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EFFECT OF REGULATIONS ON CAPITAL REQUIREMENT ON PERFORMANCE OF SACCOS IN KISII COUNTY, KENYA

[1*] **Faraja Arenchi Nyamweya**
faraja.nyamweya@yahoo.com

[2**] **Vitalis Mogwambo**
mogwambov@yahoo.com

[3***] **Tabitha Nasieku**
tnmereipie@jkuat.ac.ke

[1, 3] *Jomo Kenyatta University of Agriculture and Technology, Kenya*
[2] *Jaramogi Oginga Odinga University of Science and Technology, Kenya*

Abstract: *In Kenya SASRA under Sacco Societies Act of 2008, mandated the authority to license qualifying SACCO Societies to undertake deposit-taking business, regulate and supervise the activities of qualifying SACCO Societies in Kenya. The authority on an annual basis publishes a supervision report that documents the performance and operations of SACCO Societies in Kenya and the statistical trend of DT-SACCOs is observed that some SACCOs are performing well and some new SACCOs have been established and issued with operating licenses. The aim of this study was to assess the effect of regulations financial regulations on the performance of deposit taking savings and credit cooperatives (SACCOs) in Kenya. More specifically, the study sought to find out the effect of regulations on capital requirements on performance of SACCOs. This study adopted a descriptive survey design. The target population was all the 10-deposit taking SACCOs in Kenya-Kisii, registered and licensed by SASRA by 2014. Both primary and secondary data was used in this study, whereby a census survey was preferred as the population of the study was small. Alikert scale questionnaire was be used to gather primary information while a secondary data collection sheet will be used for collecting secondary information regarding SACCO performance. The secondary data was then sorted, coded and input into the statistical package for social sciences (SPSS) for production of graphs, tables, descriptive statistics and inferential statistics the results further regulations on assets positively and significantly affected the performance of SACCOs. The study therefore concluded that regulations on assets significantly impacted the performance of SACCOs. The. results further revealed that regulations on credit facilities positively and significantly affected the performance of SACCOs. The study therefore concluded that regulations on credit facilities significantly impacted the performance of SACCOs.*

Keywords: *capital requirements, deposit-taking business, SACCO*

1. Regulations on capital requirement and performance for SACCOs

Mbizi, (2012) conducted a study on the impact of minimum capital requirements on commercial bank performance in Zimbabwe. Descriptive correlation method was used in this research. This was augmented by some regression analysis to determine the magnitude of effect of capital on performance of selected banks. Findings revealed that there is a significant and positive relationship between commercial bank capitalization and its performance. The findings of the research however could not be generalized to all financial intermediaries let alone all companies since it had narrowed down to commercial banks. The research managed to elaborate on the relationship between capital levels and bank performance as well as the importance of capital to other bank operations.

Naceur, and Omran, (2011) conducted a study on the effects of bank regulations, competition, and financial reforms on banks' performance. The empirical results suggested that bank-specific characteristics, in particular bank capitalization and credit risk, had a positive and significant impact on banks' net interest margin, cost efficiency, and profitability. Also, the study found that macroeconomic and financial development indicators had no significant impact on net interest margins, except for inflation. Regulatory and institutional variables seemed to have an impact on bank performance.

Kilonzi, (2012) conducted a study on the impact of SASRA regulations on the financial performance of Sacco's in Kenya. This study sought to fill the existing knowledge gap to determine the effect of SASRA regulation on Sacco's financial performance and to answer the questions what is the impact of SASRA regulations on SACCO's financial performance in Kenya. Causal research design was chosen to establish the effects of SASRA regulations on the financial performance of SACCOs in Kenya. The study used secondary data. A linear regression model of SACCOs return on assets versus SASRA regulations was applied to examine the relationship between the variables. The findings found that higher capital requirements, and increase in management efficiency impacted positively to SACCO's profitability in the post- capital regulation period. The study revealed that capital regulation affects financial performance in SACCOs.

