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Customer Credit Protection and Growth of Microfinance Institutions in Bungoma County, Kenya

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Abstract

Financial regulation practices in the management of MFIs leads to customer losing confidence in the ability of a micro-finance to properly manage its assets and liabilities, including deposits, which could in turn trigger liquidity crisis. Therefore, customer credit protection may lead credit controlling being controlled improper where loan awarding procedure may be compromised and embezzlement of fund by MFIs management can be facilitated by poor financial regulatory practices put in place. Therefore, this study is meant to find out the effect of customer credit protection on growth of microfinance institutions in Bungoma County. The study targeted 13 micro-finance institutions in Bungoma with a total population of 143 employees. Census method was employed because of the small number of respondents. Both primary and secondary data were collected. Descriptive and inferential techniques were adopted. Qualitative and Quantitative analysis techniques were employed. Inferential statistic was adopted where regression and correlation analysis were used to test research hypothesis. Frequencies and percentages were adopted. Graphs and charts were used to present data. Correlation results showed that there is a positive and significant relationship between customer credit protections on growth of MFIs. Regression results depicted that customer credit protection contributes significantly to growth of MFIs, that is, an increase in growth of MFIs by 1 units leads to an increase of 0.620 units of use of customer credit protection. The results can be interpreted that, use of customer credit protection leads to growth in MFIs in terms of market shares, shareholders wealth and increase in business value. The study concluded that there is a positive and significant relationship between customer credit protections on growth of MFIs. The study thus recommends that, to increase the growth of MFIs, they should invest heavily on customer credit protection mechanisms which entails; having integrated financial management systems, having customer care desks, periodic auditing, benchmarking with successful firms, staff motivations and having accountable and transparent staff.

Keywords: *Customer Credit Protection, Growth of MFIs, County Government, Financial Regulatory Practices*

1. Background of the Study

In order to manage risks in the entire portfolio, financial sectors need to put in place risk management strategies. Since microfinance institution are more likely to be exposed to moral hazard and adverse selection when advancing loans to borrowers, credit assessment of loan is inevitable (Alexander, 2011). This should be done with a clear mind that there is great potential that most borrowers would default. Frederic (2014), pointed out that financial institutions attempt to solve these problems by coming up with ways and means for managing risk: establishment of long-term customer relationships screening and monitoring, a compensating balance requirements, loan commitments and credit rationing.

Failure by financial institutions to consider the impact of its actions on its customers, markets and employees may result in significant reputational damage and adverse publicity, even if no law has been broken. In developing economies, the micro-finance sector among other sectors has also witnessed several cases of collapses, in the case of financial institution in Nigeria for instance the Capital Finance Ltd and Okafolo microfinance have all collapse (Akpan, 2014).

It is estimated that there are 38% of Kenyans who do not have access to any type of financial services and the 35% who might be unhappy with the informal financial services they use hence they have opted for micro-finances. In the recent years micro-finances have further gained acceptance twice as banks despite few challenges like amount to lend out in comparison with the banks. Therefore, micro-finances have been systematically trying to understand the nature and pace of change in the operating environment, besides trying to identify

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opportunities, challenges and likely future developments in the market (Mbwayo, 2013). Most of the MFI have ensured regulatory compliances practices and therefore proving a chance to creating a higher profits wealth for the shareholders.

In Bungoma County the number of MFIs has been growing significantly but operation under some of regulations. It is the goal of the Central Bank of Kenya to expand the microfinance industry as its goal and purpose is to meet the needs of the clients through expanding access to financial services for poor individuals and families along with small business, particularly Micro and Small-Scale Enterprises (MSEs) and informal sector businesses. Such a goal also fulfills Kenyan Vision 2030 in which the government aims to improve and expand access to the financial sector to improve the quality of life for Kenyan citizens by 2030 (Mutheu, 2014). Despite the fact that MFIs enjoy benefits of expansion, there are also many complex issues associated with global expansion. Dymsza (2014) identified these issues like: firm must deal with multiple political, economic, legal, social and cultural environments as well as various rates of change within each of them. These factors have also proven to affect the shareholder wealth creation. This means that to guarantee stakeholders wealth, microfinance institutions need to come up with customer credit protection mechanism. Therefore, this study sought to find assess the customer credit protection on growth of microfinance institutions in Bungoma County, Kenya.

