

**RELATIONSHIP BETWEEN OPEN MEMBERSHIP POLICY AND LOAN
PERFORMANCE IN SELECTED DEPOSIT TAKING SACCOS IN MERU
COUNTY, KENYA**

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**A Thesis Submitted to the School of Business and Economics in Partial Fulfillment
for the Requirement of a Degree of Masters in Business Administration**

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DECLARATION

This thesis is my original work and has not been presented for a degree or any other award in any other University.

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DEDICATION

This work is dedicated to my spouse Mutethia and my son Max for their love, moral support, encouragement, understanding and sacrifice

ACKNOWLEDGEMENT

I wish to thank God for the gift of life and good health through the thesis period. Gratitude also goes to my supervisors Dr Benard Baimwera and Mr Moses Muriuki for their great support, advice and encouragement through the thesis from the beginning to the end. The University Librarian for his undying effort on guiding me through referencing and formatting the thesis to conform to the university standards. Friends and classmates for their encouragement and finally to my entire family for their support in prayer and material things.

ABSTRACT

Open membership policy can be a contributory factor when it comes to loan performance in SACCOs and improvement of the same. Taking into consideration opening the bond to outsiders and allowing them to becoming members of SACCO's even if they do not belong to such a community would increase the share capital volume, loan application volume, interest grown on loans and credit worthiness is also boosted. The study was motivated by the competition in the financial institutions and since SACCOs fall under this category, there was need to find possible ways and strategies that would make them remain in the competitive market while at the same time have improved performance. The purpose of the study was therefore to examine the relationship between open membership policy and loan performance in selected deposit taking SACCO's in Meru County. The research objectives were to establish how financial risk contributes to loan performance in selected SACCOs deposit taking in Meru County, to establish how repayment period contribute to loan performance in selected deposit taking SACCOs in Meru County, to determine how loan security policy contributes to loan performance in selected deposit taking SACCOs in Meru County and to determine how loan processing period contributes to loan performance in selected deposit taking SACCOs in Meru County. The theories underpinning the study were agency theory, asymmetric information theory and loanable fund theory. The study adopted a descriptive research design and primary data was collected from the respondents while secondary data was retrieved from the published data. The researcher used questionnaire as the data collection instrument. The population of the study was seventy nine respondents from the selected deposit taking SACCO's in Meru County. The study adopted a census where all the elements in the population were examined. A pilot study was conducted to establish the validity and reliability of the research instruments. The collected data was analyzed using SPSS and further explained using descriptive statistics to enhance understanding thereafter presented in descriptive tables. Multiple linear regression was used to test the relationship between the variables in the study. The study has established that all the open membership policies including Financial Risk Policy, Loan Repayment Period, Loan Security Requirement and Loan Processing Period when regressed severally against loan performance have significant effect. Joint regression of all the open membership policies with loan performance reveals that only Loan Processing Period failed to have a significant effect on loan performance. The study therefore concluded that all the four variables had a significant relationship with the dependent variable and further recommended that SACCOs should put an emphasis on all the variables in the study among other factors to aid in the improvement of loan performance while at the same time having policies that enhance the performance of loans in the deposit taking SACCOs.

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LIST OF ABBREVIATIONS

FSD	Financial Sector Deepening
KUSCCO	Kenya Union of Savings and Credit Co-operatives
MMH	Maua Methodist Hospital
SACCO	Savings and Credit Cooperative
SASRA	Sacco Societies Regulatory Authority
SPSS	Statistical Package for Social Science
WCCU	World Council of Credit Unions

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Since the establishment of SACCOs the main aim was to ensure subscribed members in various SACCOs benefit through savings and credit. This means that, if one is not a subscriber they could not enjoy the services offered. This over time has raised debates and concerns due to the stiff competition in the financial markets to date. SACCO membership is based on a common bond, a linkage shared by savers and borrowers who belong to specific community, organization, place of employment or people conducting the same form of business (Ombado, 2011). A Savings and Credit Cooperative is a type of cooperative whose objective is to pool savings for the members and in turn provide them with credit facilities (Okwany, 2010). The general objective of SACCOs is to promote the economic interests and general welfare of its members.

The first industrialized SACCOs were in Great Britain and France in the 1840s with the aim of promoting working class families in the face of the social disasters caused by industrial revolution. The second generation of the pioneers of modern cooperation emerged, in certain European rural environments in the late 19th century (Amiry, 2013). In the 1860s, these pioneers created the models of agricultural cooperatives and savings and credit cooperatives inspired by the success of the consumer cooperatives formula in Great Britain and based on old traditions of rural solidarity aimed to meet the primary economic needs, which went unsatisfied. Agricultural cooperatives then

enabled families of farmers and livestock raisers to organize their own supply systems of agricultural inputs and market their products and no longer depended on merchants and business men in the cities. The SACCOs helped them to stop depending on moneylenders and to find the credit necessary to modernize their agricultural cooperatives (Mwakajumilo, 2011).

In Africa, SACCO idea was brought about by a Roman Catholic priest, in Jirapa, a town in Ghana, in 1955. Alila and Obado (1990) states that Father John McNulty from Ireland had studied in Canada where he learnt about savings and credit co-operative societies. He helped the Jirapa villagers to form a Savings and Credit Co-operative. The co-operative assisted the members to address their financial problems that which they could not individually. Further he trained about 60 people, who were the first successful savings and credit co-operative pioneers on the African continent. The success of Jirapa savings and credit co-operative spread throughout Ghana and by 1968, the savings and credit co-operatives throughout the country came together to form the Credit Union of Ghana , which was set up to promote, organize, service and co-ordinate the activities of savings and credit co-operative in Ghana. (Atola&Oduor, 2017).

According to Kivuvo&Olweny, (2014) in a report by World Council of Credit Unions (WOCCU) 2012 statistical report, there were an estimate of 51,013 credit unions in the world, with a total of 196,498,738 members and a total penetration of 7.8% Penetration rate which is calculated by dividing the total number of reported credit union members by the economically active population age 15-64 years old. The largest markets in Africa by number of members as of December 31st 2012 are Kenya (4,183,220),

Senegal (2,231,117), Ivory Coast (1,705,712), and Benin (1,597,233) (WOCCU, 2012). All of these SACCO's had no open membership policy to everyone.

SACCOs in Kenya are currently among the leading sources of the co-operative credit for socio-economic development (Gachuhi,2015). Cooperatives in Kenya were started in 1908 and membership was limited to white colonial settlers. The first cooperative was established at Lumbwa, present day Kipkelion area. In 1944 colonial officers allowed Africans to form and join cooperatives (Tshishonga&Okem, 2016). The initial attempt to encourage African farming co-operatives was initiated by the need to implement the recommendations of the 'Swynnerton Plan' of 1953. The Swynnerton Plan was formulated to improve African farming, specifically the growing of cash crops and is recorded to have encouraged the progress and growth of African cooperatives (Atola&Oduor, 2017).

It was at this point that the recommendation for appointment of a registrar of cooperatives was made. A new cooperative society's ordinance that allowed Africans to participate in the Cooperative movement was enacted in 1945. In 1946, it happened that a registrar of cooperatives was appointed to head the department. By 1950 most colonial civil servants embraced the idea of cooperatives development which led to the registration of about 160 cooperatives by 1952 (Tshishonga&Okem, 2016). The post-independence era saw the rapid increase in the number of producer organizations and consolidation of the ones that already existed. At this time, the government saw the cooperative movement as a means for African socialism, and strengthening common

ties between the people from different regions of Kenya. Since 1963 there were about 1000 cooperatives, which rapidly grew in number since then to present.

Today, the co-operatives are an integral part of the Government economic strategy aimed at creating income-generating opportunities particularly in the rural areas. The Government has recognized the cooperatives as a vital institution for the mobilization of human and material resources for various development progress especially in the rural areas where the majority of people earn their livelihood mainly from agriculture. On estimate, at least one out of every two Kenyans derives their living from the cooperative movements and the cooperative movements contribute over 45% of Kenya's economy.

Over the years, the co-operative movement remained predominantly agriculturally oriented. However, over time to present, cooperatives have undergone significant diversification and growth and ventured into savings and credit. Other non-agro-based co-operatives have also emerged and ventured into areas such as housing; Jua-Kali, building and construction, handicrafts, transport and small scale industries (Wanyama 2014). SACCOs are one of the leading sources of rural finance and in many rural areas, the local SACCO is the only provider of financial services. While the exact number of SACCOs operating in Kenya is not known, estimates states that Kenya has over 19,600 registered corporative SACCO's (SASRA, 2013). However most SACCOs have not embraced open membership policy and this could be a limiting factor when it comes to loan performance. Opening membership would increase share capital thus increasing the amount of loans taken by members leading to better performance in terms of interests.

1.1.2 Open Membership Policy

Open membership policy in SACCO's allows people who are not in the common bond to join the SACCO and become members of the SACCO (Osoro&Ogeto, 2014). He continues to state that SACCOs over time have been operating under common bond membership where they only allow members from a particular community to join, people who share the same business, people who work for the same organization or people who have the same products. Open membership policy would allow people from outside to join even if they do not share the same business, organization, products or even do not come from the same community as long as they have the capacity to become members and agree to the terms and conditions (Minhas&Remmer, 2015). This would in turn increase the customer volume and it is the customers that take the loans in the SACCO. This would therefore see to the growth of the volumes of loans applied by the customers thus good performance in terms of the returns through the interest earned from the loans. Opening membership to everyone who can be able to meet the terms and conditions of the SACCO would contribute to customer growth and SACCO growth in terms of deposits which translates to greater loan volumes which will be taken by the customers. This is done through putting into consideration the financial risks associated with such huge lending bearing in mind that if it works the returns would be considerable (Duffie& Singleton, 2012). When the number of customers is increased through open membership policy, it means that the savings will grow thus more capital which will shorten the loan processing period as there will be ready money for disbursement.

1.1.3 Loan Performance

Loan performance can be looked at in various ways including loan being paid effectively and efficiently putting into consideration the stipulated time, loan being paid without default, loan issued to customers growing in volume and also the processing period of loans shortened meaning money to disburse to the applicants is readily available (Schmidt & Cohen, 2015). Loan performance can be measured through the number of loan applications, loan interest, and the loan amounts applied for. Performing loans are the assets that are currently generating income in an organization (Van, *et.al.*, 2011). According to CBK (2009), loan performance refers to that loan which is serviced without delay and without fail and the correct amount. Performing loans has seen to the growth of SACCO's in Kenya and across since the profits are used as assets that contribute to credibility of SACCO's (Oloo, 2011). Therefore SACCO's should try to device measures that should help their clients use the loans given for the intended purpose to ensure they are able to pay back effectively. This will see to the growth of the SACCO's and also retain their customers meaning ready market throughout.

1.1.4 SACCO's in Kenya

The savings and credit cooperatives have in a great way contributed to the growth of the economy of Kenya in that it has improved the livelihood of low-income earners. They enable their customers to save at high interests and borrow at very low interest rates. This has seen to the tremendous growth of SACCOs over the recent past with the regulating body for SACCOs SASRA giving a report that they have registered over 73 deposit taking SACCO's. SACCO's are expected to give periodic reports of their operations and the services they offer range from front office operation to taking

deposits and giving credit to the clients (Standard Financial Report, 2013). Kenya is the largest sub-sector in Africa with over 19,600 cooperative societies, where 10,000 of these are savings and credit cooperatives and over 14 million members which represents 33% of the Kenyan total population (SASRA, 2013).

Through advancement of credit to members, SACCO play a significant role in fighting poverty and creating job opportunities to citizens impacting on the economy in terms of growth. In Kenya there are deposit taking and non-deposit taking SACCO societies and they play different roles. According to Jagongo and Kinyua (2013), deposit taking SACCOs comprise of those SACCOs that have both withdrawable and non-withdrawable deposits. Odhiambo (2014) on the other Hand states that non deposit taking SACCO's comprise of the SACCO's whose business is limited to deposit mobilization and the deposits are not withdrawn but used as loan collateral and can only be withdrawn upon seizing SACCO membership.

In Meru County the number of SACCOs has grown over time leading to stiff competition and also affecting performance of loans in a great way (SASRA, 2017). This means that most of the SACCOs are struggling to survive and others consider closing down since they cannot sustain their employees and pay for their residence. SACCOs in Meru County have considered various ways to try and improve their loan performance but still challenges have persisted. They have tried to encourage members to form groups to help them qualify for loans and also for easier repayment but this has proven not to be the solution to the loan performance problem (Kiringa, *et al.*, 2017). This is so because cases of loan defaults in Meru County have become higher up to 48% since members relax and leave the group members to pay the loans for them. Maina,

Muturi&Oluoch(2018) in their study on non- performing loans in cooperatives realized that cooperatives were not able to totally cover the market well leading to reduced number of loans applied for while on the other hand leading to poor loan performance for the already issued loans since they do not try new avenues which could be through open membership policy in the effort to try and capture the whole market.

1.2 Statement of the Problem

SACCOs provide a wide range of products as compared to other financial institutions starting from loan offering at a cheaper rate as compared to banks, their interest on savings is also high leading to a high population of Kenyans not having bank accounts but go to SACCOs (Fin Access, 2009).

There is untapped market whereby in terms of loan lending and customer subscription, up to 48% of Kenyans do not have accounts whether in banks or SACCOs (UK Essays, 2018). Most SACCOs do not have open membership policy where anyone is free to join as long as they can be able to deposit savings and have the minimum requirements in terms of share capital thus the performance on their loans stagnates or in some cases go down due to the competition in the market. The level of risk SACCO's are willing to take in terms of financing determines the level of gain realized. Currently, loan performance has gotten poor over time in Meru County with up to 48% in loan defaults since many SACCO's are too cautious on the level of financial risk associated looking at factors like repayment period and the security policy in place. This in turns leads to queuing in loan processing as they take time to evaluate the repayment power and risk

attached if a collateral is not present or the guarantors do not have the capacity to cover the loans thus needs change or revision (Adhiambo, 2015; Kiringa, *et al.*, 2017).

A study carried out by Eric, *et al.*, (2018) sought to find the effects of Non- Performing loans Management practices on loan recovery performance of deposit taking savings and credit cooperatives in Kenya and found out that the one of the limiting factors was the fact that SACCOs never had open membership policy which would allow them to grow their share capital and deposit which would lead to a positive curve on the performance of loans. Therefore, this study will attempt to fill the gap of knowledge and find out the relationship between open membership policy and loan performance in selected SACCOs in Meru County.

