THE EFFECT OF CHANGE IN BASE LENDING RATE ON GROWTH OF MICROFINANCE BANKS IN KENYA

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ABSTRACT

The main aim of the study was to investigate the effect of change in base lending rate by CBK on the growth of microfinance banks in Kenya. The study is guided by market segmentation theory, classical theory and loanable funds theory. The study adapted the descriptive research design. The target population of this study comprised of 9 microfinance banks regulated by CBK and registered by AMFIs as at 31st December 2014. Out of the 12 registered microfinance banks by June 2015 by CBK only 9 were registered by 31st December 2014. Kenya's microfinance sector comprises of nearly 250 MFIs, with only 62 of these being registered with their umbrella body, Association of Microfinance institutions (AMI). The study used secondary data obtained from the following sources; Data on credit lending rate trends for the last five years from CBK. The study used Statistical package for Social Sciences-SPSS version 22, to aid in data analysis. Descriptive statistics, Pearson's correlation analysis and ordinary least squares regression model was used in the study. The study revealed that a weak positive correlation coefficient between growth of microfinance banks and increase base lending rate, as shown by correlation factor of 0.221. Further the research established that interest rate affects the profit as well as the net worth of MFIs.The research found strong positive correlation between growth of microfinance banks and credit terms as shown by correlation coefficient of 0.825. The study revealed that management decisions about credit methodology, credit terms and markets in which to operate directly affect efficiency and productivity. In relation to growth of microfinance banks in Kenya the study revealed, increased competition is an issue that creates a problem in growth and expansion of the organization. Based on the research findings the study recommends that microfinance can bring their interest rates down by continuing to increase the operational efficiency, increasing innovations in the products offered and the technology

used to service and offer loans to the poor. The CBK also have a vital role to play in getting interest rates lower, not by imposing rate ceilings which are more harmful than beneficial, but rather through setting the right environment and providing the infrastructure (human, physical and institutional) necessary to nurture increased competition.

Key words: interest rates, microfinance banks, base lending, growth

1.0 Introduction

World Bank defines base lending rate as minimum interest rate on which financial institutions base the rates they use for lending. It is credit facility in which financial institutions go to borrow funds from the Federal Reserve. In Kenya base lending rate has constantly been fluctuating time to time. Questions have been raised on the impact it have on financial sector. According to World Bank base lending rate is a minimum interest rate on which financial institutions base the rates they use for lending. These loans, which are priced at the discount rate, are often structured as secured loans to alleviate pressure in reserve markets. It helps to reduce liquidity problems for banks and assists in assuring the basic stability of financial markets.

In Kenya base lending rate is controlled by central bank of Kenya (CBK) through monetary policy committee. Kisala (2014), states that no interest rate should exceed four percent of the base lending rate of the central bank. This implies that commercial banks do not have full control of the interest rate they charge their borrowers. Central bank rate is therefore very crucial in loan absorption in Kenya. The possible causes of increase in discount rate are inflation, depreciation of local currency and to attract foreign cash inflows.

According to Kisala (2014), Microfinance is a general term to describe financial services to low income individuals or to those who do not have access to typical banking services. Microfinance is also the idea that low-income individuals are capable of lifting themselves out of poverty if given access to financial services. Microfinance is the supply of loans, savings, and other basic financial services to the poor. As these financial services usually involve small amounts of money - small loans, small savings, the term "microfinance" helps to differentiate these services from those which formal banks provide. Poor people save all the time, although mostly in informal ways.

When base lending rates increase commercial banks increases their interest rates on loans and mortgages. This therefore discourages many people from seeking credit facility to finance long term and short term projects leading to slowed economic growth. Increase in central bank rate leads to higher cost of borrowing (Kagwe, 2008). This is because commercial banks and other depository and lending institution transfer the cost to the borrower. The effect of increased base lending rate is therefore easy to tell the direction of lending for the case of commercial banks. However, the case may not be the same for microfinance since most of them are not controlled by CBK and many small and medium sized borrowers may opt to turn to MFIs due to better credit terms.

