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Factors Affecting Revenue Growth of Savings and Credit Cooperative Organizations in Kenya

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Abstract

Savings and Credit Cooperative Organizations (SACCOs) fulfill an indispensable role in providing financial services to their members, especially those who have restricted access to conventional banking facilities. In order to ensure the long-term viability and efficient delivery of services, it is imperative to comprehend the factors that determine revenue growth in SACCOs. This study aims to investigate the effect of loan default, operating costs, and membership size on the growth of revenue within the unique context of SACCOs. Through a meticulous examination of the existing literature, it becomes evident that loan default poses a significant challenge to SACCOs, resulting in substantial financial losses that have a direct impact on the wealth of the members. Furthermore, operating costs emerge as another critical concern, as they can impede profitability when SACCOs turn to expensive short-term borrowing from banks due to limited capital availability. Moreover, the size of the membership base plays a substantial role in influencing revenue growth. A larger membership base offers the potential for increased revenue generation through registration fees and additional savings, thereby enhancing the overall financial performance of the SACCO. The findings underscore the need for tailored strategies informed by the specific context, regulatory environment, and member requirements.

Keywords: Loan default, Membership size, Operating costs, Revenue growth, SACCOs

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1. Introduction

According to Auka and Mwangi (2013), Savings and Credit Cooperative Societies (SACCOS) are financial institutions in the line of cooperative societies that aim to meet the common needs of members through the mobilization of savings, loans, and financial advisory services. They enhance economic growth and development by providing funds to members through loans so as to enable them to engage in viable business ventures.

SACCOS offers services that are mostly similar to those offered by commercial banks and microfinance institutions. Hence, in this sense, they are suitable for low-income households that find it difficult to get access to credit facilities from commercial banks. According to Collins and Clark (2003), delivering financial services to members is the key function of Sacco, and these include financial products and advisory services. To do this adequately, they have to provide the services effectively.

Sales growth over time is represented by revenue growth. It is employed to gauge how quickly a company is growing. Revenue growth is more significant than a quick look at revenue, as it aids investors in seeing patterns that may be used to estimate revenue growth over time. According to [Albrecht et al. \(2023\)](#), revenue growth is the percentage increase (or decrease) in a company's revenue between two or more equal fiscal quarters. The phrase "revenue growth" describes the rate of business growth for a company. The graph shows the annual rate of growth or decline in a company's revenue or sales. The figures can be used by analysts, investors, and players to determine how rapidly a company's sales are increasing over time. Although revenue growth varies from quarter to quarter from fiscal year to fiscal year, investors look for revenue growth trends to gauge the company's growth over specific time periods.

A company that can continually increase revenue should have equivalent increases in net income, all other things being equal. By taking the derivative of revenue growth, you can determine the rate of revenue growth and how much it is changing over time. Investors use this statistic to forecast future changes in the rate of profit growth. It is an indication that something is wrong if a business that has been able to build its revenues steadily starts to experience slower revenue growth. According to [Hult et al. \(2008\)](#), organizational researchers frequently use accounting-based metrics of profitability or stock market-based indicators, such as Tobin's Q, to analyze the financial aspect of a firm's success.

When non-cash assets, such as commodity inventory, are transformed into cash or cash equivalents, like receivables, revenue is realized. It also signifies that the company registers revenue based on the principle of revenue realization (revenue registration time or revenue realization recognition) and that all processes required to earn revenue from the sale of a good or service have been completed ([Ball et al., 2016](#)). It is not necessary for the company to collect the price of the commodity or value sold until it is proven as a sale or revenue, and sales and services are recognized as revenue at the time of the transaction because the incidence of sales or service delivery constitutes the objective evidence needed to complete the procedure, as well as the potential of collecting the price of the goods or service provided ([Al-Qashi and Al-Oqlah, 2015](#)). Regardless of when the relevant cash is collected, the cost of the goods or services delivered to consumers is reported as income for the activity in the period of sale and delivery ([Ball et al., 2016](#)).