1.3 Purpose of the Study

The purpose of the study was to find out if there is a significant relationship between open membership policy and loan performance in selected deposit taking Sacco's in Meru County.

1.4 General Objective

To investigate the relationship between open membership policy and loan performance in selected deposit taking SACCOs in Meru County.

1.4.1 Specific Objectives

Below were the specific objectives

- i. To assess how financial risk policy under open membership affects loan performance in selected deposit taking SACCOs in Meru County

- ii. To determine how loan repayment period under open membership affects the loan performance in selected deposit taking SACCOs in Meru County
- iii. To determine how loan security requirement under open membership contributes to loan performance in selected deposit taking SACCOs in Meru County
- iv. To determine how loan processing period under open membership contributes to loan performance in selected deposit taking SACCOs in Meru County.

1.5 Research Hypotheses

Below were the research hypotheses

H₀₁: There is no significant relationship between financial risk and loan performance in selected deposit taking SACCOs in Meru County

H₀₂: There is no significant relationship between repayment period and loan performance in selected deposit taking SACCOs in Meru County

H₀₃: There is no significant relationship between loan security and loan performance in selected deposit taking SACCOs in Meru County

H₀₄: There is no significant relationship between loan processing period and loan performance in selected deposit taking SACCOs in Meru County.

1.6 Justification of the Study

The study was of important to the loan lending institutions as they will be able to know the level of financial risks they can take when giving out loans. The study was of importance to SACCOs since they will be able to know the type of people to accept when considering open membership. Lending institutions will also benefit from the study since they will be able to know when a loan is performing. The policy makers will

also be able to know the qualifications to set for the prospective members and finally the higher institutions of learning can use this as a learning tool for future scholars.

1.7 Scope of the Study

The study was carried out in selected SACCOs in Meru County and it targeted the loan sales officers, loans collection officers and credit analysts in charge of loans section in the respective SACCOs. The respondents were selected purposively since they are in a better position to give the intended information since they deal directly with the loans and are the custodians of the required information. Questionnaires were used to establish the current position on loan performance in the respective deposit taking SACCOs.

1.8 Limitation of the Study

Loan monitoring as soon as it is disbursed is a challenge that SACCOs have not yet been able to address fully and this can be countered through having monitoring plans that are made known to the clients too. The topic of open membership was not be clear to all the respondents thus it was equally important to do an introduction of the same before administering the questionnaire. Respondents were not be willing to disclose all the information due to fear it is an investigation and to counter this, it was important for the researcher to have an introductory letter to show that they were students and that they were carrying out the study for academic purpose only.

1.9 Significance of the Study

By the end of this study, SACCOs are able to embrace best practices and policies that would allow open membership policy thus seeing to the growth of SACCOs and also

having performing loans. If members are made aware of the policies before joining the SACCOs then they are aware from the word go what is expected of them therefore reducing the level of nonperforming loans. The study should also enlighten the public on the importance of belonging to a SACCO. The government will also be able to adjust the policies for bodies governing the SACCOs and finally the SACCO regulating body SASRA will be able to come up with accommodative policies for the SACCOs.

1.10 Assumptions of the Study

The study assumes that the information given by the respondents was true to the best of their knowledge and had no alterations. It also assumes that the information that was given was not fabricated and that the information was used in data analysis.

1.11 Operational Definition of Terms

Loan Performance: Loan performance can be looked at in various ways including loan being paid effectively and efficiently putting into consideration the stipulated time, loan being paid without default, loan issued to customers growing in volume and also the processing period of loans shortened meaning money to disburse to the applicants is readily available (Jared, 2013). While assessing the progress of the SACCO, performing loans is an indication that the SACCO is moving towards the preferred direction and a sign that operations are in agreement with the overall objective of the SACCO.

Open Membership policy: Open membership policy in Sacco's allows people who are not in the common bond to join the Sacco and become members of the SACCO (Osoro, 2014). Therefore in the study, SACCOs considering open membership would be a recommendation among other factors to enhance performance of loans in the SACCO.

Financial Risk: Financial risk is any of various types of risk associated with financing, including financial transactions that include company loans in risk of default (Greuning, 2012). Having a working financial risk policy in the SACCO helps a lot in handling the risks associated with credit which helps the organization in dealing with cases that may arise from credit.

Repayment period: The period when no advances of principal are available and during which the line must be fully repaid (Chege, 2013). Loan repayment period should be set considering the type of clients and also in line with the SACCO policy to ensure it is sufficient in relation to factors like loan amounts, security offered, mode of payment and the income of individuals for effectiveness and efficiency in loan repayment.

Loan Security: This is a property or other asset that a borrower offers as a way for a lender to secure the loan (Kilonzi, 2014). Security offered for loans taken should be properly verified and the supporting documents availed before disbursement of loans and those securities that need physical viewing should be viewed and verified before loans are issued. This is for the purpose of ensuring that in the event of loan default, the SACCO has certainty for money recovery through sale of the security offered to ensure that loans are performing.

Loan Processing Period: This is the time taken since the interest to apply for a loan is declared to the loan disbursement date (Odhiambo, 2015). It is important for SACCOs to shorten the waiting period between compliance to the requirements for a loan and the disbursement date as most loans are applied with intended purpose and institutions that take too long to process loans in most cases are not preferred by clients.

If the processing period is shortened then the performance of loans tend to improve as the loan volumes increase.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter covered the theoretical review that contains the theories underpinning the study and the empirical review on the following variables, open membership policy, financial risk, repayment period, loan security, loan processing period and their relationship with loan performance.

2.2 Theoretical Foundation of the Study

When we talk of open membership policy in SACCO, the introduction of non-bond members to SACCOs is the first thing that comes into one's mind. Therefore, this section looked at the theories that underpin the study. It expounded on how these theories helped in determining the relationship between the policies that allow members outside the bond to become members of the respective SACCOs and loan performance in the SACCOs and link the theories to the study variables as well.

2.2.1 Agency Theory

The agency theory was developed by Mitnick and Barry (1973) and they were trying to look at decision variations in relation to the principal and the agent within the members of a particular group. The theory was also interested in looking at the differences that exist between the two parties, which are caused by unclear goals. It continues to explain that the principle where in this case is the SACCO and the agent in this case the credit analysts do not look at issues from the same perspective and also may be having different goals leading to differences. This is so since the

predetermined goals have different impact on different individuals thus the diverse kind of results. An agent acts as a link between the principal and the members thus the information they give to the members is going to yield the results.

According to Odhiambo (2012), different individuals have different conception in relation to the given goals. It is always very important for the principal to identify an agent very cautiously to ensure that their goals are almost aligned as opposed to one with very diverse goals and interests. This is important since principals depend on the agents in the running of the day to day events and operations and if the goals are not aligned then there can never be realization of the expected results. The motivation levels differ from one individual to the other thus yielding to different results. This means that individuals will execute the duties to the best of their interest to the expense of the organizational goals. The actions of the agent could determine largely the overall outcome since they are the key players acting between the principal and the consumer. The theory also continues to argue that employees at all levels are held responsible for their actions as they act on behalf of the principle (Mitnick, 2015). This means that employees would put forth their best foot in ensuring achievement of the overall organizational goals.

The theory is relevant in this study since SACCOs have employed agents who see to the issuance of loans to customers, they also ensure customers subscription to the SACCO, they also ensure that the policies and regulations are well known to the clients before they join the SACCOs and also share information on loans. The agents are also responsible for ensuring the clients have the necessary loan security putting into consideration the financial risks associated while on the other hand ensuring the

loans are processed within the stipulated period of time to ensure they do not lose the customers to the competitors. This therefore would lead to recruitment of the members who meet the criteria thus improved loan performance in the respective SACCOs.

2.2.2 Asymmetric information theory

The asymmetric information theory was developed by George, Joseph and Michael (1970) where they sought to explain the effect of having two agents where one agent has more information than the other giving them some added advantage. This also extend to the members also where they may seem to have more information than their fellow members or even that the agents themselves. Mokaya and Kipyegon(2014), states that separating a good borrower from a bad borrower is the biggest challenge in most situations since in the first instance almost everybody seems genuine until the loan is issued and payment commences. By the virtue of members having more information about the lenders, it could mean more subscribers if the information is good while on the other hand, If the information is negative it means ruining the organization in the sense that even the members who had subscribed would tend to leave while discouraging others not to join. The number of the subscribed members would in turn make a significance difference in the performance of an organization in whatever perspective.

Due to this uncertainty, lending institutions should ensure they gather enough information on the customers past financial history while considering the financial risks associated with the same (Okundi, 2015). It is also important to have relevant information on the finger tips as an organization to ensure that your clients do not

outsmart you in the process thus lead to loss of monies as some mistakes while dealing with money may cost the organization a fortune. The theory is significant to the study in that it will help the agents to be more keen and aware of the kind of members to enroll and trust when it comes to giving of loans since they could be able to monitor and have more information about the borrowers. It could also help the agents to be more assertive and want to gather as much information as possible about the borrowers before they could process a loan.

2.2.3 Loanable Funds theory

According to Dennis Roberston (1937) and neo-classical economists the price or the rate of interest is determined by the demand for and supply of loanable funds. The market for loanable funds consists of arrangements and procedures to carry out transactions between people who want to borrow money and people who want to lend money. According to this theory, rate of interest is determined by the demand for and supply of loanable funds. In this regard this theory is more realistic and broader than the classical theory of interest (MacLachlan, 2005). In a business set up there has to be the party willing to give and another one willing to take. This theory exists for the purpose of explaining transactions that occur between the borrower and the lender to be able to balance the demand and supply for money.

The theory continues to argue that people are interested in short term gains as opposed to organizations that focus on long term goals (MacLachlan, 2005). The theory also explains how people are more attracted to short term gains and risk the opportunity to lose the long term gain. This could be seen in the amount of interest one pays as they

enjoy the easy come money given by the SACCOs without necessarily looking at how much they could save if they considered another option that is cheaper though not too fast to acquire. Most Saccos if not all give instant funds to their customers without necessarily asking for many requirements and they also try not to have longer waiting periods as the loan is being processed. This theory is relevant to this study since it shows how interest is accrued for the Saccos as well as indicating the demand and supply curves in the Saccos. Through the borrowing and payment behavior of customers, Saccos are able to predict the level of income as well as interest.

2.3 Empirical Review

2.3.1 Financial Risk and Loan Performance

An evaluation done by Kenneth (2017) on the impact of credit risk and the profitability of banks in Nigeria concluded that profitability in the banks was significantly influenced by the risk management procedures. It was evident that the procedures laid down in the financial risk policy were not being fully implemented thus posting poor loan performances. Further it was concluded that the non-performing loans, customer deposits and the amounts of loans and advances contributed a lot in the profit margins in the banks. This would therefore mean that the higher the financial risk the higher the expected profitability of the financial institutions. The risk management procedures in place should have a recovery mechanism in place. The study also concluded that some SACCOs were not able to follow the guidelines towards the recovery in the event of default thus delayed recovery or loss of funds. Full and proper implementation of the procedures will help the SACCOs deal with any upcoming losses and also on the other

hand, the wide risk will earn returns that could cover up for any un avoidable losses suffered by the organization.

Epure (2012) did a study on bank performance in Costa Rican banking industry in comparison to the risk associated and came to a conclusion that the existing regulations on financial risk to a great extent influenced the overall bank performance. The study further found out that the net interest margin is influenced by capital adequacy and the loans that are not performing impact negatively on the return on asset and efficiency. This would mean that proper financial risk measures if implemented as per the policy would contribute greatly to financial performance. On the other hand it is very critical to have a working financial risk policy which takes care of the possible risks that may occur. Lack of a working financial risk may lead to poor loan performance since all the foreseeable risks should be accounted for even before loans are issued to the members. This takes care of bad debts and losses that occur as a result of credit.

According to a study conducted by Al-Khoury (2011) on the impact of specific risk characteristics in banks and the overall performance of the banks operating in six of the Gulf Cooperation Council countries, the conclusion revealed some aspects that contributed to the overall performance. These factors included liquidity risk, credit risk and capital risk. While performance is achieved through various variables and parameters, the study put more emphasis on the above three as they form the larger fraction of performance in the financial institutions. The study also established that Most of the SACCOs did not have provisions for these risks thus putting them at risk of losing funds. The study continued to state that profitability measured by return on equity is majorly affected by liquidity risk. All these aspects form the financial risk

aspect in a financial institution thus if well strategized could contribute to the overall performance.

2.3.2 Repayment Period and Loan Performance

A study carried out on the determinants of loan repayment period and loan performance in Addis credit and savings institution Addis Ababa in Ethiopia, concluded that most of the credit consumers were unable to cope with the strict repayment periods that were set by the institution arguing that the period was too short and people could not be able to take huge amounts since the servicing period was not sufficient enough (Reta, 2012). The study further noted that SACCOs were not flexible so as to consider adjustment of the loan repayment periods in relation to loan amounts taken. There was need for SACCOs to set realistic loan repayment periods that would enable for the customers to service their loans without extreme Struggle to reduce cases of loan defaults and non-performance of loans. Further it seemed that those who needed huge loans diverted to other lending institutions who could offer more flexible repayment periods and terms thus the SACCO lost in terms of loan volumes thus poor loan performance. The study continued to state that the institutions were not flexible enough to ensure they are able to incorporate most of the credit consumers that improving their loan performance.

According to a research conducted by Walsh (2013) on the relationship between loan repayment period and loan default in Saccos, it concluded that members are to some extent discouraged by the repayment period which they consider short thus the temptation of salary diversion and commitment to other loans. Short loan repayment

periods tend to have high monthly installments that become a burden to the clients who in most cases earn very little to be able to service the loans. If the members are not able to meet their loan obligations then they end up defaulting the loans thus poor performance of SACCOs in terms of loans. This in return contributes to loan defaults which make the SACCOs shy away from issuing more loans to new clients for the fear of losing more finances thus poor loan performance in the SACCOs and it is always said that the higher the risk the higher the returns. Adjustment of the repayment period eliminates the crisis of non-performing loans thus good financial records and the credit worthiness of the SACCO as well as the borrowers. It also concludes that borrowers do not exercise financial discipline thus divert the loan purpose contributing to loan defaults.

