

**THE EFFECT OF REGULATIONS ON THE FINANCIAL PERFORMANCE OF  
DEPOSIT TAKING SAVINGS AND CREDIT COOPERATIVE SOCIETIES IN  
KENYA**

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**DECLARATION**

This research project is my original work and has never been presented in any other university/institution for examination.

Signature----- Date-----

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

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## **DEDICATION**

This research project is dedicated to my loving mother, Billy Mary Onguka for her hard work in supporting me throughout my education. Many thanks to my late Dad, Joel Onguka for inspiring me and making me what I am, my sisters Rubin and Nelly for the unwavering support, encouragements and without whose guidance, I wouldn't be able to complete this protect.

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## **LIST OF ABBREVIATIONS**

<b>ATM</b>	-Automatic Teller Machine
<b>BOSA</b>	-Back Office Sacco Activity
<b>CARs</b>	- Capital Adequacy Ratios
<b>CAPR</b>	- Ratio of Capital to Total Assets
<b>CBK</b>	- Central Bank of Kenya
<b>CEO</b>	-Chief Executive Officer
<b>DTI's</b>	- Deposit Taking Institutions
<b>DTS</b>	- Deposit Taking Sacco's
<b>DGF</b>	- Deposit Guarantee Fund
<b>DTM'S</b>	- Deposit taking micro-finance
<b>FOSA</b>	- Front Office Savings Activities
<b>GOK</b>	- Government of Kenya
<b>KERUSSU</b>	- Kenya Rural Savings and Credit Societies Union
<b>KUSCCO</b>	- Kenya Union of Savings and Credit Co-operative Organization
<b>KGS</b>	- Kenya Gazette Suppliers
<b>MOCD&amp;M</b>	- Ministry of Co-operative Development and Marketing
<b>PEARLS</b>	- Protection, effective financial structure, asset quality, rates of return and costs, liquidity and signs of growth.

<b>RMFI</b>	- Rural and Micro Finance Institution
<b>ROA</b>	- Return on Assets
<b>ROE</b>	- Return on Equity
<b>SASRA</b>	- SACCO Societies Regulatory Authority
<b>SACCO</b>	- Savings and Credit Co-operatives Limited
<b>SMES</b>	- Small Medium Enterprises
<b>WOCCU</b>	-World Council of Credit Unions
<b>SACCOL</b>	-Savings and Credit Co-operative League of South Africa
<b>SME</b>	- Small and Micro Enterprise

## ABSTRACT

The aim of this study was to investigate the effect of regulations on the financial performance of deposit taking savings and credit cooperatives (SACCOs) in Kenya. More specifically, the study sought to investigate the effect on management efficiency, liquidity and capital adequacy on the financial performance of deposit taking SACCOs in Kenya, as stipulated by Sacco Society Regulatory Authority (SASRA). Many studies have clearly avoided looking at specific aspects of these regulations particularly their effects on financial performance of the Sacco. This study adopted a descriptive survey design. The target population was all the 135 deposit taking SACCOs in Kenya registered and licensed by SASRA by 2014. Both primary and secondary data was used in this study, where a census survey was preferred as the population of the study was small. A likert scale questionnaire was used to gather primary information while a secondary data collection sheet was used for collecting secondary information regarding SACCO performance. Out of the 135 questionnaires sent out, 109 responded and returned the questionnaires, this represented 81% response rate. The secondary data was sorted, coded and input into the statistical package for social sciences (SPSS) for production of graphs, tables, descriptive statistics and inferential statistics. The results indicated that SACCO regulations have positive effect on capital ratio and which led to an increase in return on assets (ROA), further it was established that increase in liquidity led to a decrease in ROA. The study found out that a unit increase in management efficiency increased ROA. From the findings, the study concluded that capital regulations, capital ratio, liquidity and management efficiency significantly influence financial performance of the Deposit Taking SACCOs. Most SACCOs reported improvement in their performance both in membership, management efficiency, portfolio growth and loan cycle. Even though this was attributed to a number of factors ranging from increased membership, high efficiency, high demand and quick recoveries, one can easily attribute these results on positive influence of SASRA regulation. The study recommends that further research should be done on the effect of competition on the financial performance of the SACCOs and the effect of SASRA regulations on the organizational culture of SACCOs. Further research study should be carried out to assess the impact of Sacco's regulations, cost of intermediation and growth of Deposit Taking financial institutions, as well as regulation on non deposit taking SACCOs in Kenya.

## CHAPTER ONE: INTRODUCTION

### 1.1 Background of the Study

The Savings and Credit Co-operatives (SACCO) sector and MFIs have been of great interest to regulators because of their rate of growth, opined on the fact that they offer cheap loans to members. According to Mudibo (2005), the importance of regulations is to hedge against the high risk attributed to imbalances in financial institutions balance sheets as they serve as prudential measures that mitigate the effects of economic crises on the stability of the financial institution system and subsequent accompanying macroeconomic results. Sound regulation means the institutions are able to achieve objective of giving cheap loans, as well as protecting member's savings.

Theories on financial regulation emphasize the fact that markets do not always operate in the best interests of customers, so intervention in the form of regulation is necessary to protect consumer and industry. These theories include; financial stewardship theories, public interest theory which emphasizes public, as opposed to private, interest (Stigler, 1971), interest group theory views regulation as the products of relationships between different groups and between such groups and the state (Baldwin and Cave (1999), The economic theory, the agency theory which suggests that the stewards should make financial decisions for maximization of shareholders value (Berle & Means, 1932), and finally, the competition for regulation theory which suggests that there exist a market for regulation and it will serve the interests of those who are willing to offer the most for the regulation.

SACCOs are traditionally not for profit, member owned financial co-operatives that provide basic savings in the forms of shares on which a dividend is paid and loan

facilities to its members (Griffiths and Howell, 1991). The concept of savings is in part a misnomer, as they are not interest earning savings in the traditional sense, which is currently not permitted by the Credit Union regulations shows that reform is to be forthcoming (Quiroz, 2007). Deposits made by members are in effect shares that earn a dividend, so that when a member pays in savings they are buying shares in that credit union. A dividend is only paid where the credit union has sufficient surplus in any given year (Staschen, 2003). The relevance of regulation of financial institutions with regard to financial performance cannot be over emphasized since they constitute the main drivers for growth and financial development. Regulations can greatly assist the SACCO sector by infusing better financial practices and prudential standards. Despite the fact that SACCO Societies Regulatory Authority (SASRA) regulations have been in operation since 2009, empirical studies have clearly avoided looking at specific aspects of these regulations on the Sacco's. It is in view of this that this study seeks to examine effect of regulations on financial performance of Deposit Taking SACCOs in (DTS) Kenya.

### **1.1.1 Regulation of Financial Institutions**

According to Baskin *et al.* (2012), regulation is a supervision which subjects institutions to certain requirements, restrictions and guidelines with the aim of maintaining integrity of the financial system. The Regulations on Savings and Credit Cooperative Societies and credit schemes in Africa engaged in accepting savings and deposits from their members for an amount that is less than set minimum (WOCCU, 2002). SACCOs are also supposed to attain high minimum capital requirements to act as a barrier to market entry to possible new players that are not able to raise sufficient capital for the initial stages as a regulated institution. But, on the other hand, a high

minimum capital requirement could help to mitigate moral hazard behavior among shareholders

Beside banks, MFIs together with Savings and credit cooperative societies are important suppliers of microfinance services to middle and low income segments of the population that usually operate at a small scale in areas or with sectors of the population not favored by banks and other financial institutions in the provision of financial services. The first prudential standard is the minimum amount of liquid capital that SACCOs should raise to entry the regulated market (Staschen, 2003). This requirement is an absolute measure of solvency and is usually established by primary regulation. Capital adequacy refers to a relative measure: it establishes the maximum level of leverage that a financial institution is allowed to reach on its operations. It is measured by the ratio of risk-weighted assets relative to regulatory equity, which has been internationally recommended to be equal to 12.5 times, or commonly known as a capital adequacy ratio of 8% (Jansson, 1997).

Financial development in Kenya, like in most African countries, has generally traversed two main eras, namely, the era of state control and that of liberalization (Quiroz, 2007). By serving as instruments for implementing government socio-economic policies, cooperatives were engulfed into state politics to the extent that the failures of state policies found expression in the cooperative movement. This partly explains why literature on cooperatives in this era is awash with more stories of cooperative failure than stories of cooperative success. Such failures contributed to calls for the liberalization of the cooperative movement in the early 1990s (MOCD&M, 2012).



### **1.1.2 Financial Performance**

Financial performance is defined by Terence (1989) as a subjective measure of how well a firm can use assets from its primary mode of business and generate revenues by ensuring that resources available are used in the most efficient and effective way. The rationale is to provide maximum return for the organization on the capital employed in the business. Financial performance for firms is a very vital factor because managers need to know how well they are performing. There two fundamental rationale why SACCOs should gauge their financial performance measurement (Johnson and Mark, 1997). The former being to produce financial statements at the right time, and secondly to ensure that financial statements are analyzed to produce information about the performance of the scheme, which must be used to improve that performance of the institution.

Brealy and Myers (2003) observed that financial performance helps to highlight the facts concerning managerial performance, corporate efficiency, financial strength and weaknesses and credit worthiness of a company. Seers (1979), the performance of SACCOs depends on their operational efficiency with the purpose of development to reduce poverty, inequality, and unemployment. For Sen (1999), development involves reducing deprivation or broadening choice. Deprivation represents a multidimensional view of poverty that includes hunger, illiteracy, illness and poor health, powerless, voiceless, insecurity, humiliation, and a lack of access to basic infrastructure (Narayan et al. 2000:4-5).

### **1.1.3 Regulation and Financial Performance of SACCOs**

Financial regulation such as capital regulation and supervision are essential for stable and healthy financial system and that the need becomes greater as the number and

variety of financial institution increase. The financial sector has always received upper attention on protection due to the vital role it plays in an economy. Minimum capital regulation is one of the three pillars of macro prudential regulation. Financial institutions capital serves both as a buffer and as a disincentive to excessive risk taking. When general equilibrium effects are taken into account, however, it is not clear that higher capital requirements will reduce the level of risk in the financial sector (Gale, 2010).

The setting by regulators of minimum capital standards on financial institution was one of the vital developments in the 20th century. In most cases financial regulators find capital adequacy regulation as a means of strengthening the safety and soundness of the banking industry (Oladejo and Oladipupo, 2011). Basically, there are three arguments for financial regulation. The first is that regulation is needed for prudential reasons, Jackson *et al.* (1999). The other argument is that financial regulation is needed to counter moral hazard problems created by the regulator themselves (Benston and Kaufman, 1996). The final argument is that financial regulation is needed to protect small depositors (Craig and Hardee, 2007).

The need to forestall or manage customers' flight might also be a necessary caution in the post consolidation banking era as observed in the study of Jervey (2005) that financial regulations influence pressure deposit protection board and other regulators to ensure probity, transparency and accountability and that financial regulations is a dominating factor in affecting overall financial institution financial performances, other factors such governance, market competition ratios, operating costs; asset quality requirement overall financial performance. SACCOs regulation and performance relate in that the regulations are meant to set specific requirements on the

tools used to measure performance (PEARLS) leading to a direct relationship (Financial Sector Deepening, 2009).

#### **1.1.4 Savings and Credit Cooperative societies**

Savings and Credit Cooperative Society is a financial organization owned and operated by a group of individuals for their mutual benefit. SACCOs in Kenya are required by law to have their financial statements audited at the end of the fiscal year. In addition, they have served as a vehicle for mobilization of rural and urban savings which are important sources of funding for productive activities. In Sessional Paper number 14 on SACCO Development published in 1975, the government categorically stated its continued recognition and support for SACCOs as vital instruments for mobilizing the natural human and financial resources for national development.

The rationale behind the formation of SACCOs was simple unity in diversity. This strength in numbers led to personal economic empowerment and financial freedom for many Kenyans. SACCOs in Kenya were formed to encourage thrift. According to the Financial Sector Deepening study 49.2 percent of people mainly save for a rainy day, 37 percent for education and 34.9 percent for emergencies. SACCOs are found in both the private and public sectors. They have traversed all sectors of society and developed a much broader and deeper market penetration than the current competition. As such, SACCOs are better positioned to continue serving the ‘unbanked’ population. SACCOs reach a wide spectrum of the population because they offer a diverse range of products which include loans m mortgages (WOCCU, January 2013).