Every business seeks to maximize profit, and the factors that affect profit are similarly instructive and beneficial for evaluating income. As a result, the profitability rate is determined by the average length of time for collections, payments, and inventory. By dividing sales or revenue by total assets, one can determine operational efficiency and profitability ([Sari, 2007](#)). Profitability is determined as a dependent variable using return on sales, return on

investments, and return on sales. For businesses to generate the cash flow needed to meet immediate obligations and make capital investments, sales revenue is crucial.

Due to their significant economic contribution to the lives of their members, the number of cooperative societies in Kenya has increased exponentially and is evenly distributed across both urban and rural areas. It is evident that Saccos are more society-oriented than purely profit-motivated. In order to accomplish their goal, Saccos must deal with a number of challenges, which include the need for skilled labor, political interference, shifting government regulations, keeping up with technological advancements, and members needs.

The lack of a proper revenue growth system is one of the key problems facing most of the Sacco in the country. A good revenue growth system helps to ensure that the Sacco has improved performance and also ensures its long-term sustainability and expansion. Some Sacco have minimal investment in their capital gains, thus limiting their prospects of increased returns on their investments.

Marketing strategies also influence the amount of revenue gained, as increased marketing brings more customers to the Sacco. Most Saccos adopt a vigorous marketing approach while ignoring the impact of giving customers information on the importance of financial literacy. This helps to show the client that there's confidence in banking with them, hence increasing the membership baseline. Proper governance also plays a key role in increasing revenue growth. This is due to the fact that, with a clear governance structure, the policies being made will be properly addressed.

With the increased cost of living, the rate of loan defaults is becoming high. This reduces the amount of revenue that the Sacco is able to collect. Even with the risk of losing their properties that they declared as collateral for the amount being loaned to them, the loanee may be unable to pay it back. This makes the institution lose out on the total amount and even the interest, as maybe the valuation of the collateral was not done in a clear way and was done in a hurry, hence the security was undervalued.

The increasing rate of inflation causes the interest rates of the loans provided by the Saccos to increase, leading to the members viewing the loans as unfavorable for them as they have to pay more for the loan they take. This leads to a reduction in the amount of revenue that the Saccos get from interest on the loans, leading to low revenue growth. Providing the members with low interest rates on loans that they take increases the amount of loans taken by the members and also attracts a large number of new members, thus increasing the membership base that comes together with the new members' registration fee and the amount of money collected.

Most Saccos have stuck to the traditional view of Saccos as just depository, withdrawals, and loan-provider

institutions. They have not done extensive research on other ways and forms of investment, as well as the provision of other services such as insurance and asset financing models. This makes them lose a lot of revenue, as these possible clients go to other firms that can provide them with the services that they require.

2. Literature Review

This chapter provides a comprehensive theoretical framework for understanding the nature of revenue growth, including an overview of the key theories that inform our understanding of this concept. In addition, this chapter presents an overview of loan policies, operation costs, and membership size, exploring their roles in facilitating effective revenue growth in Saccos.

2.1. Theoretical framework

Theories concerning revenue growth are discussed here. One can conduct a compressive review and take into account the theories that anchor the study. Since theories serve as the foundation for the investigation, they are a crucial component of the literature review. In this study, we will look at theories such as credit default theory and agency theory.

2.1.1 Agency Theory

This theory was developed by Jensen and Mecklin in 1976 and explains the relationship between the principal and the agent. An agent is a person employed to do any act for another person. The person whose act is done by an agent is called the principal. When a person is employed by another to contract on his or her behalf, the relationship between them is known as agency.

Whenever one party depends on the actions of another, the relationship is said to occur. That is, an agency relationship is an agreement that services are performed on behalf of a principal by the agent. The principal also delegated the power of decision-making to agents. Agents have to make rational decisions, and this theory has the ability to motivate them. For example, the Board of Directors (BOD) is the agent who performs services on behalf of shareholders, who are the principal. The BOD may lack knowledge in some areas like finance and credit; therefore, they won't work to the expectations of the shareholders, hence making wrong credit decisions (Kawou, 2016).

