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Digital Lending and Financial Performance of Small Retail Businesses in Nairobi Central Business District, Kenya

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Abstract

Digital lending has become a central feature of the global financial system, driven by fintech innovation, mobile technology, and expanded digital access. In Kenya, the rapid growth of digital lending platforms has provided an alternative source of financing for small retail businesses, particularly those operating in Nairobi Central Business District (CBD), where access to traditional bank credit remains limited. Despite high adoption rates, empirical evidence on the effect of digital lending on firm-level financial performance remains limited, especially among urban retail enterprises. This study examined the relationship between digital lending and the financial performance of small retail businesses in Nairobi CBD, Kenya. The study focused on digital loan accessibility, loan usage in business operations, and the cost of digital lending, and their influence on profitability, liquidity, and sales growth. A positivist research paradigm and descriptive research design were adopted. The target population comprised approximately 3,500 small retail businesses, from which a simple random sample of 400 businesses was selected. Primary data were collected using structured questionnaires, yielding 360 valid responses. Data were analyzed using descriptive statistics, correlation analysis, and multiple regression analysis with the aid of SPSS. Correlation results revealed that digital loan accessibility exhibited a moderate to strong positive relationship with financial performance ($r = 0.56$, $p < 0.01$), while loan usage in business operations also showed a positive and statistically significant relationship ($r = 0.41$, $p < 0.01$). Conversely, the cost of digital lending was negatively and significantly correlated with financial performance ($r = -0.48$, $p < 0.01$). Regression analysis further established that digital loan accessibility and loan usage had positive and significant effects on financial performance, whereas the cost of digital lending had a negative and significant effect. The digital lending variables explained approximately 50 percent of the variation in financial performance. The study concludes that digital lending plays a significant role in enhancing the financial performance and operational sustainability of small retail businesses in Nairobi CBD. However, high borrowing costs substantially limit these benefits. The study recommends stronger regulation of digital lending platforms, improved pricing transparency, and prudent borrowing practices among small retail business owners.

1. Introduction

One of the most rapidly expanding sectors of finance in the world is digital lending. The global fintech sector has transformed the credit issuance model through mobile and online technologies that have been applied to provide faster loan issuance, reduced the process of applying, and made it more accessible to a wide audience compared to the traditional banking model. In other markets, including Europe and North America, marketplace lending platforms and digital lenders have grown at a remarkable rate, with digital credit constituting a substantial amount of unsecured credit to consumers and small businesses. Although international statistics show mixed data depending on the areas, a consistent trend is the rise of credit digitalization as the number of smartphone users and those with access to the internet increases throughout the world.

Over the last decade, digital credit in Sub-Saharan Africa has grown exponentially due to mobile money, fintech innovation, and high unbanked numbers. Millions of digital loans have been given out every year by countries like Nigeria, Ghana and Kenya where digital lenders have been central to bridging credit access gaps by households and small businesses that experience barriers to accessing traditional bank credit (Anunda & Kithandi, 2025). Such as example, in Nigeria, digital lending conducted through digital platforms issued around USD 865 million in 2025 and this portrays the magnitude and high rate of uptake of digital financial services in the region (Finance in Africa, 2026).

Kenya has emerged as a leading figure in innovation in the field of fintech in Africa. The digital lending sector of the country is growing at a steep rate, and the regulations have been acknowledged and have become part of the formal financial system (Kithandi, 2023). As of mid-2025, over 5.5 million loans amounting to about Ksh 76.8 billion (approximately USD 594 million) have been issued by licensed digital lenders in Kenya (Silicon Africa, 2025). This has been facilitated by the developed mobile money infrastructure in Kenya and a rise in the number of people owning smart phones, which have made digital credit accessible to wide sections of the population including small business owners (Fintech Magazine Africa, 2025: Nzuki & Kithandi, 2025)

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At the national level, Nairobi Central Business District (CBD) stands as Kenya's primary commercial hub. It hosts a dense concentration of small retail businesses that are key economic actors, contributing substantially to employment generation and local economic activity. These businesses range from kiosks and shops to service providers operating in a highly competitive urban environment. Despite their economic importance, small retail businesses often struggle with limited access to formal financing due to stringent collateral requirements and complex banking procedures (Jesse & Kithandi, 2024). Digital lending platforms offer an alternative source of capital, enabling quicker access to funds that may support working capital, inventory purchases, or expansion plans.

