MAJOR DETERMINANTS OF LOAN REPAYMENT IN SMALL SCALE ENTERPRISES IN KARIOBANGI DIVISION, NAIROBI COUNTY

BY

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DECLARATION

Declaration by the student

The project is my original work, has not been presented to any other examination body.

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DEDICATION

To my loving family and friends.

ABSTRACT

One of the most crucial and leading factors constraining Small Scale Enterprises (SSEs) development in developing countries like Kenya is limited access to financial capital and credit. This is because on one hand, these enterprises couldn't fulfill the bank's lending requirements and on the other, the banking sector considers these enterprises as involving high credit risk. This study was conducted with the objective of identifying the major determinants of loan repayment in Small Scale Enterprises (SSEs) with particular reference to SSEs in Kariobangi Division, Nairobi County. In order to achieve this objective, primarily data were collected from 50 randomly selected respondents by using questionnaires. For data analysis, descriptive statistics including mean, frequency and percentages were used to describe the socio-economic characteristics of the borrowers. A regression model was used to analyze the determinants of loan repayment.

The study found that even though many factors can lead to loan defaults, some of the factors were regarded to be of higher impact. Business related factors were significant in influencing loan repayment of the respondents with increase in input prices as the major factor that led to loan defaults while death of spouse was seen as the least factor that led to loan default. In addition, education level, family size, amount of loan applied and business experience of the respondents were found to have a positive relationship to loan repayment. Age, interest rate and change in gender had an inverse relationship to loan repayment.

The study recommended that more loans should be advanced to female SSE owners aged 30-40s as they proved to be the least loan defaulters. SSEs in Kariobangi division should insure their businesses in order to reduce risks associated with high input prices. The financial institutions should provide financial education and awareness to SSE owners as they are less educated.

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ABBREVIATIONS

CBK	-	Central Bank of Kenya
CSA	-	Central Statistics Agency
ILO	-	International Labour Organization
KES	-	Kenya Shillings
MOL	-	Ministry of Labour
MFI	-	Micro Finance Institution
MSEs	-	Micro and Small Scale Enterprises
NBFI	-	Non-Bank Financial Institutions
NBK	-	National Bank of Kenya
NGO	-	Non Governmental Organizations
NPL	-	Non Performing Loans
ROSCAs	-	Rotating Savings and Credits Associations
SSEs	-	Small Scale Enterprises
UN	-	United Nations
UNECA	-	United Nations Economic Council of Africa
UNESCAP	-	United Nations Economic and Social Council

CHAPTER ONE

1.0INTRODUCTION

1.1 Background of the study

Loan is defined as a type of debt, and like all debt instruments, a loan entails the redistribution of financial assets over time between the lender and the borrower. In a loan, the borrower initially receives or borrows an amount of money called the principal from the lender, and is obligated to pay back an equal amount of money to the lender at a later time. Typically, the money is paid back in regular installments or partial repayments in an annuity; each installment being of the same amount (Signoriello, 1991). However, loans from other financial institutions like the informal financial institutions may have a different repayment structure which is custom made for the borrower.

The loan is generally provided at a cost, referred to as interest on the debt, which provides an incentive for the lender to engage in the loan. In a legal loan, each of these obligations and restrictions is enforced by a contract, which can also place the borrower under additional restrictions known as loan covenants (Signoriello, 1991).

1.1.1 Small Scale Enterprises

A small business is an entity that is privately owned and operated, with a small number of employees and relatively low volume of sales. Small businesses are normally privately owned corporations, partnerships or sole proprietorships. There is no clear definition of small scale enterprises as small varies by country and industry. However, three criteria are mainly used in literature to define Micro and Small Scale Enterprises (MSEs). The first one, based on number of employees, defines MSEs as those enterprises below a certain number of workers (it can range from less than 10 to less than50 employees). The second criterion concerns the degree of legal formality and is mainly used to distinguish between the formal and informal sectors. According to this criterion, MSEs are those enterprises that are not registered and do not comply with the legal obligations concerning safety, taxes and labour laws. The third criterion defines MSEs by their limited amounts of capital and skills per worker. The degree of informality and size of employment have perhaps been the two most readily accepted criteria on which classification of

MSEs is based. The term MSE incorporates firms in both the formal and informal sectors. However, the terms MSEs and informal sector are normally used interchangeably as most MSEs are informal enterprises (Mead and Morrison, 1996). The third criterion definition of MSEs will be used for the purpose of this study.

Small scale enterprises are characterized by: ease of entry; small scale of activity; self-employment with a high proportion of family labour; little capital and equipment; labour intensive technologies; low skills; low level of organization with little access to organized markets, informal credit, education and training or services and amenities; cheap provision of goods and services or provision of goods and services otherwise unavailable; low productivity and low incomes (Charmes, 1997).

1.1.2 Small Scale Enterprises Finance

A financial institution is an establishment that provides financial support services to its clients or members. Most financial institutions are highly regulated by government bodies due to the high amount of monies that they handle on behalf of their clients. Broadly there are three major types of financial institution which include: Deposit-taking Institutions that accept and manage deposits and make loans. This category includes banks, credit unions, trust companies, and mortgage loan companies, insurance companies and Pension Funds, and Brokers, Underwriters and Investment Funds (Siklos, 2001).

These institutions provide service as intermediaries of the capital and debt markets. They are responsible for transferring funds from investors to companies in need of those funds. The presence of financial institutions facilitates the flow of money through the economy. To do so, savings are pooled to mitigate the risk brought about by providing funds for loans. Acting as a provider of loans is one of the principal tasks of financial institutions (Fry and Maxwell, 1995).Potential sources of finance for the small scale enterprises include commercial banks, non-bank financial institutions, non-governmental organizations (NGOs), multilateral organizations, business associations, and rotating savings and credit associations. In addition, financial transactions also take place between traders, friends, relatives and landlords, as well as commercial moneylenders (Atieno, 2001).

1.1.3 Determinants of Loan Repayment

Default on borrowed funds could arise from unfavorable circumstances that may affect the ability of the borrower to repay as pointed out by Stigliz and Weiss (1981). The most common reasons for the existence of defaults are the following: if the financial institution is not serious on loan repayment, the borrowers are not willing to repay their loan; the financial institution's staffs are not responsible to shareholders to make a profit; clients' lives are often full of unpredictable crises, such as illness or death in the family; if loans are too large for the cash needs of the business, extra funds may go toward personal use; and if loans are given without the proper evaluation of the business, Norell (2001). Wakuloba (2005) in her study on the causes of default in Government micro credit programs identified the main causes of default as poor business performance, diversion of funds and domestic problems.

Breth (1999) argued that there are many socio-economic and institutional factors influencing loan repayment rates. The main factors from the lender side are high-frequency of collections, tight controls, a good management of information system, loan officer incentives and good follow ups. In addition, the size and maturity of loan, interest rate charged by the lender and timing of loan disbursement have also an impact on the repayment rates (Oke*et al.*, 2007). The main factors from the borrower side include socio-economic characteristics such as, gender, educational level, marital status and household income level and peer pressure in group based schemes.

1.1.4 Small Scale Enterprises in Kariobangi

Kariobangi area, located approximately 10 kilometers on the north-east of Nairobi's Central Business District is a low and medium class habitat. The area became a local artisans' hub when the land on which it sits was originally acquired in 1978 by a local Member of Parliament who wished to alleviate mounting pressure for business land by jobless people in his constituency. The land was demarcated into plots and designated as a light industry area. The plots were provided to artisanal entrepreneurs who lost their employment in the formal sector as a consequence of the country's Structural Adjustment Program in the 1980s.The industrial area was demarcated bystreets and surrounded by low-income residential areas comprising mid-rise apartment buildings and slum dwellings. In 1982 construction of factories began followed by establishment of garages. Around 1986 hardware shops came up. These collective entities, currently spread in the larger Kariobangi area came to be known as Kariobangi Light Industries. As the population of business owners and workers grew, an entrepreneur wanted to start a hotel, but no more land was available. At that time, a slum had developed along the main road at one corner of Kariobangi Light Industries. The entrepreneur bought this land, burned down the slum, displaced the slum dwellers and constructed a hotel. Part of the slum was also bought by business persons who had missed the initial allocation of land. In the early 1990s more workers who had lost jobs in the formal sector as a result of the Structural Adjustment Program started streaming into Kariobangi Light Industries to establish enterprises or seek employment. As a result, machining factories were established, followed by scrap metal dealers and other factories.

To date, Kariobangi Light Industries is a concentration of micro and small metalwork enterprises, as well as hardware retail shops and machinery repair service workshops. There are approximately 300 enterprises and workshops, half of which are metalwork enterprises. The products manufactured include foundry products (such as car spacers); lathe works, welding, and metal fabrication (steel doors, windows, furniture, cooking stoves); and mechanical machines (flour millers, feed mixers, block makers, counterweight balances, band saws, candle makers, bakery machines, and chip cutters, among others).

1.2 Problem Statement

Loan recovery is one of the key objectives of financial institutions as it enables them to refinance and to reach more people. To have a positive impact on the economy of a country, the institutions must be able to loan out funds and recover the same so as to remain relevant in the finance industry. Loan recovery is a strategic activity for financial institutions. For any economy to thrive there must be funds to foster investment which leads to well-being of the population. Proper investments eventually bring about poverty reduction through creation of employment. High recovery rates reflect the adequacy of financial institution's services to clients' needs (Godquin, 2004).However, where there is low recovery rate, financial institutions raise provisions for loan loss that decrease their revenue and reduce the funds for new lending. The cutback of loans impairs the small scale enterprises as they have difficulties in expanding their working capital blocking their chances of resuming normal operations and meeting their obligations which include loan repayment. This motivates the carrying out of this study to examine loan repayment and its determinants in the small scale enterprises.

Small scale enterprises comprise of petty traders involved in such activities as selling of second-hand clothes, shoe shinning, food selling and repair and construction; operating mainly from the streets of the main urban centres. It can also be described as any activity generating income and profits, though on a small scale, uses simple skills, is dynamic and not tied to regulation of the activities. Such activities include: vegetable selling, street vendors, masonry, carpentry, among others, Amenya (2007). The informal sector is expanding from time to time as an employer, especially for the urban population. However it is encircled by so many deep-rooted challenges that worsen the livelihood of its members. Lack or shortage of capital for start-up and running expenses, is found in the centre of these diversified challenges (ILO 1991).

