DETERMINANTS OF LOAN REPAYMENT DEFAULTS IN MICROFINANCE BANKS IN KENYA

BY

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DECLARATION

I Dorothy Mumbua Musango declare that this Research Project is my original work and has not been presented for award of degree in any other university.

Signature... Date...............................

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DEDICATION

I dedicate This Project to the Almighty God for the Gift of Good Health and Strength throughout My Studies, and to My Parents & Siblings for Support, encouragement and Motivation all throughout my studies and in this research project.

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LIST OF ABBREVIATION AND ACRONYMS

CBK **:** Central Bank of Kenya

MFB **:** Micro Finance Bank

MFI **:** Micro Finance institution

ATM **:** Automated Teller Machines

ABSTRACT

The Monitoring and effective controlling of non-performing advances is of crucial importance to any Microfinance Bank financial performance and the economy's financial environment. The future is always uncertain and there is a credit risk associated with loans advances to borrowers which can lead to financial Crisis/distress in the institutions. Loan Repayment default can be voluntary or involuntary and it can lead to Lenders additional cost which include loan recovery costs and Cost of refinancing. The objective was to investigating the Determinants of Loan Repayment Default in Microfinance Banks in Kenya. In order to examine the factors that cause loan repayment default in Microfinance Banks in Kenya, descriptive Research design was applied. The Target population was 13 Licensed Microfinance banks in Kenya. A Random Sampling procedure was used amongst the target population. Two credit officers and two borrowers were randomly selected from each of the 13 MFB. The sample size was 26 credit Officers and 26 borrowers with a total of 52 Individuals. The Researcher used primary data which was obtained from credit officers and borrowers by administering of questionnaires. Analysis for the study data was done by use of descriptive statistics which made use of percentages, mean, median and frequency tables to present the data. SPSS and a regression model were employed to analyze the data. Loan Repayment default was the dependent variable, while Borrower characteristics, institutional factors and the Loan characteristics were the independent variables. The Findings of the study indicated that there was a significant positive relationship between institutional characteristics, borrowers' characteristics, the loan specific factors with loan repayment default in microfinance banks in Kenya. From the study it's recommended that the credit offering institutions should train their credit officers so that they can be competent and thorough when conducting credit appraisal. This will ensure that the institution advances credit to those borrowers who have the ability to pay back and therefore reducing the rate of loan non-repayment. It is important for the management to conduct a thorough and in depth appraisal of the borrowers before advancing credit to them this will reduce the rate of loan defaulting.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Microfinance Banks play are key to any countries economic Growth and Development. Their main activity is advancement or extension of credit facilities to borrowers. They generate most of their revenue from interest on loans as well as other income from non-funded business and transactional income from activities such as over the counter withdrawals, income from ATM/mobile banking platforms. These organizations are exposed to the different types of risk. Risk management is a critical aspect to the MFBs to ensure their survival and minimization to the risk exposures. Mac Donald and Koch (2006) as cited by Ndungu (2014) notes that although loans are the greatest contributors of operating income in microfinance institutions, they represent a greater exposure to the institutions.

A loan essentially means monies that have been advanced to a borrower who will repay back the principle plus some interest. Non loan repayment results in bad debts which have adverse negative impact on the financial performance of the institutions, since they negatively affect the profitability of firms. Kipyego (2013) notes that loan defaults is increasingly threatening the existence of the microfinance institutions. Effective credit management is therefore essential in order to ensure that the loans extended to the borrowers are repaid on time and that the profits generated are not negatively affected by provisions for bad loans.

There are different theories that explain why loan repayment default occurs. For instance, information asymmetry theory where information gap exist between the borrowers and the lender. The lender acting on the available information provided by the borrower may end up advancing credit to borrowers who do not qualify for the same. Agency problems as explained in the Agency Theory may result in the agents not performing their duties and mandates as expected by their principles. This can lead to poor monitoring and advancing credit to without performing the due diligence which the end results is non-performing loans.

Microfinance institutions at times find themselves having a loan portfolio that is non-performing (loans are not paid back by the borrowers at the agreed time and agreed repayment amount).Most of the target customers for this institutions are individuals who have no collateral for the loans and hence the institutions find themselves unable to recover back all their monies and the end result is losses due to loan defaults. This study therefore intends to investigate the determinants of Loan Repayment Defaults in Microfinance Banks in Kenya.

1.1.1 Loan Repayment Default

Different MFIs define Loan Repayment Default in many different ways according to their Credit Policy. According to Phillips and VanderHoff, (2004) Cited by Maigua (2017), a loan is said to have been defaulted when the borrower fails to pay the principle and /or interest or part of the principle. A loan is said to have been defaulted if the borrower does not make a payment after the first day when the loan instalment falls due (Ndungu, 2014). If it is not repaid within 30 days after the instalment has fallen due, its termed as a bad loan.

According to Maigua (2017) Loan defaults have effect to both the borrower and the institution. Bad loans posse a credit risk to the lender and may lead to losses and financial constraints when the borrower completely fails to repay and efforts to recover the loan are futile. The borrower might end up been blacklisted in the credit reference bureau (CRBs) and might end up unable to access credit facilities from formal financial institutions until they clear up their names by repaying back the loans to the lender. In addition their collateral end up been sold in order to recover the loans advanced to them.

1.1.2 Determinants of Loan Repayment Defaults

According to Berger and De Young (1997) cited in Ndungu (2014) most Non Performing loans in MFIs are due to inadequate loan underwriting, poor monitoring and Control by the MFI managers. Kibosia (2012) argued that loan repayment is determined by the character of the borrower, and the type of the loan as well as interest rates. The character of the individual is of great importance in extending credit to a borrower. This is because some borrowers with a bad character will borrow with no intention of repaying back the loans even if they have the ability to service the loans. High interest rates with poor economic conditions influence the ability of the borrower to repay the loans.

