

**THE EFFECT OF UNSECURED PERSONAL LOANS ON HOUSEHOLD
WELFARE OF SECONDARY SCHOOL TEACHERS IN BUNGOMA
COUNTY, KENYA**

BY

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DECLARATION

I declare that this research project is my original work and has never been submitted to any other University for assessment or award of a degree.

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

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D61/68137/2011

This management research project has been submitted for examination with my authority as the university supervisor.

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DEDICATION

I dedicate this work to my beloved wife Barbara and my son Hayne Aquila for persevering and supporting me all through my entire schooling time. Your love and encouragement has made this research a success. My Uncle Albert and my extended family members, May God bless you.

ABSTRACT

This research is a survey carried out in the nine districts in Bungoma County, Kenya. The main objective of this study is to establish the effect on unsecured personal loans on household welfare of Secondary school teachers in Bungoma County. Judgemental sampling was used to identify respondents who had accesses to unsecured personal loans in Bungoma County. Data was collected using questionnaires from 122 respondents across Bungoma County out of a total sample size of 180 teachers equally spread across the nine districts of Bungoma County. The study adopted frequencies, tables and percentages in data analysis and presentation. Regression analysis was adopted to establish the effect of unsecured personal loans on household welfare and the findings show that utilization of unsecured personal loans contributed to improved health care and better education, empowerment of female secondary school teachers, reduction of the poverty levels, creation of employment and earning of extra income, improved total household consumption, provision of startup capital for businesses, and enabled households to put up better houses. The study established that unsecured personal loans improved household welfare for Secondary school teachers in Bungoma County. The study recommended that the government comes up with monetary policies that will reduce the lending rate and enhance accessibility to unsecured personal loans to encourage development. This research also recommended that proper mechanisms be put in place to train and mentor teachers and encourage them to embrace borrowing as a means of raising capital for household development.

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ABBREVIATIONS

- ADB** – Asian Development Bank
- BBK** – Barclays Bank of Kenya
- CBK** – Central Bank of Kenya
- FSD** – Financial Sector Deepening
- KNBS** – Kenya National Bureau of Statistics
- MFI** – Micro Finance Institutions
- NBK** – National Bank of Kenya
- TSC** – Teachers Service Commission
- SACCOs** – Savings and Credit Cooperative Societies
- SME** – Small and Micro Enterprises

CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

Unsecured personal loan is a form of debt given to an individual by a financial institution without provision of collateral or security by the borrower. The main difference between a personal loan and other forms of credit given by commercial bank is that the source of repayment for personal loans is mainly from salary of the borrower. Any form of debt whose source of repayment does not come from the asset purchased but from wages or salary of the individual borrower is called a personal loan. (BBK 1999)

According to Paul (2004), empowerment theory represents an expansive view of individuals and collective behavior that includes active participation of individuals and groups in altering and shaping the socio-environmental context. This study will be based on the empowerment theory of credit which suggests that by enabling people to access credit, in this case personal loans; it is one of the ways of reducing global poverty and enhancing economic development and enabling them to meet household welfare needs. Unsecured personal loans emerged in the 1990,s as a change of strategy by commercial banks from the conventional collateralized lending as a result of fierce competition from microfinance institutions and SACCOs for the limited number of customers

Household Welfare on the other hand refers to the set of programs designed to meet the socio-economic indicators of a given group of people living the same compound with a common source of income. (Estes, 2004). Unsecured personal loans are mostly granted to people with evidence of a regular income by availing three month's consecutive pay slip. Most consumers of personal loans are teachers who access them from commercial

banks all over the country. Of late, microfinance institutions and Sacco's are granting personal loans due to the high interest charged on them and profits associated with economies of scale by lending to a large pool of borrowers (CBK, 2009).

Bungoma County has a total of 170 secondary schools spread across the nine districts namely Bungoma South, Bungoma West, Bungoma Central, Kimilili, Tongaren, Webuye East, Webuye West, Kanduyi and Bumula and Cheptais according to the Bungoma county Education records as at December 2012. Secondary school teacher's access unsecured personal loans from the large number of commercial banks located in urban centres of Bungoma, Kimilili, Chwele and Webuye. The banks that currently operate in Bungoma County include Co-operative Bank of Kenya, Bank of Africa, Consolidated Bank of Kenya, Kenya Commercial Bank, Barclays Bank, Equity Bank, Post Bank, Family Bank, National Bank of Kenya, Diamond Trust Bank Kenya Ltd and K-Rep Bank. Guide to Kenya, (2012).

Other than teachers, civil servants in various ministries and government departments, doctors, employees of education institutions in the County and social workers in nongovernmental organizations also have access to unsecure personal loans. This study seeks to establish the effect of unsecured personal loans on household welfare of secondary school teachers in Bungoma County.

1.1.1 Unsecured Personal Loans

Unsecured personal loan is a form of debt that is given to an individual borrower without collateral as long as the borrower has proved of regular income. Unsecured personal loans are obtained for consumer credit which refers to the use of credit to purchase

personal needs, such as durable goods, finance education, medical care and other expenses. (FSD & CBK, 2007).

The primary role of commercial banks is to collect deposits and lend money to earn interest. Kenya Banking act (2001). In the economic survey of 2005, economic growth in Kenya was attributed to SMEs most of which are funded by personal loan borrowings. Commercial banks have been realigning their operations and strategies to the external environment characterized by competition to achieve success Ansoff (1990). The country's leading financial institutions have continued to differentiate and diversify their products to meet the varying needs of their clientele. New consumer products reflect an on-going integration of external economic influences and understanding of local consumers' needs (Market Intelligence, 2006)

Unsecured personal loans are payable through check-off where the loan is recovered at source by the employer and remitted to the bank or through a standing order from the individuals' transaction account when his salary is received. Unsecured personal loans are considered as a risky segment to commercial banks especially to the high rate of defaulters. This is normally caused by multiple borrowing from different financial institutions against limited ability to pay by individuals and other reasons such as termination of employment, employer's failure to honor check-off arrangements with financial institutions and death of the borrower. (Ngila, 2010).

