



EFFECTS OF UNSECURED PERSONAL LOANS ON HOUSEHOLD FINANCIAL HEALTH OF PRIMARY SCHOOL TEACHERS IN EMINING DIVISION, BARINGO COUNTY, KENYA

Florence Bett, , Robert Kingwara & Mary Bosire

Masters Scholar, Accounting and Finance and Mgt Science Dept, Egerton University

bettflorence@yahoo.com

PHD Student, School of Business, University of Nairobi

rkingwara@gmail.com

Lecturer, Accounting and Finance and Mgt Science Dept, Egerton University

bosiremary@yahoo.com

ABSTRACT

Credit facilities include both secured and unsecured loans. For employees, unsecured personal loans have become more popular due to the relative ease and speed at which they can be obtained. The study focused on three areas namely: evaluate the effects of school fees loans on household financial health of primary school teachers in Emining division, assess the effects of home improvement loans on household financial health of primary school teachers in Emining division, examine the effects of emergency loans on household financial health of primary school teachers in Emining division and establish the effects of development loans on household financial health of primary school teachers in Emining division. The study used descriptive research design. Purposive sampling was used to obtain a sample of 165 respondents, 5 teachers from each of the thirty-three primary schools, in Emining Division, Baringo. A questionnaire was used to collect primary data from the respondent. Correlation analysis was conducted to test the study hypotheses. Results of the study showed that there is a statistical significant positive relationship between unsecured personal loans and household financial health. In particular, there is a statistical positive association between school fees loans, home loans, emergency loans, development loans and household financial of primary school teachers. The study concludes that unsecured loans contributes to the wellbeing of primary teachers.

Indexing terms/Keywords

Keywords: Unsecured personal loan and Financial

INTRODUCTION

In recent years, retail banking has increasingly gained popularity in Kenya due to various changes in the market especially the inclusion of unsecured loans that were previously a preserve of the Saccos (PWC on Unsecured Loans in Retail Banking, 2007). Lending is one of the main activities of commercial banks in Kenya and other parts of the world. This is evidenced by the volume of loans that constitute banks assets and the annual substantial increase in the amount of credit granted to borrowers in the private and public sectors of the economy. According to Comptroller (1998), lending is the principal business for most commercial banks. Loan portfolio is therefore typically the largest asset and the largest source of revenue for banks. The demand for unsecured personal loans is seen in the increasing number of applications that have been made by consumers. This is a product that credit providers have focused on in meeting the demand for credit. Factors that have influenced growth in this regard include the relative ease and speed at which the likes of unsecured personal loans can be obtained. Unsecured personal loans have represented an attractive market opportunity for credit providers who have actively pursued a lending growth strategy in this product, particularly as a result of the margins that can be made in the current market (World Bank Survey on Unsecured Credit in the Mortgage Market, 2012).

Unsecured loan is guaranteed based on the borrower's financial capacity, credit history, earnings potential and or liquidity. In general, if a credit is unsecured, the file should contain reliable and current financial information that is sufficient to indicate that the borrower has the capacity and can be reasonably expected to repay the debt (Branch and Agency Examination Manual on Commercial Loans, Sept 1997). The type of employment and gross monthly income assist in establishing the ability of the borrower to afford a loan (Credit Reference Bureau Data Standards Manual, 2008). The Federal Trade commission defines unsecured lending as a debt that is not tied to any asset. The CBK views the following products as forms of unsecured lending, credit card, overdrafts, commercial papers, personal loans; and financing provided to small and medium enterprises, (CBK on Unsecured Lending among Banks, 2012).

Liberalization in the finance industry in Kenya has led to increased access to credit facilities to Kenyan employees. Primary school teachers are among the beneficiaries. Credit facilities include both secured and unsecured loans. For employees, unsecured personal loans have become more popular due to the relative ease and speed at which they can be obtained. Studies in developing countries (Quach, Mullinax & Murinde 2005; Omwange, 2012; Nangila, 2013) have researched on the effects of credit on household welfare and have shown that credit contributes positively and significantly to the economic welfare of household such as improved education standards, improved healthcare, and improved sanitation, enhancing consumption and living standards, earning of extra income as well as reduction of unemployment by providing an avenue for self-employment. However, developed countries have researched on the impact of unsecured loans on household financial health and has established that indebtedness is associated with decreased financial stability (Rio & Young, 2005; Nam & Elliot, 2013). None of these studies focused on the effects of unsecured personal loans on



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house hold financial health of households. This study therefore sought to establish the effects of unsecured personal loans on household financial health in a developing economic environment. The study was guided by the following hypotheses:

H₀₁: School fees loans do not have any effect on household financial health of primary school teachers in Emining Division, Baringo County, Kenya.