The popularity of SACCOs stems on the fact that they offer affordable loans, and this has led to incredible growth of the sector. They have catered for the needs of their

members; however they are facing competition from banks. Most SACCOs in Kenya has adopted Front Office Services Activities (FOSA) to complete the services they render to clients. FOSAs have proved to be one of the key profit drivers and members have appreciated the services offered by these FOSAs enabling members to access full range of basic financial services and consolidate these services to the full satisfaction of members (IFSB, 2013). The introduction of FOSA has contributed to the positive performance of SACCOs through improved profitability which has led to a high dividend rates to the members. SASRA (2010) was therefore enacted to regulate the deposit taking SACCOs, whereas the non deposit taking cooperatives shall remain regulated by cooperative act 2008. This study focused on deposit taking SACCOs regulated by SASRA.

## **1.2 Research problem**

Financial regulations require credit unions to reconstitute their boards, improve on corporate governance and upgrade staff competence in order to improve profitability. In addition, despite the fact that regulations have been in operation in financial institution, the effects of regulations on their financial performance has not been established. Since the enactment of these regulations, there has been increased empirical attention on the effect of the regulations on the financial performance (Kioko, 2010). Regulation consists of rulemaking and enforcement. Economic theory offers two complementary rationales for regulating financial institutions. Altruistic public-benefits theories treat rules as governmental instruments for increasing fairness and efficiency across the society as a whole. Agency-cost theory recognizes that incentive conflicts and coordination problems arise in multi- party relationships and that regulation introduces opportunities to impose rules that enhance the welfare of one sector of society at the expense of another (Diamond and Dybvig, 1983).

Athanosoglou, Brissimis, and Delis (2005) investigated, in a single-equation framework, the effect of capital adequacy on MFIs profitability. Using dynamic estimation technique, Goddard, Molyneux, and Wilson (2004) studied the determinants of profitability of European MFIs. They found a significant persistence of abnormal profits from year to year and a positive relationship between the capital-asset ratio and profitability. Hence, capital regulations on risk taking can mitigate conflicts between shareholders and credit union managers concerning the choice of investment and improve credit union financial performance.

Recent economic crises have revealed the importance of regulations to hedge against the high risk attributed to imbalances in balance sheets. Regulations are a prudential measure to mitigate the effects of crises on the stability of the banking system, although excessive regulations may increase the cost of intermediation and reduce the profitability of the in credit unions (Stiglitz, 2001). In Brazil a study by Rhyne (2002) looks at the benefits of regulating the MFIs and SACCOs and comes up with the finding that it instills confidence to depositors and helps the Central Bank in achieving the financial inclusion goal. Rhyne, (2002) gives an experience of regulating MFIs through the Microcredit regulatory authority and comes up with the finding that there are challenges of overlapping borrowers, sustainability of the sector and lack of good supervisory tools to monitor foreign investment and securitization

The SASRA regulations came in against a backdrop of losses and compromised profitability, loss of members to banks, incompetent staff and poor corporate governance. Kirkpatrick and Tennant (2002) also opined that SACCOs represent one of the most important sources of financing in developing countries and in the last few years, SACCOs have experienced tremendous growth all over the world and the consequences of high related party balances. Ooko (2013) opines that regulatory

institutions that survive today exist because they turned out to be useful, whereas Wangui (2013) focused on corporate governance as important factor in financial performance of the SACCOs. Kioko, (2010) cited a relative increase on the effect of the regulations on the financial performance of SACCOs' amongst deposit taking institutions. There has been little focus on establishing the effect of regulations on the financial performance of SACCOs in Kenya. This study sought to fill the existing knowledge gap by answering the question: What is the effect of SASRA regulation on SACCOs' financial performance?

### **1.3 Objective of the Study**

To determine the effect of regulations on the financial performance of deposit taking savings and credit cooperatives (SACCOs) in Kenya.

### **1.4 Value of the Study**

This study will add value in the phenomenon of Sacco movement, microfinance institutions and deposit taking institutions and more emphatically to academic researchers and scholars. The forerunners in this area have written in depth about banks and microfinance, but they ignored Sacco's. The research thus aims at shedding more light in this field and to form bases for further researches and contribute to the body of knowledge already existing in the Sacco sector, and the findings will be of importance to academicians who wants to understand the SACCO sector, and do a comparative study and any other relevant information on this field.

SASRA, as the regulator and a policy maker will need knowledge of the cooperative movements and keep themselves abreast with dynamics and thus obtain guidance from this study in designing appropriate practices that will regulate the stakeholders in the SACCOs in Kenya. There is always danger of under or over-regulation and it's

the challenging mandate not only ensuring that the Sacco industry is stable and more competitive but also operate in a sustainable manner by responding appropriately to the ever changing financial needs of Kenyans and SACCOs. The government and the treasury can also use this study to educate those SACCOs that have not complied about the importance of being regulated.

The study will be of interest to both existing and prospective members of the SACCOs, as well as members of the public. The Sacco sector have of late opened their bond to the public and business community, hence the findings assist them in making informed decisions. This will form a base for scholars and anyone interested in conducting research in this area in future. We all know that there is little literature in the field of Sacco's and SASRA and any additional knowledge on this area is a bonus.

## **CHAPTER TWO: LITERATURE REVIEW**

### **2.1. Introduction**

This chapter focused on previous studies done by various authors in relation to regulation of financial institutions. The chapter is divided into four sections. The first section discussed theories relating to financial regulation. The second section discussed determinants of financial performance. The third section covered the empirical review and a brief description of the research methodologies used by previous studies in attaining their objectives. The fourth section covered the summary of literature review.

### **2.2. Theories of Financial Regulation**

This research was guided by three major theories of financial regulation, mainly the financial stewardship theories, the economic theory and finally agency theory by Jensen and Meckling(1976).

#### **2.2.1 Financial Stewardship Theory**

The financial stewardship theories set the financial institution's objectives as value maximization which is complemented by the firms' vision. Key among these theories is the stakeholder theory which says that corporate decisions should consider the interest of shareholders (Sundaram & Inkpen, 2004). After the required funds have been raised, they are then applied to generate income. This is the utilization of the finance raised by the society in the selected objectives. This marks the implementation stage of the investment identified by the financial institutions. However, after income has been obtained, the agent measures the results from the investment by preparing a statement of comprehensive income which shows the surplus, statement of financial position indicating the financial state of affairs as at



that time and cash flow statements. The management committee determines whether the returns are appropriate.

Financial stewardship being the routine financial decision-making of the credit Union, should embrace sound business practices. This should also revolve around the credit Union's financial discipline with a profound influence on the success of all businesses conducted by the credit Unions (Mudibo, 2005). The major financial decisions involved in financial stewardship, for instance, include decisions on finance staff, loan management, asset management and product innovation (Horne, 2003, and Mudibo, 2005). The financial stewardship should be capable of working to increase SACCOs' wealth, sustain the SACCOs' value and satisfy the shareholders' demands. Further, the financial stewardship aspect is also responsible for updating accounts, ensuring correctness of accounts, advance planning and reporting to members.

### **2.2.2 Economic Theory**

Regulation consists of rulemaking and enforcement. Economic theory offers two complementary rationales for regulating financial institutions. Altruistic public-benefits theories treat rules as governmental instruments for increasing fairness and efficiency across the society as a whole. Agency-cost theory recognizes that incentive conflicts and coordination problems arise in multi-party relationships and that regulation introduces opportunities to impose rules that enhance the welfare of one sector of society at the expense of another (Diamond and Dybvig, 1983). Each rationale sets different goals and assigns responsibility for choosing and adjusting rules differently. Altruistic theories assign regulation to governmental entities that search for market failures and correct them. It is taken for granted that we may rely on

a well-intentioned government to use its discretion and choose actions for the common good (Jensen and Michael, 1994).

Agency-cost theories portray regulation as a way to raise the quality of financial services by improving incentives to perform contractual obligations in stressful situations. These private-benefits theories count on self-interested parties to spot market failures and correct them by opening more markets. In financial services markets for regulatory service create outside discipline that controls and coordinates industry behavior. Institutions benefit from regulation that: enhances customer confidence; increases the convenience of customer transactions; or creates cartel profit. Agency-cost theories emphasize the need to reconcile conflicts between the interests of institutions, customers, regulators and taxpayers (Edward, 1997).

### **2.2.3 The Agency theory**

Jensen and Meckling (1976) put forward the agency theory and they argued that there is an increase in gap between ownership and control of large organizations arising from decrease in equity ownership. In line with agency theory, the finance theory is concerned with ensuring that managers act to maximize shareholders' wealth. The theory is an efficient market model (Blair, 1995; Keasey et al., 2004) which actually recognizes the agency costs (Jensen & Meckling, 1976). The myopic market model shares a common view with the agency theory where the firm should serve shareholders' interests only. According to the model, short-term performance are encouraged thereby sacrificing long-term value and competitive capacity of the SACCO society. However, Jensen and Mecklin (2006) explained that managers do not always run the firm to maximize returns to shareholders. Stein (1988) argues the model fosters on the maximization of shareholder welfare does mean share price

maximization. This owes to the fact that the market system tends to undervalue long-term expenditures which may lead to the increase of the shareholder welfare. Owing to myopic nature in the governance structure, the agents are forced to take short-term decisions in increasing share prices (Keasey et al, 2004).

## **2.3 Regulation of Financial Institutions**

There is a strong sense that if only policymakers in countries around the world would implement particular regulatory and supervisory practices, then financial institution safety and soundness would improve, thereby promoting growth and stability.

### **2.3.1 Prudential standards and reporting requirements by the Act**

The issues dealt with relate to the extent of external borrowing, asset categorization and provisioning, maximum loan size and insider lending and loan loss classification. Saccos' are subject to adhering to; Monthly returns (capital adequacy, liquidity, and deposits), Quarterly returns (risk classification of assets and loan loss provisioning, investment returns, financial performance) and other returns as requested by the body. The Act requires Saccos' to submit Annual returns. SASRA has the authority to inspect the premises and the records of a Sacco and to prescribe enforcement actions in case of deficiencies including the appointment of a statutory manager. Non-compliance with legal requirements carries clearly specified penalties and includes removal from office of directors and other responsible officers. SASRA has set up a Deposit Guarantee Fund (DGF) and Saccos will be expected to contribute to this coverage to a limit of shs.100, 000. The Fund shall vest on a Board of Trustees four members of which shall be nominated by the Saccos.

### **2.3.2 Conducting business in a prescribed format**

The enactment of SASRA was a wakeup call for SACCOS on how they conduct their business. The Committee Members are restricted from carrying out the routine operations of Sacco's but are required to set policies to be implemented by staff. In effect, the roles have changed and staffs are more independent in carrying out their duties without interference of the board. Risk assessment and making provision for loan losses has been made mandatory. Setting aside reserves and a fund from which members can be refunded incase the Sacco collapses has been made mandatory. They are also required to have systems that are SASRA compliant.

### **2.3.3 Regular Returns and Surveillance**

SACCOs are from time to time required to file various returns such as capital adequacy and others returns, on or before 15<sup>th</sup> day of every month. SASRA has employed qualified technocrats and personnel who go through the reports. Whenever any irregularities are detected, Sacco's can be summoned to explain. Failure to file returns attracts penalties; this has made Saccos' more vigilant in sending their returns. SASRA continuously monitor Saccos' operations through on-site and off-site surveillance.

In line with regular returns, lie regular surveillance, which stipulates that before a Sacco engages in any new operations like admitting new class of members, opening and closing branches SASRA has to be informed and inspection done before approving such activities. When a Sacco ignores stipulated requirement, heavy penalties often follow. SASRA (2010) gives it authority to license Saccos and the authority to revoke licenses upon expiry or an option not to have the license renewed.

### **2.3.4 Staff Compliance**

A licensed Sacco Society will be to meet threshold SASRA put regarding qualification of the senior staff which has meant that Saccos had to go back to the drawing board and recruit competent and qualified staff while at the same time they had to conduct regular training for the already existing staff in order to meet these regulations. According to Sasra regulations, the internal auditor should be a qualified Certified Public Accountant and should also pass the test integrity. Training of staff has been emphasized by SASRA thus the authority conducts seminars from time to time.

Previously Sacco staffs were being recruited based on nepotism and most of them did not have relevant qualification. This has changed drastically with the enactment of SASRA regulations which have brought about increased staff competence on financial performance of Deposit Taking Sacco's (SASRA, 2013). As a result, Sacco's are now at par with other financial institutions when it comes to talent recruitment.

