INFLUENCE OF CREDIT REFERENCE BUREAU ON LOAN DEFAULT STRATEGIES: A CASE OF COMMERCIAL BANKS IN KENYA

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A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION, SCHOOL OF BUSINESS, UNIVERSITY OF NAIROBI

2018

DECLARATION

I Ferdinand Maliachi Muhanda, hereby declare that this research project entitled **Influence of Credit Reference Bureau on Loan Default Strategies: A Case of Commercial Banks in Kenya** is my own original work and has not been presented for an award of a Degree in other University, college or an institution of higher learning

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ACKNOWLEDGEMENTS

It is my greatest joy and pleasure to thank the Almighty God for all the wonderful blessings that made this work possible. I am also greatly indebted to my supervisor Dr James Gathungu of the University of Nairobi for his guidance, valuable input and positive criticism throughout the various stages of the study. This research could not have been possible without the support of my colleagues and the management of the Commercial banks that allowed me an opportunity to undertake my research work at the organization. Last but not least I wish to acknowledge Mr. T for providing me with all the research materials and for the team typing, printing and binding this final document.

DEDICATION

This is dedicated to my loving family; starting with my dad Mr. Pius Muhanda for his continuous mentoring, my mother Mrs. Jennifer Muhanda for her encouragement, my loving wife Elizabeth Kwamboka and precious daughters Sharon and Charlene.

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LIST OF ABBREVIATION

CAMPARI   Character, Ability, Means, Purpose, Amount, Repayment, Interest

CBK   Central Bank of Kenya

CIS   Credit Information Sharing

CR   Credit Rating

CRB   Credit Reference Bureau

DPFB   Deposit Protection Fund Board

FSD   Financial Sector Deepening

IT   Information Technology

KCB   Kenya Commercial Bank

MFI   Micro Finance Institution

NIC   National Industrial Credit Bank

NPLs   Non Performing Loans

PIs   Participating Institutions

SACCOs   Savings and Credits Societies

UBA   United Bank of Africa

ABSTRACT

The objective of this study was to determine the influence of credit reference bureau on loan default strategies using a case of commercial banks in Kenya. In Africa, the concept of CRB has had its practice in few selected countries by multilateral companies through private credit bureaus such as Compuscan which operates in Botswana, Namibia and Rwanda while Kutz Univar, operate in Tanzania, Kenya and Uganda. The information obtained from the research would be of a very much importance to both the Government, Central Bank and in particular the Ministry of Finance Kenya to enhance credit information sharing. This study will employ Credit Rationing Theory, Adverse Selection Theory and Model of Credit Information Sharing design. Based on literature review, the study notes that if mitigation of credit risk are inadequately handled, the respective commercial banks are subject to loosing financially, increased capital recovery costs, and social role failure due to inability to provide loans to the society aiming at improving and boosting their living standards. The researcher will descriptive research is description of state of affairs as it exists. It is a method of collecting information by interviewing or administering a questionnaire to a sample of individuals. The target population of the study consisted of all the 44 licensed commercial banks in Kenya and the three credit reference bureau under the Banking Act. The researcher used census method for the research and was composed of all commercial bank headquarters credit managers. To collect primary data, the researcher used questionnaires. Besides, Secondary data required for this study collected from CBK loan books and CBK annual Bank supervisory reports. To ensure validity, questionnaire was prepared in conjunction with literature review and based on the research objectives and questions. Its content validity was pre-tested by a pilot study. The researcher acquired a research data collection letter from the University. The researcher maintained confidentiality at all times, be responsible for the work and for the contribution to the whole study. On completion the researcher organized the data received, coded, edited and tabulated to check accuracy, completeness and storing it in appropriate form. The data was presented using graphical systems which will include histograms and pie chart, frequency distributions tables and numerical methods. This study found out all the respondents (100%) had a large access to credit information from the credit information bureaus. This is reveals that both banks have embraced the introduction of credit information sharing and thus for lending to take place due diligence has to be done through sharing of information through the Credit Bureaus. This study notes that regarding the extent of effectiveness of credit information sharing on the banking industry in Kenya, the study found that thus far credit information has been effective, but it can be concluded that it is effective but only to a small scale to date. This conclusion is supported by the fact that Credit Reference Bureaus had an impact on the extent of effectiveness of credit information sharing on the banking industry in Kenya as was agreed by many respondents. This study recommended that in the process of managing loan defaults, this study recommends the registration of more Credit Reference Bureaus by the relevant authorities, because of diversity of Credit information.

1.1   Background of the Study

Referencing of credit is an actual response to the problematic flow of the asymmetric information between the borrowers and lenders. The Credit Reference Bureau (CRB) can either be owned publically or privately to help in harmonization of information concerning the borrowers from the lenders (Olegario, 2003). A very wide range of literature concerning offering of credit has depicted asymmetrical flow of the information that can be a hindrance to the allocation of loans to the borrowers in an efficient way. This can lead to rationing of the credits as well as fluctuation of the rates of borrowing as well as lending (King, 2006) .The theory involves screening and monitoring of borrowers in a more efficient way than any other investors can be able to do. It's   very specialized in the collection of data and even treating them private and confidential. The money management and account deposit. In this regard, most of the banks have information organized strategically in line with the reception and expenditure of firms' cash is concerned (King, 2006).

This study is however anchored on credit rationing Theory in support of Model of credit sharing as well as adverse selection theories. Credit rationing theory posits that banks must screen and evaluate borrowers in an efficient and effective manner Gordon (1965) the theory also further states that Banks usually charge more than just one interest rate to all customers. High-risk borrowers pay a higher interest rate and credit rationing is less likely. Since financial institutions cannot distinguish borrowers perfectly and screening

them perfectly is impossible, credit rationing may occur. Model of credit sharing theory as propounded by Stiglitz and Weiss (1981) approach is the extensively known one, and exposes the motivation of borrowers to engage in very risky investment ventures in their adventure to get higher returns in a limited liability circumstances, and in the process lowering the lenders payoff. Information sharing as shown by Pagano and Jappelli, (1993) minimizes adverse selection through improvement of information on clients by banks and other lenders

In Kenya, before the publication of the Banking (Credit Reference Bureau) regulations 2008 and the licensing of the first Kenya`s credit bureau, Credit Reference Bureaus Africa Ltd in February 2010, Kutz Univar Bureau was operating in the country. CRBs concept was given a statutory basis and legal recognition by the Banking (CRB) Regulations, 2008 published in July 2008 and came into operation on 2nd February 2009.The central bank of Kenya together with CRB had to put to closure a group that provides credit information to the relevant institution. Credit information from CRB enables the lenders to perform the credit rationing to the customers who have poor payment habit even if they are ready to pay with very high interest rates. CRB has therefore enabled sharing of credit information about borrowers among commercial banks and hence led to access of information that is valuable during assessment.

1.1.1 Credit Information Sharing

Introduction of the Credit rating bureau has acted as the main revolution factor towards lending which has boosted very many Kenyan commercial banks' performance. Before

CRB was introduced in the Kenyan financial market, many borrowers used to hock from one financial lending institution to the other without necessarily being discovered. Consequently, this brought about high levels of losses resulting from NPLs. However, with the introduction of CRB, the banks are able to be provided with historical information about the customer's credibility. This includes major information concerning any late payments, all enquiries, loaning and accounts among other critical information (Berger and Frame, 2005).

Loan portfolio consist of a very large portion of the assets which are mostly non liquid in most of the banks and are able to experience the highest rate of the credit risk. Lack of repayment of loans occasionally leads to default. Thus lending is the principle activity of commercial banks and the loan portfolio is the largest asset and the predominant source of revenue for the lending institutions When a borrower cannot repay interest and or instalment on a loan after it has become due, then it is qualified as default loan or non-performing loan (Koch, 2000).

1.1.2   Loan Default Strategies

Lending is a risky enterprise because repayment of loans can seldom be fully guaranteed. Collateral is usually some form of property or assets such as equipment, automobiles, tools or real estate that is pledged as security for a loan. Banks will use collateral as a loan default strategy to make sure they are in a more stable situation when a loan is made. If a bank wants to make a larger loan to a consumer or a business, it may require some type of collateral.

Loan default usually occurs when a debtor has not met their legal duties (obligations) according to the debt contract, example, has not made a scheduled payment, or has violated a loan covenant (condition) of the debt contract. A default is the failure to pay back a loan. Default may occur if the debtor is either unwilling or unable to pay his or her debt. This can occur with all debt obligations including promissory notes, mortgages, bonds, and loans. Thus an important strategy is to ensure they understand their legal expectations. It usually arises whenever the borrowing party does not honor the original agreement that can be able to meet the terms of the loan repayment structure which stipulates the period that the loan is supposed to be paid back to the lender. A good Bank system should be able to maintain client information with strong search capabilities, maintain customer information such as name, family information, age, gender, address (home and business), and type of business, as well as impact information. The level and the quality of credit appraisal majorly depend on, assessment of the credit risk and complete present ability of the risk (Strualitytt, 2000).

