

**INTERNATIONAL TRADE FINANCE PRODUCTS PROVIDED BY
KENYA COMMERCIAL BANK LIMITED TO SMALL AND
MEDIUM SIZED ENTERPRISES**

**BY
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DECLARATION

This research project is my original work and has not been submitted for examination to any other university.

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

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DEDICATION

I dedicate this project to my family, who did not give up on me but supported me and encouraged me throughout this MBA Programme.

ABSTRACT

SMEs would rather deal with the dreaded unscrupulous middlemen than venture into the murky and deep waters of international trade. None of the studies done has sought to address the problem of inadequate take up of the international Trade finance products by SMEs with specific reference to KCB SMEs. This study therefore sought to answer the question as to why SMEs in KCB are not quickly taking up the International Trade finance products offered to them by the bank. The study used case study research design. The data was collected among interviewees were ten KCB SME customers and five KCB staff members. Data was collected using both primary and secondary data. The primary data was collected using interview schedules data was analyzed using content analysis. From the study findings, the study concluded that their various international trade finance transactions at Kenya Commercial Bank limited. This transactions included issuance of letters of credit, bank guarantees and discounting of invoices among other products. The study concluded that the considerations that KCB gives while dealing with international trade finance products provided to small and medium sized enterprises were collateral requirement, nature of business, number of years that the SME had been a customer at KCB, customers experience in the area of specialization, whether the customer was doing business with a sanctioned country. The challenges facing KCB while issuing international trade finance products to SMEs included knowledge gap, the collateral requirement, the middlemen, impatience among some SMEs and the sanctions. On ways to curb challenges faced by KCB were through conducting awareness campaigns to sensitize SMEs customers about the various international finance products, through implement fully the tiered collateral requirements, and through structuring transactions depending on clients' needs and ability to pay. The study recommends that bank management should review the policies guiding the provision of international trade finance products to the SMEs. The study also recommends that the management should conduct regular awareness campaigns to sensitize SMEs customers on various international finance products. The study also recommends that the management should review the collateral requirement by the SMEs

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ABBREVIATIONS AND ACRONYMS

KCB...Kenya Commercial Bank Limited
SME...Small and Medium Enterprise
ICC...International Chamber Of Commerce
ITF...International Trade Finance
LC...Letter Of Credit
SOB...School Of Business
UON...University Of Nairobi
CBK...Central Bank Of Kenya
KBA...Kenya Bankers Association
KAM...Kenya Association of Manufacturers
FDI...Foreign Direct Investment
USD...United States Dollar
NSE...Nairobi Stock Exchange
KES...Kenya Shillings
GDP...Gross Domestic Product
GNP...Gross National Product
URC...Uniform Rules For Collections
URDG...Uniform Rules For Demand Guarantees
ISBP...International Standby Practices
ICT...Information Communications and Technology.

CHAPTER ONE

INTRODUCTION

1.1. Background of the study

Organizations operate in an environment where they receive goods and services as well as give out goods and services. The environment in which organizations operate is dynamic and requires organizations to be equally dynamic to stay ahead of the game. Organizations that choose to operate within their domestic market stifle their growth as the market becomes saturated. There is no room for expansion and thus will survive if they reinvent their products regularly and look for markets beyond.

Organizations that concentrate on domestic markets that is sourcing material locally and selling locally are constraining their growth. Comparative advantage theory can come into play where the organization chooses to operate in areas where they will use their synergies to make profits. Organizations will thus look beyond their borders to source for inputs and markets for their products and services. Financial institutions especially banks, should thus endeavor to meet their customers' needs by providing products and services that suit the needs of such clientele (Husted 2007).

Many organizations endeavor to maximize their returns or their shareholders equity by coming up with innovative ways to achieve this. Small and medium sized enterprises have to think out of the box to ensure they thrive. These organizations will therefore look for a financial partner, who will walk with them to achieve this. Small and medium sized

organizations are faced with stiff competition from the larger corporates and also at their level. Thus the need to partner with a dependable financial solutions provider is key.

The SMES, thus will naturally align themselves with financial institutions that understand their needs and are able to meet their need not only in time but offer the right solutions. Financial institutions especially banks are thus tasked with the duty to ensure they meet the needs of the SMEs. Banks have in the recent past embarked on strategies that are earmarked to see this sectors needs met. The SME sector is growing at a very rapid rate that for any financial institution that is not addressing the SME needs is bound to miss out on maximizing their shareholders equity (Hill 2008).

1.1.1 International Business and International Trade

An international business is any firm that engages in international trade or investment. A firm need not become a multinational enterprise by investing directly in operations in other countries to engage in international business. Hence we have SME's (small and medium enterprises) doing international business. As the world shifts towards a truly integrated global economy, more firms both large and small are becoming international businesses.

As organizations increasingly engage in cross border trade and investment, the need to have mergers recognize that their task of managing international business differs from that of managing a purely domestic business in various ways. Countries are different in their cultures, for instance, political systems, economic systems, legal systems and levels of economic development. With such differences, it is important to note that different

countries will thus require different modes of payment thus affecting different adoptions to the trade products that are available. This relates to both the importing and exporting concerns. For instance, where the culture of a people is trusting then loose payment methods will be adopted. In case the perception of the importing country is they are not trustworthy, then the exporting country will want a more tight payment mode, this is where the more complex payment mechanisms come into play.

International Trade occurs when a firm imports and or exports goods or services to consumers in another country. Foreign Direct Investment-FDI occurs when a firm invests resources in business activities outside its home country. The main difference between international business and FDI is that the international business need not invest its resources in the country it is operating in.

International business is thus the cornerstone of international trade, as it allows international trade to come about. International business and International trade are inseparable. International trade facilitates the buying and selling of goods and services across borders. Mercantilism theory is evidence enough that international trading has been around for a while.

1.1.2 Small and Medium Enterprise in Kenya

International trade has over the years been a domain for the large corporates, however with globalization, more and more businesses both large and small are engaging in international business.

According to the World Bank, an SME is an enterprise with up to 300 employees and an annual sales turnover of up to United States Dollars (USD) 15 million. (IFC 2008). The definition of an SME varies from country to country and from financial institution to another. This is due to market conditions, supervision and regulatory environments or frameworks in which these SMEs operate in. The banks strategy also defines the definition of an SME. Maalu (1990) states that the definition of a small firm varies and that there is no consensus on what constitutes a small business enterprise. This situation is further compounded by the fact that there is no credible information on the nature and extent of small businesses. Lenders definitions vary but typically, they define SMEs as businesses with six to fifty employees or with annual revenues of less than Fifty million Kenyan Shillings. Regardless of this quantitative definition, it is agreed that virtually all stakeholders that SMEs in Kenya are the missing middle.

The SME is characterized by lack of adequate capital, inadequate or inappropriate management structures or basically being family owned and basically no clear policy on various keys areas of concern-even their definition is not unilaterally agreed. This makes it very difficult for any financial institution to finance this missing middle in Kenya and yet, this is one of the key sectors that the government is suing to create employment for its population. This sector is frequently referred to as the informal sector.

1.1.3 Kenya Commercial Bank Limited

KCB is a public listed Company with its shares trading at the NSE (Nairobi stock exchange). It is owned by the government 26.2% and 73.8% by the public. Government shareholding has since increased to 23.6%.

