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UNITED STATES INTERNATIONAL UNIVERSITY - AFRICA

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STUDENT DECLARATION

I, the undersigned, declare that this is my original work and has not been submitted to any other college, institution or university other than the United States International University in Nairobi for academic credit.

Signed: ___________________________ Date___________________

Muthee Naomi Wanjiru (ID 639078)

This project has been presented for examination with my approval as the appointed supervisor.

Signed: ___________________________ Date___________________

Mr. Kepha Oyaro

Signed: ___________________________ Date___________________

Dean, Chandaria School of Business
ABSTRACT

Most commercial banks in developing countries including the Kenyan ones face a challenge of credit risk management which leads to loan losses. Credit Risk Management (CRM) which is effective reduces credit risk and also the loan losses reduce. Benchmarking surveys done in modern day on applications of credit show that missing signatures and incomplete applications as the major challenges when borrowers apply for loans. Yet another major challenge is found in the process of checking the credit reference.

Most of the studies done on bank loans related to banks general loans. Little focus has however not been directed on unsecured loans. Thus the aim of this study was to examine management practices of unsecured loans in banks in Kenya. This study was based at CFC Stanbic bank. The specific objectives of the study were to determine the effect of credit approval process of unsecured loans in commercial banks, to examine the effect of loan portfolio management on unsecured loans in commercial banks and to establish the loan recovery process in management of unsecured loans in commercial banks. The study is significant to Policy Makers and Top Management, Other Banks, Business Owners and Other Researchers. In review of literature, the section provides theoretical review.

The methodology adopted included descriptive research design. The target population comprised of 32 staff of CFC Stanbic bank concerned with loan administration, they constituted Group scheme lending relationship managers 3, Head of credit risk personal banking 1, Relationship managers 6, Branch customer consultants 12, Credit risk evaluation managers 6, and 4 collection and recoveries managers. In sampling, purposive sampling technique was adopted. The data collection techniques were the questionnaire. The data analysis technique was quantitative analysis. This was enhanced by a software known as SPSS and further presentation of findings involved distribution tables, pie charts and bar graphs.

The study findings revealed that summary section of the credit memo provides a high level overview of the request and loan size limits for new borrowers who do not have collateral can be kept small to mitigate the banks’ exposure, effective Credit Risk
Management system minimizes the credit risk, an unsecured loan is issued and supported only by the borrower's creditworthiness, rather than by some sort of collateral. There is challenge in credit reference checking process, the credit analyst takes all of the financial data that they have received and make an attempt to estimate the company’s ability to repay the loan and that depending on the type of unsecured loan the borrower is looking for. Many of the bad debts are attributable to moral hazard, the adverse incentives on bank owners to adopt imprudent lending strategies; the Bank’s portfolio is vulnerable to any adverse developments in the risk profile. On the loan recovery process in management of unsecured loans in banks, the study revealed that the banks are used to taking legal actions against chronic defaulters of bank-loans, the manager has a responsibility to fix an installment period on the basis of nature of their business.

The study concluded that incomplete applications and missing signatures are the primary challenges in credit application process as noted by a mean of 4.28. On loan portfolio the study found that the Bank operates in a very challenging and evolving environment, which continues to shape the future portfolio risk profile as confirmed by a mean of 4.24. Lastly in loan recovery process the study found that loan amount is recovered on installment basis as noted by a mean of 4.12.

The study recommended that Commercial banks in Kenya should device and implement strategies to ease and ensure effectiveness of the credit reference checking process. The credit managers should very keen on checking the completeness of the applications and missing signatures which are the primary challenges in credit application process. The banks should ensure that they have the right policies in place as regards the Unsecured Lending and to make sure that controls are in place to uphold the policies. Each Commercial Bank should have Credit management policies which include origination, approval, monitoring and recovery of the debt.
ACKNOWLEDGEMENT

I wish to express my sincere gratitude to my family for their unwavering support during this time, my supervisor Mr. Kepha Oyaro for his guidance and tireless effort during my research work. I acknowledge the Management and Staff of CfC Stanbic Bank for allowing me to undertake research in their organization. Finally, I thank the entire Management of USIU for giving me a chance to pursue my professional academic in their esteemed institution.
DEDICATION

This study is dedicated to my darlings Ryan and Joe. To my family and friends for their genuine support, and prayers. Their participation has seen me through all odds until this far. Thank you all for always standing by me whenever I needed your treasured support.
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CHAPTER ONE

1.0 INTRODUCTION

1.1 Background of the Problem

A Commercial bank is a company which proposes or carries on, any banking related business in Kenya but does not include the Central Bank of Kenya (CBK). Kenyan commercial banks are regulated, supervised and licensed by the Central Bank of Kenya (CBK) as stipulated in the Banking Act (Cap 488). A bank means a body corporate or other body of persons, which carries on their own or as agents of another corporate any banking business that is within Cap. 488 of the Banking Act in Kenya or anywhere else (Muruana, 2007). Chernykh and Theodossiou (2011) defines a commercial bank as a financial institution that provides services, such as accepting deposits, giving business loans and auto loans, mortgage lending, and basic investment products like savings accounts and certificates of deposit.

Finscope (2009) stated that the a commercial bank in the traditional sense can be said to be a brick and mortar cooperation which has safe deposit boxes, ATMs, vaults and tellers. However, there are some commercial banks which have no physical branches and customers are expected to do all the banking transactions using telephone or Internet. In exchange, the banks pay a higher interest rate on the customer’s deposits and investments, their fees are also lower.

Migiri (2012) stated the function of commercial banks as a safe place for clients to keep their money. The customer’s money in the bank is kept in vaults. This becomes convenient to the users. Other uses of commercial banks are laid out by Karimi (2012). Commercial banks provide loans to people who are in need of money. The loans given to the customers are paid within a stipulated time. The loans also are returned with interest according to the interest rate provided by the bank. Additionally commercial banks provide foreign exchange services to customers. Foreign currencies are offered to the bank customers in accordance to the currency market value. Banks are also places where customers can exchange their currencies; they also act as trustees managing the deceased...
property for the family of the deceased. This reduces disputes that can lead to business or estate losses for the deceased family.

According to Moyo and Rohan (2006) commercial banks assist traders dealing in international trade. Statements given by banks to such traders help them to transact business with other traders who view them as credit worthy. Additionally, the bank can act as collateral enabling a businessman to seal a deal. Banks are also sources of investment opportunities. They do this by selling shares to the customers on behalf of companies.

Commercial banks can also sell their own shares to the customers offering them investment opportunities. Customers also rely on banks for financial advice. They offer advice to customers who want a business loan on the best business practices to use. When asking for a loan they provide the customers with the best payment plan and much more. Customers also keep their valuable items in commercial banks. Such items can be expensive jewelry, title deeds among others. Customers also rely on banks advice relating to taxation. Commercial banks give their customers information that will be useful when preparing tax returns. This is essential so as not to default on paying taxes and be charged expensive penalties (Moyo and Rohan, 2006).

Muruana (2007) indicated that lending practices in the world could be traced to the period of industrial revolution which increased the pace of commercial and production activities thereby bringing about the need for large capital outlays for projects. Many captains of the industry at this period were unable to meet up with the sudden upturn in the financial requirements and therefore turned to banks for assistance.

Nayar (2013) noted that the emergence of commercialized banking services in Africa with the establishment of the African Banks Corporation (ABC) and later appearance of other banks in the scene during the colonial era witnessed the beginning of banks lending practice first in South Africa and Nigeria. However, during the colonial times, the banks’ lending practices were both discriminatory and biased and only the rich could access
advances and loans from banks. For this reason and others, indigenous banks in Nigeria were established.

Moyo and Rohan, (2006) in reference to credit and growth of economic activities of banks noted that prior to the advent of structural adjustment programme (SAP) in Nigeria in 1986; the lending practices of banks was strictly regulated under the close surveillance of the banks’ supervisory bodies. During the SAP period however there was some relaxation in the use of the stringent guidelines that had been used to guide the Nigerian banking practices. According to the 1998 Bank and Other Financial Act Amendment (BOFIA), banks in Nigeria should report all their large borrowings to Nigerian central bank (CBN). The CBN also stipulates that commercial banks value of their loan credit or any liability that is in respect to the borrower should not be higher than 20% of the total funds of the shareholders which are unimpaired by losses.

A study by Mkandawire (2011) found that shareholders were quick to downplay weak results from one of South Africa’s largest providers of unsecured loans, saying the decline in profits at African Bank Investments Limited (ABIL) did not signify more wide-spread problems in the sector. The findings however revealed that the number of unsecured loans sector-wide has risen steadily in recent years. The Kenyan central bank (CBK) considers the listed products as unsecured lending products: personal loans, credit cards, commercial papers, financing that is given to small and medium enterprises and overdrafts.

Oketch (2011) state that an unsecured loan can only be issued when supported by the customer’s creditworthiness and not by any form of collateral. Such a loan is issued without reliance of the borrower’s property as the loans collateral. To be approved to obtain the unsecured loans, borrowers should have higher credit ratings since they cannot be guaranteed using any kind of property. The loans are also of higher risk to the lenders and due to this, their interest rates are higher compared to secured loans.
Mkandawire (2011) did a study on Credit Risk: Pricing, Measurement, and Management of unsecured loans aimed at determining the credibility of borrowers of unsecured loans. In his study he found out that the risks of unsecured loans are found both to the lender and to the borrower. Banks usually are not very interested in giving unsecured financing because unsecured loans do not require collateral, which places banks at greater risk of not reclaiming all of their money in cases of default. Esipisu (2007) on the Profile of Borrowers Juhudi Credit Scheme in unsecured lending agrees and notes that borrowers with very good credit may be able to obtain these types of financing from banks, but most will have to settle with borrowing from a different lending source, like peer-to-peer lenders since unsecured loans are not insured by any property or assets and therefore usually carry a high interest rate.