1.1.2 Household Welfare

A household refers to a person or group of people living in the same compound, answerable to the same family head and sharing a common source of food and income. Household welfare refers to a given set of socio-economic indicators used to measure poverty levels and living standards in Kenya. The parameters used to measure household welfare are monthly household income, Women empowerment, improved education and healthcare, Poverty reduction, number of Small business started, total consumption and improved housing. KNBS (2005/2006)

Jesco and Peter (1997) assert that access of the poor to basic services such as electricity, water, sewage or gas is often viewed as very important to the well-being of households. Access of a household to such services should not only be viewed as a reflection of the household's welfare standing, but also as a determinant of the latter. Basic services will in many instances be inputs into economic activities or will support them indirectly. For example, informal home-based businesses often rely on domestic power connections; time freed from fetching water or gathering wood for fuel can be diverted to income-generating activities; and potable water and sewage help to protect household members from diarrhea and other diseases. They further argue that there are other important components such as food intake, the consumption of various non-food goods and services and the consumption of housing services.

Unsecured personal loans have also the ability to assist in poverty alleviation among developing countries through empowering low-income households financially,

governments are able to reduce the unemployment rates and improve on income per capita. The small businesses run by low income individuals and households sponsored by personal loan borrowers provide employment to many unemployed people thus improving their lives as well as those of their immediate dependants (Yunus, 2001).

1.1.3 The Effect of Unsecured Personal Loans on Household Welfare

Unsecured personal loans are the source of finance for the employed middle class with a regular income in form of salary or wages in Kenya and all over the world. The employed middle class are usually unable to save part of their salaries to a certain amount to be able to acquire an asset, finance education, cater for medical emergencies or start small businesses hence unsecured personal loans come in handy since most of this people do not have collateral. (Mash and Wild, 1990).

The other positive effect of microfinance on household welfare is its ability to assist in empowering women in low income households. Once these women are empowered financially, they are able to provide for their families thus improving the living standards of the low income people in the society. Bagchi et al. (2002). Giving of unsecured personal loans by commercial banks bridges the gap created by Conventional lending institutions between collateral holders who are rich and the uncollateralized customers. Unsecured personal loans have been advanced by commercial banks to assist individuals improve their homes, put up businesses to generate some additional income to their families, fund medical expenses, finance basic and higher level education for employees and their family members, access electricity and clean water connection, restructuring

outstanding debts to improve monthly net pay, invest in farming to guarantee food security and acquire assets such as land cars and houses. Wangura and CBK (1997).

1.1.4 Secondary School Teachers in Bungoma County.

Bungoma County is in the Western Part of Kenya. It borders the republic of Uganda, Busia, Kakamega and Trans Nzoia Counties. Bungoma's capital town is Bungoma town. Due to the local climate there, sugarcane and maize cultivation is the main economic activity that is maintained. The major economic activities in the region include: sugarcane and maize farming, livestock keeping and breeding, some poultry farming. (Guide to Kenya, 2012). According to Commission on Revenue Allocation (2009), Bungoma County has a total population of 1,630,934 people. In terms of population, it is ranked third in the Republic of Kenya. 22 % of the population of Bungoma County resides in the urban centers in the county. Bungoma is well served with financial institutions. Financial institutions offering unsecured personal loans in Bungoma County include Kenya Commercial Bank, National Bank of Kenya, Barclays Bank, Standard Chartered Bank, Equity Bank, Family Bank, Bank of Africa, Post Bank, K-Rep Bank and Diamond Trust Bank. Salaried employees in Bungoma County can also access unsecured personal loans from Bungoma Teachers Sacco, Metropolitan Teachers Sacco and deposit taking Micro finance institutions such as Faulu Kenya and Kenya Women Finance Trust. Guide to Kenya, (2012).

According to the County education directors' records, Bungoma County has a total of 170 secondary schools with a total secondary school teacher population of 2000 teachers.

The schools include mixed secondary schools, day schools and boarding schools located in the nine districts of Bungoma County. Secondary school teachers are employees of the teachers service commission (TSC) which deploys them to their respective stations.

Teachers form the largest group of employees that take up personal loans from commercial banks. These loans are payable over a maximum period of 72 months with interest rates varying from 14% to 24%. Some commercial banks have memorandum of understanding with the TSC to enable teachers access unsecured personal loans at preferential rates. Unsecured personal loans are payable through check-off or through standing orders from the borrowers transaction accounts (Bochaberi, 2007)

1.2 Research Problem

Access to unsecured personal loans has been associated with increased incomes and financial stability in many countries around the world. There is a general assumption that access to unsecured personal loans will improve household welfare with reference to consumption levels and better living standards of borrowers. The main obstacle in determining the effect of unsecured personal loans on household welfare of secondary school teachers is in establishing weather the improvement is better compared to those secondary school teachers that did not take up these loans. Empowerment Theory states that enabling people to access microcredit is one of the ways of reducing global poverty and enhancing economic development. Paul (2004).

In the past, the employed middle class particularly teachers had minimal or no access to credit facilities since they were regarded as more risky and unlikely to repay their loans allowing a few to acquire personal loans at exorbitant interest rates. However, this trend

has changed in the last decade as a result of financial liberalization and lowering of the base lending rate coupled with increase in the number of banks' branch network expansion. Some microfinance institutions such as K-REP and FAULU have been transformed into banks and local banks are competing favorably against Multinational institutions resulting to increased access to credit facilities amongst employees including secondary school teachers. Bungoma County is one of the areas in Kenya where there is evidence of microfinance institutions that have been providing microfinance loans to low income households.

