AN INVESTIGATION INTO UNIT TRUSTS INVESTMENT BY SAVINGS AND CREDIT COOPERATIVE SOCIETIES (SACCOS) IN NAIROBI

BY

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DECLARATION

This Management Research Project is my original work and has not been submitted for a degree in any other University.

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This Management Research Project has been submitted for examination with my approval as the University Supervisor.

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DEDICATION

To my parents, and grandparents for believing in the infinite value of knowledge.

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List of Abbreviations

NSE	Nairobi Stock Exchange
CMA	Capital Markets Authority
SACCO	Savings and Credit Cooperative Society
SACCOs	Savings and Credit Cooperative Societies
WOCU	World Organization of Credit Unions
G.O.K	Government of Kenya
MoCD	Ministry of Cooperative Development
GDP	Gross Domestic Product
MCs	Management Committees
US	United States of America
Ksh	Kenya shilling
US$	United States dollar

ABSTRACT

The study establishes the attractiveness of unit trusts to SACCOs based in Nairobi. The hypothesis of the study was that unit trusts would be attractive to SACCOs. The expectation then was that SACCOs would include unit trusts in their investments in the current year.

The study found slightly above average (51%) level of awareness among SACCO managers, and that only 20% had learnt of unit trusts from the promoters. In addition, of the 25 SACCOs aware of unit trusts, only 12 had discussed the probability of investing in unit trusts. Among the 12, ten had rated unit trusts as attractive, while only 2 had planned to include unit trusts in their portfolio in the current financial year. Based on the 80% positive rating by the 10 SACCOs whose MCs had appraised unit trusts as potential investments, the study concluded that unit trusts are attractive investment to SACCOs based in Nairobi. The study recommends that the Capital Markets Authority, Nairobi Stock Exchange and Unit Trusts Investment firms accelerate investor education to generate effective demand for unit trusts.

CHAPTER ONE
INTRODUCTION

1.1 Background

The role of the financial system is to aggregate capital from surplus sources (savers) and allocates the resources to investors (borrowers) through formal and informal channels. Among the formal channels are the commercial banks and the capital markets. Kenya's formal channel is dominated by commercial banks. The current capital market offerings are equities, government and corporate debt, the latter as commercial paper and bonds. The key players in the capital market are institutional investors and high-net worth individuals, with minimal participation of retail investors.

In a bid to deepen the capital markets access to retail investors, the Capital Markets Authority (CMA) issued guidelines for the development of Collective Investment Schemes (CIS) in 2001. CIS are an intermediation that pools the savings of individual investors to enable them to benefit from professional fund management, economies of scale, and to achieve a greater level of diversification than would not otherwise be possible. CIS include Unit trusts, Mutual funds (open or closed), Special Interest Collective Investment Schemes and Umbrella Schemes (NSE, 2002).

Unit trusts are a means of participation in the equity, bond and the money markets for investors (or unit holders) who in their individual capacity may not have the time, the money, or the expertise to successfully effect investments in these markets. Prior to the launch of unit trusts, CMA undertook a study in 1994 to identify the viability of the instrument. The study interviewed potential promoters (institutions likely to develop unit trusts) such as fund management companies and financial institutions and investors such as high net worth individuals and SACCOs. The study identified SACCOs as key potential investors considering their established position of pooling funds from small savers. This study intends to explore the extent of SACCOs investment in unit trusts products since their launch in line with their identification by CMA as key investors.

1.2 Statement of the problem

The link between financial deepening (broadening) and economic development is widely accepted by scholars. Moreso, long-term investment is related to the capacity of capital markets to provide attractive returns to savers (investors) and low-cost funds to borrowers. In this respect, capital markets develop products that would compete with real assets and commercial banks in aggregating capital and funding investments. Kenya's capital market has over the last five years launched a range of debt instruments such as commercial paper, corporate bonds and secondary market for government debt. Collective investment schemes are the first instruments targeting to pool retail savings in that would broaden access to capital market for more Kenyans.

The launch of unit trusts fulfils two major objectives of the government of Kenya postulated in the 2002-2008 development plan. One, accelerating the mobilization of private savings to finance investment. Gross domestic savings as a proportion to GDP declined to 17.6% in the 1996-2000 period from 20.4% in 1990-95. Likewise, private savings declined to 10.6% from 17.8% in the same period. The government targets to raise the gross domestic savings to 25-30% of GDP by 2008. Secondly, the need to increase the number of securities in the capital market to increase investors' participation. Hence, offering products that are more attractive than commercial banks deposits and real assets would be the capital market's competitive advantage. The government recognizes the key role of SACCOs in fulfilling these objectives (National Development Plan, 2002-2008).

SACCOs have an incredible financial intermediation record through pooling savings and lending to members. In addition to lending to members, SACCOs seek investment opportunities to generate income and diversify their risks. There are two broad forms of SACCO sources of income that funds investments. These are personal savings or members contributions that constitute the share capital, and corporate savings generated by statutory reserve fund (25% of surplus) and retained earnings. The investment decisions are undertaken by the management committees under the direction of the Annual General Meeting.

Unit trusts are positioned as an advanced investment to small savers which offers a diversified asset portfolio for investors, who may participate as individuals or jointly. The joint investment entities include merry-go-rounds, investment clubs and SACCOs. In this respect, SACCOs would purchase unit trusts products and distribute returns to members as dividends or retained earnings. The Cooperative Act (1997) provided SACCO managers' greater leeway to invest in capital market products. The unit trusts products will not necessarily compete with these assets, but provide a means to diversifying risk as an optimal portfolio. The portfolio assets included are savings accounts, shares, bonds, land, buildings etc. The SACCOs will gain from portfolio management expertise held by fund managers, broader diversification that would not be achieved with limited funds, and lower transaction costs from the funds' economies of scale. Furthermore, SACCOs can also be sales channels of the units to their members at a commission from the promoters.

The launch of unit trusts also coincides with increasing pressure on the SACCO management to diversify their asset portfolio in the face of declining returns from real assets investment. The SACCOs management however lack the expertise to compete effectively in a liberalized environment. Such expertise includes effective treasury management necessary to analyze, select, construct, monitor and modify diversified portfolio that would effectively meet their investment objectives (CMA, 1994; Ongore, 2001, MoCD, 2001). The unit trusts investment firms have the expertise to fill this void, and have developed products tailored that would provide competitive returns, diversified risk, and liquidity needs of SACCOs. It is not however known if SACCOs have found the unit trusts an attractive alternative investment to constructing their individual portfolio. This study will investigate the extent to which SACCOs have found unit trusts as attractive investments through establishing the existing and planned allocation of corporate savings to unit trusts in comparison with other fixed and current assets.

1.3 Objective of the Study

The objective of the study is to investigate the extent to which Nairobi-based SACCOs have invested in unit trusts. The extent of investment will be assessed by analyzing the existing and planned allocation of corporate savings to unit trusts in comparison with other assets.

1.4 Justification of the study

The study is timely as the country prepares a new foundation for economic growth. The government's economic recovery strategy is targeted to creating employment, especially through the growth of small and medium enterprises (SMEs). Improving savings mobilization to finance long-term investment is a key component of the strategy. SACCOs have expressed desire to diversify their financial products from the traditional savings-lending model. Moreso, they seek to be allowed to serve non-members who are significantly unserved by the commercial banks owing to high account transaction costs. The Ministry of Cooperative Development (MoCD) is reviewing the Cooperative policy and legislation to spur growth of the sector. Among suggestions offered by the SACCO stakeholders is creation of separate legislation to enable them operate as a second tier financial provider. The broadening of the financial system however requires generation of synergies between the formal and non-formal segments. In this case, linking the capital markets to SACCOs provides the savers broader opportunities for growing returns from diversified units. The study's findings will therefore inform the policy makers and investors of the factors that would enhance intermediation for small savers to optimize overall allocative efficiency of Kenya's financial system.

