

# ALTERNATIVE SMALL BUSINESS FINANCING OPTIONS TO MICRO-FINANCE LOANS IN KENYA

ROSE SAU LUGANO, FARAH CHARLES & HEEJIN AHN

In summer 2014 I was awarded an RTA grant that facilitated research in Kenya, with two University of Florida undergraduate students, Farah Charles and Heejin Ahn. We examined the alternative financing options utilized by self-employed women who are unable to access microfinance loans to establish business. What prompted this research was the widespread small scale businesses run by women in response to acute rising rate of unemployment. Self-employment plays an important role in Kenyan economy and has the potential for contributing to women's economic, social, political empowerment, and specifically in reducing poverty. We collected the data through surveys, in-depth interviews with individual women, and observed women's self-help groups called *chama* - rotating saving & credit associations (ROSCAs) - in two primary locations, Mombasa and Nairobi. Both rural and urban women belong to *chama*, where they contribute money monthly and lend to each other.

Women entrepreneurs' contribution to the economy of Kenya is immense, yet they cannot secure formal bank loans due to lack of collateral. In response to these challenges, many microfinance institutions have evolved from NGOs to provide historically disadvantaged women with access to financial services, such as the Kenya Women Finance Trust (KWFT), Kenya Rural Enterprise Program (K-REP), Women Economic Empowerment Consort (WEEC) and Kenya Equity Bank.

Despite this development, the current research indicate that informal forms of lending such as ROSCAs (or "merry-go-rounds") are the main source of small loans for women entrepreneurs. All the women interviewed borrowed from their group while only 4% of them also subscribed to KWFT.

The study found that the choice to borrow from formal institutions highly

depended on the socioeconomic status of the applicant and that poor women were often restricted from joining KWFT due to failure to meet collateral requirements. Furthermore, KWFT's strict penalty system for defaulters which involves confiscation of physical assets hinders women from joining. In informal lending, there is a degree of flexibility; the rules governing repayment are negotiable when borrowers encounter extenuating circumstances, such as death in the family. Thus, frequently an "emergency fund" is established to assist members at no cost.

Another deterrent to joining a formal institution is the high interest rate (20-30%) compared to informal saving groups (5-10%). The women informed us that it was advantageous to borrow from their informal groups because the interest they pay stays within their group and adds to the collective "pot" whereas formal institutions keep the interest to pay for operation costs. Although informal associations seem to be efficient in serving women entrepreneurs' needs, interviewees pointed out two major challenges; often times the informal associations do not provide them with adequate capital to expand their businesses. Also, when a default case occurs, the "informal" nature of these groups makes it challenging

for the group to successfully battle it out in court, because they are often related or friends with each other.

The ROSCAs are highly valued by small business owners due to their informal nature and their rootedness in the traditional mutual guarantee system. There are thousands of ROSCAs in Kenya, serving as the predominant source of credit for women, with many having experienced positive impact on their businesses and family life. There is a need for the formal and government financial institutions to work with the informal financial groups to strengthen them through the provision of technical and financial support in order to meet women entrepreneurs needs and enable them reach their highest production in business. Overall, the study findings indicate that ROSCAs have great potential in improving the standard of living of many people in Kenya and reducing poverty.

Rose Sau Lugano is senior lecturer in the Department of Languages, Literatures and Cultures (LLC). Farah Charles and Heejin Ahn both completed undergraduate minors in African Studies. This research was funded by the Center for International Business Education (CIBER), the Center for African Studies, and the UF Office of Research.