The findings provided by Eigen (2009) on banking sector loan portfolio, establish that one of the major challenges faced, especially by personal unsecured loan programs is that borrowers are highly risky since they are typically low net-worth individuals with little or no collateral that can be acquired by the bank in the event of default, thus, a popular remedy to this problem involves requiring borrowers to apply for credit in voluntarily formed groups. Warui (2012) findings show that there is loan delinquency among Kenyan borrowers has steadily risen. This can be because the banks’ lending programs are ineffective. Many studies have looked at the advantage and disadvantages of unsecured lending, the data available in this area is normally insufficient to draw any meaningful conclusions on the best microcredit program that should be used for such lending programs. Scholars have come up with conflicting arguments on the most efficient lending programs that should be used.

Kithinji (2010) did a study on how unsecured loans were affected by credit risk management (measured by the ratio of loans and advances on total assets and the ratio of non-performing loans to total loans and advances on return on total asset in Kenyan banks between 2004 to 2008). According to the study, most commercial banks’ profits in the Kenyan market are not affected by non-performing loans or the amount of credit.
1.2 Statement of the Problem
One of the main objectives of the Kenyan banks which are registered is to enable the unbanked poor to access financial services. Today the banks clients total more than 6.5 million clients and they have an outstanding loan portfolio of more than US$ 310 million. However, despite the fact that proliferation of banks was done after the Microfinance Act was enacted in 2006, research has shown that 35.2% of the Kenyans are not able to access the banks financial services while 30.2% of the Kenyans have been excluded from any access to the banks financial services (Kenya Bankers Association, 2013).

Previous studies have focused on loans as a credit risk for instance, Moyo and Rohan (2006) studies credit and growth of economic activities of banks. Mkandawire (2011) did a study on Credit Risk: Pricing, Measurement, and Management of loans aimed at determining the credibility of borrowers of unsecured loans. Khan and Jain (2009) did a study on a group which had done a review of startup loan applications in Accion Texas for five years; the lender was providing capital to business startups across the country.

Esipisu (2007) did a study on Juhudi Credit Scheme unsecured lending borrowers profiles. Kithinji (2010) did an analysis on how credit risk management affected unsecured loans (measured by the ratio of loans and advances on total assets and the ratio of non-performing loans to total loans). Based on the studies identified, there is no known study done on management practices of unsecured loans in banks in Kenya. Most of the studies done on bank loans related to banks general loans. Little focus has however not been directed on unsecured loans. Thus the aim of this study was to look at the management practices of unsecured loans in commercial banks.

1.3 General Objective
This study sought to examine management practices of unsecured loans in banks in Kenya.
1.4 Specific Objectives

1.4.1 To examine the credit approval process as a management practice of unsecured loans in commercial banks.

1.4.2 To examine the effect of loan portfolio as a management practice of unsecured loans in commercial banks.

1.4.3 To establish the loan recovery process as a management practice of unsecured loans in commercial banks.

1.5 Significance of the Study

This study would be of direct benefit to the following:

1.5.1 Policy Makers and Top Management

This study points out at the most appropriate ways banks can manage unsecured loans. It is therefore expected that the Banks Policy Makers and Top Management will find this study very useful in a manner that they will be able to obtain additional information regarding the unsecured loan management and what they are expected to improve on to achieve greater success in the administration of unsecured loans.

1.5.2 Other Banks

This study will be useful to other banks and firms that have purposed to adopt unsecured lending practices. The study will seek to provide some of the findings and recommendations these firms can focus on to successfully administer unsecured loans.

1.5.3 Business Owners

Business owners will find this research study useful. It is anticipated that through contributory approach about the existing ways of accessing credit facilities and matters regarding unsecured loans, this study may provide more information on how well SMEs can go about obtaining these credit facilities.
1.5.4 Other Researchers

Scholars and researchers will benefit by finding ready information on unsecured lending and default management. The study will also help them to undertake further research to provide more information on loan recovery.

1.6 Scope of the Study

This study was done so as to look at factors that are affecting unsecured loans management in Kenyan banks based on a CFC Stanbic bank case study. The target population involved in this study was Group scheme lending relationship managers, Head of credit risk personal banking, Relationship managers, Branch customer consultants, Credit risk evaluation managers, Collection and recoveries managers. The study covered a duration of six months from June 2015 to December 2015. The limitations experienced were confidentiality of information. This was based on withholding information considered very private and sensitive. Considering that some banks are faced with competitiveness nature of seeking new opportunities for investments, disclosure of information was a little bit of a challenge.

Respondents felt that that the collected information could be used to upstage them especially in this competitive market. A degree of caution on information conveyed by Management was also experienced. The collection of data from the respondent was challenged by this aspect. This arose when the management had restricted the disclosure of certain information to a certain extent. Any other disclosure would however have resulted in serious action being taken by the management on selected respondents considered to have shared information that they were not in capacity to share. There were selected areas or department within CFC Stanbic bank that were considered out of bound or inaccessible for ordinary member of the public; therefore, this had hindered the researcher from accessing such section despite the valuable information for the study. The challenge was overcome by assuring the respondents that the study was entirely for academic purpose and not for commercial purpose.
1.7 Definition of Terms

1.7.1 Credit Terms
Credit terms are the conditions under which a microfinance institution advances credit to its customers (Eigen, 2005).

1.7.2 Interest Rates
The amount that is charged over and above the borrowed funds (Finscope, 2009).

1.7.3 Loan Recovery Methods
Methods that the bank management has instituted to help recover loans that were previously advanced to customers but stand a risk to be lost (Oketch, 2011)

1.7.4 Risks Management
The tactics used by the bank to avoid plumbing business operations to danger losses (Mkandawire, 2011).

1.8 Chapter Summary
Chapter one presents the background information to the research problem, identifies the problem statement, states the purpose of the study and lists the research questions addressed in the research project. It also presents the rationale, scope and definition of terms used. Chapter two presents the literature review. It discusses the existing research literature on the management of unsecured loans. The chapter tackles the posed research questions and gives a theoretical background to the study. Chapter three presents the study’s research methodology research methodology used in this study. It details the research design, population and sampling, data collection methods, research procedures and the analysis of data collected. Chapter four presents the study’s findings results and discussions. Chapter five presents the conclusion and recommendations for action and any further research.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction
This chapter presents the review of literature related to the unsecured loans. The chapter covers the theoretical reviews, literature review and the chapter summery. The study therefore addressed the following research objectives; to examine the credit approval process of unsecured loans in commercial banks, to examine the effect of loan portfolio management on unsecured loans in commercial banks and to establish the loan recovery process in management of unsecured loans in commercial banks.

2.2 Credit Approval Process in Management of Unsecured Loans in Banks

2.2.1 Terms of Credit Period
The credit period is given by the credit terms. Credit period is the time period within which credit is given. The length of the credit period is influenced by sometimes the Collateral value, the unsecured loans, the size of the account and market competition (Braverman, and Guasch, 2009).

Esipisu (2007) notes that Global bank finance is a rapidly growing dynamic sector that offers useful services, while posing some risks. Looking at the American market, supervision in USA banks operations needs sophisticated systems to monitor and respond to changing risks, in order to protect depositor funds, while fostering critically needed financial inclusion. This niche market can develop into an effective funding channel for emerging small businesses. However, it needs a proper capital structure, good corporate governance and relevant data on both lenders and borrowers through participation in credit bureaus.

Financial publications in Africa have put unsecured lending in the spotlight (Whitfield, 2011) as the Credit Regulator (Credit Regulator, 2012) question the unsecured lending growth that has taken place in the recent past. The Federal Trade Commission defines unsecured lending as a debt that is not tied to any asset. In this project, unsecured credit is considered to be credit that is not collateralized by any assets to which the creditor can
have recourse in case of failure by the debtor to meet the credit obligations. An unsecured loan is issued and supported only by the borrower's creditworthiness, rather than by some sort of collateral Esipisu (2007). Unlike a secured loan, an unsecured loan does not require backing by assets. It is often based on the borrower’s credit history and his/her ability to pay. Unsecured loans also include bank overdrafts, lines of credit and personal loans. Getting an unsecured loan can be more difficult than getting a secured loan if the borrower does not have an established or good credit rating. Although a credit check is not always required, it is most often necessary to ensure that the borrower has a history of paying off his debt. Depending on the type of unsecured loan the borrower is looking for, it can be applied for either online or manually from a financial institution.

For Kenyan banks, Bagachwa (2009) in his study established that having agreed to the terms of credit with a repayment duration which is clear to all concerned; the creditor has a responsibility in his own best interests to ensure that the customer keeps to his promises. The customer knows that his pattern of late payment has been accepted as satisfactory by the creditor and that a precedent has been established. The outcome is that the creditor cannot now enforce the original credit terms because he has endorsed new terms. The option that is now available is for the creditor and the bank to sit and start the negotiations afresh. This scenario is all too common and a professional credit manager should never allow it to happen.

A good policy is one which strikes a balance between customer retention and defection to facilitate outreach. A credit collection policy enables a bank to limit bad debts and improve cash flows since loans are in most cases the core business activities in banks (Kariuki, 2010). Kitua (2009) explains that the issue will usually be present during the first stage of loan application and further becomes more serious during the loan approval, monitoring and controlling stages, especially when policies, procedures and strategies related to credit processing as stipulated in the Credit Rate Management (CRM) guidelines are not followed, are weak, incomplete or not followed.
2.2.2 Unsecured Loans Control

Churchill and Frankiewicz (2006) suggest that control is one of the functions of managers and nowhere is a discussion about controls more important than when addressing risks. When designing a credit management strategy, the unsecured loans controls to prevent or mitigate risks should be extremely clear and specific, and they need to be carefully monitored to ensure that they work. Controls can be conceived and structured in different ways for example; loan size limits for new borrowers who do not have collateral can be kept small to mitigate the banks’ exposure until it gets to know them better. Mutua (2000) notes that evaluation of risk measures does not differ much from assessment of other key performance indicators in different industries.

Every indicator is a measure an element of a key success factor in a given area. For example, in case of unsecured loans measures, one can talk about such indicators as a ratio of good and bad credits, number of good credits issued to small businesses, ratio of long and short term credits, percentage of secured loans, number of credits on favorable terms, credit history, creditworthiness rate etc. Each category alone does not tell much but a combination of unsecured loans control measures will certainly help bank employee make a well informed decision on whether or not to issue a loan (Braverman & Guasch, 2009).