1.5 Importance of the study

The study findings will provide useful lessons to the following:

i) Policy makers, notably Treasury and Ministry of Cooperative Development (MoCD) in developing appropriate policies for mainstreaming SACCOs into the financial system.

ii) Capital markets stakeholders, principally the Capital Markets Authority (CMA), the Nairobi Stock Exchange (NSE), and Unit Trusts Investment Companies in the development and marketing of unit trusts or other collective investment schemes.

iii) The SACCO management will be exposed to alternative long-term investment products to enhance institutional returns.

CHAPTER 2

LITERATURE REVIEW

2.1 Introduction

This section presents the features of unit trusts, the existing unit trusts, and the rationale for recommending SACCOs as key unit trusts investors by the CMA. The section will present the SACCO industry policy and their investment behaviour to indicate their likely response to unit trusts.

2.2 Unit trusts features

The Association of Unit Trusts (AUT-South Africa) describes unit trust as a vehicle that pools funds from savers and invests the funds in a portfolio of stocks, bonds, or other securities. Units in the trust are sold to investors, who become unit holders. Unit holders receive their proportionate share of dividends or interest paid by the UIT investments. The CMA regulates the structure and operations of unit trusts.

The principal features of unit trusts are:

a) Investment firm that pools funds from prospective investors by selling units.

b) Fund manager that is responsible for administering the fund, selling and buying the units and making the investment decisions. The investment firm may offer fund management services.

C) Trustee: the trustee is the custodian of the assets of the unit trust, whop ensures that the fund manager complies with the unit trust deed

d) The custodian's responsibility shall include the operations concerning the day-to-day administration of the assets and for ensuring that the sale, issue, redemption and cancellation of shares are done in accordance with the investment management guidelines of the fund.

2.2.1 *Valuation*

Unit trusts have an obligation to redeem units at notice by unit holders. CMA has provided a system for valuation of units' offer price and repurchase prices. The value of a unit is the net asset value of the portfolio (liabilities include such provisions and allowances for contingencies as the fund manager may think appropriate) by the number of shares issued and fully paid. The net asset value of the portfolio and the net asset value per unit shall be calculated by the fund manager as at the end of each business day. The number of units in issue shall be those units that are issued and fully paid. The selling price and repurchase price value of the fund shall be the value of an investment in securities listed and quoted on the securities exchange based on the last market price. With respect to unlisted securities, the trustee shall base the valuation on methods that are fair and reasonable and that are acceptable to the fund manager and approved.

2.2.2 *Income allocation*

The income earned from the investment, net of fees is allocated to unit holders. Some funds offer options for reinvestment. Firms are required to notify the unit holders the income allocation dates.

2.3 Structure of funds

There are generally two tiers of classification of funds.

2.3.1 *Market concentration*

The first tier is the market that the funds' securities are located. Hence, there are domestic, regional, international or global funds. For instance, South Africa has the following classes of funds:

Domestic Funds: Unit trusts that invest at least 85% of their assets in South African investment markets at all times.

Worldwide Funds: Unit trusts that invest in both South African and foreign markets. A minimum of 15% of the assets should be held in South African markets, and a minimum of 15% of the assets should be held offshore, at all times. The 15% minimum requirement applies to all the sub-categories with the exception of the Worldwide – Asset Allocation Funds category.

Foreign Funds: Unit trusts that invest at least 85% of their assets outside South Africa at all times.

Regional Funds: Unit trusts that invest at least 85% of their assets in a single country or region, excluding South Africa, at all times.

2.3.2 Portfolio securities

The second tier is the composition of the fund's securities. Three categories are equity funds, fixed interest funds and asset allocation funds. Equity funds consist wholly of equities, with sub-categories related to selected assets across the sectors or limited to firms in one sector, generally referred to as specialty funds. Specialty funds are investments in a group of companies sharing a specific characteristic, such as sector (energy, industrials, banking, high tech), capitalization (high, small capitalized firms), securities (options or commodities such as precious metals). Fixed income funds are mainly composed of bonds that offer periodic coupon payments and vary in exposure to risk. Asset allocation funds contain a diversity of investments such as stocks, bonds and money market securities, with the composition adjusted by portfolio managers in response to expectations. For example, a fund may concentrate on bonds if interest rates are expected to decline, or stocks if a strong market performance is expected. Annex 1 indicates the classification of South Africa unit trusts.

2.4 Investment strategies

Unit trusts funds are structured to meet the target investor's objectives based on the risk-return preferences. Common investment objectives that influence portfolio construction include:

- Time preferences: short, medium or long-term.
- Expected return: income, capital appreciation or both.
- Risk tolerance: low or high risk

- Diversification gains: specialty, market (single, regional, global).

2.5 Unit trusts market: US, South Africa

The unit trusts are well established in developed countries as part of the money market funds such as mutual funds and closed-investment funds. Unit trusts have products for investment, retirement and education. In the USA, an estimated 90 million Americans or 50 percent of all households-own mutual funds. Seven out of every 10 shareholders say they're saving primarily for their retirement, and 97 percent identify themselves as long-term investors. Data on the market value of unit investment trusts issued and outstanding as of year-end 2001 indicate a total of 7,880 trusts with a value of $49.39 billion. According to reports of sponsors, at year-end 2001 there were 6,296 tax-free bond trusts, with a market value of $19.00 billion; 174 taxable bond trusts, with a market value of $3.78 billion; and 1,410 equity trusts, with a market value of $26.60 billion (Investment Company Institute, 2002).

In Africa, South Africa has the most developed unit trusts industry. According to the Association of Unit Trusts (South Africa), there were 2.1 million unit holders in 2002. The total asset value was US$30.2 million, of which 76% were domestic funds. The industry had 460 local funds and 317 foreign funds.

2.6 History of unit trusts in Kenya

Unit trusts are a relatively new product in Kenya, covered under the Collective Investment Schemes (CIS). The regulatory framework was enacted in 2001 by the CMA, with Africa Alliance Kenya Ltd registered as the first Unit Trust Investment Company in 2001. Zimele Multi-purpose Cooperative Society has operated as a unit trust investment company through registration under the Cooperative Act, in association with Zimele Asset Management, a fund manager registered by the CMA. Zimele also had to appoint trustees and custodian to comply with CMA rules. The development of unit trusts followed consultations among the stakeholders based on a CMA study in 1994 that interviewed investors, fund managers, insurance firms and 31 SACCO managers. The study aimed at establishing the viability of authorized units, insurance units and cooperative units.

The potential market demand for unit trusts was estimated by analysing the savings patterns and the preferred assets among investors. Investors were asked to rate attractiveness of savings accounts, housing, land, quoted shares, cooperative shares, government shares/bonds on a scale of 'very good', 'fair' or 'no good'. Savings account, government shares/bonds were regarded as 'very good' by 77.6% and 42.6% respectively. Quoted shares were ranked as 'very good' by 19.6%, while land and housing scored less than 10%. The high rating of the savings account and government bonds/shares were attributed to their high yields and inflation cushion. Preferences for these investments were found to be more prevalent among urban respondents. This meant that investors were seeking initiatives which promise higher returns and security than has traditionally been the case. The respondents also ranked high yield and high growth as their preferred portfolio selection objectives.

To test likely investment selection preferences, the respondents were also asked to allocate an arbitrary windfall gain of Ksh 100,000 among the above assets. The allocations were skewed to land (24.7%) and housing (20.5%), indicating preference for traditional forms of investment, while unit trusts and quoted shares were got 13% each. The results were attributed to the 'traditional needs of individuals' preferences. The positive result was that 26% of the funds were allocated to capital market instruments, namely quoted shares and unit trusts. It is also worthy noting that the study was undertaken prior to the accelerated privatization of parastatals that have significantly increased the size of the capital markets. In all, the combined portfolio selection preferences for liquid assets (savings accounts, quoted shares, unit trusts) was higher at 54%, indicating market potential for these products.

2.7 Capital markets development

Kenya's capital market is synonymous with the growth of the Nairobi Stock Exchange (NSE). The Capital Markets Authority (CMA) was established in 1989 by an Act of Parliament, the CMA Act (Cap 485A, 1989). The Act has been amended several times in 1994 and 2000 to accommodate market developments. CMA's objective is 'deepening and broadening the capital markets in Kenya'.