Streams (2012) did an analysis on borrower repayment capacity and loan repayment in banks and concluded that the ability of a loan to perform greatly lies in the borrower's ability to pay. Thus the ability to repay loans can be affected by short loan repayment periods since the shorter the period, the higher the installments per month. If the loans are spread out over longer periods of time then it means that the installments will be smaller thus encourage the clients to pay as they look at the amount as small and get the motivation to pay. Further, concluded that a proper and comprehensive assessment of potential borrower should be done to ascertain the capacity to pay back the loan once given. This ensures that loans are paid effectively and efficiently with minimal or no hardship thus improved loan performance. The assessment would therefore enable selection of the most promising borrower and reduce the risk associated with the same.

2.3.3 Loan Security and Loan Performance

Njiru (2018) conducted a study in coffee cooperative societies in Embu district on loan security and credit risk and concluded that members had multiple subscriptions in various cooperatives within the same locality and used the same collateral as security. This therefore had implications when it came to repayment of the loans since there was not much income from the same for them to be able to service their loan leading to default which in turn led to poor loan performance in the respective cooperatives. Information search would have served a great deal in ensuring that duplication of these procedures was not there where one member was given loans by different cooperatives within the same locality with a common collateral. This also means that SACCOs should have a policy that allows for information sharing among the financial institutions to reduce the chances of having one collateral for multiple institutions and also reduce the risk of overfunding members thus they are unable to meet their obligations most especially if they fail to channel their acquired loans to activities that will generate more income to be able to repay the loans.

Omino (2014) in a study on borrower characteristics and loan default trends observed that in some cases the characteristics that borrowers have to some extent contributed to the cases of loan default if the borrower is not willing to pay even if they have the money. On the other hand, the borrower could be influenced by the lender characteristic which could stimulate the borrower towards payment of the loan or pull them away to not paying the loan. Studying the borrower characteristics and personality are key towards trying to understand the payment commitment without forgetting to look at the borrower's history. Giving loans to people with poor loan records would mean loan insecurity which would lead to poor loan performance. The borrower characteristics

differ from one person to the other as each individual possesses different characteristics. This too can be achieved through assessment of individual past records and having more time to interact and study the attitudes of the client. It is a grave mistake to judge a client just by the looks since financial matters are very sensitive and should be handled with a lot of caution. This time taken to understand the individual characteristics would reveal some characteristics that show whether one should be given a loan or not and also disclose the ability and intention to repay the loan to avoid loan default leading to poor loan performance.

Chaplin (2012) in a study on credit worthiness and loan performance and found out that policies and guidelines on the loans is an important tool toward enhancing loan security. There was need to emphasize on background check of the clients before entrusting them with loans. This check is for the purpose of ensuring that the client is worth the amount they are applying for. Giving loans to members before you understand their worth may lead to loan default as they may not have the capacity to repay back the monies given to them leading to default and poor loan performance. The ability of the borrower to comply to the loan guidelines greatly contribute to loan performance while on the other hand the lender should also play their part in ensuring they also comply and follow the set rules and guidelines on the same. This is important in the case of irregularities where written proof on the procedures could be produced thus help in ascertaining the due cause. This would also help reducing blames between the borrower and the lender and also be able to attach the parties' responsibilities.

2.3.4 Loan Processing Period and Loan Performance

HSBC Mortgages (2010) in their analysis on banks in Japan states that the process of acquiring loans from financial institutions is tedious and very complicated that people shy away from applying for loans considering the volume of documents requested for and the period taken for verification of the same. The process could also be discontinued not because the borrower does not have the capacity to pay but because the banks feel that the borrower has not filled the prequalification forms for the loans correctly. In some instances, lending institutions may request for unnecessarily too many documents that are tedious to acquire and this puts off many potential clients. In the event one is in dire need for funding, then they are interested in the institution that will speed up the processing period of the loans as opposed to those institutions that take too long to process the loans even after all the requirements are availed. The period taken between loan application attempt and loan disbursement becomes too long that to some extent the deadlines for the borrowers need is overtaken by the process.

Hoffmann (2017) analyzed a financial report by the sunflower producers (2006) and established that the SACCO needed to adopt some aspects that were not given much emphasis such as time taken to offer services to the customers and have in place systems that are user friendly for example in terms of customer reports generation. Some SACCOs had a very long waiting period even before one could get a simple report or a statement of account and this discouraged many from becoming members. It continued to state that most SACCOs took a very long time before verification of the customer requests and requirements before they could consider issuing loans to customers. A recommendation to speed up the loan processing period was given to help SACCOs capture as many clients for their loan services which in turns would

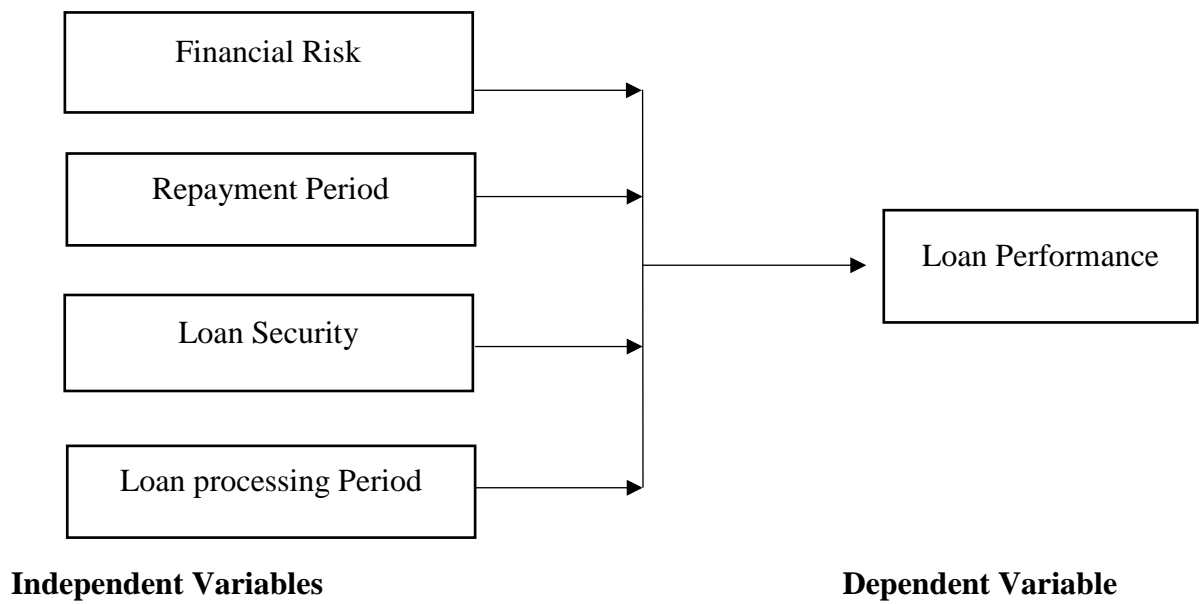
improve on their performance. This aimed at helping in speeding the customer service and also ensures timely processing of requests for the customers. This on the other hand would ensure the competitors do not take larger market share and throw you out of the market while on the other hand ensuring overall performance.

A study conducted by Otieno (2014) on factors affecting loan performance in SACCOs in Kenya established that the operational efficiency greatly affected loan performance in such a way that most SACCOs lost their customers to the institutions that had an efficient system that could handle customer requests in a timely and most convenient manner. The study further identified that SACCOs did not have clear policies and guidelines ready for implementation in relation to the time taken between application of loans and disbursements as long as the clients have met all the requirements. It was also noted that some SACCOs had poor record tracking systems such that they were not able to establish the sequence in which the loan applications came in to the SACCO. Having a clear sequence system would ensure that at least the loans are disbursed in the manner of booking into the system, this way customer complaints are reduced and work runs efficiently thus improving the loan performance as most customers will be more satisfied meaning more business. Institution with efficient operational systems would enjoy customer loyalty and increased returns over and over again. This efficiency is institution based where they adapt to the best fitting systems that favors most customers and the institution as well.

2.4 Conceptual Framework

Figure 2.1

Conceptual Framework



2.4.1 Explanation of Variables

The framework explains the relationship that is there between the dependent and independent variables.

2.4.2 Financial Risk

Financial risk is any of various types of risk associated with financing, including financial transactions that include company loans in risk of default. This would therefore mean that organizations should be able to evaluate all the risks associated with the issuance of loans and try to put corrective measures to ensure they do not unnecessarily lose funds to non-performing loans (Greuning, 2012).

2.4.3 Repayment Period

The period when no advances of principal are available and during which the loan must be fully repaid meaning that the repayment period should be sufficient enough in relation to the loan amount and customer capabilities and also considering the loan policy that should be made clear to the clients before loans are issued (Chege, 2013).

2.4.4 Loan Security

This is a property or other asset that a borrower offers as a way for a lender to secure the loan. It is therefore very important for the lending institution to ensure that the borrower has the capacity to repay the loan with an alternative security in case they are not able to efficiently service the loan. It is also very important to verify the security issued to ensure it belongs to the customer applying for the loans and also the accessibility and value of the same (Kilonzi, 2014).

2.4.5 Loan Processing Period

This is the time taken since the interest to apply for a loan is declared to the loan disbursement date. Meaning if the period is too long then the applicants will be discouraged and may move to other institutions who may be having a shortened loan processing period thus poor loan performance (Odhiambo,2015).

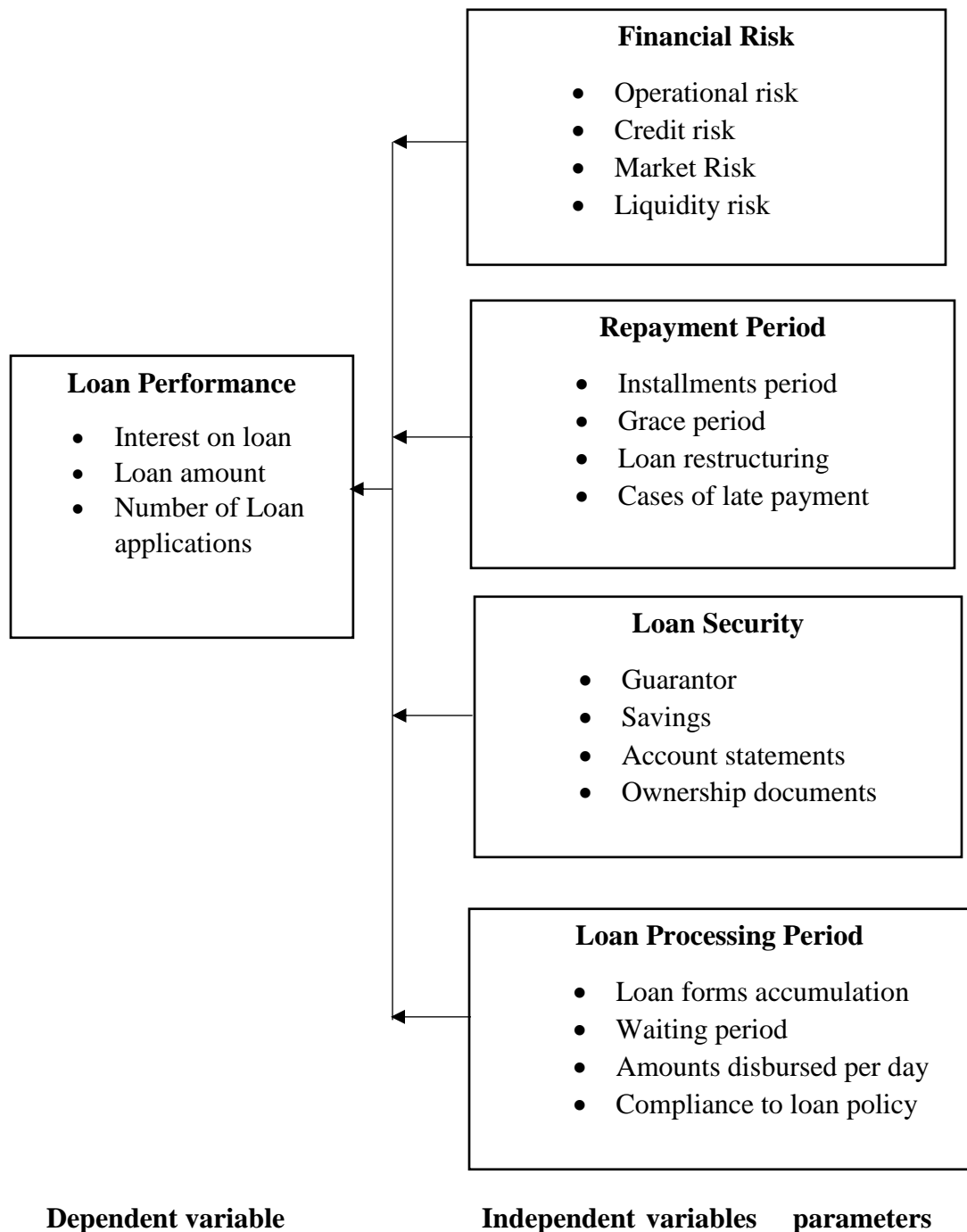
2.4.6 Loan Performance

Loan performance can be looked at in various ways including loan being paid effectively and efficiently putting into consideration the stipulated time, loan being paid without default, loan issued to customers growing in volume and also the processing period of loans shortened meaning money to disburse to the applicants is readily available. If proper policies are put in place then it means that the performance will always keep on improving (Jared, 2013).

2.5 Operational Framework

Figure 2.2.

Operational Framework



2.6 Summary of Literature and Gaps

Studies have been done revolving around loan performance in SACCOs and other variables but the studies were not conclusive to state a universal variable that influence loan performance in the SACCOs. An evaluation on credit risk and profitability in banks revealed that the key influencing factor is risk management procedures, capital risk and liquidity risk. Other studies revealed that poor loan performance was due to the inability of customers to cope with the strict repayment period, short repayment period leading to salary and income diversion to other facilitators, lack of financial discipline and lack of proper assessment of potential borrowers before the loans are given. Studies on loan security and performance concluded that multiple subscriptions offering the same collateral by the same people contribute towards poor loan performance, borrowers characteristics also contributes to loan performance through the trend in loan repayment and loan policies and guidelines in a big way contribute to loan performance if the borrowers are able to comply.