According to Ndungu (2014), institutional/Micro economic factors and customer characteristics are the main contributors of loan non repayment in Micro finance institutions. Institutional factors causing loan non repayment include: poor training to loan officers on how to appraise borrowers before extending loans to them, lack of effective and efficient monitoring information systems for tracing payments, and high interest rate charged on the loans. Macroeconomic variables such as inflations and government restrictions on interest rates also determine loan non repayment. Finally, Customer characteristics such as low income of households, the type of security or collateral for the loan and failure to use the borrowed money for the intended purpose influences loan Non Repayment in MFIs.

1.1.3 Loan Repayment default and its Determinants

The failure to repay loans is influenced by many factors. This include institutional factors, which are factors specific to the institution such as monitoring and control of loans advanced, trainings given to the loan officers; the borrower's characteristics which include the character of the individual, the income level of the borrower and the loan specific factors such as the amount of loan advanced to the borrower, the duration of repaying back the loan. Non Repayment of Loan by Borrowers may be voluntary and Non-voluntary (Waithera 2014).Institutional factors, Borrowers characteristics and the Loan specific Factors are the main Determinants of Loan Repayment Default.

In line with ensuring the loan repayment defaults are minimized, organizations that advance credit to Borrowers must know the factors that lead to loan non repayments and come up with ways to mitigate the risk of Default. This study therefore is aimed at establishing the determinants of loan repayment Default.

1.1.4 Microfinance Banks in Kenya

According to the Microfinance Act 2006, a microfinance Bank is any Licensed Company that carries out microfinance Bank Business which involves accepting deposits/cheque from members of the Public, providing short term loans to SMEs or to low income earners who are characterized by use of different collateral. Waithera (2006) argues that Microfinance involves providing credit to low income earners and the poor who form their own small scale businesses to better their living. In Kenya today, there are 13 Microfinance Bank institutions that have been licensed by the CBK namely Faulu MFB, Kenya women MFB, Rafiki MFB, Caritas MFB, Century MFB, Choice MFB, Daranja MFB, Remu, Smep MFB, Sumac,U&I, Uwezo and Maisha MFBs.Operations of MFB may be is defined geographically, or administratively or on a certain criterial as the Minister of Finance may deem necessary.

MFBs practice both individual and group lending mechanism. In a group lending mechanism, the individuals in the group provide collateral or loan guarantee to any member of the group who applies for a loan. The members monitor each other and exclude risky borrowers from participating hence making prompt loan repayments (Modurch,1999).In the event one member doesn't repay his/her loan instalment, the group members raise the installment(Ndungu,2014).This mitigates the risk involved in the group lending mechanism.

Extension of credit facilities to borrowers in microfinance banks involve the risk of default since they give out the loans with the promise from borrowers that's they will repay the Interest plus the principle amount. The future is uncertain and events can arise which may make the borrower unable to repay the loan as per the agreed terms and conditions. As a result the institutions must make sound decisions by projecting in to the future to ensure loans are repaid at the agreed time (Ndungu, 2014).

Most Microfinance Banks have come with flexible repayment frequencies which range from weekly, monthly , quarterly and even termly (mostly for schools whose mode of operation is termly).The frequency depends on the nature of the business activity, purpose of the loan and /or household cash flow generating capacity.

1.2 Research Problem

The Monitoring and effective controlling of non-performing advances is of crucial importance to any Microfinance Bank financial performance and the economy's financial environment as cited by Maigua (2017). The future is always uncertain and there is a credit risk associated with loans advances to borrowers which can lead to financial Crisis/distress in the institutions. Muthoni (2016) notes that Loan Repayment default can be voluntary or involuntary and it can lead to Lenders additional cost which include loan recovery costs and Cost of refinancing. These costs have effect to both the lender and the borrower (The borrower end up losing the recovered collateral to the lender).

Numerous global studies have been carried out on the factors that influence Loan repayment in different Sectors. Karenkye (2014) carried on a study in Ghana to find out what caused Loan defaults in MFIs. Loan Defaults were found to be caused by Inadequate Loan sizes, High interest Rates and Poor Appraisal. Makorere (2014) carried on a study in Tanzania on the factors causing Loan Repayment Default.

Local Studies have also been carried out with generalization and in Different sectors. Akehege (2011) studied on what causes Non-Performing Loans and it was evident from the study; level & Source of Income and poor credit Analysis have major impact on loan repayment Default. Kipkech (2005) conducted a study on factors that determined Loan Default basing his study on the Higher education Board. Kibosia (2012) did a study on what Determined Loan defaults in SMES in Kenya Commercial banks and found out that Loan defaults is influenced by The character of The applicant and poor credit Monitoring.

From The analysis of the various empirical studies, it's evident that studies have been done in different sectors Such as Higher Education Board, SMEs, and Commercial Banks in general, very few studies have been carried out on the Loan Repayment Defaults in Microfinance Banks. Therefore the researcher intended to investigate what are the Determinants of Loan Repayment Defaults in MFBs in Kenya.

1.3 Research Objective

The objective of this study was to find out the Determinants of Loan Repayment Default in Microfinance Banks in Kenya.

1.4 Value of the Study

This research work will be of great importance to various stakeholders and various Future scholars who would wish to carry out further study on the determinants of Loan repayment Defaults in any other sectors. It will help MFB management to know the main determinants of loan defaults in their organization. As a result they will be able to develop mechanism to curb or mitigate the risk of loan non-repayment in their organization. To the Credit Officers, this study will enlighten then on why they need to carry out a due diligence before advancing credit to the various borrowers and the Importance of credit Monitoring and control.

MFBs as a whole will be able to benefit from the study as they will know what actually determines loan Repayment Default .and be able to develop a mechanism/Model that will help in predicting the chances of loan Default. Since Loan Defaults affect the financial performance of Organizations, the management as the will understand the importance of credit officer training on customer loan appraisal, and why credit officers ought to be remunerated well to ensure that they execute their duties of loan monitoring well.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This Chapter Discusses the Theories relevant for the study and the Empirical Literature review.

