

# THE SEARCH FOR INCLUSION IN KENYA'S FINANCIAL LANDSCAPE

## ANNEX1: SUPPLY-SIDE SURVEY

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## THE SEARCH FOR INCLUSION IN KENYA'S FINANCIAL LANDSCAPE : THE RIFT REVEALED

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With support from Financial Sector Deepening Kenya



The Kenya Financial Sector Deepening (FSD) programme was established in early 2005 to support the development of financial markets in Kenya as a means to stimulate wealth creation and reduce poverty. Working in partnership with the financial services industry, the programme's goal is to expand access to financial services among lower income households and smaller enterprises. It operates as an independent trust under the supervision of professional trustees, KPMG Kenya, with policy guidance from a Programme Investment Committee (PIC). In addition to the Government of Kenya, funders include the UK's Department for International Development (DFID), the World Bank, the Swedish International Development Agency (SIDA), Agence Française de Développement (AFD) and the Bill and Melinda Gates Foundation.



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## Chapter 1

## METHODOLOGY

Table 1: Interview coverage of financial service providers by research site

	Karatina		Nyamira		Kitui		Total interviews
	No. present	No. interviewed	No. present	No. interviewed	No. present	No. interviewed	
Banks	7	6	5	5	8	7	18
SACCOs	18	8	3	3	4	4	14
MFIs	6	4	3	3	4	4	11
Other MF	6	6	1	1	2	2	9
Other:							
AFC	1	1	1	1	2	2	1
HP shops	2	0	1	1	1	1	3
Other lenders	1	1					3
	<b>41</b>	<b>26</b>	<b>14</b>	<b>14</b>		<b>19</b>	<b>59</b>

Financial service providers were identified in all three markets and interviewed using a semi-structured interview format covering details of their establishment in the market, product offering, marketing, view of market development and competition, links to other providers, and performance. Data was collected from them on their savings, loans, portfolio performance and profitability. While we endeavoured to do this for the last 3 years, there were many data gaps and hence data presented is concentrated on 2010.

The interview coverage of formal providers in each market is indicated in the table above. Concentration was on the largest institutions. Only one commercial bank declined to participate in the study, the impact of this on the data is more substantial for Kitui than any other market and we incorporate this into the discussion below. Karatina had a large number of smaller SACCOs – mainly employee and transport – so concentration was on the largest in terms of membership and assets. MFIs which did not have a branch in the town were covered when it was apparent that their coverage was important,

some had very few groups in the area. In some cases multiple branches of the same institution were also visited (this is not taken into account).

In each market there were also initiatives which promoted ASCAs: private sector ASCA managers in Karatina; CARE's COSALO programme in Nyamira and Kitui Development Centre in Kitui. In addition, where possible we interviewed other providers – HP shops, and other lenders – two private sector licensed moneylenders. Additional interviews were undertaken with District Co-operative Officers to get an overview of the SACCO sector.

The analysis below is structured as follows:

1. An overview of the sector and its performance in each site.
2. The dynamics of competition in the sector
3. Analysis of products and pricing

## Chapter 2

# OVERALL MARKET DEVELOPMENT

## 2.1 KARATINA

### 2.1.1 Overview of financial service providers

in terms of financial service providers, Karatina has a well established market and is attractive due to its relative wealth, strong agricultural economy and position on the main road going north. So, the main banks Barclays, Co-operative, Equity, KCB, NBK have been joined by new entrants: PostBank established a branch there in 2005 and more recently Ecobank in 2009. Meanwhile others have closed since 2003 i.e. Consolidated Bank. The data for the banks now also includes K-REP Bank and Jamii Bora Bank, whose branches were in Nyeri and for whom estimates have been made for their Karatina-based clientele.

The MFI sector includes the newly registered DTMs: Faulu and KWFT along with SMEP and ECLOF, of which ECLOF has established since 2003 but remains small in comparison to the others. K-REP had long been in the market and operates from its Nyeri base without an office in Karatina. Jamii Bora has been the most recent entry to this sector in 2005 but in the transition to a Bank but closed its office in Karatina in 2010 to consolidate its operations to its Nyeri branch but was planning to re-open it in March 2011.

Earlier research identified the presence of a further MF model which has been termed the “managed ASCA” model. In this, small private sector providers charge a fee to groups for managing their ASCA meetings and funds. The originator of this model was the organisation Partnership for Productivity (PFP) in the 1990s. The model has very low set up costs and in 1999 there were two organisations that had split off from PFP to set up on their own – WEDI and SEDI. In 2010 there were six such organisations though some that had appeared in the meantime had collapsed. PFP and WEDI still operated but all of the others were new since 2003: WEDA, GEDA, LCD and AMA. AMA and LCD are effectively 4th generation spin-offs from PFP as their founders have learned the model from others who had themselves moved out of WEDI.

The SACCO sector has also been long and well established. The central pillar of the sector in Karatina is SACCOs whose origins are in the cash crop common

bonds of coffee and tea. These have experienced considerable challenges from the banking sector and the new SASRA regulatory structure will intensify this. With ambitions to grow beyond their historic cash-crop base they have opened their common bonds and re-branded themselves to appeal to a wider clientele. Of the main four, Nyeri Tea SACCO has become Wanainchi SACCO; Mathira Tea has become Baraka SACCO; Nyeri Coffee Growers has become Taifa SACCO; and only Mathira Farmers has not yet renamed itself.

Employee SACCOs are dominated by Nyeri Teachers SACCO which has a branch in Karatina and a front office operation. All others are back office only (and not included in the data below). Nyeri Teachers is the largest single SACCO and also dominates the cash-crop SACCOs in terms of deposit and loan volumes but not in terms of customer numbers. This reflects the relative wealth of teachers but their relatively small numbers.

The transport sector has seen significant SACCO formation, with matatus on many smaller routes now establishing themselves, usually have grown out of Self-Help Associations of operators. With newly established licensing rules requiring that all operators belong to SACCOs or private companies operating on routes. The largest single SACCO is 2NK which is based in Nyeri but has some 40% (check) of its members in Karatina and runs the Nyeri-Karatina-Nairobi route. This has experienced significant growth and development and now operates buses, filling stations and has plans for a driving school.

In addition there were two business/trader based SACCOs in operation. One – Biashara SACCO had been moribund in 1999 but revived a few later and got a front office license in 2006. Additionally Karatina Traders SACCO had started in 2006 and grew quickly but then and scaled back to a back office operation.

AFC's office in Karatina has had a long presence and is now undergoing a new lending programme but still with a legacy of some bad debts. We also found a private licensed moneylender called Mwago Agri-Credit which lent against hard collateral such as vehicles and other movable assets.