The loan processing period in some financial institutions take too long thus the borrowers shy away from engaging in the process and operational efficiency in the Saccos influenced the customer volumes and the loan volumes as well. There being numerous studies that have been carried out on loan performance and other variables Banks and SACCOs, there has not been one that has been carried to establish the relationship between open membership policy and loan performance in SACCOs and more specifically in Meru county. Therefore this study will attempt to fill the gap of knowledge and attempt to answer the question of the relationship between open membership policy and loan performance in SACCOs

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The chapter describes the methodology that was used in conducting the study. It describes the research design, target population, sampling design, data collection and analysis methods.

3.2 Research Design

The study adopted a descriptive research design. Descriptive research design allowed representation of the entire population by the sample selected with the findings applied to the entire population. According to Mugenda (2003), descriptive research design defines a subject, often by creating a profile of a group of people or events through a collection of data and tabulation of frequencies on research variables or their interaction. Bryman and Bell (2014) stated that a descriptive design is concerned with determining the frequency with which something occurs or the relationship between variables. With presence of knowledge and information open membership policy and loan performance, descriptive research design assisted in describing the observations and the characteristics.

3.2.1 Research philosophy

The study was anchored on post-positivism philosophy point of view. Creswell (2009) state that the philosophy is not committed to any one system of philosophy or reality. It focuses on what is the problem and how to get the possible solutions for the problem. It

provides a philosophical framework for both quantitative and qualitative techniques which forms the mixed methods research. In this philosophy, the central problem is the research problem and it employs all the approaches towards understanding the problem and how to possibly solve it.

3.3 Target Population

The target population of the study included all the seventy nine respondents from the selected SACCOs in Meru County and it included the Credit analyst, loan sales officers and loan collection officers. The population was selected since the listed SACCOs have adopted open membership thus the assumption is they have information about the open membership that would be helpful for the study. The target population is the total number of items under investigation (Kothari, 2004).

Table 3.1***Target Population***

Selected SACCOs	Credit Analysts	Loan sales officers	Loan collection officers	Total
Dhabiti Sacco	1	3	2	6
Capital Sacco	1	4	3	8
NyambeneArimiSacco	1	5	4	10
Centinary Sacco	1	3	2	6
Yetusacco	1	4	3	8
Smart Sacco	1	3	2	7
Champion Sacco	1	3	3	7
MMH Sacco	1	5	4	9
Imenti Sacco	1	3	2	6
Shiraji Sacco	1	6	5	12
Solution Sacco				

Totals	10	39	30	79
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Source: SASRA (2018)

3.4 Sampling Design, Procedure and Size

Sampling design refers to rules and procedures through which some elements in a population are included in the sample (Kothari, 2004). Stratified sampling was used to derive a sample from the population. This study adopted a census where the whole population was tested to enable the researcher come up with the information required which comprised of seventy nine respondents from the selected SACCOs in Meru County. Census is more appropriate in that the researcher had the advantage of getting information from each and every character in the population reducing biasness in sample selection and again the number was manageable.

3.5 Data Collection Instruments and Procedure

Structured questionnaires taking the form of qualitative and quantitative were used to collect primary data while secondary data was acquired from the published data files. Questionnaire is a research instrument that has a series of questions and other prompts for the purpose of gathering intended information from the respondents for the purpose of answering research (Bell, 2013). The researcher setting questions from the area of interest enhanced the suitability of the questionnaire. Questionnaires was administered through drop and pick where Likert scale was used to rate the responses with options of strongly disagree, disagree, neither agree or disagree, agree and strongly agree.

3.6 Reliability and Validity of Research Instruments

Reliability refers to the consistency of measurement and its frequency assesses using test re-test reliability method (Auer &Fortuny, 2010). The term is commonly used in relation to the question of whether the measures that are devised for concepts in business are consistent. To test whether the instruments are reliable the researcher used Cronbach's Alpha whereby the scores which are between 0 - 0.6 indicate that the instrument has a low level of reliability while scores of 0.7 and above indicate that the instrument has a high level of internal consistency and reliability. Lack of respondent's knowledge could affect the reliability of data (Metcalf, 2008).The researcher conducted a pilot study in the neighboring TharakaNithi County in Transnational SACCO to enhance the reliability of the questionnaire.

Validity refers to the degree to which a study accurately reflects or assesses or reassesses the specific concept that the researcher is attempting to measure. To enhance the validity of the instrument, the researcher sought expert opinion by consulting the study supervisors in respect to content validity. Mugenda (2010) suggested that based on descriptive research design, a pilot group ranges from 5 to 10 employees, therefore, the questionnaires was distributed to two respondent in each category totaling to six (6) questionnaires which are, the credit analysts, loan sales officers and loan collection officers from Transnational SACCO in Tharaka Nithi County.

3.7 Data Analysis and Presentation

Data collected was checked for completeness and comprehensibility. Then it was summarized, coded, tabulated and entered into SPSS (Statistical Package for the Social Science) for analysis. To establish the patterns and trends for easier understanding and interpretation of the findings, descriptive statistics especially frequencies, standard

deviations, mean scores and frequency percentages were applied to establish the patterns and trends so as to make it easier to understand and interpret the implications of the findings. Linear regression analysis was also used to establish the relationship between the dependent and independent variables.

The regression equation of the linear regression analysis is:

$$LP = \alpha + \beta_1 * FRP + \beta_2 LRP + \beta_3 * LSR + \beta_4 * LPP + \epsilon_t$$

Where;

LP – Loan Performance

FRP – Financial Risk Policy

LRP – Loan Repayment Period

LSR – Loan Security Requirement

LPP – Loan Processing Period

α – Regression intercept

β_1 – Coefficient of Financial Risk Policy

β_2 – Coefficient of Loan Repayment Period

β_3 – Coefficient of Loan Security Requirement

β_4 – Coefficient of Loan Processing Period

ϵ_t – Regression error term

$$Y = -0.076 + 0.229FRP + 0.284LRP + 0.194LSR + 0.075LPP + e \dots(5)$$

3.8 Ethical Issues

The researcher introduced herself to the respondents through an introduction letter. Further the University provided an introduction letter to acknowledge that the researcher is their student and was undertaking the study for academic purpose. The researcher sought permission to collect data from the selected SACCOs from the regulating body NACOSTI. The researcher also respected the views of the respondents and the study was entirely on voluntary basis. The valued beliefs and convictions of the respondents were respected. The data that collected was not fabricated and all the sources consulted in doing this study were all referenced according to the APA guidelines version 6. Finally, the collected primary data was not personalized and was handled with the required confidentiality.

CHAPTER FOUR

RESULTS AND DISCUSSIONS

4.1 Introduction

This chapter presents findings in regards to the four objectives of the study. The study sought out to establish the relationship between open membership policies (financial risk policy, loan repayment period, loan security requirement and loan processing period) and loan performance among Saccos in Meru County. Descriptive and inferential statistics are presented in the form of tables, graphs and charts. Descriptive statistics include frequency distribution, means and correlational coefficients. Inferential statistics include F-statistic, t-statistic, Shapiro-wilk statistics, Breusch-Pagan and Koenker statistics, which have been used to test linear regression assumptions and to form conclusions on the study's hypotheses. This chapter has the following subsections: response rate, demographic description, reliability analysis, description of study variables, linear regression assumptions, hypothesis testing and chapter summary.

4.2 Response Rate

The study adopted a census approach in targeting respondents for the study. The researcher collected 60 out of a population of 79 respondents, which formed 75.95 percent return rate. According to Mugenda and Mugenda (2003), a response rate of 70% is appropriate for generalizing the sample results to the population.

4.3 Demographic Description

This section presents descriptive statistics on academic qualification and work experience. Other descriptive statistics provided in this section are related to frequency of review of internal controls, validity of the internal controls in relation to their intended function and finally, effectiveness of internal controls in revenue generation. These findings are in form of tables, pie chart and paragraphed explanations.

4.3.1 Current Position

This subsection describes the current position of the respondents divided into credit analyst, loan sales officer and loan collection officer. The description is in frequency distribution and percentages.

Table 4.1:

Current Position of Respondents

Position	Target Population	Returned (n)	Returned (%)
Credit Analyst	10	10	16.7
Loan Sales Officer	39	26	43.3
Loan Collection Officer	30	24	40.0
Total	79	60	100.0

Table 4.1 shows that the loan sales officers were the majority in number (n=26, 43.3%). This was followed by loan collection officers (n = 24, 40.0%) and finally, the credit analysts (n = 10, 16.7%). Furthermore, the distribution closely follows the target population distribution whereby the majority was loan sales officers, followed by loan

collection officers and finally credit analysts. This means that the representation was fair across the target respondents hence the collected data was a good representation of the study population.

4.3.2 Level of Education

This subsection describes the level of education of the respondents divided into the following levels: doctorate (PhD), masters, undergraduate, diploma and others. The description is in frequency distribution and percentages.

Table 4.2:

Level of Education

Education Level	Frequency (n)	Percent (%)
PhD	1	1.7
Masters	14	23.3
Undergraduate	29	48.3
Diploma	15	25.0
Other	1	1.7
Total	60	100.0

Table 4.2 shows that majority of the respondents had undergraduate qualification (n=29, 48.3%) while 15 (26.0%) had diploma qualifications and below. Those who had postgraduate qualifications were distributed as follows: masters (n=14, 23.3%) and PhD (n=1, 1.7%). These results show that the respondents possessed sufficient education to

be able to give appropriate and valid responses to the questions asked in the questionnaire.

4.3.3 Length of Service

This subsection describes the length of service of the respondents divided into the following levels: 0-2 years, 3-5 years, 6-10 years and above 11 years.

Table 4.3:

Length of Service

Years	Frequency	Percent
0-2 years	14	23.3
3-5yrs	32	53.3
6-10yrs	12	20.0
11years and above	2	3.3
Total	60	100.0

Table 4.3 shows that the distribution was 14 (23.3%), 32 (53.3%), 12 (20.0%) and 2 (3.3%) for 0-2 years, 3-5 years, 6-10 years and above 11 years respectively. Therefore, the length of service of the respondents was sufficient to enable them to be familiar with the questions asked regarding open membership policies and loan performance among the Saccos in Meru County.

4.4 Reliability Analysis

This section shows the findings on reliability as a proxy for internal consistency of the questionnaire measured during the piloting phase of data collection. Cronbach's Alpha determined the reliability whereby an alpha of 0.7 and above was required to conclude that the questionnaire section was reliable.

4.4.1 Reliability Analysis for Financial Risk Policy

This subsection presents the reliability analysis of financial risk policy, which had four questionnaire items for this research construct.

Table 4.4:

Reliability Results for Financial Risk Policy

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item- Total Correlation	Cronbach's Alpha if Item Deleted
Operational risk budget is always set aside in the organization	12.13	9.609	0.785	0.896
The risk premium in my organization considers the risk factors of an investment	12.20	9.315	0.812	0.887
My organization is aware of the possible market risk	12.02	10.051	0.778	0.899

My organization as a working liquidity risk policy	12.00	9.390	0.847	0.875
Overall Results			0.915	

Table 4.4 shows the reliability score for financial risk policy together with the change in Alpha score due to deletion of a questionnaire item. The Alpha for financial risk policy was 0.915, which was above 0.7 hence deeming the questionnaire reliable in regards to Financial Risk Policy.

4.4.2 Reliability Analysis for Loan Repayment Period

This subsection presents the reliability analysis of loan repayment period, which had four questionnaire items for this research construct.

Table 4.5:

Reliability Results for Loan Repayment Period

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item-Total Correlation	Cronbach's Alpha if Item Deleted
The instalment period is sufficient for loans taken	12.10	8.973	0.705	0.766
There is a grace period allowed for loans given	11.87	10.253	0.599	0.813
Loans are restructured were necessary	12.00	10.102	0.586	0.820

Cases of late payment				
are given special attention	11.98	9.949	0.769	0.745
			Overall Results	0.831

Table 4.5 shows the reliability score for loan repayment period together with the change in Alpha score due to deletion of a questionnaire item. The Alpha for loan repayment period was 0.831, which was above 0.7 hence deeming the questionnaire reliable in regards to loan repayment period.

4.4.3 Reliability Analysis for Loan Security Requirement

This subsection presents the reliability analysis of loan security requirement, which had four questionnaire items for this research construct.

Table 4.6:

Reliability Results for Loan Security Requirement

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item-Total Correlation	Cronbach's Alpha if Item Deleted
There is a guarantor policy on loans taken	12.37	7.355	0.731	0.675
Members savings are considered as loan security	12.32	7.779	0.784	0.656

The account statements are considered	12.48	9.237	0.438	0.825
Ownership documents for collateral are considered	12.18	9.237	0.502	0.791
Overall Reliability				0.795

Table 4.6 shows the reliability score for loan security requirement together with the change in Alpha score due to deletion of a questionnaire item. The Alpha for loan security requirement was 0.795, which was above 0.7 hence deeming the questionnaire reliable in regards to loan security requirement.

4.4.4 Reliability Analysis for Loan Processing Period

This subsection presents the reliability analysis of loan processing period, which had four questionnaire items for this research construct.

Table 4.7:***Reliability Results for Loan Processing Period***

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item- Total Correlation	Cronbach's Alpha if Item Deleted
Customer loan application forms accumulate so much	11.78	10.410	0.620	0.795
Loan waiting period is clearly defined	11.45	10.591	0.728	0.732
The loan processing period is affected by the amounts disbursed per day	11.42	10.349	0.811	0.692
Requirements for compliance to loan policy affects loan processing period	10.95	14.794	0.461	0.847
Overall Reliability				0.820

Table 4.7 shows the reliability score for loan processing period together with the change in Alpha score due to deletion of a questionnaire item. The Alpha for loan processing period was 0.820, which was above 0.7 hence deeming the questionnaire reliable in regards to loan processing period.

4.4.5 Reliability Analysis for Loan Performance in Saccos

This subsection presents the reliability analysis of loan performance, which had four questionnaire items for this research construct.

Table 4.8:

Reliability Results for Loan Performance

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item- Total Correlation	Cronbach's Alpha if Item Deleted
Interests on loans meets the set target per year	8.68	4.188	0.712	0.716
Loan amounts keep on increasing every year	8.27	4.167	0.727	0.699
The number of loan applicants increases every year	8.14	5.740	0.616	0.819
			Overall Reliability	0.821

Table 4.8 shows the reliability score for loan performance together with the change in Alpha score due to deletion of a questionnaire item. The Alpha for loan processing period was 0.821, which was above 0.7 hence deeming the questionnaire reliable in regards to loan performance.

