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Some Aspects of Financial Management Affecting Cost of Operations of Microfinance Institutions in Nakuru Town, Kenya

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Abstract *: MFIs play a fundamental role in the Kenyan economy in that they enhance financial deepening by enabling millions of Kenyans to access financial services particularly credit. MFIs in Kenya have been facing many challenges. Despite many successful MFIs containing credit risks within desired levels, they still face greater challenges in the increased volatility of their portfolio. This study sought to analyze the financial factors affecting the operations of MFIs in Nakuru town, Kenya. The target population constituted 127 MFIs' employees. A sample of 57 respondents was drawn from the target population using stratified random sampling method. A self-administered structured questionnaire was used to collect primary data from the sampled respondents. Both reliability and content validity of the instrument were tested. The collected data were analyzed with the aid of the Statistical Package for Social Sciences program. Data analyses were both descriptive and inferential. The findings of the study were presented in tables that captured both descriptive and inferential statistical results. Access to credit facilities and financial management skills were found to affect operations of MFIs positively. On the other hand, it was revealed that both cost of operations and credit risk negatively affect the MFIs' operations. The study recommends that MFIs should encourage more savings from their customers in order to minimize reliance on credit facilities from other financial institutions and should also employ measures of minimizing the costs of operations. Moreover, MFIs are advised to employ measures of minimizing the costs of operations, in addition to holding training workshops for their staff in order to equip them with requisite skills in financial management. Lastly, they should enhance the profiling of all their customers before advancing any credit facility to them.*
Keywords: *Credit Facilities, Micro finance Institutions,*

I. Introduction

According to Mohini (2007), business enterprises which are small-sized face a number of challenges that compromise their operations. Some of these challenges included lack of adequate access to credit facilities. The primary purpose of the existence of MFIs is to advance credit facilities to small business holders who, for certain reasons, are incapacitated to access such facilities from the mainstream financial institutions. Weber, Mubhoff and Petrick (2014) opine that the lending strategies employed by MFIs sufficiently reflect business conditions of micro, small, and medium enterprises (MSMEs). The authors further assert that the sizes of loans advanced by these entities are commensurate to the borrowers' income level. MFIs' operations is not only subject to credit facilities they access from other financial institutions, but there are also other factors which are part of the themes of the current study.

MFIs account for a large share of enterprises and a large share of overall employment in the private and public sector of most economies. Employment in MFIs with up to 250 employees constitutes over 40% of total employment in financial institutions in many countries, which justifies the statement that "MFIs are the emerging private sector in poor countries and thus form the base for private sector-led growth" (Hallberg, 2001). Cross-country evidence, however, also shows that MFIs are more constrained in their operation and growth than large enterprises and access to financial services features importantly among the constraints (Ayyagari, Demirgüç-Kunt and Maksimovic, 2006).

The development of MFIs enterprises has often been graded as a "missing link" in development strategies of African countries, as several import substitution policies have favored large corporations at the expense of MFIs (Parker 1995). Several arguments have been given for putting MFIs at the centre of development strategies. The main reason is on the simple observation that they constitute the large portion of employment in developing countries especially the micro-enterprise segment.

Finally, MFIs are considered to be more flexible in adapting to client requirements, being known for their ability to adapt quickly to market trends, as most of the operating costs are variable. It is, however, somewhat difficult to assess the weight of MFIs in the developing world's economies. This is not only due to lack of statistical data and research on industrial structures in developing countries, but due to problems associated with inclusion of the informal sector. However, MFIs are normally considered to employ a significant part of the working population in developing countries. Review of normal survey conducted in African countries estimates that between 17% and 27% of the working age population are employed in MFIs, being nearly twice the employment of large scale enterprises and public sector (Liedholm, 2001). USAID considers that MFIs often employ a third or more of the labour force in low income countries.

Access to and cost of finance is often ranked as one of most constraining feature of the business environment by MFIs. Access to finance is rated as major constraint by around 30% of small and medium enterprises, a similar proportion as economic policy uncertainty and corruption. Further, financing is one of the few characteristics of the business environment that – together with crime and political instability - is robustly linked to firm growth, while other features have at most an indirect effect on firm growth (Ayyagari, Demirgüç-Kunt and Maksimovic, 2006).

II. Literature Review

Lack of access credit facilities is almost a global challenge for MFIs (Amyx, 2005). Regardless of credit availability, MFIs may lack freedom of choice due to the stringent lending conditions. In Sub-Saharan Africa, small enterprises have very limited access to credit facilities and other important financial services ideally provided by financial institutions. It is exemplified that in countries like Ghana and Tanzania only less than 10 per cent of the citizenry has access to financial services (Amyx, 2005). The foregoing is in spite of the fundamental role played by the informal sector and small businesses in the economies of African countries (Lokhande, 2011). McNamara (2012) further asserts that MFIs in Africa have little access to finance; a situation that derails their growth.

