

**EFFECT OF FINANCING SOURCES ON PERFORMANCE OF REAL ESTATE  
SECTOR IN NAIROBI COUNTY, KENYA**

**BY**

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**MASTER OF SCIENCE DEGREE (FINANCE AND INVESTMENT)**

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FINANCE AND INVESTMENT IN THE SCHOOL OF BUSINESS AND PUBLIC  
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**OCTOBER 2018**

**DECLARATION**

I declare that this dissertation is my original work and has not been previously published or submitted elsewhere for award of a degree. I also declare that this contain no material written or published by other people except where due reference is made and author duly acknowledged.

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Sign.....

Date.....

I do hereby confirm that I have examined the master’s dissertation of

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And have certified that all revisions that the dissertation panel and examiners recommended have been adequately addressed.

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## ABSTRACT

Real estate sector has gained a lot of interest from investors with the perceived high returns. Kenyan government has on the other hand recently capped interest rates on loans. Considering that most investors relied on mortgage financing to invest in real estate sector, the investors have to consider other sources of financing. Venture capital financing on the other hand has left some investors shortchanged by the venture capitalists. This study sought to establish the impact of financing sources on real estate sector's performance in Nairobi County, Kenya. The specific objectives were: to investigate the effect of mortgage financing on the performance of the real estate sector in Nairobi County, Kenya; to determine the effect of venture capital financing on the performance of the real estate sector in Nairobi County, Kenya and to determine the effect of equity financing on the performance of real estate sector in Nairobi County, Kenya. The study reviewed theories relevant to financing sources and performance namely; pecking order theory, trade off theory and agency theory. Descriptive research design was adopted. The study population was 64 real estate developers registered with Kenya Property Developers Association in Nairobi County, Kenya. The study conducted a census of all 64 real estate developers. The study used primary data. Questionnaires were utilized to collect data. Data was analyzed by multiple linear regressions and presented in form of frequency tables and charts and proper inferences made towards the same. The study found out that performance of real estate sector in Nairobi County, Kenya was significantly affected by mortgage financing which was statistically significant with a p value of 0.001. The relationship between venture capital financing and performance of real estate sector in Nairobi County, Kenya was positive, however, the relationship was statistically insignificant with a p value of 0.526. The study also found out that even though the relationship between equity financing and performance of real estate sector in Nairobi County, Kenya was positive, the relationship was statistically insignificant with a p value of 0.472. The study concluded that performance of real estate sector in Nairobi County, Kenya was significantly affected by mortgage financing which was statistically significant. The study also concluded that venture capital financing insignificantly influenced performance of real estate sector in Nairobi County, Kenya. The study further concluded that the relationship between equity financing and performance of real estate sector in Nairobi County, Kenya was statistically insignificant. The research recommends that in order for the investors to maximize returns on their real estate investments, they should adopt strategies such as increasing mortgage financing up to an optimal point since it has the highest returns as compared to other financing sources. The research further recommends that to reduce risks associated with venture capital financing, investors should undertake some mitigation steps like assessing and evaluating potential investment targets regarding risk and return. Similarly, the research recommends that real estate companies should consider raising equity through private placements as opposed to public placements.

**Key Words:** Mortgage, Venture capital, Equity, Performance, Real estate.

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## ACRONYMS AND ABBREVIATIONS

<b>EPS:</b>	Earnings Per Share
<b>GDP:</b>	Gross Domestic Product
<b>IPO:</b>	Initial Public Offer
<b>IRR:</b>	Internal Rate of Return
<b>KPDA:</b>	Kenya Property Developers Association
<b>KSE:</b>	Karachi Stock Exchange
<b>NPV:</b>	Net Present Value
<b>NSE:</b>	Nairobi Securities Exchange
<b>PWC:</b>	Price Waterhouse Coopers
<b>REIT:</b>	Real Estate Investment Trust
<b>ROE:</b>	Return on Equity
<b>ROI:</b>	Return on Investment
<b>SME:</b>	Small and Medium Enterprise
<b>USA:</b>	Unites States of America

## **OPERATIONAL DEFINITION OF TERMS**

- Equity:** Refers to nominal capital, free and general reserves and retained earnings (PWC, 2016).
- Mortgage:** An agreement under which one party borrows money from another party to purchase a property and pledges the same property as collateral for the loan (Central Bank of Nigeria, 2013).
- Performance:** Refers to the profitability of a firm measured in terms of ROE, ROI and EPS (Love, 2003).
- Real Estate:** Refers to land and anything that is immovable, fixed and permanently attached to it (Business dictionary, 2018).
- Venture Capital:** Refers to all different types of risk capital investments in companies that are unlisted (Makomaski & Johansson, 2013).

## CHAPTER ONE

### INTRODUCTION

#### 1.1 Study Background

Real estate as a sector has been constantly growing over a period of time in Kenya and particularly in Nairobi County. According to a report by Cytonn Investment (2016), it contributes an average of 8.5% of the Kenya's GDP. This sector has attracted a lot of interest by investors. For the last five years, major projects have been undertaken and some are still ongoing in areas like Westlands and Upper hill. According to a report by Oxford Business Group (2017), real estate sector in Kenya has experienced a rapid growth but the financing aspect is a major challenge throughout execution of real estate projects.

In USA, the market for real estate sector has remained vibrant over the last five years. Demand for property has been strong and construction activity has been on the rise. Growth in real estate sector has contributed to overall growth of the economy in USA as a result of increased consumption by households which has been boosted by rising house prices among other factors (Global Property Guide, 2018). In Australia, real estate market has experienced growth over the last five years. Property prices have been on the rise registering a 9.98% increase in quarter two of 2017. Demand in the sector has been strong and construction activities are on the increase. The country's GDP has been boosted by the vibrant real estate sector (Global Property Guide, 2018).

In India, real estate sector has been experiencing a significant growth and it is expected that by the year 2020, the sector will be contributing an average of 11% of the country's GDP (India Brand Equity Foundation, 2018). Globally, real estate sector has been used as one of the

measures of the society's well-being and economic success. A well developed real estate sector conveys a positive message on the general economic status of a society (Chinjekure, 2018).

Real estate sector is rated among the few investments that have returns that are reliable globally (Hogan Lovells Real Estate, 2017). This makes the sector very vital to the general economic growth and therefore there is need to understand the different financing sources and their contribution to performance of the real estate sector. World over, entrepreneurs invest in real estate sector with an aim of getting an investment return. The return could be in form of periodic incomes like rents and capital appreciation. Investments in real estate sector include management, ownership, purchase, sale or rental of real estate (Baker & Chinloy, 2014).

According to a report by Construction Kenya (2016), Upper hill is christened as Africa's fastest growing real estate sector with high end commercial buildings and the investors are flocking the area to meet the ever-increasing demand for high end offices in Nairobi City. Investment in Real estate sector requires enormous capital outlay and various methods are employed to raise the funds since personal savings cannot satisfy the need. These different types of real estate financing could result to varied effects in the performance of real estate sector.

### **1.1.1 Sources of Financing**

Real estate investments are significant purchases (Martin, 2014). They require immense capital outlay unlike other securities investments which can be purchased on an incremental basis. The main issue of concern in investment and real estate development is finance. It is by nature capital-intensive and therefore demands proper as well as adequate funding so as to make it realizable (Ezimuo, Onyejiaka & Emoh, 2014). Majority of the real estate investors do not have the capital themselves and thus they utilize the available financing sources.

Real estate financing can come from various sources but each source has its unique aspects resulting to different outcomes. Investors need to consider a source of capital or a mixture of sources that will maximize their investment yield (Martin, 2014). The financing sources for real estate sector include Mortgage, Venture Capital and Equity Financing. The financing source used has a consequent outcome on the performance of the real estate investment.

According to Mwathi (2013), mortgage financing is a crucial form of financing that enhances accumulation of capital by growing economies. The uptake of mortgage by the real estate developers is however determined by interest rates. When the lenders increase interest rates, only a few real estate developers will opt for mortgage as their source of financing. Venture capital financing has proved to be a critical source of funds for businesses. In developed countries, it has gained massive popularity and it is rapidly emerging in developing countries (Ernest, Duodu & Somiah, 2016). Ernest *et al.* (2016) observed that venture capital financing has played a critical role in financing real estate companies that are on growth stage in Ghana.

A study conducted in Ghana by Manu, Edwards, Badu, Hyiaman and Love (2015) confirmed that equity financing alone cannot satisfy the demand for funds to finance real estate sector. This is due to the enormity of capital required and the developers are unable to raise the funds through equity. This is compounded by underdeveloped capital markets that would otherwise provide a way for raising funds through IPOs.

### **1.1.2 Real Estate Performance**

According to a report by PWC (2018), real estate sector has outperformed other investment sectors globally due to its superior returns. This has been demonstrated by investors increased appetite to invest in the sector as opposed to investing in other asset classes with lesser returns

and higher risk (Cytonn, 2017). Superior returns in the real estate sector are as a result of lower volatility in property prices as compared to other asset classes. Globally, real estate returns are more steady and predictable as a result of less pronounced price swings (Jorda, Knoll, Kuvshinov, Shularick, Taylor, 2017).

In the period between 2012 and 2016, the sector has been generating an average return of 25 percent as compared to an average of 10 percent in other traditional asset classes in Kenya (Cytonn, 2017). Kimmons (2018) explains that rental payments from real estate sector significantly exceed dividends from other stocks. The rental incomes are also less exposed to economic risks and are mostly predictable. Over time, real estate appreciates in value and yields capital gains which are factored in when analyzing the performance of real estate (Kimmons, 2018). According to a study done in Nigeria by Dabara, Odewande, Olatunde, Anthony and Anthony (2016), investment in real estate sector improves the overall performance of an asset portfolio due to reduced risk and reliable returns. This is also supported by a report by PWC (2018) which shows that globally, real estate sector will continue to earn investors higher returns now and in days to come.

Performance of this sector of real estate is influenced by wide-ranging factors world over. Some of these factors influence the performance positively while others influence it negatively. An observation made in India by Singh (2017) shows that there is a cycle of real estate performance and the GDP. He observed that a growth in GDP results to an increased employment levels due to additional investments in business and infrastructure, this further leads to an increase of income and purchasing power, which further fuels demand for housing. As the rule of demand and supply applies, the property prices go up and this further fuels GDP growth.

Raghavan (2016) observed that the performance of real estate sector is influenced by increase in population and the migration patterns. A rise in population leads to increase in demand for housing and therefore rise in property prices. The same applies where the population migrates to urban areas and increases demand for housing. Jain (2017) observed that inflation rate affects the performance of real estate sector. High level of inflation results to a decreased level in purchasing power and therefore reduced demand for real estate. This drives the property prices downwards.

Merrills (2015) observed that stock market operations affect the performance of real estate sector. When stock markets are bullish, interest rates drop. The investors shift their attention to real estate sector and the demand increases therefore positively affecting the performance of real estate sector. Puri (2014) argues that a Country's legislation has a direct effect on real estate sector performance. Policies like tax rates, rebates and subsidies affect the demand for real estate sector and therefore its performance.