4.4.6 Overall Reliability Analysis

This subsection presents the overall reliability analysis for all variables as whole excluding the questionnaire items, which contained demographic questions: current position, level of education and length of service.

Table 4.9:

Overall Reliability Results

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item-Total Correlation	Cronbach's Alpha if Item Deleted
<hr/>				
Operational risk budget				
is always set aside in the organization	72.37	268.962	0.772	0.950
<hr/>				
The risk premium in my organization considers the risk factors of an investment	72.42	265.800	0.833	0.949
<hr/>				
My organization is aware of the possible market risk	72.24	269.529	0.805	0.950
<hr/>				
My organization as a working liquidity risk policy	72.24	266.805	0.847	0.949
<hr/>				

The instalment period is sufficient for loans taken	72.46	263.115	0.782	0.950
There is a grace period allowed for loans given	72.22	275.002	0.558	0.953
Loans are restructured were necessary	72.36	270.095	0.656	0.952
Cases of late payment are given special attention	72.36	270.613	0.764	0.950
There is a guarantor policy on loans taken	72.27	268.098	0.719	0.951
Members savings are considered as loan security	72.22	269.761	0.770	0.950
The account statements are considered	72.34	273.193	0.628	0.952
Ownership documents for collateral are considered	72.08	277.182	0.558	0.953
Customer loan application forms accumulate so much	72.88	272.727	0.468	0.956

Loan waiting period is clearly defined	72.56	264.458	0.721	0.951
The loan processing period is affected by the amounts disbursed per day	72.53	266.116	0.715	0.951
Requirements for compliance to loan policy affects loan processing period	72.08	276.355	0.663	0.952
Interests on loans meets the set target per year	72.47	262.771	0.831	0.949
Loan amounts keep on increasing every year	72.07	266.961	0.731	0.951
The number of loan applicants increases every year	71.93	275.340	0.701	0.951
Overall Reliability				0.953

Table 4.9 shows the reliability score for the five variables (dependent and independent variables) combined together with the change in Alpha score due to deletion of a questionnaire item. The overall alpha was 0.953, which was above 0.7 hence deeming the whole questionnaire.

4.5 Description Analysis of the Study Variables

This section presents descriptive statistics for the questionnaire items for each research construct. The statistics used are frequency, percentages and means presented in form of tables. The questions were in form of a five point Likert scale where in 1, 2, 3, 4 and 5 represented strongly disagree, disagree, neutral, agree and strongly agree respectively.

4.5.1 Descriptive Statistics for Financial Risk Policy

This subsection describes the responses for financial risk policy for the four questionnaire item asked.

Table 4.10:***Descriptive Statistics for Financial Risk Policy***

N=60	Question	(1)	(2)	(3)	(4)	(5)	Mean
1	Operational risk budget is always set aside in the organization	5 (8.3%)	2 (3.3%)	4 (6.7%)	27 (45.0%)	22 (36.7%)	3.98
2	The risk premium in my organization considers the risk factors of an investment	4 (6.7%)	5 (8.3%)	5 (8.3%)	24 (40.0%)	22 (36.7%)	3.92
3	My organization is aware of the possible market risk	1 (1.7%)	8 (13.3%)	2 (3.3%)	22 (36.7%)	27 (45.0%)	4.10
4	My organization has a working liquidity risk policy	2 (3.3%)	7 (11.7%)	2 (3.3%)	20 (33.3%)	29 (48.3%)	4.12
Average		5.00%	9.15%	5.40%	38.75%	41.68%	4.03
Summary		Negative = 19.55%		Positive = 80.43%			

Table 4.10 shows that each of the four questionnaire items addressing financial risk policy had mean of at least 3.92 out of maximum of five. This indicates that majority of the respondents agreed to the following assertions: operational risk budget is always set

aside in the organization; risk premium in the organization considers the risk factors of an investment; the organization is aware of possible market risks; and that the organization has working liquidity risk policy. The overall mean was 4.03 out of 5; hence, the overall response was in support of financial risk policies in the sampled Saccos in Meru County.

4.5.2 Loan Repayment Period Descriptive Statistics

This subsection describes the responses for loan repayment period for the four questionnaire item asked.

Table 4.11:***Descriptive Statistics for Loan Repayment Period***

N=60	Question	(1)	(2)	(3)	(4)	(5)	Mean
1	The installment period is sufficient for loans taken	9 (15.0%)	0 (0.0%)	4 (6.7%)	23 (38.3%)	24 (40.0%)	3.88
2	There is a grace period allowed for loans given	3 (5.0%)	7 (11.7%)	3 (5.0%)	14 (23.3%)	33 (55.0%)	4.12
3	Loans are restructured where necessary	6 (10.0%)	4 (6.7%)	1 (1.7%)	23 (38.3%)	26 (43.3%)	3.98
4	Cases of late payment are given special attention	3 (5.0%)	5 (8.3%)	3 (5.0%)	27 (45.0%)	22 (36.7%)	4.00
Average		8.75%	6.68%	4.47%	36.23%	43.75%	4.00
Summary		Negative = 19.90%		Positive = 80.1%			

Table 4.11 shows that each of the four questionnaire items addressing loan repayment period had mean of at least 3.88 out of maximum of five. This indicates that majority of the respondents agreed to the following assertions: sufficiency of installment period of paying loans; availability of grace period for loans given; loans are restructured in a customized way; and that cases of late payment are given special attention. The overall

mean was 4.00 out of 5; hence, the overall response was support for loan repayment period in the sampled Saccos in Meru County.

4.5.3 Loan Security Requirement

This subsection describes the responses for loan security requirement for the four questionnaire item asked.

Table 4.12:***Descriptive Statistics for Loan Security Requirement***

N=75	Question	(1)	(2)	(3)	(4)	(5)	Mean
1	There is a guarantor policy on loans taken	6 (10.0%)	2 (3.3%)	3 (5.0%)	19 (31.7%)	30 (50.0%)	4.08
2	Members savings are considered loan security	4 (6.7%)	2 (3.3%)	4 (6.7%)	22 (36.7%)	28 (46.7%)	4.13
3	The account statements are considered	4 (6.7%)	5 (8.3%)	6 (10.0%)	19 (31.7%)	26 (43.3%)	3.97
4	Ownership documents for collateral are considered	3 (5.0%)	4 (6.7%)	2 (3.3%)	16 (26.7%)	35 (58.3%)	4.27
Average		7.10%	5.40%	6.25%	31.70%	49.58%	4.11
Summary		Negative = 18.75 %			Positive = 81.25 %		

Table 4.12 shows that each of the four questionnaire items addressing loan security requirement had mean of at least 3.97 out of maximum of five. This indicates that majority of the respondents agreed to the following assertions: there is a guarantor policy on loans taken; members' savings were considered as loan security; account statements were considered; and that ownership documents were used for collateral. The overall mean was 4.11 out of 5; hence, the overall response was support for loan security requirement in the sampled Saccos in Meru County.

4.5.4 Loan Processing Period

This subsection describes the responses for loan processing period for the four questionnaire item asked.

Table 4.13:***Descriptive Statistics for Loan Processing Period***

N=60	Question	(1)	(2)	(3)	(4)	(5)	Mean
1	Customer loan application forms accumulate so much	13 (21.7%)	8 (13.3%)	1 (1.7%)	17 (28.3%)	21 (35.0%)	3.42
2	Loan waiting period is clearly defined	6 (10.0%)	10 (16.7%)	3 (5.0%)	15 (25.0%)	26 (43.3%)	3.75
3	The loan processing period is affected by the amounts disbursed per day	6 (10.0%)	8 (13.3%)	3 (5.0%)	19 (31.7%)	24 (40.0%)	3.78
4	Requirements for compliance to loan policy affects loan processing period	3 (5.0%)	1 (1.7%)	3 (5.0%)	24 (40.0%)	29 (48.3%)	4.25
Average		11.68%	11.25%	4.18%	31.25%	41.10%	3.80
Summary		Negative = 27.10%			Positive = 72.35%		

Table 4.13 shows that each of the four questionnaire items addressing loan-processing period had mean of at least 3.42 out of maximum of five. This indicates that majority of the respondents agreed to the following assertions: the loan application form was comprehensive; there was a clearly defined loan-waiting period; loan processing period

is affected by the amounts disbursed per day; and that the requirements for compliance to loan policy affects loan processing period. The overall mean was 3.80 out of 5; hence, the overall response was support for loan processing period in the sampled Saccos in Meru County.

4.5.5 Loan Performance of Selected SACCOs

This subsection describes the responses for loan performance for the four questionnaire item asked.

Table 4.14:

Descriptive Statistics for Loan Performance

N=60	Question	(1)	(2)	(3)	(4)	(5)	Mean
1	Interest on loans meets the set target per year	7 (11.9%)	2 (3.4%)	6 (10.2%)	21 (35.6%)	23 (39.0%)	3.86
2	Loan amounts keep on increasing every year	5 (8.5%)	4 (6.8%)	1 (1.7%)	9 (15.3%)	40 (67.8%)	4.27
3	The number of loan applicants increases every year	2 (3.4%)	2 (3.4%)	4 (6.8%)	13 (22.0%)	38 (64.4%)	4.41
Average		7.93%	4.53%	6.23%	24.30%	57.07%	4.18
Summary		Negative = 18.70%			Positive = 81.37%		

Missing = 1 (1.7%)

Table 4.14 shows that each of the four questionnaire items addressing loan performance had mean of at least 3.86 out of maximum of five. This indicates that majority of the respondents agreed to the following assertions: the interest on loans meets the set target per year; loan amounts keep on increasing every year; and that the number of loan

applicants increases every year. The overall mean was 4.18 out of 5; hence, the overall response was support for loan performance in the sampled Saccos in Meru County.

4.6 Results of Hypotheses Testing

The study used linear regression to show the link between loan performance of Saccos in Meru County (dependent variables) and the independent variables (financial risk policy, loan repayment period, loan security requirement and loan processing period). The study tested five underlying assumptions of linear regressions, which included: absence of outliers, normality of regression residuals, linear relationship between independent and dependent variables, homoscedasticity of regression residuals and absence of multicollinearity among independent variables.

4.6.1 Outliers

The study used Mahalanobis statistics, Leverage and Cook's Distance statistics to identify outliers with the aid of SPSS. The cutoff value for Mahalanobis statistics was from the chi-square distribution, $\chi^2(5\%, \text{ five variables}) = 11.0705$ while the cut-off for Cooks Distance was $4/(n-k-1)$ where k was number of variables ($k=5$) and n was 60 cases; $4/(75-5-1) = 0.074$. The cut-off value for Centered Leverage was 0.167 computed as $2*k/n$. Eight cases had values above the aforementioned cutoff points hence deemed outliers. These outliers did not form part of testing further regression assumptions and consequent linear regression modelling.

4.6.2 Normality of Regression Residuals

To find out whether the regression residuals distributed normally, the study used histogram of regression residuals, normal P-P plots, normal Q-Q plots, Kolmogorov-Smirnov statistic and Shapiro-Wilk statistic.

Figure 4.1:

Histogram of Standardized Residuals

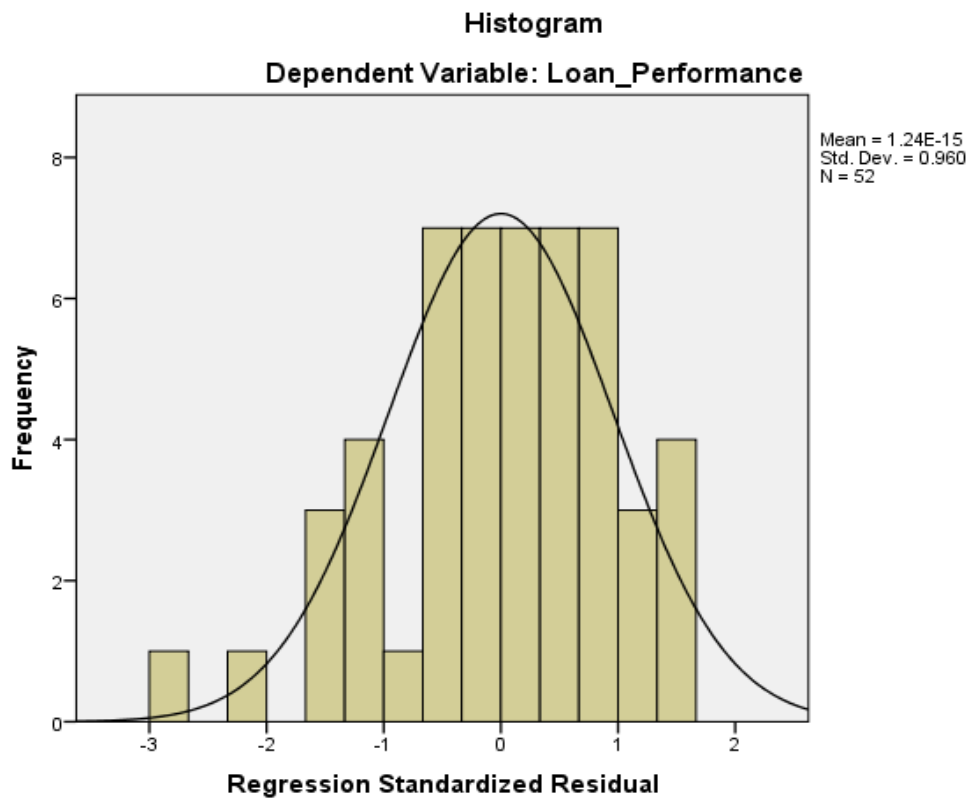


Figure 4.1 shows a histogram of standardized regression residuals. The histogram takes a bell shape, slightly skewed to the left. Overall, the residuals have a normally distributed around the zero value.