2.2 Theoretical Literature Review

This covers the theories that are relevant to the study conceptualization.

2.2.1 Agency Theory

This theory explains the agency relationship that may exist between two parties, mainly between a principle (mainly shareholders in a business) and its agent (The managers or company executives). The agents represent the principle and enter into contractual agreements with third parties on behalf on the principle. Since the decisions and contracts agreed between the agent and the third party affect the principle, agency problems may arise. Therefore the Agency theory tries to resolve the problems that may arise due to unaligned goals or risk aversion between the principle and the agent. This theory tries to find out the mechanisms that can be used to motivate the agents in order to enable them make the right decisions regarding a firm and of interest make decisions that do are aimed at maximizing the welfare of the firm in general.

In this research study, the principle is mainly the MFBs and the borrowers are the agents are the borrowers. The chances of a borrower failing to repay and its relationship with the agency theory is of a greater importance to this study. The Information asymmetry aspect, the Moral hazard perspective that make lenders give out loans to borrowers even when the chances of loan repayment is zero can be explained by the use of agency theory Adverse selection and moral hazard are some of the causes of Agency problems between a lender and a borrower. Adverse selection can be defined as a situation of Information asymmetry that can occur before a transaction. During the lending process the borrower might have information that the project been financed is not viable, and may not disclose the information to the Lender. The lender due to lack of the information, will advance the loan to the borrower who may end up not repaying the loan. On the other hand Moral Hazard means the malpractices that may occur in a financial institution mainly because one party that is insulated or protected from a risk is less concerned with the negative outcome of a risk that might occur. The loans advanced to borrowers are mainly insured against some risk, for instance if a car loan is extended to the borrower, the car is insured against accidents &theft. As a result the Borrower might not take the required precautions against the insured risk.

2.2.2 The Theory of Delegated Monitoring of Borrowers

This theory aims at reducing the cost of monitoring borrowers by the use of available information which is important in resolving problems that might arise between the borrower and the lender (Maigua, 2017). The Monitoring of a borrower is done before and after loan advancement. It involves gathering all the relevant information and screening all the available information about a borrower prior to the advancement of a loan. After the loan is processed, the MFB s also monitor the borrower to ensure that the monies are not diverted to other use. If the Borrower diverts the monies advanced to him /her to other projects other than the intended use, contributors majorly to Loan non repayment.

This Theory is of importance to this study as it highlights the importance of monitoring Borrowers and ensuring that they adhere to the Terms of agreement as stipulated in the Loan contract. MFBs require borrowers to open and operate accounts with them. This helps to ensure that they monitor the cash inflows and outflows as well as the loan payments.

2.2.3 Information Asymmetry Theory

The Theory of Information Asymmetry Is based on the notion that the lender may not have all the information about the projects the borrower is financing using the borrowed funds. As a result of the information gaps, Cases of problems of Moral Hazards and adverse selection arise.

2.3 Determinants of Loan Repayment Default

These are the factors that lead to non-repayment of loans by borrowers as stipulated in their loan/Debt Contract or when the borrower violates some conditions as stipulated in the contract. A loan Repayment Default simply means failure of the borrower to pay back loan installments when they fall due. There are various factors that determine loan Repayment Defaults as discussed below:

2.3.1 Borrowers characteristics

These are factors that are specific to the borrower which may influence his/her loan repayment (Maigua, 2017). According to Nawai & Sharrif (2010) as cited by Maigua (2017), this includes the income level of the borrower, age and the gender of the individual. According to the study by Maigua (2017), the age of the borrower, the number of years he/she banked with the microfinance institution and the kind of collateral had effect on the rate of loan repayments. Non-financing of the projects which the borrower intended to finance due to diverting borrowed funds results to projects failure to generate cash flows as projected by the lender leading to loan defaults. The character of the individual determines if the loan will be repaid or not. Some borrowers borrow with no intention of repaying back the loan which definitely leads to loan repayment default.

2.3.2 Lenders/Institutional Characteristics

These are factors internal to the financial Institution that is advancing the credit (Loan) Facility that influence the loan Repayment Rate. They Include: the time taken by the institution from when the borrower does the loan Application to the time the actual loan disbursement is actualized. Delayed loan disbursement cause delay to financing of the borrowers' projects and as a result it may delay cash flows as projected by the borrower hence leading to a loan repayment default. The Financing cost is considered as a factor influencing loan repayment default. High loan application costs, insurance costs for the loans and other costs such as valuation cost for the loan collateral influence loan repayment rate.

The training to the loan/Credit officers also contributes the loan repayment default. Poor loan appraisals by the credit officers lead to advancing loans to borrowers who may not have the ability to repay the loan leading to Loan non- repayment. Poor Monitoring and control of the loans by the institution contribute to loan non- repayment. When institutions advance loans to the borrowers and fail to monitor how the borrower uses the funds i.e. if the loan was used for the intended purpose and also monitoring if the borrowers are making loan repayments as required influences the rate of loan repayment. According to Koranky (2014), poor evaluation and absence of Checking of loan repayments are major causes of loan repayment defaults.

2.3.3 Loan Characteristics

These are factors specific to the loan advanced to the borrower. They include size of the loan, the repayment duration, the interest charged, other conditions such as penalty on late or non-loan repayment. If the borrower is underfunded (the amount of loan advanced does not fully finance his/her project) the borrower is likely to default because his business may not be able to raise sufficient cash flows for business operations as well as repaying back the credit borrowed. The interest rate that the lender charges on the loan is a factor contributing to loan repayment rate as high interest rates may make the borrower unable to service their loans as required

2.3.4 Microeconomic variables

Microeconomic Variables such as inflation and government restriction on interest rates such as interest rate capping influence the loan repayment rates by borrowers

2.4 Empirical Literature Review

Kibosia (2012) carried out an investigation on the factors that determined Loan default among SMEs in Kenyan commercial banks. Her objective was to establish the main factors that determined loan defaults In SMEs. She further narrowed her study by aiming to establish if there was a relationship between what caused loan non repayment in commercial banks and the lack of loan repayments in the SME sector. She used a descriptive study design to collect data for her study. Her study population was the 44 banks and she sampled the all the banks in Nairobi. The sample population for the study was arrived at by employing a census Survey. She used questionnaires to collect her data and multiple Liner Regression in the analysis of the data collected. From the study, the years the businesses was in operation as well as the interest charged on the loans had effect on loan non repayment rates. It also found out that the character of the borrower, the type of loan, and the repayment period. The researcher recommended that apart from commercial banks adopting credit scoring in vetting its clients during loan applications, emphasis should be put in managing the credit risk in their organizations. All determinants of loan Defaults were not covered in the study.

