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UTILISATION OF MICRO-FINANCE INSTITUTIONS' FUNDS BY BORROWERS IN ARID AND SEMI-ARID LANDS IN KENYA

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Borrowed funds utilization, economic characteristics, literacy levels.

ABSTRACT

Despite a lot of efforts in terms of resource mobilisation in Arid and Semi-Arid Lands (ASAL) , the poverty levels are still very high and the defaulted loans from the four Micro-Finance Institutions (MFIs) in Maralal town amounts KES 15 million. The study sought to establish whether economic characteristics of entrepreneurs and whether literacy levels affect application and usage of borrowed funds in the ASAL regions of Africa. The study was limited to Maralal Town, one of the main towns in the ASAL region of northern Kenya. An *ex-post facto* study design was considered appropriate for the research. Data collection was done using questionnaires from a population of 40 MFIs staff and 10,600 MFIs Clients who accessed credit in the last five years. The data collected was analyzed through both descriptive and inferential statistics and presented in form of tables. The study has established that economic characteristics of entrepreneurs determine the use of borrowed funds from MFIs. Literacy levels were found to have a significant relationship with use of borrowed funds. The findings of the study are useful to, the Government and other researchers interested in this field.

1. INTRODUCTION

The economic mainstay of Kenya's Arid and semi arid lands areas is livestock production and it experiences the highest levels of poverty at 65%. The region is also home for 12 million Kenyans. During the last two decades, microfinance has evolved from an informal sector into a semi-mature, professional industry. Microfinance institutions are now facing some of the main challenges of regular retail banks: dealing with competition, offering goods and services at low cost and monitoring credit risks. The latter is particularly important when microfinance institutions become big or start to accept savings.Since 1980, microfinance services have generated considerable infers among academics, donors and development practitioners as alternative to the documented failure of government rural credit assistance to reach low income household (Mansuri and Sunjay, 2003).The failures are attributed to cause such as urban- biased credit allocation, high transaction costs, interest rates restrictions, high default rates and corrupt practices. The reasons for poor loan recovery are related to inappropriate design feature leading to incentive problems and politicization that made borrowers view credit as a political largesse (Hulme and Arun, 2009).

The development of the microfinance sector is based on the assumption that the poor possess the capacity to implement income generating economic activities but are limited by lack of access to and inadequate provision of savings credit and insurance facilities. This approach also breaks from the directed credit strategies by reducing the government's involvement paying close attention to the incentives that drive efficient performance (Carey, 1998). The developments in microfinance services have been based on the prototype delivery model that is considered the best answer to capture financial needs of the poor in various socioeconomic and institutional systems.

Large data sample over a time frame of 10 years in Kenya has been used to calculate the loss distribution for two portfolios of loans, one consists of loans granted to male clients, the other comprises loans granted to female clients. The loss distributions are calculated with a re-sampling technique similar to the one used by Carey (1998), Calem and LaCour-Little (2004) and Schmit (2004) to estimate credit risk in private debt portfolios, in mortgage loan portfolios and in the leasing industry respectively. Inadequate financial infrastructure is a major problem in most developing countries. Financial infrastructure includes legal, information, as well as regulatory and supervisory systems for financial institutions and markets. Most governments in developing countries have focused on creating institutions or special programs to disburse funds to the poor with little attention to building financial infrastructure that supports, strengthens, and ensures the sustainability of such institutions or programs and promote participation of private sector institutions in microfinance (Basel Committee, 2004)..

Kenya's microfinance industry has come a long way since the 1980s, and particularly since the landmark Microfinance Intermediaries Act of 2006. The country now has five deposit-taking microfinance intermediaries (MFIs) operating under a regulatory framework assessed by the Economist Intelligence Unit (EIU) as the best in Africa (EIU 2010). Overall, the EIU rates Kenya as having the second best business environment for MFIs in all of Africa and one of the top ten in the world

Kenya has the second largest borrower base in the continent and Schmit (2004), and its largest savings and credit cooperatives (SACCO) movement and Schmit (2004). This is not unrelated to the country's world-leading position in mobile banking (EIU 2010), which has been proven to be a significant driving force in financial inclusion

Nonetheless, the microfinance industry globally is meeting difficulties as funding dries up, delinquencies rise and sceptics begin to question its efficacy in driving poverty reduction and development. Much of this critique focuses on some of the bolder claims, made more often by policymakers and consultants, than by practitioners themselves. (Schmit 2004).