### **1.1.3 Real Estate Sector**

Real estate sectors involve either active investment or passive investment. Active investment relates to where the investor is actively participating in making the investment pay off while passive real estate investment involves investing through real estate related mutual funds and real estate investments trusts (Kelly, 2015). In active real estate investment, the investor is directly involved in selection, purchase, maintenance and administration of the property (JWB Real Estate Capital, 2018). Active real estate investments give the investor control and choice of properties to invest in but also it could limit their investments due to budget constraints (Peer Realty, 2015).

In passive real estate investments, investors contribute funds to a trust or a mutual fund with professional managers who undertake the investments on their behalf. In return, they receive periodical incomes depending on the investments' performance. According to a report by JWB Real Estate Capital (2018), investments in passive class are usually large commercial properties and already complete residential properties which would otherwise be a dream for an individual investor to fund. Passive real estate investment has the benefit of limitation in possible loss to the investors since their liability is capped on their investment amount and also it enhances diversification in terms of property type and geography as a result of large pool of financial resources (Formigle, 2018).

A report by PWC (2017) observed that globally, real estate sector attracts high capital inflows. It further notes that investors conceive real estate sector as a safe haven and a high yield investment. This results to the investors giving real estate investments a priority over other kinds of investments. A report by India Brand Equity Foundation (2018), notes that this sector of real estate is among the mostly recognized sector in the world. The report further notes that in India, the sector is the second largest employer and its growth is influenced by growth in corporate environment, increased demand for office space and urban and semi urban accommodations.

According to a report by Superior Homes (2017), Kenya's real estate sector is well diversified in terms of income (high, middle and low income), geography (large farms and beach properties) and types (office, retail, residential and industrial properties). Nairobi County being the Kenya's capital takes the biggest share of income and types classification. A report by Cytonn (2017) details that the increased growth in the real estate sector in Nairobi is as a result of rapid urbanization, increased population growth, large housing deficit, high returns, continued

infrastructure development, better operating and legal environment, growing business and entry of global brands.

## **1.2 Statement of the Problem**

Mortgage financing has predominantly been used to finance real estate sector. Financial institutions and housing finance companies have been extending mortgage facilities to property developers and other investors in the sector. In Kenya today, as a result of interest rate capping, financial institutions have slowed down in extending debt financing to investors due to reduced returns and the high risk involved. Kenya Bankers Association (2017) report expounds that Kenyan banks have been hesitant to issue loans and this has affected the number of properties bought and hence underperformance of real estate sector. The report further explains that the growth in property prices increased by 0.98 percent in 2017's second quarter as compared to a 1.10 percent growth rate in the previous quarter. This is explained by the supply and demand concept that when the demand falls, prices move in the same downward direction (Kenya Bankers Association, 2017).

A survey conducted by KPMG (2017) on real estate industry outlook in USA established that banks have reduced lending to the real estate sector as a result of various factors such as thinning real estate market, increased regulatory requirements and pressures from the market. As a result of decreased lending by the banks, other private sector players have stepped up and are willing to provide funds to the sector including to those investments that would be considered riskier or to the borrowers that would otherwise be considered to be less established by the banks.

The decline in mortgage financing has made investors in the real estate sector to consider other sources of financing like venture capital and equity financing. A report by Ernest and

Young Global Limited (2018) notes that firms are now turning to IPOs as a way of raising capital due to decreasing financing options available. Venture capitalists look for business ideas with high growth potential and good returns and do an investment in them so as to exchange for an ownership in the shares. The essence of investing is to get returns and thus mostly they have no entrepreneur's interest in mind and they could have divergent vision. A report on Standard Digital (2013) explains how many Kenyans who have turned to venture capital firms for financing have been shortchanged and their investment ideas stolen or they are forced out of the company through buy outs. Considering these different financing sources have different aspects, they also should have varied effects on the performance of real estate sector.

Baker and Chinloy (2014) studied on the relationships between public real estate markets and investments. Ezimuo *et al.* (2014) researched on the financing aspect of the capital-intensive projects. Standard digital (2013) report explains how venture capitalists can shortchange potential real estate sector investors. The above studies and other published studies have failed to explain the influence of various sources of financing on the real estate sector's performance in the County of Nairobi, Kenya thereby leaving the area grey. This study with a bid to fill this gap sought to find out the impact of financing sources on the performance of real estate sector in Nairobi County, Kenya.

### **1.3 Research Objectives**

The study's general objective was to establish the effect of financing sources on performance of real estate sector in Nairobi County, Kenya. The following are the specific objectives.

- i. To investigate the effect of mortgage financing sources on the performance of real estate sector in Nairobi County, Kenya

- ii. To determine the effect of venture capital financing sources on the performance of real estate sector in Nairobi County, Kenya
- iii. To determine the effect of equity financing sources on the performance of real estate sector in Nairobi County, Kenya

#### **1.4 Research Questions**

Questions answered in this study include:

- i. How does mortgage financing affect real estate sector's performance in Nairobi County, Kenya?
- ii. In which ways does venture capital financing affect real estate sector's performance in Nairobi County, Kenya?
- iii. What is the effect of equity financing on the real estate sector's performance in Nairobi County, Kenya?

#### **1.5 Significance of the Study**

##### **1.5.1 Investors**

This study will be significant both to current and potential real estate investors. It sheds more light and impart relevant knowledge on the characteristics of different sources of financing and how their usage influence real estate performance, thereby providing these investors with wisdom to choose the best.

##### **1.5.2 Scholars and Academicians**

Scholars and academicians in this line of study will find this study of great benefit to them. It provides suggestions for topical selection since the study stipulates recommended areas for further research. Also, the study provides empirical literature on the financing sources and

performance which will enrich research work of current and prospective scholars and academicians.

### **1.5.3 Government and Policy Makers**

The government and other policy makers will also be a beneficiary to this study. Findings from this research provide greater insights for appropriate regulation, informed decision making as well as a platform for benchmarking. The government will also know where to intervene and offer incentives in order to enhance the performance of real estate sector.

### **1.6 Scope of the Study**

The subject scope was limited to the investigation of financing sources and performance of real estate sector in Nairobi County, Kenya. The geographical scope for this study was Nairobi County in Kenya which is basically the capital city of the country Kenya. The population for this study was confined to only real estate developers in Nairobi County as objective to the research topic. The independent variables were: mortgage financing, venture capital financing as well as equity financing. The dependent variable was real estate performance in Nairobi County, Kenya. The study ran for seven months starting January 2018 and ending in July 2018.

## **CHAPTER TWO**

### **LITERATURE REVIEW**

#### **2.1 Introduction**

This chapter captures relevant theories to the study. It reviews previous research studies done by other researchers on different financing sources namely mortgage financing, venture capital financing and equity financing and their effect on real estate sector performance. It also covers the conceptual framework and operationalization of variables.

#### **2.2 Theoretical Review**

Theoretical literature review is aimed at evaluating the already existing theories in regard to a concept. This section reviews three different theories that deal with the financing sources and decisions and the effect on the resulting performance of a firm. The theories are; trade off theory, pecking order theory and agency theory.

##### **2.2.1 Trade off Theory**

Merton Miller and Franco Modigliani proposed this theory in 1963. According to the theory, companies attain benefits from leverage up to a point where optimum capital structure is reached. The benefits accrue as a result of tax benefits on the interest payments since tax is deducted on interests. The debt's actual cost is therefore less than the nominal cost of debt. The benefit doesn't ensue to dividend on equity. The theory therefore proposes that investors should consider more debt than equity up to a point where optimum capital structure is reached (Modigliani & Miller, 1963). Trade of theory advocates for increased debt financing up to an optimal point, debt has the disadvantage of obligatory periodical repayments that are independent of the success of an investments it financed. On the other hand, equity would be less risky as it has no periodic obligatory repayment commitments although it dilutes the

shareholding of a company (Adair & Adaskou, 2015). Although increased debt results to a higher tax shield, it could also lead to bankruptcy of a firm resulting to its failure (Ghazouani, 2013).

According to Myers (1984), companies are viewed as balancing the benefits accrued from shield of interest tax against the bankruptcy costs and embarrassment on matters relating to finance. Substituting equity for debt and vice versa is important for companies till a point where the firm's value is maximized. However, corporate managers might choose to employ sub optimal debt policies to optimize their personal utility function to the detriment of optimizing shareholders value (Graham, 2000).

This theory relates to the study since it focuses on the benefits applicable to debt financing as a result of tax benefits over equity financing. Employing more debt means a higher tax shield since the interest cost is tax deductible thus giving credence to the well known fact which states that different sources of financing result to respective different outcome on real estate's performance.

### **2.2.2 Pecking Order Theory**

Majluf and Myers (1984) proposed this theory. It is founded on the assumption that optimal capital structure do not exist. Many companies consider source of financing to use in hierarchical progression starting with internal financing, by use of reserves and retained earnings, then consider external financing by first using debt financing and lastly equity financing, by issuance of shares.

Majluf and Myers (1984) argue that the least preferred source is equity financing than retained earnings and debt financing. This is as a result of asymmetrical information problem. Information asymmetries suggest that seeking finance externally will be more expensive than

internal finance as finance providers add a risk margin to cover their information disadvantage. Managers of the firm are presumed to have full knowledge of the position of the company, and when shares are issued, the investors interpret that there is an overvaluation of the firm and the management is trying to take advantage of that overvaluation. Investors therefore place a lower value to equity issuance. When a firm issues debt, it communicates to the potential investors that the management have confidence in continued profitability of a firm. To the investors, it means that the stock of the firm is undervalued (Adair & Adaskou, 2015). This explains why among the two external financing sources, debt is more preferred than equity financing. Pecking order theory assumes that more successful and profitable firms will opt to finance their investments with reserves and retained earnings before considering other sources.

This theory is based on the concept of asymmetrical information problem where the potential investors put a lower value on issuance of shares by a company, in this case, a real estate company. Potential investors presume that the owners have no confidence in the future of the firm and this directly affects the overall performance of the real estate sector. The theory advocates for retained earnings as the first priority source of financing, indicating that this will improve firm's performance more than debt and equity. This study seeks to empirically test the different financing sources and their respective performance in the real estate sector thus it will confirm the theory or otherwise.

### **2.2.3 Agency Theory**

Meckling and Jensen (1976) proposed this theory. Principal-agent association exists where one party engages another party to carry out some services which otherwise will have been carried out by the principal with some form of delegation of decision making authority (Meckling & Jensen, 1976). The principals in the context of this theory are the shareholders and the agents are

the managers of the firm. It suggests that an optimal capital structure manifests as a result of tradeoff between agency costs and the benefits in the context of increased debt form of financing. Agency costs consist of monitoring costs, residual losses as well as bonding costs (Strategic CFO, 2013) According to Adair & Adaskou (2015), an optimal debt ratio is obtained when agency costs are at minimum level.