In most parts of Africa, there is no long-term financing to SMEs (Lazear, 2005). The micro-credit institutions which would otherwise lend to SMEs do not have the financial capacity to cater for expansion of these enterprises. The high interest rates charged by lending banks are occasioned by fear of default. Insufficient collateral by SMEs due to ownership of limited fixed assets further raises the interest rates. This in turn makes accessibility and affordability of credits by SMEs to be almost impossible. Parijat, Saeed, and Pranab's (2011) assert that most lending to small firms is based on security available regardless of the prevailing cash flow.

In 2011, the microfinance information exchange compiled a data set for the financial inclusion for Sub-Saharan Africa. The data set revealed that there are myriad numbers of financial institutions that provide financial services that even reach to the low-income populations in Africa. Specialized MFIs are noted to be an important part in the provision of these financial services such as credit facilities. Notably, other financial institutions such as banks, credit unions and cooperatives, postal savings banks, savings groups other and type of providers also render financial services across Africa. Credit unions and non-banking financial institutions are found to have the largest market share with over 15 and 20million clients respectively (Linthorst &Gaul, 2011).

Objective Of The Study

To examine the influences of access to credit facilities on the cost of operations of MFIs in Nakuru town

Research Question

What are the influences of access to credit facilities on the cost of operations of MFIs in Nakuru town?

III. Methodology

This study adopted a descriptive design. Descriptive research design is a process of collecting data in order to test hypothesis or to answer questions concerning the current status of the subjects in the study (William, 2006). The study used cross sectional survey research design. Kothari (2009) asserted that descriptive research attempts to answer the "what" kind of questions in addition to describing the various opinions of the respondents in respect of the theme(s) being studied. The target population for this study comprised of the 127 employees working with the MFIs in Nakuru town, Kenya. Accessible population is that part of target population which the study can particularly reach to select a representative sample (Mugenda, 2011). Thus accessible population for this study was the aforesaid 127 employees.

In this case, therefore, all the 127 employees working with the MFIs constituted the sampling frame. Mugenda and Mugenda (2009) stated that a good sample should be large enough and logically between 10 and 30 per cent of the study population. Simple random sampling helps to eliminate bias in selecting sample elements. Cooper and Schindler (2006) assert that, simple random sampling is the purest form of probability sampling. Due to the large size of the target population (127), Nassiuma's (2000) formula was employed to calculate the exact sample size.

$$n = \frac{NC^2}{C^2 + (N-1)e^2}$$

Where:

n = Sample Size

N = Population Size
C = Coefficient of Variation (0.5)
e = Error Margin (0.05)

Substituting the values in the above equation, estimated sample size was:

$$n = \frac{127\,(0.5)^2}{0.5^2 + (127-1)0.05^2}$$

$$n = 56.19$$

n = 57 respondents

Therefore a proportionate sample size of 57 respondents was drawn from the accessible population using stratified random sampling method.

IV. Findings And Discussions

The study analyzed the opinions of the respondents regarding access to credit facilities. Table 4.6 illustrates the aforesaid opinions. It was revealed that respondents strongly agreed (mean = 4.52; std dev = 0.927) that MFIs face limitations in accessing loans from banks. In addition, it was agreed (mean ≈ 4.00; std dev > 1.000) that credit facilities available are only short-term; credit facilities available are only short-term; credit terms offered by banks are unaffordable by MFIs. Respondents were, however, non-committal whether firms rely on equity for financing or not.

Table 1: Descriptive Statistics for Access to Credit Facilities

		N	Min	Max	Mean	Std. Dev
i.	MFIs face limitations in accessing loans from banks	44	1	5	4.52	.927
ii.	Our firm has never received any credit facility	44	1	5	4.05	1.200
iii.	Credit facilities available are only short-term	44	1	5	4.00	1.364
iv.	Credit terms offered by banks are unaffordable by MFIs	44	1	5	3.52	1.285
v.	Our firm relies on equity for financing	44	1	5	3.34	1.363

The study analyzed the relationship between access to credit and cost of operations of MFIs and the results of Pearson's correlation analysis are as shown in Table 4.10. It was established that the relationship between the two variables was positive, moderately strong and statistically significant ($r = 0.543$; $p < 0.01$). The results indicated that the greater the access to credit facilities, the more effective the cost of operations of MFIs is likely to be. As such, in order to enhance the operations of these firms, it is essential to increase the accessibility of credit facilities.

Table 2: Relationship between Access to Credit and Cost of operations of MFIs

		Cost of operations of MFIs
Access to Credit	Pearson Correlation	.543**
	Sig. (2-tailed)	.000
	N	44

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

It was revealed that respondents strongly agreed that MFIs face limitations in accessing loans from banks. In addition, it was agreed that credit facilities available are only short-term; credit facilities available are only short-term; credit terms offered by banks are unaffordable by MFIs. Respondents were, however, non-committal whether firms rely on equity for financing or not. It was established that the relationship between access to credit facilities and cost of operations of MFIs was positive, moderately strong and statistically significant ($r = 0.543$; $p < 0.01$).

V. Conculsion

The study concluded that MFIs do indeed face challenges in accessing loans from commercial banks. More so, it is inferred that credit facilities available to MFIs are mainly short-term. In addition, the study concluded that cost of operations of MFIs is hugely influenced by access to credit facilities.

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