Kashuliza (1993) did a study on loan repayment and its determinants in small holder agriculture. He attempted to identify some of the main factors which influence loan repayment and default at the farm level. Results of the study indicated that better repayment rates were associated with use of machinery and hired labour in farming, optimal credit packages and higher farm incomes. Credit default was accounted for by high consumption expenditures, farmer attitudes, late input delivery, adverse production environment, and declining crop marketing margins.

Abafita (2003) did a study on Microfinance and Loan Repayment Performance in Ethiopia by analyzing the factors that influence microfinance loan repayment, evaluating the loan rationing mechanism and also assessing the impact of the program on the livelihood of borrowers. The results showed that education, income, loan supervision, suitability of repayment period, availability of other credit sources and livestock were important and significant factors that enhanced the loan repayment performance, while loan diversion and loan size were found to significantly increase loan default.

Mathara (2007) studied the response of National Bank of Kenya Ltd (NBK) to the challenges of NPLs and found that economic downturn, government interference in lending, inadequate government monetary policies and a slow inadequate judicial system, political appointments to top management, poor debt follow up, lack of management accountability for NPLs, inadequate credit policy guidelines, imprudent and reckless lending were some of the causes of NPLs.

Muasya (2009) studied the impact of non-performing loans on the performance of the banking sector in Kenya and confirmed that non-performing loans affect commercial banks in Kenya.

It is clear from the above studies that loan repayment and their determinants in the small scale enterprises in Kenya has not been done. This study therefore is intended to narrow the research gap paying attention to this sector of the economy. It focuses on identifying factors behind the loan default problem that SSEs are associated with.

1.3 Objective of the Study

The study sought to examine the determinants of loan repayment by the small scale enterprises in Kariobangi Division, Nairobi.

1.4 Importance of the Study

Financial institutions will fully understand not only the impact, but also the challenges that debtors face during the loan recovery process. After identifying the major factors influencing loan recovery from the informal sector, the financial institutions will understand the importance of offering recoverable credits. Factors that hinder recovery of loans and ways to overcome them will be expounded, and the information used by the financial institutions, possibly in capturing the emerging market and improvement of their service delivery.

The informal sector will also benefit from the study findings by understanding the reasons why financial institutions are not able to meet some of their financial demands whilst having pending loan repayment cases from their sector. They will have an understanding of the impact of non-repayment of loans and subsequently an acceptance to repay their outstanding loans.

Researchers will also benefit since some will have base data for further studies. The survey is expected to stimulate more research on factors that influence loan repayment in other sectors of the economy and develop ways in which loan repayment rates can be improved. Policy makers will use the study to develop policies that will enhance loan repayment rates since they will have an understanding of the factors that influence repayment rates.

CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction

This chapter reviews literature from previous studies that have been carried out on the small scale enterprises and loan repayment. The chapter is divided into three sections. The first section discusses the conceptual literature with specific areas covered here being the monetary circuit theory of loan, information asymmetry, the non-performing loans, small scale enterprises, their main features, the problem they encounter and the sources of their finance. The second section discusses the empirical studies related to loan repayment and the last section is the conclusion of the chapter.

2.2 Theoretical Review

2.2.1 Monetary Circuit Theory

Monetary circuit theory is a heterodox theory of monetary economics, particularly money creation, often associated with the post-Keynesian school. It holds that money is created endogenously by the banking sector, rather than exogenously by central bank lending; it is a theory of endogenous money. It is also called circuitism and the circulation approach. Circuitism is easily understood in terms of familiar bank accounts and debit card or credit card transactions: bank deposits are just an entry in a bank account book and a purchase subtracts money from the buyer's account with the bank, and adds it to the seller's account with the bank (Zarrazo, 2002).

2.2.1.1 Transactions

As with other monetary theories, circuitism distinguishes between hard money and credit money. Unlike mainstream monetary theory, it considers credit money created by commercial banks as primary, rather than derived from central bank money. Credit money drives the monetary system. While it does not claim that all money is credit, basic models begin by only considering credit money, adding other types of money later. In circuitism, a monetary transaction is not a bilateral transaction between buyer and seller as in a barter economy, but is rather a tripartite transaction between buyer, seller, and bank. Rather than a buyer handing over a physical good in exchange for their purchase, instead there is a debit to their account at a bank, and a corresponding credit to the seller's account. This is precisely what happens in credit card or debit card transactions, and in the circuitist account, this how all credit money transaction occur (Keen, 2009).

2.2.1.2 Monetary creation

In circuitism, as in other theories of credit money, credit money is created by a loan being extended. Crucially, this loan need not be backed by any central bank money: the money is created from the promise embodied in the loan, not from the lending or relending of central bank money: credit is prior to reserves. When the loan is repaid, with interest, the credit money of the loan is destroyed, but reserves are created in form of the profit from the loan. In practice, commercial banks extend lines of credit to companies – a promise to make a loan. This promise is not considered money for regulatory purposes, and banks need not hold reserves against it, but when the line is tapped and a loan extended, then bona fide credit money is created, and reserves must be found to match it. In this case, credit money precedes reserves. In other words making loans pulls reserves in instead of reserves being pushed out as loans, which is assumed by the mainstream model. The failure of monetary policy during depressions is referred to as 'pushing on a string', and is cited by circuitists in favor of their model: credit money is pulled out by loans being extended, not pushed out by central banks printing money and giving it to commercial banks to lend (Keen, 2009).

2.2.2 Information Asymmetry

The fundamental feature that creates imperfection in credit markets is informational constraints. Ray (1998) stated that informational gap occur at two basic levels. First, there is lack of information regarding the use to which a loan will be put. Second, there is lack of information regarding the repayment decision of borrowers, as well as limited knowledge of the defaulter's subsequent needs and activities. All the important features of credit markets can be understood as responses to one or the other of these informational problems. In addition, Behrman and Srinivasan (1995) stated about the arising of agency problem in the functioning of credit market. This problem exists when there are different goals between creditors, shareholders and management. Financial intermediaries may reduce agency problem by monitoring borrowers and make wise investment choices.

Adverse selection and moral hazard are the two most important problems in the functioning of credit market; both are driving from the imperfect information. The adverse selection occurs when the lender cannot easily determine which customers are likely to be more risky than others. Therefore, the lenders would like to charge riskier customers more than safer customers in order to compensate for the added probability of default. But the problem is the lender does not know who is who, and raising average interest rates for everyone often drives safer customers out of the credit market (Armendariz and Morduch, 2010). Those who are willing to repay high interest rate may, on average, be worse risky; they are willing to borrow at high interest rates because they perceive their probability of repaying the loan to be low (Stiglitz and Wiss, 1981). Moral hazard, arises because banks are unable to ensure that customers are making the full effort required for their investment projects to be successful. Moral hazard also arises when customers try to abscond with the bank's money (Armendariz and Morduch, 2010). In the absence of collateral, the lender and borrower do not have the same objectives because the borrower does not fully internalize the cost of project failure. Moreover the lender cannot stipulate perfectly how the borrower should run the project (Berhanu, 2005).

2.2.3 Switching Costs

In typical markets, say the market for oranges, the seller does not care who buys her product; one customer is the same as the next. Anyone who wants to buy oranges at the listed price can do so. This is not always the case in the bank loan market; banks are concerned with the risk profile and potential behaviour of their customers. The bank needs to find out some information about the characteristics of each and every buyer. This is a costly activity for the bank. This cost of acquiring information is often passed onto the buyer by way of a fixed up-front fee. This fee makes it costly for a buyer to switch from one bank to another. In addition, there are the regular search costs, or "shoe leather" type costs of moving from one supply source to another. Such costs include the costs of learning the different rates and conditions on the new loan. There are also costs in filling out loan application forms, obtaining the relevant documentation, and the time involved in attending interviews with the lending agent. These "search and application" costs are often more significant in banking than in most goods markets because of the bank's need to discover the risk characteristics of its customers. Klemperer (1987) shows that, in general, the existence of switching costs leads to market segmentation, and reduces the elasticity of demand facing each firm. Even with non-cooperative behaviour, the switching costs lead to outcomes similar to the collusive solution, with the derivative of price with respect to marginal cost being less than one.

2.2.4 Non-Performing Loans

Non-Performing Loans can be defined as loans which, for a relatively long period of time do not generate income; that is the principal and/or interest on these loans has been left unpaid for at least ninety days (Caprio and Klingebiel, 1999). Poor loans' quality has its roots in the information problems which affect financial markets and which are at their most acute in developing countries, in particular the problem of moral hazards. Non-performing loans problem has been a serious issue in Kenya. Theoretical literature suggests that moral hazards incentive induced by the deposit insurance under prices risks and increases the risk of default (Martin, 1998). Many factors can lead to loan defaults. An entire industry can decline because of general economic events; firm specific problems may arise from changing technology, labour strikes, and shifts in customer preferences or bad management. Individual borrowers find their ability to repay closely follows the business cycle as personal income rises and falls (Scott and Timothy, 2006)

2.3 Determinants of Loan Default

2.3.1 Credit Risk Analysis

Golden and Walker (1993) summarized the reasons for loan defaulting to 5Cs of bad credit as follows: Complacency – tendency to make assumptions that the good past performance will result to good future performance of loans e.g over reliance on guarantors, reported net worth or past loan repayment success. Carelessness - poor underwriting evidenced by inadequate loan documentation, a lack of current financial information in loan agreements. Communication ineffectiveness – bank's credit objectives and policies are not clearly communicated. Loan officers should communicate loan problems encountered as they appear to the bank managers. Completion –this involves studying the competition and adapting their strategies rather than clinging on the bank's own credit standards. Contingencies – lenders tendency to ignore circumstances in which a loan might default. The focus is on making the deal work rather than identifying downside risk.

2.3.2 Characteristics of Small-Scale Enterprises

Characteristics of small-scale enterprises make the cost of administering credit very high compared to the return on the loans. Small scale enterprises possess shallow management, often with little experience and training; they are usually undiversified, one product firms, they are sometimes new businesses, with little track record, and poor financial recording; they may have a new unproven product; they have little to offer by way of security to a lender; they may be reluctant to raise outside equity capital for reasons of expense, loss of control and increased disclosure requirements. These characteristics of small-scale enterprises provide little incentive for any aggressive loan recovery mechanisms (Baker and Dia, 1987; Kitchen, 1989).

