ANALYSIS OF FACTORS AFFECTING INSTITUTIONAL CAPITAL ADEQUACY OF DEPOSIT-TAKING SAVINGS AND CREDIT COOPERATIVE SOCIETIES IN NAIROBI.

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DECLARATION

I declare that this work has not been previously submitted and approved for the award of a degree by this or any other University. To the best of my knowledge and belief, the thesis contains no material previously published or written by another person except where due reference is made in the thesis itself.

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ABSTRACT

SACCOs Regulatory Authority (SASRA) capital adequacy requirements are key to Deposit-taking SACCOs' financial stability. The purpose of this study was to determine and analyze the factors affecting the attainment of institutional capital as prescribed by SASRA. More specifically, the study sought to investigate, the effect of the quality of the board of directors, management-staff competence and dividend payout on the attainment of institutional capital adequacy, measured by institutional capital to total assets ratio. The population for the study was 40 Deposit-taking Saccos that were registered, by SASRA, to operate in Nairobi County for the year 2017. Correlational study design was used to carry out a census. A structured questionnaire was used to collect data from the respondents who were the 40 Chief Executive Officers of DT-Saccos. Both descriptive and inferential statistical methods were used to analyze data. Study findings indicated that Dividend payout, based on members' holding of non- withdrawable share capital, had the highest influence on the attainment of institutional capital adequacy of deposit-taking Saccos Management-staff competence and quality of the board are second and third respectively, in the order of influencing the attainment of institutional. The study recommends that to counter the challenge of institutional capital inadequacy, under the influence of the various factors, SASRA should consider developing a policy on institutional capital that includes members' Share Capital. This will reduce the burden of simultaneously attaining core capital and institutional capital adequacy.

Key words: *Institutional capital, Capital adequacy, Quality of the board, Management competence, Dividend payout.*

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LIST OF ABBREVIATIONS AND ACCRONYMNS

CEO: Chief Executive Officer

DTS: Deposit Taking Savings and Credit Cooperative Society

FOSA : Front Office Services Activities

IAS: International Accounting Standards

IASB: International Accounting Standards Board

ICA: International Cooperatives Alliance

IFRS: International Financial Reporting Standards

KUSCCO: Kenya Union of Savings and Credit Cooperatives

MoITC: Ministry of Industrialization, Trade and Cooperatives

SACCO: Savings and Credit Co-operatives limited

SAP: Structural Adjustment Program

SASRA: Savings and Credit Cooperative Societies Regulatory Authority

WOCCU: World Council of Credit Unions

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CHAPTER ONE: INTRODUCTION

1.1 Background to the Study

International Cooperatives Alliance (ICA) Statement on the Cooperative Identity states that a cooperative is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly owned and democratically-controlled enterprise. Owen (2007) agrees with this definition of cooperatives in Kenya and attributes the challenges facing financial cooperatives to lack of a dedicated authority to control and supervise them. In the year 2008, Savings and Credit Cooperative Societies Regulatory Authority (SASRA) was established to license, supervise and regulate the Deposit-Taking Savings and Credit Cooperative Societies (DT-SACCOs) in Kenya.

Although SASRA introduced stringent prudential standards in 2010, DT-SACCOs still face challenges attaining SASRA-prescribed capital adequacy requirements. Odera (2012) attributes the numerous Cooperative sector challenges to poor corporate governance practices and links these to corporate governance theories namely Agency, Stewardship and Degeneration, among others. Since Deposit-taking savings and credit cooperative are a key segment of the co-operative sector in Kenya, being co-operatives in their legal form and by being financial intermediaries in their business model, financial instability among Deposit-taking savings and credit cooperatives may have a ripple effect in the economy.

The principles and values for which Cooperatives exist require a sound capital base and members' confidence, within the prescribed prudential regulations. Deposit-taking savings and credit cooperative societies have underlying core values and principles that. distinguish them from other economic enterprises in which profit-maximization is the reason for existence. Kenya's co-operative movement has adopted core values, as set out by the International Co-operative Alliance (ICA).
The core values adopted are democracy, as practiced during meetings, equality, solidary and equity.

The main underlying beliefs are social responsibility, openness and honesty (SASRA,2016) Further, ICA sets out the co-operative principles that are accepted world-wide. In Kenya, the most commonly observed co-operatives principles are voluntary and open membership, mainly derived from a single employer or common activity. Other principles are member-based democratic control, dissemination of education, training and information among members, co-operation among co-operatives, and concern for community.

1.1.1 Deposit-taking Savings and Credit cooperative Societies

Deposit-taking savings and credit cooperative societies are a specific type of cooperative societies registered under the Cooperative Societies Act with a clear purpose of mobilizing savings and advancement of credit on the collateral of such savings to promote the economic interests and general welfare of that society's members (UN-Habitat,2010).

The Cooperative Societies Act Cap 490 does not provide for a legal framework towards prudential supervision of deposit-taking Sacco, this legal framework of prudential regulations is founded in the Sacco Societies Act administered by the Sacco Societies Regulatory Authority (SASRA). The purpose of these regulations is to bring, Kenya's DT-SACCOs, in line with international best practices of financial regulations and supervision of deposit-taking financial institutions (SASRA, 2010).

The institution of SASRA has established key parameters of monitoring the trends in the growth performance of DT-SACCOs. The parameters in assets, deposits, loans, membership and capital reserves. The main purpose of this study is to determine the influence of the board and management on capital adequacy, more specifically, the institutional capital adequacy given that capital adequacy determines financial stability of DT-SACCOs (SASRA, 2017).

1.1.2 The board of directors

The board of directors is the governing body of a co-operative society to whom management of its affairs is entrusted. The Board of directors is elected by the members from their membership to run the Cooperative society. Odera (2012) argued that some whereas the one-member-vote elections are democratic, it may impair the quality of the board by electing directors based on political popularity. The board has responsibility for general control, direction and management of the affairs and records of the Cooperative society. Jensen and Meckling (1976) proposed that the board of directors, being Principals need to monitor and manage activities of their Agents, Management.

While SASRA regulation 60(8) stipulates that the Board of directors shall establish such number of board committees as may be necessary to effectively discharge its function, it is imperative that such committees are aligned to the key functional units in the Sacco society (SACCO Societies Act.2008). Board committees are established to provide expertise attention and oversight to the respective operational units. This provides an effective link between the Board of directors and the management team. The committees constituted should be cost-effective and efficient without overlap. Owen (2007) had seen ineffective Boards and lack of a supervisory framework as a key challenge for Saccos. Waiganjo (2015) recommended enhancement of qualifications for the board of directors and managers and staff knowledge of SACCO operations and work experience for better staff competence.

Given that it is the board is responsible for key areas such as policy-setting, governance and strategic direction, this study aimed to examine the influence of the quality of the board on institutional capital adequacy of the deposit-taking Sacco, under SASRA's prudential regulations and the Cooperative principles and values.

1.1.3 Management and staff of Deposit-taking Saccos

Managers and staff of a Deposit-taking Saccos are employees of the Cooperative society. Managers are indeed officers of the Saccos. An officer includes a chairman, vice-chairman, secretary, treasurer, committee member, employee or any other person empowered under any rules made under the Cooperatives Act, or by-laws of a co-operative society, to give directions regarding the business of the society (Cooperative Societies Act, 2008).

The role of the manager in the DT-Sacco is to manage the day-to day operations of the DT-Sacco and report back on its implementation to be board of directors. Daily et al (2003), under Agency theory, reduces the organization into two; the Principals- owners and the Agents- the managers. On the other hand, Davis et al (1997), under Stewardship theory is in contrast and assumes that managers work in the interests of the organization rather than solely in their own interests. This study aims at establishing the influence of management and staff competence on the attainment of institutional capital adequacy.

1.1.4 Dividend

In relation to member of a co-operative society, means that member's share of the surplus of the society which is divided amongst its members, calculated by reference to the proportion which that member's share capital bears to the total share capital of the society (Co-op Soc Act, 2008).

Modigliani and Miller (1958) argued that dividend policy of a firm is irrelevant as it does not affect the wealth of the shareholders, that the value of the firm depends on the firm's earnings, as determined by the firm's investment policy. Modigliani and Miller (1958) further argued that the value of the firm is indifferent to the decision to split earnings between dividends and retained earnings.

Modigliani and Miller's arguments are contracted by the Co-operative society's model as the profit-motive and firm -valuation are not incorporated in the Deposit-taking Sacco model. In relation to this study, dividend payout influences capital adequacy because a dividend is derived from an individual member's shareholding. Whereas share capital belongs to an individual member as well as the society- core capital, institutional capital belongs to the society and is derived from retained earnings. Members are inclined to take their money to non-refundable share capital and agitate for a dividend than have the society increase capital reserves, institutional capital, through reserves.

1.1.5 Institutional capital adequacy

Savings and Credit Cooperative Societies Regulatory Authority (SASRA), which was established to license, supervise and regulate the Deposit-Taking Savings and Credit Cooperative Societies in Kenya, defines Core Capital as the fully paid up members' shares, capital issued, disclosed reserves, retained earnings, grants and donations all of which are not meant to be expended unless on liquidation of the SACCO Society. All Deposit-taking SACCOs are required to maintain a core capital: total assets ratio of 10% (SASRA Regulations, 2010).

Institutional Capital, which is the subject of this study is defined, by SASRA, as the disclosed reserves, retained earnings, grants and donations all of which are not meant to be expended unless on liquidation of the SACCO Society. This definition summarizes institutional capital as core capital less members' share capital. All deposit-taking SACCOs are required to maintain an institutional capital: total assets ratio of 8% (SASRA Regulations, 2010). The Deposit-Taking-SACCO subsector remains a major player in the financial services sector by mobilizing savings, availing credit facilities to members and increasing financial deepening and inclusion. The total membership in the DT-SACCO segment stood at 3.6 million people in 2016, having grown from 3.1 million in 2015; while gross loans rose to Kshs.297.6 billion in 2016, from Kshs.258.18 billion in 2015 (SASRA,2016).

The general criteria for measuring and evaluating the financial soundness and stability of DT-SACCOs is examining capital adequacy, asset quality, earnings and liquidity of the DT-SACCO subsector (SASRA,2016).

Whereas there have been studies on improvement of financial incomes and liquidity of DT-SACCOs, there is need to address the capital adequacy problem with respect to Institutional Capital as currently defined by the Regulator. This is made more urgent by SASRA's evidence that out of 177 licensed DT-SACCOs, only 69 maintained and complied with the prescribed institutional capital to total assets ratio of 8% while 108, the majority, failed to comply with the minimum prescribed ratio (SASRA,2016). This means that financial stability and feasibility of majority of DT-SACCOs, as going concerns in jeopardized.

There is an opportunity to address the failure, by majority DT-SACCOs, to comply with the prescribed institutional capital adequacy. Given the importance of capital adequacy as measured by institutional capital, this study will focus on the analysis of the factors that influence of the attainment of institutional capital to total assets ratio of 8%, as prescribed by the SASRA's prudential standards on capital adequacy. These factors are the quality of the board of directors-corporate governance, management-staff competence and dividend payouts.

1.2 Historical evolution of Co-operatives in Kenya

The importance of considering the historical evolution of cooperatives in Kenya is that this helps to understand the status, structure and the accompanying legal framework of the DT-SACCO subsector. The current regulatory framework influences the operations of DT-SACCOs with respect to the board of directors, management, staff and members.

Alila and Obado (1990) and Manyara (2003) agree that the evolution of the cooperative movement started with the post-independence Sessional Paper No.10 of 1965 on "African Socialism", which gave impetus to rapid Africanization of the Kenyan economy and poverty eradication based on principles like those adopted by

the Co-operative movement in the year 1970. The first Government Co-operative Development Policy was contained in Sessional Paper No.8 of 1970 with the main goal being the consolidation of the cooperative activities (MoITC,2014).

Between 1975 and 1987 there were two sessional papers. One sessional paper aimed at the government continuing to recognize cooperatives as vital organs for mobilizing material, human and financial resources for national development (MoITC, 2014). Mucai (1992) argued that it was the pressure from the Bretton Woods Institutions, the IMF and the World Bank, that forced the introduction of the Structural Adjustment Programs (SAPs) for a market economy, with emphasis on the importance of free private sector-led economic development. Another Sessional Paper No.4 of 1987, on renewed growth through the cooperative movement, the Government reiterated its commitment to enhance the participation of Kenyans in the economy through Cooperatives (MoITC,2014).

Manyara (2003) affirms that, the Government, in consultation with the co-operative bank of Kenya, re-organized and incorporated banking societies into autonomous SACCOs, with their own board of directors elected by members. In addition to incorporation of SACCOs, the Government and the Co-operative bank of Kenya assisted the new institutions with management systems, recruitment, training and development of management staff responsible for their operations. The Government also re-organized and revitalized the Kenya Union of Savings and Credit Co-operative Ltd (KUSCCO), registered in 1973, to be the apex body for all SACCOs to which they affiliate.

Manyara (2003) suggests that it is the enactment of the Co-operative Societies Act No. 12 of 1997, removing completely the government's role in the affairs of the co-operative societies that resulted in a near collapse of the entire co-operative movement in Kenya. However, on recognizing the urgency to preserve and maintain the role of cooperatives in national economic and social development, the

government pursued legislative and institutional reforms to forestall the imminent collapse of the cooperative subsector.

In response to the inadequacies of the 1997 policy, the government amended the Cooperative Societies' Act No.12 of 1997 vide the Cooperative Societies (Amendment) Act No. 2 of 2004 and prepared a new Cooperative Societies Rules 2004, which also revamped the role of the Cooperative Tribunal Court, a specialized Cooperative Commercial Court to deal with Cooperative-related cases (MoITC,2014).

Prior to the year 2008, SACCOs were administered by the Co-operative Societies Act of 1997 (MoITC, 2014) The absence of financial supervision, prudential standards and general lack of a regulatory framework resulted in weaknesses in the management of SACCOs. Odera (2012) confirmed that the absence of rules regarding quality of the board of directors and corporate governance resulted in directors being elected on political grounds and their popularity instead of appropriate skills and fitness to serve. Owen (2007) established that there were no prudential standards that limited risk exposure nor specification of disclosure requirements. Owen (2007) further stated that the audit function, in the Cooperative movement, was extremely weak, there was no provisioning for bad and doubtful debts nor were unrecoverable loans written off. As a result, portfolio quality was not reviewed leading to overstatement of revenues and assets, and no provision or under provision for non-performing loans.

Although not directly in response to the 2008-2009 global financial crisis, the Sacco Societies Regulatory Authority (SASRA) was established by the Sacco Societies Act of 2008, becoming the regulator for the DT-SACCO segment of the SACCO subsector. Capital adequacy regulations, introduced by SASRA in 2010, classify SACCOs' Capital into Core capital and Institutional capital and further explain what constitutes Equity. Core capital comprises of the fully paid up members' shares, capital issued, disclosed reserves, retained earnings, grants and donations all of

which are not meant to be expended unless on liquidation of the SACCO Society (Kenya Gazette Supplement No.39, 2010). On the other hand, Institutional capital comprises of Core capital, but less fully paid up members' shares and capital issued. Equity refers to the difference between assets and liabilities, or total of institutional capital and other capital accounts (Kenya Gazette Supplement No.39, 2010).

1.2.1 Recent Global developments

Some recent global developments, combined, with local developments collectively impact operations of deposit-taking SACCOs in Kenya. This is mainly because Kenya is an integrated economy, with local cooperative associations being affiliated to the World Council of Cooperative Unions (WOCCU).