Research Problem

The success of MFIs largely depend on the effectiveness of their credit management systems because these institutions generate most of their income from interest earned on loans extended to small and medium entrepreneurs. Kagwe (2008), concluded by stating that because of the ability of microfinance to reach and serve clients more effectively, MFIs that meet their own costs and raise their own sufficient capital are best suited to attract and serve the large financially excluded adult population in Kenya. Interest rates determine the profitability of Commercial Banks among other factors. High interest rates have remained a macroeconomic problem that has been difficult to eliminate. According to Economic observers high interest rates are regressive to the economic development of the country. Attempt to charge higher interest rate negatively affects the quality of a bank's loan because of incentive and adverse selection effects. There is rise in the overall riskiness of the portfolio of assets. Rising interest rates reduces the returns on all projects and makes less risky projects unprofitable. Firms react by switching to more risky projects as interest rates rise. Secondly, MFIs like banks have to screen borrowers (Bichanga & Njage, 2014). This is because at a high borrowing interest rate, borrowers may be less worried about the prospect of nonpayment (adverse selection effect). This implies that the rational profit maximizing MFIs will practice credit rationing which defeats the assumption generally made in financial liberalization literature, that of interest rate liberalization eliminating credit rationing.

Mang'eli (2012), in his research study points out that interest rate spread affect the performance of commercial banks, as it increase the cost of loans charged on the borrowers, regulations on interest rates have far reaching effects on performance of financial institutions since they determine the interest rate spread in banks and also help mitigate moral hazards incidental to performance of commercial banks, credit risk management technique remotely affects the value of a bank's interest rate spread as Interest rates are benchmarked against the associated non-performing loans (NPLs) and NPLs is attributable to high cost of loans. Despite MFIs having a leeway of charging high lending interest rates which makes them record impressive financial performance some banks are actually reporting losses or very small margins despite the fact that they are being controlled by the same regulatory body CBK.

Credit lending and effective management of credit is key to the growth of MFIs. Successful MFIs have managed to maintain high levels of lending and loan recovery rates, generally over 95%. Many borrowers results to increased revenue through the payment of interest charged on money borrowed. These trigger a wave of funds from funding agencies and the subsequent inflow from a variety of social investors which they could use to expand their operations. While many MFIs continue to enjoy growth due to slow expansion of formal sectors ,interest rates charged by formal sector will be also be vital to their growth since it may encourage or discourage small and medium investors

who may turn to or away from MFIs for credit. Does change in base lending rate have any effect in the growth of microfinance banks in Kenya?

Objective of the study

To investigate the effect of change in base lending rate by CBK on the growth of microfinance banks in Kenya.

2.0 Theoretical Perspective

Market segmentation theory asserts that, long term and short term security markets are independent and there is no causal relationship. Supply and demand forces in different maturity segments of market determine rate for that particular segment. The theory assumes that investors have strict maturity preferences. In this case pension funds with long term liabilities would invest in similar bonds while banks would operate in a shorter horizon. This implies existence of "separated" market segments each having interest rate determined by its own supply-demand interaction.

According to Chikalipah, (2012), the classical theory of interest rates applies the classical theory of economics to determining interest rates. It defines the interest rate as the element that equates savings to investment. It compares the supply of savings with the demand for borrowing. The equilibrium rate is calculated by determining the curves intersection point of supply and demand curve. Thus if savings are greater than investments the interest rate drops until they reach equilibrium and vice versa, if savings are less than investment the interest rate increases until the reward for savings encourages increased savings rates causing the market to again reach equilibrium.

Lasher (2008), argues that interest rate is the price paid for the use of capital and that it is determined by the intersection of aggregate demand and supply of capital. Interest rates definitely influence the marginal propensity to save. He concludes that the rate of interest should be at a point where the demand curve for capital at different rates intersects the savings curve at a fixed income level. The study seeks to identify the rationale classical theory of interest rate on the growth of microfinance banks in relation to credit lending. However the classical theory of interest rates fails to account for factors besides supply and demand that may affect interest rates such as the creation of funds, the importance of income and wealth and changes in the primary borrowers in an economy.

Loanable funds theory holds that interest rates are determined by supply of loanable funds and demand for credit and that there exists an inverse relationship between the loanable funds and the interest rates. If both the demand and Supply of loanable funds change, the resultant rate would depend on the magnitude of movement of the demand and supply of the loanable funds. In this theory the demand of loanable funds originates from domestic business, consumers, governments and foreign borrowers.