### **2.3.5 Minimum capital requirement**

The obvious prudential standard is the minimum amount of liquid capital that MFIs should raise to entry the regulated market (Staschen, 2003). This requirement is an absolute measure of solvency and is usually established by primary regulation. It serves as a cushion in periods when the institution shows an unhealthy situation due to its own performance or to exogenous factors such as economic downturns (Christen *et al*, 2003). Sacco societies shall maintain minimum capital requirements as prescribed by SASRA or else pay a penalty interest not more than 1% of the amount of deficiency for every day with deficiency(SASRA, 2012), some argue that high

minimum capital requirements could act as barriers to market entry to possible new players that are not able to raise sufficient capital for the initial stages as a regulated institution (Jansson, 1997). But a high minimum capital requirement could help to mitigate moral hazard behavior among shareholders (Jansson *et al*, 2004). In addition, a high minimum capital requirement is often seen as one tool for limiting the number of institutions that the supervisory body should be responsible for monitoring, especially if the supervisory resources are scarce (Schmidt, 2000).

### **2.3.6 Capital adequacy**

Capital adequacy refers to a relative measure which establishes the maximum level of leverage that a financial institution is allowed to reach on its operations (Jansson, 1997). It is measured by the ratio of risk-weighted assets relative to regulatory equity, which has been internationally recommended to be equal to 12.5 times, or commonly known as a capital adequacy ratio of 8% (Jansson, 1997). Nonetheless, it has to be remembered that this prudential standard proposed by the Basel Committee was intended to be applied to international and large banking institutions from developed countries, and that it has been translated to several financial systems in developing countries despite the well-known differences in institutional risk profile, scale of operations and national economic environments (Guidotti *et al*, 2004; Jansson, 1997).

Jansson *et al* (2004) view capital adequacy as a basic and mandatory requirement in any prudential standards, however opponents are of the view that minimum leverage levels should be tailored as close as possible to the specific characteristics of the microfinance lending. These requirements should be applied to every institution engaged in lending operations; regardless their institutional form (Christen and Rosenberg, 2000).

## **2.4 Determinants of financial performances**

The determinants of financial performances can be classified into financial institution specific (internal) and macroeconomic (external) factors (Al-Tamimi, 2010; Aburime, 2005). These are stochastic variables that determine the output. Internal factors are individual bank characteristics which affect the SACCOs performance. These factors are basically influenced by internal decisions of management and the board. The external factors are sector-wide or country-wide factors which are beyond the control of the company and affect the profitability of banks.

### **2.4.1 Capital Adequacy**

Capital is one of the bank specific factors that influence the level of bank profitability. Capital is the amount of own fund available to support the bank's business and act as a buffer in case of adverse situation (Athanasoglou et al. 2005). Banks capital creates liquidity for the bank due to the fact that deposits are most fragile and prone to bank runs. Moreover, greater bank capital reduces the chance of distress (Diamond, 2000). However, its drawback is that it induces weak demand for liability, the cheapest sources of fund Capital adequacy is the level of capital required by the banks to enable them withstand the risks such as credit, market and operational risks they are exposed to in order to absorb the potential losses and protect the bank's debtors.

According to Dang (2011), the adequacy of capital is judged on the basis of capital adequacy ratio (CAR). Capital adequacy ratio shows the internal strength of the bank to withstand losses during crisis. Capital adequacy ratio is directly proportional to the resilience of the bank to crisis situations. It has also a direct effect on the profitability of banks by determining its expansion to risky but profitable ventures or areas (Sangmi and Nazir, 2010).

### **2.4.2 Asset Quality**

The SACCO's asset is another credit union specific variable that affects the profitability of a bank. The bank asset includes among others current asset, credit portfolio, fixed asset, and other investments. Often a growing asset (size) related to the age of the bank (Athanasoglou et al., 2005). More often than not the loan of a bank is the major asset that generates the major share of the credit union income. Loan is the major asset of commercial banks from which they generate income.

The loan portfolio quality has a direct bearing on bank profitability. The highest risk facing a bank is the losses derived from delinquent loans (Dang, 2011). Thus, nonperforming loan ratios are the best proxies for asset quality. Different types of financial ratios used to study the performances of banks by different scholars. It is the major concern of all commercial banks to keep the amount of nonperforming loans to low level. This is so because high nonperforming loan affects the profitability of the bank. Thus, low nonperforming loans to total loans shows that the good health of the portfolio a bank. The lower the ratio the better the bank performing (Sangmi and Nazir, 2010).

### **2.4.3 Management Efficiency**

This is one of the key internal factors that determine the bank profitability. It is represented by different financial ratios like total asset growth, loan growth rate and earnings growth rate. The performance of management is often expressed qualitatively through subjective evaluation of management systems, organizational discipline, control systems, quality of staff, and others. Yet, some financial ratios of the financial statements act as a proxy for management efficiency.



Further to the above, the capability of the management to deploy its resources efficiently, income maximization and reduction in operating costs can be measured by financial ratios. One of this ratios used to measure management quality is operating profit to income ratio (Rahman et al. 2010). The higher the operating profits to total income, the more the efficient management are in terms of operational efficiency and income generation. The other important ratio is that proxy management quality is expense to asset ratio. Management quality in this regard, determines the level of operating expenses and in turn affects profitability (Athanasoglou et al. 2005).

#### **2.4.4 Liquidity Management**

Liquidity is another factor that determines the level of bank performance. Liquidity refers to the ability of the bank to fulfill its obligations, mainly of depositors. According to Dang (2011) adequate level of liquidity is positively related with bank profitability. The most common financial ratios that reflect the liquidity position of a bank according to the above author are customer deposit to total asset and total loan to customer deposits. Other scholars use different financial ratio to measure liquidity. For instance Ilhomovich (2009) used cash to deposit ratio to measure the liquidity level of banks in Malaysia. However, the study conducted in China and Malaysia found that liquidity level of banks has no relationship with the performances of banks (Said and Tumin, 2011).

#### **2.4.5 External Factors/ Macroeconomic Factors**

The macroeconomic policy stability, Gross Domestic Product, Inflation, Interest Rate and Political instability are also other macroeconomic variables that affect the performances of banks. For instance, the trend of GDP affects the demand for banks asset. During the declining GDP growth the demand for credit falls which in turn

negatively affect the profitability of banks. On the contrary, in a growing economy as expressed by positive GDP growth, the demand for credit is high due to the nature of business cycle. During boom the demand for credit is high compared to recession (Athanasoglou et al., 2005). The same authors' state in relation to the Greek situation that the relationship between inflation level and banks profitability is remains debatable.

## **2.5 Empirical Review**

Ngaira (2011) conducted a study on impact of SASRA on DTS in Nairobi concluded that, SASRA has greatly impacted on the Sacco performance in terms of outreach and sustainability and performance of SACCOs in Kenya. Most Sacco's researched on reported improvement in their performance both in membership, portfolio and loan cycle and general efficiency. Even though this was attributed to a number of factors ranging from increased membership, high efficiency, high demand and quick recoveries, attributed to be as a result of SASRA regulatory framework. The study used primary data collected Sacco staff, the respondents from all SACCOs were conversant with the contents of the SASRA guidelines and they are working hard to comply.

Richardson (2013) in a paper on the Causes and Consequences of Failures of Financial Institutions in Antigua and Barbuda postulated that policymakers must ensure a robust regulatory and supervisory environment exists. Richardson noted that a failed institution can be a costly venture in absence of financial safety nets .Since it is often the case that the industry is ahead of regulation and supervision, there is stronger onus on the board of directors of financial institutions to ensuring that sound

governance and oversight mechanisms are in place within these entities. Institutions ought to ensure that they operate within a manageable risk appetite

Mburu (2010) conducted a study on the determinants of performance of the SACCOs in Kenya. According to his findings, lack of business planning, conflict of interest and absence of stringent monitoring and evaluation measures are among the causes of business failure in the Sacco industry. Some of his recommendations were that the government enacts a policy that can be vital in guiding the SACCOs on strategic planning, policy to ensure that qualified staff members were employed in the SACCOs and regular audit of the SACCO. His findings mirrors on SASRA'S regulation, and is addressed by quality of staff (requirements) of auditor and requirements of board as stipulated in SASRA act 2010.

Mwalonza (2014) carried out a study on the effects of corporate governance on the performance of teachers SACCOs in Kenya; the study concluded that the size of the board and composition of the board members did affect the performance of the SACCOs. The key characteristics of the supervisory committee which affected the performance of teacher SACCOs included integrity, clarity in report provisions and the supervisory committee size. The study used survey method of research design and a semi-structured questionnaire was used to collect primary data. The key challenges faced while embracing corporate governance in Teacher SACCOs included poor leadership and management styles, inadequate finances, and poor training among the management team, corruption and lack of accountability.

Njagi et al (2013) carried out a study on the impact of front office Sacco activity (FOSAs) on Sacco Performance, with study locale being Meru South and Maara district in Tharaka Nithi County. They concluded that despite low capital, Sacco's that

operated FOSAs realized a proper and relative growth in performance compared to those that did not operate FOSAs. They suggested that Sacco's that do not operate FOSAs should be encouraged to open so that members can benefit from FOSA services. They also recommended that SASRA should assist SACCOs to open Front Office Services and bring them on regulatory authority.

Wanyoike (2013) investigated the impact of SASRA regulation of DTS in Nairobi. The finding reveals that the quality of the Board of Directors was an important aspect in improving the financial performance as per the SASRA regulations. She further opines that Sacco staff competence as required by SASRA regulations had a strong influence on the financial performance of the Sacco's in the area. Finally, corporate governance was the most significant aspect of SASRA regulations on the Sacco's financial performance in the study area, hence, needed to be emphasized in order to strengthen the operations of the Sacco's in the area. Hence, based on this findings, the study concluded that all of them were important variables of the study that needed to be addressed beginning with the most crucial which was in this case corporate governance.

## **2.6 Summary of Literature Review**

According to Gompers *et al* (2003), the relationship between corporate governance and a firm's financial performance provide little inconclusive results, however there is no clear benefit to firm's financial performance provided by independent Directors. Petra (2005) argues that the mixed results may be reflective of a corporate culture wherein corporate boards are controlled by management and the presence of independent directors has no discernable impact on management decisions. Rahman and Haniffa (2003) found out that lack of regulation influences the operations of

MFI's but the percentage of directors does not significantly affect firm financial performance. This shows that despite the studies reviewed, there still remains a research gap regarding the effect of regulation on financial performance, particularly on deposit taking institutions in Kenya.

## **CHAPTER THREE: RESEARCH METHODOLOGY**

### **3.1 Introduction**

This chapter contains the research design that was used, the target population, data collection method, data analysis and presentation.

### **3.2 Research Design**

Descriptive research design was used in this study. Descriptive research design includes surveys and fact finding enquiries of different kinds and its main purpose is to describe state of affairs as they exist (Kothari, 2004). This study used a descriptive research because it intensively described and analyzed the role of management on the financial performance of the institution.

### **3.3 Population of the study**

The population of the study was 135 DTS licensed by SASRA by January 2014. Nachmias and Nachmias (1996) defined a population as the entire set of relevant units of analysis. A survey was carried out in these DTS to establish effect of compliance to regulations on financial performance of the SACCOs. The study undertook census survey as the population of the study was small and sampling was not suitable.

### **3.4 Data Collection**

Data was collected from primary and secondary sources. Primary data was collected using a semi structured questionnaire. Researcher applied the questionnaire for the Management staff because it is a group of technocrats comprising the senior management team in the SACCO, for they have the capacity to make responses even to questions that will be of technical and professional nature.

The secondary data was also used for analysis and was collected from the financial statements of the various deposit taking SACCOs. In addition, SASRA reports were used to obtain secondary data for the financial performance variable. This was the most viable sources available and of course, only secondary sources such as those mentioned above could suffice for the analysis by virtue of the nature of the variables. For data collection, the researcher first sought an appointment with the respondents in the SACCOs. Arrangements were then made to drop questionnaires, on when and how to drop and collect questionnaires. The survey also administered through email, where emails are accessible; the respondents were sent mail with an attached questionnaire. Also, secondary data was collected from the financial performance of SACCOs/balance sheets which was accessed from published end of year results, from the period 2009 to year ending 2013. Secondary data was collected using a secondary data collection sheet.

### **3.5 Data Analysis and Presentation**

Data was collected using questionnaires which was coded and analyzed for errors; data analysis was done using both descriptive and inferential statistics. Pie charts, graphs and tables were used in data presentation. The researcher also used regression analysis to help make inferences to the Secondary data which was collected from the financial performance of Sacco's balance sheets. The regression helped researcher make inference on the nature of the relationship between the dependent variable (response) and the (explanatory) independent variable. The means of the Sacco indicators was regressed against the independent variable (SACCO Performance) to establish the dependent variable from a set of predictor variables (SASRA guidelines and growth and sustainability) and this was tested by use of SPSS software.

### **Conceptual Model**

The study was guided by a regression conceptual Equation 1.

