loan. In Kenya, most SMEs use credit to finance their operations. According to Mwindi (2002), higher amounts of credit granted to SMEs are charged higher levels of interest rates but enable them to meet more of their planned operations. This results in higher profitability to the MSEs hence a positive relationship exists between the interest rates charged by Lenders and the growth of MSEs. It is therefore evident that the above mentioned local studies had focused more on the impact of microfinance on growth and performance of SMEs in Kenya. However no study had been done to investigate the influence of interest rate capping on growth of SMEs in Nairobi County.

Research Objectives

The general objective of the study was to establish the influence of interest rate capping on growth of small and medium enterprises in Nairobi City County, Kenya. The specific objectives were;

- To determine how bank credit products influence growth of small and medium enterprises in Nairobi County, Kenya
- To establish the effects of customer deposits on growth of small and medium enterprises in Nairobi County, Kenya
- To determine the extent of bank interest risks on growth of small and medium enterprises in Nairobi County, Kenya
- To find out how bank interest rate ceiling influence growth of small and medium enterprises in Nairobi County, Kenya

LITERATURE REVIEW

Theoretical Review

The Classical Theory of Interest

Interest, in real terms, is the reward for the productive use of capital, which is equal to the marginal productivity of physical capital. In a money economy, however, as physical capital is purchased with monetary funds, the rate of interest is taken to be the annual rate of return over money capital invested in physical capital assets (Gorder 2009). According to Keynes, true classical theory of interest rate is the savings investment theory. Basically, the theory holds the proposition based on the general equilibrium theory that the rate of interest is determined by the intersection of the demand for and supply of capital. (Caplan 2000) argued that an equilibrium rate of interest is determined at a point at which the demand for capital equals its supply.

Demand for capital stems from investment decisions of the entrepreneur class. Investment demand schedule, thus, reflects the demand for capital, while the supply of capital results from savings in the community. Savings schedule, thus, represents the supply of capital. It follows that savings and investment are the two real factors determining the rate of interest (Fredman, 1991). The implication of the theory, different banks have different liquidate, if what stated in the theory is true high liquid bank should charge low interest rate on funds lend in order to attract more

borrowers and interest rate on savings should be low in order to discourage savings or if it charges the same rate as other banks on money borrowed then interest rate on saving should remain very low. If that is true interest rate spread on highly liquid banks should be comparatively more than low liquid banks. Financial performance on comparatively high liquid bank should be better than low liquid bank (Rochon & Vernengo 2001).

Loanable Funds Theory

The Theory assumes that interest rates are determined by supply of loanable funds and demand for credit. The loanable funds theory is an attempt to improve upon the classical theory of interest. It recognizes that money can play a disturbing role in the saving and investment processes and thereby causes variations in the level of income. Thus, it is a monetary approach to the theory of interest, as distinguished from that of the classical economists. In fact, the loanable funds theory synthesizes both the monetary and non-monetary aspects of the problem (Wensheng, Wung and Shu, 2002). According to the loanable funds theory, the rate of interest is the price that equates the demand for and supply of loanable funds. At the equilibrium level where demand =supply of loanable funds savers and investors are the happiest possible. Fluctuations in the rate of interest arise from variations either in the demand for loans or in the supply of loans or credit funds available for lending.Ngugi (2001) argued that interest is the price that equates the demand for loanable funds with the supply of loanable funds.

Loanable funds are "the sums of money supplied and demanded at any time in the money market." The supply of 'credit' or funds available for lending would be influenced by the savings of the people and the additions to the money supply (usually through credit creation by banks) during that period. The demand side of the loanable funds, on the other hand, would be determined by the demand for investment plus the demand for hoarding money (Turnovsky, 1985). Loanable fund theory has implication on banks savers and borrowers according to this theory, these two groups should be well compensated at equilibrium. According to this theory interest rate spread should not be very wide where one party feel exploited. Interest rate should be structured in a way every party feel comfortable. (Gorder 2009)

Liquidity Preference Theory

Liquidity preference theory asserts that economic units have a preference for liquidity over investing. Applying this theory explains the premium offered in forward rates in comparison to expected future spot rates. This premium is used as payment for the use of scarce liquid resources. The preference for liquidity can be accounted for by the fact that economic units need to hold certain levels of liquid assets for purchase of goods and services and the fact that these near term future expenditures can be difficult to predict. Liquidity theory is limited by its short-term nature, the assumptions that income remains stable, and, like classical theory, only supply and demand for money are considered(Gorder 2009).

