

# **LOAN DEFAULT AND PERFORMANCE OF YOUTH ENTERPRISE DEVELOPMENT FUND IN DAGORETTI SOUTH CONSTITUENCY, NAIROBI COUNTY, KENYA**

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## **ABSTRACT**

Credit which is channeled into productive use yield good returns whereas the performance of the lender is gauged on the amount of loans disbursed, performing loans and non-performing loans. A majority of the beneficiaries of government initiated credits have had a bad history in loan repayment in that they deem the credit as a grant that should not be repaid. Government institutions (YEDF included) offering credit facilities have had a poor loan performance in that the process of obtaining the credit is tedious making the rate of loan up take to be low, the amount of loan offered is substantially low and while those who have managed to access the loan funds have decided to default. This study sought to determine the relationship between credit default among the youth beneficiaries of the youth enterprise development fund and the performance of the fund in Dagoretti constituency. The main objective of the study was to establish the effect of credit default on the performance of the Youth Enterprise Development Fund in Dagoretti constituency. Business development services like trainings to youth groups, diversion of loaned funds to other projects against the intended proposed projects, borrowers' characteristics and business failure constituted the independent variables the study concentrated on while the dependent variable was the performance of the Youth Enterprise Development Fund in Dagoretti Constituency, Kenya. Loan performance was measured by investigating the rate of

loan repayment, amount repaid and the rate of defaulted the loans. The research methodology that was be employed was of descriptive survey design and the population of the study was selected through random sampling from 124 youth groups that have benefited from the fund and the 2 YEDF officers in Dagoretti Constituency. Data was collected through oral face to face interviews and using questionnaires with both open ended and closed questions. The questionnaires adopted a five point Likert scale which ranges from strongly agree to strongly disagree. Data then was edited for accuracy, uniformity, consistency, completeness and arranged to enable coding and tabulation for final analysis. The study adopted multiple linear regressions to analyze the data. The study established that there was a significant relationship between study variables. Poor business performance, domestic problems and illiteracy were the main factors that led to diversion of the borrowed funds by the youths. This led to loan defaults and business failure. The study concluded that there is need to train the beneficiaries on how well to utilize the funds and also thorough vetting to be done to the applicants before loan disbursement. The need sensitize youths on own savings and financial management skills might mitigate the risk of failure to repay loans.

**Key Words:** *loan default and performance, youth enterprise development fund, Dagoretti South Constituency, Nairobi County, Kenya*

## **INTRODUCTION**

Many countries in the globe, Kenya being one of them in the recent past have been reforming and deregulating their financial systems by transforming their institutions into more effective financial intermediaries and providers of financial services on a sustainable manner to all the sectors of the economy as well as all segments of the population. They have tried increasing the outreach of the financial institutions as a way of alleviating poverty through affordable lending, institutional strategies and financial systems approach (Omino, 2005), thereby creating a new world of funding to the marginalized and less privileged groups in the population like youths, women and those living with disabilities.

In the past, credit has been accessible to only a few in the society. Youths have had a major obstacle in obtaining loans from conventional financial institutions in Kenya because of the credit constraints and the unwillingness of the credit providers to lend them because a majority don't have collateral to secure the loans. It's through this challenges that the Kenyan government during the Narc regime under the leadership of His Excellence the President Mwai Kibaki came up with programs aimed at providing cheap and affordable credit to special groups in the population. This was also seen as a way of solving the unemployment menace in the country by empowering the youths who contribute to 61% of the national population, women and people living with disability (KNBS, 2014).

According to the World Bank, one in every five Kenyan youths of working age (17% of youths in their working age) are unemployed. This is three times worse than in the neighboring Uganda and Tanzania where only one in twenty youths of working age are unemployed (World Bank, 2016). This has necessitated the government to come up with youth empowerment programs aimed at solving the menace of Youth unemployment which has continued cause social problems like security in that the idle youths have joined gangs like Al shaabab and other local terror groups.

The problem of youth unemployment has been a challenge even to the past government regimes. In 2006 the then Kibaki administration came up with the Youth Enterprise Development Fund to financially support youths in doing individual and group businesses. Unfortunately, many of the beneficiaries had a problem of investing the funds in viable projects that can generate income to enable them repay the loans and qualify for more loans in the future. Many of the borrower s have defaulted in repaying the loans while others have gone ahead to borrow from friends, family and relatives to clear the loans meaning the loans didn't add any economic value to them in that they either misused the funds or diverted the money into unprofitable businesses.

In both rural and urban settings, SMEs hardly get services of formal financial institutions because of loan repayment challenges like existence information asymmetry, poor record keeping and poor financial management. Banks as well as other financial providers like SACCOs consider youths and their youth owned SMEs as poor savers, not well known to them personally

and borrow in small uneconomic amounts which is considered as expensive lending (Awoke, 2004).