2.3.3 Lending Practices

Okorie and Iheanacho (1992) argued that the failure of lending agencies in playing their roles in loan disbursement and recovery process is a major contribution to loan default. They contend their view that determining credit worthiness requires investment of time and resources to evaluate firm specific and industry wide variable, structural or cyclical, by analysts with specific professional skills. A mistake on the evaluation of the borrowers' characteristics or the introduction of inappropriate loan conditions may increase the total risk of the transaction. A non-economic obstacle relating to the failure of banks lies in the risk averse attitude of loan officers (Kitchen, 1989). He revealed that financial repression and credit rationing encourage unprofessional lending practices such as collusion and corruption. He has found that unprofessional practices lead to high default rates, thereby increasing risk. Taking care of this issue is more important in development banks where accountability of loan officers is often a problem.

Fry (1995) listed bank lending criteria in East Africa in order of importance to show how the method of credit analysis is weak: first, the securities offered, second, any other additional securities, third how short the period to maturity is, fourth the commissions to receive in connection with the granting of credit, fifth the standing of the would be borrower, sixth the amount and seventh the project.

2.3.4 Political Framework

Fry and Maxwell (1995) argued that political framework, which affects credit systems from the designing stage to the recovery stage, is central to the explanation of the poor performance of small-scale credit systems. In some cases when government is involved in credit programs, recipients often fail to distinguish loans from grants. They found out that the primary causes of high arrears in India, for example, is the rapid expansion of lending in response to government pressures to achieve mandated credit disbursement targets. They listed the following as causes of loan default: failure to tie lending to productive investment; neglect of marketing and linking credit recovery to the sale of the product; defective loan policies, delayed loan disbursement, too much or too little credit and unrealistic repayment schedules; misapplication of loans; ineffective supervision; indifference of bank management with respect to recovering loans and lack of responsibility and discipline on the part of borrower.

2.4Small Scale Enterprises

Small Scale enterprises and the term informal sector are used interchangeably (Mead and Morrison, 1996).ILO(1991) defined the informal sector as consisting of "very small-scale units producing and distributing goods and services, and consisting largely of independent self-employed and procedures in urban areas of developing countries, some of whom also employ family labour and/or a few hired workers or none at all, which utilize a low level of technology and skills, which therefore operate at low level of productivity, and which generally provides very low and irregular incomes and highly unstable employment of those who work in it".

As a concept, informal sector refers to home based or individual establishments operated by the owner with a few or no employees. This concept was introduced into international usage in 1972 by the International Labor Organization (ILO) in its Kenya Mission Report, which defined informality as a "way of doing things characterized by: Ease of entry, reliance on indigenous resources, family ownership, small scale operations, labor intensive and adaptive technology, skills acquired outside of the formal sector and unregulated and competitive markets (ILO, 1991).

Since that time, many definitions were introduced by different authors and the ILO itself. The ILO (1999)international symposium on the informal sector proposed that the informal sector workforce can be categorized into three broad groups: Owner-employers of micro enterprises, which employ a few paid workers, with or without apprentices; Own-account workers, who own and operate one-person business, who work alone or with the help of unpaid workers, generally family members and apprentices; and dependent workers, paid or unpaid, including wage workers in micro enterprises, unpaid family workers, apprentices, contract labor, home workers and paid domestic workers.

2.4.1 Main Features of Small Scale Enterprises

The small scale enterprises in Africa are dominated by trade-related activities, with services and manufacturing accounting for only a small percentage of this sector (UN 1996). The characteristics of the small scale enterprises may vary depending on the socio economic status of the specific country that they operate in. There are common features that are shared by the small scale enterprises. The World Bank in its study classified their characteristics into two broad categories that included the small scale of operation and the labour intensive mode of production (World Bank 1996).

Most of Africa's small scale enterprises are characterized by activities such as selling fruits and vegetables, food operation, sale and processing, selling clothes and shoes (both second-hand and new), kiosk selling various items, water kiosks, small retailers or hawkers who sell cereals, home suppliers, fuels and other goods, small manufacturing, production, construction and repair of goods. World Bank (2006) in its comprehensive report of the on the Kenyan informal sector, housing, social services provision and slums, states that there is a tremendous increase in the activities and involvement of the population in the sector. This has been largely due to the privatization of the public sector as well as rise in the unemployment rate especially among the youth(World Bank, 2006).

2.4.2 Causes to Engage in the Small Scale Enterprises

There are four common factors cited frequently as causes leading people to engage in the small scale enterprising (CSA 2003): Ease of entry: the informal sector is not registered and regulated by government offices and the required capital to start and run the sector's activity is low. These make individuals to use the informal sector as an escaping window. Family ownership of enterprises; Labor intensive method of production; and small scale operation

2.4.3 Constraints in Small Scale Enterprises

UNESCAP (2006) documented that with low barriers to entry, in terms of capital, skills required and technology, new entrants find it easy to enter the sector to earn a living. However managing the enterprises becomes a challenge as it requires additional resources and skills. The constraints that the small scale enterprises face can be summarized as follows:

A lack of capital is one of the major constraints faced by small scale enterprises. As a result, small scale enterprises are forced to use hand-driven tools and outdated machinery, which keeps their productivity low. Due to a lack of working capital, they cannot purchase raw materials in bulk at lower prices and take their goods to market, where they can attract better prices.

Poor management and technical skills: Small scale enterprises possess limited management and modest technical skills, which constrains firm productivity and product quality. Inadequate technology: which is usually stated as an access issue, but it is also an 'internal' problem in that some enterprises could have access to improved technology available in the market if they had higher literacy and technical skills and stronger business planning and investment skills.

Disadvantageous market structures: Small scale enterprises experience this problem as too much competition in low income markets, low demand for their products and services, lack of access to physical markets where larger and higher income groups shop, difficulty in procuring inputs, low prices provided by traders, as a result, the informal sector enterprises suffer from diseconomies of scale; while market structures (which are complex) are primarily an access issue; forces external to the firm often play a key role in limiting their market access. Inadequate infrastructure: low access to services such as work sites, water & electricity, roads and communications limits productivity and access to product markets. Government policies, regulation or harassment: government is one of the most significant external forces that affect the performance of informal sector businesses.

2.4.4 Possible Sources of Finances for Small Scale Enterprises

Access to financial services by smallholders is normally seen as one of the constraints limiting their benefits from credit facilities. However, in most cases the access problem, especially among formal financial institutions, is one created by the institutions mainly through their lending policies. This is displayed in the form of prescribed minimum loan amounts, complicated application procedures and restrictions on credit for specific purposes according to Schmidt and Kropp (1987). For small-scale enterprises, reliable access to short-term and small amounts of credit is more valuable, and emphasizing it may be more appropriate in credit programs aimed at such enterprises.

Stiglitz (1990), most of the small scale enterprises are unable to access financial resources from formal financial intermediaries, such as banks, due to any of the following reasons: smaller size of their transaction, lack of collateral, inexperience, illiteracy or innumeracy of the borrower ,physical remoteness of many of the informal sector enterprise, mobility of many informal sector enterprises, lack of bookkeeping or an appropriate compliance framework and lack of general information about the borrower and of predictability of the surrounding transaction. Potential sources of finance for the informal sector include commercial banks, non-bank financial institutions, non-governmental organizations (NGOs), multilateral organizations, business associations, and rotating savings and credit associations. In addition, financial transactions also take place between traders, friends, relatives and landlords, as well as commercial moneylenders (Atieno, 2001).

Banks; Many financial institutions, especially commercial banks, rarely lend to the small scale enterprises since they emphasize collateral, which most small enterprises lack. Few enterprises are able to provide the marketable collateral and guarantee requirements of commercial banks, and as such, they have not been able to obtain credit from banks. Most of them therefore rely on their own savings and informal credit (Oketch *et al.*, 1995).

Rotating Savings and Credit Associations (ROSCAs); ROSCAs are also an important source of credit in the country. These are found in both rural and urban areas as either registered welfare groups or unregistered groups. They mainly provide credit to those who would likely be ineligible to borrow from other sources. ROSCAs have developed mostly in response to the lack of access to credit by small enterprises in the informal sector, forcing them to rely on their own savings and informal credit sources for their financing (Addisu, 2007)

NGOs; In the recent past, a number of non-governmental organizations (NGOs) have been involved in financing of microenterprises. However, most NGOs have not had positive performance. Their inexperience in financial intermediation and limited financial resources has constrained their potential. There is little coordination among the NGOs, resulting in duplication of resources and activities. Most of them have high credit costs, are donor based and sponsored, lack adequate funding, and are limited in their geographical coverage. They also discriminate against small-scale enterprises who get rationed out by lenders since cheap credit creates excess demand for loanable funds, forcing lenders to loan to large enterprises that have collateral and are perceived to be less risky (Addisu, 2007).

Informal Finance; A large part of financial transactions in Africa occur outside the formal financial system. Literature on the theory of credit markets with incomplete markets and imperfect information is largely relevant to the functioning of informal markets. Informal finance has been defined to refer to all transactions, loans and deposits occurring outside the regulation of a central monetary authority, while the semiformal sector has the characteristics of both formal and informal sectors. In Africa it has been defined as the operations of savings and credit associations, rotating savings and credit associations (ROSCAs), professional moneylenders, and part-time money lenders like traders, grain millers, smallholder farmers, employers, relative and friends, as well as cooperative societies (Aryeetey and Udry, 1997).

2.5 Empirical literature

There are a number of socio-economic and institutional factors that influence loan repayment. Several studies have been conducted regarding to the loan repayment performance of borrowers in many countries by different authors. Some of the studies are summarized below.

2.5.1 Studies done in Kenya

A study on the response of National Bank of Kenya Ltd (NBK) to the challenges of NPLs found that the causes of NPLs were both external and internal. The external causes included economic downturn, government interference in lending, inflationary tendencies in the 90s, limited supervision by CBK in the 90s, inadequate government monetary policies and a slow inadequate judicial system. Internal causes included political appointments to top management, use of qualitative methods of debt appraisal which ignored analysis of financial performance of debtors, poor debt follow up, lack of management accountability for NPLs, inadequate credit policy guidelines, imprudent and reckless lending and lack of portfolio diversification. NBK was also found to be having liquidity problems, low profitability, poor public image, high cost of recovery and other problems associated with debt collection. (Mathara, 2007)

A study assessing the relationship between interest rates and NPLs in commercial banks in Kenya found that there was a weak relationship between the two. A greater proportion of NPLs was attributed to factors other than the interest rate. (Ongweso, 2006). Another study examining the relationship between credit risk management and NPLs in the financial sector in Kenya found that the credit risk management coupled with close supervision by the Central Bank has greatly enhanced the decline of non-performing loans ratio in the banking sector. (Ocholla, 2009)

Bindra (1998) argues that the true underlying cause of non-performing loans is entirely of our own making - poor risk management. This is a situation where the bank credit officials do not properly assess the suitability of advancing credit to their customers; they do not adhere to good lending principles. He concludes that loan losses can be minimized through professional management of the lending function. This requires careful appraisal of loan requests, continuous monitoring of customer conditions and proper follow up on how the loan has been utilized as there is a possibility that the loan may not be utilized for the intended purpose leading to project failures.

