

Loan Repayment and Financial Performance of Deposit Taking Savings and Credit Cooperative Societies in Embu County, Kenya

Regina Katula¹ and Dr Stephen Kiriinya²

Correspondent Author, School of Business, Kenyatta University, Kenya¹

Lecturer at Department of Finance and Accounting, School of Business, Kenyatta University, Kenya²

ABSTRACT

Meagre earnings by SACCO'S operating in Kenya has been attributed to challenges of embracing appropriate loan repayment strategies. Though limited studies have been conducted in Kenya to establish the link between loan repayment and financial performance, it is observed that there is no clear understanding on the link between loan repayment and financial performance of SACCO'S operating in Embu County, Kenya thus formed the basis of the study. The study sought to investigate loan repayment and financial performance of SACCO'S in Embu County, Kenya. The specific objectives included; loan appraisal, loan interest rates, loan follow-up procedures and customer characteristics on performance of SACCO'S in Embu County, Kenya. The study employed descriptive research design and targeted a total population of 250 respondents selected from of 10 SACCO'S operating in Embu County, Kenya. Out of the 250 respondents, Slovin's formula was adopted to select 158 respondents to be the sample size of the study. The study used primary and secondary data. Primary data was collected using questionnaires through drop and pick later method. Secondary data was gathered by a review of existing materials that included financial statements and related empirical studies. The content validity was determined by lecturers that were drawn from department of Accounting and Finance of Kenyatta University and industry experts who were draws from SACCO's. Reliability of the study was tested using Cronbach Alpha method and values of all the four variables of the study were more than the cut-off point of 0.7 thus were reliable for the study. Statistical Packages for Social Sciences (SPSS) version 24 was applied to analyse quantitative data using descriptive statistics such as mean scores, percentages and standard deviation. Multiple regression was conducted at 95% confidence level and 5% significance level to establish the statistical significance between variables of the study. The findings of the study were presented using tables and graphs. Data analysed revealed that there exist a statistical significant relationship between independent variables (loan appraisal, loan interest rates, loan follow-up procedures and customer characteristics) and dependent variable (financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya). The study concludes that unless SACCO's embrace models of minimizing financial risks such as loan appraisal, loan interest rates, loan follow-up procedures and customer characteristics models, achieving financial performance will be an uphill task. The study recommends that SACCO's not only need to focus on non-performing loans but also seek to understand and review loan policies to encourage repayment within the stipulated timeframe.

Key Words: *Loan Repayment, Financial Performance, Deposit Taking Savings and Credit Cooperative Societies, SACCOs, Embu County, Kenya*

1. INTRODUCTION

According to the 2014 International Co-operative Alliance's World Cooperative Monitor, the turnover of the largest 300 cooperatives in the world grew by 11.6% to reach \$2.2 trillion in 2012, equivalent to the gross domestic product (GDP) of Brazil (Kiptoo, 2015). The overall turnover of nearly 2,000 cooperatives in the 65 countries surveyed by the Monitor totals \$2.6 billion. The World Council of Credit Unions (WOCCU) statistical report for 2014, recorded a total of 57,000 Credit Unions (SACCO'S), spread across 105 countries and 6 continents. The world's Credit Union system has a combined savings of \$ 1.5 trillion (US dollars), and an asset base of \$ 1.8 trillion (US dollars) out of which \$ 1.2 trillion (US dollars) constituted the loan portfolio. The average worldwide penetration rate of the Credit Union system stood at 8.2 percent (Kimenchu, 2014). In addressing challenges of deteriorating financial performance among SACCO'S operating in developing countries and more specifically in Kenya, SACCO'S are embarking on embracing strategies such as loan appraisal, interest on loans, loan follow-up procedures and customer characteristics in order to enhance their financial competitiveness (SASRA, 2013). Loan appraisal interventions that may help SACCO'S minimize cases of non-performing loans involves financial systems in place, internal procedures followed before approving loans, and assessment of business opportunities before loan approval (Mungai, Maingi, Muathe, 2014).

Further, loan repayment period, interest earned and interest rate regulations to a larger extent can direct or indirect roles in financial performance of SACCO'S in Kenya (Warue, 2012). By extension, loan follow-up procedures such as knowledge of staff, policies and credit history of borrowers can influence financial performance of SACCO'S. Similarly, customer characteristics such as income levels, age, collaterals and credit history can facilitate financial performance of SACCO'S from context to context (Laga, 2011). Chen and Pan (2012) acknowledge that Sacco's have remained to drivers of economic, social and environmental sustainability; the business model preferred by people; and the fastest growing form of enterprise by Year 2020. According to Cobia (2008), cooperative efforts have occurred throughout history. Since the early days, man cooperated with others to help kill large animals for survival and so as to achieve the objectives that they could not reach if they acted individually. Cooperation has occurred throughout the world. Ancient records show that the Babylonians practiced cooperative farming and that the Chinese developed savings and loan associations similar to those in use today (Baliwen, 2012). In North America, clearing land in preparation for the planting of crops, threshing beans, and barn raisings all required cooperative efforts. In the United States, the first formal co-operative business is assumed to have been established in 1752, almost a quarter-century before the Declaration of Independence was signed (Central Bank of Kenya, 2015).