Bofondi and Gobbi, (2003) Another strategy to manage loan default, involve the banks using CAMPARI model, which stands for Character, Ability, Means, Purpose, Amount, Repayment, Interest and Insurance. The background and experience of the individuals or business can be a pointer to the potential for success. When a debtor chooses on a loan, in spite being able to service it (make payments), this is said to be strategic default. This is most commonly done for non-recourse loans, where the creditors (bank) cannot make other claims on the debtor. The role of a guarantor is commitment by the way of agreeing to the terms and conditions of the loan and bearing liability to the extent of the loan

together with the interest and other charges. The emergence of CRBs has revolutionized lending, and hence the study aims to establish influence of credit reference bureau on loan default management in selected commercial banks in Kenya.

1.1.3   Credit Reference Bureau among Commercial Banks

In Kenya there are 44 licensed commercial banks Commercial Bank of Kenya (CBK, 2018) which dominate banking in East Africa with 282 branches outside the country (Ford, 2014). This study aims to be carried out on all the (44) commercial banks in Kenya. The researcher believes that these provided an adequate population and sample for the study and therefore give reliable results and findings. The data will be collected from the credit managers (personnel) of the respective banks in their headquarters (Nairobi). The headquarters was covered as the researcher would be able to access them easily and save on time. Further the information on the commercial banks would be easily accessed given that all the branches are connected to the headquarters.

1.2   Research Problem

Loan portfolio constitutes a large portion of assets in most banks hence relatively illiquid and exhibits the highest credit risk, Loan default is therefore related to non-recovery of loans. Information sharing through Credit Reference bureau (CRB) has greatly improved the financial performance of many commercial banks. Through the use of CRB, banks are in a position to obtain detailed information on a person's credit history, including information on their identity, credit accounts and loans, bankruptcies and late payments and inquiries (Berger & Frame (2005). A default on a loan occurs when the borrower

does not make the required payments or in some other way the borrower does not comply with the terms of a loan (Al-Tamini and Al-Mazrooei, 2007).CRB is therefore seen to be a relevant loan default strategy to minimize risk of loan default. Through CRB lenders are able to determine credit worthiness of their borrowers and therefore reduce the loan default risk. In this respect CRB assists in first, sharing information on default among banks; secondly, eliminating corrupt borrowers and thirdly provides commercial professional credit reference to prospective investors. Other strategies involve collateral or security based lending

According to Bofondi and Gobbi, (2003) commercial banks in Kenya are facing huge risks, and some of the risks emanates from the non-performing loans. These kinds of loans have a higher cost due to its level of exposure to the risk of default, for instance CBK in the year 2015 placed Dubai Bank of Kenya, Imperial Bank and Chase bank in 2016 under receivership for facing serious liquidity problems.there is a need to study and have a clear understanding of the influence of CRBs on loan default strategies. This is in spite of the gains and benefits made in Kenya since inception of credit information sharing. Since loans are the main assets to all commercial banks in Kenya it's therefore important to monitor them in order to grow a high yielding asset portfolio.

even though scholars have written much concerning the performance of banks in Kenya, few studies dwell on the risk identification against default risk rate, the effect of CRB on the rate of credit repayment and influence of CRB on loan default among commercial banks in Kenya and thus this study could be the few to add new knowledge on these areas

of interest. Sigei, (2010) for instance evaluated how effective the Credit Referencing bureau was in Kenya. Ng'anga, (2011) was able to investigate the perception of the investors towards CRB services in the credit market. Gaitho, (2010) researched on the importance of the Credit Reference Bureau on the access of the credit in the country. Mumi, (2010) was able to appraise the effect of CRB in the Kenya's commercial banks. This study therefore aims to have a deeper understating of, what is the role of CRB in risk identification against credit default among commercial banks in Kenya? What is the influence of CRB on the rate of credit repayment in selected commercial banks in Kenya? What is the contribution of CRB in effective loan default strategies among commercial banks in Kenya?

1.3   Objective of the Study

The general objective of this research is to determine the influence of credit reference bureau on loan default strategies using a case of commercial banks in Kenya. The exact goal of the research will be;

  i.   To establish CRB in risk identification against default risk rate among commercial banks in Kenya.

 ii.   To establish the effect of CRB on the rate of credit repayment among commercial banks in Kenya.

iii.   To establish the influence of CRB on loan default strategies among commercial banks in Kenya.

1.4   Value of the Study

The information obtained from the research would be of a very much importance to both the Government, Central Bank and in particular the Ministry of Finance Kenya to enhance credit information sharing. In addition, the findings of this study would be useful to the Kenya Bankers Association, in informing certain policy recommendations to mainstream the credit information industry. The outcome of the research would be crucial to contribution of knowledge to all the Kenyan commercial banks, especially the change management gurus; it will be able to assist the bank in formulation of the policies effectively relating to access of credit.

The research will be of much significance to the investors in the financial market that include managers of the bank the managers of the credit reference and even the public in general. There are pitfalls non-performing loans have now become a major challenge for many banks today, in spite of the credit reference bureau mechanism. This study will be useful for CRBs on how best to improve their services to enhance contribution on the practice of proper banking services.

The outcome of the research will majorly be used by the makers of the policies, to understand and control the impact of increasing non-performing loans from the economy due to Credit Rating (CR) risk. This research will be used as a reference point by other scholars and contribution of the study to policy makers to provide a dependable information source for the future research.

CHAPTER TWO

LITERATURE REVIEW

2.1   Introduction

In this chapter, the analysis of literature connected to the topic of study is handled. It deals with past study analysis both theoretical and empirical aspects of review as well as identification of gaps in the critical review.

2.2   Theoretical framework

Credit rationing, adverse selection and model of credit data sharing theories forms the foundation of this study. This is critical as it helps to provide the bottom line of selecting the various variables under the topic of study. The use of theoretical framework cannot be satisfactorily emphasized since the study indicates, as it lays basis of knowledge construction in the research.

2.2.1   Credit Rationing Theory

Freimer and Gordon (1965) are the founding fathers of this theory, and it was applied comprehensively by Stiglitz and Weiss (1981), where they realized that credit rationalization (lenders are unable to differentiate borrowers based on quality) can be brought by information asymmetry. De Reza and Webb, (1987) however, they indicated that inverse outcomes-lending excessively, excess credit- is a fruit of information asymmetric in the financial market especially the credit market. Banks must screen and evaluate borrowers in an efficient and effective manner to guarantee their existence (Allen and Santomero, 1998). The banks have special units that oversee collection of

personal data concerning a potential as well as their existing clients who intend to apply for loans (Freixas and Rochet, 1999). The banking institution possess high value strategic data entailing organization's receipts as well expenditures that aid in managing cash and deposit accounts (Diamond and Rajan, 2011). Despite all the plans and strategically aligned data, banks are still affected by information asymmetry in that price evolution is inadequate to do away with credit market (Freixas and Rochet, 1999). According to Stiglitz and Weiss (1981), if banks charge common interest rates to every due to high costs involved in borrower screening and evaluation on their credit worthiness, the rationing of credit becomes the only route for them to follow.

2.2.2   Model of Credit Information Sharing

It is acknowledged that various approaches to modeling credit markets hidden data and actions are employed to a greater extent in the literature review of the information asymmetry crisis.

The large interest rates according to Stieglitz and Weiss (1981), draw a higher proportion of investments with high risk in one pool, and establish the conditions for credit limiting equilibrium. The previous work outlines other aspects of moral hazard including borrower underinvesting the funds to supplement their other activities, negligence, diversifying the loan partially from viable investment ventures to current consumptions (Boot, Thakor, and Udell, 1991). The moral hazard form characterizing this model involves multiple contracting of loans, offering borrowers an advantage on credit terms and regulations by accessing diverse loans from various lenders who only access data relating on their particular contracts (Jappelli and Pagano, 2000; Bizer and De Marzo,

1992). This increases the client's chances of defaulting due to negative externalities to the many loans in form of hidden contracts that the borrower is obligated to. Consequently, credit information systems analysis is created concerning the moral hazard in particular due to escalating loan defaults influenced by many loans under one client in different loan intuitions especially in the developing economies around the globe. in turkey for instance, this challenge has been extensively documented (Kaynak and Harcar, 2001), South Africa (Daniels, 2004), and Central America (McIntosh and Wydick, 2005).