Table 2: Overview of deposit and loan volumes and account numbers by market 2010

	No of instns	Deposits (kshs '000)	%	Members	%	Loans (kshs '000)	%	Ratio loans: savings
<b>Karatina</b>								
Banks (incl JB and KREP)	7	2,774,161	71	84,769	62	1,747,626	60	63
<b>MFI sector</b>								
Mainstream MFIs (incl DTMs)	5	34,293	1	4,239	3	105,286	4	307
Other MF: Managed ASCAs	6	22,386	1	4,296	3	56,249	2	251
Sub-total		56,679	1	8,535	6	161,534	6	0
<b>SACCOs</b>								
Cash-crop	4	339,475	9	36,280	25	201,614	7	59
Employee/Transport/Business	6	693,571	18	6,550	5	647,023	22	93
Sub-total		1,033,046	26	42,830	30	848,637	29	0
<b>Other lending programmes</b>	2					43,000		
<b>TOTAL</b>		<b>3,920,566</b>	<b>100</b>	<b>144,669</b>	<b>100</b>	<b>2,919,332</b>	<b>100</b>	<b>74</b>
<b>Nyamira</b>								
<b>Formal sector</b>								
Banks (incl JB and KREP)	5	1,005,136	76	54,848	40	1,004,296	74	100
<b>MFI sector</b>								
Mainstream MFIs (incl DTMs)	3	55,392	4	8,566	6	177,218	13	320
Other NGO delivered MF: GSLs	1	54,930	4	40,566	30	81,606	6	149
Sub-total		110,322	8	49,132	36	258,825	19	0
<b>SACCOs</b>								
Cash-crop	3	196,924	15	31,635	23	94,575	7	48
Transport/Business	3	4,367	0.3	363	0.3	1,934	0.1	44
Sub-total		201,291	15	31,998	24	96,509	7	48
Other lenders						5,000		
<b>TOTAL</b>		<b>1,316,750</b>	<b>100</b>	<b>135,978</b>	<b>100</b>	<b>1,359,629</b>		<b>103</b>
<b>Kitui</b>								
<b>Formal sector</b>								
Banks (incl JB and KREP) - NBK missing	5	1,265,978	49	47,214	51	2,140,392	60	169
<b>MFI sector</b>								
Mainstream MFIs (incl DTMs)	4	88,780	3	12,052	13	207,786	6	234
Other NGO delivered MF: FSAs & vikundi	2	43,804	2	23,834	26	112,498	3	257
Sub-total		132,584	5	35,886	39	320,284	9	0
<b>SACCOs</b>								
Employee/Transport/Business	3	1,169,906	46	9,053	10	1,105,873	31	95
Sub-total		1,169,906	46	9,053	10	1,105,873	31	95
Other lending : HP	3					5,500		
<b>TOTAL</b>		<b>2,568,468</b>	<b>100</b>	<b>92,153</b>	<b>100</b>	<b>3,572,049</b>	<b>100</b>	<b>139</b>

**Table 3: Savings and loans performance of financial institutions in Karatina, Kenya 1999 and 2003 (Ksh '000s)**

	Deposits		2003		Members/savings accounts				Loans		2003		Loan/deposit ratio(%)	
	1999	%		%	1999	%	2003	%	1999	%		%	1999	2003
<b>FORMAL SECTOR</b>														
Banks	1 148 593	73	1 093 703	65	24 543	24	17 374	23	429 995	55	537 099	55	37	49
NBFIs	113 973	7	160 000	10	25 663	25	21 000	28	70 995	9	82 000	8	62	51
Parastatals	0		0	0	0	0	0	0	29 961	4	29 961	3		
Sub-total	1 262 566	80	1 253 703	75	50 206	49	38 374	51	530 951	68	649 060	67	42	52
<b>MFI SECTOR</b>														
Mainstream MFIs	18 629	1	24 947	1	1 958	2	2 911	4	28 411	4	50 500	5	153	202
Management service MFIs	43 184	3	26 628	2	10 329	10	5 790	8	82 050	10	29 919	3	190	112
Sub-total	61 813	4	51 575	3	12 287	12	8 701	12	110 461	14	80 419	8	179	156
<b>SACCOs</b>														
Cash-crop SACCOs	168 449	11	235 102	14	37 283	36	25 250	34	53 495	7	112 662	12	32	48
Employee SACCOs	90 150	6	147 343	9	2 277	2	2 048	3	80 117	10	114 257	12	89	78
Transport/Business SACCOs	12 560	1	13 373	1	396	0	396	1	11 448	1	12 170	1	91	91
Sub-total	271 159	17	395 818	24	39 956	39	27 694	37	145 060	18	239 088	25	53	60
<b>TOTAL</b>	<b>1 576 909</b>	<b>101</b>	<b>1 676 149</b>	<b>101</b>	<b>102 449</b>	<b>100</b>	<b>74 768</b>	<b>100</b>	<b>786 471</b>	<b>100</b>	<b>968 567</b>	<b>100</b>		

Source: (Johnson, 2004)

### 2.1.2 Performance

**Banks:** We can review the performance in the market against data collected in similar earlier studies in 1999 and 2003 (see table 3). Since Equity was still an NBFi in 2003 it is appropriate to compare the whole formal sector with the current banking sector data. Between 1999 and 2003 the formal sector deposit base had remained more or less stable (despite inflation) although its proportion of deposits had shrunk slightly due to some expansion of the cash-crop SACCOs. At that time the banks represented some 75% of deposits, 51% of accounts and 67% of loans balance outstanding. While the 2010 data lacks information from one bank, the deposit base had more than doubled to Kshs2.7bn but represented approximately the same proportion of deposits at 71%. In terms of accounts this proportion had risen to 59% while the proportion of loans outstanding was at 60%. Interestingly the loan to savings ratio had risen from 49% to 63% for these banks demonstrating the increased emphasis on lending although given the emphasis in the market place, it may be surprising that this figure is not higher.

The total number of bank accounts in the Karatina market has increased from 17,374 to 84,769 over the period – an almost 4 fold increase over 2003. Population growth alone would be expected to expand the population by some 30% over ten years<sup>1</sup> so this represents some significant expansion

beyond population growth. However, multiple account holding is also likely to have increased. The mean number of bank accounts held by those with bank accounts in Karatina is 1.26. While we don't have a similar figure for 1999, the banks certainly are aware that there are much higher levels of multiple account holding. Applying this to the figure of 84,769 accounts suggests that outreach may in fact only be some 68,000. With these figures in mind, we can suggest that some 45000 customers have been added beyond population growth and taking into account some level of multiple account holding. The banking sector has done relatively well in comparison to the other types of providers since the total accounts in the market at 144,669 has only approximately doubled since 2003.

**Mainstream MFIs:** By comparison the mainstream MFIs have increased their deposits from Kshs25m in 2003 to some Kshs34m in 2010 remaining at approximately 1% of the market. Membership has approximately doubled – though would be an almost three times if Jamii Bora and K-REP are included here rather than in the Banking sector, although on the deposit side their inclusion does not change the figures so substantially. In terms of the proportion of accounts in the market this remains at around 4% with JB and K-REP included. So that outreach has indeed increased but not enough to show significant changes in the market profile. In terms of loans the volume outstanding has again doubled but represents a similar proportion of the market. Interestingly however the ratio of loans to savings has increased from

<sup>1</sup> Using the World Bank Development Indicators figure of 2.6% p.a. for the past decade.