In today's society, cooperative financial institutions hold a considerable market share, with the IMF estimates that across all banking sector assets in developing countries, the market share of co-operative finance was equivalent to 14 percent in 2004 (Hesse & Cihak, 2007). Previous research on cooperative finance during crisis indicates that they tended to fare better than investor-owned savings and loans institutions, as they pursue more conservative investment policies (Chaddad & Cook, 2004). For instance, analysis from the IMF indicates that co-operative banks in developed countries tend to be more stable than commercial banks, especially during financial crisis, as their investment patterns tend to be less speculative and returns are therefore less volatile. According to Central Bank of Kenya (2015) SACCO'S in Kenya have

mobilized over Kshs. 200 billion in savings, accounting for over 30% to National Domestic Saving (Co-operative Bank of Kenya, 2010). Liquidity risk is a failure of SACCO'S to honor approved loans due to inadequacy of loanable funds (Fiedler, Brown, & Moloney, 2002). Over the last decade, SACCO societies have significantly increased to account for 50% of the registered Co-operatives. Kenya's national development blueprint, the Vision 2030 recognizes SACCO societies as important players in deepening financial access to mobilize savings for investments in enterprises and personal development.

SASRA (2013) concurs that liquidity risk needs to be monitored as part of an integrated institution wide risk management process taking into account market and credit risk to ensure stability and improvement of loan portfolio in the balance sheet. This helps a SACCO to identify its future funding requirements and any potential risks (Fiedler, Brown, & Moloney, 2002). Failure or poor management of liquidity risk and credit risk affect the quality of loan portfolio and SACCO'S that have managed liquidity risk and credit risk adequately their loan portfolio quality and performance is sound and healthy and vice versa. Baliwen (2012) avers that with the population of Kenya at 40 million it is estimated that 63% of Kenyans participate directly or indirectly in cooperative development enterprises. Kimenchu (2014) observed that Kenya has the largest SACCO movement in Africa with a total membership of 8 million followed by Senegal at 5 million. To date there are over 11,200 registered SACCO'S in the country, with a membership of 8 million Kenyans having mobilized domestic savings estimated at over \$ 2.5 Billion. Of which 5,000 are SACCO'S and 230 have Front Office Service Activities (FOSAs). The SACCO sector has mobilized over Kshs 200 billion in savings which is about 30% of the national savings. Kenya accounts for 70% of Africa's continental portfolio hence being ranked 7th worldwide. Kenya sits in the group ten largest co-operative movements (G10) member countries (SACCO Congress, 2010). However even with these developments they still don't meet the demands for the loan applications.

Muthoni (2011) observed that members are not satisfied with the shorter repayment period, and that pegging loan on deposits was denying member's money which they had ability to pay. The Kenya Union of Savings and Credit Cooperative reported that the consequences of the global financial crisis have led to reduced growth savings: 7.6 per cent growth in savings in 2008 compared to 31.2 per cent in 2007 (WOCCU, 2009). It was reported in interviews that SACCO'S in Kenya have reported increase in demand for loans, but have exercised caution in responding to requests (Nguta & Guyo, 2013). The World Council of Credit Unions (WOCCU) estimates that the Kenyan SACCO sector is the largest in Africa; in 2005, SACCO'S had an estimated membership of more than 2.5 million, share capital and deposits of US\$1.66 billion, and a loan portfolio of US\$1.24 billion (WOCCU, 2005). With over KES 230 Billion in assets and a savings portfolio estimated at KES 190 Billion, the SACCO movement in Kenya constitutes a significant proportion of about 20% of the country's savings. The Kenyan SACCO sector has been observed to contribute greatly to the total financial industry and consequently the economy. It contributes to over forty five percent of the nation's Gross Domestic Product (MOCD&M, 2010). With the enactment of the SACCO Act, 2008 (SSA) and the subsequent establishment of the SACCO Societies Regulatory Authority (SASRA), SACCO'S have been brought under regulation and supervision.

Further, the Vision 2030 strategy requires the financial services sector to play a critical role in mobilizing the savings and investments for development of the country by providing better

intermediate between savings and investments than at present. This sector will assist the mobilization of investment funds required to implement the projects of Vision 2030. SACCO'S are among the financial services strategies to be implemented in this exercise. Services provided by SACCO'S and other major financial institutions will play a crucial role in improving the reach and access of financial services (currently only 19% of Kenyans have access to formal financial services). Organization performance can be measured from financial and non-financial. Parameter of non-financial performance can range from customer satisfaction, new product development, increased market share, employee motivation while financial performance parameters can range from profits, liquidity, return on investment, costs of operation among others (Betru, 2010). Nkuru (2015) also defines performance measurement as a way of ensuring that resources available are used in the most efficient and effective way. The essence is to provide for the organization the maximum return on the capital employed in the business.