The SACCO loan officers disburse loans that will be recovered after a specified loan term, but sometimes loans may not be fully recovered. The relationship between agency theory and the probability of a borrower failing to pay back their loans is important to this research study in that creditors take loans even when the certainty of paying back the loan is minimal due to a lack of necessary information between the Sacco and the borrower.

In this research, the SACCO is the principal, and the borrowers are the agents who acquire loans and are expected

to repay them according to the loan terms of payment and at an agreed interest rate, depending on the SACCO. Loan default may occur if the SACCO does not get enough information about the borrower's social and economic life. The loan officers who are agents of the Sacco fail to meet the expectations of the Sacco, which is to ensure there is strict monitoring of loans and alert the Sacco of any sign of default for immediate action.

2.1.2 Credit default theory

Credit default occurs when an entity fails to fulfill its financial commitments by the due date (Keenan, 1999). The causes of loan default and their implications are best explained through this theory. The theory makes a clear connection between macroeconomic factors that influence the financial environment and their microeconomic consequences on shifting financial conditions, which leads to loan default.

The most commonly used credit measure for forecasting future loan performance is the credit scoring model. Credit scoring is the assigning of a particular individual a qualitative score that represents that individual's potential to be creditworthy. The models are statistical in nature and include discriminant analysis, logistical regression analysis, etc. Credit scoring techniques are used in order to determine the probability of default based on past data on the performance of loans and borrower characteristics. The application is taken into consideration for further evaluation by specialized small business units if client statistics provide a score above the cut-off score in the small business environment. It then moves on to the small business credit department for additional evaluation and approval or rejection.

In credit scoring, it is fundamentally assumed that there exists a measure that can distinguish between good credits and bad credits and classify them into two distinct distributions. Compared to consumer lending, credit scoring models used by SACCOs and MFIs were more complex (Feldman, 2000). This is due to their capacity to give aspects pertaining to the financial history of the company's owners significant weight. In their study, Frame, Srinivasan, and Woolsey (2001) discovered that increasing the number of marginal classes of borrowers considered when calculating credit scores results in an increase in lending.

2.2. Factors affecting Revenue Growth of SACCOS

2.2.1 Loan default and Revenue growth of SACCOS

A default occurs when a person or an institution fails to meet their contractual obligations by the time, they are due. Therefore, a loan default occurs when a party fails to carry out its statutory financial obligations by the due date set aside. Default happens when a debtor is unwilling or unable to repay a debt as a result of unavoidable events like losing a job, having their salary drastically reduced, having their

business fail, etc. Prior to engaging in debt, one ought to carefully evaluate all the available information and make a well-informed decision based on it. Lenders should also thoroughly investigate a potential borrower's financial situation before providing credit.

Through thorough supervision, monitoring, and evaluation of the projects funded by the loan, temporary causes can be controlled. Before a loan is disbursed, it is necessary for the loan applicant to be provided with proper training on handling the loan.

The performance of SACCOS could be influenced by the criteria for investing in reserve funds through a reduced likelihood of financial problems and the risk of defaulters, according to a study of SACCOS reserve fund investment practices by Gachara (1990). Non-performing loans, commonly known as NPLs, impede the respective Savings and Credit Cooperative Organization (SACCO) from generating interest income and consequently reduce the overall monetary pool that can be allocated towards the facilitation of fresh credit (Millan et al., 2023).

The stability of multi-billion-shilling savings and credit cooperative movements is greatly threatened by the likelihood of borrower defaults on loan repayments. This is according to Kenya's five financial sector regulators, including the Central Bank of Kenya (CBK), Retirement Benefit Authority (RBA), SACCO Societies Regulatory Authority (SASRA), Insurance Regulatory Authority (IRA), and Capital Market Authority (CMA). They added that the risk of loan default on personal loans is excessively high because the obligations of SACCOS are only covered by member guarantees. As a result of the low liquidity and solvency ratios caused by the high cost of borrowing in the banks, they have also stated that SACCOS' reliance on pricey bank loans has increased the likelihood that they may default on the loans they hold.

