EFFECT OF GROUP COMPOSITION AND FORMALIZATION ON THE FINANCIAL PERFORMANCE OF INVESTMENT GROUPS IN NAKURU.

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DECLARATION AND RECOMMENDATION

Declaration

I, the undersigned, declare that this research project is my original work and has not been presented to any other university or institution of higher learning for the award of academic credit.

Signature.....................................   Date..

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CM11/00739/13

Recommendation

This research project has been submitted for examination with my approval as the University Supervisor.

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DEDICATION

This research project is dedicated to my husband Mr. Robert Kiprono Kirui and my daughter Essy for their support both socially and materially throughout my entire education journey. Most importantly I dedicate this project to the almighty God who has kept me safe throughout my studies.

ABSTRACT

Investment groups provide a system of pooling together capital, lowering risks per individual and availing cheap capital for individual and MSEs growth. The objective of the study was to assess the effect of the group composition and formalization on the financial performance of investment groups in Nakuru Town. Descriptive survey design was used to gather information that could be used for statistical inference on the target population through data analysis. Stratified and simple random sampling technique was used to select a sample of 130 investment groups. Since the information is sensitive as it contains financial matters, ethical issues were considered. A personally administered questionnaire was used to collect data necessary to answer research questions. Data was analyzed using both descriptive and inferential statistics. In order to determine the association between the variables, correlation analysis was used. Multiple regression models were used with the help of SPSS statistical tool to assess the effect of group composition and formalization on the financial performance of investment groups. The results show that group composition and group formalization positively and significantly influence financial performance of investment groups in Nakuru town. The study concludes that group composition components which are experience, gender, occupation, business training and ethnic diversity have significant positive effect on group financial performance. The group formalization components that have significant positive effect on group financial performance were organization form, financial management and accounting and auditing. The government should come up with policies that encourage gender mainstreaming in investment groups and registration of investment groups with members from different occupational backgrounds. Kenya Association of Investment Groups should facilitate training programs and forums to educate the members on business skills and proper financial management practices. Policies to encourage formalization of investment groups and as well that demand that investment groups prepare and file audited accounts are needed. The findings can further be verified by conducting a similar study on investment groups in specific economic sector investments. Research on the effect of technology adoption by investment groups can also be done.

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LIST OF ABREVIATIONS

GEM - Global Entrepreneurship Monitor

IASB - International Accounting Standard Board

IFRS - International Financial Reporting Standards

KAIG - The Kenya Association of Investment Groups

KRA – Kenya Revenue Authority

LLC - Limited Liability Company

LLP- Limited Liability Partnership

MFI - Micro Finance Institutions

MSE - Micro- and Small-scale Enterprises

NAIC - National Association of Investors Corporation

NGO - Non Governmental Organization

NSE - Nairobi Securities Exchange

PIN – Personal Identification Number

SACCO – Savings and Credit Co-operative Societies

SBU - Strategic Business Unit

SHG - Self-Help Group

UNCTAD - The Principal Organ of the United Nations General Assembly Dealing with Trade, Investment, and Development Issues

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

In the last decade there has been a growing attention on investments as a tool of economic development across the world. Investments means the commitment of funds which have been saved from current consumption, to purchase financial instruments or other assets with the hope that some benefits will accrue in future in form of interest, income, or appreciation of the value of the instrument (Patel & Patel, 2012). Typical working people across the world are joining forces to form investment groups which are voluntary associations of a few people who pool money to save in order to do joint investments. There is no ideal number of participants for a successful investment group. It should have a manageable size to facilitate constructive discussions regarding investments and enough members to generate sufficient funds through regular contributions for the main purpose of investing (Johnson *et al.,* 2002).

The investment groups have either been transformed into saving and investment groups from self-help groups or were formed for that purpose right from inception according to Kenya Association of Investment Groups (KAIG, 2013). They are not a get-rich-quick scheme, but members are individuals who are focused on the long term investments. Since they are financial partnerships, some investment groups may incorporate to protect members' assets and to facilitate compliance with the accounting rules observed by law (Harrington, 2008). An investment group represents an archetypal example of an organization in which interactional processes can be observed (Harrington & Fine 2000). Investment groups can be composed of people of different business experiences, gender, occupational and business training backgrounds.

Based on a European model going back several generations, the first U.S. investment group was founded in Texas in 1898 and have existed in the United States for at least a century, though they did not become extremely popular until the 1990s when they constituted the major vehicle of the 'popular finance' that has attracted so much attention from the media and policy makers (Harrington, 2008). During the 1990s the popularization of investing and investment groups in the United States was facilitated by several organizational and technical developments most notably being that of discount brokerage firms and the world wide web which lowered transaction costs and made it possible to invest efficiently as a group (Harrington, 2008).

No comprehensive history has yet been written on informal savings groups in Africa, although case studies reflect on their vital supportive role for people who left the rural areas to settle in urban townships in South Africa since the early 1930’s (Verhoef, 2001). In the course of the last quarter of the nineteenth century and especially the first quarter of the twentieth century, African people moved to the growing urban centers and the traditional patterns of economic subsistence were disrupted as alternative forms of social and economic organizations emerged. Urbanization fundamentally changed the economic, power and gender relationships in African communities and informal savings groups emerged as a conscious strategy for survival (Verhoef, 2001).

The informal savings groups are Self- help groups divided into three categories which are financial, welfare and investment groups. The first category which is generally, the most common groups is financial Self-help groups. It could be defined in the name of “Rotating savings and credit associations (ROSCAs)”, or “Accumulating Savings and Credit Associations (ASCAs)". These are informal association that come together for savings (ROSCAs) and lend out with certain percentage of interest (ASCAs) in a regular basis. The second category is welfare groups are support groups, in which members provide each other with various types of help, usually nonprofessional and nonmaterial, for a particular common problem (Impio *et al.,* 2009).

The third category is investment groups, which are vehicles for investments usually in land, the stock market, or in new businesses ventures. The purpose of forming investment groups according to Malkamaki (2008) is to buy assets, exchange business ideas, network and mobilize funds for investments. The investment groups are better organized and differ from Saccos which members save to borrow, whereas in investment groups members save to invest. Currently, local investment groups in Kenya hold a total of about 35 billion Kenyan shillings, equivalent to US$469 million (KAIG, 2014). One of the major investment groups in Kenya is Transcentury Limited, a part owner of the Kenya-Uganda Rift Valley Railways. This together with Centum Investment Limited make Kenya a home to two of the region’s leading companies that have origins of investment groups (Wainaian, 2012).

Investment groups with members who are experienced in the field of business have a high chance of success. Rae & Carswell (2000) suggested that greater understanding of the ways in which people learn to work in entrepreneurial ways is needed if significant advance in entrepreneurial activity is to take place since learning is critical to entrepreneurial effectiveness. Learning is an experiential process through which concepts are derived from and modified by experience. According to Nofsinger & Wang (2011), the experience of the entrepreneur is one factor that explains the difference in external financing levels available to MSEs. Group members however, are usually amateur investors who connect with other investors to learn about investing techniques and to get advice and tips on investments (Entine, 2003).

Men and women have different approaches to investing and the combination of this in a decision making group can produce a synergistic diversity of views that is well suited to a dynamic external environment (Harrington, 2008). Men are more overconfident than women, as the latter are more risk averse (Barber & Odean, 2001; Bajtelsmit & Bernasek 1996). According to Sellappan *et al.*, (2013), younger and unmarried women are usually risk takers while older and married ones avoid taking risk. One of Harrington's most intriguing findings is that groups of men and women together are more profitable than single-sex groups (Harrington, 2008).

An investment group can have members of varying careers, experiences and occupations from all walks of life. They can be medical doctors, engineers, telecommunications technicians, plumbers, accountants or financial directors. There is therefore a broad range of knowledge and experience not only about different companies that the group may invest in but also about broader issues such as economic (Johnson *et al.*, 2002). Having members with different professional backgrounds can be critical in conducting due diligence on potential investment opportunities (Preston, 2004).

Investors with different business knowledge and training levels could be members of an investment group. Stanger (2004) defines business training as an educational class or course that imparts business or vocational knowledge and skills to entrepreneurs in any stage of the business life cycle. Kuratko (2003) observes the decision by many tertiary institutions to design and implement relevant entrepreneurship teaching programs. This means that the investors who have gone through tertiary education have basic business knowledge which include having financial, marketing, operational, human resources, legal, communication, management and being able to formulate strategic plans (Van Vuuren & Nieman, 1999).

In the past decade, most cities in many countries have seen a huge influx of people with different socio-cultural or ethnic origin (Massey & Denton 1993). An ethnic group is a tribalistic grouping that has a sense of common historic origins and frequently develops a sense of common destiny. An ethnic group shares a number of cultural traits and institutions, such as dress, food, language, and family patterns (Makoloo & Ghai 2005). Collier (2001) observes that the tribe and kin groups are the most powerful levels of social identity. In many developing countries, the ethnic makeup of local business communities is quite different from that of the population at large. It is not uncommon for members of a particular ethnic group to account for an overwhelming proportion of entrepreneurs (Fafchamps, 2000).

Most investment groups in Kenya are informal (KAIG, 2014). Informality refers to the legal economic activity taking place below the radar of government (Oviedo, 2009). Formalization refers to the process whereby previously non-compliant investment group becomes integrated into formal sector and through which it obtains a PIN certificate in the name of the enterprise. A business group compares its perceived costs of being formal including both initial registration and ongoing costs like tax payments, with perceived benefits for instance access to credits for expansion (De Mel *et al.,* 2011). These benefits are clearly driving the decision to formalize businesses groups in Kenya (Gelb *et al.,* 2009).

Locally, the word that is popularly known for an investment group is 'chama'. The Kenya Association of Investment Groups (KAIG) defines an investment group as "any collection of individuals or legal persons in any form whatsoever including but not limited to: societies registered under the Societies Act, Partnerships and Limited Liability Companies, whose objectives is the pooling together of capital or other resources with the aim of using the collated resources for investment purposes." (KAIG, 2014). It is important that members decide how the chama is to be recognized before the law, since the law has not made any special provision for these types of entities. There are two common options; a Limited liability company or a partnership.

A limited liability company is a business entity incorporated under the Companies Act CAP 486 of the laws of Kenya. It has a separate legal existence from management and its members (KAIG, 2014). It must be registered with Kenya Revenue Authority so as to acquire a PIN certificate. The group can also choose to be a general partnership which is another type of business relationship in which the terms of business relationship are clearly stipulated in the partnership deed.

General partnership has a minimum of 2 members and a maximum of 30 (KAIG, 2014). The partnership is easier to operate because members are not required to hold annual shareholder or board meetings. A partnership avoids double taxation by passing the income, losses, and credits through the partnership to the partners to be taxed at potentially lower individual rates (McEowen 1992). The partnership form of course, has serious disadvantages because all partners are unlimitedly liable for the enterprise's debts (Lamoreaux & Rosenthal, 2006). It is however recommended to register a business name for the group. This will allow them to legally engage in any business activities, with minimal legal requirements.

Some investment groups start initially as Self-help groups, but eventually transform to investment groups (KAIG 2014) but without registering either as a limited liability company or as a partnership. These are Chamas are registered also as Self-help groups, where members with a common goal come together and form a group that is aimed at improving their personal welfare. These groups can also be described as 'mutual help' or the commonly known 'merry- go rounds'. They are registered under the Ministry of Labour Social Security and Services, department of Social development. Most investment groups fall into the category of Micro and small scale enterprises (MSE). MSEs' small size and flexibility permits them to specialize in narrow niches that are generally less interesting for larger enterprises (Kraus, 2007).

Financial management is a crucial field within the endogenous environment of MSEs that presents numerous potential obstacles. Liquidity is a precondition to ensure that firms are able to meet its short-term obligations and its continued flow can be guaranteed from a profitable venture (Padachi, 2006). The lack of adequate liquidity to meet current obligations when they come due frequently results in problems which result in the failure of the enterprise (Dunn & Cheatham, 1993) but on the other hand, too much focus on liquidity will be at the expense of profitability (Padachi, 2006). Under capitalization is one planning deficiency which results from several errors made during the initial stages of financial planning and implementation. Cash flow problems are a common symptom among businesses with this problem (Dunn & Cheatham 1993).

Investment groups generate capital from the monthly contributions from the members. Members can agree to have a target figure to kick start the investments where they are all required to put in a certain amount (KAIG, 2016). Sources of financing therefore can include equity which can be raised either internally or externally. Equity has a minimum cash outflow unlike debts in which interests are paid periodically (Ou & Haynes, 2006). Other sources of funds available to investment groups include debts. According to Jun and Jen (2003) short-term debt advantages include zero interest rate in some short-term debt cases such as in the case of trade credit and lower costs of flotation than those of long-term loans or equity. Interests are also allowable expenses in tax computations. Another source of finance is from government initiatives like women and youth funds (KAIG, 2016).

One benefit of formalization among others is the fact that there will be proper book keeping, sound accounting systems and auditing by internal or independent external auditors which is a requirement for tax purposes. The auditor is one of the most important external business partners for an MSE in terms of knowledge transfer and the mitigation of internal risks (Aschauer *et al.,* 2015). Audit helps stakeholders to make informed decisions about future directions, based on how an organization is performing (Kamarudin *et al.,* 2012).

Financial reporting, consistent and dependable accounting information is a prerequisite to effective communication to creditors, suppliers, and national governments (Fearnley & Hines, 2007). International Financial Reporting Standards (IFRS) were developed in advanced economies. IASB released IFRS for micro and small scale enterprises in July 2009. The standard for MSE was a result of a five-year development process with extensive consultation of MSEs worldwide (Vasek, 2011). They are increasingly being applied in emergent economies, potentially ignoring considerations of whether IFRS are appropriate or relevant to such economies (Tyrrall *et al.,* 2007). The IFRS for SMEs is intended to be applied to the general purpose financial statements that do not have public accountability, but publish general purposes financial statements or follow generally accepted accounting principles (GAAP**)** (Fearnley & Hines, 2007).

Tax compliance refers to fulfilling all tax obligations as specified by the law freely and completely (Marti 2010). It has been found that compliance burden fall disproportionately on medium and small enterprises internationally (Pope & Abdul-Jabbar, 2008). Internal compliance costs relate to the time spent by company staff on maintaining and preparing information for professional advisers, while external compliance costs arise from payments made to acquire the services of lawyers, accountants and investment advisers from outside a company (Hanefah *et al.,* 2002). With regards to value-added taxes, investment groups that are not LLC often find it difficult to 'pass' these on to their customers because they cannot claim back the VAT that they pay on inputs as they are not legally registered (De Mel *et al.,* 2011). Investment groups therefore need to specify their tax obligation to include VAT as they register with KRA (KAIG 2016)

The move towards economic liberalization proposed in the late 1980s and 1990s was aimed at reducing distortions in the economy although deregulation of markets has had adverse impact on MSEs. The effects include increased macroeconomic instability characterized by high inflation rate and fluctuating exchange rates. While the effects have been harmful to all private enterprises, the MSEs have been particularly hurt given their small size. The major variables that impact MSEs in Kenya include inflation, interest and exchange rates, unemployment, and government legislation.

A high inflation rate raises the cost of living and results to a shift of resources from investments to consumption. High, and volatile, inflation is a threat to good financial performance and has negative effects on many of the investment groups. According to Akabueze (2002) inflation causes a rise in general price, making goods and services expensive to the common market targeted by MSE businesses. High inflations rates possess a great challenge to MSEs since they are the ones who have to increase the prices to match up the high cost of production. Inflation's effects on an economy are various and can be simultaneously positive and negative (Viviers *et al.,* 2012). Negative effects of inflation include an increase in the opportunity cost of holding money, uncertainty over future inflation which may discourage investment and savings. Positive effects include ensuring that central banks can adjust real interest rates (to mitigate recessions), and encouraging investment in non-monetary capital projects (Ligthelm, 2010).

An increase or a decrease in interest rate may affect the investment decision of the investors, if they consider interest rate as cost of capital. When for example there is a rise in interest rate and the opportunity cost goes up, individual investors would prefer to invest in non-fixed income securities such as bonds (Adam & Tweneboah, 2008). Many governments use the interest rate as a monetary policy tool to control other macroeconomic variables like investment, inflation and unemployment.

The currency volatility has effects on the stock returns. When currency appreciates, in a situation where the country is export-oriented, it is expected that there will be a reduction in the competitiveness of her exports, and would therefore have a negative impact on the domestic stock market. This is because the export-oriented companies quoted on the stock exchange market would be less profitable and this may in turn become less attractive to investors (Muthike & Sakwa, 2012). Where there is high unemployment, a lot of people are pushed into entrepreneurship for survival (Wickham, 2009) although the spending power is limited. Little earnings will therefore mean that investments will be limited (Ligthelm & Cant, 2003).