H₀₂: Home improvement loans do not have any effect on household financial health of primary school teachers in Emining Division, Baringo County, Kenya.

H₀₃: Emergency loans do not have any effect on household financial health of primary school teachers in Emining Division, Baringo County, Kenya.

H₀₄: Development loans do not have any effect on household financial health of primary school teachers in Emining Division, Baringo County, Kenya.

This research was conducted on public primary school teachers in Emining Division, Baringo County, Kenya, from March to August 2016. The study targeted public primary school teachers who have worked with the TSC for more than two years and have borrowed unsecured personal loans. Both quantitative and qualitative data was obtained concerning loans and financial health.

2.LITERATURE REVIEW

The field of personal or household finance is better reflected in recent years in several research studies. One of the most frequent associations of personal finance is with financial education, the underlying idea being that without adequate knowledge and skills one cannot satisfactorily manage his or her own finances, particularly in a dynamic and complex environment. Besides education, however, other aspects emerge from the literature, which appear to have particular importance in the process of individual financial decision. Individual can either borrow secured or unsecured personal loans. Secured loan is granted to individuals, if they deposit some form of security, such as titles, logbooks or share certificates, (KCB on Types of Loans, 2014). This means that a credit facility is fully secured where collateral used to secure the facility has a value that is sufficient to cover the carrying amount of the loan (CBK Prudential Guidelines for Institutions licensed under the banking Act, 2014). Unsecured loan on the other hand is a loan that is issued and supported only by the borrower's credit worthiness rather than a type of collateral. The relative ease and speed at which unsecured personal loans can be obtained have led to increasing number of applications, making it an area of interest in the study of personal finance.

Proponents of unsecured lending argue that access to credit benefits economic development, poverty reduction and the improve living standard of all citizens, (Hudon, 2009). On the other hand, many protest that whilst some consumers are able to manage their borrowing effectively the ease of access to credit causes over- indebtedness, (Brennan & Gallagher, 2007). These conflicting opinions have given rise to the discussion about financial health of consumers of unsecured lending. The impact of unsecured lending especially in the case of personal loans has mixed opinions. Proponents of unsecured lending claim this unprecedented phenomenon is actually a good thing. They believe it improve the economy and provides credit to those who were previously denied access. The poor and previously unbanked are now able to buy the possession they really need and improve their financial position by gaining access to food, healthcare, and jobs. Advocates of unsecured lending exclaim that opportunities have arisen of their customers through this unsecured channel to finance their cars, houses, businesses and extend their education, (Becchetti&Conzo, 2013)

Drentea&Laurakas, (2000) have suggested that debt "may be a more sensitive barometer of financial well-being than income" because it represents accumulated hardships over time. While this observation reinforces the likely importance of debt as a socio economic indicator, it also points to the potential confounding that arises from longitudinal accumulation of debt. The Normal Loan is designed to address the development needs such as building homes, Large Scale farming, Motor vehicle purchase among others, (Egerton University Sacco on types of loans, 2014). This is a loan granted mainly for the purpose of long term development. Repayment is spread over a period of 72 months, (Kentours Sacco on types of loans, 2015). The top up or refinance loans allow members to borrow more money to complete projects. These are loans for any additional money which will enable members to complete initiated projects, and boost savings by cash, (Boresha Sacco, 2015).

The Somesha Loan has been designed to meet all the school fees needs of clients. It is given to clients with existing business in a group set up. It can be a first loan for a client who feels that school fee is the most pressing issue. It can also be given as an additional loan. The money is used to pay tuition and board, textbooks, school supplies, and other expenses. This product also extends to other educational courses such driving school, short courses, training etc, (Milango Financial services on types of loans, 2014). The loan is available to finance all levels of education; Elementary, Primary, High School and College (Graduate & Post graduate), (Bank of Africa on types of loans, 2015). It is a loan intended for educational advancement, this loan can be taken out by parents/guardians for students or by salaried individuals who wish to further their studies, (Kenya Commercial Bank on types of loans 2014).

Further advances for existing borrowers who have conducted their accounts satisfactorily for the last three years or to prospective borrowers holding clean title of residential property in a city, town or municipal center, are allowed to borrow home improvement loans, (Bank of Africa on types of loans, 2015). This is a loan for Repairs / Renovations / Improvement / Extension of Home and for Furniture, Fittings & Fixtures, (Bank of Baroda on types of loans, 2015). These are loans that give the opportunity to buy own property. Homebuyers need to make provision for the upfront bond registration and



transfer costs as well as any deposit required. With this product, you can buy an existing, developed residential property and get up to 100% financing, (CFC Stanbic- Kenya on types of loans, 2014).