Stocks remain the principal product traded at the NSE. The last decade witnessed significant growth in the number of issued equities aided by the government's divestiture program. CMA (2002) reports 24 new issues were made from 1991 to 2001. The NSE also launched new debt products such as commercial paper and bonds, the latter issued by both corporate sector and Treasury. In all, the equities turnover declined from a peak of 6.5 billion in 1997 to 2.88 billion in 2002. The decline was attributed to low demand for equities due to poor economic growth as GDP growth declined to 1% in 2002. Bonds trading on the other hand rose to Ksh34.24 billion in 2002 from 15.08 billion in 1997 when listing was launched. The increase in bonds volume was attributed mainly to the development of a secondary market for government debt at the NSE. Table 1 below indicates the capital markets products growth from 1997 to 2002.

Table 1: New issues at NSE, 1997-2002

	1997	1998	1999	2000	2001	2002
New equities						
number	3	2	1	3	3	0
value (bn)	1.94	2.1	0.37	0.45	2.4	0
Commercial papers						
number	1	2	19	4	2	0
value (bn)	0.5	0.45	10.65	0.6	0.8	0
Corporate bonds						
number			1	1	2	1
value (bn)			1.2	0.35	6	1

Source CMA, 2003

The NSE did not register new equities and commercial paper issues in 2002, while the commercial paper peak was 1999 when Ksh 10.65 billion worth were issued. As at November 30, 2002, nine commercial paper issues were outstanding following renewals by the issuers. Among the corporate bonds, East Africa Development Bank (EADB) and Shelter Afrique had made two tranches each, while the remaining two note were issued by Safaricom and Mabati Rolling Mills.

2.8 SACCO industry

2.8.1 Description

The Ministry of Cooperative Development (MoCD) describes SACCOs as cooperative savings and lending organizations established by a group of people who have a common bond for the purpose of promoting thrift and providing themselves with a source of credit at a fair rate of interest. Adeyeye (1987) describes SACCOs as voluntary association of salaried people who pay fixed subscriptions, at a fixed place, at regular intervals usually monthly, to a fixed sum given to members in rotation. The common bond is mainly employment in the same organization, or membership to a trade organization. The latter form, commonly referred to as informal SACCOs are a recent phenomena.

A distinctive characteristic of cooperatives is the principle of common bond - individuals who have something in common, whether based upon working together, belonging to the same organization or living together in the same geographical areas, know one another. They have established a common bond that can be built upon to address economic and social needs. The common bond is necessary to develop mutual confidence among the members to help one another and to trust decisions made on their behalf by their elected leaders.

SACCOs are registered under the Cooperative Act, the latest amendment made in 1997 that deregulated their control by government. Previously, the Commissioner of Cooperatives, through respective cooperative officers had to approve operating and capital budgets while only cooperative auditors were allowed to audit their accounts.

SACCOs play both financial and non-financial roles that is complementary to the formal financial system (banks, NBFIs) in provision of financial resources for economic development through promotion of investment funds, determining the investment portfolio of their resources through elected leaders, training members on simple monetary principles and fair distribution of surplus profits (MoCD, 1985). There is an on-going review of the cooperative policy aimed at enhancing SACCOs position as financial services providers.

2.8.2 History & size

The cooperative movement was initiated in Germany in 1896, and spread all over the world. In Kenya, African cooperatives were only authorized in the 1930s through crop ordinances in 1932 and 1945. A remarkable milestone was the establishment of the East African School of Cooperatives in 1952 in Nairobi, later renamed the Cooperative College of Kenya. Only after independence did the government take a proactive role in promoting SACCOs when the first one was registered in 1964. (Obuon,1988).

The principle objective of SACCOs is to provide credit to members, with savings providing the funding pool and also securitising the loans. A member qualifies for a loan after consistently saving for at least 6 months, The size of the loan is on average 3 times the savings (referred to as share capital), while the repayment rate should be less than two-thirds of the salary. The loan is secured through three guarantors, whose share who are jointly and severally liable to the society for the full amount of the loan should the loanee default. The repayment period must not exceed four years. (Ongore, 2001).

The government has supported SACCO growth as the principal collective investment vehicle. As at 1992, there were 5,307 cooperatives, of which 3,925 were SACCOs. The bulk of SACCOs are located in urban areas. Only 2,243 were reported to be active. Table 4 below indicates the status of the industry in 2001. Further desegregation of the non-Nairobi SACCOs indicates that 84% were found in urban areas. The membership in 2001 was 1.5 million, with Nairobi accounting for 46% of the membership (note that country-wide SACCOs are classified under Nairobi). The industry held assets worth Ksh53 billion, had a turnover of 6.68 billion, with loans issued amounting to Ksh 37 billion (excluded Rift Valley figures). The loans issued was equivalent to 14% of the commercial banks bills, loans and advances for the same year.

2.8.3 Financial performance

Oyoo (2002) assessed financial performance of Nairobi SACCOs with reference to deregulation using World Credit Unions (WOCU) financial ratios. The analysis covered pre-deregulation (1992-96) and post-deregulation (1997-2001), whose findings are presented in table 2 below.

Table 2: Financial performance of SACCOs before and after deregulation

Indicator	BD (1992-96)	AD (1997-2001)	WOCCU target
Total members deposits:total assets	80.67%	81.54%	70%-80%
members shares: total assets	5.89%	2.66%	<20%
institutional capital: total assets	9.71%	7.91%	>10%
growth in institutional capital	33.52%	66.04%	>inflation
growth in membership	3.21%	-1.17%	>5%
liquidity ratio	30.93:1	24.89:1	>15:1
net profit:business assets	3.03%	1.16%	optimal
basic earning power	2.14%	0.96%	optimal

source Oyoo,2002

Note i) BD-before deregulation, AD-after deregulation

ii) mean inflation rate- BD-22.54%, AD-6.76%

The data in table 5 indicates that only growth in institutional capital registered a remarkable growth, while total members assets to assets went up marginally. Infact, the latter were above the recommended WOCU target. Overall, performance after deregulation declined, with failure to meet two of the targets. Of concern is the low return on assets which is an indicator of poor resource-use efficiency. The liquidity ratio remained impressive. Oyoo (2002) attributed the decline to low return from real assets that form the bulk of their investments, retrenchment that reduced share capital growth, and poor treasury management to increase yield on liquid assets.

2.8.4 Management

A SACCO is managed by a committee elected at the Annual General Meeting. The management ccommittee is the governing authority and subject to the general meeting and of the society and the by-laws has powers to enter into contracts, be responsible for the custody of all moneys belonging to the society. The committee approves membership applications, loans and the institution's investments. Large SACCOs have full time staff headed, whose chief executive is the secretary to the management committee.

2.8.5 Recommended SACCOs investment policies

The bulk of SACCOs income is derived from interest on members' loans. Other sources of income include dividends on share held or bought from other organisations, deposits with banks, Treasury Bills, and fixed assets owned such as buildings, plots, sale of products like insurance policies etc. Prior to deregulation, the Commissioner of Cooperatives had issued investment guidelines that were enforced through Cooperative Officers. After deregulation, the management committee makes investment decisions based on the members' prevailing objectives. As per the rules, the management committees are expected to transfer 25% of their income to a statutory reserve fund, with the balance allocated to dividends and retained earnings. Dividend cash may be capitalized (re-invested) and members issued bonus shares. Where the bonuses are required for re-investment by the society for capital development, or for the redemption of bonus certificates, the society shall issue bonus certificates to its members in lieu of cash payments, redeemable from a revolving fund established by the society for that purpose.

The cooperative act (1997) sates that SACCOs may invest or deposit its funds only:

i) In the post bank;
ii) In and upon such investments and securities as are for the time being authorized for the investment of trust funds;
iii) In the shares of any other cooperative society;
iv) With any bank licensed under the Banking Act

v) In the stock of any statutory body established in Kenya or in any limited liability country incorporated in Kenya, or in any other manner approved by a resolution at an annual general meeting of the said society.

The next sub-section further elaborates the place of unit trusts in the SACCOs' investment strategy.