Regulations and procedures are requirements of any orderly development and business activities. They affect enterprises, the public, policy makers and administrators. Most written regulations and procedures in Kenya owe their origin to the colonial period, when regulations were aimed at controlling and regulating growth of indigenous enterprises (K'obonyo *et al.,* 1999). Government policies should aim to encourage and promote investments. Trade and investment systems have an enormous influence on opening up economies to overseas markets and creating alliances with foreign companies (Volkman 2008). Volkman claimed that in developing countries various systems and regulations on trade and investment may burden enterprises trying to gain from international trade and investment.

The current constitutional framework and the new Micro and Small Enterprise Act 2012 (MSE Act 2012) provide a window of opportunity through which the evolution of MSEs can be realized through the devolution framework. The current constitution provides for the establishment of counties and by extension, County led institutions and regulations. The county system will therefore be governed by the current County government Act enacted in 2012. The Act is expected to oversee the operation of the county system like enacting respective county legislations related to MSEs development through the county assemblies (Ong'olo & Awino, 2013).

According to the Registration of Business Names Act (Cap 265, Laws of Kenya) firm founders who want to do business under a "business name" must register that name with the Registrar General's office in Nairobi. A number of businesses are known however not to be keen on registering their businesses for fear of paying tax (K'obonyo *et al.,* 1999). Thus, although a business name is not mandatory, it facilitates access to credit facilities from formal banking as well as trust and recognition from other formal businesses. Once a business is registered, it is required to compile and file audited accounts with the registrar. Most MSEs, especially those run on sole proprietorship basis, hardly do proper bookkeeping and may not be in a position to satisfy such requirements (K'obonyo *et al.*, 1999).

1.2 Statement of the Problem

Investment groups play a critical role in Kenya's capital formation which is a key ingredient in the realization of Vision 2030. Investment groups are expected to contribute greatly in mobilizing local capital and to command more ownership in the local economy, leading to economic development, independence from donors and closing the income generation gap. Investment decision-making process is considered to be critical for every investor and it is a cognitive process which results in the selection of a course of action from several alternatives. Investors need to make wise decisions on whom to join up with to form an investment group and whether or not to formalize their group. Investment groups can conduct economic activity in many forms and must decide whether to organize as a close or publicly held corporation, a general or limited partnership, or just a self-help group. The assessment of group financial performance in this context becomes highly essential. A lot of research on investment groups has been carried out in developed economies. These studies focused on investment groups that invest in common stocks only. There are no in-depth studies on how the group composition and formalization can affect the financial performance of investment groups in developing nations, such as Kenya. Information concerning members' perception on group financial performance is also lacking. Therefore, this study sought to fill the gap and make a contribution to current thin literature in regard to investment groups in developing countries.

1.3 Research Objectives

The objective of the study was to determine the effect of group composition and formalization on the financial performance of investment groups in Nakuru town.

1.4 Specific Objectives

Specifically, the objectives of the study were to:

i. Determine the effect of group composition on the financial performance of investment groups;
ii. Analyse the effect of group formalization on the financial performance of investment groups;
iii. Assess the effect of group composition and group formalization on financial performance of investment groups.

1.5 Hypotheses

i. Group composition does not have statistical significant effect on the financial performance of investment groups;

ii. Group formalization does not have statistical significant effect on the financial performance of investment groups;

iii. Group composition and group formalization do not have statistical significant effect on the financial performance of investment groups.

1.6 Justification of the Study

This study aimed at identifying the demographic and group attributes considered when forming an investment group and whether they have any effect in the management of the group and hence financial performance. The justification for carrying out this study was that it would lead to the creation of new knowledge that would add to the existing literature on investment groups. It will be useful to the government in policy decision making regarding promotion of investments and evaluation of the basis of issuing financial assistance. This study will be of use to NGO's and other stakeholders who are interested in boosting economic development in Kenya. In addition, it will be of use to scholars in the field of finance who are interested in learning more about investment groups and most importantly, it will help individual investors in making decisions as to which investment group to join in terms of its composition and formalization. The findings of this study will be used as a reference as far as further studies are concerned and can lead to further research on investment groups. Such a study has not been carried out in Nakuru town and therefore this study sought to shed more light on investment groups' financial performance.

1.7 Scope and Delimitation of the Study

This study targeted the only investment groups registered with the Ministry of Labour, Social Security and Services in Nakuru town. These groups carried rich information for the study since their composition and formalization are diverse thus enriching the needed information. The researcher interviewed members of groups within the study area in order to get information on experience of group member, gender of group member, their occupation, business training and ethnicity. The researcher also interviewed one official of the groups to get information on the organization forms of investment groups, financial management, accounting and auditing, financial reporting and taxation. The study area is a cosmopolitan town and the cultural background could be a source of diversity in group's composition, formalization and investment decisions. The study restricted itself only to analysis of group composition, formalization and financial performance.

1.8 Limitations of the Study

The study faced some challenges of carrying out a census study due to financial and time constrains, therefore a survey was done. Although the researcher made prior arrangements through telephone calls before administration of questionnaires, some of the respondents were unwilling to give data voluntarily and asked to be paid. The researcher managed to convince the majority of them to freely give the required information and they cooperated.

1.9 Definition of Terms

Auditing – This is an objective and systematic periodic examination and verification of a firm's financial statements and physical inspection of assets by independent auditors to make sure that the records are a fair and accurate representation of the state of affairs. In this study, it refers to the auditing of financial statements of the some of the groups, because not all groups are audited.

Business Training – This is defined as the purposeful intervention by an educator in the life of the learner to impart entrepreneurial knowledge and skills to enable the learner to survive in the world of business. In this study it refers to training attained in tertiary learning institutions, or attained through vocational training so that members can efficiently tackle investments.

Business Experience –Business experience refers to familiarity with a skill or field of knowledge acquired over time of actual practice and which, presumably, has resulted in superior understanding or mastery in business. In this study experience is measured by the number of years a member of an investment group has done investments.

Ethnic Diversity – This pertains to characteristics of a group of people that have distinctive culture and language. In this study, it refers to differences of investors business characteristics based on different ethnic backgrounds in Kenya.

Financial Performance – This is the degree to which financial objectives have been accomplished over a specified period of time, expressed in terms of overall profits and losses. It is a measure of how well assets have been used to generate revenues and it allows decision-makers to judge the results of business strategies and activities in objective monetary terms. In this study, financial performance was measured as return on investment.

Financial Management – The operational activity of a business concerned with the efficient and effective use of equity capital, borrowed cash or any other business funds as well as taking the right decision for profit maximization and value addition of an entity. In this study it refers to the management of funds accumulated through periodic contribution by member, credit from financial institutions and other sources of funds.

Financial Reporting – Financial reporting is the process of producing the external financial statements, the notes to the financial statements, press releases and conference calls regarding quarterly earnings and related information, financial information posted on a corporation's website, and financial reports to governmental agencies. In this study it refers to the reporting by some investment groups to the external stakeholders.

Group Composition – The overall mix of characteristics among people in a group, which is a unit of two or more individuals who interact interdependently to achieve a common goal. Group composition is usually either homogeneous, in which all members are the same, or heterogeneous, in which group members have significant differences. In this study, investors of diverse business experiences, gender, occupation, business training and ethnicity can combine their abilities in business to form groups that could perform well in a business environment.

Group Formalization – Refers to registration of investment groups. In this study, group formalization refers to registering with Kenya Revenue Authority.

Investment Types – An investment is a venture that an individual or a group put their funds in expectation of future cash flows. In this study it means the outlay of funds in businesses such as table banking, real estates, finacial securities, farming and general business activities. A business group could form a portfolio of these investments.

Investment Groups – A group of a few people who come together to save funds on a regular basis in order to invest collectively. In this study it means any collection of individuals or legal persons in any form whatsoever including but not limited to: Limited Liability Companies, Partnerships or Self Help groups whose objective is the pooling together of capital or other resources with the aim of using the collated resources for investment purposes.

Return on Investments – Measures the amount of return on an investment relative to the investment's cost and hence it is a performance measure that is used to evaluate the efficiency of an investment. In this study, return on investments was computed by dividing net income by the cost of the investment, and the result expressed as a percentage or a ratio.

Occupation – This refers to a person's usual or principal work or business, especially as a means of earning a living. In this study, it refers to the activities that members of a group devote themselves to, as a means of getting a living apart from their commitment to the investment group.

Organizational Form – A business can be organized in one of several ways, and the form its owners choose will affect their legal liability and income tax treatment. In this study the three major forms of organization are the limited liability companies, general partnerships and sole proprietorships.

Tax returns– These are reports filled with revenue collection authorities. Tax returns are generally prepared using prescribed forms. In this study tax returns are done to Kenya Revenue Authority, by groups that have been registered for tax purposes.

CHAPTER TWO
LITERATURE REVIEW

2.1 Introduction

This chapter covers, in detail a review of literature on the various factors that affect the investment groups' financial performance. The researcher has also review of the literature and identified possible research gaps. The conceptual frame work for the study is given and it has indicated independent and dependent variables that are deemed to play role in performance of investment groups.

2.2 Theoretical Review

This section presents a theory which has been proposed and tested together with the empirical studies which have been carried out to validate the theory and its application.

2.2.1 Social Identity Theory

Social identity theory focuses on group and intergroup processes and relations (Tajfel & Turner 1986). Under social identity theory the emphasis is on the qualitative characteristics which generate the subgroups or social categories with which social identities are associated including gender, race, and religion among others. Quantitative characteristics which are the characteristics with respect to which the subgroups or categories differ also play a part. The theory has also been applied and developed to explain organizational phenomena and dynamics of language and speech style as identity symbols (Hogg 2016).

Social identity theory (Ashforth & Mael 1996), similarity attraction theory (Mannix & Neale 2005), and social categorization theory suggest that people are drawn to similar others. Social categorization theory tells us that individuals will act differently in the presence of a homogenous group than they would in the presence of a heterogeneous group (Turner *et al.,* 1987). When category distinctions are salient, people perceptually enhance similarities within the group. Mixed gender and racial groups may segment, and diversity may elicit group conflict that interferes with efficacy. Studies show mixed effects of gender diversity on problem solving efficacy (Jackson & Joshi 2011; Jehn & Bezrukova 2004).

Research on diversity has shown contradictory results in the past. In particular, while some studies show positive effects (Jehn *et al.,* 1999; Watson, Kumar, & Michaelson, 1993), some show that diversity can have negative effects on performance (Ancona & Caldwell, 1992; O'Reilly *et al.,* 1998). Race and ethnic diversity appear to increase group conflict, reduce communication, and interfere with cooperation (Jackson & Joshi 2011). Compositional theories of tokenism and stereotype threat suggest that when members of minority groups rise from zero in an occupation, members face expectations that make it difficult to perform to their potential (Reskin, McBrier, & Kmec 1999). Stereotype threat research suggests that when the status of a minority group is primed, members may underperform because they feel they are being judged as group members rather than as individuals (Spencer, Steele, & Quinn 1999).

2.2.2 Behavioral Finance Theory

Behavioral finance theories, which are based on the psychology, attempt to understand how emotions and cognitive errors influence individual investors' behavior. Investors invest in different investment avenues for fulfilling financial, social and psychological needs and therefore while selecting any financial avenue they expect other type of benefits like, safety and security, getting periodic return or dividends. They also expect high capital gain, secured future, liquidity, easy purchase, tax benefits and meeting future contingency (Mohanta & Debasish 2011). Recent studies on the behavior of individual investors' have shown that investors do not act in a rational manner (Shafi, 2014). Investors have behavioral biases in the event of taking investment decision and their decisions also depends on the types of investors, risk tolerance capacity, education, occupation, age, sex, income, marital status, family back ground and environment (Mohanta & Debasish 2011).

Behavioral Finance focuses on how investors interpret knowledge in order to make investment decisions based on information and how they act with their investment decisions. Behavioral Finance has developed as a result of increasing interest of psychologists in economics (Kiyilar & Acar, 2009). Important drivers of entrepreneurial behavior of individuals include demographic and economic factors such as education, age, wealth, and work situation. They also include a set of subjective perceptions about entrepreneurship that they form based on the presence of role models, confidence in one's skills and ability, risk propensity, and alertness to unexploited opportunities (Arenius & Minniti, 2005).

According to social identity theory, the individual defines him or herself partly in terms of salient group memberships. Identification is the perception of oneness with or belongingness to a group, involving direct experience of its successes and failures. This study adopted the Social Identity and Behavioral Theories. The researcher also reviewed the studies on the pertinent effects of the group demographic composition and formalization, on the financial performance that had been carried out prior to this research.

2.3 Empirical Review

This section is a review of what other scholars have investigated on the effect of group demographic composition and formalization on the financial performance of investment groups. It will study in detail the aspects of each variable of group composition and group formalization and how they affect the performance of investment groups.

2.3.1. Group Composition and financial performance

Having a group of interested dedicated people is not a guarantee that an investment group will have a very good financial performance. An investment group needs a variety of men and women who will bring in diverse and unique differentiated individual skills and experiences to the group. Some of the skills and experiences have been acquired as a result investing in different industries over some time, being in different occupations over time or having undergone some business training.

2.3.1.1 Experience of Members

Young people have less life and work experience which is needed to engage in serious enterprise activities. They are therefore more likely to face greater challenges than older age cohorts because they have limited resources, less networks and less business contacts (Schoof 2006). Korniotis & Kumar (2011) examined the investment decisions of older individual investors. The main data set for the study consisted of all trades and end-of-month portfolio positions of investors at a major U.S. discount brokerage house for the 1991 to 1996 time period. Demographic information such age, income, marital status and family size were compiled by Infobase Inc. a few months after the end of the sample period, June 1997. The results indicated older investors are less effective in applying their investment knowledge and exhibit worse investment skill, especially if they are less educated and that investment skill deteriorates with age due to the adverse effects of cognitive aging.

Overconfident investors, in the context of financial markets tend to overestimate their abilities or the precision of their knowledge. As a consequence, they usually hold riskier portfolios and trade more than maximizing expected utility would suggest (Barber & Odean, 2013). Menkhoff *et al.,* (2013) analyzed whether the degree of overconfidence depends on experience and professionalism, using 496 subjects. The subject pool consisted of institutional investors, investment advisors and individual investors. The results showed that investment experience and age have a significant impact on the degree of overconfidence which goes surprisingly in opposite direction.

Most interest in risky investments will be expressed by participants with no investment experience, given the opportunity to choose among a mix of investments including risk-based fund option. Collard & Breuer (2009) examined attitudes towards investment choice and risk within the personal accounts scheme, using qualitative research in the form of 14 focus groups in five locations across the UK. They analyzed the data using descriptive statistics and found out that the participants that were willing to take higher risks to give themselves the chance of making higher returns tended to be young.

2.3.1.2 Gender of Members

Markets are dynamic and are continuously changing the exposure to risk. Jain & Mandot (2012) explored the impact of demographic factors on investment decisions and the relationship between level of risk and demographic factors of investors confined to Rajasthan state. A questionnaire approach was used for collecting primary data from 200 investors from different cities in Rajasthan state only between the periods from April 2011 to Jan 2012. Chi-Square and Correlation analysis was used to test the significant relationship between the demographic factors and the level of risk taking ability of the investors. This study concluded that various demographic factors like age, marital status, gender, city, income level, market knowledge, occupations and qualifications have major impact on investment decision of investors.

Studies show that women are more risk and competition averse than men (Croson & Gneezy, 2009). Women tend to possess less business experience. Their business growth is slower, suggesting a preference for lower risk and lower confidence (Langowitz & Minniti, 2007; Verheurl *et al.*, 2006). Apesteguia *et al.*, (2012) investigated whether the gender composition of teams affect economic performance and decision-making. They studied a large business game, designed to simulate real business decisions, played in groups of three, where each group takes the role of a general manager. They found that all women teams were significantly outperformed by any other gender combinations.

Men are risk takers who trade more than women. Barber & Odean (2001) tested this prediction. In their study the focus was on common stock investment of 37,664 households for which they were able to identify the gender of the persons that opened the brokerage account. Descriptive statistics was used for the demographic data, gross and net return and monthly turnover of each household was calculated to evaluate investment performance. Cross-sectional regression was estimated to assess whether the difference in turnover can be attributed to the demographic characteristics. Models of investor overconfidence predicted that, since men were more overconfident than women, men traded more and perform worse than women.

Depending upon risk appetite, there is an increase in the number of investment avenues available for investors like bank deposits, government and corporate bonds, shares and stocks, mutual funds, insurance, derivatives, real estate and many more (Jain & Mandot, 2012). Women are more conservative in their choice of investment avenues and are unwilling to take risks according to Bhushan and Medury (2013), who analyzed the gender differences in investment behavior among employees. Results showed that women are inclined to investing in safe investment instruments. One of Harrington's most intriguing findings is that gender-based differences in investing can create a "diversity premium". Groups of men and women together are more profitable than single-sex groups (Harrington, 2008).