Based on Stiglitz and Weiss (1981), conceptualization of information sharing impacts the operation of the credit market. The attempt to create a model to deal with this was a simplification as well as an extension of McIntosh and Wydick (2005) that considers an oligopolistic industry case of lending investors involve competing for large group of borrowers in Bertrand. Investors offering loan contracts; on a fixed costs and defined loan amount and interest charges, where the borrower's gambles on the chances of getting a yield higher to the rate charged. The project's success rate determines the payoff of loans, and it as well raises the chances of the borrower's inability to fully repay the loan; whereby amount borrowed must balance the existing loans and the proposed size of the loan. In cases where credit data sharing is absent, the current credit worthiness of the borrower is unknown to the lender who has to form assumptions concerning the client's indebtedness as noted by Stiglitz and Weiss (1981).

McIntosh and Wydick, (2005) notes the extent of advantage of lending institutions sharing constructive data on borrowers to eliminate the issue of hidden credit records of the customers. Contrary to negative data which only reveals default records, the positive and constructive information points out the features of the borrower, outstanding loans, repayment records, and past loan records. The lenders exhibit the willingness to share negative or bad information to instill discipline in customers who fear blacklisting, but are very unwilling to reveal positive information due to threat of competition in the market for clients. The positive and negative data sharing exposes borrowers to both discipline of defaulting and hiding important facts to the contract (McIntosh and Wydick, 2005).

The art of sharing both types of information aid in developing the types of borrowers as noted by McIntosh and Wydick, (2005) as follows: for one, exposed borrowers-they possess one loan contract inferior to perfect data contract. The second type is defaulting borrowers-possess various previous loan default records. Thirdly, clean borrowers-they have no defaults or bad credit records. This can only be possible if positive information sharing is increased and lowering the extend to hidden information on the credit market. The effects of information sharing include screening, incentive, and credit expansion effect, which on the overall results in reduction in default rate, thanks to the credit information systems. The function of outstanding debt is defaulting, bigger loan sizes comes from loan expansion while pooled together borrowers depicts lower defaulting rate (Jappelli and Pagano, 2000)

2.2.3 Adverse Selection Theory

According to Stieglitz and Weiss (1981), who came up, with adverse selection concept, under this the two major assumptions of the theory, in which the lending bodies display inability to differentiate, among the customers seeking loans concerning their degree of risk and extent of amount to lend. The research is based on the assumption that borrowers only repay if they have the ability to repay. The preference of borrowers to risk and risk aversion is imparted by limited liability and neutrality of risk among the lenders.

Auronen, (2003) notes that in the presences of interest rate flexibility and competition on the market, over demanding may persist. The theory states that the rates may fail to increase to ensure that all applicants will get the loan especially with limited loanable fund on the credit market. Borrowers offering collateral to secure credit obtain lower rate loans and are motivated to toil harder and in the process acquire higher returns. The inequality of wealth as assets among the borrowers escalates the levels of poverty as credit offering entities analyze and base on these to deny or award loans; banking institution may improve their knowledge about borrowers through information exchange.

As the information asymmetry theory points out, the complication in differentiating borrowers' on the basis of quality, resulting in adverse selection and moral hazard crises on the market Richard (2011). The information rich party in the contract is in a better position to negotiate for factors that favors them in the contract (borrower) than the other party (lender) who is likely to either make the right or wrong decision (Auronen,2003) and Richard (2011). The accumulation of loans that are not performing in banks has increased due to moral hazards and adverse selection problems on the credit market

(Bester, 1994; Bofondi and Gobbi, 2003). Information and data sharing on this market can aid lenders to differentiate between bad and good customers, and help them set the right terms to the loan contracts. The attractive and better terms are given to clean borrowers due to low risks associated with them, this influences the increase of credit demand, high rationalization of riskier customers on the market (Barron and Staten, 2008). The CRB would increase the operation of financial organizations and the entire sector influencing the performances of the economy where credit can be easily accessed at lower rates. The good credit record of an individual will be the collateral the lenders look for to finalize your loan, this is attainable though full addressing the issue of information asymmetry (improve trust between the parties to the loan contract) thus boosting transparency and fair completion among lenders. The participating institution (PIs) come up with quality informed decisions when the clients credit records are timely submitted to them, collateral streamlines the process, reduction in default rate and fasten the loaning process (Mutebile, 2008). Information availability will compel the PIs to over new products and affordable rates on the market.

2.3   Credit Reference Bureau and loan default strategies

Credit Reference Bureau refers to an organization that gathers data from diverse sources and makes that data available for lenders and other consumers for a number of uses. The detailing of credit history of individuals, as well as identity, late loan repayments, bankruptcy, and loan accounts are useful to various lenders on the credit market. Moreover, CRB provide proof of fraudulent and false declarations, forgeries, cheque kiting, use of false securities among other data concerning a client. The information is

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available to lenders with permissible reasons and excuses as the law outlines such as in assessing the credit worthy of the customer (Sullivan and Sheffrin, 2003).

For the purpose of credit risk evaluation, credit ranking, job consideration, apartment leasing by the CRB customers may request them to vail personal data of the client in question (Sullivan and Sheffrin, 2003). Subsequently, lenders are enabled to offer credit to less risky clients, ability to evaluate and assess bad debts to cover anticipated losses and liabilities.

The CRB acts as brokers of information on the credit market by availing reliable, relevant facts to the creditors on the client's loan repayment records and current outstanding loan balances of the loan applicant according to Sinare (2008). The creditors reciprocate by acting as the bureaus source of information on individuals, analyze it, package it into reports and proved the information to lending institutions at a fee. According to Lewis (2004) majority of financial associations and lenders value collateral as security to credit, however, they exhibit the willingness to use cash to access information on the individual that is reliable to enable them evaluate the credit worthiness of the borrowers. The desire to set up CRB services in the market emerge due to information disparity or asymmetry between the participants in the credit contract.

The problem of multiple loans and over indebtedness increases when financial lenders compete for customers on the credit market thus increasing the risk of loan defaulting in the process. The CRB plays a pivotal role in cost reduction by improving creditors ability

to sort and set side borrowers with bad credit records (Psillakiet et al, 2010). The policies, rules and laws controlling banking industry CRB licensing, running and overseeing in Kenya, the Banking CRB regulations, 2008 (hereafter referred to as "Regulations"), were gazetted in the year 2008, July and became operational 02/02/2009. Since then, CBK has licensed two CRBs; Africa CRB -licensed 2010 February while Metropole CRB -licensed April, 2011.

The Regulations mandate the entire commercial banking entities as well as the (DPFB) (Deposit Protection Fund Board) accessing and share customer negative data records via the CRBs. A survey conducted by FSD Kenya on the progress made in credit information sharing in Kenya, between 2008 and 2011, made two important findings. First, an approximate of about 5 million clients possess formal credit terms and agreements from financial organizations with accounts distributed as follows: banks and SACCOs have 2,000,000 (42 %) and 1,875,000 (40 %) accounts respectively, whilst deposit-taking microfinance institutions have 650,000 (14 %) accounts. Other institutions are said to have 200,000 accounts (4 %). The second finding of the survey was that; currently, credit information shared nears 200,000 clients with accounts that are not operational or performing. The above statistics imply that CRBs are sharing negative credit information on about 4.3 percent of borrowers with formal sector credit agreements. The limited number of accounts that the sharing by commercial banks nets coupled with the fact that the nature of information shared is largely negative, illustrates the limited value of CRBs in managing credit risk, assessment of the borrowers' extent of debt commitment and building of credit histories for use as collateral.

2.3.1 Credit Reference Bureau and Risk Identification

According to Luoto (2001), CRB can be used to control default risks associated by client's decline or lack of ability to repay the loan fully and within the time frame given. The bank is able to maximize on the adjusted risk return rates through regulating risk within an acceptable limit so as to form a basis to understand and evaluation banks benefits and profits through effective management of risk, thanks to the CRB services. The empirical proof as found by Brown and Zehnder (2007) depicts that the credit market is likely to fall due to lack of institutions or firms that share information and credible banking institutions in the banking sector. Reduction in moral hazard as a result of information sharing is supported by the theory. The borrower's loan repayment records, lease payments, improve as creditors' uses the data from CRB institutions across the globe.

Credit risk can be referred to as the risk associated with the borrower failing to comply with the loan contract terms and agreements conditions. Loans form the leading cause of credit risk. Although this risk is ever present in all transactions in any financial entity, hence the need of a credible management unity to ensure stable operations. the outstanding tools and techniques to deal with this type of risk include collateral use, netting the credit against deposit accounts of the client, and guarantees (CBK, 2010). The Central Bank of Kenya, (2010) further notes that whereas the tools employed lower credit risk, others such as legal, operating, market, and liquidity risks emanate. Thus necessitating the need for financial entities to possess strict controls on processes and guidelines to eliminate or manage listed risks and incorporate them in organization policies and regulations.