2.9 Target funds by unit trusts: corporate savings

The SACCO savings can be classified into personal and corporate savings. Personal savings (deposits) are contractual, voluntary and financial. The corporate savings (retained earnings, statutory reserves) are forced, contractual and financial. The statutory reserves fulfil liquidity requirements, liquidation and long term investments. The personal savings (deposits) are mainly targeted to fund the loan fund (share capital), which is the core business of SACCOs. Investments are funded from corporate savings, share capital or special funds created for such a purpose.

This study focuses only on corporate savings since the management committee makes the allocation decisions in line with the institution's by-laws. The general expectation is that SACCOs subscription to unit trusts will be influenced by the management committee. In assessing the target funds for unit trusts, we review literature by Obuon (1988) that anlysed the factors determining SACCOs corporate savings, and Gachara (1990), who assessed the SACCOs investment practices of reserve funds in Nairobi.

2.9.1 Determinants of corporate savings

Obuon (1988) considered SACCOs as firms, and sought to apply the theory of the firm in estimating the SACCOs savings behaviour. The study defended this approach in that their principal objective to advance the socio-economic interests of the members is a welfare maximiser, though the institutional profit maximization is perceived to subsist. As economic agents that engage in production and consumption activities, an income- earning asset function exists that has relevance to corporate savings. Estimation of the savings function is a proxy indicator of the demand function for investment funds by SACCOs. In other words, the opportunities to invest will increase the preference for re-investment of surplus income through SRF and retained earnings, thereby reducing the dividend pay-out ratios. The Cooperative Act (allows the management committee to issue bonus shares for capitalized earnings. The re-investment preference to dividends is consistent with choices influencing dividend policies among firms.

Estimating the savings function entailed evaluation of the impact of fluctuations in membership, loan defaults, loans advanced, assets, lagged dividend, management capacity, liquidity position, and share capital. Share capital had significant positive correlation with membership, which inturn pushes up demand for loans. Higher loans allocations and reduced defaults raised profits that would be allocated to savings. Lagged dividend was found to have low significance owing to high preference for dividends rather than reinvestments. Income was positively and significantly related to savings (profits taken as income variable). Overall, the main determinants of corporate savings were assets, profits and investment undertakings and loan amounts. The main determinants of deposits were loans, membership, average monthly contribution, and lagged deposits or shared capital. Main determinants of loans to members were share capital/deposits, investment undertakings, loans outstanding and loan defaults. All these variables are interlinked in one way or other.

These findings indicate that for the asset function, corporate savings and deposits were the most important factors. Hence, to increase SACCOs demand for assets or diversification of their investment portfolio, corporate savings must rise. The study did not ascertain the members' likely response to a trade-off between corporate savings and loans allocations. Such trade-offs would consider among others downsizing loan sizes to members, accelerating collection, increase income from assets, increasing demand for investment funds, review planned investments, expansion of assets, education of members to supply funds.

Profitable SACCOs had higher demand for deposits, and consequently higher corporate savings. The attractive yield on corporate savings would persuade members to accept lower dividend payout. The option for delayed dividends is s consistent with Furstenberg (1980) proposition that lagged dividend can be an incentive for motivating savings when viewed as transitory income.

These findings are significant in assessing the potential SACCOs uptake of unit trusts in two ways. One, it is apparent that the principal function of share capital (deposits) is to fund the loan pool, which is the most attractive incentive to members. Hence, on one hand, SACCOs will allocate share capital and other income to loans, especially those faced with deficit. In addition, SACCOs would tend to raise the proportional lending to members when experiencing high liquidity. Two, the asset function (attractiveness) will influence allocation of corporate savings, more so the SRF, which has an investment objective. In any case, the institutions have invested in real assets or fixed deposits. Thus, unit trusts will have to compete with existing liquid investment preferences, more so the term deposits, stocks and government paper. Moreover, the unit trusts promoters will have to educate the management and members to motivate their preferences for resource allocation. We consider the investment of corporate savings next.

2.9.2 Investment practices of reserve funds

Gachara (1990) analyzed investment practices of SACCOs in 1982-87, a period that the cooperatives followed investment guidelines issued by MoCD. The study analyzed their capital structure to establish the sources of long-term finance and application of these funds. The sources of long-term financing were share capital (83%), statutory reserve fund (3%), and retained earnings (1.9%). Examining growth in financing sources (liabilities), share capital grew at an average 29.3%, while SRF registered a mean rate of 31.44%, and retained earnings at 19%. SACCOs tended to borrow in times of fund shortages and repay immediately excess cash is available.

With regard to distribution of net income (surplus), SRF averaged 16.73%, dividends got (61.36%), while retained earnings were 22.8%. Annual surplus growth was a mean rate of 27.1% in the period. The legal requirement that 25% of the surplus per year be transferred to SRF not being strictly followed, with differential computation of surplus before/after tax. Most SACCOs used the after-tax rule. Surplus growth was dependent on income/returns to assets (loans, investments). The assets proportions were land (11%), commercial buildings (10.3%), residential buildings (5.6%), fixed bank deposits (42.1%), shares in other organizations (8.4%), while 13.1% were housed by employers and held no assets. The reasons for purchasing fixed assets were diversify income sources (75%), creation of employment (6.8%), social welfare provision (9.1%). None of the SACCOs hade purchased fixed assets merely for service provision to members.

Of significance to the subject of the study is financing strategy for fixed assets. These SACCOs financed fixed assets through specific contributions (22.7%), Loans (21.3%), SRF/Retained earnings (21.3%) and share capital (34.7%). Where specific contributions were used, the claims were only due to these members. Where share capital or corporate savings were utilized, the asset's claims diffused to entire membership through consolidation with interest income.

With regard to the investment of reserve funds, 67% of the funds were used to increase SACCOs working capital, fixed deposit accounts got 20%, and 13% financed operations. Hence, 80% are left in the society to improve liquidity, and not separated from the rest of the funds available from other sources. Attempt to find any particular asset financed by SRF proved futile.

This study further explored the preferred financing strategy for future investments. Among the respondents, 64.5% would increase share capital, 15.1% would raise debt, 4% will use SRF, while 8% would tap current assets. When asked to state how they would allocate extra funds, 47% would be allocated to loans, 39% to current assets, and 8% to pay-off existing liabilities.

Though the study was undertaken in the pre-deregulation period, the findings are relevant in understanding the composition of the SACCOs capital structure. The findings indicate that share capital, financed through regular contributions, is the principal source of long-term funds. More significant is the recognition of the need to diversify income sources as the principal motivation for term investments. Further, that the SACCOs employ a variety of options in sourcing investment funds, and that diversified allocations is a prime principal ion utilizing these funds.

2.10 Existing unit trusts funds

Though African Alliance is the first licensed Unit Trusts Investment firm, similar products were launched by Zimele in 1998. The Zimele funds include Money market, Off-shore portfolio and Balanced Portfolio. The Money Market Portfolio is invested in government of Kenya Treasury bills and bonds. The Offshore Portfolio is invested in international stocks covering over 80 companies in the USA, Europe and Asia: The Balanced Portfolio combines investments in stocks of companies listed at the Nairobi Stock Exchange; and Government of Kenya Treasury bills and bonds.

African Alliance has three products. The African Alliance Kenya Shilling Fund that invests in money markets such as call deposits, treasury bills, treasury bonds, commercial paper and corporate bonds. The other two, African Alliance Kenya Managed Fund and African Alliance Fixed Income fund are in the launch process.

2.11 Conceptual (theoretical framework)

2.11.1 Financial markets development

It's widely acknowledged that in Africa, the formal sector, principally commercial banks, relies extensively on the informal sector for deposits mobilization to finance the lending portfolio (Aryeetey, 1992). Given this significant complimentarity between formal and informal sectors in financing investment, it appears plausible for the capital market to have developed unit trusts to redirect these retail savings from commercial banks. The unit trusts are marketed as offering higher returns, risk diversification and liquidity benefits compared to real assets. There is significant potential for SACCOs to provide the window for expanding access.