1.1 Statement of the problem

Microfinance institutions occupy an important position in the economic equation of any country as they provide loans and financial support to small and micro-enterprise, hence without well-organized financial regulatory practices small business and large organizations may experience poor performance due to financial instability. Failure to implement proper customer credit protection mechanisms may contribute to slow growth and eventually collapsing of a microfinance institution as customer will be discouraged to seek their services as they can observe financial management and profit or loss earned through annual financial statement. Lack of customer credit protection mechanism by micro finance institutions can also lead markets to lose confidence in their ability to properly manage its assets and liabilities, including deposits, which could trigger liquidity crisis. Therefore, financial regulatory practices may lead credit controlling being controlled improper where loan awarding procedure may be compromised also embezzlement of fund by MFIs management can be facilitated by financial regulatory practices. Hence it is in this basis that the researcher will conduct his study.

As such to most of the studies the focus has been the effect of financial regulations and practices on the consumer and the growth of various microfinance institutions which makes it essential to find out on the same. To the best of the researcher's knowledge based on the literatures reviewed, only few studies were found in the context of Ghana micro-finances. Due to neglect of microfinance institutions sector regarding financial regulatory practices by other studies and with radical changes in financial sector in the last few years, present study therefore will aim to fill the existing gap. As such few studies concerning financial regulatory practices especially customer credit protection effect on the growth of microfinance institution has not been done therefore this study filled the existing gap.

1.2 Objectives of the Study

To find out the extent of customer credit protection effect on growth of MFIs within Bungoma town.

1.3 Research Hypothesis

H_{01} Customer credit protection has no significant effect on growth of MFIs in Bungoma town.

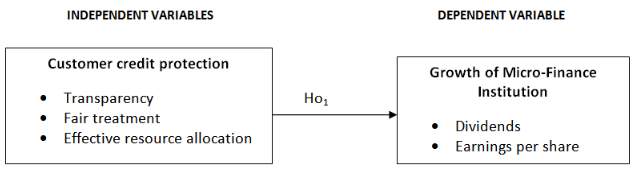

Figure 1.1 Conceptual Framework
Source: Researcher's own conceptualization

2. Literature Review

2.1 Consumer Protection Theory on Consumer Credit Protection

Consumer protection theory is a theory whose main aim is to protect the rights of consumers. This theory is designed to ensure the rights of consumers as well competition, accurate information and fair trade is practiced in the marketplace. This helped prevent businesses that engage in fraud or use unfair practices from gaining an advantage over competitors. For example, a government of the country may require business owners to disclose detailed information about their goods and services particularly in areas where safety or public health is an issue, such as food. Consumer protection is linked to the idea of the formation of consumer organizations and consumer rights which help consumers make better choices in the marketplace through consumer complaints (Reuters, 2009, Porteous, 2009; Porteous and Helms, 2005).

In relation to the study the theory is relevant as it relates to consumer credit protection in that it emphasizes on prevention of businesses that engage in specified unfair or fraud practices from gaining an advantage over competitors. Hence consumers are protected from high interest rate charged by the MFIs, also the theory emphasizes on the credit acquirement procedure to be made simply to enable easy access (Reuters, 2009, Porteous, 2009; Porteous and Helms, 2005).

2.2 Extent of customer credit protection and Microfinance Institution Growth

Thence (2013) conducted a study on the influence of trade credit protection on their growth. The study found out that investment in accounts receivables is insignificant related to the growth.

According Cheng and Pike (2012) study findings, it is noted that trade credit involves bearing the credit risk, due to the exposure to payment default by customers, resulting to negative effects on profitability and liquidity. Kans, (2012) study on contribution of MFIS financial prevention practices to growth of fish wealth in Kenya. It was noted from the study that growth of fish wealth depended on credit protection, institutional strengths, loan management and Innovativeness of MFIS Products.

3. Research Methodology

The study adopted exploratory design. The study was carried out in Bungoma County. The county has a population of 1,660,651 which is 4.15% of the population of Kenya. 52% are females and 48% males as per the 2009 population census (GoK, 2009). The average population density is 522 people per km^2. The region of study borders the following counties: Vihiga on the South, Trans Nzoia on the North, Busia and Kakamega on the West and Uasin Gishu on the East.

The study targeted all the 13 micro-finances institution in Bungoma County with a population of 143 employees. The MFIs included SMEP, Rafiki Microfinance Bank Ltd, Remu Microfinance, Jamii Bora, Choice Microfinance Bank Limited, Century Microfinance Bank Ltd, Sumac Microfinance, Daraja Microfinance, U & I Microfinance, Caritas Microfinance, Arise and shine, Eclof and Maisha Microfinance Bank Limited.

The study adopted census study because of the small size of the Population; purposive approach was adopted to ensure that only the staff knowledgeable in Micro Finance regulatory practices was considered for the research.