In addition, financial health is a term used to describe the one's personal financial situation. Financial therapy is the integration of cognitive, emotional, behavioral, relational, and economic aspects of financial health, (Financial Therapy Association, 2013). Therefore, financial health compares to the level of satisfaction a person feels about their financial situation. Financial satisfaction includes being content with one's material (objective) and non-material (subjective) financial situation, (Joo & Grable, 2004). How a person manages his or her personal finances has been shown to be a major influence contributing to satisfaction or dissatisfaction with a person's financial situation, (Porter & Garman, 1993).

The basic element of financial health is net worth. Financial health can be determined by learning how to prepare various financial statements. Financial statements are documents that accurately reflect one's personal financial position at a specific point in time. These statements include a budget (record of expected income and spending for the future, generally for a month or a year), a balance sheet (record of one's assets, what is owned) and liabilities (what one owes others) at a specific point in time, usually at the end of a month, quarter, or year) and an income statement (record of spending over a specific period of time, generally a month or a year). Net worth can be calculated using a personal balance sheet and financial ratios can be calculated using personal balance sheet and personal income statement, (Steed 2011).

Current ratios can help in determining whether or not one has enough monetary assets to pay for a large, unexpected expense or to tide an individual over in case of a period of reduced or eliminated income: the current ratio and the "month's living expenses covered" ratio. The current ratio tells how many times over one could pay off his/ her current liabilities with the cash he/ she has on hand. To calculate current ratio, divide the amount of monetary assets (your current assets) by the amount of current liabilities. The more times one can pay off his/ her current liabilities, the better off they are financially. A ratio greater than two is recommended. The second important ratio is the "month's living expenses covered" ratio. This ratio tells how many months one could survive financially if he/ she lost all current sources of income. To calculate this ratio, divide the amount of monetary assets by the amount of monthly living expenses. Living expenses should not include charitable contributions, taxes, or savings, because if one lost his/ her job, he/ she would not have these expenses or savings. A ratio that allows you to pay your living expenses for three to six months is recommended. The ratio should be equal to at least as many months as it would take to get a new job if one lost his/ her current job, (Steed 2011).

Nangila (2013) established the nature of unsecured personal loans offered by commercial banks and the effects of unsecured personal loans on Household welfare of secondary teachers in Bungoma County-Kenya. The study found that the major types of unsecured personal loans borrowed by secondary school teachers were Home improvement, Education, loans to provide capital, medical loans and loans to clear other loans. Similarly, Tilakaratna (2006), studied on the impact of micro-credit on selected household welfare attributes: evidence from Sri-Lanka. The results indicated that overall, micro-credit has enabled the household to improve their income, assets, housing condition. Nam & Elliot (2013), determined on whether student debt jeopardizes the short term financial health of U.S households. They indicated that households with outstanding student loan debt and a median 2007 net worth of \$128,828 incurred a loss of about 54 percent of net worth in 2009 compared with households with similar net worth levels but no student loan debt over the same period. Rom (2013) carried out a study on the impact of unsecured lending on the financial wellbeing of consumers and found that those who make use of unsecured lending as a means of accessing finance have a better subjective view of their financial wellbeing than those who do not make use of unsecured lending.

Farugui (2008), studied indebtedness and the household financial health: An examination of the Canadian Debt Service Ratio distribution concluded that debt and asset holdings of households are relatively well matched, the distribution of the Debt Service Ratio is skewed to the right and this skew has increased slightly since 1999. It was a cross-country comparison of the Canadian DSR distribution with the U.S distribution and the analysis showed that in 2004, the household sector in Canada seemed less vulnerable to macro-economic shocks than U.S households. The study involved calculation of mean, median, variance, skewness and Kurtosis. Using evidence from British Household Panel Survey (BHPS), (Rio & Young, 2005) carried out a research on the impact of unsecured debt on financial distress among British households. An ordered-logit model was estimated for 1995 and 2000 using a self-reported indicator of financial distress and the dependent variables. Grades et al (2007) researched on the Impact of microfinance on rural poor households' income and vulnerability to poverty: case study of Makueni district, Kenya. The main objective of the research was to analyze the impact of microfinance on household income as well as measure household vulnerability to poverty after access to microfinance. The study was an experimental case of Makueni district where participants in microfinance programmes and non-participant households were studied over time. On integrating time dynamics in the analysis, the results indicate a positive and significant impact of microfinance on household income. The study concluded that there is a role of microfinance on the improvement of household incomes.

