TRADE CREDIT AS A SOURCE OF FINANCE FOR THE MOTOR SECTOR IN KENYA: THE CASE OF GENERAL MOTORS EAST AFRICA LIMITED AND HER DISTRIBUTORS.

BY

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DECLARATION

This research is my original work and has not been presented for a degree assessment in any other university.

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This Research has been submitted for examination with my approval as Supervisor.
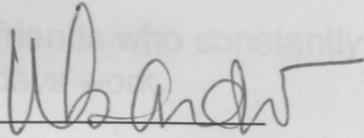
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DEDICATION

This project is dedicated my Josephine my wife and the boys Mark, Andrew and Emmanuel who bore the blunt of my unavailability at home as I attended evening and weekend classes, and studied at home instead of availing time to them.

To my parents for all the sacrifices she made to ensure that I got educated despite her not having attended any formal schooling.

To all my friends who constantly encouraged me to continue reading despite long and hard days work.

TABLE OF CONTENTS

ACKNOWLEDGEMENTS

Definition of Terms

When deciding whether to grant trade credit or not, a firm must make a decision on the credit standards, Credit terms and the Collection efforts. Each of these is defined below;

Credit standards: - These are criteria to decide the types of customers to whom goods could be sold on credit. If a firm has more slow-paying customers, its investment in accounts receivables will increase.

Credit-terms: - These specify duration of credit and terms of payment by customers. Investment in Trade Credit will be high if customers are allowed extended time period for making payments.

Collection efforts: - These determine the actual collection period. The lower the collection period, the lower the investment in Trade Credit and vice versa.

Not all customers are credit worth. Each customer has to be evaluated based on his own merit based on the five C's of credit: character, capacity, capital, collateral, and conditions. These are defined below;

Character has to do with the customer's willingness to pay. The probability that the customers will make honest efforts to honor their credit obligations is measured by their character. The moral factor is of considerable importance in credit evaluation in practice.

Capacity describes a subjective judgment of the customers' ability to pay. It is gauged by the customers' past business performance record, supplemented by physical observation of the plant or store and business methods.

Capital is measured by the general financial position of the firm as indicated by a financial ratio analysis, with special emphasis on the tangible net worth of the enterprise.

Collateral is represented by assets offered by the customer as a pledge for security of the credit extended.

Conditions have to do with the impact of the prevailing and general economic trends on the firm or special developments in certain areas of the economy that may affect the customer's ability to meet the obligation.

ABSTRACT

This study was done to determine the reasons as to why trade credit was extended to General Motors East Africa Ltd by its suppliers of materials, to her customers, dealers and distributors. To understand whether there existed a formal process that General Motors East Africa Ltd followed in assessing each customer for trade credit capacity and finally the application of trade credit funds to those who received them.

Data was collected through a drop and pick questionnaire. Interviews of critical people who were involved in credit management in each of the organizations were conducted. The credit policies were also examined. The data was analyzed using SPSS at zero correlation done at 0.05 significant levels.

The study concluded that trade credit was offered where bank credit was unavailable or limited and very expensive. It was used to match production life cycles, to match customer demands. All the respondents indicated the existence of trade credit policies and 85% of them had been reviewed in the last one year and the balance was current at time of the study. 71% of the respondents indicated that trade credit had been extended in some instances due to management influence. This brought moral hazard in the trade credit practice and may explain why there was a high level of bad debts provisions and write offs. Racial and tribal bias in the allocation of dealerships and distributors was noted as a basis for granting of trade credit.

Most firms have written down trade credit policies a formal way of credit risk evaluation and risk ranking. The legal framework was said to be slow and ineffective. The results from this study therefore supported the transactions, costs and financial theories of trade credit and that the production cycle can influence the use trade credit especially where it is used for purchases.

Abbreviations

AJS	-	A Jiwa Shamji Limited
AM	-	Associated Motors Limited
AAC	-	Associated Auto Center Limited
CFG	-	Central Farmers Garage Limited
CFC	-	Central Finance Corporation
CKD	-	Completely Knocked Down Kits
CBU	-	Completely Built Units
CMC	-	Cooper Motor Corporation
GMC	-	General Motors Corporation
GMEA	-	General Motors East Africa Limited
ICDC	-	Industrial Commercial Development Corporation
ICDC IC	-	Industrial Commercial Development Investment Corporation
KCI	-	Kenya Coach Industries Limited
KMI	-	Kenya Motor Industry
RM	-	Ryce Motors Limited
TMD	-	Thika Motors Dealers Limited
USA	-	Unites States of America

CHAPTER ONE

1.0 INTRODUCTION

1.1 BACKGROUND INFORMATION

In their 1999 book, Corporate Finance and Investment Decisions and Strategies, Pike and Neale described trade credit as finance obtained from the suppliers of goods and services over a period of time, the payment of those goods and services being made after the goods have been delivered or consumption of the services offered has taken place.

Pandey (1999) stated that trade credit occurred when a firm sold its products and services on credit. He observed that trade credit was an essential marketing tool that acted as a bridge for the movement of goods through production and distribution stages to the final customers. Trade credit could be extended when a firm is facing severe competition, to attract potential customers and to act as a marketing tool for firms with depressed or excess inventories to publicize it and expand its sales.

The ability to extend trade credit is influenced by a company's financial position and could be seen as a way of signaling information in the market or to specific buyers about the firm's products, financial strengths, future prospects and its commitment to the industry.

The bargaining power of large customers and their working capital influenced their demand for trade credit and hence the need to vary their trading terms by suppliers so as to attract customers in a bid to achieve specific marketing aims.

Pandey observed that customer relationship with a firm that has ability to offer trade credit was critical. Customers who are strong in their supplier relationships tend to get more trade credit than those in weak relationships. The suppliers extend trade credit to build long term relationships with their dealers or customers. Trade credit would be extended to cater for transit delays. Suppliers may extend trade credit to cushion their customers against any cash flow effects due to delays in the distribution channel. Industry practices and norms would influence whether a supplier was extend trade credit to his customers or not and would impact on the way trade credit is administered.

Biggs et al, (1996) used a 1993 survey of Kenya on the enforcement of contracts in an Africa credit market and stated that access to trade credit in Kenya increased with the firm size and that it is positively influenced by the owner being from an Asian origin. The study found that Asian owners had a better access to trade credit than African counterparts and that only relatively large African owners try to seek trade credit.

Petersen and Rajan (1997) outlined the various reasons on why trade credit is used. They observed that more trade credit was be used where banking institutions do not offer enough credit facilities to various sectors of the economy. It can be used both for medium and short term financing needs of most customers and therefore acted as a last resort to reduce transaction costs. Suppliers may lend to firms that no one else may extend trade credit to. This is because they have comparative advantage in form of being able to cut supplies,

repossess sold goods in cases where collaterals exists and they have all the relevant information about the customer to enable them monitor his performance.

Trade credit can be used as a form of price discrimination. This happens when a firm is launching new products and offers to her customer's terms so that they can increase sales. Firms that have better access to financial institutions are in a better position to offer trade credit to their customers. They actually act as financial intermediaries between institutional creditors and other firms who have limited access to financial institutions.

Cuevas et al (1993), in a study of Ghana's Enterprise Finance concluded that, most small firms use trade credit as their most important source of external financing. Pissarides (1999) concluded that, limited access to bank credit usually affected the growth of businesses and therefore the need for trade credit. In his study of 'Finance and growth in economics in transition', Coricelli (1999) concluded that, trade credit favors growth since it gave companies access to private credit markets.

Cook (1999) argued that, trade credit is a useful tool for financing since it gave suppliers an advantage in terms of access to customer information relative to banks. He argued that targeting criteria should take into account the market structure of the industries in question, and that any program should focus on sectors where trade credit is extensively used and where trade credit offers extensive growth potential.

Biggs et al (1994) concluded that, the use of trade credit increased with the firm size. They found out those small firms were frequently asked to make advance

payments. The study confirmed that Asian firms preferred the use of trade credit more than their African counterparts. Their findings indicated that, the ratio of various forms of trade credit to sales were below 10%, except where trade credit was provided which rose to 17% at most. They concluded that, African owned firms relied less on trade credit while large firms used more of it.

In a study conducted in relation to Zimbabwean firms, Fafchamps et al (1995) found that, large firms were likely to obtain trade credit while African owned firms that are small in size were less favored. The firm size and subsidiary status had a positive effect on the proportion of total trade credit extended. African ownership and small sized enterprises had a negative effect. This study also provided evidence that screening before trade credit extension was biased towards ethnicity. African owners were more likely to be screened and stringently than their Asian and European counterparts. The explanation provided was that African owners were more cash constrained while the large firms were more likely to obtain trade credit on their first purchase, suggesting that reputation is used as a screening device.

Fafchamps (1997) concluded that, large firms and non African owned firms were more likely to obtain trade credit. The study found that African owned firms were discriminated against irrespective of the firm size. The large firm's purchased more on trade credit terms than small firms and the use of trade credit would help improve the firm's cash flow. Fafchamps (2000) on a study focused on the importance of ethnicity for trade and bank trade credit in both Kenya and Zimbabwe, concluded that; African owners were likely to be outside the business network and ethnicity was an obstacle for access to trade credit. The study revealed that African owned firms tended to receive contracts with less trade credit period than their non African counter parts.