Abrahams & Zhan (2009) argue that costumer whose risk is higher often gives a premium interest rate so as to receive credit or borrow money. This higher interest rate govern to such customers mitigates the loss that can be incurred incase the borrower defaults on repaying the loan. The forecasting of loss involves the identification of the characteristics of the borrower and identifying any unsecured loans using the identified characteristics. The characteristics can be in form of income level, past delinquency rate or charge-offs. Migiri (2002) indicates that these include seasonal indexing and vintage curve techniques to identify the level of risk with a particular borrower. Seasonal indexing identifies the borrowers risk levels at different times of the year. The use of vintage cure techniques comes up with graphs on credit extended at different periods of time delinquency rates. It assists to access an unsecured high risk loan which has interest rates that can be
affordable but there are also things a borrower can do to improve his/her situation of accessing such a loan.

2.2.3 Credit Risk Management
Most commercial banks in developing countries including the Kenyan ones face a challenge of credit risk management which leads to loan losses. Credit Risk Management (CRM) which is effective reduces credit risk and also the loan losses reduce. Benchmarking surveys done in modern day on applications of credit show that missing signatures and incomplete applications as the major challenges when borrowers apply for loans. Yet another major challenge is found in the process of checking the credit reference. Tied into both of these issues is the challenge of turning around credit applications in a timely manner, especially when orders have already been booked (Grenier et al. 2004).

2.2.4 Identification of Loan Prospects
The credit approval process starts when the relationship manager identifies a possible loan prospect and starts discussions on the loan with the potential borrower. These discussions are inclusive of the loan term, rate and the amount of the loan. The request is ten given to the banks sales manager. The sales manager gives the go ahead for the loan whereby the customer is requested to present the bank with some important documents that are used to evaluate the loan request. This is inclusive of listings of accounts receivable, current personal and business financial statements, two years of tax returns for the borrower and the business at a minimum and any other documents that are needed for the approval of the loan request (Duffie & Singleton, 2013).

According to Duffie & Singleton (2013) the relationship manager then takes the documents to the bank credit analyst. The two have a brief discussion on the loans timing and the loans structure. The analysis is started by the credit analyst which if successful it is concluded as a loan approval statement. The summary section of the credit memo provides a high level overview of the request, and will include the loan amount, loan term, proposed interest rate, individual/corporate guarantors, use of fund among others.
This section also includes information on who the principals are, how much operating experience they have, how long the company has been in and business, what the company does before being granted credit facilities.

Migiri (2012) indicated that there is an industry research section which includes information on what the prevailing trends in the industry are, how the subject company compares to other companies in their industry and what the industry outlook is. When performing the repayment analysis, all the financial data received is considered by the credit analyst and further estimates if the company can be able to successfully repay the loan. This includes checking the business growth trends, the loan terms proposed, the company’s past data and other assumptions that enables the banks to came up with the Debt Service Coverage Ratio (DSCR).

2.2.5 Credit Reference Checking Process

Gisemba (2010) assert that even the lenders have conditions. For instance, to access a credit facility from a micro financier, borrowers would be required to organize themselves into a group, start a savings schemes with the microfinance and co-guarantee each other for every loan that the group would borrow. These conditions too, have proved challenging for many due to the group element and lack of privacy in individual financial affairs.

In a bank, being part of a group, borrowers are required to reveal their plans for the loan which many people may not want to divulge. Unlike banks, banks offer flexible and affordable loan facilities without conditions that exposes borrowers personal financial affairs. Bank savings have been proffered choice for many borrowers looking to access loans that are affordable with lower interest rates than the interest rates offered by banking institutions. With the increased demand for bank savings products, many such societies have emerged, with some offering borderless membership. They can draw members from various organizations, regions, careers and even industries (Gaitho, 2010). Until recently, banks were formed by umbrella associations, social organizations and companies, with membership restricted to staff members, organizations members and
officials. But borderless banks now give those locked out a chance to join a savings scheme. A bank provides their customers to loans that are three times bigger than the society savings. But to get the money, borrowers will first need to register as a member and channel their contribution to a bank every month for at least six months. Despite building savings with the bank within the set period of six months, members are still required to present loan guarantors with sufficient savings to cover the loan which is not easily forthcoming to get reliable guarantors (Emerson, 2008).

Kimberly (2006) found that just like getting collateral presents a headache to a bank borrower, hunting for guarantors for a bank loan can also be cumbersome. The guarantors are restricted to members only, with savings equivalent or more than the amount required. The guarantor’s number will depend on the loan applied for and the savings that the guarantors have with the bank. If a borrower have saved Sh100,0000 and want a loan of Sh300,000, with strong networking among the bank colleagues, borrower would only need one member with Sh300,000 to a guarantor. Otherwise, one will need members with less amounts to collectively act as guarantors.

According to Kithinji (2010) this is the trickiest part of getting a bank loan that many people seem to ignore. They only see the hurdle when they fail to gather sufficient guarantors. Most people however are unwilling to be banks loans guarantors for people who are not their close friends or relatives. This is because, upon guaranteeing a member for loan, the guarantors are not allowed to directly access their savings from the bank until the member services the loan. In worst case scenarios where the member defaults in repaying the loan, the savings, and that of the borrower, would be deducted to offset the debt.

Lately, Kithinji (2010) still established that networking has emerged as the surest way to build a strong wall of guarantors whenever one seeks affordable and cheap credit facilities from a bank. To improve one’s access to a loan from a bank, a member needs to grow his/her savings overtime while maintaining a strong network with other bank members. These could be the colleagues, friends or relatives. One can also build a
strong network with people not so closely related. A strong network can be simply be built by encouraging friends and colleagues to be members of the bank. This is very effective for banks whose membership is border-less. For banks with restricted membership, one can strike a rapport with other members through frequent visits, meetings and even tours.

2.3 Loan Portfolio Management of Unsecured Loans in Banks

2.3.1 Portfolio Risk Profile

The Bank environment of operation is often very evolving and challenging which further shapes the risk profile of future portfolios. This is compounded by the necessity to service different types of clients with diverse needs (Migiri, 2012). While Graeber (2007) assert that low risk investment grade and non-investment grade with high absorptive capacity located mostly within Africa region. They are experiencing socio-political problems and credit rating downgrades; Low risk countries with stable outlook and small absorptive capacity; and Low Income Countries (LICs) eligible only for non-sovereign guaranteed lending with relatively small credit limits. Some of them have recently come out of debt relief.

Chernykh & Theodossiou (2011) stated that the Bank’s credit risk exposure is also concentrated essentially in the first category that accounts for approximately 50% of the total disbursed and undisbursed portion of the loan portfolio. This makes the Bank’s portfolio vulnerable to any adverse developments in the risk profile of the countries in this category. The recent deterioration in the macro-economic and socio-political situation has resulted in increased calls for the Bank, as lender of last resort, to provide adequate response through increased lending in support of the reforms necessary to pave the way to regenerate growth while at the same time ensuring equitable allocation of resources and protecting its balance sheet.
2.3.2 Measures in Mitigating Risks

Despite recent growth in the banking sector, the sector is faced with challenges of loan repayment defaults by clients. Individual groups have tried using groups’ equity for collaterals which is expected to ensure the revolving of money for the benefits of other individual members of the group. However, loan delinquency has continued to pose serious challenges to most Banks. This is a very serious threat to the banks sustainability as credit risk on unsecured loans affects the profitability and the general performance of any bank (Esipisu, 2007).

According to Agene (2011) credit risk on unsecured loans portfolio is the deterioration in loan portfolio quality that results in loan losses and high delinquency management costs. Williams (2004) defined credit risk on unsecured loans as the risk of losing contractually obligated cash flows promised by a corporation, financial institution, government, etc. (the counterparty) due to default on the debt obligation. Defaults are usually associated with a credit event such a bankruptcy or reorganization, although delinquency in payment may also be considered a credit event even if there is not a formal bankruptcy.

Accordingly Duffie & Singleton (2013) it was noted that continuous oversight and monitoring is critical in management of unsecured loans. The annual Portfolio Credit Risk Review, part of such oversight and monitoring in banks focuses on stress testing and scenario analysis. It provides the credit offices with an assessment of developments in the Bank’s portfolio risk profile and measures contemplated/or being taken to mitigate these risks in unsecured loans. According to Warui (2012) the operating environment of the Bank portfolio has been volatile. However, the overall portfolio risk profile remains good, due in large part to the many enhancements made to the Bank’s risk management framework, including the proactive measures taken to address the expected negative impacts of the deteriorating credit environment.
2.3.3 Institutional Governance of Unsecured Loans

Nayar (2013) found that the loan portfolio growth momentum is maintained above pre-crisis levels - Following the unprecedented growth rates in 2009 for the bank’s portfolio in Kenyan Banks, approvals and disbursements of the Bank’s total lending loan portfolio had significantly decreased in 2010 but begun to slowly increase from the year 2011. Loan disbursement/commitment lags continue to be apparent; hence further efforts are deployed before approval to ensure the readiness of new transactions from different operational perspectives.

Nayar (2013) indicated that the concentration on loan risk portfolio, although improving, remains high with little scope for diversification in the bank’s loan portfolio. The constraining factors on diversification include among others: the credit policy of the Bank and the lack of cost effective hedging possibilities in the current market environment. Such high regional and sector concentrations could affect the portfolio quality. There are several threats and risks associated with the spill-over effects of the ongoing financial market turbulence and socio-political transitions on the continent begin to be felt in these regions and sectors.

2.3.4 Operating Environment of the Bank Portfolio

Stress testing of the Bank’s portfolio to systemic risks and extreme default scenarios indicates that the risk bearing capacity is expected to remain strong. However, to protect the Bank’s risk bearing capacity from erosion, Management needs to remain vigilant and indeed continuously improve in the areas of portfolio management, risk mitigation measures and the institutional governance of unsecured loans (Muruana, 2007).