The Rational Expectations Theory

This is based on the idea that people formulate expectations based on all the information that is available in the market. Rational expectation theory holds that the best estimation for future interest rates is the current spot rate and that changes in interest rates are primarily due to unexpected information or changes in economic factors. The rational expectations theory can be incorporated with the loanable funds theory in order to better consider the available information within the economy. The limiting factors of rational expectation theory are mostly related to the

difficulty in gathering information and understanding how the public uses its information to form its expectations (Caplan 2000). If expectation of the people is that interest will rise many people will avoid borrowing this in return will affect bank performance due to reduced earning on interest rate, but people expect interest rate to drop people would be willing to borrow and this will improve banks performance due to increase in interest rate earning (Swain 2002).

Conceptual Framework

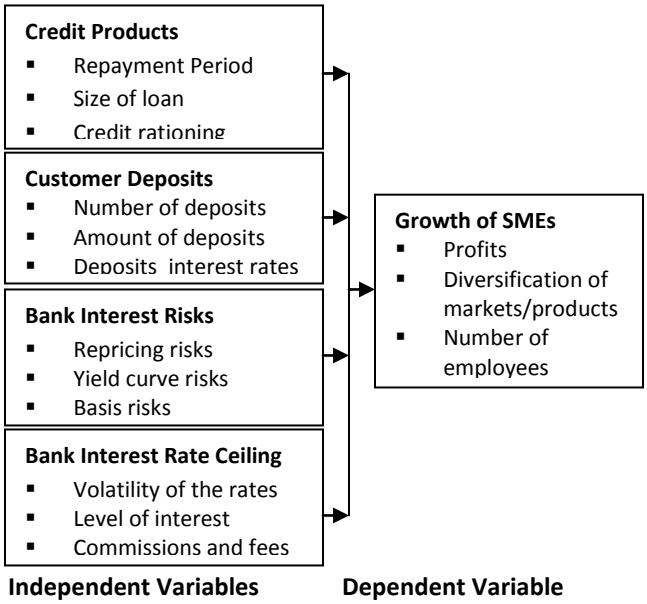

Figure 1: Conceptual Framework

Credit Products

The role of credit is basically to bridge the gap between business owner's financial assets and the required financial assets of the business. Usually there is an imbalance between the two hence creating the demand for credit. From the perspective of borrowers, lower rates can increase the potential demand for loans and financial inclusion, while excessive rates can push borrowers into over-indebtedness. From the perspective of financial institutions (FIs), lower rates can make them more dependent on "donors" while high rates can lead to higher regulatory scrutiny and attract the worst borrowers (adverse selection). The question around fair rates is therefore key to policymakers and FIs (Zachary, 2012).

The financial institutions have repayment periods of weekly and monthly depending on the size of the loan, lending rules and how one agrees with other members of the group ran by the micro-finance institution, who jointly act as guarantors of the loan. Moreover, since most of the loans offered by the institutions do not have grace period, borrowers start servicing the loans as soon as they receive them. There are many forms of loans in the market. The aim is to diversify credit facilities for different sectors of the economy and customize them to fit the intended users. However, as was the case for Germany and France, caps on interest rates may lead to a decline in the number of credit products available to consumers. This limits access to credit and innovation. Although it is still early to tell how the cap on bank interest rates will affect the Kenyan consumer, empirical evidence as indicated shows that in most cases, the outcomes are negative. This may or may not be the case for Kenya. As much as employers and job seekers are likely to benefit from the lower interest rates, we cannot tell for a fact what the outcome will be.

Customer Deposits

Commercial banks as well as the sector in general do depend on customer's deposit to advance its clients. According to Sharma (2009), the bank credit and bank deposits are very closely related with each other that they represent, roughly speaking, two sides of the same coin, the balance sheets of banks. With regard to the question whether loans make deposits or deposits make loans, two kinds of answers have been given for the puzzle. Banks, the world over, thrive on their ability to generate income through their lending activities.

The lending activity is made possible only if the banks can mobilize enough funds from their customers. Since commercial banks depend on depositor's money as a source of funds, it means that there are some relationships between the ability of the banks to mobilize deposits and the amount of credit granted to the customers. Thus, the main function of financial institutions of mobilizing funds from the surplus economic agents to the deficit economic agents is put to test in order to generate economic growth. However, the efficiency of performing this function depends on the level of development of the financial system. The finance literature provides support for the argument that countries with better/efficient financial systems grow faster, while inefficient financial systems bear the risk of bank failure. (Kasekende, 2008). Mohan (2012), Mobilization of deposits is one of the important functions of banking business. It is an important source of working fund for the bank. Deposit mobilization is an indispensable act or to increase the sources of the banks to serve effectively. Mobilization of deposit plays an important role in providing satisfactory service to different sectors of the economy. The success of the banking greatly lies on the deposit mobilization

