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Effect of Deposit Mobilization on Financial Perfomance of Deposit Taking Micro Finance Institutions in Nairobi Central Business District, Kenya

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***Abstract**:*
Microfinance Institutions borrow from the repo market at a rate that is even higher which pushes cost for MFIs. Consequently, the effect of deposit mobilization on financial performance of MFIs remains an empirical issue especially in the context of Kenya where there exists limited empirical evidence on the same. Financial performance of Deposit taking MFIs in Nairobi has not been steady, yet deposit mobilization initiatives have been on the rise. Hence, the purpose of the study was to determine the effect of mobilization of deposits on financial performance of Deposit Taking Micro Finance Institutions in Nairobi central business district, Kenya. The independent variables for this study were branch network, capital, regulations and social cultural factors. The study adopted positivism philosophy and descriptive research design. The target population was 9 deposit taking microfinance institutions. The targeted respondents were 45 branch managers and 45 financial officers. Data was analyzed using descriptive analysis and multiple regression analysis with the aid of SPSS. Data presentation was in form of tables and figures. Ethical considerations were observed during the study. The study found that the number of branches has a significant effect on financial performance of the MFIs studied. Capital has a major effect on deposit mobilization. The study found a positive and weak between regulations and financial performance of MFIs. The study concluded that the number of branches has little significant effect on financial performance. Number on branches has not done much to improve customer reach. There study findings document a relationship between the number of branches and the number of customer. Capital was found to have a significant effect on deposit mobilization. Value of equity greatly affects how MFIs performed. MFIs had made significant investments. Retained earnings had a significant effect on financial performance; Similarly, Regulations had significant effect on deposit mobilization and the same had an impact on long term financial performance of MFIs. Social-cultural factors had a significant effect on deposit mobilization. Level of education was the main social-cultural factor affecting deposit mobilization. Consequently, the study concludes that MFIS studied shows the number of branches has not done much to improve customer reach. The value of equity greatly affected how MFIs performed. Areas like internal control impacted on long term financial performance of microfinance institutions. Religion, level of education and gender had no significant effect on financial performance of microfinance institutions.

***Keywords:** Deposit mobilization, branch network, capital, regulation, social cultural factors, financial performance*

1. Introduction and Background

Microfinance institutions in Kenya have helped in filling the needed gap in the industry of financial services through providing small loans, or micro-loans, to a section of population which cannot access the conventional loans services. Within the society, financial service provides the means through which people and the businesses obtains the credit and manages the assets which are available on continuous platform (Habibullah, 2009). Accessing financial service enables operating businesses in growth and provides the start-up capital for the business. In addition, MFIs avail modern technology to the borrower in form of the credit card, ATM and the capabilities of mobile phone banking (Carpenter & Petersen, 2012). Despite the significance of MFIS to the Kenyan economy, the link between their deposit mobilization and financial performance remains unclear more so considering limited empirical literature in this area.

The regulation on Deposit-Taking MFI in Kenya is under the Microfinance act and the Microfinance (Deposit-Taking Microfinance Institutions) Regulations, 2008 prescribed there under (Prahalad, 2014). (Habibullah, 2009) The rationale for the stringent regulation of deposit-taking MFIs is to protect investor funds and ensure the stability of financial institutions in Kenya. Due to lack of regulation, non-deposit taking MFIs fail to offer guarantee of financial probity to its members and have thus remained unattractive to investors. Further, the limited regulation exposes these institutions to potentially huge losses. Due to the identified disabilities faced by non-deposit taking MFIs, there are discussions to bring these institutions under a comprehensive legal and regulatory framework. In the meantime, with the introduction of the Microfinance Act, several non-deposit taking MFIs (Jeanne & Svensson, 2007).

On 2nd May 2008 microfinance Act was established, during that time a good number of MFIs did apply for the license allowing them to take deposits from their members and the public in general (Nyanga, 2012). Microfinance Act aimed at regulating the establishments, businesses and MFIs operations in Kenya through the licenses and supervisions. In the report by the central bank of Kenya (2013), currently, there are 9 Deposit-taking microfinance institutions operating in the country with their branches in Nairobi. There has been a resurgence in nonperforming loans in deposit taking MFIs in the last five years which has resulted to increasing liquidity, this impacts negatively on the firm's investment decisions that has led to the firm poor financial performance (Olongo, 2013).

