



FACTORS AFFECTING LEASE FINANCING IN THE MANUFACTURING INDUSTRY IN KENYA

Mary Wanjiku Mburu¹, Charles Ngonjo Ngatia²

¹MPH Student: Moi University, Kenya

²Msc Student: University of Nairobi, Kenya

Abstract: Leasing involves a client company entering into a contract with a leaser to get credit for medium or long-term. The client, also known as the lessee, asks the leasing company to acquire assets, which may be movable or immovable, for business purposes. The leaser gives the assets to the lessee for a given time in return for payment in the form of rent. The general objective of this study was to establish the factors affecting lease financing in the manufacturing industry by focusing on Kariobangi Light Industries. The study also sought to determine the effects of access to information, financial resources and tax shield on lease financing in Kariobangi Light Industries. This research study used a descriptive research design. The target population was 300 managers/owners in the firms in Kariobangi Light Industry. The researcher was used a stratified random sampling to select 30% of the target population. The sample size of this study was 90 respondents. The study used primary data which was collected by use of self-administered questionnaires. Content analysis was used in processing of the data and results were presented in prose form. The quantitative data in this research was analyzed by use of descriptive and inferential statistics by use of Statistical Package for Social Sciences (SPSS). Descriptive statistics such as mean, frequency, standard deviation and percentages was used to profile sample characteristics and major patterns emerging from the data. Further, multivariate regression analysis was used to establish the relationship between the dependent and the independent variables. The study also found that financial resources influence lease financing in organizations in the manufacturing industry most followed by access to information and tax shield. The study recommends that leasing companies should hold seminars for manufacturers and train them on the benefits of lease financing. The study also recommends that small manufacturers should adopt leasing financing so as to benefit from tax benefits.

Key Words: Lease Financing, Financial Resources, Access To Information, Tax Shield

Introduction

Leasing is an essential form of financing that is widely accepted. It allows for startups and multinationals to own property, equipment and plant, though for a determined period, without them having to inject a lot of cash. According to Baker and Hayes (2006), classification of lease follows complex rules resulting from either an operating lease or a finance lease. In an operating lease, there is no recording of the leased asset or the obligation to pay for the leased entity on the balance sheet. According to Burgess (2002), leasing is primarily financing based on the asset. In a lease contract, the lessor will retain ownership of the particular asset that he leases throughout the period of that contract (this is different from the usual bank lending where either no security is brought forward or various types of collateral are sued apart from physical assets such as equipment that are generally used in leases). In a traditional bank lending, loan repayment is centered either on the primary source or secondary source, which involves cash flow generation

and credit enhancements respectively. On the other hand, leasing is focused on the ability of the lessee to service payments on the lease by generating cash flows from the operations of the business. During the whole period of the lease, the owner of the asset will retain ownership of the asset (Bierman, 2005). It is, therefore, clear that through leasing, there is a separation of the ownership of the particular asset from its initial economic use. Sometimes, the legal ownership of the leased asset is transferred to the customer at the end of the lease contract. In such a case, the contract is not referred to as a lease.

Contino (2004) says that the lessee will have to pay agreed periodic rentals for using the leased asset based on the arrangements that were made on the contract. The lessor will not rely on the credit history of the lessee for the payment of the periodic rentals, but will rather depend on the ability of the lessee to generate cash flow from the business. Therefore, leasing allows people who could not have been able to borrow from traditional bank lending systems due to the limitation in their credit histories to access the right to use capital equipment (Berger & Udell, 2005). According to Moutot et al. (2007), it is required that the leasing company makes assessment of the physical assets that are to be leased so as to be assured that they will sell on the secondary market. An assessment will also help them realize whether it is possible to lease again the asset in case the customer fails to purchase the asset at the end of the lease.

In financial studies, one cannot say with certainty that leasing and debts are substitutes or even compliments. However, leasing is often considered as an alternative to medium or long term credit (Elgers & Clark, 2010). The idea of the 'world of perfect capital markets' that are discussed by Modigliani and Miller (1958) forms the basis of buying and leasing in the traditional corporate finance. In this context, the value of the firm is not determined by use of the capital structure. This is contrary to the real financial markets that are characterized by imperfections. In the access to finance to being used in business, imperfection in the market may present itself in a deep recession or as a fundamental structural issue that occurs on an ongoing basis (Luke, 2001). Insufficient supplies of capital, as well as inadequacies in demand, are the leading causes of failure in the market. The combination of asymmetric information with uncertainty forms the basis of market failure.

In Kenya, a finance lease is a type of lease where the characteristics that are associated with the ownership of the asset transfer from the lessor to the lessee with the lessor retaining the ownership of the asset. This therefore means that the lessee will continue paying the agreed upon installments for the specified period, regardless of whether the equipment leased to function or not (Pritchard & Hindelang, 2003). In this type of lease, the lessor is limited only to financing the lease. Berger and Udell (2005) reveal that finance lease was developed so that financial institutions that did not have the knowledge regarding equipment could finance equipment-related leases without having to bare basically the risks related to the technical suitability of the equipment that is leased.

Capital leases are sometimes used to refer to finance leases. The term is used to suggest that the lessee is expected to highlight on the leased equipment as a capital entity in the prepared balance sheet (Baker & Hayes, 2006). Basing on the acceptable accounting standard in Kenya, International Accounting Standard (IAS), a capital lease is valid when all the risks and rewards that are associated with the ownership of the leased equipment are transferred to the lessee irrespective of whether the ownership of the equipment is transferred to the lessee or not. The

transfer of risks and rewards in such a case is presumed to happen when the current value of the minimum lease payments is done at the onset of the lease and all the payments made amounts to 90% of the value of the equipment leased.

