



CREDIT RISK MANAGEMENT ON FINANCIAL PERFORMANCE OF DEPOSIT TAKING MICRO-FINANCIAL INSTITUTIONS IN MOMBASA COUNTY

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ABSTRACT

The purpose of this study was to investigate the effect of credit risk management on financial performance of deposit taking MFIs in Kenya. The study employed a cross-sectional descriptive research design. The target population of the study was management of the 6 deposit taking MFIs which were licensed by CBK and had fully-pledged branches in Mombasa. The study employed stratified sampling technique whereby the target population was divided into different groups and those with similar characteristics were grouped in the same stratum then sample for the study was selected at random from each stratum. The study used primary and secondary data. A structured questionnaire was used to collect the primary data. Descriptive and inferential statistics were used to analyze information generated from respondents. Descriptive statistics analysis included mean and standard deviation while inferential statistics included correlation analysis and multiple regression analysis by use of Statistical Package for Social Science (SPSS) version 25. The study findings established that the loan applicant character was thoroughly performed by checking the applicant's background before credit approval consideration. The client character appraisal has a significant effect on the ability of the client to honor his/her obligations to the loan. The microfinance analyses collateral characteristics before approving loan. Also the borrower's capacity is critically appraised by the microfinance prior to loan approval and the microfinance utilizes credit score referencing whenever making decisions on credit. The study concluded that the Microfinance monitors borrower's performance after issuing the loan. This is essential for tracking the borrower's ability to repay over time and minimizes the rates of default. Microfinance conducts continuous risk assessment of the loan status and takes corrective remedies. Also Microfinance has in place credit risk monitoring systems and they have adopted internal risk rating systems. The study recommended that the Microfinance should report policy exceptions promptly to avoid uncoordinated responses. In addition, the microfinance should plan and execute collection enforcements geared towards ensuring loan remittances are in order. The study recommended that Microfinance should seek to recover defaulted amount from the guarantor after recovery from the borrower hits a snag. The microfinance should have dynamic client follow-up procedures.

Key Words: Client Appraisal, Credit Risk Monitoring, Collection Policy, Credit Terms

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INTRODUCTION

Globally, the economic crisis that occurred in 2007 and 2008 coupled with the credit crunch, credit risk management became a focus of regulatory attention on a global scale (Torban, 2020). Financial institutions must adhere to a number of qualitative requirements under Basel II, such as having an independent risk control and audit role and using risk reporting systems efficiently. The increased focus on risk management in microfinance institutions (MFIs) is a reflection of a fundamental shift among managers and regulators to better anticipate issues rather than just respond to them (Ewool & Quartey, 2021).

Microfinance institutions are a type of financial institution that offers financial aid to low-income people, the jobless, or other groups of people who are unable to access the financial aid offered by commercial banks (Perways & Krishna, 2017). MFIs operate in a setting where there are no credit histories or inescapable borrowing patterns among the clientele. MFIs, or microfinance institutions, could be a channel. They have a wide presence in many emerging economies and offer financial services to thousands of small and micro businesses. They may conceivably utilize that leverage to push changes in the business as their principal contact with these entrepreneurs frequently entails an enterprise loan.

Recently, emerging MFIs have been moving away from traditional grant funding and depending more and more on commercial bank finance. In addition to complicating credit and operational risks, growing microfinance sector interaction with the larger financial system and diversification into new geographies also introduce new hazards to the microfinance risk environment. The loan portfolio is one of an MFI's key assets, and its quality reflects loan delinquency, establishes predicted income, and determines its potential to increase its outreach and services to current clients (Ledgerwood, Earne & Nelson, 2017). Due to the lack of collateral and the fact that most of the loans made by MFIs are given to vulnerable and low-

income borrowers, the majority of these loans are considered high risk.

Exposure to credit risk continues to be a major source of issues for microfinance banks. With regard to the institutions that provide microfinance, this issue is even more crucial. Every business faces risk, and microfinance institutions are no exception. The absence or nearly absence of conventional risk mitigation tools like collateral and guarantees is what distinguishes microfinance. Therefore, managing credit risk becomes crucial for microfinance firms (Ewool & Quartey, 2021).