Small retail enterprises are very important in the urban economy of Nairobi CBD and constitute a sizable portion of micro-enterprises that lead to local trade and help in livelihoods. Their financial performance in terms of profitability, liquidity and sales growth is crucial in terms of business survival, as well as, economic stability in a wider region (Kithandi & Ondabu, 2024). Although there is high adoption of digital lending by the venture, as well as by small business owners, scanty empirical studies on the impacts of such credit on quantifiable business performance in the Nairobi CBD have been carried out. Kithandi & Kithandi, the given work is thus devoted to the exploration of the connection between digital lending and the financial performance of small retailers within Nairobi CBD, Kenya, to fill the gap in the current research and have a policy and practice supported by evidence.

1.2 Statement of the Problem

In Kenya, digital lending has grown quickly in the last decade and it is embraced by infrastructures of mobile money and the increased smartphone access. Mobile financial services in Kenya are known to be a world leader, and many developing economies have a low digital financial inclusion rate (World Bank, 2022). The combination of credit services and mobile platforms has helped millions of people and companies to get short-term loans in real time. According to the latest regulatory announcements, the Central Bank of Kenya has approved many digital credit providers, which means the official saturation and further development of the industry (Central Bank of Kenya, 2023).

Small retail ventures in the Nairobi Central Business District are an important source of employment and local economic development. Nevertheless, formal bank credit is still limited because of collateral and complicated processes, and expensive transactions (World Bank, 2020). Alternative working capital sources in these enterprises have thus been manifested in digital lending platforms. Mobile-based loans are often used by entrepreneurs to acquire stock, cover cash flow disruptions, or address short-term operational requirements.

Although there has been fast adoption of digital credit, there is now worry on high interest rates, short repayment terms, multiple borrowing, and over-indebtedness among borrowers (Central Bank of Kenya, 2021). Although access to finance through digital lending is better than nothing, it is not the sole metric that can be converted into better business results. The extant research on Kenya is mostly based on financial inclusion, or overall SME access to credit, but does not investigate actual financial performance indicators (profitability, liquidity and sales growth) (Kithandi & Kithandi, 2024). Furthermore, there are only a few empirical studies that focus on small retail firms in Nairobi CBD as a unique business hub.

This creates a critical knowledge gap. Although digital lending is widely used by small businesses in Nairobi CBD, there is insufficient localized empirical evidence on whether and how such credit influences their financial performance. Without clear evidence, policymakers and regulators cannot effectively assess whether digital lending enhances business sustainability or increases financial vulnerability among small retail enterprises (Oino & Kithandi, 2025).

This study therefore seeks to examine the relationship between digital lending and the financial performance of small retail businesses in Nairobi CBD, Kenya, by focusing on specific performance indicators including profitability, liquidity, and sales growth.

1.3 Purpose of the Study

To examine the relationship between digital lending and the financial performance of small retail businesses in Nairobi CBD, Kenya.

1.4 Research Hypothesis

Ho: There is no significant the effect of digital lending on the financial performance of small retail businesses in Nairobi CBD, Kenya.

1.5 Conceptual Framework

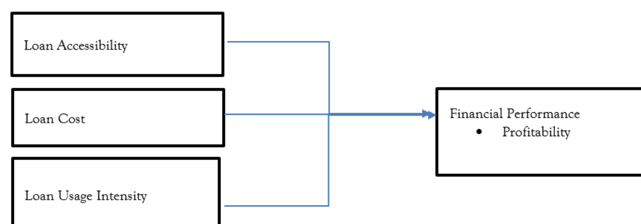

Figure 1: Conceptual Framework

2. Literature and Theoretical Review

2.1 Theoretical Literature

Financial intermediation Theory

Financial Intermediation Theory, originally advanced by Gurley and Shaw (1960) and later refined by Diamond (1984), explains the existence and importance of financial intermediaries in an economy. The theory argues that intermediaries such as banks and other financial institutions play a crucial role in channeling funds from surplus units (savers) to deficit units (borrowers) by reducing transaction costs, managing risks, and addressing information

asymmetries. In modern financial systems, technological advancement has expanded the scope of intermediation, giving rise to digital lending platforms that perform similar intermediary functions using mobile technology and data analytics.