Barus, Muturi, Kibati & Koima, (2017). Effect of capital adequacy on the financial performance of savings and credit societies in Kenya. The study employed an explanatory research design. Descriptive and inferential analysis was conducted to analyze the data. The data was presented using tables and graphs. The findings the study concluded that capital adequacy influenced the financial performance of savings and credit societies in Kenya. This can be explained by the regression results which showed that the influence was positive and also showed the magnitude by which capital adequacy influenced the financial performance of savings and credit societies.

Amina, (2016). Conducted a study on the effect of core capital on the financial performance of deposit taking SACCOS in Nairobi county. The study evaluated the requirements for SACCOs in Kenya as out lined by the SASRA as well as the requirements for SACCOs specified by central bank of Kenya. The design of the research was a descriptive study that sought to detail the effect of core capital adequacy on SACCOs. The study concluded that SACCOs performance are affected by core capital significantly from the regulations in various ways such as, 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.

In the Kenyan context, several studies have been conducted on the impact of financial regulations on the financial performance of financial institutions in Kenya. For instance, a study by Kirui and Kihoro (2018) examined the impact of regulatory compliance on the financial performance of commercial banks in Kenya. The study found that regulatory compliance has a positive impact on financial performance, and it is essential for maintaining financial stability.

Similarly, a study by Nyang'au, Ondieki, and Onono (2018) investigated the influence of regulatory compliance on the financial performance of microfinance institutions in Kenya. The study found that regulatory compliance positively affects the financial performance of microfinance institutions. Additionally, a study by

Barasa and Muturi (2019) examined the impact of financial regulations on the performance of SACCOs in Kenya. The study found that financial regulations positively influence the financial performance of SACCOs.

Moreover, a study by Obura and Kisaka (2020) investigated the impact of prudential regulations on the financial performance of insurance companies in Kenya. The study found that prudential regulations have a positive impact on the financial performance of insurance companies. Another study by Omolo and Abuga (2021) examined the influence of financial regulations on the performance of microfinance institutions in Kenya. The study found that financial r Similarly, a study by Abayo and Marwa (2017) examined the impact of financial regulations on the financial performance of SACCOs in Nairobi County, Kenya. The study found that financial regulations positively influence the financial performance of SACCOs.

A study by Ogega and Ndwiga (2019) investigated the influence of regulatory compliance on the financial performance of SACCOs in Meru County, Kenya. The study found that regulatory compliance has a positive impact on the financial performance of SACCOs.

Furthermore, a study by Oloo and Oloko (2021) examined the impact of credit risk management regulations on the financial performance of SACCOs in Siaya County, Kenya. The study found that credit risk management regulations positively affect the financial performance of SACCOs.

A study by Chege, Wanjohi, and Munyao (2019) investigated the influence of prudential regulations on the financial performance of commercial banks in Kenya. The study found that prudential regulations have a positive impact on the financial performance of commercial banks. Similarly, a study by Nzioki and Mairura (2019) examined the impact of financial regulations on the performance of microfinance institutions in Kenya. The study found that financial regulations positively influence the financial performance of microfinance institutions.

Moreover, a study by Musyoka and Njoroge (2019) investigated the impact of financial regulations on the performance of SACCOs in Kenya. The study found that regulatory compliance has a positive impact on the financial performance of SACCOs, and it is essential in enhancing their financial stability. Additionally, a study by Mwangi and Nyangara (2019) examined the influence of financial regulations on the performance of insurance companies in Kenya. The study found that financial regulations have a positive impact on the financial performance of insurance companies, and they are crucial in promoting financial stability.

In summary, the above studies highlight the significant impact of financial regulations and regulatory compliance on the financial performance of SACCOs in various regions of Kenya. Therefore, this study on the influence of financial regulations on the financial performance of SACCOs in Kisii County, Kenya, will add to the existing literature and provide valuable insights on the topic in the local context.