MFIs in Africa displayed a ROA of just 3.1% and had poor portfolio quality (Microfinance Barometer Report, 2018). African MFIs reported larger percentages of portfolios at risk, lower percentages of risk coverage, and higher percentages of non-earning liquid assets, according to a 2007 Microfinance Information eXchange (MIX) publication (Ewool & Quartey, 2021). Over the past 20 years, MFIs have seen remarkable growth in sub-Saharan Africa (SSA), expanding at a rate of 10% annually (Chikalipah, 2017). Significantly, microfinance is not only an industry that is increasingly at the center of financial inclusion; it is also a key tool for balancing consumption among the underprivileged in the SSA area.

Although the regional and institutional variety of Africa makes it difficult to generalize about the microfinance industry, there is strong evidence that the continent is continuing the worldwide trend of growing MFI regulation. Regulators frequently impose their risk management plans as more MFIs opt to become regulated institutions (Slama, 2018). In order to educate strategic choices on expanding microfinance on the continent, WWB and the Africa Microfinance Action Forum (AMAF) recently published a research that examined the successes, difficulties, and growth trends in the African microfinance sector. One outcome of the study was how few African MFIs had risk management departments in existence (Slama, 2018).

Between 2013 and 2018, Kenyan microfinance institutions expanded significantly (Kinyua, 2017). There has been significant change in the amount of new services that have been developed, the number of clients, and the variety of services and goods that are now available (Central Bank of Kenya, 2020). AMFI (2021) reports that the MFI sector's net loan portfolio expanded by 13.3% in 2018 but that its decline before taxes fell by 19% between 2017 and 2018. According to an AMFI study released in late May 2020, MFIs had limited working capital because to poor payback, which had an impact on liquidity levels. AMFI (2021) reports that as of December 31, 2020, there were 6,998 loans written off, a loan loss reserve of Ksh4.75B, and Ksh395.91M in write-offs. Total liabilities totaled Ksh65.99B within the same time period. There are 16 fully committed branches in Mombasa with a total loan portfolio outstanding of Kshs 2,031,554,311.77 (AMFI, 2021).

Statement of the Problem

According to the MFI's quarterly financial report, the sector's credit management methods, among other things, are to blame for the rise in the loan default rate (16%) and non-performing rate (15%) from Sh70.3 billion in March 2017 to Sh77.3 billion in 2018. (Kinyua, 2017). Despite using credit scoring and customer evaluation tools, MFIs still experience high default rates (20%) that have a detrimental impact on their financial success (AMFI, 2021). In addition, microfinance institutions have reported poor financial performance despite the significance and reforms in the growth of microfinance institutions in Kenya (Central Bank of Kenya, 2019). With an outstanding loan portfolio of Kshs. 2,031,554,311.77 as of December 2020, MFIs in Mombasa have continued to report a high rate of non-performing loans (AMFI, 2021). This has made it necessary to do research to determine how credit risk management affects DTMFIs' financial performance.

There is now important empirical research on credit risk management and performance. Locally, Mburu, Muathe, and Mwangi (2020) conducted research on

the loan performance and credit management procedures of commercial banks in Kenya. The financial performance of microfinancial institutions in Nairobi's Central Business District was the subject of research by Kipkirui (2018). In Kenyan microfinance institutions, Murigi (2018) looked into the relationship between credit risk management and loan performance. Few research have specifically examined credit risk management and financial performance in deposit-taking microfinance institutions in Mombasa County, despite the fact that studies on credit risk management and financial performance have been conducted. This study aimed to empirically explore the impact of credit risk management on the financial performance of microfinance institutions in Mombasa County, Kenya, in light of the above-mentioned context.