The main economic activity in the Kenyan Arid and semi arid lands areas is livestock production. The region is home for 12 million Kenyans. The area experiences the highest levels of poverty incidence at 65%. Access to financial service has been identified as a major problem experienced by many in attempt to do business in Kenya. Though there have been sustained efforts to finance the low income earners of the society which has been facilitated by the upcoming microfinance institutions which operate in most parts of Kenya including Maralal town. Despite all these interventions, a large percentage of the rural people are still living below the poverty line yet microfinance institutions have continued to offer financial service to these members of the society for a long period. Given that, the defaulted loans in Maralal town amounts to Kshs. 15 million (KWFT, 2010). The study was carried out in Maralal town and targeted all the MFIs within the town. Maralal town is a very key town in the ASAL region in Kenya. The study was carried out between October 2011 and June 2012.

Large percentage of the rural poor have been unable to effectively service the credit borrowed from micro-financial institutions (EIU, 2010).Whether this is as a result of problems in applicability and usage of the credit from the MFIs remains to be seen. Therefore this study examined the applicability and use of credit from MFIs and sort to answer the following questions:

i. What particular economic characteristics of entrepreneurs affect applicability and usage of funds borrowed from MFIs?

ii. Do literacy levels of borrowers affect applicability and usage of funds borrowed from MFIs?

The findings of this study are useful to both microfinance organizations and individual all over the world. Foremost, the study can form a basis for future research by scholars who are interested in studying microfinance in Maralal town. The study also benefits the Microfinance institutions, currently engaged in lending out their credit to the economically marginalized groups.

The borrowers of micro-finance credit also benefits from this study in the sense that they will understand their responsibility in servicing the credit. This will enable the MFIs to recover their credit in time and consequently lower the default rates.

Currently, the government is working towards the realization of vision 2030. To realize this vision, the MFIs must compliment the government efforts towards poverty alleviation and sustainable development. This cannot be overstated when it comes to ASAL regions of Kenya were realization of the sustainable development, through poverty alleviation is key to the Kenya Government.

The paper contains four (4) main sections. Section 1: Introduction, gives the general background of the study as well as an introduction to the field of study. Section 2: Methodology, outlines the research design used, target population, sample size, data collection, data analysis techniques employed and data presentation. Section 3: Results and Findings, presents the results and findings of the study. The results and findings are presented based on the research questions addressed by the study. The last section is Section 4: Summary of Findings and Conclusion. This section gives a summary of the findings as per the study questions. It also gives research recommendations based on the study findings.

2. METHODOLOGY

The study was quantitative research in the sense that it typically involved a large number of subjects and elaborate statistical analysis (Cohen et al, 1996). Since the relationship between the main variables (independent and dependent variables) already exists, *ex-post facto* study design was considered appropriate for the research. According to Fraenkel and Wallen (1996), *ex post facto* study design, also known as causal – comparative research design, involves comparing groups in order to explain the existing differences between the variables of interest. Kothari (2003) argues that the main characteristics of the causal comparative design is that the researcher has no control over the variables but can only report what has happened or what is happening. Consequently, this study examined the existing relationships, the applicability and usage of funds by borrowers of micro-financial institutions. The researcher did not have control over the independent variable because the manifestations have already occurred or they are inherently not manipulatable (Kerlinger, cited in Black, 1999). Thus, this study was concerned with the existing relationship between the applicability and usage of funds by borrowers of micro-financial institutions

The study was carried out in Maralal town and targeted all the MFIs within the town. Maralal town is a very key town in the ASAL region in Kenya. The study was carried out between October 2011 and June 2012.