Wagacha (2000) argues that insider lending and fraudulent activities by directors of some banks have led to the problem of non-performing loans. He further reiterated that poor lending by political banks has added to non-performing loans as related to lending to dominant shareholders has led to a situation where prominent people are advanced credit with no intention of paying back. Muasya (2009) studied the impact of non-performing loans on the performance of the banking sector in Kenya and confirmed that non-performing loans affect commercial banks in Kenya. Further analysis of individual commercial banks with more than KES 25 Billion worth of asset indicated that the impact on non-performing loans to interest income and profitability are not adverse to these banks.

2.5.2 Studies done in Other Countries

Reta (2011) in his study on determinants of loan repayment performance analyzed and identified the factors that influence the loan repayment performance of the beneficiaries of Addis Credit and Saving Institution (AdCSI) - a microfinance institution in Ethiopia. He found out that age and five business types (baltina & petty market, kiosk & shop, services providing, weaving & tailoring and urban agriculture) were important in influencing loan repayment performance of the borrower. In addition, sex and business experience of the respondents were found to be significant determinants of loan repayment rate.

Brehanu (2008) studied on the determinants of loan repayment performance of smallholder farmers in North Gondar, Ethiopia. In order to analyze the factors that affect loan repayment, he employed the tobit model. A total of 17 explanatory variables were considered in the econometric model. Out of these seven variables were found to significantly influence the repayment performance. These were land holding size of the family, agro-ecology of the area, total livestock holding, number of years of experience, number of contacts, sources of credit and income from off-farm activities. The remaining variables (family size, distance between main road and household residence, purpose of borrowing, loan amount and expenditure for social festivals) were found to have insignificant effect on loan repayment performance of smallholder farmers.

Bhatt and Tang (2002) studied the determinants of loan repayment in microcredit evidence from programs in the United States. Their study showed that women has low repayment rate because some women entrepreneur in the study might have been engaged in high risk and low return activities. Godquin (2004) also examined the microfinance repayment performance in Bangladesh. His result is female borrowers did not proven to have a significant better repayment performance. The size of loan and the age of the borrower showed the negative impact on the repayment performance. On the contrast, Abreham (2002) did a study on loan repayment and its Determinants in Small-Scale Enterprises Financing in Ethiopia and showed that male borrowers are the undermining factors for repayment.

2.6 Conclusion

As mentioned above, various studies were conducted on the determinants of loan repayment performance in different countries. Most of these studies were focused on the credit associated with agricultural activities and they identified the socio-economic factors that affect the loan repayment rate of rural household. Studies done in Kenya have focused more on non-performing loans in relation to various aspects such as credit risk, causes of non-performing loans and performance of the banking institutions. However in the literature review there is no indication of coverage of loan repayment and its determinants in the small scale enterprises in Kenya. Therefore, this study aims at addressing this research gap.

CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents the methods and procedures that were followed in conducting the research with the aim of examining loan repayment and its determinants in the small scale enterprises in Kenya's Kariobangi Division, Nairobi County. The chapter discusses the research design, population and sample, data collection techniques used, data analysis method that was employed in the study and data validity and reliability.

3.2 Research Design

This study used the descriptive research design to examine the determinants of loan repayment in small scale enterprises in Kenya's Kariobangi Division, Nairobi County. A descriptive study was the most appropriate because it presents facts concerning the nature and status of a situation as it exists at the time of study. In addition, this approach tries to describe present conditions, events or systems based on the impressions or reactions of the respondents of the research (Robson, 1993).

3.3 Population

The population of the study comprised 126 small scale enterprises based in Nairobi's Kariobangi Light Industries. There are 126 small scale enterprises in Kariobangi according to the Ministry of Labour, Department of Micro and Small Enterprise, Jua Kali Demontration and Training Centre as at June 2012. The owners of these businesses were the population elements in this study.

3.4 Sampling

This research used a simple random sampling technique. This is sampling in which every member of the population has an equal chance of being selected. A total of 50 small scale enterprises were sampled for response to the designed data collection instruments. This sample was obtained by giving each of the elements in the sampling frame a number, 50 numbers were then selected at random to form the sample which represented 40% of the population.

3.5 Data collection

The study used primary data which was obtained from small scale enterprises with the aid of questionnaires. The questionnaire was developed by the researcher and structured according to the objectives of the study. This was used to generate information on personal characteristics of the target group and to determine the factors affecting their repayment performance. Both closed and open ended questions were used to obtain responses. The questionnaire was physically administered to each respondent, who was allowed enough time to respond.

3.6 Data Analysis

Descriptive statistics was used to summarize the data collected from the sample. This involved the use of frequency tables and measures of central tendency such as, mean, median, standard deviation and percentages. Data was analyzed using the Statistical package for Social Sciences (SPSS) Version 17. Factor analysis was used to analyse the determinants of loan repayment. Explanatory variables selected for this study were broadly categorized under socio-economic and loan related factors. The loan repayment could be affected by these factors either positively or negatively. Econometric regression model was applied to analyse the data. Loan repayment was a dependent variable, while different socio-economic and lender related factors were considered as independent variables.

In this case the dependent variable loan repayment is the function of personal characteristics, business and lender related factors. The function specified as:

$$LRi = f(S, Lo, B)$$

where:

LRi = loan repayment for the i^{th} borrower

S = represent the personal characteristics that affect the decision whether to repay their loan or not

Lo = stands for the loan specific characteristics of the individual enterprises

B = represent business specific characteristics of each enterprises

The above function will be depicted in the model below:

$$LR_i = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4 \ldots\ldots\ldots\ldots \beta_nX_n + \varepsilon$$

Where: LR_i - Loan repayment

β_0 - Constant

ε - error term

$\beta_1X_1, \beta_2X_2, \beta_3X_3,$

$\beta_4X_4 \ldots\ldots \beta_nX_n$ - Different factors that influence loan repayment

There are many factors that determine loan repayment. The variables that were used in this study were categorized into three major classes. The first category is the personal characteristics variables namely, age, gender, education level and family size; the second category is the loan characteristics variables such as loan amount, interest, repayment amount and the third category is the business related characteristics such as sales and business experience.

3.7Data Validity and Reliability

A pilot test was conducted to pretest and validate the questionnaires. This helped the researcher to refine the questionnaire so that the respondents could not have a problem in answering the questions. It also helped the researcher to obtain assessment of the questions' validity and the likely reliability of the data that was collected. To enhance the content validity the researcher sought the opinion of the experts especially the supervisor and the lecturers. Reliability was established through test-retest method whereby questionnaires were administered twice to the same group of respondents. A time lapse of one week was allowed before the questionnaires were administered again. A comparison between the two sets was made using Pearson's correlation co-efficient to determine the reliability of the questionnaires.

CHAPTER FOUR

4.0 DATA FINDINGS AND RESULTS

This chapter covers data analysis and findings of the research. The data was summarized and presented in the form of proportions, means, and tables. Consequently, the collected data was analyzed and interpreted in line with the aim of the study to examine the determinants of loan repayment by the small scale enterprises in Kariobangi Division, Nairobi.

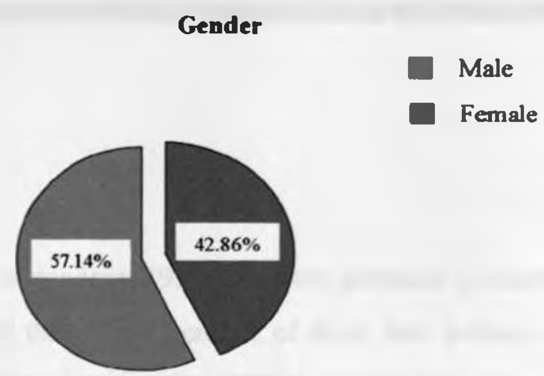
Of the 50 questionnaires distributed for this research, 41 useable questionnaires were returned giving a response rate of 82 percent, which was considered satisfactory for subsequent analysis.

4.1. Personal Characteristics of the Respondents

4.1.1 Gender

The respondents were asked to indicate their gender. From the research findings, it was established that 57.14 percent were female while 42.86 percent were male as shown in chart 4.1.1 below. This suggests that most SSEs in Kariobangi division are run by female.

Chart 4.1.1: Gender



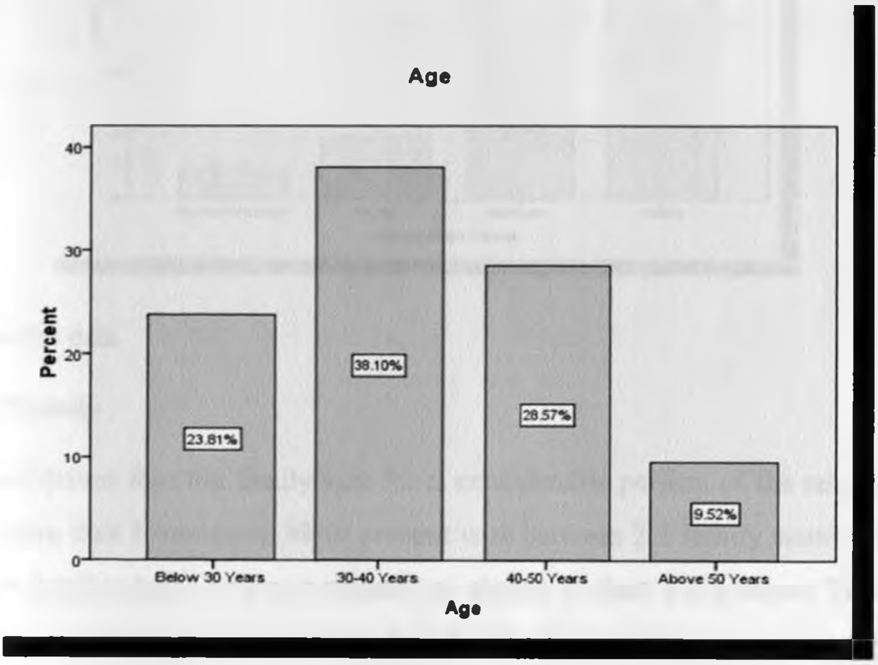
Source: Research data

4.1.2 Age

The respondent's lowest age is 24 while the highest is 69. The age distribution of the respondents indicated that 38.10 percent of the respondents are between 30-40 years, 28.57 percent between

40-50 years, 23.81 percent below 30 years and 9.52 percent of them are above 50 years as shown in chart 4.1.2 below. This suggests that most businesses in Kariobangi division are run by individuals at the age of 30s and 40s.