In his study on the trade credit in Kenyan Manufacturing firms, Isaksson, (2002) concluded that the determinants of demand for trade credit were the firm size, indebt ness, demand conditions, firm's status, promotion and the skill level of the firm staff. He claimed that to some extend the age of the firm may play a role in the use of trade credit.

1.1.1 The Motor Industry Overview

According to the August 2005 KMI sales report, the motor industry is segmented into two major groups: the formal and informal sectors. The formal sector refers to the established local franchise holders who import vehicles in CKD form and assemble them locally and also import new completely build vehicles

The major motor vehicle brands sold in Kenya include Toyota, Nissan, Mazda, Mitsubishi, Peugeot, Subaru, Mercedes Chevrolet and Isuzu. The overall set of all vehicles from all the brands in the Industry are divided into various segments depending on the size of the vehicle engine and the sector of the economy where they are used. Cars which are small vehicles that ranges from hatchbacks to estates. The sport utility vehicles which are luxury vehicles with powerful engines and travel at high speeds and can either petrol or diesel powered.

The pickup trucks are small commercial vehicles sold as either four wheel drives or two wheel drive depending on their application and where they are used in the country. They are also sold as crew cabins or single cabins. The light commercial vehicles, which are the 3 to 5 ton models while the heavy commercial vehicles are Lorries ranging from 7 tones to 14 tones. The passenger vehicles are those used to ferry people and include microbuses, minibuses and large buses.

1.1.2 History of General Motors East Africa Ltd.

General Motors East Africa Ltd was formed in 1975 and the current shareholders are; GMC (USA) 57.8%, ICDC (Kenya) 20.0%, ICDCIC (Kenya) 17.8%, and Itochu Corporation (Japan) 4.4%. The current share capital is in excess of US$ 40.0 million.

The vehicle assembling plant is situated in industrial area, Nairobi and assembles full range of Isuzu trucks and buses. It currently employs over 350 people and exports 30% of production throughout East, Central, and Southern Africa. General Motors East Africa Ltd is the largest assembler of the widest range of commercial vehicles in Kenya, and offers technical assistance and supply agreements with Isuzu Motors Limited.

GMC, the world's largest industrial company, founded in 1908 is the parent company of General Motors East Africa Ltd and has management contract to it. It market spans over 190 countries and has established manufacturing facilities in over 50 countries in the world employing over 575,000 employees worldwide

According to the August 2005 KMI report and using historical data published by KMI, graph 1 below shows how General Motors East Africa ltd has managed to maintain market share among a very stiff competition in the Motor Sector.

Graph 1.

Kenya Industry and GMEA Market Share

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005 BP	2005 (4+8F)
Total Industry	6,950	11,586	12,061	11,026	9,345	8,090	5,865	6,331	6,926	7,867	9,979	10,000	9,000
GMEA %	11.7%	14.2%	14.0%	13.0%	14.8%	14.9%	14.9%	17.3%	17.9%	19.8%	20.7%	22.8%	22.8%

Though General Motors East Africa Ltd lags behind in the overall market share, she still commands the lead in the commercial vehicle segment where her strength lies as per pie chart below as per the August 2005 KMI sales report

Pie Chart 1.

Isuzu Maintains Number one in Commercial Vehicles YTD
August 2005 Total
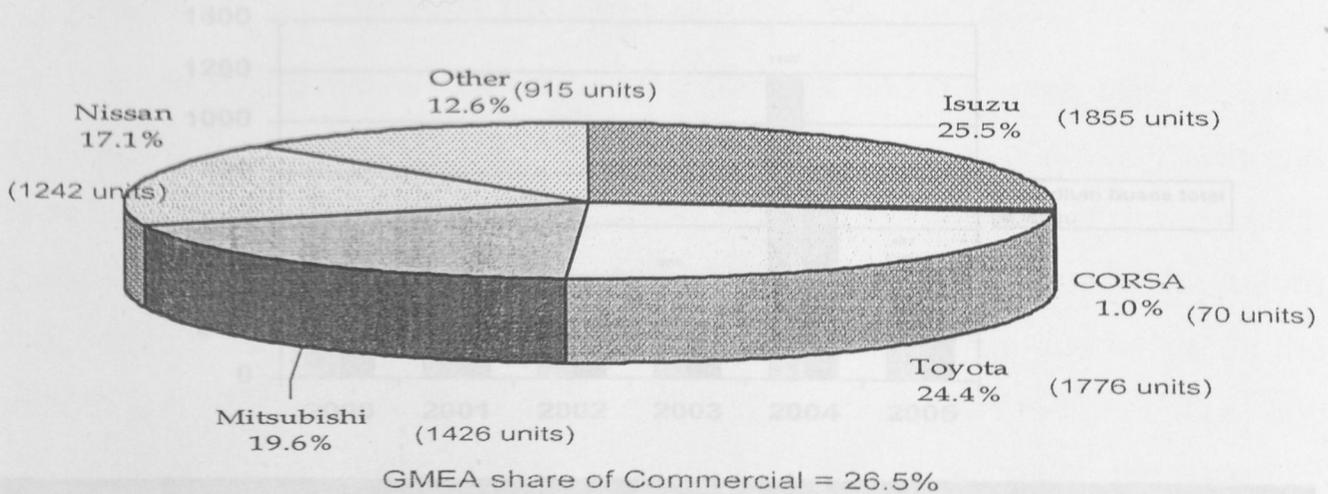
Other (915 units)
12.6%

Isuzu
25.5%   (1855 units)

Nissan
17.1%

(1242 units)

CORSA
1.0%   (70 units)

Toyota
24.4%   (1776 units)

Mitsubishi
19.6%   (1426 units)

GMEA share of Commercial = 26.5%

The manufacturing sector, its distribution network and the availability of trade credit to the final customer are essential to the country's economic growth and development. Extending trade credit therefore becomes an important activity for any industry. As the production process kicks off, the process of moving such goods and services to the final customer has to be assured. The nature of goods and services in the motor sector is that of high value. For smooth operation of this sector, trade credit is critical which can be administered either directly by the manufacturers or through the banks.

According to the KMI report for August 2005 a portion of which is summarized in Graph 2, GMEA still controls over 57% of the public sector transport sales which as a percentage of total sales, GMEA's share is 26.5%. The revenues for GMEA have grown from Kshs 3.9 Billion in 2002 to above the 5.0 Billion mark in 2004.

Graph 2.

MEDIUM BUS MARKET- KENYA
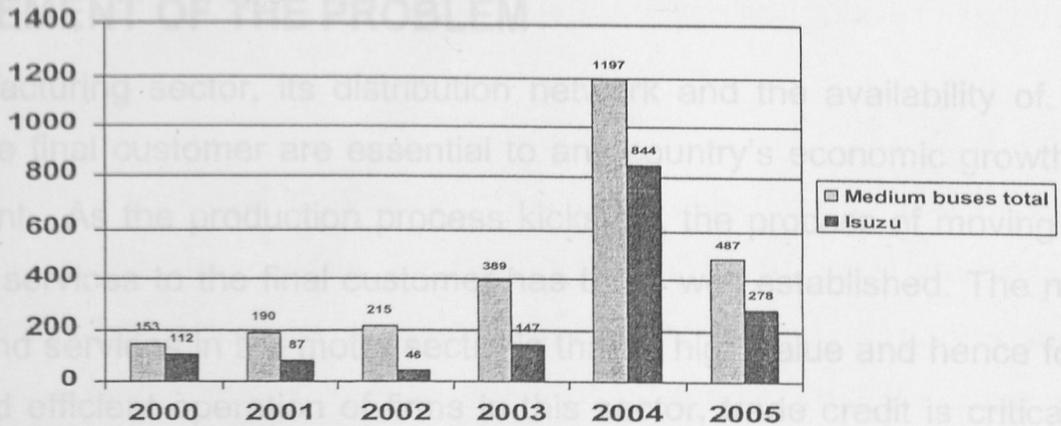
General Motors East Africa Ltd has been extending trade credit to both her dealers and retail customers. However, since banks are more qualified in trade credit administration, General Motors East Africa Ltd has had her share of bad trade credit practices. Samcon Ltd, one of her biggest Dealers went into receivership in 2003. Nairobi Motors Cooperation another big and fast growing dealership had folded her operation in early 1990 and Raju Motors in 2002.

There are clear cases where customers receive trade credit and are unable to pay eventually going into receivership.

In June, 2005, Kenya Bus Services Ltd, one of the biggest bus operators in Nairobi, got into financial problems with its suppliers. At this time, they owed General Motors East Africa Ltd over Kshs 170.0 Million and other debts to the rest of the creditors. By the time of the high court ruling of August 16th 2005, General Motors East Africa Ltd had extended credit to this big customer on an

arms length transaction. There were no securities or chattels signed to protect GMEA.

1.2 STATEMENT OF THE PROBLEM

The manufacturing sector, its distribution network and the availability of trade credit to the final customer are essential to any country's economic growth and development. As the production process kicks off, the process of moving such goods and services to the final customer has to be well established. The nature of goods and services in the motor sector is that of high value and hence for the smooth and efficient operation of firms in this sector, trade credit is critical and can be administered either directly by the manufacturers or through the banks...