Previous studies on the effect of credit on household welfare have shown a positive impact. For instance Mugabi (2010) who conducted a study on micro-credit utilization and its impact on household income, it was a comparative study of rural and urban areas in Iganga district, Uganda. Sengsourivong (2006) conducted a study on the impact of microfinance on household welfare. Odell (2010) conducted a study on measuring the impact of microfinance in selected countries including Kenya. Grades (2007) carried out a study on the impact of microfinance on rural poor households' income and vulnerability to poverty in Makueni district, Kenya. However other studies such as Zeller (2001) while conducting a research on access to credit and its impact in Malawi suggested that loans did not have any significant effect on household welfare. There is evidence of mismanagement of personal loans, multiple borrowing and defaults leading to legal suits against secondary school teachers making them to suffer more as a result of accessing such loans.

There is evidence of previous research by Omwange and Omoro (2013) on household welfare in Bungoma County which associated utilization of microfinance loans with improved household welfare. However, no study has been carried out on the effect of unsecured personal loans on household welfare of secondary school teachers in Bungoma County despite the fact that this type of loan forms the greater portion of loan portfolios in commercial banks and the largest beneficiaries are teachers. This study seeks to bridge this gap by examining the effect of unsecured personal loans on household welfare with specific reference to secondary school teachers in Bungoma County. The study seeks to answer the following question: What is the effect of unsecured personal loans on the household welfare of Secondary school teachers in Bungoma County?

1.3 Research Objective

The objective of this study was to determine the effect of unsecured personal loans on household welfare of Secondary school teachers in Bungoma County

1.4 Value of the Study

The study sought to contribute to theory by providing additional evidence to support the empowerment theory of credit. Scholars will use information in this study as part of their literature review while carrying out further research on unsecured personal loans and household welfare. This study also identified the research gaps to enhance further investigation by scholars on accessibility to unsecured lending and its impact on the welfare and general living standards of borrowers.

This research will also enable policy makers in Commercial banks to appreciate the impact of unsecured lending to salaried customers and develop measures that will increase accessibility to unsecured loans by lowering the interest rates levied on unsecured credit facilities. This will enhance credit access and improve profitability of commercial banks. The government on the other hand shall use the findings of this study to establish monetary policies that will reduce the base lending rate which will translate to reduced interest rates charged by commercial banks thus enhancing accessibility to unsecured facilities. Salaried employees will also find this research work useful by appreciating what unsecured loans have contributed to the welfare of secondary school teachers. This in turn will enhance accessibility since most people fear accessing loans from financial institutions due to financial illiteracy.

TWO: LITERATURE CHAPTER REVIEW

2.1 Introduction

This chapter summarizes the literature that is already in existence regarding unsecured personal loans. Relevant theories and empirical evidence is reviewed in this chapter. There are a number of theories that try to explain the growth in access to unsecured personal loans over time. This chapter review The Neoclassical theory, The Welfarist theory and The Empowerment theory of credit

2.2 Theories Underpinning the study

The Neoclassical theory emphasizes the importance of saving in order for a country's economy to grow. Todaro et al. (2003) established that the main limitation for poor households in developing countries is lack of access to financial services caused by imperfect financial markets and poor lending culture by commercial banks offering their services almost exclusively to the medium and large companies perceived to be credit worthy therefore hampering accumulation of capital and growth of the economy.

The Welfarist theory as discussed by Robinson (2001) suggests that credit is provided to poor borrowers at below market interest rates in order to reach the extremely poor to help overcome poverty and empower them. Welfarist theory focuses on credit as a tool of reducing poverty. Performance of Commercial banks is done using the assets base, number of performing loans and size of the loan book, income and corporate social responsibility such as education, health and humanitarian activities undertaken by financial institutions in improving the household welfare of people.

The empowerment theory advocates for empowering or enabling the poor financially. Proponents of this theory argue that the poor who are about 19.3 million usually lack access to credit facilities. Most women despite lack of collateral are able to access credit in order to invest in businesses that they own. Most of them have good credit history, in spite of the challenges they face, hence they have come out strongly to show that it is a good idea to lend to the poor and middle class (Cheston and Kuhn, 2002).

The prospect theory was developed by Kahneman & Tversky, (1979) as a psychologically realistic alternative to expected utility theory. It allows one to describe how individuals make choices in situations involving alternatives and risk i.e. financial or credit decisions. It describes how individuals evaluate gains and losses in arriving at financial decisions.

2.3 Unsecured Personal Loans

Access to unsecured personal loans refers to the borrower's willingness and ability to borrow a certain amount of money at a specified interest rate and pay without default or strain within the agreed loan term. The change of Strategy by Commercial Banks has led to increased accessibility to unsecured personal loans. The primary role of Commercial Banks is to mobilize deposits and lend money to earn interest. Performance of commercial banks is measured by the degree of how much money has been lent and the proportion of the loan book that is performing, Kenya Banking Act (2001).

The economic survey of 2005 economic growth was attributed to SMEs most of which are funded by personal borrowings. Therefore when Commercial banks introduced

unsecured personal loans as a growth and retention strategy there was phenomenal access by salaried customers. Major breakthrough of personal loans has been to find a cost effective way to judge the credit worthiness of secondary school teachers and transforming the bank and understand their needs hence cross sell products to them (Stensland and Pedersen,1995)

Following the roll out of borrower's credit referencing in Kenya on 31st July 2010, commercial banks have submitted both the positive and negative credit history of their borrowers to the two licensed bureaus i.e. CRB Africa and Metropol CRB that offer banking sector credit information sharing. Information shared on this platform includes loan defaults and late payment. This has served as a deterrent measure against willing defaulters. It is worth noting that negative information does not amount to black-listing rather banks should take such information into account when granting credit. On the other hand positive information can be used by unsecured loan borrowers to negotiate for favorable interest rates on credit facilities. Credit information sharing has reduced information asymmetry and it is expected in future to lower the appraisal costs and ultimately reduce the cost of borrowing by individuals and improved accessibility to unsecured lending which will help borrowers without security (Finance Credit Reference Regulations, 2008).