Performance of SACCO'S is very important because managers need to know how well the SACCO'S are performing. There are two major reasons as to why SACCO'S should have financial performance measurement (Johnson & Mark, 1997). The first one is to produce financial statements at the right time. Secondly, financial statements should be analyzed to produce information about the performance of the scheme, which must be used to improve that performance. Based on WOCCU's standards of measuring performance, the factors which determine the performance of SACCO'S include; asset base, Liabilities, Performance of the loan book, corporate governance and the quality of staff and regulations in the industry. According to SASRA, the SACCO'S society regulations are meant to improve the competitiveness of SACCO by setting financial and operating standards commensurate to the deposit taking business conducted by SACCO'S. This is ultimately expected to drive efficiency and improve the level of savings in the SACCO'S societies as envisaged in the financial sector strategy in vision 2030. SACCO'S Regulations and performance relate in that the regulations are meant to set specific requirements on the tools used to measure performance (PEARLS) leading to a direct relationship (Financial Sector Deepening, 2009).

While there have been several reform initiatives in SACCO'S subsector in the past, the introduction of a SACCO'S specific law is recognition of the unique financial intermediation function that SACCO'S play in an economy. Thus the operational regulations and performance standards are specific and prescriptive; not to make SACCO'S non-competitive and stifle their growth but to ensure that they operate and grow within a framework that promotes sound financial and business management practices (Mungai, Maini & Muathe, 2014). Munyi (2006) argues that financial performance of SACCO'S has continued to be measured through non-conventional models such as social/cultural changes on members and extent of financial outreach. Through government intervention by legislation, SACCO'S have become more structured and hence adoption of more conventional ways of measuring their performance such as profitability, Return on Assets and Return on Equity. It's from this development that SACCO'S have attracted more members and lenders who invest with expectation of good return on their investments. Loan repayments poses the greatest risk to stability of the multi-billion shilling Savings and Credit Co-operative (SACCO'S) movement (Campion, 2002). Financial sector regulators have warned SACCOS to be more cautious while advancing loans to their clients to avoid the loan defaulting (Nicholas, 2010). Omondi (2008) argues that default occurs when a debtor has not met his or her legal obligations according to the debt contract. Default

may occur if the debtor is either unwilling or unable to pay his or her debt. This can occur with all debt obligations including bonds, mortgages, loans, and promissory notes (Derban, 2005). Defaulting on debt obligation can place a company or an individual in financial trouble. The lender will see a default as a sign that the borrower is not likely to repay the loan and the interest. Loan default is the failure to pay back a loan which may occur if the debtor is either unwilling or unable to pay his/her debt. A defaulted loan is a cost to SACCO'S in terms of forgone or delayed interest, high recovery cost and finance cost associated with external borrowing (Baliwen, 2012).

SACCO societies in Kenya were established in Africa in (1931). The major objective was to improve the social economic well-being of low income earners. The concept was first practices in developed countries where English was the native language. First countries in Africa that adopted the concept of SACCO'S were; Ghana, Uganda, Nigeria, Tanzania and Kenya. Most non-English speaking nations in Africa appreciated SACCO'S much later. In Kenya, the first co-operative society was Lumbwa co-operative Society formed in 1908 by the European Farmers with the aim of supporting agricultural activities and products to take advantage of economies of scale (Kenya Union of Savings and Credit Co-operatives, 2014). SASRA (2015) revealed that after independence, the Kenyan government recognized co-operatives as suitable for achieving economic development of the nation. Necessary steps were then taken by the government which saw the rapid expansion and growth of SACCO society movement in the country. The SACCO sub-sector is part of the larger co-operative movement in Kenya that has contributed greatly on social economic developments. The major categories of co-operatives operating in Kenya include: Financial co-operatives (Savings & Credit co-operatives societies – SACCO'S) and Non-financial co-operatives (includes farm produce and other commodities marketing co-operative, housing, transport and investments co-operative). In the recent past, SACCO'S have witnessed faster growth than other co-operatives. And the establishment of SACCO societies Act 2008 places regulation under the armpit of SACCO regulatory Authority (SASRA). The new legal framework has been introduced to guide the growth and development of SACCO'S (KUSCCO, 2014).

2. STATEMENT OF THE PROBLEM

Mungai, Maingi, Muathe (2014) established that loan repayment and sustainability of Government funded micro-credit was determined by regular income streams among rural borrowers. Furthermore, their study revealed that system development to minimize uncertainties was one of the approaches that enhanced loan repayment among rural borrowers. However, it was noted that their study was confined to Government funded micro-credit but not deposit taking SACCO's in Embu County. SACCO'S are ultimately expected to drive efficiency and improve the level of savings among the Kenyan citizens as envisaged in the financial sector strategy in vision 2030 (KUSCCO, 2009). Kenya has continued to record a significant improvement in social economic development as through initiatives stipulated in Kenya's vision 2030. SACCO'S have greatly contributed to the social economic developments in Kenya ranging from empowerment of entrepreneurs thus economic growth. Nguta and Guyo (2013) acknowledge that despite the concept that SACCO'S contribute to social economic developments in both developed and developing countries of the world, SACCO'S operating in developing countries and more especially in Kenya have continued experiencing deteriorating financial performance due to issues of loan repayment. A survey conducted by SASRA (2015) further revealed that SACCO'S in Kenya were underperforming due to issues of technology,