According to Mcmenamin, (1999), weak trade credit management is a primary cause of many business failures. A common approach to customer trade credit selection and analysis is the use of the six "c" (capacity, capital, character, collateral, conditions and control) of trade credit as an initial screening and risk assessment device. Generally, institutions are expected to manage their trade credit risks to avoid exposing their organizations to unnecessarily high risk levels and subsequently a decline in returns

Petersen and Rajan (1997), observed that where banking institutions offer less trade credit or discriminate against various sectors of the economy, then trade credit is used both for medium and short term financing needs of most customers, acting as a last resort to reduce transaction costs. This means that suppliers may lend to firms that banks may have declined to extend trade credit to.

In this case suppliers assume they have comparative advantage in form of having more information about the customer through the constant daily interactions and therefore being able to cut supplies, repossess sold goods in cases where collaterals exists and selling the repossessed goods to recover the monies owed.

Pandey (1999), concluded that trade credit was useful to a firm for various financial and marketing reasons. He observed that trade credit was essential marketing tool that acted as a bridge for the movement of goods through production and distribution stages to the final customers and therefore would help firms tied with depressed or excess inventory and facing severe competition, to attract potential customers to increase their sales volumes by offering trade credit.

He observed that the bargaining power of large customers and their working capital demands influenced their demand for Trade Credit since they could use such power to bargain with their suppliers to vary their trading terms so as to retain them. It is upon such a background that this research seeks to answer the questions;

- What are the motives behind trade credit extension in the General Motors East Africa Ltd and her dealers?
- Has there been moral hazard in trade credit extensions? Have there been any defaults in repayment?
- What has been done to strengthen the process of granting trade credit among the General Motors East Africa Ltd family?

1.3 OBJECTIVES OF THE STUDY

This study will seek to:-

1. Determine the reasons behind the extension of trade credit to the dealers, distributors and customers in the motor vehicle sector.
2. Establish, whether there is any formal process that is followed in assessing the capacity for trade credit.
3. Establish how dealers and distributors utilize trade credit extended to them by their suppliers.

1.4 THE IMPORTANCE OF THE STUDY

The findings of this study will be important to different players in various sectors. These include;-

Managers:- Managers not only in the motors sector but also the hire purchase companies who will be enlightened on the best trade credit management practices to use as they advance trade credit to their dealers, distributors and other important fleet customers

Financial analysts: - They will have additional materials on how trade credit can be managed and therefore can use the same to advise their clients appropriately.

To scholars and Researchers: - The study will add to the scholarly body of knowledge in the finance discipline and form a basis for further research.

To the Shareholders:- The study will enlighten share holders on the reasons why the management of their companies extend trade credit, the methods they

use for the assessment, the weaknesses thereof and recommendations for future improvements.

To Hire Purchase Banks:- The study will be critical to banks because they will be able to get additional ways of extending secured trade credit to the motor sector so that they can enhance the banks earnings at reduced trade credit exposure.

To the Trade credit departments: - The trade credit departments of both the banks and the motor industry will be provided with a pool of knowledge from where they can draw better risk assessment skills and criterion. This will improve the speed with which the loan applications are processed. The quality of trade credit will also be enhanced, collections will be faster and the bad debts provisions was be low thus ensuring improved returns for the companies.

CHAPTER TWO:

2.0   LITERATURE REVIEW

2.1 THEORETICAL STUDIES

2.1.1 Advantage in Controlling the Buyer Theory

According to Schwartz (1974), the supplier may have an advantage over traditional lenders in investigating the trade credit worthiness of his clients, as well as a better ability to monitor and enforce repayment of the trade credit. This may give him a cost advantage over financial institutions in offering trade credit to a buyer. He also sees trade credit terms as an integral part of the firms pricing policy.

Biais et al (1997) concluded that, suppliers have a better capacity to investigate the credit worthiness of buyers. This is because they have knowledge of the industry wide economic climate. They are able to collect periodic information concerning the buyer's financial health in the normal course of business relationship.

Smith (1987) and Brennan et al (1993) argued that financial institutions can claim the firm's assets to pay off the firm's loan. However, if a supplier already has a network for selling her goods, the cost of repossessing and resale was be lower than that of an institution. The advantage of suppliers offering financial support through trade credit are based on the seller having superior information to financial institution or the seller using trade credit terms to entice buyers of his goods and services.

2.1.2 Advantage in Salvaging Value from Existing Assets Theory

Smith (1987) postulated that when customers start asking for installment payments, this is an indication of their risk ness as it may imply financial constraints and hence the need to be careful on the amount of trade credit extended. This means that, clients need time to verify the quantity and quality of the product supplied to them before making any payment for these goods. Verification is also relevant in the case of trade credit extensions

According to Emery (1987), by offering trade credit selectively, both across customers and over time, the firm may be able to manage its inventory position better. The firm can thus reduce warehousing costs, especially if its customers have a better ability to carry inventory.

2.1.3 Transaction Costs Theory

Ferris (1981), focused on trade credit as a way of reducing transaction costs by way of using trade credit. Rather than paying bills every time goods are delivered, a buyer might want to cumulate obligations and pay them on a monthly or quarterly basis. This was also enabling an organization to separate the payment cycle from the delivery schedule. In cases of highly seasonal goods in terms of consumption patterns trade credit can be used in order to smooth out production cycles through building up large inventories. This has two costs: the costs of warehousing the inventory and the costs of financing it. Of course, the firm could lower prices in order to effect early sales. But there may be many costs in doing this, as well as a loss in discretionary ability. The study concludes that trade credit terms provide the buyer of goods the time to comply with the contract terms and prevent him from engaging in speculative and opportunistic behaviors. He avers that such terms protect the buyers from potential non compliance by the seller.

2.1.4 Price Discrimination through Trade Credit Theory

When studying the trade credit decision Schwartz et al (1979), supported the view that trade credit may be offered even if the supplier does not have a financing advantage over financial institutions because it can be used to price discriminate. Since trade credit terms are usually invariant to the trade credit quality of the buyer, it reduces the effective price to low-quality borrowers. If this is the most price elastic segment of the market, then trade credit is an effective means of price discrimination. A natural reason why this segment's demand may be more price elastic is because it is typically trade credit rationed. If so, trade credit both lowers the effective price of the good and permits this segment to express its demand.

The study affirmed that firms with high margins (the difference between Net Sales and Variable Costs) for their product, clearly have a strong incentive to make additional sales, but without cutting the price to existing customers. Since their profit on the next unit is higher, they would be wishing to incur a positive cost to sell an additional unit, so long as it does not affect their previous sales. Under the assumption that there are laws that prevent direct price discrimination, high-priced trade credit may be a subsidy targeted at risky customers. Trade creditworthy customers will find the trade credit overpriced and repay it as soon as possible. On the other hand, risky customers was find it worthwhile to borrow because trade credit may still be cheaper than the other sources of finance that they may have access to finance their working capital needs.

A related version of the transaction theory is that the supplier does not discriminate in favor of the risky customer solely because the customer's demand is more elastic in the short run. Rather, the supplier may have a long-term interest in the survival of the customer firm. This is especially true if the

supplier has no potential substitutes for the customer. The supplier then factors in not only the net profit margins on current sales but also the present value of the profit margins on future sales when deciding whether to help the customer with trade credit. In other words, the supplier may want to protect the value of its implicit equity stake in the customer by providing temporary short-term financing. Of course, if there are multiple trade creditors including financial institutions, bankruptcy laws may prevent a trade creditor from seizing particular goods unless the sale is on consignment, in which case this advantage may be irrelevant.

Petersen and Rajan (1994), found that once the decision to grant trade credit has been taken, the trade credit terms seem to follow industry practice. They are usually not tailored to the particular borrower.

2.1.5 Verification and Compliance Motive Theory

Lee and Stowe's (1993) claimed that, the producers of low quality goods instead offer high discounts to entice customers to buy their goods while Brick and Fung (1984) suggest that tax must be considered in order to compare trade credit cost with other alternatives of financing. If buyers and sellers are in different tax brackets, then their borrowing costs will be different. This is true since interest is tax deductible. However, this disadvantage can be countered by offering trade discounts that are also tax deductible. They hypothesize that companies at higher tax brackets tend to offer higher trade credit than those in lower tax brackets. This argument is supported by the fact that buyers at lower tax brackets can borrow from financial institutions at lower costs and negotiate for lower cash prices.

Fisman (1999) brought another angle to the discussion on why trade credit exists. He argues that firms lacking trade credit are likely to face inventory shortages, as they first need to sell their products in order to have resources with which to acquire new inputs. This in turn leads to lower capacity utilization and lower utilization and profitability of physical capital and fixed investment. Pissarides, (1999) concluded that limited access to bank Credit usually affect the growth of businesses.