Kariuki (2014) sort to find out the factors that were key in Influencing Non -performing Loans among MFIs in Kenya. He aimed at assessing the effect of institutional characteristics, customer characteristics and micro economic Variables on non-performing loans. He used a Descriptive survey approach in his study in all the 52 MFIs in Kenya which were his population. His sample size was 52 Respondents from the 52 MFIs who were mainly credit officers/Managers from the MFIs.A response rate of 69%

was realized from the questionnaires issued. In analyzing the collected Data, descriptive statistics were used which aided in measuring the interrelationship between the variables. He used MS excel and SPSS version 17 to display the information. The study found out that Institutional characteristics contributed most to non-performing loans of MFIs followed by Macroeconomic variables and lastly Customer characteristics. From the study, it was recommended that MFIs should have good Credit Procedures that were to assist the organization in selecting clients for loan approvals. The study also recommended that organizations should have systems to aid in monitoring of loans and mechanisms of dealing with customers who defaulted in repaying back the loans by coming up with clear plans and procedures

Kiraithe (2015) conducted a study on the factors that influenced Loan Defaulting by SME owners in Kenya. The researcher studied the SMEs within Thika Township of Kiambu County. The study was aimed at investigating what influenced loan defaulting among SME owners In Thika Township in Kiambu County. He also sought to establish the considerations that MFIs used in granting Loan to SMEs Owners, the characteristics of SME owners that influenced defaulting. The researcher also aimed at understanding the loan Trainings that was given to the SME owners and its relation to loan defaulting. The researcher also aimed at examining the enterprise related factors that fostered loan defaulting by SME owners. The researcher used as descriptive study design. The population of the study was 500 SME owners who operated in Thika Township, Kiambu County. The researcher used stratified random sampling for the SME owners with a sampling size of 50 respondents and 10 key informants. In order to collect data structured questionnaires were administered to the SME owners and detailed discussion questions for the key informants. The study found out that diversion of loan funds and lack of need to achieve business influence SME owner's defaults.

Muriithi (2013) studied on why there was nonperformance of Loans among Kenyan commercial banks In Kenya. He aimed at finding out the causes of non-performing Loans He targeted the 43 banks in Kenya as per the CBK banking supervision Report of 2012.The data used for the study covered a five year period from 2008 to 2012 with the use of secondary data from published annual reports .The statistical package for SPSS version 17 in analysis of the collected data while spreadsheets were used to aid in data presentation. There existed a positive relationship between the non-performing loans and the inflation rate (0.136) with a negative correlation between the real interest rate (which was -0.468 as per the study) as well as to the negative correlation among growth rate in loans (-0.013).It was from this findings that it was recommended that the government needed to come up with measures that controlled real interest rate in Kenya and commercial banks needed to come up with policies that control the amount of loans.

Mosha (2016) carried out an investigation on what determined loan defaults in microfinance institutions in Tanzania. He selected two Microfinance institutions in two selected branches which were PRIDE and FINCA. The objective was determining factors for loan defaults in MFIs in Tanzania. The study was covered a period of 10Years that is from the Year 2004 to 2014.Cross sectional study design was used to gather information for the study. Structured and semi structured interviews were administered among the selected 196 respondents to gather primary data. Descriptive statistics and logistic regression were employed in analyzing the collected data. He found out that that the loss of collateral and the denial of future loans were the major effects of loan defaults.

Asongo and Idama (2015) studied on the factors causing of Loan defaults in microfinance banks in Nigeria. They based their study on the case Standard Microfinance bank, Yola in Adamawa State in Nigeria. They used Questionnaires to collect data. The data was the analyzed by the use of SPSS version 21.It was found out that failure to supervise the Utilization of Loans advanced, Client Dropouts and staff Turnover, not reminding some customers on loan repayment, lack on penalty on loan non repayment by some customers, multiple borrowing and failure of some staff to comply with the policies. It was recommended that microfinance banks should practice best policies and optimum performance.