Liberalization of credit market and lowering of interest rate has contributed to growth in uptake of personal loans. Interest rate refers to the cost of borrowed money or a reward to the lender for the opportunity cost foregone. It also includes payment for the risks involved and to compensate against an uncertain future (Stanlake, 1987). Since 1997, the

Central Bank of Kenya does not dictate the rate of interest charged by commercial banks on borrowed money or the rate paid on customer s' deposits. This has allowed commercial banks to enter into Memorandum of understanding with various employers; a case in point being the MOU between NBK and TSC. (CBK, 2007)

Increased competition and marketing strategies adopted by SACCOs and MFIs has also been a contributing factor towards growth in personal loans. The Kenyan Banking industry has experienced competition from SACCOs and MFIs. This led to the withdrawal of Multinational Banks from some rural areas a case in point being closure of many Standard Chartered Bank branches in the 1990s. The competition for few depositors and the need to grow the loan book has led to the improvement in bank's efficiency in operations and lowering of the interest rates and the cost of accessing credit.

Increased marketing efforts and the struggle to attract and retain salaried customers due to competition from commercial banks, MFIs and SAACOs has led to the change in what attracts most customers. Customers are only opening accounts and changing their pay points to specific institutions when they are guaranteed of accessing unsecured personal loans. Commercial banks are using unsecured loans to lure salaried individuals to open accounts and channel their salaries through their accounts. This has led to increased access to unsecured personal loans. FSD Kenya, (2009).

Commercial banks have also changed their strategic view of their operating environment, a factor that has enhanced access to unsecured personal loans. Pearce and Robinson (1991) describe external environment as all conditions that affect a firm's strategic options but which are beyond a firms' control. Ansoff and Mc Donnel, (1990) noted that

changing environment brings about unpredictability. They referred to this as environment turbulence. Aosa, (1992) noted that this environment changes bring about changes to the management. Chandler (1962) and Draft (1986) separately argued that organizations are environmentally dependent and changes in the environment bring about opportunities. The banking environment has been changing rapidly since the 1990's bringing about radical redesign and business reengineering of the bank's core business i.e. lending. This has led to the development of uncollateralized loan products therefore improving accessibility to unsecured personal loans.

2.4 Household Welfare

Household welfare is measured by real consumption of goods and services which should be approximated at the same price across households. This should reflect the average marginal utility to the consumer. When households are able to access services such as electricity, water, sewage system or gas is often viewed as very important to the well-being of households. This is not only viewed as a reflection of the household's welfare standing, but also as a determinant of the latter. Basic services will in many instances be inputs into economic activities or will support them indirectly. For example, informal home-based businesses often rely on domestic power connections; time freed from fetching water or gathering firewood can be diverted to income-generating activities; and potable water and sewage help to protect household members from diarrhea and other diseases (Jesco and Peter, 1997).

Commercial banks play a major role in improving the household welfare by granting unsecured personal loans which help in poverty alleviation, provide emergence cushion,

used to pay school fees and further education costs, provide startup capital for small businesses, access better health care and housing as well as to finance agricultural activities.

Previous studies both locally and outside Kenya on household welfare have examined Microfinance Institutions and their impact in alleviating poverty and improving household welfare. In Kenya some Microfinance Institutions and SACCOs have been licensed to take deposits and give loans including the unsecured personal loans. Some MFIs have been converted into commercial banks such as K-Rep Bank and Faulu Kenya and Kenya Women Finance Trust. Equity bank and Family Bank which started as building Society institutions are now commercial Banks offering both Micro-credit and Unsecured personal loans. These institutions, despite upgrading to commercial banks have not stopped giving Micro-Credit. Main stream commercial Banks such Kenya Commercial Bank, National Bank, Eco Bank, Bank Of Africa, Commercial Bank of Africa and Co-operative Bank of Kenya have adopted Micro-finance as a result of competition. FSD & CBK (2009).

Tilakaratna (2005) carried out a study on the impact of Microfinance in Sri – Lanka. The study was an analysis of outreach of microfinance and impact on poverty in Sri-Lanka. The study found out that microfinance in Sri-Lanka has a wide outreach to low income people. It was also established that microfinance has assisted the poor people to smooth their income and expenditure. It was also clear that even though microfinance is meant to assist the poor, majority of those who had positively benefited from microfinance were non poor people from Sri-Lanka.

Mahjabeen (2008) conducted a study on the micro financing in Bangladesh. The objective of the study was to assess the impact on households, consumption and welfare. The main findings of the study indicate that MFIs raise income and consumption levels of households reduce income inequality and enhance welfare. This implies that microfinance is an effective development strategy and has important policy implications regarding poverty reduction, income distribution and achievement of millennium development goals.

The Asian Development Bank ADB (2007) carried out a special evaluation on the effect of microfinance operations on poor rural households and the status of women. The main objective of evaluation study was to assess the extent to which selected Asian Development Bank (ADB) microfinance projects have reduced the poverty of rural poor households and improved the socioeconomic status of women in developing member countries. Bangladesh, Philippines, and Uzbekistan were selected for the study, representing three of the five operational regions of ADB. The projects selected for in-depth review were: Rural Microenterprise Finance Project in the Philippines; Participatory Livestock Development Project in Bangladesh; Second Participatory Livestock Development Project in Bangladesh; Rural Livelihood Project in Bangladesh; and Small and Microfinance Development Project in Uzbekistan. The results of the evaluation study show that the availability of microcredit loans had positive and mildly significant impacts on the per capita income of the beneficiaries. The income of those

that received microcredit loans increased compared with those that did not receive a loan (ADB, 2007).

Nghiem et al., (2007) conducted a quasi-experiment survey on the welfare effects of microfinance in Vietnam. The study analyzed the effects of microfinance programs upon household welfare in Vietnam. Data on 470 households across 25 villages was collected using a quasi experiment survey approach to overcome self-selection bias. In the study's econometric analysis, the welfare effects of microfinance are substituted using measures of household income and consumption. The empirical results indicate that participation in microfinance has a positive effect upon household welfare, with the size of the effect increasing at a decreasing rate as a household spends more time in the microfinance program.