The relationship between financial conditions, savings and economic growth is hinged on the Mackinon-Shaw financial intermediation hypothesis. The link between savings and growth as postulated by the Mackinnon-Shaw hypothesis is investment. However, behaviourally, savings and investment differ since transfer of savings to investment depends on a host of other factors other than the real interest rate (Bhatia and Khakhate, 1975; Fry, 1978). Such factors include availability of investment opportunities at rates exceeding the cost of funds, institutional constraints and cost of administration. In developing countries, policy makers take a pro-active role in designing appropriate strategies that take cognizance of existing financial system's capability to support new products. Given the reach and tradition of pooling funds, SACCOs provide a significant window for expanding access to capital market products by small savers.

In analyzing financial markets development, the terms deepening and broadening overlap somewhat (IFC, 1998). Generally speaking however, deepening refers to the increase of financial assets as a percentage of GDP, and broadening to building an increasing number and variety of participants and instruments – for example, a larger percentage of the population with savings, more market intermediaries, more types of savings vehicles, or more firms borrowing or raising external equity. It is best to consider the two concepts at once. Taken together, the crucial process of deepening and broadening usually includes:

- Expanding saver/investor participation in the formal financial markets, such as banks, 'non-banks', and stock and bond markets;
- Increasing the number and variety of market institutions;
- Widening the array of financial instruments to suit varying risk/reward preferences;

- Improving a market's ability to price, intermediate and settle transactions in a variety of instruments that lower transaction costs and spreads;
- Ensuring that transactions are conducted with free and genuine competition between efficient and credible institutions and players;
- Regulating market players on the basis of well-designed and enforced regulations;
- Providing a transparent market by promoting the wide dissemination of information on the companies raising capital, the transaction price, price benchmarks, and the financial state of market intermediaries;
- Conforming to international standards of settlement, accounting, corporate disclosure, capital adequacy and other building blocks of finance.

Using this perspective, the launch of unit trusts and targeting SACCOs falls within market broadening arena for two reasons. One, as aforementioned, SACCOS had close to 1.5 million members in 2001. Subscription to unit trusts significantly extends capital markets access to a wider audience, more so, retail investors. Two, we have demonstrated that SACCOs have an investment objective to diversify their income/risk profiles. Unit trusts can target the corporate savings allocated to term deposits and real assets by offering competitive options for long-term investment assets' selection. The challenge to unit trusts promoters is to position their products as competitive investment assets that the management and members ought to prioritize in selection of assets. From the management committee (customer) perspective, the relevant theoretical framework is portfolio selection approaches.

2.11.2 Modern investment theory

Haugen (1990) takes a fund managers' perspective in postulating the 'modern investment theory'. He traces the development of investment theory back to Harry Markowitz (1952) paper entitled 'portfolio selection'. Markowitz showed how to create a frontier of investment portfolios, such that each of them had the greatest possible expected rate of return, given their level of risk. William

Sharpe (1963) developed a simplified version of the technique, now referred to as the *single index model.* Haugen (ibid) states that the single index model is widely employed to allocate investments in the portfolio between individual common stocks, while the original, more general model of Markowitz is widely used to allocate investments between types of securities, such as bonds, stocks, and real assets. These models have been packaged as computer software making portfolio construction quite practical to compute the required return on assets for consideration in selecting portfolio assets. The models are the capital asset pricing model (CAPM) by Sharpe (1964), Litner (1965) and Mossin (1966), and the arbitrage pricing theory developed by Ross (1976).

It is not within the scope of this study to test the selection of portfolio assets by unit trusts investment firms. The CMA (2000) guidelines are quite elaborate on the licensing of fund managers, pricing of units and performance benchmarks. The latter is to ensure ethical disclosure to avoid misleading the public. The relevance of the investment theory is that they provide tools for the managers to construct the units, and in this aspect resolves the .hurdles that SACCO management would face in selection of assets, construction of the portfolio and allocation of investments. The unit trusts are therefore designed to suit the range of investment objectives by the target market.

The unit trusts marketing guidelines seek to help customers to select the funds that meet these objectives. The key issues the customers are to consider are:

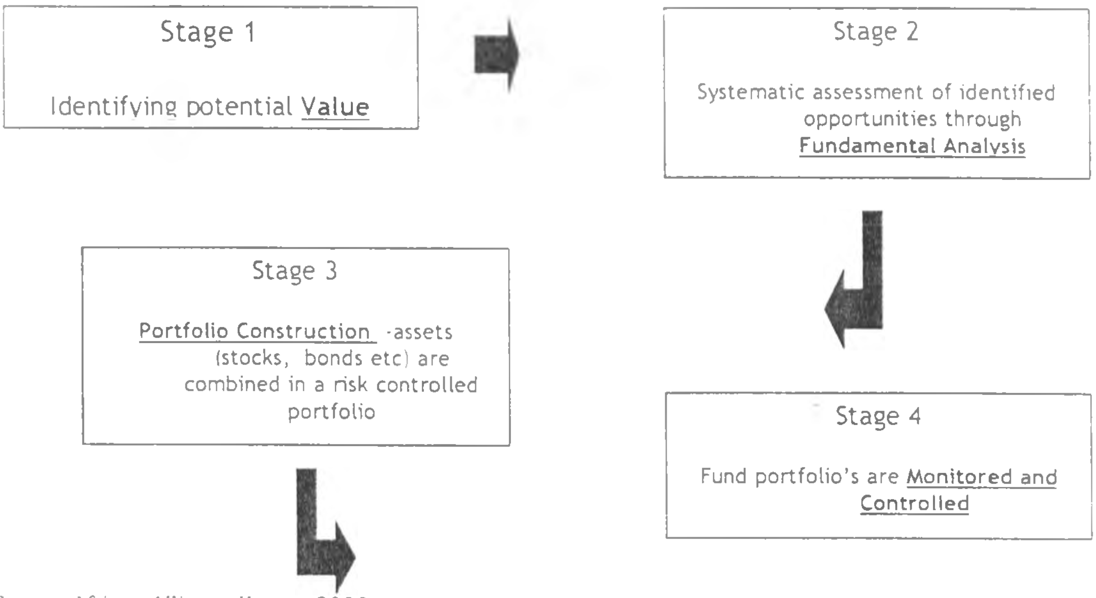
i) Time scale: short or long-term. Unit trusts are a medium to long-term investment (minimum three to five years) so that market fluctuations have time to smooth out. Hence, they need time to grow

ii) Risk preference: the type of selected ought to suit the risk an investor is prepared to take. An investor seeking security and income would be best advised to select either a money market fund, an income fund, a prudential fund, a flexible fund or a general fund or mix. A more aggressive investor can select an equity fund that invests in a specific sector of the market such as financial and industrial companies, mining and resources companies or fast-growing emerging companies. Bond funds are designed to benefit the investor that requires good total returns (capital and income).

The management committee ought to test the units feasibility based on their investment policies. The objective of the investment strategy is expected to maximize the wealth of the members in line with the theory of the firm.

2.11.3 The unit trusts investment process

The investment process has four stages, shown here below:



Source: African Alliance Kenya, 2003

2.12 Study hypotheses

H_A: Units trusts are an attractive investment option to SACCOs.

H_0: Unit trusts are not an attractive investment option for SACCOs.

CHAPTER 3
METHODOLOGY

3.1 Population

The population comprised all SACCOs in Nairobi described as active by the Nairobi Provincial Cooperative Officer's register as at 31st December 2001. There were 1,162 active SACCOs in Nairobi as 31st December 2001 (Nairobi Province Annual Report, 2002).

3.2 Sampling plan

The sample units were selected from a data-base developed by the Kenya Leadership Institute (KLI) of SACCOs in Nairobi. The data-base consists of five-year financial data (1997-2001). Of the 1,162 SACCOS reported as active in Nairobi by the MOCD in 2001, data for more than a year was available for 540 SACCOs. The SACCOs were be ranked in a descending order by size, based on the share capital in 2001.

Using a cluster sampling method, 60 SACCOs were selected from a list of the leading 100. The SACCOs were classified into sector-clusters such as public, private and civil society to enhance representation, with the number of units in each cluster units picked on a proportional basis. The SACCOs whose contact persons were not readily accessible were substituted.