Agency problem arise as a result of shareholders desire for payouts for their investments, therefore leading to a reduction of internal resources that are controlled by firm managers (Jensen, 1986). Managers on the other hand get frequent compensation based on the accounting profits. They are therefore motivated to be involved in information manipulation or favouring of projects with low and poor NPV in case they provide immediate profits (Smith & Dogan, 2002). The higher rewards desire induces the management to be involved in the manipulation of the indicators like inefficient debts budgets so as to achieve their goals to the detriment of the value of the firm (Thomson, 2007).

When the management have authority to control assets of a company, but they have divergent goals from those of the shareholders, they may be motivated to implement decisions that are beneficial to them at the expense of shareholders wealth. The agency costs are incurred to deter the management from engaging with those actions that may be harmful to the company's performance (Laiho, 2011)

Performance of real estate sector can therefore be directly affected by the management's decision to apply sub-optimal financing mix like inefficient debt and choosing projects with poor NPV so long as they achieve their goals and negatively affecting the performance. Also, increased agency costs may outweigh the benefits that may accrue as a result of financing sources employed by a firm.

## **2.3 Empirical Review**

Empirical literature review relates to review of studies that are supported by empirical data. This section reviews studies done in the past that relate to our current study. It focuses on the topic of the study, objectives to be determined, methodology used and the findings. Various studies on mortgage financing, equity financing and venture capital financing have been covered.

### **2.3.1 Mortgage Financing and Performance of Real Estate Sector**

Nwankwo (2014) examined the implications of mortgage financing on the housing for all in Nigeria by the year 2020. He sought to determine the effect of credit on supply of housing for all. Panel data research design was used and the population of the study constituted data from 5 sources namely; Supply of Housing and Housing Activities; Mortgage Credit; Commercial Bank Credit; Private Sector Investment and Central Bank of Nigeria over a period of 13 years from 2000 to 2012. The study found out that mortgage financing gives a significant positive impact on the supply of housing for all in Nigeria by year 2020.

Tauseef, Lohano and Khan (2015) conducted a study on the impact of debt financing on corporate performance: evidence from Pakistan's textile firms. The study sought to examine the impact of financing using debt on the performance of a firm using return on equity as a form of measurement. Panel data research design was adopted and data sources comprised of a sample of 95 textile companies which were selected from 182 companies listed on KSE which was the population under study. A period of six years was considered from 2002 to 2008 whereby observations were made and data was obtained from State Bank of Pakistan (2009). The study established that debt level that is optimal exists for the performance of a company and any debt beyond that point decreases performance due to increased interest costs.

Ndinda (2014) carried out another study on the impact of financing using mortgage on real estate market performance in Kenya. The paper sought to ascertain the association that exist between real estate market performance and repayment of mortgage; determine the relationship between mortgage interest rates and the rental income; examine the performance of real estate market. Research design was cross sectional data and the study conducted a census of all 35 licensed mortgage and financial institutions in Kenya. Target population consisted of 19,177 outstanding loan owners. The study established that there exists a significant and positive relationship between real estate market performance and mortgage financing in Kenya.

Mackenzie (2013) carried out a study on the influence of financing using mortgage on real estate industry performance in Nairobi, Kenya. This study sought to determine how interest rates affect the real estate industry performance in Nairobi, Kenya as well as to find out the impact of terms of loan on real estate industry performance in Nairobi, Kenya. Also the paper assessed the influence of risks associated with mortgage on real estate performance in Nairobi, Kenya and to investigate inflation effects on real estate industry performance in Nairobi, Kenya. Cross sectional data research design was adopted and the data sources comprised of a sample of 32 real estate firms in Nairobi selected from a population of 182 firms. The study established that mortgage financing was greatly influenced by interest rates and it's significantly correlated to the performance of real estate industry. On the loan terms, the study found out that promptness and approval process for mortgage loans greatly influence the access to financing using mortgage thus affecting real estate industry performance. On mortgage risks, the study found out that the industry involved in real estate is at high risk in matters of non-occupancy rate which in turn affects the performance of real estate industry. On inflation, the study established that few

investments are made when inflation rates go up and investors are less willing to acquire mortgage loans thus affecting the performance of real estate industry.

Another study by Makanga (2015) on the effect of debt financing on performance of finances of companies that are listed at the NSE sought to ascertain the impact of debt financing on the performance of the firms. Cross sectional data research design was adopted and the study conducted a census of all 50 firms listed on NSE, financial institutions excluded, as at 31<sup>st</sup> December 2014. The study ascertained that both current and long-term debt do not significantly affect the firms' performance.

### **2.3.2 Venture Capital Financing and Performance of Real Estate Sector**

Peneder (2010) conducted a study on the effect of venture capital on firm growth and innovation behavior. The study sought to test the effect of financing using venture capital on corporate performance through the application of a two-stage propensity score matching employed on micro data of Australia. Cross sectional data research design was adopted and data sources constituted of 3 main sources namely; a test group comprising of 174 venture capital companies in Austria; also a group of comparison of very similar firms that were selected using wide range of control variables as the basis as well as employing the database of an Austrian credit rating agency that is on the lead; a comprehensive survey of the enterprise that involves both the control group and venture capital financed firms was carried out to gather enough information on the performance of the firm, their motive as they come up with financing instruments as well as any other missing variable that may have an effect on the selection process. The paper found out that firms that are financed using venture capital grow faster as far as turnover and employment is concerned and that they are also more innovative than any other firms.

Industry Canada (2013) undertook a study on Canadian firms' performance that are financed using venture capital. The study sought to assess the influence of venture capital on Canadian firms' performance. The study adopted panel data research design and data sources constituted a population of a good number totaling 2,762 Canadian companies that were fully disclosed and had acquired venture capital funding between 1990 and 2009. A sample of 1,545 firms was selected from the population. The study established that firms that are financed using venture capital had wonderful performance while considering a number of measures such as stronger growth in sales, growth of revenue, growth of employees and growth of assets.

Lyxell and Nordén (2013) conducted a study on performance dynamics of firms financed using venture capital. Swedish venture capital market was used as a case for the study. The study sought to establish whether firms that are financed by venture capital outperform those that are not financed by venture capital in an area of business development. The study adopted panel data research design and the study conducted a census of all 220 Swedish firms that were financed by venture capital and were exited either through IPO or acquisition, between the period between 1996 to 2011. The study established that venture capital financed firms do show superior performance in terms of significantly faster sales growth.

Memba (2011) undertook a study on the influence of financing using venture capital on the performance of Kenya's small and medium enterprises. The study sought to investigate; if venture capital leads to growth of SMEs; to establish if SMEs that make use of venture capital attracts other finance sources; to determine the effect of venture capital on the used style of management; to investigate the impact of venture capital on finance management of SMEs. The study adopted an exploratory research design and the population consisted of all 400 SMEs in Kenya that have used venture capital. A sample of SME firms totaling 100 was taken from the

population. The sample consisted firms from Nairobi, Mombasa, Kisumu and Nakuru. The study established that in this respect, the venture capital's impact on performance of SMEs is both practical and real and that venture capital facilitates wealth creation.

Njama (2013) carried out a study on the impact of financing using venture capital on small and medium enterprises' growth in Kenya. This paper sought to investigate the effect of financing using venture capital on SMEs' growth in Kenya. Panel data research design was adopted and the population consisted of 100 SMEs in Kenya. From the population, a sample totaling 30 SME firms was taken and data was from 2009 to 2012 covering a period of five years. The study established a significant and positive relationship between SMEs' growth and financing using venture capital.

### **2.3.3 Equity Financing and Performance of Real Estate Sector**

Khan, Shaikh, Shah, Zahid and Shaikh (2017) conducted a study on the influence of financing decisions on performance of the firm, an empirical study on Pakistani listed firms at KSE. The study sought to give an analysis on the effect of financing decisions on the performance of the Pakistani firms listed at KSE. Panel data research design was employed and a census was carried out of all 100 publicly traded firms that are between 2004 and 2009. The study established that the value of the firm is not affected by the financing decision employed.

Saad, Ghani, Ahmad and Salim (2014) conducted a study on the effect of financing using equity and debt on the performance of SME in Malaysia. The study intended to verify as well as examining whether there is existence of the relationship between SME performance in Malaysia and the source of capital through financing using debt and equity. Cross sectional data research design was adopted and a sample of 177 Malaysian SME firms in manufacturing and agriculture

sectors were selected from all states. The study found out that there is a positive and significant effect on the performance of business but for debt financing it was found to be insignificant.

Another study by Musila (2015) on the relationship between financing using equity and performance of finances of the petroleum and energy companies that are listed at NSE. It sought to establish whether the relationship between financing using equity and performance of finances of the petroleum and energy companies quoted at the NSE exist. Panel data research design was adopted and the study population consisted of all companies quoted at NSE from 2005 to 2014 covering a 10 year period. From this population, 5 companies listed on energy and petroleum sector namely; KenGen Ltd, KenolKobil Ltd, Kenya Power & Lighting Company Ltd, Total Kenya and Umeme Ltd were selected from the population. It was found out from the study that there is an insignificant relationship between the variables that were involved in the study.

Raude, Wesonga and Wawire (2015) carried out a study on strategy of financing using equity and small and medium enterprises' performance in Kenya. The paper sought to ascertain how equity financing impacts SMEs' performance in the Municipal of Kakamega, Kenya. Cross sectional data research design was adopted and the population consisted of a good number of enterprises of about 2,713 that were in operation as at December 2013 in that Municipality of Kakamega, Kenya. A sample consisting of 95 enterprises was randomly selected from the available population. The study ascertained that financing using equity empirically had an effect on SMEs' performance and there exist a significant positive relationship between financing strategy using equity and the performance variables.