The degree of loan recovery forms the basis of decisions on the customer's loan application by bank institutions. The applicants past credit records are key in establishing the loan recovery as a relationship exists between the past loan repayment and future. Banks realize the unbearableness of losses after occurring and financial sector commercialization, increased competition, and securitization underlines the two folds of using CRB as a tool of managing credit risk (Demirguc and Huzinga, 1999). A lender advancing loans looks forward to repayment of the principal amount plus interest. To mitigate the risk of default, lenders call for security which they can seize and realise as a last resort to recover full or partial payment of the advanced amount. Unsecured creditors, therefore, pose a relatively high risk compared to secured creditors (Demirguc and Huzinga, 1999). According to Holden (1985), notes that, the most important qualification for successful lending is the ability to judge the character and credit-worthiness of borrowers.

2.3.2   Credit Reference bureau and Rate of Credit Repayment

Epure and Lafuente, (2012) observe that all over the world, commercial banks face enormous risks of (NPLs). The behavior of borrowers is key for institution to eliminate the risks. The creation of (CRB) was the idea that emerged to aid financial entities to establish the credit worthiness of clients as an initiative to scrap risk of defaulting. According to Epure and Lafuente, (20120 CRB shares defaulting information of customers among the banks thus, helping them to shun such borrowers in an attempt to eliminate the default and credit risk. It allows commercial banks to share data, which play an important role to in information asymmetry decrease. The CRB reports assist commercial banks to eliminate malpractices in the sector by implementing stringent

terms and conditions on clients with bad credit history. The level of NPLs are reduced as banks add to the loan books.

According to Paroush (1999), argues that commercial banks plays a vital and efficient role in appealing to investors with excess funds to supply the funds to those with limited wealth and resources, promising compensation for their savings and deferred consumption, a fee that borrowers must shoulder in return for using the borrowed funds (Wong, 2002).

In the Kenyan perspective, CRBs facilitates quick and efficient decisions by financial lenders in disseminating funds and loan approvals. With regulatory basis in the country, such as the CRB banking regulation 2008 effected 02/02/2009, empowers the CRB to gather, monitor data on the customer's credit records. Individual's credit records provide the fundamental variables and inputs required for loan underwriting and enabling clients to move their loan history from one financial entity to another, promoting credit market competitiveness and affordability.

2.3.3   Credit Reference Bureau, Default Strategies, Risk Identification and Repayment

According to Gieseche (2004), credit risk refers to the financial loss distribution because on undesirable changes in one party's terms and agreements. He indicated that this risk is one that promises cash in-flows from financial instruments and loans under the custody of financial entities with are not guaranteed of full payment in the future. This creates the possibility of defaulting either in interest or principal payment thus amounting to financial losses to the entity.

Based on Greuning and Bratanavic (2003) viable and effective management and mitigation techniques are vital to eradicate default risk as this increases the firm's financial vulnerability. Collins and Wanjau, (2011) note that borrowers with higher default record are charged larger fees for borrowing (risk-based pricing practice). The following factors contribute to this: the purpose of the loan, credit scoring or ranking, and the loan to value ratio. The loan covenants are incorporated in the loan agreement terms to address the same issue.

According to Berger and Frame (2005), such covenants include requirements for borrowers to report from time to time their financial status, abstain dividend payment, share repurchase, limited access to loans. These actions negatively impact the financial position of the firm and may elicit the lender to demand full loan repayment due to varying in the person's wealth conditions, like ratio of loan coverage. In Kenya, as at 31st December 2012, the loans requested by both customers and banks accumulated to 2.3 million (banks) and 28,733 (customers). Stabilization of loan reports requested by banks in the year ended 31/12/2012 at 1,015,327 as contrasted to 1,021,717 reports the previous year. High use of credit reports are expected are aimed at reduction in data search costs and subsequently offer competitive terms of borrowing to customers with a good credit track record and ultimately reduce the level of NPLs (KCB, Bank Supervision Annual Report, 2012).

2.4   Summary of Knowledge Gaps

Based on literature review, the study notes that if mitigation of credit risk are inadequately handled, the respective commercial banks are subject to loosing financially,

increased capital recovery costs, and social role failure due to inability to provide loans to the society aiming at improving and boosting their living standards. Moreover, the study further notes that empirical evidence indicates that a number of studies relating credit reference among the commercial banks have been done in Africa but solid and up-to-date empirical evidence for loan default management strategies are very scanty and at times even lacking. The measurement for credit risk management often applied various research factors, according to the accurate services and goods provided by the bank to enables firms to compare before and after changes in establishing CRB management strategies on loan defaults in the Kenyan banking sector.

Table 2.1: Empirical studies summary

No.	Study	Method	Main Findings	Knowledge gap	Focus of current study
1	Consumers' Credit Card Usage attitude and intentions in an Advanced Developing Country. Kaynak, E. & Harcar,T. (2001).	Cross-sectional survey	Consumer welcomed Credit Card Usage as long as they gave them advantages and gave them positive credit ratings.	The study did not look at how credit reference bureau vetted credit card holders on risk identification against credit default among commercial banks.	The study will focus on CRB in risk identification against credit default among commercial banks.
2	Seven steps to fixing your credit report.Lewis,H. (2004).	Survey study	The research came up with several steps to fixing credit report.	In fixing credit reports the study did not exhaust the influence of CRB on the rate of credit repayment among banks.	The study will focus on CRB on the rate of credit repayment among commercial banks in Kenya.
3	Credit Risk and the Performance of Nigerian Banks. Kargi, H.S. (2011).	Cross-sectional survey	The study was able to identify the Credit Risk and the Performance of various Nigerian Banks.	In the process of the research, the study did not review CRB in complementing loan default management in Nigeria.	The CRB in complementing loan default management strategies among commercial banks in Kenya
4	Lewis, G. (2007). Essays on choice and matching under information asymmetry: PhD, thesis. Lewis,G. (2007).	Cross-sectional survey	This thesis studies asymmetric information in the context of two major corporate.	The essay on corporate takeovers investigates the role of asymmetric information in corporate takeovers.	The CRB in complementing loan default management strategies among commercial banks in Kenya
5	Credit Risk Transfer between Insurance, Banking and Other Financial Sectors. International Association of Insurance Supervisors (2003).	Cross-sectional survey	Although the paper Concludes that it is Very difficult to gather definitive global data on credit risk transfer transactions.	It appears that credit derivatives are only a relatively small proportion of insurers' investment activities, even though the industry.	The CRB in complementing loan default management strategies among commercial banks in Kenya

Source: Research (2018)

CHAPTER THREE

RESEARCH METHODOLOGY

3.1   Introduction

This particular chapter was able to study the important design, the samples of the population that was used in the research, the design of the samples and the different sizes, the instruments for collection of data, the techniques of collection and analysis of data, the consideration of the ethnical basis, the shortcomings of the research as well as its expected outcomes.

3.2   Research Design

The study adopted the descriptive survey design. Kombo and Tromp (2006), state that the major purpose of descriptive research is description of state of affairs as it exists. It is a method of collecting information by interviewing or administering a questionnaire to a sample of individuals. According to Orodho, (2003) when using this design the researcher ensured that: construct questions that solicited the desired information; identify the individuals that were surveyed; identify the means by which the survey was conducted; and summarize the data in a way that provides the designed descriptive information.

The research study utilized both qualitative and quantitative data, though this study had a slight bias towards qualitative data sources. It must be appreciated that qualitative research is founded on the measurement of quantity or amount. It is useful in research whereby data can be expressed in terms of numbers. Qualitative research on by contrast is concerned with data relating to or involving quality or kind. It is particularly useful in discovering underlying motives and desires of subjects (Kothari, 2004).

3.3   Target Population

A population is defined as a complete set of individuals, cases or objects with some common observable characteristics (Mugenda and Mugenda, 2003). Target population in statistics is the specific population about which information is desired, thus the inclusion criteria included all the registered commercial banks in Kenya according to Central Bank of Kenya Annual Supervision Report, (2018).

It should be noted that at the moment there are a total of about 44 publicly commercial banks, and thus the study target all the 44 banks for data collection, in the process 4 banks were used for the pilot study, 1 bank declined the research data collection exercise, and only 39 banks agreed to participant in the research process. This study picked on only one credit personnel per commercial bank. The proportion of the target population that has the characteristics to be measured constitutes the credit managers in charge who work in the headquarters of the respective banks. The category of this proportion was as shown follows;

African Banking Corporation, Bank of Africa, Bank of India, Barclays Bank of Kenya, Baroda Bank, CFC Stanbic Bank, Charterhouse Bank, Chase Bank, Citibank,

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Commercial Bank of Africa, Consolidated Bank of Kenya, Cooperative Bank, Credit Bank, Development Bank of Kenya, Diamond Trust Bank, Dubai Bank, Ecobank Kenya, Equatorial Commercial Bank, Equity Bank, Family Bank, Fidelity Bank, Fina Bank, First Community Bank, Giro Commercial Bank, Guardian Bank, Gulf African Bank, Habib A.G. Zurich, Habib Bank, I&M Bank, Imperial Bank, Jamii Bora Bank, Kenya Commercial Bank, K-Rep Bank, Middle East Bank, National Bank of Kenya, NIC Bank, Oriental Commercial Bank, Paramount Universal Bank, Prime Bank, Standard Chartered Bank, Trans-National Bank and UBA Bank Kenya.