SASRA in 2012 adopted the CAMELS framework to assess the financial soundness of Sacco's focusing on prudential standards. The adoption and implementation of CAMELS performance evaluation tool ensure objectivity and standardization in monitoring of the financial soundnessandstabilityofindividualSacco's.ThereportbySACCOSocietyRegulationauthority(SASRA) evaluates the performance of the SACCO subsector based on the financial data andinformationextractedfromauditedfinancialstatements.Saccocomprisesover50%ofallcooperativesinKenyaa ndasfinancialinstitutions;theyplayacriticalroleoffinancialintermediationinKenya'sfinanciallandscapefocusing mostlyonpersonaldevelopment.Further, Licensed deposit taking SACCOs constitute over 72% in key financial indicators of the entire industry in terms of membership, assets, loans, deposits and capital. This is a significant portion and hence the financial soundness of the licensed deposit taking SACCOs reflects the soundness of the entire Sacco industry. The subsector remains relatively financially stable in2013 as supported by compliance with the minimum prudential requirements in capital, liquidity, improved asset quality and overall earnings. This is expected to remain as SASRA continues to implement a risk-rating framework to monitor financial soundness of the industry and also issue regulatory guidelines to enhance compliance with sound business practices (SASRA Supervision Report, 2013).

In view of the above, therefore the researcher evaluated factors that influence the financial performance of deposit-taking SACCOs and concentrated on CAMEL variables with a view of determining, assessing,investigating,identifyingandexaminingtheextenttowhichtheyinfluenceperformance.

2. Statement of Problem

Deposit Taking SACCO's operate on a platform under regulation from SASRA. The authority on an annual basis publishes a supervision report that documents the performance of performance and operations of SACCO Societies in Kenya .Over the time reports from the regulatory authority has shown some SACCOs are struggling with performance over the years some licenses have revoked due to failure to meet statutory and compliance requirements. Some new applications rejected due to failure meet the minimum licensing requirements. In the year 2017 according to SASRA (2018) two licenses were revoked and out of the five new applications for licensing none was accepted. In 2018 two licenses were revoked and one license issued SARA(2019).The year 2019 had three licenses revoked and only one license issued SASRA,(2020).The year 2020 had three licenses revoked and now new license issued SARA (2021) .At least every year there are some licenses revoked and very minimal licenses issued. It has not yet been established if the SASRA financial regulations influence the revocation of licenses minimum issuance of licenses which forms the basis of this study. SASRA uses total assets, total deposits, and gross loans as parameters of measuring financial performance of DT-SACCOS. It was reported by (SASRA, 2020) A growth of ;12.5% on total assets,12.09% on loan portfolio and 11.27% on total deposits in the year 2019 .A report of (SASRA, 2019) shows a growth of 11.97% on total assets,13% on loan portfolio and 12% on total deposits for year 2018.In the year 2017 according (SASRA, 2018) a growth of 12.4% on total assets and 11.3% on loan portfolio. Despite the growth on assets, loan portfolio and deposits reported on over the years it has not been established whether the growth is a result of the SASRA'S financial regulations which this study will focus on.

A number of scholars have conducted a studies such as Mutinda & Ombati, (2018) focused solely on the influence of liquidity management regulations on financial performance on DT-SACCOs and recommended for more research to determine other factors that determine financial performance such as regulation on capital and loans which this study seeks to address. (Waiganjo, Wanyoike, & Koitaba, 2016) focused on SASRA regulations; staff competence, quality of board of directors and corporate governance on financial performance of SACCOs, the study overlooked SASRA financial regulations on assets, regulations on capital requirements, regulations on credit facilities. This study seeks to address the existing gap by assessing the effect of SASRA's regulations on capital requirements on performance of SACCOs, regulations on assets of performance of SACCOs, regulations on credit facilities on performance of SACCOs.

3. Scope of the study

The study covered influence of financial regulation on the financial performance of Sacco's operating in Kisii County, Kenya. The target population covered 70 respondents from all 10 Sacco's in Kisii County, Kenya. The study will restrict itself to; Regulations on Capital Requirements, regulations on assets; Regulations on credit i and the financial performance of Sacco's. Also the study collected the data from 2015 to 2020 from SASRA reports

4. Data Analysis and Presentation

General Information of Respondents in the Study

The study sought the general information of the respondents. The study result is summarized in Table 1 below.