Moyo and Rohan (2006) assert that more systematic and integrated Enterprise-wide approaches to risk management, currently under development, should continue to be strongly encouraged by all stakeholders (Board, Senior Management and Staff) and supported by the departments involved. Enterprise Risk management (ERM) and the risk dashboard implementation are expected to allow for more informed loan risk decision-making, improved loan risk reporting and greater accountability for risks. Maintaining
the momentum in ERM journey is critical to ensure the long term financial sustainability of the Bank.

Nayar (2013) noted that also known as default loan risk, credit risk on unsecured loans on unsecured loans relates to client failure to meet the terms of a loan contract. An effective and sound credit risk on unsecured loans management is critical to the stability of Banks. Mpiira et al. (2013) examined that effective risk on unsecured loans management is the process of managing the Bank’s activities which create credit risk on unsecured loans exposures, in a manner that significantly reduces the likelihood that such activities will impact negatively on Banks earnings and capital. Credit risk on unsecured loans is not confined to a Banks’ loan portfolio alone, but can also exist in its other assets and activities.

Oketch (2011) gives a number of reasons have been identified as contributing to the spate of banking distress which one notable cause is the issue of bad loans. NDIC (2004) observed that one single, biggest contributor to the bad loans portfolio of many of the failed banks in Kenya was insider trading. According to Brown bridge (2008), many of the bad debts were attributable to moral hazard, the adverse incentives on bank owners to adopt imprudent lending strategies, in particular insider lending and lending at high segments of the credit markets contrary to the interests of the bank’s creditors (mainly depositors or government if it explicitly insures deposits) which if unsuccessful, would jeopardize the solvency of the bank.

Nayar (2013) indicated that since the definition of the Bank’s risk appetite, there have been several noteworthy developments in the Bank’s loan portfolio operating environment that will have implications for the Banks future portfolio profile. These developments include the macro-economic difficulties and socio-political problems in Africa (where almost 50% of the bank’s portfolio is concentrated) and the financial market turmoil that may have some spill-over effects on both the RMC borrowers and their banking sector (mainly through the assets rather than liability sides of banks’
balance sheet and through contagion of Pan African financial groups operating in the absence of effective consolidated supervision).

Muruana (2007) given the dynamic context, this annual portfolio review in addition to providing the Board with the customary overview and assessment of the loan portfolio profile of the consolidated public and private sector portfolios, pays special attention to the Bank’s resilience and capacity to absorb further shock. It also articulates the measures aimed at protecting the Bank’s risk bearing capacity from rapid depletion in the face of these emerging challenges.

2.4 Loan Recovery Process in Management of Unsecured Loans in Banks
2.4.1 Bad-Loans
In the distant past, banks worldwide had to deal with only few cases of bad-loans. They were used to taking legal actions against chronic defaulters of bank-loans. By international parameter, non-performing assets of a bank should not exceed ten percent while such an indicator is estimated to have been crossed by 26 percent, mainly due to the increase in willful defaulters in the banks (Murray, 2007). In finance the term recovery refers to collection of amount due. Normally recovery depends on the purpose, time and condition; business running process. Loan amount is recovered on installment basis. The manager can fix an installment period on the basis of nature of their business as noted by (Howorth, 2003).

2.4.2 Recovery Rate
The recovery rate must be calculated for an estimation of the unexpected credit loss. The loss given default is an important parameter when using the advanced IRB approach of the Basel II-reform to calculate the capital requirements (Eigen, 2005). Banks that use this approach have to estimate the loss given default based on a suitable self-provided model. In return, these banks are confronted with lower capital requirements. The estimation of the loss given default should consider the potential influence of deteriorating economic conditions and the potential dependency with the probability of default.
An entry is required for the collection by debiting cash and crediting accounts receivable, Eigen (2005) observed that a high ratio of recoveries to write-offs may signify to the analyst that the firm writes off uncollected debts too quickly. Malimba and Musafiri (2009) stated that recoveries may come from several sources: the borrower's voluntary payment of some or all of the principal or interest payments due; foreclosure and sale of the borrower's assets pledged as loan collateral; or garnishment of the borrower's wages, salary, or bank assets.

2.4.3 Legal Processes

In order to recover a non-performing loan whether secured or not, a bank must first obtain a court order. Before 1996, this involved filing a legal suit in the civil court system. In this suit the banks had to state the particulars of the case and request that the court direct the borrower to pay the money to the banks (Awuonyo, 2012). If the loan is unsecured the bank must request that the court liquidate the firm assets and distribute the proceeds from the liquidation among all the creditors according to the priority of their claim. If the loan is secured it must request that the court enforce its security interest that is allow the sale of collateral so that the bank may recover its dues (Howorth, 2003).

Graeber (2007) explains that most unsecured loans for bad credit do have their fair share of fees associated with them. The unsecured loans for bad credit tend to have an origination fee, processing fee, administrative fee or sometimes a repayment fee. The unsecured loans for bad credit tend to add a decent amount of money to the balance when one accept the terms of the loans. Alila and Obado (2010) found that they also have a rather wide range of Annual Percentile Rate (APR) associated with them. Some of the interest is lower and offers a larger payback period, while others are very short term with high interest rates. Unsecured loans for bad credit can range from double digit interest all the way to triple digit interest depending on the type of loans that you choose to take.

Duffie and Singleton (2013) say there is a great diversity of ratios used to measure loan recovery and delinquency and it is important to understand how to choose and use them. Gaitho (2010) stated that in particular a monitoring system is needed that highlights
repayment problems clearly and quickly, so that loan officers and their supervisors can do something before it gets out of hand.

2.4.4 Legal Actions

Deloof (2003) suggests that recovery of bad loans by banks has turned into a big issue in the financial sector. This has greatly caused negative impact upon Banks' profit, Government revenue and the overall performance of the financial sector of the country. This therefore calls for an effective system and mechanism that allows for the early recovery of debts of Banks. Kimuyu and Omiti (2010) indicated that against this backdrop, a special institutional mechanism has been developed to address the debt-recovery problem through judicial steps and early settlement of cases. This initiative needs to be transparent and informative to all concerned. Limited education poses a challenge to the non-educated business owners unlike their educated counterparts who can easily go through the loan borrowing procedures.

Abrahams and Zhan (2009) found that the condition is tailored to fit the needs of a particular Bank, and the scope and detail commensurate with the complexity of the Bank’s lending activities. In all but very small community Bank, the lending conditions are written. Maina and Kibanga (2009) noted that the Bank lending conditions provide a realistic description of where the Bank wants to position itself on the risk/reward spectrum. It needs to provide sufficient latitude for a Bank to respond to good business opportunities while concurrently controlling loan risk.

Alila and Obado (2010) suggest that based on newly formed groups, credit is provided to small groups that guarantee the loans to their members. This approach emphasizes responsibility in the selection of clients, appraisal, approval and collection of loans while at the same time cutting administrative costs. Kirui and Kalio (2012) observed that members make weekly contributions to a joint account in the name of the group and the Bank, which acts both as a savings account for each member and a loan guarantee fund. Members can only receive a second and bigger loan after the first loan is repaid.
The responsibility for loan administration by the group provides peer pressure, which keeps up repayment. The group then on lends to the members at a higher interest rate. Members repay to the group, which then repays the Bank. The method is a cost-effective way of extending credit since the members do the administrative work (Gupta, 2013). Malimba and Musafiri (2009) assert that the groups have achieved high levels of cohesiveness and are effective in reaching each member. In one type of the minimalist individual credit model, credit provision is restricted to those who can secure it with tangible collateral; the condition is that in the scenario where tangible security is not required, it is replaced with guarantors or chattel mortgages.

2.4.5 Proceeds from the Liquidation

Loan security is one of the important aspects of credit to Bank members. Most lending to Bank members is security based, without any regard for potential cash flow. However, banks’ lending to members have devised alternative forms of collateral (Morara and Mureithi, 2009). These include: group credit guarantees, where Bank lend to individuals using groups as guarantors, and personal guarantors, where individuals are given loans based on a guarantor’s pledge. Loan guarantee schemes are increasingly being implemented as a means of encouraging financial institutions to increase their lending to the risky sectors and those without the traditional formal security (Lwanga, 2012).

In addition to establishing strategic objectives for the loan portfolio in Banks, management and the board are responsible for setting loan limits on the Bank lending activities. Loan limits take into consideration the Banks’s historical loss experience, its ability to absorb future losses, and the bank’s desired level of return (Mugure and Wanjohi, 2008). Limits may be set in various ways, individually and in combination. For example, they may be applied to a characteristic of individual loans, to the volume of a particular segment of the loan portfolio, and to the composition of the portfolio as a whole. Limits on loans to certain industries or on certain segments of the portfolio should be set with an eye to their impact on the portfolio’s aggregate risk (Mkandawire, 2011).
2.5 Chapter Summary

Chapter two presents the literature review. It discusses the existing research literature on the management of unsecured loans. The discussion tackles all the research questions posed and provides a firm theoretical background for the study.

Chapter three presents the research methodology used in this study. It details the research design, population and sampling, data collection methods, research procedures and how data collected was analyzed.
CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction
This chapter describes the research design and methodology that was used to carry out the research. The study adopted descriptive research design, the population, sample size and sampling procedure, data collection and data analysis techniques.

3.2 Research Design
The research design appropriate for this study was descriptive survey design. Mugenda and Mugenda (2003) note that this study involves collecting information from a larger number of cases, perhaps using questionnaires, because of the larger number of cases, survey generally involve some quantitative analysis. Survey studies are usually used to find about the facts by collecting the data directly from population or sample. Shamoo and Resnik (2003) many a time survey study intends to understand and explain the phenomena in a natural setting, organization or compare different demographic groups or see the cause and effect of relationship to make predictions. For this it requires responses directly from respondents of large population in general.

While Bray and Maxwell (2010) say extensive survey carried out when researcher want to make generalization, whereas intensive survey is done for making estimation. Survey researches demands various tools to collect the data from samples. They are ranging from questionnaire or interviews. So the kind of survey study needed for any study is based on its purpose, nature of data and population and sample of the study.