The regression model below was used to determine the relationship.

$$Y = f(X_1 + X_2 + X_3) \dots\dots\dots 1$$

Where, Y = Dependent Variables

(X<sub>1</sub>; X<sub>2</sub>; X<sub>3</sub>)= (Protection guidelines, SACCO operations guidelines, regulatory guidelines)

### **Analytical Model**

The analytical model is represented by Equation 2 as

$$Y_{t-i} = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + e \dots\dots\dots 2$$

Where:

Y<sub>t-i</sub>= Financial Performance of the SACCO

α = the constant

B<sub>1-n</sub> = the regression coefficient or change included in Y by each χ

e = error term

X<sub>1</sub>= Liquidity

X<sub>2</sub>= Management efficiency

X<sub>3</sub>= Capital Adequacy

To complete the analysis regarding the effects of SASRA regulations on performance of SACCOs, the profitability variable was represented by the return on assets (ROA



and ROE) which was reflected by the ability of a SACCO to generate profits (surplus/deficits) from the SACCO's assets. The return on assets versus regulations guidelines were applied to measure relationship between variables.

Liquidity incorporated the ratio of net loans over deposit and short term borrowing. Higher figures denote lower liquidity. This variable measured the risk of not having sufficient reserve of cash to cope with withdrawal of deposits. Predictions vary regarding the effects of liquidity on the cost of intermediation and profitability. Alternatively, in a tight financial market where demand for credit is limited, SACCOs may be forced to raise the cost of intermediation in an attempt to increase profits.

Management efficiency is the ratio of earning assets to total assets. The higher the ratio the higher management efficiency, as SACCO managers strive for more earnings, it is likely that they would increase the cost of intermediation, which would enhance profits.

Finally, capital adequacy was a measure of the ratio of capital to total assets (CAPR) where CAPR is equal to Equity over total assets. This was in line with the act, which stipulates that Sacco societies shall maintain minimum liquid assets as prescribed by regulator. The Regression specifications fit the component data reasonably well and help in establishing effect of SASRA regulation on SACCO performance. The response on protection guidelines, SACCO operations guidelines, regulatory guidelines were measured by computing indices based on the responses derived from the Likert-Scaled questions.

## CHAPTER FOUR : DATA ANALYSIS AND INTERPRETATION

### 4.1 Introduction

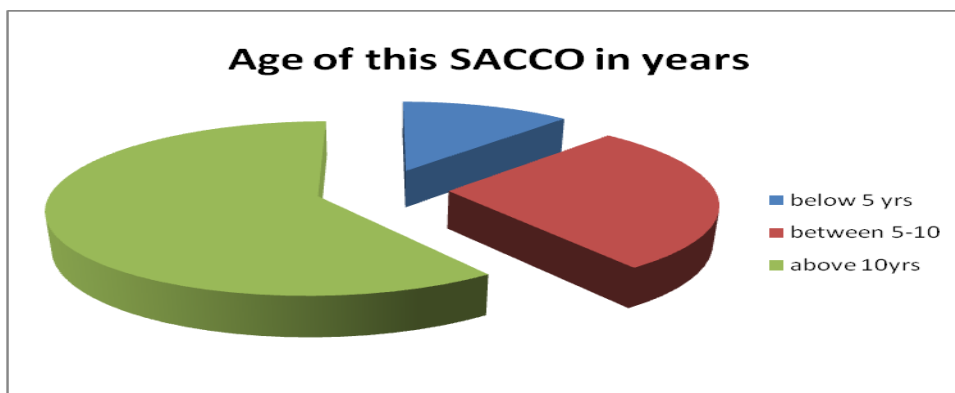
This chapter focused on the data analysis and results presentations. The study sought to determine the effect of regulations on the financial performance of deposit taking SACCOs in Kenya. The presentation of the data analysis and results was based on the sequence of research objectives.

**Table 4.1: Summary of the instrument response rate.**

Number of issued questionnaires	Number questionnaires returned	Response rate (%)
135	109	81

The study was able to get a response from 109 respondents out of the 135 questionnaires distributed to the Sacco staffs, as shown in Table 4.1; this represented a response rate of 81% which was acceptable according to (Kothari, 2004).

**Figure 4.1: represents the age of the SACCO in years**



The study sought to know the age of the SACCOs in years and from the findings, over 60% indicated that the SACCOs had been in operation for over 10 years, while

28% of the respondents indicated that the SACCOs had been in operation for between 5-10 years, whereas 12% said SACCOs existed for less than 5 years.

**Table 4.2: Location of the institution**

	Frequency	Percentages
Nairobi County	39	36
Mombasa County	12	11
Kisumu County	6	06
Others	52	48
Total	109	100

The study sought to investigate the location of the institution. From the findings, majority 36% of the respondents indicated the location of the institution was Nairobi County, 11% said Mombasa County while 06% of the respondents said that Kisumu County was the location of the institution. 48% were from other counties.

**Table 4.3: Total client's number**

	FREQUENCY	PERCENTAGE OF YES
Below 10,000	25	23
Between 10,001-20,000	35	32
Between 20,001-50,000	31	28
Between 50,001-100,000	12	11
Above 100,000	6	6
TOTAL	109	100

On the size of the clientele, the analysis was as indicated in Table 4.3 above, which indicates that 32% of the respondent SACCOs have between 10001 to 20,000 members, whereas only 6% of the SACCOs have above 100,000 membership, this shows that majority of the Sacco's are relatively medium sized

**Table 4.4: Number of Employees in SACCOs**

	Frequency	Percentages
Above 51 employees,	63	58
Between 11-50 employees	37	34
Below 10 employees	9	8
Total	109	100

In terms of number of employees the institutions had, the data was analyzed and summarized in table 4.4 which indicates that 58% of the respondents had above 63 employees in their Sacco's, whereas 34 % of Sacco's has between 11-50 employees. A partly 8% of the Sacco's had less than 10 employees. This clearly indicates that the Sacco's are relatively big in size and employs a large number of staff.

## **4.2 Policy and regulations**

### **4.2.1 Extent to which SASRA regulations have affected the SACCO on the given issues**

The study sought to know the extent to which SASRA regulations have affected the SACCO in terms of predetermined factors namely: Ownership, Corporate Governance, Accountability and image of the SACCO. From the findings in table 4.5, majority of the respondents indicated that accountability and corporate governance had a very high effect on the financial performance of the SACCO as indicated by a mean of 4.67 and 4.59 with standard deviation of 0.63 and 0.54. Most of the respondents indicated that SACCO's image and ownership has a high effect on the financial performance of SACCOs as indicated by a mean of 4.53 and 4.50 with standard deviation of 0.55 and 0.52.

**Table 4.5: How SASRA regulations have affected the SACCO on the issues listed below:**

	Mean	Standard deviation
Ownership	4.50	0.52
Corporate Governance	4.59	0.54
Accountability	4.67	0.63
SACCOs image	4.53	0.55

**Table 4.6: How Current policy and regulatory environment affected Operations on the predetermined variables.**

Effects of policy and regulatory environment on your Operations	Mean	Standard deviation
Corporate governance	4.44	0.48
Competition	4.31	0.46
Access of funds	4.70	0.67
Supervision	4.68	0.51
Performance standards	4.84	0.78
Sacco Image	4.71	0.63

Source: Survey data (2014)

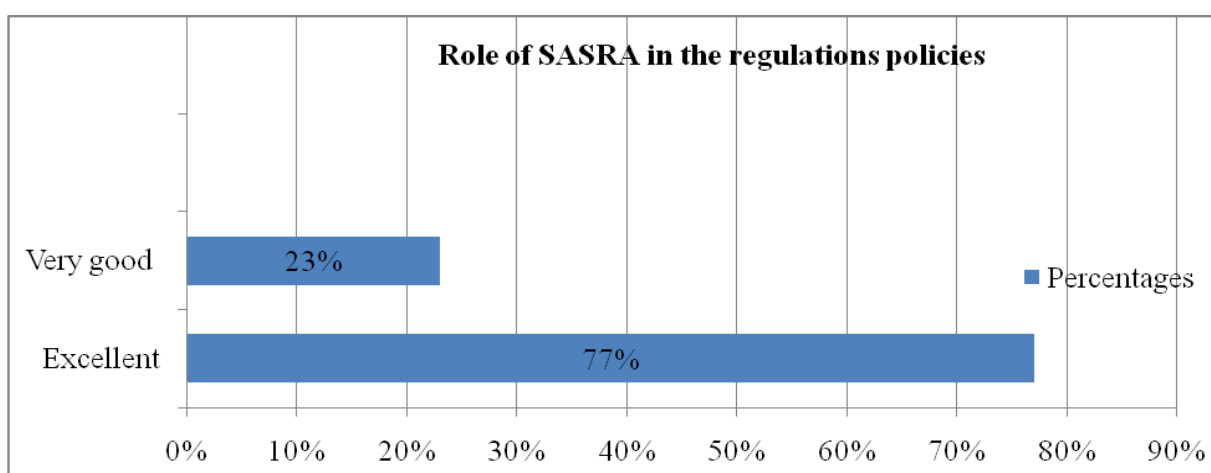
The study sought to know how the current policy and regulatory environment affected operations. From the findings, the respondents indicated that performance standards, Sacco image, access of funds and supervision affected operations and financial performance of SACCOs to a very high extent as indicated by a mean of 4.84, 4.71, 4.70 and 4.68 with standard deviation of 0.78, 0.63, 0.67 and 0.51. Most of the respondents indicated that corporate governance and competition affected operations

and financial performance of SACCOs to a high extent as indicated by a mean of 4.44 and 4.31 with standard deviation of 0.48 and 0.46.

### 4.3 Role of SASRA in the regulations policies

The study sought to know the role of SASRA in helping the institution in understanding regulations policies, and from the findings, respondents termed role of SASRA in helping the institutions in the regulations policies was rated as excellent and very good. The results are shown in figure 4.2

**Figure 4.2 Role of SASRA in the regulations policies**



Source: Survey data (2014)

**Table 4.7: Rating the overall performance of the SACCO improvement indicators**

Performance indicator	Mean	Standard deviation
Safety of members savings	4.21	0.34
Accessibility to funds	4.85	0.79
Speed of loan processing	4.57	0.44
Regular Dividend payout	4.68	0.64
Growth of SACCOs in terms of membership	4.63	0.51
Performance on loan book	4.45	0.39
Growth of SACCOs in terms of assets	4.56	0.53

Legal and regulatory framework compliance	4.80	0.73
Liabilities	4.54	0.40

Table 4.7 shows the respondents response on the rating of the overall performance of the SACCO in terms of the given aspects since SASRA legislation. From the findings, majority of the respondents indicated that there was very high improvement of accessibility to funds, legal and regulatory framework compliance, regular dividend payout and growth of SACCOs in terms of membership as indicated by a mean of 4.85, 4.80, 4.68 and 4.63 with standard deviation of 0.79, 0.73, 0.64 and 0.51. Most of the respondents indicated that there was very high improvement of speed of loan processing, growth of SACCOs in terms of assets and liabilities as indicated by a mean of 4.57, 4.56 and 4.54 with standard deviation of 0.44, 0.53 and 0.40. Most of the respondents indicated that there was high improvement of performance on loan book and safety of member's savings as indicated by a mean of 4.45 and 4.21 with standard deviation of 0.39 and 0.34.

**Table 4.8: whether SASRA prudential guidelines addressed current challenges**

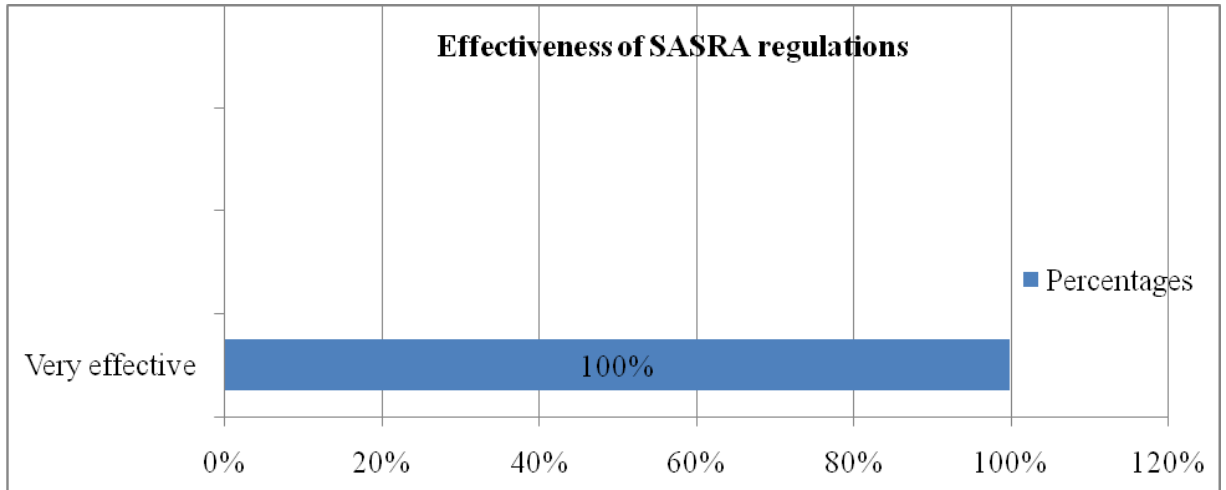
	Frequency	Percentages
Completely	67	61
Moderately	42	39
Total	109	100

Source: Survey data (2014)

The study sought to know whether the SASRA prudential guidelines address current challenges. From the findings in table 4.8 above, 61% of the respondents indicated that the guidelines completely address current challenges while 39% said to a moderate extent. From the findings, SASRA prudential guidelines address poor

governance, market structure established and regulatory framework enhancing competitiveness. The Act and Regulations include clear standards regarding among others, capital, liquidity, the extent of external borrowing, asset categorization and provisioning, maximum loan size, and insider lending.

