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BORROWER DETERMINANTS OF LOAN REPAYMENT IN COMMUNITY VILLAGE BANKS (VICOBA) IN LUSHOTO DISTRICT TANZANIA: A CASE STUDY OF MSHIKAMANO VICOBA

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Abstract

Village Community Banks (VICOBA) are the fastest growing and highly dependable MFIs among the majority of people in Tanzania particularly the rural poor who usually lack collaterals as pre-requisite of loan application in commercial banks which are centralised in urban areas. Despite the rapid development in microfinance institutions, sustenance of VICOBA in Tanzania remains uncertain because of inadequate information regarding their performance including the repayment of loans by borrowers. This study examined borrower determinants of loan repayment in VICOBA in Tanzania particularly for Mshikamano VICOBA. A cross-sectional research design was adopted whereas quantitative approach was applied. The study used stratified random sampling to select 62 borrowers including loan repayment defaulters and loan repayment non-defaulters from a total of 73 borrowers of 2018 VICOBA operational cycle. Structured questionnaire was used as an instrument of data collection. SPSS was used to run descriptive statistics and binary logistic regression analysis. The results show that there was 70% default rate of in Mshikamano VICOBA which is high. Borrower determinants of repaying loan in Mshikamano VICOBA include gender (β2= -3.564, p=0.018), business (β6= -2.073, p=0.023) and amount of loan (β9= 0.000, p=0.049). The study recommends that VICOBA should establish and adopt an effective appraisal system which will consider gender, business experience and size of loan requested to scrutinize potential borrowers in order to avoid loan repayment defaults

Keywords: VICOBA, MFIs, loan repayment, borrower, default loan, non-default loan.

1. INTRODUCTION

Microfinance is not a new conception in financial sector since savings and credit community groups have been operating in many countries. For instance, in Ghana it is known as “susus”, “chit funds” in India, “tandas” in Mexico, “tontines” in West Africa and “pasanaku” in Bilivia (MCGE, 2009). In Tanzania, rural microfinance operates in different forms but among the most famous informal microfinance schemes is known as Village Community Banks (VICOBA). According to UNDP (2003), microfinance referred as an option of financial service to the poor people who are lacking collaterals required by commercial banks. For many decades, since they are neglected by commercial banks, poor people have been operating savings and credit schemes (Ngalemwa, 2013). Rural and community banks, popularly called community banks including VICOBA in Tanzania are microfinance institutions which are operated and managed by members usually the poor through purchasing of shares. VICOBA

and other informal microfinance schemes have a great role in promoting savings and credit extension among the low income people especially in the rural areas (Evans, 2015).

The VICOBA scheme in Tanzania was initiated by CARE international non-governmental organisation in 2002. The goal was to address challenges related to credit and development of poor people to help own and operate microfinance institutions as a way of reducing income poverty (Mkombe, 2005). In the VICOBA scheme, shares of the bank are owned by members through purchasing. The scheme is governed using by-laws and regulations where members invest their shares throughout the financial year and have access to loans for generating income generating activities for an agreed period (Kombe, 2005). However, during their operations, VICOBA usually encounter a problem of loan repayment default from some of their borrowers. Default due to failure to repay loans within specified period of contract have adverse effects on the performance of MFIs such as VICOBA since loan default increases costs of operation and loss of properties of borrowers (Maigua, 2017).

Village banks in Tanzania are among the MFIs run by community members in form of informal banks to enhance their access to loans and saving especially in remote areas where many people have very limited access to loans from commercial banks and other MFIs. However, failure to repay the loans and delayed repayment of loans have been constraining the performance of VICOBA and hence, limit the poor to improve their livelihoods. Loan defaults diminish access to loans among members and consequently the VICOBA fails to support fighting poverty and enhance sustainability (Pasha&Negese, 2014). Borrower information is important for VICOBA loan management in order to continue operate in efficient way by enhancing loan repayment performance, generate profits, continue providing quality services and eventually contribute to improved living condition. However, there still unclear knowledge about borrower determinants of loan repayment in VICOBA in Tanzania despite some few studies which which have already done assessing VICOBA operations (e.g. Muganyizi, 2015; Brown et al, 2015; Lushakuzi, 2017). This study was carried out to address the information gap by exploring borrower determinants of loan repayment in VICOBA in Tanzania, using Mshikamano VICOBA in Lushoto District as a case study. The specific objectives were; to assess loan repayment performance in Mshikamano VICOBA in Lushoto District Tanzania; and to examine borrower factors affecting loan repayment in Mshikamano VICOBA.