3.4   Sample Design

This study used judgment sampling technique which is a non-probability method. The selected sample was based on judgment. The research targeted the entire sample from the population using census approach. With confidence the chosen sample was a true representative of the entire population. All credit commercial bank managers at the headquarters and credit reference bureau managers were utilized for the research.

3.5   Data Collection

The main method of data collection technique employed included questionnaire method for the credit managers from the respective banks and key informant interview for the credit officers from the respective credit reference bureau offices. The questionnaire consisted of a well-structured, both closed and open ended questionnaire and it comprised of the two sections. The part of the second section is much devoted to establish the impact of the credit reference bureau on the loan strategies and default, using the specific

case of all Kenyan commercial bank regulated by the Central Bank of Kenya. The questionnaire was able to help in collection of enough information. A pilot study was carried out on 4 banks to pre-test the research instrument before its actual administration. The interview will be done to Credit Reference Bureaus.

3.6   Data Analysis

In the data analysis, data was organized to ensure orderliness in research. On completion the data was organized,   received, coded, edited and tabulated to check accuracy, completeness and stored in an appropriate form. The data was stored in electronic form and paper form for the purpose of data analysis. The descriptive type of statistics is composed of the central tendency and the standard deviation. The frequency table was also part of the descriptive data. The regression analysis is one of the types of inferential statistics. The researcher will acquire a research permit. The researcher will also have an introduction letter from the University. The researcher will then administer the questionnaires to the respondents. An electronic spreadsheet will be used by the researcher to keep the date for the study. The descriptive data was used just to make a description of what exactly is going on in the research proposal. The finally obtained results was able to be presented in the form of frequency tables, and narration.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1   Introduction

This chapter presents data analysis and interpretations of the findings of the data collected from the respondents in trying to determine the influence of credit reference bureau on loan default strategies using a case of commercial banks in Kenya. The main method of collecting data was by use of questionnaire method to the credit managers from the respective banks and key informant interview to the credit officers from the respective credit reference bureau offices.

It should be appreciated that most of the final data analyzed was quantitative in nature and thus the data was quantitatively analyzed. Initially there are a total of about 44 publicly commercial banks, then 4 were used for the pilot study, 1 bank declined the research during the data collection exercise, and only 39 banks agreed to participant in the study.   The results of the findings were presented in the form of tables, pie charts and narrative. This study found that 37 out of 39 questionnaires that were administered were successfully filled and returned back. This represented 94 percent return rate, ensuring that the sample size remained as close to the original sample size as possible.

Campion (1993) suggested that authors need to make reasonable efforts to increase questionnaire return rates, address the influence of non-respondents, and that they do not contain any obvious biases. In order to increase the turn rate for this study, the

questionnaires were administered using the strategy described in chapter three of this study.

4.2   Demographic Information

The study sought demographic information, so as to establish the current statistical characteristics of the entire respondent in the study. The demographic information is crucial so as to clearly identify a group of people bound together by the sharing of common experience.

4.2.1   Gender of Respondents

Table 4.1: Gender of Respondents

Gender	Frequency	Percent (%)
Male	24	64.9
Female	13	35.1
Total	37	100.0

Source: Field data (2018)

Table 4.1 presents that 64.9 percent of the respondents were male while 35.1 percent were female, the number of males that responded was higher than that for female yet it is expected that the gender rule is applied in all organizations. This implies that there are factors that might have contributed to existence of more males than females in the banking sector.

4.2.2 Age of Respondents

Table 4.2: Age of Respondents

Age	Frequency	Percent (%)
30 years below	6	16.2
30-39 years	13	35.1
40-49 years	11	29.7
50-59 years	7	18.9
Total	37	100.0

Source: Field data (2018)

The ages were grouped into four classes with a difference of ten years apart, The Modal class being the ages between 30-39 which was represented by 35.1percentfollowed by 40-49percentwhich had a percentage of 29.7percent, 50-59 years had 18.9percentwhile those who were below 30 had 16.2 percent and this infers that generally the employees were well distributed in terms of age.

4.2.3 Years Worked at the Bank

Table 4.3: Years worked at the Bank

Years Worked	Frequency	Percent (%)
0-5 years	10	27.0
5-10 years	8	21.6
10-15 years	3	8.1
15-20 years	3	8.1
20 & above years	13	35.1
Total	37	100.0

Source: Field data (2018)

The table 4.3 presents the years worked by the employees at the bank, it was established that 35.1 percent had worked at the cooperation for more than 20 years, the years worked by the employees was useful it gave out information that could be considered as relevant for this study.

4.2.4 Level of Education

Table 4.4: Highest Level Education

Level of Education	Frequency	Percent (%)
Secondary	2	5.4
Tertiary College	12	32.4
Undergraduate	14	37.8
Postgraduate	9	24.3
Total	37	100.0

Source: Field data (2018)

Table 4.4 presents that about 37.8% of the respondents had attained a university degree at graduate level, 32.4% had tertiary college education, and 24.3% of the respondents had attained postgraduate level of education while 5.4% had secondary education. At face value, this implied that the more a person is educated the more retaining them is hard unless they are motivated and working in environment that encourages growth, education gives them a more bargaining power hence they can always look for better paying jobs incase need be ,this is unlike when ones levels of education are not high they may be constrained in a job because they are not sure of other opportunities, this implication prompted the researcher to further establish if there was a relationship between years

worked and levels of education, a correlation analysis was performed to establish the relationship, this was then presented as follows.

It should be appreciated that at a significance level of 0.005,(5%) the Pearson correlation between years worked at the corporation and highest level of education is -0.390. This is a weak negative correlation implying that there is no significant relationship between years worked and levels of education.

4.3 The role of CRB in risk identification against default risk rate among banks

The respondents were asked to rate various components on the role of CRB in risk identification against default risk rate among selected Kenyan commercial banks.

4.3.1 "Role of CRB

Respondents rate CRB on a five point Likert summated rating scale. Range was strongly agree (5) to strongly disagree (1). The scores of strongly disagree and disagree were taken to represent a component that had an impact to a Small Extent (S.E) equivalent to a mean score of 0 to 2.5 on a continuous summated Likert scale; ($0\leq$ S.E$\leq$ 2.4). Scores of neutral were taken to represent a component that had an impact of a Moderate Extent (M.E) equivalent to a mean score of 2.5 to 3.4 on the continuous summated Likert scale: (2.5$\leq$M.E$\leq$ 3.4). The scores for both agree and strongly agree were taken to represent a component which had an impact to a Large Extent (L.E) equivalent to a mean score of 3.5 to 5 on a continuous summated Likert scale; (3.5$\leq$ L.E$\leq$ 5.0).The study found out all

the respondents (100%) had a large access to credit information from the credit information bureaus.

4.3.2 Access to CRB

The study found that all the respondents 37 (100%) accessed credit information from the credit information bureaus through the mode of subscribing. This is an indication that the two banks have joined other member banks to share credit information through subscribing to CRB.

4.3.3 Credit Reporting systems and risk identification

It should be noted that some of the issues arising included the fact that many other players, does not allow more complete credit profile of a consumer to be drawn hence causing a serious challenge to effective credit information sharing. The found that out of total respondents, (54%) strongly agreed while (40%) agreed and (6%) were neutral that lack of Comprehensive Credit Reporting systems that include many other players, does not allow more complete credit profile of a consumer to be drawn causing a serious challenge to effective risk information sharing.

4.4 The effect of CRB on the rate of credit repayment among banks

The study sought to establish the Effectiveness of Credit Information Sharing, so as to establish the for sure if Effective credit information sharing has led to increase of the bank's market share, has led to growth in profitability, has helped shape the lending policy, if it has helped the bank to positively shape its business model and finally if Effective credit information sharing has helped banks to shape its competitive structure in the credit market. This information was important to the study because Effective credit

information sharing allows credit providers to submit accurate and verifiable borrower information to a CRB so that it can be shared with other credit providers, in the process enabling credit provider to understand borrower's loans track record.