Although financial cooperatives, world-wide, have separate statutory capital requirements per the individual regulator, financial cooperatives, such as DT-SACCOs in Kenya, are influenced by the Basel Accords on Capital Adequacy, the Basel accords provide capital adequacy guidance to commercial banks. Hoel (2008) argued that from a regulatory perspective, capital is a measure of the relative financial strength and ability to handle unexpected losses by any given financial institution and that financial institutions are expected to have adequate capital to serve as a buffer against credit, operational and market risks.

Since the financial cooperatives' business model is different from the commercial banks' model, Wilcox (2003) advocated for alternative sources of capital for financial cooperatives and, like the Basel Accord on Capital Adequacy for banks, supports the classification of the components of capital into two main categories or tiers; (i) Tier 1 or core capital consists of the types of capital considered the most reliable and permanent, such as equity and disclosed reserves and (ii). Tier 2 or supplementary capital is the second most reliable form. Tier 2 capital is that which does not, under any circumstances during the term of the instrument, require the financial institution to repay or redeem until a fixed due date or fixed maturity date.

In the year 2010, the Societies Regulatory Authority (SASRA), whose main objects and functions include licensing SACCOs to carry out deposit-taking business in accordance with the SASRA Act and to regulate and supervise SACCO societies, ushered in prudential regulations to promote and maintain financial soundness of in the DT-SACCOs subsector. Growth of members' deposits depends on the strengthening of efficiencies in access and safety to boost depositors' confidence. The capital adequacy regulation requires that a DT-SACCO must maintain the prescribed Core capital of Kshs.10 million and must maintain a prescribed Core capital to Total assets ratio of 10%, Core capital to Total Deposits ratio of 8% and Institutional Capital to total assets of 8%

The status of the DT-SACCO subsector has made the concept of Institutional capital more important for deposit-taking SACCOs than ever before. This is because Deposit-taking SACCOs operate Front Office Savings Activity (FOSAs)- whose activities are like commercial bank activities. Members deposit and withdraw money from their savings accounts and may also maintain interest-bearing Fixed Deposit Accounts. This requires a sound capital base and is the responsibility of the directors, managers and staff of DT-SACCOs to motivate members of their respective SACCOs to raise capital to the prescribed levels, since distribution of surplus to members may impair the financial stability of the SACCO and cause a ripple effect in the financial system. A financial crisis in key financial intermediaries, the DT-SACCOs, may trigger some financial stress in the economy. It is therefore important that DT-SACCOs are not undercapitalized.

Whenever financial cooperatives are undercapitalized, Wilcox (2003) proposed the use of alternative types of capital instruments. Some of the alternative sources of capital are; membership equity shares, preferred shares, trust-preferred shares, subordinated debt, uninsured long-term deposits, prorated share capital and minority stake listing. However, deposit-taking savings and credit cooperative societies, being public financial entities, are required to comply with requirements of the International Accounting Standard (IAS32). The IAS 32 Financial instruments:

presentation outlines the accounting requirements for the presentation of financial instruments, particularly as to the classification of such instruments into financial assets, financial liabilities and equity instruments (IASB). The standard also provides guidance on the classification of related interest, dividends and gains, losses, and when financial assets and financial liabilities can be offset. IAS 32 was reissued in December 2003 and applies to annual periods beginning on or after 1 January 2005.

The fundamental principle of IAS 32 is that a financial instrument, a contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity, should be classified as either a financial liability or an equity instrument according to the substance of the contract, not its legal form, and the definitions of financial liability and equity instrument (IASB). The application and interpretation of the provisions if IAS 32 pose a challenge to the boards and managers of DT-SACCOs.

In complying with requirements of IAS32, Savings and credit cooperatives societies also face limitations imposed by IFRS 2: members' shares in co-operatives entities and similar instruments". This clarifies how requirements of IAS 32 relating to debt/equity classification should be applied to co-operative entities. Many financial instruments issued by co-operative entities, including members' shares, have characteristics of equity, including voting rights to participate in dividend distributions. However, some of these instruments also give the holder the right to redeem them for cash or another financial asset. This poses a big accounting and disclosure challenge to boards and managers of DT-SACCOs.

Whereas a lot has been achieved towards ensuring compliance with the prescribed minimum prudential standards, there remain challenges such as the absence of a DT-SACCO fund for financial crisis management, absence of a deposit insurance facility and lack of a mechanism for determining suitability and fitness of persons serving or seeking to serve in key positions (SASRA, 2016). However, a major challenge that

is of special concern to the board of directors, management and staff as well as members is that by end of 2016, only 39% (69 out of 177) DT-SACCOs in Kenya, had complied with one of the prescribed capital adequacy ratios, the institutional capital to total assets ratio of 8% (SASRA, 2016). The failure, by 108 DT-SACCOs to comply with this key regulatory minimum puts into question the financial soundness and stability of the DT-SACCO subsector.

1.3 Problem statement

SASRA prudential standards require, for financial stability, that DT-SACCOs maintain the minimum capital adequacy ratios as prescribed. DT-SACCOs are required to reconstitute their boards of directors, enhance corporate governance and upgrade management-staff competence. This is expected to assist DT-SACCOs maintain financial stability and boost members confidence. Whereas most SACCOs are meeting Core capital: Total assets ratio of 10%, majority of SACCOs are finding it difficult to meet the Institutional capital: Total assets ratio of 8%. This reality is confirmed by SASRA's Annual supervisory report of 2016.

Most SACCOs have been able to achieve the Core capital: Total assets ratio (10%) and Core capital: Deposits ratio (8%) since core capital includes members' share capital. The board of directors, management and staff have been able to motivate members to boost their individual share capital holdings, initially through bonus issues and promises to declare and pay high dividends. However, the reality is that Institutional capital is raised through earnings retentions.

Individual DT-SACCO members cannot make contributions or cash injections towards Institutional capital. This means that as the 2010-2014 capital adequacy compliance window closed, directors and managers of DT-SACCOs were compelled to retain earnings at a higher rate to meet the Institutional capital: Total assets ratio of 8%. This has become a challenge to majority DT-SACCOs (SASRA,2016), hence the subject of this study.

Owen (2007), examined the status of the SACCO industry and the need for a regulatory authority. Kilonzi (2012), focused on the impact of SASRA regulations on financial performance of SACCOs, but this was before the closing of SASRA compliance window at the end of 2014. Odera (2012) showed that corporate governance is a major challenge to SACCOs.

Waiganjo (2013) focused on the impact of SASRA regulations on financial performance of SACCOs, whereas Kahuthu, Muturi and Kiweu (2015) focused on the effect of core capital on financial performance. Olando, Jagongo and Mbewa (2013) studied the impact of financial stewardship on growth of wealth for the DT-SACCO, but the context was that of investor-controlled firms rather than member-controlled DT-SACCO environment. DT-SACCOs find it easy to meet the Core capital: Total assets ratio of 10% since the definition of core capital includes members' share capital. However, Institutional capital: Total assets ratio of 8%, as prescribed by SASRA, is to be attained through profit retention. The actions by the board of directors, management and staff towards attaining Institutional capital: Total assets ratio of 8% may result in conflict with the members, additionally, total assets fluctuate from year to year. Therefore, to address the undesirable situation, there is need to analyze the factors that influence institutional capital adequacy in DT-SACCOs

1.4 Research Objectives

The research objectives originated from the desire to assist directors, management, staff and membership of DT-SACCOs to eliminate the perennial problem of struggling to attain the Institutional Capital to Total assets ratio of 8% as prescribed SASRA.

1.4.1 General objective

The general objective of this study was to examine the influence of directors, management and dividend payout on Institutional capital adequacy of Deposit-Taking SACCOs in Nairobi County.

1.4.2 Specific objectives

i. To determine the influence of the quality of the board on institutional capital of deposit- taking SACCOs in Nairobi County.
ii. To analyze the influence of the management-staff competence on institutional capital of deposit- taking SACCOs in Nairobi County.
iii. To determine the effect of dividend payout on institutional capital of deposit-taking SACCOs in Nairobi County.
iv. To determine the order of influence of factors affecting institutional capital of deposit-taking SACCOs in Nairobi County

1.5 Research questions

i. To what extent does the quality of the board of influence institutional capital adequacy of Deposit-taking SACCOs of Nairobi County?
ii. To what extent does Management and Staff competence influence institutional capital adequacy of Deposit-taking SACCOs of Nairobi County?
iii. To what extent does Dividend payout influence institutional capital adequacy of Deposit-taking SACCOs of Nairobi County?
iv. What is the order of influence of the factors affecting institutional capital of Deposit-taking SACCOs in Nairobi County?

1.6 Scope of the Study

The study investigated three factors; the quality of the board-corporate governance, management and staff competence and dividend payout influence on the prescribed institutional capital adequacy of deposit-taking SACCOs in Nairobi County. The study covered all the forty SACCOs licensed to undertake deposit-taking SACCO business, in Nairobi County for the financial year ending December 2016. The study was a census for Nairobi-based Deposit-taking SACCOs, this excluded three Nairobi-based deposit-taking SACCOs with restricted licenses and one SACCO under statutory management.

1.7 Significance of the study

Several stakeholders stand to benefit from this study: (i) Deposit-taking SACCOs: This study is likely to benefit various groups involved in the DT-SACCO business. The knowledge and guidance obtained from the study will help shape the competing expectations and demands by DT-SACCO members, staff, management, and the board of directors. The study is significant and justified because the DT-SACCO sub-sector's internal and external environment has changed tremendously since the founding of the Cooperative movement and the introduction of the SASRA prudential regulations. Members' confidence in their respective DT-SACCOs would be boosted by the findings that the Board, Management and Staff are all working towards meeting the prescribed institutional capital levels. This is because sound financial standing of the DT-SACCOs is the safety of their members' investment. (ii) The Regulator and policy makers: the regulators and policy makers will gain knowledge of the cooperative movement's dynamics and thus obtain guidance from this study in designing appropriate policies, by-law guidelines, and practices that will regulate the stakeholders in the DT-SACCO sub-sector. The study also provides a better understanding of what influences capital adequacy in member-owned financial institutions. Financial reporting standards, disclosure requirements and best practices in capital management can be tailor-made for the SACCO sub-sector (iii) Researchers and scholars: The study enables researchers to gauge the influence of the quality of the board and corporate governance on capital management and adequacy and identifies knowledge gaps on capital adequacy in SACCOs and provides suggestions for further research in areas such as optimal capital structure of SACCOs and appropriate management skills and best practices for SACCOs.(iv) Potential members and investors: potential members as well as current members will be interested in the objectives of the study with regards to examining if the board, management and staff had influence on institutional capital. Increasing money available for lending to members is possible by increasing available capital, through profit retention. Potential members and current members need to be assured that the

board, management and staff have sound practices to provide loans, to members, at lower interest rates and efficient services.

1.8 Organization of the thesis

The thesis is organized as follows: Chapter 2 summarizes information from other researchers who have carried out research in the same field of study. The specific areas covered being the theoretical review, empirical review, conclusion and conceptual framework. Chapter 3 contains the research design that was used, the population targeted, data collection instruments and procedures that were used, pilot testing and validity, data analysis and presentation. Chapter 4 presents findings of the study. The data analysis aligning with the specific objectives, research questions and inferences made on the results obtained. Chapter 5 presents a discussion of research findings in the context of the broader literature review for similar studies. Chapter 6 presents the recommendations of the study; reflects on implications of the findings, brings out the limitations and makes suggestions on areas of further research.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

This chapter reviews the main theoretical and empirical perspectives that have been used in understanding corporate governance with respect to the board of directors, management competence and dividend payout and how the various theories relate with board of directors, management and staff to influence institutional capital adequacy in deposit-taking SACCOs. The chapter also provides a summary of the empirical studies carried out in similar areas to this research study, a critique of existing literature and the research gaps. A conceptual framework, is included, explaining the relationship between the variables and how they influence capital adequacy of deposit-taking SACCOs.

2.2 Theoretical review

Cooper and Schinder (2011) define theory as a set of systematic interrelated concepts, definitions and propositions that are advanced to explain and predict phenomena. This study explores the various corporate governance theories- Agency theory, Stewardship theory and Degeneration theory.

Corporate governance tends to be more complex in Cooperative structures, compared with classical firms, due to their democratic principle for decision-making, but also because their ownership is usually much more diffuse. Agency, Stewardship and Degeneration theories are linked to each other as they explain conflicts that arise in all forms of organization, including the deposit-taking SACCOs.

2.2.1 Agency Theory

Since the early work of Berle and Means in 1932, corporate governance has focused upon the separation of ownership and pedals which results in principal-agent problems arising from the dispersed ownership in the modern corporation.

Berle and Means (1932), Pratt and Zeckhauser (1985) state that in the modern corporation, in which share ownership is widely held, managerial actions depart from those required to maximize shareholder returns Agency theory is, indeed, derived from the problems that arise from the separation of ownership and controllability. Jensen and Meckling (1976) defined the agency problem as a problem that arises when one party, the Principal, makes contract with another party, the Agent, aiming to make decisions on behalf of the Principal. Although this definition fits well with a large for profit-making organizations, it also coincides with the situations that prevail in deposit-taking SACCOs.

Abdullah and Valentine (2009) specifies that in the SACCO context, agency theory explains the relationship between the principals (members) and agents (managers and staff). Indeed, in Deposit-taking Saccos, members hire the directors by electing them to the management boards as agents. Agency theory is suitable for this study because it conceptually helps to understand Saccos as entities which are under two participants namely the SACCO members or shareholders who are principals and Sacco managers who agents.

Jensen and Meckling (1976) argued that when management's stake or interest is low, there is a greater chance that the management will involve itself in value-decreasing activities. This assertion is supported by several fraudulent activities by senior managers of big corporations all over the world. Odera (2012) cites cases of SACCO Executives setting goals which contradict those of their boards and members' interests, resulting in losses to the members. Craig (2010) suggested that the agency relationship should be viewed as the many relationships entailed in the delegation of decision-making authority from one party, the principal to another party, the agent. This implies that managerial responsibility and authority must, necessarily, be delegated from an organization's principals to their key agents. Delegation comes with risks that cause moral hazards to the executives. Jensen and Meckling (1976) asserted that it is the existence of moral hazards that provides executives the opportunity to seek for additional compensation through opportunistic means.

Jensen and Meckling (1976) further argued that some of the opportunistic means may include rent-seeking activities, fraudulent activities, conflict of interest activities. These activities, by the agents, compel the principals to increase monitoring fees and agents' incentives.

Clarke (2004) established the relevance of agency theory to SACCOs. This is due to the Principals (members) delegating the running of business to the management board, which in turn, hires and delegates authority to the managers. Indeed, Daily et al (2003) noted that two factors can influence the prominence of agency theory. First, the theory conceptually reduces the organization into two participants; the owners and the managers. Second, agency theory suggests that employees or managers in SACCOs can be self-interested. Shareholders of a SACCO, members, just like shareholders in a company, expect the agents to act and make decisions in the principals' interest. Padilla (2002) confirmed that the agents may not necessarily make decisions in the best interests of the principals.

Jensen and Meckling (1976) proposed that risk and compliance monitoring systems should be put in installed and both internal and external auditors be engaged to monitor actions by agents and costs associated with agency problems. Three types of costs identified with agency problem include: monitoring, bonding and residual costs. The cost of hiring external auditors, by the principal, to audit financial reports, prepared by agents, is an example of monitoring costs, arising from the need to prevent agents from increasing their ultimate share of incentives or bonus, thus controlling agents' self-interest driven actions. Padilla (2002) agreed that since agents will not always act in the best interests of the principals, it is logical, that the principals should extend appropriate incentives and bonuses to the agents, but also put in place monitoring mechanisms through internal control systems.

Henderson et al (1992) argued that because agents are focused on their own wealth-maximization, a mechanism should be crafted to align the manager-agent interest with owners-shareholder-principal interest. This thinking has led to the creation of schemes to align agent-principal interests.