Chart 4.1.2: Age

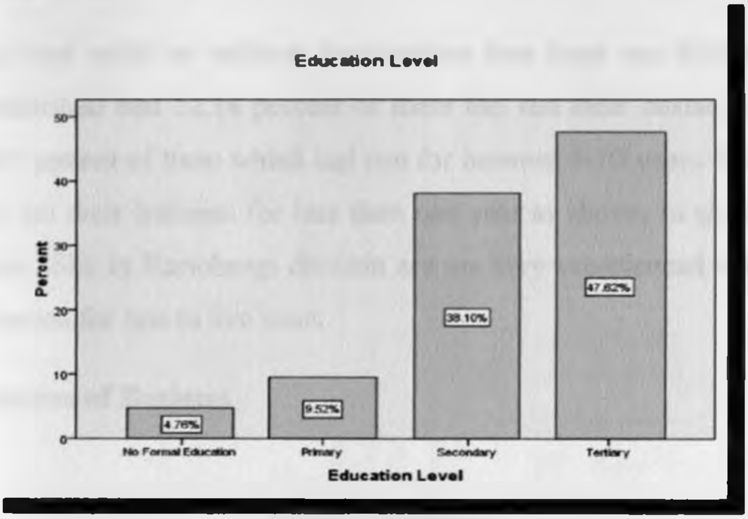


Source: Research data

4.1.3 Education Level

The majority of the sample respondents (95.24%) have attended primary, secondary or tertiary education. It was established that 47.62 percent of them had tertiary education level, 38.10 percent of them had secondary education level, 9.52 percent had primary education level and 4 76 percent had no formal education as shown in chart 4.1.3 below. This shows that most people who run SSEs in Kariobangi division have attained tertiary education. Therefore these SSEs possess limited management and modest technical skills.

Chart 4.1.3: Education Level

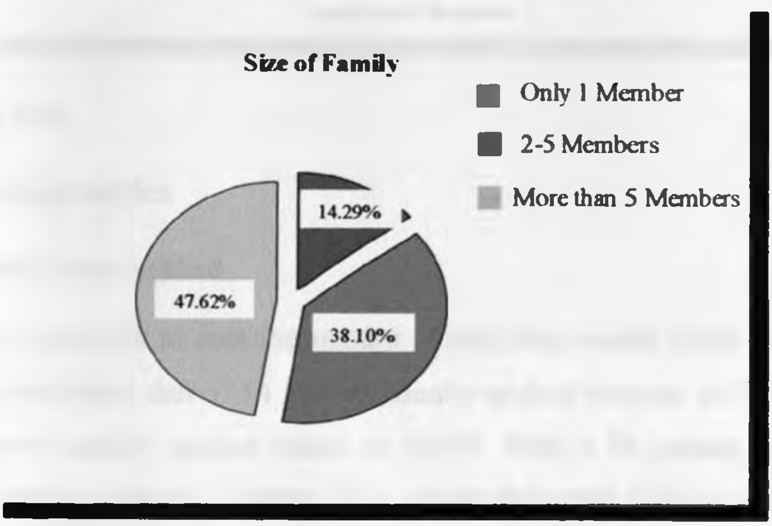


Source: Research data

4.1.4 Size of Family

The study established that the family size for a considerable portion of the respondents, 47.62 percent had more than 5 members, 38.10 percent with between 2-5 family members. Only 14.29 percent of the families have only one member as shown in chart 4.1.4 below. This implies that most families who borrow loans have more than five family members.

Chart 4.1.4: Size of Family

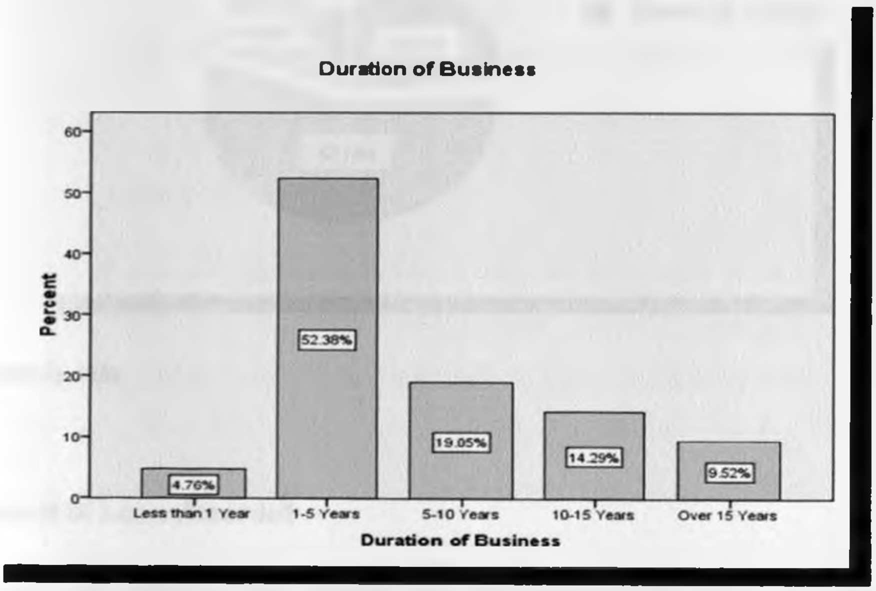


Source: Research data

4.1.5 Business Experience

The respondents were asked to indicate the duration they have run their business. From the study, it was established that 52.38 percent of them had run their business between 1-5 years followed by 19.05 percent of them which had run for between 5-10 years. It was noted that only 4 76 percent had run their business for less than one year as shown in chart 4.1.5 below. This suggests that most SSEs in Kariobangi division are not very experienced in business since they have been in operation for one to five years.

Chart 4.1.5: Duration of Business



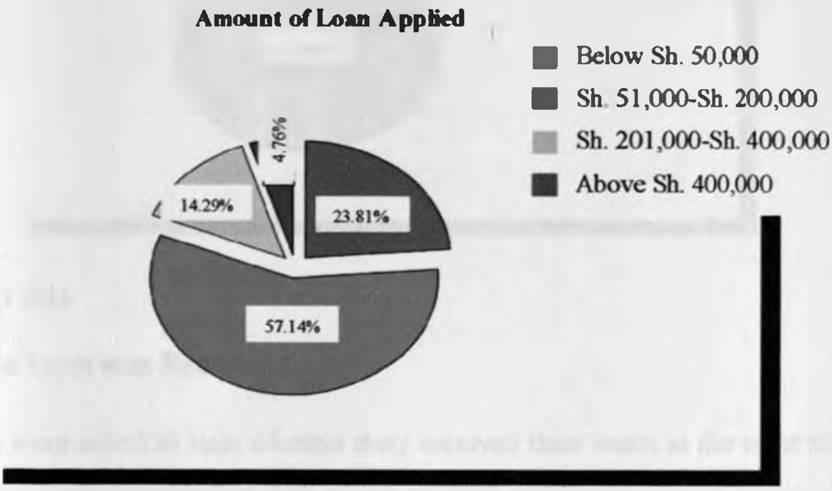
Source: Research data

4.2 Loan Characteristics

4.2.1 Amount of Loan Applied

The respondents were asked to state the amount of loan they usually apply. From the research findings, it was established that 57.14 percent usually applied between sh.51,000 - sh.200,000 while 23.81 percent usually applied below sh.50,000. Only 4.76 percent applied for above sh.400,000 as shown in chart 4.2.1 below. This implies that most SSEs in Kariobangi division apply low amounts of loans. Due to a lack of working capital, they cannot purchase raw materials in bulk at lower prices and take their goods to market, where they can attract better prices.

Chart 4.2.1: Amount of Loan Applied

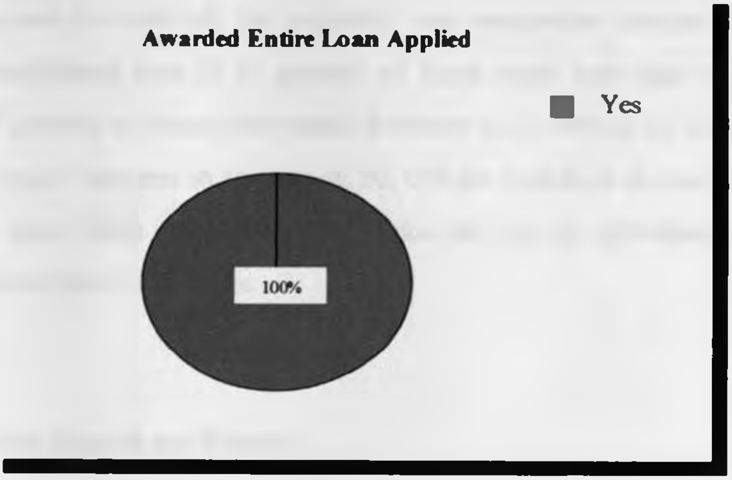


Source: Research data

4.2.2 Amount of Loan Awarded

The respondents were asked to state whether they were awarded the entire loan they had applied. From the research findings, it was established that 100 percent were awarded the entire loan they had applied as shown in chart 4.2.2 below. This implies that most SSEs usually got the whole amount they had applied. This may be attributed to the small amounts of loans they usually applied. For small-scale enterprises, reliable access to short-term and small amounts of credit is more valuable, and emphasizing it may be more appropriate in credit programs aimed at such enterprises.

