REASONS WHY BANK CUSTOMERS FAIL TO SERVICE THEIR LOANS IN KENYA: A DATA SURVEY OF STANDARD CHARTERED BANK (K) LTD

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BY

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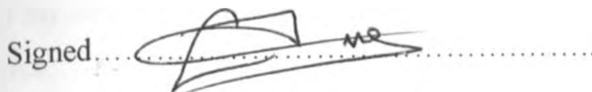
DECLARATION

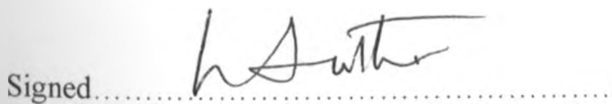
This project is my original work and it has not been submitted for a degree in any other university.



Signed.. Date 08/10/2003..............................

Roche Charles Juma

This project has been submitted for examination with my approval as the university supervisor.



Signed.. Date 8th Oct 2003..............................

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DEDICATION

To my best friend and beloved wife, Emmy and our greatest gift and source of happiness, Mike.

ACKNOWLEDGEMENT

Honour and glory to my Almighty God and saviour Jesus Christ for granting me this opportunity.

Thanks to my wife Emmy for the patience, moral and material support without forgetting our dear son Mike.

I also appreciate my parents, Margaret and Michael for showing me the importance of education and more so encouragement from my brothers Joseph, George, Ben, Jared and my only sister Gaudencia for their prayers.

Thanks to my only sister-in-law, Philly for helping in typing most of my work, my brother-in-law, Eddie besides Mr. and Mrs. Oscar, without forgetting my friends and colleaques for their support and prayers.

Last but not least Iam grateful to my supervisor Mr. Otieno Luther, for developing my mind into this subject and his continuous support on the same.

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ABSTRACT

This study sets out to determine to what extent do other factors other than interest rate contribute to the problem of Non-performing Loans (NPLs) in commercial banks in Kenya. Kenyan banks suffer from serious financial fragility manifested by high proportions of Non-Performing Loans (NPLs). In this paper, the research considered Standard Chartered Bank (K) Limited and segmentation of the branches were done into two regions, Nairobi and upcountry branches. To rank the factors that cause loan default, statistical measures such as the mean, mode and standard deviation were used.

Non-performing Loans (NPLs) in commercial banks were found to be caused by various reasons other than the much-assumed factor of high interest rate such as: diversion of funds, economical decline, loss of job, multiple banking, poor management, operation and system errors, illness, disasters, politics, competition, lack of knowledge, death, take over, treasury bill rate, conflict with the law, dissolution, base lending rate, bankruptcy, breach of contract, KRA interference, poor monitoring and control slow and unmoving stock. The findings show that the most predominant cause of loans default is the diversion of funds followed by the poor state of the economy while the least are poor monitoring and control and KRA interference.

This study recommends that the commercial banks need to take into consideration all the factors that cause loan defaults and besides this, they should find out ways of protecting themselves against such factors. They need to train all their staff on the basic principles of credit and should take a bold step in implementing Know Your Customer (KYC) project.

Further research should be done in this area and should incorporate concrete solutions in reducing the incidences of non-performing loans in the commercial banks books. An inter-banks study should be carried out to determine which bank is prevalent to the problem. This study may be carried out annually to determine whether the solutions suggested are effective and if not so, what can be done to alleviate the problem.

CHAPTER ONE

INTRODUCTION

1.1 Background:

To start off this paper, there is need to understand what is meant by the term credit. Therefore, credit is the delivery of money, goods or services today in exchange for promise to pay in the future. Credit also is a reflection of the customer and a lender's offer of credit is an expression of trust in the client. It is important to note that before a commercial bank lends to a customer, the ability to repay must be matched by the ability to borrow. In case the promise of paying in future is not honoured then the issue Non-Performing Loans (NPLs) crops up

The question of Non-Performing Loans (NPLs) is an ordeal to commercial bank managers in Kenya. This is because Non-Performing Loans (NPLs) impact adversely on bank's profitability. Bank's profitability is an important indicator of bank's performance that indicates the rate of return a bank has been able to generate from using the resources at its command in order to produce and sell services. A glance at the commercial banks' financial reports and more specifically the profit and loss and balance sheet show the magnitude of Non-Performing Loans (NPLs) and the provisions for the same, which are junks of losses to the commercial banks.

According to Neuberger (1998), a financial system consists of institutional arrangement designed to transform savings into investments. These arrangements are determined by legal rules concerning the design of financial instruments and the regulation of banks, but also by banking practices and social customs which affect the relationship between banks and their borrowers. A bank-oriented system as prevalent in Kenya is characterized by

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long term relationships between banks and firms. This imply bank interests in firms and cross-selling activities of banks as the supplier of credit. A bank is expected to 'lean against the wind' and accommodate its debtors during difficult financial times. Such flexibility is not available in an anonymous security market.

In any banking system, the bad loans problem consists of a stock component, old debt that is not performing, and a flow component, new lending that may become non-performing. The two components are linked by the normal client relationship in banking and in some countries, by the government's encouragement or even directing State-Owned Enterprises (SOEs). New lending to a client with non-performing old debt is likely to become a bad loan. Government encouraged loans to SOEs that are chronic loss-makers are likely to be non-performing, Bonin and Huang (2001). Both aspects must be considered in designing policy for bad loans in Kenya.

Furthermore Non-Performing Loans (NPLs) is a source of credit risk that is the probability that some of bank's assets, particularly its loans, will decline in value and become worthless or generate returns below the required level. On examination of financial statements of a majority of commercial banks, one notices substantial amount listed as losses on loans and advances to customers. What is not clear is the specific circumstances that make it difficult for borrowers to service their debts. The popular belief is that the commercial banks have been charging exorbitant interest rates on the amounts they advance. The effect of this assumption is that other factors that could have contributed to non-servicing of advances are ignored.

1.2 The magnitude of Non-performing Loans (NPLs):

The quality of assets, measured by the share of Non-Performing Loans (NPLs) to total loans remained poor in the year to May 2003, declining marginally to 29.4 percent from 29.8 percent in May 2002, Kenya Monthly Economic Review (June, 2003).

Non-Performing Loans (NPLs) & Provisions (Ksh Bn):

1	Total Advances	244.3	252.2
2	Specific Provisions	27.7	32.7
3	General Provisions	2.6	2.5
4	Total Provisions (2+3)	30.3	35.2
5	Net Advances (1-4)	214.0	217.0
6	Total Non-Performing Loans (NPLs)	72.9	74.1
7	Net Non-Performing Loans (6-2)	45.2	41.4
8	Value of Securities (estimated)	37.2	34.6
9	Net Exposure (7-8)	8.0	6.8
10	Total NPLs as % of total Loans (6/1)	29.8	29.4
11	Total Provisions as % of total loans (4/1)	12.4	14.0
12	Exposure as % of total loans (9/1)	3.3	2.7

Source: Central Bank of Kenya.

1.3 INTERNATIONAL EXPERIENCES WITH BAD-DEBT WORKOUT:

Klingebiel (1999) considers the experiences of several countries in setting up centralized asset management companies both to deal with NPLs and to resolve solvency problems of distressed financial institutions. Two types of agencies are identified: rapid asset disposition agencies and longer term restructuring agencies. Of the seven case considered, four are in the former category. Of these, only the U.S. Resolution Trust Company (RTC) has been wound up. Klingebiel concludes that the asset management agencies hid the extent of the bad loan problem and prolonged the effective resolution of the banking crisis.

The Resolution Trust Company in the United States

The Resolution Trust Company (RTC) was set up as a rapid asset disposal agency in 1989 to resolve bad loans from the portfolios of failed Savings and Loan Associations (S&Ls). As part of a public agency, the RTC had several objectives: to maximize the net revenues from the sale of transferred assets, to minimizing the impact on local real estate markets and financial markets and to maximize available and affordable housing for low-income individuals. According to Klingebiel (1999), several unfavorable factors influenced the RTC's operations. First, sporadic government funding increased resolution costs. Second, rapid asset disposal was hampered by inconsistent multiple objectives. On the other hand, several favorable factors were identified. First, the amount of assets transferred was a relatively small percentage of overall financial assets and many of these were performing at the time. Second, the assets could be bundled and securitized for quick sale in deep capital markets. Third, the RTC was able to contract out the disposal of assets to private sector agents having the necessary skills and expertise.

Bank restructuring in Central Europe

The experiences of the fast-track Central European (CE) countries, i.e., the Czech Republic, Hungary and Poland, with bank insolvency and bad loans provide a list of more don'ts than do's. Furthermore, at the beginning of the banking reform in 1990 in then Czechoslovakia, all of the working capital of SOEs was funded by short-term, low-interest, revolving bank credit referred to as TOZ loans. A centralized hospital bank, Konsolidacni Banka (KnB), was created for restructuring these loans on commercial terms. All TOZ loans were transferred along with a comparable amount of enterprise deposits from the other banks. However, the SOE clients remained with their parent banks that provided banking services and new loans. In several stages, other loans classified as bad were transferred from the largest Czech banks to Konsolidacni Banka (KnB) for work out and the government recapitalized the parent banks. Although

considered appropriate at the time, the Czech solution failed to insure the strength of the domestic banking system.

What went wrong? The incentive (flow) problem was not solved as the banks not only retained their clients but they became even more involved with some of them as a result of voucher privatization. In the privatization process, banks through their investment funds took ownership stakes in some of their clients so that the potential arose for a conflict of interest between the bank as an equity holder and the bank as a debt holder. When a mini-currency crisis hit, Czech firms became distressed and the banks' balance sheets suffered. Interestingly, the Czech government's protectionist policy had allowed domestic banks to maintain high spreads and, hence, earn reasonable profit margins. Even in this environment in which banks could self-capitalize, the bad loans problem was not resolved because soft lending practices were continued.

Hungary pursued a policy of privatizing state banks by selling controlling shares to strategic foreign investors as rapidly as possible. The Hungarian experience points to the importance of achieving independent governance both from the state and from undesirable clients. Of more importance than inherited bad loans to the forward-looking operations of the bank are inherited bad clients. The Hungarian bank with the most exposure to loss-making SOEs was Magyar Hitel Bank (MHB). Prior to searching for a strategic foreign investor but after recapitalization, MHB's loan portfolio was divided into good and bad assets. The bad loans along with these clients' deposits were separated from the good part of MHB and a department was set up to work with these clients in an attempt to recover some portion of the bad loans. Financial restructuring dominated bankruptcy as the preferred option (Gray and Holle, 1996).

The main instrument used to restructure loans was the debt-equity swap; this option was chosen disproportionately by the weaker banks. Furthermore, new bank credit was provided to ailing enterprises in about a third of the cases surveyed by Gray and Holle (1996). In a case study of one Polish bank, Bonin and Leven (2000) found that new credit extended to three large military-industrial clients in the program exceeded the total

amount of bank recapitalization and left the bank with more, rather than less, exposure to these clients after financial restructuring.

1.4 Implications for Kenya:

How can the policy makers who are concerned with the Non-Performing Loans (NPLs) in commercial banks in Kenya use these international experiences? Obviously it is unreasonable to expect Kenya to follow the U S, Resolution Trust Company (RTC) which was set up as a rapid asset disposal agency to resolve bad loans or the Hungary experience in selling off majority stakes in state-owned banks (SOBs) to strategic foreign investors, neither can Kenya emulate Czech's solution in dealing in bad loans If resolving the bad loan problem and promoting independent, sound commercial lending decisions the factors causing the customers to default must be first of all looked at critically and then means and ways must be instituted to resolve this problem of loan default. Thus this should be done the Kenyan style because the circumstances are different between Kenya and the developed world.