2. LITERATURE REVIEW

2.1 Theoretical literature review

This study used concepts of Information Asymmetry to explain loan repayments and the criteria of granting loans to the applicants in MFIs including VICOBA. The Information Asymmetry Theory posits that borrower usually have very understanding regarding the project risks receiving fund than lender. This results to adverse selection of loan applicant by lender (Mathews&Thompson, 2008). Improper borrower selection may reduce the efficiency of the transfer from benefits to deficit (Kariuki, 2014). The theory put forward that in order to enhance selection to obtain potential borrower, banks and MFIs must establish long-term relationships with clients, promote information sharing and applying delegated monitoring of borrowers.

Theoretically, loan repayment may have better and poor repayment rate. Loan repayment policy and borrower information necessary for appraisal of loan application may vary between MFIs. The VICOBA loan is considered to be default if has not repaid for three or more instalments within a month (Fund & Bureau, 2006 cited in Maigua, 2017). Similarly, According to Phillips & VanderHoff (2004), default of loan repayment is a failure of borrower to repay principal or interest. This study refers default loan as failure by member to pay back the loan within a specified time of a contract.

This theory is relevant to VICOBA loan operation since it informs lenders that before providing loan, borrower must have a long-term relationship with MFIs; must have sufficient and relevant information such use of loan, previous repayment record and business plan; and efficient loan monitoring procedures in order to avoid loan repayment default.

2.2 Empirical literature review

The study carried out by D'Espalliers et al. (2011) revealed that females are better payers of loans because they are usually committed to loans due to their historical poor access to credits. In contrast, Richman & Fred (2010) revealed that male clients have demonstrated good repayment in MFIs which are dominated by males. The influence of age show that younger borrowers are defaulters because they are have frequent migration from rural areas to urban areas for searching better employment and social life (Oke et al., 2007).

Access to training meeting among borrowers is associated with loan repayment in MFIs (Olomola, 2000). Basing on education level of clients of MFIs, borrowers with better education demonstrate a higher efficiency in business and hence better repayment of loans (Bhatt & Tang, 2002). The influence of experience in business of clients reveal that borrowers having better experience in business are very successful and consequently non defaulters in MFIs. Armendariz & Morduch (2010) and Madajewics (2004) found that larger loan amount is associated to default as borrowers may invest the loan in risky or irrelevant business.

Pasha & Negese (2014) assessed socio-economic factors and loan related factors that determine loan repayment performance among borrowers in Sidama MFI in Ethiopia. Bothe primary and secondary data was collected. The 296 (10%) respondents were selected using simple random sampling technique. Results show that age, education, time laps, loan size, loan diversion, repayment period, number of dependants, training and supervision were significant factors of loan repayment and negatively related except education, level and time lapse of loan contract.

Haile (2015) examined the determinants of performance in loan repayment in Harai Microfinance Institution in Ethiopia. A randomly selected sample of 120 respondents comprising of 50% loan defaulters and 50% non-defaulters was used in the study. The collected data was analysed descriptively and by using logistic regression. The results show lack of training, negative perception on loan repayment duration, size of the family, lack of experience in business, lack of diversified income sources and poor saving culture increase the chance of borrower to be a defaulter.

3. MATERIALS AND METHODS

The study population comprised of 73 loan borrowers who are members of Mshikamano VICOBA provided loans in 2018. Mshikamano VICOBA was selected by using purposive sampling since it has existed for more than three years while operating as rural microfinance which provide financial services including saving and credit as well as community support fund to its members. Many of Mshikamano VICOBA members have poor access to loans from commercial banks and other financial institutions. From the survey population, the sample size was obtained by using Slovins's as shown below:

$$n = \frac{N}{1 + Ne^2} = \frac{73}{1 + 73(0.05)^2} = 62$$

Whereby,

n is minimum sample size; ***N*** is survey population and ***e*** is error at 95% confidence interval.

From sample size calculated, the study used stratified random sampling to select 43 loan repayment defaulters and 19 loan repayment non-defaulters (Table 1).

