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Financial Literacy and Growth of Medium Enterprises in Kisumu County, Kenya

Gideon Obota Ochola[1], Caroline Kimutai[2]
[1,2]Department of Accounting and Finance, School of Business, Economics and Tourism, Kenyatta University
Corresponding email: ocholagideon@yahoo.com

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Abstract

This study investigated the impact of financial literacy on the growth of medium-sized enterprises (MEs) in Kisumu County, Kenya. Specifically, it assesses four dimensions of financial literacy, investment literacy, working capital management literacy, accounting knowledge, and financial analysis skills, and their association with enterprise growth. A descriptive research design was applied, and structured questionnaires were distributed to a stratified sample of 400 registered MEs, yielding 112 usable responses. Data were analyzed employing descriptive statistics, Pearson's correlation coefficient, and multiple regression analysis. Results indicate that overall financial literacy explains 60.3% of the variation in enterprise growth ($R^2 = 0.603$). Working capital management literacy, accounting knowledge, and financial analysis skills had statistically significant positive effects on growth, whereas investment literacy did not have a significant effect. The study recommends targeted capacity building in practical financial management skills for ME owners and calls for further research to investigate additional factors explaining the remaining variance of 39.7% in growth.

Keywords: *Financial literacy, Medium enterprises, Enterprise growth, Working capital management, Accounting knowledge, Financial analysis, Kisumu County*

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1. Introduction

Medium Enterprises (MEs) are widely recognized as engines of economic development. In Kenya, MEs form a substantial portion of the private sector, contributing to employment creation, income generation and local economic dynamism. Their roles encompass job creation for youth and women, mobilization of local resources, and promotion of entrepreneurship that supports regional development. Despite their importance, many MEs face persistent challenges that constrain their growth, including limited access to finance, weak managerial capacity, and inadequate financial record-keeping.

Financial literacy, defined as the ability to obtain, process and understand basic financial information for decision making, has been identified as a core capability that influences how entrepreneurs plan, invest, and manage day-to-day finances. Empirical evidence from both developed and developing countries shows that higher financial literacy levels among business owners are associated with better financial management practices, improved access to credit, and enhanced firm performance (Lusardi & Mitchell, 2014; Abdallah, 2024). For MEs operating under tight liquidity constraints, practical competencies such as working capital management and basic accounting are especially important for survival and growth.

This study focuses on Kisumu County, a regional commercial hub in western Kenya, where MEs play a significant socio-economic role but often exhibit varying performance levels. Local studies on financial literacy and ME performance remain limited and heterogeneous, creating a knowledge gap about which specific financial skills most strongly influence growth. By disaggregating financial literacy into investment literacy, working capital management literacy, accounting knowledge, and financial analysis skills, this research aims to provide actionable insights for policymakers, business development service providers, and enterprise owners in Kisumu and similar contexts.

1.1 Objectives of the Study

1. To examine the effect of investment literacy on the growth of medium enterprises in Kisumu County.
2. To assess the influence of working capital management literacy on the growth of medium enterprises in Kisumu County.
3. To determine the impact of accounting knowledge on enterprise growth in Kisumu County.
4. To evaluate the contribution of financial analysis skills to the growth of medium enterprises in Kisumu County.

1.2 Hypotheses

H_{01}: Investment literacy has no significant effect on the growth of medium enterprises in Kisumu County.

H_{02}: Working capital management literacy has no significant effect on the growth of medium enterprises in Kisumu County.

H_{03}: Accounting knowledge has no significant effect on enterprise growth in Kisumu County.

H_{04}: Financial analysis skills have no significant effect on the growth of medium enterprises in Kisumu County.

2. Literature Review

2.1 Theoretical Review

The study is grounded in multiple complementary theories. First, Dual Process Theory (Kahneman & Tversky, 1979; Glaser & Walther, 2013) posits that decision-making arises from the interaction between intuitive and analytical cognitive processes. In the context of financial decision-making by entrepreneurs, this theory suggests that both heuristic (experience-based) and deliberative (analytical) approaches shape investment and management choices. Financial literacy strengthens the analytical process, enabling entrepreneurs to complement intuition with systematic evaluation.

Second, the Knowledge Spillover Theory (Romer, 1986) highlights how information diffusion — via networks, training, or sectoral interactions — creates productive externalities. For MEs, spillovers from formal training programs, peer learning, and advisory services can transmit financial management practices that uplift firm-level performance. This theory underpins the expectation that improvements in accounting practices and financial analysis skills can spread across enterprises and improve growth prospects.

Third, Financial Literacy and Behavior frameworks link knowledge to financial behaviors such as budgeting, saving, and prudent credit management; these behaviors mediate the relationship between knowledge and outcomes. Additionally, Stages of Growth theories (e.g., Greiner, 1972; Rostow adaptations) emphasize that firms progress through phases where different managerial competencies become salient. Together, these perspectives justify examining distinct financial literacy dimensions, each may be more or less relevant at particular growth stages of MEs.

2.2 Empirical Review

Studies linking investment literacy to firm outcomes present mixed evidence. Husnan (2012) found that investment efficiency positively influenced firm value among listed firms in Iran, while Nunoo and Andoh (2015) indicate that investment knowledge correlates with greater participation in formal investment avenues. Locally, Muigai and Muigai (2018) and IJARPR reports on Kisumu boda-boda operators suggest that investment decisions among small operators are constrained by liquidity and access to formal investment products.

Extensive literature demonstrates the importance of working capital management (WCM) for SME performance. Padachi (2006) identified that efficient management of receivables and inventories is positively associated with profitability, and Abuzayed (2012) reported similar findings in emerging markets. In the Kenyan context, Kangangi (2020) found that cash management practices had a significant positive effect on the growth of SMEs in Nyeri County, while Muneria and Otinga (2019) reported that financial literacy, together with WCM practices, positively influenced the financial growth of small businesses in Kakamega County.