According to Carpenter and Petersen (2012) mobilization of deposits is one of the important functions of MFI business. This involves collecting savings from all sectors of the economy and having this cash banked in form of cash deposits, mpesa and electronic transfers. Nyanga (2012) opines that branch network play a major role in deposit mobilization. Mamun (2007) says that capitalization influences the MFIs ability to mobilize deposits. According to Akhtar (2007), government regulation greatly affects deposit mobilization among MFIs in Kenya. Habibullah (2009) argues that social-cultural factors like lifestyle, customs, and the values which characterize the society. The financial performance of MFIs is defined as the ability to covering its financial and operational costs.

2. Statement of the Problem

Financial performance of MFIs is largely explained by deposit mobilization which is owed much to liquidity management. The link between the two remains unresolved especially in the context of MFIs in Kenya. Liquidity analysis considers the MFIs ability to meet its obligations and is very critical for MFI to remain a going concern. The absence of liquidity can lead to failure of MFIs deposit mobilization. Higher liquidity gap can create liquidity risk to majority of MFIs in Kenya. Habibullah (2009) analyzed the relationship between capital and earnings for banks in US. The findings show there is a positive relationship between returns on equity and the capital. According to Obawale & Oladunjoye (2013), the impact of banks profitability depends on funding that fall due in short term. It holds that if banks really on short term funds the bank must hold more liquid assets to maximize banks' profits. A high liquidity level is considered to be a sign of financial stability and strength. Maaka (2013) studied the role of financial intermediation in the mobilization and allocation of household savings in Ethiopia and found that the performance of the formal financial system in mobilizing and promoting household saving in Ethiopia is very low. MFIs borrow from the repo market at a rate that is even higher which pushes cost for MFIs. Consequently, the effect of deposit mobilization on financial performance of MFIS remains an empirical issue especially in the context of Kenya where there exists limited empirical evidence on the same.

Maaka (2013) found that deposit taking microfinance institutions are involved in mobilization of deposits among customers. This study context was therefore unique to warrant further investigation. Mobilization of deposits is important for MFIs financial performance in Kenya. However, from the above studies, none has addressed on how MFIs can improve mobilization of deposits and MFIs financial performance. Many studies have focused on effect of mobilization of deposits on financial performance in general, but few have focused on deposit taking microfinance institutions, therefore finds the need at investigating the factors affecting mobilization of deposits and financial performance of deposit taking MFIs in Nairobi central business district, Kenya.

3. Specific Objectives

The study sought to achieve the following specific objectives:

- To establish the effect of branch network on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- To determine the effect of capital on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- To examine the effect of regulations on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- To assess the effect of social cultural factors on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- Hypotheses were formulated and tested (at a significance level of 0.05) for each of the respective objectives listed above.

4. Significance of the Study

The findings of this study are resourceful to MFIs in Kenya since they will understand the factors affecting mobilization of deposits and financial performance of deposit taking MFIs. This study will be important to the bodies governing and regulating the MFIs and management of financial institutions to be aware of mobilization of deposits and financial performance of MFIs. This area of study will add to the pool of knowledge on the researched area on factors affecting mobilization of deposits and financial performance of deposit taking MFIs in Nairobi, Kenya. Future researchers will have a reference point from the information gathered that will contribute to understanding the factors as well as contributing to subsequent studies.

5. Literature Review

The study reviewed key theories as well as empirical literature as documented hereunder.

5.1. Theoretical Review

The study was anchored on 3 theories which are highlighted here under. Bank-led theory offers distinct alternatives to the conventional branches-based banking in which customer conduct the financial transaction at the whole range of the retail agent instead of the branches of the bank or the employees of the bank. Financial services are ultimately provided by the bank and in an institution where the customers maintain the accounts (Carpenter & Petersen, 2012). The retail agents encounter face-to-face interactions with the customers and the cash-in/cash-out performances function much as the branch-based tellers take deposit and the processes withdrawal.

The economic theory of entrepreneurship is one of key theories supporting the study conceptualization. The theory holds that entrepreneurial behavior is influenced by economic factors. The theory sees an entrepreneur as the person who brings together the factors of production, that is, land, capital and labor, into a combination that makes their value better than before (Prahalad, 2014). According to Mamun (2007), an entrepreneur introduces new combinations in the form of new products, new production methods, new markets, and new sources of materials and other supplies. This ends up creating disequilibrium in the economy.

Liability Management Theory was initially pioneered by financial institutions during the 1970s as interest rates became increasingly volatile, liability management is the practice of managing risks that arise due to mismatches between the assets and liabilities. Mamun (2007) postulates that the theory of liability management focuses on banks matching their liabilities and assets to meet their liquidity needs. The liability and Liquidity management are very closely related. One of the aspects of the liquidity risk controls is the prudential level build-up of the liquid assets. The other aspect is the deposit taking MFIs management (Jeanne & Svensson, 2007).