Another study was also carried out by Kondo et al., (2008) on the impact of microfinance on rural households in the Philippines. The study established that the impact of the availability of microfinance loans on per capita income is shown to be positive and marginally significant. This is also true for per capita total expenditure and per capita food expenditure. But it was also found that this impact is insignificant for poorer households and becomes only positive and increasing with richer households. It was also established that microfinance kept clients economically active with more enterprises and more employees. The study recommended that for microfinance to be an effective poverty-alleviation tool there is a need to review targeting procedures to know whether these are correctly identifying the intended beneficiaries

Hira (2009) while studying the need for personal financial literacy established lack of working knowledge on personal finance incapacitates individuals from making vital economic decisions. This explains why the government, academia, commercial banks and non-governmental organisations have shifted attention on financial literacy of individuals to ensure economic growth. According to Aghion and Murdoch, (2005) lack of good information about personal borrowers results to adverse selection effect making banks unable to distinguish between risky and good borrowers. This restrains future access to credit from

Collender (1994) recognizes three important reasons for financial services efficiency in his research. A general principal is that improved efficiency and financial accessibility leads to economic wellbeing and economic growth, Secondly there is need to establish the root causes of observed financial inefficiency and develop policies to improve efficiency. The third reason is that fear persists in rural areas that relaxing bank regulations will decrease lending to small local business, small communities and agriculture.

Most big banks in developed economies pursue large corporate loans as their main clientele. This is because large loans enable banks to grow their market size and profitability at minimal cost. In contrast SME and personal loans are seen to be less attractive because of the large costs of processing and monitoring. Most loan officers have been trained to evaluate borrowers with accounting records and information. Many lack the necessary language and skills to appraise personal and SME loans which lack adequate information to determine the risk levels (Ram Consultancy services, 2005)

According to Nduba (2010), in the current environment where banking is characterised by cutthroat competition, the challenge is for the loan officer to do a thorough assessment of the loan and avoid losing the customer to the competitor. Despite all the risks related to SMEs due to lack of collateral, banks cannot afford to ignore the unsecured loan segment since it forms the large portion of the credit market. Financial institutions have therefore developed complex credit appraisal and scoring tools to analyse unsecured lending.

2.5 Summary of Literature Review

Most studies have associated credit especially micro credit with improved household welfare. Omwange and Omoro (2013) associated utilization of microfinance loan with improved Welfare in Bungoma County. However not much has been done to assess the effect of unsecured personal loans on household welfare of Secondary school teachers in Bungoma County despite the fact that this forms the largest portion of loan portfolios in commercial banks. Secondary school teachers are also the major beneficiaries of this facility due to its flexibility in repayment and ease of access.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents the appropriate research design that was used to conduct the study. The section sets out the target population, design of the sample size that will be used in the study to arrive at the required sample size and the type of instruments that will be used to collect data and how the same will be analyzed and presented.

3.2 Research Design

A descriptive survey research design was employed to determine the effect of unsecured personal loans and household welfare in Bungoma County. Most employed Secondary school teachers reside in the urban areas of Bungoma County. This is the most appropriate design to investigate the effect of Unsecured Personal Loans on House hold welfare because it intends to come up with findings that show the prevailing effect of personal loan borrowing on the welfare of Secondary school teachers in Bungoma County.

3.3 Target Population

The population studied were secondary school teachers spread over the nine districts of Bungoma County namely Bungoma South, Bungoma West, Bungoma Central, Kimilili, Tongaren, Webuye district, Kanduyi and Bumula districts and Cheptais who had accessed unsecured personal loans. The county has a total of 170 secondary schools and a total teacher population of 2000 according to the Bungoma County. The researcher

targeted 20 secondary school teachers from each county forming a total population of 180 teachers from the nine districts in Bungoma County.

3.4 Sample Size

Judgemental sampling technique was used to select equal number of respondents from each district in Bungoma County. Out of the total Secondary school teacher population of 2000, the researcher sampled 20 teachers from each district in Bungoma County giving a total sample size of 180 teachers. This type of technique will be employed since not all secondary school teachers have taken personal loans. It therefore requires the researchers' judgement in choosing respondents

3.5 Data Collection

The study made use of primary data. Primary data is information gathered directly from the respondents (Kothari, 2004) .Primary data will be collected using a semi-structured questionnaire (Appendix 1). The questionnaire was divided into three sections to establish the borrowers' profile, the nature of unsecured loans accessed by borrowers from commercial banks and the implications of borrowing unsecured loans on their household welfare. The questionnaires were administered to teachers within their schools.

3.6 Data Analysis

Descriptive statistics and Regression model was used in the analysis of the data. descriptive statistical method will be used to explain the socio- economic characteristics of the households. This will involve the use of frequencies, tables and percentages. The regression model measured the effect of having taken a personal on household welfare

indicators. The basis of this regression model was to determine the effect of unit increase in each welfare indicator on the household welfare of Secondary school teachers

The model is expressed as;

$$Y = a + b_1x_1 + b_2x_2 + b_3x_3 + b_4x_4 + b_5x_5 + b_6x_6 + b_7x_7 + \epsilon_i$$

Y = Household welfare; a = y intercept when x is at zero value; b₁, b₂, b₃, b₄, b₅, b₆ and b₇ are the weights associated with the independent variables; x₁ = Total monthly household income which will be measured by evaluating income before and after utilization of unsecured personal loans; x₂ = Women empowerment which will be measured by ability of female secondary school teachers to earn extra income and provide for their families; x₃ = improved education and healthcare which will be measured by the ability to access better healthcare and education before and after use of unsecured personal loan; x₄ = Poverty reduction which will be measured by improvement in general living standards after use of unsecured personal loan; x₅ = No of Small business started to be measured by the number of business startups before and after use of unsecured personal loans ; x₆ = Total consumption which will be measured by evaluating the total household consumption as a result of unsecured personal loans; x₇ = Improved housing which will be measured by better housing standards after use of unsecured personal loans and ϵ_i = Error term. From the regression model the household welfare was measured by observing the effect of a unit increase on the independent variables on the household welfare factor.