A pilot examination of customers' accounts with the commercial bank reveals a number of factors that contribute to Non-Performing Loans such as: politics, poor economy, interest rates, death, illness, loss of job, lack of knowledge, poor management, dissolution, disasters, diversion of funds, take-over, base lending rates, KRA interference, treasury-bill rates, poor monitoring and control, bankruptcy, operation and system errors, slow or unmoving stock, conflict with the law, competition, breach of contract and multiple banking.

This paper analyses the above reasons that have contributed to Non-Performing Loans (NPLs) in the Kenyan banking sector which are covered in detail in the literature review and research findings and interpretations sections. What emerges is a line up of factors that could be contributing to the problem of Non-Performing Loans (NPLs). The high interest rates we see in the commercial banking sector may be linked to these factors if the banks may factor them in borrowing rates

1.5 Definitions of terms used:

1. Loans overdue: Loans not repaid when due or not repaid after the due date has been extended.

2. Doubtful loans: Loans that have been overdue for more than two years or operation of the projects have been stopped.

3. Bad debts: Loans that have not been repaid after the enterprises' bankruptcy or liquidation.

4. Unsecured loan: A loan that only has a general claim to the assets of the borrower if default occurs.

5. Secured loan: A loan that is backed by a first claim on certain assets (collateral) of the borrower if default occurs. This in other words can be said to be the one backed by specific assets of the borrower, if the borrower defaults, the lender has a first lien or claim on those assets. In the terminology of finance, secured debt is senior to an unsecured loan that has only a general claim on the assets of the borrower if default occurs.

6. Corporate customers: This is a segment of customers who can borrow a minimum amount of one million and a maximum of one billion shillings.

7. Business customers: This is a segment of customers who have at their disposal three hundred thousand to thirty million shillings of which they can borrow.

8. Personal customers: This is a segment of customers who can borrow a minimum of one hundred thousand and a maximum of ten million shillings.

1.6 Research Problem:

Bank management may be most interested in high profitability while not exposing their firms to unacceptable risk levels. The major concern is the probability that the advances made by the bank to its customers will significantly decline in value and even become worthless. This requires that for banks to make quality lending they should have quality credit information relating to its current and potential customers. The assumption is that proper use of information lead to optimal lending decisions. The second point is that preventing the new bad loans is more important than getting rid of the stock of existing bad loans. It is only by banks having accurate information at its disposal will it be able to separate good clients from bad ones.

The research question in this study is to what extent do other factors, other than interest rate, contribute to the problem of Non-Performing Loans (NPLs)? This will help me explore methods of controlling such factors should I establish that they have substantial influence.

1.7 Objective of the study:

To identify reasons why borrowers fail to honour their loan obligations and make recommendations to the commercial banks on how to reduce the problem of Non-Performing Loans (NPLs).

1.8 Justification of the study:

The various interest groups that might find this study useful include:

1. Commercial Banks who are the lenders might improve on their decision making.
2. Borrowers, who will be able to know exactly what the lending institutions or commercial banks require of them.

3. Depositors to have confidence in the commercial banks to avoid panic withdrawals.
4. Government whose interest is to avoid seeing more commercial banks collapsing.
5. Academicians for their study and even for further research.

CHAPTER TWO

LITRETURE REVIEW

2.1 Background:

Mugo (2000) attempted to establish the appropriateness of theoretical financial crisis predictive model to bank failure in Kenya. The other objective of the study was to identify the key macro-economic variables in predicting bank failure in Kenya. The concern was that Kenya suffered three major bank failures in 1989 and 1998 and that a total of thirty-seven banks collapsed between 1984 and 1998. Mugo's study focused on changes in selected annual average macro-economics variables, namely interest rates, reserve money, Gross Domestic Product (GDP) and the Nairobi Stock Exchange (NSE) index for the period 1984-1998. The period was significant because it covered a period when thirty-seven financial institutions collapsed. Increases in lending rates will increase the interest burden on loans leading to defaulting by borrowers. This in turn will lead to an increase in Non-Performing Loans (NPLs) which are loans in arrears and not being regularly serviced. He found out that rocketing interest rates builds up a financial crisis. The other finding is that while interest rate theory, that capture a key macro-economic variable is useful in predicting bank failure in Kenya, the monetary theory of financial crisis is not applicable in Kenya. Reserve money is also not a key, macro-economic variable in predicting bank failure in Kenya. The limitation of Mugo's study is that it only considered interest rates, reserve money, NSE index as the only signals of bank failures. It is possible that other internal and external factors not included as variables in this study could have contributed to bank failure. For example there is suggestion that the probability of bank failure is high after boom periods of economic growth for firms that thrived and expanded. When the boom ends and growth declines, a business performance deteriorates and businesses face difficulties in servicing their loans.

Kagondu (2002) studied factors influencing credit rationing by commercial banks in Kenya. The objective was to determine how commercial banks allocate credit to their borrowers. Kagondu (2002) concludes that commercial banks in Kenya ration credit. The most commonly used form of credit rationing was by refusing to lend some borrowers even if they were willing to repay at a higher interest rate but issuing full credit to other borrowers. The main reason for credit rationing includes; inadequate information needed to adequately determine the credit worthiness of borrowers, failure to identify profitable investment projects and weak financial position (Balance sheet risk).

Obiero (2002) researched on adequacy of the banking sector regulatory framework in reducing bank failures. His hypothesis was that effective regulation reduces both bank failure and loss of deposits. He reviews the Kenyan regulatory framework during the period 1984-2001. The objective was to determine whether the existing regulation is effective as to reduce the probability of bank failures. It also helped in identifying factors causing bank failures in Kenya. The sample consisting of thirty-seven firms was chosen from a total of thirty-nine failed institutions. He concludes that the most dominant factor causing bank failure in Kenya is ineffective board and management. The directors didn't formulate appropriate policy guidelines to guide senior management on how to run the institutions. The second most dominant cause of failure was Non-Performing Loans (NPLs). His other observation was that bad loans arise due to poor macro-economy performance, poor lending policies or failure in risk analysis when making lending decision.

Obiero (2002) observes that throughout the period there was no clear legal provision aimed at reducing the incidences of Non-Performing Loans (NPLs). The Central Bank of Kenya (CBK) concentrated in identifying the Non-Performing Loans (NPLs) that existed in the commercial banks books. It is not until 1999 that the CBK started formulating laws on credit reference and rating agencies that allowed or encouraged banks exchange information on the bad borrowers, CBK (Jan 1997). During the 1970s the government encouraged credit rationing. For a long time the government held directly or indirectly a

majority interest in more than half of the banking institutions that enabled it to control the banking sector. Some of those controls ensured that credit was extended to borrowers unlikely to service their debts i.e. in a number of instances the lending rates were unrelated to the credit risk of the underlying borrower. Small firms in particular were largely rationed out of the credit market and it was observed that for many developing countries including Kenya, government and public enterprise were the main recipients of domestic credit receiving more than 50 percent of the loans.

In Kenya, the government directed credit programs damaged the financial system and many directed loans became Non-Performing Loans (NPLs). The growth, recessions and higher real interest rate resulting in many firms being unable to service their debts and accruing high levels of arrears. The era also witnessed many instances of misuse of selective credit flows and was noted that the gross rationing of the private sector versus the public-sector borrowers and the failure to use price (interest rate) mechanism to discriminate among large corporate and public sector borrowers resulted in significant inefficiencies.

In China the profitability of the State-Owned Banks (SOBs) declined significantly in the 1990s. However, if uncollected interest payments are excluded from the revenue side of the financial accounts, most SOBs, except the Bank of China, would report financial losses by 1996 and in the following years (Li, 1998).

The theory of financial intermediation suggests that banks specialize in information production and loan contract designed to resolve credit-rationing problems is why asymmetric information is most severe (Fama 1985, Diamond 1984). Their comparative advantage in tackling this task increases with their ability to reap economies of scale and scope of information production. The more information the banks obtain about borrowers, the less they have to improve borrower incentives by setting loan contract terms on lending variables such as interest rates and collateral requirements. Since information gathering is costly, banks will expand their search for information until the expected marginal benefit of search equals zero.

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The existence of information asymmetry induces a risk premium that is transferred to lenders, thus making borrowing expensive. The objective is to make loans at affordable rates. The degree of information asymmetry depends on borrower characteristics such as firm size, firm age and governance, or legal form, Martinelli (1997) and for individual borrowers on the earnings of the borrower, family structure etc. In the case of size one would expect small firms to provide less information to outside financiers than large firms. For old borrowers one would expect the information asymmetry to decrease because of the reputation that might have been built.

Information about a borrower may be prohibitive if lender and borrower have a one off transaction. Learning from repeated transactions can reduce this. For example, each time a bank renews a loan contract, the renewal acts as an acknowledgment of the firm's ability to meet its debt obligation and thus lowers the monitoring cost. Thakor, (1995) asserts that information asymmetry can create economies of scale in information production. Furthermore economies of scope arise if the bank resorts to information gathered in other transactions, e.g. deposit accounts, Petersen and Rajan (1994) The private information contained in bank records over time provides a valuable character and composure of the borrower and enables low-cost renegotiating of debt contracts.

The bank can only meet customer needs if either the customer is able to offer credible information or the lending institution is able to collect the relevant information. To cultivate trust it would be better if the bank and the customer co-operate with regard to provision of appropriate and timely information. Such co-operation results in a stable relationship, in which the bank and the customer feel obliged to each other, Fisman and Khanna (1999).

Fisman and Khanna (1999) distinguish between deterrence-based trust, knowledge-based trust and identification-based trust. Deterrence-based trust is based on the threat of punishment is derived from the theory of repeated games. It is based on the assumption that there is a positive correlation between trust and information. Furthermore trust based on information reduces monitoring cost and induces lower interest rates in the lender-

borrower relationship. Knowledge-based trust occurs when a party has enough information about the other to accurately predict its behavior. Identification-based trust applies, when each party has fully internalized the other's preferences, Fisman and Khanna (1999). In the cases of knowledge-based trust and identification-based trust, superior information flows mean more trust by learning about the other's behavior. This line of thinking is consistent with the theory of social interactions in business-to-business relationships, Blois (1999).

To capture mutual trust in the bank-borrower relationship earlier studies introduce variables relating to borrowers past, the obligation of the bank to the partner and vice versa, the notion of the stability of the relationship and the flow of information. Past experience may reflect the shared in a relationship, Blois (1999). The stability of the relationship depends on consistent behavior, in the sense of deterrence-based trust, Fisman and Khanna (1999). Finally, the flow of information may reflect knowledge-based trust. The literature suggests that that these variables are significant for the lending relationship, Blois (1999), Fisman and Khanna (1999). Terms of lending are affected by such interaction variables in addition to collateralization and or by the duration of the lending relationship. This kind of information can be built up by examining customers' records

In terms of our claim or function matrix, the staff responsible for determining whether a loan is performing against the agreed-upon terms and conditions, specifically whether the borrower is meeting all the loan covenants found in the agreement, is servicing the claim. In doing so, the lending institution can discover problem loans in a variety of ways. The borrower may simply and blatantly default or notify the lender of pending difficulties. Or the borrower's financial reports may signal financial deterioration of the core business. Internal audits may also disclose possible loan violations or fraud. Death of an owner-manager (as in the case of Robert Maxwell, media mogul and lead of Maxwell Enterprise) filing for bankruptcy by the borrower's main customer, or some after major event may put the loan at greater risk, Thygerson (1995).