Objectives of the Study

The general objective of the study was to investigate the effect of credit risk management on financial performance of deposit taking Microfinance Institutions in Mombasa County, Kenya. The specific objectives were;

- To establish the effect of client appraisal on financial performance of deposit taking Microfinance Institutions in Mombasa County, Kenya
- To determine the effect of credit risk monitoring on financial performance of deposit taking Microfinance Institutions in Mombasa County, Kenya
- To examine the effect of collection policy on financial performance of deposit taking Microfinance Institutions in Mombasa County, Kenya
- To establish the effect of credit terms on financial performance of deposit taking Microfinance Institutions in Mombasa County, Kenya

The study was guided by the following research hypotheses

- **H₀₁**: There is no significant effect of client appraisal on financial performance of deposit

taking Microfinance Institutions in Mombasa County, Kenya

- **H₀2:** There is no significant effect of credit risk monitoring on financial performance of deposit taking Microfinance Institutions in Mombasa County, Kenya
- **H₀3:** There is no significant effect of collection policy on financial performance of deposit taking Microfinance Institutions in Mombasa County, Kenya
- **H₀4:** There is no significant effect of credit terms on financial performance of deposit taking Microfinance Institutions in Mombasa County, Kenya

LITERATURE REVIEW

Theoretical Framework

Asymmetry Information Theory

When a customer, typically the borrower, requests for a loan, there is information asymmetry since the borrower typically has greater knowledge of the potential risks and rewards associated with the business or investments for which the loan is being asked for (Arora & Kumar, 2016). Typically, the lender lacks full knowledge about the borrower and the anticipated project. Information asymmetry issues in the setting of financial institutions are typically divided into two categories: moral hazard and adverse selection (Rukwaro, 2017). Because it is illogical to devote financial resources to the monitoring and evaluation of tiny quantities of loans, commercial banks face difficulties in resolving these pervasive issues. This is due to the potential costs associated with the data required to screen applicants and monitor borrowers (Ali, 2015). As a result, MFIs encounter an information asymmetry issue when conducting their business.

This study is related to asymmetry theory because it explains how borrowers outwit lenders by taking advantage of their better knowledge of them

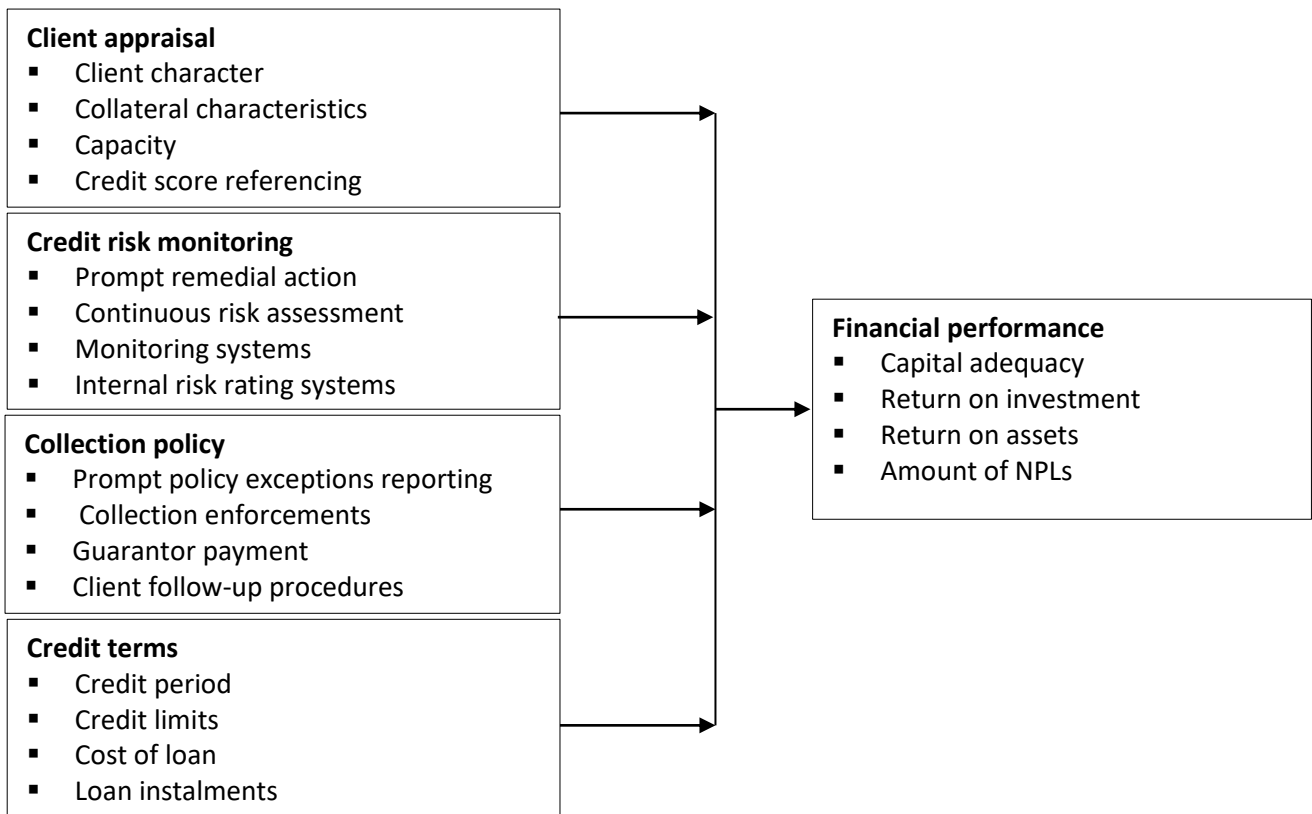
(commercial banks) by withholding some crucial information. information that could raise the rate of interest that will be charged or information that could make it more difficult to get a loan. The credit terms and conditions variable was connected to the hypothesis.