The significance of the above regression model will be tested using the R² value. A higher percentage will mean that indicate that the coefficients explain well the dependent variable while a low percentage will be the reverse. In this case therefore an R² value of

more than 60% will be significant to explain the dependent variable. In order to operationalize the variables, the researcher will regress the dependent variable (Responses on whether secondary school teachers had taken loans) against the above independent variables.

The instrument will be tested to verify that it measures what it is supposed to. The self-administered questionnaire shall be validated using the content validity by analyzing critically items in the questionnaire.

CHAPTER FOUR: DATA ANALYSIS RESULTS AND DISCUSSION

4.1 Introduction

This chapter presents findings of this research work. Data was collected using a semi structured questionnaire administered to secondary school teachers who had accessed unsecured personal loans. The objective of this study was to establish the effect of unsecured personal loans on household welfare on secondary school teachers in Bungoma County, Kenya. Data is presented in tables. A total of 180 questionnaires were issued equally to nine districts in Bungoma County for the research. Data was collected successfully from 122 respondents out of a sample size of 180 secondary school teachers while the remaining 58 questionnaires were returned either with no responses or incomplete responses hence were excluded from further analysis. This represented 67% response rate which was sufficient for this study.

4.2 Demographic Information

The research sought the general information of the respondents such as gender, age and period worked with the TSC.

4.2.1 Gender of Respondents

The study established that most of the respondents were females represented by 57.4 percent. Male respondents constituted 42.6 percent. This is an indication that women are making use of unsecured personal loans more than men as indicated in table 4.2.1 below

Table 4.2.1 Gender of respondents

Age Bracket	Frequency	Percentage	Cumulative %
Male	52	42.6	42.6
Female	70	57.4	100
TOTAL	122		

Source- Research Data, 2013

4.2.2 Age of Respondents

Age distribution of respondents was also of an interest to the researcher. Majority of the respondents were aged between 31-40 years since this is the most productive age hence most teachers accessed unsecured loans from this age group. The young generation of teachers aged between 18-30 years does not appreciate loans as indicated by table 4.2.2 below

Table 4.2.2 Age Bracket of Respondents

Age Bracket	Frequency	Percentage	Cumulative %
18-30 years	21	17	17
31-40 years	61	50	67
41-50 years	40	33	100
TOTAL	122	100	

Source: Research Data, 2013

4.2.3 Period Worked with TSC

When asked about the number of years respondents had been with the TSC, Majority of the respondents (70%) had worked with the TSC for over 10 years while newly employed

teachers accounted for 10% of the respondents as shown by table 4.3. This shows that teachers who had worked with the TSC for less than 5 years shunned unsecured personal loans.

Table 4.2.3 Number of years worked with TSC

Number of Years	Frequency	Percentage	Cumulative %
Below 5 years	12	10	10
6-10 years	25	20	30
Over 10 years	85	70	100
TOTAL	122	100	

Source: Research Data, 2013

4.3 Nature of Unsecured Personal Loans Offered by Commercial Banks

The researcher sought to establish characteristics of unsecured personal loans accessed by the respondents. The details sought included the source of the loan, loan purpose, preferred repayment period and factors that affect the teachers' decision to borrow unsecured personal loans.

4.3.1 Access to Unsecured Personal Loan

As to whether respondents had taken unsecured personal loans, the study established that all respondents had access to unsecured personal loans. This shows that most secondary school teachers have access to unsecured personal loans as shown by table 4.3.1 below

Table 4.3.1 Access to Unsecured Personal Loans

Access to Unsecured Personal Loan	Frequency	Percentage	Cumulative %
Yes	122	100	100
No	0	0	0

Source: Research Data, 2013

4.3.2 Source of Unsecured Personal Loan

When asked about the source of unsecured personal loan borrowing, most teachers preferred borrowing from Commercial banks at 75%, SACCOs accounted for 15% while MFIs accounted for 10% as illustrated by table 4.4.

Table 4.3.2 Source of Unsecured Personal loan

Source of Loan	Frequency	Percentage	Cumulative %
Commercial Banks	92	75	75
MFIs	12	10	85
SACCOs	18	15	100
TOTAL	122	100	

Source: Research Data, 2013

4.3.3 Purpose of Unsecured Personal Loan

The study also sought to establish how respondents utilized the unsecured personal loans. It was determined that most respondents (55%) used their loans for home improvement while the least proportion of respondents (2%) borrowed to clear other loans to improve their net pay as illustrated in table 4.3.2.

Table 4.3.3 Use of Unsecured Personal Loans

Number of Years	Frequency	Percentage	Cumulative %
Home Improvement	67	55	55
Education	37	30	85
To provide Capital	12	10	95
To Pay Medical Bills	4	3	98
To Clear Other Loans	2	2	100
TOTAL	122		

Source: Research Data, 2013

4.3.4 Unsecured Personal Loan Repayment Period

When asked about the preferred repayment period, most respondents (63.1%) preferred repaying their loan over a longer period of 49-72 months. This is because the repayment per month is lower over a longer duration.

Table 4.3.4 Unsecured Personal loan Repayment Period

Number of Years	Frequency	Percentage	Cumulative Percentage
12-36 months	15	12.3	12.3
37-48 months	30	24.6	36.9
49-72 months	77	63.1	100
Total	122		

Source: Research Data, 2013

4.3.5 Factors Affecting Teacher’s Decision to Borrow Unsecured Personal Loans

The study also sought to determine the level at which respondents considered the above conditions before applying for unsecured personal loans, from the findings the study established that majority of the respondents considered the following important, conditions and procedures as shown by mean of 1.74, the net pay and ability to pay as shown by mean of 1.78, level of interest as shown by mean of 1.80, ease of access to top up loan as shown by mean of 1.89, and finally the time taken before approval as shown by a mean of 1.92 as illustrated by table 4.7. All the cases were supported by low mean which implies that respondents were of similar opinion.