Prihatiningtyas (2012) examined the impact of the presence of women in the boardroom on firm financial, social and environmental performance. Qualitative and quantitative approaches were used in this study. The sample was the Indonesian financial firms publicly-listed in the Indonesian Stock Exchange in 2005-2008. The result of the quantitative analysis showed that gender diversity has both positive and negative influence on firm financial performance and the results from the qualitative approach demonstrated that the women board members, especially women directors, believe that they may bring positive effect in organizational improvement, which may then enhance firm performance as a whole.

Using an advertising firm, Ibarra (1992) studied men's and women's interaction patterns and found that men were more likely to form strong homophilous ties across multiple networks, while women evidenced a differentiated network pattern in which they obtained social support and friendship from women and instrumental access through network ties to men. Ibarra concluded that relative to women, men appeared to reap greater network returns from similar individual and positional resources, as well as from homophilous relationships.

Business training is an important factor influencing entrepreneurial performance and income because it increases education level in general. Shirokonova & Tsyganova (2010) explored gender differences in efficient-driven countries based on data from Global Entrepreneurship Monitor (GEM) in order to provide explanation for the gender differences in entrepreneurial activity. The results of the conducted regression analysis indicated that training affects both female and male entrepreneurship in a positive manner, although what is more is the fact that the influence of business training is greater on female entrepreneurial activity than on male entrepreneurship.

2.3.1.3 Member Occupation

The personal as well as environmental factors influence investors in formulating their perceptions on investment avenues (Mohanta & Debasish, 2011). In decisions relating to investment, investors have certain weaknesses like cognitive and emotional which take a predominating role. They have behavioral biases in the event of taking investment decision. They simply react to the information available with them and accordingly react to the environment. Investors adopt some investment avenues after analyzing different factors which are influenced by their internal and external environments. Men and women have very different occupational experiences and therefore gender differences in investing may be seen as a result. The gender gap in investing experience is as a result of women less likely than men to have been offered opportunities (U.S. Department of Labor, Women's Bureau, 1994). Levisauskaite & Kartasova (2013) sought to know the similarities and differences between: the behavior of investors having degree in economics or finance and degrees in other fields, investors having different investment experience and to evaluate the relationship between the occupation and experience of investors and the rationality of their investment decisions. The results of the research showed that without taking into consideration the reasons of overconfidence, the Lithuanian individual investors, who have acquired the degree in economics or finance are more overconfident in comparison to investors with a different occupation. The study concluded that the degree acquired and the experiences gained are important factors, affecting the behaviour and decisions adopted in the Lithuanian capital market.

Investors hardly act rationally in taking decisions while investing. Investors simply react on the available information possessed by them and react accordingly. Singh & Yadav (2016) sought to find out the factors that have major influence on the share investment decisions of a sample of 100 investors in Moradabad city of Uttar Pradesh. The study concluded that investors should as far as possible try to make fundamental, technical and financial analysis before investing in the shares. There are lots of considerations while investing such as tax planning, future needs, safety of investments and recurring income. Investors who possess financial information therefore make better investments decisions.

Harrington examined decision making processes in investment groups, employing the conceptual and analytical tools of economic sociology. As formal associations for consultation and discussion of financial decisions, Harrington found that investment groups provide an interesting arena for scholarly observation in which decision-making processes in finance are made transparent. She analyzed how the composition of groups in investment groups, on the one hand, and the way in which information is used in group processes, on the other hand, impact on investment performance. Harrington's findings on the diversity premium suggest interesting implications. Group heterogeneity impacts on investment performance in positive ways, the more decision-making processes in the group can withstand the numerous forces pushing members toward conformity of opinion (Harrington 2008).

Using the principles of behavioral finance Mohanta & Debasish (2011) explored the psychological concept of individual attachment style, mainly the urban investors to different available investment avenues and their investment preference process. Systematic analysis was made by taking primary data and detail information for analysis was collected through structured questionnaire. This study indicated that there is significant role of income and occupation in investment avenue selection by the investors.

2.3.1.4 Business Training

Education is one of the factors that impact positively on growth of firms (King and McGrath, 2002). Chittithaworn *et al.,* (2011) indicated that among other critical success factors that are perceived to be necessary for success of small businesses are education and training. Investors with business knowledge have the ability to get appropriate information from the business environment that is relevant and useful for their investments.

Business training helps investors to cope with the latest accounting systems, information technology, management concepts and production techniques (Jones, 2004). De Mel *et al.,* (2014) conducted an experiment among women in urban Sri Lanka to measure the impact of the most commonly used business training course in developing countries, the Start and Improve Your Business (SIYB) program. Business training lead to some changes in business practices for women already in business, but had no impact on business profits, sales or capital stock. However, both profitability and business practices of the new entrants were increased by training, suggesting that business training may be more effective for new investment than for existing businesses.

Due to gender differences in education or business networks, women might be relatively uninformed about investment opportunities and they might also be untrained in basic cost-benefit analysis (Karlan & Valdivia, 2011). Field *et al.,* (2010) conducted a two-day business training intervention in conjunction with SEWA Bank, which is based in the city of Ahmedabad in western India. 636 women were randomly drawn from the pool of SEWA Bank customers ages 18 to 50 who were both active savers within the past two years. The randomly selected sample of poor self-employed women were trained in basic financial literacy and business skills and encouraged to identify concrete financial goals. For the experiment two, part of these women were randomly assigned to the treatment group. Field *et al.,* (2010) observed a positive and significant effect of the training on business income.

Those investment groups with larger proportion of members with business education and (or) vocational training, are better placed to adapt their enterprises to constantly changing business environments (King & McGrath, 2002). Berge *et al.,* (2012) sought to know the most efficient tool for microenterprise development in a developing country context. They carried out a field experiment in Tanzania, which jointly investigated the importance of a human capital intervention (business training) and a financial capital intervention (business grant). Using data from three survey rounds, a lab experiment and administrative records of the microfinance institution, they concluded that business training is essential to transform financial capital into productive investments.

Business training of investors always lead to improved profitability of an investment. Karlan & Valdivia (2011) evaluated the effectiveness of integrating business training with microfinance services using a randomized control trial to a Peruvian group lending program for female micro entrepreneurs. Treatment groups received thirty- to sixty-minute entrepreneurship training sessions during their normal weekly or monthly banking meeting over a period of one to two years. The study found that entrepreneurship training led to improved business knowledge, practices and revenue.

Individuals can be taught to engage in certain good business practices, which can lead to increased sales. Bjorvatn & Tungodden, (2010) through a field experiment documented that a business training program given by professional trainers from the University of Dar es Salaam Entrepreneurship Centre (UDEC) significantly affected business skills, entrepreneurial attitudes, business practices, and business outcomes among microfinance clients of the microfinance institution, Promotion of Rural Initiative and Development Enterprise (PRIDE) Tanzania. They concluded that business training enabled the entrepreneurs to better identify business opportunities, leading to changes in business practices and ultimately higher sales and profits.

Development of new financial products and the complexity of financial markets have led to an increased importance of improving financial literacy amongst investors. Hassan & Kalli (2009) examined the relationship between financial literacy and investment decisions of the UAE individual investors who invest in the local financial markets. They used a questionnaire divided into three parts with the first part covering demographic variables, the second part identified 37 factors affecting the investment decision of the UAE investors and the third part was devoted to financial literacy. A convenient sample of 290 of UAE national investors was used. The results indicated that there is a significant relationship between financial literacy and investment decisions and women have a lower level of financial literacy than men.

A 1998 study by the National Center on Women and Aging showed that men have more informational diversity than women. Women, unlike men did not read specialty financial publications such as Wall Street Journal on investors and Business, but got their business ideas from friends, relatives and general interest newspapers (National Centre on Women and Aging 1998). Men get investing ideas form financial specialty publications and internet (Harrington, 2008). The most important principal factors that influence investment decisions are past performance of the company stock, expected stock split, bonus, dividend policy and expected corporate earnings. To investigate this, Obamuyi, (2013) carried out a study that covered individual investors in the Nigerian Capital Market, using convenient sampling method to obtain information from 297 respondents through a questionnaire. Independent t-test, Analysis of variance (ANOVA) and post hoc tests were employed. The findings of the study were that investors are enlightened on the factors that are necessary to maximize their wealth in the capital market.

The economic liberalization and globalization have brought a fervent environment for the common and small investors who are willing to participate in the various investment avenues available. Velmurugan *et al.,* (2015) reviewed literature to understand the effect of demographic factors affecting the choice of investment, to ascertain the factors influencing the investor towards selection and order of preference of various investment avenues and to find out the perception of investors relating to safety, liquidity and high returns dimensions. The study concludes that investments are done in various investment avenues with the expectation of capital appreciation and short and long term earnings. The investor should therefore analyse the market cautiously and then make investment decision.

2.3.1.5 Ethnic Diversity

Conflict of preference, ethnicity, prejudice can easily lead to management difficulties in an investment group, however an ethnic mix can also bring about a variety in abilities, experiences, cultures which may be productive and may lead to innovation and creativity (Alesina & Ferrara, 2005). Ethnic diversity is likely to have important cultural, economic, fiscal, and developmental benefits. In the short run however, ethnic diversity tend to reduce social solidarity and social capital. New evidence from the US suggests that in ethnically diverse neighborhoods residents of all races tend to 'hunker down'. Trust (even of one's own race) is lower, altruism and community cooperation is rarer (Putnam 2007). Collier and Gunning (1999) placed much emphasis on ethno linguistic fractionalization as a major explanation for the lack of social capital, productive public goods and other growth enhancing policies.

In many developing countries, the ethnic makeup of local business communities is quite different from that of the population at large. It is not uncommon for members of a particular ethnic group to account for an overwhelming proportion of entrepreneurs (Fafchamps, 2000). Sociologists have emphasized that African entrepreneurs prefer to do business with members of their own ethnic group (Himbara, (1994). They have emphasized the role that trust and reputation among individuals and communities play in creating an enabling environment for trade. There is a consensus that sharing the same ethnicity and religion are elements that favor the establishment of trust (Cornell & Welch 1996).

La Ferrara (2002) explicitly focused on ethnic heterogeneity and economic performance in her study. The study used an original dataset on production cooperatives in the informal settlements of Nairobi, and got information on all members of the surveyed groups, which allowed construction of exact measures of group composition in terms of income, education, age and ethnicity. She found that members who share the same ethnicity as the chairperson are 20 to 25 percentage points more likely to borrow from the group or from other members; hence ethnicity matters in gaining access to group resources, especially in the form of cheap loans.

An application to lending groups is provided by Karlan (2003). He uses data on members of a Peruvian microfinance organization, and exploits the random selection of people into groups to estimate the effect of group composition on repayment performance. He finds that members of more "homogeneous" groups, both in terms of geographical proximity and of cultural affiliation, are more likely to save and to repay their loans. "Cultural" homogeneity is measured through a score attributed by enumerators to each respondent on the basis of his/her language, dress and hair style. These findings suggest that monitoring and enforcement within groups are easier, the greater the social affinity among their members.

The basic idea of network effects is that information about opportunities circulates along interpersonal networks. Investors with better networks collect more accurate information, which enables them to seek out market opportunities more aggressively. Bigsten *et al.,* (2000) investigated differences in productivity, investment and growth across the formality and ethnicity divide. The study concluded that the network implications of ethnicity account for the differences in firm productivity, investment and growth prospects.

Similarly, Fafchamps (2003) investigated the role of ethnicity, religion, gender, and networks in domestic agricultural trade in Africa. He tested the idea that traders who start with an ethnic or network advantage grow faster. The study used original survey data collected in Benin, Malawi, and Madagascar. The study concluded that network effects have a strong and systematic effect on trust and information sharing.

2.3.2 Group Formalization

Informality is pervasive amongst firms in developing countries, and a simple comparisons of formal and informal firms usually reveal that formal firms are more productive and profitable. Formal firms are defined as those that are registered to pay taxes (i.e. have a tax code), a common indicator of formality in the literature (Fajnzylber et al. 2009; McKenzie and Sakho 2010; Rand and Torm 2012). The attributes of group formalization are: organizational form, financial management, accounting and auditing, financial reporting and tax returns

2.3.2.1 Organizational Forms

The choice of organizational form for business has been of interest to investors. The law offers a menu of choices, including liability companies (LLCs) and general partnerships (GPs). Each organizational form has its own set of default rules. Baker & Krawiec (2005) examined the choice of organizational form by New York law firms. The authors concluded that the prevailing theories based on unlimited liability, profit-sharing, and illiquidity are insufficient and posit that, the choice of form decision is quite complex. It depends on a variety of factors, including the behavior of other similarly situated firms that the decision makers consider competitors for prestige and clients. Nonetheless, it is apparent that unlimited liability is generally considered burdensome, and it is the authors' prediction that, at some point in time, nearly all the firms in their sample will choose to file as limited liability partnerships.

Businesses planning in general involve minimization of income taxes, limitation of individual liability, and provision of flexibility and ease in operation (Esch & Spaccarotella 1994). By taxing the income of corporate firms at a different rate than non-corporate firms, taxes can play an important role in a firm's choice of organizational form. The sensitivity of the organizational form decision to tax rates provides a key indicator of the distortion created by the corporate income tax. Goolsbee (2004) used cross-sectional data on organizational form choices across states compiled in the Census of Retail Trade to estimate this sensitivity. The results documented a significant impact of the relative taxation of corporate to personal income on the share of real economic activity that is done by corporations. The double taxation issue bears quite heavily on the choice of organizational form.

The LLC can replace the general partnership with a business that has all of the advantages of the partnership, but also provides owners with limited liability. Chrisman (2009) sought to demonstrate that the LLC is now undeniably the most popular form of new business entity in America. He used data from all 50 states and the District of Columbia on the number of new business entities formed in the years 2004-2007 and data from the Internal Revenue Service regarding the taxation of LLCs for tax years 2002-2006. The study concluded that the LLC is the most commonly formed new business entity in the United States.

MSEs may be better off, if they can adopt a more flexible form of organization that allows them to trade off the advantages and disadvantages of both corporations and partnerships as suits their particular type of business Guinnane *et al.,* (2007) challenged the idea that the corporation is a globally superior form of business organization. Although the corporation had important advantages over the main alternative form of organization (partnerships), it also had disadvantages that limited its appeal to micro and small enterprises. As a result, when businesses were provided with an intermediate choice, the private limited liability company that combined the advantages of legal personhood and joint stock with a flexible internal organizational structure, most chose not to organize as corporations.

2.3.2.2 Financial Management

Financial management is one of the key aspects of the well-being and survival of a business. Hoe (2010) investigated the financial management components and techniques practiced by the micro and small scale enterprises in Malaysia. There was clear evidence that three important core financial management components were used by the MSEs namely financial planning and control, financial accounting, and working capital management. The study also found that three other financial management components namely, financial analysis, management accounting, and capital budgeting were used by a smaller percentage of these enterprises.

Large corporations have reaped the benefits of following best practice in financial and management accounting to become more competitive. Such best practice can be used as a benchmark to improve performance in micro and small enterprises but very few studies have been undertaken to determine this. Zaman & Gadenne (2002) developed and tested a conceptual model of 'best financial and cost accounting practice' (BFCAP) based on the practices of strategic planning, budgeting and budgetary control, and financial and cost accounting as related to financial effectiveness. They concluded that the model does in fact explain relationships between strategic planning, best practice financial and cost accounting practices, and financial effectiveness. Nandan (2010) argued that like large firms, MSEs also require adequate and also sophisticated management accounting techniques and systems to better manage scarce resources hence better financial performance.

Most of the studies have been concentrating on long-range strategic planning with little attention being devoted to financial planning. Wijewardena & de Zoysa (2001) analyzed the impact of both financial planning and control on performance. The study was based on the results of a study involving a questionnaire survey of budgeting and budgetary control processes of 473 manufacturing SMEs in Australia. The results revealed that both financial planning and control processes lead to higher sales performance of these firms. In a different study, financial planning propensities of owner-managers and use of debt finance were examined empirically by Kotey (1999). The study demonstrated that owner-managers who use debt and engage in financial planning achieve higher performance levels than those who do not engage in such activities.

A business borrowing from a bank to finance the working capital will be subject to increased financial requirements which come with a cost from the bank's interest charges. Jarvis *et al.,* (1996) reported that cash flow problems of many small businesses are made worse by poor financial management and in particular lack of planning cash requirements. Overtrading in the MSE business would result to working capital constraints and affect business profitability which arises from increased working capital requirements. Chittenden et al (1998) in their theoretical studies reported that MSEs have limited access to long term capital markets and rely heavily on owner financing, trade credit and short term bank loans to finance their needed investment in cash, accounts receivables and inventory. Deakins *et al.,* (2001) reported that managing cash flows and cash conversion cycle is a critical component of overall financial management for firms especially those who are capital constrained and more reliant on short term sources of finance.