2.5 Conceptual Framework

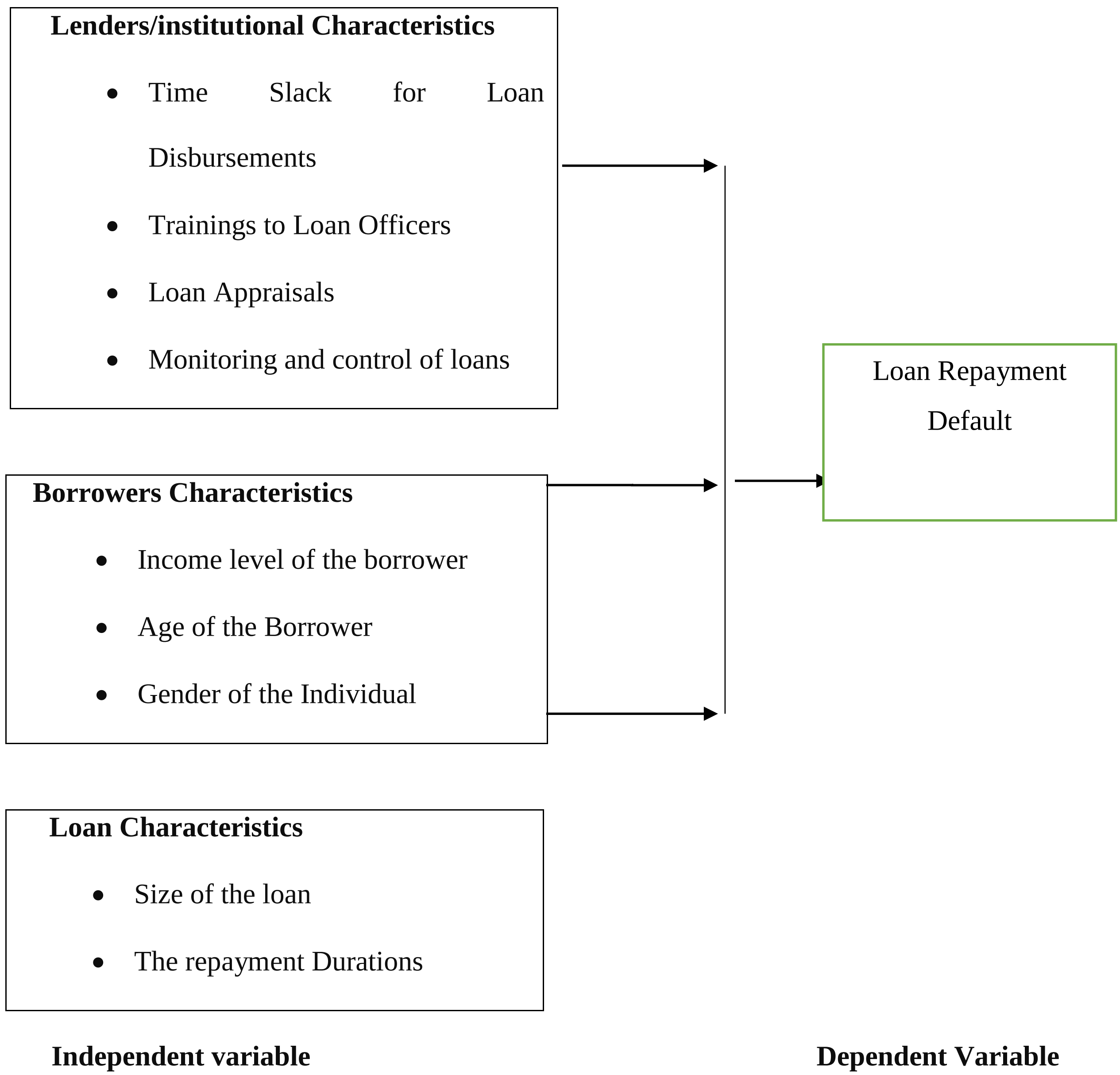

Figure 2.1: Determinants of Loan Defaults

2.6 Summary of Literature Review

The propositions that explain why Loan repayment Default occur have been analyzed in the chapter. The existing studies that relate to the researchers intended study were reviewed. It was evident loan repayment default is determined by varies factors that include the borrowers' characteristics such as the income level of the borrower, the age of the borrower as well as the character of the individual. Other factors include the institutional characteristics and loan specific factors. Most of the studies already done had been generalized in different sectors such as commercial banks, SMEs. Very few studies had been done on microfinance banks and therefore the researcher will bridge the gap by the research study.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The research design, the target and sample population, the sampling procedure, and the data collection tools are discussed in this chapter.

3.2 Research Design

A descriptive research Design was used to examine the factors that cause loan repayment default in Microfinance Banks in Kenya.

3.3 Population

The population elements were credit officers and the borrowers in the institutions. The Target population was 13 Licensed Microfinance banks in Kenya. This study targeted two Credit officer and two borrowers from each of the 13 MFBs.

3.4 Sample and Sampling procedure

A Random Sampling procedure was applied amongst the target population. One credit officer and one borrower were randomly selected from each of the 13 MFB. The sample size was 26 credit Officers and 26 borrowers with a total of 52 Individuals.

3.5 Data Collection

In gathering the Data, the researcher administered questionnaires to credit officers and borrowers. The questionnaires were structured in accordance to main purpose of the research. The data collection tools were designed in line with the study objective to enable the researcher obtain the required information.

3.6 Data Analysis

The data that was collected was analyzed with the aid of Descriptive statistics. Data presentation was done by use of percentages, mean, median and frequency tables. SPSS and a regression model were employed to analyze the data. Loan Repayment default was the dependent variable, while Borrower characteristics, institutional factors and the Loan characteristics were the independent variables

$LRD_I = f\ (X_1, X_2, X_3 \ldots\ldots Xn\ )$

Where,

LRD_I Is the Loan Repayment Default

$X_{1\ldots}Xn$ are the Determinants of loan Repayment defaults

The Above Function was depicted in the model as below.

$LRD_1 = a + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \sum$

Where,

LRD_1 = Loan Repayment Default, which is the dependent variable

β = Regression Coefficient

X_1 = Institutional Characteristics

X_2 = Borrowers Characteristics

X_3 = Loan Characteristics

$\sum$ = Error Term

CHAPTER FOUR

DATA ANALYSIS AND INTERPRETATION OF FINDINGS

4.1 Introduction

This will outlines how the collected data was presented and analyzed. The main aim of the study was to find out the Determinants of Loan Repayment Default in Microfinance Banks in Kenya.

4.2 Response Rate

This research work considered a sample size of 26 credit Officers and 26 borrowers from which 19 credit officers and 20 borrowers dully filled and gave back the questionnaires forming a response rate of 73.1% and 76.9% respectively.

Table 4.1: Response Rate

Questionnaires	**Officers**		**Borrowers**	
	Frequency	**Percent**	**Frequency**	**Percent**
Returned	19	73.1	20	76.9
Unreturned	7	26.9	6	23.1
Total	**26**	**100**	**26**	**100**

Source: research data, (2018)

4.3 Demographic Information

The Demographic information of the respondents which included the gender and age was found out from the study.