It can be difficult for managers to come up with a suitable collection of performance indicators for their firms (Johnson et al., 2005). This is so because, even if they have many indicators, only a small number of them provide a helpful overall picture. A number of indicators are qualitative in nature, which makes evaluating financial performance challenging.

A loan default caused losses for savings and credit cooperative societies, which in turn affected member wealth. The suggestion that was made was for savings and credit cooperative societies to integrate their information systems with employers and to provide members with regulations on loan lending and the extension of the credit duration.

In a study undertaken in Tanzania at Kibaigwa Financial Services and Credit Co-operative, management complacency on loan follow-ups, which has been going on for some time, is the primary contributory factor for loan default. One of the most significant factors affecting the functioning of commercial banks and SACCOS'

microfinance institutions is loan default (Karumuna & Akyoo, 2011).

This is a consequence of the manner in which they lend, which influences loan repayment. Karumuna and Akyoo (2011) conducted research on the variables that affect the repayment of loans. They discovered that these variables included insufficient management loan follow-up, an ineffective repayment procedure, insufficient asset verification, and so on.

2.2.2 Operating costs and Revenue growth of SACCOS

Mumanyi (2014) investigated the link between SACCOS operating costs and financial growth. He discovered that as the SACCO grew, operating expenses increased, and, as a result, profit was reduced. It also demonstrated that administrative costs, inadequate loan management, and high borrowing rates for member loans were barriers to the expansion of Kenyan SACCOS. He added that the ineffective climate and dysfunctional infrastructure in which SACCOS operates contributed to the rise in operating costs. In their analysis, Makori, Munene, and Muturi (2013) noted that SACCOS' heavy reliance on short-term borrowing was the primary contributor to their high operating costs. A condensed working capital cycle results in heightened profitability through the enhancement of cash flow, the reduction of financing expenses, and the improvement of operational efficiency (Ngari, 2023).

Due to their poor capital base, SACCOS borrows money from banks at exorbitant interest rates in order to fund loans to their members, preventing SACCO members from borrowing from banks. Because of the high interest rate associated with borrowing from commercial banks, SACCOS's financial performance is impacted. Due to their poor capital base, SACCOS borrows money from banks at high interest rates in order to fund loans to their members, thus preventing SACCO members from borrowing from banks. Because of the high interest rate associated with borrowing from commercial banks, SACCOS's financial performance is impacted. High costs of operations lead to low profitability for a firm, resulting in low revenue.

2.2.3 Membership size and Revenue growth of SAACOs

By completing the membership form, paying the requisite membership fee, and consistently saving in the form of shares, a member voluntarily joins the SACCO. A SACCO's members may be divided into two main groups: active members and dormant members. Active members routinely deposit shares into their SACCOS, and as a result, they get the SACCOS's annual dividends, whereas dormant members do not. As a result of this, a SACCO may be defined as a group of individuals who have joined forces with the intention of raising their standard of living through improving their economic situation (SASRA report, 2013).

According to signaling theory, companies with high

growth rates may readily distribute dividends to their shareholders as a means of informing the marketplace about their strong potential performance. Connolly and Dhanani (2009) discovered that companies in New Zealand that employ recent revenue growth distribute lesser dividends. Growth is viewed as a means of achieving profitability and giving a company an edge over rivals when it is utilized as a performance indicator. Larger companies benefit from economies of scale and perform better on the market. However, more expansion comes with many challenges because of rising costs, which results in lower profitability and financial hardship. For the majority of SACCOs, growth without profitability is a difficulty. A SACCO has to depend on debt or equity financing when it is unable to finance its growth through retained earnings. This demonstrates the significance of the correlation between profitability and growth.