The issue of finance has been identified as an immediate reason why businesses in developing countries fail to start or to progress (Abor 2007). An investment group can have various sources of funds, after it has been in business for a while, including debt from financial institutions. Kinyua (2005) carried out a study to determine the relationship between gearing and profitability of MSEs in Kenya. Through the use of questionnaires primary and secondary data was collected from finance managers of 50 sample companies, which fitted the definition of an MSE. Correlation analysis and regression analysis were used to test the relationship between various factors and the debt ratios of the sample enterprises. The descriptive statistics on net profit indicate that the net profit after access of credit from MFIs was more than the net profit before access of credit.

2.3.2.3 Accounting and Auditing

Financial distress in MSEs is a common phenomenon across the world. MSEs are found most vulnerable to the macro-economic as well as internal management crises hence they fall into financial distress. In view of this, a study by Jahur & Quadir (2012) aimed at identifying the causes of financial distress in MSEs of Bangladesh. Using financial and statistical techniques for analyzing the data, the study identified some most important causes of financial distress such as fund management, poor accounting system, poor financial control, poor productivity and profitability. In their study, Berry *et al.*, (2012) found that accountants, academics and consultants who are the external advisors may be key agents of change. However their perceived value was relatively low. The findings of this survey suggested that when accounting is perceived to be relevant then its use does support business growth.

Most MSEs draw on external support, and their main advisors are external accountants. Bennett & Robson (1999) analyzed the impact of external business advice to MSEs in Britain. The survey which covered 2547 respondents demonstrated a very wide extent of external advice used by 95% of respondent MSEs. In recent years there has been much discussion regarding the burdens imposed on small firms by administrative requirements and in particular those imposed by accounting requirements. Keasey & Short (1990) examined whether the relative burden of accounting requirements is general to small firms or specific to certain types of small firm. Using ordered probit analysis on a sample of 100 small firms, the main empirical finding of the study is that there is a relative burden of accounts perceived by small firms.

Audit helps both shareholders and stakeholders to make informed decisions about future directions, based on how the company is performing. Kamarudin *et al.,* (2012) explored the factors associated with a push for audit exemption among medium and small enterprises in Malaysia. They examined MSEs' perceptions of audit value, audit burden and audit costs factors have implications for the acceptance of the current audit provisions. The survey yielded a response rate of 83 percent, with 360 valid responses received. The results indicated that all three factors have a significant relationship with the level of acceptance of audit exemption.

Audits are performed to ascertain the validity and reliability of financial information provided by the managers of the reporting entity and an assessment of the entity Internal Control System. Olasupo *et al.*, (2016) accessed the impact of statutory auditing of micro and small enterprises on their performance. The study employed survey design and content analysis. The sample for the study comprised of 100 MSEs operators and 25 practicing public accountants purposively selected across Lagos State Nigeria, using stratified sampling techniques. The primary data for the study was gathered from a combination of survey questionnaire and semi structured interviews of key informants. The data was analyzed through descriptive statistical methods. Findings from the study revealed that effective and proper accounting system has a profound impact in successful auditing of Small and Medium Enterprises and by extension on the performances of the firms.

Carey (2015) investigated whether Micro and small enterprises benefit from their external accountants' business advice through enhanced firm performance. Data were collected from questionnaires mailed to a random sample of Australian MSEs. An analysis of 380 survey respondents confirmed a positive relationship between the voluntary purchase of business advice and MSE performance and that performance is further enhanced when business advice is purchased jointly with auditing.

2.3.2.4 Financial Reporting

Developing economies are now following the IFRS which were developed in advanced economies. Tyrrall *et al.,* (2007) examined the relevance and implementation of IFRS to the emerging economy of Kazakhstan from independence in 1991 to 2006. This study indicated that IFRS relevance is likely to increase as Kazakh economic development continues although its implementation was problematic. IFRS are suitable for all enterprises, but their application in case of MSEs would be very expensive and could significantly increase compliance costs of taxation. Bohušová (2014) discussed the IFRS modifications, which should be done in case of MSEs. IFRS for MSEs should be designed to apply to the general purpose harmonized financial statements and other financial reporting.

For IFRS to be acceptable to MSEs, the gains should exceed the costs of IFRS for MSE application. Nerudova & Bohusova (2008) assessed the possibility of introduction of IFRS for MSE in the Czech enterprises. Based on the questionnaires, respondents were highly interested in the costs and gains of IFRS for MSE application. The study found that the first application of IFRS for MSE in the Czech was expensive and time demanding, due to the different philosophy, principles and methodology of recording used in IFSR for MSE. A few people also consider that the IFRS for MSEs in its current form is adequate. Bunea *et al.,* (2012) investigated the attitude of Romanian professional accountants about the financial reporting of MSEs. Data was collected through questionnaires on a sample of 190 accountants. The results indicate that more than a half of respondents consider that the current regulations do not provide a reasonable level of simplification for MSEs.

Despite international interest, academic research investigating the accounting and financial reporting needs of small enterprises remains relatively scarce. Sian & Roberts (2009) assessed the potential demand for and usefulness of reporting guidelines specifically designed for small enterprises in the UK. Data were gathered from accountants providing services to these enterprises and the owners of such enterprises using postal questionnaires. It was found that most of the enterprises produce accounting records, often based on computerized packages and that most small enterprise owners rely on their accountants to prepare their financial statements and are often left bewildered by the complexity of the information provided. The findings also indicated that some aspects of existing regulations were too complex, indicating that regulators need to carefully consider the possibility of developing guidance for the small business entities.

Increasing the complexity of reporting requirements for small companies would not necessarily lead to more accurate reporting. Fearnley & Hines (2007) evaluated the changing attitudes to IFRS, and the accounting model being adopted, particularly focusing on the problems facing smaller companies. The study employed qualitative analysis of data from two main sources: first, a series of interviews with financially literate individuals before IFRS was implemented in the UK; and second, from responses to consultations on the future of financial reporting for non- listed entities. The conclusion was that one reasonably coherent system of accounting regulation will be much harder to achieve under IFRS which potentially leaves a large number of diverse organizations outside the scope of full IFRS.

2.3.2.5 Tax Returns

Formalization affects investment groups in various ways. De Mel, McKenzie, & Woodruff (2013) conducted a field experiment in Sri Lanka in order to measure the latent demand for formalization, and the consequences that formalizing has on informal firms which provided incentives for informal firms to formalize. They concluded that formalized firms do more advertising and are more likely to use receipt books, but don’t appear to get the more touted benefits of formalizing such as increased access to credit, obtaining government contracts, or participating in government programs.

Micro and small businesses are under no legal obligation to produce accounting reports, but must comply with taxation provisions (Mwangi *et al.,* 2011). This sector's growth is hindered by among others, taxation policy which does not favor their growth potential. Mwangi *et al., (*2011) examined tax influence on MSEs sector growth in Kenya. A sample of 268 respondents representing 30% of targeted population of 806 enterprises in the production sectors of Nyeri Industrial area was selected through stratified and random sampling techniques. Data was collected through questionnaires, interviews and was analyzed using binary logistic regression empirical model. The study found that the sales, profits, capital and employment level in the enterprises under study had drastically reduced. It was clear that they were operating under a heavy tax burden which was prohibiting their growth and development.

It has been argued that the regulatory requirements on businesses, particularly those on MSEs, are burdensome and can be a constraint on their growth and so success. Hansford & Hasseldine (2012) evaluated and compared tax compliance costs affecting micro and small scale enterprises in UK. A questionnaire was developed to investigate the amount of money and time spent on accounting and tax related activities. Data was processed by an online survey website and formed the basis of the input for analysis using SPSS. The study concluded that compliance costs fall disproportionately on small firms, although the benefits of having to comply with tax obligations helps improve the record keeping of the business. The results of another empirical research have proved that in the Czech Republic there is negative relation between the size of the enterprise and the amount of compliance costs of taxation (Nerudova & Bohusova 2008).

Rand & Torm (2012) examined the relationship between legal status and firm level outcomes in micro, small and medium manufacturing enterprises in Vietnam. They sought to get a better understanding of the characteristics and dynamics of the informal sector, as well as the perceived benefits associated with formalization. The study covered 10 informal and formal micro household businesses, and semi-structured interviews were carried out in the Hanoi area in November 2009. The results suggested that registration of businesses lead to an increase in profits and investments for Vietnamese MSEs.

Using firm-level data from Mexico, Fajnzylber et al. (2009) investigated the firm characteristics associated with participation in credit markets, access to training, tax payments and membership in business associations. The investigation showed that being formal increases profits by at least 20 per cent. In another study, Fajnzylber *et al.*, (2011) investigated whether high tax rates and complex tax regulations really constitute a barrier to the formalization of micro-firms, and if formalization improves firm performance. The study exploited an extensive Brazilian micro-enterprise survey and the 1996 introduction of a business tax reduction and simplification scheme “SIMPLES” (Integrated System for the Payment of Taxes and Social Security Contributions of Micro and Small Enterprises). The results indicated that there were much higher revenues, employment and profits among firms which register.

According to Fajnzylber *et al.*, (2009) firms that borrow from formal or informal sources and those that pay taxes are significantly more likely to stay in business. Tax advantages derived from debt would lead firms to be completely financed through debt. The interest payments associated with debt are tax deductible, while payments associated with equity, such as dividends, are not tax deductible. Therefore, this tax effect encourages debt use by the firm (Modigliani & Miller, 1963). Jaramillo (2009) however had a different conclusion from his study. He analyzed the demand for formality by using experimental data from micro firms in downtown Lima. He argued that for some firms formalization may not be desirable at any cost. This is likely to be associated with the recurrent costs of being formal, the low perceived value of the benefits of formalization, and the limited growth perspectives of these firms.

McKenzie & Sakho (2010) estimated the impact of registering for taxes on firm profits in Bolivia, the country with the highest levels of informality in Latin America. The sample frame consisted of a geographic information database, based on a census of economic establishments. They found that tax registration appeared to increase profits for the mid-sized firms, but to lower profits for both the marginal smaller and larger firms, in contrast to the standard view that formality increases profits.

2.4 Group Financial Performance

Performance has been defined as the result of an activity. It is the function of the ability of an organization to gain and manage the resources in several different ways. Almajali *et al.,* (2012) argues that there are various measures of financial performance for instance return on sales, which reveals how an organization earns in relation to its sales, return on assets which explains an organization’s ability to make use of its assets and return on equity reveals what return investors take for their investments in equity capital. The advantages of financial measures as compared to other forms of performance measures are the easiness of calculation and that definitions are agreed worldwide.

Financial performance measures are typically based on profit and return on capital employed. Some of the most popular and most commonly used accounting measures are net income, earnings per share, or ratios such as return on investment (ROI), return on equity (ROE), return on assets (ROA) and return on sales (ROS) (Aliabadi et al 2013). This study will use a financial ratio which is the return on investment (ROI). It is frequently used by market and financial analysts in assessing a company's performance, and is also consistent with other studies on organizational performance (Erhardt *et al.,* 2003; Schrader *et al.,* 1997). ROI analysis (when applied correctly) is a powerful tool in making informed decisions on investments (Botchkarev, 2015). In any type of investment, investors want to find out what their return will be. The return is calculated by dividing the profit by the investment. It is a straightforward calculation when measuring a capital investment (Mogollon & Raisinghani 2003).

Return on investment measured as net income divided by invested capital, is arguably one of the most popular financial performance measurements (Erdogmus & Strigel 2004; Andru & Botchkarev , 2011). The choice of ROI for this study is due to the fact that it enables the quantification of the effect of group composition and formalization on financial performance (Harrington, 2008). It is also straight forward, easy to understand and easy to compute. Data to be used for analysis is available in the accounting system or official documentation of the investment groups. ROI also permits comparisons of profitability of dissimilar investment groups (Andru & Botchkarev 2011).

Jacobson (1987) examined the validity of ROI as a measure of economic rate of return by ascertaining the existence and extent of the association of corporate level accounting ROI with stock return, a widely accepted indicator of business performance. Income statement and balance sheet information was required to obtain estimates of accounting ROI and stock price data needed were available through Standard and Poor's Compustat and the University of Chicago's Center for Research in Security Prices (CRSP) data files. It was observed that ROI is significantly correlated with stock return and has a statistically greater association with stock return than commonly advocated alternative measures of profitability. The findings of this analysis suggest that ROI is a useful, and perhaps best available, indicator of business performance.

Jahera & Lloyd (1992) extended the work of Jacobson (1987) into the validity of return on investment (ROI) as a performance measure. The rate of return of a firm's common stock is a well-accepted method of assessing business performance. They argued that if the firm does not have publicly traded common stock, then an alternative, nonmarket based measure is required. As an alternative, ROI is usually employed. For this research, an objective indicator is deemed to be more appropriate as financial gain is the ultimate concern of any investment group. However, most of the investment groups are MSEs without public offering, therefore their return on equity (ROE), return on assets (ROA), and return on capital employed (ROCE) were not available. Therefore, the study adopted ROI as the indicator of financial performance.

2.5 Research Gap

Most of the reviewed literature is from the developed countries whose strategic approach and financial footing could be different from that of Kenya. A few studies that were carried out in developing economies include a study that related strategic planning to wealth creation in investment groups (Icharia, 2014). Another study related ethnic heterogeneity to economic performance of investment groups (La Ferrara, 2002). Specific studies on effect of group composition and group formalization on financial performance of investment groups are lacking in the Kenyan context. Thus, there was a need to carry out the same in developing economies specifically Kenya. This study therefore sought to fill this gap by establishing the effect of group composition and formalization on the financial performance of investment groups in Nakuru town.

2.6 Conceptual Framework

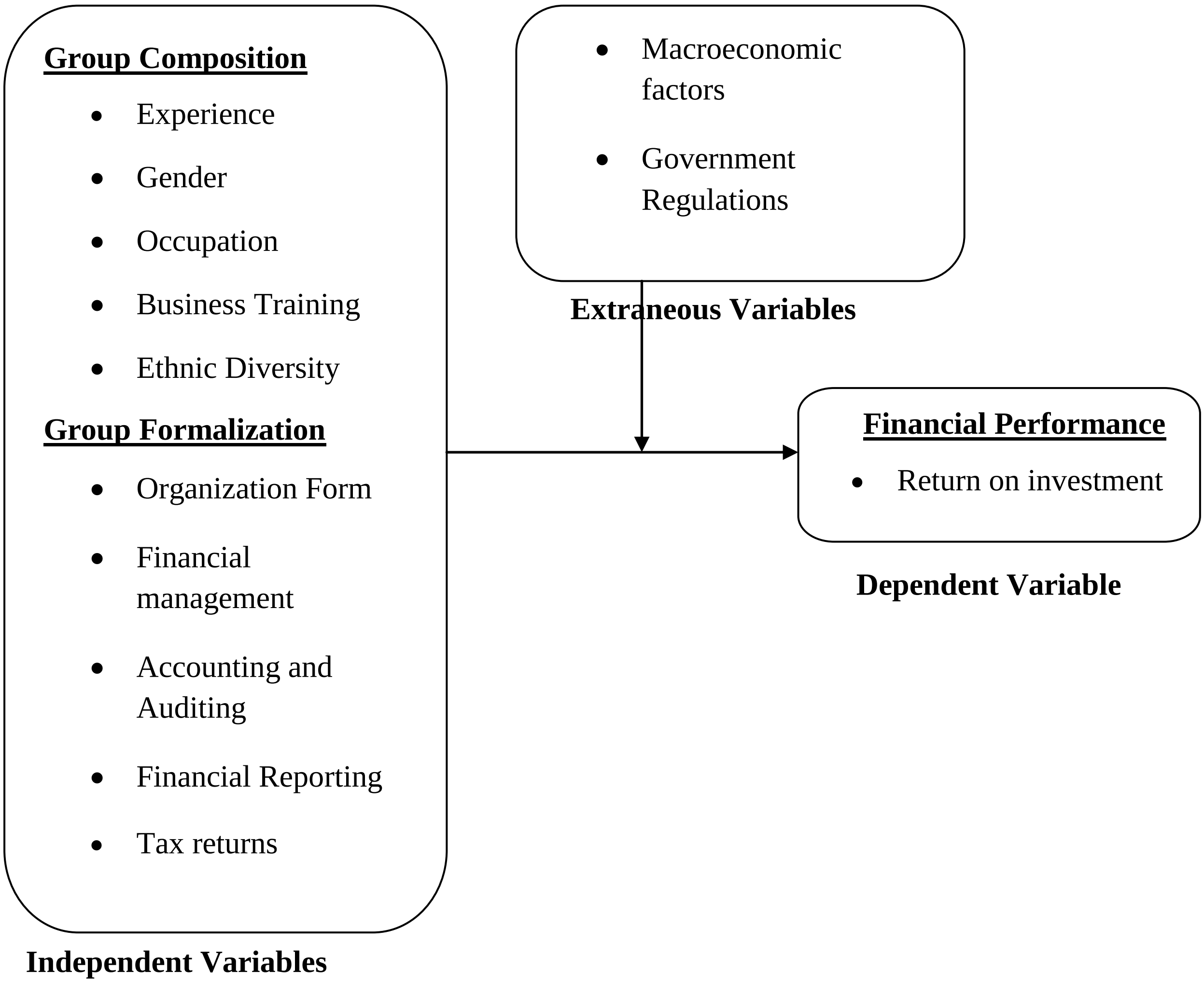

Figure 2.1: **Conceptual framework showing the relationship between group composition, group formalization and financial performance**

Source: Own conceptualization (2019)

Conceptual framework shown in Figure 2.1 above represents a diagrammatical relationship between the dependent variable and the independent variables together with extraneous variables. In this study, the dependent variable is group financial performance measured by the return on investments. The independent variables are group composition of individual group members. Group composition are measured in terms of experience, gender, occupation, business training and ethnic diversity while group formalization are measured in terms of organizational forms, financial management, accounting and auditing, financial reporting and tax returns. Extraneous variables for this study are macroeconomic factors and government regulations since the group members and groups have no control over them.

CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction

This chapter seeks to highlight the various elements necessary to ensure that data collected is not only reliable but also viable. The chapter further discusses details on research design, target population, the sample, research instruments as well as methods that were used in data analysis. The sampling procedure is also included in the chapter.

3.2. Research Design

The study aimed at collecting information from respondents on their opinions regarding the effect of group composition and formalization in financial performance of investment groups. This study employed a descriptive survey design. The use of a descriptive survey research design was employed because it gave an in depth investigation of the case that was under study and gave a wide coverage within a short time. It also gave a description of the state of affairs as it exists (Kothari, 2004). This design has also been used by Icharia (2014) and Olango (2014) in their studies of factors influencing wealth creation in investment groups in Kenya and the effects of international financial reporting standards adoption on SMEs Performance, respectively.

3.3 Target Population

The entire group or subjects that the researcher was interested to investigate formed the population of the study. Currently the population of registered groups in Nakuru town is 17,945 (Ministry of Labour, Social Security and Services, Nakuru 2017). Nakuru town is divided into Nakuru east and Nakuru west sub counties. 17,368 groups are in Nakuru East Sub County and 577 are in Nakuru West Sub County. The groups that were registered between January 2012 and December 2016 total 2874. Out of this, 627 groups were support groups and 50 groups were registered with no specification as to their main activity. The target population under the study was therefore 2197 groups with 1816 from Nakuru East Sub County and 381 from Nakuru West Sub County. The target population from these groups was 38,526 members with 29,931 from Nakuru East and 8595 from Nakuru West. Individual group members were targeted to provide information on demographic attributes while one group official was targeted to provide information concerning the group attributes and annual financial information for particular investment groups.

3.4 Sample Size and Sampling Procedure

A sample represents a part or a subset of the target population while sampling procedure is the process of selecting elements scientifically from the populations (Mugenda, 2008). The study selected a sample of members of investment groups and a sample of investment groups using a stratified random sampling technique and simple random. To determine the sample size, Kothari (2004) developed a formula shown below.

$$n = \frac{z^2.\text{p.q}}{e^2}$$

Where;

n= sample

Z= standard 1.96 (as per table of area under normal curve for the given confidence level of 95%).

p= Proportion of the target population

q=proportion of the population not included in the study (1-q)

e = Standard error of 5%.

Mugenda & Mugenda (2003) suggested that if objectively selected, a sample of between 10-30% of the population is considered adequate for generalization of the findings. Consequently the sample size of the study was 10% of the population and substituting in the formula above 138 was sampled as shown below.

$$n = \frac{1.96^2 * 0.1 * (1-0.1)}{0.05^2} = 138$$

A smaller sample size for adjusted minimum sample size can be used without affecting the accuracy of the study where the population is less than 10,000 (Saunders *et al.*, 2009). This is calculated using the following formula:

$$n' = n/(1 + \frac{n}{N})$$

Where

n' is the adjusted minimum sample size

n is the calculated sample size

N is the total population

Substituting the calculated figures into the formula the minimum sample size was130.

The investment groups were divided according to investment types, then represention from each strata were picked using simple random sampling so as to get the samples. A proportionate sampling was done to get a representative sample size to ensure that there was no biasness in determining the sample size. From each stratum, a representative sample of group members and investment groups were picked randomly. Investment groups were divided into five stratas based on the type of business. The targeted groups are involved in various investments such as table banking, real estates, financial securities, farming, and general businesses activities.

Table 3.1: Sample of Group Members

Type of investments	**Total population of group members**		**Sample size**
Table banking	19,548	19,548/38526*130	66
Real Estates	3,292	3,292/38526*130	11
Financial Securities	116	116/38526*130	1
Farming	5,086	5,086/38526*130	17
General Business	10,484	10,484/38526*130	35
TOTAL	38,526		130

Table 3. 2: Sample of Investment Groups

Type of investments	**Total population of group**		**Sample size**
Table banking	904	904/2197*130	53
Real Estates	176	176/2197*130	10
Financial Securities	10	10/2197*130	1
Farming	485	485/2197*130	29
General Business	622	622/2197*130	37
TOTAL	**2197**		**130**

Table 3. 3: Sample of Group Members and Investment Groups from Nakuru East and Nakuru West Sub counties

Type of investment	**Sample size NE**	**Sample size NW**	**Total Sample size**
	Group Members		
	29931/38526*130 = 101	8595/38526*130 = 29	**130**
Table banking	19548/38526*101 = 51	19548/38526*29 = 15	66
Real Estates	3292/38526*101 = 9	3292/38526*29 = 2	11
Financial Securities	116/38526*101 = 1	116/38526*29 = 0	1
Farming	5086/38526*101 = 13	5086/38526*29 = 4	17
General Business	10484/38526*101 = 27	10484/38526*29 = 8	35
TOTAL	**101**	**29**	**130**
	Investment Groups		
	1816/2197*130 = 107	381/2197*130 = 23	**130**
Table banking	904/2197*107 = 44	904/2197*23 = 9	53
Real Estates	176/2197*107 = 8	176/2197*23 = 2	10
Financial securities	10/2197*107 = 1	10/2197*23 = 0	1
Farming	485/2197*107 = 24	485/2197*23 = 5	29
General Business	622/2197*107 = 30	622/2197*23 = 7	37
TOTAL	**107**	**23**	**130**

A sample of 101 group members was selected from those within Nakuru East and 29 from those within Nakuru West as shown in Table 3.3. Out of the sample from Nakuru East, 51 were investors in table banking, 9 were investors in real estate, 1 was an investor in financial securities, 13 were investors in farming and 27 were investors in general business. Out of the sample form Nakuru West, 15 invested in table banking, 2 invested in real estate, 4 invested in farming and 8 invested in general business.

Likewise a sample of 107 groups was selected from those within Nakuru East Sub County, and 23 groups from those in Nakuru West Sub County. Out of the sample from Nakuru East, 9 groups invested in table banking, 2 groups invested in real estate, 1 group invested in financial securities, 5 groups invested in farming and 7 groups invested in general business.

3.5. Validity and Reliability of the Instrument

3.5.1 Validity

Validity of an assessment is the degree to which it measures what it is supposed to measure. It refers to how accurately an assessment or measurement tool taps into the various aspects of the specific construct in question. In data validity, the study relied on the data collection method that enhances valid data for conclusive analysis and recommendation. The extent, to which a measuring instrument provides adequate coverage of the topic under study, is referred to as content validity (Kothari, 2004). Discussion with the supervisor and fellow classmates regarding the questions in the instrument ensured the content validity.

3.5.2 Reliability

Reliability is concerned with consistency of research results (Mugenda, 2008). A measuring instrument is reliable if it provides consistent results. Reliability of the instrument ensures that a questionnaire has internal consistency. It is concerned with the estimates of the degree to which a measure is free from random error and a reliable instrument can be used with confidence that transient and situational factors are not interfering (Schindler, 2008). In this study reliability of the instrument was measured using Cronbach’s Alpha whose results is presented in Table 3.4.

Table 3. 4: Reliability Statistics

	Cronbach's Alpha	N of Items
Group composition	.729	66
Group formalization	.934	82

Results showed a Cronbach's Alpha coefficient of 0.729 and 0.934 for the first and the second instruments respectively, which is greater than 0.7. The instruments were therefore reliable for data collection.

3.6 Data Collection Procedure

The study collected data from primary sources. This comprised raw data gathered by the researcher through the data collection instruments. A questionnaire, consist of a series of questions and other prompts for the purpose of gathering information from respondents (Mugenda 2008). There were two questionnaires. Questionnaire 1 was used to get information on member demographic attributes and perception of group members on investment groups. This questionnaire was administered to group members because they have a lot of information on group activities. Questionnaire 2 was used to collect information on group formalization. This questionnaire was given to group officials, because they have a lot of information on the group financial performance. The set of questions was simple and straight-forward, that required straight-forward answers. The questions were presented with exactly the same wording and in the same order to all respondents in order to ensure consistency of responses. The method was convenient and cost effective to the study. A drop and pick method was preferred since it gave enough time to the respondent to answer the questions with ease (Mugenda, 2008).

3.7 Data Analysis

Data analysis is the process of bringing orderly structure and meaning to the mass of information collected. It involves examining what has been collected and making deductions and inferences (Kombo & Tromp, 2006). The primary data was analysed using a descriptive statistics as well as regression analysis. Statistical packages for social science (SPSS) assisted in getting the descriptive statistics. Also further analysis using correlation and regression was done to establish the association and effect of group demographic composition and formalization on financial performance respectively. The model is given equation 3.

3.7.1 Effect of Group Composition on Financial Performance

To determine the effect of demographic composition on group performance, the relationship was modeled as in equation 1 :

$$Y = \beta_0 + \beta_1 EXP + \beta_2 GEN + \beta_3 OCC + \beta_4 BTR + \beta_5 EDY + \varepsilon. \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots \quad 1$$

Where:

Y = Financial Performance captured as ROI and measured as net income divided by invested capital, given as a percentage

B_0= y-intercept or constant

EXP – The experience of the group members measured as the number of years in investments

GEN – Gender is a categorical variable coded as male = 1 and female =0

OCC – Occupation is a categorical variable coded as teacher/lecturer=1, farmer=2, entrepreneur=3, valuer=4, accountant=5, engineer=6, social worker =7, security guard=8, clerk=9 and health worker=10

BTR – Business training was measured based on whether the respondent had undergone business training, coded as yes=1 and no=0

EDY- Ethnic diversity is a categorical variable coded as ethnically diverse =1 and not ethnically diverse =0

ε = is the error term or residual that cannot be explained by the model.

3.7.2 Effect of Group Formalization on Financial Performance

The effect of group formalization on group financial performance was modeled as in equation 2:

$Y = \beta_0 + \beta_1 OFM + \beta_2 FNM + \beta_3 AAD + \beta_4 FNR + \beta_5 TRN + \varepsilon$. ………………………… 2

Where:

Y = Financial Performance captured as ROI and measured as net income divided by invested capital, given as a percentage

B_0 = y-intercept or constant

OFM - Organization of the group coded as: incorporated as a limited liability company as = 1 registered as a partnership =2 Self Help group =3

FNM –Financial Management coded as: Performs financial management =1 Does not perform financial management = 0

AAD – Accounting and auditing coded as: group's books of accounts audited = 1 group's books of accounts are not audited = 0

FNR – Financial reporting coded as: group produces annual financial statements = 1 and group does not produce annual financial statements = 0

TRN – Tax Returns coded as: makes tax returns =1 and does not tax returns = 0

ε = is the error term or residual that cannot be explained by the model.

3.7.3 Effect of Group Composition and Formalization on Financial Performance

The two models in equation 1 and 2 are generalized in equation 3 as:

$Y = \beta_0 + \beta_i X_i + \beta_j X_j + \varepsilon$. …………………………………………………… 3

Where:

Y = Financial Performance was captured as ROI and measured as net income divided by invested capital, given as a percentage

B_0= y-intercept or constant,

β_i- β_j= Coefficients beta for each variable.

X_i= Group Composition (experience, gender, occupation, business training and ethnic diversity)

X_j= Group Formalization (Organizational form, Financial Management, Accounting and Auditing, Financial Reporting and Tax returns)

ε = is the error term or residual that cannot be explained by the model.

The significance of this model, which is the overall model was assessed by comparing the p-value of the F statistic with the level of significance at an alpha of 0.05.

3.8 Data Presentations

Data presentation refers to the systematic arrangement of results into meaningful information. This helps the reader to conceptualize the information by attaching meaning.

3.9 Ethical Considerations

The study took into account the ethical issues relating to the research process. First the researcher obtained an authority letter from the Faculty of Commerce of Egerton University to proceed to the field for data collection. Secondly the researcher sought for the permission (permit number NACSTI/P/17/10930/17078) to conduct the study from the Nation Council for Science, Technology and Innovation, first, before the administration of the questionnaire. An attachment of this permit is in appendix II. In addition, no photographs or audio recording were taken without the permission of the respondents. Lastly, all the information given by the respondent were handled with a lot of confidentiality and used for the academic research purpose only.

CHAPTER FOUR

RESULTS AND DISCUSSION

4.1 Introduction

This chapter presents the analysis, presentation, discussion and interpretation of the data collected from the administered questionnaires. The collected data was edited and cleaned for completeness in preparation for coding. Descriptive statistics such as mean was used to analyze the data. Correlation analysis was used to test the study hypotheses. In addition, regression analysis was utilized to establish the association between the variables under the study. Data were presented using tables, graphs and charts

4.2 Response Rate

The study targeted 130 members of investment groups and similarly 130 investment groups. 103 respondents participated in the study of members of investment groups and 107 respondents from investment groups. The Table 4.1 indicates the proportion of respondents of members of investment groups and investment groups from the two Sub-Counties.

Table 4. 1: Response Rate

	Location of Investment Groups	**Target**	**Frequency**
Members	Nakuru East	101	71
	Nakuru West	29	32
Total		**130**	**103**
Groups	Nakuru East	107	91
	Nakuru West	23	16
Total		**130**	**107**

The results from Table 4.1 show that 71 members were from Nakuru East while 32 members were from Nakuru West. This represent a response rate of 79.23 percent. The study also targeted 130 groups but only 107 groups responded and of these, 91 groups were from Nakuru East while 16 groups were from Nakuru West. This represents a response rate of 82.3 per cent. The response rate is reasonable to sufficiently provide the needed information on the study variables.

4.3 Demographic Information

The study first sought to determine the demographic characteristics of the respondents in order to obtain some basic insight about the respondents. The characteristics considered in the study were; period of investments by the respondents, gender, occupation business training and ethnic diversity.

Table 4. 2: Demography of the Respondents

		Frequency	Percent
Period of investing	1 - 4 years	67	66.3
	5 years and above	34	33.7
Gender of group members	Female	53	51.5
	Male	50	48.5
Occupation of the respondent	Teacher/Lecturer	17	17.3
	Farmer	6	6.1
	Entrepreneur	48	49.0
	Valuers	1	1.0
	Accountant	13	13.3
	Engineer	3	3.1
	Social Worker	2	2.0
	Security guard	3	3.1
	Clerk	1	1.0
	Health worker	4	4.1
Training on business	Have training on business	52	51.0
	Do not have training on business	50	49.0
Ethnic Diversity	Group is ethnically diverse	74	71.8
	Group is not ethnically diverse	29	28.2

Results from Table 4.2 above, indicate that 66.3 percent of the investment group members had invested for a period of less than 4 years, while 33.7 percent had invested for a period more than five years. Male respondent constitute 48.5 percent while female consist of 51 percent. The results also indicate that the majority of investment group members were entrepreneurs (49 percent) followed by teacher (17.3 percent) and accounts at 13.3 percent. 51 percent of group members have had training on business while 8 percent had not gone through business training. Also, 71.8 percent of investment group members belong to groups that are ethnically diverse, and 28.2 percent are in ethnically homogenous groups.

The results for the study indicate that majority of investment group members had done investment between 1-4 years. This indicates that the phenomenon of investment groups has gained popularity in the last few years due to improvement in technology which has enabled the investors to gain access to investment information. There was an indication of gender balance in investment group participation and this implies that both male and female investors are equally interested in investment groups. The results also show that most members of investment groups had business training and that most of them are ethnically diverse. Investment groups are formed by investors who work together in an organization go to the same religious institutions or are just friends and neighbors. This has greatly contributed to these groups being ethnically diverse.