**Figure 4.1: Effectiveness of SASRA regulations on financial performance**



The study sought to know whether the SASRA regulations have been effective on overall financial performance of the SACCO. From the findings, all the respondents indicated that SASRA regulations have been very effective on overall financial performance of the SACCO as shown in figure 4.3. This means that the respondents unanimously agreed that SASRA regulations have been very effective in improving financial performance of their SACCOs.



**Table 4.9: The Influence of Capital Regulations on SACCO Financial Performance in Year 2009**

Regression Statistics								
Multiple R	0.612858							
R Square	0.375596							
Adjusted R Square	0.152594							
Standard Error	4.643217							
Observations	32							
ANOVA								
	df	SS	MS	F	Significance F			
Regression	5	181.5601	36.31202	1.684273	0.203007			
Residual	14	301.8325	21.55947					
Total	19	483.3926						
	Coefficients	Standard Error	t Stat	P-value	Lower 95%	Upper 95%	Lower 95.0%	Upper 95.0%
Intercept	4.842	9.664938	1.53565	0.14691	35.5712	5.887226	35.5712	5.887226
X Variable 1	2.618221	4.280447	1.078911	0.298866	4.56242	13.79887	4.56242	13.79887
X Variable 2	2.0257	15.80846	0.76071	0.459451	45.9315	21.8801	45.9315	21.8801
X Variable 3	1.5954	2.573459	0.61994	0.545254	7.11492	3.924124	7.11492	3.924124

From the findings of the study in the above table, the following regression equation was established by the study for the year 2008,

The established regression equation for year 2008

$$Y=4.842+ 2.618221X_1- 2.0257X_2+1.5954 X_3 +e$$

Where Y= ROA/ROE

$B_0$ = intercept (defines value of leverage without inclusion of predictor variables)

$X_1$ = Variable 1 (Capital Ratio),  $X_2$ = Variable 2 (Liquidity) and  $X_3$ = Variable 3 (Management Efficiency)

From the findings in the above table the study found that holding profitability, growth, size, liquidity and non debt shield constant Return on Equity or Assets would be 1.5954, the study also found that a unit increase in capital ratio cause a 2.618 increase in ROA or ROE, further it was established by the study that a unit increase in liquidity led to a decrease in ROA or ROE by 2.0257 ,it was also found by the study that a unit increase in management efficiently would lead to an increase in ROA or ROE by a factor of 4.257.

**Table 4.10: The Influence of Capital Regulations on SACCO Financial Performance in Year 2009**

Regression Statistics								
Multiple R	0.775618							
R Square	0.601583							
Adjusted R Square	0.459291							
Standard Error	4.237022							
Observations	32							
ANOVA								
	df	SS	MS	F	Significance F			
Regression	5	379.4956	75.89911	4.227809	0.014942			
Residual	14	251.3329	17.95235					
Total	19	630.8285						
	Coefficients	Standard Error	t Stat	P-value	Lower 95%	Upper 95%	Lower 95.0%	Upper 95.0%
Intercept	4.6332	9.024315	1.64369	0.1225	34.1884	4.522019	34.1884	4.522019
X Variable 1	2.554705	3.874089	0.504559	0.621717	6.35439	10.2638	6.35439	10.2638
X Variable 2	-3.7412	13.90149	1.34815	0.199021	48.5569	11.0745	48.5569	11.0745
X Variable 3	2.1800	2.409864	1.0706	0.30246	7.74865	2.588641	7.74865	2.588641

From the finding of the study in the above table the following regression equation was established by the study for the year 2009.

$$Y=4.6332+ 2.554705X_1-3.7412X_2+2.1800X_3 +e$$

where Y= ROA/ROE

$B_0$ = intercept (defines value of leverage without inclusion of predictor variables)

$X_1$ = Variable 1 (Capital Ratio)

$X_2$ = Variable 2 (Liquidity)

$X_3$ = Variable 3 (Management Efficiency )

From the finding in the above table the study found that holding capital ratio, liquidity and management efficiency constant Return on Equity or Assets would be 4.6332, the study also found that a unit increase in capital ratio cause a 2.554705 increase in ROA or ROE, further it was established by the study that a unit increase in liquidity led to a decrease in ROA or ROE, it was also found by the study that a unit increase in management efficiently would led to an increase in ROA or ROE by a factor of 3.42617.

**Table 4.11: The Influence of Capital Regulations on SACCO Financial**

**Performance in Year 2010**

Regression Statistics								
Multiple R	0.477561							
R Square	0.228064							
Adjusted R Square	-0.04763							
Standard Error	3.498729							
Observations	32							
ANOVA								
	df	SS	MS	F	Significance F			
Regression	5	50.632	10.1264	0.827246	0.550968			
Residual	14	171.3755	12.2411					
Total	19	222.0075						
	Coefficients	Standard Error	t Stat	P-value	Lower 95%	Upper 95%	Lower 95.0%	Upper 95.0%
Intercept	3.91667	6.471637	-0.48159	0.637539	16.9969	10.76362	16.9969	10.76362
X Variable 1	3.421026	2.452744	0.171655	0.866165	4.83959	5.681638	4.83959	5.681638
X Variable 2	-2.12351	6.477831	-0.79093	0.442179	19.0171	8.770058	19.0171	8.770058
X Variable 3	3.54605	2.159905	-0.90479	0.380884	6.66605	2.67405	6.6505	2.67205

From the finding of the study in the above table the following regression equation was reestablished by the study for the year 2010.

$$Y = 3.91667 + 3.421026X_1 - 2.12351X_2 + 3.54605X_3 + e$$

where Y= ROA/ROE

B<sub>0</sub>= intercept (defines value of leverage without inclusion of predictor variables)

X<sub>1</sub>= Variable 1 (Capital Ratio)

X<sub>2</sub>= Variable 2 (Liquidity)

X<sub>3</sub>= Variable 3 (Management Efficiency )

From the findings in the Table 4.11, holding capital ratio, liquidity and management efficiency constant Return on Equity or Assets would be 3.91667, the study also found that a unit increase in capital ratio cause a 3.421026 increase in ROA or ROE, further it was established by the study that a unit increase in liquidity led to a decrease in ROA or ROE by 2.12351, it was also found by the study that a unit increase in management efficiency would led to an increase in ROA or ROE by a factor of 3.54605.

**Table 4.12: The Influence of Capital Regulations on Deposit Taking SACCOs Financial Performance in Year 2011**

Multiple R	0.82761							
R Square	0.68494							
Adjusted R	0.57241							
Standard	2.49392							
Observatio	32							
ANOVA								
	df	SS	MS	F	Significance			
Regression	5	189.298	37.8595	6.08708	0.00339			
Residual	14	87.0751	6.21965					
Total	19	276.373						
	Coefficie nts	Standard Error	t Stat	P-value	Lower 95%	Upper 95%	Lower 95.0%	Upper 95.00%
Intercept	5.827	5.12672	2.02521	0.06235	21.3784	0.61305	21.3784	0.61305
X Variable 1	6.327	1.93154	0.91358	0.3764	2.37813	5.90736	2.37813	5.90736
X Variable	4.80427	4.58981	4.31484	0.00071	9.96012	29.6484	9.96012	29.6484
X Variable 3	5.31574	1.25348	0.571	0.57705	3.40419	1.97272	3.40419	1.97272
Multiple R	0.82761							

From the findings of the study in the above table the following regression equation was established by the study for the year 2011.

The established regression equation

$$Y=3.91667+ 6.327X_1-4.80427+5.31574X_3$$

where Y= ROA/ROE

$B_0$ = intercept (defines value of leverage without inclusion of predictor variables)

$X_1$ = Variable 1 (Capital Ratio)

$X_2$ = Variable 2 (Liquidity)

$X_3$ = Variable 3 (Management Efficiency )

From the findings in the above table the study found that holding capital ratio, liquidity and management efficiency constant Return on Equity or Assets would be 5.827, the study also found that a unit increase in capital ratio cause a 6.327increase in ROA or ROE, further it was established by the study that a unit increase in liquidity led to a decrease in ROA or ROE by 4.80427,it was also found by the study that a unit increase in management efficiently would lead to an increase in ROA or ROE by a factor of 5.31574

#### 4.4 Regression Analysis

**Table 4.13 The Influence of Capital Regulations on SACCOs Financial Performance in Year 2012**

Regression Statistics					Significance F			
Multiple R	.0887011(a)							
R Square	.07868							
Adjusted R Square	.07645							
Standard Error	0.4797							
Observations	43				0.001			
ANOVA								
	df	SS	MS	F	Significance F			
Regression	4	50.631	10.1264	11.8272	0.015509			
Residual	39	169.3755	12.2411					
Total	43	231.0075						
	Coefficients	Standard Error	t Stat	F-value	Significance F	Upper 95%	Lower 95.0%	Upper 95.0%
Multiple R	0.90634	6.471637	5.48159	0.637530	0.0013	10.7636	16.99	10.76
X Variable 1	0.82102	2.352744	2.172655	0.866165	0.0210	5.68163	4.839	5.681
X Variable 2	0.62350	6.477831	12.79093	0.442179	0.0015	8.77005	-19.01	8.770
X Variable 3	0.44600	2.159905	15.90479	0.38088	0.0032	2.67405	6.650	2.672

The established regression equation

$$Y = 0.90634 + 0.82102X_1 - 0.62350X_2 + 0.44600X_3$$

where Y = ROA/ROE

B<sub>0</sub> = intercept (defines value of leverage without inclusion of predictor variables)

X<sub>1</sub> = Variable 1 (Capital Ratio)

X<sub>2</sub> = Variable 2 (Liquidity)

X<sub>3</sub> = Variable 3 (Management Efficiency)



From the finding in the above table the study found that holding capital ratio, liquidity and management efficiency constant Return on Equity or Assets would be 0.90634, the study also found that a unit increase in capital ratio cause a significant increase in return on Assets by  $r = 0.82102$ . The study also found that a unit increase in liquidity led to a decrease in ROA or ROE by  $r = 0.62350$ , it was also found by the study that a unit increase in management efficiently would lead to an increase in ROA or ROE by a factor of 0.44600. This implied that regulations in Deposit taking SACCOs impact positively on financial performance.

**Table 4.14: The Influence of Capital Regulations on SACCO Financial Performance in Year 2013**

Regression Statistics								
Multiple R	0.4034							
R Square	0.4361							
Adjusted R Square	0.0243							
Standard Error	0.0213							
Observations	109							
ANOVA								
	df	SS	MS	F	Significance F			
Regression	5	50.632	10.1264	0.827246	0.550968			
Residual	14	171.3755	12.2411					
Total	19	222.0075						
	Coefficients	Standard Error	t Stat	P-value	Lower 95%	Upper 95%	Lower 95.0%	Upper 15.0%
Intercept	2.454556	6.47163	-0.4815	0.694639	-16.2911	10.76331	16.6342	2.21362
X Variable 1	3.211021	2.45274	0.17165	0.034216	-4.83959	5.451612	4.2314	2.23163
X Variable 2	1.123523	6.47783	-0.7909	0.423117	-19.0171	8.223005	19.2132	3.77005
X Variable 3	0.132602	2.15990	-0.9047	0.20874	-6.16901	2.67405	3.6782	1.67205

From the findings of the study in the above table, the following regression equation was established by the study for the year 2013.