The loan servicing function must incorporate effective policies and procedures to identify and quickly handle deteriorating credit. To perform this function, managers at the planning stage must develop delinquency and problem loan tracking reports, late notice of payment notifications, periodic reviews of financial statements, collateral inventorying and analyses of borrower information that may impact the borrower, Thygerson (1995).

As alluded earlier the most common problem loan is one simply in default. Which occurs when loan payment is past due or when the borrower fails to meet a specified term or condition of the loan contract or a covenant in the loan or security agreement, Thygerson (1995).

At one time or another you may have missed a credit card or student loan payment, putting an account into default. Once a loan goes into default, the credit management team can initiate a number of defensive activities to minimize loss to the institution. Credit managers' start by asking; what are the prospects of repayments? What can we do to improve our prospects? Can we work with the customer to identify problems leading to default and possible strategies for solving them? If not, what steps can we take immediately to ensure the best possible recovery? Thygerson (1995).

If working with the borrower's current management is feasible, then the intermediary may develop a loan modification that supports the borrower in implementing a recovery plan. Such a loan modification may involve substantially altered terms and conditions and loan covenants, or it might rely on additional new collateral, if any is available. In exchange the borrower may receive an extended loan repayment period, or possibly even additional funds if needed to keep the firm viable and to forestall, if not prevent bankruptcy. Since lender will always profit by responding to a problem loan earlier rather than later, the lending institution must develop adequate loan servicing and monitoring capabilities, Thygerson (1995).

Countries like Germany with bank based financial systems have experienced higher economic growth than countries with a more advanced and competitive financial market.

Close ties between the banks and the corporate sector enhance the availability and reduce the cost of loans to firms. Petersen and Rajan (1994) show that the bilateral credit relationship may be considered as an enduring commitment between a bank and a borrower. Both parties have dealt with each other for sometime and expect to do so in the future.

Another point of view holds that the bank-borrower transactions are not 'standardized' in the spirit of Williamson (1985). Unlike the case of standardized transactions, the signing of a loan contract does not represent the end of the relationship between the contracting parties. During the bank-borrower relationship, many events may occur which alters the bank's cost of providing the credit as well as the borrowers willingness to pay for it. Once the contract has been signed, the borrower and the bank are trapped in a situation of bilateral monopoly. Both parties may reap gains from this relationship. On the other hand, the bank collected information ex ante and ex interim, which would constitute sunk costs, if the borrower leaves the relationship. On the other end, the ending of the relationship by the borrower is likely to convey a negative signal about its quality to outside banks, Von Thadden, (1998).

2.2 FACTORS LEADING TO CUSTOMERS FAILING TO SERVICE LOANS

Political environment:

Political environment is a very important aspect in consideration to business operation in Kenya and thus politics play a vital role on the business environment in the country. The relationship, which the business holders have with political figures, has to be taken into consideration. Due to political uncertainty in Kenya mainly during the general elections, some communities who own most of the businesses in the country tend close down businesses. Incase such persons had a loan with a commercial bank, then there are very high chances of doubtful loans arising.

Economic environment:

Economical decline may result into loan default as the economy poor performance results in the businesses poor perfomance. Economic low performance at times considered as economy downturn, make business entities to close down. If such business entities or an individual had a loan with a commercial bank then they find themselves in a fix, as they do not have any income to repay such a loan, hence bad debts.

The sectors of economy such as agriculture, manufacturing, building and construction, financial services, transport, storage and communication and tourism get affected due to the economy decline. This results into the rise of Value Added Tax (VAT) and with it, then it is expected that the consumer demand would decrease hence decrease in production. Decrease in production results into decrease in investment allowance, this will do a lot of harm to the manufacturing and tourism sectors through increase on capital expenditure for building, machinery and equipment used for manufacturing and hotel premises.

In the tourism sector, the total number of tourists who arrived in the country through the main entry points of Jomo Kenyatta International Airport (JKIA), Moi International Airport Mombasa (MIAM) and by cruise ships declined 2002. This situation even got worse by the recent negative travel adversories on Kenya by the US and the British governments, which led to the cancellation of flights to the country by some airlines including the British Airways (Kenya Monthly Economic Review, June 2003). This measure affected trade, restaurants and hotels and in general the tourism sector was adversely affected.

Economic low performance or non-performance can adversely affect the operations of a business. This can be evidenced in what took place in Kenya in the 1990's where quite a number of businesses were shut down. When such a thing happens then the affected organizations, in our case the borrowing institution is struggling or closes down which leads to non-repyment of the borrowed funds. This exposes the lending institution, the commercial bank, to bad debts.

Interest Rate:

Loans can be made at either fixed rates of interest or floating rates. A fixed-rate loan has the rate of interest set at the beginning of the contract period. This rate remains in force over the loan contract period no matter what happens to the market rates. In the floating-rate, contractual terms, the loan rate can be periodically adjusted according to a formula so that the interest rate risk is transferred in large part from the bank to the borrower unlike the fixed-rate one which the bank bears all the interest rate risk, Saunders (2000). Interest determination is demonstrated both in tables 1 and 2.

This is the factor, which has been thought to be the major reason why bank customers fail to pay their loans in good time. The main cause of high interest rates in Kenya include high government domestic borrowing, which was Kshs 172 billion by end of September 2000, high Non-Performing Loans (NPLs), which stood at Kshs 114 billion or 39% of

total advances by end of September 2000; tax judicial system and an unavoidable high cash ratio requirement, dictated by monetary conditions, now standing at 10% of total deposits. The other cause, is high operating cost of many commercial banks. In most cases such inefficiencies are factored in interest rates charged to customers. This can be seen more clearly in Appendix I.

Death:

There is a saying that goes, "as sure as death". Death is inevitable event in a human being's life. It has got various causes such natural and artificial phenomena that include accidents, illness, suicide, murder, draught, floods, wars and the likes.

When we look at this point critically, as much as one can argue that the borrower is insured and that the lending institution needs not be worried of this type of loss, the experience is that most of the insurance covers are inadequate. For example, the insurance cover offered by Standard Chartered Bank, the Group Creditor Premium Service Fee, the insurer only honours the specified happenings as per the contractual agreement between it and the bank. This insurance cover is very specific and if the borrower died in any other circumstances that is not stipulated in the insurance contract then the commercial bank is bound to suffer great loss as the insurance company is not liable to repay the interest and the principal amount borrowed.

Illness:

Under certain circumstances, illness has got negative impact to the case before us. The borrower instead of repaying the loan ends up using the funds borrowed to cater for medical expense instead of the intended purpose. This can be seen in the illness like HIV Aids, which can be very expensive, to the extent that even the medical insurance covers try to elude them. Due to illness of such borrowers they will find it difficult in honouring

their loan obligations. In a number of cases where the borrower is terminally ill, the borrowers may end up not repaying the loan in good time or not even repaying at all. This kind of problem could be more pronounced in cases where the borrower is either an individual or a principal partner or a closed company. The general health of the business owners should be taken into consideration and also the health of a close relative.

Loss of job:

Lack of job can be brought about by different circumstances such as retrenchment, retirement sacking or firing due to events such as strikes among others. When such a thing takes place and may that such an individual had borrowed from a commercial bank, then such a lending institution is likely to loose money and at this juncture it should be known that employees benefits such as pension are not tied to any type of loan. Incase the unfortunate happens then this brings in the issue of loans overdue.

Lack of knowledge:

Having proper know-how is very important in this case of excessive loan default. This mainly affects an individual, the sole-proprietor who has the sole say in the business, partners or even at times the corporate company whose staff may not be equipped with proper knowledge of loans.

Such knowledge as interest rate prediction has to be done with a lot of keenness and care and most probably by experts in that field. This is so, because if not done well then the interest rate might be so high that one might not be able to repay the interest and the principal amount. For example an understanding of the interest rate trend and the business trend enable prediction of cost of borrowing and its impact on a firm's profitability. Owners of businesses must have a proper knowledge in the business that they are engaging in to avoid business failure.

From the lending institution perspective, the lending institution must seek answers relating to; who are we lending to and the reputation and integrity of the lender and any other risk inherent to the lender. Risk analysis is a must and this requires that the lender regarding the borrowers collect sufficient information. The key risk factors to be considered at this point include business risks; management risks; structural risks; and account performance risks, this leads to bad debts. Banks should take into consideration the skills and preferably the professional skills of the owners and the employees of the business they are to advance loans to.

Poor management:

Poor management is another source of business decline. Management needs a force with effective and efficient management style to survive and succeed in this competitive market. Effective management can make the company to retain the number one position in the market. That would mean good profits and improved cash flows that ensure effective servicing of debt obligations. The lending institution is sure of being paid interest and the principal amount. Controlling for differences in the management skills, firms with better management pay lower interest rates. This may reflect a higher bargaining power of management in the renegotiation process. This implies reduced risk, Lehmann and Neuberger (1998).

Incase there is poor management then this can increase the incidence of Non-Performing Loans (NPLs) and this can be wtnessed in Bonin and Huang (2001), "At the end of last year, the People's Bank Of China (PBOC) inspected fifty branches of State-Owned Banks (SOBs) having a large increase in bad loans. Dozens of managers, including two senior officials at Bejing branches of Industrial Bank and Commercial Bank of China (ICBC), were dismissed for incompetence and mismanagement (Financial Times, March 22, 1991)" In Kenya, the availability of outside expertise is limited and expensive so that emphasis must be placed attracting and retaining competent staff for the commercial

banks to manage and dispose of the asset sales. This is at times referred to as the management deficiency, Bonin and Huang (2001).

At this point efficient and effective loan officers should be able to classify borrowers in risks classes or credit ratings on the basis of their observations and lack of proper knowledge and skills in this, brings in the issue of Non-Performing Loans (NPLs) or bad debts. There has to be a distinction between borrowers with different risks and a borrower's willingness to accept the collaterised loan contract offering lower interest will be inversely related to its default risk, Besanko/Thakor (1987)

Corruption is another monster, which makes a business interests to have low performance in their competitive market. Corruption has got a negative impact to the business and the ones who gain are the reckless who have got no business interest at heart. Incase a business entity is involved in corrupt deals then it stands high chances of being run down and incase such a business entity had some loans, then it might be unable to honour its pledge and thus fail to pay the loan in good time or even default.

Dissolution of an organization:

In the sense in which the term is used in Britain, the dissolution of a company is effected by the registrar removing the name of the company from the register. Dissolution of a company ends its legal personality and dissolves the relationship between the company and the members. In European community document, the term 'dissolution' is used in the sense in which that term is understood in Continental legal systems, that is for what in Britain is called the commencement of winding up On the Continent, the transition from going concern to company in winding up is thought as a point at which the company is dissolved. In Britain the final end of a company legal personality on completion of winding up is regarded as the point of dissolution, but on the Continent this is regarded as the end of winding up, Mayson, French and Ryan (1994-95.)

An organization can be dissolved for various reasons, but in our case lets take the issue of when the partners in an organization can not see eye to eye. If such an organization had borrowed some funds from a commercial bank and the funds at its disposal is not enough to take care of its debts then the commercial bank ends up loosing money it advanced in anticipation of getting good returns.