3. Methodology

Descriptive survey research design was used in this study to assess the Effects of Unsecured Personal Loans on household financial health of salaried primary school teachers in Emining Division, Baringo County, Kenya. The rationale for choosing this design is based on its ability to provide information about the naturally occurring status, behavior, attitudes or other characteristics of a particular group and describes what exists and may help to uncover new facts and meaning to depict the participants in an accurate way. The study targeted a population of 6,084 teachers spread over 676 primary schools (Education office, Baringo County, 2016). According to the District Education Office, Mogotio Sub-



International Journal of Management and Information Technology County (2016), Eming division has a total of population of 278 primary school teachers. The teachers are evenly spread over 32 public primary schools; with only one school having 22 teachers. A sample of 165 was purposively picked. Five teachers in every 33 schools participated in the study. A structured questionnaire was used to collect primary data. Reliability and validity of the study was done through a pilot study in Mogotio division, Baringo County. The pilot data was used to test for reliability using Cronbach Alpha coefficient. A coefficient of 0.70 and above was considered adequate for adoption (Gay, 1992). Primary data was analyzed using Pearson Correlation. This formed the basis for rejecting or failing to reject the null hypothesis.

4.0 Results and Discussion

This study set out to test hypotheses on four predictor variables; school fees loans, home improvement loans, emergency loans and development loans. The dependent variable was household financial health, measured in terms of net worth, liquidity ratio, debt ratio and savings ratio. In this case, Pearson's Moment Correlation Coefficient was used to study the relationship between these variables and household financial health at alpha level of $p < 0.05$. The results were as shown in Table 4.1.

		Correlations				
		school fees loan	home loans	emergency loans	development loan	financial health
school fees loan	Pearson Correlation	1				
	Sig. (2-tailed)					
	N	35				
home loans	Pearson Correlation	.570**	1			
	Sig. (2-tailed)	.000				
	N	35	117			
emergency loans	Pearson Correlation	.680**	.924**	1		
	Sig. (2-tailed)	.000	.000			
	N	35	105	105		
development loan	Pearson Correlation	.682**	.985**	.970**	1	
	Sig. (2-tailed)	.000	.000	.000		
	N	35	117	105	122	
financial health	Pearson Correlation	.779**	.944**	.916**	.952**	1
	Sig. (2-tailed)	.000	.000	.000	.000	
	N	35	103	103	103	103

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

The results in Table 4.1 shows that school fees loan has a positive correlation coefficient 0.779 ($R = 0.779$, $P < 0.005$). It implies that a unit increase in school fees loans leads to 0.779 units increase in financial health. This is a significant positively association with the financial health. The null hypothesis states that School fees loans do not have statistical significant effect on household financial health of primary school teachers. Based on the above results in Table 4.1, we reject the null hypothesis and accept the alternate hypothesis that school fees loan have a statistical significant effect on household financial health. From these results, school fees loans affect the welfare of the primary teachers in Eming. An increase in school fees causes an improvement on net worth. Nangila (2013) confirm study results that loans improves education level and clearance of existing debt.

The study result established that home improvement loans has a positive correlation coefficient of 0.944 ($R = 0.944$, $P < 0.005$). The association between home improvement and financial health is statistically significant. It implies that a unit increase in loan improvement causes a 0.944 units increase in financial health of primary school teachers. The null hypothesis states that Home improvement loans do not have a statistical significant effect on household financial health of primary school teachers. We reject the null hypothesis and accept the alternate hypothesis that there is a statistical significant effect on household financial health of primary school teachers. When teachers access home improvement loan, their assets increases as well as development. Nangila (2013) made the same observation that it leads to improve total household consumptions and welfare. Similarly, Muayila (2012) concur with the study results that access to credit result in increasing economic welfare.



Further, the results in Table 4.1 indicates that emergency loans has a correlation coefficient of 0.916 ($R=0.916$, $P<0.005$). The association between home emergency loans and financial health is statistically significant. It implies that a unit increase in emergency loan leads to a 0.916 units increase in financial health of primary school teachers. The null hypothesis states that emergency loans do not have statistical significant effect on household financial health of primary school teachers. We reject the null hypothesis and accept the alternate hypothesis that there is a significant statistical effect on household financial health of primary school teachers. Omwange (2012) confirm study results that access to credit significantly impact on household welfare.

Finally, the results in Table 4.1 indicates that development loans has a correlation coefficient of 0.952 ($R=0.952$, $P<0.005$). The association between home development loans and financial health is statistically significant. It implies that a unit increase in emergency loan leads to a 0.952 units increase in financial health of primary school teachers. The null hypothesis states that emergency loans do not have statistical significant effect on household financial health of primary school teachers. We reject the null hypothesis and accept the alternate hypothesis that there is a significant statistical effect of emergency loan on household financial health of primary school teachers. Quach et.al (2005) observed that credit has greater positive effects on the economical welfare.

5.2 Conclusions

The study conclude that school fees loans, home improvement loans, emergency loans and development loans have a statistically significant positive effect on household financial health. Teachers improve their household welfare by utilizing either of these loans. The welfare of primary teachers can improve in terms of assets, education, household consumptions, and other developments. The study found out that unsecured loan contributes positively to the welfare of primary school teachers.

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