5.2. Empirical Review

The study reviewed several key empirical literatures from the local context as well as foreign markets. Mwanik (2009) studied strategies for credit risk management, factors of the organization and MFIs performance in Kenya. Performance measurements were in term of the loan volumes, borrower's number, delinquent loan volume and non-performing loan ratio to the performing loans. The factors of the organizational are size, age and the MFI structure of management. Fielden et al., (2013) conducted a study on MFIs Ghana capital city Accra using the approaches of branch network and the strategies of deposit mobilization and the credit deliveries. In the relation to the objectives of marketing, strategy, mission statements and the approaches, it was found that sampled MFIs were not market-oriented in delivering the services.

The Christopher et al., (2010) studied factors that were critical for the success and defined minimum MFIs pre-conditions considering the commercial funding as the alternative sources of funding (Christopher et al., 2010). The Christopher et al., 2010) the findings show the extent to which organization formalization and the transparent financial reporting which are critical when drawing the commercial lenders for investing in the microfinance. The findings further indicated that investors looked for the larger, a regulated and a profitable MFI and low-risk profiles in the environment which has low levels of inflation for the investment portfolio. Bwisa et al., (2011) study in Ghana and Senegal found that the licensing process was the most difficult aspect of transformation for most institutions. A relatively long period of time (2-3 years) was taken to complete the licensing process as the regulations usually require MFIs to make internal improvements in areas like internal control, reporting capabilities, branch physical security, and finding an acceptable ownership and management structure.

Habibullah (2009) observed in his study of the role of financial intermediation in the mobilization and allocation of household savings in Ethiopia that the performance of the formal financial system in mobilizing and promoting household saving in Ethiopia is very low. However, he noted that the semi-formal and the informal market has proved to be much more successful in this regard and concluded that the semi-formal institutions and arrangements are very widespread and appreciated by the majority of the population and called for the formal financial institutions in the country to learn from the success of the informal sector. The study by Habibullah (2009 found that social cultural factors to have major influence among MFIs. The study recommended that MFIs should create awareness among the communities on the importance of MFIs.

Prahalad (2014) studied the challenges that women entrepreneurs face in accessing loans from Microfinance institutions'. The field research covered 20 women entrepreneurs from Nakuru town, as well as further in-depth interviews with 10 key informants composed of leaders and practitioners in the micro finance industry. The recommendations are the result of a research paper conducted by the researcher in process of undertaking an academic paper in master study. From this research it indicates that while each of the woman borrowers may face particular barriers from access to finance, there are also significant barriers to financing encountered by various women in business and intending to borrow. These barriers include, collateral requirements, business skills, cultural beliefs, and perception about women's borrowing all have significant effects on financing opportunity available to women. As such, while the focus of this project remains on investigating financing barriers faced by various women in accessing finance, for analytical purposes it was useful to contextualize these findings by situating them within the broader context of gender equality in relation to financing

6. Methodology

This section reviews key methodology issues adopted by the study. The research design adopted was a descriptive survey design. This ensures collections and descriptive analysis of data from the population of study. The target population was 9 deposit taking microfinance institutions. The targeted respondents were 45 branch managers and 45 financial officers. The target population was important since it provided the required information on determinants of financial performance of deposit taking MFIs in Kenya. Purposive sampling technique was used to obtain a representative sample of the population for the study. The study picked 45 branch managers and 45 financial officers to form the respondents. Hence, the total sample size was 90 respondents.

The data collected was first edited by ensuring that it is complete and correct which reduced biases, increases precision and achieves consistency. Data was analyzed using multiple regression analysis and descriptive analysis (percentages, means and standard deviations) with the aid of sciences (SPSS) software version 22.0. Data presentation was in the form of graphs, tables and charts. The normality tests were used to determine whether the data set was modeled well by the normal distributions and computing how it was likely for the random variables which underlays a data set in normal distribution. The multicollinearity was detected through the help of tolerance and its reciprocal, called the variance inflation factor (VIF).

7. Results and Findings

The section presents results and makes interpretations of the same besides a discussion.