The target population involved all employees and customers of the four micro-financial institutions in Maralal Town, namely; Kenya Women Finance Trust, Faulu Kenya, Samburu Teachers Saccco and Samburu Traders Employees. The employees consisted of all the three levels of management that is, management, middle and lower levels. The customers consisted of those who have accessed credit facilities from the MFIs for the last five years. There are a total of 40 employees in the five MFIs. On the other hand, the MFIs have a total of 10,600 customers who have accessed credit for the last five years. This can be broken down in the table below:

Table 1: Target Population

Micro-finance Institution	Employee	Customers
Kenya Women Finance Trust	5	1,500
Faulu Kenya	5	2,300
Samburu Teachers Sacco	10	2,500
Samburu Traders Employees	20	4,060
Total	**40**	**10,600**

Source: Survey data, 2011.

Out of the 10,600 customers, only 4,000 had accessed credit for the last five years and were currently servicing it. Therefore the study opted to include only those customers who had accessed credit for the last five years and were currently servicing it.

For this study, stratified random sampling method was used to divide the target population into three strata: strategic, tactical and operations. Then from each stratum simple random sampling was used to select cases that constituted the sample for the study. The division of the population into strata allowed a more representative sample in that a sample will be selected from each stratum. Employees in each stratum were asked to pick a paper from a container in which the papers were written 'yes' or 'no'. The total number of papers to be picked was 10% of the total number of employees and customers of MFIs. All the managers who picked 'yes' paper constituted the sample.

A sample of 10% of the total population is justified as representative of the active population in *ex-post facto* studies, according to Cohen et al (1996). Thus, from Cohen at al (1996) perspective, a sample of 10% of the total population was deemed representative enough. Consequently, the study targeted a sample of 416 cases.

Data was collected using the questionnaire administered to all cases that constituted the sample. The questionnaire comprised of 20 items covering all the objectives of the study. The 20 items were rated on a 5-point Likert Scale. The Likert Scale on the questionnaire provided the respondents with an opportunity to indicate the degree of agreement or disagreement on each statement concerning employee development programmes and organizational goals. The Likert scale questionnaire was preferred because of is extensively used to determine attitudes and behaviour or respondents in respect to existing phenomena.

The collected data was analyzed quantitatively. Inferential statistics was used to analyze the relationships between the variables in the objectives. Descriptive statistics was used to describe the

sample characteristics where measures of relationships do not apply. The level of significance for inferential statistical analysis was 0.05. According to Aiken (1994), this level of significance is most commonly used in behavioural science, hence its adoption in this study. The analysed data was presented using frequency tables and spearman rank correlation tables.

3. RESULTS AND FINDINGS

The study was based on two research questions. Data was collected so as to answer these research questions. The research questions are answered as follows:-

What is the effect of economic characteristics of entrepreneurs on the use of borrowed funds?

In order to answer this question, the respondents were asked to respond to the item on the questionnaire on the economic characteristics of entrepreneurs. The responses of economic characteristics of entrepreneurs were scored and the results prosecuted in Table 2.

Table 2: Economic characteristics of Entrepreneurs

Variable	Standard Deviation	Mean	Strongly Agree (5)	Agree (4)	Neutral (3)	Disagree (2)	Strongly Disagree (1)
Income levels	1.07	4.12	47.1	33.7	5.3	13.0	1.0
Poverty levels	1.34	3.80	42.8	28.1	7.9	12.0	9.1
Expenditure levels	1.07	4.13	47.6	33.2	5.3	13.0	1.0
Availability and access to credit	1.10	4.06	44.5	33.9	5.5	14.9	1.2

n = 416

Table 2 and Table 3 shows that there were four economic characteristics of entrepreneurs who had accessed credit from MFIs in Maralal town. These characteristics were income levels, poverty levels, expenditure levels and availability and access to credit. The results of descriptive statistics imply that the respondents were in agreement that income levels (80.8%), poverty levels (70.9%), expenditure levels (80.8%) and access to credit (78.4%) were positively perceived as the economic characteristics of entrepreneurs who had accessed /borrowed funds from MFIs. These characteristics therefore serve as indicators of use of borrowed funds. For instance the income levels, poverty levels, expenditure levels, and levels of access to credit show the extent of use of borrowed funds in various business ventures by the entrepreneurs.