According to Gorder (2009), the supply is generated by domestic savings, dispersion of money balances money creation in the banking system and foreign lending. With these factors determining long-term interest rates, short term interest rates are decided by financial and monetary conditions in the economy. The study seeks to identify the rationale of the liquidity preference theory on the relationship between the money supply in form of loans by MFIs in times of rising and or falling lending rate, and the growth of the lender. The borrowers will only invest where the returns on their investment profile exceed the borrowing rates, when it is short of this the borrower may abandon the investment or source for interest free fund such as family borrowing.

3.0 Research Methodology

The study adapted the descriptive research design. A descriptive study is one in which information is collected without changing the environment (nothing is manipulated). Descriptive studies are conducted to demonstrate associations or relationships between naturally occurring variables in the world. Descriptive studies are usually the best methods for collecting information that demonstrate relationships and describe the situation as it exists (Cooper and Schindler, 2006). Descriptive study is used to describe characteristics of a population or phenomenon being studied. It does not answer questions about how/ when/why the characteristics occurred. Rather it addresses the "What" question hence descriptive research was found to be in tandem with the research question which sought to answer the question. What is the effect of increase in credit lending interest rates on the growth of MFIs in Kenya?

The target population of this study comprised of 9 microfinance banks regulated by CBK and registered by AMFIs as at 31st December 2014. Out of the 12 registered microfinance banks by June 2015 by CBK only 9 were registered by 31st December 2014. Kenya's microfinance sector comprises of nearly 250 MFIs, with only 62 of these being registered with their umbrella body, Association of Microfinance institutions (AMI). The remaining institutions are unregulated by the Central Bank and offer microfinance services in combination with other services (Microfinance (amendment Act), 2013).

The study used of secondary data obtained from the following sources; Data on credit lending rate trends for the last five years from CBK. Annual financial statements and banking supervision reports on the microfinance banks under consideration was obtained from the CBK. Secondary data on the total asset held by depository financial institution was obtained from CBK. Data on monthly financial statements were obtained from individual microfinance banks under study. Finally the study also used secondary data from the Association of Microfinance Institutions in Kenya (AMFIs) on the growth and performance of the registered MFIs. The study adopted a period of five years from 2010-2014.

Data Analysis

The study used multivariate regression model to determine the relationship between the dependent and the independent variables. The study used Statistical package for Social Sciences-SPSS version 22, to aid in data analysis. Descriptive statistics, Pearson's correlation analysis and ordinary least squares regression model was used in the study. Ordinary least squares regression model suit this study as it is depicted to be a valid method where stable relationships are shown across a given variable over several periods. This method was successfully applied by Haron (2012), in his study on the impact of macroeconomic variables on the profitability of listed commercial banks in Pakistan.

A multivariate regression model was used in this study; $Yt = \alpha + \beta 1X1 + \beta 2X2 + \beta 3X3 + \varepsilon$

Yt = Growth of microfinance banks in period t

X1 = Increase base lending rate

X2 = Credit terms

X3 = Management Efficiency

βi = Co-efficient of variable i that measures the responsiveness of a unit change in Y for a unit change in i

ε = Error term

Where;

Yt = Growth of microfinance banks in period t as measured by asset base; the percentage change of the total asset held by microfinance in period t.

α = the regression constant

X1 = Increase in base lending rate as measured by the difference between the minimum monetary policy rate held by CBK from the percentage increase from time to time as provided by CBK.

X2 = Credit terms as measured by credit period and interest rate

X3 = Management Efficiency as measured by Non-interest expense to total assets

The Pearson product moment coefficient (R) was used to establish the association between the variables (growth of microfinance institutions and base lending rates) based

on the population data. A co efficient of determination (R2) was performed to determine how much of the dependent variable comes about as a result of the independent variable being tested. Analysis of variance (ANOVA) was done to test the significance of the findings.

4.0 Study Findings

This section presents analysis and findings of the research. The objective of this study was to establish the effect of change in base lending rate by CBK on the growth of microfinance banks in Kenya.

Increase in Base Lending

Table 4.1: Descriptive statistics on Base Lending

Year	Base Lending rate as issued by CBK
2010	0.49%
2011	0.50%
2012	2.50%
2013	0.50%
2014	0.45%

From the findings, it can be noted that the year 2012 recorded the highest value for change in CBK lending rates shown by of value of 2.50 while the year 2014 recorded the lowest value for change in CBK lending rates as shown by 0.45%. The findings revealed that change in CBK lending rates remain below 1% of most of the years.