Category of borrowers	Total Number of borrowers	Number of selected borrowers
Defaulters	51	43
Non-defaulters	22	19

Table: 1 Sample stratification of VICOBA loan borrowers

The study used survey method to collect quantitative data through self-administered structured questionnaire. Independent variables of the research are possible borrower factors which were adopted from previous empirical studies (e.g. Ochung, 2013; Muganyizi, 2015; D'Espallier et al., 2011; Olomola, 2000; Bhatt & Tang, 2002; Armendariz & Morduch, 2010) (Table 2).

Variable	Measurement
X_1=age	Years
X_2=gender	1=if male, 0=female
X_3=education	1=if primary education, 0=otherwise
X_4=marital status	1=if married, 0=otherwise
X_5=employed in farming	1=if farmer, 0=otherwise
X_6=employed in business	1=if business dealer, 0=otherwise
X_7=experience	1=if loaned in the past, 0=otherwise
X_8=dependants	Number of dependants
X_9=size of loan	Tanzanian Shillings

Table: 2 Independent variable of the study

This study assumed that independent variables (borrower factors) have effect on dependent variable (VICOBA loan repayment). SPSS computer software was applied to run binary logistic regression which examined borrower factors which affect paying back of loan in Mshikamano VICOBA. Loan repayment as a dependent variable was measured using binary indicators, coded 1 if loan repayment defaulter and 0 if loan repayment non-defaulter. The logistic regression model and explanations are presented below.

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + \beta_7 X_7 + \beta_8 X_8 + \beta_9 X_9 + \epsilon_t$$

$$Y = \frac{Odds}{1 - Odds} = \frac{exp\ (\beta)}{1 - exp\ (\beta)}$$

Whereby;

Y = dependent variable (loan repayment). Y=1 if defaulter, Y=0 if non-defaulter

Odds=exp (β) is a chance for occurring loan defaulter in VICOBA

X_1, X_2, X_3, X_4, X_5, X_6, X_7, X_8 and X_9 are independent variables (borrower factors)

β_1, β_2, β_3, β_4, β_5, β_6, β_7, β_8 and β_9 are coefficients of Xs (independent variables)

β_0 = constant term

ϵ_t = error term

4. RESULTS AND DISCUSSION

4.1 Demographic characteristics of respondents

From the sample size of 62 respondents who borrowed loans from Mshikamano VICOBA, 61 of them filled and returned the questionnaire. The survey identified that respondents have different demographic characteristics as shown in Table 3. The demographic characteristics surveyed include gender, marital status, occupation, age and education

Variable	Measurement
Gender:	
Male	11.5%
Female	88.5%
Marital status:	
Married	70.5%
Single	3.3%
Widow	26.2%
Main occupation:	
Farmer	90.2%
Business	8.2%
Housewife	1.6%
Age:	
20-29years	18%
30-39years	18%
40-49years	34.5%
Above 49years	29.5%
Minimum	20years
Maximum	68years
Mean + SD	42.9±12.9years
Education:	
Non-formal education	9.8%
Primary school education	80.4%
Secondary school education	9.8%

Table: 3 Distribution of respondents based on demographic characteristics

Most of respondents were females (88.5%) and only 11.5% comprised males. Large number of females was identified to be members in VICOBA, and this is justified that women usually lack assets which can help them to obtain loans provided by formal MFIs such as banks compared to males who traditionally and socially given opportunity to own and control economic assets such as land, houses and livestock in Tanzania. Therefore, males can use assets as collaterals to obtain loans or sell to obtain capital for business, and hence majority of males have no much demands to join VICOBA. Marital status of survey participants show that 70.5% constituted married respondents and 26.2% comprised widows. A few number of respondents constituted women who are single since they are not yet married.

Moreover, the survey identified that main occupation of most respondents was smallholder farming (90.2%) while a few number of participants comprised business dealers (8.2%) and housewives who are unemployed (1.6%). Based on age distribution, majority of respondents had 40 to 49 years (34.5%) and 29.5% had age above 49 years. Young people aged 20-29 years constituted about 18% of survey participants. Other respondents (18%) belong to a middle age group of adults from 30 to 39 years. The minimum age of respondents was 20 years and maximum age was 68 years. An average age of survey participants was 42.9 years having the standard deviation 12.9.

