INTERNATIONAL JOURNAL OF SOCIAL Sciences and Information Technology
ISSN 2412-0294 www.ijssit.com

http://www.ijssit.com Vol II Issue VIII, October 2016
ISSN 2412-0294

EVALUATION OF STRATEGIC FACTORS INFLUENCING LOAN PERFORMANCE IN AGRICULTURAL LENDING INSTITUTIONS. A CASE OF AGRICULTURAL FINANCE CORPORATION (AFC), KENYA

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Abstract

The purpose of the study is to evaluate the strategic factors influencing loan performance in agricultural lending institutions in Kenya. The study established that to ensure effective credit administration system cooperatives should provide education and training for members, elected representatives, managers, and employees so they can contribute effectively to the development of their cooperatives. The study also revealed that debt recovery system is crucial in loan Performance in agricultural lending institutions in Kenya, purchasing debts from creditors for a percentage of the value of the debt and pursue the debtor for the full balance, sometimes plus interest should be employed as this prevents a debtor from merely defaulting or forgetting a debt. The study further revealed that credit risks when effectively mitigated positively affect the loan Performance in agricultural lending institutions in Kenya to a great extent. The study recommends that there is need for agricultural lending institutions in Kenya to enhance their credit administration system in loan performance as the study revealed that credit administration system had appositive impact on loan Performance in agricultural lending institutions in Kenya. There is also need for agricultural lending institutions in Kenya to put in place an effective debt recovery system as the study established that debt recovery system is crucial in recovering debts and affect loan performance of in agricultural lending institutions in Kenya

Keywords: Strategic Factors, Agricultural Lending Institutions

1. Background of the study

Strategic factors influencing performance of agricultural lending institution from a global point of view is a complex task for any organization and increasingly important in a world where economic events are linked. The literature on factors influencing loan performance among agro-lending institutions targeting the farming community are very sparse and limited mainly to microfinance experience in low-income countries (Derban et al., 2005; Silwal, 2003). Based on past literature, the factors affecting performance of these institutions can be divided into four factors namely individual/borrowers factors, firm factors, loan factors and institutional/lender factors.

From the Regional Perspective Strategic factors influencing performance of agricultural lending institution can be divided into 3 categories, bank related factors, economic factors and customer related factors. Other factors are noted as; poor monitoring and control of loans by bank management, breach of contract, lack of proper knowledge, artificial and natural disasters, bank takeovers by other banks, company dissolution due to loan default, loss of job by the borrower, bankruptcy of the debtor and closing down of businesses with commercial bank loan due to competition. Commercial banks should have proper monitoring systems and sound credit management to alleviate the problem (Chemjor: Sylvia, 2007)

The financial sector in Kenya at independence was unable to serve the interest of African farmers and businessmen, or provide adequate long term capital to finance economic growth. This was largely due to the inherent weak structure of the sector at the time (Gupta, 1987). In response, the Government of Kenya took a deliberate effort to set up various DFIs with the responsibility to provide enterprises and projects with equity and long-term loans that commercial banks were unable or unwilling to supply (Popiel, 1994). Among the DFIs, The Agricultural Development Corporation (ADC), through its subsidiary called Lands Limited, was responsible for purchasing large-scale farms from British farmers and leasing them to citizen farmers, (Yaron, 1992). Agricultural Finance Corporation (AFC) was to provide long-term credit to individuals and groups to purchase farms and to finance farm improvement, as well as seasonal credit for production. By providing suppliers with credit, cooperative societies also supported farmers (Yaron, 1992). These organizations have been mismanaged and run down and are no longer important sources of finance for agriculture. The surviving DFIs however are faced with numerous challenges as risks associated with agriculture financing, the land laws and tenure systems in Kenya, political interference, the character of the borrowers, poor financial records on the side of the farmers, effects of credit bureau scores, competition, cost of credit and location of the institution in relation to the agricultural areas (Mayer, 1989). Compared to other financiers, Agricultural financers especially AFC operates supervised type of credit. This ensures that the funds are utilized for Agricultural purposes, that the funds disbursed are not diverted to other purposes and misapplied and that the borrower's loan repayment capacity from the proceeds of the financed project is enhanced.