Table 1: General information of Respondents in the Study

		f	Percentage
Gender	Male	37	57.1
	Female	28	42.9
	Total	**65**	**100.0**
Age in Years of Respondent	Below 30	6	9.5
	31-35	6	9.5
	36-40	25	38.1
	41-45	22	33.3
	46 years and above	6	9.5
	Total	**65**	**100.0**
Number of Years of Existence of the SACCO	Less than 1 year	3	4.8
	2-5	3	4.8
	6-10	12	19.0
	More than 10 years	47	71.4
	Total	**65**	**100.0**
Level of education of Respondents	CPS/CPA	3	4.8
	Diploma/Certificate	28	42.9
	Degree Level	31	47.6
	Post graduate Degree	3	4.8
	Total	**65**	**100.0**

The study result showed that 57.1% of the respondents were male while 42.9% were of female gender. The results revealed that majority of respondents were of aged between 36 to 40 years of age while 33.3% of the total respondents were aged between 41 to 45 years. In addition, the findings showed that 71.4% of the SACCOs have existed for more than 10 years while 19% of the SACCOs have operated for 6 to 10 years. On the level of education, the study result indicated that 47.6% of the respondents had degree level of education, while 42.9% were holders of diploma or certificate level of education.

Regulation on Capital Requirements and Performance of SACCOs

The study established the effect of regulation on capital requirements on the financial performance of SACCOs. The information obtained from the field is presented as in table 2 next page.

Table 2: Regulation on Capital Requirements and Performance of SACCOs

Core Capital to Total Assets Ration	Frequency Response per SACCO	Percentage	Rank Performance of SACCOs
Between 10% to 12% ration	1	10%	Fair
Between 13% to 15% ration	3	30%	Moderate
Between 16% to 18% ration	2	20%	High
Above 18% ration	4	40%	Very High

The results in table 2 indicate that those SACCOs with core capital to total assets ratio of above 18% are performing very highly, followed by those with 16% to 18% ration in core capital ratio. It is observed that those SACCOs with ration of between 10% which is at its minimum and 12% of the ration are struggling as their performance is fair as indicated by results in table 4.2 above

The study further established the necessity of the regulation on capital requirements towards the performance of the SACCOs. The respondents rated the following indicators as per the regulation and their contribution to performance. The responses obtained from the field are presented as in the table 3 below

Table 3: Benefit of Capital Requirements Indicators to SACCOs Performance

Benefit indicators of Capital Requirements to SACCOs	Frequency Response (Yes)	Percentage
Efficient Management of Credit within the SACCO	63	97%
Efficient provisions of a Safety Net	58	89.2%
Ensures Confidence of from the Public and Shareholders	61	93.8%
Efficient Operational Capital Benefit	54	83.1%
Promotion of Organizational Growth benefit	59	90.76%
Prevention of Illiquidity	60	92.3%

The results in table 3 reveal that efficient management of credit within the SACCO is as a result of compliance with the capital regulations and this was rated by 97% of the respondents in this study. Further the results reveal that efficient provision of safety net is possible due to the compliance to the capital requirements regulations and is indicated by 89.2% response rate. The study results show that in ensuring the confidence from the public and shareholders this capital requirements compliance is of necessity and this boost performance of the SACCO as it promotes loyalty by members. The operational capital benefit cannot be ignored, respondents at 83.1% indicated that this parameter promotes performance of SACCOs in Kenya. For organizational growth benefit 90.76% response rate indicated that compliance to this regulation promotes organizational growth in the SACCOs. Further 92.3% of the respondents indicated that compliance to this regulation helps in preventing illiquidity among SACCOs.