Some of these alignment mechanisms include; employee-share-ownership programs and profit-sharing schemes, in accordance with financial performance of organizations. Production of financial statements is costly and such costs are referred to as bonding cost.

Williamson (1998) argued that, residual loss could still occur, even if monitoring and bonding costs are provided for. This is because agents could still make decisions which do not maximize principals' interest. Monitoring and bonding mechanisms do not control all agents' interests and actions, leading to residual costs of some kind whenever agents are appointed.

The principal-agent relationship, under Agency theory, may be summarized as comprising agents' propensity for self-serving actions influencing or causing agents' self-serving or owner-serving, which must be impacted by monitoring, incentives, and legal sanctions put in place by the principal.

2.2.2 Stewardship Theory

Stewardship theory has its roots in psychology and sociology. Davis, Schoorman and Donaldson (1997) defined stewardship theory as "a steward protects and maximizes shareholders wealth through firm performance, because by doing so, the steward's utility functions are maximized". Similarly, Donaldson and Davis (1997) assert that managers will make decisions and act in the best interest of the firm, putting collectivist options above self-serving options. A steward protects and maximizes shareholders' wealth through firm performance, because by so doing, the steward's utility functions are maximized. In this perspective, which is reflected in the SACCOs, stewards are managers working to protect and make surplus for the members. Since SACCO managers and staff are also members of the SACCOs they run, the managers are considered stewards, integrating their goals as part of the organization. Donaldson and Davis (1997) further suggest that managers, stewards, are satisfied and motivated when organizational success is attained.

The Stewardship theory assumes that the effective control held by professional managers empowers them to maximize firm performance and corporate profits. Stewards are empowered by the shareholders to protect and maximize the shareholders' wealth through enhancement of the profitability and return of the firm. The shareholders also provide some intrinsic and extrinsic motivation in form of managerial perks to discourage the steward from succumbing to self-interest and conflict of interest behaviors which could fall short of congruence between the aspirations of the shareholders. However, Daily, Dalton and Cannella (2003) cautioned that managers, being decision-makers, ought to ensure the firm maximizes profitability leading to the principals' maximization of return on capital employed.

Abdullah and Valentine (2009) argued that, under the stewardship concept, when an organization is successful, this will lead to happiness and motivation for the stewards, that individual success or goal attainment did not matter. The stewardship theory of governance focuses on the relationship between the board and management and on the roles of various stakeholders. This theory assumes that managers and staff are honest, trustworthy, and capable. Unlike the principal-agent theory, management and the board work together in partnership, seeking to protect both financial and nonfinancial organizational assets such as human resources and organizational reputation, and not just shareholder value. The board-management-staff-member relationships in DT-SACCOs closely resemble the scenario assumed by the stewardship theory.

2.2.3 Degeneration theory

Meister first came up with the degeneration theory in 1974, explain that the degeneration process has a life-cycle of four phases. Meister (1984) pessimistic view argued that, under the degeneration theory, mutuality is always a transient phase on a deterministic trajectory either away from mutuality to prioritize commercial goal, or towards further mutuality and accompanying commercial failure. Meister (1984) further mapped the process of degeneration into a life-cycle of four distinct phases; (i) The first phase as being characterized by high idealism and commitment which

enables the Co-operative to get off the ground. However, over time there are clashes between a direct democracy jealous of its prerogatives and an economic activity still badly established. The need for greater efficiency leads to the establishment of full-time management. (ii) Meister (1984) suggested that the second phase is a period of transition in which, if the Co-operative survives, further economic consolidation takes place and conventional principles of organization are increasingly adopted. These changes are not always accepted peacefully, and conflicts continue between idealists and managers. (iii) In the third phase, Co-operatives lose their radical ideals and market values are accepted. As the Co-operative develops, democracy becomes restricted to the management board and the gap between management and membership increases. (iv) Meister (1984) further concluded that during the fourth phase, members and the management board lose all effective power as control is assumed by managers because of their superior expertise and ability to control information. Although conflicts and pressures exist in DT-SACCOs, it is only in very few extreme cases that SACCOs degenerate through the phases assumed by the most pessimistic view of the degeneration theory.

There are counter arguments against the pessimist view. Cornforth, Thomas, Lewis and Spear (1988) argued that, with the democratic culture in Cooperatives, regeneration can take place in Co-operatives. Cornforth (1988) further suggested that Meister's four-phase life cycle seemed too pessimistic since Co-operatives have been known to progress starting with zeal to maturity, through a decline marked with lack of democracy and recruitment outside the common bond, lack of harmony between managers and members and finally to resurgence of democracy. Hernandez (2006) argued that Co-operative degeneration is not a must and Co-operatives can also regenerate. Hernandez (2006) further argued that since Co-operatives are both partially democratic and partially oligarchic, they represent unresolvable contestation between oligarchic and democratic forces. Indeed, research into challenges such institutional capital adequacy that DT-SACCOs face may offer solutions.

Cornforth et al (1988) asserts that market pressures tend, over the course of time, to lead to SACCO-operations resembling those of other enterprises, particularly for-profit-capitalist enterprises. Market pressures make themselves felt in several ways, such as price competition and liquidity of investment.

In SACCOs, these pressures are experienced as tensions of different kinds over the extent to which surpluses should be retained or distributed to members, over whether One-Member-One-Vote system should be modified, over whether the common bond should be opened or not. Attempts to resolve such tensions can lead to degeneration.

Cornforth et al (1988) suggests that degeneration in SACCOs is mainly caused by weak internal democracy and abandonment of the principle of member-ownership and control. However, the more pessimist view of degeneration theory suggests that employee-owned businesses, such SACCOs, tend towards failure- they either fail commercially, or they relinquish their democratic characters. Storey *et al* (2014) argued that co-operatives may be possible alternatives to conventional investor-owned capital firms, although recent academic literature on member-owned businesses has been dominated by the degeneration theory.

2.3 Empirical review

This section covers a discussion of previous studies related to the influence of board of directors, corporate governance, management-staff competence and efficiency and prudential regulations have on capital, financial performance and growth in SACCOs.

2.3.1 Quality of the board and corporate governance

Owen (2007) established that some SACCOs were large enough to become banks and commended the Co-operative Bank for assisting SACCOs to set up banking agencies. KUSCCO, the industry association, was also commended for its capacity to develop services that are demanded by SACCOs and its ability to remain

financially profitable over time. However, the absence of supervision was the biggest weakness of the Kenya SACCO system, while the biggest threat was competition from banks and Micro-Finance Institutions. Owen (2007) saw the proposed SASRA bill as an opportunity for the SACCO sector to consolidate and modernize, having benefited from a broad range of stakeholders.

Owen (2007) anticipated that the new law would revolutionize the SACCO sector with new financial management requirements, application of prudential rules, and proper supervision. Owen (2007) further recommended the introduction of the SASRA law and its effective implementation, ensuring a professional supervisory entity is created, and allocated adequate resources, to enforce the prudential rules.

Although Owen (2007) articulated the urgency to reform the SACCO sector, his entire study was based on secondary data, failing to capture the true sentiments of stakeholders on the ground. Collection of primary data could have changed some of the findings and final recommendations. Another critique is that the fundamental differences between the SACCO model and Bank model were not considered.

Odera (2012) agreed with Owen (2007) on the corporate governance challenges faced by Savings, Credit and Cooperative Societies (SACCOs). Odera (2012) examined both the corporate governance theories and conflicts of governance associated with SACCOs. Odera (2012) attributes the problems in SACCOs to the following; lack of clear and proper rules separating the roles of the board and management in decision-making, unqualified personnel in management, inadequate managerial competitiveness, failure by the membership to recognize that management and the board of directors have a fiduciary responsibility to ensure that all the prescribed capital adequacy requirements are maintained. Odera (2012) alludes to the board's fiduciary responsibility and ensuring that SACCOs have a firm financial base, without fully considering the prudential regulations on capital adequacy.

2.3.2 Management and Staff competence

Kilonzi (2012), with a sample size of 30 SACCOs, studied the impact of SASRA regulations on financial performance of SACCOs in Kenya, for the period between the period 2008- 2011.Financial performance was measured using Return on Assets (ROA) and Return on Earnings (ROE). Regressions were run for 2008-2009 and 2010-2011 and coefficients compared for differences. The findings were that Return on Earnings, Capital ratio, liquidity and management efficiency improved for the period 2010-2011 compared to 2008-2011.

Kilonzi (2012) covered thirty-SASRA registered deposit-taking SACCOs without indicating how this was representative of the population of DT-SACCOs in Kenya. The study's scope was limited as it only gathered secondary data from financial reports, leaving out primary data from SACCO managers and staff, further, the period covered ought to have been prior and post- the SASRA compliance window, which closed in the year 2014 In agreement with Kilonzi (2012), Waiganjo et al (2015) confirmed the positive association of high quality of the board of directors with the financial performance of DT-SACCOs and recommended more specific and stringent SASRA regulations regarding the nomination and election to the board of DT-SACCOs.

However, neither Kilonzi (2012) nor Waiganjo et al (2015) considered that the cooperative model is not based on profit-maximization. Financial performance is high when management and staff competence is high, leading to efficiency, but if capital ratios, including institutional capital to total assets ratio, are not attained, on overall basis, this is a failure to comply with prudential regulations (SASRA Supervisory report, 2016). High financial returns without a sound financial base would not be desirable. Further, Waiganjo et al (2015) did not perform a comparative analysis between pre-and post-SASRA regulations period, therefore, to attribute the significant improvement of financial performance, entirely to the SASRA regulations may not be accurate.

Olando et al (2013) examined the contribution of SACCO financial stewardship to the growth of SACCOs in Kenya, using a case study of the Meru County SACCOs. The objectives were to establish the association of loan management and the growth of SACCO wealth, establish the association of institutional strengths and the growth of SACCO wealth, and establish the association of innovativeness of SACCO products and the growth of SACCO wealth. Data was collected from forty-four SACCOs in Meru County using a questionnaire and analyzed using both descriptive and inferential statistics. Overall finding was that growth of SACCO-wealth depended on loan management, institutional strengths, and the innovativeness of SACCO products.

Kahuthu et al (2015) sought to examine if core capital requirements and member-retention had any significant impact on the deposit-taking SACCOs' financial incomes. to establish the influence of core capital and membership retention on SACCOs' financial position. The study grouped analysis results into the period before and after the regulatory reforms. Conclusions based on findings were that Core capital and membership growth have positive impact on SACCOs' financial performance.

Although Olando et al (2013) had similar objectives to the objectives of this study; namely; the influence of the quality of the board-corporate governance, management-staff competence and dividend payout on institutional capital, an indicator of financial stability, Olando et al (2013) recommendation for a review of the legal framework to ensure that institutional capital is used to grow SACCOs wealth is a contradiction of the prudential regulation on capital adequacy.

2.3.3 Dividend payout

The major theories and studies on Dividends are found in the field of financial management. Although dividend theories are relevant for the shareholder-controlled listed companies, the underlying philosophy can be extended to DT-SACCO shareholders.

Modigliani and Miller (1958) argued that dividend policy of a firm is irrelevant as it does not affect the wealth of the shareholders; that the value of the firm depends on the firm's earnings, as determined by the firm's investment policy. Modigliani and Miller (1958) further argued that the value of the firm is indifferent to the decision to split earnings between dividends and retained earnings Modigliani and Miller's hypothesis of irrelevance is based on the assumptions that; the firm operates in a perfect capital market, taxes do not exist, the firm has a fixed investment policy and the risk of uncertainty does not exist. The main criticism of the Modigliani and Miller (1958) assumptions is that they are unrealistic.

Countries designated as tax havens may provide support for the no-tax assumption. However, the reality is that withholding tax on dividend earnings, exists in most tax regimes. Modigliani and Miller (1958) equates internal financing to external financing. This is not accurate since there are costs of floating new capital issues. Breadley & Myres (2008) confirms that there are floatation costs hence the pecking order theory.

2.4 Summary of the literature

The main literature on SASRA regulations and its impact on SACCOs in Kenya is set off by Owen (2007) assertion that, due to the value of their assets, some SACCOs may convert into banks, the commendation of the Co-operative Bank for assisting SACCOs to set up FOSAs and KUSCCO, the industry association for developing services meeting demands by SACCOs and its ability to remain financially profitable at the same time. More relevant literature reviewed, Odera (2012) focused on corporate governance theories and corporate governance

challenges facing SACCOs, with specific emphasis on the roles of the board of directors, management and staff. The board's fiduciary responsibility in view of the one-member-one vote system is linked to SACCOs financial viability and survival in a competitive environment.

Further literature reviewed is by Kilonzi (2012) and Wainganjo et al (2015) who covered financial performance of DT-SACCOs in the post-SASRA era with both attributing improving financial performance to the SASRA prudential regulations, but without reviewing and comparing financial performance before the SASRA prudential regulations were enacted. Indeed, although SASRA prudential regulations took effect in 2010, DT-SACCO were granted a four-year full-compliance window which closed in the year 2014.

Reviewed literature on financial growth of SACCOs is by Olando et al (2013) and Kahuthu et al (2015) Whereas Olando et al (2013) recommended availing of institutional capital for SACCO growth purposes, SASRA's prudential regulations on capital adequacy stipulates, inter alia, that institutional capital should be maintained at 8% of total assets and should not be expended unless the SACCO is under liquidation. Similarly, Kahuthu et al (2015) established the influence of core capital and membership retention on SACCOs' financial position and financial income growth. The study grouped analysis results into the period before and after the regulatory reforms.

2.5 Research Gap

Literature review shows most studies on member-controlled Cooperative societies, in relation to financial performance, do not focus on capital adequacy and its implications for financial stability. The literature available is mainly on impact of corporate governance on investor-owned companies in the first world. The Degeneration theory literature focuses on member-owned firms, such as SACCOs, and has a pessimistic view of the Cooperative-society model. Some of these studies

may not accurately describe Kenya's thriving Cooperatives sector and the DT-SACCO scenario, which is the subject study's objectives.

A considerable number of studies have examined the relationship between corporate governance, prudential regulations, staff competence, quality of the board and SACCO membership-retention with financial performance. Owen (2007) focused on the status of the SACCO industry and the need for a regulatory authority. Kilonzi (2012), Waiganjo et al (2015) focused on the impact of SASRA regulations on financial performance of SACCOs, Olando et al (2013) focused on financial stewardship and growth, Odera (2012) focused on corporate governance challenges and Kahuthu et al (2015) focused on the effect of Core Capital requirements on financial returns of SACCOs. However, capital adequacy, as a basis for financial stability in DT-SACCOs in Kenya, is not covered.

SASRA Reg. 9 of the Regulations 2010 requires DT-SACCOs to maintain the prescribed minimum core capital of not less than Kshs 10 Million; in addition to the prescribed capital adequacy ratios of core capital to total assets, core capital to total deposits and institutional capital to total assets of 10%, 8% and 8% respectively (SASRA, 2016).

The aim of this study is to fill the research gap on DT- SACCO capital adequacy in relation to the influence of the quality of the board of directors, corporate governance, management-staff competence and dividend payout on institutional capital, as prescribed by SASRA. Nairobi County has been selected; being home to the largest DT-SACCOs with a national coverage. This study is particularly relevant to the operations of DT-SACCOs since they are now in direct competition with commercial banks. Whereas commercial banks are supervised and licensed by the Central Bank of Kenya, SASRA licenses and supervises DT-SACCOs. Additionally, the study draws attention to the need to appreciate the reality that DT-SACCO members' share capital is not withdrawable and has no capital market.