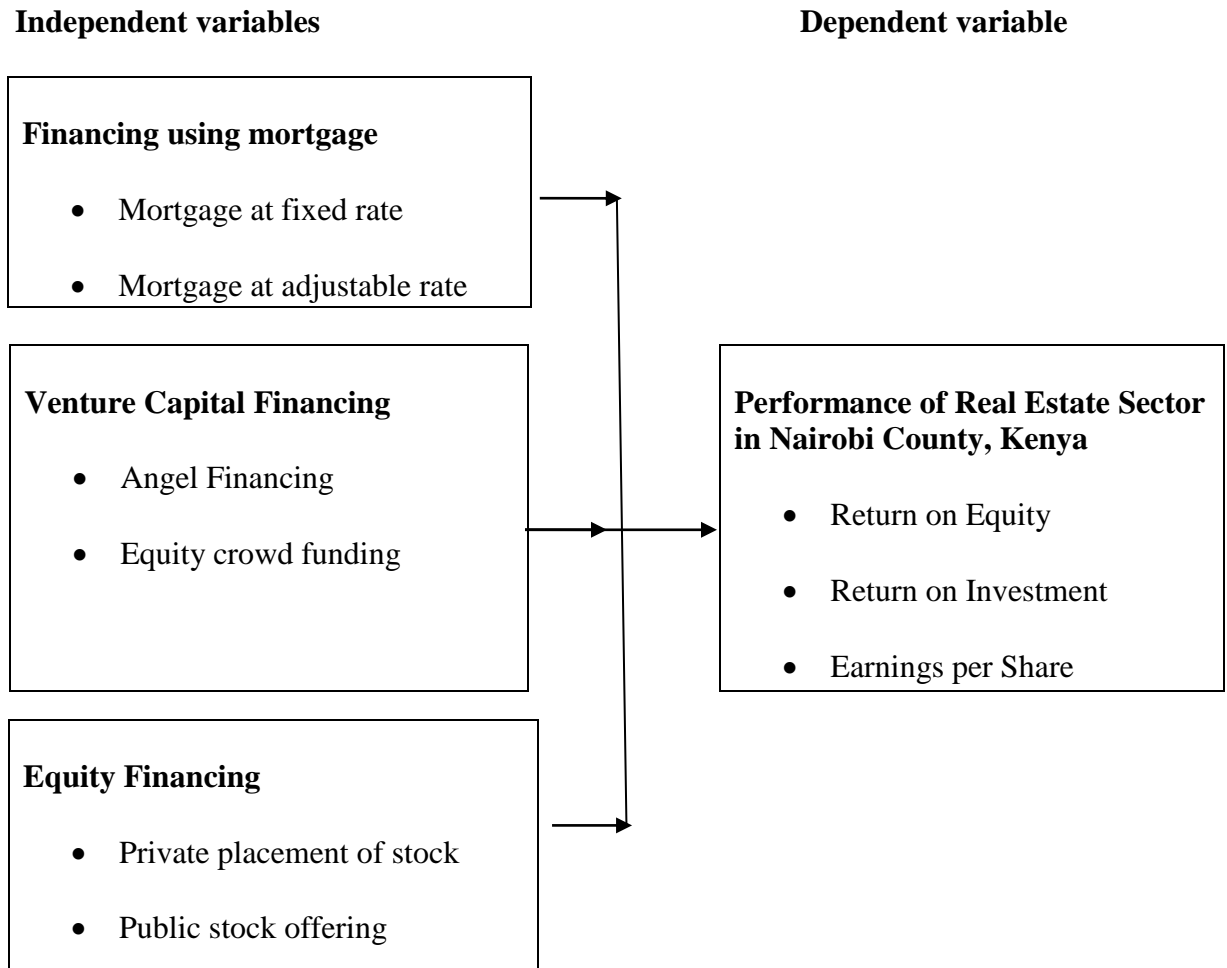
Njagi, Maina and Kariuki (2017) conducted a study on equity financing and SMEs' financial performance in Embu town, Kenya. The study sought to determine the influence of financing using equity on SMEs' financial performance in Embu town, Kenya. Cross sectional

data research design was used and the population comprised of 300 accessible registered SMEs in Embu. A sample of 60 SMEs was selected from the population. The study found out that financing using equity had a relationship to the SMEs financial performance.

#### **2.3.4 Critique of Literature**

Past studies relating to the topic have come up with mixed findings. Some studies have established that mortgage financing has a significant relationship with performance especially in developing countries. Other studies done in developed countries contradict this by establishing that the source of financing does not have an impact on performance. Some studies are of the view that debt financing, in our case mortgage financing affect performance positively up to a certain point, then performance decreases. The studies reviewed however are in agreement that venture capital financing leads to superior performance and facilitate wealth creation. The studies have used one of either panel data or cross-sectional data for the analysis process. The studies have however failed to compare the three financing sources to establish whether they would give similar or different performance outcomes. This study seeks to fill this knowledge gap by establishing the effect on real estate sector's performance in Nairobi County, Kenya by the sources of financing.

## 2.5 Conceptual Framework



**Figure 2.1: Conceptual framework**

## 2.6 Operationalization of Variables

Mortgage financing comprise of long term debts to finance real estate sector. To measure the profitability of a mortgage financing, the internal rate of return is used. IRR measures profitability of potential investments and it equates the NPV of all future cash flows to zero. The formula of calculating the IRR of a mortgage financing is explained in table 2.1.

Equity financing consist of shareholders equity. It is measured by subtracting the company's entire liabilities, both short and long-term from entire assets, both current and long-term. Alternatively, shareholders equity can also be obtained by summing together the share

capital as well as retained earnings and then deduct treasury shares. Treasury shares consist of that portion of shares that the company retains either by not issuing them to the public or through shares repurchase.

Venture capital financing is a part of the company's total equity. It is that portion of company's equity that is injected by high net worth individuals and firms with an appetite for high returns and are risk takers. It is obtained by subtracting ordinary and preference share capital from the company's total share capital.

Performance of real estate is measured using various methods like ROE, ROI and EPS. ROE gives a percentage of profit made by the company per monetary unit of equity that is invested in the company (Berzkalne & Zelgalve, 2014). It is measured as net income divided by shareholder's equity. According to CFI (2018), ROI is said to be a ratio that is employed in the calculation of the benefit an investor expects to receive in relation to the investment cost. It is calculated as net income divided by investment cost. EPS is the portion of company's profit attributable to individual outstanding shares. It is obtained by just dividing total earnings obtained by the total number of shares that are outstanding at the end of the period.

**Table 2. 1: Operationalization of variables**

<b>Variable</b>	<b>Type of Variable</b>	<b>Measurement</b>	<b>Type of Scale of Measurement</b>
Mortgage financing	Independent	$Ln - Fs = \frac{P_1}{1+i} + P_2/(1+i)^2 + \dots (P_n + B_n)/(1+i)^n$ <p>Where: <math>i</math> = Internal rate of return, <math>Ln</math> = Loan amount, <math>Fs</math> =Points as well as other lender fees, <math>P</math>= payment on monthly basis, <math>n</math>= Specific month when the balance is fully paid, <math>B_n</math>= Balance in a given month <math>n</math></p>	Ratio
Equity financing	Independent	<ul style="list-style-type: none"> <li>• Share capital + retained earnings - treasury shares</li> <li>• Total assets – total liabilities</li> </ul>	Ratio
Venture capital financing	Independent	<p>Total share capital – (ordinary and preference share capital)</p> <p>Where total share capital = Ordinary share capital + preference share of capital + venture capital)</p>	Ratio
Performance of real estate	Dependent	<p>ROE = Total net income/Shareholders' equity</p> <p>ROI = (Total net income/Cost of Investment) * 100%</p> <p>EPS =Total earnings / Number of outstanding shares</p> <p>Where total earnings= Net earnings- Preferred dividends</p>	Ratio

## **CHAPTER THREE**

### **METHODOLOGY**

#### **3.1 Introduction**

According to Kothari (2004), research methodology can be defined as a way of solving a research problem in a systematic way. This chapter covers the research design and target population, research instruments, validity and reliability of research instruments, data collection procedure, data processing and analysis.

#### **3.2 Research Design**

Research design can be explained as a conceptual structure where research is done. It comprises the blueprint purposely for collection and measurement as well as the analysis of data (Kothari, 2004). This study employed descriptive survey design. This design was chosen since the researcher was involved in identifying the characteristics of different financing sources and their effect on performance of real estate sector in Nairobi County. Descriptive design of research aims at gathering of information as per the prevailing circumstances or situations purposely for interpretation and description. It involves proper analysis, comparisons, interpretation, identification of trends as well as relationships (Aggarwal, 2008).

#### **3.3 Target Population**

According to Taylor (2018), population is the aggregate of all subjects, items or members of a certain study. This study's population comprised of all real estate developers' firms in Nairobi County that are registered with Kenya Property Developers Association (KPDA). According to KPDA (2018), there are 64 registered real estate developers in Nairobi County, Kenya. The study conducted a census of the entire population.

### **3.4 Research Instruments and Data Collection Procedure**

This study adopted semi structured questionnaires to collect primary data. The questionnaires used both the open-ended and close ended questions. These questions that were close ended necessitated the choice by respondents a degree of agreement on a five level Likert scale that have scores such as strongly disagree and disagree, neutral, agree and strongly agree. The scores starts with 1 for strongly disagree and ascends to 5 for strongly agree in that order. Open ended questions were designed for the respondents to give their views on certain variables.

This study employed primary data. Questionnaires were used to collect primary data which were dropped and picked at the registered offices of real estate developers' firms in Nairobi County. Questionnaires gave individual response on each variable as per our objectives.

### **3.5. Validity and Reliability of the Instruments**

The study conducted reliability and validity of the instruments. Reliability refers to how often the same results will be obtained if the study is repeated (Makomaski & Johansson, 2013). The study used Cronbach's alpha which measures internal consistency of research instrument. If this coefficient for the instrument is greater than 0.70, it have passed reliability test (Institute of Digital Research, 2017).

Validity refers to how well measurements, concepts and conclusions accurately correspond to the reality (Makomaski & Johansson, 2013). Questionnaires for the study were formulated to give unbiased information possible. A pilot test of the research instruments was conducted to establish their validity. The researcher formulated the instruments with a 3-point Likert scale with relevant, quite relevant and not relevant and gave to different knowledgeable individuals for them to give their degree of relevance of the instruments.

### 3.6 Data Analysis and Presentation

Quantitative analysis as well as descriptive statistics methods were used to analyze data. A knowledge base is provided by descriptive analysis which is taken to be the ground and foundation for further analysis of quantitative nature, as it maps a specific phenomenon's landscape (Travers, 1978). Quantitative analysis aided in determining the magnitude of the effect of financing sources. The methods enabled the researcher to describe the way independent variables affect performance of real estate sector in Nairobi County, Kenya. With the help of SPSS (Version 21), data was analyzed using the multiple linear regression model.

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

Y is performance of real estate sector

$\beta_0$  Is constant term

$X_1$  is mortgage financing

$X_2$  is venture capital financing

$X_3$  is equity financing

$\beta_1, \beta_2, \beta_3$ , are Beta coefficients

$\varepsilon$  Is the disturbance term

After data was analyzed, results were presented using frequency tables and charts and proper inferences made towards the same.

### 3.7 Diagnostic Tests

The study performed several preliminary diagnostic tests in view of multiple linear regression analysis. The diagnostic tests conducted include: normality test, multicollinearity test homoscedasticity test and ANOVA.

Normality test is a test of whether the residuals are normally distributed. This study used Shapiro-Wilk and quantile-quantile plots (Q-Q plots) to test for normality owing to its usefulness in comparing two samples to see if they arise from the same distribution. In linear regression, this helped to ascertain the normality of the residuals. The quantile-quantile plot is a graphical technique for determining if two data come from populations with a common distribution. A Q-Q is a plot of the quantiles of the first set of the quantiles of the second data set. A quantile is a fraction or percentage of a point below the given value, for instance, a 0.0 or 30% quantile is the point at which 30% of the data fall below and 70% fall in that value (Llido & Todeschini, 1994).

Multicollinearity is the state of very high inter-correlations among the independent variables. It's therefore, a type of disturbance in the data. Statistical inferences made about the data may not be reliable if multicollinearity is present in the data (Brook, 2008). The study used variance inflation factor (VIF) to test for Multicollinearity. Absence of multicollinearity is confirmed when the VIF values are less than 10.

Homoscedasticity refers to the assumption that the dependent variable exhibits similar amounts of variance across the range of values for an independent variable. This study used Breusch Pagan test to test for homoscedasticity. For variance to be homoscedastic, the test statistic should have a p value greater than 0.05.