A finance lease can be compared to a loan in terms of economics, though this is not a legal loan. The periodic rents that are paid by the lessee for a capital lessee are the sum of the cost of the leased equipment together with its interest over the fixed term, also known as the primary period. In the event that the lease will continue past the primary period, and then a reduction in the rent is made as the lessor will have recovered his money (Burgess, 2002). Motor vehicles are normally acquired through finance leases in Kenya by big businesses.

Despite the lack of specific statute that deals with leasing, this practice has been in use for many years in Kenya. The original leasing regulation, section 12, was said to have been misused and thus in 1994, this regulation was repealed. However, In April 2002 the then Kenyan Minister for Finance gazetted the Income Tax Leasing Rules, 2002 in a legal notice No. 52 of the Kenya Gazette. This law targeted the upmarket, but there are institutions that adopted this scheme. In Kenya, the Income Tax Act (CAP 470) and VAT Act (CAP 476) are used in combination to determine the lease transaction in the event that there is no particular statute to govern the lease.

According to Contino (2004), assets that can currently be leased ranges from apartments, formal clothing, limousines, moving vans, appliances, automobiles, art to computers, cameras, furniture, stereos, as well as jewelry. The advantages of leasing involve cash conservations and preservation of the working capital in firms, says Yan (2002). Equipment leasing is advantageous in that it provides a better alternative source of capital as well as a flexible alternative to cash necessary for the acquisition of assets and equipment that are critical to business. Leasing also allows for the smaller or zero marginalized firms to transfer tax shields that are unusable to lessors that pay tax. In turn, they can get lower lease payments. On the other hand, it is argued that leasing is negatively linked to profitability over a period and again linked positively to asset growth. It is however not guaranteed that leases will be terminated before the completion of the original term, and thus the lessor will have to pay off the lease (Erickson, 2004). To this effect, Bierman (2005) claims that this can be a financial challenge for entrepreneurs whose businesses are experiencing a fall.

There are many studies that have been carried out in the field of leasing. For example, Nyachieng'a (2010) did a similar study to identify the determinants of financing lease related contacts among small as well as medium enterprises in Kenya. Another study was conducted by Fatma (2012) as she tried to identify factors that influenced the strategies that medium-sized companies used to lease assets in Kenya. All the same, there are limitations in the literature that talks about lease financing in Kenya and its predisposing factors. In this light, the study aimed at addressing the factors that determine the lease financing within the manufacturing industries, while paying attention to light industries in Kariobangi.

The specific objectives of this study were;

- i. To determine the effects of access to information on lease financing in Kariobangi Light Industries
- ii. To establish the effects of financial resources on lease financing in Kariobangi Light Industries

- iii. To find out the effects of tax shield on lease financing in Kariobangi Light Industries

Theoretical Orientation

According to Cooper and Schindler (2003), a theory refers to a set of statements or principles that are created with the intention of giving meaning to a category of facts or phenomena, more so to that which has been tested over and over again. It can also be used to refer to a phenomenon that is accepted widely and can be used to make effectively predictions on natural occurrences. This study mainly focused on the financial contracting theory and the pecking order theory.

Financial Contracting Theory

Stanton and Wallace (2004) say that financial leasing theory has in the past focused mainly on the differential tax position of the lessee as well as the lessor being the primary rationale behind leasing. The argument has been that if a firm is unable to pay tax fully, then purchasing as well as depreciating an asset may become costly as there is a possibility that only a low capital will be used (Imhoff, Robert & David, 2004). On the other hand, leasing an asset can lead to the lesser making a claim on tax allowance while the tax benefits can in turn be transferred to the lessee indirectly by use of lower lease payments.

Leasing has been viewed widely as being in the category of financial contacting (Standard & Poor's, 2002). Recent studies have given greater emphasis to the abilities of the various types of financial contracts to determine the costs of agency (Gosman & Ernest, 2000). The theory of financial contracting recommends that the characteristics of a company such as business risks should in one way or another affect the contracting costs implying the likelihood of leasing an asset rather than buying it. Asset substitution problems are the conflicts that are raised by the agency costs and suggest that the borrowed capital may be otherwise used to finance other projects that may be riskier or can be used to as dividends to shareholders (Goodacre, 2003). Leasing, on the other hand, addresses these conflicts as the working capital of the company that acted as the lessee is high.

Pecking Order Theory

This order has been widely accepted through numerous researchers. According to Baskin (2002), debt ratios are positively linked to the growth demand and negatively related to profitability. However, a pecking order mechanism as not been used in leasing. There have been concerns that previous studies had purposely omitted the availability of internally generated funds and growth from their models, and thus there have been gross problems in specifications (Sonobe, Akoten & Otsuka, 2011).

Asymmetries in information may lead or contribute to a firm opting for a pecking order approach (Myers & Majluf, 2006). This is to say that information asymmetries available to managers may lead these managers to maintaining a reserved borrowing capacity while avoiding equity markets that are external to the firm (Rao & Drazin, 2002). The pecking order theory implies that individual capital structures will indeed reflect profitability and growth as historically expected rather than an optimal combination of both debt and equity.

In a study conducted by large U.S. firms, Baskin (2002) reports that debt ratios relate negatively to profitability and relate positively to assets growth. In previous literature on leasing, the effects of profitability and growth in leasing were typically ignored, and this resulted in misspecifications thus making the tests unreliable (Pritchard & Hindelang, 2003).