The SME challenging factors can be categorized into; individual or borrower, Firm or lender and Loan characteristics (Chijoringa & Cassimon, 1997). In 2005 Derban, Binner and Mullineux further grouped the factors into three i.e. the inherent characteristic or behavior of the borrower, characteristic of the lender or financial provider and the systematic risks from external factors like economic, political and the business environment which can lead to business failure hence loan defaulting. (Derban, Binner & Mullineux, 2005).

The availability of finance for investment in positive net present value projects is vital to the sustainability and viability of new SMEs. A vast majority of new SMEs owned by young people below the age of 35 depend on internal finance (contribution from the owners, family and friends). Internal finance is often inadequate for new youth owned SMEs to survive and grow. It is increasingly difficult to keep the costs within the constraints of self-financing. Therefore new SMEs need capital from external sources.

A large percentage of SMEs fail due to cash flow challenges during their first two years of inception. Lack of adequate capital ensue due to limited access of bank credits and or lack of financial management skills (Nieman & Nieuwenhuizen, 2009). Moreover, a majority of SME operators are financially illiterate with a lack of financial management skills. This results to misplaced business priorities characterized by allocation of funds to unproductive business activities resulting to business failure.

Lack of knowledge and financial trainings are some of the reasons for slow growth of SMEs and entrepreneurial creation. They also escalate the rates of closure of SMEs which are associated with the uptake and default of heavy loans (Fatoki & Garwe, 2010). Many institutions consider lending to the youth as laborious and a daunting activity when sustainability factors are taken into consideration. Inappropriate accounting procedures and procedures are haunting SMEs in that getting accurate business information is a challenge. Some entrepreneurs even go ahead to mix their individual finances with business capital hence complicating the assessment of creditworthiness to the assessor.

### **Loan Repayment**

The borrower's ability to repay their loans is a major issue requiring attention in that some borrowers can repay the loan while others can decide not to pay resulting to 'loan default'. Loan defaulting was categorized by (Berhanu & Fufa, 2008) into voluntary loan defaulting which is associated with the borrower's morals and or behaviors. The borrower has the ability to repay but he/ she chooses not to repay because of inadequate or lack of law enforcement mechanisms used by the institution that offers the credit. Involuntary defaulting on the other hand comes as a result

of unexpected circumstances beyond the borrower like lower business revenue generations, natural calamities and or borrower's illness which affect the business.

Borrowers with bigger loan amounts with longer repayment periods are likely to have repayment problems as compared to small loan amount borrowers with compressed repayment period which encourages repayment. With small loan amounts, the borrower is likely to service the loan on time and graduate to a higher loan amount. Loan default can be classified into two i.e. defaulting the principal amount as well as the interest and delayed repayment. Lenders should check the past credit history of the borrower and his economic prospects, the collateral offered, capital employed in the business, the character of the borrower, loan conditions if they favor the applicant and the capacity of the borrower to repay the loan before advancing him / her with the credit.

### **Youth Enterprise Development Fund (YEDF)**

The Kenyan economy is faced with the problem of unemployment which stands at 40% of the entire working age population. The majority of those affected are youths in their productive age, accounting for 61% of the population in the country. Youth unemployment ranges from 60% to 80%. (KNBS, 2014) This has forced the government to come up with strategies aimed at creating employment and or creating a business friendly environment to encourage the unemployed population to establish businesses.

It was considered that unemployment is essentially the major youth problem which has led to an increase in social crimes like drug abuse, prostitution and theft in that the energetic youths are so idle hence engaging in these unlawful activities. Institutional financing was started by the government to finance small and micro enterprises that the existing financial institutions were unwilling to fund citing the challenge of defaulting and lack of collateral for securing the loans.

In the December, 2006, the Youth Enterprise Development Fund was formed and gazette to assist the government in solving the unemployment problem by offering cheap affordable loans to youths to venture into business. In 11th May 2007, through an Act of parliament, the YEDF was transformed into a state corporation as flagship project of vision 2030 under the social pillars. According to the Act, the YEDF was mandated with the provision of financial support and business development services to youth owned enterprise and hence turn youths into job creators instead of being job seekers. (YEDF, 2012)

There has been a high rate of loan defaulting among the youth beneficiaries since the fund became operational. The rate of loan uptake and disbursement as well as the rate of loan recoveries has been so discouraging. This performance has been attributed to poor administration of the fund as well as corruption where non-deserving youths are funded who end up not repaying their loans and sometimes embezzlement of the funds by top management. Other youths in the past have complained that they wait for too long for them to get the funds hence

they get discouraged with continuing with their intended project, they get funded when they have given up on the project or when they have disbanded their group hence they engage the loan funds into other non-productive activities.