2. Statement of the problem

Most financial institutions funding clients in the agricultural sector in Kenya have been experiencing financial difficulties due to high loan delinquency rate. This trend is threatening to cut off services to this crucial sector adding to the problem of inadequate and skewed financial services.

3. Purpose and Objectives of the Study

The general objective of this study was to establish the strategic factors influencing loan performance in agricultural lending in a bid to suggest measures that can be effectively instituted to save the sector from liquidity problems. The study's specific objectives were to;

i. Establish how credit administration system influence loan performance by agricultural based financial institutions.

ii. Establish how loan collection and debt recovery system influence loan performance by agricultural based financial institutions.

iii. Investigate how credit risk affect loan performance by agricultural based financial institutions.

iv. Establish the effect of loan classification on loan performance by agricultural based financial institutions.

4. Research methodology

The study adopted descriptive case study. The target population was 44 respondents who were employees of Agriculture Finance Corporation selected by census sampling technique. Primary data was collected using a structured questionnaire.

DATA ANALYSIS, INTERPRETATIONS AND PRESENTATION

5. Credit Administration System

Table 1: Effects of credit administration system on loan performance in agriculture lending institutions

Opinion	Frequency	Percent
Yes	40	95.2
No	2	4.8
Total	**42**	**100**

The study sought to establish whether credit administration system affect loan performance in Agriculture lending institutions, from the research findings, majority of the respondents as shown by 95.2% agreed that credit administration system affect loan performance in agriculture lending institutions whereas 4.8% of the respondents disagreed. This implies that credit administration system affect loan performance in agriculture lending institutions in Kenya.

Table 2: Extent to which credit administration system affect loan performance

Extent	Frequency	Percent
Very great extent	12	28.6
Great extent	18	42.9
Moderate extent	6	14.3
Little extent	4	9.4
No extent	2	4.8
Total	**42**	**100**

The study sought to establish the extent to which credit administration system affect loan performance in agriculture lending institutions, from the research findings, majority of the respondents as shown by 42.9% indicated to great extent, 28.6% of the respondents indicated that credit administration system affect loan performance in agriculture lending institutions to a very great extent, 14.3% of the respondents indicated to a moderate extent, 9.4% indicated to a little extent whereas 4.8% indicated to no extent. This implies that credit administration system affect loan performance in agriculture lending institutions to a great extent.

Table 3: Statements on effect of credit administration system on loan performance

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree	Mean	Std Deviation
credit administration system is a vital strategic factor for effective orientation of loan performance	10	31	1	0	0	1.79	0.32
credit administration systems are positively significant to influence loan performance	11	28	2	1	0	1.83	0.28
Although the credit administration systems differ and may be complex in different agricultural institutions, the principles of these strategies and loan performance are applicable to both	12	27	2	1	0	1.81	0.27

The study sought to establish the extent to which respondents agreed with the above statements relating to credit administration system, from the study findings, majority of the respondents agreed that credit administration system is a vital strategic factor for effective orientation of loan performance as shown by a mean of 1.79, Although the credit administration systems differ and may be complex in different agricultural institutions, the principles of these strategies and loan performance are applicable to both as shown by a mean of 1.81, credit administration systems are positively significant to influence loan performance as shown by a mean of 1.83. The study findings concur with Mintzberg, (2004). He asserts that Cooperatives provide education and training for members, elected representatives, managers, and employees so they can contribute effectively to the development of their cooperatives. Members also inform the general public about the nature and benefits of cooperatives Cooperatives serve their members most effectively and strengthen the cooperative movement by working together through local, regional, national, and international structures

6. Debt recovery system

Table 4: Effects of debt recovery system on loan Performance

Opinion	Frequency	Percent
Yes	39	92.9
No	3	7.1
Total	**42**	**100**

The study sought to establish whether debt recovery system influence loan performance in agricultural lending institutions, from the research findings, majority of the respondents as shown by 92.9% agreed that debt recovery system influence loan performance in agricultural lending institutions whereas 7.1% of the respondents were of the contrary opinion. This implies that debt recovery system influence loan Performance in agricultural lending institutions.

