

**Series 1 – Economic Pillar: Financial Services**

# Role of Financial Capabilities in Harnessing Digital Mobile Payments for Enterprise Success

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## Key Messages

*The important role played by the financial capabilities of entrepreneurs to enhance translation of the benefits of innovative financial products to the success of MSEs. Need for strong consumer protection regulations to ensure no hidden or exploitative charges to increase the quality of financial inclusion.*

## Context

In Kenya, Micro and Small Enterprises (MSEs) are key engines for growth, creation of employment, innovation, industrial development and GDP growth. The 2016 Kenya National Bureau of Statistics data indicates that this sector accounted for 45 per cent of the establishments and 85 per cent of employment (KNBS, 2016). Despite their great importance, the sector has experienced many challenges and one of them being the exclusion, in terms of access and use, of formal financial products.

Financial capability, the theory in which this study is anchored, proposes that an MSE must have the opportunity to access suitable quality financial products (Storchi and Johnson, 2016). However, it emphasizes that the performance of the MSEs and in turn the well-being of the entrepreneur hinges on the financial capabilities of the entrepreneur to embed the use of financial products. We examine two aspects of financial capabilities in this study: financial literacy and financial behaviour.

While the literature has focussed on the importance of access, and Kenya has made great strides in term of increase in access (Upadhyaya, 2020), research on financial capabilities of entrepreneurs is still scarce (Storchi and Johnson, 2016).

Furthermore, there has been overwhelming attention in the literature to credit products with literature ignoring payment products available to MSEs. This study focuses on one such product, *Lipa na MPesa* that was designed to reduce the over-reliance by MSEs on cash for making and receiving payments. Use of cash has several challenges including loss due to theft, difficulty in tracking, and impulse buying. Therefore, this study focused on the role of capabilities in determining the impact of the use of *Lipa na MPesa* on MSE performance.

## Operationalizing Financial Capabilities

This study's key strength was developing a detailed operationalization of the key variable – financial capabilities, ensuring that several attributes of financial capabilities were taken into account. Financial capabilities were operationalized at three levels:

1. *Financial Literacy* –
  - (a) Financial knowledge (know about it) including education, planning, risk identification, contracts, and cash flow management;
  - (b) Financial skills (how to experience) including business plan, budgets, standards adherence, credit management, coping with emergencies.

Source: Safaricom Website



2. *Desirable financial behaviour* – (actually doing it) includes investments, savings management, tracking income, timeliness, comparing prices.

3. *Digital payments* – (level of use) including receipts, payments, savings, bank loans, and digital loans.

Further, MSEs success was operationalized as sales volumes, profits, employment, livelihoods, self-assessment.

## Approach and Results

This study adopted a mixed methods research design to determine the impact of financial capabilities. The choice of the study area, Starehe Constituency in Nairobi County, was guided by literature which has shown that urban areas have higher adoption of formal financial products. The study began with a mapping of MSEs that use *Lipa na MPesa* establishing a population of 344. A total of 103 MSEs were sampled which was approximately 30% of the mapped population.

The bivariate analysis found out that overall financial capability measure of financial behaviour had the greatest significant correlation to enterprise success. The measures of the capability of financial knowledge, financial skills, and financial behaviour had a significant correlation with the level of use of the digital financial service of *Lipa na MPesa*. There was a significant relationship between financial capabilities and enterprise success at a confidence level of 95%.

Qualitative analysis brought out two key messages. First, enterprise success means different things to different entrepreneurs. To some, it is an increase in sales, profitability, while others cited growth in terms of opening of new branches. However, improvement in livelihoods was considered the most important, with respondents giving examples of being able

to pay school fees for their children. Secondly, the use of *Lipa na MPesa* increased the credit ratings of the enterprises with most respondents saying they can easily access bank loans when they need it. However, it was noted that the uptake of digital loans was very poor. Most respondents said that they only uptake the loans for personal use but not for use in their businesses

outcome from the study may lead to policies that enhance their financial capability which is a road to financial inclusion and is theoretically linked to outcomes of increased performance, productivity, and employment. This will lead to the increased success of the MSEs which play a very critical role in the Kenyan economy.

## Policy Recommendations

### Short-Term

- The emerging issues of consumer protection should be urgently addressed. Some of the respondents felt there were hidden costs that the digital payments services make them incur without their knowledge. Improvement in consumer protection will ensure that MSEs continue to increase their use of formal financial products rather than turn to informal products.
- There should be a proper clarification on all the costs implication to all the parties for both the buyers and the sellers so that a person can make an informed decision when using the product.

### Medium-Term

- This study revealed that there exists a positive relationship between financial capability and enterprise success. Aspects of financial capabilities should, therefore, be enhanced through awareness creation and capacity building.
- The key variable, financial behaviour, is difficult to influence through training only. A more in-depth case study analysis is therefore needed to understand why some MSEs display positive financial behaviour. The

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