Table 4.3.5 Factors Affecting Teachers’ Decision to Borrow Unsecured Personal loan

Factor	Very Important	Important	Moderately important	Less important	Not at all	Mean	Std deviation
Level of interest	34	78	10	0	0	1.80	0.27
Ease of access to top up loan	33	69	20	0	0	1.89	0.23
Conditions and procedures	37	80	5	0	0	1.74	0.28
Time taken before approval	30	72	20	0	0	1.92	0.24
Your net pay and ability to pay	36	77	9	0	0	1.78	0.27

Source: Research Data, 2013

4.4 Effect of Unsecured Personal Loans on Household Welfare

The study sought to determine the level at which respondents agreed or disagreed with the statements which relate on unsecured personal loans contribution to household welfare, from the finding the study established that majority of the respondents agreed that; Female secondary school teachers are economically empowered as a result of accessing personal loans as shown by mean of 1.70, respondents further agreed that their household has been able to accessed improved healthcare and higher education as a result of a personal loans as shown by a mean of 1.73, Unsecured personal loans provides startup capital enabling families to earn extra income, Personal loans have enabled secondary school teachers put up better houses than before, the level of poverty in majority of respondents households had reduced significantly due access to personal loan, as shown by mean of 1.75 in each case, Total household consumption has improved because of personal loans as shown by mean of 1.80, Personal loans have enabled households start new business to create employment and earn extra income for family members as shown by a mean of 1.82 . All the cases were supported by a low mean which implies that respondents were of similar opinion.

Table 4.4.1 Statements relating to unsecured personal loans and their contribution to household welfare

Relationship	Strongly agree	Agree	Neutral	Disagree	Strongly disagree	Mean	Std deviation
Improved healthcare and better education	46	68	4	3	1	1.73	0.25
Female secondary school teachers are economically empowered	41	76	5	0	0	1.70	0.28
Poverty Reduction	46	68	2	5	1	1.75	0.25
Extra Income and Employment	41	72	2	4	3	1.82	0.26
Improved Household Consumption	42	72	1	5	2	1.80	0.26
Provision of startup capital for small business	40	76	3	2	1	1.75	0.27
Development of better housing	44	70	4	2	2	1.75	0.26

Source: Research Data, 2013

4.5 Regression Analysis

In this study, a multiple regression analysis was conducted to test the influence among predictor variables. The research used statistical package for social sciences (SPSS V 20) to code, enter and compute the measurements of the multiple regressions

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.691(a)	.653	.645	.19440

Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable, from the findings in the above table the value of adjusted R squared was 0.645 an indication that there was variation of 64.5% on household welfare due to changes in total monthly household income, women empowerment, improved education and healthcare, poverty reduction, no of small business started and total consumption and improved housing at 95% confidence interval . This shows that 64.5% changes in household welfare could be accounted for by total monthly household income, women empowerment, improved education and healthcare, poverty reduction, no of small business started and total consumption and improved housing . R is the correlation coefficient which shows the relationship between the study variables, from the findings shown in the table above there was a strong positive relationship between the study variables as shown by 0.691.

Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	Constant	.298	.453		2.165	.006
	Total monthly household income	.237	.160	.198	1.479	.012
	Women empowerment	.231	.126	.245	1.834	.001
	improved education and healthcare	.239	.145	.008	.065	.023
	Poverty reduction	.281	.114	.031	.246	.016
	No of Small business started	.138	.072	-.290	-1.931	.032
	Total consumption	-.131	.064	-.264	-2.050	.048
	Improved housing	.093	.060	-.184	-1.546	.031

From the data in the above table the established regression equation was

$$Y = 0.298 + 0.237 X_1 + 0.231 X_2 + 0.239 X_3 + 0.281 X_4 + 0.138X_5 - 0.131 X_6 + 0.098 X_7$$

From the above regression equation it was revealed that holding total monthly household income, women empowerment, improved education and healthcare, poverty reduction, no of small business started and total consumption and improved housing to a constant zero, household welfare would be at 0.298, a unit increase in total monthly household income would lead to increase in the household welfare by a factor of 0.237, unit increase in women empowerment would lead to increase in house welfare by factor of

0.231, a unit increase in improved education and healthcare would lead to increase in household welfare by a factor of 0.239, unit increase in poverty reduction would lead to increase in household welfare by a factor of 0.281, unit increase in number of small business started would lead to increase in household welfare by factors of 0.138, a unit increase in total consumption would lead to decrease in household welfare by a factor of 0.239, unit increase in improved housing would lead to increase in household welfare by a factor of 0.281.

4.6 Discussion

Just like this research, previous studies have shown strong relationships between access to Credit especially micro finance loans and improved Household welfare. For instance Omwange, Omoro (2013), in their study on Utilization of Micro Finance Loans in Emerging Markets in Bungoma County, Kenya established that there is a strong relationship between micro finance loans and Household Welfare. However, their study involved a sample size of 62 respondents who had been advanced and were still servicing micro finance loans since 2009 across the urban centers of Bungoma County. Just like in this study, they used Regression Analysis to determine the relationship between microfinance loans and Household Welfare in Bungoma County

CHAPTER FIVE: SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATION

5.1 Introduction

This chapter provides a summary of the key findings from the research data, conclusions made with reference to the effect of unsecured personal loans on the house hold welfare of secondary school teachers in Bungoma County, a highlight of the major limitations during research and suggestions for further research concerning the subject.