The history of Kenya Commercial Bank (KCB) dates back to 1896 when its predecessor, the National Bank of India opened an outlet in Mombasa. Eight years later in 1904, the bank extended its operations to Nairobi, which had become the headquarters of the expanding railway line to Uganda. The next major change in the bank's history came in 1958 when Grindlays Bank merged with the National Bank of India to form the National and Grindlays Bank. Upon Kenya's independence in 1963, the Government of Kenya acquired 60% shareholding in National & Grindlays Bank in an effort to bring banking closer to the majority of Kenyans. In 1970, the Government of Kenya acquired 100% ownership of the bank's shares and it was renamed Kenya Commercial Bank. The Government has over the years reduced its shareholding in KCB to 23%, as of December 2008 and a rights issue which was concluded in August 2010 further reduced shareholding by the Kenyan Government to 17.74%. KCB Website (2012)

In 1972, Savings & Loan (Kenya) Limited was acquired to specialize in mortgage finance; this has since been incorporated into the KCB Group as Mortgage Centre. This division of KCB specializes in the provision of mortgage facilities to individual and institutional investors both locally and to citizens in the diaspora. The Bank has a well-established domestic retail and corporate banking franchise. Outside Kenya, the Bank has

banking subsidiaries in Tanzania, Uganda, South Sudan and Rwanda. The Bank's shares are cross listed on the Kenya, Uganda, Tanzania and Rwanda Stock Exchanges and are widely held by Kenyan and other international investors.

KCB is the region's largest bank in terms of total assets at KES. 280 billion most capitalized at KES. 38.4 billion and total number of branches at 222 spread in five countries, namely; Kenya has 169 branches, Tanzania has 11 branches, Southern Sudan has 19 branches, Uganda 14 and Rwanda has 9 branches. This is complemented by over 920 ATMs that offers a twenty-four hour services across the region.

According to information on the KCB Website, KCB has a wide range of products tailor made for its vast clientele base. These products are structured or designed to ensure the customers receive value for their money. KCB SME products designed for promoting international trade range from letters of credit both for imports and exports, documentary collections both for import and exports, various types of bank guarantees, bills discounting, open account trading and Advance payments KCB website (2012).

KCB has classified these international trade finance products dependent on their risk. A risk ladder has therefore been designed to ensure the customers' needs are well taken care of. For the exporter, payment in advance would be recommended followed by the letter of credit, the documentary collection and most insecure would be open account trading. For the importer, he will be advised to do open account trading, and then followed by the import documentary collection, and then the import documentary credit and he will be in

a worse position if he did an advance payment to his customer, the importer. One of the main guidelines that KCB is therefore inclined to use to recommend a product dependent on whether her customer is importing or exporting. Pascioli (2010) In most economies, smaller enterprises are much greater than large companies. SMEs are often said to be responsible for driving innovation and competition in the Kenyan economy. In KCB, the SME is a business enterprise with an annual turnover of KES 50Million and below and with a workforce off between five and fifty. Therefore, it is important that KCB continues to provide innovative and real-time solutions to this sector of the economy. Although KCB has been providing these services to the SMEs, there are some problems. Nduba (2010)

1.2 Research Problem

All organizations have come to appreciate the need to empower SMEs do business. International trade is considered foreign to domestic traders in the country. These traders would rather deal with the dreaded unscrupulous middlemen than venture into the murky and deep waters of international trade. In recent times, there are emerging issues in international trade that have led to a lot of disgruntled traders in the business world.

KCB has undertaken various marketing strategies to their SMEs to encourage uptake of their trade finance products but with minimal success. Various studies on SMEs and on KCB have been undertaken but none has addressed the issue of provision of international trade finance products to the SME.

Nduba (2010) did a study on a survey of the factors that determine the credit worthiness of SMEs for bank loans. The study says that SMEs have historically faced difficulties in accessing funding for credit worthy projects due to lack of credible information about them which can be used to establish their credit worthiness. The research concluded that most financial institutions have the tools required to establish the credit worthiness of an SME, however they should have these tools used in a manner that will allow the SME to pass the credit standard set by the Bank.

Nyamai (1989) carried out a research on the structure and growth of the banking industry in Kenya. Waruci's (2001) evaluated competitive strategies employed by commercial banks that participate in the clearing house, Kiptugen (2003) identified strategic response by KCB to an increasing environment. Pacioli (2010) did a study on corporate social responsibility and sustainability at KCB, the study concluded that KCB's success has been influenced by its corporate social responsibility which creates goodwill amongst the communities within which KCB operates in. Njogu (2010) attempted to analyze how SMEs were impacted by the 2008 -2009 financial crunch; he gave recommendations but did not talk of the innovations of bank products to mitigate such risky situations.

Maunda (2011) did a study on the internationalization process of KCB. Though studies have been done on how financial institutions including banks can access the credit worthiness of SMEs no study has been on the uptake of international Trade finance products by SMEs and the challenges faced by SMEs. None of the studies done has sought to address the problem of inadequate take up of the international Trade finance

products by SMEs with specific reference to KCB SMEs. This study therefore sought to answer the question as to why SMEs in KCB are not quickly taking up the International Trade finance products offered to them by the bank.

1.3 Research Objective

The objective of this study was to find out how KCB uses the international Trade Finance Products to serve the SMEs in their customer base and how they can increase the utilisation of these products.

1.4 Value of the Study

The findings from the study may particularly be useful in providing additional knowledge to existing and future institutions on international trade finance products provided by Kenya Commercial Bank Limited to small and medium sized enterprises and provide information to potential and current scholars on critical success factors in Kenya. This may expand their knowledge on critical success factors in the insurance industry and also identify areas of further study. The study may be a source of reference material for future researchers on other related topics; To the academia, the information may be relevant as it may provide a basis for further study. To the current and potential scholars in the business field more especially those who have interest in critical success factors, the findings from this study may provide information to expand the one already that exists. The findings may also be of critical importance to those who have got interest of further studying the field because the researcher intends to give suggestions for further studies.

This study may enable KCB begin to understand why the SME in her client base is not fully utilising the products available for international trade and what they can do to remedy this. The findings from this study may therefore be of importance because they may have the capacity of being used to formulate positive banking policies which are relevant and sensitive to the forces influencing the insurance sector in Kenya.

The SMEs may be able to fully understand the various options available to them and how to use these products. Other financial institutions, with specific reference to Banks may be able to adopt the recommendations and put in place strategies that may ensure the SME is fully taking advantage of the international Trade finance products available for use. Most importantly the findings of this study may help in enlightening the key decision makers banking industry in Kenya toward policies formulation

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter reviews the literature that is relevant to the research by looking at what other authors have written that could add more insight into the topic under study. The study will seek to use literature on the concept of international business and international trade with specific reference to the SMEs. The study will seek to use literature available on KCB and seek solutions both proposed and documented for the KCB SME International business customers. This will be done by making reference to theories already in existence as well as borrowing from banks that have mastered the art of offering the best financial solutions to SMEs with regards to International Trade finance products.

2.2 International Business

International business consists of business transactions between parties from more than one country. The goal of private companies is to make profits whereas for governments may or may not be motivated by profits. Domestic business involves transactions occurring within the boundaries of a single country i.e. international business is cross national boundaries. International business differs from domestic business because of the differences in currencies, legal systems, cultures and resources availability. International boundary has grown in the recent years dramatically because of strategic imperatives and environmental changes.