4.3.1 Gender of the Respondents

The Respondents gender was analyzed in Table 4.2 as they had indicated in the questionnaires.

Table 4.2: Gender of the Respondents

	Borrowers		**Officers**	
	Frequency	**Percent**	**Frequency**	**Percent**
Male	8	40	9	47.4
Female	12	60	10	52.6
Total	**20**	**100.0**	**19**	**100.0**

From the findings, 12(60%) of the borrowers were female while 8(40%) were male. For the credit officers 10(52.6%) were female while 9(47.4%) were male. This shows that the study used respondents of both genders and therefore the study was not gender biased. Most (60% and 52.6%) of the respondents were female.

4.3.2 Age of the Respondents

Respondents indicated their age which was summarized below;

Table 4.3: Age of the Respondents

	Borrowers		Officers	
Age Bracket	**Frequency**	**Percent**	**Frequency**	**Percent**
18 -30	5	25	3	15.8
31-40	4	20	7	36.8
41-50	4	20	6	31.6
51-60	4	20	3	15.8
61-70	3	15	0	0.0
Total	**20**	**100**	**19**	**100**

From the findings on borrowers, 5(25%) indicated that they were aged 18 to 30 years, 4(20%) aged 31 to 40 years, 4(20%) aged 41 to 50 years, 4(20%) aged 51- 60 years, and 3(15%) aged 61 to 70 years. This showed that the study used borrowers with varied ages with most (25%) being aged 18 to 30 years.

On the findings of credit officers, the study found that 7(36.8%) fall in the age bracket of 31-40years, while 6(31.6%) in the age bracket of 41-50years, 3(15.8%) were aged 18 to 30 years, and 3(15.8%) were aged 51 to 60 years. This shows that the credit officers used in the study are of varied ages with most (36.8%) being aged 31 to 40 years.

4.4 Factors Affecting Loan Repayment

4.4.1 Institutional/Lenders Factors

The Respondents indicated their agreement to various factors using the scale of 1-5; where 1- Strongly Disagree, 2- Disagree, 3- Neutral, 4- Agree, and 5- Strongly Agree. The results are as shown in Table 4.4.

Table 4.4: Credit Officers opinion on Lenders Factors

	N	Minimum	Maximum	Mean	Std. Deviation
Delay in Loans processing is a factor to loan repayment Default	19	1.00	5.00	3.5000	1.04319
Lack of trainings to credit officers and poor knowledge on credit processes is a factor to loan repayment default.	19	1.00	5.00	3.7222	1.22741
Poor loan appraisal lead to loan repayment Default	19	3.00	5.00	4.2778	.75190
Proper Credit monitoring is key to loan repayments	19	3.00	5.00	4.2222	.64676
The credit procedures and policies within the institution have effect on loan repayment	19	1.00	5.00	3.3889	1.24328
Valid N (listwise)	**19**				

From the findings, the credit officers agreed that poor loan appraisal lead to loan repayment default as shown by a mean of 4.2778, proper credit monitoring is key to loan repayments as shown by a mean of 4.2222, lack of trainings to credit officers and poor knowledge on credit processes is a factor to loan repayment default as shown by a mean of 3.7222, and delay in loans processing is a factor to loan repayment default as shown by a mean of 3.5000. They also disagreed that the credit procedures and policies within the institution have effect on loan repayment with a mean of 3.3889. This was in agreement with study by Koranky (2014), who indicated poor evaluation and absence of Checking of loan repayments are a major causes of loan repayment defaults.

4.4.2 Borrowers Characteristics

Credit officers and borrowers indicated their level of agreement to the borrowers' characteristics leading to loan repayment default using a scale of 1-5 as indicated in the questionnaires.

Table 4.5: Extent to Which Borrowers' Characteristics Lead to Loan Repayment Default

	N	Minimum	Maximum	Mean	Std. Deviation
Failure by the borrower to disclose some vital information during loan application results to loan default	39	2.00	5.00	3.8205	.82308
Diversion of funds from the intended purpose of borrowing leads can lead to default	39	1.00	5.00	3.3846	1.20559
The income level of the borrower determines if the loan will be repaid	39	2.00	5.00	4.2821	.79302
The age of the Borrower Influences the repayment rate	39	1.00	5.00	3.1795	.99662

High Loan Amounts advanced to borrowers with low income levels Influences high Loan default rates	39	2.00	5.00	4.2564	.90954
Short Loan repayment durations leads to loan defaults	39	1.00	5.00	3.6923	1.32096
Valid N (listwise)	**39**				

The findings Indicated that income level of the borrower determines if the loan will be repaid as shown by a mean of 4.2821, high loan amounts advanced to borrowers with low income levels influences high loan default rates as shown by a mean of 4.2564, failure by the borrower to disclose some vital information during loan application results to loan default (mean=3.8205) and short loan repayment durations leads to loan defaults (mean=3.6923). The findings further showed diversion of funds from the intended purpose of borrowing leads does not lead to default, as indicated by a mean of 3.3846, and the age of the borrower influences the repayment rate (mean= 3.1795). This did not fully agree with the study by Maigua (2017) that the age of the borrower, the number of years he/she banked with the microfinance institution and the kind of collateral had effect on the rate of loan repayments.

4.4.3 Loan Characteristics

Credit officers and borrowers indicated the extent to which the Loan characteristics lead to loan repayment default by the using a scale of 1-5; where 1- Strongly Disagree, 2- Disagree, 3- Neutral, 4- Agree, and 5- Strongly Agree. The table below shows the results on the opinion of the credit officers.