The fund's strategic focus is on enterprise development as a key strategy that will increase economic opportunities for, and participation by Kenyan youth in nation building. In the year 2010, the Fund developed a three year strategic plan to address varied needs and aspirations of the youth, and to address challenges it has faced in the past. The Fund is currently working on a 5 year strategic plan with the Medium Term Plan (MTP) of vision 2030.

The Fund's objectives is to provide on-lending to the youth enterprises, attract and facilitate investment in micro, small and medium oriented commercial infrastructure that will be beneficial to youth enterprises, support youth oriented micro, small and medium enterprises to develop linkages with large enterprises and facilitate marketing of products and services of youth enterprises both in domestic and international markets.

The Fund also provides business development services to youth enterprises. The Fund comes with free entrepreneurship training, charges no interest at the start up stages and does not require any collateral. The Fund also guarantees convenient appraisal and repayment terms. The Fund has financed over 944,000 youth enterprises to the tune of Kshs.11.2 billion nationally where Ksh 49.1 Million benefited Youths in Dagoretti North Constituency. It has also helped thousands of the youth build their enterprises through market support and enterprise training. The Fund has trained over 1.2 Million Youth entrepreneurs (YEDF, 2016).

## **STATEMENT OF THE PROBLEM**

It is generally accepted that credit which is channeled into productive use yield good returns whereas the performance of the lender is gauged on the amount of loans disbursed, performing loans and non-performing loans. A majority of the beneficiaries of government initiated credits have had a bad history in loan repayment in that they deem the credit as a grant that should not be repaid. Government institutions (YEDF included) offering credit facilities have had a poor loan performance in that the process of obtaining the credit is tedious making the rate of loan uptake to be low, the amount of loan offered is substantially low and while those who have managed to access the loan funds have decided to default. Several studies carried out in Kenya among them; Amenya (2011), Mburu (2010), Gudda & Ngoze (2012) show that government micro credit programs perform poorly in terms of slow payment and high default rates. The studies have not gone into analyzing the factors influencing such repayment of YEDF loans but instead they have focused on analyzing the effectiveness and impact of such programs on the economy. This implies that no specific study has been able to address the factors influencing repayment of YEDF loan hence creating a gap that needs to be filled by the study in question.

According to YEDF Nairobi Region loan status report 2016, Out of the Ksh.49.1 million that has been disbursed in Dagoretti South constituency since 2007 to November 2016, only Kshs. 16.27 Million has been recovered whereby only 124 youth groups have benefited against the projected Kshs. 100 Million benefiting over 1000 groups. Only 12 groups have cleared their loans, 56 groups are struggling to make their monthly installments while the rest have completely ignored their obligation. The low up take of loans, low rate of loan recovery and high rates of loan default has been directly linked with business failures established with the borrowed money, financial illiteracy, borrowers' characters and lack of mechanisms by the fund to follow up on cases of defaulters resulting to poor loan performance of the Fund (YEDF, 2016). The failure of youths to channel the loaned funds into profitable businesses to generate enough funds to offset the loans as well as create employment opportunities despite the existence of YEDF for the last ten as an avenue for youths to obtain affordable credit raises questions. There exist huge default rates raising questions on effectiveness on management of the fund. On average the national repayment rate stands at 32.2% while Dagoretti South constituency repayment rate stands at 44.17 % hence default rate of 56.83% which is way up the banking industry default rate of 8% (CBK, 2016). The Women Fund stands at 22%. Moreover, out of 124 youth groups funded in the constituency only 12 have cleared the loans advanced to them while fifty six groups have completely failed to repay (YEDF, 2016). In the report, also new groups applying for the loans has declined significantly painting the picture of poor loan performance in the Fund's loan book. It is against this background that this study therefore sought to investigate the effects of credit default on the loan performance of Youth Enterprise Development Fund in Dagoretti South constituency.

## **GENERAL OBJECTIVE**

The general objective of the study was to investigate the Effect of Loan Default on the Performance of The Youth Enterprise Development Fund in Dagoretti South Constituency.

## **SPECIFIC OBJECTIVES**

1. To determine the effect of business development services to youth owned enterprises on the performance of the Youth Enterprise Development Fund in Dagoretti South constituency.
2. To establish the effects of diversion of loan funds by youth beneficiaries on the performance of Youth Enterprise Development Fund in Dagoretti South Constituency.
3. To establish the effect of borrowers' characteristics on the performance of the Youth Enterprise Development Fund in Dagoretti South constituency.
4. To determine the effect of business failure on the performance of Youth Enterprise Development Fund in Dagoretti South Constituency.