It is of utmost importance to acknowledge that effective corporate governance is a vital factor that holds the potential to exert a substantial impact on the overall performance and resilience of a company (Kamau et al., 2023). Proper governance will facilitate an augmentation in the number of individuals becoming members of SACCO and subsequently lead to an improvement in revenue performance. Studies demonstrate that small businesses expand more quickly and with greater variability than bigger businesses. The underlying conceptual framework that explains the connection between a firm's size and its financial development is based on the concept of economies of scale. These economies of scale may happen for a number of reasons, including organizational, financial, and technical ones, among others. The main justification for mergers, takeovers, and acquisitions is the economies of scale that large organizations receive due to their lower cost of capital than small enterprises. The size of the large organization is restricted in order to generate economies of scale. The company then encounters diseconomies of scale as managing huge groups becomes expensive owing to their complexity, bureaucracy, and inefficient processes.

Large companies benefit from higher interest and discount rates when they purchase in bulk (Pervan & Višić, 2012). Large businesses are more likely to achieve significant strategic diversification, benefit from economies of scale, and have more negotiating leverage with clients and creditors.

Large businesses also have simple access to investment finance and a wide variety of competent human resources. As a result, we draw the conclusion that a positive relationship exists between a firm's size and its financial success.

SACCOS should use prudence when selecting new members, ensure that the savings first concept has been implemented, and keep an eye out for the needs of present members. Members of SACCOS may only obtain credit through others in an environment where credit is limited.

In addition, widespread poverty creates the ideal environment for predatory pyramid-selling schemes to succeed, thanks to a robust informal economy and related informal financing. Savings and credit cooperative societies must create and put into practice systems to carefully examine the legality and authenticity of loan application requests before making loans to members in such a situation.

2.2.4 Revenue Growth

The implementation of effective governance practices within a SACCO, including but not limited to transparent decision-making processes, accountability, and adherence to ethical standards, is widely recognized as a crucial factor in achieving sustainable financial growth and stability. Through the establishment of robust governance structures, such as a well-functioning board of directors and committees, SACCOs can ensure that their operations are conducted in a manner that promotes the best interests of their members and the organization as a whole. By upholding principles of good governance, such as integrity, fairness, and transparency, SACCOs can build trust and confidence among their members, which will in turn lead to increased participation and engagement.

In addition to good governance practices, another key aspect that has been found to have a significant impact on SACCO revenue is the level of loan default. Low levels of loan default indicate that members are able to meet their financial obligations, which not only helps to maintain the financial health of the SACCO but also ensures that funds are available for lending to other members. This, in turn, leads to increased revenue for the SACCO as more members are able to access credit and contribute to the overall growth of the organization.

Furthermore, reducing operating costs is another important factor that can contribute to the enhancement of SACCO revenue. By implementing efficient and cost-effective systems and processes, SACCOs can streamline their operations and minimize unnecessary expenses. This can include measures such as automating routine tasks, leveraging technology to improve efficiency, and negotiating favorable terms with suppliers. By optimizing their cost structure, SACCOs can allocate more resources towards revenue-generating activities, such as expanding their product and service offerings or investing in marketing and outreach initiatives. This, in turn, can lead to increased revenue and profitability for the SACCO.

Finally, increasing membership is another crucial strategy that can contribute to the growth of SACCO revenue. By attracting new members, SACCOs can expand their customer base and increase their market share. This can be achieved through targeted marketing and outreach efforts, as well as by offering competitive and attractive products and services. Increasing membership not only leads to an increase in the number of potential customers

and revenue streams but also provides an opportunity for cross-selling and up-selling to existing members. By effectively managing and nurturing their member relationships, SACCOs can maximize their revenue potential and ensure long-term financial sustainability.