Table 4.15:

Tests of Normality

	Kolmogorov-Smirnov ^a			Shapiro-Wilk		
	Statistic	Df	p-value	Statistic	df	p-value
Unstandardized Residual	0.071	52	0.200*	0.974	52	0.306

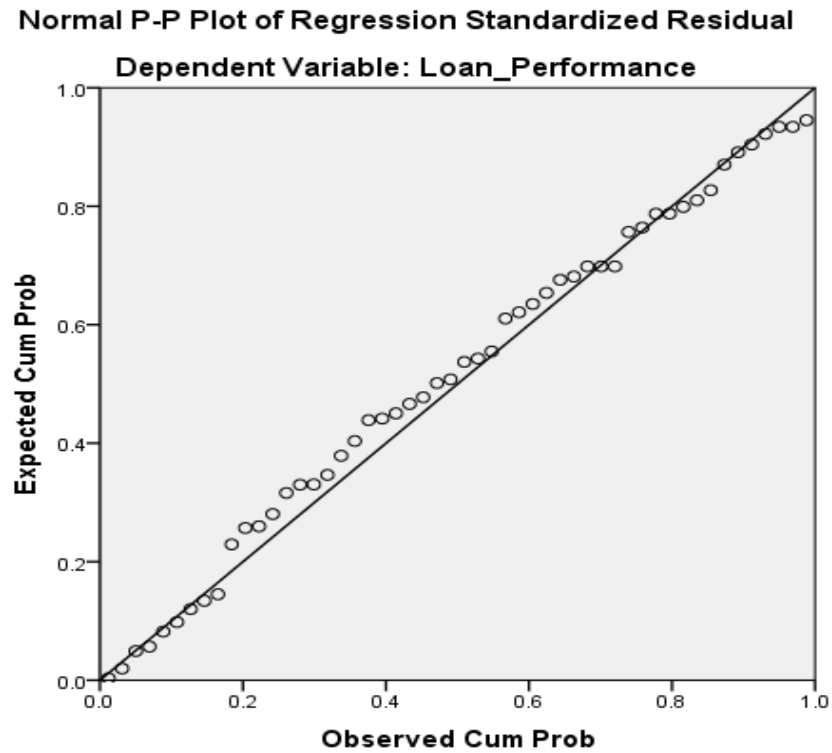
*. This is a lower bound of the true significance.

a. Lilliefors Significance Correction

Table 4.15 shows results for Shapiro-Wilk test and Kolmogorov-Smirnov test of normality. These tests assume the null hypothesis of normally distributed unstandardized residuals. The alternate hypothesis being the absence of normality. The p-values of both Shapiro-Wilk statistics and Kolmogorov-Smirnov statistic are 0.200 and 0.306 respectively. Since both p-values are more than 5% significance level, the study concludes that the unstandardized residuals are normally distributed.

Figure 4.2:

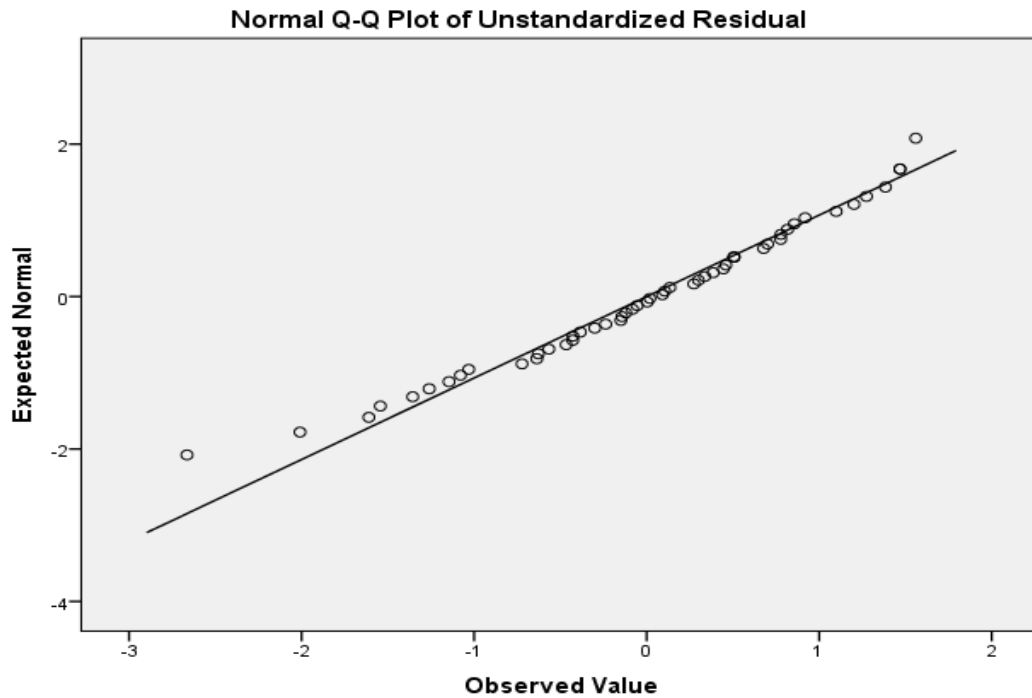
Normal P-P Plot of Standardized Residuals



The observed cumulative probability values in Figure 4.2 spread closely around the expected cumulative probability curve. This indicates normal distribution of the regression residuals hence corroborating the findings from Shapiro-Wilk test in Table 4.15 and the bell shape of the histogram in Figure 4.1 for regression residuals.

Figure 4.3:

Normal Q-Q Plot



The observed values in Figure 4.3 fit closely along the expected normal curve in the Normal Q-Q plot. These findings also confirm the statistical results observed from Shapiro-Wilk normality test in Table 4.15, normal p-p plot (Figure 4.2) as well as histogram of unstandardized residuals (Figure 4.1).

4.6.3 Multicollinearity (Additivity)

Linear regression further requires little correlation among the independent variables. High correlation among the independent variable leads to amplification of standard error hence reducing the accuracy of the reported regression coefficient. Furthermore,

high correlation between two independent variables leads to redundancy in representation of a research construct.

Table 4.16:

Collinearity Statistics

Model	Collinearity Statistics	
	Tolerance	VIF
(Constant)		
Financial Risk Policy	0.206	4.846
Loan Repayment Period	0.318	3.150
Loan Security Requirement	0.311	3.219
Loan Processing Period	0.460	2.172

Assessment of collinearity in this study uses variance inflation factors (VIF) and Tolerance values shown in Table 4.16 (collinearity statistics). The highest VIF was 4.846 while the least value of VIF was 2.172. According to Akinwande, Dikko, & Samson (2015), VIF of less than five is acceptable for deeming absence of multicollinearity amongst the independent variables.

4.6.4 Linearity

The study also tested the linear relationship between the independent variables and the dependent variable. Linear regression requires an inherent linear relationship between the independent and dependent variable. Linearity was measured using analysis of variance (ANOVA), Pearson’s coefficient correlation and partial regression plots.

Table 4.17:

Analysis of Variance for Combined Independent Variables

Model	Sum of Squares	df	Mean Square	F	p-value
Regression	342.177	4	85.544	90.047	0.000 ^b
Residual	44.650	47	0.950		
Total	386.827	51			

a. Dependent Variable: Loan Performance

b. Predictors: (Constant), Loan Processing Period, Loan Repayment Period, Loan Security Requirement, Financial Risk Policy

Analysis of variance tests the null hypothesis that loan performance have no linear relationship to the independent variables (Financial Risk Policy, Loan Repayment Period, Loan Security Requirement and Loan Processing Period). Rejecting the null hypothesis means that at least one predictor is a linearly related to the dependent variable. The observed p-value in Table 4.17 for the F-statistics was 0.000 ($P < 0.05$). Therefore, the study reject the null hypothesis hence leading to the conclusion that there is a linear relationship between the independent variables and the dependent variable (loan performance).

Table 4.18:

Model Summary for Combined Independent Variables

R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
0.941 ^a	0.885	0.875	0.97468	1.621

a. Predictors: (Constant), Loan Processing Period, Loan Repayment Period, Loan Security Requirement, Financial Risk Policy

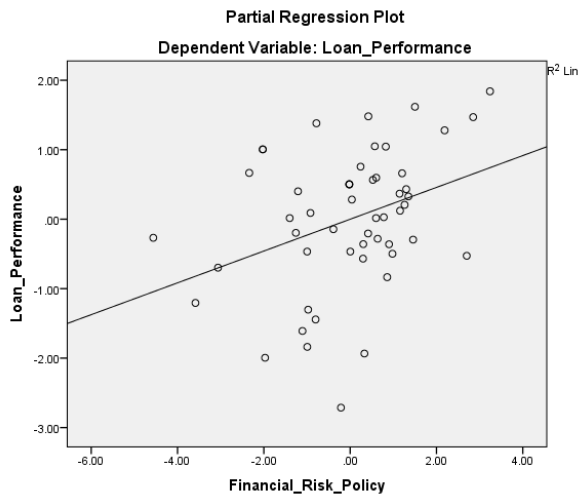
b. Dependent Variable: Loan Performance

Pearson's coefficient of multiple correlation (R) in Table 4.18 was 94.1%, which indicates strong correlation between loan performance and the independent variable (Financial Risk Policy, Loan Repayment Period, Loan Security Requirement and Loan Processing Period). This further corroborates the findings from Table 4.17 for Analysis of Variance.

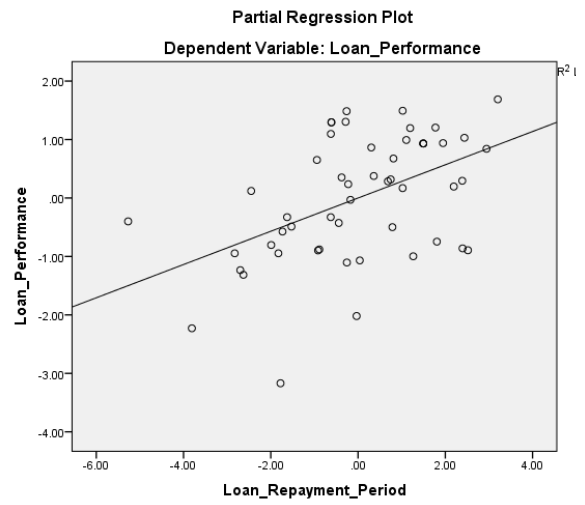
Figure 4.4:

Partial Linearity Plots

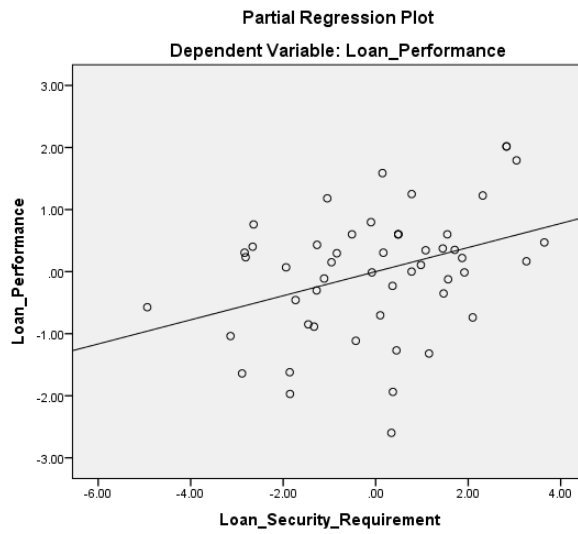
Partial Plot 1



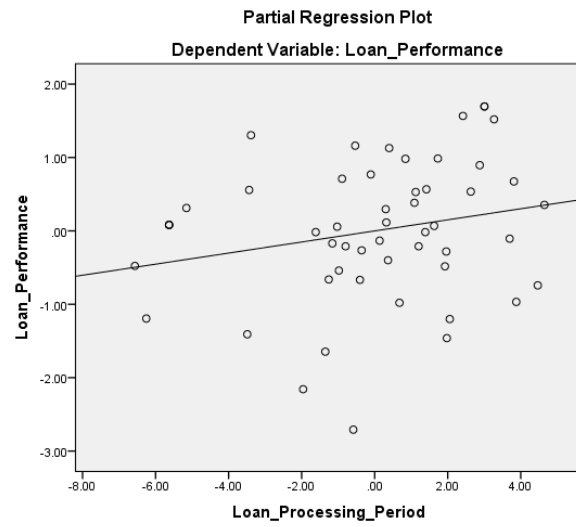
Partial Plot 2



Partial Plot 3



Partial Plot 4



The partial plots in Figure 4.4 shows that each independent variable had a linear relationship with the dependent variable albeit at different degrees. Financial risk policy (partial plot 1), loan repayment period (partial plot 2) and loan security requirement (partial plot 3) were more linearly related to loan performance. However, loan repayment period (partial plot 4) had a lesser linear relationship compared to the other three partial plots. However, the slope on all the four plots was positive and clearly visible as depicted by the trend lines therein.

4.6.5 Homoscedasticity

Linear regression assumes homogeneity of variance among the regression residuals. In this study, Breusch-Pagan and Koenker tests are used to infer the presence or absence of homoscedasticity (homogeneity of variance). These tests assume the residuals to be normally distributed. Table 4.19 shows the results for these tests.

Table 4.19:

Breusch-Pagan and Koenker test

Test Statistic	LM	P-value
BP	5.021	0.285
Koenker	4.814	0.307

The null hypothesis under the Breusch-Pagan (BP) and Koenker test is homoscedasticity (that is, homogeneity of variance. The observed p-values of BP and Koenker tests are 0.285 ($p < 0.05$) and 0.307 ($p < 0.05$) respectively. The study therefore concludes that there is homogeneity of variance in the regression residuals.

4.7 Hypothesis Testing

Following the four specific objectives, the study set out to investigate the following hypotheses.

H_{01} : There is no significant relationship between financial risk policy and loan performance in selected Saccos

H_{02} : There is no significant relationship between loan repayment period and loan performance in selected Saccos

H_{03} : There is no significant relationship between loan security requirement and loan performance in selected Saccos

H_{04} : There is no significant relationship between loan processing period and loan performance in selected Saccos

For the relationship between each independent variable and the dependent variable, the study carried out simple linear regression to show the several relationship of each independent variables (financial risk policy, loan repayment period, loan security requirement and loan processing period) and dependent variable (loan performance in selected Saccos). The inferential statistic used to test the four corresponding hypotheses was t-statistic. The following subsections 4.7.1, 4.7.2, 4.7.3 and 4.7.3 show the simple regression results for financial risk policy, loan repayment period, loan security requirement, and loan processing period against loan performance respectively.