The pecking order theory suggests that leasing is negatively related to profitability and is related positively to asset growth over time. Among the factors that most researchers have agreed upon as being the determinants in leasing is the tax bracket of the lessee. In leasing, it is possible to transfer unusable tax shields for firms with low or zero marginal tax rates, to taxpaying lessors and in turn the lessee pays lower lease payments. To this effect, the tax bracket is said to be negatively related to leasing (Toy et al., 2001).

Conceptual Framework

In this study, financial resources, access to information and the tax shield formed the independent variables. Lease financing among the manufacturing companies was the dependent variable. There seem to be both positive and negative effects of the amount of available financial resources on the acceptability of lease financing. It is evident that small companies need to have access to the relevant information that will assist them in acquiring finances for their businesses as well as in buying equipment. This is due the fact that SMEs have proven to be lacking in the relevant information required in business. However, some businesses may find it uneconomical to lease equipment if at all its income tax liability is high.

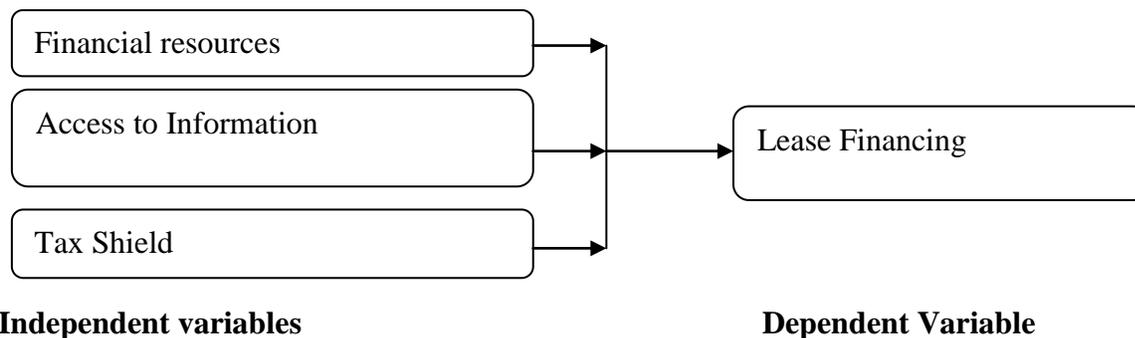


Figure1: Conceptual Framework

Financial Resources

The magnitude of available resources can impact a positive or negative effect on the opportunities identified by entrepreneurs (Hoegl, Gibbert & Mazursky, 2008). Increased amount of resources gives room for more experimentation, and thus there are increased chances of getting more ideas as well as innovation (Paladino, 2007). On the other hand, limitations in resources can create room for creativity. For example, an organization can explore all available avenues to satisfy its needs in the event that it has limited finances and in effect obtain information about lease financing.

According to Ozkan (2001), there is a mix on the impact of resource limitations on the identification of opportunity and the innovative performance that may result therewith. Constraints in the financial resources can limit the ability of the firm to promote innovation that

increases the performance of the organization. A shortage in the number of qualified managers can also restrict the capability of a firm in making right decisions on financing (Rao & Drazin, 2002). Besides, small companies that are limited in resources are unable to hire the required employees that can guide on whether to take a loan or to lease an asset.

According to Nyachieng'a (2012) limitations in resources creates a shift in the attention of entrepreneurs to the opportunities that are related to the various challenges that they are experiencing. The only way to identify this effect is by associating the types of limitations to the different sources of opportunities. This then suggests that the explanation of types-of-resources is unable to present a comprehensive description of the effect of the limitations of resources in identifying opportunities.

One of the major problems that small manufacturing companies face is the lack of finances or the access to credit facilities. This in turn affects the number of choices that a firm can have as regards financing as they do not have many alternatives that they can turn to (Myers & Majluf, 2002). According to Baker (2007) the limitations in the availability of credit forces the entrepreneurs to rely only on finances that are emanating from their savings or in other cases by borrowing from friends and realities.

Access to Information

Moyi (2000) admits that there is a need for small manufacturing companies to acquire information necessary to enable them to make decisions that are related to financing their businesses and in buying equipment. The creation of vibrant SMEs, as well as efficient utilization of useful information on business is essential to achieving long-term, as well as economic growth that is sustainable (Corps, 2005). However, it is evident that most small manufacturing companies in developing countries lack access to quality business information. This information is said to be available to stand-alone institutions. In effect, it is argued that most SMEs rely on informal institutions to provide them with information that is not authenticated to be useful (Okello-Obura et al., 2008). Moutot et al. (2007) admit that SMEs need to have access to information that is made to suit their demands in business financing.

According to Okello-Obura et al. (2008), the information made available to SMEs should be thoroughly researched using local and international information as this will make such SMEs have recognition both locally and on the international arena. There is thus the need for different organizations ranging from professional bodies, private entities, and trade organizations to government departments to freely provide SMEs with relevant information as doing so will assist these enterprises in accessing business finances (Mellahi & Wilkinson, 2010).

Tax Shield

Yan (2002) reveals that the most significant difference between leasing and buying equipment is in the manner in which both are treated as regards income tax. A business with high-income tax might decide not to lease equipment based on its inability to bring forth economic advantage. Uwe (2008) says that the purpose of a leasing company to buy equipment is due to taxes. But because the equipment needs to be used in any way, the company is obliged to lease the equipment to other firms. It has been reported that the majority of businesses can make higher

after-tax costs in buying equipment than the costs faced by the leasing company. This allows the leasing company to divide some of its profits to entrepreneurs while at the same time making a profit.