Today's global events and competitors affect almost all companies irrespective of size and industry. Strategic imperatives include the need to leverage on core competencies, acquire resources, and seek new markets that match the actions of rivals. It's important to note political and technological environments have facilitated the explosive growth in international activity. The growth of the internet and other information technologies is definitely redefining global competition and ways of doing international trade. The SME cannot afford to be left behind. There are three main modes of international business. These are; import and export of both services and merchandise, investments either direct investments or portfolio and turnkey operations and finally collaborative arrangements with other companies by way of franchising. Todaro (2008)

According to Daniel et al (2007), some of the main reasons why companies engage in international business is to expand sales, acquire resources, minimize risks and cost, and to enhance their global presence.

2.3 International Trade

According to Husted (2007), all countries participate in international trade, meaning some goods and services produced within every country are sold to economic agents (industries, firms, governments etc.) in other countries, these products are known as exports. Some goods and services consumed within a country have been purchased from economic agents in other countries; these goods are known as imports.

Countries differ in how much they participate in international trade. A measure of this participation (crude measure) is given by the ratio of exports to Gross Domestic Product (GDP) (Gross National Product) multiplied by 100. This measure is known as the index of openness. Generally this number will vary between 0 – 100. Sometimes it will go higher though very rare to more than 100. Countries with high values of this index trade a lot with the rest of the world and are said to be relatively open, those with low values are said to be relatively closed because international trade is only a small part of their economic activity (Husted, 2007). The extent of economic activity in a country can be measured in many ways. The two most common measures are GNP and GDP of a country. GNP, this is the value of final goods and services by domestic faction of production. No matter where they are located, be it locally or abroad. And, GDP which is the value of final goods and services produced within a country no matter whether the factors of production are domestic or foreign (McDaniel, 2008).

2.4 International Trade theories

International Trade theories have been used to explain international trade. These theories are broadly categorized into two. These are the Free trade theories and Trade pattern theories.

2.4.1 The free trade theories

International trade theories are broadly categorized into two, the free trade theories and Trade pattern theories. In the earlier centuries, 16th& 17th centuries mercantilism was propagated. Mercantilism advocated for exports and simultaneously discouraged imports

(Hill 2008). This theory advocated for government's intervention to achieve a surplus in the balance of payments. This theory however was flawed in that it viewed trade as a zero sum game, a gain in one country resulted in a loss in another country.

Mercantilism was discredited and Adam Smith's theory of absolute advantage was encouraged. He stated that economies should specialize in the production of goods for which they have an absolute advantage. Adam Smith stated thus in a free economy, specialization and trade would occur between economies resulting in a positive sum game.

In the 19th century, David Ricardo built on Adam Smith's theory to come up with the theory of comparative advantage. He stated that it was better for a country to specialize in the production of those goods that it produces efficiently. This theory however was riding on assumptions that were unrealistic.

2.4.2 Trade pattern theories

In the 20th century, Ricardo's work was refined by two Swedish economists, Eli Heckscher and Bertil Ohlin, whose theory is known as the Heckscher-Ohlin theory. This theory argues that countries have different factor endowments which explain differences in factor costs. This theory advocated for trade patterns were determined by factor endowments. Heckscher-Ohlin theory was subjected to further tests by Wassily Leontief and the result was the Leontief paradox. This theory discredited the Heckscher-Ohlin theory and advocated for Ricardo's theory. Hill (2008)

The product life cycle theory was advocated by Raymond Vernon, he stated that a product goes through various phases in the product life cycle, each stage with its own characteristics. The product goes through the four stages of production which are introduction, growth, maturity and finally decline. The introduction stage is characterized by innovation in response to observed need, exporting by the innovative country, evolving product characteristics, growth stage is characterized by increase in exports, increase in competition, increase in capital intensity and some foreign production, maturity stage is characterized by decrease in exports from innovating country, more product standardization, more capital intensity, production startups in emerging economies, the final stage, which is decline is characterized by concentration of production in developing countries and the innovating country becoming a net importer.

The new trade theory states that trade allows a nation to specialize in the production of certain goods attaining economies of scale and lowering the costs of production of these goods and buying the goods that it does not produce from other nations that are similarly specialized. The first mover concept also applies. This theory is supported and governments encouraged to use subsidies to increase chances of its domestic firms becoming first movers in newly emerging industries or economies (Hill, 2008).

In 1990, Michael Porter theorized that four broad attributes of a nation shape the environment in which local firms compete. These attributes promote or impede creation of competitive advantage. The four attributes are; factor endowments-a nations position in factors of production such a skilled labor or infrastructure are necessary to compete in a given industry, thus the less the factor, the less competitive a firm will be, secondly,

demand conditions in a nation-the nature of home demand will either propel or still growth of a given industry. Where there is adequate demand, there will be no need to go out to the new markets. Third, relating and supporting industries-the presence or absence of supplier industries and related industries that are internationally competitive will drive the direction of trade, finally the firm's strategy, structure and rivalry-the conditions governing how companies are created, organized and managed and the nature of domestic rivalry determine international trade flows. Where the rivals are going out to new market, a firm may opt to go the same route to beat competition. Other attributes could be chance and government policy (Husted, 2007)

Michael Porter thus summarizes by saying all their factors matter and may be important as they impact the four components of the national diamond.

2.5 International Trade Finance Products.

Mechanisms for financing SMEs have evolved over the centuries in response to a problem that can be particularly acute in international trade. The lack of trust that exists when one must put faith in a stranger therefore the need to have financial devices to mitigate this risk evolves. Firms engaging in International Trade must resort to an intermediary to assure both parties of either or payment or performance. The intermediary would thus use international Trade Finance products. UCPDC Version 2007(2010)

International trade finance products are mainly classified into two depending on their main mode of security/collateral. In this classification the two main divisions are vanilla products and structured trade finance products. The payment mechanism is also used to classify the international trade finance products. This is dependent on their risk weightings.

2.5.1 Vanilla Products in Banking

Vanilla products are the products where adequate collateral must be availed. These products then are paid in the four modes indicated hereunder. There are four main payment mechanisms or modes of trading these are; open account trading, letters of credit, documentary collections and finally the advance payment. Kenya being a net importer, the risk weightings or ladder is as follows.

Open account trading, this is the payment mode that supports payment for goods and or services after shipment. The importer will receive his goods and or services and pay at a later date. This mode applies where the importer and exporter have a very good working relationship and thus have established a level of trust (Srinath, 2012)

The most common international trade finance product is the letter of credit. The letter of credit-A letter of credit is a written undertaking from the importers bank (issuing/opening bank) to pay at sight or at a future date an agreed sum to the exporter/seller/beneficiary on behalf of the buyer/importer/applicant provided the exporter presents certain documents to the issuing bank in compliance to the terms and conditions of the

LC. Letters of credit can either be import or export. The importer will issue an import LC that will be received by an exporter and to the exporter it will become an export LC. There are various types of letters of credit; these include sight LCs, Usance LCs, revolving, Standby LCs, confirmed/unconfirmed LCs, revocable/irrevocable LCs, back to back LCs, transferable LCs, Red/Green clause LCs among others (Srinath 2012).

Why use letters of credit? Mitigates the buyer/ country risks, Issuing bank guarantees payment, Confirming bank (if any) also guarantees the payment, May be used to source pre-shipment finance, Allows for multiple/continuous shipments among other benefits. However as a payment mode, most users state it is very hard to understand. UCPDC Version 2007 (2010)

Documentary collections are another payment mode. Here, documents of title sent to the buyer through the buyers Bank with specific delivery instructions. The instructions could be for the bank to release documents against receipt of funds or against acceptance of the bill of exchange. Why use a documentary collection? This payment mode allows the importer to get an assurance that he is paying for a consignment that has actually landed. However to get the documents of title, he needs to pay or commit to pay. This mode of less risky to the importer in that he is paying for an actual shipment however a confirmation as to what he is actually paying/committing to pay, can only be done after he pays and gets the documents to clear the goods or get access to the goods.