competition, change of regulations and management issues. However, it was noted that the findings of the study were confined to different variables which included regulations, credit risk and credit policies but failed to address the variables of this study. Majority (75%) of the SACCO'S in Kenya are facing stiff competition from commercial banks and microfinance institutions (Nkuru, 2015). On the other hand it was noted that non-performance of loans were some of the aspects that contributed to deteriorating financial performance of SACCO'S in Kenya. However, it was noted that the study was limited to SACCO'S within the agricultural sector in Meru County, Kenya. Another survey conducted by KUSCCO (2009) established that loan repayment has been a key challenge of SACCO'S operating in developing countries and more especially in Kenya. It was observed that issues of corporate governance and credit risk management are directly associated with non-performance of SACCO'S from the financial perspective. Further, it is noted that a number of stakeholders ranging from SASRA and shareholders have continued to raise concerns on the financial performance of the SACCO's.

Kimenchu (2014) noted that internal control practices like audit and corporate governance were associated with profitability of SACCO'S. However, it was observed that that study was confined to internal control practices like internal audit, communication and risk management. By extension, Sheila (2011) established that SACCO'S were more likely to perform well if they laid down risk management frameworks. However, it was observed that the study was limited to Sacco's in Uganda and sought to address different variables such as proactive internal audit and control. Furthermore, Nishimura, Kazuhito and Yukiko (2001) observed that loan appraisal procedures was a key factor of financial performance of SACCO's in Japan. However, from the findings of previous empirical studies, it was noted that conceptual, contextual gaps were evident and none of the studies conducted specifically addressed the variables of this study. For instance, some studies conducted by Nguta & Guyo (2013); Sheila (2011); (Nkuru, 2015) & Kimenchu (2014) were confined different variables like regulations, applicant knowledge, economic trends and credit policies. Further, other studies conducted by Olomola (1999); Nishimura, Kazuhito & Yukiko (2001); Chen & Pan (2012) were confined to different countries such as Nigeria, Japan and Taiwan among others. Therefore, it is in this view that this study aimed to investigate effects of loan repayment and financial performance of deposit taking SACCO'S operating in Embu County, Kenya.

3. OBJECTIVES OF THE STUDY

The main objective of the study was to examine effects of loan repayment and financial performance of deposit taking savings and credit societies in Embu County, Kenya.

The specific objectives that guided the study were:

- i. To determine the influence of loan appraisal on financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya.
- ii. To find out the effects of interest rates on financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya.
- iv. To determine the influence of loan follow up procedures on financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya.
- v. To establish the influence of customer characteristics on financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya.

4. THEORETICAL REVIEW

The study was anchored on Financial Theory and supported by other two theories namely; Credit Risk Management Theory and Resource Dependency Theory.

4.1 Financial Theory

Financial Theory was established by Miller in the 20th century. It suggests that risk management can smooth variability in firm value (Chen & Pan, 2012)). Theory says that risks should be redistributed to those better equipped to handle them. Industrial companies are unlikely to have a comparative advantage in bearing foreign-exchange risk, interest-rate risk or commodity risk. We redistribute the risk by hedging: buying and selling derivatives. We decrease the variance of the expected value of the firm. This removes the tails of the distribution. Cole (2000) identifies three major costs associated with higher variability in cash flow: higher expected bankruptcy costs, higher expected payments to stakeholders and higher expected tax payments. Firms can enhance their performance through diversification, new product development and market expansion. Al-Saleh and Al-Kandari (2012) argue that if risk management can enhance financial performance of the firm and shareholder value. Financial risks associated with non-performing loans among SACCO'S can be directly linked to system weaknesses and inappropriate corporate governance. As for tax payments, risk management works in the simple way as to manage taxable income so to ensure that the largest possible proportion of corporate income falls within the optimal period in the business cycle. The applicability of this theory in this study is based on the notion that SACCOS are likely to maximize their revenue based on the criteria they adopt to appraise loans, the ability to assess economic trends in terms of interest rates and techniques employed to follow- up loans.

By extension, Bhunia and Sarkar (2011) argues that concepts of finance theory have evolved over time to behavioural finance which is an emerging area of that intend to study the irrational behaviour of the investors in a given business environment. The behavioural finance discipline closely combines individual behaviour and market phenomena and uses the knowledge taken from both the psychological field and financial theory. It attempts to identify the behavioural biases commonly exhibited by investors and also provides strategies to overcome them. The theory suggest that always consumers tend to be rational in making financial decisions. For instance, loan applicants of SACCO'S are more sensitive with interest charged on loans applied and policies of engagement. SACCO'S on the other hand they have to minimize their financial risks by establishing appropriate loan follow-up procedures or models in the long run. Furthermore, to minimize chances of financial risk, SACCO's can train their credit management staff on new approaches of loan recovery compared to traditional approaches that are inefficient and ineffective. Balcaen and Ooghe (2004) argue that financial institutions ranging from SACCO'S MFI's and commercial Banks are shifting to behavioural finance which seeks to supplement the modern theories of finance by introducing behavioral aspects to the decision making process. It focuses on the application of psychological and economic principles for the improvement of financial decision-making (Barr, 2004). In addition, a number of acknowledged scholars like Aasen (2011) argues that market anomalies that cannot be explained with the help of standard financial theory, such as abnormal price movement in connection with IPOs, mergers and stock splits, can be resolved by using underlying principles of rational behaviour that are dependent on efficient market hypothesis. Consequently, human decisions are subject to several cognitive illusions which can range from income, age, attitude and peer influence. The human

illusions can be illusions identified within the prospect theory, and the illusions identified within the heuristic decision process.