3.3 Population and Sampling Design
3.3.1 Population
The target population is the number of elements that has one or more characteristics in common that which can be studied or can provide information for studying; this is according to Peil (2011), while Mugenda and Mugenda (2003) a research population is also known as a well-defined collection of individuals or objects known to have similar characteristics therefore, all individuals or objects within a certain population usually
have a common, binding characteristic or trait. The target population comprised of staff members of CFC Stanbic Bank.

Table 3.1 Target Population

<table>
<thead>
<tr>
<th>Description</th>
<th>Target Population</th>
</tr>
</thead>
<tbody>
<tr>
<td>Group scheme lending relationship managers</td>
<td>3</td>
</tr>
<tr>
<td>Head of credit risk personal banking</td>
<td>1</td>
</tr>
<tr>
<td>Relationship managers</td>
<td>6</td>
</tr>
<tr>
<td>Branch customer consultants</td>
<td>12</td>
</tr>
<tr>
<td>Credit risk evaluation managers</td>
<td>6</td>
</tr>
<tr>
<td>Collection and recoveries managers</td>
<td>4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>32</strong></td>
</tr>
</tbody>
</table>

Source: CFC Stanbic Bank (2015)

3.3.2 Sampling Design

3.3.2.1 Sampling Frame

In sampling Frame, Sekaran (2003) defines a sampling frame as a list of all population from which, one draws the sample. From this study sampling frame constituted of 32 respondents. They were composed of branch customer consultants and relationship managers, group scheme lending relationship managers, head of credit risk personal banking segment, credit risk evaluation managers, collection and recoveries managers.

The target population was 32 staff of CFC Stanbic Bank at the head office who administers the credit facilities. They comprised branch customer consultants and relationship managers, group scheme lending relationship managers, head of credit risk personal banking segment, credit risk evaluation managers, collection and recoveries managers (Prospectus CFC Stanbic Bank, 2014).
3.3.2.2 Sampling Technique
Census design was used in the study. The population was 32 staff. This design is useful because in cases where population is manageable, the researcher has to involve the entire population. According to Glass and Hopkins (2010) census design helps to guaranty lack of biasness. Bray and Maxwell (2010) define census as being the procedure of systematically acquiring and recording information about the members of a given population. It is a regularly occurring and official count of a particular population. The census can be contrasted with sampling in which information is obtained only from a subset of a population, sometimes as an intercensal estimate. Census data is commonly used for research, business marketing, and planning, as well as a baseline for sampling surveys.

3.3.2.3 Sample Size
Sample size determination is the act of choosing the number of observations or replicates to include in a statistical sample. The sample size is an important feature of any empirical study in which the goal is to make inferences about a population from a sample (Sekaran, 2003). In practice, the sample size used in a study is determined based on the expense of data collection, and the need to have sufficient statistical power. In the study a total of 32 respondents were used.

3.4 Data Collection Methods
Questionnaires was used as a data collection tool to collect primary data. The questionnaires are defined by Glen (2013) as any written instruments that present respondents with a series of questions or statements to which they are to react either by writing out their answers or selecting from among existing answers.

Primary data refers to data collected using semi structured questionnaires. The questionnaire were administered using the drop and pick method. Questionnaires were used because they allowed the respondents to give their responses in a free environment and assist the researcher get information that would not have been given out had interviews been used, Cohen (2011). Secondary data refers to the information obtained
from articles, books, newspapers, internet and magazines. Secondary data indicates what other scholars have written about the topic in question.

Questionnaires were used because as explained by Lyon (2007) they are used to collect data about phenomena that is not directly observable such as inner experiences, opinions, values, interests, they are more convenient to use than direct observation when used for collecting data therefore the advantages of using questionnaires are as follows: can be given to large groups, respondents can complete the questionnaire at their own convenience, answer questions out of order, skip questions, take several sessions to answer the questions, and write in comments. The cost and time involved in using questionnaires is less than with interviews.

3.5 Research Procedures
In pre-testing the questionnaires, Trochim (2006) defines validity as the degree to which a test measures what it is supposed to measure. It is rare, if nearly impossible, that an instrument be 100% valid, so validity is generally measured in degrees. As a process, validation involves collecting and analyzing data to assess the accuracy of an instrument. To confirm validity, the questionnaires were confirmed by the research supervisor and the research assistant. While reliability of a research instrument concerns the extent to which the instrument yields the same results on repeated trials; reliability must be determined because there is generally a good deal of consistency in the results of a quality instrument gathered at different times (Lyon, 2007). To confirm reliability five questionnaires were developed then pilot tested among the staff at the organization.

Questionnaires were developed into structured and unstructured questions. Thereafter, all the questionnaires were distributed to the staff at CFC Stanbic Bank. This was achieved by a basic approach of hand delivery. A period of four days was allowed for the purpose of the staff to respond to the questionnaires before they are collected back for the analysis.
To ensure there is high response, the questions were phrased clearly in order to make clear dimensions along which responses were analyzed. In open ended questions, space was provided for relevant explanation by the respondents, thus giving them freedom to express their opinion, as questionnaires was administered, they were hand-delivered to the respondents and thereafter collected after a period of one week.

3.6 Data Analysis Methods
Kothari (2011) defines data analysis procedure as the process of packaging the collected information, putting it in order and structuring its main components in a way that the findings can be easily and effectively communicated. After all the necessary data has been collected; editing, coding and tabulation were carried out. The data was analyzed quantitative techniques guided by SPSS system of analysis. The presentation of analyzed data was in form of tables, graph and charts. Correlation Analysis was also used.

Correlation analysis is the statistical tool that can be used to determine the level of association of two variables (Trochim, 2011). The study developed a correlation matrix to analyze the relationships between the independent variables. The variables that were correlated were; Approval process, Loan portfolio management and Loan recovery process against the dependent variable- management of unsecured loans. Therefore, a correlation value of 0 shows that there is no relationship between the dependent and the independent variables. On the other hand, a correlation of ±1.0 means there is a perfect positive or negative relationship (Williamson, 2011). The values were interpreted between 0 (no relationship) and 1.0 (perfect relationship). The relationship was considered small when \( r = \pm 0.1 \) to \( \pm 0.29 \), while the relationship was be considered medium when \( r = \pm 0.3 \) to \( \pm 0.49 \), and when \( r = \pm 0.5 \) and above, the relationship was considered strong.

3.7 Chapter Summary
The chapter covered research design, population and sampling design, data collection methods, research procedures and data analysis methods. Chapter four presented the results and findings of the study.
CHAPTER FOUR

4.0 RESULTS AND FINDINGS

4.1 Introduction
This chapter discussed the interpretation and presentation of the findings obtained from the field. The chapter presented the background information of the respondents; findings of the analysis based on the objectives of the study.

4.2 General Information
In the response, the study targeted 32 respondents from which 25 filled and returned the questionnaires making a response rate of 78%. This response rate was satisfactory to make conclusions on the management practices of unsecured loans in banks in Kenya. According to Mugenda and Mugenda (2003), a response rate of 50% is adequate for analysis and reporting; a rate of 60% is good and a response rate of 70% and over is excellent. Based on the assertion, the response rate was considered to excellent.

4.2.1 Work Experience at CfC Stanbic Bank
From the study findings most of the respondents as represented by 36% had work experience at CfC Stanbic bank of between 9-12 years, 28% of the of the respondents had work experience at CfC Stanbic bank of between 5-8 years, 20% of the respondents had work experience at CfC Stanbic bank of between 13-15 years, 12% of the respondents had work experience at CfC Stanbic bank of between 1-4 years whereas 4% of the respondents had work experience at CfC Stanbic bank of 15 years and above.

Figure 4.1: Work Experience at CfC Stanbic bank
4.2.2 Highest Level of Education

From the study findings majority of the respondents as represented by 68% of the respondents had Post graduate qualification, 28% of the respondents had undergraduate degree whereas 4% of the respondents had College certificate/Diploma. This implies that the respondents were well educated to respond to the questions with ease.

![Figure 4.2: Highest Level of Education](image)

4.2.3 Gender

The study sought to find out the respondents gender. The study findings are shown by the figure below.

From the study findings majority of the respondents as represented by 56% of the respondents were male whereas 44% of the respondents were female. This implies that there were more male respondents than female.

![Figure 4.3: Gender](image)
4.2.4 Age of Respondents in Years

From the study findings most of the respondents as represented by 44% of the respondents were aged between 34-41 years old, 28% of the respondents were aged 42 years and above, 24% of the respondents were aged between 26-33 years whereas 4% of the respondents were aged between 18-25 years old. This implies that most of the respondents were youth and middle aged.

![Figure 4.4: Age of Respondents in years](image)
4.3 Effects of Credit Approval Process on Management Practices of Unsecured Loans in Commercial Banks

The study sought to find out the extent to which respondents agree or disagree with each of the following statements on the credit approval process in management of unsecured loans in banks. The findings are as shown by the table below.

4.3.1 Challenges in Credit Applications

Table 4.1 provided a study finding in which it was established that incomplete applications and missing signatures are the primary challenges in credit application process as indicated by a mean of 4.28. This implied that the bank had a responsibility to adopt a technical approach to verifying signatures application procedures.

<table>
<thead>
<tr>
<th>Category Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Responses</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>18</td>
<td>7</td>
<td>4.28</td>
<td>0.31</td>
</tr>
</tbody>
</table>

4.3.2 Effective Credit Risk Management

Table 4.2 comprised of study findings in which respondents confirmed that effective credit risk management system minimizes the credit risk considering that majority of respondents agreed and strongly agreed going by a mean of 4.32. This implied that adopting effective risk management systems reduced the risks involved in unsecured loans.

<table>
<thead>
<tr>
<th>Category Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Responses</td>
<td>0</td>
<td>0</td>
<td>2</td>
<td>13</td>
<td>10</td>
<td>4.32</td>
<td>0.24</td>
</tr>
</tbody>
</table>
4.3.3 Credit Reference Checking Process
Table 4.3 constituted study findings which showed that there is challenge in credit reference checking process. In the analysis, majority of respondents strongly agreed as well as those who strongly agreed to the statement. This was confirmed by a mean of 4.2. An indication that as much as banks continues to experience challenge in credit reference, there would be more challenges in managing unsecured loans.