Table 4.6: Credit Officers Opinion on how the Loan Characteristics Lead to Loan Repayment Default

	N	Minimum	Maximum	Mean	Std. Deviation
The amount of loan Advanced determines the repayment rate	39	1.00	5.00	3.2564	1.06914
The Loan Repayment Duration influences the Loan repayments	39	2.00	5.00	3.8718	.89382
The penalties and additional fees associated with loan non repayment is a factor to Loan repayment	39	1.00	5.00	3.6667	1.17727
Valid N (listwise)	**39**				

The Findings indicated that loan repayment duration influences the loan repayments as shown by a mean of 3.8718, and the penalties and additional fees associated with loan non repayment is a factor to loan repayment as shown by a mean of 3.6667.From the findings, loan advanced does not determine the repayment rate, the mean was 3.2564. The findings agree with findings of Kibosia (2012) who carried an investigation on what determined non repayment of loans in SMEs in Kenyan commercial banks and found out that the character of the borrower, the type of loan, and the repayment period.

4.5 Inferential Statistics

4.5.1 Correlation Analysis

The study used the Pearson Moment Correlation analysis to determine the association between institutional characteristics, borrowers characteristics, and loan characteristics with loan repayment default in microfinance banks.

Table 4.7: Correlations Coefficient

		Loan Repayment Default projects	Institutional characteristics	Borrowers characteristics	Loan characteristics
Loan Repayment	Pearson Correlation	1			
Default	Sig. (2-tailed)				
	N	254			
Institutional	Pearson Correlation	.788**	1		
characteristics	Sig. (2-tailed)	.001			
	N	254	254		
Borrowers	Pearson Correlation	.713**	.359	1	
characteristics	Sig. (2-tailed)	.000	.062		
	N	254	254	254	
Loan characteristics	Pearson Correlation	.775**	.516	.538	1
	Sig. (2-tailed)	.001	.058	.079	
	N	254	254	254	254

**. Correlation is significant at the 0.01 level (2-tailed).

The results show positive correlation between institutional characteristics and loan repayment default in microfinance banks in Kenya as shown by r = 0.788, statistically significant p = 0.001<0.01; there was a positive correlation between borrowers characteristics and loan repayment default in microfinance banks in Kenya as shown by r

= 0.713, statistically significant P = 0.000; there was a positive correlation between loan characteristics and loan repayment default in microfinance banks in Kenya as shown by r = 0.775, statistically significant P = 0.001. This implies that institutional characteristics, borrowers' characteristics, and loan characteristicswith loan repayment default in microfinance banks in Kenya are related.

4.5.2 Multiple Regression Analysis

The below three tables presents the results as a results of this Analysis.

4.5.2.1 Model Summary

The variation of dependent Variable as a result of changes of independent variables is analyzed by the use of Model. The variations of loan repayment default in microfinance banks in Kenya due to the changes of institutional characteristics, borrowers' characteristics, and loan characteristics was analyzed.

Table 4.8: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.879[a]	0.773	0.741	0.0453

The Adjusted R squared was 0.741 implying 74.1% variation of loan repayment default in microfinance banks in Kenya due to the changes of institutional characteristics, borrowers' characteristics, and loan characteristics. The remaining 21.9% implied that there were other factors that determined loan repayment default. R, shows the the relationship that exists between variables.With R=0.879,this implied that a positive relationship existed between the study variables

4.5.2.2 Analysis of Variance

This was used to determine the significance of the study data.

Table 4.9: Analysis of variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	23.533	3	7.844	22.964	.001[b]
	Residual	11.956	35	0.342		
	Total	**35.489**	**38**			

There was a significance level of 0.001 of the processed data from the ANOVA statistics, this indicated that the data was good for making decisions as the (p-value) was less than 5%. The computed F was greater than F critical (22.964 > 2.874), indicating institutional characteristics, borrowers' characteristics, and loan characteristics significantly influence loan repayment default in microfinance banks in Kenya.

4.5.2.3 Beta Coefficients of the study Variables

The equation used was;

$Y = 1.007 + 0.532\ X_1 + 0.678\ X_2 + 0.512\ X_3$

The shows if institutional characteristics, borrowers characteristics, and loan characteristics are held at a constant zero, the variables will significantly determine loan repayment default in microfinance banks in Kenya as shown by constant = 1.007 summarized in Table 4.10

Table 4.10: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.007	0.146		6.897	0.002
	Institutional characteristics	0.532	0.099	0.333	5.374	0.009
	Borrowers characteristics	0.678	0.102	0.523	6.647	0.003
	Loan characteristics	0.512	0.085	0.405	6.024	0.005

Institutional characteristics is statistically significant to loan repayment default in microfinance banks in Kenya with ($\beta = 0.532$, $P = 0.009$).There was a significant positive relationship between the Institutional characteristics and loan repayment default in microfinance banks in Kenya.

Borrowers characteristics is statistically significant to loan repayment default in microfinance banks in Kenya with ($\beta = 0.678$, $P = 0.003$). This showed that borrowers' characteristics had significant positive relationship with loan repayment default in microfinance banks in Kenya.

Loan characteristics is statistically significant to loan repayment default in microfinance loan in Kenya as shown by ($\beta = 0.512$, $P = 0.005$). This showed there exists a positive relationship between loan characteristics and loan repayment default in microfinance banks in Kenya.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

The Findings and the Conclusion made as a result of the study are summarized in this chapter. Recommendations in line with the study objective are also outlined.

5.2 Summary of Findings

5.2.1 Institutional/Lenders Factors

The study found that poor loan appraisal lead to loan repayment default, proper credit monitoring is key to loan repayments, lack of trainings to credit officers and poor knowledge on credit processes is a factor to loan repayment default, and delay in loans processing is a factor to loan repayment default. The study further found that credit procedures and policies within the institution have no effect on loan repayment. The findings are in agreement with Koranky (2014), who indicated that poor evaluation and absence of Checking of loan repayments are major causes of loan repayment defaults.

5.2.2 Borrowers Characteristics

The study established that the income level of the borrower determines if the loan will be repaid, high loan amounts advanced to borrowers with low income levels influences high loan default rates, failure by the borrower to disclose some vital information during loan application results to loan default, and short loan repayment durations leads to loan defaults. The study further found that diversion of funds from the intended purpose of borrowing doesn't lead to default, and the age of the borrower does not influence the repayment rate. The findings of the study do not fully agree with the study by Maigua (2017) that the age of the borrower, the number of years he/she banked with the microfinance institution and the kind of collateral had effect on the rate of loan repayments.