In order to determine the relationship between economic characteristics and use of borrowed funds, Spearman Rank Correlations technique was used to correlate the two variables. Spearman Rank Technique was used because the data on the questionnaire was ranked in a scale of 1 to 5. The results of Spearman Rank Correlation showed that there was a significant positive relationship between the economic characteristics of borrowers and the use of borrowed funds.

Table 3: Relationship between economic characteristics of borrowers and use of MFI credit

		Income Levels	Poverty Levels	Expenditure Levels	Availability and access to credit	Use of borrowed funds
Income levels	**Correlation Coefficient**	1.000	.463(**)	.611(**)	.088	.289(**)
	Sig.(2-tailed)	.	.000	.000	.073	.000
	N	416	416	416	416	416
Poverty levels	**Correlation Coefficient**	.463(**)	1.000	.698(**)	.241(**)	.330(**)
	Sig.(2-tailed)	.000	.	.000	.000	.000
	N	416	416	416	416	416
Expenditure levels	**Correlation Coefficient**	.611(**)	.698(**)	1.000	.157(**)	.314(**)
	Sig.(2-tailed)	.000	.000	.	.001	.000
	N	416	416	416	416	416
Availability and access to credit	**Correlation Coefficient**	.088	.241(**)	.157(**)	1.000	.510(**)
	Sig.(2-tailed)	.073	.000	.001	.	.000
	N	416	416	416	416	416
Use of borrowed funds	**Correlation Coefficient**	.289(**)	.330(**)	.314(**)	.510(**)	1.000
	Sig.(2-tailed)	.000	.000	.000	.000	.
	N	416	416	416	416	416

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

The results of the Spearman Rank Correlation thus imply that there is a significant relationship between all the economic characteristics and use of borrowed funds.

What is the effect of literacy levels on the use of borrowed funds?In order to answer this research question; the respondents were asked to respond to the item on the questionnaire concerning literacy levels. The literacy levels were identified as: No formal education, primary level of education, secondary level of education. Respondents from each of these levels were scored, as the results presented in Table 4.

Table 4: Literacy level of borrowers

Variable	Standard Deviation	Mean	Strongly Agree (5)	Agree (4)	Neutral (3)	Disagree (2)	Strongly Disagree (1)
No formal education	1.11	4.02	42.1	35.6	6.7	13.2	2.4
Primary education	1.20	3.90	41.1	31.7	6.5	17.5	3.1
Secondary education	1.08	4.07	44.5	34.4	5.8	14.4	1.0
Tertiary education	1.08	4.07	44.5	34.4	5.8	14.4	1.0
University education	1.08	4.07	44.5	34.4	5.8	14.4	1.0

The results of descriptive statistics in Table 4 suggest that the respondents were in agreement that there are five literacy levels that affect the use of borrowed funds. These literacy levels were no formal education (77.7%), primary education (72.85), secondary education (78.9%), tertiary education (78.9%) and university education (78.9%).

Having established the literacy levels, the study further sought to determine the relationship between literacy levels and use of borrowed funds. Spearman Rank Correlation was used to correlate the two variables and the results presented in Table 5.