Bank Interest Risks

Olweny (2011) argued that interest rate risks can also come in a variety of forms, including repricing risk, yield curve risk and basis risk. A bank will face repricing risk if either the average yield on its assets or that on its liabilities is more sensitive to changes in market interest rates. Such a difference in sensitivity could reflect a number of possible mismatches in the characteristics of assets and liabilities. First, fixed rate assets and liabilities could have different maturities. Second, floating rate assets and liabilities could have different repricing periods, with base rates that have maturities similar to their respective repricing periods (assets that reprice annually based on a one-year rate and liabilities that reprice quarterly based on a three-month rate, for example). Third, floating rate assets and liabilities could have base rates of different maturities (assets that reprice annually based on a long-term rate along with liabilities that reprice annually based on a one-year rate, for example). Fourth, in many countries there are assets and liabilities for which banks can adjust pricing at will (e.g. savings deposits and some types of retail loans) and the rate-setting policies that banks follow determine the effective repricing behaviour of such instruments. The pricing decisions in these cases will presumably depend on a variety of factors in addition to market interest rates, including the expected behaviour of bank customers and the extent of competition in the markets concerned. Finally, in some cases, bank customers have the option either to repay loans or withdraw their deposits at low (or no) cost, and the decisions of such customers will influence the response of the average pricing of such assets or liabilities to changes in market interest rates

Interest Rate Ceiling

The interest rates ceiling is a key economic aspects that impact the economic growth in a country. Corb (2012) explained that interest rate ceiling is a key fiscal tool used by CBK to regulate inflation and enhance economic growth. Regulation of inflation or deflation in Kenya is a role assigned to the Central Bank by the government. The need to regulate the interest charged on credit or any other financial instrument is founded on the necessity to control economic patterns that has great effects to the economy. Controlling and setting of interest rates has huge fiscal implication to the economic development hence the need for rational decision making process within the industry.

Many countries have established interest rate ceilings to protect consumers from unscrupulous lenders. Governments often also face political or cultural pressure to keep interest rates low. A study by Lydia, (2012) revealed that interest rate capping in Germany and France led to a high degree of exclusion from small loans for SMEs in these countries and created a market for illegal lending. According to Kihimbo (2012) capping interest rates in Kenya might solve the high interest rate spreads in the banking sector but will lead to other challenges such as, locking out of SMEs and other "high risk" borrowers from accessing credit as banks will prefer to loan to the government as was experienced in 2016.

Straining small banks who effectively have been shut out from the interbank market and now have to mobilise funds at rates higher than what they are getting now and can only lend out within the stipulated margins. Furthermore it is based on an unreasonable premise that the highest extra risk premium in the Kenya market is 3.5%, banks colluding so as to push up the yields on the treasury instruments, and the emergence of shadow banking systems which may results into inefficiencies in terms of transmitting the effects of policy decision into the economy.

Empirical Review

Credit Products

Zachary (2012) sought to evaluate the effect of interest rates on demand for loans by SMEs in Nairobi County. The research findings revealed that there was a very strong positive relationship between demand for credit, interest rate, annual profit and owner's equity. The study also revealed that demand for credit by SMEs could be explained by interest rates. From this study it was evident that credit produced statistically significant values and can be relied on to explain demand for loans by SMEs from lending institutions. The findings further revealed that effective interest rates, annual profits and owners‟ equity explained demand for loans in that order.

According to Swain (2002) loan quantity rationing arises when the potential borrower is denied credit while loan size rationing occurs when the loan amount received by the borrower is smaller than the one they demanded. Credit rationing has been found to influence credit demand to small-scale investors as reported by Okurut (2004). The research focused on identifying factors that influence credit demand and also those that result in the poor being rationed by lenders in Uganda. Using logit regressions, analysis of credit demand was performed at individual levels with dataset containing social economic characteristics of households. The findings reviewed that it is possible most small-scale entrepreneurs who seek credit would be able to obtain it, but costs and conditions may be prohibitive for the high risk borrowers. Lenders determine how much credit is allocated based on the probability of default, often resulting in credit rationing.

Customer Deposits

Tuyishime, Memba and Memba (2015) sought to establish the effects of customer deposits on the bank financial performance in commercial banks in Rwanda. A case study of Equity bank Rwanda limited. Deposits are an indispensable tool commercial banks use to enhance its profitability through advancing deposits mobilized to its customers in form of loans which make in return interest to commercial banks. The study findings indicated that deposits interest rate affects the level of deposits received and later on the profitability of the bank. The study revealed that the introduction of innovative banking technology has led to the increase in deposits at a low cost as opposed to the

usual way of getting deposits through term deposits and made financial services accessible in the unbanked people. This also made the ROA, ROE, net profit increasing due as the loans volume increases. The statistical correlation revealed that there is a positive relationship between deposits mobilization and financial performance of commercial banks in Rwanda, the case of Equity Bank. The study recommends the bank to develop other strategies towards marketing and mobilize more deposits as they are indispensable tools towards the profitability of the bank.