Leasing has its effects on the cash flows and thus it has an impact on the cost of capital after taxation (Kilpatrick & Nancy, 2007). In leasing, the amounts used to make direct payments and the timings made are crucial (McCue, 2007). In the event that taxation rates for the lessor and the leaseholder are not the same, the leasing operation gives room for a transfer of the effect of the tax shield to be made to the best available company (Kilpatrick & Nancy, 2007). In some instances, it is possible to agree on the conditions that may be advantageous to both the lessor and the leaseholder by use of the leasing tax laws.

According to Katila and Shane (2005), the rules to be applied in determining financial requirements are simplified by the availability of strong tax advantages of leasing. The financial solutions that can give rise to higher tax benefits are used. These solutions are available to the operators in question and considered by the leasing companies in placing their preferred products (Pritchard & Hindelang, 2003).

Tax depreciation is accelerated in comparison to the fundamental rules used in normal depreciation (Imhoff, Robert & David, 2004). This means that a company with tax profits will have to bring forward its costs of tax thus deferring taxable income and the paid taxes (Goodacre, 2003). According to Craig and Schallheim (2006), additional costs are not created in comparison to the purchase that has been financed through borrowing. On the contrary, the deductibility of the costs is generally brought forward, and this is necessary for defining a cost of capital that is not expensive.

Research Methodology

Research design refers to the method used to carry out a research. This research study used a descriptive research design. This design involves gathering data that describe events and then organizes, tabulates, depicts, and describes the data. The study population of this study was all the General Managers / owners in the firms in Kariobangi Light Industry. Kariobangi Light Industry is comprises of informal companies that employ a lot of people. However, these companies do not have enough financial resources and hence they depend highly on loans from microfinance institutions and banks. According the Ministry of Industrialization (2012) there are 300 manufacturing enterprises in Kariobangi Light Industry. The target population of this study was therefore 300 General Managers / owners.

The study used a stratified random sampling to select 30% of the target population. According to Kothari (2004), a method of sampling that involves the division of a population into smaller groups known as strata. In stratified random sampling, the strata are formed based on members shared attributes or characteristics. A random sample from each stratum is taken in a number proportional to the stratum's size when compared to the population. These subsets of the strata are then pooled to form a random sample. According to Mugenda & Mugenda (2003) a sample size of between 10% and 30% is a good representation of the target population. The sample size of this study was therefore 90 General managers/owners.

Table 1: Sample Size

Nature of Business	Target population	Sample Size (30%)
Wood work	28	8
Fabrication of metal products	88	26
Casting or machining of metal parts	54	16
Car repairing	48	14
Soap making	18	5
Hardware Retailing	44	13
Paints manufacturing	6	2
Miscellaneous services	14	4
Total	300	90

Source: Author (2013)

The study used primary data which was collected by use of self-administered questionnaires; the questionnaires included structured and unstructured questions. Questionnaires items may be closed ended or open ended type. As regards to the former, closed ended questions only allowed specific types of responses (such as Yes or No and likert scales) while with respect to the open ended type, the respondents stated responses as they wished. Self-administered questionnaires were preferred in this study because they are very economical in terms of time, energy and finances. The structured questions was used in an effort to conserve time and money as well as to facilitate an easier analysis as they are in immediate usable form; while the unstructured questions were used as they encouraged the respondent to give an in-depth and felt response without feeling held back in revealing of any information.

Data analysis was done after data collection. Qualitative data was checked for completeness and cleaned ready for data analysis. Content analysis was used in processing of the data and results were presented in prose form. The quantitative data in this research was analyzed by use descriptive and inferential statistics by use of Statistical Package for Social Sciences (SPSS). Descriptive statistics such as mean, frequency, standard deviation and percentages were used to profile sample characteristics and major patterns emerging from the data. Data was presented in form of tables and figures. Further, multivariate regression analysis was used to establish the relationship between the dependent and the independent variables. The multivariate regression model was;

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \varepsilon$$

Where: Y = lease financing in manufacturing companies; β_0 = Constant Term; β_1 , β_2 , and β_3 = Beta coefficients; X_1 = Tax shield; X_2 = financial resources; X_3 =access to information; ε = Error term

Results and Discussions

The sample size of this study was 90 General managers/owners, out of which 87 questionnaires were filled and returned which represents a 96.67% response rate. According to Babbie (2002)

any response of 50% and above is adequate for analysis thus 96.67% was even better. The researcher selected a pilot group of 5 individuals from human resource department who were not involved in the main study to test the reliability of the research instrument. The study sought the opinions of experts in the field of study especially the supervisors. The study also made corrections according to the supervisor's guidelines and ensured that the questions were in accordance of the objectives of the study.

A construct composite reliability co-efficient (Cronbach alpha) of 0.6 or above, for all the constructs, is considered adequate. The acceptable reliability coefficient is 0.6 and above, if the Cronbach alpha is below 0.6 the reliability of the questionnaire is considered too low and thus the research tool should be amended. Three constructs were studied. In order to ascertain the extent to which the data collection instrument was reliable in measuring the study constructs (or factors), reliability tests were carried out on measures of financial resources, access to information and tax shield. The findings of the pilot test showed that 'performance metrics' scale had a Cronbach's reliability alpha of 0.713, 'financial resources' scale had an Alpha value of 0.732, 'access to information' had an Alpha value of 0.674 and 'tax shield' had a reliability value of 0.722. This implies that the scales measuring the objectives met the reliability criteria ($\alpha > 0.6$). This therefore indicated that the research tool was sufficiently reliable and valid and needed no amendment.

Table 2: Cronbach's Alpha Values

Construct	Cronbach's Alpha
Financial resources	0.713
Access to information	0.732
Tax shield	0.674

Lease Financing

The respondents were also asked to indicate whether their companies were using lease financing. The findings are shown in figure 1.