## **THEORETICAL REVIEW**

### **Game Theory in Group Lending**

Game theory is applied to intuit how group borrowers play the microfinance game with the micro-finance institution or the lender. The group lending mechanism described by (Yunus, 1998) is vulnerable to moral hazard problems. In particular, free-riding by individual group members and collusive behavior by the whole group against the financial institution. Initially, the group-based borrowers plays the lending game according to the rules set out by the microfinance institution. As such, they are cautious in their investment strategies to ensure that the loans are paid back in order to secure loans for the future. However, as play ensues, groups become savvier on how to play the game to their advantage. Therefore, while group liability is used to harness the cooperative relationship among the members of the group to the advantage of the lender, in time, these same cooperative relationships are used to collude against the lender. That is, groups begin to make riskier investments to increase their expected payout. This eventually results in reduced loan repayment rates. Hence, as play continues, the probability of the lender receiving repayment on the loan decreases. The lender will be faced with financial constraints in the long run resulting to the inability to meet its obligations; that is, inability to pay on time employee salaries, inability to lend out hence the entire system of the lender is affected.

### **Solidarity Theory in Lending**

The solidarity theory is the main theory that will be applied in this study which is considered as a ‘solution’ to information asymmetry in developing countries. In this theory, (Karlan & Morduch, 2009), careful selection and individual behavior of group members is known before assigning responsibility from the lender to clients. The cohorts who normally consist of five to ten members then borrow a loan in solidarity. Members select each other on how well they know each other, their reputation and relationship and in some cases their age. In case one member of the cohort defaults, the other members will be responsible for the payment. In the system of group liability fund, members have the responsibility to vet other fellows to ensure only thee trustworthy are allowed into borrowing. Group lending in the theory allows clients to monitor each other to ensure the funds are well invested and efforts made in clearing the loans in full. Reduced non-repayment with time improves the credit records of the cohorts and their welfare enabling them obtains more credit without collateral.

## **EMPIRICAL REVIEW**

### **Business Development Services and Loan Repayment**

Capital access alone is not enough for SMEs'; Business Development Services need to accompany financing to provide entrepreneurs and businesses with knowledge and tools for doing business. BDS are expensive in Kenya and many SMEs' cannot afford. According to World Bank; training, consultancy and advisory services, marketing and marketing linkages,

information technology and development, transfer and business promotions are the major BDS. They may also include strategic services and operational services that are essential for the day to day running operations like management of accounts, compliance with the labour laws and other regulations, information communication technology and tax records.

On the other hand, strategic services address the medium and long term issues affecting or which can affect the performance of enterprises, its competitiveness and access to credit (World Bank Group, 2001). BDS are important in the development of MSEs' in that they provide a range of business advice, information and support to the sector as well as enhancing the sustainability of MSEs' growth by improving the business environment in general (Kabahanga, 2015). Business Development Services provide a mechanism through which market failures which are particularly evidenced in the transition economies such as inadequate information which act as a barrier for fostering economic development and growth in particular geographical areas (UNDP, 2014).

Provision of non-financial services like accounting and legal services to MSEs' at friendly costs, supplementing the role of financial services, MSEs' support in their growth and sustainable development and facilitating MSEs' development of competitive advantage are some of the main objectives of BDS. Incubation concept is one of the best BDS for promotion of growth of MSEs'. Business and Technology incubation which involves the development, provision and maintenance of controlled conditions to assist in the cultivation of new growth oriented or innovation driven establishments.

An incubator can be helpful in the provision of office and office equipment, technical support, financial management, development of business plan, business training, mentoring and business coaching. Incubation facilitates business startup and assist entrepreneurs until they 'graduate' and have capacity to 'survive' in the external business competitive environment. Incubators provide local, on – spot diagnosis and treatment of business challenges in addition to facilitating access to capital (UNDP, 2014). The main type of BDS provided by the YEDF is training of loan recipients.

### **Diversion of Loaned Fund and Loan Repayment**

A diversion of funds is the use of funds for purposes other than for which they are meant. Diversion of funds to unrelated business, lapses in initial borrower due diligence, and inefficiencies in the post-disbursement monitoring process are the main reasons for the bad loans predicament of banks, according to an EY report.

A major portion of loaned funds ends up being diverted into other projects that were not intended earlier. The projects sometimes are unattainable due to the limited capital (usually the loaned amount) thereby resulting to failure. The beneficiaries at the end find difficulties in raising money to offset the loan. The major reason why the YEDF funds are diverted by the

beneficiaries is the delayed disbursement. The YEDF loans sometimes delay up to six months hence discouraging the applicants with going on with their project in that the projected budget will have increased at the time of disbursement because of inflation. Some youths also come together to form groups and apply for the funds, because of the delay in disbursement others leave the group and those who are patient to remain in the group divert the money into other projects or divide the money among themselves with the intention of not repaying the loan.

Timely disbursement of loans by the fund will result to performance of YEDF loans as the beneficiaries will carry on with their project in mind. The fund has given a turnaround time of one month for the loans, complying with time will result in high uptake of loans as many youths will be encouraged to apply and high recovery rates in that after repaying the first loan the group will graduate to a higher loan.