Credit Terms

Table 4.2: Descriptive statistics on Credit Terms

Year	Median	Minimum	Maximum	Mean	Std deviation
2010	13.25	13.16	13.76	13.50	0.25
2011	12.14	11.93	12.15	12.12	1.13
2012	10.15	10.26	10.03	10.20	1.24
2013	10.09	9.85	10.11	10.13	0.13
2014	9.06	9.01	9.13	9.07	0.01

From the findings, it can be noted that the year 2010 recorded the highest value for interest rate as shown by a mean of value of 9.07 while the year 2014 recorded the lowest value for interest rate at 9.07. In addition, values for stardard deviation depicts variability

in interest rate during the five –year period with the highest deviation of 1.24 in the year 2012 and the lowest 0.01 in the year 2014. The findings revealed that there have been a significant decrease in interest rate during the five-year period.

Management Efficiency

Table 4.3: Descriptive statistics on Management Efficiency

Year	Median	Minimum	Maximum	Mean	Std deviation
2010	43.32	23.19	44.36	44.5	1.23
2011	34.34	33.94	35.87	34.52	1.33
2012	27. 46	24.57	26.56	26. 49	1.09
2013	24.45	22.33	25.32	24.43	1.01
2014	19.12	19.19	22.45	21.38	1.12

From the findings, it can be noted that the year 2010 recorded the highest value for non-interest expense to total assets as shown by a mean of value of 44.56 while the year 2014 recorded the lowest value for non-interest expense to total assets at 21.38 in addition, values for stardard deviation depicts variability in non-interest expense to total assets during the five –year period with the highest deviation of 1.33 in the year 2011 and the lowest 1.01 in the year 2013. the findings revealed that there have been a significant decrease in non-interest expense to total assets during the five-year period.

Growth of Microfinance Banks

Table 4.4: Descriptive statistics on Growth of Microfinance Banks

Year	Median	Minimum	Maximum	Mean	Std deviation
2010	63.71	60.24	65.07	63.81	1.12
2011	70.21	54.21	76.23	71.13	1.28
2012	83.43	78.51	86.56	85.10	2.96
2013	86.21	80.02	88.34	87.33	1.01
2014	92.22	82.15	95.92	95.36	3.16

From the findings, it can be noted that the year 2010 recorded the lowest value for growth of microfinance banks at as shown by a mean value of 63.81 while the year 2014 recorded the highest value for growth of microfinance banks at 95.36. in addition, values for stardard deviation depicts variability in growth of microfinance banks during the five –year period with the highest deviation of 3.16 in the year 2014 and the lowest at 1.01 in the year 2013. the findings revealed that there have been a significant increase in growth of microfinance banks during the five-year period.

Correlations

Table 4.5: Correlations

		Growth of microfinance banks.	Increase Base lending Rate	Credit Terms	Management Efficiency
Growth of microfinance banks	Pearson Correlation	1	.221*	.825**	.532**
	Sig. (2-tailed)		.001	.0001	.003
	N	9	9	9	9
Increase Base lending Rate	Pearson Correlation	.221**	1	.340**	.310*
	Sig. (2-tailed)	.001		.003	.028
	N	9	9	9	9
Credit Terms	Pearson Correlation	.825**	.340**	1	.389**
	Sig. (2-tailed)	.003	.011		.007
	N	9	9	9	9
Management Efficiency	Pearson Correlation	.532**	.310*	.389**	1
	Sig. (2-tailed)	.002	.028	.007	
	N	9	9	9	9

On the correlation of the study variable, the researcher conducted a Pearson moment correlation. from the finding in the table above, the study found that there was weak positive correlation coefficient between growth of microfinance banks and increase base lending rate, as shown by correlation factor of 0.221 this strong relationship was found to be statistically significant as the significant value was 0.001 which is less than 0.05, the study found strong positive correlation between growth of microfinance banks and credit terms as shown by correlation coefficient of 0.825, the significant value was 0.003 which is less than 0.05, the study found strong positive correlation between growth of microfinance banks and management efficiency and development as shown by correlation coefficient of 0.523. This strong relationship was found to be statistically significant as the significant value was 0.002 which is less than 0.05

Regression analysis

In this study, a multiple regression analysis was conducted to test the influence among predictor variables. The research used statistical package for social sciences (SPSS V 21.0) to code, enter and compute the measurements of the multiple regressions.

