
**THE EFFECT OF CAPITAL ADEQUACY REGULATIONS ON PERFORMANCE
OF SAVINGS AND CREDIT COOPERATIVE SOCIETIES IN KAKAMEGA
COUNTY**

Lumatete Irine Nanzala

Department of Finance and Accounting, Masinde Muliro University of Science And
Technology

Accepted 21th April, 2021

ABSTRACT

The objective of the study was to identify the effect of capital adequacy regulations on performance of Savings and Credit Cooperative Societies in Kakamega County, Kenya. The study was a descriptive study that sought to detail the effect of capital adequacy regulation on SACCOs. Setting. The study was carried out in Kakamega County. The population under study was the Front office Savings Activity, FOSA, operating SACCOs within Kakamega County whereby a census was taken of these SACCOs operating within the county. Data collection was carried out by means of questionnaires and interviews with respondents being chosen randomly from within the SACCOs. From the results, many of the study revealed that the majority of respondents had a membership base greater than 8,000 members represented by 56.7 of the respondents. 23.3% had a membership of between 400 and 1,000 members, 16.7% had a membership of between 1,000 and 5,000 members, and a minority of 3.3% had membership of less than 400 members. At significance level of 0.05, there was significant correlation between ownership, public confidence, corporate governance and performance.

Keywords: *Capital Adequacy regulations, Performance*

INTRODUCTION

The first Co-operative Society was established in Kenya in 1908 as a dairy Co-operative. In 1931 the government's first formal involvement in Cooperatives when the first Co-operative

Ordinance was enacted to regulate the operations of co-operatives; 1946, the inclusion of Africans in the Movement of cooperative when the colonial government acknowledged that Africans needed to participate in the economy through co-operatives resulting in the enactment of a new Co-operative Societies' Ordinance. However, it has evolved over the last 50 years into a powerful force for the social and economic transformation of the society in Kenya. (Co-operative Bank of Kenya, 2019).

Credit unions are defined as “non-depository institutions mutually organized and owned by their members” (Kioko, 2016). Savings and Credit Co-operatives (SACCOs) are “user-owned financial institutions that offer both savings and credit services to their members” (Philip, 2003). As such, the terms, SACCO and credit union, refer to the same institutions but are used in different regions of the world. In Kenya, the common term used is SACCO.

These organizations' primary goal is to improve the social and economic well-being of their members, who can be both net savers and net borrowers. They pay a membership fee and put money into the union to buy at least one share. Members are often expected to deposit their money in the credit union, and these assets are then lent to other members, not the general public, as is the case for commercial banks. In most cases, when forming a credit union, partners share a common bond, such as a similar profession or social affiliation (Walter, 2006). A rural neighborhood youth group is an example of the above. As a result, SACCOs are critical to social and economic growth.

Several banks in the globally faced takeover, bankruptcy, receivership, and government bailouts after the financial crisis of 2007-2008. This spread like a virus, with consequences affecting other countries. It wasn't just banks that were affected; other deposit-taking financial institutions were as well (Basel Committee on Banking Supervision, 2010). As a result, the Basel Committee on Banking Supervision (BCBS) identified insufficient banking sector legislation in terms of resources and risk distribution for assets. The Basel III system was released in 2011 with the aim of improving financial sector stability by implementing tighter capital ratios for banks.

During the latest bank crisis, some SACCOs were harmed. As a result of the timely passage of the SACCO Societies Act 2008, the SACCO Societies Regulatory Authority is now in charge of deposit taking licenses, oversight, and enforcement (SASRA). Prudential regulations have been adopted as part of this new regulatory structure to direct SACCO

growth and production by tracking capital adequacy and liquidity, among other primary performance metrics (Birchall & Ketilson, 2009).

Since the amendment of the SACCO Act in Kenya, fundamental guidelines were set forth for the continuous licensing of FOSA operations. Ngaira (2014) studies the impact of SACCO regulatory authority guidelines on SACCO operations in Kenya specifically examining the level of knowledge and understanding that SACCOs have in respect to the SASRA proposed regulations and supervision and any improvement in the performance of the FOSA. Makori, Munene and Muturi (2013) explore the challenges facing deposit-taking Savings and Credit Cooperative Societies' regulatory compliance in the Gusii region of Kenya following the commencement of the SACCO Act. as a result of the new SASRA regulations. The study sought to identify the effect of capital adequacy regulations on performance of Savings and Credit Cooperative Societies in Kakamega County, Kenya.