According to Ashiq (1993), " Kenya Partnership Act provide that the following events will dissolve a partnership, unless there is a contrary agreement by the partners. A dissolution occurs without *any order of the court* in the following circumstances: By the exercise of an option, by the partners, if one of the partners charges his share in the partnership property to the court in respect of his own personal separate debt". Dissolution of an organization comes in with the bad debts issue.

Disasters:

Disasters can either be natural or artificial. Natural disasters can be in form of rain, flood and drought. Man has got no control over the natural disasters, while the ones that can be manipulated by human beings if not controlled by them are known as the artificial disasters. Artificial disasters include theft, robbery and fire.

Business entities can be highly affected by natural phenomena like flood, which cause a business to cease operating normally. Incidences like heavy rains can greatly affect the agricultural sector like coffee, tea and horticultural products. Incase the business entity had engaged in such like cash crops, then it will have no alternative but to default in repaying the loans. Artificial phenomena like theft and robberies affect most of the business entities and in most instances end up making the businesses to close down.

Diversion of funds:

Funds borrowed have to be used only for a particular or the purpose it was intended for. But more often than not, such funds are not used for the primary purpose they were intended for and as such many projects become halfway done, termed as "white elephants". Incase these funds were meant for an income generating project, then this has to be followed strictly such that if the project turns out to be viable, the borrower of these funds will be in a position of repaying the interest and the principal amount in good time. However in real life situation a borrower takes up a loan for one project, only to divert it to an entirely different project. This is seen clearly when one takes up loan for a certain project buts ends up in leisurely activities like taking out a girlfriend to the U.S or the UK and when such an individual clears the funds then the reality dawns on him. Repaying such a loan becomes so hard and this gives birth to loans overdue. Also this can be seen in when one uses funds for hospital bills, paying school fees and the likes instead of business expansion. In nutshell diversion of the use of funds for the purpose not intended.

Take-over:

In the case of take-over more so the hostile takeover, if the firm being taken over had borrowed some funds then the commercial bank might end up loosing funds lent. In such a case even the bitter pill method of resisting the takeover bid fails and no other remedy can be found this results into loss of funds to commercial banks. The takeover tender offer, in which a company attempts to acquire a target firm against its will, has come into vogue. One of the most notorious examples was announced intent of American Express to take over McGraw-Hill in early 1979. At that time McGraw-Hill was selling at $ 26 per share. The initial American Express was for $ 34 per share and eventually went upto $ 40. McGraw-Hill fought off the offer by maintaining that the American Express would obstruct the independent character required by the publisher. Not all the companies are able to fend off the unwanted advances of the suitors. An entire vocabulary has developed

on Wall Street around the concept of the target takeover (Block and Hirt, 1992). With this situation doubtful loans or loans overdue settle down.

Interference by the KRA officials:

There exists tax implications of borrowing that may make it difficult for a borrower to service debt. At times the Kenya Revenue Authority (KRA) feels that the commercial bank is charging high interest rate than they are supposed to charge and thus they come in with their predetermined rates, which in their opinion acts as ceilings and which the commercial banks need to adhere to. KRA does not take into consideration other factors, which make the interest rate to go up like the cost of funds among others.

Kenya Revenue Authority usually to some extent has say in loans as car loans, mortgages and shamba loans. They usually put a ceiling for the maximum and the minimum interest rates as 9.45 percent and 6.6 percent respectively (Standard Chartered Bank). KRA relate these rates to the prevailing market conditions in liaison with the Central Bank of Kenya on a quarterly basis. They come with a list, which the commercial banks should adhere to. Due to the above conflict between the KRA and the commercial banks, this generates the circumstance of the loans overdue problem.

Changes in the Treasury-Bill rates:

Treasury-Bill rate is a running average of interest rates in the prevailing current market conditions for a period of 91 days or 180 days. It reflects government's intervention on money markets. When the Central Bank of Kenya is advising on the applicable Treasury-Bill rates they usually consider the average base lending rates of all commercial banks for a period of 91 days or 180 days. The criteria for choosing its applicability lies with the individual banks depending on the facilities they have for their customers as given by Standard Chartered Bank for 91 days the applicable rate is 6.6 percent up to one year,

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while for 180 days it is 7 percent for more than one year. Commercial banks have an interest in the overall stability and predictability of the benchmark rate, which is used to determine lending rates.

Presently, two rates are quoted after each Treasury-Bill tender rate for the amount raised that week and the 12-week moving average. A different opinion well expressed on the use of moving average Treasury-Bill preferring the average tender Treasury-Bill rate be used to avoid a mismatch that is the rate of last Friday of the last month which brings out disparity over the two rates, Kenya Monthly Economic Review (May, 2003). This poses another problem to the commercial banks as per the issue of Treasury-Bill rate, which needs to be sorted out urgently.

"Banks are expected to shy away from heavy investments in government securities as the income from this stream is usually pegged on the ruling 91-day Treasury-Bill rate that continue to diminish fast. The Stanbic Bank set the pace for the latest series of base rate reductions when it dropped its base rate to 10 percent. At present, National Bank of Kenya charges the highest rate at 19 percent"(Market Intelligence, April 2003). This factor comes in with the problem of loans overdue.

Prolonged change in the Base-Lending Rate:

Incase there is prolonged change in the base lending rate, then the commercial bank might end up losing some anticipated income. Incase the bank gave out a loan when its base lending rate was 15 percent as in the case of Standard Chartered Bank, then it gets more income than when the base rate gets lower to its current rate of 13.5 percent and even lower than that, which means that the banks' anticipation of more income is substituted by more loss to the commercial banks. When the opposite happens, that is the base lending rate increases which is to the advantage of the commercial banks, the customers find it difficult to service their loans and thus the problem of excessive loan

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default interms of loans overdue crops up. The table below shows a comparative spread of the T-bill and the commercial banks lending rates between Kenya and other countries.

COMPARATIVE SPREADS

Countrry	91 days T-Bill Rate	Commercial Bank Lending Rate	Variances
Kenya	11.1	20.6	9.5
Uganda	16.4	25.4	9.0
Tanzania	12.3	20.9	8.7
South Africa	10.3	14.5	4.3
Thailand	6.5	7.5	1.0
United Kingdom	5.8	6.0	0.2
Germany	4.8	9.9	5.1

Source: Reuters

It should be noted that in none of the above countries' central banks regulate interest rates.

Poor monitoring and control:

Monitoring loans in arrears by the commercial banks has been a difficult task in the past. This is because the task's support system was manual and could be only done once a year to determine the customers who have been defaulting. In order to achieve efficiency in this area, the commercial banks had to use an automated system. This reduced the time from one year to one month and more efficiency was seen when this time span was reduced to five days and this gave birth to centralization to curb the problem of excessive default.

The other aspect of poor control comes in when the age factor is not taken into consideration when striking out the contract as specified by the commercial banks. For example in a bank such as Standard Chartered Bank, for one to qualify for any loan one has to be above 21 years of age and not above 53 years. If this is not followed properly then a problem arises and which results to excessive default. This is attributed to poor risk management.

Bankruptcy:

The bankruptcy proceedings in Kenya are governed by the Kenya Bankruptcy Act (Cap 53). This Act is based on the English Bankruptcy Act 1914. According to Blackstone: "Bankruptcy is a proceeding by which, when a debtor cannot pay his debts or discharges his liabilities or the person to whom he owes money or has incurred liabilities cannot obtain satisfaction of their claims the courts in certain circumstances take possession of his property by an appointed agent for the purpose and such property is realized and distributed in equal proportions among the persons to whom the debtor owes money or has incurred pecuniary liabilities, Ashiq (1993)

A person is insolvent or bankrupt who cannot pay his debts or discharge his liabilities on the due date. The creditors or the debtor himself may present a petition to the court that a receiving order should be made. No bankruptcy petition can be presented against any corporation or association or company registered under any enactment. Thus a company registered under the Companies Act cannot be made insolvent; it must be wound up under the Act (Ashiq, 1993). From the above circumstance, a commercial bank ends up loosing money incase of such loan contracts which ends up in bad debts.

Operation and system errors:

Operation errors are kind of commissions and omissions done in the normal business operations. Thus incase a procedure was supposed to be done in a particular way and the procedure or the process is not followed to the latter then an omission or commission comes in.

System error occurs when the computers at one point fail to monitor and register the status of the problematic loan accounts. This may happen when systems have failed, for example to effect the standing orders or the bankers orders which is an instruction to the to effect payment from the customer's account to the bank.

Slow moving or unmoving stock:

At times an individual, partnership or a company engages in a business like the distribution of stocks of Fast Moving Consumer Goods (FMCGs) such as Kenya Breweries products, Coca-Cola products and the likes. Such an individual goes go to a commercial bank, take a loan and then stocks his enterprise with an aim of selling the stock the soonest time possible and then repay the loan, which includes interest and the principal amount. A rude shock is gotten when the stock bought moves slowly or doesn't move as anticipated and thus such an individual or organization fails to pay up the interest and the principal amount and such a case gives rise to bad debts.

Conflict with the law:

Law is meant to protect individuals and institutions and it is not by any chance meant to punish anyone. When the law of the land is not adhered to, then this results into conflict of interest as an individual or an institution interest is to go on producing or offering a service in which the government deems it not appropriate for the wellbeing of the

country. Incase an institution is engaged in a business of wood products and the government decides to put a ban logging then such an institution has no otherwise apart from closing down.

Competition:

Competition is in two forms either fair or unfair competition. Fair competition is a situation in which the concerned business entity compete against one another in which the result is positive as these business performance increases. Unfair competition is where the businesses concerned do not have a level playing ground, thus a section of business institutions have got an upper hand than the rest. Here there is no level playing ground unlike the former one. In this paper the focus is on the unfair competition as it is the one which has devastating effects in the business institutions.

A business institution may be subjected to the unfair competition, which is unhealthy for the business to thrive. When such a circumstance arises, then the business ends up being closed down. With the commercial banks advancing loans to such institutions, then they are likely to lose these funds as such accounts turn out to be among the problematic loan accounts within the commercial banks' books.

Breach of contract:

In this factor, instead of the parties involved in the contract honouring their parts, one party decides to dishonour its part and thus makes the other party to suffer loss interms of finances. This occurs in most circumstances when a debtor fails to honour its obligation of repaying the debt and thus making the creditor lack funds to repay their loan which they had with the commercial bank and loan default occurs.

Multiple-banking:

This becomes a problem when a customer has more than one banker and at times it is done without the bankers' knowledge, which results into information asymmetry. Information asymmetry relates to a transaction where two parties involved have unequal accesses to information about the deal at hand, Thygerson (1995). This brings in about the problem of moral hazard and adverse selection.

Claims of inadequate or misleading information account for a growing amount of consumer-oriented financial regulation not necessarily because of underhanded activity but because of financial contracts like insurance policies are becoming more complex and difficult to interpret. And so, public policy majors and consumer groups demand new regulations and disclosure toward standardization of product and service description, so as to provide consumers with equal access to information. There are a number of regulations concerning equal and fair access to information. The first major piece was the consumer Credit Protection Act of 1968. This act requires the lenders to use a consistent methodology for quoting interest rate on loans, referred to as truth-in-lending, and so that consumers can more easily compare interest rates offered by various institutions, Thygerson (1995).