The sampling criteria were based on two assumptions, exposure and size. The 31 SACCOs surveyed in the CMA (1994) study were considered to have had exposure to unit trusts and selected first. The CMA (1994) study had selected them on the basis of their size and that they were considered opinion leaders in the industry. Their size, in terms of membership and share capital also make them the leading targets by unit trusts promoters. The remaining 29 units were picked on a descending size order.

3.3 Data collection

This is a survey. Primary data were collected using structured questionnaires for SACCO managers, and unstructured questionnaires for Unit Trusts Investment Firms (Zimele, African Alliance Kenya). The SACCO managers, who are secretaries to the management committees were the primary respondents, while Zimele and African Alliance provided insights into unit trusts' market performance. Questionnaires were dropped at the respondent's offices and picked once completed. Only 49 of the 63 SACCOs responded. The study was conducted in June – July 2003.

3.4 Data analysis and presentation

Descriptive statistics were used, with presentation in tables, graphs, charts. These statistics helped the researcher establish the distribution of variables with regard to awareness, asset allocation, investment selection criteria and rating of unit trusts. Comparative analysis was undertaken to establish if the responses had cross-sectoral significance.

CHAPTER 4

DATA ANALYSIS AND INTERPRETATION

This chapter presents the study findings on the SACCO's rating of unit trusts as an attractive investment (asset). The SACCOs' investment decisions are made by the Management Committees (MCs). The attractiveness was assessed by:

- establishing if the MCs had discussed unit trusts as a potential asset,
- establishing if the MC, having discussed unit trusts had approved it as a potential asset;
- if the MC has already allocated funds or have plans to allocate funds.

The results are presented in this chapter, while chapter five discusses the significance of these findings and makes recommendations.

4.1 Characteristics of the respondents

Data from 49 of the targeted 60 SACCOs, representing 82% response rate was obtained through a questionnaire using drop-and-pick method. The researcher interviewed fund managers of the two unit trust firms, African Alliance and Zimele. The respondents' characteristics in terms of sector, members, share capital, loans issued and investments in 2001 are outlined in annexe 1. Table 3 below presents the respondents' distribution according to their occupational sectors.

Table 3: Respondents distribution by sector

Sector	*number*	%
Public	29	59%
Private	16	33%
Civil society	4	8%
Total	49	100%

source: research data

Of the 49 respondents, 29 (59%) were drawn from the public sector (includes government ministries, parastatals, universities and colleges), while 16 (33%) were private sector SACCOs. Only 4 were from the civil society (Non-governmental organizations, industry associations). The number of public sector SACCOs in the sample due to their higher share capital values, despite representing 34% of the top 100 SACCOs from the population. Private sector SACCOs are 50% of the top 100.

4.2 Existing investments and selection criteria

The respondents were asked to indicate their asset classes, their values in 2001 and the investment selection criteria. The respondents held investments worth Ksh3.59billion in 2001, allocated to land and buildings, housing, fixed deposits, government securities, quoted shares and unquoted shares. Land and buildings were worth 45.3% of the total value , unquoted stocks shared 23.9%, while housing, fixed deposits, government securities and quoted stocks were worth 22.1%, 4.4%, 3.9% (0.4% respectively. The real assets' higher share of funds is due the traditional preferences' theory, while the unquoted stocks are holdings in the cooperative-linked firms such as the Cooperative Bank, Cooperative Insurance Services and KUSSCO.

The study further asked the respondents to rank their asset selection criteria, whose results are outlined in table 4 below:

Table 4: Investment selection criteria

	Rank			
Indicator	**First**	**second**	**third**	**Average**
Compliance with Cooperative Act	16	3	3	7
Expected returns	10	7	12	10
Risk	7	13	5	8
Familiarity	4	2	3	3
Past returns	2	3	5	3
Liquidity	1	9	7	6
Diversification	1	0	1	1
Total	41	37	36	38

source research data

The criteria is ranked on a descending order, and weighted to provide the pre-dominant indicator. Only 41 respondents indicated their criteria, with the weighted average consisting of 38 respondents. On the basis of the first indicator, 16 SACCOs (39%) sought to comply with the Cooperative Act (1997), while 24% were motivated by the level expected returns of the assets. Risk was rated as the top second criteria by 35%, while expected returns led in the third preference set. Overall, expected returns were the most important factor to 26% of the SACCOs, followed by risk and compliance with cooperative Act (1997) respectively. Compliance with Cooperative Act (1997) ranked top in all sectors.

The dominant position of the rate of return is evident of the SACCOs interest to maximize return to their corporate savings, which inturn expands the SACCOs capital base for lending and re-investment. Hence, the unit trusts would have to yield returns that are competitive to their existing investments to attract corporate savings.

4.3 Awareness of unit trusts

The respondents were asked to state if they were aware of unit trusts, whose results are indicated in table 5 below.

Table 5: Awareness of unit trusts

	Sectors				
Response	*Private*	*Public*	Civil soc.	number	%
Aware	11	13	1	25	51%
Un-aware	5	16	3	24	49%
Total	16	29	4	49	100%

source research data

Only 25 or 51% of the respondents were aware of unit trusts. Those aware of the unit trusts were further asked to state the source of the information. Only 10 of the respondents had learnt about unit trusts from an NSE/Promoter's seminars, 7 had read media articles, 6 learnt in their professional training, and had been informed by their investment advisors. Within the clusters, a higher proportion (69&) of private sector SACCOs were aware of unit trusts. More than half (55%) of public sector SACCOs were not aware of unit trusts. The higher awareness among the private sector may be attributed to the wider exposure of the employees to current market trends. In addition, private sector SACCOs' hold a lower proportion of real assets and are therefore more likely to seek non-real assets to invest the surplus.

Of the 31 SACCOs contacted in the CMA (1994) study, only 18 responded to this study, with 8 expressing awareness of unit trusts. The difference may have been due to management changes or the nine year lag between the two studies. The results indicate that only a simple majority were aware of unit trusts, while the promoters had contacted only 10 SACCOs or 17% of the sample population. The key explanation for the low exposure is that the products are quite new in this market.

4.4 Rating of unit trusts' attractiveness

Since the SACCOs investment decisions are made by the Management Committees (MCs), the attractiveness rating was limited to those whose MCs had discussed the products as potential investment. Among the 25 respondents aware of unit trusts, 12 had discussed the unit trusts as potential investment. These SACCOs are those that had attended promoters' seminars, professional courses or informed by their financial advisors. Their rating of unit trusts' attractiveness is shown in table 6 below.

Table 6: Unit trusts' attractiveness rating

Rating	*number*	%
Attractive	10	83%
Unattractive	2	17%
Total	12	100%

source research data

As table 6 indicates, 10 of the 12 MCs rated unit trusts as attractive. The 10 were asked to state the indicators of unit trusts' attractiveness. The attractive features are outlined in table 7 below. The 2 SACCOs that rated low rate of underlying assets (money markets) and low liquidity

Table 7: Unit trusts' attractive features

Feature	%
Higher returns	47%
Diversification	26%
Liquidity	16%
Professional management	11%
Total	100%

source research data

The respondents rated high returns and diversification gains as the most attractive features while liquidity and professional management scored lower on the scale. The response is in line with the unit trusts objectives of optimizing returns generated from diversification gains. These demonstrate that the MCs understand the principal investment objectives of unit trusts.

4.5 Relationship between information source and rating

There is an identifiable relationship between the source of information, the appraisal by the MCs, and rating as outlined in table 8 below. Of the

Table 8: Relationship between information source & rating

Information source	Number	MC appraisal	Positive rating
Promoters/NSE seminars	6	6	5
Media	7	1	1
Professiona training	9	2	2
Investment advisors	3	3	2
Total	25	12	10

source research data

Of the 6 SACCOs that had attended the promoters/NSE seminars, all had discussed the unit trusts' attractiveness, and 5 rated unit trusts as attractive. A similar trend is evident among the SACCOs informed by their investment advisors. Media and professional training sources only prompted less than 20% of the SACCOs to appraise unit trusts. The findings indicate that the quality of information available to SACCO managers will influence their decision to seek

MC's appraisal of new assets, and consequently increases the probability of positive rating.