According to Srinath (2012), the fourth payment mode is the advance payment mode. This is where the importer remits cash in advance before shipment or a service is done. As per the risk ladder and considering Kenya is a net importer, it is safest to trade in open account trading, followed by the LCs, and then the documentary collection, the worst mode of payment for an importer would be the advance payment. As the importer will actually part with his money before receiving a good or a service. Such a mode is applicable where the level of trust between seller and buyer is minimal.

Bank Guarantees are other trade finance instruments available in the market. A Guarantee is an undertaking by the bank/financial institution that the liabilities of a debtor will be met in the event of default. In other words, if the debtor fails to settle a debt, the bank will cover it. There are various types of bank guarantees. These are; Tender/ Bid Bonds, Performance Bonds, Advance Payment Guarantees, Retention bonds, Shipping Guarantees, Customs Bonds, Security Bonds, credit guarantees among others. URGD 758 (2007)

Other simple international trade finance products include invoice discounting. This is the giving value for invoices/Bills issued by the exporter/ seller. Mostly used where the seller needs cash upfront whereas the invoices/Bills provide for usance-credit period. The integrity of the buyer must be impeccable. There is also the bills Availisation. This is the bank's undertaking on behalf of the importer, to honor payments of bills of exchange from the supplier.

2.5.2 Structured Trade Finance Products.

In the international trade finance space there are some products which are considered complex not only to the SMEs but also to other people in the finance industry. As the name suggests, these products are structured to meet a client specific need. In most cases, the plain vanilla products are used to come up with a structured deal tailor made to suit the clients need. These products are all very useful to the business people as they offer bridging finance gap. These products are grouped under the name structured International Trade Finance basket. Such products are usually tailor made to meet client specific needs. These include post import financing solutions. This is designed to take care of the customers import bills when they mature. The bank settles the bill and recovers from the customer as a loan, there is also pre-shipment financing, and this is specific for exporters. This product meets the need of the export by providing funding to enable the exporter meet his obligations to the importer. This could be to enable the exporter source raw material from others to enable him manufacture and export, there is also the stock financing option, where the SME, may require to buy stocks and hold to sell later. This could be in an instance where there is a bumper harvest of maize. Traders would want to buy the maize hold and sell when the price has appreciated. KCB, would thus come in and facilitate the buying of such stock, hold it under a collateral manager and release it to the trader after payment.

Srinath (2012) says, with the various international trade finance products/ solutions available, it is important to establish why most SMEs are not utilizing these products despite the various highlighted benefits.

2.6 International Trade regulations

Countries differ as regards to cultures, legal regulatory framework and interpretation of contract law. SMEs operating in the international arena need to know how to handle legal issues as regards to the contractual obligations for international businesses. An SME operating in Kenya only must follow the Kenyan laws and customs while an international business faces a more complex task. This SME must obey not only laws at home but also laws of all the other host countries where it conducts its business. It is on the strength of these that the International Chamber of commerce was set up. The ICC came up with rules that govern international trade. These rules are product specific and are regularly reviewed to meet the needs of international business in this dynamic economic environment. The ICC rules are classified as follows:

Uniform Customs and Practice for Documentary Collections, Uniform Rules for Demand Guarantees, Uniform Rules for Collections-URC, Uniform Rules for Reimbursements-URR, and the international Standby Practices ISPB98. The rules were formulated to create a level understanding of expectations of the parties in an international trade transaction. In the event of arbitration, the ICC comes in to mediate between the two disagreeing parties. It is worth noting that the rules of a domain country precede the ICC rules. ICC Hand book(2007).

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter explains the methodology used to conduct and report the research. According to Leedy (1993), he defined research methodology as the approach by which the meaning of data is extracted and it is a continuous process. The research methodology gives the direction to follow to get answers to the issues that are of concern. According to Kothari, research methodology is a way to systematically solve the research problem.

According to Wiersman (1986), the development of a strategy for conducting research is another step after identifying a research problem and the completion of background literature review. In the same breadth, this study discusses the following: the research design, the population sample, how data collection was done and instruments used in analyzing the data.

3.2 Research Design

For this study, the case study research design was the most ideal. A research design is the conceptual structure within which research would be conducted. The purpose of a research design is to provide for collection of relevant evidence with minimal expenditure of effort, time and money.

According to Cooper and Schindler (2003), research design provides answers to questions such as: what techniques were used to collect data, the tools to be used, time and cost constraints. It also helps to control and give meaning to the study variables. The case study provides an in-depth and comprehensive investigation of organizations strategy. Yin (1984), states that the case study research methodology is an empirical inquiry that investigates a contemporary phenomenon within its real life context.

Young (1960) describes the case study as a comprehensive study of a social unit be it that of a unit of a person, a group, a social institution, a district or a community. The importance of a case study is emphasized by Young (1960) and Kothari (1960) who were in agreement that a case study is a very powerful form of qualitative analysis that involves a careful and complete observation of a social unit irrespective of what types of unit is under study. It is a method of study that drill down rather than casts wide. KCB is thus the social unit under scrutiny as regards its SME international Trade Finance product provision.

3.3 Data collection

Data was collected from both primary and secondary sources. Primary data was by way of interviewing and observation by the interviewers, whereas secondary data was by way of referring or reading data from KCB on their products uptake. Comparison was also made to other banks data on their uptake of international trade finance products by the SMEs.

Simple questionnaires were used by the interviewer to get answers from selected respondents. The respondents were a variation of KCB SME customers selected randomly from the Nairobi portfolio. The sample size was a manageable ten customers. The KCB staff members working in the SME clients at the head office level were also interviewed. The staff number to be interviewed was five.

3.4 Data Analysis

The data was obtained from the various management team members belonging to different departments and compared against each other in order to get more revelation on the issues under study and KCB clients.

This research yielded qualitative data from the interview schedules and which was analyzed using content analysis because this study sought to solicit data that was qualitative in nature. Then the study identified the key themes and concepts expressed by the respondents, with particular attention on the choice of words. The themes and concepts were categorized according to the objectives of the study so as to provide a preliminary overview of how the objectives were met and the research question answered. Analysis of data collected was compared with the theoretical approaches and documentations cited in the literature review.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter presents the data that was found on the international trade finance products provided by Kenya Commercial Bank Limited to small and medium sized enterprises. The research was conducted among interviewees who included ten KCB SME customers and five KCB staff members. All the respondents participated in the study making a response rate of 100%. Mugenda and Mugenda (2003) stated that a response rate of 50% and above is a good for statistical reporting.