4.4.1 Effective credit information sharing has led to increase of the bank's market share

Figure 4.1: Effectiveness of Credit Information Sharing to bank market share

EFFECTIVE CREDIT SHARING TO MARKET SHARE VALUE

0% — 12% — 4% — 34% — 50%

- Strongly Disagree
- Disagree
- Neutral
- Agree
- Strongly Agree
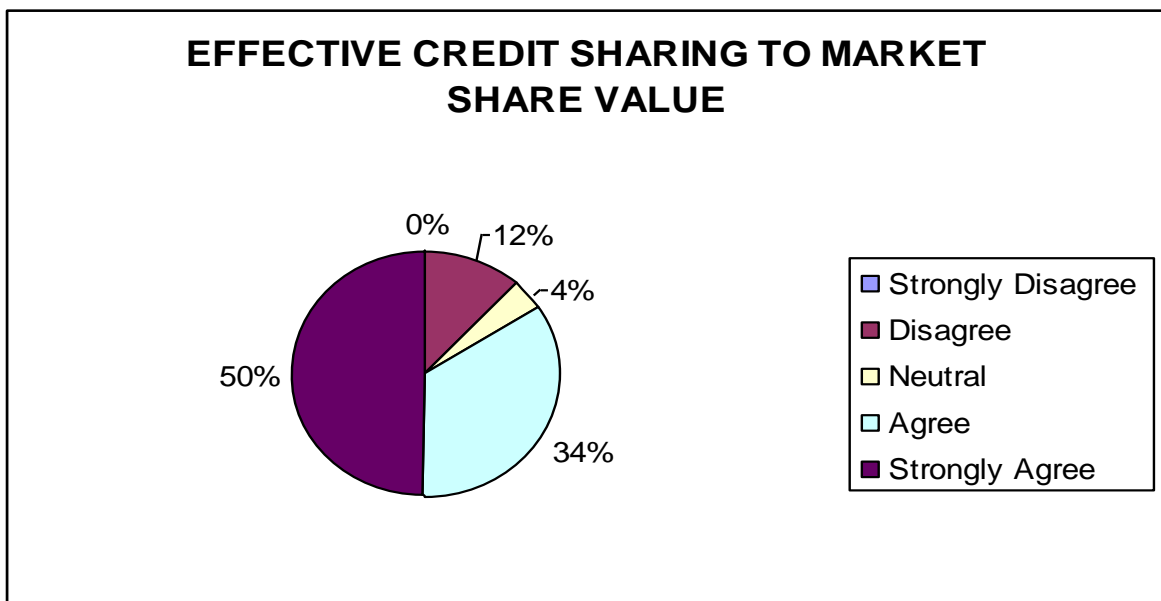
Source: Field data (2018)

The pie chart Figure 4.1 presents at least (50%) of the entire respondent strongly agreed that credit information sharing lead to an increase of the bank's market share. This is an indication that the banks have been able to increase market share through sharing of credit information hence able to lead to good clients who continue to generate more income through the interest income thus increasing market share.

4.4.2 Effective credit information sharing has led to growth in profitability

The study found that majority of the respondents strongly agreed and some respondents agreed respectively, that effective credit information sharing has led to growth in profitability of the banks. Credit information sharing has so far facilitated the building of information capital that will guide the pricing of loans by financial institutions; banks are now able to price loans with vastly enhanced information set as compared to the current situation in the past.

4.4.3 Effective credit information sharing has helped shape the lending policy

Table 4.5: Effective credit information sharing on lending policy

Response	Frequency	Percentage (%)
Strongly Disagree	0	0
Disagree	0	0
Neutral	0	0
Agree	0	0
Strongly Agree	37	100
Total	**37**	**100**

Source: Field data (2018)

Table 4.5 presents the findings that out of a total of 37 (100%) respondent, the majority strongly agreed that effective credit information sharing on lending policy of the bank. This is an indication that the introduction of credit information sharing in Kenya has shaped the lending policy thus banks able to adhere to the lending terms beyond the CAMPARI principles of lending by sharing customers history.

4.4.3 Effective credit information sharing has helped the bank to shape its business model

This study shows that all the respondents agreed that effective credit information sharing has helped the bank to positively shape its business model. This shows that effective credit information sharing among banks have enabled banks to shape up business model by sharing information in a large market of information pull which reduces the cost of exchanging information making returns high.

4.5   The influence of CRB on loan default strategies among Kenyan commercial banks

The study was keen to ascertain the influence of presence of Credit Reference Bureaus. This was important because as players in Credit Information Sharing - information brokers provide creditors with reliable, relevant and comprehensive data on the repayment habits and current debt of their credit applicants. The study aimed to prove if really Effective credit information sharing at the banks has been made possible due to the presence of Credit Information Bureaus, to know the impact on the extent of effectiveness of credit information sharing on the banking industry in Kenya and on the reduction in non-performing loans as a result of credit information sharing..

4.5.1 Effective credit information sharing at both banks has been made possible due to the presence of Credit Information Bureaus

This is a clear revelation that under reciprocity agreements, credit bureaus obtain data from creditors and other sources, consolidate and package information into individual

reports, and distribute it to creditors for a fee. The population covered by credit bureaus is mostly the middle to lower income segments of the population.

Figure 4.2: Credit Reference Bureau Presence
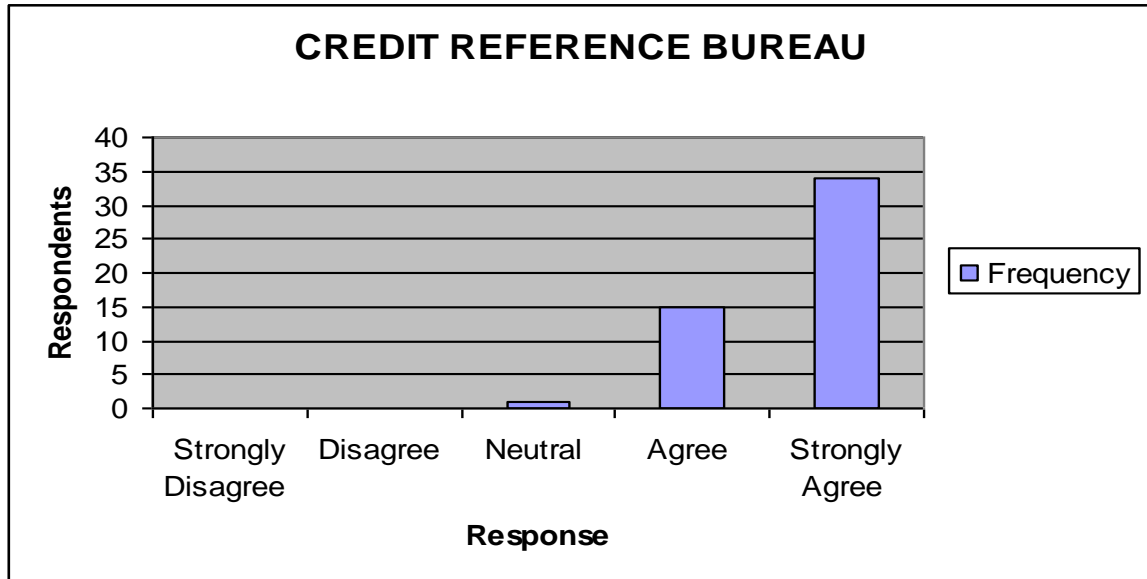
Source: Filed data (2018)

Figure 4.2 presents the majority of the entire (37) respondent interviewed, strongly agreed that effective credit information sharing at both banks has been made possible due to the presence of Credit Information Bureaus.

4.5.2   Credit Reference Bureaus have had an impact on the extent of effectiveness of credit information sharing on the banking industry in Kenya

This is a clear indication of the benefits of the Credit Reference Bureau in enhancing the extent of effective credit information sharing. In addition these CRB have expanded access to credit by allowing creditors to differentiate good and bad credit risks; lower the cost of borrowing to good risks by increasing competition; and , created a credit culture

as borrowers become aware that the market rewards and sanctions them based on their repayment history.

Figure 4.3: Credit Reference Bureau's impact on effectiveness
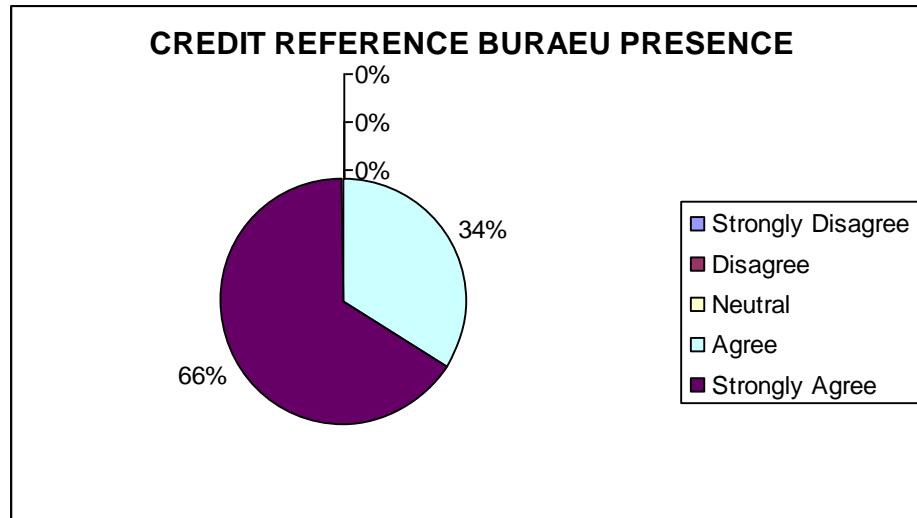
Source: Field data (2018)

Figure 4.3 presents that (66%) strongly agreed while respondents (34%) agreed that having Credit Reference Bureaus had an impact on the extent of effectiveness of credit information sharing on the banking industry in Kenya.