4.4 Group Composition

This variable consist of experience, gender, occupation, business training and ethnic diversity**.**

4.4.1 Experience.

Table 4. 3: Experience

	N	Minimum	Maximum	Mean	Std. Deviation
Young investors do not have business experience	103	1	4	3.80	.647
Young and inexperienced investors have less networks and business contacts	103	2	5	3.64	.803
Investment skill deteriorates with age due to cognitive effect of aging	103	1	4	2.71	.893
Overconfident investors have less business experience	103	2	5	3.78	.685
Inexperienced investors choose risky investment	103	1	5	3.63	1.120
Valid N (listwise)	103				

The results from table 4.3 indicate that the respondents agreed that young investors do not have business experience (mean=3.80) with less variability (standard deviation= 0.647). The respondents also agreed that young and inexperienced investors have less networks and business contacts (mean=3.64) with less variability (standard deviation= 0.803). However, they neither agreed nor disagree that investment skills deteriorates with age due to cognitive effect of aging (mean=2.71) also with less variability (standard deviation= 0.893). The respondents agree that overconfident investors are the ones with less business experience (mean=3.78) and standard deviation of 0.685, and that inexperienced investors choose risky investments (mean=3.63).

The results indicate most respondents agreed that young investors are overconfident, inexperienced and choose risky investments. This implies that investors of different experiences should join up to form an investment group. The results support the findings by Menkhoff *et al*., (2013), who argued that experience and age have a significant impact on degree on overconfidence.

4.4.2 Gender

Table 4. 4: Gender

	N	Minimum	Maximum	Mean	Std. Deviation
Women tend to possess less business experience than men	103	1	4	2.41	.822
Women have preference for lower risk investments	103	2	5	3.80	.677
Men are risk takers who trade more than women	103	2	5	3.24	1.142
Men are more overconfident than women	103	2	5	3.72	.901
Groups of men and women together are more profitable than single-sex groups	103	3	5	4.10	.409
Men have stronger business network ties with other men than with women	103	2	5	3.34	1.081
Valid N (listwise)	103				

According to table 4.4 the respondents disagreed that women tend to posses less business experience than men (mean=2.41) with less variability (standard deviation= 0.822). The respondents also agreed that women have preference for lower risk investments (mean=3.8) with standard deviation of 0.677. The findings also reveal that the respondents were not sure whether Men are risk takers who trade more than women (mean = 3.24), and a standard deviation of 1.142. These responses here were quite spread owing to the fact that the standard deviations a quite high. The respondents however agreed that men are more overconfident that women (mean=3.72) with standard deviation=0.409. The respondents agreed that groups of men and women together are more profitable that single-sex groups (mean=0.901), standard deviation =0.409 but were not sure if men have stronger business network ties with other men than with women (mean=3.34).

The findings of this study indicate that women generally are risk averse and are less confident than men. This implies that groups with good representation of both gender, tend to perform better than single sex groups. This is in agreement with the findings by (Langowitz & Minniti, 2007; Verheurl *et al.*, 2006) who concluded that, for women business is characterized by slower growth, suggesting a preference for lower risk and lower confidence.

4.4.3 Occupation

Table 4. 5: Occupation

	N	Minimum	Maximum	Mean	Std. Deviation
Business environmental factors influence choice of investment avenues	103	2	5	3.70	.790
Women and men have very different occupational experiences	103	1	4	2.91	.715
Experience gained in occupations affect decision making in investments	103	2	4	3.51	.712
Young professionals prefer to invest in Real Estate	103	2	5	3.63	1.048
There is significant role of income and occupation in investment avenue selection by the investors	103	2	5	3.73	.888
Valid N (listwise)	103				

The findings in Table 4.5 reveal that the respondents agreed that business environmental factors influence the choice of investment avenues (mean=3.70) with less variability (standard deviation=0.790). They also agreed that women and men have very different occupational experiences (mean=2.91) and standard deviation of 0.715. The respondents further agreed that experience gained in occupations affect decision making investments (mean=3.51) standard deviation of 0.712, and that young professionals prefer to invest in

Real Estates with standard deviation of 1.048. The respondents agreed that there is significant role of income and occupation in Investment Avenue selection by investors (mean=3.73), with standard deviation of 0.888.

The results of this study indicate most respondents agree that a person gains knowledge and experience in any occupation, which contributes a lot in decision making as at to which investment to choose. This implies that investment groups with members from different occupations can easily invest in different industries. According to Singh & Yadav (2016) investors who possess financial information therefore make better investments decisions.

4.4.4 Business Training

Table 4. 6: Business Training

	N	Minimum	Maximum	Mean	Std. Deviation
Investors with business knowledge have the ability to get appropriate information from the business environment	103	2	5	3.57	.966
Business training leads to changes in business practices for investors who are already in business	103	2	5	3.43	.903
Business training has no impact on business profits	103	1	4	1.84	.978
Business training enables the entrepreneurs to better identify business opportunities	103	2	5	4.03	.568
There is a relationship between financial literacy and investment decisions	103	4	5	4.28	.452
Women have a lower financial literacy than men	103	2	5	2.45	.825
Valid N (listwise)	103				

According to results in Table 4.6 the respondents agreed that that investors with business knowledge have the ability to get appropriate information from the business environment (mean=3.57) and standard deviation of 0.966. However they were not sure that Business training leads to changes in business practices for investors who are already in business (mean=3.43 and standard deviation of 0.903. The respondents disagreed that Business training has no impact on business profits (mean=1.84) and standard deviation of 0.978, but agreed that Business training enables the entrepreneurs to better identify business opportunities (mean=4.03) with less variability. The results also indicate that there is a relationship between financial literacy and investment decisions (mean=4.28) and a standard deviation of 0.452, however the respondents were not could neither agree nor disagree that women have a lower financial literacy than men (mean=2.45) and standard deviation of 0.825.

This information is important as it indicates that with business knowledge and financial literacy, investors can easily get appropriate information, and identify viable opportunities in the business environment. This implies investors who are trained in business have high chances of success in financial performance. This supports the study by Chittithaworn *et al.*, (2011), who indicated that among other critical success factors that are perceived to be necessary for success of small businesses are education and training.

4.4.5 Ethnic Diversity

Table 4. 7: Ethnic Diversity

	N	Minimum	Maximum	Mean	Std. Deviation
Conflict of ethnicity can easily lead to management difficulties in an investment group	103	1	5	4.05	.632
Ethnic makeup of local business communities is quite different from that of the population at large	103	2	5	3.26	.896
Members of more homogenous groups in terms of cultural affiliation are more likely to save and repay loans	103	3	5	4.04	.441
An ethnic mix brings about a variety in abilities that lead to innovation and creativity	103	2	5	3.83	.720
Traders who start with an ethnic network advantage grow faster	103	2	5	3.64	.895
Valid N (listwise)	103				

According to the results on Table 4.7, the respondents agreed that conflict of ethnicity can easily lead to management difficulties in an investment group (mean=4.05) and (standard deviation=0.632). The respondents were however indifferent whether ethnic makeup of local business communities is quite different from that of the population at large (mean 3.26) also with less variability standard deviation=0.896. The respondents agreed that members of more homogenous groups in terms of cultural affiliation are more likely to save and repay loans (mean=4.04) with (standard deviation=0.441), and that an ethnic mix brings about a variety in abilities that lead to innovation and creativity (mean=3.83) and a standard deviation of 0.720. The results show that respondents agreed that traders who start with an ethnic network advantage grow faster (mean=3.64) and a standard deviation of 0.895.

According to the results, the majority of the respondents agreed that an ethnic mix brings about a variety in abilities that lead to innovation and creativity (Alesina & Ferrara, 2005).

This implies that investors from different ethnic backgrounds have different abilities investing and in management of investment groups.

4.5 Group Formalization

This variable consists of organizational form, financial management, accounting and auditing, financial reporting and taxation**.**

4.5.1 Organizational Form

Table 4. 8: Organizational Form

	N	Minimum	Maximum	Mean	Std. Deviation
The choice of organizational form for business is of interest to investors	108	1	5	3.27	1.099
Unlimited liability is generally considered burdensome	108	1	5	3.25	1.276
The double taxation issue bears quite heavily on the choice of organization form	108	2	5	3.42	.866
LLC is now undeniably the most popular form of new business entity	108	1	4	2.68	1.118
Valid N (listwise)	108				

Table 4.8 indicate that the respondents were indifferent whether the choice of organizational form for business is of interest to investors (mean=3.27) and a standard deviation of 1.099, nor that unlimited liability is generally considered burdensome (mean=3.25) and a standard deviation of 1.276. The respondents also could not agree nor disagree that the double taxation issue bears quite heavily on the choice of organization forms (mean=3.42). The results also reveal that the respondents were indifferent as to whether LLC is now undeniably the most popular form of new business entity or not (mean=2.68).

The results of the study indicate that most respondents have little or no knowledge about the types and characteristics of different organizational forms. This implies that majority of investment groups are just registered as self help groups and operate as sole proprietors. The results support the study by Baker & Krawiec (2005), who argued that the choice of organization form is quite complex.

4.5.2 Financial Management

Table 4. 9: Financial Management

	N	Minimum	Maximum	Mean	Std. Deviation
Financial management is a key aspect of the well being and survival of a business	108	1	4	1.98	.957
Best practice in financial management practiced by large corporations can be used as a benchmark to improve performance in micro and small enterprises	108	2	4	2.37	.678
Cash flow problems of many small business are made worse by poor financial management	108	2	2	2.00	.000
Issue of finance has been identified as an immediate reason why businesses in developing countries fail to progress	108	2	5	3.28	1.109
The net profit after access of credit from MFIs is more than net profit before such access	108	2	5	3.61	.946
Valid N (listwise)	108				

According to table 4.9 the respondents disagreed that financial management is a key aspect of the well-being and survival of a business (mean=1.98) and a standard deviation of 0.957. They also disagreed that best practice in financial management practiced by large corporations can be used as a benchmark to improve performance in micro and small enterprises (mean=2.37) and a standard deviation of 0.678 and that cash flow problems of many small business are made worse by poor financial management (mean=2.00). The respondents were however indifferent as to whether the issue of finance has been identified as an immediate reason why businesses in developing countries fail to progress (mean=3.28) and a standard deviation of 1.109. The respondents agreed that the net profit after access of credit from MFIs is more than net profit before such access (mean=3.61) and a standard deviation of 0.946.

The finding of this study indicates that most respondents do not believe in effective financial management. This implies that there is poor financial management in most of the investment groups. Nandan (2010) argued that like large firms, MSEs also require adequate and also sophisticated management accounting techniques and systems to better manage scarce resources hence better financial performance.

4.5.3 Accounting and Auditing

Table 4. 10: Accounting and Auditing

	N	Minimum	Maximum	Mean	Std. Deviation
Accountants, who are external advisors may be key agent to change in investment groups	108	1	5	3.62	1.471
There is a relative burden of accounts perceived by small firms	108	1	4	2.01	.717
Effective and proper accounting system has a profound impact in successful auditing	108	1	5	3.10	1.485
MSEs' perceptions of audit cost have implications for the acceptance of audit provisions	108	1	5	2.61	1.324
Valid N (listwise)	108				

The results from Table 4.10 indicate that the respondents agreed that accountants, who are external advisors, may be key agent to change (mean=3.62) and a standard deviation of 1.471. The respondents disagreed that there is a relative burden of accounts perceived by small firms (mean = 2.01) and a standard deviation of 0.717 The respondents could not agree nor disagree whether effective and proper accounting system has a profound impact in successful auditing (mean=3.10) and a standard deviation of 1.485. They also were indifferent as to whether MSEs' perceptions of audit cost have implications for the acceptance of audit provisions (mean=2.61 and a standard deviation of 1.324. These responses here were quite spread owing to the fact that the standard deviations a quite high.

The results indicate that the respondents agree that accountants may bring change to the way investment groups operate. The results also indicate that most respondents are not knowledgeable about accounting systems. This implies that investment groups' members should engage accountants to train them on accounting systems. Carey (2015), indicated that the voluntary purchase of business advice purchased jointly with auditing enhances financial performance.

4.5.4 Financial Reporting

Table 4. 11: Financial Reporting

	N	Minimum	Maximum	Mean	Std. Deviation
Most of the enterprises produce accounting records often based on computerized packages	108	1	4	2.34	.811
Small enterprise owners rely on their accountants to prepare their financial statements	108	1	4	2.60	1.253
Small enterprise owners are left bewildered by the complexity of the financial information provided in the financial statements	108	1	5	2.94	1.560
Increasing the complexity of reporting requirements do not necessarily lead to more accurate reporting	108	1	5	2.61	1.214
Micro and small businesses should produce accounting reports	108	1	5	2.50	1.308
Valid N (listwise)	108				

Table 4.11 shows the results that the respondents disagree that most of the enterprises produce accounting records often based on computerized packages (mean=2.34) and a standard deviation of 0.811. The respondents however were indifferent as to whether small enterprise owners rely on their accountants to prepare their financial statements (mean=2.60) and a standard deviation of 1.283. They were also indifferent whether small enterprise owners are left bewildered by the complexity of the financial information (mean=2.94) and a standard deviation of 1.560. The results further indicate that the respondents could not agree nor disagree whether or not increasing the complexity of reporting requirements do not necessarily lead to more accurate reporting (mean=2.61) and a standard deviation of 1.214

nor whether or not micro and small businesses should produce accounting reports (mean=2.50) and a standard deviation of 1.308.

The majority of the respondents portrayed lack of understanding on preparation of financial statements. This implies that record keeping in groups might not be up to date and this might lead to inefficiencies. The results of this study support the study by Bunea *et al.*, (2012), who concluded that the current regulations on reporting requirements do not provide a reasonable level of simplification for MSEs.

4.5.5 Taxation

Table 4. 12: Taxation

	N	Minimum	Maximum	Mean	Std. Deviation
Performance of micro and small enterprises is hindered by taxation	108	1	5	3.07	1.419
Regulatory requirements on business particularly those on MSEs are burdensome	108	2	5	3.63	1.197
Registration leads to an increase in profits	108	1	5	3.15	.975
Compliance costs fall disproportionately on small firms	108	1	5	3.94	1.530
Tax advantages derived from debt would lead firms to be completely financed through debt	108	2	5	3.56	1.292
Valid N (listwise)	108				

The results from Table 4.12 indicate that the respondents could not agree nor disagree as to the fact that performance of micro and small enterprises is hindered by taxation (mean=3.07) and a standard deviation of 1.419. The respondents agreed that regulatory requirements on business particularly those on MSEs are burdensome (mean = 3.63), and a standard deviation of 1.197 but were indifferent whether or not registration leads to an increase in profits (mean = 3.15) and a standard deviation of 0.975. The respondents however agreed that compliance costs fall disproportionately on small firms (mean=3.94) and a standard deviation of 1.530, and that tax advantages derived from debt would lead firms to be completely financed through debt (mean=3.56) and a standard deviation of 1.292.

From the results, it is clear that most respondents agree that regulatory requirements for tax compliance are burdensome to investment groups. This implies that investment groups struggle to comply with tax provisions and this will increase costs and reduce profitability. The results of this study supports that of Mwangi *et al.*, (2011) who found that operating under a heavy tax burden was prohibiting the growth and development of most MSEs in Kenya.

4.6 Correlation Analysis

The study used Pearson correlation analysis to establish the association between the independent and dependent variables.

4.4.1 Relationship between Group Composition and Return on Investments

The study determined the effects of group composition on group financial performance by correlating the group composition and group performance. Group composition consists of experience of members, gender, occupation, business training and ethnic diversity. The mean response consisting of these factors was obtained. Group financial performance consists of Return on Investments and similarly mean of return on investments for all the investment groups was obtained. The mean of the observed responses for group composition was estimated and correlated with the Return on Investments mean.

Table 4. 13: Correlations Matrix of Group Composition

		Group Composition	ROI
Group Composition	Pearson Correlation	1	.601**
	Sig. (2-tailed)		.000
	N	103	103
ROI	Pearson Correlation	.601**	1
	Sig. (2-tailed)	.000	
	N	103	103

**. Correlation is significant at the 0.01 level (2-tailed).

According to the results in Table 4.13, correlation coefficient of 0.601(R=0.601, $P<0.05$) exists between group composition and Return on Investments. This implies that a unit increase in group composition leads to 0.601 unit increase in Return on investments. Therefore, the study failed to accept the null hypothesis.

These results show that experienced investors who have done investments over a longer period of time, have greater knowledge and skills in investment decisions as opposed to those who have done investments over a shorter period of time. This supports the study by Korniotis & Kumar (2011) argued that experienced investors tend to hold less risky investments and maximize their utility. Similarly, this study agrees with that of Collard & Breuer (2009) argues that participants in risky investments lack investment experience. In addition, this study corroborates that of (Apesteguia *et al.*, 2012) who concluded that women are inclined to safe investment instruments limiting their returns.