4.2 Demographic Data

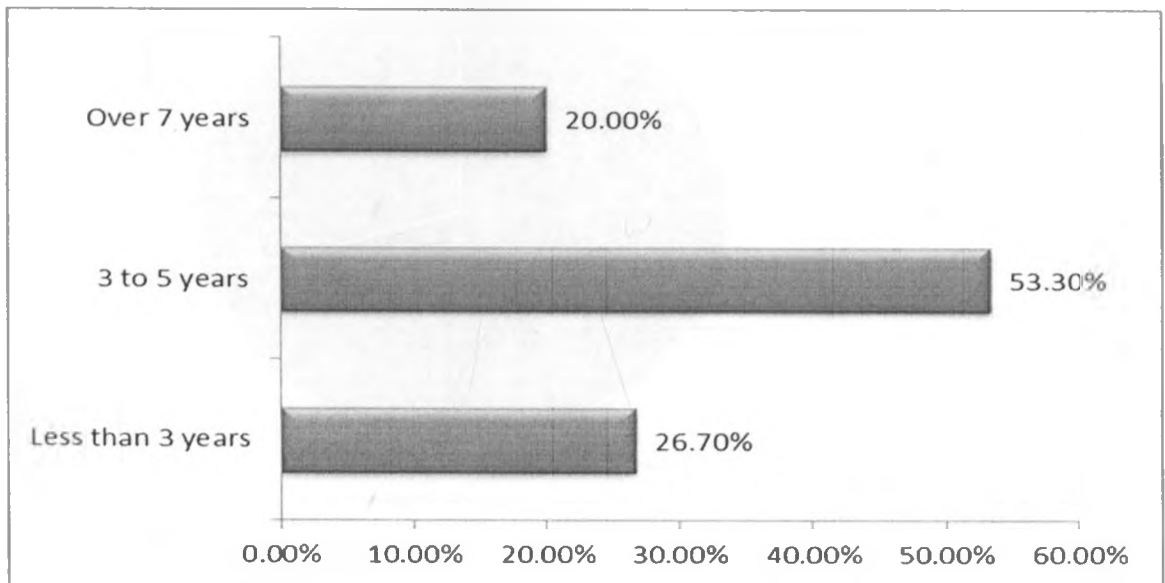
The study initially sought to inquire information on various aspects of respondents' background, i.e. the respondent's number of years while working at the present capacity, number of years while working in the banking industry and the respondents' role in International trade finance products provided by Kenya Commercial Bank limited to small and medium sized enterprises . This information aimed at testing the appropriateness of the respondent in answering the questions regarding the international trade finance products provided by Kenya Commercial Bank Limited to small and medium sized enterprises.

4.2.1 Demographic Information for KCB Staff

Respondents level of experience based on number of years in the current position

The research sought to establish respondents' level of experience based on the number of years they have worked in their current position.

Figure 4.1 Respondents level of experience based on number of years in the current position



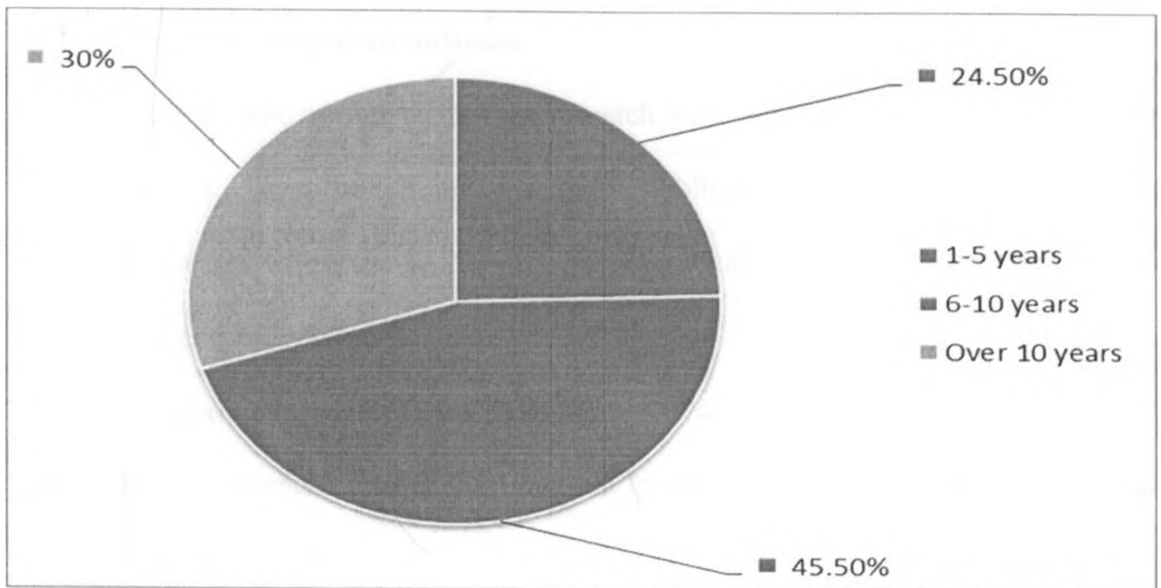
Source: Research 2012

Figure 4.1 shows that majority of the respondents (53.3%) had worked in their current position for 3-5 years, 26.7% for less than 3 years while 20% had worked for over 7 years. This illustrates that the respondents had worked in the organization long enough to give credible information on the international trade finance products provided by Kenya Commercial Bank Limited to small and medium sized enterprises. It also depicts that the respondents were highly experienced owing to the many years they had worked in the organization.

Respondents' experience based on the number of years while working in the banking Industry

The respondents were required to indicate the number of years they had worked in the banking industry.

Figure 4.2 Respondents' number of years working in the Banking industry



Source: Research 2012

From the findings, the most of the respondents (45.5%) posited that they had worked in the banking industry for 6-10 years, 30% for over 10 years while 24.5% had worked in the banking industry for over 1-5 years. This illustrates that the respondents had accrued a lot of skills owing to their many years of working in the banking industry.

Respondents' role in International trade finance products provision

The respondents were also required by the study to indicate their role in International trade finance products provided by Kenya Commercial Bank limited to small and medium sized enterprises. From the findings, the respondents' attested that their role was

to ensure customers are offered solutions that enable them participate in international Trade. They further explained that the solutions they offered to the customers were comprehensive and easy to understand by the customers.

4.2.2 Demographic Information for KCB SME clients

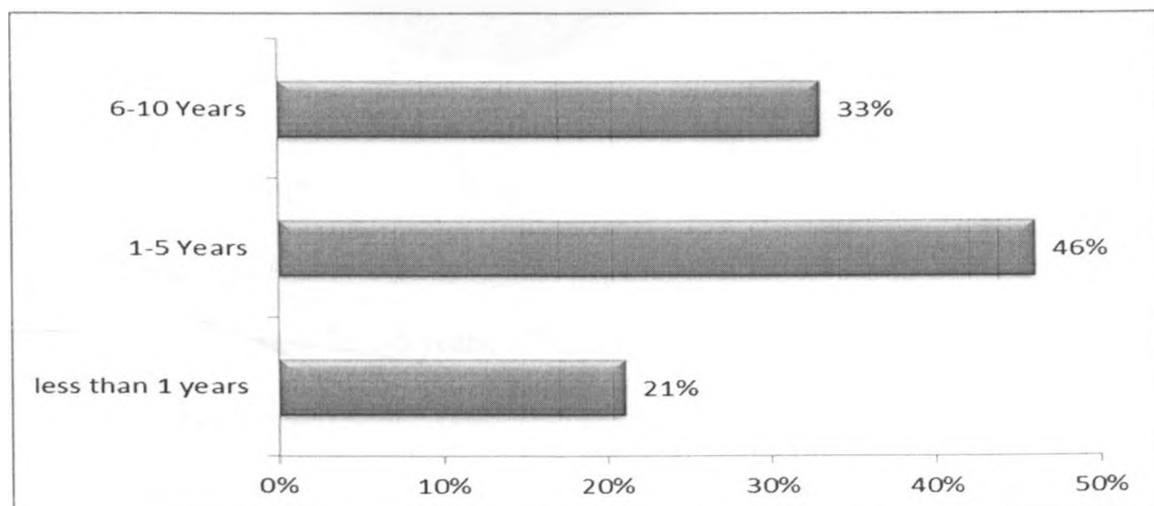
KCB SME clients' nature of business

The SME clients who participated in the research were required to indicate the nature of their businesses. From the findings, the study established that the SME clients operated diverse businesses which included Agro- business, clothing businesses, hotels, garages, food and beverages industry, health facilities.