Accounting knowledge and formal record-keeping enable reliable financial planning and access to credit. Nyathi et al. (2018) in Zimbabwe documented that accounting information systems improved decision-making in SMEs, and Onaolapo et al. (2011) observed in Nigerian SMEs that robust accounting systems are linked to better performance. In Kenya, studies of record-keeping practices (e.g., Mutiso & Muigai, 2018) report that bookkeeping correlates with improved financial outcomes and creditor confidence.

Financial analysis skills, the ability to interpret ratios and performance indicators, are associated with improved profitability and risk management (Ross et al., 2006; Georgeta & Elena, 2016). Recent reviews (Abdallah, 2024) confirm that entrepreneurs who frequently perform financial analysis report stronger firm performance, particularly where access to external advisory services is limited.

3. Methodology

A descriptive research design was used. The target population comprised 400 registered medium enterprises in Kisumu County. A stratified random sampling technique yielded 112 usable responses. Data were collected via structured questionnaires measuring four financial literacy subscales (investment literacy, working capital management literacy, accounting knowledge, and financial analysis skills) and enterprise growth (annual sales). Reliability tests yielded Cronbach's alpha exceeding 0.70 for all scales. Data analysis used SPSS to compute descriptive statistics, Pearson correlations, and multiple regression; diagnostic checks included variance inflation factors (VIF), Breusch–Pagan test for heteroscedasticity, and tests of normality.

4. Results and Discussion

4.1 Descriptive statistics

Table 1: Descriptive statistics for study variables

Variable	Mean	Std. Dev.	N
Investment literacy	3.40	0.87	112
Working capital management literacy	3.60	0.90	112
Accounting knowledge	3.70	0.92	112
Financial analysis skills	3.70	1.00	112
Enterprise growth (annual sales index)	3.85	1.05	112

The means indicate respondents report moderate familiarity with most financial competencies; working capital, accounting and financial analysis skills register slightly higher means than investment literacy.

4.2 Correlation Analysis

Table 2: Pearson correlation matrix

Variable	1 Invest	2 WCM	3 Acct	4 FinAnal	5 Growth
Investment literacy	1.00	0.28	0.22	0.25	0.05
Working capital management literacy	0.28	1.00	0.45**	0.43**	0.48**
Accounting knowledge	0.22	0.45**	1.00	0.50**	0.54**
Financial analysis skills	0.25	0.43**	0.50**	1.00	0.50**
Enterprise growth	0.05	0.48**	0.54**	0.50**	1.00

(n = 112) — correlations significant at $p < 0.01$ are marked with **

Working capital management literacy, accounting knowledge, and financial analysis skills show moderate positive correlations with enterprise growth ($r = 0.48–0.54$, $p < 0.01$). Investment literacy exhibits a negligible correlation with growth, consistent with regression results.

4.3 Regression Analysis

Table 3: Multiple regression predicting enterprise growth (n = 112)

Predictor	B	β	t	p
Constant	1.210		3.45	0.001
Investment literacy	-0.005	-0.002	-0.07	0.947
Working capital management literacy	0.085	0.094	2.14	0.034
Accounting knowledge	0.012	0.013	2.05	0.042
Financial analysis skills	0.044	0.046	2.35	0.021

$R = 0.776$, $R^2 = 0.603$, Adjusted $R^2 = 0.586$, $F (4,107) = 40.8$, $p < 0.001$. Financial literacy variables collectively explain 60.3% of the variance in enterprise growth. Working capital management literacy, accounting knowledge, and financial analysis skills had statistically significant positive effects; investment literacy did not.

4.4 Discussion

The findings emphasize the primacy of operational financial skills for medium enterprise growth in Kisumu County. The significant predictors, working capital management literacy, accounting knowledge, and financial analysis skills are consistent with regional studies (Kangangi, 2020; Muneria & Otinga, 2019) that highlight cash management and bookkeeping as central to SME resilience. The nonsignificant effect of investment literacy may reflect liquidity constraints and limited formal investment opportunities for medium enterprises in the locality.

5. Conclusion

Financial literacy contributes meaningfully to enterprise growth in Kisumu County, with practical competencies being more influential than investment literacy. Interventions should focus on working capital and accounting capacity building.

6. Recommendations

1. Based on the study findings, policymakers, financial institutions, business development agencies, and entrepreneurs should prioritize enhancing financial literacy and strengthening financial management practices, particularly in working capital management and accounting.
2. Develop short courses and practical workshops on cash and inventory management tailored to the needs of medium enterprises.
3. Promote user-friendly accounting templates and low-cost bookkeeping solutions to improve financial record-keeping.
4. Facilitate access to financial advisory services that enable entrepreneurs to apply basic financial analysis in decision-making.

5. Encourage entrepreneurs to routinely adopt financial analysis practices to anticipate risks and identify growth opportunities.
6. Conduct studies to explore why investment literacy had no significant effect and to investigate additional factors explaining the remaining 39.7% of variance in enterprise growth.
7. Promote future research using panel or experimental designs to isolate causal pathways and strengthen the evidence base.

6.1 Contribution to Knowledge

This study extends the application of financial literacy theories to medium enterprises in Kisumu County. It provides the novel insight that investment literacy does not significantly influence enterprise growth in this context, highlighting a unique, context-specific finding that informs both theory and practice.

6.2 Suggestions for Further Research

Future studies should investigate the reasons why investment literacy had no significant effect and explore additional factors that may explain the remaining 39.7% of unexplained variance in enterprise growth.

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