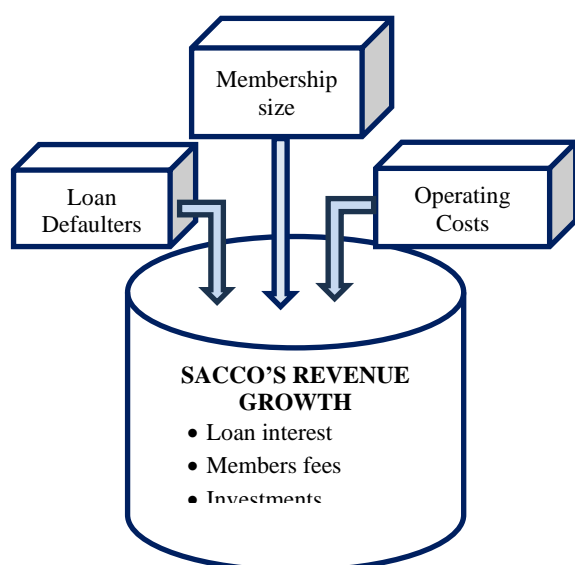


Fig 1: Factors affecting revenue growth

In summary, Figure 1 illustrates how factors like loan default, membership size, and operating expenses are connected to SACCO's revenue growth. The figure implies that SACCOs should manage loan defaults, aim to increase membership size, and control operating expenses effectively to promote revenue growth. Additionally, it highlights the multiple revenue streams that contribute to the growth of SACCOs, including loan interest, members' fees, and investment income. The figure suggests a complex interplay between these variables. For example, a higher membership size can contribute positively to revenue growth, but it may also increase the risk of loan defaults if proper risk management is not in place. High operating expenses can negatively impact revenue growth by reducing the net income generated by the SACCO.

3. Summary and Conclusion

In conclusion, this study has explored the various factors that affect the revenue growth of Savings and Credit Cooperative Societies (SACCOs). SACCOs play a crucial role in providing financial services to their members, especially those who may have limited access to credit facilities from commercial banks. Revenue growth is a vital indicator of their financial performance and sustainability. The literature review has shed light on key factors influencing revenue growth in SACCOs. These factors include loan default, operating costs, and membership size.

Understanding and managing these factors are essential for SACCOs to thrive and continue to serve their members effectively.

Loan default has been identified as a significant challenge, leading to losses for SACCOs and affecting the wealth of their members. The research has shown that proper risk assessment, loan follow-up, and member education on responsible borrowing can mitigate loan default and contribute to revenue growth. Operating costs have also been a concern, with high costs affecting profitability. SACCOs have sometimes resorted to expensive short-term borrowing from banks due to their limited capital base, further impacting their financial performance. Effective cost management strategies and exploring alternative funding sources can help alleviate this issue and boost revenue growth.

Membership size is another crucial factor influencing revenue growth. A growing membership base can lead to increased revenue through registration fees and additional savings. However, SACCOs must carefully select new members, ensure adherence to the "savings first" principle, and address the needs of existing members to sustain growth. Furthermore, the theoretical framework has delved into agency theory and credit default theory, providing insights into how agency relationships between SACCOs, borrowers, and loan officers can impact loan repayment and revenue growth.

In light of the research presented, it is evident that SACCOs face multifaceted challenges and opportunities in their quest for revenue growth. While the study has highlighted key factors, it is imperative for SACCOs to adopt strategic approaches tailored to their unique circumstances, regulatory environments, and member needs. This may include risk management, cost containment, and prudent membership management. The findings from this study can be instrumental in guiding SACCOs and policymakers in addressing these challenges and fostering sustainable revenue growth. Ultimately, the success of SACCOs in promoting financial inclusion and economic development depends on their ability to manage these factors effectively and ensure the long-term financial health of the organization and its members. In conclusion, a combination of good governance practices, low loan default, reduced operating costs, and increased membership can significantly contribute to the enhancement of SACCO revenue. By adopting and implementing these strategies, SACCOs can create a solid foundation for sustainable growth and success in the long term.

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