<table>
<thead>
<tr>
<th>Category Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Responses</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>18</td>
<td>6</td>
<td>4.2</td>
<td>0.31</td>
</tr>
</tbody>
</table>

4.3.4 Level of Overview of the Request
Table 4.4 provided findings from a study that focused on determining whether the summary section of the credit memo provides a high level overview of the request. Majority of respondents agreed to the statement and was represented by a mean of 0.29. The study implied that the summary provided appropriate overview of clients.

<table>
<thead>
<tr>
<th>Category Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Responses</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>16</td>
<td>9</td>
<td>4.36</td>
<td>0.29</td>
</tr>
</tbody>
</table>
4.3.5 Company’s Ability to Repay the Loan

The presentation of findings on table 4.5 confirmed that the credit analyst takes all of the financial data that they have received and make an attempt to estimate the company’s ability to repay the loan. This was represented by a mean of 0.35. An indication regular follow up makes an attempt to estimate the company’s ability to repay the loan.

Table 4.5 Company’s Ability to Repay the Loan

<table>
<thead>
<tr>
<th>Category Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Responses</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>20</td>
<td>5</td>
<td>4.2</td>
<td>0.35</td>
</tr>
</tbody>
</table>

4.3.6 Collateral Value and the Unsecured Loans

Table 4.6 showed findings in which respondents indicated that credit analyst takes all of the financial data that they have received and make an attempt to estimate the company’s ability to repay the loan as shown by a mean of 4.24. The study revealed that the length of the credit period is influenced by sometimes the Collateral value.

Table 4.6 Collateral Value and the Unsecured Loans

<table>
<thead>
<tr>
<th>Category Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Responses</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>19</td>
<td>6</td>
<td>4.24</td>
<td>0.33</td>
</tr>
</tbody>
</table>
4.3.7 Borrower's Creditworthiness
The study findings presented on table 4.7 showed that an unsecured loan is issued and supported only by the borrower's creditworthiness, rather than by some sort of collateral. This was confirmed by a mean of 0.27. Therefore, the study revealed that banks were expected to focus more on credit worthiness rather than the collateral aspect.

Table 4.7 Borrower's Creditworthiness

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>15</td>
<td>9</td>
<td>4.32</td>
</tr>
</tbody>
</table>

4.3.8 Unsecured Loan versus Secured Loan
Table 4.8 provided study findings that focused on determining whether getting an unsecured loan can be more difficult than getting a secured loan if the borrower does not have an established or good credit rating. From the responses it was found that a good number of respondents agreed and strongly agreed as shown by a mean of 4.32.

Table 4.8 Unsecured Loan is more difficult than getting a Secured Loan

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>15</td>
<td>9</td>
<td>4.32</td>
</tr>
</tbody>
</table>
4.3.9 Loan Size Limits New Borrowers
Table 4.9 constituted study findings focusing on determining whether loan size limits for new borrowers who do not have collateral can be kept small to mitigate the banks’ exposure. This was a mean of 4.36. Based on the study findings, it was a clear indication that Loan size limits for new borrowers who do not have collateral can be kept small to mitigate the banks’ exposure.

Table 4.9 Loan Size Limits New Borrowers

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>16</td>
<td>9</td>
<td>4.36</td>
<td>0.29</td>
</tr>
</tbody>
</table>

4.4 The extent to which Loan Portfolio affects Management Practices of Unsecured Loans in Commercial Banks
The study sought to find out the extent to which respondents agreed or disagreed with each of the following statements on effect of loan portfolio in management of unsecured loans in banks. The study findings are as shown by the table below.

4.4.1 Bank Operates in Challenging and Evolving Environment
Table 4.10 showed study findings in which respondents indicated that the bank operates in a very challenging and evolving environment, which continues to shape the future portfolio risk profile. The findings were in correspondence with a mean of 4.24. Considering majority of respondents were in agreement to this statement, it was a confirmation that banks do operate in a very challenging and evolving environment.

Table 4.10 Bank Operates in Challenging and Evolving Environment

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>17</td>
<td>7</td>
<td>4.24</td>
<td>0.29</td>
</tr>
</tbody>
</table>
4.4.2 Developments in the Bank’s Portfolio Risk Profile
The study summarized data analysis in which it was established from table 4.11 that Scenario analysis provides the credit offices with an assessment of developments in the Bank’s portfolio risk profile and measures taken to mitigate these risks in unsecured loans. The findings shown were confirmed by a mean of 0.31. This indicates that use of scenario analysis helps banks to take measures to mitigate these risks in unsecured loans.

Table 4.11 Developments in the Bank’s Portfolio Risk Profile

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>18</td>
<td>6</td>
<td>4.2</td>
<td>0.31</td>
</tr>
</tbody>
</table>

4.4.3 The Bank’s Portfolio is Vulnerable to Adverse Developments
Table 4.12 showed findings in which respondents were in total agreement that the Bank’s portfolio is vulnerable to any adverse developments in the risk profile. This was confirmed by a mean of 4.36. Based on the findings shown, it was therefore noted that adverse development in the market resulted in challenges of managing unsecured loans.

Table 4.12 The Bank’s Portfolio is Vulnerable to Adverse Developments

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>14</td>
<td>10</td>
<td>4.36</td>
<td>0.26</td>
</tr>
</tbody>
</table>
4.4.4 The Operating Environment of the Bank Portfolio is Volatile
The presentation of findings shown on table 4.13 was a confirmation of summarized responses from respondents who were in agreement that the operating environment of the Bank portfolio has been volatile as noted by a mean of 0.38. Therefore, this implied that change in operating environment had a direct effect on management of unsecured loans.

Table 4.13 The Operating Environment of the Bank Portfolio is Volatile

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>22</td>
<td>3</td>
<td>4.12</td>
<td>0.38</td>
</tr>
</tbody>
</table>

4.4.5 Risk Mitigation Measures and Institutional Governance of Unsecured Loans
Table 4.14 comprised of findings from a study which showed that management needs to remain vigilant and improve areas of portfolio management, risk mitigation measures and the institutional governance of unsecured loans. This was expressed from respondents by a mean of 4.32. The study findings implied that management needs to remain vigilant and improve areas of portfolio management to enhance management of unsecured loans.

Table 4.14 Risk Mitigation Measures and Institutional Governance of Unsecured Loans

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>15</td>
<td>9</td>
<td>4.32</td>
<td>0.27</td>
</tr>
</tbody>
</table>
4.4.6 Credit Risk on Unsecured Loans is not confined to a Banks’ Loan

Table 4.15 expressed study findings in respondents indicated that many of the bad debts are attributable to moral hazard, the adverse incentives on bank owners to adopt imprudent lending strategies as expressed with a mean of 4.40. Therefore, this confirmed that banks’ loan portfolio can also exist in its other assets and activities.

Table 4.15 Credit Risk on Unsecured Loans is not confined to a Banks’ Loan

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>15</td>
<td>10</td>
<td>4.4</td>
<td>0.28</td>
</tr>
</tbody>
</table>

4.4.7 Bad Debts are attributable to Moral Hazard and the Adverse Incentives

Table 4.16 summarized study findings in which it was found that many of the bad debts are attributable to moral hazard, the adverse incentives on bank owners to adopt imprudent lending strategies. This implied that the bank had a role to enhance effectiveness in management of unsecured loans.

Table 4.16 Bad Debts are attributable to Moral Hazard and the Adverse Incentives

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>15</td>
<td>10</td>
<td>4.40</td>
<td>0.28</td>
</tr>
</tbody>
</table>
4.5 The Effect of Loan Recovery Process on Management Practices of Unsecured Loans in Commercial Banks

The study sought to find out the extent to which respondents agreed or disagreed with each of the following statements on the loan recovery process in management of unsecured loans in banks.

4.5.1 Loan Amount is recovered on Installment Basis

Table 4.17 provided study finding on whether loan amount is recovered on installment basis. In regards to the responses provided, the study found that majority of respondents agreed and strongly agreed going with a mean of 4.12. The study implied that recovering unsecured loan through installment was found to be effective.

Table 4.17 Loan Amount is recovered on Installment Basis

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>20</td>
<td>4</td>
<td>4.12</td>
<td>0.34</td>
</tr>
</tbody>
</table>

4.5.2 Manager has a Responsibility to Fix an Installment Period

Table 4.18 constituted study findings in which there was need to determine whether manager has a responsibility to fix an installment period on the basis of nature of their business. In relations to the study findings majority of respondents agreed to the statement with a mean of 4.40. Therefore, this implied that the manager has a responsibility to set installment based on the capability of the debtor.

Table 4.18 Manager has a Responsibility to Fix an Installment Period

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>15</td>
<td>10</td>
<td>4.40</td>
<td>0.28</td>
</tr>
</tbody>
</table>
4.5.3 Banks take Legal Actions against Chronic Defaulters

Table 4.19 the summary of study findings provided was based on the need to address the findings on which there was need to establish whether the banks are used to taking legal actions against chronic defaulters of bank-loans. In relations to the study, majority of respondents mainly focused on agreeing to the statement with a mean of 4.48. As a result, the study confirmed that taking legal action to chronic defaulters may help recover the unsecured loans.

Table 4.19 Banks take Legal Actions against Chronic Defaulters

<table>
<thead>
<tr>
<th>Category/ Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>13</td>
<td>12</td>
<td>4.48</td>
<td>0.27</td>
</tr>
</tbody>
</table>

4.5.4 Deteriorating Economic Conditions

Table 4.20 constituted study findings in which there was need to establish whether estimation of the loss given default should consider the potential influence of deteriorating economic conditions. As per the study findings, it was confirmed that majority of respondents were in agreement to the statement as indicated by a mean of 3.68. This implied that due to deteriorating economic conditions could jeopardize the state of managing and recovering unsecured loans.