The central argument of Financial Intermediation Theory is that financial markets are imperfect, mainly due to information asymmetry between borrowers and lenders. Borrowers typically possess more information about their financial condition and repayment ability than lenders, making direct lending inefficient and risky. Financial intermediaries emerge to bridge this gap by screening borrowers, monitoring loan use, and diversifying risks across many clients. In the context of digital lending, platforms use alternative data such as mobile money transaction histories and digital footprints to assess creditworthiness, thereby extending credit to small retail businesses that lack formal credit records or collateral.

The theory rests on several assumptions. It assumes that intermediaries have superior access to information, technology, and expertise compared to individual market participants. It also presumes that efficient intermediation leads to improved allocation of resources and that borrowers will use the funds productively to enhance their financial performance. Additionally, the theory assumes rational behavior on the part of both lenders and borrowers, and that the benefits of reduced transaction costs and improved access to credit outweigh the costs associated with borrowing.

Despite its strengths, Financial Intermediation Theory has been critiqued for being overly optimistic about the efficiency and benevolence of intermediaries (Kithandi, 2025). The theory does not sufficiently account for situations where intermediaries prioritize profit maximization at the expense of borrowers, leading to high interest rates and unfavorable loan terms. In digital lending, especially in developing economies such as Kenya, short repayment periods and high effective interest rates can place significant financial pressure on small retail businesses. The theory also underplays the risks of over borrowing and debt dependence that may arise due to the ease and speed of accessing digital credit, as well as the impact of limited financial literacy among small business owners.

Financial Intermediation Theory is highly relevant to the current study on digital lending and the financial performance of small retail businesses in Nairobi Central Business District, Kenya. Digital lenders act as financial intermediaries by bridging the financing gap faced by small retail businesses that are often excluded from traditional banking systems. The theory provides a useful framework for understanding how digital lending can enhance access to working capital, improve liquidity, and support business operations. Kithandi (2025) asserts that theory of financial intermediation: At the same time, it offers a basis for examining whether the cost and structure of digital loans undermine profitability and long-term financial sustainability. As such, Financial Intermediation Theory provides a strong conceptual foundation for analyzing the relationship between digital lending and financial performance among small retail businesses in Nairobi CBD.

2.2 Empirical Literature

Globally, empirical studies show that digital lending has significantly influenced the financial performance of small and medium enterprises (SMEs), particularly in developing and emerging economies. In India, Ghosh and Vinod (2017) used a quantitative cross sectional survey design to examine the effect of digital lending on SME performance. Data were collected from small business owners through structured questionnaires and analyzed using regression analysis. The study found that access to digital loans significantly improved working capital availability and short term sales growth, though high interest rates constrained net profitability for small retail firms.

In China, Chen, Huang, and Ye (2021) adopted a panel data econometric approach, analyzing secondary financial data from digitally funded small enterprises over multiple years. Using fixed effects regression models, the study established that fintech credit eased financing constraints and positively influenced liquidity and revenue growth. The methodology enabled the authors to observe performance changes over time, although the study acknowledged that excessive borrowing increased financial risk for smaller firms.

In developed economies, studies largely rely on secondary data analysis and econometric modeling. Beck et al. (2018) examined European SMEs using bank and fintech lending datasets and applied regression and matching techniques to assess performance outcomes. Their findings showed improved credit access and operational efficiency but insignificant long term profit effects. Similarly, Jagtiani and Lemieux (2019) used logistic and regression analysis on U.S. fintech lending data and found that while fintech lenders expanded credit access, high pricing reduced performance gains for small retail businesses.

In Ghana, Agyekum, Frempong, and Mensah (2020) employed a descriptive cross sectional survey targeting SMEs engaged in retail trade. Primary data were collected using structured questionnaires and analyzed using descriptive statistics and multiple regression analysis. The study found that mobile loans improved business liquidity and stock turnover, but high loan costs negatively affected profit margins.

In Nigeria, Ozili (2018) adopted a conceptual and empirical mixed methods approach, combining secondary fintech adoption data with regression analysis. The study established a positive relationship between digital lending and SME revenue growth, but highlighted regulatory weaknesses that exposed firms to high borrowing risks. The methodology allowed broad sectoral analysis but did not focus specifically on retail enterprises. In Tanzania, Mndeme and Mutalemwa (2021) used a descriptive survey design to study micro and small enterprises, collecting primary data through questionnaires. Correlation and regression analysis revealed that mobile loans enhanced cash flow stability and sales growth, although weak financial literacy increased loan default risks. The limitation of the study was its reliance on short term performance measures.