Table 5: Extent to which debt recovery system affect loan performance

Extent	Frequency	Percent
Very great extent	13	31.0
Great extent	23	54.7
Moderate extent	3	7.1
Little extent	2	4.8
No extent	1	2.4
Total	**42**	**100**

The study sought to establish the extent to which debt recovery system influence loan performance in agricultural lending institutions in Kenya, from the research findings, majority of the respondents as shown by 59.5% indicated to great extent, 31% of the respondents indicated that debt recovery system influence loan Performance in agricultural lending institutions to a very great extent, 7.1% of the respondents indicated to a moderate extent, 4.8% of the respondents indicated to a little extent whereas 2.4% indicated to a no extent. This implies that debt recovery system influence loan performance in agricultural lending institutions in Kenya to a great extent.

Table 6: Statements relating to debt recovery system

Statements	Strongly agree	Agree	Neutral	disagree	Strongly disagree	Mean	Std deviation
Effective debt recovery system requires a reporting and review structure to ensure that loan defaults are effectively identified and assessed and that appropriate controls and responses are in place	14	25	2	1	0	1.76	0.26
Debt recovery system is the last step in the corporate debt management process	18	21	2	1	0	1.67	0.24
Debt recovery system can be used to make sure that loan performances are in line and proper debt recovery system also helps the management to be in a position to make future plans	13	24	4	1	0	1.83	0.24

The study sought to establish the extent to which respondents agreed with the above statements relating to debt recovery system, from the study findings, majority of the respondents agreed that; debt recovery system is the last step in the corporate debt management process as shown by a mean of 1.67, effective debt recovery system requires a reporting and review structure to ensure that loan defaults are effectively identified and assessed and that appropriate controls and responses are in place as shown by a mean of 1.76, debt recovery system can be used to make sure that loan performances are in line and proper debt recovery system also helps the management to be in a position to make future plans as shown by a mean of 1.83, the above findings concurs with the findings by (Kromschroder & Luck, 2008). According to Kromschroder & Luck (2008), in many countries there is legislation to limit harassment and practices deemed unfair, for example limiting the hours during which the agency may telephone the debtor, prohibiting communication of the debt to a third party, prohibiting false, deceptive or misleading representations, and prohibiting threats, as distinct from notice of planned and not illegal steps.

7. Credit Risks

Table 7: Effects of credit risks on loan performance in agricultural lending institutions

Opinion	Frequency	Percent
Yes	38	90.5
No	4	9.5
Total	**42**	**100**

The study sought to establish whether credit risks have a direct effect on loan performance in agricultural lending institutions in Kenya, from the research findings, majority of the respondents as shown by 90% agreed that credit risks have a direct effect on loan performance in agricultural lending institutions in Kenya whereas 9.5% of the respondents disagreed. This implies that credit risks have a direct effect on loan performance in agricultural lending institutions in Kenya

Table 8: Extent to which credit risks affect loan performance

Extent	Frequency	Percent
Very great extent	10	23.8
Great extent	22	52.4
Moderate extent	6	14.3
Little extent	3	7.1
No extent	1	2.4
Total	**42**	**100**

The study sought to establish the extent to which credit risks influence loan performance in agricultural lending institutions in Kenya, from the research findings, majority of the respondents as shown by 52.4% indicated to great extent, 23.8% of the respondents indicated that credit risks influence loan performance in agricultural lending institutions to a very great extent, 14.3% of the respondents indicated to a moderate extent, 7.1% indicated to a little extent whereas 2.4% indicated to no extent. This implies that credit risks influence loan performance in agricultural lending institutions in Kenya to a great extent.