200% to 300%. This represents the fact that MFIs are now lending higher multiples of savings, so for example, KWFT has lowered the compulsory savings for a first loan from 20% to 10% so doubling the multiple from 5 to 10. However, Jamii Bora for example lends only twice savings – this in turn puts it at a competitive disadvantage compared to other institutions.

**Managed ASCAs:** The managed ASCA sector in Karatina has by contrast declined. While the figures here are estimates based on averages for three institutions since most of the organisations did not possess detailed records, the figures presented are entirely consistent with the interviews. Hence the volume of deposits has remained roughly stable in absolute terms while declining as a proportion of the total. At the same time the numbers of clients has fallen compared to 2003 although the loan volume has more than doubled. The situation reported to us by the managed ASCA organisations was that it was now very difficult to establish new groups in the Mathira area and they were travelling to much more distant markets to develop their businesses while still based in Karatina. Hence some were travelling as far as Embu, Meru, interior areas of Murang'a and as far as Subukia. According to one of the organisations managed ASCA groups “got spoilt” in Mathira. Some staff of some organisations mis-appropriated group funds and the name “gubasho” (meaning “advance” – the short term loans which are easily accessed at every meeting) came to mean losing money. Hence the groups that exist in Mathira are predominantly those established by the older organisations PFP and WEDI which have been there for some time. This also explains the increase in the lending:saving ratio from some 112% in 2003 to 251% in 2010 since older groups will have built up the value of their funds through retained profits. Moreover, other key informants told us that people had learned the methodology of ASCAs and did not see the need of paying a “teacher” to run the group for them, they were able to run them themselves. So it is likely that this has also reduced demand for their services.

**Cash-crop SACCOs:** These have increased their deposit base by some 50% and reducing their market share of deposits to 9% from 14% in 2003. Meanwhile customer numbers have increased from 2003 and approximately returning to their 1999 levels, but now representing a smaller proportion of the market at 25% compared to 34% in 2003. This reflects the growth in bank accounts and smaller deposit sizes in SACCOs compared to many banks. For loans they have doubled their OLB compared to 2003 but now represent only 7% of the market. The lending ratio of 59% is interestingly very similar to that for the banks and similarly to banks has increased since 2003 from 48%.

**Employee, transport and business SACCOs:** For 2010 this data has been consolidated with business and transport SACCOs since we only collected data from one employee SACCO and our policy is not to present data that enables a particular institution's performance to be revealed. However, as indicated above, Nyeri Teachers dominates the whole SACCO sector in terms of deposits and loan volumes although having a much smaller proportion

of clients. Compared to 2003 the combined deposits of these two types of SACCOs has almost doubled as a proportion of the market from 10% to 18% and demonstrates the strength of employee SACCOs based in sectors such as teachers in competing with the banks and being able to retain the salary payments market. Their lending is also significant and some 29% of the overall market, again representing the strength of Nyeri Teachers and its ability to lend against salary. As will be discussed below this is a key area of competition for the banks and SACCOs.

The overall volume of deposits at Kshs3.9bn is some 148% higher than it was in 1999. Interestingly the CPI has increased by some 222% over this same period, and hence it appears that there is some reduction in the real value of financial sector deposits over this period. This applies to bank deposits also. Explanations for this are many. It could be that the Karatina economy is not as vibrant as it was in 1999 – but this is not the sense of it, and 1999 was a year of low to negative growth in the Kenyan economy as a whole. An alternative is that relatively more deposits from this area are in fact being held outside the area or in other financial sector mechanisms. A further possible reason is that it is very vibrance of the economy that means that Karatinans tend not to hold funds in banks that can be invested in viable projects – in this sense the vibrant growth of Kenya's economy presents an alternative opportunity for funds outside of the banks.

## 2.2 NYAMIRA

### 2.2.1 Overview of financial service providers

Nyamira is a very small town with many households having tea farms right next to the town. Moreover, Nyamira District is itself small and has a relatively small catchment area around it. Kisii is easily accessible from areas to the south and being a larger city means that Nyamira is less attractive as a business centre. Indeed there is little space for business area expansion as it has steep hills either side of the main road for much of its length. It was host to the rapid bank branch expansion underway in Kenya in 2007. KCB is of the longest standing and situated in the building of the District Headquarters. Due to its length of standing and earlier government-owned status, this means that it is home to many of the large government and institutional accounts in the area. Equity, Barclays and Co-operative opened there in 2007, followed by Family in early 2008. While all thought that this would be a market with potential, this degree of expansion has not brought the returns to all players that were hoped for as Nyamira's economic base is relatively limited. Although a district headquarters offering an employment base, the small size of Nyamira and its surrounding areas means that there is not a particularly large employment market of teachers or other employees. Although the tea industry is significant, providers estimate that only about half of tea farmers are in fact banked with the other half still collecting their payments in cash. While they are actively competing for business in winning tea farmer's accounts this is proving a difficult sector to penetrate, not least because regular tea incomes

are often very small (<Kshs1000 per month) and they are also competing with the SACCOs for this market.

Agent banking was just beginning in January 2011 when the research was undertaken in Nyamira. One agent was just being established in a nearby market by Equity. At that stage no other providers in Nyamira were discussing setting up agencies.

The SACCO sector comprises three cash-crop based SACCOs: Nyamira Tea SACCO in Nyamira itself; Wakenya Pamoja SACCO based in Kisii with branches in Nyamaiya and Kebirigo; and Borabu Farmers SACCO based in Keroka and with a branch in Kebirigo. The research covered these branches in Nyamaiya and Kebirigo. Wakenya Pamoja SACCO has its origins in the coffee sector but expanded into tea in the 1990s and has since opened its common bond. It has also expanded into microfinance since 2005 with a group-based microfinance scheme (assisted by CIDR and DFS to do this) and this has brought in significant additional business to become a mainstay of its operations.

Beyond the cash-crop sector, the SACCO sector in Nyamira is relatively under-developed. While government employees may belong to SACCOs based outside of the area (eg the teachers SACCO in Kisii) there were three small employee-based SACCOs in Nyamira itself, two based in church organisations and one for a bus company's employees. There was only one transport SACCO, along with one jua kali; two traders SACCOs; and one multi-purpose SACCO formed by dairy farmers and all of these were relatively small and experiencing associated difficulties. This contrast strongly with Karatina where collective action to form SACCOs was strong and would seem to reflect the contrast of approaches with Karatinans wishing to retain wealth in their own area while the social relations to undertake this effectively in Nyamira have not been developed.

Faulu and KWFT both opened branches in Nyamira in 2004. Also present is K-REP's Juhudi Kilimo programme which concentrates on group lending to farmers, mainly for dairy cows and also for other assets.

CARE commenced its Group Saving and Loan programme (GSL) in late 2008. This programme had a target of reaching 100,000 clients with a terminating ASCA model of microfinance by 2011 using different delivery channels in the form of church-based partners and private sector trainers.