In his study of 'Finance and growth in economics in transition, Coricelli (1999) concluded that trade credit favors growth since it gives companies access to private credit markets. Cook (1999), found that trade credit is a useful tool of financing since it gives suppliers comparative advantage in form of customer information that can be used to assess their risk ness and capacity as compared to banks. He argues that, targeting criteria should take into account the market structure of the industries in question. Any program should focus on sectors where trade credit is extensively used and on areas where trade credit offers extensive growth potential

2.2 EMPIRICAL STUDIES

Biggs et al (1994) confirmed that the use of trade credit increases with the firm size and for this reason small firms are frequently asked to make advance payments because of their inability to qualify for trade credit from their suppliers or banks.

Pike and Neale (1999), described Trade Credit as finance obtained from the suppliers of goods and services over a period elapsing between delivery of goods and the subsequent settlement of the account by the recipient. During this period, they argue that the customer can enjoy the goods or services before making payments due to the favorable trade credit terms extended to him.

Pandey (1999), described Trade Credit as occurring when a firm sells its products and services on credit and does not receive cash immediately. He observes that trade credit is an essential Marketing tool that acts as a bridge fro the movement of goods through production and distribution stages to the final customers and thus its use depends on the level of competition, the companies bargaining power, the buyers requirements, the buyers status, the suppliers relationship with his dealers, the industry practice, and in cases where the products are in transit, the transit delays have to be captured. He argues that trade credit can also be used as a marketing tool.

Long et al (1993) concluded that, small firms and those producing goods that need quality check may extend more trade credit to allow time for verification before making payment. It actually casts a vote of confidence in the quality of goods the supplier provides to the buyer and removes any doubts on their quality before making any payments. This proofs the importance of asymmetric information, not only about the firms but also about their products.

2.2 EMPIRICAL STUDIES

2.2.1 Determinants of the Supply of Trade Credit Theory

Demirque-Kunt and Maksomovic (2001) compared manufacturing firms in 40 countries and found the use of trade credit to be complement to bank credit. This finding suggests that suppliers do act as financial intermediaries between banks and borrowers. The study of suppliers as financial intermediaries, emphasize the use of trade credit enhancing a countries development. The study concluded that the development of the banking and legal systems favors the use of trade credit.

Petersen and Rajan (1997), found some evidence of finance constraints and trade credit demand using data on firms' relationships with their banks. Using the duration of a firm's relationship with its primary financial institution as an indicator of the degree to which a firm is credit rationed, they found that firms with shorter banking relationships rely more on trade credit.

Using a sample of firms and compared the use of trade credit in those firms and larger firms, they documented that the extension of trade credit is dependent on the Customers Credit quality, the customer relationship with financial institutions, the customer's relationship with suppliers and the liquidation costs.

The study concluded that where there is a negative relationship with financial institutions, there is more use of trade credit. They also document that, firms that are liquid tend to demand less trade credit from their suppliers. One of the most surprising findings was that net profits are negatively related to the amount of trade credit offered, and that even distressed firms with low sales growth and negative profits offer trade credit. They suggested that this may be a matter of window dressing, in that firms in trouble attempt to keep the sales numbers up by offering trade credit to low-quality customers. It has also been suggested that predatory behavior may explain the provision of trade credit by distressed firms. If stronger firms bundle goods and credit together, weak firms may also have to offer both to compete.

Cunat (2004) examined the interaction between the financial and Industrial aspects of the supplier customer relationship. He concluded that suppliers have a better ability to monitor their borrowers since they have a comparative advantage over the banks in terms of information availability that can be used to assess trade credit capacity. This will reduce the likelihood of moral hazard since

they can threaten their buyers of their ability to cut off future supplies in case of non payment.

2.2.2 Determinants of Demand for Trade Credit

The study of Biggs et al (1996), using a 1993 survey of Kenyan manufacturing firms found that, access to trade credit in Kenya increases with the firm size and that it is positively influenced by the owner being from an Asian origin. Asian owners have a better access to trade credit than African owners and that only relatively large African owners try to seek trade credit.

Elliehausen and Wolken (1973), concluded that trade credit can be explained in the terms of its supply and demand. On the supply side, they argued that; trade creditors firm access to financing, leading to a higher supply of trade credit; The trade creditors internal cash and profit generation; The existence of a long term relationship with the buyer, leading to a greater confidence in repayment and hence more supply; Sales growth with similar effects; and the existing incentives for price discrimination, lead to a higher supply of trade credit.

On the demand the study documented that access to other sources of financing particularly interest rates on bank loans, with higher rates and lower availability leading to higher demand; the change in sales, as proxy for investment opportunities of the firm.

As a proxy, Trade Credit should lead to a larger demand for investment, though it could imply that the firm has a larger amount of internal resources and thus less dependence on foreign financing; the ratio of short term assets to total assets, as a firm might tend to avoid maturity mismatches and trade credit is usually of a short term nature; the firm cash flow and profit generation; the

volume of purchases, as a control for higher level of trade credit due to simply the size of trade operations; and the variability in the timing of the delivery of payments for the firm's products, give more incentives to obtain more trade credit.

Fafchamps et al (1995), in a study in relation to Zimbabwean firms found that large firms were likely to obtain trade credit. African owned firms that are small in size were less likely to do so. The firm size and the status of the firm being a subsidiary had a positive effect on the proportion of total trade credit extended. The fact of being an African owner and being small sized had a negative effect. This study also provides some evidence that some screening before trade credit is granted is purely based on ethnicity. African owners are more likely to be screened and more stringently. The explanation provided for this was that African owners are more cash constrained while the large firms are more likely to obtain trade credit on their first purchase, suggesting that reputation is used as a screening device.

Fafchamps (1997), in a related study of Zimbabwean firms, concluded that large firms and non African owned firms are more likely to obtain trade credit. The study found out that African owned firms were discriminated against irrespective of the firm size and that larger firm's purchase more on trade credit terms than small firms. It concluded that the reasons for use of trade credit were because it helps improve the firm cash flow.

Fafchamps (2000), on a study focused on the importance of ethnicity for trade and bank trade credit in both Kenya and Zimbabwe, concluded that; African owners were likely to be outside the business network and ethnicity was an obstacle for access to trade credit. The study revealed that African owned firms

tended to receive contracts with less duration than their non African counter parts.

Isakson (2002), in his study on Trade Credit in the manufacturing sector in Kenya concluded that trade credit can be determined by the age of the firm, the size of the firms, the status of the firm, the indebtedness of the firms, its level of promotion activity and the level of skill of its staff.

Summers and Wilson (2002), using a multivariate models of trade credit use concluded that trade credit is an important factor in an economy. The results from this study supported the transactions costs and financial theories of trade credit and that the production cycle can influence the use of trade credit especially where it use used for purchases.

Nilsen (2002) argued that firms with reduced access to other sources of credit use trade credit as a poor substitute for other sources of financing. The study found evidence that supported this view and showed that trade credit is particularly likely to be used as a substitute for other credit during periods of tight monetary policy. Firms that are constrained monetary tend to borrow more from their suppliers and as a result trade credit is less applied in countries where companies are in good relationship with the banks.

2.2.3 Sales Promotion and Marketing Motive Theory

Nadiri (1969) found empirical evidence that, the amount of trade credit supplied is positively related to sales growth, and to improvements in the firm's own liquidity position. He considered trade credit as a selling expense like advertising and argued that there were various ways of doing this; first, the supplier may want to offload some of his excess inventories onto the client. To enable

persuade the client, the idea the supplier may allow payments after taking delivery. Further more the supplier may allow trade credit to gain competitive edge over the competitors.

2.2.4 Advantage in Salvaging Value from Existing Assets Theory

Mian and Smith (1992), found that durable goods had a higher collateral value and favored credit extension. They argued that, if the buyer defaults, the supplier could seize the goods that are supplied. The more durable the goods supplied the better collateral they provide and the greater the trade credit the supplier can provide. The study showed that bond-rated firms, which are assumed to have better access to low-cost financing, provide more trade credit than unrated firms do.

CHAPTER THREE

3.0 RESERCH DESIGN AND METHODOLOGY

3.1 RESEARCH DESIGN

The study was conducted through a case study. A case study is a phenomenon specific to time and place. It is used to capture the complexity of a single case. It investigates a contemporary phenomenon within a real life context especially when the boundaries between the phenomenon and the context are not clearly evident.

A case study is usually defined by interest in an individual case and by the methodology being used. It copes with the technically distinctive situations in which there was be many more variables of interest than the data points, and as one result. It relies on multiple sources of evidence, with the data needing to converge in a triangulating fashion.

By using a case study methodology, the following benefits were expected;

- To show and explain complex casual links in trade credit policy formulations, reviews and applications in the formal motor industry players

- To describe how trade credit is administered in General Motors East Africa Ltd family and its determinants in the quality and quantity.

- To describe the factors that interfere with the quality and quantity of trade credit administration

- To explore the way forward in overcoming the interferences that influence the quality and quantity of trade credit as a source of finance.

The research using a case study of General Motors East Africa Ltd family was ideal since it places more emphasis on full contextual analysis of fewer events or conditions and their inter-relationships. This emphasis on detail provided more insight for problem solving, evaluation and strategy. It allowed evidence to be verified and avoided missing data.