Table 3.1: Population frame

MFIS	Manager	Employees	Total
SMEP	3	8	11
Rafiki Microfinance	3	8	11
Remu Microfinance	3	8	11
Daraja Microfinance	3	8	11
Jamii Bora	3	8	11
Choice Microfinance	3	8	11
Century Microfinance	3	8	11
U&I Microfinance	3	8	11
Caritus Microfinance	3	8	11
Sumac Microfinance	3	8	11
Arise and Shine	3	8	11
ECOLF	3	8	11
Maisha	3	8	11
Total	**39**	**104**	**143**

Source: Ministry of Trade, Bungoma County Government (2016)

The researcher sought permission from the National council for Science, Innovation and Technology through the School of Graduate Studies, Masinde Muliro University of Science and Technology, and then informed the respective Micro Finance Institutions of the intention to collect data for the research in their organization. The researcher personally visited all the sampled micro finance institutions and administers the questionnaires to respective respondents and was present to clarify the points of difficulty. The questionnaires were administered using a drop and pick method.

To ensure reliability of the research instruments, the data sheets that was used for the purposes of this study was subjected to a pilot study. The results of the pilot were used to carry out a Cronbach analysis that helped to determine the reliability of the research questions. The researcher established the reliability of the questionnaires by computing the Cronbach's alpha coefficient of the items (questions) in the questionnaire. Cronbach's alpha of 0.7 and above indicates a high level of internal consistency in the questionnaire (Gay, 1996). The pilot study was conducted in Kakamega County involving microfinance institution in Kakamega Town. Since the researcher sampled 143 respondents, 14 respondents were used for piloting. because according to Mugenda and Mugenda (2012) a thumb rule of 10% is used to find out the respondents to be piloted. The researcher administered 14 questionnaires to the piloted respondents and obtained a Cronbach's alpha of 0.843 which was considered reliable because it is above the acceptable Cronbach's alpha of 0.7 as shown in Table 3.2.

Table 3.2: Reliability test

	Cronbach's Alpha if Item Deleted
Systematic risk reduction	.883
Financial crime prevention	.769
Customer credit protection	.778
Organizational factors	.720
Growth of MFIs	.839
Overall	**.843**

Source: Field data (2017)

The validity of the questionnaire was determined by ensuring that questions or items in it conform to the study’s conceptual framework. Face validity was determined by assessing the items on the instrument and ensuring they appeared relevant, meaningful and appropriate to the respondent. To ensure content validity, the researcher used expert judgment through consultation with the supervisor and lecturers from the School of Business and Economics of Masinde Muliro University of Science and Technology. The expert advice helped improve the quality of the questionnaire to ensure the relevance, wording and clarity of the questions or items in the instrument. Their suggestions were used to improve the clarity of the items on the questionnaire. Construct validity was established by correlating the scores on one instrument with scores from another instrument, a high correlation of 0.7 and above indicated that the measuring instrument were measuring the same construct (Rapando, 2010).

Quantitative data was analyzed using descriptive and inferential statistics. The descriptive statistics thus was presented in the form of frequencies tables and percentages. Graphs and charts will also be used to present data. Regression analysis was also used to test research hypothesis by adopting the simple linear regression model in the form of:

Y =α+ βX+Є, Where: Y =Growth of Microfinance Institution, X=Customer credit protection, β= Regression coefficients Constant and ϵ= Error term

4. Results and Discussions

4.1 Response Rate

Table 4.1: Response rate of respondents

Response	f	%
Successful	23	83.9
Unsuccessful	120	16.1
Total	143	100

Source: Field data (2017)

The respondents were given a total of 143 questionnaires out of which 120 questionnaires were successfully returned. This represents a response rate of 83.9% that is considered adequate to be used for data analysis. Babbie (2004) asserted that return rates of 50% are acceptable, 60% is good and 70% is very good to analyze and publish research findings.

4.2 Descriptive statistical analysis

Table 4.1: Customer credit protection

	N	Minimum	Maximum	Mean
Our firm credit policy is transparent.	120	1.00	3.00	1.9083
Our firm has segmented the market based on unique customer characteristics.	120	1.00	2.00	1.7250
Valid N (listwise)	120			

Source: Field data (2017)

Table 4.1 results show that most respondents agree that their firm has customer credit protection mechanisms in places shown by a mean of 2. These mechanisms entails having a transparent credit policy and segmenting the market based on the customer characteristics. Interview conducted involving MFIs top level managers reveal that the organization should put in place the following customer credit protection strategies: having integrated financial management systems, having customer care desks, periodic auditing, benchmarking with successful firms, staff motivations and having accountable and transparent staff. The study findings concur with Thence (2013); Cheng and Pike (2012); and Kans (2012) assertion that customer credit protection leads to financial growth of MFIs.