Number of years as a customer at KCB

The KCB SME clients' were further required to indicate the number of years they had been customers at KCB.

Figure 4.3 Number of years as a customer at KCB



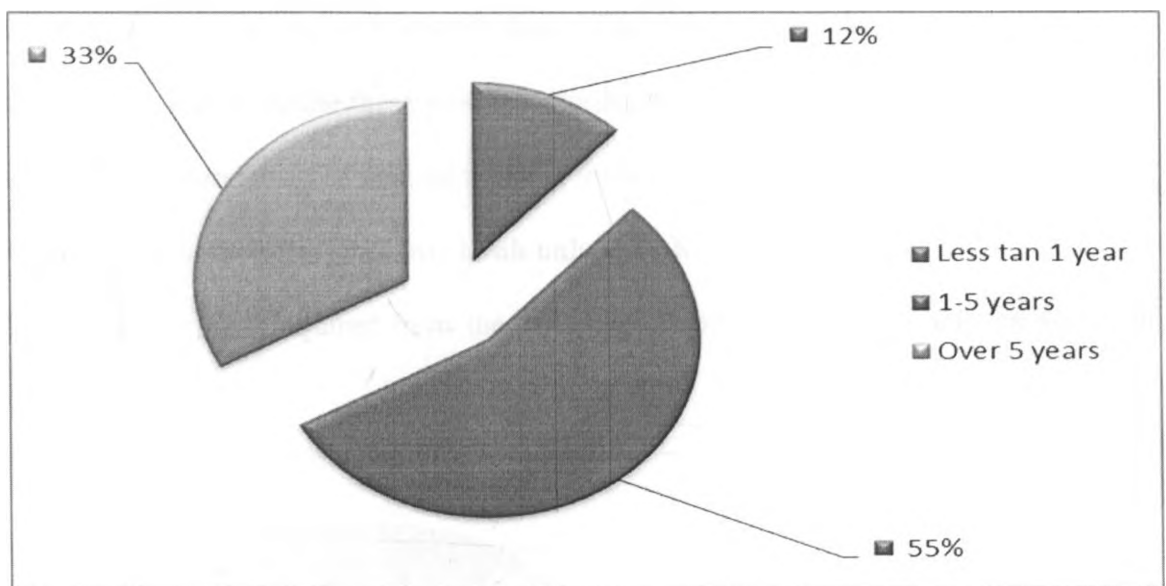
Source: Research 2012

From the findings, most of the KCB SME clients (46%) had been customers of the bank for 1-5 years, 33% for 6-10 years while 21% had been customers of the bank for less than 1 year.

SME customers' use of finance products

The study also sought to establish the SME customers had been using finance products provided by Kenya Commercial Bank limited.

Figure 4.4 SME customers' use of finance products



Source: Research 2012

Figure 4.8 indicates that majority of the respondents (55%) attested that they had been using finance products for 1-5 years, 33% for over 5 years while 12% had been using the finance products for less than 1 year.

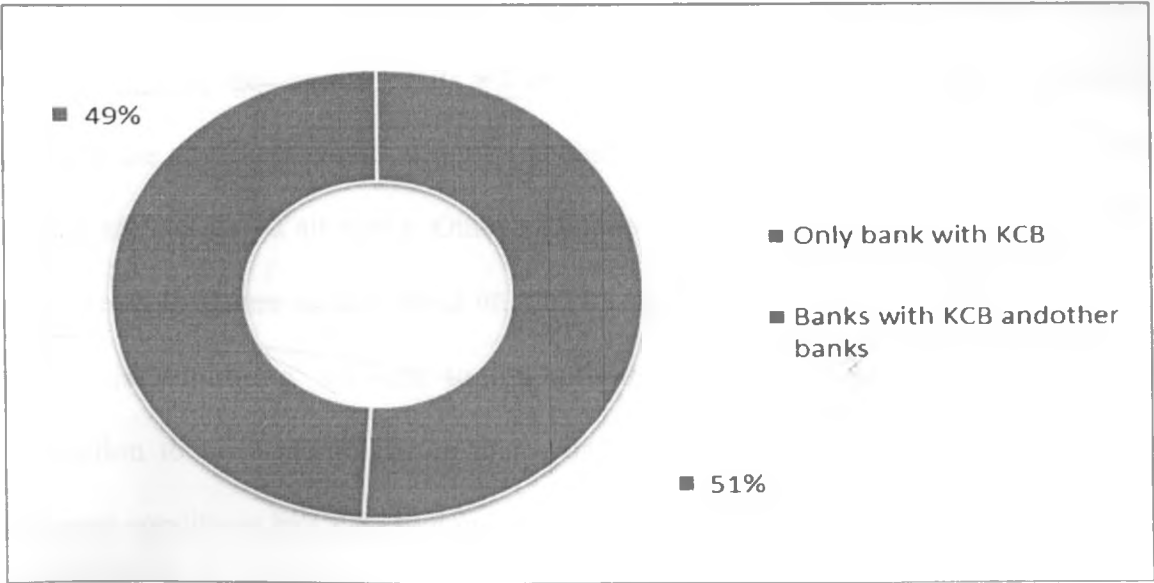
SME customers' Rating of KCB business performance

Based on their experience, the SME customers from KCB were required by the study to

rate their business performance regarding finance products provided by Kenya Commercial Bank limited to small and medium sized enterprises. According to the findings, the majority of the SME customers rated their business performance as good owing to the trade finance products provided by Kenya Commercial Bank limited to them. They further posited that KCB was very supportive to them. However they also indicated that they did not understand the products very well and this made them hesitant from taking these products. In addition the SME customers posited that the International trade finance products offered to them by KCB were complicated and not easy to understand how they would benefit them. The barrier was also based on the hard terminology used to define these products. Further they indicated that KCB required them to submit collateral most of the international trade finance transaction.

Figure 4.5 Whether Respondents bank only with KCB

The researcher also inquired from the SME clients on whether they only banked with KCB.



Source: Research 2012

Figure 4.8 indicates that majority of the respondents indicated that the majority of SME clients (51%) attested that KCB was their sole bank. They further explained that KCB was very supportive to all their trade finance and offered their products at competitive rates as compared to others banks. On the other hand, 49% of the respondents indicated that apart from KCB they had other accounts with other banks owing to the fact that the other banks like Equity did not ask for collateral on most of their trade finance product to the SME clients. However they complained that the company products were offered at exorbitant rates.

4.3 International trade finance products provided by KCB to SMEs

4.3.1 International business transactions at Kenya Commercial Bank limited

The study sought to establish the various international business transactions at Kenya Commercial Bank limited. From the findings, the majority of the respondents attested that the international business transactions at KCB included issuance of letters of credit which is done by getting collaterals and other relevant critical documentation. The letters of credit are governed by the international chamber of commerce, thus the terminologies used is similar across all banks. Other international business transactions included bank guarantees which are issued based on various bank specific conditions. The bank also offers discounting of invoices to the customers as another international business transaction to the SME clients. The respondents further indicated that KCB has put stringent conditions like the requirement of collaterals which is a major challenge to the SMEs. The documentary collections are guided by international guidelines and since for

one to use this product the level of trust between buyer and seller was the guiding factor and not the banks. The international guidelines include provision of collateral by the customers which is major barriers to the SMEs customers. In the discounting of invoices the collateral requirement also affects the access of this product to the SME customer.