4.5.3 The presence of Credit Reference Bureaus has led to a great reduction in non-performing loans as a result of credit information sharing at the bank

The frequency that out of 37 (100%) total respondents, most strongly agreed that the presence of Credit Reference Bureaus has led to a great reduction in non-performing loans as a result of credit information sharing at the bank. CRBs help lenders make faster and more accurate credit decisions. They collect, manage and disseminate customer information to lenders with in a provided regulatory framework. Credit histories not only

provide necessary input for credit underwriting, but also allow borrowers to take their credit history from one financial institution to another, thereby making lending markets more competitive and, in the end, more affordable.

4.5.4 The presence of Credit Reference Bureaus has helped to positively shape the banks

This study found that all the respondents 37 (100%) strongly agreed that the presence of Credit Reference Bureaus has helped to positively shape the banks' lending policy. Banks play a central role in extending financial services within an economy. In support of this role, credit bureaus help lenders make faster and more accurate credit decisions.

4.6 CRB Effectiveness on Credit Information Sharing in Commercial Banks

In the process of trying to establish the influence of credit reference bureau on loan default strategies using a case of commercial banks listed in Kenya data collection was undertaken, key informant interview for the credit officers from the respective credit reference bureau offices.

4.6.1 Balance risk identification and client privacy

The balance between strict consumer privacy is a huge impediment to effective credit information sharing in the financial industry. This study found that majority of the respondents were in agreement, (44%) strongly agreed and (40%) agreed while (6%) neutral and (8%) strongly disagreed.

4.6.2 Setbacks of CRB on the rate of credit repayment

This informant guide pointed out that CRB faced some challenges in the process of trying to review effect of CRB on the rate of credit repayment. This study thus concludes that

entire respondents, most (48%) were in agreement, (46%) strongly agreed while (6%) strongly disagreed, hat unethical business practices was a setback to effective credit sharing.

4.6.3 Creating consumer awareness

Creating consumer awareness has been as a way to spreading effective credit information sharing. This study found that the majority of the respondents (58%) were in agreement that creating consumer awareness was a way to mitigate credit information sharing challenges.

4.6.4 Effective of the CRB on loan default strategies using a case of commercial banks

Effective legislation that addresses all aspects of credit bureau operations, data management and consumer protection, will be a major boost to credit information sharing in the financial sector and results showed that all the respondents (37) were in agreement that creating effective legislation that addresses all aspects of credit bureau operations, data management and consumer protection will be a major boost to credit information sharing in the financial sector.

4.7 Discussion of results

4.7.1   The role of CRB in risk identification against default risk rate among banks

In regards to this objective the study found that both banks have embraced the introduction of credit information sharing and thus for lending to take place due diligence has to be done through sharing of information through the Credit Bureaus. This is align

with a study by Epure & Lafuente, (2012) who found that it is important credit bureaus assist in making credit accessible to more people, and enabling lenders and businesses reduce risk, fraud and reduction in non-performing loans

The majority of respondents to large extent accessed the credit information which means that for all their lending due diligence is crucial not only through CAMPARI but also the borrower history which is accessed through the Bureau. The mode commonly used by most of the respondent is through subscribing to the Bureaus and therefore controls have to be put in place by assigning the senior credit managers with the responsibilities.

4.7.2   The effect of CRB on the rate of credit repayment among commercial banks

It is important to appreciate that this study found that pertaining the rate of credit repayment among commercial banks. Customer privacy, the lack of privacy may reduce the development of intimacy and trust in the bank-customer relationship and business competition in the process may hamper the effectiveness of credit information sharing. This conclusion is in agreement with a similar one found by Marquez *et al.*, (2003) who stated generally that, increased customer privacy and bank competition gradually inhibits the effectiveness of credit information sharing.. More so it was noted that sharing of information has led to growth in profitability, this is due to advancing credit to good borrowers who will service the loans without delinquencies and to the bank continue earning more interest income. The cost of lending is reduced and volume of lending increases. Further it was noted that credit information sharing has shaped the business model for banks by having quality loans portfolios which in-turn reduce default rate. Improved information flow has increased the efficiency and stability of financial systems.

It was interesting to find out that most of the respondent during this research study indicated that lack of privacy did not reduce the development of intimacy and trust in the bank-customer relationship and hence not reducing the effectiveness of CIS. This is probably because privacy in relation to credit information sharing is substantiated in the legal frame work to the extent of the information to be shared and by the end of the day is to benefits both the customers and the bank., Moreover in regard to lack of privacy vis-a-vis fundamental rights of the customers most of the respondent indicated that it didn't reduce the effectiveness of credit this is so because the customer has a right to know the information being shared from his/her bank and safeguard good reputation by having good credit history.

It was evidenced in the course of the reach study that credit Reference Bureau has played a great role in effective credit information sharing. In far and large CRB has contributed to reduction of NPLs this is because once the lending officers subscribes and finds out a delinquency or default they escalate the same to the borrower who due to reputation risks settles the loan in default for future good record. This have seen most of the banks NPLs being paid up and upon issuance of a clearance letter by the previous lender the clients are able to continue accessing loans, However the scores for such customers would be low which would guide the lending officer the much to advance and the interest rates. as evidenced from 100 percent of the respondents said Credit Reference Bureau has helped to positively shape the banks' lending policy by reducing asymmetry in the information assisting the banks to identify those borrowers who are overextended and avoid them

since they may be unable to pay; conversely identify clients with good credit profiles and potentially increasing lending offers.

4.7.3 The influence of CRB on loan default strategies among commercial banks

This study found that it is a clear indication of the benefits of the Credit Reference Bureau in enhancing the extent of effective credit information sharing on loan default strategies among commercial banks. In addition these CRB have expanded access to credit by allowing creditors to differentiate good and bad credit risks; lower the cost of borrowing to good risks by increasing competition; and, created a credit culture as borrowers become aware that the market rewards and sanctions them based on their repayment history. According to Ahmad and Ariff, (2007) credit histories not only provide necessary input for credit underwriting, but also allow borrowers to take their credit history from one financial institution to another, thereby making lending markets more competitive and, in the end, more affordable. The majority of the respondent 94 percent of the respondents felt that business ethics play a major role in enhancing effectiveness of credit information sharing, thus a bank has to adhere to the laid down rules by the CBK to be able to share the information with other banks. This is in terms of down grading their loan portfolios as per the CBK guidelines and able to identify the defaulters and forwarding the reports to the CRB. As pertains virtues of honesty and integrity which are key in business ethics any shortfall lenders ineffective credit information sharing thus the banks have a duty to uphold banking ethics.

In regard to challenges to effectiveness of Credit Information Sharing majority of the respondent felt that a more comprehensive Credit Reporting system is critical. These

include collecting information from banks, MFI, Insurance and utility companies and share both positive information. Lack of it does not allow more complete credit profile of consumer to be drawn causing a serious challenge to effective information sharing. Its paramount to note that strict consumer privacy has been highlighted as a huge impediment to effective credit information sharing, therefore with the emerging of more comprehensive reporting systems the institutions need to relax the rule of customer privacy so that they are able to provide necessary information to be shared. Another major challenge which scored highly from the respondent is presence of unethical business practices continue to hinder effectiveness of credit sharing since no bureau will be in a position to collect data from such businesses hence a lapse in sharing information.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1   Introduction

This chapter attempted to give summary; conclusion and recommendations related to the study findings 60determine the influence of credit reference bureau on loan default strategies using a case of commercial banks listed in Kenya.

5.2 Summary of the Study

In spite of the gains and benefits made in Kenya since the inception of credit information sharing, there are some factors that still hinder the smooth running of credit information sharing in banks.This study found that the position held in the department by the respondents indicated that majority (54%) of respondents were assistant credit mangers while very few (2%) were credit officers. Figure 3 showed that the respondents access to credit information, the largest group being the Credit managers (45) followed by Assistant Credit mangers (4) and finally Branch manager (1) respectively.