Model Summary

The model summary are presented in the table below

Table 4.6: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.868 [a]	.753	.671	.36241

The study used coefficient of determination to evaluate the model fit. The adjusted $R^{2,}$ also called the coefficient of multiple determinations, is the percent of the variance in the dependent explained uniquely or jointly by the independent variables. The model had an average adjusted coefficient of determination (R^2) of 0.671 and which implied that 67.1% of the variations in Growth of microfinance banks are explained by the independent variables understudy (increase base lending rate, credit terms, and management efficiency).

Analysis of Variance

The study further tested the significance of the model by use of ANOVA technique. The findings are tabulated in table below.

Table 4.7: Summary of One-Way ANOVA Results.

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	17.919	3	5.973	5.324	.001[b]
	Residual	5.61	5	1.122		
	Total	23.529	8			

Critical value = 3.86

From the ANOVA statics, the study established the regression model had a significance level of 0.1% which is an indication that the data was ideal for making a conclusion on the population parameters as the value of significance (p-value) was less than 5%. The calculated value was greater than the critical value (5.324 > 3.86) an indication that increase base lending rate, credit terms, and management efficiency all have a significant effects on growth of microfinance banks. The significance value was less than 0.05 indicating that the model was significant.

Coefficients

In addition, the study used the coefficient table to determine the study model. The findings are presented in the table below.

Table 4.8: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.226	.237		5.173	.000
	Increase Base Lending Rate	.423	.096	.397	4.406	.020
	Credit Terms	.513	.111	.497	4.622	.011
	Management Efficiency	.447	.103	.423	4.340	.003

As per the SPSS generated output as presented in table above, the equation

($\mathbf{Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3}$) becomes:

$$\mathbf{Y = 1.226 + (0.423 X_1) + 0.513 X_2 + 0.447 X_3}$$

From the regression model obtained above, a unit change in increase base lending rate while holding the other factors constant would lead to an increase in growth of microfinance banks by a factor of 0.423, a unit increase in credit terms while holding the other factors constant would lead to an increase in growth of microfinance banks by a factor of 0.513, a unit change in management efficiency while holding the other factors constant would lead to an increase in growth of microfinance banks by a factor of 0.447.

This implied that management efficiency had the highest influence on growth of microfinance banks (p - value .003) followed by credit terms (p - value .011) and increase base lending rate (p - value .020). it was an implication that, increase base lending rate credit terms, and management efficiency enhanced growth of microfinance banks and vice versa.

The analysis was undertaken at 5% significance level. The criteria for comparing whether the predictor variables were significant in the model was through comparing the obtained probability value and $\alpha = 0.05$. If the probability value was less than α, then the predictor variable was significant otherwise it wasn't. All the predictor variables were significant in the model as their probability values were less than $\alpha = 0.05$

Discussion of the findings

The study revealed that a weak positive correlation coefficient between growth of microfinance banks and increase base lending rate, as shown by correlation factor of 0.221, The research revealed that increase in base lending severely limit the sustainability (profitability) and the outreach of MFIs, rendering them unable to reach more poor persons, an interest rate set too low constrains the ability of the MFI to operate efficiently, low rates prevent MFIs from covering the costs of their operations and so they are unable to meet their financial obligations, failing in this area makes it impossible for MFIs to expand their operations and reach new clients. The findings concurs with Hudon (2010), explains, using a religious, Marxists or Keynesian lens, high interest rates are revealed as either intrinsically unjust or potentially harmful.

Further the research established that interest rate affects the profit as well as the net worth of MFIs, because net interest income is a major part of MFIs' profit, increase in the interest rate depresses the borrowers and depositors, like investment and saving. MFIs by charging high interest rate gain high returns from borrowers and discouraging the depositors by giving low return to them which results in inclusive spreads, further the findings concurs the findings by Ngumi (2014), who found out that a strong relationship exists between lending interest rates and financial performance of DTMs.