The 5 Cs Client Appraisal Model

Financial institutions employ the 5Cs model as a tool for credit management when assessing potential customers (Abedi, 2016). Collateral, character, condition, capital, and capacity are the five Cs. Character is used to estimate a customer's credit worthiness; it is typically used to weight numbers for the customer's various attributes (Njanike, 2016). It is thought that a customer's decisions are influenced by economic, cultural, and personal variables (Migiri, 2016). In a similar vein, a person's psychological well-being depends more on his or her inner worth than on any outward signs of success. Banks take these aspects into account by researching and learning more about the customer (Kibor et al., 2015).

The 5 C's Model, which states that financial institutions' loan performance is boosted by that performance, is relevant to this study. Utilizing client appraisal helps reduce default, which improves loan performance. Customer screening to determine ability and willingness to repay loans is the first step in reducing credit risk. Commercial banks use the 5Cs methodology to assess potential customers (Abedi, 2016). These aid banks in performing better and better understanding their clients. As it helps lenders better understand their clients' (borrowers') needs, the 5Cs assist banks in improving the performance of loans (Waweru & Kalam, 2016). The 5 C's model of client appraisal, however, is not taken into account when applying for the first time. The theory was linked to client appraisal variable.

Conceptual Framework



Independent Variables

Dependent Variable

Figure 1: Conceptual framework

Empirical Review

Isanzu (2017) empirically investigated the effect of credit risk on the financial success of Chinese banks on a global scale. For a seven-year period, from 2008 to 2014, secondary data were gathered from the nation's top five commercial banks. Non-performing loans, capital adequacy ratio, impaired loan reserve, and loan impairment charges were utilized in the study as measures of credit risk, while return on asset was employed as a measure of financial performance. The study's findings show that capital adequacy and nonperforming loans have a significant impact on the financial performance of Chinese commercial banks, demonstrating the importance of managing credit risk for bank financial performance. Data analysis was conducted using a balanced panel data regression model.

A study on the correlation between credit terms, credit, and performance of agricultural cooperatives in Rwanda was conducted by Byaruhanga (2017). 196 active agricultural cooperatives were chosen at random from a variety of districts in the southern province. Models of correlation and regression were applied. The results showed a strong and significant correlation between lending terms, credit availability, and agricultural cooperative performance.