4.6 Planned allocation of funds to unit trusts

Only three SACCOs, Harambee, Finnlemm and Sawa indicated they plan to include unit trusts in their asset portfolio in the current financial year. The other nine have postponed investment in the current financial year due to insufficient funds, and commitment to existing priorities.

4.7 Sources of funds

The respondents who plan to purchase unit trusts in the current financial year were asked to state the source of their funds. Harambee plans to use corporate savings and set up a special fund that interested members would subscribe to. Both Finnlemm and Sawa plan to finance unit trusts from a special fund only.

4.8 Other capital markets products

The respondents were asked to identify other capital market products they would be interested in. Their choices are shown in table 9 below.

Table 9: Other attractive capital markets products

Product	number	%
Bonds	14	29%
Quoted stocks	7	14%
Commercial paper	4	8%
No response	24	49%
Total	49	100%

source research data

Of the 25 (51%) SACCOs that responded, 14 ranked bonds as the preferred capital market product, while 7 chose quoted stocks. Almost half of the sample (49%) did not respond. The higher rating of bonds is attributable to the recent establishment of a secondary market for corporate and government bonds at the NSE. The selection of bonds also indicates preference for predictable earnings, which is less volatile than stocks. Those SACCOs that failed to select other products may not have sufficient information on capital markets operations.

4.9 Unit trusts Companies' perspective

The study also interviewed unit trusts managers to establish the size of their portfolio, the level of SACCOs subscription, and their assessment of the SACCOs response. The findings were:

i) Both Zimele and African Alliance were unwilling to reveal the size of their portfolio citing confidentiality restrictions.

ii) They had no SACCO clients.

iii) They attribute the zero response to the SACCO model that emphasizes lending to investment that takes up corporate savings; illiquidity among SACCOs due to high loan demand, default, and low returns of real assets that has locked-in the surplus; and low level of SACCO managers' knowledge of capital markets.

The respondents were confident that the SACCOs will invest in unit trusts in the medium-term once managers and members are adequately educated, and pressure to diversify owing to low return from real assets.

4.10 Testing the study hypotheses

The hypotheses for testing were:

H_A: Units trusts are an attractive investment option to SACCOs.

H_0: Unit trusts are not an attractive investment option for SACCOs.

The research established that unit trusts are attractive to SACCOs based on the positive rating by 80% of the MCs that had appraised unit trusts as potential asset. The study therefore dismisses the null hypotheses and accepts the alternative hypotheses.

CHAPTER 5

DISCUSSION OF RESEARCH FINDINGS, CONCLUSIONS, RECOMMENDATIONS, LIMITATIONS OF THE STUDY AND SUGGESTIONS FOR FURTHER RESEARCH

5.1 Summary of findings & Conclusions

5.1.1 Summary of findings

This study set to establish the rating of unit trusts' attractiveness by SACCOs based in Nairobi. The interest in studying the SACCOs response was prompted by their ranking by the CMA (1994) study as potential investors, based on the significance intermediation role they play among small savers. The researcher then expected that Unit trusts investment firms would have prioritized SACCOs in their marketing programs. The SACCOs response was expected to have been positive since they seek attractive investments to maximize their shareholders' welfare. The researcher hence aimed to provide insights to policy makers, unit trusts investment firms and the SACCO managers of the. potential trends of unit trusts, and in the process support Kenya's financial broadening process.

The key findings of the study are:

a) SACCOs had allocated most of the corporate savings (91.3%) to non-liquid assets such as land, buildings and un-quoted stocks, leaving only 8.7% in liquid assets. Hence, their capacity to change the portfolio set in the short-run would be limited.

b) SACCOs employ a return maximizing criteria in selecting assets, though they have to comply with the provisions of the Cooperative Act and Rules. The preference for higher returns and diversification of the portfolio set is positively correlated to the key investment objectives of unit trusts.

c) Only 51% of the targeted SACCO managers had knowledge of unit trusts. This group includes 8 SACCOs contacted by the CMA (1994) study, less than half the 18 that responded to the current study.

d) Among the 25 SACCOs aware of unit trust awareness of unit trusts was low at 51% of the sample population, less than half the SACCOs MCs had discussed the probability of including unit trusts in the current financial year's investments. This may be attributed to insufficient information as the promoters had only contacted 20% of the sample.

e) Among the 12 SACCOs that had considered unit trusts as potential investment, 10 had rated the asset as attractive.

f) The SACCOs described returns and diversification as the key attractive features of unit trusts.

g) There is a significant relationship between the source of information and MCs appraisal of the unit trusts. All the 6 SACCOs that had attended promoters seminars held MCs appraisal meetings and 5 rated unit trusts as attractive.

h) Among the 10 SACCOs that had found unit trusts attractive, 3 plan to invest in the current financial year, while the rest will not invest in this year owing to existing commitments.

i) The source of funds for unit trusts investment are corporate savings and special funds set for interested members, separate from share capital.

j) Bonds and quoted stocks were rated as other attractive capital markets products. However, 49% of the sample appear insufficiently exposed to capital markets operations.

k) Based on the 80% positive rating of unit trusts by SACCOs whose MCs had met to appraise the unit trusts' attractiveness, the study concludes that unit trusts are attractive investments to SACCOs based in Nairobi.

5.1.2 Conclusions

The study explored the SACCOs' investment behaviour by presenting their portfolio, the asset selection criteria, knowledge of unit trusts, rating and investment decisions made by those aware of unit trusts. The investment decision process indicates that SACCOs have established criteria for appraising potential investments. In essence, they seek to maximize the members' return, which is consistent with the goal of the firm. These findings are consistent with Gachara (1990) and Obuon (1988).

An analysis of the SACCOs balance sheets (see annexe 1) indicated that not all SACCOs hold assets. This is consistent with Gachara (1990) study of investment practices for SACCOs' corporate savings which found that SACCOs prioritise increasing lending from corporate savings, which is their core business, to acquiring assets. This may explain the incapacity to purchase unit trusts in the current year by 70% who cited commitment to existing priorities. The probability of liquidity crunch being a significant drawback to unit trusts uptake was confirmed by the Unit trusts Investment firms' managers. Infact, the three SACCOs that plan to purchase unit trusts intend to set up special funds.

The marginal awareness rate of unit trusts and capital markets is characteristic of developing economies which face low financial deepening/broadening. The study established significant difference between public sector and private/civil society SACCOs. The latter had a higher awareness rate that may be attributable to the greater market exposure of their employees. Overall, the low uptake rate concurs with the anxieties expressed by potential unit trusts promoters interviewed in the CMA (1994) study that insufficient knowledge will limit effective demand in the short run. The Unit trusts investment firms mangers also acknowledge that uptake among small savers will take longer since the concept is fairly new, and have therefore prioritized corporate and high net-worth customers.

The study found significant market potential for unit trusts among the SACCOs provided they have sufficient information, and can mobilize funds. This is supported by the positive rating of unit trusts by 5 of the six SACCOs that had attended promoters' seminars.

5.2 Limitations of the study

There were three key limitations of the study:

i) Owing to time and resource limits, the study drew its sample only from Nairobi.

ii) The analysis was limited only to the SACCOs whose addresses were available, and whose managers responded within the time set for data collection.

iii) The use of a self-administered questionnaire limited the researcher's ability to clarify some of the gaps.

5.3 Recommendations

The study recommends that:

i) The Capital Markets Authority (CMA), the Nairobi Stock Exchange (NSE) and Unit trusts investment firms intensify public education targeting SACCOs' management committees and members to generate effective demand for unit trusts.

ii) The CMA and NSE to continue developing products that would held SACCOs diversify their investment from real assets.

iii) The Ministry of Cooperatives Development to revise the Act and Rules to provide greater flexibility for MCs to optimize investment selection.

iv) The Ministry of Cooperative development to enforce the statutory reserve rule for SACCOs to invest the funds in liquid assets rather than lending.

v) The SACCOs that face liquidity crunch set up separate funds for members who may be interested in unit trusts.