Table 5:Relationship between literacy levels and the use of borrowed funds

		Use of borrowed funds	Secondary education	Primary education	Tertiary education	University education
Use of borrowed funds	**Correlation Coefficient**	1.000	.854(**)	.730(**)	.854(**)	.854(**)
	Sig. (2-tailed)	.	.000	.000	.000	.000
	N	416	416	416	416	416
Secondary education	**Correlation Coefficient**	.854(**)	1.000	.862(**)	1.000(**)	1.000(**)
	Sig. (2-tailed)	.000	.	.000	.	.
	N	416	416	416	416	416
Primary education	**Correlation Coefficient**	.730(**)	.862(**)	1.000	.862(**)	.862(**)
	Sig. (2-tailed)	.000	.000	.	.000	.000
	N	416	416	416	416	416
Tertiary education	**Correlation Coefficient**	.854(**)	1.000(**)	.862(**)	1.000	1.000(**)
	Sig. (2-tailed)	.000	.	.000	.	.
	N	416	416	416	416	416
University education	**Correlation Coefficient**	.854(**)	1.000(**)	.862(**)	1.000(**)	1.000
	Sig. (2-tailed)	.000	.	.000	.	.
	N	416	416	416	416	416

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

The results of Spearman Rank Correlation show that there was a significant relationship between literacy levels and the use of borrowed funds. The literacy levels thus determine the accessibility and use of credit. The tables also imply that literacy levels increase as the accessibility and use of borrowed funds increase. Thus, education is a determinant factor in the borrowers' use of credit from MFI institutions. Education determines how, where, when and why MFI credit is being sought and how it will be used by borrowers.

4. SUMMARY OF FINDINGS AND CONCLUSION

Summary of Findings

Effect of Economic characteristics of borrowers on the use of borrowed funds:

The study has established that income levels, poverty levels, expenditure levels and access to credit are the key economic characteristics essential in the use of borrowed funds. These characteristics were positively perceived by the respondents as essential in the use of borrowed credit. The study established that the characteristics are indicators of use of MFI credit. Since the data sought in the questionnaire was ranked, Spearman Rank Correlation technique was used to determine the relationship between the economic characteristics and use of borrowed funds. The study finally established that there is a significant relationship between the economic characteristics of borrowers and the use of MFI credit.

Effect of Literacy levels on the Use of borrowed funds:

The literacy levels of borrowers were operationalized as the borrowers' level of education. This level of education ranged from no formal education, primary education, secondary education, tertiary education and university education. The descriptive statistics of these levels of education were ascertained and suggested that the respondents positively perceived the levels of education as essential in the use of borrowed funds. The results of Spearman Rank Correlation confirm a significant relationship between the literacy levels of respondents and their access and use of MFI credit. Education, that is, formal skills, is therefore a determinant of MFI credit use.

5. CONCLUSIONS

The study has established that income levels, expenditure levels, poverty levels and access to credit are factors that determine the use of borrowed funds from MFIs in ASAL regions of Kenya. These economic characteristics also are indicators of the use of borrowed funds from the MFIs. The study therefore concludes that there is a significant relationship between the economic characteristics of borrowers and their use of credit from MFIs by clients in the ASAL regions. To this extent, the first research question of the study is answered.

The literacy levels of borrowers identified in the study are no formal education, primary education, secondary education, tertiary education and university education. These literacy levels are a determinant of credit access and use from the MFIs. Besides, the literacy levels have a significant relationship with use of borrowed funds. There is a significant relationship between the literacy levels of respondents and their access and use of MFI credit. Formal education is therefore a determinant of MFI credit use in the ASAL regions. This might be attributed to the fact that this region experiences the highest levels of poverty incidences in Kenya at 65%.

From the study findings, the research recommends the following:-

i. The government is called upon to institute viable financial infrastructure such as legal, information and regulatory and supervising systems for financial institutions and markets. The government needs to refocus on special programmes that disburse funds to the poor to

ensure sustainability of such programmes and promote private sector institutions in micro-finance.

ii. The MFIs need to strengthen the capacity building initiatives that help promote credit use and recovery. This will educate borrowers on the proper utilization and investment of borrowed funds. This will in turn lower the default rate on credit.

Formal financial institutions need to focus more on the poor currently, these institutions do not focus on the poor because of perceived high risks high risks involved in small transactions, and how profitability as well as the inability of the poor to provide collateral for credit. By opening up to the poor, the burden on the poor relying on MFIs will be eased. This will diversify credit access.

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