5.2.3 Loan Characteristics

The study found that the loan repayment duration influences the loan repayments, and the penalties and additional fees associated with loan non repayment is a factor to loan repayment. The study further found that the amount of loan advanced doesn't determine the repayment rate. The findings agree with findings of Kibosia (2012) who studied on causes of Loan non repayment in SMEs in Kenya commercial banks and found out that the character of the borrower, the type of loan, and the repayment period.

5.3 Conclusions

The study found that institutional characteristics are statistically significant to loan repayment default in MFBs in Kenya. It was evident from the study that institutional characteristics had significant positive relationship with loan repayment default in microfinance banks in Kenya. The study therefore concludes that a unit increase in institutional characteristics will result to increase in loan defaults in MFBs.

The study established that borrowers' characteristics are statistically significant to loan repayment default in MFBs in Kenya. It was found that borrowers' characteristics had significant positive relationship with loan repayment default in MFBs in Kenya. It was concluded a unit increase in Borrowers characteristics results to increase in loan repayment default in microfinance banks in Kenya.

The study revealed that loan characteristics are statistically significant to loan repayment default in microfinance loan in Kenya. The study further found that loan characteristics had significant positive relationship with loan repayment default in microfinance banks in Kenya. As a results of the findings, the study concludes that a unit increase loan characteristics increases loan repayment default in microfinance banks in Kenya.

5.4 Recommendations

A unit increase in institutional characteristics will result to unit increase in loan repayment default in MFBs in Kenya. It’s recommended from the study that credit offering institutions ought to train their credit officers so that they can be competent and thorough when conducting credit appraisal this will ensure that the institution advances credit to those borrowers who have the ability to pay back and therefore reducing loan non-repayment.

Poor Monitoring and control of the loans by the institution contribute to loan non-repayment, the institution should monitor how the funds are being used by the borrowers in terms of whether the loan is used for the intended reason and whether the borrowers are making loan repayments as agreed this will have a positive influence on rate of loan repayment.

A unit increase in borrowers’ characteristics results to increased loan repayment default in microfinance banks in Kenya. Borrowers’ characteristics which includes the level of income affect repayment of loans. It is important for the management to conduct a thorough and in depth appraisal of the borrowers before advancing credit to them this will reduce the rate of loan defaulting.

5.5 Suggestions for Further Studies

The objective of this research was to find out the Determinants of Loan Repayment Default in Microfinance Banks in Kenya. The study focused on Microfinance Banks in Kenya. The study therefore recommends replication of the study in other institutions such as Sacco and Mobile money lenders.

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APPENDICES

Appendix I: Letter of Introduction

UNIVERSITY OF NAIROBI

SCHOOL OF BUSINESS

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P.O. Box 30197
Nairobi, Kenya

DATE 19/11/2018

TO WHOM IT MAY CONCERN

The bearer of this letter MUSANGO DOROTHY MUMBUA

Registration No. D61/88947/2016

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

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

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

Thank you.

UNIVERSITY OF NAIROBI
SCHOOL OF BUSINESS
19 NOV 2018
P.O. Box 30197-00100, NAIROBI

PROF. JAMES M. NJIHIA
DEAN, SCHOOL OF BUSINESS

Appendix II: Questionnaire to Credit Officers and Borrowers

Questionnaire on the Determinants of Loan repayment Default in Microfinance Institutions in Kenya.

Please take a few minutes and assist to fill in the questions in this questionnaire. The information provided will confidentially and solely be used for this Research study. Kindly fill in by ticking (√) against the appropriate answer and writing down the responses as per the questions. Please do not indicate your Name or name of the organization anywhere on the Questionnaire.

Please tick below field as appropriate

Credit Officer [ ]   Borrower [ ]

SECTION A: DEMOGRAPHIC INFORMATION

1. Gender: Male [ ]   Female [ ]

2. Age Bracket (Years)

18 -30 [ ]	51-60 [ ]
31-40 [ ]	61-70 [ ]
41-50 [ ]	71 and above [ ]

SECTION B: FACTORS AFFECTING LOAN REPAYMENT

1. **INSTITUTIONAL/LENDERS FACTORS (T be filled by Credit Officers only)**

Kindly use the scale below to indicate the Level of agreement to the listed factors:

1	2	3	4	5
Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree

		1	2	3	4	5
IF_1	Delay in Loans processing is a factor to loan repayment Default.					
IF_2	Lack of trainings to credit officers and poor knowledge on credit processes is a factor to loan repayment default.					
IF_3	Poor loan appraisal lead to loan repayment Default					

IF_3	Proper Credit monitoring is key to loan repayments					
IF_4	The credit procedures and policies within the institution have effect on loan repayment					

2. BORROWERS CHARACTERISTICS (To be filled by both officers and Borrowers)

a).Please tick against factors listed below the extent to which the borrowers' characteristics lead to loan repayment default using above scale;

		1	2	3	4	5
BC_1	Failure by the borrower to disclose some vital information during loan application results to loan default					
BC_2	Diversion of funds from the intended purpose of borrowing leads can lead to default					
BC_3	The income level of the borrower determines if the loan will be repaid					
BC_4	The age of the Borrower Influences the repayment rate					
BC_5	High Loan Amounts advanced to borrowers with low					

	income levels Influences high Loan default rates					
BC_6	Short Loan repayment durations leads to loan defaults					

3. LOAN CHARACTERISTICS (To be filled by both officers and Borrowers)

		1	2	3	4	5
LC_1	The amount of loan Advanced determines the repayment rate					
LC_2	The Loan Repayment Duration influences the Loan repayments					
LC_3	The penalties and additional fees associated with loan non repayment is a factor to Loan repayment					

4. Please indicate any other factor that Causes Loan Defaults

………………………………………………………………………………………………

…………………………………………………………………………………