### 2.2.3 Performance

**Banks:** The banking sector had deposits of Kshs1bn at end 2010, although one banker commented that this was a relatively low figure due to the payouts of the tea sector in November. However, the situation would have been similar in Karatina regarding tea payments so in this sense is comparable. This represented 76% of deposits. The number of accounts at 54,848 reflects the smaller market than Karatina, though given the level of economic activity

it is perhaps not as small as might be expected. This however represents a smaller proportion of accounts due to the scale of the cash-crop SACCOs and the GSL programme of CARE. The loan figure of Kshs1bn is interesting as it demonstrates a situation where the sector is re-cycling the full extent of its deposits into the local economy and represents an aggressive lending stance on the part of the sector.

**Mainstream MFIs:** Interestingly the mainstream MFI sector has some 60% more deposits and loans by volume and double the number of clients, compared to Karatina. This is surprising given the less well developed micro-enterprise sector in the town and its environs. Moreover, these figures exclude the MF programme of Wakenya Pamoja SACCO which was running quite successfully. This may reflect more on the lack of alternative options for finance than in Karatina which has a more vibrant history of SACCOs and ASCAs. With Kshs177m of loans outstanding these represent some 13% of the market

**Other MF:** The GSL programme of CARE has achieved rapid coverage of 40,566 by end 2010 although little is known about the long-term sustainability of this form of provision since groups are, in theory<sup>2</sup>, left to manage the system on their own once the first cycle lasting usually about a year, is complete. This represents some 30% of clients while deposits are similar to those of the mainstream MFIs at Kshs54m and 4% while the outstanding loans are some 6% of the market representing the much smaller loan sizes achieved through these systems. While MFI loans are rarely below Kshs10,000, GSL loans tend to start at a few hundred shillings

**SACCOs:** The SACCO sector with 31,635 members is approaching the size of the sector in Karatina, and representing a similar proportion of clients, though a larger proportion of the market in terms of deposits and a similar proportion in terms of loans. Its lower ratio of loans to deposits at 48% compared to 59% in Karatina suggests it is less effective at lending. From the customer side, many tea payments are really very small (<1000kshs per month) which makes lending against them difficult as it may leave the recipient with no funds to collect each month. This leaves them lending mainly against bonuses. Moreover, "soko huru" for tea is operating in Nyamira whereas it is not operating in Karatina. In Nyamira there are more private sector tea factories due to the private sector tea plantations around Kericho and hence there are tea buyers who visit the farms. This gives tea farmers a means of selling their tea and avoiding repaying loans taken through tea SACCOs. Higher rates per kilo are achieved by selling to "soko huru" in the short term because these reflect the final price for tea, in contrast to the rates paid through the KTDA factories where a small monthly payment is made followed by the bonus to reflect the final prices which is paid the end of the year.

<sup>2</sup> Other research being undertaken on this model suggests that church-based trainers who are still present in the community continue to support the operations of the groups, though this may also improve their potential long-run sustainability.

The rest of the SACCO sector is very very small by comparison and barely registers in the overall profile, in stark contrast to the case in Karatina and Kitui.

## 2.3 KITUI

### 2.3.1 Overview of financial service providers

The banking sector in Kitui town benefits from the fact that it is the major town for a large geographic area, although it was the most sparsely populated of our research sites it has a large catchment area.

It has also experienced the rapid bank branch expansion of the 2007 period. National Bank took over the Standard Chartered Bank when it withdrew in the 1990s and was the only fully established bank there for some time, hence it is again therefore home to a significant portion of the institutional business base of the district. PostBank's branch is also of relatively long standing. KCB has had a presence for some time as a satellite office, later developing into a full branch. K-REP had operated as a microfinance institution in Kitui since 1994 and then, after its conversion to a bank in 1999, established a branch in 2004. The branch expansion of the last few years has brought Barclays back in 2007 – it had previously had a branch in Kitui which it closed in the 1990s. Equity established in 2008 and Co-operative in 2009. Equity had established 12 agencies by March when the research was undertaken with many more planned.

The MFI sector is also well represented. K-REP has had its MF programme there since 1994 and has developed over the decade. BIMAS established in 2000; KWFT in 2001; Faulu in 2007 and SMEP is the most recent arrival in late 2010. KWFT is the largest and has split its offices into two to serve the east and west of the greater Kitui area.

The other MF programmes in operation included Financial Service Associations (FSAs) established by K-REP Development Agency and now managed under contract by K-REP Fedha Services (a spin off from K-REP Development Agency). This model is essentially a village level bank which is owned by its members and has a local board. It operates a flexible savings account and a loan scheme based in a group lending model. There are 11 in Kitui with some 22,000 shareholders, the largest one having approximately 4000 shareholders. They have been undergoing a significant programme to attempt to achieve financial and organisational sustainability and this has been achieved at the level of the FSA itself but the KFS organisation providing the support services has not quite achieved sustainability, though the Kitui region office was at 99% financial sustainability.

The Kitui Development Centre was found to have promoted a programme of self-help groups now locally known as "vikundi" (the Swahili term for group). This model differed to the standard GSL model that was being promoted in Nyamira or the ASCA model in Karatina. As KDC had promoted it, it involved

groups of 15–20 women. There is no fixed office position and a different member of the group acts as "moderator" for each meeting. It involves very small weekly contributions of Kshs10 per member into a fund from which loans are taken at each meeting. The loan is not related to the amount of savings in the group only to the frequency of saving and is decided on a needs basis. The interest was flat rate at 5 or 10% depending on the groups decision for one to three months based on amount borrowed and there is a minimum payment per week rather than a repayment schedule. Another loan can be taken once the loan is cleared. While the figures reported here are for the groups promoted by KDC in the area, in our demand-side research we encountered an area where the model had been replicating itself. An additional "innovation" that groups have developed is what is called the "moderator loan". Since the moderator for the meeting takes any remaining funds away after the meeting to be returned the following week (having to pay double for any funds not returned), members subsequently borrow directly from the moderator outside of the meeting – usually at a rate of 10% for the week.

The SACCO sector was dominated by Kitui Teacher's SACCO which was a very significant player in the sector and in heavy competition with the Banks. A smaller SACCO for School support workers (KISCWO) was operating as a back office only. Kitui Biashara SACCO was growing its base of traders in the town and had interesting emerging practices eg of daily savings collection.

### 2.3.2 Financial performance

**Banks:** The banking data in Kitui is missing a key bank which decided not to participate in the research. This means that the deposit base is an underestimate and a guesstimate would put this at nearer Kshs2bn. This is much bigger than Nyamira which is likely due to the fact that Kitui Town has a much wider catchment area as a district than Nyamira, but does not rival Karatina. In terms of numbers of accounts the estimates are likely less distorted as it is likely that the deposit base is largely institutional rather than personal. In this case the banks have 51% of accounts by number being rivalled for numbers by the FSAs who have 26% of the clientele.<sup>3</sup> However, what is rather interesting is that for the banks that were captured by the research the loan to savings ratio is much the highest of the three areas. Even accounting for the fact that in Nyamira the timing of the research was at a time after the November tea bonus payout and hence when loans outstanding were likely to have been lowest in seasonal terms, the shift in the ratio for the banks in Kitui is extremely interesting. This underlines what the banks were telling us in terms of the major competition between them – and with Kitui Teachers SACCO – being over salaried lending and much of this to the large number of teachers in Kitui. Indeed teachers are the major proportion of the salaried employment market. This net debt position is also a very interesting contrast to the Nyamira and Karatina markets.