### **Borrower's Characteristic and Loan Repayment**

In their study, Derban et al (2005), the causes of credit default can be grouped into characteristic of the business, borrower's social economic variables like gender, integrity and honesty, personal stability, age and health, education level and household income. They pointed out that a higher education level is positively related to better repayment performance. At the same time, they alluded that female borrowers, household income levels, type of business and borrower's experience has no adverse effect on repayment behavior.

In a study conducted by Roslan and Abd Karim (2009) on micro credit loan borrowers in Malaysia, they concluded that male borrowers and borrowers with long term repayment duration had high chances of defaulting and or meeting their repayments on time. They did a study on micro credit loan borrowers from Agro Bank which is a commercial Bank institution which has specialized in Agricultural business. Borrowers engaged in non- production oriented businesses like service support sector but had training in a particular business and had borrowed higher loans had lower probabilities of defaulting.

Reikne (1996) assessed the factors that lead to the failure of group based lending system in urban areas and went on to the extent that he recommended an individual credit system for a better loan repayment. According to him presence of high geographical mobility, low attachment to specific neighborhoods and peer groups consisting of competitors are the factors that frustrate the solidarity of groups in urban areas, and hence group lending is more applicable to the rural environment than to urban society.

Amenya (2011) carried out a study on challenges facing YEDF in Nyaribari Chache constituency. The study found out that despite the fact that YEDF could be a preferred source of funding among the youths, the fund has not employed enough staff to vet all the applicants to determine their creditworthiness and willingness to repay the loan. Projects funded by the funds have not been properly managed and hence low repayment rates.

The fund lacks proper monitoring and capacity building programs as a result of inadequate personnel. Majority of the defaulters from the year 2007 were funded without a background check, they were funded without proper assessment of their business proposals, individual characters and their intention to apply for the funds. The fund should employ more field officers to visit the groups and business sites to assess their ability and monitor the projects after funding. This will ensure the funds are put into proper use to enable the individuals repay the loans.

### **Business Failure and Loan Repayment**

A report by KNBS in collaboration with the Institute for Development Studies (IDS) of the University of Nairobi, Africa Center for Economic Growth (ACEG) and K-rep further indicates that some of the reasons for closure of these businesses include shortage of operating funds, too few customers or raw materials and competition. Many businesses are opened every year but only a few go through into their second year, also attributed to the scenery is the quality of products that they offer (Institute for Development Studies, University of Nairobi, 2016).

In the survey, a majority of youth entrepreneurs are Survival Driven with the intention of becoming rich so soon after starting a business. They set unrealistic goals which the business cannot attain. They strain the limited available business resources without the innovation of new quality products and services that will add value to the target market. Seeking money before adding value has led to massive closure of youth owned enterprises.

According to KNBS, 49.8% of SME's closed down between July 2014 and June 2015 due to non-compliance with government regulations (KNBS, 2016). For businesses to operate they have to obtain a trading license or Business permits from the county governments, get certification from KBBS in case of manufacturing, health and safety permits and file tax returns. This proved to be a challenge to SME's leading to their closure citing high operational costs.

On the other hand competition from established businesses becomes unbearable to SME's. The established businesses purchases in bulk thereby getting discounts hence offer products to the public at competitively lower prices. This has swept away small establishing firms out of the market. It's though this challenge that the government came up with an initiative to reserve 30% of all government tenders to Youth owned enterprises of which a majority fall under the SME bracket. The fund through its newly introduced LPO and SLO financing should finance youths doing business with government on time to take advantage of this initiative. This will encourage more youths to register new companies and apply for tenders. They will take up more loans and repay on time.

## **RESEARCH METHODOLOGY**

### **Research Design**

The researcher used descriptive research design which Saunders et al (2015) defined as one that intensely looks at the accuracy of the phenomena at the moment of study and preciously describes what the researcher sees. Survey research can be descriptive, exploratory and or involving advanced statistical analysis (Mugenda & Mugenda, 2003). Descriptive research design was employed as it serves many research objectives which may include; description of the phenomena and or the characteristics associated with subject population, population proportion estimation that have similarities in characteristic as well as discovery of association among many different variables. The Descriptive survey design was very useful in this study as it assisted in investigating ‘the effects of loan repayment and the performance of The Youth Enterprise Development Fund in Dagoretti South Constituency,’ It gave the researcher useful information on the problem under study.

### **Target Population**

The study targeted the registered youth groups whose projects have been funded by YEDF. A total of 124 youth groups with average membership of 12 members making a total of 1488 youth and 3 officials per group totaling to 372 officials. The 2 YEDF officers in Dagoretti South also were included in the composition of the target population. Therefore, a total of 1862 were targeted by the researcher.

### **Sampling Design**

The study targeted members of youth funded groups, youth group officials and YEDF Cos’. The sample was selected from the entire population of 1,862 members. The researcher used stratified random sampling to identify sub groups of officials and their proportions to ensure representation from two strata and also ensure that no strata is over represented.