Mohanta & Debasish (2011) indicated that investors decision making in relation to investments is influenced by their internal and external environments. Consequently, young salaried investors tend to invest in mutual funds. Training and education positively affects the performance of the group. Business training helps investors to cope with market dynamic (King and McGrath 2002). Due complexity in financial markets such as new financial products, changes in both economic and social factors, there is need for improved financial literacy among investors (Hassan & Kalli, 2009). Similarly, Shirokonova & Tsyganova (2010) contend that training equip investors with entrepreneurial skills thus increase their earning capabilities. Furthermore, an ethnic mix brings about a variety in abilities, experiences and cultures which may be productive and may lead to innovation and creativity (Alesina & Ferrara, 2005).

4.4.2 Relationship between Group Formalization and Return on Investments

The study determined the effects of group formalization on group financial performance by correlating the group formalization and group performance. Group formalization consists of Organizational Forms, Financial Management, Accounting and Auditing, Financial Reporting and Tax Returns and group financial performance consists of Return on Investments. A mean was computed from group formalization and group financial performance thus correlating the mean.

Table 4.14: Correlations Matrix of Group Formalization

		Group Formalization	ROI
Group Formalization	Pearson Correlation	1	.940**
	Sig. (2-tailed)		.000
	N	108	108
ROI	Pearson Correlation	.940**	1
	Sig. (2-tailed)	.000	
	N	108	108

**. Correlation is significant at the 0.01 level (2-tailed).

According to the correlation results in Table 4.14, correlation coefficient of 0.940(R=0.940, $P<0.05$) exists between group formalization and Return on Investments. This implies that a unit increase in group composition leads to 0.940 unit increase in Return on investments. The study therefore failed to accept the null hypothesis.

The choice of organizational form for any investment is important. The form of organization of an investment group determines taxation of its profits. Taxes play an important role in a firm's choice of organizational form (Goolsbee 2004). The practices of strategic planning, budgeting and budgetary control, and financial and cost accounting improve performance in small enterprises (Zaman & Gadenne 2002). Deakins *et al.,* (2001) reported that managing cash flows and cash conversion cycle is a critical component of overall financial management.

Investment groups draw external support and their main advisors are external accountants. Effective and proper accounting system has a profound impact in successful auditing and by extension on the financial performances (Bennett & Robson 1999). Developing economies are now following the IFRS and its relevance is likely to increase as economic development continues Tyrrall *et al.,* (2007). Fajnzylber *et al.,* (2011) stated that being formal by registering for tax purposes lead to much higher revenues and profits.

4.4.3 Relationship between Group Composition, Group Formalization and Return on Investments

The study determined the combined effect of group composition and group formalization on group financial performance by correlating the group composition and group performance with financial performance. Group composition consists of experience of members, gender, occupation, business training and ethnic diversity. Group formalization consist of organizational forms, financial management, accounting and auditing, financial reporting and tax returns. Group financial performance consists of returns on investment. A mean was computed from group composition, group formalization and group financial performance, thus correlating the mean.

Table 4. 15: Correlations Matrix of Group Composition and Group Formalization

		Group Composition	Group Formalization	ROI
Group Composition	Pearson Correlation	1	.525**	.563**
	Sig. (2-tailed)		.000	.000
	N	103	103	103
Group Formalization	Pearson Correlation	.525**	1	.937**
	Sig. (2-tailed)	.000		.000
	N	103	108	103
ROI	Pearson Correlation	.563**	.937**	1
	Sig. (2-tailed)	.000	.000	
	N	103	103	103

**. Correlation is significant at the 0.01 level (2-tailed).

The results in Table 4.15 indicate the slope of each variable against the dependent variable and the degree of associations.

According to the correlation results in Table 4.15 above, there is a significant positive, moderate association between group composition and financial performance (r=0. 563, P<0.05). This implies that group composition has a positive significant association with financial performance.

In addition, the results in Table 4.15 above indicate that there is a high significant positive relationship between group formalization and financial performance (R=0.937, P<0.05). It implies that group attributes have a significant positive, high association with financial performance.

The risk element determines the group performance. Women generally are risk averse while men are risk takers. Depending on risk appetite, men trade more in investment opportunities than women. An investment group composed of men and women from different occupations, who have business experience and business training and also have differs business skills and abilities. Jain & Mandot (2012) stated that various demographic factors like age, marital status, gender, city, income level, market knowledge, occupations and qualifications have major impact on investment decision of investors, and the results from this study agree with this.

The consequences of formalizing is that investment groups keep good accounting records and use receipt books for ease of tax calculation (De Mel, McKenzie, & Woodruff 2013). In addition they receive advise on financial management by these auditors who are also consultants which leads to business growth (Berry *et al.,* 2012).

4.5 Hypothesis Testing

The study was guided by three hypotheses namely: Group composition do not have significant effect on the financial performance of investment groups, group formalization do not have significant effect on the financial performance of investment groups and group composition and group formalization do not have significant effect on the financial performance of investment groups.

The study further evaluated the effect of group composition on group financial performance, effect of group formalization on group financial performance and combined effect of group composition and group formalization on group financial performance of investment groups. For the regression purposes, mean representing each of the group composition factors (experience of members, gender, occupation, business training and ethnic diversity) and group formalization factors (organizational form, financial management, accounting and auditing, financial reporting and tax returns) was obtained and regressed against financial performance mean. The regression coefficients between the group composition, group formalization and return on investment were obtained to help determine whether to accept or reject the hypotheses.

4.5.1 Effect of Group composition on the Financial Performance of Investment Groups

As seen from the above relationship between the group composition and the financial performance, a significant positive association exists. It is important to determine how variability in financial performance was explained by changes in indicators of group composition.

Table 4.16: Model Summary of Group Composition

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.926[a]	.857	.85	1.366

a. Predictors: (Constant), Ethnic Diversity, Experience, Business Training, Gender, Occupation

From Table 4.16, the results indicate an Adjusted R Square value of 0.85. This implies that 85 per cent of the total variation in group financial performance was explained by changes in indicators of group composition.

Table 4. 17: ANOVA[a] of Group Composition

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	1087.569	5	217.514	116.586	.000[b]
1	Residual	180.972	97	1.866		
	Total	1268.541	102			

a. Dependent Variable: ROI

b. Predictors: (Constant), Business Training, Occupation, Ethnic Diversity, Experience, Gender

The analysis of variance in this study was used to determine whether the regression model is a good fit for the data. The results in Table 4.17 show that the model was significant since the p-value is 0.000 which is less than 0.05 thus the model is statistically significance in predicting the influence of the independent variables on the dependent variable. This was supported by a significant F statistic of 116.586.

Table 4. 18: Effect of Group Composition on Financial Performance

	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	7.120	3.254		-2.188	.031
Experience	-.144	.053	-.111	-2.700	.008
Gender	-.099	.045	-.093	-2.207	.030
Occupation	.302	.063	.204	4.827	.000
Business Training	.532	.023	.901	23.071	.000
Ethnic Diversity	-.178	.050	-.143	-3.574	.001

a. Dependent Variable: ROI

Table 4.18 shows the beta values for each variable and their level of significances. The results indicate the coefficient of -0.144 of experience. This indicates that the coefficient is greater than zero and significant meaning that a unit reduction in group experience causes an increase of 0.144 in financial performance.

Experienced investors portray a behavioral pattern in their investments profile that depicts risk aversion. As investors age, their experience level increases hence they shy away from risky ventures. The results of this study support that of Korniotis & Kumar (2011) who argued that cognitive aging affects investment skills negatively however much knowledge is depicted by portfolio decision. Similarly, this study supports that of (Barber & Odean 2013) who indicated that young investors are willing to take higher levels of risk that is associated with higher returns than older investors. This is also associated with the high degree of overconfidence

From Table 4.18 the results show that the coefficient for group homogeneity of gender was -0.99 (p=0.03) which was statistically significant at the 5 per cent level of significance. This implies that a unit reduction in gender homogeneity causes an increase of 0.99 in financial performance. As a group tends towards being a mixed gender group, it’s financial performance improves.

Homogenous groups are outperformed by mixed gender groups. It is argued that women are more conservative in their choice of investment avenues and are unwilling to take risks. On the other hand groups of men alone take risks and could get into great lose. Moreover women tend to possess less business experience. The results of this study support other studies by

Langowitz & Minniti, 2007; Verheurl *et al.,* 2006, who argued that businesses of women have slower growth, suggesting that they have preference for lower risk and have lower confidence (Langowitz & Minniti, 2007; Verheurl *et al.,* 2006).

The results from Table 4.8 show that the coefficient for group occupational mix was 0.302 (p=0.00) which was statistically significant at the 5 per cent level of significance. This implies that a unit increase in occupational mix causes an increase of 0.302 in financial performance.

When more investors from diverse occupational backgrounds join an investment group, the financial performance of this group will improve. Knowledge gained as a result of being in a certain occupation influence investors' behavioral biases in investment decision making. They react on the available information possessed by them and act accordingly. Levisauskaite & Kartasova (2013) argued that the degree acquired in any educational field and the experiences gained are important factors affecting the behavior and investment decisions of investors. The results of this study support this argument.

Table 4.18 also indicates the coefficient for business training was 0.532 (p=0.00) which was statistically significant and the 5 per cent level of significance. This implies that a unit increase in business training leads to 0.532 unit increase in financial performance. Business training helps investors to cope with the latest accounting systems, information technology, management concepts and production techniques (Jones, 2004). It also enables the entrepreneurs to better identify business opportunities, to get appropriate information hence leading to changes in business practices and ultimately higher sales and profits (Bjorvatn & Tungodden, (2010); Berge et al. (2012). This study therefore agrees with the findings in the literature above.

From Table 4.18 the results indicates that the coefficient ethnic mix was -0.178 (p=0.001) which was statistically significant at the 5 per cent level of significance. This implies that a unit decrease in ethnic mix leads to 0.143 unit increase in financial performance. Trust and reputation among individuals and communities play in creating an enabling environment for trade. There is a consensus that sharing the same ethnicity and religion are elements that favor the establishment of trust (Cornell & Welch 1996). The results of this study corroborates that of Karlan (2003) who insinuated that ethnically homogenous groups perform better financially because monitoring and enforcing of rules and regulations within investment groups are easier the greater the social affinity among the members.

This study hypothesized that group composition does not have a statistical significant effect on financial performance. Based on the findings, this study therefore failed to accept the null hypothesis at it found that group composition positively and significantly affect group financial performance.

4.5.2 Effect of Group Formalization on the Financial Performance of Investment Groups

As seen from table 4.14 above, the relationship between the group formalization and the financial performance is a significant positive association. It is important to look into how variability in financial performance is explained by group formalization. For the regression purposes, mean representing each of the factors (organizational form, financial management, accounting and auditing, financial reporting and tax returns) was obtained and regressed against financial performance mean as shown below.

Table 4. 19: Model Summary of Group Formalization

R	R Square	Adjusted R Square	Std. Error of the Estimate
.990[a]	.980	.979	.505

a. Predictors: (Constant), Tax Returns, Financial management, Financial Reporting, Organizational form, Accounting and auditing

From Table 4.19, the results indicate an Adjusted R Square value of 0.979. This implies that 97.9 per cent of the total variation in group financial performance was explained by changes in indicators of group formalization.

Table 4. 20: ANOVA[a] of Group Formalization

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	1367.505	5	273.501	1023.349	.000[b]
1	Residual	27.261	102	.267		
	Total	1394.766	107			

a. Dependent Variable: ROI

b. Predictors: (Constant), Organizational form, Tax Returns, Financial Reporting, Financial management, Accounting and auditing

An Analysis of Variance (ANOVA) results in table 4.20 indicates that the overall model was significant. This was supported by an f statistic of 1023.349 (p value = 0.000).

Table 4. 21: Effect of Group Formalization on Financial performance

	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	2.073	.641		3.235	.002
Organizational form	.604	.038	.822	15.906	.000
Financial management	.167	.018	441	9.404	.000
Accounting and auditing	-.096	.022	-.245	-4.288	.000
Financial Reporting	-.023	.021	-.055	-1.086	.280
Tax Returns	.014	.007	.038	1.980	.051

a. Dependent Variable: ROI

Table 4.21 shows the beta values for each variable and their level of significances. The results indicate the coefficient for organizational form to be 0.604 (p=0.00) which was statistically significant at the 5 per cent level of significance. This indicates that a unit increase in group organizational form causes an increase of 0.604 in financial performance.

Investment groups get formalized by being registered to pay taxes at group level. The groups that are registered as self help groups and as partnerships are taxed at individual member level. Investment groups that are formalized, have to pay tax to the government. The results of this study agrees with that of Goolsbee (2004) who concluded that, The double taxation issue bears quite heavily on the choice of organizational form. The revenue authorities require that a group's books of accounts be audited for tax purpose. This forces an investment group to adopt the best financial and cost accounting practices which leads to financial effectiveness (Zaman & Gadenne 2002). Formal firms therefore are more productive and profitable. The study findings also support the study by Chrisman (2009) who concluded that LLC was the most profitable business entity in the United States.

From Table 4.21 the results that the coefficient for financial management was 0.167 (p=0.00). This was statistically significant at the 5 percent level of significance. This implies that a unit increase in the level financial management leads to 0.167 unit increase in financial performance. These results agree with that of Nandan (2010), who argued that like large firms, MSEs also require adequate and also sophisticated management accounting techniques and systems to better manage scarce resources hence better financial performance. The findings of this study, also agrees with that of Wijewardena & de Zoysa (2001), who concluded that both financial planning and control processes lead to higher sales performance of these firms. Cash management, being a component of financial management is very important because access to finance for expansion of investments is needed for better financial performance of investment groups, according to Abor (2007). Kinyua (2005) indicated that net profit after access of credit from MFIs was more than the net profit before access of credit. The results of this study also supports this.

From Table 4.21 the results show that the coefficient for accounting and auditing was -0.096 (p= 0.00) which was statistically significant at the 5 per cent level of significance. This implies that a unit decrease in accounting and auditing leads to 0.096 unit increase in financial performance. Most investment groups operate as small firms and if they were to employ accountants and auditors for administrative requirements, and in particular those imposed by accounting requirements they would have to pay a lot in terms of salaries and fees. This study supports findings of studies that found that there is a relative burden of accounts perceived by small firms which makes the perceived value of accountants and auditors relatively low (Keasey & Short, 1990; Berry *et al.*, 2012).

The results from Table 4.21 the results indicates that the coefficient for financial reporting was -0.023 (p=0.28). This implies that a unit decrease in financial reporting leads to 0.023 unit increase in financial performance. Financial reporting requirements can impose a significant burden on smaller enterprises. The study findings supports Tyrrall *et al.,* (2007) study that application of IFRS in case of MSEs would be very expensive and could significantly increase compliance costs of taxation. The results also support the study by Bunea *et al.,* (2012), who reported that the current regulations do not provide a reasonable level of simplification for the financial reporting of MSEs.

From Table 4.21 the results indicate that the coefficient for tax returns was 0.014. This implies that a unit increase in tax returns leads to 0.014 unit increase in financial performance. This study supports the findings that that keeping proper accounting records, for the purposes of tax returns, leads to better financial management through which costs are minimized and profits maximized (Rand &Tom 2012). The finding of this study also concurs with that of Fajnzylber *et al.,* (2011) who found that registration of business for tax purposes leads to an increase in profits. Another reason for improved financial performance is that interest payments on debt is deductible tax deductible, hence an improved financial performance (Fajnzylber *et al.*, 2009).

The second hypothesis stated that group formalization does not have significant effect on the financial performance of investment groups. Based on these results the study failed to accept the null hypothesis. The study established group formalization as a significant factor that influences financial performance of investment groups. Organization form, financial management and accounting and auditing affect the financial performance of investment groups. 98 per cent of the total variation in financial performance is explained by changes in indicators of group formalization. Based on the results obtained from the second model, group formalization indicators are also good predictors of financial performance of investment groups.

4.5.3 Effect of Group Composition and Group Formalization on the Financial Performance of Investment groups

The study determined the combine effect of group composition and formalization on financial performance.

Table 4. 22: Model Summary of Group Composition and Group Formalization

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.941[a]	.885	.883	1.207

a. Predictors: (Constant), Group Formalization, Group Composition

From Table 4.22, the results indicate an R^2 of 0.883. This implies that 88.3 per cent of the total variations in group financial performance was explained by changes in indicators of group composition and formalization.

Table 4. 23: ANOVA[a] of Group Composition and Group Formalization

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1122.976	2	561.488	385.731	.000[b]
	Residual	145.565	100	1.456		
	Total	1268.541	102			

a. Dependent Variable: ROI

b. Predictors: (Constant), Group Formalization, Group Composition

ANOVA was used to estimate significance of regression model, from which an f significance value of p=0.000 was established. This indicated that the overall model was significant since the reported probability was less than the conventional probability of 5% significance level. Thus using the findings in this study it can be concluded that group composition and group formalization influence the financial performance of investment groups. This was supported by an f statistic of 385.731.