A study on the impact of credit management on the financial performance of commercial banks in Rwanda was conducted by Kagoyire (2018). The research used a descriptive survey methodology. 57 workers of Equity Bank's credit department made up the study's target demographic. The entire population was employed as the sample, yielding a 57-person sample. The entire population was included in the sample process using a purposeful

sampling strategy. The researcher administered questionnaires to the respondents in order to gather primary data. To examine the data, descriptive and inferential statistics were utilized. The study discovered that the financial performance of Equity Bank was impacted by client evaluation, credit risk management, and collection policies.

In their 2017 study, Njeru, Mohammed, and Wachira looked at the impact of credit appraisal effectiveness on Kenyan commercial banks' loan performance. The research design was descriptive. Using a self-administered questionnaire, data was gathered. The performance of commercial banks was found to be significantly influenced by credit appraisal. Findings also showed that lending depended heavily on the use of historical data; as a result, credit history and references were used more frequently in credit appraisal.

The impact of debt collection tactics on the financial performance of local authorities in Kenya was the subject of a study by Wambugu (2017). There was a descriptive analysis as well as a correlation and regression analysis. Through the use of a questionnaire, data was gathered. The study discovered that proactive debt collection techniques had a negative association with the number of debts while subcontracting to third parties and enforcement strategies had a positive link.

METHODOLOGY

Cross-sectional survey research design was used for the study. There were 13 regulated microfinance banks in Kenya, according to CBK (2020). However, the management of the six deposit-taking MFIs with fully operational branches in Mombasa and a CBK license served as the study's target population. The sample size was determined using Slovin's formula. The key data for this investigation were research data. Close ended questionnaires that were organized depending on the research objectives were used to gather the primary data. Statistical Package for Social Sciences (SPSS) version 25 was used to analyze the collected data. To give

significance to the data gathered, descriptive statistics in the form of mean and standard deviation (SD) were used. Financial performance (dependent) and credit risk management were correlated using inferential statistics like linear regression and Pearson's correlation (independent). The following linear regression model was adopted to test the statistical significance of the study predictor variables on dependent variable;

$$Y = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4 + \epsilon$$

Where:

Y= Financial performance

β_0 = Regression intercept

β_1 - β_4 are the coefficient of the regression model

X_1 = Client appraisal

X_2 = Credit risk monitoring

X_3 = Collection policy

X_4 = Credit terms

ϵ = Error term

FINDINGS AND DISCUSSIONS

Descriptive Analysis

Utilizing statistical techniques to describe the population under study is a part of descriptive analysis. The responses to each of the variable's items, as well as their means and standard deviation, were included in this section.

Client Appraisal

The study examined the descriptive statistics for the variable to determine the impact of client evaluation on financial performance. A five-point Likert scale was used to gauge the respondents' level of agreement, with 1 denoting strong disagreement, 2 disagreement, 3 neutrality, 4 agreement, and 5 strong agreement. The average of each person's ranking on each item was calculated to create the client appraisal index. Therefore, the derived mean served as an index for client evaluation. According to Table 1's findings, respondents concur that microfinance evaluates collateral qualities before issuing loans and that it considers a borrower's character before making a credit decision, as indicated by means of 4.17 and

4.23, respectively. Additionally, respondents felt that the borrower's capacity is critically evaluated (mean: 4.02; median: 4.26); and that microfinance

uses credit score references while making lending decisions.

Table 1: Client Appraisal

	Mean	Std. deviation
The microfinance examines the borrowers character prior to making credit decision	4.17	.231
The microfinance analyses collateral characteristics before approving loan	4.23	.536
The capacity of the borrower is critically appraised	4.02	.444
The microfinance uses credit score referencing in making credit decisions	4.26	.703

Credit Risk Monitoring

The purpose of the study was to look into the relationship between employee commitment and assessed policies and practices in Kenyan state businesses. A five-point Likert scale was used to gauge the respondents' level of agreement, with 1 denoting strong disagreement, 2 disagree, 3 undecided, 4 agree, and 5 strongly agree. According to a mean of 4.41 and 4.26, respectively, Table 2

demonstrates that respondents agreed that microfinance continuously assesses risk and monitors borrower performance. Respondents also concurred that credit risk monitoring systems are in place in microfinance (mean: 4.15). The assertion that the Microfinance has developed internal risk evaluation methods received neutral responses from respondents (mean=3.01; range=0–3).