Bank Interest Risks

Calice, Chando, & Sekious (2012) argued that the majority of the banks (56 percent) allow past SME losses to affect the pricing of future loans, specifically interest rates. The effect can be felt at the level of the single SME or at the level of the total SME loan portfolio. The rationale for impacting specific SME clients, according to most banks, was that past losses on a specific SME would negatively affect the risk rating of that particular client, and therefore increase the risk premium required from the client. If the overall loan performance experience on the SME portfolio was poor, the whole portfolio would then be affected, and the pricing would change to reflect the new risk/return trade-off. However, the effect of past losses on capital requirements was not exactly similar to the effect of past losses on pricing, with half of the banks claiming that past losses do not feed into their capital requirements

Bank Interest Ceiling

Edakasi, (2011) carried out to study the effect of interest rates ceiling on loan repayment in Uganda's commercial banks with specific regard to Equity Bank, analyzing the impact of interest rates fluctuation (rising and falling interest rates) on loan repayment in Uganda‘s commercial Banks a case study of Equity Bank and analyzing the effects of interest rate on the supply of loans. The study established that most Equity Bank customers were aware of the influence interest rates have on micro-credits in regard to business performance. It was established that the provision of loans to entrepreneurs has a great impact on the businesses performance. The study also established the most important cause of poor business performance and collapse as being amongst others the high interest rates, limited amount lent, lack of entrepreneurship skills and high taxes.

Olweny,(2011) did a study on modelling the volatility of short term interest rates in Kenya where he sought to establish the link between the level of interest and the volatility of interest rates in Kenya using the Treasury bill rates from August 1991 to December 2007. The main variable for the study was the short term interest rate series. In Kenya, this is the Central Bank three month Treasury bill rate. The interest rate volatility was studied using the general specification for the stochastic behavior of interest rates which is tested in a stochastic differential equation for the instantaneous risk free rate of interest. The study applied the monthly averages of the 91-day Treasury bills for the period between August 1991 and December 2007 which were obtained from the Central Bank of Kenya. The results of the study were consistent with the hypothesis that the volatility is positively correlated with the level of the short term interest rate as documented by previous empirical studies. The key findings revealed that there exists a link between the level of short-term interest and volatility of interest rates in Kenya.

METHODOLOGY

This design was used because it helped the researcher obtain information concerning the current status of the phenomena. Descriptive

research portrayed an accurate profile of persons, events or situations (Robson, 2012). Data available from the Ministry of Trade and Ministry of Industrialization (2017) reveal that there were 2500 SMEs in Manufacturing, 1500 SMEs Trading and 560 SMEs in the service industry (RoK, 2017). This made a total of 4,560 SMEs in Nairobi County. A multiple regression model was then fitted to determine the combined effect that the independent variables had on the dependent variable when acting jointly and was expressed as follows:

$\mathbf{Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon,}$ Where;

Y= Growth of SMES

β_0= constant (coefficient of intercept),

X_1= Credit product;

X_2= Deposit mobilization;

X_3= Bank interest rate risks

X_4= Bank interest rate ceiling;

$\beta_1 \ldots \beta_4$= Regression coefficient of four variables.

ε = Error term.

FINDINGS AND DISCUSSIONS

Credit Products

The first objective of the study was to establish the influence of credit products on growth of SMEs in Nairobi City County, Kenya. Respondents were thus asked to indicate the extent to which they agreed with various statements relating to credit products on growth of SMEs in Nairobi City County, Kenya. Responses were given on a five-point scale where: 1= Very small extent; 2= Small extent 3= Moderate extent; 4 = Great extent; 5= Very great extent. The scores of 'Very small extent' and 'Small extent' have been taken to represent a statement Small Extent, equivalent to mean score of 0 to 2.5. The score of 'Moderate extent' has been taken to represent a statement moderately, equivalent to a mean score of 2.6 to 3.4 the score of 'Great extent' and 'Very great extent' have been taken to represent a statement great extent upon equivalent to a mean score of 3.5 to 5.0. Table 1 below presented the findings. With a grand mean of 3.220, a majority of respondents can be said to have highly agreed to moderate extent with most statements posed as regards influence of credit products on growth of SMEs in Nairobi City County, Kenya. Majority particularly agreed to a moderate extent that the enterprise offer low prices due to low cost of production to increase profits (M=3.248); The firm gets a favorable repayment period from the banks thus increase of profits (M=3.125); The enterprises receive adequate loans from the banks to enhance competitiveness in the market (M=3.908); The banks offer a flexible credit rationing to enhance diversification of the market for our products (M=3.218); The repayment period is adequate thus help the business to gain competitive advantage thus diversification of the market (M=3.290). From the perspective of financial institutions (FIs), lower rates can make them more dependent on "donors" while high rates can lead to higher regulatory scrutiny and attract the worst borrowers (adverse selection). The question around fair rates is therefore key to policymakers and FIs (Zachary, 2012).The financial institutions have repayment periods of weekly and monthly depending on the size of the loan, lending rules and how one agrees with other members of the group ran by the micro-finance institution, who jointly act as guarantors of the loan. Moreover, since most of the loans offered by the institutions do not have grace period, borrowers start servicing the loans as soon as they receive them. There are many forms of loans in the market. The aim is to diversify credit facilities for different sectors of the economy and customize them to fit the intended users.