Table 4.24: Effect of Group Composition and Group Formalization of Financial Performance

	B	Std. Error	Standardized Coefficients Beta	t	Sig.
(Constant)	1.824	2.892		.631	.530
Group Composition	.209	.086	.097	2.447	.016
Group Formalization	.424	.019	.886	22.259	.000

a. Dependent Variable: ROI

According to the results in Table 4.24, the coefficient for group composition was 0.209 (p=0.016) which was statistically significant at the 5 per cent level of significance. This suggests that a unit increase in group composition causes 0.209 an increase in financial performance. Also, the coefficient for group formalization was 0.424 which was statistically significant at the 5 per cent level of significance. This suggests that a unit increase in group formalization leads to 0.424 unit increase in group performance.

Business experience according to this study was measured by the number of years a member of an investment group has done investments. As investors do investments over time, they also get older. Cognitive change as a normal process of aging affect some abilities, such as conceptual reasoning, memory, and processing speed, which decline gradually over time. The results of this study corroborates that of Korniotis & Kumar (2011), who indicated that older investors could accumulate greater knowledge about the fundamental principles of investing, but on the other hand, their declining cognitive abilities would hinder the effective application of those principles. Overall, the adverse effects of aging dominate the positive effects of experience.

The risk propensity of men and women are different. Since women are more risk averse, investment groups of women only tend to invest in low risk but low return avenues leading to poor financial returns. Men are more risk takers therefore groups of men only will tend to invest in high risk high return avenues, exposing them to chances of making great losses hence poor financial performances. This study therefore agrees with the studies that concluded that groups of men and women together are more profitable than single sex groups (Bhushan & Medury, 2013; Harrington, 2008).

The results of this study corroborates that of Bjorvatn & Tungodden (2010) business training enable investors to better identify business opportunities leading to changes in business practices and ultimately higher sales and profits. Business environment is dynamic, and investors with business training find it easy to cope with emerging improved information technology, management concepts, production techniques and financial systems. Therefore investors who have training in accounting and finance will be able to monitor the group's financial progress as well as get timely relevant information from the business environment. The result of the study also supports that of Hassan & Kalli (2009) who indicated that there is a significant relationship between financial literacy and investment decisions.

Formalized investment groups are those that are registered with tax authorities and as such have the obligation to make periodic returns. In order to minimize tax liabilities, these groups must issue tax receipts for every transaction and must keep good records. This will increase efficiency in the operations of the groups leading to improvement in financial performance. In addition, the groups that are registered as limited liability companies must have their books audited by independent external auditors. The auditors normally give the management letters after auditing, highlighting areas of weaknesses in terms of operations. If the management of such groups take keen interest in such weaknesses and take measures for improvement, costs will be minimized and financial performance will improve. The results of this study support a study by Fajnzylber *et al.*, (2011) who indicated that there were much higher revenues and profits among firms which register for tax.

Investment groups that are formalized can access credit for expansion of operations, from financial institutions which can lead to improved financial performance. The results of this study support the conclusion Olango, (2014), who stated that the financial institutions evaluate the formalizes businesses on the basis of a checklist, which include audited financial statements for the last three years including management accounts and are keener to finance a formal business due to several considerations such as sustained book keeping, transparency of businesses processes and access to contractual opportunities.

The results of this study agrees with that of Straub (2005) who indicated that one of the benefits of being formal is the access to public goods and services. Investment groups that are registered as limited liability companies or limited liability partnerships can have access to government contracts and tenders. This gives them a chance to more transactions that can lead to improved financial performance..

The third hypothesis stated that group composition and group formalization do not have significant effect on the financial performance of investment groups. The results regression analysis indicated that there was a positive significant relationship between group composition, group formalization and financial performance of investment groups thus, study failed to accept the null hypothesis. It implies that both group composition and group formalization are key factors that determine investment group performance. In addition, the third model shows that group composition and formalization significantly predicts financial performance of investment groups.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1. Introduction

This chapter provides a detailed summary of the major findings of the actual study. It then draws conclusions and discusses implications emanating from these findings. Finally, recommendations are made on policy and for academic issues and also suggestions on areas of further study.

5.2 Summary of the Findings

The study results indicated that majority of the respondents were from Nakuru East sub-County. More than 79 per cent of the respondents were from this sub-County. On the issue of period of investment of members of investment groups, majority of them had invested for less than four years while others invested for more than five years. Similarly, the study sought to establish the period of group investments and the results indicated that majority of the investment groups were two to four years old. Interestingly, almost half of the respondents were female, and most of the respondents were entrepreneurs. Majority of the groups were ethnically diverse. Majority of the groups invest in table banking, followed by real estate and financial securities. Few of the groups do farming and general business activities. Accordingly, the results reveals that majority of the groups are self-help groups. Only few are registered as companies and partnerships.

5.3 Conclusion of the study

The findings revealed that group composition components which are experience, gender, occupation, business training and ethnic diversity have significant positive effect on group financial performance. The group formalization components that have significant positive effect on group financial performance were organization form, financial management and accounting and auditing. Correlation analysis results indicated a moderate positive relationship between group composition and investment group financial performance. Regression results further indicate a significant positive effect. Group heterogeneity impacts on investment performance in positive ways (Harrington 2008). This is because a well-diversified group has members that can bring about a variety in abilities, experiences, knowledge and cultures which may be productive and may lead to innovation and creativity (Alesina & Ferrara, 2005). Secondly, group formalization has strong positive significant effect on group financial performance. Formalized investment groups must comply with tax provisions. This forces them to keep good books of accounts and to utilize services of external financial consultants. Formalized investment groups can therefore access credit for expansions because banks normally evaluate them on the basis of a checklist, including audited financial statements for the last three years including management accounts (Olango, 2014). Lastly, regression results indicate that group composition and group formalization have a positive significant effect on group financial performance. In conclusion, diversified investment groups in terms of experience, gender, occupation, business training and ethnic diversity which are formalized, will experience the best financial performance.

5.4 Recommendation of the study

5.4.1 Policy and Practical Implication

The study found that as investment groups tend towards being gender homogeneity, their financial performance deteriorates. The government should design and implement policies, with a view to promoting equality between women and men, in registration of investment groups.

The study also found that investment groups with members from diverse occupational backgrounds perform better financially. The government should put in place rules that groups should only be registered in members come from different occupation backgrounds.

Business training leads to improved financial performance. The study therefore recommends that the government should organize seminars and business drills for the investment groups. Umbrella bodies such as Kenya Association of Investment Groups should facilitate training programs and forums to educate the members on business skills and proper management practices. The government should make it compulsory that members attend seminars and business drills for investment groups.

According to the study majority of investment groups invest in table banking. The study recommends that the umbrella body KAIG should provide education and information on the current and new avenues of investment available through various formats such as periodic investment talks, investment tours, regular investment updates and investments alerts. Investment groups should therefore register as members of KAIG.

Despite the voluntary nature of association of investment groups there is need to have a regulator who can monitor the activities of the groups and even educate their officials and members so that they can diversify their investments and minimize risk and maximize returns.

Formalized investment groups perform better financially according to the study. Investment groups should therefore register their businesses formally as a means of increasing their credit access chances and reducing the likelihood of mismanagement. The government should make it a rule that investment groups be formalized either as limited liability companies or as partnership and to have their books of accounts be audited annually.

The study found that financial management is a key aspect that determines the financial success of an investment group. The study recommends that the government should offer basic business and financial management skills as this will enable investment groups to make informed investment decisions. The government should conduct annual training forums on matters of proper maintenance of required records, and accurate and timely tax returns. The government can use media like television, newspapers and social media which is very influential in Kenya.

The government can use

5.4.2 Recommendation for Further Studies

The following directions for future research should be carried out. The study focused only on investment groups registered with ministry of Labour and Social Security and Services, Department of Social Development while there are many other investment groups that are members of the umbrella body KAIG, but invest in different economic sectors. The findings can further be verified by conducting a similar study on other investment groups which are invest in specific investment areas.

Research on the effect of technology adoption by investment groups should be done. Use of technology in the business can competitively position the groups in the market. This is because the business environment is dynamic. Use of technology in the business is likely to enable investment groups to exchange information with the environment efficiently and effectively, hence enhance financial performance. Lastly this study was done in Nakuru town. In future, other investment groups in other towns should be involved to enable the researcher to make adequate conclusions.

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APPENDICES

APPENDIX I: INTRODUCTION LETTER

ROSE KIRUI,
P. O. BOX 3561-20100,
NAKURU
Tel. 0722 807 802

THE SUB COUNTY SOCIAL DEVELOPMENT OFFICER,
P.O. BOX 2815-20100,
NAKURU

Dear Sir/ Madam,

RE: DATA COLLECTION FROM INVESTMENT GROUPS REGISTERED WITH MINISTRY OF LABOUR, SOCIAL SECURITY AND SERVICES DEPARTMENT OF SOCIAL DEVELOPMENT WITHIN NAKURU TOWN

My name is Rose Kirui. I am a student at Egerton University, Nakuru Town Campus undertaking a Masters Degree in Business Administration. I am conducting an academic research to study "***Effect of group composition and formalization on the financial performance of investment groups in Nakuru town, Kenya."*** The findings will help to understand the contribution of group composition and formalization on financial performance of investment groups. Permission has been sought from the relevant authorities. Any information provided by you will be used solely for research purposes and will be treated with utmost confidentiality.

There will be no direct benefits for those participating in the study. In addition there will be no risks involved. All the information gathered in this study will be confidential and will only be used for academic purposes. Respect and dignity will be maintained during the study. Attached is a copy of the study approval from the supervisor.

Thank you in advance for your consideration.

Yours faithfully

....

Rose Kirui.

APPENDIX II: QUESTIONNAIRE 1

SECTION A: INFORMATION ON MEMBERS

From the following questions provided, please tick (√) where appropriate.

Provide the following information.

1. How long have you done investments? ________________

2. Gender. Male [ ] Female [ ]

3. What is your occupation? ________________

4. Do you have any training on business? Yes [ ] No [ ]

5. Your group is ethnically diverse Yes [ ] No [ ]

SECTION B: GROUP COMPOSITION

Please Tick where you think it is appropriate for the following questions.

Where; 1 represents= Strongly Disagree. 2= Disagree 3= Neither Agree nor Disagree, 4= Agree, and 5 represents= Strongly Agree

6.	Young investors do not have business experience	1	2	3	4	5
7.	Young and inexperienced investors have less networks and business contacts	1	2	3	4	5
8.	Investment skills deteriorates with age due to the effects of cognitive aging	1	2	3	4	5
9.	Overconfident investors have less business experience	1	2	3	4	5
10.	Inexperienced investors choose risky investment	1	2	3	4	5
11.	Women tend to possess less business experience than men	1	2	3	4	5
12.	Women have a preference for lower risk investments	1	2	3	4	5
13.	Men are risk takers who trade more than women	1	2	3	4	5
14.	Men are more overconfident than women	1	2	3	4	5
15.	Groups of men and women together are more profitable than single-sex groups	1	2	3	4	5
16.	Men have stronger business network ties with other men than with women	1	2	3	4	5

17.	Business environmental factors influence choice of investment avenues	1	2	3	4	5
18.	Men and women have very different occupational experiences	1	2	3	4	5
19.	Experiences gained in occupations affect decision making in investments	1	2	3	4	5
20.	Young professionals prefer to invest in Real Estate	1	2	3	4	5
21.	There is a significant role of income and occupation in investment avenue selection by the investors.	1	2	3	4	5
22.	Investors with business knowledge have the ability to get appropriate information from the business environment	1	2	3	4	5
23.	Business training lead to changes in business practices for investors who are already in business	1	2	3	4	5
24.	Business training has no impact on business profits,	1	2	3	4	5
25.	Business training enables the entrepreneurs to better identify business opportunities	1	2	3	4	5
26.	There is a significant relationship between financial literacy and investment decisions	1	2	3	4	5
27.	Women, unlike men did not read specialty financial publications	1	2	3	4	5
28.	Conflict of ethnicity can easily lead to management difficulties in an investment group	1	2	3	4	5
29.	Ethnic makeup of local business communities is quite different from that of the population at large	1	2	3	4	5
30.	Members of more "homogeneous" groups, in terms of cultural affiliation, are more likely to save and to repay their loans.	1	2	3	4	5
31.	An ethnic mix brings about a variety in abilities that lead to innovation and creativity	1	2	3	4	5
32.	Traders who start with an ethnic or network advantage grow faster.	1	2	3	4	5

APPENDIX III: QUESTIONNAIRE 2

SECTION C: INFORMATION ON GROUP

From the following, questions provided, please tick (√) where appropriate.

Provide the following information.

1. How long have you carried out your investment business? ________________

2. What proportion is the number of:

Male ________________

Female _______________

3. What type of investment does your group venture in?

Table banking [ ] Real Estate [ ] Financial Securities [ ] Farming [ ]

General business [ ]

SECTION D: GROUP FORMALIZATION

4. What is the organizational form of your group?

Limited liability company [ ] General Partnership [ ] Self – Help [ ]

5. Your group performs financial management Yes [ ] No [ ]

6. Your group prepares budgets and cash flow forecasts? Yes [ ] No [ ]

7. Your group effects working capital management Yes [ ] No [ ]

8. Your group keeps books of accounts Yes [ ] No [ ]

9. Your group's books of accounts get audited Yes [ ] No [ ]

10. Your group receives external financial advice. Yes [ ] No [ ]

11. Your group produces annual financial statements. Yes [ ] No [ ]

12. Your group has the financial statements audited. Yes [ ] No [ ]

13. Your group is registered for tax purposes? Yes [ ] No [ ]

14. Your group makes tax returns? Yes [ ] No [ ]

Please Tick where you think it is appropriate for the following questions.

Where; 1 represents= Strongly Disagree. 2= Disagree 3= Neither Agree nor Disagree, 4= Agree, and 5 represents= Strongly Agree

15.	The choice of organizational form for business is of interest to investors	1	2	3	4	5
16.	Unlimited liability is generally considered burdensome	1	2	3	4	5

17.	The double taxation issue bears quite heavily on the choice of organizational form	1	2	3	4	5
18.	LLC is the most popular form of new business entity	1	2	3	4	5
19.	Financial management is a key aspect of the well-being and survival of a business.	1	2	3	4	5
20.	Best practice in financial management practiced by large corporations can be uses as a benchmark to improve performance in micro and small enterprises	1	2	3	4	5
21.	Cash flow problems of many small businesses are made worse by poor financial management	1	2	3	4	5
22.	The issue of finance has been identified as an immediate reason why businesses in developing countries fail to start or to progress	1	2	3	4	5
23.	Net profit after access to credit from MFIs becomes more than the net profit before such access	1	2	3	4	5
24.	Accountants who are the external advisors may be key agents of change in investment groups	1	2	3	4	5
25.	There is a relative burden of accounts as perceived by small firms.	1	2	3	4	5
26.	MSEs Perceptions of audit costs have a significant relationship with the level of acceptance of audit provisions	1	2	3	4	5
27.	Effective and proper accounting system has a profound impact in successful auditing	1	2	3	4	5
28.	Most of the enterprises produce accounting records, often based on computerized packages	1	2	3	4	5
29.	Small enterprise owners rely on their accountants to prepare their financial statements	1	2	3	4	5
30.	Small enterprise owners are often left bewildered by the complexity of the information provided in financial statements	1	2	3	4	5
31.	Increasing the complexity of reporting requirements for small companies would not necessarily lead to more accurate reporting	1	2	3	4	5

32	Micro and small businesses should produce accounting reports	1	2	3	4	5
33.	Performance of micro and small enterprises is hindered by taxation	1	2	3	4	5
34	Regulatory requirements on business particularly those on MSEs are burdensome	1	2	3	4	5
35.	Registration leads to an increase in profits	1	2	3	4	5
36.	Compliance costs fall disproportionately on small firms	1	2	3	4	5
37.	Tax advantages derived from debt would lead firms to be completely financed through debt	1	2	3	4	5

SECTION E: PERFORMANCE

Please indicate the annual Net profits and capital Investment for your group during 2017

Year	**2017**
	KSHS
Net Profits	
Capital Invested	

APPENDIX IV: RESEARCH PERMIT

THIS IS TO CERTIFY THAT:
MS. ROSE CHEBET KIRUI
of EGERTON UNIVERSITY, 3561-20100
NAKURU,has been permitted to conduct
research in *Nakuru County*

on the topic: *EFFECT OF GROUP COMPOSITION AND FORMALIZATION ON THE FINANCIAL PERFORMANCE OF INVESTMENT GROUPS IN NAKURU TOWN, KENYA*

for the period ending:
18th July,2018

Permit No : NACOSTI/P/17/10930/17078
Date Of Issue : 18th July,2017
Fee Recieved :Ksh 1000

....
Applicant's Signature

...
Director General
National Commission for Science, Technology & Innovation

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RESEARCH CLEARANCE PERMIT

Serial No.A 15039

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