However in the discounting of invoices, there are no international guidelines that govern the discounting of invoices. Thus, the banks put their own guidelines. KCB requires collateral from the SME clients and does not discount 100% of the invoices unlike the competing banks who discount more than 80% but charge a very high interest rate. The SME clients suggested that KCB should consider discounting a higher factor and charging a higher rate. The findings are collaborated by Srinath (2012) who recommends that banks offer various international trade finance products to SMEs like the letter of credit among other products to SMEs but at an affordable rate and with minimum conditions all but protecting the banks shareholders wealth.

4.3.2 Considerations by KCB while dealing with international trade finance products

The respondents were also required to indicate the considerations that KCB gives while dealing with international trade finance products provided to small and medium sized enterprises. From the findings, the majority of the respondents attested that while dealing with international trade finance products to SMEs, KCB considers collateral, nature of business, number of years that the SME had been a customer at KCB, customers experience in the area of specialization, whether the customer is in the unsanctioned list and whether the customer is dealing with a sanctioned country.

International trade regulation that KCB complies to

The study sought to find out the international trade regulation that KCB complied to while offering International trade finance products to SMEs. From the findings, the majority of the respondents indicated that KCB subscribes to the International Chamber of commerce (ICC) publications on the various trade finance products. This is in line with the ICC Hand book (2007) which stipulate that SMEs and banks must obey not only laws at home but also laws of all the other host countries where they conducts business which are based on the International Chamber of commerce rules. These rules are product specific and are regularly reviewed to meet the needs of international business in this dynamic economic environment (ICC Hand book, 2007).

4.4 Challenges faced by KCB while using trade finance products to SMEs

The research sought to establish the challenges faced by KCB while issuing trade finance products to SMEs. From the findings, the majority of the respondents attested that the challenges KCB faces included knowledge gap since most SMEs clients never understand how international trade finance products work. The collateral requirement is another challenge as customers are not ready to provide collaterals for their trade finance instruments. In addition, the middlemen are also a major challenge since most of the SMEs clients engage the services of middlemen who still get the financing product from the bank but charge the SMEs high charges that reduces the margins of the SME significantly. The sanctions are another challenge whereby customers who do business

with countries that are on the UN Sanctioned list cannot access international trade products from the bank. The findings are collaborated by Husted (2007) who attested that in the international trade finance space there are some products which are considered complex not only to the SMEs but also to other people in the banking industry. That despite their many benefits to the SMEs, their uptake by SMEs is limited owing to lack of understanding of these products and some of the SMEs result to seeking middlemen to assist them in gaining access to use these products (Husted, 2007).

4.5 Ways to curb challenges faced by KCB while trading international finance products to SMEs

The research further required the respondents to suggest ways to curb challenges faced by KCB while selling trade finance products to SMEs. According to the findings, the respondents recommended that KCB should conduct an awareness campaign to sensitize their SMEs customers about the various international finance products offered by the bank. The campaign should also enable the SMEs clients understand the various requirements for them to qualify for the various products. This will reduce the knowledge gap substantially hence enable customers to use the international trade finance products easily. This will also reduce the option of using middlemen that some SMEs are using now and increase their profit margins. The bank should also implement fully the tiered collateral requirements it has introduced with a view to help SME customers meet the collateral requirement by the bank. Thus the bank will structure transactions depending on clients' needs and ability to pay.

The study findings indicates that with the various international trade finance products/ solutions available, it is important to establish why most SMEs are not utilizing these products despite the various highlighted benefits. Solution to these challenge include educating them so as to understand how to access these services, and reviewing of the barriers that hinder their uptake like the collateral requirement

4.6 Meeting clients' needs while selling trade finance products to SMEs

The study sought to establish if KCB was adequately meeting clients' needs while selling international trade finance products to small and medium sized enterprises. From the findings, the majority of respondents attested that the bank was not adequately meeting clients' needs while selling international trade finance products to SMEs. However they explained that the bank required improving its service delivery in provision of trade finance products by educating the customers who did not fully understand the international trade finance products. They also indicated that the bank should find ways to cushion the SMEs clients in meeting the collateral requirement which was a major challenge to them. The respondents further indicated that there was a lot of bureaucracy in accessing the trade finance products and requirements that the SMEs found prohibitive like the criteria for assessing the credit worthiness of the SMEs, the collateral requirement among others.

The Respondents further argued that KCB should relax some of the unnecessary requirement like their competitors to allow uptake of the finance products by the SMEs. According to Srinath (2012) the financial institutions should come up with a structured

deal tailor made to suit the clients need. These include post import financing solutions. This is designed to take care of the customers import bills when they mature. The bank settles the bill and recovers from the customer as a loan, there is also pre-shipment financing, and this is specific for exporters Srinath (2012).

4.7 Recommending KCB International Trade Finance Product offering to other SMES

The respondents were also asked whether they would recommend KCB International Trade Finance Product offering to other SMES. According to the findings, the majority of the respondents (100%) indicated that they would recommend KCB International Trade Finance Product offering to other SMES. They further explained that the KCB was in the process of repackaging its product which would be favorable to SMEs. Considering KCB's history dating back to 1896, regional presence and good correspondent banking relationship, SMES using KCB international trade finance products voiced their opinion that should KCB improve the areas indicated above, then more than 80% of the economies SMES doing a lot of international banking will move to KCB as they will benefit more by being in KCB than in other banks.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter presents summary, conclusion and recommendations of the study in line with the purpose of the study aimed at examining the international trade finance products provided by Kenya Commercial Bank Limited to small and medium sized enterprises.

5.2 Summary

The study established that the various international business transactions at Kenya Commercial Bank limited included issuance of letters of credit which is done by getting collaterals and other relevant critical documentation. The letters of credit are governed by the international chamber of commerce, thus the terminologies used is similar across all banks. Other international business transactions included bank guarantees which are issued based on various bank specific conditions. The bank also offers discounting of invoices to the customers as another international business transaction to the SME clients. The respondents further indicated that KCB has put stringent conditions like the requirement of collaterals which may need to be relaxed to be able to remain competitive in the banking industry. The documentary collections are guided by international guidelines. The trade finance international guidelines include provision of collateral by the customers which is a major barrier to the customers. In the discounting of invoices the collateral requirement also affects the access of this product to the SME customer. However in the discounting of invoices, there are no international guidelines that govern

the discounting of invoices. Thus, the banks put their own guidelines. KCB requires collateral from the SME clients and does not discount 100% of the invoices unlike the competing banks who discount more than 80% but charge a very high interest rate. The SME clients suggested that KCB should consider discounting a higher factor and charging a higher rate.

The study established that the considerations that KCB gives while dealing with international trade finance products provided to small and medium sized enterprises were collateral requirement, nature of business, number of years that the SME had been a customer at KCB, customers experience in the area of specialization, whether the customer was doing business with a sanctioned country.

The study established that the international trade regulation that KCB complied to while dealing with international trade finance products to SMEs was the International Chamber of commerce (ICC) publications on the various trade finance products.