<sup>3</sup> There may be some non-comparability here as FSAs stretch across Kitui but we did not remove those from the total that were closer to other bank markets.

**MFIs:** The mainstream MFIs in Kitui appear to have a larger deposit base, but representing only 3% of the market, and more clients representing 13% of the market than either of the other two markets. Along with a loan portfolio rivalling that of Karatina. This again probably reflects Kitui's being a more major centre than Karatina or Nyamira. However the loan to savings ratio is a little lower, also representing the lower absorptive capacity of Kitui in terms of lending.

**Other MFIs:** This sector has some 26% of the customer base but only 2% of deposits. This represents its attempt to bank the rural poor population and 3% of loans. It is therefore providing significant outreach in relation to the total banked population. Its rural outreach is reflected by the fact that there is no branch in Kitui town for example. The high loan to deposit ratio for FSAs reflects their capital structure.

**SACCOs:** The SACCO sector is dominated by Kitui Teachers SACCO and the deposit base here is clearly larger as a result for this sector even than Karatina. However, again it represents a relatively much smaller portion of clients at 10% although a significant portion of loans outstanding at 31% with a high loans to savings ratio of 95% – underling the business opportunity that the banks are eager to capture.

## 2.4 COMPETITION DYNAMICS AMONG PROVIDERS ACROSS MARKETS

### 2.4.1 Banks

With the above background we discuss the main areas of competition across these three markets, starting with the Banks.

#### Transaction and deposit accounts

Most banks, and especially the market leaders, now have active marketing teams that run marketing campaigns in market centres, at barazas and at school and other institutional events. These work on a commission basis and marketers sign up customers. Bank managers now recognise that they have to pursue customers in contrast to early years where they waited for the to walk through the door. In Karatina in particular, managers reported that customers are much more educated about the terms and conditions of accounts and now “shop around” between banks.

However, with these much more aggressive recruitment strategies, the levels of dormancy are of interest. Equity is the bank with the most stringent dormancy policy – an account becomes dormant after six months during which there is no transaction. A fee of Kshs200 is charged to “wake up” the account. Other banks do not charge but operate KYC to ensure that accounts that customers using accounts after some time can indeed identify themselves. Hence while Equity tends to report quite high numbers of dormant accounts this is largely

a result of its own policies – never the less these are included in the above figures as other banks do not remove them from their figures.

#### Loans

The most aggressive competition in the market is in pay-slip lending. Again banks have marketing teams who actively sell loans. The key development here has been that check-off lending does not require that people have the account through which they receive their salary in the bank from which they borrow. Check-off agreements have been developed between lenders and the Teachers Service Commission (TSC) and other large government and private sector employers that enables this to take place at source and independently of the salary being paid through a bank account.

Many banks are engaged in what might be called a “battle of the buy-offs” in this sector. The competition is over loan term and interest rate. As these respectively lengthen and lower, so banks are continuing to aggressively market their products to those who already have outstanding loans with other providers. By offering them higher loans against the proportion of their salary that is available for loan repayment through check-off they can offer additional capital while buying the loan from the previous lender. This is now being further facilitated by the formal establishment of the Credit Reference Bureau in 2010. However, previous to this borrowers had to establish procedures through which they could ensure that loans from other institutions would indeed be bought off. This would usually involve first releasing a cheque to the borrower for the outstanding balance at the other institution and then only releasing the cheque for the balance when the borrower produced evidence to show the loan had been cleared. Prior to these procedures this aggressive lending had led to bad loans. However, banks have had different policies on whether or not to in fact buy-off from other institutions.

In addition this salary lending market has brought the banks into close competition with the SACCOs who do not in turn buy-off loans from the banks. This was particularly evident in our research sites with respect to lending to teachers, but is present more generally. Since SACCOs lend as a multiple of savings or shares to a level of 3 or 4 times depending on their liquidity, customers are starting to realise that this is tying up their funds. By shifting to the banks which only lend against the pay-slip and do not require a deposit they can free up their savings in SACCOs and the most astute realise that moving to the banks therefore means they can withdraw these funds. Some informants indicated that although some had done this, they had experienced terms and conditions with the banks that were less conducive and had regretted the experience.

The extent to which this aggressive pay-slip lending leads the market was particularly marked in Kitui. This is also evident in the loan to savings ratio (see table 3). Where banks also receive the employee's salary, they will also make advances against the remainder of the pay-slip that is not dedicated to check-

off. Bank managers also reported their awareness of money-lenders who were lending to teachers in advance of them getting loans from the banks and being repaid once the loan was disbursed. Kitui was the only one of the three sites where we also found that a Nairobi based money-lending company had set up an office. The degree of leverage that teachers were subjecting salary slips to started therefore to appear problematic and in excess of the two-thirds guideline from the Government. A financially very well informed teacher explained that most teachers were not entirely dependent on their pay-slips but ran other businesses too and, in Kitui, tended to support an extended family. Hence their salary was the key means through which lending could be accessed and so was leveraged as much as possible.

Some banks are attempting to make in-roads into the microfinance market. While Equity's product offering is the most developed in this respect having a range of enterprise and agriculture loans along with youth groups and women group lending. Co-operative has now a long history in this sector starting with the Biashara Plus loan in 2000 and has expanded its product range although it does not have agricultural loans with which to attract tea farmers. KCB has also developed micro and small business products, though again has not ventured into agricultural lending. Family has both micro business and tea scheme lending.

#### 2.4.2 Mainstream microfinance

The transition of KWFT and Faulu to DTM status during 2009 and 2010 had not so far made a significant difference to their operations. If anything, KWFT had primed its clients so well on the change that there was then some impatience that branches had not arrived in their locations sooner. Both DTMs are expecting clients to use their DTM accounts to save and are requiring them to hold minimum deposits in these accounts.

In terms of products the core group lending product has been added to by KWFT to include a range of products tied to particular purchases such as education, agriculture or consumer lending. Many of these products finance purchases directly, but the most popular was the loan for LPG gas stoves which came under consumer lending. This loan for Kshs10,000 appeared to operate as a top-up loan that borrowers could turn to when they had a need for additional cash and because it was not paid directly to the supplier by KWFT.

For Faulu, an innovative product has been Pesa Chap-Chap – which offers loans of up to 20% of the loan security account at a flat rate of 10% for 10 days accessed over the mobile phone and with repayment deducted directly from the voluntary savings account (Hazina). Eligibility required no arrears in the last two months, and the incentive for repayment was that future access to the facility was barred if it was not paid on time.

Both of these products for KWFT and Faulu represent a response to demands for additional liquidity from customers.