Chart 4.2.2: Amount of Loan Awarded

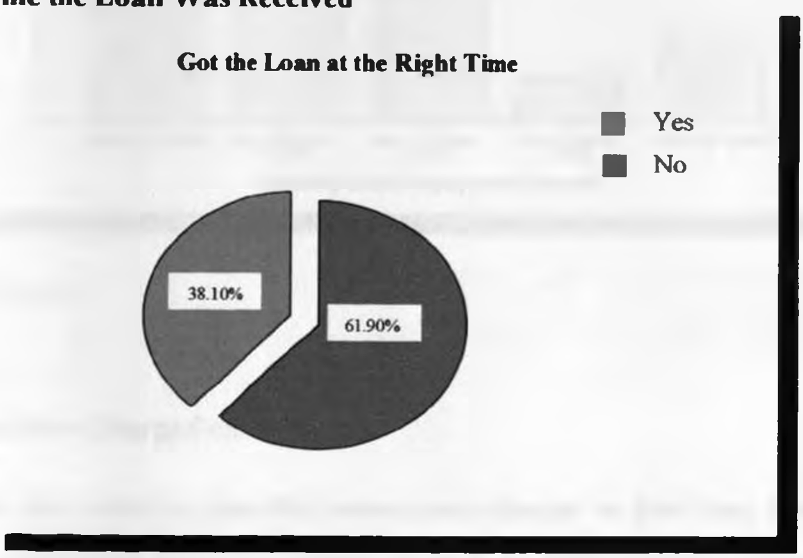


Source: Research data

4.2.3 Time the Loan was Received

The respondents were asked to state whether they received their loans at the right time. From the research findings, it was established that 61.90 percent got their loans at the right time while 38.10 percent did not get their loans at the right time as shown in chart 4.2.3 below. This implies that the loan processing for SSEs is faster due to too much competition in low income markets

Chart 4.2.3: Time the Loan Was Received

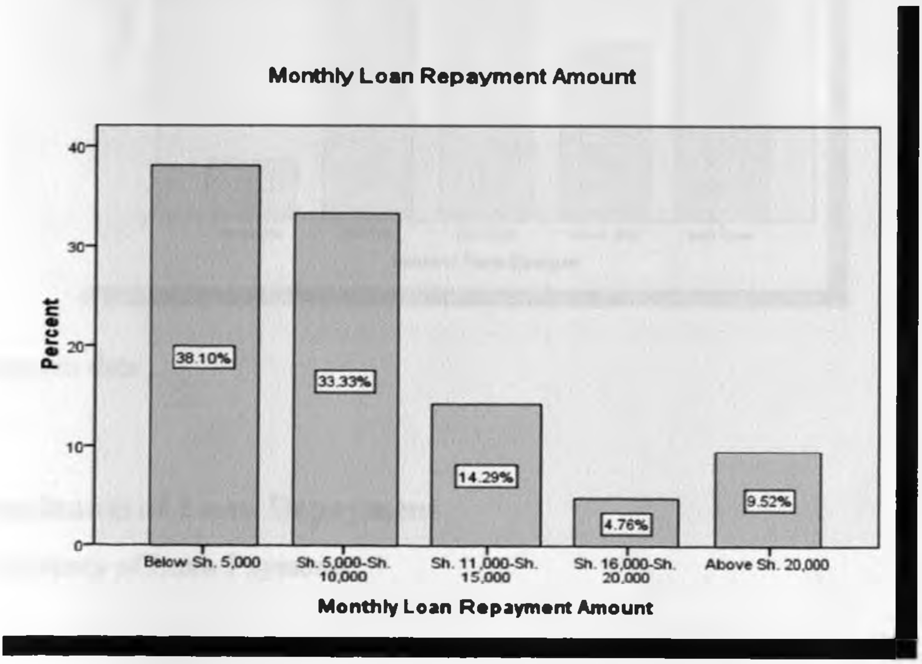


Source: Research data

4.2.4 Amount Repaid per Month

The researcher wanted to establish the monthly loan repayment amount. From the research findings, it was established that 38.10 percent of them repay less than sh.5, 000 per month followed by 33.33 percent of them who repaid between sh.5, 000-sh.10, 000. It was noted that only 4.76 percent repaid between sh.16, 000-sh.20, 000 per month as shown in chart 4.2.4 below. This suggests that most SSEs in Kariobangi division are run by individuals with low incomes due to the small size of their businesses.

Chart 4.2.4: Amount Repaid per Month

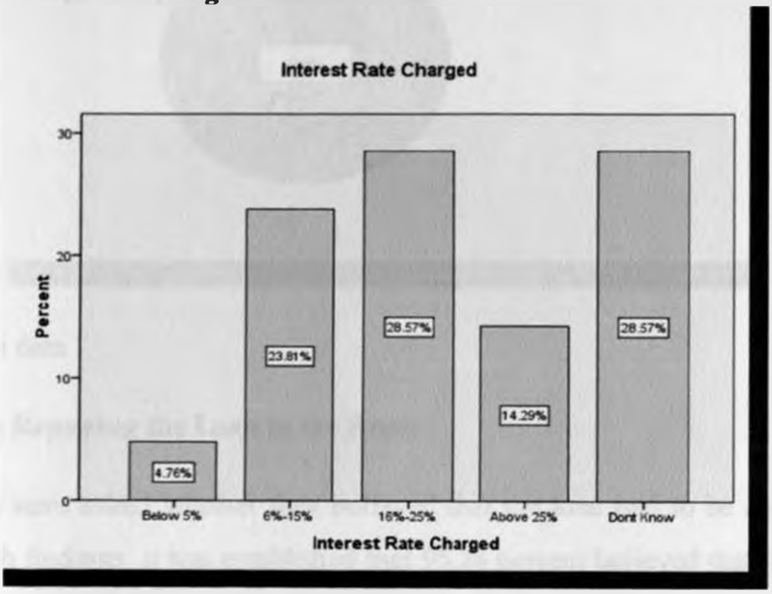


Source: Research data

4.2.5 Interest Rate Charged on the Loan

The respondents were asked to state the interest rate charged on their loan. From the research findings, it was established that 28.57 percent of them are either charged between 16%-25% or do not know the interest rate they are charged. 23.81 percent are charged an interest rate of between 6%-15%. It was noted that only 4.76 percent are charged an interest rate of below 5% as shown in chart 4.2.5 below. This suggests that most SSEs are run by individuals who do not know the interest rate they are charged on their loans. This may be attributed to limited management and modest technical skills of the borrowers.

Chart 4.2.5: Interest Rate Charged on the Loan



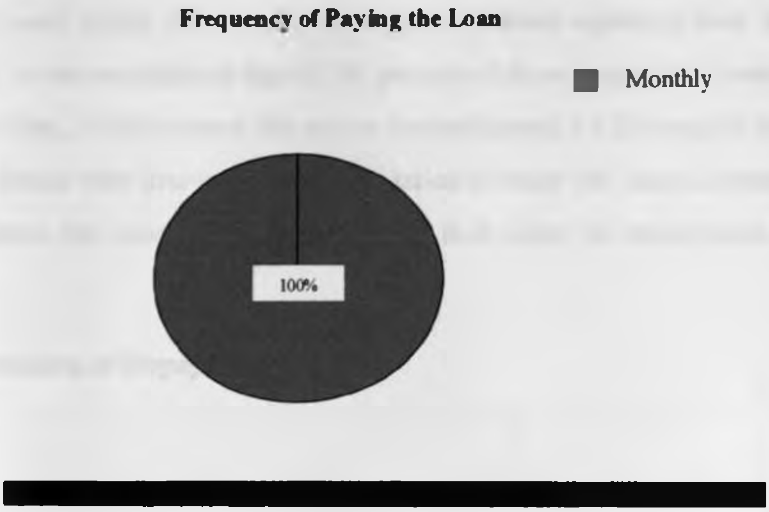
Source: Research data

4.3 Determinants of Loan Repayment

4.3.1 Frequency of Loan Payments

The respondents were asked to state the frequency at which they pay their loans. From the research findings, it was established that 100 percent of them repay their loans on a monthly basis as shown in chart 4.3.1 below. This implies that most SSE owners in Kariobangi division prefer to repay monthly as they do not have a constant source of income.

Chart 4.3.1: Frequency of Loan Payments

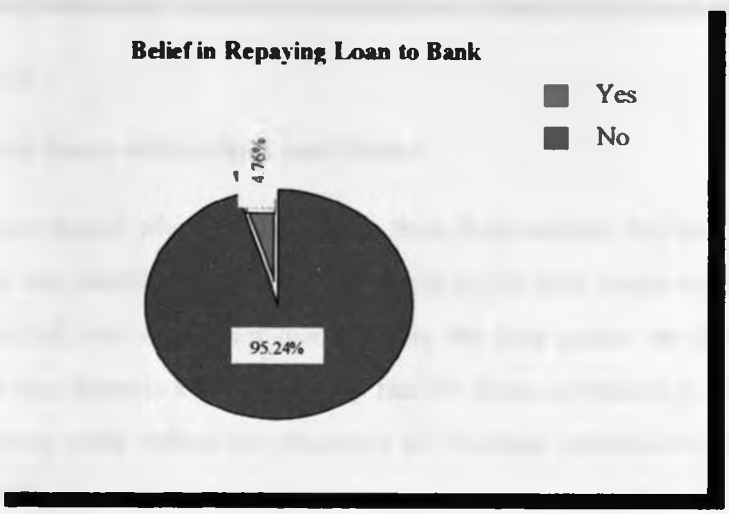


Source: Research data

4.3.2 Belief in Repaying the Loan to the Bank

The respondents were asked whether they believed that the loan had to be repaid to the bank. From the research findings, it was established that 95.24 percent believed that the loan had to be repaid to the bank while 4.76 percent did not believe that the loan had to be repaid to the bank as shown in chart 4.3.2 below.