2.6: The Conceptual Framework

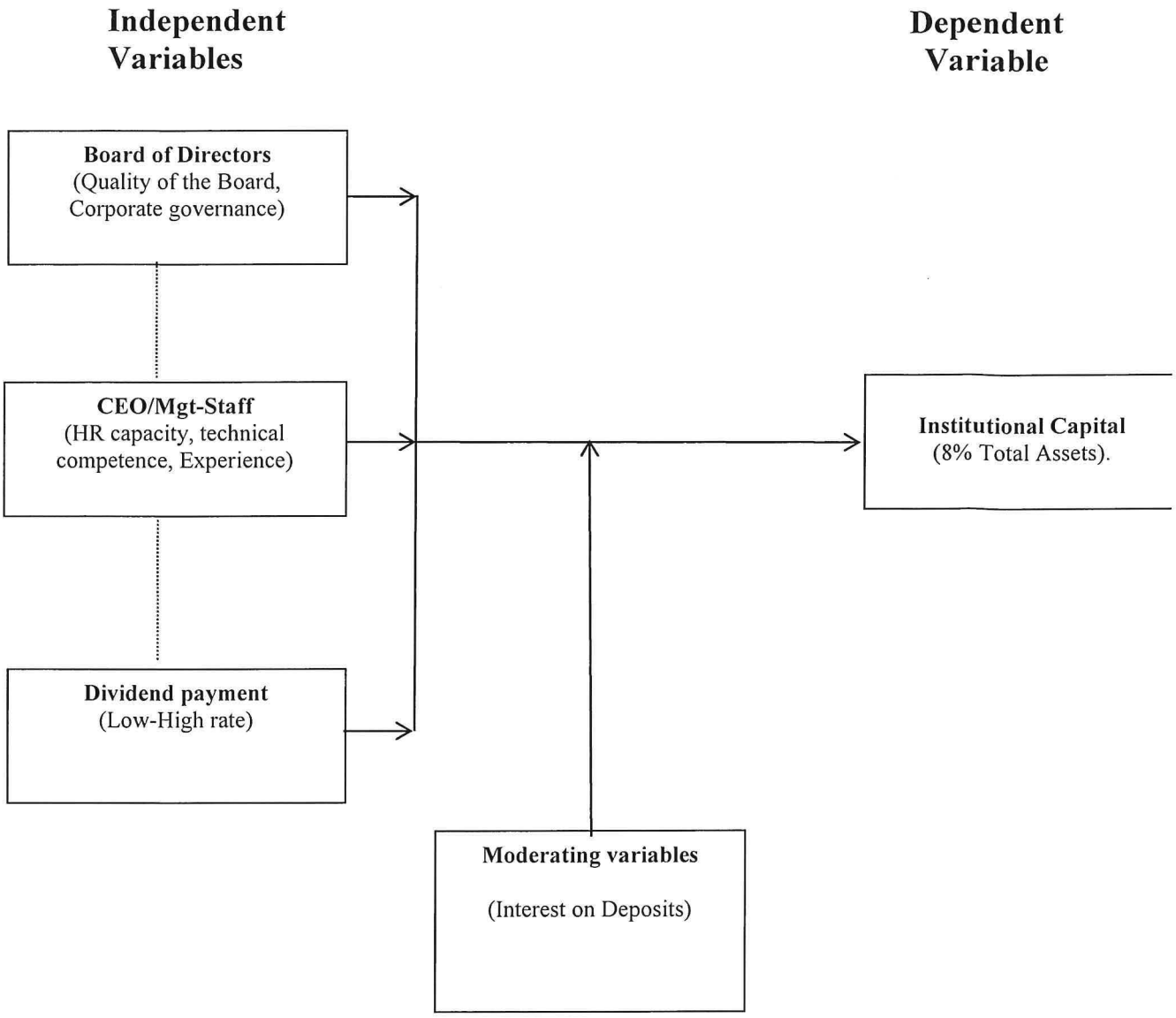

Figure 2.1 The conceptual framework

In the conceptual frame work, the dependent variable is the institutional capital which is affected or influenced by the independent variables namely, quality of the board and corporate governance, management and staff competence, and dividend payment. The moderating variable between independent and dependent variables is the interest payments. Overall composition of the board in terms of work experience, training and knowledge of SACCO operations and independence is what constitutes

good quality of the board. The board gives direction to the SACCO through the Chief Executive Officer.

Table 2.1: Operationalization of the study variables

Variable	Indicators	Measure 5-point rating scale	Supporting Literature
Quality of the Board of Directors (Independent Variable)	-Corporate governance structures, manuals. - Independence. -SACCO-management	1= Strongly disagree 2=Disagree 3=Neutral 4=Agree 5=Strongly agree	Owen (2007), Odera (2012) Waiganjo et al (2015).
CEO-Managers-Staff competence (Independent Variable)	-Competence. -Work Experience. -Professional Qualifications. -SACCO-management.	1= Strongly disagree 2=Disagree 3=Neutral 4=Agree 5=Strongly agree	Owen (2007), Odera (2012) Waiganjo et al (2015) -Kilozi (2012), Olando et al (2013), Kahuithu (2015)
Dividend payout (Independent Variable)	Knowledge on; -Sources of Capital. -Capital structure. -Appropriation of surpluses and SASRA regulations.	1= Strongly disagree 2=Disagree 3=Neutral 4=Agree 5=Strongly agree	Owen (2007) Odera (2012) Waiganjo (2015)
Institutional Capital (Dependent variable)	-Less than 8% -Equals 8% -Above 8%	1= Strongly disagree 2=Disagree 3=Neutral 4=Agree 5=Strongly agree	Owen(2007)Odera(2012) Waiganjo (2015) -Olando(2013) Kahuthu(2015)

Quality of the Board of directors and Corporate governance - Quality is fitness of purpose. Measured by examining qualifications of members of the board, whether board members have passed the Proper and fitness test, frequency of board training and examining the number of years of work experience. Corporate governance,

measured in terms of implementation of board manuals, independence in decision-making, accountability and transparency and relationships with management and auditors and dissemination of member-education.

Labie and Mersland (2011) defines corporate governance as system or set of mechanisms by which an organization is directed and controlled to attain its mission and objectives. Measured in terms of existence and implementation of the code of conduct of board of directors and the fit and proper test.

Managers-Staff Competence: Competence means having skills, traits and knowledge required for a person to be effective in a job. -measured by level of education, working experience, participation in decision-making, participation mentorship programs, adequacy and relevance of their knowledge of SACCO industry issues, professional qualifications, frequency of staff training and membership of professional bodies, and support for member-education.

Dividends-Measured by perceptions and understanding of dividends as a return on share capital holders, knowledge and understanding of the SASRA requirements on separation of deposits and share capital, understanding of when dividends are paid and the policy. Understanding of effects of dividend payment on share capital levels, understanding of the different categories of capital, perceptions of satisfaction on actual dividends declared.

Institutional Capital adequacy- Knowledge of the definition of and components of core capital and institutional capital, computation and levels of institutional capital since SASRA capital regulation came into force, the actual capital ratios as of 31st December 2016, comparing with SASRA requirements.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter provides a discussion on the design and methodology adopted in this study. The chapter details the research design, population, instruments, data collection procedures and data analysis techniques that were used in the study.

3.2 Research Design

The cross-sectional design was adopted. Saunders, Lewis and Thornhill (2012) defines cross-sectional design as one that is a "snapshot" taken at one moment in time. More specifically, correlational research design was used to determine the relationships between different independent variables and the Institutional capital: Total assets ratio of 8 percent as prescribed by SASRA.

3.3 Population.

As at January 2017, SASRA had fully licensed 40 SACCO Societies to undertake deposit-taking SACCO business in Nairobi for the financial year ending December 2017. These 40 SACCOs were the population of interest for this study. Since the population size was small, all the 40 SACCOs were targeted. The study was carried out in these deposit-taking SACCOs to establish the influence of the quality of the board, management-staff competence and dividends on institutional capital as at 31st December 2016. This was two years after the SASRA prudential regulations compliance window (2010-2014) had closed. The targeted respondent SACCOs were represented by their respective Chief Executive Officers, being the person with the professional information on individual SACCO operational matters and SASRA prudential regulations compliance status. This information was pertinent to the completion of the questionnaires, which were developed in consultation with ordinary members, some directors and staff of the researcher's Sacco.

3.4 Data Collection Methods

A research questionnaire was used to collect primary data. Questionnaires were sent to Chief executive officers in all the forty Nairobi-based Deposit-taking SACCOs. The Chief executive Officers to responded to the same set of questions that were designed in line with the research objectives.

Closed-ended questions were used for ease of analysis. The questionnaire was divided into Section A: to capture general information on the respondent SACCO, Section B: to cover quality of the board/corporate governance, Section C: to cover Management-Staff competence, Section D: to cover Dividend payments on members' share capital and Section E: to cover capital adequacy status, on self-disclosure basis. Secondary data was collected from SASRA's SACCO Supervision Annual Reports for 2015, 2016 and 2017.

3.5 Data Collection Procedure

Clearance to carry out the study was sought from Strathmore University, School of Business. The United Nations SACCO's marketing intern informally accepted to assist in this study, this being the researcher's SACCO. The marketing intern provided a list of Chief Executive Officers. The respondents were assured that information obtained was purely for educational purposes. A self-administered questionnaire was applied for data collection. Saunder et al (2012) confirmed that a self-administered questionnaire is cost-effective, easier to analyze, most people are familiar with it, it is more standardized, objective, less intrusive and least disruptive to the respondents' operations. After the initial contact and introduction, the drop-and-pick-later method was used, with the study maintaining care and control to ensure questionnaires issued were accounted for.

3.6 Reliability

In this study, the reliability of the instrument was tested using Cronbach Alpha on the study respondents. However, the recommended formula (N/10+K) was simplified to exclude K, where N is 40 and K is 10. The result obtained a sample of 4 respondents and 4 questionnaires were distributed with an intention of pre-testing

the questions. Pilot testing done to determine any weaknesses in the interview design.

A reliability test was carried out using the internal consistency technique, assessed using the Cronbach Alpha Coefficient. The standard is that reliability should be at least 0.70 or higher. If coefficient alpha of 0.7 is obtained, the instrument is accepted otherwise it will be revised to attain accepted standard, equal to or greater than 0.7.

$$\alpha = \frac{N.\bar{c}}{\bar{v} + (N-1).\bar{c}}$$

Where N=number of items, C-bar is the average inter-item covariance among items and v-bar = the average variance. The coefficient obtained was 0.8 and this being higher than 0.7, was accepted for the data being examined.

Table 3.1 Reliability Test of results

Reliability Statistics		
	Cronbach's Alpha	**N of Items**
Quality of the Board -Corporate Governance	.763	13
Management Staff competence	.870	8
Dividend payout	.820	9

Table 3.1 shows that the statements and responses provided under each independent variable was not consistent because they had alpha value of less than 0.75. However, the statements were used in the analysis as they remain relevant for this study.

3.7 Data Validity

In keeping with Saunders *et al* (2009) definition that validity is the extent to which data collection method or methods accurately measure what they were intended to measure, the researcher discussed the questionnaires with some respondents before distributing them.

3.8 Data analysis

After data collection, to enhance accuracy and precision, questionnaires were coded and edited to detect errors and omissions. Descriptive and inferential statistics were used to analyze results Data was further analyzed using SPSS software.

Demographic information and descriptive statistics were presented followed by inferential statistics.

Factor analysis, a measurement model of a latent variable, was used because of the multiple variables involved in the study, with similar patterns of responses and all associated with a latent variable, the anxiety of failure to attain institutional capital adequacy ratio.

The data reduction techniques capture the variance in variables in smaller sets. The Eigenvalue is a measure of how much of the variance of the observed variables a factor explains. Eigenvalues were used in this study to measure how much of the variance there is in each variable and the change in direction of the screen plot confirmed how many factors to include in the analysis.

Principal component analysis is a data reduction technique. It was also used in this study because of its ability to capture the variance in many variables in a smaller easier- to-work set of variables. Principal component analysis uses composite variables or components, as predictors, instead of the variables- this avoids the challenges of potential multicollinearity.

3.9 Ethical Issues

All ethical principles were observed by researcher: Integrity and objectivity was maintained through acting openly, truthfully and promoting accuracy. Respect, avoidance of harm and privacy of those taking part in the research were of paramount importance.

The researcher fully explained to the respondents the voluntary nature of participation and the right to withdraw, leading to informed consent to participate under confidentiality and anonymity of information and respondents.

CHAPTER FOUR: DATA ANALYSIS, RESULTS AND INTERPRETATIONS

4.1 Introduction

This chapter presents the findings of the data as described in chapter three. The unit of analysis was a Deposit-taking SACCO, as targeted population was all the 40 licensed deposit-taking SACCOs in Nairobi as at 31st December 2016. Descriptive statistics was performed to establish the characteristics of the population. Data analysis was in line with the specific objectives, research questions and inferences made on the results obtained.

4.1.1 Response rate

Out of the 40 questionnaires administered, 32 were filled and returned. This represents 80% response rate. Mugenda and Mugenda (2003) suggested that a response rate over 50% is considered very good and reasonable to make conclusions for the study. A high response rate in this study is attributable to the Chief Executive Officers' interest in the research study and a diligent research assistant.

4.1.2 Demographic characteristics of the DT- SACCOs

The demographic data of the respondent SACCOs are categorical variables which provide some basic underlying knowledge about the SACCOs. The characteristics considered were age of the SACCOs, source of membership and size of SACCO by number of members, staff and directors. Data was collected using questions in Section A of the Questionnaire- found in Appendix 3.

4.1.3 DT- SACCOs' age distribution

DT-SACCO ages range between 11 to over 30 years as indicated in Table 4.1 below.

Table 4.1 DT-SACCO by age

	11-20 years	21-30 years	Above 30 years	Total
Frequency	3	3	26	32
Percentage (%)	10%	10%	80%	100%

The age demographic characteristics indicated that 3 SACCOs (10%) were between 11-20 years old, another 3 (10%) were 21-30 years old whereas 26 (80%) were above 30 years old, this is an indication that 80% of the Nairobi- based SACCOs had lived through the various legal and regulatory changes that affected SACCOs in the last 30 years, therefore, although SASRA's capital adequacy regulations are stringent, they are not the first regulatory reforms experienced by the respondent SACCOs.

4.1.4 DT- SACCO by source of membership.

Table 4.2 below shows DT-SACCO by source of membership.

Table 4.2 SACCO by source of membership

	Frequency	Percentage (%)	
Employees of Parent Org.	3	10%	
Employees/Retirees of Parent Org.	23	70%	
Employees/Dependents of Parent Org.	3	10%	
Open to all	3	10%	
Total	32	100%	

The majority of DT-SACCOs derive membership from a single employer. 23 (70%) of respondent SACCOs derive their membership from one employer in the category of current employees and retirees. This implies that membership from a single employer and bond may be easier to manage, disseminate knowledge and education as expected from the Cooperative societies in keeping with the spirit of the cooperative movement.