7.1. Descriptive Analysis

The number of branches was found to have little influence on organization performance as evidenced by a lower mean of 1.83. The number of branches leads to customer reach as evidenced by a higher mean of 1.91. Number of branches was indicated to lead to increased number of customers as shown by a lower mean of M=1.8333, this shows there is a relationship between the number of branches and the number of customers. Microfinance institutions were indicated to spread across the geographical area as evidenced by a high mean of 2.2692. The organization has invested adequately as evidenced by a low mean of 1.3846. Retained earnings affect the performance of MFIs as evidenced by a higher mean of 1.897, this shows that retained earnings has significant influence on performance of MFIs. The value of equity affects the performance of MFIs as evidenced by a high mean of 3.1154.

Regulations usually require MFIs to make internal improvements in areas like internal control as shown by high mean of 3.4872. Supervisory framework requires MFIs to make internal improvements in areas like reporting capabilities as evidenced by high mean of 3.4872, this shows that supervisory framework leads to internal improvement which impacts on financial performance. Legal framework usually requires MFIs to make internal improvements in areas like management structure as shown by high mean of 3.4872, this shows that legal framework leads to internal improvement that impacts on MFIs overall performance.

Religion influence deposit mobilization as evidenced by a high mean of 2.9359, this shows that some religions greatly affected deposits mobilization which impacts on the overall MFIs performance. Challenges affecting women borrowers have never been critically highlighted and their impact on women SMES as evidenced by a high mean of 2.7436. Level of education influences deposit mobilization as shown by a high mean of 2.2569. MFIs experience has a positive moderating impact on the both dimensions of institutional distance/performance relationship as evidenced by a high mean of 4.3974. Ratio of non-performing loans to performing loans determines performance of MFIs as shown by a higher mean of 4.4744.

7.2. Inferential Analysis

The section presents results and findings on Pearson's Correlation Analysis and Multiple Regression Analysis. In view of correlation analysis, the study found a positive but weak relationship between branch network and financial performance (r = 0.079) hence branch network has some link with financial performance of the MFIs studied. The results on correlation analysis similarly document a positive and weak relationship between capital and financial performance (r = 0.041) hence capital has some link with financial performance. The results further indicate a positive and weak relationship between regulations and financial performance (r = 0.018) hence regulations have a relationship with financial performance of the MFIs. Lastly, results further indicate a negative relationship between social-cultural factors and financial performance (r = -1.9) hence a finding that social-cultural factors had a weak link with financial performance. The output of multiple regression analysis is summarized in terms of coefficient of determination, beta coefficients and p-values (to test hypothesis). First, the simple correlation (R-value) results of 0.221 indicate a positive but fairly weak relationship between branch network, capital, regulations and social-cultural factors collectively (Deposit mobilization) and financial performance of the MFIs studied. The coefficient of determination results R^2 indicates that explanatory power of the independent variables is 0.049. This means that 4.9% of changes in financial performance are explained by deposit mobilization (Branch network, Capital, regulations and Social-cultural factors). Hence, it appears that much of the financial performance of the MFIs is attributed to other factors other than deposit mobilization: this is largely contrary to empirical evidence elsewhere. In addition, Enova results indicate that deposit mobilization (branch network, capital, regulations and social-cultural factors) do not have collective significant effect on financial performance of MFIs (p = 0.457). This indicates that deposit mobilization is not a very good predictor of financial performance of the MFIs. Table 1 below presents output on relevant coefficients for multiple regression analysis.

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	4.619	.334		13.815	.000
	Branch Network	.016	.088	.022	.179	.859
	Capital	.023	.056	.048	.406	.686
	Regulations	-.017	.055	-.040	-.318	.751
	Social-Cultural Factors	-.082	.046	-.218	-1.780	.079

Table 1: Coefficients
a. Dependent Variable: Financial Performance

The study extracts the following regression function from results in Table 1 above.

$Y=4.619+0.016X_1+0.023X_2-0.017X_3-0.082X_4$

Where: X_1= branch network
X_2= capital
X_3= Regulation
X_4 = Social Cultural factors

The beta coefficients document the influence of each component of deposit mobilization on financial performance all other factors held constant. This model implies that every unit increase in branch network leads to a 0.016 unit increase in financial performance all other factors held constant; a unit increase in capital leads to a 0.023 increase in financial performance all other factors held constant. A unit increase in regulations leads to a -0.017 change in financial performance all else held constant. Lastly, a unit increase in socio-cultural factors leads to a-0.082 change in financial performance all else held constant.