Table 2: Credit Risk Monitoring

	Mean	Std. Deviation
Microfinance monitors borrowers performance and prompt remedial action is taken	4.41	.817
Microfinance conducts continuous risk assessment	4.26	.634
Microfinance has in place credit risk monitoring systems	4.15	.509
The Microfinance has adopted internal risk rating systems	3.01	.822

Collection Policy

A Likert scale of five points (1–5) was used to gauge the respondents' degree of agreement, with 1 denoting very high agreement and 5 denoting very low agreement. According to a mean of 4.13 and a mean of 4.20, respectively, respondents agreed that

Microfinance swiftly discloses policy exceptions and that Microfinance performs collection enforcements. Additionally, respondents concurred that the microfinance has dynamic customer follow-up procedures and recovers default amounts from the guarantor (mean: 4.82; median: 4.89).

Table 3: Collection Policy

	Mean	Std. Deviation
Microfinance promptly reports policy exceptions	4.13	.882
Microfinance conducts collection enforcements	4.20	.887
Microfinance recovers default amount from the guarantor	4.82	.883
The microfinance has dynamic client follow-up procedures	4.89	.881

Credit Terms

The researcher examined the descriptive statistics for the chosen variables in order to look into the relationship between compensation and employee commitment. The degree of agreement among the responses was assessed using a Likert scale with five possible outcomes: strongly disagree (1), disagree (2), disagree (3), undecided (4), agree (4), and strongly agree (5). According to a mean of 3.66

and a mean of 4.66, respectively, respondents agreed that microfinance offers flexible credit payback periods to borrowers and places credit limitations on the high risk clients. Additionally, respondents concurred that Microfinance offers modest loan costs for its loans (mean=4.52) and that the loan repayment installments are proportionate to the loan amount (mean=4.04).

Table 4: Credit Terms

	Mean	Std. Deviation
Microfinance offers flexible credit repayment period to the borrowers	4.66	.753
Microfinance puts credit limits on the high risk clients	4.66	.748
Microfinance provides its loans with low loan cost	4.52	.741
The Microfinance loan repayment installments are commensurate to the amount of loan taken	4.04	.756

Correlation Analysis

The Pearson correlation coefficient (r), which produces a statistic with a range of -1 to 1, was employed by the researcher to analyze the degree of link between two variables. The strength of the link between the relevant variables is demonstrated through correlations. The Pearson's Product Moment was used to obtain inter-correlation coefficients (r). A researcher can find out the size and direction of the relationship between two variables using the Pearson correlation coefficient; the higher the coefficient, the more strongly the two variables are related.

According to Table 5's correlation data, client appraisal and financial success are significantly positively correlated. Table 5, which shows that the p-value was at 0.000 and that this fulfilled the criterion because $p < 0.05$, provided evidence of this. The correlation coefficient of 0.568 indicated that the association was positive. The correlation results

also demonstrate a strong positive association between credit risk management and financial performance. Table 5, which shows that the p-value was at 0.000 and that this fulfilled the criterion because $p < 0.05$, provided evidence of this. The correlation coefficient of 0.453 indicated a positive association.

The relationship between the collecting strategy and the financial results was both significant and favorable. Results showed that the p-value was at 0.01 and that this met the criteria since $p < 0.05$, provided evidence of this. The correlation coefficient of 0.284 indicated a positive association. The correlation data demonstrate a strong positive association between credit terms and financial performance. Results, which shows that the p-value was at 0.000 and that this fulfilled the criterion because $p < 0.05$, provided evidence of this. The correlation coefficient of 0.402 demonstrated the existence of a positive link.