4.2 Credit Risk Management Theory

Risk management theory by Moody (2003) involves the process that a bank puts in place to control its financial exposures to risk. Credit is the provision of goods and services to a person or entity on agreed terms and conditions where the payments are to be made later with or without interest. During the contract period, not all debtors will repay their dues as and when they fall due. When the debtor does not pay their dues on the due date, the lender is exposed to credit risks which may in turn lead to default. Credit risk is therefore the investor's risk of loss, financial or otherwise, arising from a borrower who does not pay his or her dues as agreed in the contractual terms (Robichech, 2001). Balcaen and Ooghe (2004) suggests that the process of risk management comprises the fundamental steps of risk identification, risk analysis and assessment, risk audit monitoring, and risk treatment or control. Whereas a risk in simple terms can be measured using standard deviation, some risks may be difficult to measure requiring more complex methods of risk measurement. Good risk management is not only a defensive mechanism, but also an offensive weapon for commercial banks and this is heavily dependent on the quality of leadership and governance. Huang (2001) argues that a Sacco exists not only to accept deposits but also to grant credit facilities, therefore inevitably exposed to credit risk. Credit risk is by far the most significant risk faced by banks and the success of their business depends on accurate measurement and efficient management of this risk to a greater extent than any other risks.

According to Chen and Pan (2012), credit risk is the degree of value fluctuations in debt instruments and derivatives due to changes in the underlying credit quality of borrowers and counter parties. Pandey (2004) regard credit risk as losses from the refusal or inability of credit customers to pay what is owed in full and on time. Credit risk is the exposure faced by banks when a borrower (customer) defaults in honouring debt obligations on due date or at maturity. This risk interchangeably called 'counterparty risk' is capable of putting the bank in distress if not adequately managed. Credit risk management maximizes bank's risk adjusted rate of return by maintaining credit risk exposure within acceptable limit in order to provide framework for understanding the impact of credit risk management on banks' profitability (Armstrong, 2007). Al-Tamimi (2002) opined that credit risk management is in two-fold which includes, the realization that after losses have occurred, the losses becomes unbearable and the developments in the field of financing commercial paper, securitization, and other non-bank competition which pushed banks to find viable loan borrowers. The main source of credit risk include, limited institutional capacity, inappropriate credit policies, volatile interest rates, poor management, inappropriate laws, low capital and liquidity levels, direct lending, massive licensing of banks, poor loan underwriting, laxity in credit assessment, poor lending practices, government interference and inadequate supervision by the central bank.

An increase in bank credit risk gradually leads to liquidity and solvency problems. Credit risk may increase if the bank lends to borrowers it does not have adequate knowledge SACCO'S about (Santomero, 2007).The theory is applicable in this study based on the notion that SACCO'S are likely to minimize cases of loan default if they establish loan appraisal procedures and systems, evaluate customer characteristics like income levels and credit history. The ability of the SACCO to measure credit, market and operational risks can enhance financial

performance. The consistent assessment of the three types of risks is an essential prerequisite for successful risk management. While the development of concepts for the assessment of market risks has shown considerable progress, the methods to measure credit risks and operational risks are not as sophisticated yet due to the limited availability of historical data (Bhunja & Sarkar, 2011). Aasen (2011) argues that expected losses are derived from the borrower's expected probability of default and the predicted exposure at default less the recovery rate. The expected losses should be accounted for in income planning and included as standard risk costs in the credit conditions. Unexpected losses result from deviations in losses from the expected loss. Unexpected losses are taken into account only indirectly via equity cost in the course of income planning and setting of credit conditions. They have to be secured by the risk coverage. Risk monitoring is used to check whether the risks actually incurred lie within the prescribed limits, thus ensuring an institution's capacity to bear these risks. In addition, the effectiveness of the measures implemented in risk controlling is measured, and new impulses are generated if necessary (Al-Saleh & Al-Kandari, 2012).

4.3 Resource Dependency Theory

The study was established by Pfeffer and Salancik in (1978). Resource dependence theory has implications regarding the optimal divisional structure of organizations, recruitment of board members and employees, production strategies, contract structure, external organizational links, and many other aspects of organizational strategy (Robinson, 2001). Milligan (2002) argues that resource dependence concerns more than the external organizations that provide, distribute, finance, and compete with a firm. Although executive decisions have more individual weight than non-executive decisions, in aggregate the latter have greater organizational impact. Robichech (2001) suggests that managers throughout the organization understand their success is tied to customer demand. Managers' careers thrive when customer demand expands. Thus customers are the ultimate resource on which companies depend. Although this seems obvious in terms of revenue, it is actually organizational incentives that make management see customers as a resource. The theory concentrates on the role of board directors in providing access to resources needed by the firm. Pandey (2004) contends that resource dependency theory focuses on the role that directors play in providing or securing essential resources to an organization through their linkages to the external environment.