Consequently, a major issue in information asymmetries deals with accuracy, breath and timeliness of financial statements reporting and press releases. Investors, analysts and managers of financial intermediaries, to have a few, all expect sound decisions but not so much detail as divulge trade secrets and jeopardize the future earnings. What might managers of financial institutions want to consider when trading in countries where insider dealings are legal?

Another abuse of information is outright fraud, where people dealing on either side of a transaction cook the data or stretches the truth to the other party for personal gain. Accusations of fraud usually, involve IPO's and lending; that's why a financial firm's

reputation for screening candidates is so important to potential investor, Thygerson, (1995).

A case study suggests that in a relationship lending of Germany banks, credit assessment is more concerned with the behaviour of the borrowing firm's reliability and qualifications of the relevant persons, than with the investment program as such, Burghof/Henschel (1998). Thus when a customer is not given the full picture of the operations as per the loan contract, then after some time the client fails to pay the interest and the principal amount because the interest becomes unbearable and this results into excessive loan default specifically known as loans overdue

2.3 BAD LOANS AND BANK PERFORMANCE

Commercial Banks:

The effect of not servicing the loan in time has a devastating impact on the commercial banks' performance, Kenya Monthly Economic Review (May 2003). The commercial banks operate in a cyclic manner, in that funds deposited by the customers who are given low interest rate is the same funds which are loaned out to prospective borrowers who pay high interest rate. When a borrower starts repaying, these funds are lent out to a prospective borrower and so on and so forth. The chain continues and this makes the bank to continue its central business, which is lending money. If the chain is broken along the way, for whatever reason, then the commercial banks are at a greater risk of collapsing.

Depositors:

Depositors of funds in commercial banks suffer a great deal when loans are not paid up in good time as per the contractual agreement between the commercial banks and the borrowers. This can make them end up loosing their money incase the bank collapses as this can be evidenced in the Euro Bank saga in which Kenyatta National Hospital (KNH), 86 million and National Social Security Fund (NSSF), 256 million deposits were lost, Market Intelligence (April, 2003). Depositors can cause bank failure incase there is a wrong signal sent to the public as they come at once to withdraw their deposits usually referred to as " Panic withdrawals".

In reference to Deposit Insurance Cost, depositories are required to insure premiums to their respective deposit insurance corporations. For example as a result of the Financial Institutions Reform Recovery and Enforcement Act 1989, the cost of deposit insurance has changed significantly. The cost of deposit insurance for commercial banks insured by

the Bank Insurance Fund and thrifts insured by the Savings Association Insurance Fund in Early 1994 ranged from 23 to 31 basis points computed off at deposit balance, Thakor (1995).

Borrowers:

Whenever the chain of borrowing is interfered with, the bank will not be able to make available to the prospective borrower the much-needed funds thus making it difficult for the borrower to carry on with the development projects. It is possible that under such circumstances, borrowing can become costly because trustworthy borrowers end up paying high interest so as to compensate for the loans which had been written off as bad debts by the commercial banks.

The existing borrower who has failed to service the loan in time also ends up loosing so much money because of the penalty he has to pay in terms of the interest rate the bank charges and the other charges like commissions when the standing orders bounce and this adds the pain of it all.

It is perhaps interesting for banks to note the sentiments of Professor Alfred Cockrell of the University of Witwatersrand on the subject, "It is clear that the prohibition of interest *in duplum* shows sensitivity towards the social position of borrowers in the market place, since it seeks to protect debtors from abuse at the hands of the creditors. However, in a modern economy the rule is both inappropriate and arbitrary. Since interest is the " life blood of finance", it is difficult to believe that there is any place for the *in duplum* rule. In any event, the reference to the yardstick of "double" provides an inherently arbitrary measure of consumer protection, since it bears no rational relationship to interest rates or the period of time for which the borrower has the use of the money."

Economy:

The effect of the clients not servicing the loans in time may make a commercial bank collapse. The collapse brings in a chain of bad events like loss of jobs and business opportunities. With the loss of jobs, the dependants of such employees fail to have shelter, food and clothing as basic needs besides failures to secure education and other benefits. This comes in as a result many organizations laying-off their staff in the name of retrenchment.

The result of job loss is that the general economy performance becomes low, which results into the currency of the country to be weaker and this brings in instability within the financial sector. Such an incidence was witnessed in Kenya when the shilling weakened against the world's major currencies like the United States Dollar, the Sterling Pounds, the Japanese Yen and the Euro among others, during 1986 and 1992 banking crisis, Market Intelligence (April, 2003).

The client's failure to repay a loan in good time has a devastating effect to the economy of a country. This can be evidenced by what the then CBK Governor, Nahashon Nyagah said about the closure of banks in the Kenya, that if the norm was the closure of such banks as a matter of policy, then the Kenyan banking industry would be left with only a handful of big institutions. A situation that would be imprudent and harmful to economic development, Market intelligence (April, 2003).

Yamori and Mukarami (1999) provided evidence of the economic value of bank relationship for client firms. Firms with a closer relationship to the failed banks were more likely to record larger negative abnormal returns. If the problem of loans repayment is not solved, then the economic general performance declines as the banking sector plays a major role in the well being of the country's economy.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Population:

The population interest in this study is Standard Chartered Bank (Kenya) Limited customers who have taken advances interms of the clientele or group like corporate, business and on personal capacity.

3.2 Sample:

For the purpose of this study there was the segmentation of branches into two, the Nairobi and the upcountry branches. In Nairobi a total of eleven branches were considered while nine of the upcountry branches were taken into consideration.

3.3 Data collection:

The source of Data was predominantly the problematic customers' loan records with the bank.

3.4 Data Analysis:

This is a survey that will employ summary statistics such as mean, mode and standard deviation.

CHAPTER FOUR

RESEARCH FINDINGS AND INTERPRETATIONS

4.1 Introduction:

The table below gives a summary of the occurrence of factors that cause loan default and percentages of the same. A more detailed information can be got from Appendix II in which the data collected is presented in raw form.

Frequency of reasons for loan default:

Reasons	R1	R2	R3	R4	R5	R6	R7	R8	R9	R10	R11	R12	R13	R14	R15	R16	R17	R18	R19	R20	R21	R22	R23
Total	7	28	7	4	10	20	6	15	3	11	40	4	3	2	5	2	3	15	2	5	8	3	17
Total(%)	5	19	5	3	7	13	4	10	2	7	27	3	2	1	3	1	2	10	1	3	5	2	11
Rank	9	2	9	13	7	3	12	5	17	7	1	13	17	21	13	21	17	5	21	13	9	17	4

Where:

1 implies that the reason brings in loan default to the case, 0 implies that the reason does not bring in loan default to the case, R1 – Political, R2 – Economical, R3 – Interest Rate, R4 – Death, R5 – Illness, R6 – Loss of job, R7 – Lack of knowledge, R8 – Poor management, R9 – Dissolution, R10 – Disasters, R11 – Diversion of funds, R12 – Take over, R13 – Base lending rate, R14 – KRA interference, R15 – Treasury bill rate, R16 – Poor monitoring and control, R17 – Bankruptcy, R18 – Operation and system errors, R19 – Slow or unmoving stock, R20 – Conflict with the law, R21 – Competition, R22 – Breach of contract and R23 – multiple banking.

4.2 FINDINGS AND INTERPETATIONS

The following are the reasons why customers fail to service their loans to the commercial banks. According to the data survey conducted, their contributions in percentages are indicated besides recommendations to the commercial banks to consider for the reduction of non-performing loans (NPLs) in their books.

Diversion of funds:

According to the findings, this factor is the highest cause of loan default to both the corporate and the business customers as it takes 27 percent of the cases considered in the data survey. The funds lent by the banks to its customers are not used for the purpose they are intended for, but diverted to other usages. Reasons why funds are diverted to unintended purpose vary from one customer to another. From records examination, customers diverted funds granted for working capital to purchase machinery, construction of business premises, paying hospital bills and maintenance cost for vehicles. On the same, a customer diverted funds granted for working capital to construction of beach cottages leading to default as the construction took too long to finish.

A case came out strongly from the records examined as a customer borrowed funds for expansion of business premise, but ended up diverting it to paying school fees for his children who were studying abroad, he proceeded by financing another business and property development and this resulted into loan default. Records examination also revealed that funds borrowed by customers were diverted to politics during the general elections campaign of 1992 and 1997.

From the records examination, a debtor diverted funds from the business operations locally to importation of tyres from Hong Kong and iron sheets from Malaysia. This business failed and the owner could not repay the loan granted. This is an incidence in which business sales were diverted to other uses by the proprietors. An incidence worth noting from the records examination was that a business had not picked up properly

resulting into use of borrowed funds and most of its income on daily maintenance and paying hire purchases instead of the business needs. This business later on defaulted on its loan obligations, as it had no funds at its disposal to repay the loan.

The commercial banks need to ensure that the funds borrowed are used for the intended purposes. Besides this, the commercial banks should make the purpose, which the funds have been borrowed to form part and parcel of the terms and conditions for the loan contract. This will enable them take legal action when such borrowed funds are diverted which results to default.

Economic environment:

The economical climate falls into the category of high ranked factors that cause loan default in Kenya. According to the data survey it takes 19 percent, which is the second highest reasons why customers fail to honour their loan obligations. Adverse economic climate results into business decline.

From the examination of records one could easily pick that a borrower who was dealing in distribution of juices, beverages, tinned foods and sauces found it difficult in servicing his loan because of poor sales. On the same, it was revealed that the European Union banned on importation of fish from East Africa, this forced firms in the sector to close down leading to their failure to service their loans. The agricultural sector was neither spared by the current difficult economic situation in the country. This had a negative impact on the banks that lent to firms in this sector in that such firms could not service their loans. The same applied to the tourism industry as per the records examination.

In the circumstances of economic recessions according to the survey, the government couldn't pay their liabilities forcing businesses that relied on it to close down. Such firms are likely to default on loans from the commercial banks. Obiero (2002), reports that bad loans arise due to poor macro-economic performance.

The banks can not manage economy of the country single handedly. They need the support of the parties concerned and more so the government. They need to convince the government of the advantages of reducing VAT that will make the banks' interest and base lending rates to go down. The government should protect agriculture and tourism sectors. Bans by the international communities like the ban of fishmeal products by the European Union and the actions of the US and Britain on ban of its flights to Kenya for fear of terrorist attacks should be lifted.

Loss of job:

In terms of loan default this factor is the third highest as it accounts for 13 percent and affects personal customers and to some extent the business customers. Banks grant funds to individuals who later lose their jobs due to disabilities, business failure, misconduct or retrenchment. Once such an individual losses a job, he or she cannot repay the loan and thus default.

Before a commercial bank advances funds to a personal customer, it needs to find out the organization that employs such a customer. The employer should be in the list known as the status list, which has reputable employers for example, Kenya Airports Authority, Kenya Breweries Limited, Kenya Power and Lighting Company, Kenya Airways among others.

Multiple banking:

This reason is seen to be among the major causes of loan default according to the data survey as it takes 11 percent of the reasons for default. Having the full information about a cusomer who is borrowing is very crucial to the commercial banks. Incase a bank does not adhere to the requirement of having full information about its customer, then the Financial Services Authority (FSA) can fine such a bank heavily.

According to the survey, most of the customers do multi-banking such that in case there is a problem with one bank then they run to other banks and this is done without the bankers' knowledge. On the same note, customers have habits of cross firing cheques, making empty promises that are never honoured and they are unco-operative in clearing their loans, which are overdue. At times customers refuse to clear excesses in their current accounts and all in all this comes in with one word 'untrustworthy'.