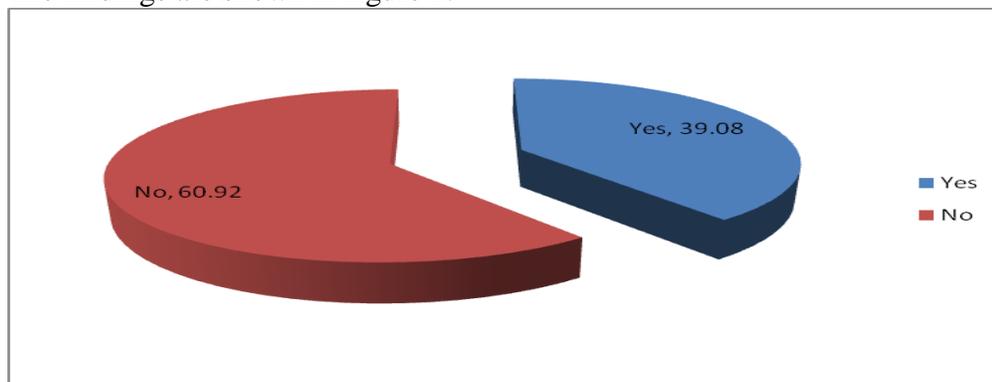


Figure 1: Use of lease financing

From the findings, 60.92% of the respondents indicated that their companies were not using lease financing while 39.08% indicated that their companies were using lease financing. From these findings we can deduce that most of the organisations in this study were not using lease financing. From the respondents who indicated that their companies were using lease financing, the study also sought to establish they were using lease financing in which areas. From the

findings, the respondents indicated that they were using lease financing in equipment, vehicles, land as well as warehouses. The respondents indicated that length of lease term; renewal and purchase options; cancellation provision and penalties; guarantees by lessees of residual values; amount and timing of lease payment; Interest rates; Degree of risk assumed by the lessee; and, payment of certain costs such as maintenance, insurance and taxes were influencing the use of lease financing.

Financial Resources

The study sought to establish the effects of financial resources on lease financing in Kariobangi Light Industries. The respondents were also requested to indicate the extent to which the stated aspects of resources affect the adoption of lease financing in the manufacturing industry.

Table 3: Aspects of Lease Financing

Aspects of resources	Mean	Std Deviation
Collateral	3.45	0.562
Equipments	3.98	0.726
Financial resources	4.01	0.572
Qualified employees	3.87	0.827

According to the findings, the respondents indicated with a mean of 4.01 and a standard deviation of 0.572 that financial resources were influencing adoption of lease financing in the manufacturing industry to a great extent. The respondents also indicated with a mean of 3.98 and a standard deviation of 0.726 that equipment were influencing the adoption of lease financing in the manufacturing industry to a great extent. Further, the respondents indicated with a mean of 3.87 and a standard deviation of 0.827 that qualified employees were influencing the adoption of lease financing in the manufacturing industry to a great extent. Lastly, the respondents indicated with a mean 3.45 and standard deviation of 0.562 that collateral was influencing the adoption of lease financing in the manufacturing industry to a moderate extent.

Access to Information

The study also sought to determine the effects of access to information on lease financing in Kariobangi Light Industries. The respondents were also asked to indicate whether they got financial information and advice from the stated sources.

Table 4: Financial Information and Advice

	Frequency		Percent	
	Yes	No	Yes	No
Libraries	3	84	3.4	96.5
Radio station	42	45	48.2	51.7
Television	45	42	51.7	48.2
Financial Institutions (Banks, MFIs)	56	31	64.3	35.6
Leasing companies	6	81	6.9	93.1

According to the findings, 3.45% of the respondents indicated that they were getting financial information and advice from libraries while 96.55% disagreed. In addition, 48.25% of the respondents indicated that their organizations were getting financial information and advice from radio stations while 51.72% disagreed. Further, 51.72% of the respondents indicated they were

getting financial information and advice from televisions while 48.28% disagreed. Additionally, 64.37% of the respondents indicated that they were getting financial information and advice from financial institutions (banks and MFIs) while 35.63% disagreed. Lastly, 6.9% of the respondents indicated that they were getting financial information and advice from leasing companies while 93.10% disagreed. From these findings we can deduce that most of the companies were getting financial information and advice mostly from financial institutions (banks and MFIs) followed by televisions, radio stations, leasing companies and libraries.

The respondents were further asked to indicate the extent to which the stated aspects of access to information affect lease financing in the manufacturing industry.

Table 5: Aspects of Access to Information

Aspects of Access to information	Mean	Std deviation
Information technology	4.01	0.452
Level of education	3.98	0.625
Credibility of information	3.45	0.672

From the findings, the respondents indicated with a mean of 4.01 and a standard deviation of 0.452 that information technology affects lease financing in the manufacturing industry to a great extent. In addition, the respondents indicated with a mean of 3.98 and a standard deviation of 0.625 that level of education affects lease financing in the manufacturing industry to a great extent. Lastly, the respondents indicated with a mean of 3.45 and a standard deviation of 0.672 that credibility of information affects lease financing in the manufacturing industry to a great extent.

Tax shield

The study also sought to find out the effects of tax shield on lease financing in Kariobangi Light Industries. The respondents were requested to indicate the extent to which lease financing affects the stated factors related to credit risk.