Table 1: Credit Products

Statements	Mean	Std. Dev
The enterprise offer low prices due to low cost of production to increase profits	3.248	1.380
The firm gets a favorable repayment period form the banks thus increase of profits	3.125	.328
We change receive adequate loans from the banks to enhance competitiveness in the market	3.908	.321
The banks offer a flexible credit rationing to enhance diversification of the market for our products	3.218	.123
The repayment period is adequate thus help the business to gain competitive advantage thus diversification of the market	3.290	1.132
Average mean	**3.220**	

Customer Bank Deposits

The second objective of the study was to establish the influence of customer Bank deposits on growth of SMEs in Nairobi City County, Kenya. Respondents were thus asked to indicate the extent to which they agreed with various statements relating to customer bank deposits on growth of SMEs in Nairobi City County, Kenya. Responses were given on a five-point scale where: 1= Very small extent; 2= Small extent 3= Moderate extent; 4 = Great extent; 5= Very great extent. The scores of 'Very small extent' and 'Small extent' have been taken to represent a statement small extent, equivalent to mean score of 0 to 2.5. The score of 'Moderate extent' has been taken to represent a statement agreed upon moderately, equivalent to a mean score of 2.6 to 3.4 the score of 'Great extent' and 'Very great extent' have been taken to represent a statement great extent upon equivalent to a mean score of 3.5 to 5.0.

Table 2 below presented the findings. With a grand mean of 2.874, a majority of respondents can be said to have highly agreed to moderate extent with most statements posed as regards influence of customer deposits on growth of SMEs in Nairobi City County, Kenya. Majority particularly agreed to a moderate extent that the financial institutions offer credit facilities on the number of guarantors we have to expand our business (M=2.908); The business gets a sizeable loan which depends on the amount of deposits thus increase of profits (M=3.112); The banks offer attractive interest rates on the deposits every time (M=2.887); The banks loans are based on the deposits to enhance diversification of the market for the products (M=2.786);The business have adequate deposits thus help the business to gain competitive advantage thus diversification of the market (M=3.004). The lending activity is made possible only if the banks can mobilize enough funds from their customers. Since commercial banks depend on depositor's money as a source of funds, it means that there are some relationships between the ability of the banks to mobilize deposits and the amount of credit granted to the customers. Thus, the main function of financial institutions of mobilizing funds from the surplus economic agents to the deficit economic agents is put to test in order to generate economic growth. However, the efficiency of performing this function depends on the level of development of the financial system. The finance literature provides support for the argument that countries with better/efficient

financial systems grow faster, while inefficient financial systems bear the risk of bank failure. (Kasekende, 2008). Mohan (2012), Mobilization of deposits is one of the important functions of banking business. It is an important source of working fund for the bank. Deposit mobilization is an indispensable act or to increase the sources of the banks to serve effectively. Mobilization of deposit plays an important role in providing satisfactory service to different sectors of the economy. The success of the banking greatly lies on the deposit mobilization.

Table 2: Customer Deposits

Statements	Mean	Std. Dev
The financial institutions offer credit facilities on the number of guarantors we have to expand our business	2.908	.908
The business gets a sizeable loan which depends on the amount of deposits thus increase of profits	3.112	.328
The banks offer attractive interest rates on the deposits every time	2.887	.412
The banks loans are based on our deposits to enhance diversification of the market for our products	2.786	.524
The business has adequate deposits thus help the business to gain competitive advantage thus diversification of the market	3.004	.803
Average mean	**2.874**	