3.2 POPULATION AND SAMPLE

The population of the study consisted of General Motors East Africa Ltd and her 8 dealers, Associated Motors Ltd, Associated Auto Center Ltd, A Jiwa Shamji Ltd, Thika Motors Ltd, Central Farmers Garage Ltd, Kenya Coach Ltd, Ryce Motors Ltd and General Motors East Africa Ltd Retail Outlet. Since the population was small, 8 dealers including General Motors East Africa's Ltd own wholesale and retail outlet, a census was conducted and therefore, there was no sampling.

3.3 DATA COLLECTION

Primary data for the study was collected through a drop and pick questionnaire. This was meant to generate as much information as possible from the respondents. The questionnaire was pre tested for clarity and conciseness in pilot survey.

The respondents comprises of finance managers and their credit controllers, sales and marketing managers. The finance managers and the credit controllers of these firms are involved in the trade credit policy formulations and had the data on the performance of the trade credit extended to the customers. Most of the historical data of the customers is available with the finance managers. They also had the information on trade credit operation and whether at any one time

there exists any overrides. The credit controllers who are the key implementers of the trade credit policies were also interviewed.

Finance managers are key company contacts in the source of funding that is used as a back up for trade credit and also make decisions on whether doubtful debts should be written off or not. Another group of respondents were the sales and marketing managers. This is a key group that is in constant contact with the customers who are in need of trade credit and have the reasons as to why customers need trade credit. Therefore it was important to involve them in this study.

3.4 DATA ANALYSIS

The data to be collected was basically descriptive. Data was cleaned and filtered to check for completeness and consistency of the given responses. The responses were then coded, entered and analyzed to draw conclusions and document whether the objectives of the study were met.

Descriptive statistics was used to analyze the data. Frequency tables, percentages and graphs were used to present the data in an organized and meaningful way. Independent variables were the firm size, the relationship with the suppliers of trade credit, the trade credit policies, the management behavior and the industry practice. Tables to represent all the various types of information from each of the dealers were used to summarize each of the variables that were studied. The data was then presented in tables, charts and graphs.

CHAPTER FOUR

4.0   RESEARCH FINDINGS AND INTERPRETATION

4.1 INTRODUCTION

This chapter contains the data extracted from the fully completed and screened questionnaires. The statistical parameters included zero correlation done at 0.05 significant levels (2 tailed test) and 0.01 significant levels (2 tailed tests). Data was done using SPSS and verified at 95% degree of confidence level.

4.2 BACK GROUND OF RESPONDENTS

A total of 24 interviews were conducted and 16 of the questionnaires were fully completed. Therefore 67% of the questionnaires were received back and credit policies of the companies were collected and reviewed.

The estimated turnover of the firms from which data was collected ranged between Kshs 100.0 Million to over Kshs 3.0 Billion with the highest annual turnover being estimated at over Kshs 3.0 Billion(57%)

Pie Chart 2: Annual Turnover

100-500m
7%

500-1000m
29%

over 3000m
57%

1000-3000m
7%

4.3 FINDINGS

4.3.1 Objectives of Extending Trade Credit

The findings of the study indicated that General Motors East Africa Ltd, her dealers and distributors granted trade credit to her dealers and customers to maximize on sales volumes, win big customers who have strong purchasing power and to finance the period between order placements by her dealers to the time when the dealer receives cash from the customers.

The study concluded that General Motors East Africa Ltd receives trade credit from her key suppliers to finance the production cycles from the date of order placement to the time the stock are ready and available for sale. More trade credit is sourced from the suppliers of money to fund the working capital

requirements of the company. General Motors East Ltd extends trade credit to her dealers and distributors to finance their working capital needs.

Graph 3: Reasons for seeking trade credit
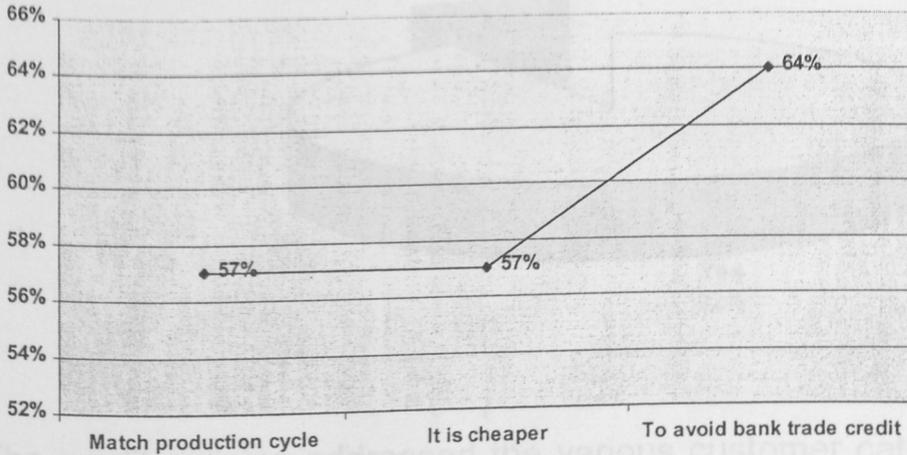
4.3.2 Credit Policy development

From the study, there was a clear effort in establishing very detailed and precise credit policies that were currently in existence in all the dealers and distributors. These policies have been reviewed on an annual basis. 92% of the responses have a credit policy that is in a written form.

Pie Chart 3: Existence of a written Credit Policy
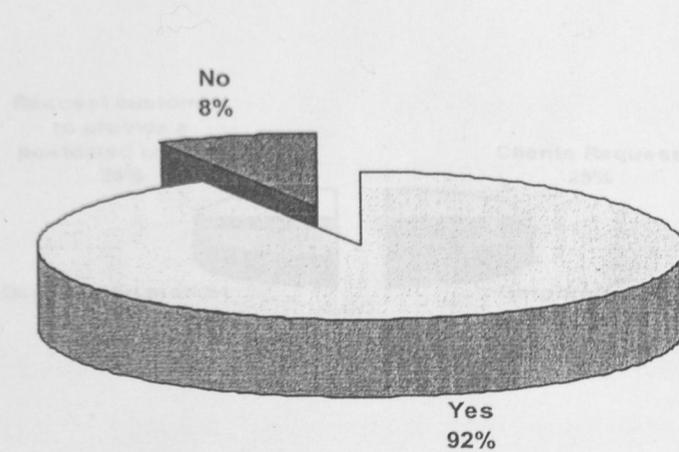
The credit policies addressed the various customer categories, analysis of their risk levels and the maximum trade credit exposure allowance to each of the categories. They also covered the levels of authorization to be obtained so that trade credit could be extended to the various types of customers.

The responses showed that there was a clear criterion for granting and sourcing for trade credit. This was documented and a clear categorization of the various types of customers was in place. Some of the bases for the extension of trade credit are as summarized in the pie chart below;

Pie Chart 4: Bases for trade credit extension

Request customer
to provide a
postdated cheque
25%

Clients Request
25%

Depends on market
reputation
25%

Corporate LPO
issued
25%
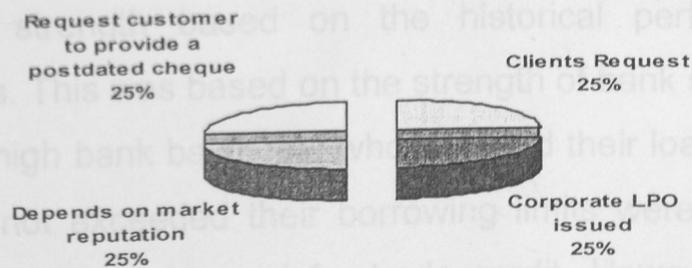
In August 2005, General Motors East Africa Ltd put in place a process for evaluating the credit risk of each of the customers. Parameters for this process included:-

- Size of Proposed business. This establishes the risk associated with the volume of the business upon which trade credit is being sought. The higher the value, the higher the risk associated with that business/

- Payment terms. Where cash or bank financing was available, this was taken to be of low risk. Local purchase orders from reputable multi nationals were taken as a medium risk while where customers were granted extended terms with no specific securities, then such a purchase was classified as high risk for extending trade credit.

- Level of security provided. Cases where securities in form of bank guarantees were provided, the trade credit was taken as low risk while high risk existed where there was no securities provided.

- Customer background. New customers whose background and business was unknown was said to be high risk while the customers making repeat purchases and had a good payment history were classified as low risk customers.

- Financial strength based on the historical performance of the key customers. This was based on the strength of bank statements. Customers who had high bank balances, who serviced their loans regularly and those who had not exceeded their borrowing limits were classified as low risk customers when assessed for trade credit. However those who had no banking history, bounced checks, missed payment commitments and had exceeded their borrowing limits were classified as risky customers for the trade credit extension.

In the process of assessing customer for trade credit, the following information was found to be useful.