Table 5: Correlation Matrix

		Client appraisal	Risk monitoring	Collection policy	Credit terms	Financial performance
Client appraisal	Pearson Correlation	1				
	Sig. (2-tailed)					
	N	59				
Credit risk monitoring	Pearson Correlation	.742**	1			
	Sig. (2-tailed)	.000				
	N	59	59			
Collection policy	Pearson Correlation	.613**	.407**	1		
	Sig. (2-tailed)	.000	.000			
	N	59	59	59		
Credit terms	Pearson Correlation	.596**	.772**	.251**	1	
	Sig. (2-tailed)	.000	.000	.000		
	N	59	59	59	59	
Financial performance	Pearson Correlation	.568**	.453**	.284**	.402	1
	Sig. (2-tailed)	.000	.000	.010	.000	

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

Regression Analysis

A regression model was adopted in the study to establish the statistical relationship between the

credit risk management and financial performance of deposit taking Microfinance Institutions in Mombasa.

Table 6: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.678 ^a	.461	.428	1.9620

a. Predictors: (Constant), Client appraisal, Credit risk monitoring, Collection policy, Credit terms

A moderate relationship between the research variables was seen in the regression results. According to the model summary's coefficient of

determination (R²) of 0.461, predictors can account for a change of 46.1% in the financial performance of MFIs that accept deposits.

Table 7: Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2068.395	4	517.098	11.542	.000 ^b
	Residual	2419.218	54	44.800		
	Total	4487.613	58			

a. Dependent Variable: Financial performance

b. Predictors: (Constant), Client appraisal, Credit risk monitoring, Collection policy, Credit terms

The significant value for testing the model's dependability was determined to be 0.000, which is

less than 0.05, the critical value at the 95% significance level, according to the ANOVA results in

Table 7. As a result, the model successfully predicts the association between DTMFIs' financial performance and credit risk management.

Table 8: Regression Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
(Constant)	10.660	3.171		3.361	.000
Client appraisal	.519	.204	.491	2.509	.000
Credit risk monitoring	.481	.189	.463	2.576	.030
Collection policy	.203	.101	.188	2.009	.042
Credit terms	.416	.145	.394	2.868	.000

a. Dependent Variable: Financial performance

The derived regression coefficients of the model are:

$$Y = 10.660 + .519X_1 + .481X_2 + .203X_3 + .416X_4$$

The findings of the regression analysis indicated that all of the important independent variables had significant values below 0.05. The findings indicated that the change in financial performance would be 10.660, maintaining all other variables constant at zero. The regression analysis's findings also revealed that a unit change in client evaluation would result in a 0.519 unit change in financial performance. Financial performance would fluctuate by 0.481 units for every unit change in credit risk monitoring. A unit change in credit conditions would result in a 0.416 unit change in the financial performance of deposit-taking MFIs in Mombasa County, while a unit change in collection policies would result in a 0.203 unit change.

Discussion of Key Findings and Hypothesis Testing

Regression analysis supplied a platform for fulfilling research objectives selected in this study. The study's first goal was to look into how clients rated deposit-taking microfinance firms' financial performance. The results of the conducted regression analysis, which were 1 = 0.519, t = 2.509, and p 0.05, demonstrated that there was a significant and favorable influence. A unit change in customer appraisal efforts, according to the study, would result in a 0.519 unit change in financial performance. Furthermore, the null hypothesis that

client appraisal has no significant impact on financial performance is rejected because the p-value is less than 0.05.

The second goal was to look into how credit risk monitoring affected deposit-taking microfinance institutions' financial performance. The results of the regression analysis suggested a substantial and favorable influence, as shown by the numbers 2 = 0.481, t = 2.576, and p0.05. According to the study, financial performance would fluctuate by 0.481 units for every unit change in credit risk monitoring. The null hypothesis that credit risk monitoring has no meaningful impact on financial performance is rejected in hypothesis testing because p0.05.

The third goal of the study was to investigate how collection policy affected financial success. The results of the regression analysis indicated a substantial and favorable influence, as indicated by the numbers 3 = 0.203, t = 2.009, and p0.05. According to the study, a unit change in collecting strategy would result in a 0.203 unit difference in financial performance. The null hypothesis that collection policy has no meaningful impact on financial performance is rejected based on hypothesis testing because p 0.05.