ANOVA test helps to determine whether the survey results are significant. Analysis of variance tests to determine the results that the independent variables have on the dependent variable. For the results to be significant, the p value should be less than 0.05 significance level.

## CHAPTER FOUR

### DATA ANALYSIS, FINDINGS AND DISCUSSION

#### 4.1 Introduction

This chapter captures the study results, data analysis, findings and presentation of the results obtained. Descriptive and inferential statistics were used to analyze the study results with a view of documenting the findings.

#### 4.2. Response Rate

The study targeted a population size of 64 respondents from which 42 filled in and returned the questionnaires, making a response rate of 65.6%. This response rate was satisfactory to make conclusions for the study. The total response rate was above the 51 percent response threshold for questionnaire surveys in social sciences (Pinsonneault & Kraemer, 1993) and thus the use of the collected data was considered reliable for this study.

**Table 4.1: Response Rate**

	<b>Frequency</b>	<b>Percentage</b>
Successful	42	65.6
Unsuccessful	22	34.4
<b>Total</b>	<b>64</b>	<b>100</b>

**Source: Survey Data (2018)**

#### 4.2.1 Reliability Statistics

The study used Cronbach's alpha coefficient to test for reliability of the instrument as indicated in table 4.2.

**Table 4. 2: Reliability Statistics**

<b>Cronbach's Alpha</b>	<b>Cronbach's Alpha Based on Standardized Items</b>	<b>N of Items</b>
.932	.583	42

**Source: Survey Data (2018)**

For the research instrument to be reliable, the alpha coefficient should be greater than 0.7 (Cronbach, 1951). The result in Table 4.2 shows an overall Cronbach’s Alpha value of 0.932. The research instrument was therefore considered as reliable since it surpassed the minimum threshold of 0.7.

### 4.3 Demographic Information

This sub-section presents results of gender of the respondents, number of years the business has operated, type of business ownership, size of real estate investment in Nairobi County and the kind of financing employed to fund real estate investments.

#### 4.3.1 Gender of Respondents

The respondents were asked to indicate their sex to make the study gender sensitive. Their responses were as indicated in the table below.

**Table 4. 3: Gender of respondents**

	Frequency	Percent	Valid Percent	Cumulative Percent
Male	20	47.6	47.6	
Female	22	52.4	52.4	47.6
<b>Total</b>	<b>42</b>	<b>100.0</b>	<b>100.0</b>	100.0

**Source: Survey Data (2018)**

The research study sought to establish the respondent’s gender distribution. From the findings above, the females were slightly above at 52.4% while the males were at 47.6%. The gender distribution above confirms that both male and female were well represented in the study.

#### 4.3.2 Number of years in Business

To assess the responsibility of the businesses, the respondents were requested to give the number of years the business have been in existence, and their responses were as shown in table 4.4.

**Table 4. 4: Number of years in Business**

	<b>Frequency</b>	<b>Percent</b>	<b>Valid Percent</b>	<b>Cumulative Percent</b>
5-10 Years	15	35.7	35.7	35.7
10-15 Years	7	16.7	16.7	52.4
Above 15 Years	20	47.6	47.6	100.0
<b>Total</b>	<b>42</b>	<b>100.0</b>	<b>100.0</b>	

**Source: Survey Data (2018)**

Findings in Table 4.4 indicate that 35.7% of the businesses had existed for between 5-10 years, 16.7% were between 10-15 years and 47.6% were above 15 years. An increase in the number of businesses that have come up in the last five years may be as a result of the increased interest by the investors to venture into the real estate sector. All the businesses being in operation for more than 5 years was an indication that the data obtained was dependable as a result of better understanding and experience in the real estate sector.

#### **4.3.3 Types of Business Ownership**

The respondents were requested to provide type of business ownership, and their responses were as portrayed in table 4.5.

**Table 4. 5: Types of Business ownership**

	<b>Frequency</b>	<b>Percent</b>	<b>Valid Percent</b>	<b>Cumulative Percent</b>
Sole Proprietorship	1	2.4	2.4	2.4
Partnership	1	2.4	2.4	4.8
Limited Company	40	95.2	95.2	100.0
<b>Total</b>	<b>42</b>	<b>100.0</b>	<b>100.0</b>	

**Source: Survey Data (2018)**

Findings in Table 4.5 indicate that a small number of businesses were sole proprietorship and partnership. This is shown by 2.4% each, 95.2% were limited companies. Limited companies seem to be the most preferred mode of business ownership due to its ease in raising additional capital through IPO, dilutive secondary offering and its enhanced capacity to get debt financing and also its legal personality thus a separate entity from the owners.

#### 4.3.4 Size of Real Estate Investment in Nairobi County

As a precondition to assess the reliability of the data collected, respondents were requested to indicate the size of real estate investment in Nairobi County. Their responses were as shown in table 4.6.

**Table 4. 6: Size of real estate investment in Nairobi county**

	<b>Frequency</b>	<b>Percent</b>	<b>Valid Percent</b>	<b>Cumulative Percent</b>
0-100 Million	1	2.4	2.4	2.4
100-250 Million	6	14.3	14.3	16.7
250-500 Million	11	26.2	26.2	42.9
Above 500 Million	24	57.1	57.1	100.0
<b>Total</b>	42	100.0	100.0	

**Source: Survey Data (2018)**

From the analysis in the table above, 2.4% had an investment size of 0-100 Million, 14.3% had an investment of 100-250 Million, 26.3% had an investment of between 250-500 Million and 57.1% had an investment above 500 Million. A large number of firms investing above 500 Million confirms that real estate sector is a capital-intensive sector and requires an enormous capital outlay (Ezimuo, Onyejiaka & Emoh, 2014).

#### 4.3.5 Kind of Financing Employed to Fund Real Estate Investments

The study also sought to find out the kind of financing employed by real estate investments as indicated in table 4.7.

**Table 4. 7: Kind of financing employed to fund real estate investments**

	<b>Frequency</b>	<b>Percent</b>	<b>Valid Percent</b>	<b>Cumulative Percent</b>
Mortgage	22	52.4	52.4	52.4
Venture Capital	7	16.7	16.7	69.0
Equity	13	31.0	31.0	100.0
<b>Total</b>	42	100.0	100.0	

**Source: Survey Data (2018)**

The research study wanted to establish the kind of financing employed by real estate investments in Nairobi. The findings as shown in Table 4.7 indicate that 52.4% of the respondents preferred mortgage financing, 31% preferred equity financing and 16.7% preferred venture capital financing. Venture capital as a source of financing revealed a small percentage as compared to the other sources of financing. This can be explained by interest of few venture capital firms to finance real estate sector. Mortgage was the most preferred source of financing since it a cheaper financing source as a result of interest tax shield and it was followed in preference by equity which is considered less risky by the investors. This is in agreement with a study done by Bjorkholm and Johansson (2015) on how interest rate levels have an effect on capital structure decisions. The study collected data from 19 Swedish companies over a period of 15 years from 1998 to 2014. The study found out that debt financing is cheaper as compared to equity financing.

#### **4.4 Study Variables**

This section consists of descriptive findings on the dependent and independent variables as used in the study. Descriptive statistics enable the description of the distribution (mean) and variation (Standard deviation) of responses of the target population as well as allowing the researcher to determine average scores on the variables used in the study. The scores in the study used Likert-type scale where 1=Strongly disagree, 2=Disagree, 3=Neutral, 4=Agree and 5=Strongly Agree.

##### **4.4.1 Mortgage Financing**

The study analyzed how mortgage financing affects performance of real estate sector in Nairobi County, Kenya. The findings showing the minimum and maximum scores, mean score and standard deviation of each statement are shown in table 4.8.

**Table 4.8: Findings in relation to mortgage financing**

	N	Min	Max	Mean	Std. Deviation
Fixed rate mortgages are favorable financing source for better performance	42	2	5	4.05	.623
Adjustable rate mortgages are favorable financing source for better performance	42	2	5	4.14	.872
Interest rate capping has significantly reduced mortgage uptake	42	2	5	4.12	.772
Mortgage uptake is highly bureaucratic in Kenya	42	3	5	4.12	.705
Credit rating is the main factor that determine mortgage access	42	2	5	4.10	.906
Mortgage financing affect performance of real estate	42	3	5	4.21	.682
Valid N	42				

**Source: Survey Data (2018)**

According to Table 4.8, the mean value of the statement that fixed rate mortgages are favorable financing source for better performance is 4.05 with a standard deviation of 0.623. Using the 68-95-99.7 rule of normal distribution (Galarny, 2018), 68% of the responses fall within one standard deviation of the mean. This implies that about 68 % of the responses were between 3.427 and 4.673 indicating that most respondents were in agreement that fixed rate mortgages are favorable financing source for better performance. This is mostly evident in cases where there is a general interest rates rise and therefore fixed rate mortgages will remain constant at the predetermined rate. The statement that adjustable rate mortgages are favorable financing source for better performance has a mean value of 4.14 and a standard deviation of 0.872. This indicates that about 68% of the responses were between 3.268 and 5.012 confirming that adjustable rate mortgages are favorable financing source for better performance. This is mostly apparent in cases where there is a general interest rates fall.

The results from Table 4.8 show that the mean value of the statement that interest rate capping has significantly reduced mortgage uptake is 4.12 with a standard deviation of 0.772.

This implies that about 68% of the responses were between 3.348 and 4.892 indicating that interest rate capping has significantly reduced mortgage uptake. The results further show that the mean value of the statement that mortgage uptake is highly bureaucratic in Kenya is 4.12 with a standard deviation of 0.705. This indicates that about 68% of the responses were between 3.415 and 4.825. This confirms that mortgage uptake is highly bureaucratic in Kenya.

Table 4.8 further shows that the mean value of the statement that credit rating is the main factor that determines mortgage access is 4.10 with a standard deviation of 0.906. This indicates that about 68% of the responses were between 3.194 and 5.006. This confirms that credit rating is the main factor that determines mortgage access. The results further show that the mean value of the statement that mortgage financing affect performance of real estate is 4.21 with a standard deviation of 0.682. This indicates that about 68% of the responses were between 3.528 and 4.892. This confirms that mortgage financing affect performance of real estate.

#### **4.4.2 Venture Capital Financing**

The research study analyzed how venture capital financing affects performance of real estate sector in Nairobi County, Kenya. The findings indicating the minimum and maximum scores, mean score and standard deviation of each statement are shown in table 4.9.

According to Table 4.9, the mean value of the statement that venture capital financing offers high interest rates is 4.17 with a standard deviation of 0.696. Using the 68-95-99.7 rule of normal distribution (Galarny, 2018), 68% of the responses fall within one standard deviation of the mean. This signifies that about 68 % of the responses were between 3.474 and 4.866 indicating that most respondents were in agreement that venture capital financing offers high interest rates. The statement that venture capital financing offers opportunity for monitoring and efficiency has

a mean value of 4.33 with a standard deviation of 0.754. This indicates that about 68% of the responses were between 3.576 and 5.084 confirming that venture capital financing offers opportunity for monitoring and efficiency.