#### 2.4.3 Other microfinance

The promotion of ASCAs is present in each of the markets. While in Karatina this is via private sector ASCA managers who operate on a fee-for-service basis, as has been pointed out above, the Mathira market for their services is no longer a vibrant one. It appears that this technology is sufficiently well known about that people feel that they no longer need "teachers" to support them. In Nyamira on the other hand CARE's promotion has reached some 40,000 clients in two years. Both here and in Kitui the approach is one of promotion followed by the expectation that groups will be left to continue themselves, although in Kitui there is also intended to be an ongoing support structure through the federation of groups into Clusters. The sustainability of these groups as a technology is the subject of other FSD studies.

We indicated above the rapid self-replication of the KDC initiated methodology in the sub-location of Kitui where we undertook our survey. This is important in that it signals that the technology was not only highly appropriate to the context in terms of its affordability of savings and access to loans but that people felt able to adopt it very easily.

#### 2.4.4 SACCOs

SACCO competition in the traditional cash-crop sector is strong in both the Karatina and Nyamira markets. In Karatina all tea and coffee farmers are paid through an account while in the Nyamira market, a significant proportion – estimated at 50% – do not have accounts and are still paid in cash. There is therefore significant competition to obtain this business both by the SACCOs and the banks. Since tea factories contract financial institutions to make the payments, some farmers believe they have an account with a particular institution and these are the first target for SACCOs to convert into actual accounts. SACCOs in Nyamira still ran mobile vans in order to undertake this outreach and in the case of Wakenya Pamoja this had proved a means through which it could make paypoints more accessible to its microfinance customers also.

SACCOs in Karatina and Nyamira that had changed their names from locally specific names, had intentions to expand their businesses beyond their immediate locales. From Nyeri this meant that Wananchi SACCO was seeking to expand to Subukia, while Wakenya Pamoja in Kisii was planning to expand beyond (the old) Kisii District.

Competition had been aggressive between some of the SACCOs in recent years, with some malpractice regarding the movement of farmer's tea paypoints. In this there were allegations that some SACCOs had made fraudulent requests to KTDA so that a farmer's payment would be moved to a different SACCO. This kind of malpractice reflects political as well as market competition among SACCOs.

The larger SACCOs indicated that they were well placed to comply with SASRA regulations, while some of the middle-sized were likely to experience further

pressures as a result of these regulations as their ability to on-lend was reduced by its requirements. The teacher's SACCOs in Karatina and Kitui were the home to significant deposit bases which have developed historically while holding a much smaller portion of accounts. This makes them a target for the banks in search of business as explained above.

Transport SACCOs were most prevalent in Karatina. In Kitui there has been a recently new formed SACCO on the Nairobi route which has raised competition there too. The matatu business is a saturated market and developing new routes is a costly business and takes significant new investment to open

stages in new locations. Matatu owners tend to now need to run a number of vehicles in order to be able to make good profits i.e. ensuring that their vehicles can get business. The largest SACCOs such as 2NK have therefore developed their own SACCO owned projects into which members can invest and with the planned upgrading to buses with no future 14-seater licenses being issued by the Transport Board, investment in new vehicles now requires more capital. Purchasing buses will therefore be easier as a collective project than by individual owners and some argued that this will be the only way to develop in future. The existing model for the matatu business is therefore likely to need to change significantly over the coming years.

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<sup>4</sup> See [www.oxfam.org](http://www.oxfam.org)

## Chapter 3

# PRICING

### 3.1 TRANSACTION AND DEPOSIT ACCOUNTS

Data was collected on the most basic accounts that each institution offered. Since it is hard to model savings account use, we simply present an overview of the key features and prices involved. In terms of presenting a baseline of data for FSD to consider change, data collected (available on request) offers a profile of charges against which future significant changes can be assessed.

From the point of view of extending access the important points to note here are:

- Only two banks (Co-operative and KCB) and the FSAs operate accounts where there is neither an opening minimum balance or the need for an operating balance.
- The majority operate on the basis of unlimited withdrawals and some SACCOs retain a one per week use policy (after which additional charges apply).
- ATM card acquisition is only free at PostBank, for others it is a minimum of Kshs250
- Over the counter withdrawal fees are cheapest for the FSAs, then SACCOs (at Kshs30) followed by K-REP and Equity Banks.
- ATM withdrawal charges are a minimum of Kshs25 (also M-PESA withdrawal fee for under Kshs2,500).
- While Banks have mostly abolished ledger fees, the SACCOs retain these annually.
- The main banks accounts are now mostly linked to mobile phones which allows balance checking, mini-statements and transfers to M-PESA (which will then incur the M-PESA withdrawal charge which is dependent on amount withdrawn). However pricing for these services ranges from a minimum of Kshs10 per minute to Kshs20-30 per alert.

It is important to get a perspective on these charges. During our research, the price of a kilo of unmilled maize was Kshs25-35, while a 2kg packet of milled was Kshs 80-100, by April the price had increased to Kshs135.<sup>4</sup> An ATM withdrawal fee of Kshs25-30 therefore represents the price of a kg of maize, which would feed a three-four people for one meal. In a context where the bottom end of the market is earning around Kshs70 for piece rate agricultural work such as tea picking in a day (not a full day) or Kshs200 for other casual labour, then these charges are much higher than such a potential market will afford. Pressure on food prices only serves to underline how problematic the costs of maintaining an account would be.

The addition of M-PESA withdrawals via mobile phone enabled accounts also adds a layer of costs since the withdrawal fee is added to the transfer fee and then the M-PESA withdrawal fee would be paid in addition when the cash was withdrawn.

In terms of interest rates, as the table makes clear, the rates on savings accounts where offered by banks are 3% down to 0%. SACCO rates are little different though Taifa SACCO in Karatina was offering 4%. These rates for SACCOs are independent of annual dividends on back office share accounts which the mature SACCOs still pay at approximately 5%.

### 3.2 LOANS

In table 4 the effective interest rates using a range of loan sizes have been calculated for a range of loan products. The products chosen to make these calculations are either those with the lowest entry point in terms of loan amount and usually those directed to the small or micro-enterprises. Where such products are not available (eg Barclays) then the most used product (in the case of Barclays, their salaried lending product or "scheme" loan), but of course this does not then give a realistic comparative view of rates on salaried lending.

In general rates fall with larger loan amounts due to fixed rate fees eg for application or chattel registration. Co-operative Bank's rate of over 100% for a Kshs10,000 loan is due to these charges plus a monthly standing order fee of Kshs150 which consequently have a significant impact on the effective interest rate on a loan of Kshs10,000.

Overall, where interest rates are based on reducing balance they are lower overall than where they are based on flat rates (this is not a comparison with the flat rate), this means that institutions charging flat rates do not compensate for this by having lower fees and charges for other aspects such as application, insurance, account operation etc. The lowest rate in the three markets we reviewed was for Kitui Teacher's SACCO which with a reducing balance rate of 12% and very low additional fees, charges only 14.43%. The second lowest is KCB's Boresha Loan followed by Equity Bank's Equiloan.