4.7.1 Linear Regression Loan Performance in selected Saccos against Financial Risk Policy

The linear relationship between loan performance in selected Saccos and financial risk policy is in accordance to general form below

$$LP = \alpha + \beta * FRP + \epsilon_t$$

Where;

LP – Loan Performance

FRP – Financial Risk Policy

α – Regression intercept

β – Coefficient of Financial Risk Policy

ϵ_t – Regression error term

LP =	1.321	+	0.694*FRP (1)
<i>t-statistic</i>	1.567		14.080	
<i>p-value</i>	0.124		0.000	

R	0.894 (89.4%)
R-square	0.799 (79.9%)
F-statistic	F = 198.253; p = 0.000

H_{01} : There is no significant relationship between financial risk policy and loan performance

In equation 1, loan performance is the dependent variable while financial risk policy was the independent variable. The results show that loan performance has a significant positive relationship ($R=89.4\%$) with financial risk policy, implying that both variables moves in same direction in significantly close proportions. Pearson's coefficient of determination, ($R\text{-square}=0.799$) shows that financial risk policy explains 79.9% of variations in the loan performance of Saccos in Meru County. Equation 1 further shows that marginal increase in financial risk policy leads to 0.694 increase in the loan performance while holding other factors constant. The p-value of the coefficient of financial risk policy was 0.000 ($p<0.05$). Therefore, H_{01} is rejected hence concluding that at a significance level of 5%, financial risk policy is significantly related to loan performance of Saccos in Meru County. These results concur with those of Al-Kouri (2011) in a study on the impact of specific risk characteristics and bank performance in Gulf Cooperation Council countries and realized that liquidity risk, credit risk and capital risk significantly influenced the financial performance of Banks.

4.7.2 Linear Regression of Loan Performance in selected Saccos against Loan Repayment Period

The linear relationship between loan performance and loan repayment period is in the general form below

$$LP = \alpha + \beta * LRP + \mathcal{E}_t$$

Where;

LP – Loan Performance

LRP – Loan repayment period

α – Regression intercept

β – Coefficient of loan repayment period

ϵ_t – Regression error term

$$\begin{array}{l} \text{LP} = \quad 1.721 \quad + \quad 0.675 * \text{LRP} \quad \dots\dots\dots (2) \\ t\text{-statistic} \quad 1.963 \quad \quad 13.090 \\ p\text{-value} \quad 0.055 \quad \quad 0.000 \end{array}$$

R 0.880 (88.0%)
R-square 0.774 (77.4%)
F-statistic F = 171.337; p = 0.000

H_{02} : There is no significant relationship between loan repayment period and loan performance

In equation 2, loan performance is the dependent variable while loan repayment period is the independent variable. The results show significant positive relationship (R=88.0%) between loan repayment period and loan performance. This implies that both variables moves in same direction in significantly close proportions. The coefficient of determination, (R-square=0.774) shows that loan repayment period explains 77.4% of variations in the loan performance of Saccos in Meru County. Equation 2 further shows that marginal increase in loan repayment period leads to 0.675 increase in the loan performance while holding other factors constant. The p-value of the coefficient of loan repayment period was 0.000 ($p < 0.05$). Therefore, H_{02} is rejected

hence concluding that at a significance level of 5%, loan repayment period is significantly related to loan performance of Saccos in Meru County. The results concur with those of Walsh (2013) in a study on the relationship between loan repayment period and loan default in SACCOs which concluded that an increase in loan repayment period or adjustment in the repayment period eliminates the crisis of non-performing loans thus good financial records and credit worthiness.

4.7.3 Linear Regression of Loan Performance against Loan Security Requirement

The linear relationship between loan performance and loan security requirement is in the general form below

$$LP = \alpha + \beta * LSR + \epsilon_t$$

Where;

FP – Loan Performance

LSR – Loan Security Requirement

α – Regression intercept

β – Coefficient of Loan Security Requirement

ϵ_t – Regression error term

$$LP = 1.813 + 0.663 * LSR \dots\dots\dots (3)$$

t-statistic 1.865 11.698

p-value 0.068 0.000

R 0.856 (85.6%)

R-square 0.732 (73.2%)

F-statistic F = 136.839; p = 0.000

H_{03} : There is no significant relationship between Loan security requirement and loan performance

In equation 3, loan performance is the dependent variable while loan security requirement was the independent variable. The results show that loan performance has significant positive relationship ($R=85.6\%$) with loan security requirement. This implies that both variables moves in same direction in significantly close proportions. The coefficient of determination, ($R\text{-square}=0.732$) shows that loan security requirement explains 73.2% of variations in the loan performance of Saccos in Meru County. Equation 3 also shows that marginal increase in loan repayment period leads to 0.663 increase in the loan performance while holding other factors constant. The p-value of the coefficient of loan security requirements was 0.000, which was less than 5% (0.05). Therefore, H_{03} is rejected hence concluding that at a significance level of 5%, loan security requirement is significantly related to loan performance of Saccos in Meru County. The results are in agreement with those of Chaplin (2012) who did a study on credit worthiness and loan performance and concluded that loan security is enhanced through policies and guidelines in place to regulate loan issuance and compliance to the same.

Chaplin (2012) in a study on credit worthiness and loan performance and found out that policies and guidelines on the loans is an important tool toward enhancing loan security.

4.7.4 Linear Regression of Loan Performance against Loan Processing Period

The linear relationship between loan performance and loan processing period is in the general form below

$$LP = \alpha + \beta * LPP + \mathcal{E}_t$$

Where;

LP – Loan Performance

LPP – Loan Processing Period

α – Regression intercept

β – Coefficient of Loan Processing Period

ϵ_t – Regression error term

$$\begin{array}{l} \text{LP} = \quad 5.684 \quad + \quad 0.460 * \text{LPP} \quad \dots\dots\dots (4) \\ t\text{-statistic} \quad 5.226 \quad \quad 6.899 \\ p\text{-value} \quad \quad 0.000 \quad \quad 0.000 \end{array}$$

R 0.698(69.8%)
R-square 0.488 (48.8%)
F-statistic F = 47.595; p = 0.000

H_{04} : There is no significant relationship between loan processing period and loan performance

In equation 4, loan performance is the dependent variable while loan-processing period was the independent variable. The results show that loan performance has significant positive relationship (R=69.8%) with loan processing period, which implies that both variables moves in same direction. The coefficient of determination, (R-square=0.488) shows that loan-processing period as an independent variable explains 48.8% of variations in the loan performance of Saccos in Meru County. Equation 4 also shows that a unit increase in loan processing period leads to 0.460 increase in the loan

performance while holding other factors constant. The p-value of the coefficient of loan processing period was 0.000, which was less than 5% (0.05). Therefore, H_{04} is rejected hence concluding that at a significance level of 5%, loan processing period is significantly related to loan performance of Saccos in Meru County. The results concur with the results of a study conducted by Otieno (2014) on the factors affecting loan performance in SACCOs in Kenya and concluded that efficiency in operations in terms of processing of loans applied by clients enhances loan performance and also build customer confidence and loyalty since they believe in their systems in terms of handling customer requests in a timely and efficient manner.

4.7.5 Multiple Linear regression of Loan Performance against Open Membership Policy

The linear relationship between loan performance and open membership policies is in the general form below

$$LP = \alpha + \beta_1*FRP + \beta_2LRP + \beta_3*LSR + \beta_4*LPP + \epsilon_t$$

Where;

LP –Loan Performance

FRP – Financial Risk Policy

LRP – Loan Repayment Period

LSR – Loan Security Requirement

LPP – Loan Processing Period

α – Regression intercept

β_1 – Coefficient of Financial Risk Policy

β_2 – Coefficient of Loan Repayment Period

β_3 – Coefficient of Loan Security Requirement

β_4 – Coefficient of Loan Processing Period

\mathcal{E}_t – Regression error term

The regression equation of the linear regression analysis is:

$$Y = -0.076 + 0.229FRP + 0.284LRP + 0.194LSR + 0.075LPP + e \quad \dots(5)$$

<i>Std. error</i>	0.701	0.088	0.075	0.072	0.048
<i>t – stat</i>	- 0.109	2.601	3.769	2.687	1.588
<i>p-value</i>	0.914	0.012	0.000	0.010	0.119

R 0.941(94.1%)

R-square 0.885 (88.5%)

F-statistic F = 90.047; p = 0.000

Equation 5 shows the results from the multiple linear regression analysis with all open membership policies of the study entered jointly as the independent variables while loan performance was the dependent variable. The results contain t-statistic and the corresponding p-values that were used to form conclusions on the study's hypotheses. The beta coefficients for each open membership policy show the increment of loan

performance with respect to the marginal increment of each respective open membership policies.

The p – value corresponding to financial risk policy was 0.012 ($p < 0.05$), hence the null hypothesis is rejected. Therefore, financial risk policy significantly affects loan performance of Sacco banks in Meru County while holding other factors constant. Marginal increase in financial risk policy leads to 0.229 increase loan performance of Sacco banks in Meru County while holding other factors constant.

The p – value corresponding to loan repayment period was 0.000 ($p < 0.05$), hence the null hypothesis on loan repayment period is rejected. Therefore, loan repayment period significantly affects loan performance of Sacco banks in Meru County while holding other factors constant. Marginal increase in loan repayment period leads to 0.284 increase loan performance of Sacco banks in Meru County while holding other factors constant.

The p – value corresponding to loan security requirement was 0.010 ($p < 0.05$), hence the null hypothesis on loan security requirement was rejected. Therefore, loan security requirement significantly affects loan performance of Sacco banks in Meru County while holding other factors constant. Marginal increase in loan security requirement leads to 0.194 increase loan performance of Sacco banks in Meru County while holding other factors constant.

The p – value corresponding to loan processing period was 0.119 ($p > 0.05$), hence the null hypothesis on loan processing period is not rejected. Therefore, loan processing period does not significantly affect loan performance of Sacco banks in Meru County while holding other factors constant. Marginal increase in loan processing period leads

to 0.075 increase loan performance of Sacco banks in Meru County while holding other factors constant.

4.8 Chapter Summary

The study has established that all the open membership policies (Financial Risk Policy, Loan Repayment Period, Loan Security Requirement and Loan Processing Period) when regressed severally against loan performance have significant effect as shown in equations 1, 2, 3 and 4. Jointly regression in equation 5 of all the open membership policies with loan performance reveals that only Loan Processing Period failed to have a significant effect on loan performance.

A summary of the regression results are provided in Table 4.20.

Table 4.20:***Hypotheses Summary based on Independent Linear Regressions***

Null Hypothesis	P-Value Simple Regression	P-Value Multiple Regression
H_0 : There is no significant relationship between financial risk policy and loan performance	0.000	0.012
H_0 : There is no significant relationship between loan repayment period and loan performance	0.000	0.000
H_0 : There is no significant relationship between loan security requirement and loan performance	0.000	0.010
H_0 : There is no significant relationship between loan processing period and loan performance	0.000	0.119

Table 4.20 show that all our hypotheses of the study were rejected according to the simple linear regression ($p = 0.000 < 0.05$). However, loan-processing period failed to have a significant relationship ($p = 0.119 > 0.05$) with loan performance when the entire research constructs were regressed jointly. This means that loan processing period in the presence of financial risk policy, loan repayment period and loan security requirement is not significant.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This is the final chapter and it presents the summary of the study findings. The chapter also presents the conclusions on the key issues covered in the study, also presents the recommendations of the study and finally proposes areas for further research. The problem identified in the study was Sacco failure to embrace open membership policy which allows members who do not belong to the common bond to be members of the Sacco thus enhancing performance of loans in the Sacco. This was seen through loan repayment periods that were not flexible as to accommodate those members, the security requirement for one to secure a loan were also way far beyond the ability of the targeted members, the loan processing period was also another factor that contributed to the poor loan performance as it took loan periods and finally, the financial risks associated with the loans were not fully factored hence poor compliance to the loan policy. The objectives of the study were to assess how financial risk policy under open membership affects loan performance in selected SACCOs in Meru County, to determine how loan repayment period under open membership affects the loan performance in selected SACCOs in Meru County, to determine how loan security requirement under open membership contributes to loan performance in selected SACCOs in Meru County and to determine how loan processing period under open membership contributes to loan performance in selected SACCOs in Meru County.

5.2 Summary of the Findings

The study had a response rate of above seventy percent which is an acceptable representation in research. Respondents held different positions in the organizations with majority being loan sales officers and minority group being credit analysts. Majority of respondents were undergraduate degree holders in the Saccos. The respondents served the Saccos for varied periods with majority serving between three to five years. This shows that the Saccos had qualified employees who were experienced for the tasks assigned.

The first objective on financial risk the Saccos seemed to have a policy that was meant to ensure that the financial risks are reduced or eliminated where possible. There was an operational risk budget that ensured funds were used for the right purpose while at the same time ensuring facilitation for operations was available when needed. Before investment of any type, the Sacco ensured it has taken all the risk factors to avoid losses like in the event of loans to ensure they are not totally defaulted. There was an assessment of the market before any commitment to be aware of the possible market risks. The organizations also have a working liquidity risk policy that enables them to account for wealth in terms of assets.

Loan repayment period objective was a major concern in the Saccos where repayment of loans have a consideration of all the members to make sure they are able to repay their loans within a favorable period thus reducing the rates of loan defaults. Those with loans were allowed sufficient time to be able to repay their loans in full. Members were also allowed some grace period before they could start repayment of their loans to allow

them to put the funds to work then they can start their installments. Loans were restructured upon request by members or in the event a member experienced difficulties from the sources of payment to enable them repay promptly. If members had issues with loan repayment and have to pay later than agreed, then there were arrangements to adjust the repayment dates to avoid penalties and fines and to ensure that loans are in positive performance.

The third objective on loan security emphasized on the need to consider the collateral and securities to be considered to ensure loans are not defaulted without which they can be recovered. Guarantors were considered as security for loans given to ensure that Saccos do not lose finances if loans are defaulted. Members were also required to have savings with the Saccos which form a basis for lending loans to them. These loans are used as a security on loans given to members to reduce the risk associated with non-payment of loans. Upon application of loans members are also expected to produce statements of accounts which help in tracing their history and helps in establishing the credit worthiness of a client. Depending on the loan one is applying for, the Sacco demands for ownership documents for the security one is offering to confirm the assets truly belongs to the applicant before they are accepted as security for the loan amount applied for.