### **Data Collection Instruments**

The research employed the use of primary source of data which collected using questionnaires and oral interviews. The questionnaires were open ended and in two set with one comprising structured questions for the two YEDF officers working on the ground and another set for the youth beneficiaries of the loaned funds who are in the process of repaying and those yet to repay. Secondary data was obtained from YEDF bulletins, scholarly articles and researches done in the past.

### **Data Collection Procedure**

Data was collected after getting the required permit from the university and consent from the National Commission for Science, Technology and innovation and the YEDF office. The

researcher then embarked on field trip to gather information on the variables under study. Questionnaires were formulated by the researcher, distributed to the various respondents and collected later to give the responded enough time to read through the questions, think and give accurate information. The researcher employed the use of two sets of questionnaires where one was administered to youth groups to solicit information about access procedures and repayment of the youth fund loan and the other one to YEDF officers in Dagoretti South to solicit information on loan uptake and repayment and the effect of repayment and the general performance of YEDF loans. The researcher also carried out oral face to face interviews to get information from the YEDF Officers in Dagoretti South, group officials and other beneficiaries of the Fund. The interviews were conducted randomly where by the researcher asked questions relevant to the study and then record the response from the responded in a note book for it to form part of the findings of the study.

### **Data Analysis and Presentation**

Both qualitative and quantitative methods of data analysis were used in this study. Qualitative data from open questions was analyzed using content analysis and presented in prose form. Data which was obtained from research instruments was analyzed through Statistical Package for Social Science (SPSS) and findings presented using descriptive statistical tools like graphs, tables and other measures of central tendency. Data was classified in tables, graphs and charts for common characteristics and responses being coded for easy statistical analysis. In the analysis, the researcher employed a reduced form economic model that is similar to Jimenez and Saurina(January 2005) to ascertain the Effects of credit default on the performance of Youth Enterprise Development Fund. The model is a simple regression function that links the ratio of credit default and loan performance.

$$Pr(Y) = B_0 + B_1 X_1 + B_2 X_2 + B_3 X_3 + B_4 X_4 + \epsilon_i$$

Where: **X1** = Performance of the fund; **X2** = Diversion of loan funds; **X3** = Business failure; **X4** = Borrowers' characteristics;  **$\epsilon_i$**  = Error term.

Quantitative data was analyzed using descriptive statistics and inferential Statistics (Logit Regression) using SPSS data analysis software program. The models helped to establish whether there is a zero-order relationship among the variables. If there is a significant relationship, the regression coefficient for indirect effect represents the change in Y for every unit change in  $X_i$ , and hence influences the results. Qualitative data was analyzed through content analysis by capturing common themes and group. Final result of data analysis presented through tables and figures for easy understanding and interpretation.

## **RESEARCH RESULTS**

Several empirical studies have been done in the past to investigate the effect of credit default on the performance of lending institutions in Kenya, but studies on loan default in YEDF as a government program in the form of a revolving fund has invariably produced conflicting results as discussed in chapter one. Although these studies attest that business failure, inadequate business development services, borrowers' characteristics and loan diversion has effect on loan repayment, few have attempted to measure how the variables have affected the performance of YEDF. This study was designed to analyze the effect of loan repayment and the performance of the YEDF in Dagoretti South constituency in Nairobi County, Kenya. The Government of Kenya initiated the YEDF as revolving fund towards alleviating youth unemployment which is now reaching alarming levels, however; the tedious process of accessing the funds and the high default rate has affected its performance. Studies done in Kenya show a lot has been disbursed but very little has been recovered and if the trend is not monitored then the intended purpose of the initiative will not have achieved the desired and anticipated result. The study was descriptive in nature with the aim of investigating the empirical determinants behind the poor loan repayment that has affected the performance of YEDF.

The specific objectives that guided the study were: To determine the effects of Business Development services on the performance of the Youth Enterprise Development Fund in Dagoretti North Constituency, Nairobi County – Kenya, to establish the effect of Diversion of loaned funds on the performance of the Youth Enterprise Development Fund in Dagoretti South constituency, Nairobi County Kenya, to establish the effect of borrowers' characteristics on the performance of the Youth Enterprise Development Fund in Dagoretti South Constituency, Nairobi County – Kenya and to Determine the effect of Business Failure on the performance of the Youth Enterprise Development Fund in Dagoretti Constituency, Nairobi County – Kenya.

The study adopted a cross-sectional descriptive survey research design using quantitative approach to data collection, analysis and reporting through some elements of qualitative approach of data aimed at analyzing the effect of loan repayment and the performance of YEDF in Dagoretti South Constituency, Nairobi County- Kenya. To look into the first objective of Business Development services on the performance of YEDF, the study derived frequency distribution tables to capture trainings on youth and youth entrepreneurs as well as the number of trainings done and their frequency. Composite index was established to consolidate the factors into one variable. The Pearson correlation coefficient and logit regression was used to ascertain the relationship between business trainings and performance of the lender the YEDF. It was found that a relationship exist between business development services and the performance of the Fund in Dagoretti South Constituency in Nairobi county- Kenya.