Okemwa (2020) examined the effect of mobile lending on micro and small enterprises in Nairobi Central Business District using a descriptive survey research design. Data were collected through structured questionnaires from business owners and analyzed using descriptive statistics and multiple regression. The study found that mobile lending significantly enhanced liquidity and business continuity, though profitability was affected by high interest rates and short repayment periods. Maina (2022) investigated the influence of digital credit on SME performance in Nairobi County using a quantitative descriptive design. The study sampled SME owners using stratified random sampling and analyzed data using SPSS through correlation and regression analysis. Findings showed that digital credit improved sales growth and cash flow management, but multiple borrowing reduced net financial performance.

Ndungu, Kithandi, and Onchomba (2025) examined Cost Leadership Strategies and Credit Access Among Micro, Small, and Medium Enterprises in Nairobi City County, Kenya. The study adopted a descriptive research design and collected primary data from MSME owners and managers using structured questionnaires. Data were analyzed using descriptive statistics, correlation, and multiple regression analysis.The findings indicated that cost leadership strategies had a positive and statistically significant influence on access to credit. MSMEs that practiced cost minimization, efficient inventory management, and operational efficiency were more likely to secure external financing due to improved cash flows and increased lender confidence. However, limited managerial capacity and high operating costs constrained the effectiveness of these strategies for some enterprises. The study is relevant in demonstrating that internal business strategies affect access to finance. However, it focused on cost leadership rather than digital lending and did not examine the effect of accessed credit on financial performance. Additionally, it analyzed MSMEs broadly across Nairobi City County, whereas the present

study focuses specifically on digital lending and financial performance of small retail businesses in Nairobi CBD, thereby extending this literature.

Musa and Njeru (2023) adopted a descriptive research design to study digital financial innovation among SMEs in Nairobi City Centre. Primary data were collected using questionnaires and analyzed using regression analysis. The study established that online lending had a statistically significant positive effect on financial performance, while other digital financial services had insignificant effects. Murage (2021) examined mobile loans and SME performance in Nairobi County using a descriptive survey methodology. Data were analyzed using both descriptive and inferential statistics. The study found a positive relationship between loan accessibility and profitability, although inadequate financial literacy hindered effective loan utilization.

Terry, Kithandi, and Onchomba (2025) conducted a study titled "Fintech Adoption and Credit Access of Micro, Small, and Medium Enterprises in Nairobi City County, Kenya." The study examined the extent to which adoption of financial technology influences access to credit among MSMEs operating within Nairobi City County. The study adopted a descriptive research design and targeted micro, small, and medium enterprises across various sectors within Nairobi City County. Primary data were collected using structured questionnaires administered to MSME owners and managers. Data analysis was conducted using descriptive statistics and inferential techniques, including correlation and regression analysis, to establish the relationship between fintech adoption and access to credit. The findings revealed that fintech adoption had a positive and statistically significant effect on access to credit among MSMEs. Specifically, the study established that the use of mobile money platforms, digital banking services, and online lending applications significantly improved loan accessibility by reducing documentation requirements, approval time, and transaction costs. MSMEs that actively adopted fintech solutions were more likely to obtain credit compared to those relying solely on traditional banking channels. However, the study also noted that despite improved access to credit, high borrowing costs and short repayment periods associated with some fintech credit products posed challenges for MSMEs. While fintech platforms enabled faster access to loans, some enterprises experienced debt stress due to expensive loan terms, highlighting the need for responsible borrowing and improved fintech regulation.

Chemaket and Kithandi (2025) examined Credit Access and Financial Performance of Micro, Small, and Medium Enterprises in Dagoretti North Sub County, Kenya. The study adopted a descriptive research design and collected primary data from MSME owners and managers using structured questionnaires. Data were analyzed using descriptive statistics, correlation, and multiple regression analysis to assess the effect of credit access on financial performance. The findings revealed that access to credit had a positive and statistically significant effect on financial performance. MSMEs with access to external finance reported improved liquidity, better working capital management, and increased profitability. Timely credit access enabled businesses to replenish stock, meet operational expenses, and respond to market opportunities. However, high interest rates and rigid repayment conditions were found to strain cash flows, particularly for smaller enterprises, indicating that credit affordability influences sustainability. The study is relevant as it provides empirical evidence linking credit access to improved MSME performance. However, it focused on general credit access and did not isolate digital lending as a distinct financing mechanism. Additionally, the study was conducted in Dagoretti North Sub County, while the present study focuses on small retail businesses in Nairobi CBD. The current study therefore extends the literature by examining the specific influence of digital lending variables on financial performance in a competitive urban context.