Indeed, Santomero (2007) concurs that resource dependency theorists provide focus on the appointment of representatives of independent organizations as a means for gaining access in resources critical to firm success. For example, outside directors who are partners to a law firm provide legal advice, either in board meetings or in private communication with the firm executives that may otherwise be more costly for the firm to secure. It has been argued that the provision of resources enhances organizational functioning, firm's performance and its survival (Sarker, 2005). Further, Trautmann (2006) argues that it is the responsibility of directors to bring resources to the firm, such as information, skills, access to key constituents such as suppliers, buyers, public policy makers, social groups as well as legitimacy. The relationship of the theory to this study is based on the assumption that SACCO'S are likely to perform in the changing business environment if they utilize their resources effectively. Effective and efficient internal control mechanisms will enhance transparency and accountability of resource allocation and utilization thus shareholder and investor confidence. Investment in a competent staff, modern

technologies and excellent customer service delivery will be based on how the firms prioritize on resource management to achieve improved productivity (Wright, 2002).

5. CONCEPTUAL FRAMEWORK

The conceptual framework illustrates the interrelationship between independent variables on the dependent variable. It was established that loan appraisal, interest on loans, customer characteristics and loan follow-up procedures had a significant effect on the performance of SACCO'S in Embu County, Kenya.

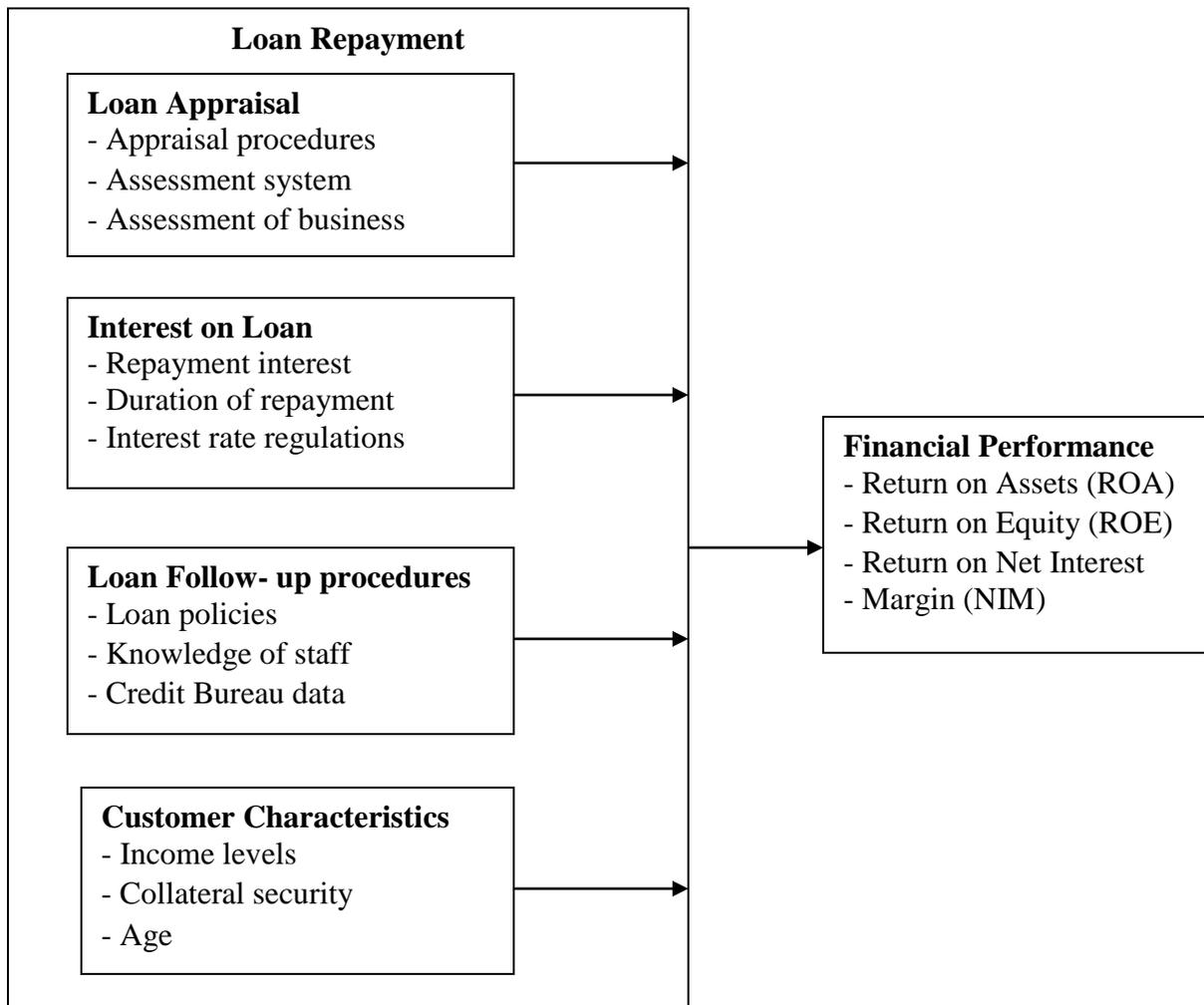


Figure 1: Conceptual Framework

As illustrated in Figure 1, it was fulfilled that that financial performance of SACCO'S in Embu County was influenced by loan appraisal aspects such as appraisal procedures, assessment system and assessment of business. Aspects of interest on loans like repayment interest duration and regulations also influenced financial performance of deposit taking SACCO'S in Kenya. On the other hand, loan follow-up procedures aspects such as loan policies, knowledge of staff and

credit bureau data influenced performance of SACCO'S. Finally, customer characteristic aspects such as income level, collateral security and credit history of the customer influenced performance of SACCO'S in Kenya. Furthermore, it was revealed that financial performance was measured using Return on Assets (ROA), Return on Equity (ROE) and Return on Net Interest Margin (NIM) parameters.

6. RESEARCH METHODOLOGY

The study employed descriptive research design. Further, descriptive research design was considered appropriate because it facilitates analysis and interpretation of data in a quantitative manner, provides the opportunity to discover new knowledge that leads to prediction and control of the problem under investigation and it provides the opportunity to test the association between variables of the study thus making conclusion and recommendation of the study in an objective manner rather than subjective approach which is biased. The study targeted all employees of the 09 deposit taking SACCO'S operating in Embu County in Kenya. Therefore, 250 respondents were the target population of the study. Purposive sampling was used to select the respondents for the study. The study adopted Slovin's formula to determine the sample size. The study relied on primary data which was collected through structured questionnaires containing both open ended and closed questions. The questionnaires were administered to respondents through drop and pick later method. The questionnaire was divided into six section which included the population demographic, loan appraisal, loan interest rates, loan follow-up procedures and customer characteristics and financial performance section. Data was analyzed using descriptive, correlation and regression analysis and presented in form of mean scores, standard deviations, percentages and frequency distribution. Multiple regression method was conducted to determine the relationship between variables at 95% confidence level and 5% significance level.