Kagondu (2002) observes that the main reason of credit rationing includes inadequate information needed to adequately determine the credit worthiness of borrowers. Bankers before lending to a customer, should be satisfied that they have valuable and material information about the customer. Information collection is very expensive but by all means it should be done to minimize the incidence of Non-Perfoming Loans (NPLs). Fama (1985), Diamond (1984), records that banks specialize in information production and loan contract is designed to resolve credit-rationing problems.

Poor management:

This factor is among the high causes of loan default contributing 10 percent. Poor management refers to misplaced or abused skills. Management delinquency should not be put aside nor forgotten when it comes to the issue of Non-Perfoming Loans (NPLs). This is more pronounced where there is lack of co-operation between partners, specifically where the husband and the wife are the core directors of companies.

The records examination reveal that one director, the husband gave out a different business directive from the other director, the wife. This brought about conflict of orders and businesses run on those lines close down. Disagreement of the principal directors and family squabbles affect the business, which may result into loan defaults. From the records examination it came out that weak debt collection results into delayed payments or lengthy delay by clients in settling debts which inturn results into loan default. The records revealed that over reliance on a key customer, could end up in a disaster incase

such a customer pulls out of the business agreement. Poor sales management, poor stock procurement and chronic absence of management from the borrowers are factors that contribute to poor business performance that translates into loan default as per the records examination. Records examination reveals that there was a case of a disputed debt as a result of poor management.

Bankers should know who are involved in a business management, if possible their academic and professional qualifications and how the business is managed before they get involved in a loan contract with such a party.

Operation and system errors:

This cause for loan default takes 10 percent, which should be a major concern to the commercial banks. Operation error occurs in the course of the day-to-day activities of the banking business. The incidences occur mostly in the personal customers' accounts than in either the corporate or the business customers' accounts as per the records examination. System error occurs when at one point in the system, there is failure to identify the correct position of a situation, for example, the correct account balance.

On records examination there was an incidence where a loan came about as a result of the errors, a cheque was advertently processed through an account in absence of sufficient funds. Another case reveals that a debt came in as a result of technical fault with the fax machine which indicated that the schedule for unpaying the cheque had gone through while it had not, therefore resulting into a cheque which was unpaid not being reversed. An incidence reveals that an account was overdrawn due to system error affecting the clearance of cheques while the excesses did not appear on the excess report of that day.

It is found out from records examination that due to operation and system errors, a bank disbursed funds to a customer when such funds had not been applied for and default arose. A case like this is really embarrassing. For example, a long time customer stopped

operating an account that was opened in 1994, after some funds were fraudulently withdrawn from the account. The account became dormant and the customer ended up suing for the stolen funds.

Operation and system errors can not be done away with, but can be minimized. When employing, the commercial banks should make sure that they employ experts and not mediocre employees.

Disasters:

Disaster affects most of the businesses and should be considered seriously as it takes about 7 percent of the reasons for default as per the data survey. From records examination, this occurs in form of fire, frequent robberies, rains or theft. On the same, a business was attacked seven times by thugs which severely affected the business operations. The fateful USA embassy bombing in Nairobi in August 1998 affected many businesses that resulted into loan default by the affected businesses.

Records examination revealed that a business premise was severely affected by heavy rains in January 2001. The flooding of the premises damaged machines, which made the operations of the business to come to a stand still. The same also revealed that fire burnt down a business premise situated at the city center, paralyzing the business operations that resulted into loan default.

From records examination one can easily pick that the most targeted businesses by the robbers are the filling service stations and restaurants. Hence the commercial banks when making lending decision to such institutions, should know their locations and whether the management of such institutions have taken precautionary measures against such happenings. The bankers should evaluate the security of the borrower, the guarantors and adequate insurance cover that exists before approving a loan.

Illness:

Illness is a threat to the survival of a business as it takes 7 percent of the cases as per the data survey. On records examination it was noted that when a close relative of a principal owner of a business for example mother, father or children get admitted in a hospital, then the funds which were meant to repay a loan are diverted to the emergency which results into default. Records examination reveals a case where one of the directors fell ill, the business could not be run effectively and efficiently, and the funds that were meant to finance the business were used to cater for the patient needs. On the same, an owner of a business was partially paralyzed due to stroke, there was disability of the owner to run the business, this resulted to business poor performance causing a loan default.

The commercial banks need to be careful on the health status of the borrowers of funds and to some extent the health status of their immediate family members. Banks should even go as far as asking for a full medical report from medical practitioners besides having an adequate insurance cover.

Interest Rates:

This factor has been thought by many to be the major cause of loan default. Surprisingly, it is not among the major causes of loan default as it takes 5 percent of the 150 cases considered. This contradicts Mugo (2000), that reports that rocketing interest rates builds up financial crisis. The banks have the funds at their disposal and the main aim of them lending is to get income interms of interests they charge. The interest rate determination should be both beneficial to the bank as well as the customer, thus they should not charge exorbitant rates neither should their rates be too low.

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Political environment:

Is a factor that causes loan default, however it takes 5 percent of the cases examined. The impact of political event such as general elections is observable as the Asian community, who own most of businesses in the country tend to close down businesses, which results into loan default as per the survey. Lees and Mauer (1998) observe that international lenders and investors recognize that the political risk must be addressed. The difficulty is in defining and measuring it.

Banks in Kenya are making an attempt to define political risks, for example, politically exposed persons (PEPs), influential individuals or persons with high level of political connections who include cabinet ministers, members of parliament, permanent secretaries and the likes should be treated cautiously when it comes to lending. For example a bank is currently undergoing a process known as rectification process which involve segmentation of customers into different categories or levels (1,2 and 3) of risks. PEPs are ranked highest, level 3, which imply that they are the most risky persons.

Businesses that drive revenue by transacting with state corporations, whose financial year ends 30th June, suffer a great deal if the government of the day delays in payments. From records examination, there was loan default due to the fact that a business relied on the government. Politicians involvement in some sectors for example the sugar industry where they did importation of sugar from other countries, thus killing the local sugar industry like what is happening in Muhoroni and Chemelil led to loan default by sugar companies.

Competition:

According to the data survey of the 150 cases considered, this factor took 5 percent of the reasons why there is failure by bank customers in servicing their loans. As much as it is not among the major causes, it should be taken in with all the seriousness it deserves as it

also causes default. Unfair competition is where a business does not have a level playing ground while other businesses. A good example from the records examination is the clothe industry, in which there was stiff competition due to new entrants into the market of second hand clothes, mitumba by politically correct individuals.

Some businesses have gone under due to unfair competition like in the pesticide industry, food industry or from other players offering similar products and. A business can also fail due to the fact that their clients use an alternative means, in terms of products or services to satisfy their needs thus resulting into low sales by the former business. Incase such a business entity had a loan with a bank, then it becomes very hard for them to honour their promises, which brings in the issue of bad debt. Commercial banks when lending should put the competition surrounding the borrowing business into consideration.

Lack of knowledge:

Accoding to the data survey, the statistics show that it takes 4 percent of the reasons for default. Less informed managers can not manage firms properly. This arises when the management doesn't have that basic or technical knowledge required for the day-to-day running of a business. This is different from poor management that arises due to misplaced skills.

There were cases from the survey where the directors were illiterate, for example, there was an expansion of business operation into Tanzania and Uganda without proper feasibility study. The borrower experienced financial difficulties, thus defaulting on its loans. Diversification into business, which seem to be lucrative without proper business knowledge might be costly. The bankers should demand to know how qualified one is to run a business before lending.

Treasury-Bill Rate:

The data survey reaveals that the T-bill rate takes 3 percent of the reasons why customers fail to service their loans. Banks compete for deposits with the government, account of this is that the higher the T-bill rates the more expensive the deposits. To pay interest on deposits the banks are forced to charge interest on borrowing at a higher rate. This makes loans expensive. In 1999, the T-bill rate rose to 22 percent and customers found it difficult in servicing loans because the banks adjusted their rates upwards. Some managers are not sophisticated enough to carry out sensitivity analysis to counteract the rise in T-bill rates.

The banks before lending, they should consider ones ability to repay and not the willingness. This would require forecasts of changes in T-bill rate. There is need to take into consideration the possibility of default, thus the commercial banks should demand for adequate security and a valuation report of the same.

Conflict with the law:

This factor contributes 3 percent of the reasons for default. Records examination show that a principal owner of a business, the director, got involved with the law and ended up being implicated with some criminal activities that he disputed. This brought the business into financial difficulty, which ended up affecting the business operations. The business closed down and this resulted into loan default. On the same, there is business that dealt in timber production, unfortunately the government banned logging. This affected the business operations and financial difficulty arose resulting into default. In another case, one of the principal partners, a husband was a foreigner and indisposition to his mother country affected the business negatively, as other partner couldn't manage the business alone. After sometime the wife wound up the business and it so happened that the business had borrowed funds from a commercial bank. These funds had to be written off because the lady could not repay the loan.

When individuals come in to borrow from the commercial banks, the bankers should take each and every detail of the business owners and if possible forward such details to the concerned authority, criminal investigation depatrment (CID), for a search to be done. If this is not done well, then the banks might end up financing criminal activities without knowing and end up loosing funds.

Death:

The data survey reveals that death takes 3 percent of the causes of Non-Performing Loans (NPLs). Death has got adverse effect to the business customers who are the principal owners of businesses. When an owner of a well-established business dies then the business also dies. It makes the bank to end up writing-off loans taken by such persons for the business use, which adds to the magnitude of Non-Performing Loans (NPLs) and their provisions to the commercial banks books. This is more pronounced in the soleproprietorships than in partnerships or companies as per the data survey.

The banks need to be careful when lending to soleproprietors and incase they do so then more tight conditions have to be put in place to safeguard the funds lent. For example, such an owner has to give the bank a surety that incase of his or her death then the business shall not cease in its operations and besides this, the bank should have a realisable security. A good case is witnessed in Thygerson (1995) in the case of Robert Maxwell, a media mogul whose death caused big loan default.

Take-over:

This factor is among the least causes of loan default according to the data survey as it takes 2 percent. According to the records examination, there was speculation that a certain company was facing financial difficulties, this made its share prices to go down in the stock exchange market. A competitor who was eyeeing the company succeded in the

Bankruptcy:

Bankrupty takes 2 percent of the reasons for default as per tha data survey. Banks end up loosing funds, which are disbursed to businesses that end up bankrupt. From the examination of records, Mr. Z's matatus were impounded by the financiers due to failure to meet his debt obligations and thereafter declared bankrupt resulting into default.

The commercial banks before lending to a customer, should determine whether the business is in a good fianancial status or not and estimate the possibility of the business being declared bankrupt in the near future. Thygerson (1995), reports that filing for bankruptcy by the borrowers' main competitor may put the loan at a greater risk. He continues by recording that at times there are very risky businesses such as the one seen above, the matatus, and advises that great care should be taken when lending out to such businesses. The banks need to know how the business has been insured and who are the insurers. Better still, they need to know that incase of default, how are they going to recover their funds, thus the security available and whether it is easily realisable besides having a list of adequate guarantors.

Breach of contract:

The data survey reaveals that it takes 2 percent of the reasons for default. From the examination of records, a company that deals in the sale of motor vehicles, supplied the products to its customer, the government who failed to honour its part. This forced the company to close down because the firm had borrowed funds for the importation of the vehicles whoich resulted into default.