Credit Reference Bureau presence found that majority of the entire respondent interviewed, (37) strongly agreed that effective credit information sharing at both banks has been made possible due to the presence of Credit Information Bureaus. In regard to business ethics, it was found that lack of business ethics compromises the bank's standards and norms reducing effectiveness of credit information sharing. On business ethics the study also that of the entire 50 (100%) respondents, most (48%) were in agreement, (46%) strongly agreed while 3 (6%) strongly disagreed that unethical business practices are emerging as an setback to effective credit sharing.

5.3 Conclusion of the Study

This study notes that regarding the extent of effectiveness of credit information sharing on the banking industry in Kenya, the study found that thus far credit information has been effective, but it can be concluded that it is effective but only to a small scale to date. This conclusion is supported by the fact that Credit Reference Bureaus had an impact on the extent of effectiveness of credit information sharing on the banking industry in Kenya as was agreed by many respondents. This conclusion has been supported by Central Bank Kenya, (2010) who stated that as per the years 2010 / 2011a total of 1,306,439 and 6,041 credit reports have so far been accessed by banks and bank customers respectively from the two licensed credit reference bureaus. This translates to a monthly average of 76,849 and 355 credit reports for banks and bank customers respectively and thus this uptake of credit referencing is quite encouraging, it shows effectiveness of credit information sharing and it will be a pillar of growth in the Kenyan financial sector. These effects have two direct consequences. First, intermediaries compete more aggressively because the reduction in private information for each bank implies that their competitors suffer less from adverse-selection problems. Second, however, less information production means that banks are more prone to make errors in their lending decisions as competition intensifies.

The study also further concludes that Credit Reference Bureaus had an impact on the extent of effectiveness of credit information sharing on the banking industry in Kenya. It was evidenced that despite the presence of challenges hindering effectiveness of information sharing the respondents noted some mitigating factors like creation of

consumer awareness as a way of promoting credit information sharing. This is by ensuring both lenders and borrowers are sensitized on the merit of a robust CIS mechanism and are able to use it to their advantage.

On the challenges to the effectiveness of credit information sharing on the banking industry in Kenya – the study concluded that indeed that lack of Comprehensive Credit Reporting systems that include many other players, does not allow more complete credit profile of a consumer to be drawn causing a serious challenge to effective information sharing. The study also concludes that unethical business practices were a major challenge when it came to effective credit information sharing. The research further concluded that information sharing does not constitute a genuine moral violation of privacy since the information disclosed by banks is well defined by the law governing credit information sharing

5.4   Recommendations of the Study

Base on the findings, the recommendations would be as follows;

1. In the process of managing loan defaults, this study recommends the registration of more Credit Reference Bureaus by the relevant authorities, because of diversity of Credit information.

2. The education and public awareness on the importance of credit information sharing in the financial industry and its benefits to all the prospective clients.

3. The merging of all the credit information sharing system to include many other key players. The banks through their association should spearhead education of

stakeholders about credit information sharing and the benefits thereof is a critical success factor, and keep the design of the system simple.

4. Appropriate technological solution and responsiveness should be applied in the influence of credit reference bureau on loan default strategies using a case of commercial banks in Kenya.

5.5 Limitations of the Study

The study information was limited to only two banks which are among the few banks that are among member banks, therefore the research information could be biased to the experiences only of the sampled banks and the two bureaus. The researcher would recommend a similar extensive research study on other banks.

5.6 Areas suggested for further research

1. Credit information and the youths

2. Credit sharing and the emerging businesses

3. Credit and the cost of business in Kenya

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APPENDICES

Appendices 1: Letter of Introduction

UNIVERSITY OF NAIROBI

SCHOOL OF BUSINESS

Telephone: 020-2059162	P.O. Box 30197
Telegrams: "Varsity", Nairobi	Nairobi, Kenya
Telex: 22095 Varsity	

DATE.....21.11.2018

TO WHOM IT MAY CONCERN

The bearer of this letter ... FERDINAND MALIACHI MUHANDA

Registration No........D61/71656/2008...........................

is a bona fide continuing student in the Master of Business Administration (MBA) degree program in this University.

He/she is required to submit as part of his/her coursework assessment a research project report on a management problem. We would like the students to do their projects on real problems affecting firms in Kenya. We would, therefore, appreciate your assistance to enable him/her collect data in your organization.

The results of the report will be used solely for academic purposes and a copy of the same will be availed to the interviewed organizations on request.

Thank you.

0 2 NOV 2018

PROF. JAMES M. NJIHIA
DEAN, SCHOOL OF BUSINESS

Appendices 2: Structured Questionnaire

Introduction

My name is **Ferdinand Maliachi Muhanda** I am a student at University of Nairobi. I am carrying out a research to establish the influence of credit reference bureau on loan default strategies, using the case of selected commercial banks in Kenya. Kindly answer all the questions as truthfully as possible. Kindly complete the following questionnaire with specific regard to the above enquiry, by placing a (tick) in the box. In addition, please write any further comments in the spaces provided.

A. Personal Information

1. Name of the organization (Optional)……………….…………………………………..

2. In which department do you work…………………….…………………………………

3. For how long has this bank been in operation in Kenya and when was it registered as a commercial
bank?………………..

4.To which CRB does your bank forward its customer's credit
information...
....

5. How many CRB inquiries do you make per month
……...
....……………………

B. Influence of CRB on the Rate of Credit Repayment

6. Does your banks forward credit histories of its customers to CRB?

Yes ☐

No ☐

Which report do you forward

……………………………………………………………………………………………

……………………………………………………………………………………………

7. How many loan applications are approved based on CRB report in your organization?

……………………………...……………………

8. Do your customers sometimes fail to meet the terms of any contract with your bank?

Yes ☐

No ☐

Why……………………………………………………………………………………

……………………………………………………………………………………………

…..

9. Which one of these techniques for managing credit risk is used in your bank?
   a) Collateral ☐
   b) Guarantees ☐
   c) Netting off of loans ☐

10. Which risk have you encountered in your bank? (Can tick more than one)
   a) Legal ☐
   b) Operational ☐

c) Liquidity ☐

d) Market risks ☐

Others specify …………………………………………………..……………

13. Does CRB report reduce credit risk rates?

Yes ☐

No ☐

How……………………………………………………..………………………

……………………………………………………………………………………

C. Effects of CBR on Rate of Loan Repayment

16. Has your bank experienced decrease in non-performing loans since the inception of CRB

Yes ☐

No ☐

If Yes by which percentage………………

If No by which percentage…………………

17. Is CRB report appropriate in managing potential loan default.

Yes ☐

No ☐

How…………………………………………………………………………………………………

……………………………………………………………………………………………………

.

18. Apart from CRB report which other ways does your financial institution determine customer

    a) Character   ☐

    b) Capacity   ☐

    c) Condition   ☐

    d) Source of income   ☐

    e) Collateral   ☐

19. Do you use a credit reports to establish customers repayment behaviour.

Yes   ☐

No   ☐

How…………………………………………………………………………………………………

……..………………………………………………………………………………………………

D. CRB in complementing loan default strategies

22. Does CRB lead to increased access to credit in your Bank?

Yes ☐

No ☐

Why…………………………………………………………………………………………

…

23. Does high financial cost of borrowing reduce borrower's repayment capacity in your bank?

Yes ☐

No ☐

How……………………………………………………………………………………………

.

……………………………………………………………………………………………………

24. Respond with Strongly Agree (SA) Agree (A) Neutral (N) , disagree (SD) and Strongly Disagree

Question	SA	A	N	SD	D
CRB prevent serial loan defaulters from accessing credits from commercial banks.					
CRB provides reliable and inexpensive system to exchange information on the character and ability to pay of borrowers.					
CRB has reduced cases of multiple borrowing.					
CRB offers commercial access to databases that capture relevant aspects of clients' borrowing					

behaviour					
CRB strive to provide credit reports with information that is relevant, complete, accurate and recent.					
CRB incorporate credit investigation and background checks.					
CRB provision of up to date borrower credit information has significantly reduced cases of nonperforming loans.					

Appendices 3: Focus Group Discussion

The discussion and filling in instructions

Please complete the following questionnaire with specific regard to the above enquiry, by placing a cross (X) in the box. Please write any further comments in the spaces provided.

Credit Reference Bureau

1. Description of the Credit Reference Bureau
   a) A group of banks ☐
   b) A group of other financial intermediaries ☐
   c) Individual shareholders ☐
   d) Foreign owned ☐

2. Who uses a credit reference bureau?
   a) Financial institutions ☐
   b) Insurance ☐
   c) Utility companies ☐
   d) Others specify …………………………..

3. What is the role of CRB in risk identification against credit default among commercial banks in Kenya?

4. What is the influence of CRB on the rate of credit repayment in selected commercial banks in Kenya?

5. What is the contribution of CRB in effective loan default strategies among commercial banks in Kenya?

6. Other comments.

END