Alumasa and Muathe (2021) used an explanatory research design, employing regression analysis to examine mobile credit and performance of micro and small enterprises across Kenya. The findings showed that credit accessibility and loan size positively affected performance, while the cost of credit had a significant negative impact. This aligns to Kithandi (2022) who asserts that Financial Performance Of Deposit-Taking Savings And Credit Co-Operative Societies In Nairobi City County, Kenya is highly depenended on credit accessibility to members.

3 Methodology

This study adopted a positivist research paradigm and a descriptive research design to examine the relationship between digital lending and financial performance of small retail businesses in Nairobi Central Business District. The target population comprised approximately 3,500 small retail businesses, from which a simple random sample of 400 businesses was selected. Primary data were collected using structured questionnaires, yielding 360 valid responses. Data were analyzed using descriptive statistics, correlation analysis, and multiple regression analysis with the aid of SPSS to determine the influence of digital loan accessibility, loan usage, and loan cost on profitability, liquidity, and sales growth. Ethical considerations including informed consent, confidentiality, and voluntary participation were observed throughout the study.

4 Results and Discussion

4.1 Descriptive Statistics

The study reported the descriptive statistics for the study variables as shown in Table 1.

Table 1: Descriptive Statistics

Variable	Mean	Standard Deviation
Digital Loan Accessibility	4.08	0.71
Loan Usage in Business Operations	3.74	0.76
Cost of Digital Lending	3.89	0.73
Financial Performance	3.62	0.69

The descriptive results indicate that digital loan accessibility recorded the highest mean value of 4.08 (SD = 0.71). This suggests that, on average, small retail businesses in Nairobi CBD perceive digital lending platforms to be highly accessible. The relatively low dispersion implies consistency among respondents in terms of ease of loan application, approval speed, and availability of digital credit platforms. This finding reflects the maturity of Kenya's digital finance ecosystem, where mobile-based credit products are deeply embedded in day-to-day business operations.

The loan usage in business operations variable recorded a mean of 3.74 (SD = 0.76), indicating moderate to high utilization of digital loans for productive business activities such as inventory purchase, working capital management, and short term operational financing. The moderate variability suggests differences in borrowing intensity across firms, with some businesses using digital credit occasionally while others rely on it more frequently. This pattern

reflects the heterogeneous nature of small retail enterprises in Nairobi CBD, where cash flow needs vary depending on business size, seasonality, and sector.

The cost of digital lending recorded a relatively high mean score of 3.89 (SD = 0.73), indicating that respondents generally perceive digital loans as expensive. This perception is consistent with the short repayment periods, high effective interest rates, and associated fees typical of many digital lending products. The relatively high mean underscores borrower sensitivity to loan costs and suggests that while digital credit is accessible, its pricing structure may pose financial strain for small retail businesses operating on thin profit margins.

The dependent variable, financial performance, recorded a mean score of 3.62 (SD = 0.69), suggesting moderate financial performance among small retail businesses in Nairobi CBD. This reflects modest profitability, reasonably stable liquidity positions, and moderate sales growth levels. The results imply that although digital lending supports business operations, overall performance outcomes remain influenced by both positive credit access effects and negative cost pressures.

4.2 Correlation Analysis

Correlation analysis was conducted to examine the strength, direction, and statistical significance of the relationship between digital lending variables and the financial performance of small retail businesses in Nairobi Central Business District. Pearson's correlation coefficient was used since the variables were measured on continuous Likert scales and the data met the assumptions for parametric analysis.

Table 2: Correlation Matrix

Variable	Correlation Coefficient (r)	p-value
Digital Loan Accessibility	0.56	0.000
Loan Usage in Business Operations	0.41	0.000
Cost of Digital Lending	−0.48	0.000

Source: Field Data (2026)

The results indicate that digital loan accessibility has a moderate to strong positive correlation with financial performance ($r = 0.56$, $p < 0.01$). This statistically significant relationship suggests that small retail businesses that are able to access digital loans easily—through faster approval processes, minimal documentation, and platform convenience—tend to exhibit better financial outcomes. Improved access to credit enhances liquidity, enables timely stock replenishment, and supports uninterrupted business operations, thereby positively influencing profitability and sales growth.