The level of education show that most of participants completed primary school education (80.4%) and a few possessed secondary school education (9.8%). On the other hand, only 9.8% of respondents lack formal education because they never attended formal educational institutions such as primary school. Since majority of VICOBA members completed formal schools, they can easily understand instructions and training because they are able to write and read books of business skills and financial management.

4.2 Loan repayment of borrowers in Mshikamano VICOBA in Lushoto District

The study assessed loan repayment in Mshikamano VICOBA by using three measurements including number of defaulters, number of non-defaulters and rate of default loans (Table 4).

Total number of members	Total Number of borrowers	Number of Non-defaulters	Number of defaulters	Rate of default loans
91	73	22	51	70%

Table: 4 Default loans and non-default loans in Mshikamano VICOBA

According to Mshikamano VICOBA operation cycle for the year of 2018, there were 73 borrowers among the 91 total members. Based on loan repayment contract agreed by VICOBA and borrowers, 22 borrowers completed repayment of their loans on time. However, 51 borrowers didn't afford to complete repayment their loans on time. Therefore, the rate of default loans for 2018 operation cycle of Mshikamano VICOBA was 70%. Following such high rate of loan default, VICOBA management team decided to take part of shares contributed by defaulters like other members to recover their outstanding loans.

4.3 Borrower factors affecting loan repayment in Mshikamano VICOBA in Lushoto District

The study used binary logistic regression to examine borrower factors which affect repayment of loan in Mshikamano VICOBA. In a logistic regression model presented in Table 5, Omnibus test of model coefficients has revealed the model fitness. In the model fitness test, block 1 provided significant results following addition of explanatory variables.

		Chi-square	df	Sig.
Step 1	Step	20.716	9	0.014
	Block	20.716	9	0.014
	Model	20.716	9	0.014

Table: 5 Omnibus tests of model coefficients

The results from Omnibus tests show that a p-value (sig.) of Chi-square for block is 0.014 which is significant at 5% level. This means that block 1 model as a result of addition of explanatory variable is a significant improvement to the block 0 model (before addition of explanatory variables). Results revealed by Omnibus tests of model coefficients justify that there is a good fitness of logistic regression model to the data. The model summary in Table 6 provided 2 pseudo R^2 (Cox & Snell R^2 and Nagelkerke R^2**)** which both measure the variation in dependent variable brought by explanatory variables in the logistic regression model.

Step	-2 Log likelihood	Cox & Snell R^2	Nagelkerke R^2
1	54.958	0.288	0.405

Table: 6 Model summary

From Table 6, the study justify that between 28.8% and 40.5% of the variation in loan repayment in Mshikamano VICOBA can be explained by the model in block 1. Results revealed by logistic regression analysis shown in Table 7 indicate the effect of borrower factors on loan repayment in Mshikamano VICOBA. Loan repayment was measured by using binary indicators; coded as 1 if loan repayment default and 0 if loan repayment non-default.

Borrower factor	β	S.E.	Wald	Sig.	Exp(β)	95% C.I. for Exp(β)	
						Lower	Upper
Constant	2.787	3.062	0.829	0.363	16.229		
Age(X_1)	0.023	0.035	0.437	0.509	1.023	0.956	1.096
Gender(X_2)	-3.564**	1.503	5.626	0.018	0.028	0.001	0.538
Education(X_3)	0.731	1.017	0.517	0.472	2.078	0.283	15.253
Marital status(X_4)	1.285	0.979	1.723	0.189	3.615	0.531	24.620
Farming(X_5)	-1.344	1.336	1.011	0.315	0.261	0.019	3.582
Business(X_6)	-2.073*	0.914	5.142	0.023	0.126	0.021	0.755
Experience(X_7)	-2.083	2.507	0.690	0.406	0.125	0.001	16.962
Dependants(X_8)	0.263	0.202	1.683	0.194	1.300	0.875	1.933
Size of loan(X_9)	0.000*	0.000	3.872	0.049	1.000	1.000	1.000

*significant at p<0.05; **significant at p<0.01

Table: 7 Logistic regression analysis of borrower factors affecting loan repayment in Mshikamano VICOBA

Among the 9 assessed borrower factors shown in Table 7, three (3) of them including gender, business and size of loan have significant affects on loan repayment in Mshikamano VICOBA. Gender and business have negative relation with loan repayment default and hence, the two factors are decreasing the likelihood of a loan borrower to be a defaulter. Size of loan has positive influence on loan repayment default and therefore, it increases the likelihood of Mshikamano VICOBA loan borrower not complete paying back of loan on time of agreement.