Table 6: Aspects of Tax

	Mean	Std Deviation
Tax depreciation	4.09	0.762
Taxable income	4.01	0.625
Net of tax cost of capital	3.89	0.512
Debt value	3.01	0.423

According to the findings, the respondents indicated with a mean of 4.09 and a standard deviation of 0.762 that leasing financing was influencing tax depreciation to a great extent. In addition, the respondents indicated with a mean of 4.01 and a standard deviation of 0.625 that lease financing was influencing taxable income to great extent. Further, the respondents indicated with a mean of 3.89 and a standard deviation of 0.512 that lease financing was influencing net of tax cost of capital to a great extent. Finally, the respondents indicated with a mean of 3.01 and a standard deviation of 0.423 that lease financing was influencing debt value to

a moderate extent. The findings, the respondents indicated tax benefits that are accrued to lease financing were motivating organizations in the manufacturing industry to adopt lease financing.

Regression Analysis

The researcher conducted a multiple linear regression analysis so as to determine the relationship between the dependent variable (lease financing) and independent variables (financial resources, access to information and tax shield).

The multivariate regression model was;

$$Y = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \varepsilon$$

Where: Y = lease financing in manufacturing companies; β_0 = Constant Term; β_1 , β_2 , and β_3 = Beta coefficients; X1= Tax shield; X2= financial resources; X3=access to information; ε = Error term

Table 7: Model Summary

Model	R	R Square	Adjusted Square	R	Std. Error of the Estimate
1	0.843	0.711	0.709		0.4216

The three independent variables that were studied, explain 71.1% of factors affecting lease financing in organizations in the manufacturing industry as represented by the R^2 . This therefore means that other factors not studied in this research contribute 28.9% of factors affecting lease financing in organizations in the manufacturing industry.

Table 8: ANOVA

	Sum of Squares	df	Mean Square	F	Sig.
Regression	22.340	4	5.585	2.362	.022
Residual	128.639	82	.688		
Total	150.979	86			

The significance value is 0.022 which is less than 0.05 thus the model is statistically significant in predicting how financial resources, access to information and tax shield influence lease financing. The F critical at 5% level of significance was 2.362. Since F calculated is greater than the F critical (value = 2.290), this shows that the overall model was significant.

Table 9: Coefficient of Determination

	Un-standardized Coefficients	Std. Error	Standardized Coefficients	t	Sig.
	B		Beta		
(Constant)	1.344	1.33		1.61	0.02
Tax shield	0.421	0.12	0.265	3.98	0.02
Access to information	0.425	0.24	0.076	3.64	0.02
Financial resources	-0.652	0.22	-0.186	-3.78	0.02

The regression equation was;

$$Y=1.344+ X_10.421 + X_20.425 - X_30.652$$

The regression equation above has established that taking all factors into account (financial resources, access to information and tax shield) constant at zero lease financing in organizations in the manufacturing industry will be 1.344. The findings presented also shows that there is a significant relationship between tax shield and lease financing in organizations in the manufacturing industry as shown by a coefficient of 0.421. In addition, there is a significant relationship between access to information and lease financing in organizations in the manufacturing industry as shown by a coefficient of 0.425. Further, the findings show that there is a significant inverse relationship between financial resources and lease financing in organizations in the manufacturing industry as shown by a coefficient of 0.652. This infers that financial resources influence lease financing in organizations in the manufacturing industry most followed by access to information and tax shield.

Discussion of the Key Findings

The study established that most of the respondents knew what lease financing is. In addition, most of the organisations in this study were not using lease financing and those that were using it were using it in equipment, vehicles, land as well as warehouses. The study further established that factors like length of lease term; renewal and purchase options; cancellation provision and penalties; guarantees by lessees of residual values; amount and timing of lease payment; Interest rates; Degree of risk assumed by the lessee; and, payment of certain costs such as maintenance, insurance and taxes were influencing the use of lease financing. According to Baker & Hayes (2006) leasing is an important and widely used source of financing that enables entities, from start-ups to multinationals, to acquire the right to use property, plant and equipment without making large initial cash outlays. Entities currently account for leases as either operating leases or finance leases.

Financial Resources

The study sought to establish the effects of financial resources on lease financing in Kariobangi Light Industries. The study established that financial resources affect the adoption of lease financing in the manufacturing industry to a great extent. These findings agree with Hoegl, Gibbert and Mazursky (2008) argument that the amount of available resources appears to have both negative and positive effects on opportunity identification by entrepreneurs. In addition, most of the organizations in this study had obtained a loan from banks or MFIs in the last 2 years and had experienced liquidity problems in the last 2 years.

The study also established that financial resources, equipment and qualified employees were influencing the adoption of lease financing in the manufacturing industry to a great extent while collateral was influencing the adoption of lease financing in the manufacturing industry to a moderate extent. These findings concur with Katila and Shane (2005) argument that experienced administrators or finance managers can advise a firm on whether to go for credit or lease financing. On the other hand, resource constraints can spur necessity-driven creativity and lead to identifying promising opportunities.

In relation to the effects of financial resources on lease financing, the study established that when an organization has enough resources it does not need to lease as it can be in a position to acquire. In addition, organizations with collateral can easily obtain loans from banks and by equipment, land or vehicles. According to Rao and Drazin (2002) missing specific capabilities, caused by a shortage of qualified managers and employees, also reduces decision making processes on financing. Rao and Drazin (2002) also argue that small firms with financial constraints are not able to hire the necessary employee, which reduces their ability to weigh between credit and leasing.

Access to Information

The study also sought to determine the effects of access to information on lease financing in Kariobangi Light Industries. The study found that access to information affects lease financing in the manufacturing industry to a great extent. These findings agree with Corps (2005) argument that small manufacturing companies need to have access to adequate information to equip them in making decisions on business financing and buying of equipment. The establishment of an active SMEs sector - and the effective utilization of quality business information - has been identified as crucial in attaining long-term and sustainable economic growth.