Graph 4: Requirements before extending trade credit
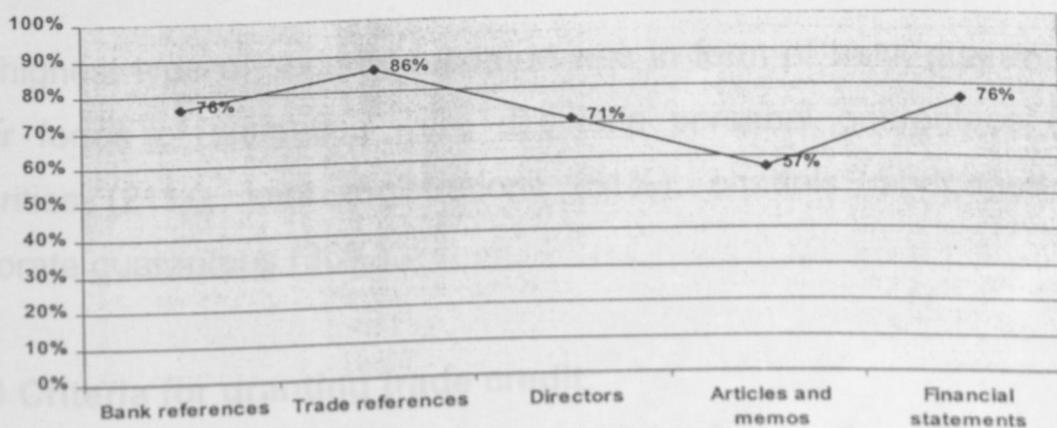
This detailed way of establishing the risk exposure of a customer before extending trade credit did not exist in majority of the dealers and distributors.

As the trade credit policies of the dealers and distributors evolved, they started requesting customers to provide securities as per the graph below:

Graph 5: Types of securities

The highest type of security recorded was in form of bank guarantees at 64%. Other forms of securities were director's personal guarantees (41%), cash securities (21%), joint registrations (51%), chattels mortgages (51%) and corporate guarantees (36%).

4.3.3 Criteria for granting trade credit

In order to perform a detailed analysis of the factors that may expose General Motors East Africa Ltd to credit risk, a risk ranking criteria upon which decisions

are made on whether trade credit should be approved, reviewed so that exposure is reduced or rejected if the company is fully exposed had been established. 98% of the respondents practice credit risk ranking. A similar percentage also practices risk quantification before ranting trade credit. The bases of the evaluations are as in the graph below;

Graph 6. Risk Ranking Factors
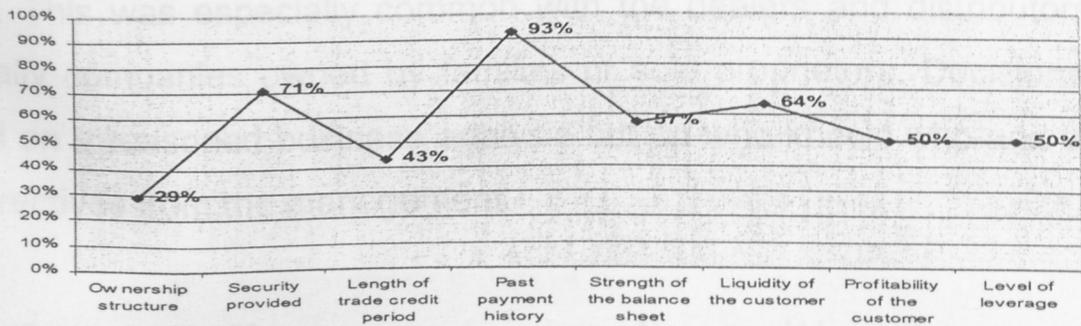
4.3.4 Biases on Trade Credit Extension

During the study and discussions held with the relevant people from each of the dealers and distributors, it was established that, 5 out of the 7 General Motors East Africa Ltd dealers were from the Asian origin. The balance, 2 are from the largest tribe in Kenya, of the parts and accessories dealers and distributors, 7 out of the 9 authorized distributors are from the Asian origin, 2 of the balance are from the largest tribe in Kenya. The 2 dealers that went into liquidation in the last three years, 2 were of Asian Origin. Of the biggest 12 fleet and bus operators 8 are from the Arab origin, 2 from the largest tribe in Kenya, and 2 from a smaller sub tribe.

From this analysis, race and tribe play a key role in granting trade credit though this has not been empirically tested to document and proof this conclusion.

4.3.5 Management Override

There was a very high incidence of extension trade credit without securities (71%). On a few occasions and during discussions with the credit controllers, it emerged that there were cases where pressure comes to bear on them to extend trade credit to customers who may not have otherwise qualified for trade credit. This was especially common with the dealers and distributors who are basically companies owned by families or sole proprietors. Decisions were not based on a reasoned business analysis but on who knows who and the case of the directives from the management.

Graph 7. Reasons for lending without security
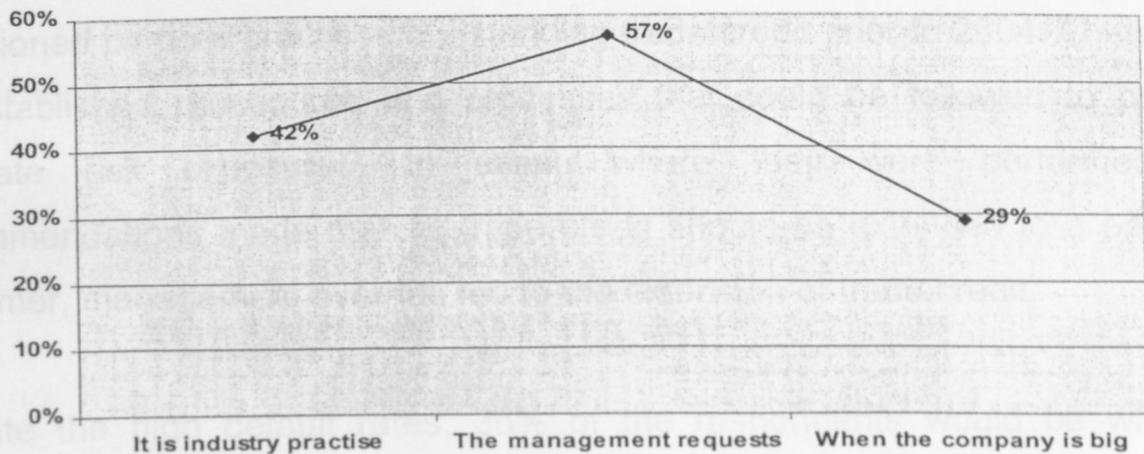
It was notable that the highest percentage of lending without security was due to management influence.

4.3.6 Level of Bad and Doubtful debts

Doubtful Debts as Percentage of Net Sales

Year/%age	Less than 1%	1%-2.5%	2.5%-3.0%	+3%
2003	50%	29%	7%	14%
2004	65%	21%	7%	.75
2005	79%	0%	7%	14%

Bad Debts written off

Year/%age	0%-15%	15%-30%	+30%
2003	79%	14%	7%
2004	86%	14%	0%
2005	86%	14%	0%

The level of doubtful debts has been high in the years 2004 and 2005. This was occasioned by poor practices of extending trade credit prior to 2004. There were no established procedures and processes that could be followed to properly evaluate risk exposures. In cases where they were performed and recommendations made that no trade credit should be extended to a particular customer, management override led to the extension of trade credit.

Despite the high default rates, 36% of the respondents would be willing to continue extending trade credit to their customers. However 21% would extend trade credit conditionally as they seem to have learnt from prior mistakes.

The top debtors of the firms interviewed were composed of the following;

Graph 8: Composition the top ten debtors
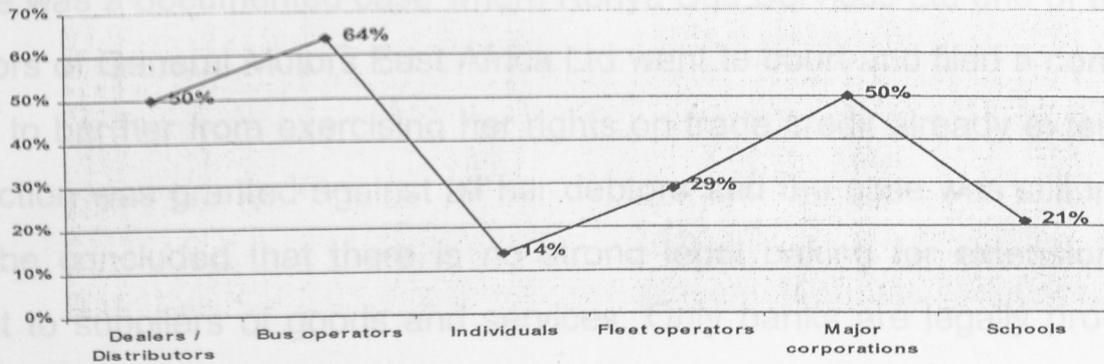
It is noteworthy that the highest debtors are bus operators who are considered high risk clients. This was observed to be true due to the slow nature in which old debts were being liquidated.

The main reasons given for writing off bad debts were bankruptcy, inability to pay, changes in ownership, court cases, disputes in payments and product complains.