4.4 Inferential data Analysis

Table 4.2: Customer Credit Protection on Growth of MFIs correlation results

		Growth of MFIs
Customer credit protection	Pearson Correlation	**.573****
	Sig. (2-tailed)	.000
	N	120
Growth of MFIs	Pearson Correlation	**1**
	Sig. (2-tailed)	
	N	120

*. Correlation is significant at the 0.05 level (2-tailed).
**. Correlation is significant at the 0.01 level (2-tailed).
Source: Field data (2017)

Study results in Table 4.2 reveal the following: there is a positive and significant relationship between customer credit protection and growth of MFIs at 0.01 level of significance (r=.573; p=.000; N=120). The study result are in agreement with past research findings that found out the financial regulatory practices have a positive and significant relationship with growth of MFIs (Thence, 2013; Cheng and Pike, 2012; and Kans, 2012).

Table 4.3: Customer credit protection and growth of MFIs regression results

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.590[a]	.348	.331	.39036

a. Predictors: (Constant), Customer credit protection, Systematic risk reduction, Financial crime prevention

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	9.431	3	3.144	20.631	.000[b]
	Residual	17.676	116	.152		
	Total	27.107	119			

a. Dependent Variable: Growth of MFIs
b. Predictors: (Constant), Customer credit protection, Systematic risk reduction, Financial crime prevention

Coefficients

Model		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.
1	(Constant)	1.129	.212		5.332	.000
	Customer credit protection	.620	.124	.613	5.017	.000

a. Dependent Variable: Growth of MFIs
Source: Field data (2017)

Summary of multiple regression model results in Table 4.3 show that there is a positive relationship between customer credit protection on growth of MFIs (R=0.590). it also reveal that customer credit protection accounts for

34.8% of the growth in MFIs and the rest 63.2% of the growth in MFIs is as a result of other factors a part from customer credit protection (R^2=0.348).

ANOVA results in Table 4.3 reveal that the overall multiple regression model is feasible in measuring the relationship between customer credit protection effects on growth of MFIs. This is shown by a significant F-statistical test (F=20.631; p=0.000).

Coefficient results in Table 4.3 depict that systematic risk reduction and financial crime prevention is an insignificant measure of MFIs growth thus an increase by 1 units leads to an increase of 0.620 units of use of customer credit protection. The results can be interpreted that, use of customer credit protection leads to more growth in MFIs in terms of market shares, shareholders wealth and increase in business value.

From the results, the overall simple linear regression model can me written as;

Y (growth of MFIs) = 1.129-0.620CCP, Where: CCP=customer credit protection. 0.620 represents β. Since β≠0, the study rejects the research null hypotheses and concludes that there is a significant relationship between customer credit protections on the growth of MFIs. The study results are in agreement with past research findings that found out the financial regulatory practices have a positive and significant relationship with growth of MFIs (Thence, 2013; Cheng and Pike, 2012; and Kans, 2012).

5. Summary, Conclusions and Recommendations

5.1 Summary

The study found out that MFIs have customer credit protection mechanisms which entail having a transparent credit policy and segmenting the market based on the customer characteristics. This has enabled the MFIs to increase its; internal efficiencies, shareholders wealth maximization and business value. The study proposed the following customer credit protection strategies: having integrated financial management systems, having customer care desks, periodic auditing, benchmarking with successful firms, staff motivations and having accountable and transparent staff.

The study correlation results found out that there is a high positive and significant relationship between customer credit protection and growth of MFIs. The study findings on regression analysis found out that customer credit protection is a significant determinant of growth of MFIs hence its increase leads to an increase in MFIs growth by a big margin. The study thus rejected the third research hypothesis and concluded that customer credit protection has a positive and significant relationship on growth of MFIs.

5.2 Conclusion

The study concludes that MFIs have customer credit pretention strategies which entail having integrated financial management systems, having customer care desks, periodic auditing, benchmarking with successful firms, staff motivations and having accountable and transparent staff. It was also concluded that there is a high positive and significant relationship between customer credit protection and growth of MFIs.

5.3 Recommendations

Since there is a high correlation between customer credit protection and growth of MFIs, the study recommends that MFIs should invest heavily in customer credit protection strategies so as to realize increased growth. Some of these strategies entails; having integrated financial management systems, having customer care desks, periodic auditing, benchmarking with successful firms, staff motivations and having accountable and transparent staff.

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