The established regression equation

$$Y = 2.454556 + 3.211021X_1 - 2.12351X_2 + 0.132602X_3 + e$$

where Y = ROA/ROE

$B_0$  = intercept (defines value of leverage without inclusion of predictor variables)

$X_1$  = Variable 1 (Capital Ratio)

$X_2$  = Variable 2 (Liquidity)

$X_3$  = Variable 3 (Management Efficiency)

From the finding in the above table the study found that holding capital ratio, liquidity and management efficiency constant Return on Equity or Assets would be 2.454556, the study also found that a unit increase in capital ratio cause a 3.211021 increase in ROA or ROE, further it was established by the study that a unit increase in liquidity led to a decrease in ROA or ROE by 1.123523, it was also found by the study that a unit increase in management efficiently would led to an increase in ROA or ROE by a factor of 0.132602.

**Table 4.15: Mean financial performance of SACCO for Year 2009, 2010, 2011, 2012 and 2013**

Financial Performance indicator	2009	2010	2011	2012	2013
ROA (Mean)	5.0	4.81	5.43	5.62	6.78
ROE (Mean)	6.30	5.51	4.9	7.27	8.34
Liq (mean)	3.45	3.17	3.76	3.51	5.57
Maneff (Mean)	6.54	7.00	10.45	11.23	12.82

The study also found that Return on Equity of the Deposit Taking SACCOs had also improved from 6.30 in the year 2009 to 8.34 in the year 2013. The study found that Capital regulation has a positive influence on Deposit Taking SACCOs' Liquidity as ratio of net loans to customer and short term funding (LOFUND) increase from 3.45 in the year 2009 to 5.57 in the year 2013. The study further found that capital

regulation by SASRA on Deposit Taking SACCOs improve management efficient where SACCOs attain a positive improvement after adoption of capital regulation from 6.54 in the year 2009, 7.00 in the year 2010, 10.45 in the year 2011, 11.23 in the year 2012 and 12.82 in the year 2013. This implied that Deposit Taking SACCOs ratio of earning assets to total assets was improving on implementation of capital regulation from regulation SASRA. The higher the ratio the higher management efficiency implied that SACCO managers were striving for more earnings which could improve profitability of the SACCOs.

**Table 4. 1 Financial Performance of SACCO Between year 2009 to 2013**

Table 2 – Summary statistics Mean		Std. Dev.	Mean before Adoption of SASRA Regulation	Mean after Adoption of SASRA Regulation	Difference in mean
Nim1	0.019	0.016	0.015	0.022	0.006*** (4.15)
Nim2	0.018	0.015	0.014	0.021	0.006*** (4.02)
ROA	0.012	0.012	0.011	0.012	0.001 (0.99)
ROE	0.129	0.127	0.141	0.219	-0.021* (-1.62)
Capratio	0.092	0.051	0.083	0.100	0.016*** (3.14)
Liq	0.451	0.133	0.405	0.487	0.081*** (6.24)
Implicit	-.0039	.0006	-.0059	-.0026	0.003** (2.62)
Maneff	0.929	0.059	-0.005	-0.002	0.003** (2.62)
Costeff	0.018	0.009	0.018	0.018	0.000 (0.06)
Reserves	0.044	0.054	0.052	0.041	-0.012* (-1.81)
Mpower	0.041	0.071	0.046	0.036	-0.009 (-1.37)
Inf	0.08	0.058	0.134	0.037	-0.096*** (-28.98)

From the finding, the NIM1 of the Deposit Taking SACCOs improve significantly from 0.015 (average of the mean ranging from 2009-2010) to 0.022 (average mean between five years 2011 to 2013). This implied that the short-term dummies of capital regulations impact significantly on the liquidity of the SACCO.

The NIM2 (Net Income Margin) improved significantly from 0.014 for 2009 to 2010 to 0.021 for the year 2012 to 2013 after adoption of capital requirements. This implied that the long-term dummy variable were statistically significant, indicating that capital regulations have a sustained long-term effect on the financial performance of Deposit Taking SACCOs. The study found that there was no significant improvement on Return on Assets for the SACCOs after adoption of the capital regulations average ROA for the SACCOs was at 0.011 for the period of 2009 to 2010 and 0.012 for the year 2012 and 2013 after adoption of the capital requirement .The study also found that there was significant improvement of Return on Equity in SACCOs after adoption of Capital requirements from SASRA as the ROE increase from 0.141 to 0.219, with a P value of 0.021 at 95% significant level. On management efficiency, the study found that capital requirement had statistically significant influence on financial performance of SACCO as it improves from -0.005 to -0.002 with a P value of 0.003 at 95% confidence level. The lagged dependent variable measures the degree of persistence in the effects of capital requirement. The lagged dependent variable is statistically significant across all models, indicating a high degree of persistence characterizing capital requirement in SACCOs and justifying the use of dynamic models.

The capital variable (capital/assets) has a positive and statistically significant effect; due to adoption of capital requirement as it increase from 0.083 to 0.100 at 95% significant level. SACCOs raise the capital adequacy to make up for a higher risk to

shareholders. This implied that well capitalized SACCOs in Kenya face lower costs of bankruptcy which facilitate a reduction in the cost of funding, hence higher profitability. Capital regulation has an impact on Liquidity which improves positively from 0.405 to 0.487 with a P value 0.081 at 99% confidence level and statistically significant. This implied that the ratio of net loans to customer and short term funding (LOFUND) is statistically significant and positively related to the profitability of domestic SACCOs, indicating a negative relationship between capital requirement and the level of liquid assets held by the SACCOs.

**Table 4.2 Effect of capital regulation on Deposit Taking SACCOs Financial Performance**

Repressors	Capratio		Caplong		Capshort	
	ROA	ROE	ROA	ROE	ROA	ROE
Intercept	-0.1463* (-3.88)	0.877* (-3.07)	-0.053* (-1.64.)	-0.512* (-1.79)	-0.054* (-1.90)	-0.601* (-1.80)
ROA&E <sub>t-1</sub>	0.479* (6.15)	0.456* (0.03)	0.567* (7.52)	0.441* (4.00)	0.579* (8.45)	0.425* (4.00)
Liq	0.001 (1.08)	0.043 (0.82)	0.004 (0.02)	0.047 (0.78)	-0.001 (-0.05)	0.005 (0.10)
Capratio	0.122* (2.27)	0.522 (0.70)	-	-	-	-
Capratio*Dumcap	-0.004 (-0.16)	-0.068 (-0.22)	-	-	-	-
Caplong	-	-	0.000 (0.02)	-0.026 (-0.79)	-	-
Bdate	-	-	-	-	0.004* (2.06)	0.059* (2.12)
Bdate1	-	-	-	-	0.002 (1.42)	0.035 (1.33)
Bdate2	-	-	-	-	0.006 (3.02)	0.077* (2.64)
Bdate3					0.002 (0.75)	0.034 (1.11)
Implicit	-0.303* (-3.50)	-0.2.63* (-3.66)	-0.357* (-4.26)	-3.011* (-4.41)	-0.313* (-4.43)	-2.657* (-4.62)
Maneff	0.097* (3.11)	0.681* (2.89)	0.053* (1.93)	0.534* (2.46)	0.048* (2.40)	0.518* (2.42)
Costeff	-0.005 (-0.005)	0.428 (0.31)	-0.115 (-0.71)	0.815 (0.57)	0.139 (1.00)	0.837 (0.61)
Markpower	0.001 (0.02)	0.074 (0.18)	-0.015 (-0.51)	-0.179 (-0.73)	-0.017 (-0.85)	-0.394* (-1.82)
Fst	0.056 (0.76)	0.333 (0.44)	-0.026 (-0.27)	-0.738 (0.404)	0.153 (1.55)	2.063* (1.77)
Inf	-0.056* (-2.34)	-0.074 (-0.39)	-0.019 (-1.03)	-0.251 (-1.18)	-0.006 (-0.40)	0.121 (0.70)
Deposit Taking SACCO conc	0.033 (1.40)	0.178 (0.75)	0.025 (0.93)	0.274 (1.14)	-0.008 (-0.29)	-0.107 (-0.31)
Hansen test	11.88	10.41	15.49	13.37	5.82	12.93
AR(1)	-2.77*	-1.73*	-2.61*	-1.70*	-2.66*	-1.65*
AR(2)	0.79	-0.88	0.63	-0.67	0.47	-1.12
N.of obs		32	32	32	32	32

\* Note: Dependant variables are ROA and ROE.

Estimation method is one-step GMM-in-System estimator.

Hansen = Hansen test for validity of over-identifying restrictions, distributed as indicated under null. AR (2) = test of null of zero second-order serial correlation, distributed  $N(0,1)$  under null. Numbers in parentheses are t-statistics indicates statistical significance at the 5% level.

To complete the analysis regarding the impact of capital regulations on financial performance of Deposit Taking SACCOs, the study determinants of Deposit Taking SACCO' profitability, as measured by the returns on assets and equity. Table 4.16 summarizes the results of the model explaining return on equity using dynamic estimation. The GMM-in-System specifications seem to fit the panel data reasonably well since the Hansen test shows no evidence of over-identifying restrictions and the second-order autocorrelation was absent.

#### **4.5 Interpretation of the Results**

The study found out that the capital regulations from SASRA regulations had a positive and significant impact on return on equity (ROE) as indicated by 3.79 in table 4.16, with a  $P = 0.0456 < 0.05\%$  meaning capital regulation significantly increase Return on equity of the SACCOs. The study also found that Capital requirement from SASRA has a positive and significant impact Return on Assets to their lag and indicated in table 4.16 by 6.15 with P Value of 0.479 at 95% significant level Figure, justifying the use of dynamic panel data modeling. Besides, this persistence of profit means the forces of competition are not sufficiently strong to cause all abnormal profits to dissipate within a one-year time span. In the present study the estimates on lagged profitability ratios ranges from 0.425 to 0.579.

The study established that capital adequacy variable (capital/assets) had a positive and significant effect on returns on assets in SACCOs as indicated by 2.27, in table 4.16 with a P Value of 0.122 at 95% significant level. This implied that has SACCOs with capital adequacy face lower costs of going bankrupt and reduce the cost of funding, resulting in higher profitability.

The study established that high capital ratio does not increase returns on equity (ROE) as indicated by 0.70. This clearly indicates that unexpected losses have been exactly offset by an increase in the capital regulations and profits through an interest margin increase. Moreover, the effect of capital regulation on Deposit Taking SACCOs' ROE was would not be sustained over time. The study by Demirguc-Kunt, Laeven, and Levine (2003) analyzes the impact of credit regulations as well as other internal determinants, which include concentration, and institutions, on MFIs profit margins. The study analyzes the impact of MFIs regulations, concentration, and institutions using bank- level data across 72 countries while controlling for a wide array of macroeconomic, financial, and bank-specific traits. Doliente (2003) investigate the determinants of net interest margins of banks in four Southeast Asian countries. Net interest margins are partially explained by bank-specific factors, namely operating expenses, capital loan quality, collateral and liquid assets.

Sacco's liquidity determines return on assets or equity significantly as indicated in Table 4.2. The study found that management efficiency had positive and significant effect on SACCO's profits Return on Assets and Equity. The study found that capital requirement had a positive and significant effects management Efficiency which would influence Return on Assets of Deposit Taking SACCOs as indicated by 3.11 in table 4.16 with a P Value 0.097 at 99% level of significant Level, The study found that influence of Capital requirement in SACCOs influence SACCOs Return on



Equity by 2.89 with a P Value of 0.682 at 99% level of confidence. This implied that SACCOs with capital adequacy face lower costs of going bankrupt and reduce the cost of funding, resulting in higher profitability. Athanosoglou, Brissimis, and Delis (2005) investigated, in a single-equation framework, the effect of capital adequacy on MFIs profitability. Using dynamic estimation technique, Goddard, Molyneux, and Wilson (2004) study the determinants of profitability of European MFIs. They find a significant persistence of abnormal profits from year to year and a positive relationship between the capital-asset ratio and profitability. Higher leverage or a low equity/asset ratio reduces the agency costs of outside equity and increases its value by constraining or encouraging managers to act more in the interest of shareholders. Hence, capital regulations on risk taking can mitigate conflicts between shareholders and credit union managers concerning the choice of investment and improve bank's performance.

## **CHAPTER FIVE : SUMMARY, CONCLUSION AND RECOMMENDATIONS**

### **5.1 Introduction**

This chapter presented summary, conclusions and recommendations of the findings based on the objective of this study was to determine the effect of regulations on the financial performance of Deposit Taking SACCOs in Kenya.

### **5.2 Summary and Conclusions**

This section presents the findings from the study in comparison to what other scholars say as noted under literature review. It looks at the effects of regulation on financial performance of SACCOs.