**Table 4. 9: Findings in relation to venture capital financing.**

	<b>N</b>	<b>Min</b>	<b>Max</b>	<b>Mean</b>	<b>Std. Dev</b>
Venture capital financing offers high interest rates	42	3	5	4.17	.696
Venture capital financing offers opportunity for monitoring and efficiency	42	3	5	4.33	.754
Venture capital financing is less bureaucratic and has less paperwork	42	3	5	4.86	.502
Venture capital financing offers more informal capital	42	2	5	4.05	.882
Venture capital financing leads to more innovations and better performance	42	2	5	4.33	.786
Venture capital is a risky mode of financing	42	3	5	4.38	.661
<b>Valid N</b>	42				

**Source: Survey Data (2018)**

The results from Table 4.9 show that the mean value of the statement that venture capital financing is less bureaucratic and has less paperwork is 4.86 with a standard deviation of 0.502. This implies that about 68% of the responses were between 4.358 and 5.362 confirming that venture capital financing is less bureaucratic and has less paperwork. The results further show that the mean value of the statement that venture capital financing offers more informal capital is 4.05 with a standard deviation of 0.882. This indicates that about 68% of the responses were between 3.168 and 4.932. This confirms that venture capital financing offers more informal capital.

Table 4.9 further shows that the mean value of the statement that venture capital financing leads to more innovations and better performance is 4.33 with a standard deviation of 0.786. This implies that about 68% of the responses were between 3.544 and 5.116. This confirms that venture capital financing leads to more innovations and better performance. The

results further show that the mean value of the statement that venture capital is a risky mode of financing is 4.38 with a standard deviation of 0.661. This indicates that about 68% of the responses were between 3.719 and 5.041. This confirms that venture capital is a risky mode of financing.

#### 4.4.3 Equity Financing

The research study analyzed how equity financing affects performance of real estate sector in Nairobi County, Kenya. The findings showing the minimum and maximum scores, mean score and standard deviation of each statement are shown in table 4.10.

**Table 4. 10: Findings in relation to Equity Financing.**

	N	Min	Max	Mean	Std. Dev
Equity financing is less risky	42	2	5	4.14	.783
Public stock placement through IPOs results to unfavorable dilution of company's ownership	42	3	5	4.45	.670
Private placements are less bureaucratic and more favorable	42	3	5	4.40	.627
IPO leads to publicity of the company and improves performance	42	2	5	4.12	.861
Secondary placement of shares decreases the value of the firm	42	2	5	4.07	.838
<b>Valid N</b>	42				

**Source: Survey Data (2018)**

According to Table 4.10, mean value of the statement that equity financing is less risky is 4.14 with a standard deviation of 0.783. Using the 68-95-99.7 rule of normal distribution (Galarny, 2018), 68% of the observations fall within one standard deviation of the mean. This implies that about 68 % of the responses were between 3.357 and 4.923 indicating that most respondents were in agreement that equity financing is less risky. The statement that public stock placement through IPOs results to unfavourable dilution of company's ownership has a mean value of 4.45

and a standard deviation of 0.670. This means that about 68% of the responses were between 3.78 and 5.12 confirming that public placement through IPOs results to unfavourable dilution of the company's ownership as new investors will acquire some shareholding previously held by existing owners.

The results from Table 4.10 show that the mean value of the statement that private placements are less bureaucratic and more favorable is 4.40 with a standard deviation of 0.627. This implies that about 68% of the responses were between 3.773 and 5.027 confirming that private placements are less bureaucratic and more favourable. The results further show that the mean value of the statement that IPO leads to publicity of the company and improves performance is 4.12 with a standard deviation of 0.861. This indicates that about 68% of the responses were between 3.259 and 4.981. This confirms that IPO leads to publicity of the company and improves performance.

Table 4.10 further shows that the mean value of the statement that secondary placement of shares decreases the value of the firm is 4.07 with a standard deviation of 0.838. This indicates that about 68% of the responses were between 3.232 and 4.908. This confirms that secondary placement of shares decreases the value of the firm. This is in agreement with an observation made by Caplinger (2013) on why companies offering more shares can hurt the investors. Caplinger (2013) observed that reduction in value of the firm is because secondary placements, especially by insiders of the company, sends a signal to the potential investors that the company could be facing difficulties and its going concern is in doubt therefore resulting in a dip in the share price and consequently a decrease in the value of the firm.

#### **4.5. Diagnostic Tests**

This study carried out some diagnostic test including test for normality, test of multicollinearity, test of homoscedasticity and ANOVA.

### 4.5.1. Test for Normality

Given multiple regression analysis, the study used Shapiro-Wilk to test for normality of the residuals as shown in the table 4.11.

**Table 4. 11: Tests of Normality**

	Shapiro-Wilk		
	Statistic	Df	Sig.
	.954	42	.392

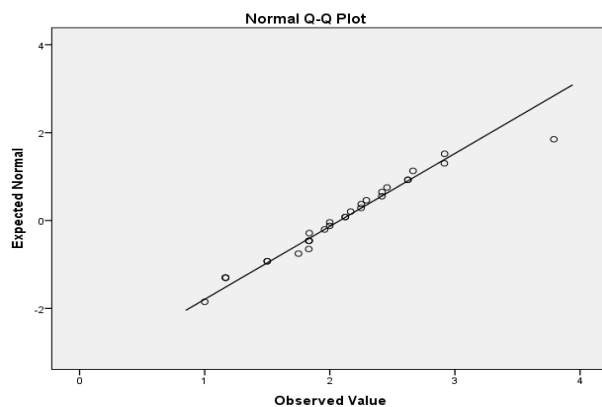
**Source: Survey Data (2018)**

H<sub>0</sub>: Normal distribution

Fail to reject H<sub>0</sub> if the p value is greater than 0.05, otherwise, reject H<sub>0</sub> (Ghasemi & ZahediasI, 2012).

The p value in Table 4.11 is 0.392 which is greater than 0.05 and therefore, the study accepted the null hypothesis. There was therefore no evidence of significance deviation from normality of the residuals.

Using Q-Q plot on Figure 4.1 below, the points fall along the straight 45-degree line, this indicates that the sample data quantiles follow the normal distribution quantiles. The study can therefore safely conclude that data used was normally distributed.



**Figure: 4.1: Normal Q-Q Plot**

#### 4.5.2 Tests of Multicollineality

The table below provides the output of multicollinearity test using VIF.

**Table 4. 12: Tests of Multicollinearity**

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics
	B	Std. Error	Beta			VIF
(Constant)	.181	1.532		.118	.907	
Venture	.007	.218	.005	.034	.973	1.045
Mortgage	.820	.252	.477	3.248	.002	1.070
Equity	.062	.221	.040	.280	.781	1.027

a. Dependent Variable: Performance

**Source: Survey Data (2018)**

Kennedy (1992) recommends 10 as the maximum levels of VIF acceptable in measuring multicollinearity. VIF that exceed 10 confirms presence of multicollinearity. Based on the coefficients output collinearity statistics obtained in Table 4.12, VIF values were between 1 and 10. It was therefore concluded that there was no multicollinearity problems.

#### 4.5.3 Tests of Homoscedasticity

The study used Breusch Pagan to test for homoscedasticity of the residuals as shown in the table below.

**Table 4.13: Tests of Homoscedasticity**

	LM	Sig
BP	3.660	.301
Koenker	1.973	.578

**Source: Survey Data (2018)**

H<sub>0</sub>: heteroscedasticity not present (homoscedasticity)

Fail to reject  $H_0$  if the p value is greater than 0.05 significance level, otherwise reject  $H_0$  (Su & Berenson, 2017).

Since the p value in Table 4.13 was greater than 0.05 significance level, the study accepted the null hypothesis and concluded that the variance of the residuals was constant.

#### **4.6 Inferential Statistics**

Inferential statistics is concerned with making predictions or inferences about a population from observations and analyses of a sample (Kern, 2014). Thus, inferential statistics attempts to generalize the results of descriptive statistics to a larger population of interest. The study applied correlation analysis, regression analysis and ANOVA to make inferences about the population of the real estate companies in Nairobi.

##### **4.6.1. Correlation Analysis**

The study determined the correlation between the independent variables used in the study. For this analysis, Pearson correlation was used to determine the degree of association within the independent variables and also between independent variables and the dependent variable. The analysis of these correlations seems to support the hypothesis that each independent variable in financing sources had its own particular informative value in the ability to explain the performance of real estate sector in Nairobi County, Kenya.

**Table 4. 14: Correlation Matrix**

		<b>Mortgage Financing</b>	<b>Venture capital Financing</b>	<b>Equity Financing</b>	<b>Performance</b>
Mortgage	Pearson Correlation	1	.202	.155	.484**
	Sig. (2-tailed)		.199	.327	.001
	N	42	42	42	42
Venture	Pearson Correlation	.202	1	-.013	.101
	Sig. (2-tailed)	.199		.935	.526
	N	42	42	42	42
Equity	Pearson Correlation	.155	-.013	1	.114
	Sig. (2-tailed)	.327	.935		.472
	N	42	42	42	42
Performance	Pearson Correlation	.484**	.101	.114	1
	Sig. (2-tailed)	.001	.526	.472	
	N	42	42	42	42

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

**Source: Survey Data (2018)**

A Pearson correlation test was done to investigate the statistical significance effect of mortgage financing on performance of real estate sector in Nairobi County, Kenya. The study found out that performance of real estate sector in Nairobi County, Kenya was significantly affected by mortgage financing which was statistically significant at  $r = .484^*$  and p value of 0.001 which is less than the significance level of 0.05. The relationship between venture capital financing and performance of real estate sector in Nairobi County, Kenya was positive with a coefficient of correlation of .101, however, the relationship was insignificant as shown by p value of 0.526 which is greater than the significance level of 0.05. The relationship between equity financing and performance of real estate sector in Nairobi County, Kenya was positive with a coefficient of correlation of .114, however, the relationship was insignificant as shown by p value of .472 which is greater than the significance level of 0.05.

#### 4.6.2. Regression Analysis

A multiple linear regression analysis was undertaken to examine the effect of mortgage financing, venture capital financing and equity financing on performance of real estate sector in Nairobi County, Kenya. Table 4.15 presents the summary model for the regression analysis.

**Table 4. 15: Regression and Model Summary**

<b>Model</b>	<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Std. Error of the Estimate</b>
	.585 <sup>a</sup>	.396	.364	3.01542

a. Predictors: (Constant), Equity, Venture, Mortgage  
b. Dependent Variable: Performance

**Source: Survey Data (2018)**

**significance level=0.05**

Result in table 4.15 indicates that the goodness of fit of the model was adequate. This is reported by an r squared of 0.396 which means that 39.6% of the variation in real estate sector performance is explained by mortgage financing, venture capital financing, and equity financing. This further implies that 60.4% of the variation in real estate sector performance is explained by other factors not captured in the model.