The diversion of loaned funds and the performance of YEDF in Dagoretti South Constituency in Nairobi County, Kenya, the study found that poor business performance, domestic problems and

illiteracy as the factors that lead to diversion of funds. The factors were consolidated into one common variable and a relationship established through the Pearson correlation and logit regression analysis with the performance of YEDF in Dagoretti South Constituency, Nairobi County- Kenya. After the analysis, the results indicated significance of the variable in question which alluded that there is a clear relationship between diversion of loaned fund and the performance of YEDF in Dagoretti South Constituency.

The other objective of the study, intended to establish the effect of borrower characteristics to the performance of YEDF in Dagoretti South Constituency, Nairobi County Kenya. The study derived frequency distribution tables, and a pie-chart to capture spouse influence, informal borrowing and loan diversion as factors influencing credit default which at the end affect the performance of the lender the Youth Enterprise Development Fund in Dagoretti South Constituency. A composite index was also established to make one variable that was to be regressed. After the Pearson Correlation and the logit regression analysis, the results indicated that there is a relationship between borrowers' characteristics to the performance of YEDF in Dagoretti South Constituency, Nairobi County- Kenya.

The final objective of the study intended to determine the effect of Business failure on the performance of The Youth Enterprise Development Fund in Dagoretti South Constituency, Nairobi County Kenya. The results from the Pearson correlation and the logit regression analysis, there was a relationship between business failure and performance of YEDF in Dagoretti South Constituency in Nairobi County Kenya.

## **CONCLUSIONS**

This study examined the effect of diversion of loaned funds, business development services, borrowers' characteristics and business failure that result to loan defaulting that undermine the performance of YEDF in line with Vision 2030 for gender and youth, which tries to advance for equity in resource distribution and improved livelihoods for all, the main goal according to the vision laid down to increase opportunities, all-round among youth, women, and all other disadvantaged groups in the society. Special strategies were to involve the increasing participation of the said groups in all economic, social and decision-making in the country at large. From the study, it can be concluded that there is a significant relationship between credit default and the performance of the Youth Enterprise Development Fund.

For implication of socio-economic functions namely; the level of education, age brackets of the group members, marital status of the group members, level of earnings of the members, the main economic activity had either a positive or negative influence on loan repayment. Members with high education (graduates) were very few in most of the groups, majority being high school dropouts. Knowledge learnt in school was found not exhibited in groups' dynamics. Majority of the group members were in the age bracket of (21-32) years, most of whom were women. The marital status in most groups did not have a positive relationship to loan repayment and those

who earned fewer incomes were found to be better in repaying for their obligations. Business was found to be the main source of income to most of the group members most of which were small businesses like salons, barbers shops and grocery with little income. The study concluded that, socio-economic functions have a significant relationship to loan repayment.

On the effect of borrower' characteristics; loan diversion was found to be high due to poor business performance prevalent at times and high level of illiteracy was common to most group members. The spouse influence was found to be very high affecting loan repayment as a result of extreme level of ignorance. There has been excessive level of snowballing, where group members perceive government loans as grants, and fail to repay because others are not paying affecting the performance of the fund. Most of the group members' advocated for prosecution/blacklisting of all the loan defaulters. The study concluded that, borrower characteristics have a significant relationship to the performance of YEDF in Dagoretti South Constituency in Nairobi County.

For business failure it found that there exists a relationship to the performance of YEDF. Most of the groups that started business for the first time using the loaned funds defaulted because their businesses failed. The causes of failure ranged from wrong choice of a business, poor management, illiteracy and inadequate capital for running the daily operations of the business. The study further concluded that dire need to train the beneficiaries on how well to utilize the funds and also thorough vetting to be done to the applicants before loan disbursement. The need sensitize youths on own savings and financial management skills might mitigate the risk of failure to repay loans. Youth women groups were found to be more organized and repaying their loans better than the Male youth groups.

## **RECOMMENDATIONS**

The study made some policy recommendations to loan repayment and performance of Youth Enterprise Development Fund. To start with, the study underpins the importance of demanding business plans by YEDF which in the past has been a formality. Business plans help one to organize his/her thoughts, as well as the individual resources. It helps one to communicate the specifics of the business idea to others, including business advisors, potential suppliers and major customers, family and friends. The plan provides a "yardstick" against which one can measure progress during the initial years of the business.

In view of the above, business plans should be subjected to a thorough adjudication process by the qualified staffs that are able to review and make decisions on certain plans, to demonstrate viability for better loaning operation procedure. Use of business plan as one of the revolving fund loaning operation procedure was found to have a significant relationship to repayment of loans. Constituency loan officers, on top of dissemination of information on what makes a business plan, should be in a position to review the plans to measure their viability and advise accordingly before loans are issued. This would help reduce uncertainty in repayment.