#### **5.2.1 Effect of regulation on financial performance of Deposit Taking SACCOs**

The main objective was designed to establish the effect of regulation on financial performance of the SACCO's. This was established by analyzing the individual components of financial performance as measured by return on assets or equity. The results provide a clear illustration of the effects of SASRA regulations on the cost of intermediation and SACCOs' profits, as referenced in Table 4.15. Further, from figure 4.3 all the respondents were in agreement that SASRA regulations have been very effective on financial performance of the SACCOs.

As the capital adequacy ratio internalizes the risk for shareholders as indicated in Table 4.15, Deposit Taking SACCOs significantly increases the operation cost, which supports higher return on assets and equity. These effects appeared to increase significantly and progressively over time as indicated in Table 4.9, 4.10 and 4.16 respectively, starting in the period in which capital regulations were introduced and continued one year after the implementation.

### **5.2.2 Management efficiency**

The empirical estimation unveiled interesting features about the effects of Deposit Taking SACCO banking-specific and macro variables on the performance of Deposit Taking SACCOs in Kenya. From Table 4.15, Management efficiency was found to increase Deposit Taking SACCO return on assets and Return on Equity with the implementation of the SASRA Regulation. The study found that a unit increase in management efficiency increased ROA. The study also found that management efficiency had positive and significant effect on Deposit Taking SACCO's profits, Return on Assets and Equity. As indicated in Table 4.09, to Table 4.15, shareholders benefit directly from improvement in management efficiency.

### **5.2.3 Liquidity**

The study established that increase in liquidity led to a decrease in ROA. Sacco's liquidity determines return on assets or equity significantly as indicated in table 4.8. Further, a unit increase in liquidity led to a decrease in ROA by 2.0257. The study found that Capital regulation has a positive influence on Deposit Taking SACCOs' Liquidity as ratio of net loans to customer and short term funding (LOFUND) increase from 3.45 in the year 2009 to 5.57 in the year 2013, as shown in Table 4.15

### **5.2.4 Capital adequacy**

The study established that SACCO regulations have positive impact on capital ratio and led to an increase in ROA. Table 4.16 shows that influence of Capital requirement in SACCOs influences return on Equity by 2.89 with a P Value of 0.682 at 99% level of confidence. This implied that SACCOs with capital adequacy face lower costs of going bankrupt and reduce the cost of funding, resulting in higher profitability. This clearly indicates that Return on assets increased due to the implementation of SASRA

regulations, to sum, a number of factors that contributed positively to Deposit Taking SACCO' profitability. Among the macro variables, inflation proved to be an important factor that depresses the cost of intermediation in an effort to stimulate demand for credit. A pickup in output growth appears to be the most important factor that increases demand for credit, enabling Deposit Taking SACCO to charge a higher cost of operation.

### **5.3 Conclusions**

The study concluded that higher capital requirements, and increase in management efficiency led significantly positive to Deposit Taking SACCOs' profitability in the post- capital regulation period. Countering effects on Deposit Taking SACCOs' profitability were attributed to the reduction in economic activity and, to a lesser extent, to the reduction in reserves.

The study concluded that capital regulation significantly improve management efficiency which impacted positively on profitability. This was due to increase in management efficiency is likely to have been absorbed in Deposit Taking SACCOs' fees and commissions. There is also a general belief that SASRA prudential guidelines completely addressed the current Sacco challenges as seen from the study. Respondents rated the SASRA highly with respect to addressing their current challenges as seen in table 4.8

The study finally concluded that importance of capital regulation significantly influence liquidity management resulting into significantly and positive increase in profitability Deposit Taking SACCOs and financial stability in Kenya and that the state of the economy was a major factor that determines the performance of the Sacco's. The study concluded that financial stability could be at risk as a result of

shocks impinging on the economic system, absent proper policy adjustments to mitigate the effects of these shocks.

The study concluded that SACCO regulations had significant positive impact on increase in ROE in Deposit Taking SACCOs. This implied that Capital requirement in SACCOs influences Return on Equity and SACCOs with capital adequacy face lower costs of going bankrupt and reduce the cost of funding, resulting in higher profitability

The study concluded that increase in liquidity led to a significant decrease in ROA. SACCO's liquidity determines return on assets or equity significantly due to increase in liquidity led to a decrease in ROA. The study also concluded that Capital regulation significantly increase Deposit Taking SACCOs' Liquidity as ratio of net loans to customer and short term funding (LOFUND) increase.

#### **5.4 Limitations of the Study**

The study faced a number of limitations, especially obtaining data from the SASRA and SACCOs was quite difficult. Management in the SASRA and the SACCOs were uncooperative, however the researcher explained that the data that was to be obtained was for academic purpose only. In attaining its objective the study was limited to 109 SACCOs which are registered with SASRA for 5 year from whose data was sourced. The study was also limited to the degree of precision of the data obtained from the SACCOs financial reports.

The study also faced challenges of time, limiting the study from collecting information for the study particularly where respondents delayed in returning the

questionnaire. To mitigate this, the researcher made follow up and enhanced quick feedback from the respondents.

The period of study was limited to five years. The SASRA regulations have been implemented in Deposit SACCOs for five years hence SACCOs management has been in a period of adjustment. This could have affected the financial performance of Deposit Taking SACCOs. SASRA regulations were also enacted in 2008 thus there's lack of enough material since a lot of research has not been conducted in this area.

### **5.5 Recommendation of the Study**

The study recommends that regulatory reforms should aim at increasing more competition in the deposit taking Sacco-sector, rather than to discourage entry and competition. The performance indicators were commensurate with the optimal practices of the intermediation function that guarantees financial stability over time providing a high and strong demand for credit.

The Government should review and SASRA should review legal and regulatory framework to ensure all Sacco's, both deposit taking and non deposit taking Sacco's to be brought under one regulatory body. This will be vital for Non deposit taking Sacco's to open deposit taking services. It further recommends that SASRA should enforce regulatory and prudential guidelines and monitor adherence to the same in SACCOs, hence, improved financial performance and growth of deposit taking SACCOs.

### **5.6 Suggestions for Further Study**

From the study, the directions for future research regarding regulation and financial performance of SACCOs are recommended to be done on other factors affecting the

financial performance of SACCOs in Kenya. Further, a study should be done to assess the impact of regulations, cost of intermediation and growth of Deposit Taking SACCOs in Kenya. Finally, a study to investigate the likely impact of proposed merger of all financial regulators in Kenya under one regulator; this forms an area of study to look at financial effects of such proposals on performance and growth of SACCO sub-sector.

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## **APPENDICES**

### **APENDIX 1: LETTER OF INTRODUCTION**

UNIVERSITY OF NAIROBI

SCHOOL OF BUSINESS

TO ALL RESPONDENTS,

Dear Sir/Madam,

**RE: EFFECT OF REGULATIONS ON THE FINANCIAL PERFORMANCE OF  
DEPOSIT TAKING SAVINGS AND CREDIT COOPERATIVE SOCIETIES  
IN KENYA**

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I am a post graduate student at the University of Nairobi pursuing Master of business Administration degree in Finance. I am carrying out a research for a study as referenced above, among the Deposit Taking SACCOs (DTS) in Kenya in partial fulfillment of the requirements for the award of the degree.

I kindly request you to fill the attached questionnaire to enable me to gather the required information. My supervisor and I assure you that this information will be used purely for academic purposes and your name will not be mentioned in the report. A copy of final project shall be availed to you upon request. Your cooperation will be highly appreciated and thanking you in advance.

Yours faithfully,

Elishaphan Onguka,

MBA Student,

University Of Nairobi.

## APPENDIX 2: QUESTIONNAIRE

### Introduction

Dear respondent, the purpose of this questionnaire is to get the actual scenario of your SACCO regarding the topic addressed purely for academic proposes. Please read the statement and give the response that represents your most honest opinion. The information so given will be accorded the confidentiality it deserves and not used for any other purpose other than for the research. Your name should not appear on the questionnaire. Kindly respond to all the items.

### Instructions

1. Do not write your name on the questionnaire.
2. Please respond to all the questions accurately and honestly.
3. You should respond by ticking [] the appropriate spaces and filling the spaces that have been provided.

### Part A: Background information

This section of the questionnaire refers to background information. Although we are aware of the sensitivity of the questions in this section, the information will allow us to compare groups of respondents

1. What is the name of the SACCO.....
2. What is the age of this SACCO in years? (Tick  where appropriate)  
Below 5 years [  ]  
Between 5-10 [  ]  
Above 10 years [  ]
3. Location of the institution (Tick  where appropriate)  
Nairobi County [  ] Kisumu County [  ] Mombasa County [  ] others [  ]  
.....
4. Total client number (Tick  where appropriate)

Below 10,000 [ ] Between 10,001-20,000 [ ] Between 20,001-50,000 [ ]  
 Between 50,001-100,000 [ ] Above 100,000[ ]

5. How many employees do you have (Tick  $\checkmark$  where appropriate)

Below 10 [ ] Between 11-50 [ ] Above 51 [ ]

### Section B. Policy Regulations

This section of the questionnaire explores knowledge and effect of policy regulations as set out by SASRA Act.

6. To what extent has SASRA regulations affected your institution in the following listed areas ([ $\checkmark$ ] Tick the appropriate degree of influence)

[1] No effect [2] Low effect [3] Moderate effect [4] High effect [5] Very High effect

	Effect on	1	2	3	4	5
i	Ownership					
ii	Corporate Governance					
iii	Accountability					
iv	SACCOs image					

7. How has the current policy and regulatory environment affected your Operations

([ $\checkmark$ ] Tick the appropriate degree of influence)

[1] No effect [2] Low effect [3] Moderate effect [4] High effect [5] Very High effect

	Effects of policy and regulatory environment on your Operations	1	2	3	4	5
i	Corporate governance					
ii	Competition					
iii	Access of funds					
iv	Supervision					
v	Performance standards					
vi	Sacco Image					

8. Do you think the role played by SASRA in helping the SACCO in meeting the regulations policies can be rated as (tick [√])

[1] Poor      [2] Fair      [3] good      [4] Very good      [5] Excellent

9. On a scale of 1 to 5 please rate the overall performance of the SACCO improvement in terms of the following aspects since SASRA legislation. (Where 1 is no improvement and 5 is very high improvement).

	Performance indicator	1	2	3	4	5
i	Safety of members savings					
ii	Accessibility to funds					
iii	Speed of loan processing					
iv	Regular Dividend payout					
v	Growth of SACCOs in terms of membership					
vi	Performance on loan book					
vii	Growth of SACCOs in terms of assets					
viii	Legal and regulatory framework compliance					
ix	Liabilities					

10. Has the SASRA prudential guidelines addressed your current challenges

[ 1 ] completely [ 2 ] moderately [ 3 ] Just a little [ 4 ] not at all [ 5 ] don't know

13. Overall, how do you think SASRA regulations have been effective on overall financial performance of the SACCO?

(i). Very Effective

(ii).Effective

(iii).Fairly effective

(iv).Ineffective

**Thank you for taking your time to fill this questionnaire.**

### APPENDIX 3: LIST OF DEPOSIT TAKING SACCO SOCIETIES

NO	NAME OF SCOCIETY	POSTAL ADDRESS
1.	AFYA SACCO SOCIETY LTD	P.O BOX 11607-00400, NAIROBI
2.	AIRPORTS SACCO SOCIETY LTD	P.O BOX 19001-00501, NAIROBI
3.	ASILI SACCO SOCIETY LTD	P.O BOX 49064-00100, NAIROBI
4.	BANDARI SACCO SOCIETY LTD	P.O BOX 95011-80104, MOMBASA
5.	BARAKA SACCO SOCIETY LTD	P.O BOX 1548-10101 KARATINA
6.	BIASHARA SACCO SOCIETY LTD	P.O BOX 1895-10100, NYERI
7.	BINGWA SACCO SOCIETY LTD	P.O BOX 434-10300, KERUGOYA
8.	BORESHA SACCO SOCIETY LTD	P.O BOX 80-2103 ELDAMA- RAVINE
9.	BURETI SACCO SOCIETY LTD	P.O BOX 601-20210, LITEIN
10.	BUSIA TESO TEACHERS SACCO SOCIETY LTD	P.O BOX 448-50400, BUSIA
11.	CAPITAL SACCO SOCIETY LTD	P.O BOX 1479-60200, MERU
12.	CENTENARY SACCO SOCIETY LTD	P.O BOX 1207-60200, MERU
13.	CHAI SACCO SOCIETY LTD	P.O BOX 278-00200, NAIROBI
14.	CHEMELIL SACCO SOCIETY LTD	P.O BOX 14-40112, AWASI
15.	CHEPSOL SACCO SOCIETY LTD	P.O BOX 81-20225, KIMULOT
16.	CHUNA SACCO SOCIETY LTD	P.O BOX 30197-00100, NAIROBI
17.	COMOCO SACCO SOCIETY LTD	P.O BOX 30135-00100, NAIROBI
18.	COSMOPOLITAN SACCO SOCIETY LTD	P.O BOX 1931-20100, NAKURU
19.	COUNTY SACCO SOCIETY LTD	P.O BOX 21-60103, RUNYENJES
20.	DAIMA SACCO SOCIETY LTD	P.O BOX 2032-60100, EMBU
21.	DHABITI SACCO SOCIETY LTD	P.O BOX 353-60600, MAUA
22.	DIMKES SACCO SOCIETY LTD	P.O BOX 886-00900 KIAMBU
23.	EGERTON UNIVERSITY SACCO SOCIETY LTD	P.O BOX 178-20115, EGERTON
24.	ENEA SACCO SOCIETY LTS	P.O BOX 1836-10101, KARATINA
25.	FARIJI SACCO SOCIETY LIMITED	P.O BOX 589-00216, GITHUNGURI
26.	FORTUNE SACCO SOCIETY LTD	P.O BOX 599-10300, KERUGOYA
27.	FUNDILIMA SACCO SOCIETY LTD	P.O BOX 6200-0200, NAIROBI
28.	GITHUNGURI DAIRY & COMMUNITY SACCO SOCIETY LTD	P.O BOX 896-00216 GITHUNGURI