**Table 4. 16: ANOVA**

<b>Model</b>	<b>Sum of Squares</b>	<b>df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
Regression	12.078	3	4.026	3.905	.016 <sup>b</sup>
Residual	39.181	38	1.031		
Total	51.259	41			

a. Dependent Variable: Performance  
b. Predictors: (Constant), Equity, Venture, Mortgage

**Source: Survey Data (2018)**

**significance level=0.05**

An Analysis of Variance (ANOVA) results in Table 4.16 indicates that the overall model was significant. This was supported by a p value of 0.016. The ANOVA results demonstrated that the

sources of financing, that is mortgage financing, venture capital financing and equity financing were good predictors of real estate performance.

**Table 4. 17: Coefficients**

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	.181	1.532		.118	.907
Mortgage	.820	.252	.477	3.248	.002
Venture	.007	.218	.005	.034	.973
Equity	.062	.221	.040	.280	.781

a. Dependent Variable: Performance

**Source: Survey Data (2018)**

**significance level=0.05**

From the data in the above table, the established regression equation is extracted as shown below:

$$Y = 0.181 + 0.820X1 + 0.007X2 + 0.062X3$$

Table 4.17 presents regression of coefficient results which indicates that there was a positive relationship between mortgage financing and real estate performance. The results also indicate that the relationship was significant since the reported p value of 0.002 was less than the critical value of 0.05. Results further indicate that all the other sources of finance had an insignificant effect on real estate performance.

### **4.6.3 Discussion of the Findings**

From the findings, R-squared of 0.396 means that 39.6% of the variation in real estate performance is explained by mortgage financing, venture capital financing and equity financing. This further implies that 60.4% of the variation in real estate performance is explained by other factors not captured in the model.

The study found out that performance of real estate sector in Nairobi County, Kenya was significantly affected by mortgage financing which was statistically significant at  $r = .484^*$  and p value of 0.001 which is less than 0.05. The relationship between venture capital financing and performance of real estate sector in Nairobi County, Kenya was positive with a coefficient of correlation of .101. The relationship was insignificant as shown by p value of 0.526 which is greater than 0.05. The relationship between equity financing and performance of real estate sector in Nairobi County, Kenya was positive with a coefficient of correlation of .114. The relationship was insignificant as shown by p value of .472 which is greater than 0.05.

An Analysis of Variance (ANOVA) results in table 4.16 indicates that the overall model was significant. This was supported by a p value of 0.016. The ANOVA results demonstrated that mortgage financing, venture capital financing and equity financing are good predictors of real estate performance. Finally, the study found out that there was a positive relationship between mortgage financing and real estate performance. The results also indicated that the relationship was significant since the reported p value 0.002 was less than the critical value of 0.05. The results further indicated that all the other sources of finance had an insignificant effect on real estate performance.

#### ***4.6.3.1 Mortgage Financing and Performance of Real Estate Sector***

From the study, mortgage financing had a statistically significant effect on real estate sector performance in Nairobi County, Kenya. The result is consistent with Nwankwo (2014) who examined the implications of mortgage financing on the housing for all in Nigeria by the year 2020. The study found out that mortgage financing gives a significant positive impact on the supply of housing for all in Nigeria by year 2020. The study is also consistent with Ndinda (2014) who carried out a study on the impact of financing using mortgage on real estate market

performance in Kenya. The study established that there exists a significant and positive relationship between real estate market performance and mortgage financing in Kenya.

Similarly, the study is in agreement with Tauseef, Lohano and Khan (2015) who conducted a study on the impact of debt financing on corporate performance: evidence from Pakistan's textile firms. The study established that debt level that is optimal exists for the performance of a company and any debt beyond that point decreases performance due to increased interest costs. Also, the study is in agreement with Mackenzie (2013) who carried out a study on the influence of financing using mortgage on real estate industry performance in Nairobi, Kenya. The study established that mortgage financing was greatly influenced by interest rates and it's significantly correlated to the performance of real estate industry.

The study however is not in agreement with Makanga (2015) who studied on the effect of debt financing on performance of finances of companies that are listed at the NSE. The study ascertained that both current and long-term debt do not significantly affect the firms' performance.

#### ***4.6.3.2 Venture Capital Financing and Performance of Real Estate Sector***

The study found out that venture capital financing had a statistically insignificant effect on real estate sector performance in Nairobi County, Kenya. The findings are not in line with Peneder (2010) who conducted a study on the effect of venture capital on firm growth and innovation behavior. The paper found out that firms that are financed using venture capital grow faster as far as turnover and employment is concerned and that they are also more innovative than any other firms. The findings are also not in agreement with Industry Canada (2013) who undertook a study on Canadian firms' performance that are financed using venture capital. The study sought to assess the influence of venture capital on Canadian firms' performance. The study established

that firms that are financed using venture capital had wonderful performance while considering a number of measures such as stronger growth in sales, growth of revenue, growth of employees and growth of assets.

Further, the study is not in agreement with Lyxell and Nordén (2013) who conducted a study on performance dynamics of firms financed using venture capital. Swedish venture capital market was used as a case for the study. The study established that venture capital financed firms do show superior performance in terms of significantly faster sales growth. Also, the study is not consistent with Memba (2011) who undertook a study on the influence of financing using venture capital on the performance of Kenya's small and medium enterprises. The study established that in this respect, the venture capital's impact on performance of SMEs is both practical and real and that venture capital facilitates wealth creation. Additionally, the study is not in agreement with Njama (2013) who carried out a study on the impact of financing using venture capital on small and medium enterprises' growth in Kenya. The study established that there is a significant and positive relationship between SMEs' growth and financing using venture capital.

#### ***4.6.3.3 Equity Financing and Performance of Real Estate Sector***

The study found out that equity financing had a statistically insignificant effect on real estate performance in Nairobi County, Kenya. The findings are in agreement with Musila (2015) who studied on the relationship between financing using equity and performance of finances of the petroleum and energy companies that are listed at NSE. The study found out that there is an insignificant relationship between the variables that were involved in the study.

The study however is not in agreement with Saad *et al.* (2014) who conducted a study on the effect of financing using equity and debt on the performance of SME in Malaysia. The study

found out that there is a positive and significant effect on the performance of business but for debt financing it was found to be insignificant. The study also does not agree with Raude, Wesonga and Wawire (2015) who carried out a study on strategy of financing using equity and small and medium enterprises' performance in Kenya. The paper sought to ascertain how equity financing impacts SMEs' performance in the Municipal of Kakamega, Kenya. The study ascertained that financing using equity empirically had an effect on SMEs' performance and there exist a significant positive relationship between financing strategy using equity and the performance variables.

## **CHAPTER FIVE**

### **SUMMARY, CONCLUSION AND RECOMMENDATIONS**

#### **5.1 Introduction**

This chapter presents the summary and description of the findings derived from the study. This chapter further draws conclusions from the findings and makes concrete recommendations to various stakeholders and gives suggestions for further studies based on the specific objectives of this study.

#### **5.2 Summary**

The general objective of the study was to establish the effect of financing sources on performance of real estate sector in Nairobi County, Kenya. The specific objectives were to investigate the effect of mortgage financing sources on the performance of real estate sector in Nairobi County, Kenya, to determine the effect of venture capital financing sources on the performance of real estate sector in Nairobi County, Kenya and to determine the effect of equity financing sources on the performance of real estate sector in Nairobi County, Kenya.

##### **5.2.1 Mortgage Financing on the Performance of Real Estate Sector**

The study found out that performance of real estate sector in Nairobi County, Kenya was significantly affected by mortgage financing which was statistically significant with a correlation coefficient  $r$  of 0.484\* and  $p$  value of 0.001 which is less than 0.05. The regression analysis indicates that a one unit increase in mortgage financing will increase the performance of the real estate sector by 0.82 unit. From the findings, mortgage financing is the most ideal financing source for the real estate sector. The findings are consistent with the trade off theory by Modigliani and Miller (1963) which states that companies attain benefits from leverage up to a point where optimum capital structure is reached.

Majority of the respondents agreed that fixed rate mortgages were favourable for better performance. This is as a result of the fixed interest rate for the entire loan period and the predictability of all future payments. Majority of the respondents were of the view that in an instance where the overall interest rate falls, adjustable interest rate mortgages would be more ideal as the overall interest rate fall would mean that they will pay less interest for their mortgages. This will translate to a better real estate performance.

Interest rate capping was viewed by most respondents as the main hindrance in mortgage uptake and has effectively reduced the mortgage uptake. The respondents claim that as a result of interest rate capping, the financial institutions have been selective on whom to advance mortgages and profile most investors as risky thus declining their mortgage applications. This has resulted in reduction of funds available for new investments in the real estate sector.

Majority of the respondents were of the view that mortgage uptake is so bureaucratic and involves a lot of paperwork and documentation. They also agreed to the fact that credit rating is a major factor that any financial institution takes into account while making a decision on whether to advance a mortgage. The credit rating scores are usually obtained from the licensed credit reference bureaus which give the past repayment history of the borrower.

### **5.2.2 Venture capital financing on the Performance of Real Estate Sector**

The study indicates that the relationship between venture capital financing and performance of real estate sector in Nairobi County, Kenya was positive but insignificant with a correlation coefficient  $r$  of 0.101 and  $p$  value of 0.5263 which is greater than 0.05. The regression analysis indicates that a one unit increase in venture capital financing results to a 0.007 unit increase in the performance of real estate sector.

Majority of the respondents agreed that venture capital financing offer high interest rates. This is because the venture capitalists invest in businesses deemed by other capital providers as risky thus need for a higher compensation for the risk. They also agreed that venture capital financing offers an opportunity for monitoring and efficiency. The venture capitalists undertake the monitoring of the businesses they have financed to ensure that there is efficiency and decrease the chances of the businesses collapsing.

The respondents agreed that venture capital financing leads to more innovations and better performance of the real estate sector. The venture capitalists involve experts on the businesses they are investing in to ensure rapid growth through innovations and efficiency. A high number of respondents agreed that venture capital financing is less bureaucratic and has less paperwork as it is mostly an informal mode of financing. The respondents also agreed that venture capital financing is a risky mode of financing due to the possibilities of investors being shortchanged by the venture capitalists.

### **5.2.3 Equity Financing on the Performance of Real Estate Sector**

The study found out that the relationship between equity financing and performance of real estate sector in Nairobi County, Kenya was positive but statistically insignificant with a correlation coefficient  $r$  of 0.0114 and a  $p$  value of 0.472 which is greater than 0.05. The regression analysis indicates that a one unit increase in equity financing will result to a 0.062 unit increase in the performance of real estate sector.

Majority of the respondents were of the view that equity financing is less risky since the equity providers are also the owners of the business. They also agreed that public stock placement through IPOs results to unfavourable dilution of the company's ownership since it

involves bringing in new shareholders thus diluting the ownership of already existing shareholders.

The respondents agreed that private placements are favourable and less bureaucratic since they only involve selling shares to a few selected individuals or entities that can bring in a substantial amount of funds. They were of the view that IPOs lead to publicity of the company which further fuels performance of real estate sector. This is as a result of marketing that is involved in the IPO process to inform the prospective investors about the company and its business. The respondents were of the view that secondary placement of shares decrease the value of the firm as the investors offloading their shareholding send a signal that the company could be facing some future uncertainties, effectively reducing the value of the company.