MFIs and MFIs that have converted to banks, have rates that are overall higher than either banks or SACCOs. The Wakenya Pamoja Microfinance product is also priced at the upper end in contrast to normal and development loan SACCO products. Of course, MFIs would defend these higher prices on the basis of their outreach to customers and the costs that this incurs.

However, these prices do not include the equity deposits or ongoing savings requirements that MFIs impose. Table 4 shows how these prices rise when the equity deposit and ongoing savings requirements are included in the calculations. The inclusion of these terms and conditions changes the interest rates significantly for MFIs and SACCOs but not for banks. This underlines the point made about competition in salary lending above, that some clients are realising that the tying up of their savings in institutions raises the effective interest rate as well as tying up their capital. The highest increase is for Jamii Bora loans. This is due to the fact that the lending multiple is two so that half of the loan amount is held in savings. K-REP FSAs is at 25%, K-REP Bank at

20% while Faulu, KWFT and SMEP are at 10%. In addition where DTMs now require minimum operating balances in the individual savings accounts which are separate from the accounts in which members keep their collateral savings, this further adds to the costs incurred. The point to be made here is that these additional requirements raise the costs of loans significantly.

Compared to data collected in 2003, Bank nominal rates are considerably lower. Whereas they were quoting approximately 25% for a range of products, declining balance rates are mainly now in the region of 15% up to 20%. This gives a fall of approximately 10% for the headline nominal rates in the sector. Table 4 gives an average of 39% falling to 29% for effective rates as loan sizes rise.

MFI quoted flat interest rates by contrast have fallen by up to 3% except for Faulu which has stayed the same. This relatively small fall does however produce a much larger reduction in the effective rate. Hence the mean rate for MFIs and here we have included K-REP and Jamii Bora Banks at 44% falling to 39% for Kshs100,000. SACCO rates are little changed having historically been operating at 12% per month for normal and development loans. Where they have introduced new products these rates may be higher (eg Wakenya Pamoja's Microfinance product) but advances (as in the case of Nyeri Teachers Salary advance) have always been priced more highly as short-term loans. The exceptions in this list are Taifa SACCO and Mathira SACCO which have higher rates for normal or development products and this is a result of liquidity

constraints. They are still the cheapest, with the average rate falling from 33% to 25%. So that Banks are now only a couple of percentage points on average more expensive than MFIs for low loan amounts and only 4% more expensive than SACCOs for amounts of Kshs100,000.

In terms of effective loan prices therefore, banks are now cheaper than they were and some are very competitive with SACCOs. MFIs remain the most expensive though it can be argued that this represents higher transactions costs – in most cases of loan officers visiting groups and hence reduced transactions costs for clients in respect of contact with the institution. However, once equity deposits and ongoing savings requirements are brought in as a cost, MFIs and SACCOs become much more expensive, with MFIs remaining much more expensive and in fact their prices have risen since 2003. In 2003 effective interest rates when equity deposits and savings were included on a Kshs20,000 loan ranged from 66% for SMEP to 102% for Faulu, and averaged 80% across four MFIs (including K-REP Bank and KWFT). The average for these same MFIs in 2010 is 101% for Kshs10,000 falling to 95% for Kshs 25,000 and 83% for Kshs100,000. Hence rates have overall increased by over 10% for loans of some Kshs 20,000. This is caused by ongoing savings requirements being higher (eg. a minimum of Kshs100 per week compared to Kshs 50 per week in 2003) despite the fall in headline flat rates and the fall in equity deposits as a proportion of loan size. By this measure MFI rates remain considerably higher than others in the market.

Table 4: Loan pricing: Effective interest rates

Institution	Product name	Quoted interest rate	Interest calculation	10,000	25,000	50,000	100,000
Barclays	Scheme Loan	15-19%	Flat Rate up to 80k then declining	38.72%	38.72%	38.72%	25.43%
KCB	Boresha Biashara	15%	Reducing Balance	19.55%	19.55%	19.55%	19.55%
Cooperative Bank	Biashara Plus	30%	Flat Rate	86.81%	69.97%	64.22%	51.48%
Equity Bank	Equiloan	15%	Reducing Balance	21.41%	21.41%	21.41%	21.41%
Family Bank	Biashara Boost	19%	Reducing Balance	29.02%	29.02%	29.02%	29.02%
<b>Average</b>				<b>39.10%</b>	<b>35.74%</b>	<b>34.58%</b>	<b>29.38%</b>
K-Rep Bank	Group Loan	16.50%	Flat Rate	43.09%	38.22%	36.61%	35.82%
Jamii Bora	Micro business loan	18%	Flat Rate	37.82%	31.32%	30.53%	34.13%
MFIs				39.49%	35.46%	34.30%	30.98%
Faulu Kenya	Mkopo Biashara	22%	Flat	76.12%	52.12%	50.13%	49.14%
SMEP	Inuka 1 Loan	20%	Flat	44.67%	42.55%	41.88%	41.55%
KWFT	Biashara Loan	19%	Flat below Ksh 100k	39.01%	39.01%	39.01%	39.01%
BIMAS	Msingi Loan	17%	Flat	37.15%	37.15%	37.15%	37.15%
K-Rep FSAs	Biashara Loan	15% 1st, then 18%	Flat Rate	31.79%	34.13%	33.92%	33.82%
<b>Average (incl K-Rep Bank &amp; Jamii Bora)</b>				<b>44.23%</b>	<b>39.21%</b>	<b>38.46%</b>	<b>38.66%</b>
<b>SACCOs</b>							
Kitui Teachers SACCO	Normal Loan	12%	Reducing Balance	14.43%	14.43%	14.43%	14.43%
Nyeri Teachers SACCO	Salary Advance	10% p.m.	Flat	46.49%	41.17%	39.45%	38.59%
Taifa SACCO	Development Loan	18%	Reducing Balance	36.77%	31.53%	29.77%	28.88%
Nyamira Tea SACCO	Normal/Development	12%	Reducing Balance	29.21%	19.12%	15.60%	13.81%
Baraka SACCO	Development Loan	12%	Flat	25.80%	25.56%	25.48%	25.40%
Mathira SACCO	Normal Loan	14%	Reducing Balance	25.56%	24.32%	23.90%	23.70%
Wakenya Pamoja SACCO	MF Loan	18%	Flat	65.43%	48.67%	42.42%	39.15%
Biashara SACCO (Ktn)	Development Loan	12%	Flat	28.43%	26.61%	26.00%	25.70%
Biashara SACCO (Kitui)	Normal loan	12%	Reducing Balance	21.86%	18.22%	17.03%	16.44%
<b>Average</b>				<b>32.66%</b>	<b>27.74%</b>	<b>26.01%</b>	<b>25.12%</b>