5.4 Areas for further research

Related areas for further research that could compliment this study include:

i) Study of the SACCO MCs understanding of capital markets products to stimulate effective demand of such products.

ii) Exploration of the viability of alternative collective investment schemes (CIS) such as Real Estate Investment Trusts, since SACCOs have traditionally invested in real assets.

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Annexe 1: Study sample key statistics for year 2001

	Sacco	Sector	Members	Finacial statistics (Kshmn)							
				Share capital	Loans issued	Land/ building	Housing	Fixed deposits	Government securities	Quoted shares	Un-quoted shares
1	Afya	PB	45,000	2,400 00	1,700.00		90.00			0 46	650.00
2	Amref	CS	571	79.30	78.41			1.10	2 00		0 06
3	Asili	PB	9,000	393 14	199.37	205 00					57 10
4	Amiair	PV	247	18 93	18.21	0 07				0 07	
5	Bunge	PB	500					7.00			0.01
6	Corotech	PB	500	17.81	18.62						
7	Concorde	PV	382	45 55	36.25			0.38			
8	Energy	PB	500	18 43	15.08					0 10	0 30
9	Eimu	PB	10,000		128 13	104 84				1.00	17 53
10	Finnlemm	PV	600	24.00	18.00	0 49		0.57		0 20	3 30
11	Garo	PV	38	5.64	2 44						
12	Haraka	PV	270	21.01	10 81						0 11
13	Hewa	PV	143	25.10	17.13				0 98	0 47	
14	Hazina	PB	4,582	372.41	288.00	13 56	4 56	32 32			2.89
15	Harambee	PB	87,000	4,231.93	3,271.46	319.78	623 40			2.04	92.80
16	Jamii	PB	4,974	256 50	179.29	45 67	45.67	0.52			3 98
17	Kewisco	PV	1,600	63.00						1.30	
18	Kenya Insurers	CS	500	31 00	30 00			0.19			0 47
19	Kenya Re	PB	101	15.00	13.00						0.22
20	Kenya Bankers	CS	13,000	1,500.00	840.00		2.60	70.00	150.00		0.50
21	Lompasango	PV	1,391	44.81	44 15						0 90
22	Magereza	PB	16,280	745 80	627.50	23 70	23 70	15.00			
23	Mhasibu	PB	1,200	93.50	79.15						0.44
24	Mwito	PB	3,163	161.51	133.25	5 40	4 11	3.40			4 30
25	Mwalimu	PB	43,412	3,430.75	3,022 74	1 00	0 08	0.18		3.19	
26	Nacico	PB		563.56	92 40						
27	Nation Staff	PV	900								
28	Nulaka	PB	1,000	74.36	80.57			1 00		0.20	0.17
29	Naserian	PV	540	35.33	33.51			4 00		0 05	0.12
30	Nyayo Chai	PB	312	19 10	20.69						
31	Nahiho	PB	300	24 00	18 00				1 70		0.04
32	Peugeot	PV	416	39.30	33 10				1 90		
33	Post Bank	PB		90.54	94.81						
34	Radio Guard	PV	1,200	16.59	11.35	0.14					0 09
35	Reli	PB	7,000	536 00	41 90						15 80
36	Sawa	PV	412	28.00	27.00			3 00		0 40	
37	Standard	PV	500	41 05				1.26		0.12	
38	Sauti	PB	1,500	121 00	120 00	5.00					2 00
39	Sheria	PB	3,559	289 19	245 06	6.27					4 23
40	Transcom	PB	5,500	319.00	258.29						
41	Tibett & Britten	PV	270	15 14	9.32						1.09
42	Telepost	PB	18,313	1,088 23	494 13						0 02
43	Tarda	PB	368	21.57	22.36			0 35	1.00		
44	Twiga	PV	190	20.53	13.20			0 44			
45	Ulinzi	PB	1,500	54.00							0.41
46	Uzazi Bora	CS	500	39.31	32.13	0.15					
47	Wanandege	PV	2,003	279 78	61.31	45.00				3.52	
48	Wauzaji	PV	2,197	111 39	100 75	850.00					0 70
49	Wananvumba	PB	334	18 44	21 00	1,626 06	794 12	140 70	157 58	13 12	859 60
	Total		45,346	2,999	1,458	2,533	794	146	159	17	884

Key PV=private PB=public, CS=civil society

Source: research data

UNIVERSITY OF NAIROBI
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P.O Box 30197
Nairobi, Kenya

DATE........June 11th 2003..........

TO WHOM IT MAY CONCERN

The bearer of this letter ....Githuku Mwangi........

Registration No: ....D/61/P/8788/99........

is a Master of Business Administration (MBA) student of the University of Nairobi.

He/she is required to submit as part of his/her coursework assessment a research project report on some management problem. We would like the students to do their projects on real problems affecting firms in Kenya. We would, therefore, appreciate if you assist him/her by allowing him/her to collect data in your organization for the research.

The results of the report will be used solely for academic purposes and a copy of the same will be availed to the interviewed organizations on request.

Thank you.

JACKSON MAALU
CO-ORDINATOR, MBA PROGRAM

OFFICE
NAIROBI.
NAIROBI UNIVERSITY COMMERCE FACULTY

Questionnaire For SACCO Managers

Background information

A unit trust is a vehicle that pools funds from savers and invests the funds in a portfolio of stocks, bonds, or other securities. The purpose of this study is to establish your organization's likely (potential) or existing investment in unit trusts.

1.Name of SACCO:

2. If you have a subsidiary, please state its name and mission.

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3. Members ------------

4. Share capital in 2001 (Ksh'000) -------------

5. Loans issued in 2001 (ksh'000) --------

Please state the existing investments, value and proportion as at 2001

Asset	Value (Ksh'000)	Proportion/total (%)
Land		
Housing		
Fixed deposits		
Government securities		
Quoted shares		
Unquoted shares		
Other (specify)		

6. Please rank (in order of importance using 1, 2, 3...) the factors you considered when selecting the investments above.

Familiarity	
Previous returns	
Expected returns	
Liquidity	
Comply with Cooperative Act	
Risk	
Other (specify)	

7. Are you aware of unit trusts: 1. Yes 2.No

8. If yes to how did you learn (please tick the correct one)
   1. Attended NSE/Promoters' seminar ( )
   2. Media ( )
   3. Professional training ( )
   4. Other (state) ( )

9. Have you shared this knowledge with your management committee?
1.Yes 2. No

10. If Yes to question 7, what is their rating of unit trusts?

1. Attractive 2. Unattractive

11. If (2) to question 10, what are the reason (s)?

----

12. If (1) to question 10, what are the reasons?

----

13. If (1) to question 10, have you included unit trusts in your planned investments for the current financial year? 1.Yes 2.No

14. If no to question 13, what is the reason(s)?

----

16. If yes to question 13, what proportion (%) of your funds will you allocate to unit trusts? ----------

17. If yes to question 13, how will you raise the cash to invest in unit trusts?

Source	Tick as appropriate
Use cash in fixed deposits	
Liquidate Securities (government, quoted shares)	
Liquidate fixed assets	
Future statutory reserve/retained earnings	
Special fund (contributions by members)	
Others (state)	

18. Please state if there are other capital market products (funds) you would be interested in.

Thank you

Interview schedule for Unit Trusts Management Companies

A. Performance (since launch)

i) List the number of products (funds), their size, closing prices and return (state period).

Product (fund)	Size (Ksh'000)	Closing price	Return (%)

ii) Who are the key investors (categories) in the funds?

Category	Proportion (%)
Individuals	
Investment groups/clubs	
Institutional investors	
Other (please specify)	

B. Experience with SACCOs

a) Please state if any SACCO has invested in your funds.

Fund	Number of SACCOs	Amount invested (Ksh'000)

b) In your discussions with SACCOs, what is their appraisal of unit trusts in comparison to their existing investments?

----

c) What are the SACCOs principal investment objectives?

----

d) When designing your products, did you consider the SACCOs' interests?

----

e) Which form of savings (personal or corporate) among SACCOs are you targeting?
----

f) Please give reasons for the selection in (e) above.

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g) What initiatives ought to be employed to increase SACCOs investment in unit trusts; and who ought to do it?