Other sources of membership were Employees of Parent organization only 3 (10%) Employees and dependents of parent organization only 3 (10%) and Open-to-the public membership 3 (10%). Different sources of membership have different implications for the board of directors and management of DT-SACCOs

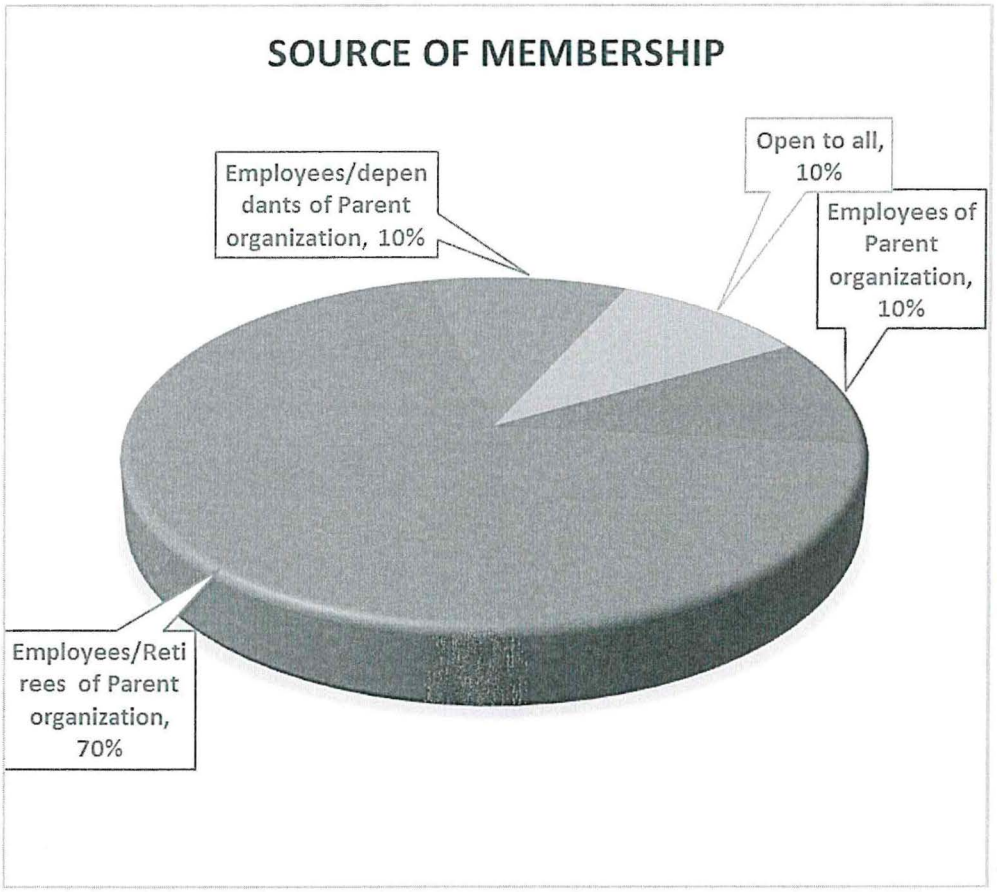

Figure 4.1. SACCO by source of membership

Figure 4.1 shows the sources of members for the 32 DT-SACCOs in the study.

4.1.5 Respondent SACCOs' size by number of employees.

Table 4.3 below shows the range of number of staff employed by DT-SACCOs as 15 to over 35 employees.

Table 4.3 DT-SACCO by number of Staff

	15-25	26-35	Above 35	Total
Frequency	16	3	13	32
Percentage (%)	50%	10%	40%	100%

Classification by number of employees indicates that 50% (16) of DT-SACCOS have between 15-25 staff members followed by 40% (13) of DT-SACCOS employing over 35 staff and 10% (3) of DT-SACCOs employing. between 26-35 staff. This may suggest increased levels of automation, with ICT aiding decision-making.

4.1.6 Respondent SACCOs' size by number of members.

Table 4.4 below shows DT-SACCOs by number of members.

Table 4.4 Size of SACCO by number of directors

	2,501-4,000	4,001-5,000	Over 5,000	Total
Frequency	3	9	20	32
Percentage (%)	10%	30%	60%	100%

DT-SACCO classification by number of members indicated that 60% (20) of DT-SACCOS have over 5,000 members followed by 30% (9) of SACCOS with members between 4,001- 5,000 and 10% (3) of SACCO having 2501-4000 members. A high number of members may imply high complexity in management of the DT-SACCO.

4.1.7 Respondent SACCOs' size by number of directors.

Table 4.5 below shows DT-SACCO by number of directors

Table 4.5 DT-SACCO by number of directors

	6-8	9-11	Total
Frequency	6	26	32
Percentage (%)	20%	80%	100%

Categorization by number of directors shows that 80% (26) of SACCOS have between 9-11 directors, whereas 20% (6) have between 6-8 directors. This numbers suggest adherence to guidelines on the maximum number of directors and ease of doing board business. SACCOs are expected to maintain an odd number for avoidance of stalemates whenever a vote is necessary.

4.2 Qualitative results

The study sought to find out the CEOs' perceptions on the influence of the quality of the board of directors, Management-Staff competence and Dividend payouts, as independent variables, on the Institutional Capital, the dependent variable. Data was collected from the Chief Executive Officers in the various SACCOs using a questionnaire (Appendix 3).

4.2.1 Capital adequacy status as at 31st December 2016.

Capital adequacy status as at 31st December 2016 indicated that 59% (19) of the DT-SACCOs had not attained the institutional capital to total assets ratio of 8%. This meant that only 41% (13) of the DT-SACCO complied with SASRA prudential regulations on institutional capital adequacy.

The Core capital to total deposit liabilities ratio was attained by all the 32 (100%) DT-SACCOs whereas the core capital: total assets ratio of 10% was attained by 81% (26) of the DT-SACCOs with 19% (6) failing to attain this ratio. The purpose of attaining and maintaining capital adequacy ratios is to ensure all Deposit-taking SACCOs are put on sound financial footing, to avoid financial stress in the subsector and the general financial system.

Table 4.6 Capital adequacy status as of December 2016.

	Number of SACCOS below Statutory ratio	Number of SACCOS On/above Statutory Ratio	Total
Core capital to assets (10%)	6 (19%)	26 (81%)	32
Core capital to total deposit liabilities (8%)	0	32(100%)	32
Institutional capital to total assets (8%)	19 (59%)	13 (41%)	32

Source: Researcher

Table 4.6 on capital adequacy indicates that Core capital: Total assets: 26 (81%) attained the requirement whereas 6 (19%) failed to meet the requirement. Core capital: Deposits: 32(100%) met the requirement. Institutional Capital: Total assets:13(41%) met the requirement whereas 19(59%) failed to meet the requirement.

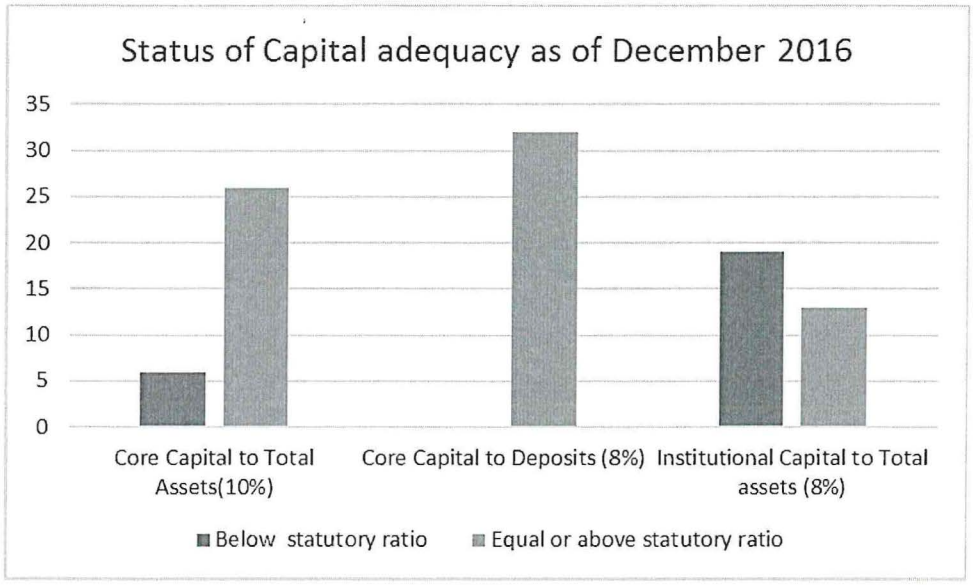

Figure 4.2 Capital adequacy status 2016.

Figure 4.2. depicts the Capital adequacy status at the end of 2016, for Nairobi County DT SACCOs.

4.2.2 Alternative capital in issue as at 31st December (2012-2016).

All 32 DT-SACCOs had issued membership equity shares and none had issued any alternative sources of capital. The alternative sources of capital, that could be used by DT-SACCOs, are membership equity shares, Preferred shares, Prorated share system capital which can be raised from members only. Other types of capital, requiring amendment of SASRA's regulations, are Trust-preferred shares, Subordinated Debt, Uninsured Long-term deposits and Minority stake listing.

4.3 Inferential statistical analysis

This section presents the results of several data reduction techniques and correlation carried out in the study to evaluate the nature of the relationships between the independent variables and the dependent variable. The Chief Executive Officers were requested to state their level of agreement with the statements in the questionnaire, ranging from Strongly Agree with highest weight to Strongly Disagree with the lowest weight. To convert these responses into quantitative data,

for ease of analysis, weights on a five-point Likert scale ranging from 5= Strongly Agree to 1= Strongly Disagree were assigned.

The combination of reduction techniques used, in the SSPS software, were: Factor analysis, a measurement model of a latent variable, was used because of the multiple variables, involved in the study, with similar patterns of responses and all associated with a latent variable, the anxiety of failure to attain institutional capital adequacy ratio. Factor loadings are part of the outcome from factor analysis, which serves as a data reduction method designed to explain the correlations between observed variables using a smaller number of factors. Factor loadings are coefficients found in a factor pattern matrix.

The data reduction techniques capture the variance in variables in smaller set.

Eigenvalues are used in this study to measure how much of the variance there is in each variable and the change in direction of the screen plot confirms how many factors to include in the analysis.

Principal component analysis is a data reduction technique. It is also used in this study because of its ability to capture the variance in many variables in a smaller easier- to-work set of variables. The Principal component analysis uses composite variables or components, as predictors, instead of the variables themselves, thereby, avoiding potential multi-collinearity.

4.3.1 Quality of the board of directors

For the quality of the board of directors and corporate governance, as an independent variable, exploratory factor analysis (EFA), a data reduction technique, was performed to condense a set of 13 questions into groups that reflect underlying latent factors. Questions with factor loading of less than 0.4 were dropped from the analysis. Factor rotation was used where more than one factor was generated. The factors loadings were checked to remove questions which had factor loadings less than 0.4. Cronbach's alpha value of 0.7 or higher is considered satisfactory and any measure of internal consistency with a value <0.7 was considered unsatisfactory, hence was dropped. The latent variable was computed using descriptive statistics, the mean.

4.3.1.1 Factor extraction - Quality of the board

Principal component analysis was used to identify factors, independent variable statements, that account for the highest variability and new factors, statements, extracted based on the total variance.

Table 4.7 Principal Component Analysis (Quality of the board)

Total Variance Explained						
		Initial Eigenvalues		Extraction Sums of Squared Loadings		
Component	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	5.149	39.605	39.605	5.149	39.605	39.605
2	2.868	22.058	61.663	2.868	22.058	61.663
3	1.730	13.305	74.968	1.730	13.305	74.968
4	1.005	7.733	82.701	1.005	7.733	82.701
5	0.704	5.418	88.118			
6	0.605	4.652	92.770			
7	0.374	2.877	95.647			
8	0.285	2.192	97.839			
9	0.192	1.477	99.316			
10	0.079	0.606	99.922			
11	0.010	0.078	100.000			
12	0.000	0.000	100.000			
13	(0.000)	(0.000)	100.000			
Extraction Method: Principal Component Analysis.						

Table 4.7 shows the 4 components of the quality of the board-corporate governance independent variable, used in the Factor Analysis. The initial Eigenvalues are the variances of the factors to be extracted. The total column contains the Eigenvalue. The first factor, with highest Eigenvalues, account for the most variance. The next factor accounts for as much of the left-over variance as it can and the same will continue until the last factor. The percentage of variance represents the percent of total variance accounted by each factor and the cumulative percentage gives the cumulative percentage of variance accounted.

The section labeled "Rotation Sums of Squared Loadings," shows those factors that met cut-off criterion, the extraction method only. The eigenvalues- greater-than-one rule is one way of choosing the number of components that can be extracted.

Under the first objective, examining the influence of the quality of board on institutional capital, using the greater-than-1 rule, four factors or components with eigenvalues greater than 1 were identified. Instead of examining all the thirteen components, only four are examined: The Factor 1: "All Board members have more than five years of work experience" with eigenvalue 5.149 accounting for 39.605% of the variability in all the 13 variables.

Factor 2: "All Board members have appropriate SACCO- management training, education and knowledge" with eigenvalue 2.868 accounting for 22.058% of the variability in all the 13 variables.

Factor 3 "Directors are frequently trained on SACCO management and operations with eigenvalue of 1.730 accounting for 13.305% of the variability in all the 13 variables and

Factor 4: "Directors have relevant professional qualifications in addition to financial literacy" with eigenvalue 1.005 accounted for 7.733%. of the variability in all 13 variables These four factors explain 82.701% of the total variability. Since the first four factors have Eigen values greater than 1, this means they accounted for most variability. This is confirmed by a screen plot, mapping eigenvalues against all the components.

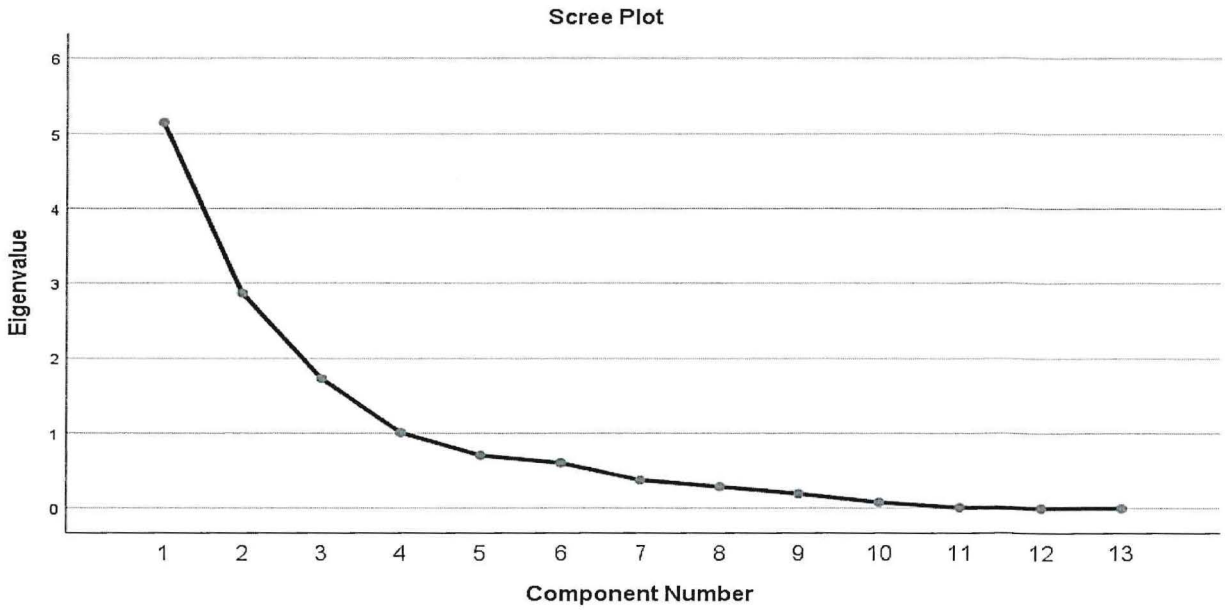

Figure 4.3 Eigenvalue-Principal Component (Quality of the board)

Figure 4.3 confirms the number of factors to be extracted-using the greater than 1 rule. In this case the curve started to level off or becoming less steep after the fourth component hence only four factors were extracted.

4.3.1.2 Factor rotation- Quality of the board of directors

After extraction of factors, the variables were subjected to varimax rotation. The Rotated component matrix represents the rotated factor loadings, which are the correlations between the variables and the initial three factors. The factor column represents the rotated factors that have been extracted out of the total factor.