29.	GUSSI MWALIMU SACCO SOCIETY	P.O BOX 1335-40200 KISII
30.	HARAMBEE SACCO SOCIETY LTD	P.O BOX 47815-00100, NAIROBI
31.	HAZINA SACCO SOCIETY LTD	P.O BOX 59877-00200, NAIROBI
32.	IMARIKA SACCO SOCIETY LTD	P.O BOX 712-80108 KILIFI
33.	IMARISHA SACCO SOCIETY LTD	P.O BOX 682-20200, KERICHO
34.	IMENTI SACCO SOCIETY LTD	P.O BOX 3192-60200, MERU
35.	ISIOLO TEACHERS SACCO SOCIETY LTD	P.O BOX 105-60300, ISIOLO
36.	JAMII SACCO SOCIETY LTD	P.O BOX 57929-00200, NAIROBI
37.	JIJENGE SACCO SOCIETY LTD	P.O BOX 6222-00100, THIKA
38.	KAKAMEGA TEACHERS SACCO SOCIETY LTD	P.O BOX 1150-50100, KAKAMEGA
39.	KEIYO TEACHERS SACCO SOCIETY LTD	P.O BOX 512-30700, ITEN
40.	KENPIPE SACCO SOCIETY LTD	P.O BOX 314-00500, NAIROBI
41.	KENVERSITY SACCO SOCIETY LTD	P.O BOX 10263-00100, NAIROBI
42.	KENYA ACHIEVAS SACCO SOCIETY LTD	P.O BOX 30800-40200, NAIROBI
43.	KENYA BANKERS SACCO SOCIETY LTD	P.O BOX 73236-00200 NAIROBI
44.	KENYA CANNERS SACCO SOCIETY LTD	P.O BOX 1124-01000, THIKA
45.	KENYA HIGHLANDS SACCO SOCIETY LTD	P.O BOX 2085-002000, KERICHO
46.	KENYA MIDLAND SACCO SOCIETY LTD	P.O BOX 287, BOMET
47.	KENYA POLICE STAFF SACCO SOCIETY LTD	P.O BOX 51042-00200, NAIROBI
48.	KIAMBAA DAIRY RURAL SACCO SOCIETY LTD	P.O BOX 669-00219, KARURI
49.	KINGDOM SACCO SOCIETY LTD	P.O BOX 8017-00300, NAIROBI
50.	KIPSIGIS EDIS SACCO SOCIETY LTD	P.O BOX 228, BOMET
51.	KITE SACCO SOCIETY LTD	P.O BOX 2073-40100, KISUMU
52.	KITUI TEACHERS SACCO SOCIETY LTD	P.O BOX 254-90200, KITUI
53.	KMFRI SACCO SOCIETY LTD	P.O BOX 80862-MOMBASA
54.	KONOIN SACCO SOCIETY LTD	P.O BOX 83-20403 MOGOGOSIEK
55.	K-UNITY SACCO SOCIETY LTD	P.O BOX 268-00900, KIAMBU
56.	LAIKIPIA TEACHERS SACCO SOCIETY LTD	P.O BOX 414-10400, NANYUKI
57.	LENGO SACCO SOCIETY LTD	P.O BOX 371-80200, MALINDI
58.	MAGADI SACCO SOCIETY LTD	P.O BOX 13-00205, MAGADI
59.	MAGEREZA SACCO SOCIETY LTD	P.O BOX 53131-00200, NAIROBI

60.	MAISHA BORA SACCO SOCIETY LTD	P.O BOX 30062-00100, NAIROBI
61.	MARAKWET TEACHERS SACCO SOCIETY LTD	P.O BOX 118-30705, KAPSOWAR
62.	MARSABIT TEACHERS SACCO SOCIETY LTD	P.O BOX 90-60500, MARSABIT
63.	MENTOR SACCO SOCIETY LTD	P.O BOX 789-10200, MURANGA
64.	MERU SOUTH FARMERS SACCO SOCIETY LTD	P.O BOX 514-60400, CHUKA
65.	METROPOLITAN SACCO SOCIETY LTD	P.O BOX 871-00900, KIAMBU
66.	MILIKI SACCO SOCIETY LTD	P.O BOX 43582-00100, NAIROBI
67.	MMH SACCO SOCIETY LTD	P.O BOX 469-60600, MAUA
68.	MOMBASA PORT SACCO SOCIETY LTD	P.O BOX 95372-80104, MOMBASA
69.	MOMBASA TEACHERS SACCO SOCIETY LTD	P.O BOX 86515-80100, MOMBASA
70.	MUDETE TEA GROWERS SACCO SOCIETY LTD	P.O BOX 221-50104, KAKAMEGA
71.	MUHIGA SACCO SOCIETY LTD	P.O BOX 83-10300, KERUGOYA
72.	MURATA SACCO SOCIETY LTD	P.O BOX 816-10200, MURANGA
73.	MWALIMU NATIONAL SACCO SOCIETY LTD	P.O BOX 62641-00200 NAIROBI
74.	MWITO SACCO SOCIETY LTD	P.O BOX 56762-00200, NAIROBI
75.	NACICO SACCO SOCIETY LTD	P.O BOX 34525-00100, NAIROBI
76.	NAFAKA SACCO SOCIETY LTD	P.O BOX 30586-00100, NAIROBI
77.	NAKU SACCO SOCIETY LTD	P.O BOX 78355-00507, NAIROBI
78.	NANDI HEKIMA SACCO SOCIETY LTD	P.O BOX 211-30300, KAPSABET
79.	NAROK TEACHERS SACCO SOCIETY LTD	P.O BOX 158-20500, NAROK
80.	NASSEFU SACCO SOCIETY LTD	P.O BOX 43338-00100, NAIROBI
81.	NATION SACCO SOCIETY LTD	P.O BOX 22022-00400, NAIROBI
82.	NAWIRI SACCO SOCIETY LTD	P.O BOX 400-16100, EMBU
83.	NDEGE CHAI SACCO SOCIETY LTD	P.O BOX 857-20200, KERICHO
84.	NDOSHA SACCO SOCIETY LTD	P.O BOX 532-60401, CHOGORIA
85.	NG'ARISHA SACCO SOCIETY LTD	P.O BOX 1199-50200, BUNGOMA



86.	NITUNZE SACCO SOCIETY LTD	P.O BOX 295-50102, MUMIAS
87.	NRS SACCO SOCIETY LTD	P.O BOX 572-00902, KIKUYU
88.	NTIMINYAKIRU SACCO SOCIETY LTD	P.O BOX 3213-60200, MERU
89.	NYAHURURU SACCO SOCIETY LTD	P.O BOX 2183-20300, NYAHURURU
90.	NYALA VISION SACCO SOCIETY LTD	P.O BOX 27-20306 NDARAGWA
91.	NYAMBENE ARIMI SACCO SOCIETY LTD	P.O BOX 493-60600, MAUA
92.	NYAMIRA SACCO SOCIETY LTD	P.O BOX 633-40500, NYAMIRA
93.	NYERI TEACHERS SACCO SOCIETY LTD	P.O BOX 1939-10100, NYERI
94.	ORIENT SACCO SOCIETY LTD	P.O BOX 1842-01000, THIKA
95.	PUAN SACCO SOCIETY LTD	P.O BOX 404-20500, NAROK
96.	SAFARICOM SACCO SOCIETY LTD	P.O BOX 66827-00800, NAIROBI
97.	SHERIA SACCO SOCIETY LTD	P.O BOX 34390-00100, NAIROBI
98.	SIMBA SACCO SOCIETY LTD	P.O BOX 977-20200, KERICHO
99.	SIRAJI SACCO SOCIETY LTD	P.O BOX PRIVATE BAG, TIMAU
100.	SKYLINE SACCO SOCIETY LTD	P.O BOX 660-20103, ELDAMARAVINE
101.	SOLUTION SACCO SOCIETY LTD	P.O BOX 1694-60200, MERU
102.	SOT TEA SACCO SOCIETY LTD	P.O BOX 251-20400, NAIROBI
103.	SOTICO SACCO SOCIETY LTD	P.O BOX 959-20406, SOTIK
104.	STAKE KENYA SACCO SOCIETY LTD	P.O BOX 208-40413, KEHANYCHA
105.	STIMA SACCO SOCIETY LTD	P.O BOX 75629-00100, NAIROBI
106.	SUKARI SACCO SOCIETY LTD	P.O BOX 841- 50102, MUMIAS
107.	SUPA SACCO SOCIETY LTD	P.O BOX 271-200600, MARALAL
108.	TAI SACCO SOCIETY LTD	P.O BOX 718-00216, GITHUNGURI
109.	TAIFA SACCO SOCIETY LTD	P.O BOX 1649-10100, NYERI
110.	TAITA TAVETA SACCO SOCIETY LTD	P.O BOX 1186-30304, WUNDANYI
111.	TARAJI SACCO SOCIETY LTD	P.O BOX 605-40600, SIAYA
112.	TEMBO SACCO SOCIETY LTD	P.O BOX 91-00618, NAIROBI
113.	TENHOS SACCO SOCIETY LTD	P.O BOX 391-20200, BOMET
114.	THAMANI SACCO SOCIETY LTD	P.O BOX 467-60400, CHUKA
115.	THARAKA NITHI TEACHERS SACCO SOCIETY LTD	P.O BOX 15-60400 CHUKA
116.	TIMES SACCO SOCIETY LTD	P.O BOX 310-60202, NKUBU
117.	TOWER SACCO SOCIETY LTD	P.O BOX 269-20303, OL KALAU
118.	TRANS NATIONAL SACCO SOCIETY	P.O BOX 2274-300200,

	LTD	KITALE
119.	UFANISI SACCO SOCIETY LTD	P.O BOX 2973-00200, NAIROBI
120.	UKRISTO NA UFANISI SACCO SOCIETY LTD	P.O BOX 872-00605, NAIROBI
121.	UKULIMA SACCO SOCIETY LTD	P.O BOX 44071-00100, NAIROBI
122.	UNAITAS SACCO SOCIETY LTD	P.O BOX 1145-10200, MURANGA
123.	UNITED NATIONS SACCO SOCIETY LTD	P.O BOX 30552-00100, NAIROBI
124.	UNIVERSAL TRADERS SACCO SOCIETY LTD	P.O BOX 2119-90100, NAIROBI
125.	VISION POINT SACCO SOCIETY LTD	P.O BOX 42-40502 NYANSIONGO
126.	WAKENYA PAMOJA SACCO SOCIETY LTD	P.O BOX 829-40200, KISII
127.	WAKULIMA SACCO SOCIETY LTD	P.O BOX 232-10103, NYERI
128.	WANAANGA SACCO SOCIETY LTD	P.O BOX 34680-00501 NAIROBI
129.	WANANCHI SACCO SOCIETY LTD	P.O BOX 910-10106, OTHAYA
130.	WANANDEGE SACCO SOCIETY LTD	P.O BOX 19074-00501 NAIROBI
131.	WARENG SACCO SOCIETY LTD	P.O BOX 3466-30100, ELDORET
132.	WASHA SACCO SOCIETY LTD	P.O BOX 83256-80100, MOMBASA
133.	WAUMINI SACCO SOCIETY LTD	P.O BOX 66121-00800, NAIROBI
134.	WINAS SACCO SOCIETY LTD	P.O BOX 696-60100, EMBU
135.	YETU SACCO SOCIETY LTD	P.O BOX 511-60202, NKUBU

(Source: SASRA, 2014)