The commercial banks need to take an extra step in verifying the sincerity of the parties involved in a business deal They even need to examine the history of all parties involved in a business contract before lending.

Dissolution:

Though it is not among the major causes of loan default as it gets to 2 percent, it should be taken seriously. From the examination of records, there are customers who defaulted after they ceased operating under the name in which they held the contract with the bank and started operating under a different name altogether.

At times, it is very healthy for the commercial banks to know the history of a businessman. He might be that type of a man who starts businesses day-in day-out with a bad motive of conning bankers. It is advisable to do a search for such individuals at the registrar of companies to determine whether they have had businesses previously. If so, what duration had it taken them to start another business and why were the earlier ones closed? It is also advisable for the banks to ask for quarantors before lending. With these, the commercial banks will play it safe when it comes to lending.

Interference by KRA:

According to the data survey, this reason for loan default takes 1.3 percent. The Kenya Revenue Authority (KRA) regulations affect business operations. From the records examination, an owner of a business which deals in importation of goods, got a rude shock when goods imported from Dubai were held at Port of Mombasa for puportedly not paying the right amount of tax for the goods. This adversely affected the operations of the firm making it difficult in servicing a loan.

Before lending to importers of goods, the commercial banks need to be aware if such individuals at any point have come into loggerheads with the KRA officials in paying taxes. Banks need to deal with straightforward businesspersons because it is an institution of trust. Incase an individual or business had come into conflict with the authority on tax issues then such persons should not be lent to because these are the loans, which become bad debts.

Poor monitoring and control:

It is among the least causes of the reasons for default as it contributes to 1.3 percent. The bank is responsible for monitoring the customer's transactions that is to take due care when it comes to customers' funds. The bank's accounting system is supposed to capture all the accounts that show potential for loan default. At times the banks are not aware of the reasons why their clients default. There is a case when bank went ahead and honoured a cheque with no prior arrangement with the owner of an overdrawn account, thus creating unauthorised loan. The customer later on defaulted.

Bankers have a duty of due care when it comes to its customers accounts. They should know the customer's type of transactions and incase the bankers notice any irregular transactions, they should let the customer know and if need be then they alert the Frauds and Invstigations Unit within the bank's network. Bankers should never take any irregular transactions in their customer's account for granted.

Slow moving or unmoving stock:

From the data survey, it takes 1.3 percent of the reasons for default. From the records examination, a business that was involved in importation of goods could not honour its business agreement with its customers as some its consignments arrived late in which they were as late as two months. These were fertilizers for farmers' use and such stock could not be sold until the next planting season. There was loan default due to the fact that there was no adequate time to sell the stock, this resulted into no cash-in-flow for the business

The commercial banks should take an initiative of knowing the type of stocks in which their borrowers deal in. Fast Moving Consumer Goods (FMCGs) like Coca-cola products, sodas, should be given the first priority. Incase a borrowing business has a suitable location, and the turnover is satisfying then there is no reason why the commercial banks

should fear lending to such institutions. But when it is the vice-versa as the businesses involved deals in goods like motor vehicles, then the banks should be a little bit cautious before advancing funds because more often than not such funds lent turn out to be Non-Performing Loans (NPLs).

4.3 Summary of findings and interpretations:

The objective of this study was to identify factors that explain failure by commercial bank borrowers to service their debts. This was in response to the belief that it is high interest rates that contribute significantly to difficulty in servicing loans.

The commercial banks also need to know whom they are lending to. This they can adhere to by adopting Know Your Customer (KYC) project. Besides knowing the customer, their ability to pay should be evaluated.

The bankers need to understand the root causes of Non-Performing Loans (NPLs). Once the root causes have been identified, the symptoms of the problem, then the right steps, the cure, should be taken to alleviate the problem. Among the reasons, which emanated, there some which can be controlled as they are brought about by human beings activities while others can not be controlled

The findings in this study confirm the existence of other factors that bank managers need to pay attention to inorder to reduce the incidences of Non-Performing Loans (NPLs). The major reasons, top six, help in explaining customers failure to service loans include diversion of funds, loss of job, multiple banking, decline in economy, poor management and operations and system errors. With correct action plans in place, these issues can be addressed satisfactorily.

CHAPTER FIVE

CONCLUSIONS AND RECOMMENDATIONS

5.1 Conclusions:

Political aspect can not be avoided but the repercussions can be minimized through taking corrective measures. For example, a bank customer's political star rose by being Member of Parliament if not receiving a political appointment. Such a person turns out to be a politically exposed person (PEP). When such happens, if the bank had taken correct steps, incase of loan default like Knowing Your customer (KYC) and having realisable security then there is no need to worry even if there is default.

As per the economy, the commercial banks should sit side by side by the parties concerned. This can end up seeing VAT to go down, protection of agricultural and tourism sectors and incase of economic bans, the government should talk to the concerned parties for their lifting like the ban of fishmeal products from East Africa by the European Union.

Interest and base lending rates should not be too high to be burdens to the customers but if possible then they should be done on demand-supply principle. There should be a ceiling and the government should set this up. This will protect the customers against exorbitant interest rates recovered by the banks besides making the loans affordable, thus minimizing the chances of default.

In conclusion there are factors that are beyond the human beings control, only precautions against them can be taken while the ones that can be controlled, prevention for their occurrence can be taken in good time.

5.2 Recommedations:

To minimize the problem of Non-Performing loans (NPLs) the commercial banks need to do securitization. Securitization is the tranformation of an illiquid asset into a security that is market tradeable. This will enable borrowers to sell off their liabilities at an early stage thus minimising their loss. Securitization has been adopted by commercial banks as a means of alleviating problems associated with the debt crisis in away of developing emerging market operations to generate income without taking on credit exposures and to further the development of investment banking and related activities.

Another aspect that should be taken into consideration is the poor risk management. The bank need to have very accurate means and ways of dealing with risks involved in lending. There should not be a situation in which ones head is buried in the sand like the ostrich but should face the danger inorder to see ways of evading it if not minimizing it. The banks should be risk takers and not risk averse as the higher the risk the higher the return. The key risks to be considered are business, management, financial, structural, account performance and security.

Business risks entails markets or products, competition, business location, cost structure, supplier power, buyer power or customer base, maturity or age of the industry and business, business cycle business strategy and environmental and social issues. Management risks involves age and experience of key players, work force and labour relations, health of key player, succession and characters of the key players. Financial risks include profitability, capital structure whether it is share capital, reserves, debt or ratio of networth, cash flow projections, capital investment cycle, contingent liabilities and the accounting policy whether there is change of auditors or qualified statements.

Structural risks include the type of facility vis-a-vis purpose, inter-company relationship, split banking, amount sought-adequate and level of own lending. Account performance risks entails account turnover or fluctuations, unpaid cheques and previous utility usage or historical repayments. Lastly security risks considers whether the security is easy to take, easy to realise and its stability in value. Consideration is put on the location adequacy, perfection process, ownership third party guarantees and changes in legislation.

Staff training is very vital in the war against Non-Performing Loans (NPLs). Simple causes like the Basic Banking Course on Principles of Credit should be done internally to all the bank members of staff. This course covers all the important areas of credit and the main acronym used is PRACTISE, P-purpose, R-repayment, A-amount, C-character, T-term, I-interest, S-security and E-experience.

Briefly on the acronym, PRACTISE, the *purpose* of the loan could be working capital, asset acquisition, restructuring liabilities and unexpected expenses. *Repayment* involves; whether the source of repayment has been identified, which could be bullet, balloon, moratorium or scheduled (armotized). *Amount* should be adequate for the purposes sought. *Character* involves Know Your Customer (KYC), who is the bank lending to, the reputation and integrity of the borrower. *Term* considers the proposed tenure of the facility and risk involved is structural (long term vs short term borrowing) and whether the term meets the bank requirements. *Interest* brings concerns like; how does the bank price the interest risks? What is the profit margin for the bank? The components of interest are the base plus margin. *Security* is equally important as it safeguards against the loan default losses. The security should be easy to take, easy to realise and stable in value. *Experience* includes concerns such as; what is the experience of the key persons in this particular line? Any other relevant experience and what is being done to bridge the skills gap.

The commercial banks need to demand from the borrowing customers' realisable securities, insurance covers and adequate quarantors to safequard their funds against loan default

5.3 Limitations of the study:

The obvious limitation of this study is the accuracy of records. The records involved are not in the soft copy but rather physical files, which makes the extraction of information tedious and their accuracy raises qestions. Thus the section of data collection became a nightmare.

The research covers a very sensitive and confidential part of the borrower-lender relationship. At certain stages in the research, the sicerity of the reasons for default cast shadows of doubt, as there was no total freedom of expression lest a breach of contract is committed in the borrower-lender relationship.

There is so much to be done in the research, but the time factor is a limitation. The time factor acts as a barrier for the research as it seems that the area of the research is so vast that it could not be effectively handled within the time frame.

5.4 Suggestions for further study:

Future research in this area may consider finding out other reasons other than the ones mentioned in this research as causes of Non-Performing Loans (NPLs) to the commercial banks.

Undertaking a study in credit risks and management of credit risks may further this reseach. Credit risks if not tackled well, contribute significantly to the prolem of Non-Performing Loans (NPLs). This will give a clearer picture of all the risks involved in lending as well as the solutions for them that could result in reduction to the magnitude of Non-Performing Loans (NPLs) in the commercial banks' financial stataements.

This research could be possibly carried out annually to evaluate how effective the solutions offered in the reduction of the magnitude of Non-Performing Loans (NPLs) in the commercial banks' financial statements.

Doing inter-bank study inorder to determine which commercial bank is vulnerable to Non-Performing Loans (NPLs) problem can further this research in finding out solutions before the bank collapses.

TABLES

Table 1

FACTORS TO DETERMINE MONTHLY FIXED LOAN REPAYMENT AT AN INTEREST RATE OF 19% PER ANNUM:

o of onths	Installment Factor	No. of Months	Installment Factor	No. of Months	Installment Factor	No. of Months	Installment Factor	No. of Months	Installment Factor	No. of Months	Installment Factor
	1.015833	51	0.028725	101	0.019906	151	0.017462	201	0.016537	251	0.016146
	0.511906	52	0.028365	102	0.019827	152	0.017434	202	0.016525	252	0.016141
	0.343944	53	0.028020	103	0.019749	153	0.017407	203	0.016514	253	0.016137
	0.259974	54	0.027687	104	0.019673	154	0.017380	204	0.016503	254	0.016132
	0.209599	55	0.027378	105	0.019599	155	0.017354	205	0.016492	255	0.016127
	0.176024	56	0.027061	106	0.019527	156	0.017328	206	0.016481	256	0.016122
	0.152047	57	0.026765	107	0.019456	157	0.017302	207	0.016471	257	0.016118
	0.134069	58	0.026480	108	0.019387	158	0.017277	208	0.016460	258	0.016113
	0.120092	59	0.026205	109	0.019319	159	0.017253	209	0.016450	259	0.016109
	0.108913	60	0.025941	110	0.019253	160	0.017229	210	0.016440	260	0.016104
	0.099771	61	0.025685	111	0.019189	161	0.017205	211	0.016431	261	0.016100
	0.092157	62	0.025438	112	0.019126	162	0.017182	212	0.016421	262	0.016096
	0.085716	63	0.025200	113	0.019064	163	0.017159	213	0.016411	263	0.016092
	0.080199	64	0.024970	114	0.019003	164	0.017137	214	0.016402	264	0.016088
	0.075420	65	0.024747	115	0.018944	165	0.017115	215	0.016393	265	0.016084
	0.071241	66	0.024532	116	0.018886	166	0.017093	216	0.016384	266	0.016080
	0.067557	67	0.024324	117	0.018830	167	0.017072	217	0.016375	267	0.016076
	0.064283	68	0.024122	118	0.018774	168	0.017051	218	0.016366	268	0.016072
	0.061357	69	0.023927	119	0.018720	169	0.017031	219	0.016358	269	0.016068
	0.058725	70	0.023738	120	0.018667	170	0.017011	220	0.016349	270	0.016064
	0.056346	71	0.023554	121	0.018615	171	0.016991	221	0.016341	271	0.016061
	0.054185	72	0.023377	122	0.018564	172	0.016972	222	0.016333	272	0.016057
	0.052214	73	0.023204	123	0.018515	173	0.016953	223	0.016325	273	0.016054
	0.050409	74	0.023037	124	0.018466	174	0.016934	224	0.016317	274	0.016050
	0.048749	75	0.022875	125	0.018418	175	0.016916	225	0.016309	275	0.016047
	0.047219	76	0.022718	126	0.018371	176	0.016898	226	0.016301	276	0.016043
	0.045804	77	0.022565	127	0.018326	177	0.016880	227	0.016294	277	0.016040
	0.044491	78	0.022416	128	0.018281	178	0.016863	228	0.016287	278	0.016037
	0.043271	79	0.022272	129	0.018237	179	0.016846	229	0.016279	279	0.016034
	0.042133	80	0.022131	130	0.018194	180	0.016829	230	0.016272	280	0.016030
	0.041069	81	0.021995	131	0.018152	181	0.016812	231	0.016265	281	0.016027
	0.040074	82	0.021863	132	0.018110	182	0.016796	232	0.016258	282	0.016024
	0.039140	83	0.021608	133	0.018070	183	0.016780	233	0.016251	283	0.016021
	0.038262	84	0.021486	134	0.018030	184	0.016765	234	0.016245	284	0.016018
	0.037436	85	0.021367	135	0.017991	185	0.016749	235	0.016238	285	0.016015
	0.036656	86	0.021251	136	0.017953	186	0.016734	236	0.016232	286	0.016012
	0.035920	87	0.021138	137	0.017916	187	0.016719	237	0.016225	287	0.016010
	0.035223	88	0.021029	138	0.017879	188	0.016705	238	0.016219	288	0.016007
	0.034564	89	0.020922	139	0.017843	189	0.016690	239	0.016213	289	0.016004
	0.033938	90	0.020817	140	0.017808	190	0.016676	240	0.016207	290	0.016001
	0.033344	91	0.020716	141	0.017773	191	0.016663	241	0.016201	291	0.015999
	0.032778	92	0.020617	142	0.017739	192	0.016649	242	0.016195	292	0.015996
	0.032241	93	0.020520	143	0.017706	193	0.016636	243	0.016189	293	0.015994
	0.031728	94	0.020426	144	0.017674	194	0.016622	244	0.016184	294	0.015991
	0.031239	95	0.020334	145	0.017642	195	0.016610	245	0.016178	295	0.015989
	0.030773	96	0.020244	146	0.017610	196	0.016597	246	0.016173	296	0.015986
	0.030327	97	0.020244	147	0.017580	197	0.016584	247	0.016167	297	0.015984
	0.029900	98	0.020157	148	0.017549	198	0.016572	248	0.016162	298	0.015989
	0.029492	99	0.020071	149	0.017520	199	0.016560	249	0.016157	299	0.015979
	0.029100	100	0.019988	150	0.017491	200	0.016548	250	0.016151	300	0.015977

To determine the fixed monthly loan repayment amount, application form eligibility analysis section item J): -

Multiply the loan amount times the installment factor adjacent to number of months the loans is to be repaid.

For example: - a loan of Kes. 500,000 a 19% for 48months: -

Repayment is = 500000x 0.029900=Kes. 14950 00 per month

Instalment factors will charge with change in base rate and it is the responsibility of credit Department to replace this schedule.

Source: Standard Chartered Bank (K) Limited

Table 2

PERSONAL LOANS REPAYMENT SCHEDULES

(i) Fixed monthly loan repayments @ 23%

	Repayment period in months				
Loan amount	6	12	24	30	36
10,0000.00	17,802.00	9,408.00	5,237.00	4,414.00	3,871.00
20,0000.00	35,605.00	18,815.00	10,475.00	8,828.00	7,742.00
30,0000.00	53,407.00	28,223.00	15,712.00	13,242.00	11,613.00
40,0000.00	71,210.00	37,630.00	20,949.00	17,656.00	15,484.00
50,0000.00	89,012.00	47,038.00	26,187.00	22,070.00	19,355.00

(ii) Schedule for unsecured personal loan

Net salary	Maximum loan(three times Net salary)	40% of Net take home pay(i.e monthly repayment limit)	Arrangemet fee(3%, max Kes 10,000)	Repayment period(months)		
				12	24	36
30,000.00	90,000.00	12,000.00	2,700.00	7,500.00	3,750.00	2,500.00
40,000.00	120,000.00	16,000.00	3,600.00	10,000.00	5,000.00	3,333.00
50,000.00	150,000.00	20,000.00	4,500.00	12,500.00	6,250.00	4,167.00
100,000.00	300,000.00	40,000.00	9,000.00	25,000.00	12,500.00	8,333.00
200,000.00	500,000.00	80,000.00	10,000.00	41,667.00	20,833.00	13,889.00
500,000.00	500,000.00	200,000.00	10,000.00	41,667.00	20,833.00	13,889.00

Source: Standard Chartered Bank (K) Limited

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APPENDICES

APPENDIX I

SUMMARY OF REASONS WHY CUSTOMERS DEFAULT:

LOAN TYPE	AMOUNT	TENURE	INTEREST RATE PAYABLE	CLIENT'S PREFERED INTEREST RATE	WHY DEFAULT
Overdraft	250M	1 year	28%	16%	(i) Dissolution of the company
Medium Term Loan	16M	3 years	20%	18%	(ii) Bankruptcy
					(iii) Take over
					(iv) Prolonged change in Base Lending Rate
					(v) KRA Advised rate
					(vi) T-Bill Rate Verses Banks" Base Lending Rate
					(vii) Diversion of resources due to corruption
					(viii) High interest rate
					(ix) Poor monitoring and control
					(x) Competition
					(xi) Operation and system errors
					(xii) Multi-banking
Short term Loan	20M	2 years	22%	15%	(i) Sole proprietor's death
Overdraft	12M	1Year	20%	16%	(ii) Sole proprietor falls sick
					(iii) Distributors tied to stock by manufacturers
					(iv) Rise of interest rate
					(v) Decline of business due to economic, social and political factors
					(vi) Mixing business and family interests
					(viii) Lack of proper knowledge in the business and interest rate trends
					(viii) Diversion of resources or funds borrowed
					(ix) Dissolution of the partnership or the solepropriatorship
					(x) Poor monitoring and control
					(xi) Breach of contract
					(xii) Conflict wit the law
					(xii) Multi-banking
Secured loans	3M	4 years	16%	9%	(i) Loss of job
Unsecured Loans	1.5M	2 years	21%	7%	(ii) Death
					(iii)High interest rate not foreseen in the repayment projection
					(iv) Diversion of resources or funds borrowed

APPENDIX II

DATA COLLECTION

Case no.	R1	R2	R3	R4	R5	R6	R7	R8	R9	R10	R11	R12	R13	R14	R15	R16	R17	R18	R19	R20	R21	R22	R23
1	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
2	0	1	0	0	0	0	0		0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
3	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
4	0	0	0	0	0	0	0	1	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0
5	0	0	0	0	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0	0	0	0
6	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
7	0	1	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
8	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
9	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0
10	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0
11	0	0	0	0	1	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	1
12	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
13	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
14	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
15	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
16	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
17	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0
18	0	1	0	0	1	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
19	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0
20	0	1	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
21	0	0	0	0	0	1	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
22	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
23	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
24	0	1	0	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0	1	0	0	0
25	0	1	0	0	0	0	1	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
26	0	0	0	0	0	0	0	0	0	0	0	0	1	0	1	0	0	0	0	0	0	0	0
27	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
28	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0
29	0	0	0	0	0	0	1	1	0	1	0	0	0	0	0	0	0	0	1	0	0	0	0
30	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	1	0	0	0	0
31	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0
32	0	0	0	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0	1	0	0	1
33	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	1	0	0
34	0	0	0	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
35	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0
36	0	1	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
37	0	0	0	0	0	0	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0	1
38	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
39	0	1	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
40	0	0	0	0	0	0	0	0	0	1	1	0	0	0	0	0	0	0	0	0	1	0	0
41	0	0	0	0	1	0	0	0	0	0	1	0	0	0	0	0	0	0	0	1	0	0	0
42	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
43	0	1	0	0	0	0	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0	0
44	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
45	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0

46	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
47	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	1
48	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0
49	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	1	0	0
50	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
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52	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0
53	0	0	0	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0	0	1	0	0
54	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0
55	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
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57	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
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63	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0
64	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
65	0	1	0	0	0	0	1	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
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71	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
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75	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
76	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
77	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
78	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
79	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
80	0	0	0	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
81	0	1	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
82	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
83	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0
84	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
85	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
86	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
87	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
88	0	0	1	0	0	0	0	0	0	0	0	0	1	0	1	0	0	0	0	0	0	0	0
89	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
90	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
91	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
92	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	1	0	0
93	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
94	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
95	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
96	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1

97	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
98	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
99	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
100	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	1	0	0
101	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
102	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
103	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
104	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	1
105	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
106	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
107	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
108	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
109	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
110	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
111	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
112	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
113	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
114	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
115	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
116	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
117	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
118	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
119	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
120	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
121	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
122	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0
123	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
124	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
125	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0
126	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
127	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
128	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
129	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
130	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
131	0	0	1	0	0	0	0	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0
132	0	0	1	0	0	0	0	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0
133	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
134	0	0	0	0	1	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
135	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
136	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
137	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
138	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
139	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
140	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
141	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
142	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
143	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0
144	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
145	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
146	0	1	0	0	0	0	0	0	0	0	0	0	1	0	1	0	0	0	0	0	0	0	0
147	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0

148	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
149	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
150	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0
Total	7	28	7	4	10	20	6	15	3	11	40	4	3	2	5	2	3	15	2	5	8	3	17
Total(%)	5	19	5	3	7	13	4	10	2	7	27	3	2	1	3	1	2	10	1	3	5	2	11
Rank	9	2	8	13	7	3	12	5	17	7	1	13	17	21	13	21	17	5	21	13	9	17	4

Where:

1 implies that the reason brings in loan default to the case, 0 implies that the reason does not bring in loan default to the case, R1 – Political, R2 – Economical, R3 – Interest Rate, R4 – Death, R5 – Illness, R6 – Loss of job, R7 – Lack of knowledge, R8 – Poor management, R9 – Dissolution, R10 – Disasters, R11 – Diversion of funds, R12 – Take over, R13 – Base lending rate, R14 – KRA interference, R15 – Treasury bill rate, R16 – Poor monitoring and control, R17 – Bankruptcy, R18 – Operation and system errors, R19 – Slow or unmoving stock, R20 – Conflict with the law, R21 – Competition, R22 – Breach of contract and R23 – multiple banking.

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