The matrix gives the correlation of the variables with each of the extracted factors. Each of the variables is highly loaded in one factor and less loaded towards the other factors. To identify the variables, included in each factor, the variable with the maximum value in each row is selected to be part of the respective factor.

Table 4.8 Rotated Component Matrix (Quality of the board)

Rotated Component Matrix[a]				
	Component			
	1	2	3	4
SecB_19	0.967	0.105		
SecB_18	0.967	0.105		
SecB_17	0.967	0.105		
SecB_13	0.898	-0.202		0.256
SecB_11	0.702	-0.230		0.332
SecB_15	0.602	-0.441		0.356
SecB_113		0.934		
SecB_110		0.896		0.338
SecB_112	-0.108	0.874		
SecB_16			0.892	
SecB_14	-0.114		0.869	-0.203
SecB_12	0.222			0.818
SecB_111	0.172	0.224	-0.370	0.710
Extraction Method: Principal Component Analysis. Rotation Method: Varimax with Kaiser Normalization. a. Rotation converged in 5 iterations.				

Table 4.8 indicates that Factor 1 comprises the questions as to whether; (i) the board members have autonomy and freedom in decision-making (0.967), (ii) DT-SACCO had a board evaluation manual and documented code of conduct for directors (0.967), (iii) the board ensures that the Supervisory Committee and Internal audit work independently and harmoniously (0.898), (iv) directors are frequently trained on SACCO management and operations (0.702), (v) all board members have more than five years of work experience and (vi) as to whether board reconstitution takes place at least once a year (0.602).

Factor 2 comprises questions examining as to whether;(i) the board is aware of other sources of capital, other than members' equity (0.934), (ii) there is enough separation of power and responsibilities between management staff and the directors (0.896) and (iii) the board has a positive perception of external sources of capital (0.894). Factor 3 comprises two questions; (i) as to whether the board of directors

engages and rotates competent external auditors (0.892) and (ii) directors have relevant professional qualifications, in addition to financial literacy (0.869).

Factor 4 comprises two questions; (i) as to whether all board members have appropriate SACCO management training, education and knowledge (0.818) and (ii) as to whether the board leads the responsibility for attainment of capital adequacy ratios to SASRA's prescribed levels (0.710).

4.3.1.3 Correlation analysis -Quality of the board

The study sought to obtain the CEOs' perceptions on whether the quality of the board and corporate governance systems put in place influence impact on institutional capital adequacy level. To do this, Spearman's rank correlation analysis was performed to check for the relationship between the various independent variables, four factors generated using principal component analysis and the dependent variable, institutional capital. Spearman's rank correlation coefficient (Rs) ranges from -1 to 1. (i) The 00- 0.19 range shows very weak relationship, (ii) the 0.20-0.39 range shows weak relationship, (iii) the 0.40-0.59 shows moderate relationship, (iv) the 0.60-0.79 range shows strong relationship and (v) the.0.80 -1.0 shows very strong relationship.

Table 4.9 Spearman's rho Correlations (Quality of the board)

Spearman's rho Correlations						
		Factor 1	Factor 2	Factor 3	Factor 4	Institutional Capital
Factor 1	Correlation Coefficient	1.000	-0.203	**.500***	-0.309	**-.500***
	Sig. (2-tailed)		0.352	0.015	0.152	0.015
	N	23	23	23	23	23
Factor 2	Correlation Coefficient	-0.203	1.000	0.152	-0.365	**.505***
	Sig. (2-tailed)	0.352		0.489	0.087	0.014
	N	23	23	23	23	23
Factor 3	Correlation Coefficient	**.500***	0.152	1.000	-0.244	-0.197
	Sig. (2-tailed)	0.015	0.489		0.262	0.367
	N	23	23	23	23	23
Factor 4	Correlation Coefficient	-0.309	-0.365	-0.244	1.000	-0.237
	Sig. (2-tailed)	0.152	0.087	0.262		0.277
	N	23	23	23	23	23
Institutional Capital	Correlation Coefficient	**-.500***	**.505***	-0.197	-0.237	1.000
	Sig. (2-tailed)	0.015	0.014	0.367	0.277	
	N	23	23	23	23	23

*. Correlation is significant at the 0.05 level (2-tailed).

The results in the Table 4.9 show (i) that there was a moderate relationship (0.40-0.59) between institutional capital and Factor 1- (Board members having more than five years of work experience). This relationship between institutional capital and Factor 1 was negative (-0.500) and statistically significant at 1% significance level (R_s = -0.500, p value = 0.015< 0.05). (ii) There was a moderate relationship (0.40 - 0.59) between institutional capital and Factor 2- (Board members having appropriate SACCO-management, training, education and knowledge). This relationship between institutional capital and Factor 2 was positive (0.505) and statistically significant at 5% significance level (R_s = 0.505, p value = 0.014< 0.05).

(iii)Factor 3- (Directors having frequent training on SACCO management and operations) and (iv) Factor 4- (Directors having relevant professional qualifications in addition to financial literacy) had a very weak (00-0.19) relationship with

institutional capital and negative correlation coefficient which was not statistically significant at 5% level of significance (R_s = -0.197, p value = 0.367 > 0.05) and (r_s = -0.237, p value = 0.277 > 0.05) respectively.

The results are in line with Odera (2012) attributing corporate governance challenges in SACCOs to lack of clear and proper rules separating the board's responsibilities from day to day management and decision-making, unqualified directors on the board, and ineffective one-member-one vote board election system.

4.3.2 Management and Staff competence.

Using a set of nine relevant questions in the questionnaire, the study sought to obtain the perceptions of CEOs concerning the influence of management and staff competence on attaining of institutional capital adequacy as required by the prudential regulations.

4.3.2.1 Factor extraction- Management and Staff competence.

Principal component analysis was used to identify factors, independent variable statements, that account for the highest variability and new factors, statements, extracted based on the total variance.

Table 4.10 Principal Component Analysis (Management-staff competence)

Total Variance Explained						
	Initial Eigenvalues			Extraction Sums of Squared Loadings		
Component	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	3.255	36.164	36.164	3.255	36.164	36.164
2	2.598	28.862	65.026	2.598	28.862	65.026
3	1.353	15.030	80.056	1.353	15.030	80.056
4	1.013	11.254	91.310	1.013	11.254	91.310
5	0.513	5.700	97.011			
6	0.201	2.228	99.238			
7	0.069	0.762	100.000			
8	0.000	0.000	100.000			
9	0.000	0.000	100.000			
Extraction Method: Principal Component Analysis.						

Table 4.10-the principal component analysis shows how the four factors were extracted, using the eigenvalue greater than 1 and variability.

Factor 1-(i) External and internal training sessions for management and staff are regularly carried out, had eigen value of 3.255 accounting for 36.164% of the variability out of the 9 variables. (ii) Factor 2- Management encourage staff development had eigen value of 2.598 accounting for 28.862% of the variability (iii) Factor 3- Performance appraisals for staff are conducted frequently, at least once a year had eigen value of 1.353 accounting for 15.030% and (iv) Factor 4- Staff has relevant SACCO management skills had eigen value of 1.013 accounting for 11.254%. These factors explain 91.310% of the total variability. Since the first 4 factors have Eigen values above 1, this means they account for most variability.

Figure 4.4 Eigenvalue-Principal Component (Management-staff competence)

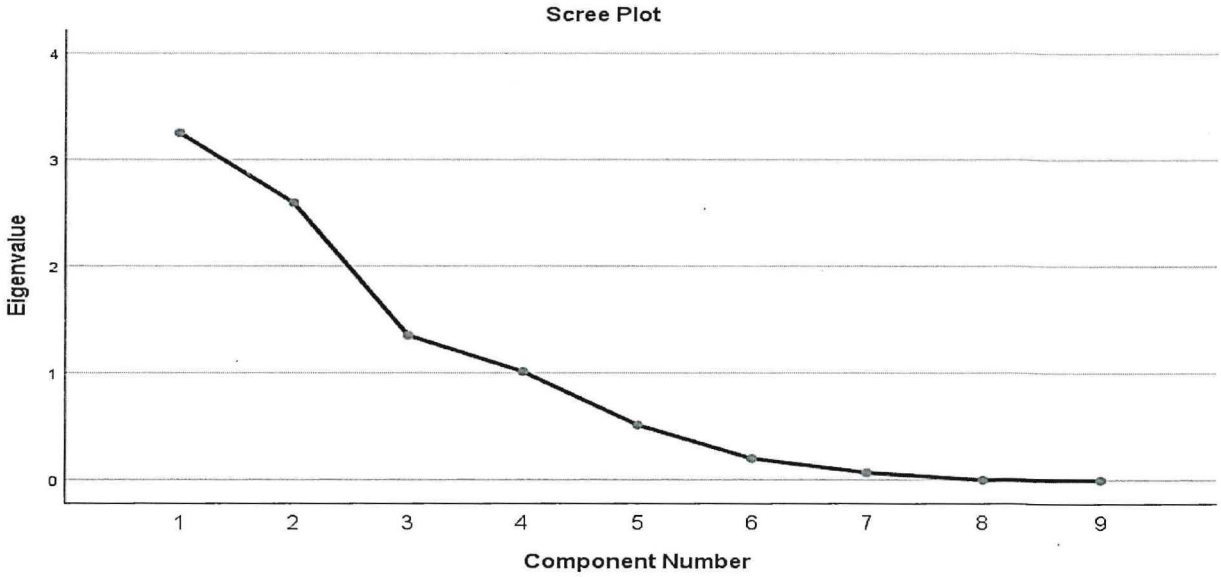

Figure 4.4 shows that the curve started to level off or becoming less steep after the fourth component, confirming that only 4 extracted factors are relevant.

4.3.2.2 Factor rotation- Management and Staff competence.

After extraction of factors, the variables were subjected to varimax rotation. The Rotated component matrix represents the rotated factor loadings, which are the

correlations between the variables and the factors. The factor column represents the rotated factors that have been extracted out of the total.

Table 4.11 Rotated Component Matrix (Management-staff competence)

Rotated Component Matrix				
	Component			
	1	2	3	4
SecB_28	0.985			
SecB_29	0.985			
SecB_21	0.948	0.109		
SecB_26	-0.136	0.979		
SecB_25	-0.136	0.979		
SecB_23	0.422	0.798		-0.216
SecB_27	-0.268		0.828	0.131
SecB_24	-0.343		-0.795	
SecB_22				0.985

Extraction Method: Principal Component Analysis.
Rotation Method: Varimax with Kaiser Normalization.
a. Rotation converged in 4 iterations.

Table 4.11 shows the correlation of the variables with each of the extracted factors. Usually, each of the variables is highly loaded in one factor and less loaded towards the other factors. To identify the variables, included in each factor, the variable with the value maximum in each row is selected to be part of the respective factor. We can conclude that:

Factor 1 is loaded with the following variables: (i)The SACCOs have a staff-mentoring programs and encourage internal promotions (0.985) (ii) majority of staff have worked with their respective SACCOs for at least five years (0.985) and (iii) External and internal training sessions for staff are regularly conducted (0.798).

Factor 2 is loaded with following variables: (i) Staff has relevant professional qualifications (0.979) (ii) Staff are updated on emerging SACCO-industry issues especially SASRA regulations (0.979) and (iii) performance appraisal for staff is conducted frequently- at least once a year (0.798). Factor 3 is loaded with (i) Staff are SACCO members and contribute to the decision-making process (0.828) and (ii) Staff have relevant SACCO management skills (-0.795). Factor 4 is loaded with one variable; (i) management encourages staff development (0.985).

4.3.2.3 Correlation analysis- Management and Staff competence.

The study sought to obtain the CEOs' perceptions on whether the management and staff competence, as an independent variable, had influence on Institutional Capital, being the dependent variable. Spearman's rank correlation analysis was performed to check for the relationship between the various independent variables, the four factors generated using Principal Component Analysis and the dependent variable- institutional capital.

Spearman's rank correlation coefficient (Rs) ranges from -1 to 1. (i) 00- .19 shows very weak relationship, (ii).20-.39 shows weak relationship, (iii) .40-.59 shows moderate relationship, (iv).60-.79 shows strong relationship and (v) .80 -1.0 shows very strong relationship.

Table 4.12. Spearman's rho Correlations (Management-staff competence)

Spearman's rho Correlations						
		institutional capital	Factor 1	Factor 2	Factor 3	Factor 4
institutional capital	Correlation Coefficient	1.000	0.029	-0.399	**-.689****	-0.063
	Sig. (2-tailed)		0.897	0.059	0.000	0.775
	N	23	23	23	23	23
Factor 1	Correlation Coefficient	0.029	1.000	**.444***	0.079	**-.631****
	Sig. (2-tailed)	0.897		0.034	0.721	0.001
	N	23	23	23	23	23
Factor 2	Correlation Coefficient	-0.399	**.444***	1.000	0.254	-0.354
	Sig. (2-tailed)	0.059	0.034		0.242	0.098
	N	23	23	23	23	23
Factor 3	Correlation Coefficient	**-.689****	0.079	0.254	1.000	-0.096
	Sig. (2-tailed)	0.000	0.721	0.242		0.664
	N	23	23	23	23	23
Factor 4	Correlation Coefficient	-0.063	**-.631****	-0.354	-0.096	1.000
	Sig. (2-tailed)	0.775	0.001	0.098	0.664	
	N	23	23	23	23	23

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

***. Correlation is significant at the 0.05 level (2-tailed).**

The results in the Table 4.12 above show that there was a moderate relationship between institutional capital and (i) Factor 3: Performance appraisals for staff are conducted frequently and at least once a year. The relationship between institutional capital and factor 3 was negative and statistically significant at 1% significance level (R_s = -0.689, p value = 0.000 < 0.01).

Factor 1 (ii) Regular external and internal training sessions for management and staff had a very weak positive relationship with institutional capital. The weak correlation coefficient was not statistically significant at 5% level of significance (R_s = 0.029, p value = 0.897 > 0.05).

Factor 2 (iii): Management encouragement of staff development had a very weak negative relationship with institutional capital and a correlation coefficient which was not statistically significant at 5% level of significance (R_s = -0.399, p value = 0.059 > 0.05).

Factor 4 (iv) Staff possession of relevant Sacco management skills had a very weak negative relationship with institutional capital. The correlation coefficient was not statistically significant at 5% level of significance (R_s = -0.063, p value = 0.775)

4.3.3 Dividend payout

The study sought to find out if dividend payouts had influence on institutional capital adequacy. The CEOs' perceptions were obtained by asking them to indicate their level of agreement with nine statements linking dividend payouts to institutional capital.

4.3.3.1 Factor extraction -Dividend payout

Principal component analysis was used to identify variables that account for most variability and extracted new factors based on the total variance explained as shown in the table below.

Table 4.13: Principal Component Analysis -Dividend payout

Total Variance Explained						
	Initial Eigenvalues			Extraction Sums of Squared Loadings		
Component	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	4.936	54.841	54.841	4.936	54.841	54.841
2	1.566	17.403	72.244	1.566	17.403	72.244
3	0.963	10.704	82.949			
4	0.780	8.668	91.616			
5	0.387	4.305	95.921			
6	0.289	3.209	99.130			
7	0.078	0.870	100.000			
8	0.000	0.000	100.000			
9	0.000	0.000	100.000			
Extraction Method: Principal Component Analysis.						

Table 4.13 shows that: (i) Factor 1: Creation of non-withdrawal share capital has resulted in financial stability for the SACCO, with a mean of 4.936, accounting for 54.841% of the variability out of the 9 variables whereas (ii) Factor 2: Individual member share capital growth over the last five years has been slow, with a mean of 1.566, accounting for 17.403%. of the variability out of the 9 variables. These factors explain 72.244% of the total variability. Since only the first 2 factors have Eigen values greater than 1, this means the 2 factors accounted for most variability. The screen plot below also confirms the number of factors to be extracted.