Bank Interest Risks

The third objective of the study was to establish the influence of bank interest risks on growth of SMEs in Nairobi City County, Kenya. Respondents were thus asked to indicate the extent to which they agreed with various statements relating to bank interest risks on growth of SMEs in Nairobi City County, Kenya. Responses were given on a five-point scale where: 1= Very small extent; 2= Small extent 3= Moderate extent; 4 = Great extent; 5= Very great extent. The scores of 'Very small extent' and 'Small extent' have been taken to represent a statement small extent, equivalent to mean score of 0 to 2.5. The score of 'Moderate extent' has been taken to represent a statement agreed upon moderately, equivalent to a mean score of 2.6 to 3.4 the score of 'Great extent' and 'Very great extent' have been taken to represent a statement great extent upon equivalent to a mean score of 3.5 to 5.0. Table 3 below presented the findings. With a grand mean of 2.766, a majority of respondents can be said to have highly agreed to moderate extent with most statements posed as regards influence of bank interest risks on growth of SMEs in Nairobi City County, Kenya. Majority particularly agreed to a moderate extent that the bank reprising risks affects amount of loans received for the business expansion to enhance our business (M=3.218); The floating assets and liabilities affect the repricing risks thus affecting our business profits (M=2.994); The yield risks marketing strategies every time to enhance competitiveness in the market (M=3.180); The banks yield risks are based on our deposits to enhance diversification of the market for our products (M=2.842); The basis risks affects deposits thus help the business to gain competitive advantage thus diversification of the market (M=2.866).

Table 3: Bank Interest Risks

Statements	Mean	Std. Dev
The bank reprising risks affects amount of loans received for the business expansion to enhance our business	3.218	1.864
The floating assets and liabilities affect the repricing risks thus affecting our business profits	2.994	1.652
The yield risks marketing strategies every time to enhance competitiveness in the market	3.180	1.806
The banks yield risks are based on our deposits to enhance diversification of the market for our products	2.842	.999
The basis risks affects deposits thus help the business to gain competitive advantage thus diversification of the market	2.866	1.098
Average mean	**2.766**	

Bank Interest Ceiling

The fourth objective of the study was to establish the influence of bank interest ceiling on growth of SMEs in Nairobi City County, Kenya. Respondents were thus asked to indicate the extent to which they agreed with various statements relating to bank interest ceiling on growth of SMEs in Nairobi City County, Kenya. Responses were given on a five-point scale where: 1= Very small extent; 2= Small extent 3= Moderate extent; 4 = Great extent; 5= Very great extent. The scores of 'Very small extent' and 'Small extent' have been taken to represent a statement small extent, equivalent to mean score of 0 to 2.5. The score of 'Moderate extent' has been taken to represent a statement agreed upon moderately, equivalent to a mean score of 2.6 to 3.4 the score of 'Great extent' and 'Very great extent' have been taken to represent a statement great extent upon equivalent to a mean score of 3.5 to 5.0.

Table 4 below presented the findings. With a grand mean of 2.820, a majority of respondents can be said to have highly agreed to moderate extent with most statements posed as regards influence of bank interest ceiling on growth of SMEs in Nairobi City County, KenyaMajority particularly highly agreed to a moderate extent that the volatility of the bank rates affects amount of loans received for the business expansion to enhance our business (M=2.998); The bank level of interest affect the repricing risks thus affecting our business profits (M=2.780); The bank commissions and fees affect our marketing strategies every time to reducing our competitiveness in the market (M=3.211); The banks volatility of the rates are based on our deposits to enhance diversification of the market for our products (M=3.201); The commission and fees affects deposits thus help the business to gain competitive advantage thus diversification of the market (M=3.004)

Olweny (2011) argued that interest rate risks can also come in a variety of forms, including repricing risk, yield curve risk and basis risk. A bank will face repricing risk if either the average yield on its assets or that on its liabilities is more sensitive to changes in market interest rates. Such a difference in sensitivity could reflect a number of possible mismatches in the characteristics of assets and liabilities. First, fixed rate assets and liabilities could have different maturities. Second, floating rate assets and liabilities could have different repricing periods, with base rates that have maturities similar to their respective repricing periods (assets that reprice annually based on a one-year rate and

liabilities that reprice quarterly based on a three-month rate, for example).

Table 4: Bank Interest Ceiling

Statements	Mean	Std. Dev
The volatility of the bank rates affects amount of loans received for the business expansion to enhance our business	2.998	.423
The bank level of interest affect the repricing risks thus affecting our business profits	2.780	1.642
The bank commissions and fees affect our marketing strategies every time to reducing our competitiveness in the market	3.211	1.220
The banks volatility of the rates are based on our deposits to enhance diversification of the market for our products	3.201	1.742
The commission and fees affects deposits thus help the business to gain competitive advantage thus diversification of the market	3.004	.892
Average mean	**2.820**	

Growth of SMEs

On the extent to which growth of SMEs in the study area in terms of amount of profits, customer base, number of new markets, number of new employees' added and new branches established. The data was collected from the different indicators of the variable growth of SMEs which was ordinal categorical. The data was therefore presented in frequency tables with the mode being used as the appropriate measure of central tendency. The results were presented in Table 5. The first indicator for the dependent variable required to know what the performance of SMEs in terms of amount of profits was, 10% of the respondents had 0-10% , 30% had 10-20% , 20% had 21-30% , 15% had 31-40%, 20% had 41-50% and 5% had stated over 50% The mode was found to be 2 which imply that on average the performance of SMEs in amount of profits was between 10%-20%.