Table 4.20 Deteriorating Economic Conditions

<table>
<thead>
<tr>
<th>Category/ Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>16</td>
<td>5</td>
<td>3.68</td>
<td>0.27</td>
</tr>
</tbody>
</table>
4.5.5 Unsecured Loans, the Bank Requests the Court Liquidate the Firm Assets
The presentations of findings on table 4.21 sought to establish whether the loan is unsecured the bank must request that the court liquidate the firm assets and distribute the proceeds from the liquidation among all the creditors and this was confirmed by majority of respondents with a mean of 4.24 who were in total agreement. The study implied that if the loan is unsecured the bank must request that the court liquidate the firm assets.

Table 4.21 Unsecured Loans, the Bank Requests the Court Liquidate the Firm Assets

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>17</td>
<td>7</td>
<td>4.24</td>
<td>0.29</td>
</tr>
</tbody>
</table>

4.5.6 Unsecured Loans for Bad Credit have Fair Share of Fees
Table 4.22 provided findings in which the study sought to establish whether most unsecured loans for bad credit do have their fair share of fees associated with them. Based on the responses provided, majority were those who were in total support to the statement and were represented with a mean of 4.28. This therefore revealed that there is fee charged above normal fees in relations to unsecured loans.

Table 4.22 Unsecured Loans for Bad Credit do have their Fair Share of Fees

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>16</td>
<td>8</td>
<td>4.28</td>
<td>0.28</td>
</tr>
</tbody>
</table>
4.5.7 There are Institutional Mechanisms to Address the Debt-Recovery Problem

Table 4.23 showed findings that majored on determining whether institutional mechanisms have been developed to address the debt-recovery problem through judicial steps and early settlement of cases. In regards to the responses the study established that majority of respondents agreed to the statement the result backed by a mean of 4.28. This finding implied that the presence of institutional mechanism to recover loans was considered a positive move towards managing unsecured loans.

<table>
<thead>
<tr>
<th>Category/Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>16</td>
<td>8</td>
<td>4.28</td>
<td>0.28</td>
</tr>
</tbody>
</table>

4.5.8 Correlation Analysis

Correlation analysis is the statistical tool that can be used to determine the level of association of two variables (Levin & Rubin, 1998). This analysis can be seen as the initial step in statistical modelling to determine the relationship between the dependent and independent variables. Correlation analysis helped to detect any chance of multicollinearity. Correlation value of 0 shows that there is no relationship between the dependent and the independent variables. On the other hand, a correlation of ±1.0 means there is a perfect positive or negative relationship (Hair et al., 2010). The values were interpreted between 0 (no relationship) and 1.0 (perfect relationship). The relationship was considered small when $r = ±0.1$ to $±0.29$, while the relationship was be considered medium when $r = ±0.3$ to $±0.49$, and when $r = ±0.5$ and above, the relationship was considered strong.
Table 4.24 Correlations

<table>
<thead>
<tr>
<th></th>
<th>Unsecured Loans</th>
<th>Approval process</th>
<th>Portfolio management</th>
<th>Recovery process</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unsecured Loans</td>
<td>Pearson Correlation</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Approval process</td>
<td>Pearson Correlation</td>
<td>-.853*</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.039</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Portfolio management</td>
<td>Pearson Correlation</td>
<td>-.597*</td>
<td>-.087</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.011</td>
<td>.483</td>
<td></td>
</tr>
<tr>
<td>Recovery process</td>
<td>Pearson Correlation</td>
<td>.689**</td>
<td>.781**</td>
<td>-.065</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.005</td>
<td>.000</td>
<td>.600</td>
</tr>
</tbody>
</table>

*. Correlation is significant at the 0.05 level (2-tailed).

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

Source: Research Data

Results in table 4.24 above reveal that the correlation between unsecured loans and approval process is negative and significant (R= -0.853, p value=0.039). This implies that an increase in credit approval process is associated with a decrease in unsecured loans and a decrease in credit approval process is associated with an increase in unsecured loans.

Findings reveal that the correlation between unsecured loans and portfolio management is negative and significant (R= -0.597, p value=.011). This implies that an increase in loan portfolio management is associated with a decrease in unsecured loans and a decrease in loan portfolio management is associated with an increase in unsecured loans. In addition, the study reveals that the correlation between unsecured loan and loan recovery process is positive and significant (R= 0.689, p value=.005). This implies that an increase in loan recovery process is associated with an increase in unsecured loan and a decrease in transaction cost is associated with a decrease in unsecured loan.
4.6 Chapter Summary

This chapter presented the results and findings of the study. The study focused on the Effects of Credit Approval Process on Management Practices of Unsecured Loans in Commercial Banks, the extent to which Loan Portfolio affects Management Practices of Unsecured Loans in Commercial Banks and The effect of Loan Recovery Process on Management Practices of Unsecured Loans in Commercial Banks. Chapter five presented the discussion, conclusion and recommendations for action and further research.
CHAPTER FIVE

5.0 DISCUSSION, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction
This section provides the summary of the project which include all the chapters and their subsections such that chapter one covering introduction of the study, chapter two addressing review of literature, chapter three methodology employed, chapter four data analysis. This section covers the discussion addressing the findings of the study, the conclusion, recommendations for improvement and the recommendations for further study.

5.2 Summary
The general objective was to examine the management practices of unsecured loans in commercial banks in Kenya. The specific objectives were to establish the credit approval process as a management practice of unsecured loans in commercial banks, to examine the effect of loan portfolio as a management practice of unsecured loans in commercial banks and to establish the loan recovery process as a management practice of unsecured loans in commercial banks.

In the methodology of the study, descriptive survey design was adopted. Descriptive survey design involves finding out facts by collecting the data directly from population or sample. The population of the study comprised of staff members of CFC Stanbic Bank. From the entire staff population, the study sampled 32 staff that comprised of branch customer consultants and relationship managers, group scheme lending relationship managers, head of credit risk personal banking segment, credit risk evaluation managers, collection and recoveries managers. However, sampling technique was census design. Questionnaire was used as data collection tool. The collected data was quantitatively analysis. The analyzed data was presented by use of tables and figures.

The findings generated from the study on effect of credit approval process as a management practice of unsecured loans in commercial banks found that credit memo provides a high level overview of the request and loan size limits for new borrowers who
do not have collateral can be kept small to mitigate the banks’ exposure. It was further established that the length of the credit period is influenced by sometimes the Collateral value, the unsecured loans and the size of the account.

The findings based on the effect of loan portfolio as a management practice of unsecured loans in commercial banks established that many of the bad debts are attributable to moral hazard, the adverse incentives on bank owners to adopt imprudent lending strategies, thus, the bank’s portfolio is vulnerable to any adverse developments in the risk profile.

The findings showed that on loan recovery process as a management practice of unsecured loans; banks are used to taking legal actions against chronic defaulters of bank-loans. It was also noted that the manager has a responsibility to fix an installment period on the basis of nature of their business and that institutional mechanisms have been developed to address the debt-recovery problem through judicial steps and early settlement of cases.

5.3 Discussion
5.3.1 Effect of Credit Approval Process as a Management Practice of Unsecured Loans in Commercial Banks
The findings in the study showed that credit memo provides a high level overview of the request and loan size limits especially for new borrowers who do not have collateral. The findings reveal that the bank enforces a highly secured process of assessing the borrowers in order to mitigate risks of default from new borrowers. These findings agreed with the studies done by Mutua (2000) who found that evaluation of risk measures does not differ much from assessment of other key performance indicators in different industries.

The study found that effective credit risk management system minimizes the credit risk that a bank would have encountered from credit defaulters. The findings revealed that an unsecured loan is issued and supported only by the borrower’s creditworthiness; these findings were in confirmation with those of Esipisu (2007) who found that unlike a
secured loan, an unsecured loan does not require backing by assets. It is often based on the borrower’s credit history and his/her ability to pay. The findings showed that some of the unsecured loans included bank overdrafts, lines of credit and personal loans. It was established that getting an unsecured loan can be more difficult than getting a secured loan if the borrower does not have an established or good credit rating. This implied that not having a credible history of a borrower means that chances of defaults are high.

The findings expressed in this research regarding the credit approval process showed that incomplete applications and missing signatures are the primary challenges in credit application process. These findings were similar to those of Grenier et al. (2004) who found that major challenge are found in processes of checking the credit reference. Tied into both of these issues is the challenge of turning around credit applications in a timely manner, especially when orders have already been booked.

The length of the credit period is influenced by sometimes the collateral value, the unsecured loans and the size of the account, there is challenge in credit reference checking process and the credit analyst takes all of the financial data that they have received and make an attempt to estimate the company’s ability to repay the loan and that depending on the type of unsecured loan the borrower is looking for. Therefore, it was found that it can be applied for either online or manually from a financial institution.

5.3.2 The Effect of Loan Portfolio as a Management Practice of Unsecured Loans in Commercial Banks

The study established that many of the bad debts are attributable to moral hazard and the adverse incentives on bank owners to adopt imprudent lending strategies. These findings were in agreement with those provided by Brown (2008) who established that in particular insider lending and lending at high segments of the credit markets contrary to the interests of the bank’s creditors (mainly depositors or government if it explicitly insures deposits) which if unsuccessful, would jeopardize the solvency of the bank. The study further established that the bank’s portfolio is vulnerable to any adverse
developments in the risk profile. The findings were not relating to any of the studies done.

There is a notable need for management need to remain vigilant and improve on areas of portfolio management, risk mitigation measures and the institutional governance of unsecured loans. On the overall, credit risk on unsecured loans is not confined to a Banks’ loan portfolio alone, but can also exist in its other assets and activities. These findings were found to relate with those of Muruana, (2007) who established that stress testing of the bank’s portfolio to systemic risks and extreme default scenarios indicates that the risk bearing capacity is expected to remain strong and serves to protect the Bank’s risk bearing capacity from erosion. The bank operates in a very challenging and evolving environment which continues to shape the future portfolio risk profile.