Chart 4.3.2: Belief in Repaying the Loan to the Bank

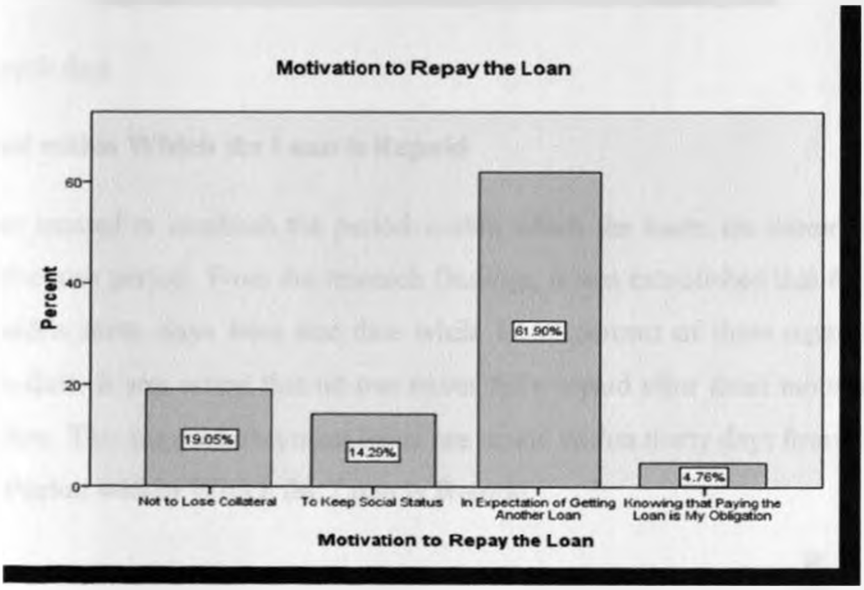


Source: Research data

4.3.3 Motivation of Repaying Loan

The respondents were asked to state the motivation behind repaying their loans. From the research findings, it was established that 61.90 percent of them repay their loans in expectation of getting another loan, 19.05 percent fear not to lose collateral, 14.29 repay to keep social status and 4.76 repay because they know it is their obligation to repay the loan as shown in chart 4.3.3 below. This suggests that most SSEs owners repay their loans in anticipation of getting more loans in future.

Chart 4.3.3 Motivation of Repaying Loan

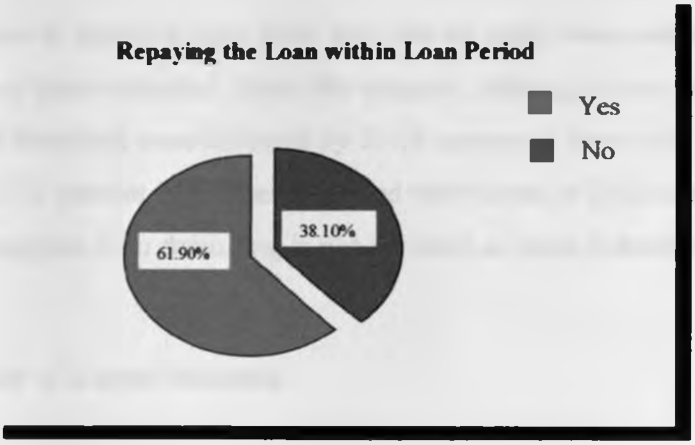


Source: Research data

4.3.4 Repaying the Loan within the Loan Period

The respondents were asked whether they repay their loans within the loan period. From the research findings, it was established that 61.90 percent repay their loans within the loan period while 38.10 percent did not repay their loans within the loan period as shown in chart 4.3.4 below. This implies that there is a high recovery rate for loans advanced to SSEs in Kariobangi division. High recovery rates reflect the adequacy of financial institution's services to clients' needs (Godquin, 2004).

Chart 4.3.4: Repaying the Loan within the Loan Period

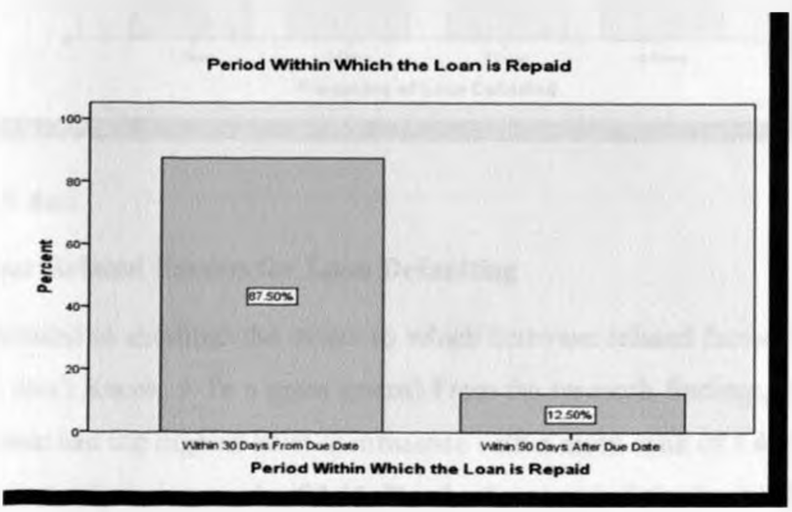


Source: Research data

4.3.5 Period within Which the Loan is Repaid

The researcher wanted to establish the period within which the loans are repaid for those who repay within the loan period. From the research findings, it was established that 85.50 percent of them repay within thirty days from due date while 12.50 percent of them repay within ninety days after due date. It was noted that no one never fully repaid after three months as shown in chart 4.3.5 below. This suggests that most loans are repaid within thirty days from due date

Chart 4.3.5: Period within Which the Loan is Repaid

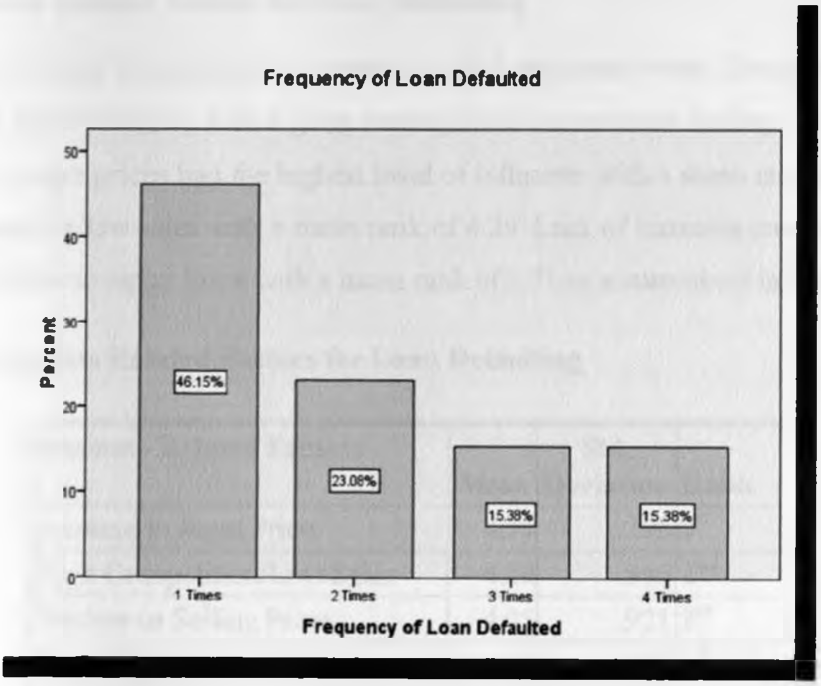


Source: Research data

4.3.6 Number of Loans Defaulted

The researcher wanted to establish from those who did not repay loans within the loan period the number of loans they have defaulted. From the research findings, it was established that 46.15 percent of them had defaulted once followed by 23.08 percent of them who had defaulted twice. It was noted that 15.38 percent had either defaulted three times or four times as shown in chart 4.3.6 below. This suggests loan defaulting is not common as most defaulters had only defaulted once.

Chart 4.3.6: Number of Loans Defaulted



Source: Research data

4.3.7 Borrower Related Factors for Loan Defaulting

The researcher wanted to establish the extent to which borrower related factors lead to failure to repay loans (1-I don't Know, 5-To a great extent).From the research findings, it was established that family problem had the highest level of influence with a mean rank of 3.48 followed by lack of formal education with a mean rank of 2.62. Death of spouse had the least influence on failure to repay loans with a mean rank of 2.14 as summarized in table 4.3.7 below

Table 4.3.7 Income controls adopted by secondary schools.

Borrower Related Factors	Mean	Std. Deviation	Rank
Family Problem	3.48	.928	1st
Lack of Formal Education	2.62	.740	2nd
Ill Health	2.48	1.209	3rd
Death of Spouse	2.14	.727	4th
Average	2.68		

Source: Research data 2012

4.3.8 Business Related Factors for Loan Defaulting

The researcher wanted to establish the extent to which business related factors lead to failure to repay loans (1-I don't Know, 5-To a great extent).From the research findings, it was established that increase in input prices had the highest level of influence with a mean rank of 4.33 followed by high competition/low sales with a mean rank of 4.29. Lack of business premises had the least influence on failure to repay loans with a mean rank of 2.71 as summarized in table 4.3.8 below.

Table 4.3.8: Business Related Factors for Loan Defaulting

Business Related Factors	Mean	Std. Deviation	Rank
Increase in Input Price	4.33	.796	1st
High Competition/Low Sales	4.29	.845	2nd
Decline in Selling Price	4.05	.921	3rd
Lack of Business Premises	2.71	.902	4th
Average	3.845		

Source: Research data (2012)

4.3.9 Lender Related Factors for Loan Defaulting

The researcher wanted to establish the extent to which lender related factors lead to failure to repay loans (1-I don't Know, 5-To a great extent).From the research findings, it was established that higher interest rates had the highest level of influence with a mean rank of 4.29 followed by political instability with a mean rank of 3.62. Extraneous caused had the least influence on failure to repay loans with a mean rank of 2.29 as summarized in table 4.3.9 below

Table 4.3.9 Lender Related Factors for Loan Defaulting

Lender Related Factors	Mean	Std. Deviation	Rank
Higher Interest Rate	4.29	.644	1st
Political Instability	3.62	.740	2nd
Smaller Loan Size	2.48	1.209	3rd
Extraneous Causes	2.29	1.309	4th
Average	3.17		

Source: Research data (2012)

4.4 Regression Analysis

The research study wanted to examine the determinants of loan repayment by the small scale enterprises in Kariobangi Division, Nairobi. The research findings indicated that there was a strong positive relationship (R= 0.816) between the variables. The study also revealed that 66.7% of loan repayment can be explained by the independent variables. From this study it is evident that at 99% confidence level, the variables produce statistically significant values for this study when combined hence can be relied on to explain loan repayment. The findings are as shown in table 4.4.1 below.

Table 4.4.1 Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.816[a]	.667	.487	.914

Source: Research Data 2012

The results of the regression equation below shows that for a 1- point increase in the independent variables, loan repayment by the small scale enterprises in Kariobangi Division, Nairobi is predicted to increase by 32.571, given that all the other factors are held constant. The findings are as shown in tables 4.4.2 below.