It was also established that most of the companies were getting financial information and advice mostly from financial institutions (banks and MFIs) followed by televisions, radio stations, leasing companies and libraries. Okello-Obura et al. (2008) argue that there is a need for collaboration between various industrial and trade organizations, professional bodies, private enterprises and government departments to provide SMEs with a comprehensive range of business information, advice and facilities

Further, the study revealed that information technology, level of education and credibility of information affect lease financing in the manufacturing industry to a great extent. According to Moyi (2000), poor information quality can create chaos. Unless its root cause is diagnosed, efforts to address it can be worthless.

The study also established that most of the managers/owners did not have enough information to make a decision on whether to go for lease financing. Further, most owners/managers were not aware of companies that offering leasing services and were only getting information on loans from MFIs and banks. According to Ladzani (2001), the priority ranking of the SMEs needs, clearly puts information provision at the top of the list of services to be provided. The SMEs development is hampered by an "information-poor" environment. SMEs perform better in information-rich environments

Tax Shield

The study also sought to find out the effects of tax shield on lease financing in Kariobangi Light Industries. The study also found that organizations in the manufacturing industry that were using lease financing were enjoying tax advantages as a result of lease financing. According to Yan (2002), one of the most important economic differences between leasing and buying equipment is the way each is treated for income tax purposes.

It was also established that taxation affects cash flows in organization in the manufacturing industry and lease financing influences the tax benefits of organizations in the manufacturing industry to a great extent. According to Standard & Poor's (2002) the decision to use leasing has various consequences on the cash flows and therefore influences the cost of capital after taxation

The study also revealed that that leasing financing was influencing tax depreciation, taxable income, net of tax cost of capital to a great extent and debt value to a moderate extent. In addition, tax benefits that are accrued to lease financing were motivating organizations in the manufacturing industry to adopt lease financing. Kilpatrick & Nancy (2007) argue that the leasing tax laws make it possible to reach advantageous conditions for both the leaseholder and the lessor, the advantage being divided in accordance with the contractual force of the two parties.

Conclusion

The study concludes that there is a significant relationship between tax shield and lease financing in organizations in the manufacturing industry. In addition, most of the organizations in this study had obtained a loan from banks or MFIs in the last 2 years and had experienced liquidity problems in the last 2 years. The study also established that financial resources, equipment and qualified employees were influencing the adoption of lease financing in the manufacturing industry.

The study also concludes that there is a significant relationship between access to information and lease financing in organizations in the manufacturing industry. It was also established that most of the companies were getting financial information and advice mostly from financial institutions (banks and MFIs). Further, the study revealed that information technology, level of education and credibility of information affect lease financing in the manufacturing industry.

Further, the study concludes that there is a significant inverse relationship between financial resources and lease financing in organizations in the manufacturing industry. It was also established that taxation affects cash flows in organization in the manufacturing industry and lease financing influences the tax benefits of organizations in the manufacturing industry. The study also revealed that that leasing financing was influencing tax depreciation, taxable income, net of tax cost of capital to a great extent and debt value.

Recommendations

This study established that most of the organizations in this study had obtained a loan from banks or MFIs in the last 2 years and had experienced liquidity problems in the last 2 years. This study therefore recommends that even if companies have enough financial resources they should go for lease financing.

The study also found that access to information was influencing the use of lease financing to a great extent. This study therefore recommends leasing companies should embark on marketing their services in television and radio stations. Further, the study recommends that leasing

companies should hold seminars for manufacturers and train them on the benefits of lease financing.

The study also established that tax benefits accrued to lease financing were motivating organizations in the manufacturing industry to adopt lease financing. The study therefore recommends that small manufacturers should adopt leasing financing so as to benefit from tax benefits.

To the policymakers the study recommends that they should increase tax shield for leasing products so as to encourage small-scale manufacturers to make use of leasing financing rather than having high credits.

Areas for Further Studies

From the study and related conclusions, the researcher recommends further research in the area of the effects of lease financing on the financial performance of firms in the manufacturing industry. The study also recommends further studies on the effects of lease financing on the working capital of firms in the manufacturing industry.

References

- Babbie, E. (2002). *Survey research methods* (2nd ed.). Belmont: Wodsworth.
- Baker, C.R., Hayes, R.S. (2006). *Lease Financing: A Practical Guide*. New York, NY: John Wiley & Sons.
- Baker, T. (2007). Resources in play: Bricolage in the Toy Store(y). *Journal of Business Venturing*, 22(5), 694–711.
- Baskin, J. (2002). An Empirical Investigation of the Pecking Order Hypothesis, *Financial Management*, 3(2), 26-35.
- Berger, A. & Udell, G. (2005). A More Complete Conceptual Framework for Financing of Small & Medium Enterprises. *World Bank Policy Research Working Paper No. 3795*. December 2005.
- Bierman, H. (2005). *The Lease versus Buy Decision*. Englewood Cliffs, NJ: Prentice-Hall.
- Burgess, D.O. (2002). Buy or lease: the eternal question. *Journal of Accountancy*, 187(4), 25-33.
- Contino, R.M. (2004). *Negotiating Business Equipment Leases*. New York, NY: Amacom.
- Cooper, D., & Schindler, P. S. (2003). *Business research methods* (8th ed). New Delhi: Tata McGraw-Hill Publishing Company.
- Corps, M. (2005). *Information and communications technologies in small and medium enterprise development*. Retrieved on 19th April from www.globalenvision.org/library/7/698
- Craig, M. L. & Schallheim, S. J. (2006). Are Debt and Leases Substitutes. *Journal of Property Research*, 6(2), 41-49.
- Elgers, P.T. & Clark, J.J. (2010). *The Lease/Buy Decision: A Simplified Guide to Maximizing Financial and Tax Advantages in the 1980s*. New York, NY: The Free Press.
- Erickson, S. M. (2004) An Empirical Investigation of the Cross Sectional Determinants of Lease Use. *Commercial Lending Review*, 15, 53-60.