Table 9: Effect of credit risk on loan performance

Statements	Strongly agree	Agree	Neutral	disagree	Strongly disagree	Mean	Std deviation
Information sharing and identifying credit risks can help agricultural institutions in determining their effects on loan performance	11	28	2	1	0	1.83	0.28
Effective credit risk management requires a reporting and review structure to ensure that credit risks are effectively identified and assessed and that appropriate controls and responses are in place	10	30	2	0	0	1.81	0.30
Risk monitoring can be used to make sure that credit risk management are in line and proper risk monitoring also helps institutions ensure proper loan performance	18	21	1	1	1	1.71	0.24

The study sought to establish the extent to which respondents agreed with the above statements relating to credit risks, from the study findings, majority of the respondents agreed that risk monitoring can be used to make sure that credit risk management are in line and proper risk monitoring also helps institutions ensure proper loan performance as shown by a mean of 1.71, effective credit risk management requires a reporting and review structure to ensure that credit risks are effectively identified and assessed and that appropriate controls and responses are in place as shown by a mean of 1.81, Information sharing and identifying credit risks can help agricultural institutions in determining their effects on loan performance as shown by a mean of 1.83, the finding above concurs with the study findings by Fuser, (2009), that Credit risk arises whenever a borrower is expecting to use future cash flows to pay a current debt. Investors are compensated for assuming credit risk by way of interest payments from the borrower or issuer of a debt obligation. Credit risk is closely tied to the potential return of an investment, the most notable being that the yields on bonds correlate strongly to their perceived credit risk.

8. Loan Classification

Table 10: Effects of types of loans on loan performance in agricultural lending institutions

Opinion	Frequency	Percent
Yes	29	69
No	13	31
Total	**42**	**100**

The study sought to establish whether the various types of loans affect loan performance in agricultural lending institutions in Kenya, from the research findings, majority of the respondents as shown by 69% agreed that various types of loans affect loan Performance in agricultural lending institutions in Kenya whereas 31% of the respondents disagreed. This implies that various types of loans affect loan performance in agricultural lending institutions in Kenya.

Table 11: Extent to which loan classification affects loan performance

Extent	Frequency	Percent
Very great extent	11	26.2
Great extent	17	40.5
Moderate extent	7	16.7
Little extent	4	9.5
No extent	3	7.1
Total	**42**	**100**

The study sought to establish the extent to which loan classification affect loan performance in agricultural lending institutions in Kenya, from the research findings, most of the respondents as shown by 40.5% indicated to great extent, 26.2% of the respondents indicated to a very great extent, 16.7% of the respondents indicated to a moderate extent, 9.5% indicated to a little extent whereas 7.1% indicated to no extent. This implies that which loan classification affect loan performance in agricultural lending institutions in Kenya to a great extent.

Table 12: Statement relating to the effect of loan classification on loan performance

Statements	Strongly agree	Agree	Neutral	disagree	Strongly disagree	Mean	Std deviation
Loan classification is vital for effective loan performance	15	22	3	2	0	1.81	0.23
Loan classification is positively significant to influence loan performance	12	24	4	1	1	1.93	0.23
Although the loan rates of agricultural lending institutions differ and may be complex than conventional financial institution, the principles of loan classification are applicable to both	13	22	1	2	4	2.10	0.21

The study sought to establish the extent to which respondents agreed with the above statements relating to loan classification, from the study findings, majority of the respondents agreed that loan classification is vital for effective loan performance as shown by a mean of 1. 81, loan classification is positively significant to influence loan performance as shown by a mean of 1.93, although the loan rates of agricultural lending institutions differ and may be complex than conventional financial institution, the principles of loan classification are applicable to both as shown by a mean of 2.10, the above findings concurs with the study finding by Karmann (2008). Karmann asserts that loan amounts are determined strictly on the basis of input eligibilities determined in the crop license. Loan sums and inputs in kind are given to the cooperative for disbursement to individual members according to their eligibility Private farmers who are not members of farmer associations, apply individually and make individual arrangements for drawing the cash part and taking delivery of inputs.

SUMMARY OF FINDINGS

Credit Administration System

The study established that credit administration system affect Loan Performance in Agriculture lending institutions to a great extent implying that credit administration system affect Loan performance in Agriculture lending institutions in Kenya

The study also established that cooperatives should provide education and training for members, elected representatives, managers, and employees so they can contribute effectively to the development of their cooperatives.