A significant negative effect of gender on loan repayment justifies that male borrower in Mshikamano VICOBA is most likely not become a defaulter (β_2= -3.564, p=0.018). One unit increase in gender (being a male borrower) may results to decrease for a chance of loan repayment default by exp (β_2) = 0.028. The Wald statistics of 5.626 justifies a strong relationship between gender and loan repayment. Moreover, the lower confidence interval, CI = 0.001 and upper CI = 0.538 are boundaries of chance for not occurring the loan repayment default among male borrowers at 95% confidence level. According to the findings, male borrowers are not more likely become loan defaulters than female borrowers in Mshikamano VICOBA.

Engaging in diversified business among borrowers minimize the possibility of becoming loan repayment defaulters in Mshikamano VICOBA. Borrower who day-to-day works with diversified business including selling of non-farm commodities such as clothes and shop and crops demonstrated significant effect and negative relation with possibility of becoming the loan repayment defaulter (β_6= -2.073, p=0.023). Moreover, identified that a unit increase in borrower employed in regular business minimizes occurrence of loan repayment default by a chance of exp (β_6) = 0.126. There is strong relationship between borrower business and loan repayment in Mshikamano VICOBA (Wald=5.142). The chance of not occurring loan repayment default among borrower dealing with business is between the lower CI = 0.021 and upper CI = 0.755 at 95% confidence level. Therefore, borrower engaging in day-to-day business of different commodities is more likely not become a loan repayment defaulter than borrower who is depending on seasonal farming or staying at home as housewife. Borrower involving in day-to-day business in markets usually increases his or her cash flow and profits which may ensure the repayment of loan on time.

Size of loan provided to the borrower by Mshikamano VICOBA has positive significant effect on default (β_9= 0.000, p=0.049). The likelihood of obtaining loan repayment default by one unit increase in size of loan is increased by exp (β_9) = 1.000. Moreover, the survey revealed a strong relationship between size of loan and loan repayment default (Wald=3.872). The possibility of obtaining loan repayment default due to increase in size of loan is between lower CI = 1.000 and upper CI = 1.000 at 95% confidence level. The findings justify that when borrower provided an amount of loan which is large enough due to lack of clear or exaggerated business plan, there is high possibility of borrower not to repay that loan according to agreement.

Other borrower factors apart from gender, engagement in business and amount of loan including age of a borrower, education, marital status, farming, loan experience and dependants identified that they do not affect loan repayment in Mshikamano VICOBA. Therefore, occurrence of loan default and non-default loan among borrowers of Mshikamano VICOBA has no relationship with other assessed borrower factors apart from gender, business and size of loan.

5. CONCLUSION AND RECOMMEDATIONS

Poor people in Tanzania particularly are mobilized together and establish informal microfinance institutions in form of VICOBA. These informal microfinance institutions facilitate savings and credit among members who contribute their shares and cannot qualify for credits from formal MFIs such as commercial banks. Mshikamano VICOBA in Lushoto District Tanzania is an informal microfinance institution based in rural areas while serving the poor with credit and savings for about since 2017.

Despite its existence for some years, Mshikamano VICOBA is not well performing in loan repayment. There is high rate of loan repayment default. Many borrowers fail to complete loan repayment on time and remain with outstanding loans for a long period contrary to the loan repayment contract. VICOBA management team decides to recover the outstanding loans by compensation from borrowers' shares while other borrowers decide to escape their place of living to avoid to be sued by the VICOBA management team.

Borrower factors have effect on loan repayment in Mshikamano VICOBA. Gender with regard to male borrowers and regular engagement in business among members reduce the likelihoods of loan repayment default. Although they are small in number, male borrowers demonstrated a good habit of repaying their loans compared to females. Moreover, increase in size of loan identified to increase the chance of a borrower to become a loan repayment defaulter in Mshikamano VICOBA.

It is recommended that VICOBA management team before providing loans should scrutinise borrower's information as much as possible by taking into consideration borrower factors particularly gender, borrower engagement in business and size of loan applied in order to avoid non-performing loans and enhance profits.

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