The study further revealed that the challenges faced by KCB while issuing international trade finance products to SMEs included knowledge gap whereby most SMEs clients never understand how international trade finance products work. The collateral requirement was another challenge as customers are not ready to provide collaterals for their trade finance instruments. In addition, the middlemen are also a major challenge since most of the SMEs clients engage the services of middlemen who still get the finance product from the but charge the SMEs high charges that reduces the margins of

the SME significantly. The sanctions are another challenge whereby customers who do business with countries that are on the UN Sanctioned list cannot access international trade products from the bank

On ways to curb challenges faced by KCB while trading international finance products to SMEs, the study established them to include conducting awareness campaigns to sensitize SMEs customers about the various international finance products offered by the bank. The campaign should also enable the SMEs clients understand the various requirements for them to qualify for the various products. This will reduce the knowledge gap substantially hence enable customers to use the international trade finance products easily. This will also reduce the option of using middlemen that some SMEs are using now and increase their profit margins. The bank should also KCB has also implement fully the tiered collateral requirements it has introduced with a view to help SMEs customers meet the collateral requirement by the bank. Thus the bank will structure transactions depending on clients' needs and ability to pay.

The study further revealed that the KCB was adequately meeting clients' needs while selling international trade finance products to SMEs. However the research also established that the bank should improve its service delivery in provision of trade finance products by educating the customers who did not fully understand the international trade finance products. They also indicated that the bank should find ways to cushion the SMEs clients in meeting the collateral requirement which was a major challenge to them. The study also established that the majority of the respondents would recommend KCB

International Trade Finance Product offering to other SMES. KCB was in the process of repackaging its product which would be favorable to SMEs.

5.3 Conclusions

The study concluded that the various international business transactions at Kenya Commercial Bank limited included issuance of letters of credit which is done by getting collaterals and other relevant critical documentation. The letters of credit are governed by the international chamber of commerce, thus the terminologies used are similar across all banks. Other international business transactions included bank guarantees which are issued based on various bank specific conditions. The bank also offers discounting of invoices to the customers as another international business transaction to the SME clients.

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The study concluded that the considerations that KCB gives while dealing with international trade finance products provided to small and medium sized enterprises were collateral requirement, nature of business, number of years that the SME had been a customer at KCB, customers experience in the area of specialization, whether the customer was doing business with a sanctioned country.

The study concluded that the international trade regulation that KCB complied to while dealing with international trade finance products to SMEs was the International Chamber of commerce (ICC) publications on the various trade finance products. The study further concluded that the challenges facing KCB while issuing international trade finance products to SMEs included knowledge gap whereby most SMEs clients never understand how international trade finance products work. The collateral requirement was another challenge as customers are not ready to provide collaterals for their trade finance instruments. In addition, the middlemen are also a major challenge since most of the SMEs clients engage the services of middlemen who still get the finance product from the bank but charge the SMEs high charges that reduces the margins of the SME significantly. The sanctions are another challenge whereby customers who do business with countries that are on the UN Sanctioned list cannot access international trade products from the bank.

On ways to curb challenges faced by KCB while trading international finance products to SMEs, the study concluded that they include conducting awareness campaigns to sensitize SMEs customers about the various international finance products offered by the bank. The campaign should also enable the SMEs clients understand the various requirements for them to qualify for the various products. This will reduce the knowledge

gap substantially hence enable customers to use the international trade finance products easily. This will also reduce the option of using middlemen that some SMEs are using now and increase their profit margins. KCB should also implement fully the tiered collateral requirements it has introduced with a view to help SMEs customers meet the collateral requirement by the bank. Thus the bank will structure transactions depending on clients' needs and ability to pay.

The study further concluded that the KCB was adequately meeting clients' needs while selling international trade finance products to SMEs. However the research also established that the bank should improve its service delivery in provision of trade finance products by educating the customers who did not fully understand the international trade finance products. They also indicated that the bank should find ways to cushion the SMEs clients in meeting the collateral requirement which was a major challenge to them. The study also established that the majority of the respondents would recommend KCB International Trade Finance Product offering to other SMES. KCB was in the process of repackaging its product which would be favorable to SMEs.

5.4 Recommendations

The study recommends that bank management should review the policies guiding the provision of international trade finance products to the SMEs with a view to making them friendlier to the SMEs to comply with.

The study also recommends that the management should conduct regular awareness campaigns to sensitize SMEs customers on various international finance products offered by the bank. The campaign will enable the SMEs clients to understand the various requirements needed for them to qualify and eliminate SMEs use of middlemen to access the products.

The study also recommends that the management should review the collateral requirement by the SMEs since it's a major barrier towards their uptake of international finance products.

5.5 Suggestions for further studies

Since this study explored the international trade finance products provided by Kenya Commercial Bank Limited to small and medium sized enterprises, the study recommends that; Similar study should be done in another commercial bank for comparison purposes and to allow for generalization of findings on the provision of international trade finance products to SMEs in Kenya.

5.6 Implication of the study on policy, theory and practice

The study contributed to the policies development in that the emerging issues like ICT, changing international trade finance products environment due to the restructuring of the international banking industry, that affect implementation need to be incorporated in the formulation of policies in international trade finance products.

The study also identified the international trade finance products adopted by the KCB, citing the strategy adopted in offering international trade finance products to SME that have made KCB gain a competitive edge in the international banking. The strategy could be adopted by other players in the industry in their practice on offering international trade finance products to SME.

The study also contributed towards development of the theories on the concept of international trade finance products. It argued that the changing environment and technological advancement in the international banking necessitates review of the existing theories in the international trade finance products to SME.

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APPENDIX II

Interview Guide:

This interview guide is designed to collect views on the usefulness of international Trade Finance products on SMES as provided by your bank –KCB. The information given will be strictly for academic purposes and will be treated with utmost confidence. Your honest views on and opinions will assist the researchers to come with useful information on how to improve the International Trade Finance product offering for SMEs not only for KCB but in the Kenyan banking industry.

Respondent no:

Date:

Demographic data for KCB staff members

1. What is your designation?
2. How long have you been working in your present capacity?
3. How long have you worked for the industry?
4. What is your role in International trade finance products provided by Kenya Commercial Bank limited to small and medium sized enterprises?

Demographic data for SME clients of KCB

1. What nature of business are you carrying out?
2. For how long have you been a customer at KCB?
3. How long have you been trading with finance products provided by Kenya Commercial Bank limited to small and medium sized enterprises?
4. Based on your experience, how will you rate your business performance regarding finance products provided by Kenya Commercial Bank limited to small and

medium sized enterprises?

5. Is KCB your sole Banker? If yes why? If No, which other banks and why?

International trade finance products provided by Kenya Commercial Bank limited to small and medium sized enterprises

1. What are the international business transactions at Kenya Commercial Bank limited how are they carried out?
2. What are the International trade finance products provided by Kenya Commercial Bank limited to small and medium sized enterprises and how are they carried out?
3. What consideration does KCB give while dealing with international trade finance products provided to small and medium sized enterprises?
4. Are there international trade regulation that KCB follow while dealing with International trade finance products to small and medium sized enterprises
5. What challenges faced by KCB while trading finance products to small and medium sized enterprises?
6. Recommend on ways to curb this challenges in faced by KCB while trading finance products to small and medium sized enterprises
7. Is KCB adequately meeting clients' needs while trading finance products to small and medium sized enterprises? If yes how? If No, why?
8. Would you recommend KCB International Trade Finance Product offering to other SMES?

Thank you very much for your patience and time.