Loan processing period objective affirmed that SACCOs put much effort in ensuring the loans do not take too long before they are disbursed as long as the applicant has complied to all the requirements. The institutions ensure they do not accumulate loan forms for loan applications. This reduced the processing time for loans applied and improves on loan performance. The waiting period for loans is also reduced to enable

the SACCOs disburse many loans and be able to hit their targets set for specific periods. SACCOs have amounts set to be disbursed in a day thus in some cases determine the performance of loans and finally the periods for waiting after loan application may be longer if the applicant is not able to comply to the loan requirement policy with the expected speed. Some of the requirements also may need more time before they are met hence delaying the period for loan processing and affecting performance of loans.

5.3 Conclusions

In conclusion, the financial risk policy may not be made available to all or even may not be understood by all. The policy on financial risk may also be present but not in practice thus posing a risk to the SACCO since finances may be lost due to laxity and lack of seriousness in practice. Operation risk policy was not totally utilized thus led to losses in some instances as the funds were not used for the purpose intended fully leading to poor overall performance of loans. Some SACCOs did not consider the risk factors associated with loans and developments hence suffered losses and poor performance of loans. While the business could have chances of thriving and outperforming its competitors, failure to assess the market risk was evident in some SACCOs that made the loans perform poorly especially were they were not aware of what the market offered and what it was ready to take. Most SACCOs had a liquidity policy that enabled them to account for finances in terms of assets and be able to anticipate for any possible loss associated with the loans.

The study also concluded that there were guidelines in place to regulate the loan repayment period to ensure all are complying though in some cases, clients were unable

to comply since they felt the installments period was not sufficient for loans taken thus loans did not perform as expected. Most SACCOs allowed a grace period after disbursement of loans though not all the SACCOs allowed the grace period. This period was meant for clients to reorganize themselves even as they start repayment of installments as per the loan agreement. In the event of unnormalcies, loan restructuring was considered in some SACCOs allowing the loans to be serviced with reduced cases of defaults. Late payment was treated with a lot of seriousness and follow up was keenly done in most of the SACCOs. This helped in ensuring the loans were fully paid and ensured loan performance was on a positive curve.

Objective three concluded that SACCOs had loan security policies that provided a guideline on the securities that were acceptable for one to qualify for a loan. The guidelines provided for a guarantor policy that explained the qualifications one needed to have to qualify to be a guarantor. All the SACCOs required one to have a guarantor as a form of security for a loan to be issued. This enhanced trust and confidence that the clients would pay since they had a link to access the client in case in default. Savings were also a requirement in all the SACCOs for one to qualify for some loan. They served as a security for loans applied for since they are easily accessible to the SACCOs that are issuing the loans. Anyone who had a loan in the SACCOs also had savings as per the policy on loans and savings. Those applying for loans needed to have accounts with the respective SACCOs and also upon application of loans they were required to have statements of accounts as evidence they were regular on their savings and also as security they had some form of regular income hence some form of assurance on loan repayment capability and credit worthiness. Upon loan application, the assets offered as

collateral needed to have ownership document thus all the SACCOs needed one to produce the ownership documents as security that in case one is not able to pay they could recover their monies by disposing the assets. This gave confidence to the SACCOs to issue loans with the security documents in their possession while on the other hand the clients committed to repay the loans for fear of losing their assets thus enhance loan performance.

Finally, loan processing period was an essential factor in ensuring performance of loans in the SACCOs. This was because loans meant to help in sorting out needs and once they take too long to be disbursed then it is a discouraging factor towards application of the loans. SACCOs tried not to accumulate loan forms for the loans applied and reduced the processing period through quick action on the loans applied for. The loan waiting periods in some SACCOs was not defined and this would make the loans delay hence affecting performance of loans and also loss of confidence from the clients. Some SACCOs had specific amounts to be disbursed in a day thus affecting the number of loans to be processed and issued in the effort to comply to the daily limit for loan disbursements. This in the long run affected the performance of loans since it limits on the period of processing and rate at which loans are issued as they avoid violation of the maximum disbursement policy. Some SACCOs have too much of requirements before they can process a loan thus delaying the whole process and in some other cases, the required documents are difficult to get thus some loans ends up being declined thus affecting the overall performance of loans in many SACCOs.

5.4 Recommendations

It is recommended that SACCOs should come up with a practical operational risk policy that should be known to all and practiced by all to enhance the performance of the SACCO as a unit in all aspects. Further, there should be a working credit risk premium that takes care of all the credit risks in the SACCO which also takes care of finances in form of assets to enhance performance of loans in the SACCO. It is paramount for all the SACCOs to conduct a market analysis to ensure they are aware of what is happening in the market in terms of loans before they formulate policies concerning loans to be able to understand the trend in the market, know their competitors and at the same time know what the market takes and what it offers. This could help in enhancing loan performance as the SACCO offers what is required and hence be able to compete favorably in the market. It is also important to have a working liquidity risk policy in order for SACCOs to understand their worthiness in terms of assets and credit. This will help in establishing to what level the organization extend its risk in terms of credit.

SACCOs have varied repayment periods as per their policies and guidelines. It is recommended that SACCOs should consider allocating sufficient repayment periods for loans issued to reduce chances of non-payment of loans to avoid recording poor loan performance. It is also recommended that SACCOs should consider allowing some grace period after they disburse loans to allow for the client to reorganize themselves and be in a position to start paying the installments. This is in the faith that one has put their monies to work and that it has started bearing some returns. Further the study recommends that if one is not able to fully and regularly service the loans given, they can be considered for loan restructuring to avoid cases of loan default and also ensure

the loan is still performing. The study also recommends that cases of late payment of loans should be treated individually since the cases are not identical for the SACCO to know the most appropriate action to take as per the individual case to ensure enhanced loan performance.

On the loan security objective, it is recommended that loans should always have a form of security which guarantees recovery in the event the loan is not paid as per the agreement. Further a guarantor policy should be well developed and designed and made a mandatory requirement that all clients understand the implications before committing to be a guarantor. This will help in ensuring that follow up on loan payment is an initiative for both the SACCO, the client and the guarantor thus commitment to repay. In addition the study recommends that savings contribution should be made a mandatory requirement done regularly even after the loan is issued to ensure there is more security for the loan. The study also recommends that the statements of account should be a mandatory requirement and that all of them should be certified to ensure they are genuine and can be considered a security for credit worthiness and a tool to show history on the previous loans and savings. If collateral is offered it is recommended that all ownership documents should have a serial numbers that match the items upon verification. This will help during auction in the event the loan is not paid as per the agreement thus enhance loan performance.

Finally, on loan processing period, the study recommends that forms should be acted upon as fast as possible to ensure they do not accumulate causing delays in loan process and disbursement ruining the opportunity to serve more customers and earn more income in form of interests earned through loans. It is also recommended that the loan

processing waiting period should be shortened to encourage more clients to borrow and also to be able to outperform your competitors in terms of efficiency and effectiveness. Further, the study recommends that SACCOs should review the amounts allocated as daily disbursement and try to settle for a figure that accommodates more disbursements to allow for more loans to be disbursed in a day. This will improve on loan performance as clients will not have to queue awaiting disbursements while on the other hand reduces forms accumulation. On the other hand, the study recommends that if possible the loan policy should have minimal requirements that are very necessary and reduce on too much paperwork that may be unnecessary and not even mandatory to the process. This will reduce on the number on discouraged clients who at some point in time feel the requirements are way too many in some SACCOs and tend to look for other financial facilities. If this is accomplished and the client volume increases then it leads to improved loan performance in SACCOs.

5.5 Areas for Further Research

The results from the study pointed out a number of opportunities for further research;

- i. There is need to carry out a similar study in other sub-counties in order to see if the results are similar.
- ii. There is need to investigate whether open membership policy has been established in different SACCOs
- iii. There is also need to establish the most appropriate open membership policy to be adopted in SACCOs.

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APPENDICES

APPENDIX 1: COVER LETTER TO RESPONDENT

Faith Mwari Chokera

Kenya Methodist University

School of Business and Economics

Department of Business Administration

P O B ox 267 – 60200

MERU.

Dear Sir/Madam

RE: LETTER OF TRANSMITTAL OF DATA COLLECTION INSTRUMENTS.

I am a student at Kenya Methodist University pursuing a Master's Degree in Business Administration specializing in Finance. As a compulsory requirement, I am expected to carry out a research on relationship between open membership policy and loan performance in selected Saccos in Meru County. This will assist organizations realize the importance of incorporating everyone for membership as long as they meet the necessary requirements as per the SACCO regulations in ensuring loan performance.

I humbly request that you spare a few minutes of your schedule to complete the attached questionnaire. The questions seek your opinions regarding your organization's membership policy in relation to loan performance. There are no right or wrong answers; I only need your honest opinion. Your anonymity is assured and the information you will provide will remain confidential.

Thank you for your participation in this study. Much appreciation for your cooperation and contribution in this study.

Yours faithfully,

Faith Mwari Chokera

Encl.

APPENDIX 2: RESEARCH QUESTIONNAIRE

Kindly tick [] the appropriate response or provide information as is relevant. Your responses will be anonymous and confidential and will only be used for the purposes of this study. As such, do not write your name on the questionnaire.

Section One: Demographic Information of Respondents

1. Indicate your current position in the organization.

Credit Analyst [] loan sales officer [] loan collection officer []

2. Indicate your highest level of education.

PhD. [] Master's degree [] Undergraduate degree [] Diploma []

Other specify: _____

3. Indicate your length of service in the organization.

0 - 2 years [] 3 -5 years [] 6 -10 years [] 11 years and above []

Section Two: Financial risk

This section deals with financial risk and how it is practiced in the Sacco. The following action points are evidence of the existence of financial risk measures in the Sacco. To what extent do you agree with the below statements? 1 = strongly disagree 2= Disagree 3= neither agree nor disagree 4= Agree 5= strongly agree.

STATEMENT	1	2	3	4	5
4. Operational risk budget is always set aside in the organization					
5. The risk premium in my organization considers the risk factors of an investment					
6. My organization is aware of the possible market risk					
7. My organization has a working liquidity risk policy					

Section Three: Repayment period

This section deals with repayment period and how it is implemented in the Sacco. The following action points are evidence of the practice in the Sacco. To what extent do you agree with the below statements? 1 = strongly disagree 2= Disagree 3= neither agree nor disagree 4= Agree 5= strongly agree

STATEMENT	1	2	3	4	5
8. The instalment period is sufficient for loans taken					
9. There is a grace period allowed for loans given					
10. Loans are restructured where necessary					
11. Cases of late payment are given special attention					

Section Four: Loan security

This section deals with loan security and the considerations in the Sacco. The following action points are evidence of the practice in the Sacco. To what extent do you agree with the below statements? 1 = strongly disagree 2= Disagree 3= neither agree nor disagree 4= Agree 5= strongly agree

STATEMENT	1	2	3	4	5
12. There is a guarantor policy on loans taken					
13. Members savings are considered loan security					
14. The account statements are considered					
15. Ownership documents for collateral are considered					

Section Five: Loan processing period

This section deals with loan processing period and how it is done in the Sacco. The following action points are evidence of the periods taken for the same. To what extent do you agree with the below statements? 1 = strongly disagree 2= Disagree 3= neither agree nor disagree 4= Agree 5= strongly agree

STATEMENT	1	2	3	4	5
16. Customer loan application forms accumulate so much					
17. Loan waiting period is clearly defined					
18. The loan processing period is affected by the amounts disbursed per day					
19. Requirements for compliance to loan policy affects loan processing period					

Section Two: Loan Performance

This section deals with loan performance and the trend in the institutions. The following action points are evidence of achievement of loan performance. What is the range for returns on loan interest?

STATEMENT	1	2	3	4	5
20. Interest on loans meets the set target per year					
21. Loan amounts keep on increasing every year					
22. the number of loan applicants increases every year					

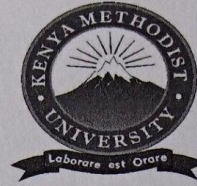
APPENDIX 3: BUDGET

S. NO.	ACTIVITY	COST(KSH)
1.	Typing	13,500
2.	Printing papers	8,500
3.	Photocopy	9,500
4.	Binding	8,500
5.	Internet	18,000
6.	Transport	8,000
7.	Telephone and letters	8,500
8.	Meals	10,000
	TOTAL	84,500

Source: Researcher, (2019)

APPENDIX 4: LIST OF SACCOS

1. Dhabiti Sacco
2. Capital Sacco
3. NyambeneArimi Sacco
4. Centinary Sacco
5. Yetusacco
6. Smart Champion Sacco
7. MMH Sacco
8. Imenti Sacco
9. Shiraji Sacco
10. Solution Sacco



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Our ref: NAC/ MBA/1/2020/15

11TH AUGUST 2020

Commission Secretary,
National Commission for Science, Technology and Innovations,
P.O. Box 30623-00100,
NAIROBI.

Dear Sir/ Madam,

RE: FAITH MWARI CHOKERA (BUS-3-0077-1/2018)

This is to confirm that the above named is a bona fide student of Kenya Methodist University, undertaking masters in Business Administration. She is conducting a research titled: **RELATIONSHIP BETWEEN OPEN MEMBERSHIP POLICY AND LOAN PERFORMANCE IN SACCOs IN MERU COUNTY, KENYA.**

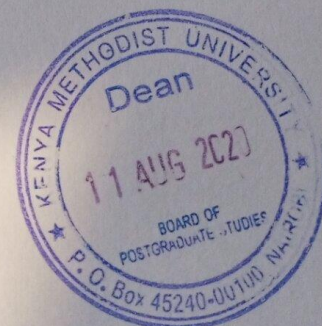
We confirm that this thesis proposal has been defended and approved by the university.

In this regard, we are requesting your office to issue a permit to enable her collect data for her masters dissertation.

Any assistance accorded to her will be appreciated.

Yours faithfully,

PROF. Evangeline Gichunge, PhD.
ASS DIRECTOR POSTGRADUATE STUDIES



Encl.



REPUBLIC OF KENYA

Ref No: 546325



NATIONAL COMMISSION FOR SCIENCE, TECHNOLOGY & INNOVATION

Date of Issue: 12/August/2020

RESEARCH LICENSE



This is to Certify that Ms. chokera mwari faith of Kenya Methodist University, has been licensed to conduct research in Meru on the topic: RELATIONSHIP BETWEEN OPEN MEMBERSHIP POLICY AND LOAN PERFORMANCE IN SELECTED SACCOS IN MERU COUNTY, KENYA for the period ending : 12/August/2021.

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Walter Mwangi

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