**Table 5: Increase in effective interest rates when equity deposits and ongoing savings requirements are included**

Institution	Product name	10,000	25,000	50,000	100,000
Barclays	Scheme Loan	0.00%	0.00%	0.00%	0.00%
Kenya Commercial Bank	Boresha Biashara	0.00%	0.00%	0.00%	0.00%
Cooperative Bank	Biashara Plus	0.00%	0.00%	0.00%	0.00%
Equity Bank	Equiloan	0.00%	0.00%	0.00%	0.00%
Family Bank	Biashara Boost	0.00%	0.00%	0.00%	0.00%
K-Rep Bank	Group Loan	40.11%	125.46%	106.82%	97.43%
Jamii Bora	Micro business loan	237.71%	156.54%	130.51%	114.29%
MFIs					
Faulu Kenya	Mkopo Biashara	53.81%	32.30%	33.84%	28.54%
SMEP	Inuka 1 Loan	73.86%	18.53%	12.94%	10.52%
KWFT	Biashara Loan	33.09%	15.60%	11.30%	9.37%
BIMAS	Msingi Loan	28.70%	12.85%	8.98%	7.24%
K-Rep FSAs	Biashara Loan	72.68%	41.91%	31.77%	27.44%
SACCOs					
Kitui Teachers SACCO	Normal Loan	15.06%	15.06%	15.06%	15.06%
Nyeri Teachers SACCO	Salary Advance	15.45%	13.49%	12.87%	12.56%
Taifa SACCO	Development Loan	37.22%	32.98%	31.51%	30.76%
Nyamira Tea SACCO	Normal/Development	14.01%	9.84%	8.26%	7.42%
Baraka SACCO	Development Loan	13.54%	13.40%	13.36%	13.31%
Mathira SACCO	Normal Loan	28.37%	26.91%	26.43%	26.19%
Wakenya Pamoja SACCO	Microfinance Loan	25.51%	21.60%	19.88%	18.91%
Biashara SACCO (Ktn)	Development Loan	15.02%	13.99%	13.65%	13.48%
Biashara SACCO (Kitui)	Normal loan	24.57%	20.33%	18.96%	18.28%

## Chapter 4

# CONCLUSIONS

This portrait of the supply-side across three markets presents some interesting dynamics. There is fierce competition between the banks and SACCOs in terms of both deposit accounts and loans. In terms of deposit accounts, the SACCOs appear to be losing out to the banks. The Karatina data suggests that the numbers of bank accounts have increased substantially since 2003 and beyond the 1999 level. While SACCO accounts have resurged since 2003, this is not to the level of 1999, and they certainly have not increased to the level the banks have. So that while they still have very strong roots in communities – politically as well as economically – and are still capturing some 25% of the customer base, it is likely that more dual use is also present. For Karatina, 55% of our survey respondents using a SACCO account were also using a bank account; and exactly half of those having a bank account also had a SACCO account. These figures dropped significantly for Nyamira: to 21% and 13% respectively. This also suggests that some of the bank account growth is potentially due to greater dual use.

There is fierce competition between banks and employee SACCOs in particular for salaried lending customers. What we call a “battle of the buy-offs” which is using lengthening loan terms and slightly lower rates to leverage salaries further. This was most rampant in Kitui in competition for the teachers market. This was a dynamic that some customers were exploiting with little co-operation between banks, but the arrival of the credit bureau is expected by bankers to improve performance.

However, the way in which this market is being approached by lenders is interesting for what it tells us about the demand for loans. Any institution where there are salary recipients is now a target. Banks have developed agreements with a wide range of employers to institute check-off schemes to enable them to undertake this lending, and once this is done it makes employees a marketing target for the banks. Given the ease of borrowing against these sources – and the fact that diversified incomes usually mean they are not the only source of income to an individual or household especially in more rural and small town settings where other enterprises can be easily operated – the “battle of the buy offs” enables a re-leveraging of an already committed salary rather than having to wait for the loan to be fully repaid before a new loan can be taken and represents ever increasing leverage over salaries. It is unclear where this trend will actually stop, but as loan terms increase to 4 years and above the banks become more vulnerable to the vagaries of employment churn.

Perhaps surprisingly given its vibrant micro-enterprise base, mainstream microfinance was doing least well in Karatina – compared to Nyamira and Kitui (although Kitui figures cover a much larger geographic area) despite being one of the areas to which it moved first and hence is well established. In some of our in-depth interviews we found that local experiences of default and repossession were cited in relation to MFI groups which – even if they had perhaps become apocryphal – appeared to be resulting in disinclination to engage with them. The maturity of the market means that early growth has been followed by a more cautious ongoing engagement.

Other microfinance – CARE’s GSLs and K-REP FSAs in Kitui are making important contributions to the market in terms of numbers of customers. This is particularly the case in Kitui where these services are rural biased and hence more accessible to clients. However these services did not register very strongly in our user survey data – which identified a only few CARE clients and no FSA clients.

ASCAs while having been vibrant in Karatina ten years ago now appear to be on the wane as far as ASCA management agents are concerned. For these too, problems with the model had arisen and in particular accounts of misappropriation had led to a decline. However there was also evidence that ASCAs were now regarded as a technology for it was not necessary to pay a facilitator.

Loan to deposit ratios are highest for MFIs who lend at multiples of savings and mobilise funds from outside their markets to do so. This is followed by employee SACCOs – with rates of over 90%. The cash-crop SACCOs find it harder to lend effectively but the differential performance between Karatina and Nyamira in this regard is notable – in part demonstrating the difficulties Nyamira SACCOs are having in lending effectively due to the liberalised tea market. Banks perform least well at circulating locally mobilised deposits into their local markets but the historical evidence shows that this has improved for Karatina compared to ten years ago. This is due to the reduced government deficit leading to banks having to lend rather than buy Treasury Bills as they were doing then.

On the basis of a comparison with our historical data, some interesting observations arise from the Karatina market. First, it is notable that the real value of deposits in the market as a whole appears to have fallen compared to ten years ago and this has occurred in the context of much higher numbers of accounts held. So, although more people are using services, they are holding smaller amounts. This may reflect a preference for “saving” funds in enterprises or investments rather than keeping them in banks given more vibrant economic conditions than ten years ago. The banks have retained their share of deposits, increased their share of account numbers, and roughly maintained their share of loans, but the ratio of loans to deposits has risen demonstrating the shift in banks towards lending has occurred in practice.

However across the three markets the loans to deposit ratio is lowest in Karatina compared to Nyamira and highest in Kitui. This is in part a result of the more buoyant deposit base in absolute terms in Karatina but given that environment it is surprising that it is not also easier to lend that base out. However, Karatina has a strong local investment dynamic which may explain the lower real value of deposits compared to ten years ago. Further, people there have a strong understanding of when resources are flowing outside the area. As a bank manager commented: “people have a culture of doing things together. . . there is the element of family. . . they shield themselves even business wise”.

They also have a history of setting up their own institutions to retain these resources locally. This was evident in the 1990s in the setting up of Mathira Tea and coffee SACCOs - to a degree in opposition to Nyeri based SACCOs. This is replicated by the sense that they no longer need to pay ASCA managers to run ASCAs for them. So that it may also translate into low levels of borrowing from banks and MFIs for similar reasons – because interest and fees leave the area - along with having found encounters with these institutions not entirely satisfactory.