The credit reference bureau which has been a preserve of the commercial banks should be made compulsory to YEDF and should be networked to share some important information on borrowers. It should assist in making credit accessible to more young people, and enabling lenders and businesses to reduce risks and fraud. YEDF plays a great role in extending financial services within an economy especially to young population. In support of this role, credit bureaus will help lenders to make faster and more accurate credit decisions. The YEDF systems should be strengthened to facilitate up-to-date loan repayment statements to loanees' follow-up and take action early in case of defaults. Some groups identified prosecution/blacklisting of defaulters as a solution to some of the problems they are currently facing. Due to problems of high risk and high cost of borrowing, uncertainty of repayment capacity on the rural borrower has been reported high due to irregular income streams. Systems should be developed to ensure consistent incomes and expenditure to reduce/remove uncertainty.

It was found that most of the group members were high school drop outs and few had attained form four-level of education showing a negative relationship between group membership and level of education. The highly educated individuals that have studied business in high school were lowly engaged in groups' affairs. Due to this unique circumstance, it is important to train the young individuals on how to run and own businesses at their early stage of life before they graduate from lower primary.

A good number of the graduates at this level do not proceed to secondary school where business study as a subject is handled. This subject, which was taught in the primary curriculum and used to provide basic knowledge on how to own and run a business was good but was stopped in the Kenyan Curriculum. Developers of the Curriculum should revise the earlier decision and revert the teaching of business subject to both primary schools and primary colleges.

Lack of awareness as a category to improve loan repayment, was found to be in existence among many youth groups, especially those in the slums of Kabiria and Ngando where the groups were found to have opened businesses that didn't even see their second year in operation. The YEDF should conduct an awareness campaign on the need to repay the loans. Doing advertisements to the potential borrowers in the local vernacular media will help improve awareness and consequently loan repayment and performance of the Fund. These campaigns will go a long way towards enhancing to the better the borrower characteristics' which was found to have a positive significant relationship to loan repayment and informing the youths not to fear venturing into private business and rid them of their obsession with white collar jobs which are not easy to find.

The start-up amount of Ksh 50,000 that was recommended when the funding initiatives was rolled out has been overtaken by events including inflation and is too low according to the respondents and needs review. The YEDF start-up amount was recently adjusted to Ksh 100,000 according to the constituency loan officers. Again, the 5% administration fees charged may appear small but the respondents felt it was too high, and should be reduced further.

Reduction of this fee would go a long way in enhancing the borrower capability and encourage them to rely on government revolving fund for sources of credits which would now be cheaper by far, compared to sources from the informal lenders. The three months grace period as per the loaning operation procedure given to the borrowers before they start repaying should be extended to six months and beyond to give the borrowers room to make adjustment so as to improve on the rate and amount of loan repayment.

The study noted irresponsible lending and borrowing that has caused stress and deaths to good number group members, as a result of worsening borrower' characteristics, that was found to have positive significant relationship to YEDF loan repayment and its performance. The operation structure of both YEDF funds, may be contributing to this behavior. Most of the Constituency Loan Officers are on contract employment terms which affect their morale in service delivery. Due to the structures, circumstances make some of the officers irresponsible in their actions, which affects supervisory and monitoring of groups in their jurisdiction.

The study noted increased issues on loan diversion and spouse influence during the time of borrowing and repayment in almost all the groups that took part in this research. Some spouses were reported to have run away from homes after receiving the loans to evade repayment or to evade the nagging demands from their partners, to part with some/all the amount borrowed.

Improvement of the YEDF structures needs to be re-looked, to adequately provide resources and systems to capture and monitor groups, and be able to put in check; loan diversion, the spouse influence and elements of informal borrowing. Spouses should be encouraged to have all the relevant information concerning the amount and when borrowing has been done, and should be made to appreciate the purpose of borrowing to avoid misunderstanding, misuse and diversion of the borrowed funds. On this regard, there is need to invite spouses to sign for loans in front of the loan officer and ensure ownership documents are attached where collateral is needed for a loan, to reduce cheating and loan diversion.

For the last ten years, youths have been the platform on which politicians have played their dangerous games of control and power, feeding on leftovers put across at them by the political class. For the initial government plan to reduce poverty and unemployment among the youths who happen to be the majority in the country to succeed, the bad game with the politicians should be put to an end. They should not determine the running of funds as they have done in the past, once certain mechanisms to run them are laid down. Un-healthy use of the youths by the politicians influences their social-economic aspect negatively wasting precious time doing very little that is economical if any. The study recommended the establishment of a consolidated social protection fund to rehabilitate and build youth empowerment centers in all the constituencies.

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