The study findings are in agreement with studies on Capital adequacy requirements which indicate that Capital Adequacy Ratio (CAR) or minimum amount of capital to be maintained by a financial institution (Staschen, 2013). In 1988, the first Basel Capital Accord was published, recommending a risk-weighted CAR of 8% for all internationally active banks. Since then, the ratio has gained worldwide acceptance as the minimum standard for all financial institutions. CAR protects depositors as SACCOs or financial institutions grow in size and expand their risk profile (Haq et al., 2016). According to Mathuva (2009), capital adequacy, is a major driver for the profitability of financial institutions. Further, he added that these regulations help in reducing negative externalities in addition to promoting the economic development of a country. The study added that undercapitalized institutions find themselves subjected to high levels of short term borrowings at very high costs when money is tight. Therefore SACCOs are not exceptional to this scenario.

The study results concur with other scholar in this SACCO sector of the economy. The core capital is valued as the total of the members' shares, reserves, retained earnings and donations; this amounts are not meant to be used up except on liquidation of the SACCO and must be fulfilled before licensing and must be maintained throughout the life of the SACCO (SASRA, 2019). SASRA (2019) regulations place this amount at KES 10 million or at 10% as core capital to total assets ratio. Prior to the year 2008, there were no regulations governing the deposit taking arm of SACCOs. This introduced a risk to the financial sector. The major problem was the liquidity issue (Manyara, 2003) when some SACCOs were not able to pay the members deposits on demand. As a result, the SACCO regulatory reorganizations were introduced , which required a SACCO to have a minimum core capital to KES 10 million, to safeguard member deposits and improve their loyalty and confidence in the SACCO sector (SASRA, 2010).

The capital requirements compliance is important as results in table 2 and table 3 show; according to the Sacco Society Regulations, 2010, setting a core capital for deposit taking Sacco's will grow the efficiency of running the SACCO which will in turn lead to increased productivity and improved financial performance (SACCO society's regulations, 2010). The importance of maintaining a minimum core capital is to ensure that member deposits are protected. Additionally, it guards creditors against losses that are as a result of business risks.

5. Regression analysis Results.

The study regression analysis on financial regulations and financial performance of SACCOs. The results are shown table 4 next page.

Table 4: Regression Analysis Results

Model		Unstandardized Coefficient		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	.528	.574		.920	.371
	Regulations on Capital requirements	.183	.176	.123	1.036	.315
	Goodness of Fit: R = .914[a] R^2 = .835 Adjusted R^2= .806 F = 28.754 P < 0.05(.000[b])					

a. Dependent Variable: Performance of SACCOs

b. Predictors: (Constant), Regulation on Capital Requirements, Regulation on Assets, Regulation on Credit Facilities

The results in table 4 indicate a strong and positive correlation (r= .914) between financial regulations as provided by SASRA and financial performance of SACCOs (profitability). The results further indicate that the predictor variable used in this study can explain upto 83.5% of the variation in financial performance of SACCOs (R^2 = .835, P= 0 .000 < 0.05) and the variable can be relied upon in the prediction of financial performance of the SACCOs upto 80.6% (Adjusted R^2= .806; F= 28.754; P= 0 .000 < 0.05). Substituting the Coefficients of the variables used in this study in the regression model

$$Y = \beta_0+\beta_1X_1 +\varepsilon \qquad (1)$$

for this study it becomes: $Y = 0.528+0.183X_1$. This indicate that unit compliance with capital requirements regulation results in 0.183 units increase in financial performance of SACCOs.

6. Summary

The study established that 57.1% of the respondents were male while 42.9% were of female gender. The results revealed that majority of respondents were of aged between 36 to 40 years of age while 33.3% of the total respondents were aged between 41 to 45 years. In addition, the findings showed that 71.4% of the SACCOs have existed for more than 10 years while 19% of the SACCOs have operated for 6 to 10 years. On the level of education, the study result indicated that 47.6% of the respondents had degree level of education, while 42.9% were holders of diploma or certificate level of education.

The study established the effect of regulation on capital requirements on the financial performance of SACCOs. The results indicated that those SACCOs with core capital to total assets ratio of above 18% are performing very highly, followed by those with 16% to 18% ration in core capital ratio. It is observed that those SACCOs with ration of between 10% which is at its minimum and 12% of the ration are struggling as their performance is fair as indicated by results.

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