The research found strong positive correlation between growth of microfinance banks and credit terms as shown by correlation coefficient of 0.825, The study also revealed that local market competition among MFIs in Kenya is driven by credit terms especially in terms of loan amounts, interest rates and repayment time and that some borrowers and MFIs opt for a package of low interest rates tied with low amount of loan disbursed and some other borrowers and MFIs settle for a package of high interest rates tied with high amount of loan disbursed. The study revealed that Most MFI loans are of short duration, normally between 12-18 months, a connection between the maturity and the ability of the poor to pay back such high are that the high interest rate loans are used for short term consumption and not long term investments to get out of poverty.

The study revealed that management decisions about credit methodology, credit terms and markets in which to operate directly affect efficiency and productivity, well performing MFIs are able to attract even more investors which then promote growth and more outreach of these institutions, commercial investment is an integral part for the long term existence of microfinance, productivity assist the institution to have a competitive edge in the industry, the findings supports Chikalipah (2012), argument that personnel, administrative expenses, and client base are basic variables in this area, in efficient management prevent MFIs from covering the costs of their operations and so they are unable to meet their financial obligations. Failing in this area makes it impossible for MFIs to expand their operations and reach new clients.

To increase efficiency, technology use and management quality need to be considered, further, because the effect of efficiency on lending rates increases with the initial size of

MFIs, governments need to consider the possibility of fostering mergers and acquisitions in this sector, given the lending technology that most MFIs use, how much public policy could help increase efficiency will depend on how difficult is for loan officers to reach their target clients.

Relating to of growth of microfinance banks in Kenya the study revealed, Increased competition is an issue that creates a problem in growth and expansion of the organization, Legislation and regulatory frameworks creates a problem in growth and expansion of the organization that most of the MFIs in Kenya lack capacity to leverage funds which is a key pillar in growth, the findings supports Haron (2012), argument that MFBs in many developing countries do not have access to sufficient subsidized funds and are unable to invest in expensive ICTs. This is the major reason that MFIs in developing countries have not attained considerable development sustainability. There are number of Microfinance banks and Institutions which leads to increased competition. Increased competition from commercial banks was found threat to the survival of the business of MFIs Nowadays, awareness among clients has increased and as a result they demand more financial services from MFI's and MFIs. Many donors are reluctant to provide funds to MFIs, as the requisite financial support is not provided to MFIs so as a result the lack of access to funding creates a problem in growth and expansion of MFIs s, Government or concerned authority should establish fund raising unit in order to support MFIs. The Policy makers have not design strict rules and regulations of contract execution.

5.0 Conclusion and Recommendations

The study revealed a weak positive correlation between growth of microfinance banks and increase base lending rate, (correlation factor 0.221) further the established that when base lending rates increase financial institutions increases their interest rates on loans and mortgages, This therefore discourages many people from seeking credit facility to finance long term and short term projects leading to slower economic growth, therefore the study concludes that increased in base lending rates had negative impact on growth of microfinance banks in Kenya.

The research established that a correlation between growth of microfinance banks and (correlation factor 0.825) further it was revealed local market competition among MFIs in Kenya credit terms is driven by credit terms especially in terms of loan amounts, interest rates and repayment time and that some borrowers and MFIs opt for a package of low interest rates tied with low amount of loan disbursed. Therefore the study concludes that favorable credit terms had a positive impact on growth of microfinance banks in Kenya.

The stud reveled that management decisions about credit methodology, credit terms and markets in which to operate directly affect efficiency and productivity of MFIs, and that Well performing MFIs are able to attract even more investors which then promote growth

and more outreach of these institutions, the study also found a strong positive correlation between growth of microfinance banks and management efficiency and development (correlation coefficient of 0.523) therefore the study concludes that ensuring efficiency in management could les to a positive impact on growth of microfinance banks in Kenya.

Based on the research findings the study recommends that microfinance can bring their interest rates down by continuing to increase the operational efficiency, increasing innovations in the products offered and the technology used to service and offer loans to the poor.

The CBK also have a vital role to play in getting interest rates lower, not by imposing rate ceilings which are more harmful than beneficial, but rather through setting the right environment and providing the infrastructure (human, physical and institutional) necessary to nurture increased competition.

On lending terms, the management of MFIs need to formulate lending and repayment terms which are more favorable to the poor given that the target market for MFIs is mostly on poor in the community. These policies should most feature on collateral repayment terms and monitoring.

The management of MFIs needs to institute quality management practices in order to ensure efficiency in operation as this factor was found to be positively related to growth of microfinance banks in Kenya.

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