### **5.3 Conclusions**

#### **5.3.1 Mortgage Financing on the Performance of Real Estate Sector.**

The study concluded that performance of real estate sector in Nairobi County, Kenya was significantly affected by mortgage financing which was statistically significant. The study further concluded that mortgage financing is the most ideal financing source for the real estate sector.

Also, the study concluded that fixed rate mortgages are more favourable for better performance, interest rate capping has reduced the mortgage uptake, mortgage uptake process is so bureaucratic and involves a lot of paperwork and documentation and that credit rating is a major factor that determines mortgage access.

#### **5.3.2 Venture Capital Financing on the Performance of Real Estate Sector**

The study concluded that the relationship between venture capital financing and performance of real estate sector in Nairobi County, Kenya was positive. However, the relationship was insignificant in influencing the performance of real estate sector in Nairobi County, Kenya. Even

though the relation was insignificant, venture capital financing offers an opportunity for monitoring and efficiency. Venture capitalists undertake monitoring of the businesses they have financed to ensure that there is efficiency and decrease the chances of the businesses collapsing.

The study further concluded that venture capital financing leads to more innovations and better performance of the real estate sector, is less bureaucratic and has less paperwork as it is mostly an informal mode of financing. Venture capital financing is however considered a risky mode of financing due to the possibilities of investors being shortchanged by the venture capitalists and also attracts higher interest rates.

### **5.3.3 Equity Financing on the Performance of Real Estate Sector**

The study concluded that the relationship between equity financing and performance of real estate sector in Nairobi County, Kenya was positive. However, the relationship was statistically insignificant in influencing the performance of the real estate sector in Nairobi County, Kenya. Also, the study concluded that equity financing is less risky since the equity providers are also the owners of the business.

The study further concluded that public stock placement through IPOs results to unfavourable dilution of the company's ownership since it involves bringing in new shareholders thus diluting the ownership of already existing shareholders, private placements are favourable and less bureaucratic, IPOs lead to publicity of the company which further fuels performance of real estate sector and secondary placement of shares decrease the value of the firm.

## **5.4 Recommendations**

### **5.4.1 Mortgage Financing on the Performance of Real Estate Sector.**

The research recommends that in order for the investors to maximize returns on their real estate investments, they should adopt strategies such as increasing mortgage financing up to an optimal

point since it has the highest returns as compared to other financing sources. The research further recommends that the government should consider repealing laws capping the interest rates as they have resulted in a credit crunch as commercial banks ration credit which has slowed down mortgage uptake. Commercial banks have become more selective about who they lend to and have lost the incentive to grant long-term loans and finance emerging economic sectors, as the cap means that the rate will be the same as for safer short-term loans.

#### **5.4.2 Venture Capital Financing on the Performance of Real Estate Sector**

The study established that venture capital is a risky mode of financing real estate sector hence the research recommends the following mitigating steps: Real estate investors should assess and evaluate potential new investments, assess and evaluate potential investment targets regarding risk and return, e.g. performing different types of due diligences like financial, product, market, customer, legal, competitor analysis internally and externally and analyzing audited financial statements, check the risk associated with the management by verifying the track record of the management team and board members and performing criminal background checks. Further measures to be conducted before an investment decision is made can be the consideration of synergies with existing ventures and the risk preferences of the investors of the fund, financial contracting can be used by venture capitalists and the real estate investors as a protection against downside risk and also to generate value in portfolio companies by mitigating the agency problem. Agency problem as it has been explained in the agency theory by Meckling and Jensen (1976) will affect the performance of a firm. Financial contracting is one measure next to active involvement and direct monitoring to reduce information asymmetry, motivational and financial problems.

### **5.4.3 Equity Financing on the Performance of Real Estate Sector**

The research recommends that real estate companies should consider raising capital through private placements as opposed to public placements. This is because private placements are less bureaucratic, less costly and can raise substantial capital. The real estate companies should also distribute idle cash. Idle cash in excess of what the business needs to continue operations reduces the apparent profitability of the company when measured by return on equity.

### **5.5 Recommendations for Future Research**

Further research should be undertaken on the effect of regulation and supervision on mortgage uptake. Further research should also be done on the reasons behind high default rates among the consumers of mortgages from the clients' perspective.

The present study reveals that venture capital financing had no significant effect on real estate performance in Nairobi County, Kenya. However, further research should be undertaken on the government's role in regulation of venture capital financing sector.

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**APPENDICES**

**APPENDIX I: QUESTIONNAIRE**

Dear respondent,

This questionnaire is designed to collect primary data on **The Effect of Financing Sources on Performance of Real Estate Sector in Nairobi County, Kenya**. Due to your wealth of knowledge on the real estate sector financing sources, you are kindly requested to fill in the questions as per the instructions. The questions are meant for academic research purposes only and any information given will be treated with utmost confidentiality.

**PART I: Background information**

- 1. Name of company (optional).....
- 2. Respondent’s designation.....
- 3. Kindly indicate with a tick in the corresponding box.

i. Gender of respondent

Male	<input type="checkbox"/>
Female	<input type="checkbox"/>

ii. Number of years in business

1 – 5	<input type="checkbox"/>
5 – 10	<input type="checkbox"/>
10 – 15	<input type="checkbox"/>
Above 15	<input type="checkbox"/>

iii. Type of business ownership

Sole proprietor	
Partnership	
Limited company	
Other (Specify)	

iv. What is the size of your real estate investment in Nairobi County?

0 – 100 million	
100 – 250 million	
250 – 500 million	
Above 500 million	

v. What kind of financing do you employ to fund the real estate investments?

Mortgage	
Venture capital	
Equity	
Other (Specify)	

**PART II: CONTEXT QUESTIONS**

**Section 1: Mortgage Financing and Performance**

This section aims to get information on mortgage financing

Kindly indicate with a tick the degree to which you agree with the following statements; 1

Strongly Disagree (SD), 2 Disagree (D), 3 Neutral (N), 4 Agree (A), 5 Strongly Agree (SA).

	SD	D	N	A	SA
	1	2	3	4	5
Fixed rate mortgages are favourable financing source for better performance					
Adjustable rate mortgages are favourable financing source for better performance					
Interest rate capping has significantly reduced mortgage uptake					
Mortgage uptake is highly bureaucratic in Kenya					
Credit rating is the main factor that determine mortgage access					
Mortgage financing affect performance of real estate					

How has the existing interest rate cap influenced the availability of mortgage financing to the real estate sector.....  
 .....

What are the factors to consider in determining an appropriate financial institution to acquire a mortgage from.....

.....

**Section 2: Venture Capital Financing and Performance**

This section aims to get information on venture capital financing

Kindly indicate with a tick the degree to which you agree with the following statements; 1

Strongly Disagree (SD), 2 Disagree (D), 3 Neutral (N), 4 Agree (A), 5 Strongly Agree (SA).

	SD	D	N	A	SA
	1	2	3	4	5
Venture capital financing offers high interest rates					
Venture capital financing offers opportunity for monitoring and efficiency					
Venture capital financing is less bureaucratic with less paperwork					
Venture capital financing offers more informal capital					
Venture capital financing leads to more innovations and better performance					
Venture capital is a risky mode of financing					

What are your suggestions on how to mitigate the risks associated with venture capitalists shortchanging the real estate investors on the proposed investments .....

.....

.....

.....

**Section 3: Equity Financing and Performance**

This section aims to get information on equity financing

Kindly indicate with a tick the degree to which you agree with the following statements; 1

Strongly Disagree (SD), 2 Disagree (D), 3 Neutral (N), 4 Agree (A), 5 Strongly Agree (SA).

	SD	D	N	A	SA
	1	2	3	4	5
Equity financing is less risky					
Public stock placement through IPOs results to unfavorable dilution of company's ownership					
Private placements are less bureaucratic hence more favourable					
IPO leads to publicity of the company therefore improving performance					
Secondary placement of shares decreases the value of the firm					

What strategies should equity finance providers adopt to maximize the returns on their real estate investments.....

.....

.....

.....

**Section 4: Performance**

This section aims to get information on performance

Kindly indicate with a tick the degree to which you agree with the following statements; 1 Strongly Disagree (SD), 2 Disagree (D), 3 Neutral (N), 4 Agree (A), 5 Strongly Agree (SA).

	SD	D	N	A	SA
	1	2	3	4	5
Real estate sector has been growing over the last 10 years					
Rental prices have been steadily rising and therefore profits					
Real estate investment is less risky as compared to other investments					
Returns in the real estate sector are much higher than those of other investments					

Amongst the different financing sources, i.e. mortgage, equity and venture capital financing, which of them results to a superior performance in your own opinion and why .....

.....

.....

.....

## **APPENDIX II: POPULATION**

1. Acorn Management Services Ltd
2. Actis Africa Ltd
3. Africa Reit Ltd
4. AHCOF Investments (Kenya) Ltd
5. Africa Infrastructure Development Company (AIDC)
6. Amazon Projects Ltd
7. Amboseli Court Ltd
8. AMS Properties Ltd
9. Blueline Properties Ltd
10. Boleyn Magic Wall Panel Ltd
11. Camelot Consultants Ltd
12. Century City Properties Ltd
13. Cheriez Properties Ltd
14. Chigwell Properties Ltd
15. Coral Property International Ltd
16. Cytonn Real Estate
17. Daykio Plantations Ltd
18. Diamond Properties Merchants Ltd
19. Dream Homes Construction Ltd
20. Dunhill Consulting Ltd
21. Edifice Ltd
22. Elm ridge Ltd

23. Enkavilla Properties Ltd
24. Hass Consult Ltd
25. Heri Homes Properties Ltd
26. HF Development Investment
27. Homescape Properties Ltd
28. Ijenga Ventures Ltd
29. Kamhomes Investment Ltd
30. Karibu Homes
31. Karume Holdings Ltd
32. Kings Developers Ltd
33. Kzanaka Ltd
34. Leo Capital Holdings Ltd
35. Lifestyle Estates Ltd
36. Lordship Africa
37. Manrik Holdings ltd
38. Meera Construction Ltd
39. Mentor Management ltd
40. National Cooperative Housing Union
41. Natureville Homes
42. Oakpark Properties Ltd
43. Optiven Ltd
44. Panda Development Holdings Ltd/Aderdare Hills Golf Resort
45. Paradigm Projects

46. Parmalen investments Ltd
47. PDM (Kenya) Ltd
48. Pediment Developers
49. Pentagon Properties Ltd
50. Pioneer Holdings Ltd
51. Property Reality Company Ltd
52. Rozana Properties
53. Scion Real Estate Ltd
54. Sherry Blue Properties Ltd
55. Sigimo Enterprises Ltd
56. SJR Properties Ltd
57. Sohail Developments Ltd
58. Spartan Developers Ltd
59. Superior Homes Kenya Ltd
60. Suraya Properties Ltd
61. The Epic Properties Ltd
62. Urban Nirvana Property Solutions Ltd
63. Username Investment Ltd
64. Vaal Real Estate

Source: KPDA (2018)