7. FINDINGS

7.1 Correlation Results

Pearson's product moment correlation analysis was conducted using Statistical Package for social sciences (version 21) to code, enter and compute the measurements of the correlation coefficients to determine the relationship between the variables while multiple regressions was used to determine the predictive power of the consolidated four variables of loan repayment on financial performance of deposit taking SACCO'S operating in Embu County, Kenya as shown in Table 1.

Table 1: Correlations Analysis

		Loan Appraisal	Interest Rates	Loan Follow-Up Procedures	Customer Characteristics	Financial Performance
Loan Appraisal	Pearson Correlation	1				
	Sig. (2-tailed)					
Interest Rates	Pearson Correlation	.888**	1			
	Sig. (2-tailed)	.000				
Loan Follow-Up	Pearson Correlation	.900**	.945**	1		

		Loan Appraisal	Interest Rates	Loan Follow-Up Procedures	Customer Characteristics	Financial Performance
Procedure	Sig. (2-tailed)	.000	.000			
Customer Characteristics	Pearson Correlation	.909**	.962**	.956**	1	
Financial Performance	Sig. (2-tailed)	.000	.000	.000		
	Pearson Correlation	.938**	.920**	.909**	.940**	1
	Sig. (2-tailed)	.000	.000	.000	.000	

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

As depicted in Table 1, Pearson’s correlations analysis was conducted at 95% confidence interval and 5% confidence level 2-tailed. The findings denotes the correlation matrix between the factors (loan appraisal, loan interest rates, loan follow-up procedures and customer characteristics) and financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya. The results reveals that all the correlation coefficients of the four independent variables were less than the critical value of 0.05 which indicates that there was a positive relationship between financial performance of deposit taking SACCO’s and loan repayment practices (loan appraisal, loan interest rates, loan follow-up procedures and customer characteristics at a magnitude of 888, 945, 956 and 940 respectively. Furthermore, taking all the factors at a constant all the significance values of the four independent variables are less than the critical value of 0.05 at 95% confidence level and 5% 63 significance level. Therefore, these results denotes that there was a statistical correlation between the independent variables (loan appraisal, loan interest rates, loan follow-up procedures and customer characteristics) and the dependent variable (financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya). These findings are in agreement with that of Chen & Pan (2012); Bhunia & Sarkar (2011) & Bratanovic (2009) who revealed that despite conflicting thoughts from scholars on the specific aspects that influence loan repayment, to a larger extent there is a statistical relationship between loan appraisal, interest rates and loan of follow-up procedures as compared to customer characteristics which is uncertain.

7.2 Regression Analysis

Further, to confirm the strength of the statistical relationship between variables of the study, multiple regression analysis was conducted at 95% confidence level and 5% significance level. Regression coefficients of determination explains the extent to which changes in the dependent variable can be explained by the change in the independent variables or the percentage of variation in the dependent variable (financial performance of deposit taking SACCO’s in Embu County) that is explained by all the four independent variables (loan appraisal, loan interest rates, loan follow-up procedures and customer characteristics).