7.3. Hypothesis Testing

The null hypotheses were tested using p-value methods at a significance level of 0.05 in order to either accepted or reject them. The null hypothesis is supported if P value is greater than the significant level of 0.05

- H01Branch network does not have a significant effect on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- The p-value of the test for this variable is 0.859. Since the p-value is greater than the significance level of 0.05, the null hypothesis is supported. Hence, the study finds that branch network does not have a significant effect on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- H02 Capital does not have a significant effect on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- The p-value of the statistic for the variable capital is 0.686. Since the p-value is greater than the significance level of 0.05, the null hypothesis is hereby supported. Hence, the study finds that capital does not have a significant effect on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- H03Regulations do not have a significant effect on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- The p-value of the variable regulations is 0.751. Since the p-value is greater than the significance level of 0.05, the null hypothesis is supported. Hence, the study finds that regulations do not have a significant effect on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- H04Social cultural aspects do not have a significant effect on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya.
- The p-value of the statistics for the variable regulations is 0.079. Since the p-value is greater than the significance level of 0.05, the null hypothesis is supported. Hence, the study finds that social cultural aspects do not have a significant effect on financial performance of deposit taking micro finance institutions in Nairobi central business district, Kenya. Consequently, it appears that deposit mobilization does not significantly explain financial performance of the MFIs studied. And this remains an issue for further empirical investigation.

8. Discussion

The study found number of branches to have little influence on organization performance. The number of branches has led to increased number of customers which agrees with Prahalad (2014) who cited the World Bank databases had underlined a presence of the multitude of the MFIs which, except the unstable countries, can be widespread, with unforgotten regions. Respondents were of the opinion that MFIs have invested adequately. The study findings agree with study by Christopher et al (2010) who argued that the extent to organization formalization and the transparent financial reporting which are critical when drawing the commercial lenders for investing in the microfinance.

The study found out that the regulations requires the MFIs to make internal improvements in areas like internal control which agrees with the study by Habibullah (2009) who compared other countries suggested that the licensing process was the most difficult aspect of transformation for most institutions. The study found that religion had little influence on deposit mobilization, this agrees with Kimari (2013) who argued that business skills, cultural beliefs, and perception about women's borrowing all have significant effects on financing opportunity available to women.

9. Conclusions and Recommendations

The study found out that the number of branches has significance on financial performance of the MFIS studied therefore number on branches has not done much to improve customer reach. The study found a positive and weak between regulations and financial performance of MFIs AS Value of equity greatly affected how per MFIs performed. The study found out that regulations usually require MFIs to make internal improvements in areas like internal control which impacted on long term financial performance of MFIs. There was a negative relationship between social-cultural factors and financial performance as religion, level of education and gender had no effect on performance of MFIs.

In view of the study findings, several recommendations are hereby made. The management of MFIs should increase the number of branches with the aim of reducing financial inclusion among the population. The management of MFIs should adopt technology to ensure efficiency in deposit mobilization. Government should regulate MFIs to ensure they are able to mobilize more deposits while helping the poor. Regulations should aim at supporting financial improvement among microfinance institutions. The government should license more MFIs to operate in order to ensure financial inclusion among the poor. The government regulations should ensure that the depositor's funds are protected. The management of MFIs should be able to mobilize deposits across social-cultural boundaries. The management of MFIs should develop products that cover all the social cultural backgrounds which should help in mobilization and improved financial performance.

10. Contribution to Knowledge

This study makes a major theoretical and empirical contribution in the literature of the effect of mobilization of deposits on financial performance of Deposit Taking Micro Finance Institutions in Nairobi Central Business District, Kenya. Prospect theory will help MFIs in decision making. The Prospect Theory, on the other hand, takes into consideration the alternatives that come with uncertain outcomes. The study will make contribution to finance theories on the effect of mobilization of deposits on financial performance of Deposit Taking Micro Finance Institutions in Nairobi Central Business District, Kenya. The study will contribute to Modern Portfolio Theory (MPT) on how rational investors should use diversification in order to optimize their portfolios. It also discusses how a risky asset should be price. The study findings provide an in-depth understanding to business managers, entrepreneurship consultants and the government on the effect of mobilization of deposits on financial performance of Deposit Taking Micro Finance Institutions.

11. Areas for further study

The study supported all null hypotheses indicating insignificant predictor variables. Hence, there should be further study on why deposit mobilization does not seem to explain financial performance, yet it is the core of micro financing business. Kenya has seen the emergence of religious financial institutions, the current study has not conclusively shown how social economic factors like religion has affected deposit mobilization of MFIs, further study is recommended to identify more on how religion influence deposit mobilization of MFIs. The study recorded a low coefficient of determination- this means that there are other factors which are key in explaining financial performance other than deposit mobilization. Such factors could be investigated by other scholars.

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