- Erickson, S.M. & Trevino, R. (2004) A pecking order approach to leasing: The airline industry case. *Journal of Financial and Strategic Decisions*, 7(3), 23-31.
- Goodacre, A. (2003). Assessing the potential impact of lease accounting reform: A review of the empirical evidence. *Journal of Property Research*, 20, 49-66.
- Gosman, M. L. & Ernest I. H. (2000). The impact of leasing on lenders' evaluations of firms' debt levels. *Commercial Lending Review*, 15, 53-60
- Hoegl, M., Gibbert, M. & Mazursky, D. (2008). Financial constraints in innovation projects: When is less more? *Research Policy* 37(8), 1382–1391.
- Imhoff, E. A., Robert C. L. & David, W. W. (2004). Operating leases: Impact of constructive capitalization, *Accounting Horizons*, 5, 51-63
- Katila, R. & Shane, S. (2005). When does lack of resources make new firms innovative? *Academy of Management Journal*, 48(5), 814-829.
- Kilpatrick, B. G. & Nancy L. W. (2007), Off-balance-sheet financing & operating leases impact on lessee financial ratios. *RMA Journal* 89, pp. 80-87
- Kothari, C. R. (2004). *Research methodology: Methods and techniques*. New Delhi: New Age International (P) Limited Publishers.
- Luke, R. (2001). Leasing gridlock. *Banking Strategies*, 77(2), pp.32-6.
- McCue, M. J. (2007). Factors Associated with Lease Financing in the Hospital Industry. *Journal of Health Care Finance*, 33(3), 72-84.
- Mellahi, K. & Wilkinson, A. (2010). A study of the association between level of slack reduction following downsizing and innovation output. *Journal of Management Studies*, 47(3), 483-508.
- Ministry of Industrialization (2012). Small and Large Manufacturing companies www.industrialization.go.ke/
- Modigliani, F. & Miller, M. (1958). The Cost of Capital, Corporation Finance and the Theory of Investment. *American Economic Review*, 48(3), pp. 261-297.
- Moutot, P., Gerdesmeier, D., Lojschová, A. & von Landesberger, J. (2007). The role of other financial intermediaries in monetary and credit developments in the Euro Area. *American Economic Review*, 48(3), 261-297.
- Moyi, E. (2000). *An analysis of the information-search process in micro and small manufacturing enterprises*. Retrieved on 19th April from <http://www.ipar.or.ke/dp15.pdf>
- Mugenda, O. M., & Mugenda, A. G. (2003). *Research methods: Quantitative and qualitative approaches*. Nairobi: Acts Press.
- Myers, S.C. & Majluf N.S. (2006), Corporate Financing and Investment Decisions When Firms Have Information That Investors Do Not Have. *Journal of Financial Economics*, 23, 187-221.
- Myers, S. C., & N. S. Majluf, (2002). Corporate financing and investment decisions when firms have information that investors do not have. *Journal of Financial Economics*, 7(2), 187-221.
- Nyachieng'a, W. M. (2012). *Determinants of lease financing in Kenya: a case of small and medium enterprises in Kisii municipality*. Kenyatta University. Unpublished Research Project.
- Okello-Obura, C., Minishi-Majanja, M. K., Cloete, LM. & Ikoja-Odongo, J. R. (2008). Proposed Business Information System Design (BISD) for Small and Medium Enterprises (SMEs) in Northern Uganda, Libri. *International Journal of Libraries and Information Services*, 59(1), 34-38

- Ozkan, A. (2001) Determinants of Capital Structure and Adjustment to Long Run Target: Evidence from UK Company Panel Data. *Journal of Business and Accounting*, 28(1), 175-198.
- Paladino, A. (2007). Investigating the drivers of innovation and new product success: A comparison of strategic orientations. *Journal of Product Innovation Management* 24(6), pp. 534-553.
- Pritchard, R.E. & Hindelang, T.J. (2003). *The Lease/Buy Decision*. New York, NY: Amacom.
- Rao, H. & Drazin, R. (2002). Overcoming resource constraints on product innovation by recruiting talent from rivals: A study of the mutual fund industry, 1986-94. *Academy of Management Journal*, 45(3), 491-507.
- Sonobe, T., Akoten, J. & Otsuka, K (2011). The growth process of informal enterprises in Sub-Saharan Africa: A case study of a metalworking cluster in Nairobi. *Small Business Economics*, 36(3), 323-335.
- Standard, L. & Poor's, K. (2002). *CreditStats operating lease analytical model*. New York: Standard & Poor's.
- Stanton, R. & N. Wallace, (2004), An Empirical Test of a Contingent Claims Lease Valuation Model. *Economics*, 31(3), 313-315.
- Toy, N., Arthur, S., Lee, R., Richard, W., & Theo, B. (2001). A Comparative International Study of Growth, Profitability, and Risk as Determinants of Corporate Debt Ratios in the Manufacturing Sector. *Journal of Financial and Quantitative Analysis*, 2, 875 -886.
- Uwe, R. F (2008). Impact of lease capitalization on financial ratios of listed German companies. *Simply the best research*, 60(1), 122-144.
- Yan, A. (2002). Leasing and Debt Financing: Substitutes or Complements? *Journal of Financial and Quantitative Analysis*, 3(4), 56-61