The next indicator required the respondents to state level of the growth of SMEs in terms of increase of customer base was, 15% of the respondents had 0-10% , 40% had 10-20% , 10% had 21-30% , 15% had 31-40%, 15% had 41-50% and 5% had stated over 50% The mode was found to be 2 which imply that on average the growth of SMEs in the increase of customer base was between 10%-20%.When the respondents were asked what the state level of the growth of SMEs in terms of increase of customer base was, 15% of the respondents had 0-10% , 40% had 10-20% , 10% had 21-30% , 15% had 31-40%, 15% had 41-50% and 5% had stated over 50% The mode was found to be 2 which imply that on average the growth of SMEs in the increase of customer base was between 10%-20%.

In terms of rate of increase of new employees as the measurement for growth of SMEs, 55% of the respondents had 0-10% , 10% had 10-20% , 5% had 21-30% , 10% had 31-40%, 10% had 41-50% and 10% had stated over 50% The mode was found to be 1 which imply that on average the growth of SMEs in the increase of number of new employees added was between 0%-10%.When the respondents were asked what the state level of the growth of SMEs in terms of increase of new markets established was, 75% of the respondents had 0-10% , 4% had 10-20% , 4% had 21-30% , 9% had 31-40%, 8% had 41-50% and 0% had stated over 50% The

mode was found to be 1 which imply that on average the growth of SMEs in terms of increase of new markets established was between 0%-10%. Finally, when the respondents were asked to indicate the state level of the performance of SMEs in terms of increase of new branches established was, 85% of the respondents had 0-10% , 5% had 10-20% , 2% had 21-30% , 2% had 31-40%, 6% had 41-50% and 0% had stated over 50% The mode was found to be 1 which imply that on average the growth of SMEs in terms of increase of new branches established was between 0%-10%.

Table 5: Growth of SMEs

Description	**0%-10%**	**11%-20%**	**21%-30%**	**31%-40%**	**41%-50%**	**Above 50%**	**Mode**
Amount of profits	10%	30%	20%	15%	20%	5%	2
Customer base	15%	40%	10%	15%	15%%	5%	2
Number of markets established	75%	4%	4%	9%	8%%	0%	1
Number of employees	55%	10%	5%	10%	10%	10%	1
Number of branches established	85%	5%	4%	4%	6%	0%	1

Multiple Regression Analysis Model (Combined Effect)

Table 6: Multiple Regression (Combined Effect)

Model Summary

Model	R	R^2	Adjusted R^2	Std. Error of the Estimate
1	.828	.685	.674	.000

ANOVA

Model	Sum of Squares	d.f	Mean Square	F	Sig.
Regression	60.346	4	15.0865	33.370	.000
Residual	33.908	75	.4521		
Total	94254	79			

NB: F-critical value = 23.418;

Regression Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		β	Std. Error	**β**		
1	(Constant)	2.873	.427		6.726	.000
	X_1-Credit products	.820	.139	.702	5.880	.001
	X_2-Customer Deposits	.790	.169	.655	4.658	.004

X_3-Bank Interest Rates	.756	.179	.505	4.220	.006
X_4-Bank Interest Ceiling	.723	.186	.409	3.884	.009

CONCLUSION AND RECOMMENDATIONS

From the descriptive statistics the study established that a majority of respondents stated to a moderate extent that the enterprises offer low prices due to low cost of production to increase profits. The firm gets a favorable repayment period from the banks thus increase of profits. The enterprises receive adequate loans from the banks to enhance competitiveness in the market. The banks offer a flexible credit rationing to enhance diversification of the market for our product. The repayment period is adequate thus help the business to gain competitive advantage thus diversification of the market.

From the study results it was established that to moderate extent with most statements posed as regards influence of customer deposits on growth of SMEs in Nairobi City County, Kenya. Majority particularly agreed to a moderate extent that the financial institutions offer credit facilities on the number of guarantors we have to expand our business. The business gets a sizeable loan which depends on the amount of deposits thus increase of profits. The banks offer attractive interest rates on the deposits every time. The banks loans are based on the deposits to enhance diversification of the market for the products. The business has adequate deposits thus help the business to gain competitive advantage thus diversification of the market.