The study revealed that scenario analysis provides the credit offices with an assessment of developments in the Bank’s portfolio risk profile and measures taken in mitigating these risks in unsecured loans. These findings were in collaborated those of Warui (2012) who found that the operating environment of the Bank portfolio has been volatile. However, the overall portfolio risk profile remains good, due in large part to the many enhancements made to the Bank’s risk management framework, including the proactive measures taken to address the expected negative impacts of the deteriorating credit environment. The analysis of findings revealed that the bank’s portfolio risk profile and measures taken to mitigate these risks in unsecured loans, the operating environment of the Bank portfolio has been volatile.

5.3.3 The Effect of Loan Recovery Process as a Management Practice of Unsecured Loans in Commercial Banks

On the loan recovery process in management of unsecured loans in banks, the study revealed that the banks are used to taking legal actions against chronic defaulters of bank-loans. These findings were not in relations to other study findings however, it was found to differ with Murray (2007) who instead found that non-performing assets of a bank
should not exceed ten percent while such an indicator is estimated to have been crossed by 26 percent, mainly due to the increase in willful defaulters in the banks. The analysis revealed that the manager has a responsibility to fix an installment period on the basis of nature of their business in order to provide flexibility in payment among debtors.

The study further established that institutional mechanisms have been developed to address the debt-recovery problem through judicial steps and early settlement of cases, estimation of the loss given default should consider the potential influence of deteriorating economic conditions. The study found that in order to recover a non performing loan whether secured or not, a bank must first obtain a court order and most unsecured loans for bad credit do have their fair share of fees associated with them. These findings were in agreement of Eigen (2005) who found that banks that use this approach have to estimate the loss given default based on a suitable self-provided model. In return, these banks are confronted with lower capital requirements.

Still, it was found that if the loan is unsecured the bank must request that the court liquidate the firm assets and distribute the proceeds from the liquidation among all the creditors, an entry is required for the collection by debiting cash and crediting accounts receivable. This was agreeable with the findings of Malimba and Musafiri (2009) who stated that recoveries may come from several sources: the borrower's voluntary payment of some or all of the principal or interest payments due; foreclosure and sale of the borrower's assets pledged as loan collateral; or garnishment of the borrower's wages, salary, or bank assets. Lastly, the analysis revealed that loan amount is recovered on installment basis and the recovery rate must be calculated for an estimation of the unexpected credit loss.

5.4 Conclusion
The following conclusions were drawn following the foregoing discussions above, each corresponding to the specific objectives of the study as under:
5.4.1 Effect of Credit Approval Process as a Management Practice of Unsecured Loans in Commercial Banks

The study concluded that in credit approval process, paying attention to credit memo provides a high level overview of the request and loan size limits for new borrowers who do not have collateral and thereby mitigating the banks’ exposure. Effective Credit Risk Management system minimizes the credit risk and an unsecured loan is issued and supported only by the borrower's creditworthiness rather than by some sort of collateral. Getting an unsecured loan is more difficult than getting a secured loan if the borrower does not have an established or good credit rating.

5.4.2 The Effect of Loan Portfolio as a Management Practice of Unsecured Loans in Commercial Banks

The study concluded that in loan portfolio, the bank’s portfolio is vulnerable to any adverse developments in the risk profile. The management needs to remain vigilant and improve areas of portfolio management, risk mitigation measures and the institutional governance of unsecured loans and credit risk on unsecured loans is not confined to a Banks’ loan portfolio alone but can also exist in its other assets and activities. It was noted that the Bank operates in a very challenging and evolving environment.

5.4.3 The Effect of Loan Recovery Process as a Management Practice of Unsecured Loans in Commercial Banks

Finally the study concluded that on the loan recovery process, banks are used to taking legal actions against chronic defaulters of bank loans. The manager has a responsibility to fix an installment period on the basis of nature of their business. Institutional mechanisms have been developed to address the debt-recovery problem through judicial steps and early settlement of cases. Estimation of the loss given default should consider the potential influence of deteriorating economic conditions and in order to recover a non performing loan whether secured or not, a bank must first obtain a court order and most unsecured loans for bad credit do have their fair share of fees associated with them.
5.5 Recommendations

The study provides the recommendations for improvement and recommendations for further study as follows.

5.5.1 Recommendations for Improvement

5.5.1.1 Effect of Credit Approval Process as a Management Practice of Unsecured Loans in Commercial Banks

Commercial banks in Kenya should device and implement strategies to ease and ensure effectiveness of the credit reference checking process. The customer consultants assisting in the loan application process together with the credit managers should be keen on ensuring the completeness of the loan applications affecting the quality of applications processed and by extension the credit approval process which were the primary challenges in this management practice.

5.5.1.2 The Effect of Loan Portfolio as a Management Practice of Unsecured Loans in Commercial Banks

Commercial Banks should ensure that they have the right policies in place with regards to Unsecured Lending and to make sure that controls are in place to uphold these policies. Each Commercial Bank should have in place Credit management policies which include origination, approval, monitoring and recovery of the debt. Commercial Banks should review their Lending Policies from time to time in order to capture continuous changes in both the Money and Financial Markets.

5.5.1.3 The Effect of Loan Recovery Process as a Management Practice of Unsecured Loans in Commercial Banks

Central Bank of Kenya should also put in place strong guide lines and regulations to check unsecured lending by Commercial Banks so that banks do not go overboard and give more unsecured loans to their customers and non-customers that might become hard to recover and bring failure of some commercial banks in future. This will assure
Commercial Banks to continue enjoying the gains from Unsecured Lending and strong loan performance.

5.5.2 Recommendations for Further Study
The study examines the management practices of unsecured loans in banks in Kenya. The study recommends a study be done on the effects of unsecured lending on loan performance of commercial banks in Kenya.
REFERENCES


APPENDIX I: LETTER OF INTRODUCTION

RE: REQUEST TO COLLECT DATA

I am a student at United States International University pursuing a degree of Masters in Business Administration. Pursuant to the pre-requisite course work, I am currently conducting a research project on management practices of unsecured loans in banks in Kenya. The focus of my research will be on CFC Stanbic Bank Limited.

I kindly request you to participate in this study by assisting in filling the questionnaires and providing with any other relevant information. The information collected will be treated with utmost confidentiality and is for academic purpose only. The findings and recommendations of the research will be availed to you upon completion of the research. Thank you in advance.

Yours faithfully,

Naomi Muthee
APPENDIX II: QUESTIONNAIRE

Dear respondent this questionnaire aims to collect information on “management practices of unsecured loans in financial institutions in Kenya” CfC Stanbic Bank, Head Quarters. The information given is for academic purpose only and would be treated as very confidential. Please fill the questions by ticking on the boxes or provide opinion according to the question.

SECTION A: BACKGROUND INFORMATION

1. The Work Experience at CfC Stanbic bank
   1-4 years
   5-8 years
   9-12 years
   13-15 years
   15 and above

2. Highest Level of Education
   High school certificate
   College certificate/Diploma
   Undergraduate degree
   Post graduate qualification
   Others (specify)

3. Gender
   Male
   Female

4. Age of Respondents in years
   18-25 years
   26 - 33 years
   34 - 41 years
   42 and above years
5. SECTION B: Credit Approval Process in Management of Unsecured Loans

Please state the extent to which you agree or disagree with each of the following statements on the credit approval process in management of unsecured loans in banks. Where SD= strongly disagree, D =disagree, N= neutral, A= agree, SA= strongly agree

<table>
<thead>
<tr>
<th>Statement</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
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<tbody>
<tr>
<td>Incomplete applications and missing signatures are the primary challenges in credit application process.</td>
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<td>Effective Credit Risk Management system minimizes the credit risk.</td>
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<td>There is challenge in credit reference checking process.</td>
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<td>The summary section of the credit memo provides a high level overview of the request.</td>
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<td>The credit analyst takes all of the financial data that they have received and make an attempt to estimate the company’s ability to repay the loan.</td>
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<td>The length of the credit period is influenced by sometimes the Collateral value, the Unsecured loans and the size of the account.</td>
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<td>An unsecured loan is issued and supported only by the borrower's creditworthiness, rather than by some sort of collateral.</td>
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<td>Getting an unsecured loan can be more difficult than getting a secured loan if the borrower does not have an established or</td>
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good credit rating.

Loan size limits for new borrowers who do not have collateral can be kept small to mitigate the banks’ exposure.

### 6. SECTION C: Effect of Loan Portfolio management on unsecured loans in banks

Please state the extent to which you agree or disagree with each of the following statements on effect of loan portfolio in management of unsecured loans in banks. Where SD= strongly disagree, D =disagree, N= neutral, A= agree, SA= strongly agree

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<tr>
<th>Statement</th>
<th>SD</th>
<th>D</th>
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<tr>
<td>The Bank operates in a very challenging and evolving environment, which continues to shape the future portfolio risk profile</td>
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<td>Scenario analysis provides the credit offices with an assessment of developments in the Bank’s portfolio risk profile and measures taken to mitigate these risks in unsecured loans</td>
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<td>The Bank’s portfolio is vulnerable to any adverse developments in the risk profile</td>
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<td>The operating environment of the Bank portfolio has been volatile</td>
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<td>Management needs to remain vigilant and improve areas of portfolio management, risk mitigation measures and the institutional governance of unsecured loans</td>
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7. SECTION D: Loan Recovery Process in Management of Unsecured Loans

Please state the extent to which you agree or disagree with each of the following statements on the loan recovery process in management of unsecured loans in banks.

Where SD = strongly disagree, D = disagree, N = neutral, A = agree, SA = strongly agree

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<tr>
<th>Statement</th>
<th>SD</th>
<th>D</th>
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<tr>
<td>Loan amount is recovered on installment basis.</td>
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<td>The manager has a responsibility to fix an installment period on the basis of nature of their business.</td>
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<td>The banks are used to taking legal actions against chronic defaulters of bank-loans.</td>
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<td>The estimation of the loss given default should consider the potential influence of deteriorating economic conditions.</td>
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<td>If the loan is unsecured the bank must request that the court liquidate the firm assets</td>
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</table>
Thank you for your response

and distribute the proceeds from the liquidation among all the creditors.

Most unsecured loans for bad credit do have their fair share of fees associated with them.

Institutional mechanisms have been developed to address the debt-recovery problem through judicial steps and early settlement of cases.

Thank you for your response