The goal of the study was to determine how credit terms affected deposit-taking microfinance institutions' financial performance. The results of the regression analysis indicated a substantial and favorable influence, as indicated by the numbers 4

= 0.416, $t = 2.868$, and $p < 0.05$. According to the analysis, financial performance would fluctuate by 0.416 units for every unit change in credit terms. The null hypothesis that credit terms have no meaningful impact on financial performance is rejected by hypothesis testing because $p < 0.05$.

CONCLUSIONS AND RECOMMENDATIONS

According to the study's findings, a thorough evaluation of a loan applicant's character occurs before credit approval is taken into account. The client's capacity to uphold the loan's conditions is strongly influenced by the client's character assessment. The conclusion is that before approving a loan, microfinance examines the features of the collateral. Prior to loan acceptance, the microfinance company also conducts a thorough evaluation of the borrower's capacity and always refers to credit scores when making credit choices.

The study comes to the conclusion that after lending money, microfinance keeps an eye on the borrower's progress. This reduces the likelihood of default and is crucial for tracking the borrower's capacity to pay back over time. Microfinance continuously assesses the danger of the loan situation and implements remedial measures. Additionally, credit risk monitoring tools and internal risk assessment systems have been implemented by the microfinance industry.

The study comes to the conclusion that the Microfinance immediately notifies policy exceptions and undertakes collection enforcements to make sure the loans are remitted in a timely manner. The study comes to the conclusion that microfinance has dynamic client follow-up procedures and recovers default amounts from the guarantor in cases where the debtor fails to pay the cash after an acceptable amount of time.

The study comes to the conclusion that the borrower can choose a flexible credit payback time using microfinance. The borrowers may now fulfill their debts to the MFI thanks to this. Additionally, the study finds that when a client is not a high-risk borrower, the MFI offers loans with cheap loan

costs and places credit limitations on the clients who pose a credit risk. The amount of the loan provided to the borrower is a factor in the microfinance loan payback installments.

The report suggested that behavioral systems be purchased by microfinance to aid in doing background checks on loan applicants. This is acceptable since human subjectivism can result in disastrous decisions, which would cost the MFI. Before approving the loan, the microfinance should examine the borrower's provided collateral qualities. Before approving the loan, the microfinance institution should closely evaluate the borrower's capacity and use credit score referencing if the borrower's background check does not produce meaningful results.

The study suggested that microfinance should have a system in place to regularly check on a borrower's progress once a credit decision has been made. By doing this, the microfinance will be able to identify any irregularities in the borrower's remittance habits and prevent potential loan default. This project has the potential to significantly reduce the risk of loan default. Microfinance should continuously examine the danger of the loan situation and start implementing remedial measures. In order to improve the efficiency of the monitoring operations, the microfinance industry should also employ systems for credit risk monitoring.

The study advised the Microfinance to notify policy exceptions as soon as can to prevent disorganized replies. In order to make sure loan reimbursements are made on time, the microfinance organization should also plan and carry out collection enforcements. The study suggests that, if recovery from the borrower runs into trouble, microfinance should try to recover the defaulted amount from the guarantor. The microfinance should implement flexible client follow-up methods.

The study suggested that microfinance institutions should give borrowers flexible credit repayment terms. Due to the MFI's flexibility regarding the loan

payback time, struggling borrowers can simply return the whole amount of their loan. Credit limits should be imposed by the microfinance on the high risk clients. When a customer is not a high-risk borrower, the MFI should also offer loans with low loan costs, and the loan repayment installments should be determined in relation to the amount of credit extended.

Areas of Further Study

The investigation into credit risk management and financial performance in the context of deposit

taking MFIs has been restricted. However, the researcher advises that a study be conducted on additional credit risk management components that have an impact on the financial performance of deposit accepting MFIs because only 42.8% of the change in financial performance was explained by the adopted constructs. The report suggests that additional research be done on other industries, such as Saccos and non-deposit taking MFIs, to look into how credit risk management can affect the financial performance of these industries.

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