Graph 9:Reasons for the bad debts write off
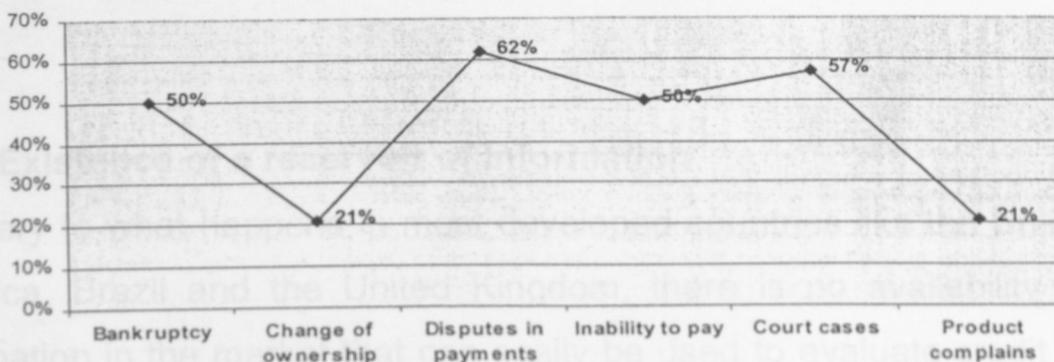
4.3.7 Legal system Support

There was a documented case where Kenya Bus Services Ltd one of the largest debtors of General Motors East Africa Ltd went to court and filed a constitutional case to bar her from exercising her rights on trade credit already extended. The injunction was granted against all her debtors and the case was still in court. It can be concluded that there is no strong legal baking for extension of trade credit to suppliers of goods and services. Only banks are legally protected but manufacturers have no title to fall back to in case of default.

It is curious to note that 86% of the respondents regard the judicial framework as very slow and inefficient as opposed to efficiently disposing off cases.

Graph 10: Performance of the legal framework in trade credit management
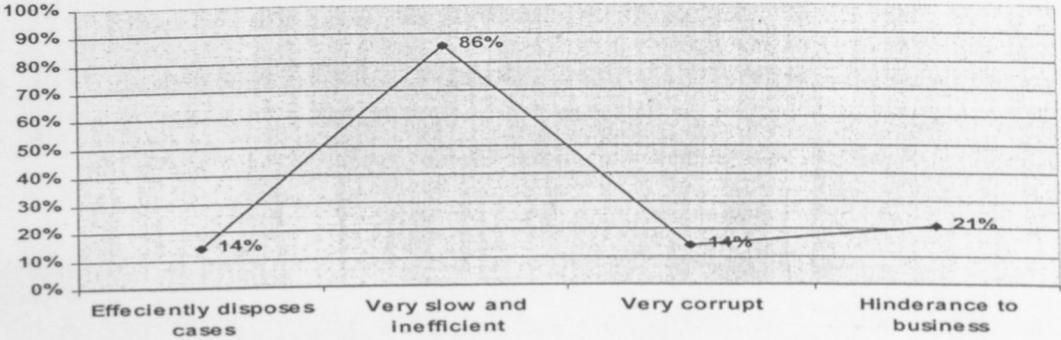
4.3.8 Existence of a reservoir of Information

Contrary to what happens in most developed countries like the United States of America, Brazil and the United Kingdom, there is no availability of customer information in the market that can easily be used to evaluate credit risk. Most of the information is only available through the grape vine or through the trading peers of the customers. The authenticity and hence reliability of this information

cannot be easily ascertained. The credit reference bureaus are far from being developed. The study did not reveal any clear reliance on such bureaus for reference in cases where customers are seeking trade credit.

5.0 CONCLUSIONS AND RECOMMENDATIONS

5.1 CONCLUSIONS

Based on the results of the study, trade credit is an essential marketing tool that acts as a bridge between the movement of goods through production and distribution stages to the final customers and thus its use depends on the level of competition, the companies bargaining power, the buyers requirements, the buyers status, the suppliers relationship with her dealers, the dealers, the industry practice, and in cases where the products are in transit, the transit delays have to be captured.

Trade credit is an important tool of trade in the motor vehicle industry. The study found the use of trade credit to be a compliment to bank credit. These findings suggest that suppliers do act as financial intermediaries between banks and borrowers. The study of suppliers as financial intermediaries emphasizes the use of trade credit, enhancing a countries development. The study concluded that due to the unavailability of bank credit, customers preferred trade credit. The legal institutions are considered to be hindrances to trade credit. These institutions considerably delay dispensation of justice.

Trade credit could be extended when a firm is facing severe competition to attract potential customers and as a marketing tool for firms with depressed or excess inventories to publicize it and expand its sales.

CHAPTER FIVE

5.0 CONCLUSIONS AND RECOMMENDATIONS

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Trade credit could be extended when a firm is facing severe competition to attract potential customers and as a marketing tool for firms with depressed or excess inventories to publicize it and expand its sales.

It is clearly notable that management influence and sometimes override play a major role in trade credit defaults and hence the need to reduce influence of the management in making decisions on trade credit extension. Trade credit is an important factor in an economy. The results from this study supported the transactions costs and financial theories of trade credit and that the production cycle can influence the use of trade credit especially where it is use for purchases.

The study also found evidence that the amount of trade credit supplied is positively related to sales growth and to improvements in the firms own liquidity position. Trade credit can be considered as a selling expense like advertising and there were various ways of doing this. First, the supplier may want to offload some of his excess inventories onto the client. To persuade the client the supplier may allow payments after taking delivery. Further more may allow trade credit to gain competitive edge over the competitors.

There is need to strengthen the institutional frame work of the judicial to better deal with trade credit related cases. This will reduce the delay in dispensing justice by ensuring that the suppliers of trade credit are able to exercise the securities without hindrance in cases of default.

Firms should reduce extension of trade credit outside the company's credit policy. This will make it easy for the implementers to stick to what had been formulated by the management. Perhaps credit risk and control departments should report directly to the board of directors.

The government should come up with clear legal frame work on conflict resolution mechanism for all the suppliers that extend trade credit to their

customers so that this critical business support mechanism is not frustrated by unscrupulous individuals.

5.2 LIMITATIONS OF THE STUDY

Some of the firms did not have up to date records on their trading activities hence limiting the amount of information they could offer. If all the information was availed, and 100% of the questionnaires returned, the results of the study might have been different.

The study was also limited to General Motors East Africa Ltd, her dealers and distributors only instead of the whole motor vehicle sector. A study of the full motor vehicle sector could possibly have given different findings since General Motors East Africa Ltd produces and sells only 22% of the total new vehicles market.

The study did not also cover the whole spectrum of goods and services that are financed through trade credit. It only covered vehicles that have documents of title. A study on trade credit to other sectors with different types of goods and services may present varying scenarios.

5.3 SUGGESTIONS FOR FURTHER RESEARCH

A full motor vehicle sector study should be conducted to establish how trade credit is practiced and evaluate whether similar results will be achieved.

A study on how trade credit is practiced in other sectors of the economy should be conducted. This would assist in establishing the results whether the same results will be achieved.

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APPENDIX 4

Research Question

Trade credit Risk Management by the Motor Sector in Kenya, the case of General Motors East Africa Ltd and her dealers and distributors

(Please freely answer the questions below. The information provided was be treated with the highest degree of confidence)

Section A

1. Please tick the appropriate category that is relevant to your company
   a) Vehicle Assembler   (   )
   b) Vehicle Dealer   (   )
   c) Vehicle Distributor   (   )
   d) Parts and Accessories Distributor   (   )

2. What is your estimated annual turn over in Kshs Millions
   a) Below 100 Mil   (   )
   b) 100 to 500 Mil   (   )
   c) 500 to 1,000 Mil   (   )
   d) 1,000 to 3,000 Mil   (   )
   e) Over 3,000 Mil   (   )

3. Do you extend trade credit to your customers
   a)   Yes   (   )
   b)   No   (   )

4. What are the types of customers that you have
   a) Cash Customers   (   )
   b) Credit Customers   (   )
   c) Both a) and b)   (   )

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3. Do you extend trade credit to your customers
   a)   Yes   (   )
   b)   No   (   )

4. What are the types of customers that you have
   a) Cash Customers   (   )
   b) Credit Customers   (   )
   c) Both a) and b)   (   )

5. Are the trade credit terms that you extend to your customers in writing?
   a) Yes   (   )
   b) No   (   )

6. If the trade credit terms that you extend to your customers are not in writing, how do you decide how to extend trade credit? Please explain?
   a) _____   (   )
   b) _____   (   )
   c) _____   (   )
   d) _____   (   )

7. What types of services do your suppliers offer to your company?
   a) Raw materials   (   )
   b) Services   (   )
   c) Money   (   )
   d) Other (please specify)
   _____
   _____
   _____

Section B

8. Do you require a security before extending trade credit?
   a)   Yes   (   )
   b)   No   (   )

9. Specify the types of securities you require before extending trade credit to your customers
   a) Bank Guarantees   (   )
   b) Directors personal Guarantees   (   )
   c) Cash securities   (   )
   d) Joint Registrations   (   )
   e) Chattels Mortgages   (   )
   f) Corporate Guarantees   (   )
   g) Any Other (Please specify)
   _____
   _____

10. Does your organization have a trade credit policy?
    a)   Yes   (   )
    b)   No   (   )

11. If the answer to the above is Yes, please state whether it is in written form
    or not.
    a)   Yes   (   )
    b)   No   (   )