Table 2: Model Coefficients

Model	Unstandardized Coefficients	Standardized Coefficients	Beta	t	Sig
(Constant)	1.139	1.2235		1.515	0.0133

Model	Unstandardized Coefficients	Standardized Coefficients	Beta	t	Sig
Loan Appraisal	0.887	0.1032	0.152	4.223	0.0122
Interest Rates	0.752	0.3425	0.154	3.424	0.0112
Loan Follow-Up Procedure	0.645	0.2178	0.116	3.236	0.0111
Customer Characteristics	0.539	0.1937	0.163	3.147	0.0554

As depicted from Table 2, holding all the four independent variables constant, the study revealed that at 95% confidence level and 5% significance level, a unit increase of loan appraisal will result to a positive effect on financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya by magnitudes of 887. The significance value of the variable is 0.0122 which indicates a positive significant relationship between loan appraisal and financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya. The findings corresponds with that of Nkuru (2015) who also established a moderate significant relationship between loan appraisal and financial performance of agricultural SACCO's in Kenya. Further, Warue (2012); Nguta and Guyo (2013) acknowledge that there is a significant relationship between loan appraisal and financial performance of firms in Kenya. The study revealed that there exist a significant positive relationship between loan interest rates and financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya by magnitudes of 752. The significance value of the variable of is 0.0112 which indicates a significant positive relationship between loan interest rates and financial performance of agricultural SACCO's in Kenya. The findings contracts with the findings of Omondi (2008); Olando, Jagongo and Mbewa (2013) who pointed out that even though interest rates contributed to deteriorating financial performance of SACCO'S, to a larger extent majority of the borrowers complied to loan policies based on the income levels and economic stability.

The study revealed that there exist a positive significant relationship be loan follow-up procedures and financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya by magnitudes of 0.645. The significance value of the variable is 0.0111 which indicates that there is a significant positive relationship between the variables. However, this findings contradicts with that of Arishaba (2011); Nguta and Guyo (2013) who established that to a larger extent there is no relationship between loan follow-up procedures and financial performance of deposit-taking Savings and Credit Co-operative Societies. Their study revealed that if internal loan policies are weak, loan follow-up procedures have less impact on performance of loans. The study established that there is no significant positive relationship between customer characteristics and financial performance of deposit-taking Savings and Credit Co-operative in Embu County, Kenya by magnitudes of 0.539. The significance value of the variable is 0.0554 which indicates insignificant relationship between variables. The findings contradicts that of Nkuru (2015); Nguta & Guyo (2013) & KUSCCO (2009) who revealed that customer characteristics such as age, income can influence financial performance of deposit-taking Savings and Credit Co-operative.

Table 3: Model Summary

Model	R	R Square	Adjusted Square	R	Std. Error of the Estimate
1	0.923	0.852	0.789		0.6273

The four independent factors that were studied, explain only 85.2% of financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya as represented by the R^2 . This therefore indicates that other factors not studied in this research that influences financial performance of deposit taking SACCO's contribute to 14.8%. Therefore, further research should be conducted to investigate the other factors that constitute (14.8%) that influence financial performance of deposit-taking Savings and Credit Co-operative Societies in Embu County, Kenya.

8. CONCLUSIONS

It can be concluded that for deposit taking SACCO's to maximize profits they should embrace practices that enhance loan repayment behaviour from beneficiaries such as establishing loan appraisal policies that are customer friendly such as assessing customer economic stability before approving loans. Further, the SACCO's should not only focus on maximizing profits but also to consider Central Bank of Kenya policies that determine interest rates charged. Loan follow-up procedures should not only reviewed but also emphasize on adequate training of credit officers on financial risk management. In addition, SACCO's should go beyond the concept of assessing customer character but also seek to understand the economic stability of the individual through evidence of job security and collateral security provided.

9. RECOMMENDATIONS

The study revealed that to some extent, deposit taking SACCO's were finding it difficult to determine viability of business and their sustainability in the long term period. Therefore, this study recommends that management of deposit taking SACCO's in Kenya should seek to evaluate sustainability of business enterprises of loan beneficiaries by establishing the period the business has operated and also establish a criteria of determining ownership of properties presented as collateral security. The study established that interest rates on loans were largely influenced by policies of Central Bank of Kenya. Therefore, this study recommends that top management of deposit taking SACCO's should seek to anticipate changing trends of interest rates in relation to Central Bank of Kenya regulation. Aspects that influence change of interest rates should be considered internally by the management before incorporated in loan policies. The study found that to some extent some loan beneficiaries violated loan regulations. Therefore, this study recommends that credit committees of deposit taking SACCO's should always seek to review some policies such loan repayment period, legal procedure, and employee skill development in order to maximize profits. The study found that it was difficult to measure prospect ability of repaying the loan by assessing his or her character alone. Therefore, this study recommends that credit officers and credit committees should go beyond customer character before approving loans but assess other factors such as job security and the amount borrowed by the prospect.

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