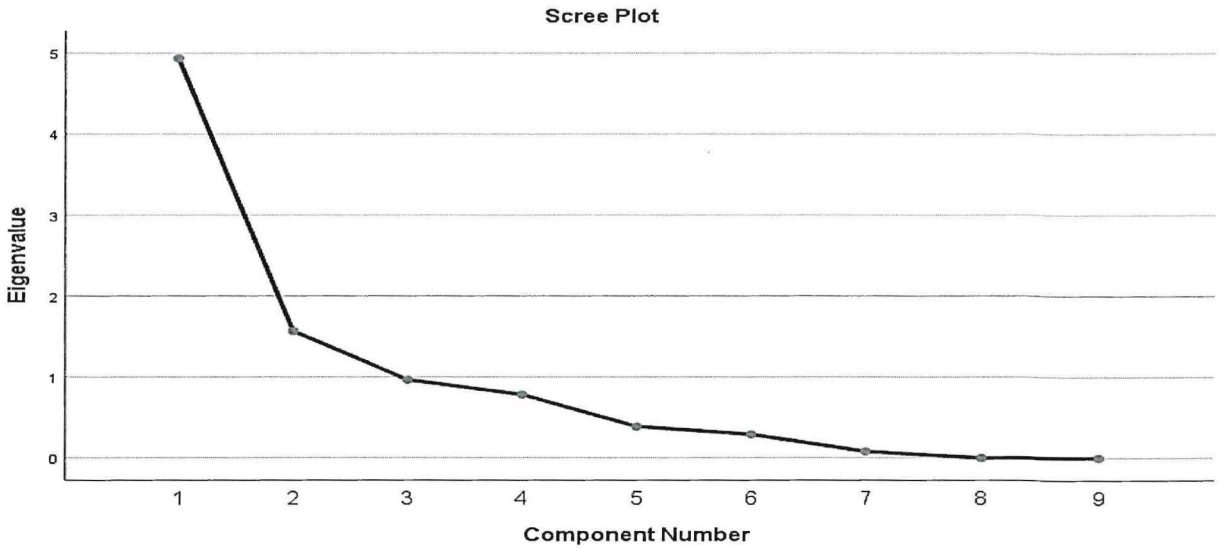

Figure 4.5 Eigenvalue- Component (Dividend payout)

Figure 4.5 shows the curve started to level off or becoming less steep after the second component hence only 2 factors were extracted.

4.3.3.2 Factor rotation -Dividend payout

After extraction of factors, the variables were subjected to varimax rotation. The Rotated component matrix represents the rotated factor loadings, which are the correlations between the variables and the factors. The factor column represents the rotated factors that have been extracted out of the total.

Table 4.14 Rotated component matrix -Dividend payout

Rotated Component Matrix		
	Component	
	1	2
SecB_33	0.945	-0.104
SecB_37	0.938	
SecB_38	0.938	
SecB_39	0.938	
SecB_31	0.781	-0.168
SecB_35	0.703	
SecB_32	0.414	-0.264
SecB_36		0.888
SecB_34	-0.134	0.877
Extraction Method: Principal Component Analysis. Rotation Method: Varimax with Kaiser Normalization. a. Rotation converged in 3 iterations.		

Table 4.14 The factor column represents the rotated factors that have been extracted out of the 9 factors that represent the dividend payout variables. The matrix gives the correlation of the variables with each of the extracted factors. Usually, each of the variables is highly loaded in one factor and less loaded towards the other factors. To identify the variables, included in each factor, the variable with the value maximum in each row is selected to be part of the respective factor.

Factor 1 has six statements, variables, namely; (i) a high dividend payout motivates members to increase their individual share capital, (ii) individual members' share capital increase is deterred by lack of a capital market, (iii) initial share capital was issued as a bonus, (iv) members have to be compelled to increase capital to the prescribed levels, (v) creation of share capital has led to financial stability and (vi) pegging share capital to eight percent of a member's deposits is enforceable.

Factor 2 has two statements, variables, namely; (i) majority members have a negative perception of external sources of capital and (ii) majority members are comfortable if a mandatory, flat minimum share capital is imposed for each membership.

4.3.3.3 Correlation analysis -Dividend payout

The study sought to obtain the CEOs' perceptions on the effect of dividend payout on institutional capital of deposit-taking SACCOs in Nairobi County. Spearman's rank correlation analysis was performed to check for the relationship between the independent variables, the 2 factors generated using Principal Component Analysis and the dependent variable, being institutional capital.

Table 4.15 Spearman's rho Correlations -Dividend payout

Spearman's rho Correlations				
		institutional capital	Factor 1	Factor 2
institutional capital	Correlation Coefficient	1.000	**-.705****	-0.192
	Sig. (2-tailed)		0.000	0.379
	N	23	23	23
Factor 1	Correlation Coefficient	**-.705****	1.000	0.262
	Sig. (2-tailed)	0.000		0.228
	N	23	23	23
Factor 2	Correlation Coefficient	-0.192	0.262	1.000
	Sig. (2-tailed)	0.379	0.228	
	N	23	23	23
**. Correlation is significant at the 0.01 level (2-tailed).				

Table 4.15 shows that there was a strong relationship between institutional capital and Factor 1-the creation of non-withdraw able share capital has resulted in financial stability for the SACCO. The relationship between institutional capital and factor 1, was negative

(-0.705) and statistically significant at 1% significance level (R_s = -0.705, p value = 0.000 < 0.01).

Factor 2, individual member share capital growth has been slow in the past five years, had a very weak negative (-0.192) correlation coefficient which was not statistically significant at 5% level of significance (R_s = -0.192, p value = 0.379 > 0.05).

4.4 The order of influence of independent variables on institutional capital

Another objective of the study was to determine the order of influence of the independent variables on institutional capital. Using factors generated from the individual independent variables, a correlation was ranked using all the factors against institutional capital.

Table 4.16 Spearman correlation coefficient ranking -Independent variables

Variable	R	Sig. (2-tailed)	N
Dividend payout_factor1	-.705**	0.000	23
Management Staff competence_factor3	-.689**	0.000	23
Quality of the Board -Corporate governance factor 2	.505*	0.014	23
Quality of the Board -Corporate governance factor 1	-.500*	0.015	23
Management Staff competence_factor2	-0.399	0.059	23
Quality of the Board -Corporate governance factor 4	-0.237	0.277	23
Quality of the Board -Corporate governance factor 3	-0.197	0.367	23
Dividend payout_factor2	-0.192	0.379	23
Management Staff competence_factor4	-0.063	0.775	23
Management Staff competence_factor1	0.029	0.897	23

Table 4.12 shows ranking based on the correlation coefficient. The only significant factors influencing institutional capital of DT-SACCOs were:(i) Dividend payout-

Factor 1: the creation of non-withdraw able share capital has resulted in financial stability in SACCOs (ii) Management- staff competence-Factor 3: Staff performance appraisals are carried out at least once a year (iii) Quality of the board -corporate governance Factor 2: all board members have appropriate Sacco- management training, education and knowledge and (iv) Quality of the board -corporate governance Factor 1: all board members have more than 5 years of work experience. These were the only significant factors influencing institutional capital of deposit-taking SACCOs in Nairobi County.

CHAPTER FIVE: DISCUSSIONS

5.1 Introduction

This chapter presents a discussion on the research findings guided by the study objectives and in the context of the literature for similar studies. The chapter summarizes how the objectives of the study have been achieved

5.2 Findings in relation to the objectives

The primary objective of this study was to determine the influence of people-related-factors on the attainment of institutional capital of Deposit-taking Savings and Credit Cooperative Societies in Kenya. The first objective of the study was to determine the influence of the quality of the board of directors on institutional capital. The second objective sought to analyze the influence of management-staff competence on institutional capital. The third objective sought to determine the effect of dividend payout on institutional capital. The fourth objective sought to find out the order of influence of the factors on institutional capital.

5.2.1 Quality of the board influencing institutional capital.

The study affirmed the influence of the quality of the board on institutional capital attainment of Deposit-taking SACCOs in Nairobi County. The results indicated that there is a significant relationship between the quality of the board and institutional capital adequacy, the attainment of the prescribed institutional capital: total assets ratio of 8%.

There are two key findings under the quality of the board. The factor relating to board members' having appropriate SACCO-management training, education and knowledge. suggests that boards of directors with higher levels of SACCO-management training, education and knowledge will have higher board quality, leading to the attainment of higher institutional capital adequacy levels.

This also suggests that an increase or improvement in the quality of the board, through training of directors or positive change in corporate governance structures will result in a positive change in institution capital adequacy ratio. In summary, the higher the quality of the board, the higher the level of institutional capital adequacy.

The second key finding is the factor related to the board members having more than five years of work experience. This suggests that having experienced directors may increase the quality of the board, but this may not ensure compliance with institutional capital adequacy. This could be due to the negative influence of having experienced, but ineffective directors on the board.

These findings support previous studies such as Odera (2012) which advocated having high quality of the board of directors and enhanced corporate governance structures as the solution to SACCOs' governance challenges. Owen (2007) established that some SACCOs were big enough to become commercial banks, but only required quality on the board of directors, quality supervision and a SACCO-dedicated regulator, this indeed led to the formation of SASRA and the accompanying SASRA prudential standards, which include institutional capital adequacy ratio.

5.2.2 Management and staff competence influencing institutional capital

The second objective of the study was to analyze the influence of management-staff competence on institutional capital of deposit- taking SACCOs in Nairobi County. A major finding of the study is that although management-staff performance appraisals, which assess competence, are conducted at least once a year, this has a negative relationship with the attainment of institutional capital. This suggests that the presence or increase of management-staff competence and institutional capital adequacy do not travel in the same direction. This key finding is in line with the Agency theory, which was developed as a framework for analyzing interrelated, and sometimes, conflicting interests in an organization. Abdullah and Valentine (2009) equates SACCO members to a principal who elect directors to the board as their agents, to protect members' interests. Directors, in turn, become principals and hire management and staff as agents to run operations of the SACCO. It follows, therefore, that even if management-staff have the competence to run the SACCOs, they are only agents. It is the principals' actions that will cause the SACCOs to attain SASRA's prescribed institutional capital adequacy ratio.

A further finding is that management's encouragement of staff development leads to increased staff competence. This confirms that management-staff competence is an agent's attribute, but a principal's attribute is what is necessary for a positive influence on institutional capital adequacy.

The findings that annual staff appraisals and staff development programs, which seek to increase management-staff competence, have a negative relationship with institutional capital, agree with Jensen and Meckling (1976) who argued that there are bound to be bonding and motoring costs, whenever an Agent-Principal relationship exists, as in the case of the DT-SACCO environment. Williamson (1998) confirmed that residual loss or costs could still occur even if Agent-monitoring and bonding costs are provided for.

5.2.3 Dividend payout influencing institutional capital.

The third objective of the study was to determine the influence of dividend payout on institutional capital of deposit-taking SACCOs in Nairobi County. The key finding under this objective is that the creation of non- withdraw able share capital, on which dividends are declared, has resulted in financial stability for SACCOs. The study established that Dividend payout is a key influencer of attainment of institutional capital adequacy ratio of institution capital: total assets (8%). This suggests that whereas increasing individual member's share capital, with the expectation to earn a dividend, boosts the Core capital of a DT-SACCO, it does not increase Institutional capital of the DT-SACCO. This is because the definition of Institutional Capital is: all Core capital less members' share capital. This further suggests that increasing share capital increases the pressure to pay a dividend to members who prefer a return on their capital to financial stability of their SACCO.

Further, DT-SACCOs are expected to attain institutional capital adequacy by retaining earnings, this slows down capital growth. It is also to be noted that individual members can not contribute to their DT-SACCO's Institutional capital. However individual members do contribute to the DT-SACCO's Core capital through purchase of share capital which is not withdrawable ad whose shares are not on the capital market.

This finding is not in line with Saunders and Cornett (2012) who argued that new shares will dilute owner's profit and the owner runs the risk of losing control of the company. This is because the pecking order argument is not relevant to the DT-SACCO- model. Under the DT-SACCO model, as prescribed by SASRA, new shares are aimed at increasing Core capital, thereby, financial stability rather than control nor is the value of the firm affected, this being a DT-SACCO without tradeable securities.

However, this scenario suggests that there may be no need for Institutional Capital in DT-SACCOs since Core capital through members' non-withdrawable share capital achieves financial stability. Modigliani and Miller (1958) argued that dividend policy of a firm is irrelevant as it does not affect the wealth of the shareholders, that the value of the firm depends on the firm's earnings. He further argued that the value of the firm is indifferent to the decision to split earnings between dividends and retained earnings. The findings of the study show that the decision to split earnings between dividends, to go to DT-SACCO shareholders, and retained earnings, to go financial stability- institutional capital, does matter to all the relevant players in the DT-SACCO subsector.

5.2.4 The order of influence of factors on institutional capital

The study sought to determine the order of influence of the quality of the board, management-staff competence and dividend payout on institutional capital of deposit-taking SACCOs in Nairobi County. Correlation rankings, from findings, indicate that the order of influence is: dividend payouts, management-staff competence and quality of the board. This finding contradicts Modigliani and Miller (1958) who argued that dividends do not matter. However, the contexts differ since the SACCO -model is not based on profit-wealth maximization and firm-valuation.

SACCO members' shares, in Kenya, do not have a capital market, these can only be transferred within the membership at a fixed value per share. The order of influence finding is in line with several previous studies, to the extent that management-staff competence and quality of the board are ranked. Owen (2007) argued that quality of the board and a regulatory framework were important for financial stability of SACCOs. Odera (2012) agreed that corporate governance structures, put in place by

quality boards and competent managers was key to the success of the SACCOs. Waiganjo et al (2015) specifically ranked quality of the board, staff competence and corporate governance as the key influencers of the financial performance of any given DT-SACCO.

5.2.5 Moderating role variable of Interest payment on Deposits

Based on the DT-SACCO model, the Chief Executive Officers' responses to the question of mandatory minimum share capital per member, and the cooperative principles and values, SACCO members use their deposits and the common bond principles to access relatively cheaper credit from their DT-SACCOs. This study did not determine whether interest paid on members' deposits acted as a moderating variable between the independent variables; quality of the board, management-staff competence and dividend payout and the dependent variable, institutional capital. However, if interest paid on a member's deposits has any moderating influence between independent variables and institutional capital, this secondary rather than primary. This is because the primary objective of a DT-SACCO member is to save towards relative cheaper credit based on a member's accumulated deposits.

CHAPTER SIX: CONCLUSIONS AND RECOMMENDATIONS

6.1 Introduction

This chapter presents the recommendations of the study, reflects on the implications of these findings to deposit-taking SACCOs in Kenya, points out the study limitations and recommends areas for further research.

6.2 Conclusions

The study sought to determine the influence of the quality of the board-corporate governance, management-staff competence and dividend payout on institutional capital of deposit-taking SACCOs. Failure, by DT-SACCOs, to meet institutional capital adequacy requirement, is a contemporary problem whose consequences are severe and include revoking of operating license, deregistration, placing under receivership, take-overs, forced mergers and even outright dissolution.

When DT-SACCOs fail, it is often because of the actions of the board of directors and management that cause under-capitalization. The study has indeed established that some components of the quality of the board and corporate governance have both a positive and negative relationship with institutional capital adequacy. Management and staff competence affect institutional capital adequacy. The dividend payout variable had the highest effect on institutional capital adequacy as prescribed by SASRA.