12. If in written form, when was it last revised?
    a) Current Year   (   )
    b) One year ago   (   )
    c) Two years ago   (   )
    d) More than two years ago   (   )

13. Do you obtain trade credit from your suppliers?
    a)   Yes   (   )
    b)   No   (   )

14. If the answer to the above is yes, how frequently do you borrow?
    a)   Daily   (   )
    b)   Monthly   (   )
    c)   When need arises   (   )

15. If the answer to No. 13 is yes, do you have a borrowing policy?
    a)   Yes   (   )
    b)   No   (   )

16. If the answer to no. 13 is Yes, please state whether it is in written form or
    not.
    a)   Yes   (   )
    b)   No   (   )

17. How frequently do you revise your borrowing policy?
    a) Current Year   (   )
    b) One year ago   (   )
    c) Two years ago   (   )
    d) More than two years ago   (   )

18. Do you ever extend trade credit outside the established Trade credit policy?
    a)   Yes   (   )
    b)   No   (   )

Section C

19. What reasons may force your company to go outside the established trade credit policy?
    a) Because the customer is good   (   )
    b) When requested by top management   (   )
    c) Because the customer cannot get trade credit elsewhere(   )
    d) Because the customer has requested   (   )
    e) Any other (Please specify
    _____
    _____
    _____

20. For what reasons does your company require trade credit?
    a) To match the production cycle   (   )
    b) It is cheaper   (   )
    c) To avoid bank trade credit   (   )
    d) All the above   (   )
    e) Any other (Please specify)
    _____
    _____
    _____

21. For what reasons do you extend trade credit to your customers?
    a) To match the competition   (   )
    b) To match customer needs   (   )
    c) To attract customers   (   )
    d) To allow the customers to sale   (   )
    e) Borrowing is more expensive   (   )
    f) Bank lines are not available   (   )
    g) All the above   (   )
    h) Any other (Please specify)
    _____

22. Do you ever ask for advance payments before extending trade credit?
   a) Yes   (   )
   b) No   (   )
   c) If the answer is yes, is the payment predetermined, if yes, please
      specify_____
      _____
      _____

23. What reasons may force you to ask for advance payments?
   a) To reduce risk   (   )
   b) To cover body building cost   (   )
   c) To commit the customer   (   )
   d) To reduce final payment   (   )
   e) It is a bank requirement   (   )
   f) Any other (please specify)

      _____
      _____

24. Do you ask for the following background information before extending
    trade credit?
   a) Bank references   (   )
   b) Trade references   (   )
   c) Directors   (   )
   d) Articles and Memos   (   )
   e) Financial Statements   (   )
   f) Any other (please specify)

      _____
      _____

25. Do you require the following before extending trade credit to your
    customers?
   a) Bank Statements   (   )
   b) Audited Accounts   (   )
   c) Management Accounts   (   )
   d) All the above   (   )

26. Were there any doubtful debts 2003? If yes, please specify below
    a) Less than 1%
    b) Between 1% and 2.5%   (   )
    c) Between 2.5% and 3%   (   )
    d) More than 3%   (   )

27. In reference to the above, how much of the doubtful debts were written off
    in that year?
    a) 0-15% of the above   (   )
    b) 15%-30% of the above   (   )
    c) 30%-45% of the above   (   )
    d) More than 45% of the above   (   )

28. Were there any doubtful debts 2004? If yes, please specify below
    a) Less than 1%
    b) Between 1% and 2.5%   (   )
    c) Between 2.5% and 3%   (   )
    d) More than 3%   (   )
                                                             (   )

29. In reference to the above how much of the doubtful debts were written off
    in that year?
    a) 0-15% of the above
    b) 15%-30% of the above   (   )
    c) 30%-45% of the above   (   )
    d) More than 45% of the above   (   )
                                                             (   )

30. Were there any doubtful debts 2005? If yes, please specify below
    a) Less than 1%
    b) Between 1% and 2.5%   (   )
    c) Between 2.5% and 3%   (   )
    d) More than 3%   (   )
                                                             (   )

31. In reference to the above how much of the doubtful debts were written off
    in that year?
    a) 0-15% of the above
    b) 15%-30% of the above   (   )
    c) 30%-45% of the above   (   )
    d) More than 45% of the above   (   )
                                                             (   )

32. Do you have a policy to provide for doubtful debts?
    a) Yes   (   )
    b) No   (   )

33. If the answer in 32 above is yes, is this policy written down?
    a) Yes   (   )
    b) No   (   )

34. What were the reasons for the bad debts write off?
    a) Bankruptcy   (   )
    b) Change of ownership   (   )
    c) Disputes in payments   (   )
    d) Inability to pay   (   )
    e) Court cases   (   )
    f) Product complains   (   )
    g) Any other, please specify

    _____

    _____

    _____

35. Do you do customer ranking?
    a) Yes   (   )
    b) No   (   )

36. Do you perform risk quantification before granting trade credit?
    a) Yes   (   )
    b) No   (   )

37. What are the factors used in risk ranking?
    a) Ownership structure   (   )
    b) Security provided   (   )
    c) Length of trade credit period   (   )
    d) Past payment history   (   )
    e) Strength of the balance sheet   (   )
    f) Liquidity of the customer   (   )
    g) Profitability of the customer   (   )
    h) Level of leverage   (   )
    i) Any other, please specify

    _____

    _____

Section D

38. Given another chance, would you extend trade credit to your current debtors?
    a) Yes   (   )
    b) No   (   )
    c) Yes but(Please explain)

    _____
    _____
    _____

39. What is the composition of your top ten debtors?
    a) Dealers/Distributors   (   )
    b) Bus operators   (   )
    c) Individuals   (   )
    d) Fleet operators   (   )
    e) Major Corporations   (   )
    f) Schools   (   )
    g) Matatu Operators   (   )
    h) Any other (please specify)

    _____
    _____
    _____

40. Is there any relationship with the suppliers of your trade credit? If yes, please specify below, if no, please go to No. 41
    a) Shareholders   (   )
    b) Suppliers of materials   (   )
    c) Banks   (   )
    d) Any other (please specify)

    _____
    _____
    _____

41. What role has the legal framework played in increasing defaults?
    a) Efficiently disposes cases   (   )

b) Are very slow and inefficient   (   )
c) Are very corrupt   (   )
d) They are a hindrance to business   (   )

42. Which are the special characteristics within the Motor Sector?
     a) Very expensive individual items   (   )
     b) Very risky customers   (   )
     c) Segmentation not very clear   (   )
     d) Finance not easily available   (   )
     e) Financing is expensive   (   )
     f) All the above   (   )

43. Do you extend trade credit without security?
     a) Yes   (   )
     b) No   (   )

44. What are the reasons for lending without security?
     a) It is industry practice   (   )
     b) The management requests   (   )
     c) When the company is big   (   )
     d) Any other (please specify)
     _____
     _____

45. Suggest three ways to minimize your current the default rate?
     a)
     b)
     c)

APPENDIX 2

LETTER OF INTRODUCTION/INTRODUCTION

University of Nairobi,
Department of Accounting and Finance,
School of Business,
P.O Box 30197,
00100-Nairobi

TO WHOM IT MAY CONCERN

Dear Respondent,

Ref. Request for Research Data

I am a post graduate student at the University of Nairobi, School of Business. In partial fulfillment of the requirements for the award of the degree in Master of Business Administration, I conduction a study entitled, ' *Trade credit as a Source of Finance for the Motor Sector in Kenya. The Case of the General Motors East Africa Ltd (GMEA) and her vehicle distributors'.* Your company has been selected to participate in this study.

For the purpose of enhancing my research work, I wish to collect data through the questionnaire method. I shall be grateful if you would kindly extend to me the help I may need to have this questionnaire completed.

Needless to say, this information is purely for the purpose of my project work and I pledge to you that it shall be treated with strict confidentiality. A copy of final research report was be availed to you upon request.

Thank you for your cooperation.

Yours Faithfully

Johannes M Kitaka
MBA Candidate

Mrs. Winnie I Nyamute,
Lecturer,
Department of Accounting and Finance,
Supervisor.

APPENDIX 3

GENERAL MOTORS EAST AFRICA LIMITED
LIST OF DISTRIBUTORS

Name of Distributor	Location	Contact person	Telephone	Post Office Box
RM Ltd	Nairobi	Srinivas	Tel 0733607610	P.O BOX 49729 00100-Nairobi
CFG Ltd	Kitale	Evanson Njenga	Tel 020-551828	P.O BOX 27778 00506-Nairobi
KCI Ltd	Nairobi	S.N Sokhi	Tel.020-553770	P.O BOX 18354 00100-Nairobi
AM Ltd	Nairobi	Moez Jamal	Tel 020-650560	P.O BOX 30789 00100-Nairobi
AAC Ltd	Nakuru	Moez Jamal	Tel 020-650560	P.O BOX 30789 00100-Nairobi
AJS Ltd	Kisii	Jamil Shamji	Tel. 0720633001	P.O BOX Kisii
TMD Ltd	Thika	George Wambugu	Tel. 0722526746	P.O BOX Kisumu
GMEA-Head Office	Nairobi	Peter Wartnaby	Tel.0206936395	P.O BOX 30527 00100-Nairobi

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