5.2 Summary of the Findings

The study established that most of teachers who had taken unsecured personal loans were women. Majority of those who had taken unsecured personal loans were found to be between the ages of 31-40 years. This is the age at which most people are active and involved in activities to make their financial status stable in future. It was also determined that most teachers preferred borrowing from commercial banks as opposed to SACCOs and MFIs. This is because of the low interest charged by commercial banks, flexible repayment period and ease of accessibility for top up loans as compared to SACCOs and MFIs. Most teachers borrowed unsecure personal loans to improve their homes and educate their family members. It is evident that home improvement and education were prioritized by borrowers as compared to provision of capital, medical bill payment or offsetting other loans. The study also established that most respondents preferred repaying their loans over longer periods to ease the burden on their salary.

The study found out that respondents regarded interest rates, ease of access to top up, conditions and procedures, time taken before approval and their net pay and ability to repay the loan as important factors influencing their decisions to access unsecured personal loans. The study further established that unsecured personal loans had positive effect on the household welfare indicators. It was determined that access to improved health care and better education, Women empowered, Extra Income, Small business startups, Poverty reduction and better housing among Secondary school teachers in Bungoma County were as a result of access to unsecured personal loans.

From the regression analysis carried out with household welfare as the dependent variable and household welfare indicators of unsecured personal loans has improved healthcare and better education, Unsecured personal loans has led to female teachers empowerment, Unsecured personal loans has reduced poverty of Secondary school teachers, Unsecured personal loans has led to new business start ups and extra income for households, Unsecured personal loans has increased total household consumption, Unsecured personal loans have enabled Secondary school teachers put up better housing and Unsecured personal loans have reduced poverty levels for secondary school teachers as the independent variables, it was found out that there was a strong relationship between the independent and the dependent variables. The model $Y = 0.298 + 0.237 X_1 + 0.231 X_2 + 0.239 X_3 + 0.281 X_4 + 0.138X_5 - 0.131 X_6 + 0.098 X_7$ therefore adequately explains the effect of unsecured personal loans on household welfare in Bungoma County.

5.3 Conclusions

Access and utilization of unsecured personal loans by secondary school teachers in Bungoma County has various positive effects on the welfare of households. Access and use of unsecured personal loans led to improved healthcare and better education, female teacher's empowerment, poverty levels reduction, new business start ups, improved total household consumption, provision of startup capital for new businesses and development of better housing by Secondary school teachers. Unsecured personal loans have a strong positive effect on household welfare of Secondary school teachers in Bungoma County.

There exists a strong positive relationship between household welfare as the dependent variable on one hand and improved healthcare and better education, female teacher's empowerment, poverty levels reduction, new business start ups, improved total household consumption, provision of startup capital for new businesses and development of better housing as the independent variables on the other hand. This study therefore concludes that 64.5% of improvement in household welfare among Secondary school teachers in Bungoma County is accounted for by access and use of unsecured personal loans.

5.4 Recommendations

Since it is evident from this study that unsecured personal loans improve household welfare among Secondary school teachers in Bungoma County, the government should initiate monetary policies that will contribute to the lowering of the base lending rate to enhance accessibility to unsecured personal loans to increase economic development. Proper training and mentorship programs should be prioritized to encourage teachers who

fear taking up loans to embrace borrowing as a means of accessing capital for household development.

5.5 Limitation

The extent of this study and its findings are limited to Bungoma County alone out of the 47 counties in Kenya. The research findings may differ when a similar study is carried out in other Counties across Kenya. This study was limited by time to administer and collect questionnaires since the research involved personal delivery of questionnaires to the respondents followed by personal explanations and clarifications. Accessing respondents was also difficult since most of them were busy currying out school work hence out of the 180 questionnaires administered, only 122 were successfully completed. The rest were either incomplete or not returned at all.

5.6 Suggestions for Further Study

From the regression analysis results, there is a variance of 33.7 on household welfare that is not explained by the independent variables in this study. It is prudent that further research be undertaken to determine other factors that affect household welfare other than unsecured personal loans. A comparative study should also be carried out in other counties to determine the extent of use of unsecured personal loans by secondary school teachers in other counties and reveal the similarities and differences that exist as far as household welfare of Secondary school teachers is concerned.

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APPENDICES

Appendix 1: RESEARCH QUESTIONNAIRE:

PART A: Respondent's Profile

1. Name your district

.....

2. Gender

- Male Female

3. Age

- a) 18-30 years
- b) 31-40 years
- c) 41- 50 years

4. How long have you worked with the TSC

- Below 5 years
- 6-10 years
- Above 10 years

PART B: Nature of Unsecured Personal Loans Offered By Commercial Banks

5. Have you ever taken unsecured personal loan?

Yes No

6. Where did you access the Unsecured Personal Loan?

- Commercial Bank
- SACCO
- Micro Finance Co

7. For what purpose did you take unsecured personal loan

- Education
- Home Improvement
- To provide capital
- To pay medical bills
- To clear other loans

8. How long is the repayment period

- 12-36 months
- 37-48 months
- 49-72 months

9. How do the following factors affect your decision to borrow unsecured personal loan

	Very important	Important	Less important
• Level of interest rate	[]	[]	[]
• Ease of access to top up loan	[]	[]	[]
• Conditions and procedures	[]	[]	[]
• Time taken before approval	[]	[]	[]
• Your net pay and ability to pay	[]	[]	[]

PART C: Effect of Unsecured Personal Loans on Household Welfare of Secondary school teachers in Bungoma County- Kenya

Kindly rate the following statements according to the unsecured personal loans contribution to household welfare

NO.	Relationship	Strongly agree	Agree	Neutral	Disagree	Strongly disagree
1	Your household has accessed improved healthcare and better education as a result of a personal loan					
2	Female secondary school teachers are economically					

	empowered as a result of accessing personal loans					
3	The level of poverty in your household has reduced because of access to a personal loan					
4	Personal loans earn extra income and create employment for family members					
5	Total household consumption has improved because of personal loans					
6	Unsecured personal loans provide startup capital enabling families to earn extra income					
7	Personal loans have enabled secondary school teachers put up better houses than before.					