Table 4.4.2 Regression Analysis

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	21.712	7	3.102	3.713	.020[a]
Residual	10.859	13	.835		
Total	32.571	20			

Source: Research Data 2012

Positive effect was reported on education level, size of family, amount of loan applied and duration of business (β_3=0.035, β_4=0.138, β_5=0.634 and β_7=0.44) respectively. However, negative effect was reported for gender, age, and interest rate (β_1=-0.120, β_2= -0.495 and β_6= -0.272) respectively. The findings are as shown in table 4.4.3 below

Table 4.4.3 Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	.810	2.015		.402	.694
Gender	-.302	.425	-.120	-.710	.490
Age	-.669	.462	-.495	-1.449	.171
Education Level	.053	.332	.035	.158	.877
Size of Family	.240	.396	.138	.607	.554
Amount of Loan Applied	1.044	.388	.634	2.691	.019
Interest Rate Charged	-.270	.179	-.272	-1.511	.155
Duration of Business	.514	.308	.444	1.668	.119

Source: Research Data 2012

From the research findings above, the equation for the regression model will be expressed as below:

$LRi = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 .... \beta_n X_n + \varepsilon$

$LRi = 32.571 - 0.120 X_1 - 0.495 X_2 + 0.035 X_3 + 0.138 X_4 + 0.634 X_5 - 0.272 X_6 + 0.444 X_7 + e$

Where LRi - Loan repayment

β_0 - Constant

ε - error term

β_1X_1, β_2X_2, β_3X_3, and β_4X_4 - personal factors that influence loan repayment

β_5X_5, and β_6X_6 - loan specific factors that influence loan repayment

β_7X_7 - business specific factor that influence loan repayment

CHAPTER FIVE

5.0 SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary

The objective of the study was to examine the determinants of loan repayment by the small scale enterprises in Kariobangi Division, Nairobi. From the research findings, it was found that SSEs in Kariobangi division are run by female at the ages of 30s and 40s. It was noted that this group of borrowers had less loan defaults who repay their loans in anticipation of getting more loans in future. This is supported by the results the various descriptive and inferential statistics.

Most SSEs in Kariobangi division are small in size since they have been in operation for one to five years. Moreover, most SSE owners in Kariobangi division possess limited management and modest technical skills. It was established that they have attained formal education with most of them attaining primary, secondary or tertiary level. The study established that education level, size of family, amount of loan applied and business experience had a positive effect on loan repayment while gender, age, and interest rate had a negative effect on loan repayment

5.2 Conclusions

From the study findings it can be concluded that even though many factors can lead to loan defaults, some of the factors were regarded to be of higher impact. This is evident from the way respondents replied to questions and the analysis arising thereof. This study has shown that most of the factors are business related. Increase in input prices was the major factor that led to loan defaults while death of spouse was seen as the least factor that led to loan default.

Therefore it can be concluded that higher education level, large family size, large amount of loan applied and longer duration of business result in increased loan repayment and vice versa. However an increase in age, interest rate and change in gender leads to more loan default and vice versa.

5.3 Policy Recommendations

This study recommends that more loans should be advanced to female SSE owners aged 30-40s as they have proved to be the least loan defaulters. SSEs in Kariobangi division should insure their businesses in order to reduce risks associated with high input prices. The financial institutions should provide financial education and awareness to SSE owners as they are less educated. The financial institutions also need to invest more with the latest technology innovations in loan management to improve loan administration efficiency.

5.4 Limitations of The Study

This study was successfully undertaken but not without a few limitations. One such limitation was that some of the respondents declined to respond to the questionnaires. The time period covered by the study and the resources available to the researcher were also limited.

5.5 Suggestions for Further Research

Arising from this study, the following directions for future research in Finance were recommended as follows: First, this study focused on determinants of loan repayment of SSEs in Kariobangi division, Nairobi. Therefore, generalizations cannot adequately extend to other SSEs outside Kariobangi division, Nairobi. Based on this fact among others, it is therefore, recommended that a broad based study covering all SSEs in all major towns be done to find out the determinants of loan repayment.

Finally, Similar surveys to this can be replicated in a few years to come to assess if the determinants have changed as more SSEs are established in Kariobangi division.

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APPENDICES

Appendix I

QUESTIONNAIRE

This questionnaire is divided into two sections. Please complete each of the questions as instructed.

SECTION A: Personal Characteristics

1. Gender: male ☐ female☐

2. Your age (in years): Below 30 ☐ 30-40 ☐ 40-50 ☐ above 50 ☐

3. What is your education level:(Tick appropriately)

   No formal Education ☐
   Primary ☐
   Secondary ☐
   Tertiary ☐
   Other ☐ Please Specify…………………………………

4. What is the size of your family?...

5. For how long have you run your business? (Tick Appropriately)

   Under 1 year ☐
   1-5 years ☐
   5-10 years ☐
   10 – 15yrs ☐
   over15 years ☐

SECTION B: Loan Characteristics

6. How much loan did you apply for? ………………………………

7. Did you get the entire loan you applied for?

Yes ☐ No ☐

8. Did you get the loan at the right time?

Yes ☐ No ☐

9. What is your monthly loan repayment amount? ....

10. What interest rate are you charged on the loan? ....

SECTION C: Determinants of Loan Repayment

11. How do you pay your loan? (tick appropriately)

Weekly ☐

Fortnightly ☐

Monthly ☐

Other ☐ Please specify..

12. Do you have belief that loan has to be repaid to the bank? Yes ☐ No ☐

13. What motivates you to repay your loan?

☐ Not to lose collateral

☐ To keep social status

☐ In expectation of getting another loan

☐ Knowing that paying the loan is my obligation

☐ Others (specify)

14. Do you pay your loans within the loan period? Yes ☐ No ☐

15. If Yes, within which period do youmake your loan repayment? (tick appropriately)

- Within thirty days from due date ☐
- Within ninety days after due date ☐
- Not fully repaid after three months ☐

16. If No to question 13, how many times have you defaulted

1 time ☐

2 times ☐

3 times ☐

4 times ☐

Others ☐ Please specify……………………………………………………………

17. Please indicate the reason for failure to repay your loan by indicating the extent to which each of the factors listed below influenced. (Tick Appropriately):

1 –I don't know, 2 –To no extent at all, 3- To a very little Extent, 4 –To some Extent, 5 – To a great extent

Factors	**1**	**2**	**3**	**4**	**5**
Borrower related causes Ill health					
Death of spouse/partner					
family problem					
lack of formal education					
Business related causes:					

increase in input price					
lack of business premises					
high competition/low sales					
decline in selling price					
Lender related causes: smaller loan size					
higher interest rate					
Extraneous causes					
political instability					
Others: Please Specify					

Thank you for your time

Appendix II

LIST OF JUA KALI ARTISANS IN KARIOBANGI LIGHT INDUSTRIES

1	Abbutty's Enterprises
2	Aberdare Steel & Hardware
3	Alfa Coate Industries
4	Anoten Fabricators
5	Barco Painters Kariobangi
6	Batian Construction Co
7	Calvin Painters
8	Carbo Tech Engineering
9	Charge Auto
10	Choda Fabricators
11	Chuma Fabricators
12	Chuma Fabricators
13	Dave Auto
14	David Engineering
15	Desbro Engineering
16	Diarim Enterprises
17	Donholm Painters
18	Donholm Spares
19	East Africa Foundry Works
20	Elmco Paints & Hardware (K) Ltd
21	F. Omodi Painters
22	Fair Masters Upholstery Ltd
23	Fine Engineering works
24	Gume Painters
25	HauJua kali
26	Hemco Feeds (K) Ltd
27	Hertzian Engineering Services
28	HonzonElectroweld Services
29	Ibra Graphics
30	Improve Your Business Kenya
31	J.G Fabricators
32	J.Ochieng painters
33	Jackin Hardware
34	Jako Investments
35	Jamuhe Auto Electrician Ltd
36	Jiba Glass Mart & Hardware

37	Johana Leather Store
38	Jowab Hardware & Paints
39	Juakali K/S
40	K. South Painters
41	K. South Garage
42	K/S Juakali
43	K/south Auto
44	Kamash Painters
45	Kamco Stainless
46	Kangaroo Brands Ltd
47	Kanouvo Auto Parts
48	Kayole Graphics
49	Kayole Painters
50	Kayole Spray Painters
51	Kihara Cushion Makers
52	Kiwamma Electrical & Hardware Store
53	Kodisata garage
54	Komarock Auto Spares
55	KuteJua Kali
56	Lakeside Autos
57	Lamuwala Auto
58	Lily Atieno Agencies
59	Lovely Enterprises
60	MagamboJuakali
61	Majo Tec Enterprises
62	MakauFabricaters
63	Makenzi Signs
64	Marvel Hardware
65	Maxi-Oti Painters
66	Mbachimu Enterprises Ltd
67	Mid-Seven Hardware & Tools
68	Mini Bakeries (Nairobi) Ltd
69	Moha Graphics
70	Morrison Hardware
71	Motor Masters
72	Muto Auto Spares
73	N.C.C.K painters
74	N.C.C.K Panel beaters
75	Nanyuki Timber & Hardware

76	Ngetu Enterprises Ltd
77	Nikoyoo Painters
78	North View Machineries
79	Novus Engineering works
80	Ntado Fabricators
81	Nyagah Mechanical Engineers Ltd
82	Nyagah Mechanical Engineers Ltd
83	OboyoDonholm Auto
84	Ochieng Welders
85	Ochii Fabricators
86	Oduor Painters
87	OgutuJua Kali
88	Okoth Garage
89	Onyango Beaters
90	Otieno Industries
91	Otieno Mechanical and Spares
92	OtienoOketch Painters
93	Outering Road Motor Services
94	Owi Painters
95	Owino Auto
96	Owino Gym
97	Pakman Agencies
98	Plansteel Engineering
99	Prime Coatings Ltd
100	Profivex (K) Ltd
101	Rabai Garage
102	Reesi Engineering
103	Richfield Enterprises
104	Rico steel Fabricators
105	Riggers Enterprises
106	Rilsteel Hardware & Pipe Bending
107	Riziki Electronics Communications
108	Riziki Electronics Communications
109	Rolmil Fabricators
110	Ropa Engineering
111	Samphil Engineering & General Works
112	Sarang Company Ltd
113	Sekol Fabricators
114	Seweco Auto

115	Sisbro Co
116	SkanSteelmills
117	Stibloc engineers
118	Subard Masters
119	Subaro Masters
120	Super Fit Gym
121	Technosteel ltd
122	Timwood fabricators
123	Tito Mukere Garage
124	V. Onyango Painters
125	Viosfa Auto
126	Wooven Fabric Labels (E A) Ltd

Source: *Ministry of Labour, Department of Micro and Small Enterprise, Jua Kali Demontration and Training Centre, 2012*