Loan usage in business operations also demonstrates a positive and statistically significant correlation with financial performance ($r = 0.41$, $p < 0.01$). This finding implies that businesses that actively utilize digital loans for productive purposes such as inventory purchase, working capital financing, and short-term operational needs are more likely to achieve improved financial performance (Ubul, & Kithandi, 2025). The moderate magnitude of the correlation suggests that while loan usage contributes positively, its effect depends on how strategically the borrowed funds are deployed within the business.

Conversely, the cost of digital lending exhibits a negative and statistically significant correlation with financial performance ($r = -0.48$, $p < 0.01$). This indicates that higher interest rates, transaction fees, and short repayment periods associated with digital loans are linked to poorer financial outcomes among small retail businesses. High borrowing costs reduce net profits and place pressure on business liquidity, potentially offsetting the benefits derived from easy access to digital credit.

4.3 Regression Analysis

The study sought to examine the effect of digital lending on the financial performance of small retail businesses in Nairobi CBD and tested the following null hypothesis:

H_0: Digital lending has no significant effect on the financial performance of small retail businesses in Nairobi CBD.

The regression results are presented in Table 3.

Table 3: Effect of Digital Lending on Financial Performance

Variable	Beta Coefficient	p-value
Constant	0.812	0.000
Digital Loan Accessibility	0.45	0.001
Loan Usage in Business Operations	0.32	0.006
Cost of Digital Lending	−0.39	0.002

Model statistics indicated an $R = 0.71$ and an $R^2 = 0.50$, implying that digital lending variables jointly explain approximately 50 percent of the variation in financial performance among small retail businesses in Nairobi CBD. The overall model was statistically significant ($p < 0.05$), demonstrating that digital lending is a strong predictor of business financial outcomes.

The regression coefficients reveal that digital loan accessibility ($\beta = 0.45$, $p = 0.001$) has a positive and statistically significant effect on financial performance. This indicates that improved access to digital credit enhances business liquidity, enables timely stock replenishment, and supports smoother operations, leading to improved profitability and sales growth.

Similarly, loan usage in business operations ($\beta = 0.32$, $p = 0.006$) showed a positive and significant effect on financial performance. This suggests that when digital loans are channeled toward productive activities such as inventory acquisition and working capital financing, they contribute positively to business outcomes. This finding highlights the importance of strategic loan utilization rather than borrowing frequency alone.

Conversely, the cost of digital lending ($\beta = -0.39$, $p = 0.002$) exhibited a negative and statistically significant effect on financial performance. This

indicates that high interest rates, fees, and short repayment terms erode profitability and place pressure on liquidity. The negative coefficient confirms that excessive borrowing costs can offset the benefits of easy credit access, ultimately undermining financial performance.

Since all p values are less than 0.05, the null hypothesis was rejected. The study therefore concludes that digital lending has a statistically significant positive effect on the financial performance of small retail businesses in Nairobi CBD.

5 Conclusions and Recommendations

The study concludes that digital lending plays a significant role in shaping the financial performance of small retail businesses in Nairobi Central Business District. Improved accessibility to digital loans and productive use of borrowed funds positively influence profitability, liquidity, and sales growth. However, the high cost of digital lending significantly constrains these benefits, reducing net performance outcomes for many businesses.

Based on these findings, the study recommends that regulators and policymakers strengthen oversight of digital lending platforms to promote transparent pricing and borrower protection. Caps on excessive fees and clearer disclosure of effective interest rates would help reduce financial stress among small retail borrowers.

Digital lending institutions should design products tailored to the cash flow realities of small retail businesses by offering longer repayment periods, lower interest rates, and flexible repayment schedules. Incorporating credit products linked to business performance metrics could improve sustainability for both lenders and borrowers.

Finally, small retail business owners should adopt prudent borrowing practices by directing digital loans toward income generating activities and avoiding excessive reliance on repeat borrowing. Improved financial planning and basic financial literacy can help ensure that digital credit supports growth rather than creating long term financial strain.

Declaration of Competing Interests

The authors declare that they are not aware of any competing financial interests or personal relationships that may have influenced the work described in this document.

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Ethical considerations

The article followed all ethical standards appropriate for this kind of research.

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