Methods

The study was conducted in Kakamega county and ethics approval was obtained from Masinde Muliro University of Science and Technology ethics board. No further approval was needed since the project did not require access to customers and personal data. A descriptive survey design. The study was conducted at three Saccos – Bukhungu Sacco Society Ltd, Nitunze Sacco Society Ltd, Wevasity Sacco Society Ltd, Sukari Sacco Society Ltd, Mudete Factory Tea Growers Sacco Society Ltd. Western region, Kenya. Structured questionnaires with closed and open-ended question items were used. Data analysis was done using the statistical program for social sciences (SPSS) version 25. Inferential and descriptive statistics were used to analyze data. Descriptive analysis of data was done using the mean, frequencies and percentages.

RESULTS

Of the respondents, 36.7% stated that capital adequacy greatly influenced lending capacity where as 53.3% said that there was a significant influence on lending capacity. 6.7% stated that capital adequacy slightly influenced lending capacity and 3.3% stated that there was no influence. Membership base is one of the indicators to the size of the institution. Respondents were requested to indicate the number of members that the institution had clustered into categories of less than 400 members, 400 to 1000 members, 1000 to 5000 members and more than 8000 members. The study revealed that the majority of respondents had a membership

base greater than 8,000 members represented by 56.7 of the respondents. 23.3% had a membership of between 400 and 1,000 members, 16.7% had a membership of between 1,000 and 5,000 members, and a minority of 3.3% had membership of less than 400 members.

The respondents were required to respond with regard to the extent to which they have benefited in the prescribed ways to the regulations along the following parameters: not at all, slightly, significantly, greatly. The benefits under investigation were meeting regulatory requirements, managing credit risk, improved public confidence, providing a safety net for members’ deposits, provision of operating capital, increased lending capacity, providing a base for future growth, and preventing insolvency. Majority, 66.7%, of the respondents agreed that attention to capital adequacy was greatly beneficial in meeting regulatory requirements, whereas 25.6% stated that it was significant in meeting regulatory requirements. 7.7% of the respondents asserted that it was slightly beneficial in meeting capital requirements.

Correlation analysis

The study undertook a correlation matrix analysis to establish the relationship between the variables.

Table 1: Correlation matrix analysis

		Performance			
Ownership	Pearson Correlation	.613**	1		
	Sig. (2-tailed)	0.001	0.001		
	N	38	38		
Public Confidence	Pearson Correlation	.657**	.312	1	
	Sig. (2-tailed)	0.012	0.012	0.012	
	N	38	38	38	
Corporate Governance	Pearson Correlation	.784**	.347	.682**	1
	Sig. (2-tailed)	0.000	0.000	0.000	0.001
	N	38	38	38	38

From the findings there was a moderate positive correlation $r=0.613$ between ownership and performance. The correlation was statistically significant $p=0.001 < 0.05$ at 95% confidence level. There was a moderate positive correlation $r=0.657$ between public confidence and

performance. The correlation was statistically significant $p=0.012 < 0.05$ at 95% confidence level. There was a strong positive $r=0.784$ between corporate governance and performance. The correlation was statistically significant $p=0.000 < 0.05$ at 95% confidence level.

Conclusion & Recommendation

The study established that SACCOs have benefited from the introduction of capital adequacy regulations. The study recommends that managers of the SACCOs closely adhere to the requirements provided by regulation so as to continue to reap the benefits. As the capital adequacy ratio internalizes the risk for shareholders, Deposit Taking SACCOs significantly increases the operation cost, which supports higher return on assets and equity. These effects appeared to increase significantly and progressively over time. The study concluded that capital regulation significantly improve management efficiency which impacted positively on performance. This was due to increase in management efficiency is likely to have been absorbed in Deposit Taking SACCOs' fees and commissions. There is also a general belief that SASRA prudential guidelines completely addressed the current Sacco challenges as seen from the study. The study finally concluded that ownership, public confidence and corporate governance significantly influence the performance of Deposit Taking SACCOs in Kenya.

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

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