From the descriptive results the study established that to a moderate extent that the bank reprising risks affects amount of loans received for the business expansion to enhance our business. The floating assets and liabilities affect the repricing risks thus affecting our business profits. The yield risks marketing strategies every time to enhance competitiveness in the market. The banks yield risks are based on our deposits to enhance diversification of the market for our products. The basis risks affects deposits thus help the business to gain competitive advantage thus diversification of the markets.

From the descriptive statistics the study findings indicate to moderate extent with most statements posed as regards influence of bank interest ceiling on growth of SMEs in Nairobi City County, Kenya. Majority particularly highly agreed to a moderate extent that the volatility of the bank rates affects amount of loans received for the business expansion to enhance our business. The bank level of interest affects the repricing risks thus affecting our business profits. The bank commissions and fees affect our marketing strategies every time to reducing our competitiveness in the markets. The banks volatility of the rates were based on our deposits to enhance diversification of the market for our products. The commission and fees affects deposits thus help the business to gain competitive advantage thus diversification of the market.

Conclusion of the Study

The study revealed that credit products statistically, strongly and significantly correlated to growth of the SMEs as it had a positive relationship with the dependent variable. This reveals that credit products is an important factor that can enhance growth of SMEs. Therefore, from these quantitative results it can be deduced that the study which sought to establish the influence of credit products on growth of SMEs was achieved because it established that it influences growth of SMEs.

From the study results it was established that customer deposits statistically, strongly and significantly correlated to growth of the SMEs as it had a positive relationship with the dependent variable. This reveals that customer deposits are an important factor that can enhance growth of SMEs. Therefore, from these quantitative results it can be deduced that the study which sought to establish the influence of customer deposits on growth of SMEs was achieved because it established that it influences growth of SMEs

According to the study results it was established that bank interest risks statistically, strongly and significantly correlated to growth of the SMEs as it had a positive relationship with the dependent variable. This reveals that bank interest risks are an important factor that can enhance growth of SMEs. Therefore, from these quantitative results it can be deduced that the study which sought to establish the influence of bank interest risks on growth of SMEs was achieved because it established that it influences growth of SMEs

Finally, from the study results it was established that bank interest ceiling statistically, strongly and significantly correlated to growth of the SMEs as it had a positive relationship with the dependent variable. This reveals that bank interest ceiling is an important factor that can enhance growth of SMEs. Therefore, from these quantitative results it can be deduced that the study which sought to establish the influence of bank interest ceiling on growth of SMEs was achieved because it established that it influences growth of SMEs.

Recommendations for the Study

The role of credit is basically to bridge the gap between business owner's financial assets and the required financial assets of the business/enterprise. There is need to remove that imbalance between the two hence creating the demand for credit. From the perspective of borrowers, lower rates can increase the potential demand for loans and financial inclusion, while excessive rates can push borrowers into over-indebtedness.

The bank credit and bank deposits are very closely related with each other that they represent, roughly speaking, two sides of the same coin, the balance sheets of banks. The lending activity is made possible only if the banks can mobilize enough funds from their customers. Since commercial banks depend on SMEs money as a source of funds, it means that there are some relationships between the ability of the banks to mobilize deposits and the amount of credit granted to the customers.

The banks face repricing risk if either the average yield on its assets or that on its liabilities is more sensitive to changes in market interest rates. Such a difference in sensitivity could reflect a number of possible mismatches in the characteristics of assets and liabilities. The pricing decisions in these cases will presumably depend on a variety of factors in addition to market interest rates, including the expected behaviour of bank customers and the extent of competition in the markets concerned. Finally, in some cases, bank customers have the option either to repay loans or withdraw their deposits at low (or no) cost, and the decisions of such customers will influence the response of the average pricing of such assets or liabilities to changes in market interest rates

The interest rates ceiling is a key economic aspects that impact the economic growth in the MSEs.. The need to regulate the interest charged on credit or any other financial instrument should be founded on the necessity to control economic patterns that has great effects to the SMEs. Controlling and setting of interest rates has huge fiscal implication to the economic development hence the need for rational decision making process within the banking industry.

Areas for Further Studies

A review of literature indicated that there is limited research on the influence of bank interest rate capping on the growth of SMEs in the Kenyan context. Thus, the findings of this study serve as a basis for future studies on need for the control of the influence of bank interest rate capping on the growth of the SMEs. This study confined itself to SMEs in the in Nairobi City County, Kenya. A comparative study should be carried out to compare whether the findings also apply for other SMEs in different regions in order to validate whether the findings can be generalized in Kenya. Additionally, the study did not tie the variables explained in this study as the only factors of bank interest rate capping which influence growth of SMEs in the study area since the remaining 31.50% can explained by the other variables which the study recommends for further study.

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