6.2.1 Quality of the board

No DT- SACCO can maintain its members' trust for long if it is not properly managed or lacks adequate capital. Since capital is the last line of defense against liquidation, SASRA's prudential capital adequacy regulations are fundamental elements of financial supervision.

The study concluded that the quality of the board is greatly enhanced when all board members have the appropriate SACCO- management training, education and knowledge. It is, therefore, the responsibility of the board of directors to demonstrate, to the regulators, the limitations of raising institutional capital through retaining earnings.

6.2.2 Management and staff competence

Based on findings of the study, management-staff competence has influence on institutional capital adequacy. More specifically, frequent manager-staff performance appraisals are significant for enhanced competence. However, managers and staff are agents of the principals, the board of directors and members. Maintaining a strong institutional capital position, by increasing earnings retention, entails reducing of dividend payout and guarding against financially catastrophic events. Whereas a strong capital base will deepen members' trust and confidence, required by all deposit-taking SACCOs, management-staff competence, being an agent's attribute, is limited in comparison to the principals' responsibility for the attainment of institutional capital adequacy.

6.2 3 Dividend Payout

Based on findings of the study, dividend payout has the strongest influence on the attainment of institutional capital. This is because members increase their individual share capital, in anticipation of a return, a dividend payout. Whereas increasing share capital increases core capital adequacy, it does not increase institutional capital since the definition of institutional capital excludes share capital.

The study confirmed the existing challenges in relation to DT-SACCO members' expectation of a dividend payout whenever they increase their individual share capital. When the DT-SACCO increases institutional capital through earnings retention, this often means less dividend payout or no dividend payout at all. The conclusion is that this conflict will continue if the definition of institutional capital remains: Core capital less members' share capital.

6.3 Recommendations of the study

From the conclusions of the study and review of literature, several recommendations can be made. The study has established that dividend payouts, quality of the board-corporate governance and management- staff competence, have varying degrees of influence on institutional capital in DT-SACCOs.

Deposit-taking SACCOs are important to the Kenyan economy for financial deepening and financial inclusion. Based on conclusions of this study, DT-

SACCOs' capital adequacy regulations should not be equated to capital adequacy requirements of investor-controlled commercial banks. Globally, SACCOs are of different sizes and importance in their respective financial systems. Consequently, SACCOs should be prudentially managed and regulated by competent managers, staff and regulators. Owen (2007) and Odera (2012) both suggested that directors, managers and staff should have sound knowledge and understanding of the financial, operational, structural and social differences of DT-SACCOs, relative to other deposit-taking institutions. The study also recommends that SASRA's supervision and enforcement of capital adequacy regulations should be based on the individual DT-SACCO's risk profile.

Since DT-SACCOs have no access to capital markets, they can only raise institutional capital internally, over time, from retained earnings. Although institutional capital is stable capital, there is need to eliminate duplication occasioned by the requirement to raise core capital and institutional capital simultaneously. Regulators should recognize that DT-SACCOs, being member-oriented institutions, present minimal systemic risk to financial systems.

Based on this study, it is recommended that the regulators should focus on a strong supervisory regime as opposed to implementing, across the board, the capital adequacy ratios, especially the institutional capital adequacy requirement.

DT-SACCOs that have failed to meet the institutional capital to total assets ratio of 8% have had to obtain authority to continue with operations as they strive to attain the ratio. This is burdensome since the ratio is a moving target and requires forfeiture of earnings in favor of retained earnings.

Given that the presence or increase of management-staff competence and institutional capital adequacy do not travel in the same direction, this study recommends enhancing of controls and expenditure on DT-SACCO staff costs. This is because it was established that monitoring and bonding costs may increase without resulting in increased institutional capital adequacy. This recommendation is in line with the Agency theory, which was developed as a framework for analyzing interrelated, and sometimes, conflicting interests in an organization. Abdullah and Valentine (2009) equates SACCO members to a principal who elects directors to the

board as their agents, to protect members' interests. Directors, in turn, become principals and hire management and staff as agents to run operations of the SACCO. It follows, therefore, that even if management-staff have the competence to run the SACCO, they are only agents. It is the principals' actions that will cause the Sacco to attain SASRA's prescribed institutional capital adequacy ratio. Waiganjo (2015) agrees that SASRA should tighten the requirements for directors and managers who wish to serve the DT-SACCOs.

Although no member is permitted to own more than 5% of a DT-SACCO's issued Share capital, there should be a restriction on the level of share acquisitions through cash injections and the level of dividends declared. This study recommends this restriction so that DT-SACCO boards and managers are not restricted by the pressure to pay dividends to shareholders who may be investors seeking returns on their shares, in contravention of the cooperative tenets.

6.4 Contributions to knowledge

The study's contribution to new knowledge is the demonstration of the importance of investor-member sentiment to capital structure in deposit-taking SACCOs in Kenya. It has demonstrated that board members, management and staff are all aware of the principles of the cooperative movement and how this differs from an investor-controlled listed company. If members prefer dividend income over future financial stability, the regulators and policy makers should accommodate members' sentiment.

6.5 Limitations

The design of the study took a snap shot of institutional capital adequacy of DT-SACCOs in Nairobi County at the end of 2016. Data collected was based on Chief executive officers' perceptions This study, therefore, may carry the Chief Executive Officers' biases.

Measuring Chief Executive Officers perceptions across the different deposit-taking SACCOs and their internal operating environments is difficult since there is no common measure of one's perceptions and responses to the questions in the

questionnaire. Different DT-SACCO environments may modify values, skills, behaviors and missions, making a common approach a challenge.

6.6 Suggestions for further studies

The findings on institutional capital adequacy, in this study, and current SACCO's regulations demonstrate that there is room for further research on capital adequacy in SACCOs. More specifically, since there is no capital market for SACCO's shares, further research can be conducted on attainment of institutional capital adequacy through issuance of marketable SACCO shares, while maintaining the cooperative principles.

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APPENDICES

Appendix 1: LETTER OF INTRODUCTION

Dear Vincent,

Good morning, I do hope that you are doing well.

Kindly find attached research project introduction letter to help you in data collection.

Thank you and wish you the very best as you finalize your research project.

Kind regards

Moses Mugo
MBA Program Administrator.
Ole Sangale, Madaraka
P.O. Box 59857 - 00200
Cell: +254 (0) 703 034 414
Personal +254 720937851

Strathmore Business School

Tuesday, 03 May 2016

To Whom It May Concern:

Dear Sir/ Madam,

FACILITATION OF RESEARCH – VINCENT OCHIENG OMINGO

This is to introduce Vincent Omingo, who is an MBA student at Strathmore Business School, admission number **MBA/76877/13.** As part of our Masters Program, Vincent is expected to do applied research and to undertake a project. This is in partial fulfillment of the requirements of the Master of Business Administration course. To this effect, he would like to request for appropriate data from your organization.

Vincent is undertaking a research paper on "**The Capitalization Challenge for Savings & Credit Cooperative Societies (SACCOs) in Kenya**". The information obtained from your organization shall be treated confidentially and shall be used for academic purposes only.

Our MBA seeks to establish links with industry, and one of these ways is by directing our research to areas that would be of direct usefulness to industry. We would be glad to share our findings with you after the research, and we trust that you will find them of great interest and of practical value to your organization.

We very much appreciate your support and we shall be willing to provide any further information if required.

Yours sincerely,

Eliud Njogu

Ag. Director – MBA Programs

Strathmore UNIVERSITY

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Twitter: @ SBSKenya

Appendix 2: SELF- INTRODUCTORY LETTER

Dear Sir/Madam,

I am Vincent Omingo, an MBA student of Strathmore Business School undertaking a study on the **"Effects of corporate governance, staff competence and dividend on Capital adequacy as per SASRA regulations".** This is to humbly request you to take some time to fill in this questionnaire. The information provided shall be used only for this study and will be treated with strict confidentiality.

Once the Questionnaire is filled, I would prefer to be contacted on **0733 995125 or 0718 266361** to pick as soon as possible.

Alternatively, a scan may be e-mailed to **Vomingo@worldbank.org**

Thank you.

Appendix 3: RESEARCH QUESTIONNAIRE SECTION A

SECTION A: General Information

1. Name of the Deposit-Taking SACCO (optional)

.....

2. How long has the SACCO been in existence? (Please tick as appropriate)
   - **a.** 0--10 years [ ]
   - **b.** 11--21 years [ ]
   - **c.** 22--32 years [ ]
   - **d.** Above 32 years [ ]

3. Membership of the SACCO is drawn from:
   - a) Employees of Parent Organization [ ]
   - b) Employees and Retirees of Parent Organization [ ]
   - c) Employees and Dependents –Co. and sister Cos. [ ]
   - d) Other.....

4. Size of the SACCO as at 31st December 2015

   Members

   a) Below 1000 [ ]
   b) 1001- 2500 [ ]

c) 2501- 4000 [ ]

d) 4001- 5500 [ ]

e) Other.....

Staff

a) Below 15 [ ]

b) 16- 25 [ ]

c) 26- 35 [ ]

d) 36- 45 [ ]

e) Other.....

Directors

a) 3-5 [ ]

b) 6- 8 [ ]

c) 9- 11 [ ]

d) 12- 15 [ ]

e) Other.....

Appendix 4: RESEARCH QUESTIONNAIRE SECTION B

SECTION B

Please tick (☑) the response that most closely reflects the extent to which you agree with each statement. Strongly Disagree = 1; Disagree =2; Neutral= 3; Agree = 4; Strongly Agree=5. Your responses will be used exclusively to analyze the effects of the variables (below) on Capital Adequacy requirements as per SASRA regulations.

Quality of the Board -Corporate Governance

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
1. All Board members have more than 5 years of work experience.	☐	☐	☐	☐	☐
2. All Board members have appropriate SACCO-management training/education/knowledge.	☐	☐	☐	☐	☐
3. Directors are frequently trained on SACCO Management /Operations	☐	☐	☐	☐	☐

4. Directors have relevant professional qualifications, in addition to financial literacy.	☐	☐	☐	☐	☐
5. Board reconstitution takes place at least once a year.	☐	☐	☐	☐	☐
6. The Board of Directors engages and rotates competent external auditors.	☐	☐	☐	☐	☐
7. The Board ensures that the Supervisory Committee and the Internal Auditor work independently, but harmoniously	☐	☐	☐	☐	☐
8. The SACCO has a Board evaluation manual and a documented code of conduct for Directors.	☐	☐	☐	☐	☐
9. Board members have autonomy and freedom in decision-making.	☐	☐	☐	☐	☐
10.There is enough separation of power and responsibilities, for smooth Operations, between STAFF and DIRECTORS	☐	☐	☐	☐	☐
11. The Board spear-heads the responsibility for raising SHARE CAPITAL to SASRA's required level.	☐	☐	☐	☐	☐
12. In general, the Board has a positive perception of External Sources of Capital.	☐	☐	☐	☐	☐
13. The Board is aware of alternative sources of Capital (other than members' equity).	☐	☐	☐	☐	☐
	☐	☐	☐	☐	☐

Management Staff competence

	Strongly Disagree		Disagree	Neutral	Agree	Strongly Agree
1. External/Internal training sessions for staff are regularity conducted.	☐		☐	☐	☐	☐
2. Management encourages Staff Development.	☐		☐	☐	☐	☐
3. Performance appraisal for Staff are conducted frequently (at least once a year)	☐		☐	☐	☐	☐

4. Staff has relevant cooperative management skills.	☐		☐	☐	☐	☐
5. All staff are updated on emerging SACCO industry issues, specifically SASRA regulations	☐		☐	☐	☐	☐
6. Staff has relevant Professional qualifications.	☐		☐	☐	☐	☐
7. Staff are members of the SACCO and contribute to decision-making.	☐		☐	☐	☐	☐
8. The SACCO has a Staff-mentoring program and encourages internal promotion.	☐		☐	☐	☐	☐
9. Currently, most staff have been with the SACCO for at five years.	☐		☐	☐	☐	☐
	☐		☐	☐	☐	☐

Dividend payout

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
1. Creation of **non-withdraw able Share Capital** has resulted in financial stability for the SACCO	☐	☐	☐	☐	☐
2. Individual member **Share Capital** growth over the last five years has been slow.	☐	☐	☐	☐	☐
3.A high **Dividend rate** declaration tends to motivate members to increase their Share-holding	☐	☐	☐	☐	☐
4. The most members are not comfortable with a mandatory, flat, minimum membership Equity Shares	☐	☐	☐	☐	☐
5. If minimum **Share Capital** is pegged, by law, on 8% of a member's **Deposits**, this would be easily enforceable **(Membership Equity Shares =8% of a**	☐	☐	☐	☐	☐

member's Deposits)					
6. In general, most members have a negative perception of raising **Share Capital** from **external sources** since this is considered "too risky" for SACCO operations.	☐	☐	☐	☐	☐
7. Individual member's increase of **Equity Share Capital** is deterred by absence of a Capital Market/ potential to transfer at a premium.	☐	☐	☐	☐	☐
8. The initial **membership Equity Shares**, per member, was through a Bonus issue since members would rather increase their **DEPOSITS** than **SHARES**.	☐	☐	☐	☐	☐
9. On average, for the SACCO to meet SASRA Capital adequacy requirement, a member must be compelled to increase **Share Capital**.	☐	☐	☐	☐	☐

Appendix 5: RESEARCH QUESTIONNAIRE SECTION C

SECTION C

Please complete the CAPITAL ADEQUANCY Table below for the year ended 2012-2016.This will indicate compliance with SASRA Capital regulations and trends.

CAPITAL ADEQUACY

Ratio		**SASRA Capital Adequacy Requirement**	**2012 SACCO (%)**	**2013 SACCO (%)**	**2014 SACCO (%)**	**2015 SACCO (%)**	**2016 SACCO (%)**
Core Capital to Total Assets		**10%**					
Institutional Capital to Total Assets		**8%**					
Core Capital to		**8%**					

Total Deposit Liabilities							
Core Capital of not less than		**Ksh. 10m**	**Ksh.**	**Ksh.**	**Ksh.**	**Ksh.**	**Ksh.**

Appendix 6: RESEARCH QUESTIONNAIRE SECTION D

SECTION D

Please mark YES or NO for **types and sources of Capital** in issue for the year ended 2012-2016.

Alternative Capital in issue as at year end:

Type of Capital		**Source of Capital**	**2012 Yes/No**	**2013 Yes/No**	**2014 Yes/No**	**2015 Yes/No**	**2016 Yes/No**
Membership Equity Shares		Members					
Preferred Shares		Members					
Trust-Preferred Shares		Non-members					
Subordinated Debt		Non-members					
Uninsured Long-term Deposits		Members & non-members					
Prorated Share System Capital		Retained earnings					
Minority Stake Listing		Non-members					

Appendix 7: RESEARCH QUESTIONNAIRE SECTION F

SECTION F

Key Definitions

(Source: SASRA)

Core Capital: The fully paid up members' shares, capital issued, disclosed reserves, retained earnings, grants and donations all of which are not meant to be expended unless on liquidation of the SACCO Society.

Institutional Capital: Disclosed reserves, retained earnings, grants and donations all of which are not meant to be expended unless on liquidation of the SACCO Society.

Supplementary capital: general provisions which are held against future and presently unidentified losses that are freely available to meet losses which subsequently materialize, twenty-five per cent asset revaluation as approved by the Authority, subordinated debt, hybrid capital instruments or such other form of capital as may be determined by the Authority from time to time.

Total Capital: the total sum of core capital and supplementary capital of a Sacco society.

Total Deposit Liabilities: Total deposits which are repayable on demand or after a fixed period or after notice under agreed terms and conditions.

Savings: deposits payable on demand

Equity: The difference between assets and liabilities, or the total of institutional capital and other capital accounts.