Debt Recovery System

The study revealed that debt recovery system influence loan Performance in agricultural lending institutions in Kenya to a great extent.

The study further revealed that in many countries there is legislation to limit harassment and practices deemed unfair, for example limiting the hours during which the agency may telephone the debtor, prohibiting communication of the debt to a third party, prohibiting false, deceptive or misleading representations, and prohibiting threats, as distinct from notice of planned and not illegal steps.

Credit Risks

The study revealed that that credit risks influence loan Performance in agricultural lending institutions in Kenya to a great extent. The study also established that Credit risk arises whenever a borrower is expecting to use future cash flows to pay a current debt. Investors are compensated for assuming credit risk by way of interest payments from the borrower or issuer of a debt obligation. Credit risk is closely tied to the potential return of an investment, the most notable being that the yields on bonds correlate strongly to their perceived credit risk.

Loan Classification

The study established that various types of loans affect loan Performance in agricultural lending institutions in Kenya. The study also revealed that loan classification affect loan Performance in agricultural lending institutions in Kenya to a great extent. The study further established that loan amounts are determined strictly on the basis of input eligibilities determined in the crop license. Loan sums and inputs in kind are given to the cooperative for disbursement to individual members according to their eligibility Private farmers who are not members of farmer associations, apply individually and make individual arrangements for drawing the cash part and taking delivery of inputs

Conclusions

The study established that to ensure effective credit administration system cooperatives should provide education and training for members, elected representatives, managers, and employees so they can contribute effectively to the development of their cooperatives. Members also inform the general public about the nature and benefits of cooperatives. In so doing cooperatives are in a position to serve their members most effectively and strengthen the cooperative movement by working together through local, regional, national, and international structures

The study revealed that debt recovery system is crucial in loan Performance in agricultural lending institutions in Kenya, purchasing debts from creditors for a percentage of the value of the debt and pursue the debtor for the full balance, sometimes plus interest should be employed as this prevents a debtor from merely defaulting or forgetting a debt. It also generates immediate revenue, albeit much reduced, for the creditor and reduces the public relations risks involved with defaulted debt collection. Some states have specific laws regarding debt buying the study therefore concludes that debt recovery system had appositive impact on loan Performance in agricultural lending institutions in Kenya.

The study revealed that credit risks when effectively mitigated positively affect the loan Performance in agricultural lending institutions in Kenya to a great extent , thus the study concludes that mitigation of credit risk positively affect loan Performance in agricultural lending institutions in Kenya to a great extent since credit risk is closely tied to the potential return of an investment, the most notable being that the yields on bonds correlate strongly to their perceived credit risk.

The study revealed that loan classification affect loan performance in agricultural lending institutions in Kenya to a great extent, thus the study concludes that loan performance had a positive effect on loan Performance in agricultural lending institutions in Kenya.

Recommendations

The study recommends that there is need for agricultural lending institutions in Kenya to enhance their credit administration system in loan performance as the study revealed that credit administration system had appositive impact on loan Performance in agricultural lending institutions in Kenya.

There is need for agricultural lending institutions in Kenya to put in place an effective debt recovery system as the study established that debt recovery system is crucial in recovering debts and affect loan performance of in agricultural lending institutions in Kenya.

It is essential that agricultural lending institutions give due consideration to their target market while devising credit risk. The credit procedures should aim to obtain an in-depth understanding of the agricultural lending institutions' clients, their credentials & their businesses in order to fully know their customers as credit risk positively affect their loan performance.

The senior management of agricultural lending institutions should develop and establish proper loan classification policies and credit administration procedures as a part of overall evaluation strategy affecting loan performance. Such policies and procedures shall provide guidance to the staff on various types of lending, as the study revealed that loan classification had a positive effect of on loan performance in agricultural lending institutions in Kenya.

Recommendations for further studies

This research had intended to establish the strategic factors influencing loan performance in Agricultural lending institutions in Kenya. Other researcher may focus on the relationship between lending strategies and financial performance of Agricultural lending institutions in Kenya.

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