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Assessment of the Challenges Faced by Microfinance Banks in Recovering Loans from Customers in Ibadan North Local Government Area, Ibadan, Oyo State, Nigeria

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Abstract: The Nigerian economy is currently in a state of decline as a considerable amount of its population is living below the global poverty line. The influence of the poor economy has brought high inflation that ran most businesses into debt, depleted capital and defaulted from repaying loans to financial institutions backing them. This further created a problem of loan recovery for both microfinance banks and commercial banks. Therefore, this study was conducted to assess the challenges facing these microfinance banks in recovering loans from customers and appraise their financial performance and sustainability. This was a banking institution-based descriptive cross-sectional study that utilized the qualitative method of data collection to elicit information on status of loan recovery, challenges influencing loan recovery, effects on their financial performance and sustainability. The interviews were conducted with the aid of Key-informant interview guide and recorded using digital audio recorder. The audio recordings were transcribed verbatim, analysed using ATLAS. ti version 8 and presented using thematic analysis and description. This study shows that loan recovery status is fair among those MFBs assessed. Also, the micro-finance banks face challenges that are policy-related, customer-related, poor documentation processing and poor staff attitude in recovering their loans. Decline in Economy, COVID-19 Pandemic and inflation were the factors responsible for the challenges. The poor loan recovery reportedly led to increase in high-risk portfolio, reduction in stakeholder's profit and investment and inability to meet target profit and bank foreclosure. It was concluded that loan recovery status is not as expected as a fair repayment rate was reported. The challenges highlighted were from both banks and the customers, therefore, microfinance banking industry should endeavour to provide flexible loan packages to customers in order to reduce their burden and put all the necessary measures in place to check the lapses on the part of staff.

Keywords: Loan Recovery, Loan Defaults, Loan Repayment, Microfinance Banks, MSMEs, Financial Institutions, Economy, Nigeria

1. Introduction

Since independence Nigeria has undergone series of turbulent economic situation, which is currently in a declining state due to the effects of COVID-19 pandemic. The result of the declining economy has led to the reformation of economic policies that have ushered in some policies like National Development Plans (NDP), Structural Adjustment Programme (SAP), Poverty Reduction Strategy Paper (PRSP), National Poverty Eradication Strategy (NAPEP), National Economic Empowerment Development Strategy (NEEDS), National Vision 20:2020 and the Transformation Agenda of 2011-2015, yet a considerable amount of its population (40.1%) are considered to be poor by national standard in 2019, despite recording an annual GDP growth of 2.3% in the same year [1, 2]. Even though majority of Nigerians especially in the rural areas, live below the poverty line, they are actively engaged in micro businesses that are constantly in need of capital and loans for business expansion and higher income and this development prompted the Central Bank of Nigeria to introduce microfinance banks (MFBs) in 2005 for the purpose of serving this target group that may not have what it takes to secure loans with commercial banks [3]. The MFBs established are charged with the role of financial mediators, intermediaries and links between the commercial banks or lending investors and the MSMEs by facilitating the process of micro-savings and micro-credits [4].

The micro finance institutions in Nigeria are faced with loan defaults, which may have long-term consequences if not addressed [5]. The chance that a microfinance institution (MFI) may not receive its money back from borrowers (plus interest) is the most common and often the most serious vulnerability in a microfinance institution [6]. One may then ask, what are the several problems faced by MFBs during loan recovery? What are the effects of loan default on Micro-Finance banks? What are the major reasons customers find it difficult to pay back loans? Is there any standard procedure for collecting loans? What are the measures that will help reduce the incidence of loan default? All these questions necessitated a good reason to a study that assessed the major challenges faced by Microfinance banks in retrieving loans in Nigeria using Ibadan North Local Government Area of Oyo State, Nigeria as a case study.

2. Literature Review

2.1. The Concept of Microfinance

According to CBN, microfinance is a development tool used to create access for the economically active poor to financial services at a sustainably affordable price [7]. According to Conroy, micro-financing is the provision of financial services to poor and low-income households without access to formal financial institutions [8]. According to Eluhaiwe, microfinance involves the provision of thrift, credit and other financial services and products in very small amounts to the poor to enable them raise their income levels and improve their standard of living [9].

2.2. Business Characteristic

The size of business relates to the amount of income obtained from it. Mpunga asserts that the level of business income is an important factor that would determine the credit worthiness of a client [10]. At low levels of income, businesses have little money to save while at higher levels much can be saved and even used to purchase collaterals which can be used as loan securities. Such securities can be sold to repay loans. According to Horne, the excess of the security pledged over the amount of the loan determines the lender's margin of safety [11]. If the borrower is unable to meet an obligation, the lender can sell the security to satisfy the claim. If the security is sold for an amount exceeding the amount of the loan and interest owed, the difference is remitted to the borrower. If the security is sold for less, the lender becomes unsecured for the credit or amount of the difference. The levels of incomes can also be used as an indicator to determine the credit worthiness of clients. Because secured lenders do not wish to become general creditors, they usually seek security with a market value sufficiently above the amount of the loan to minimize the likelihood of their not being able to sell the security in full satisfaction of the loan. The degree of security protection a lender seeks varies with the credit worthiness of the borrower, the security the borrower has available, and the financial institution making the loan.

3. Research Methodology

This study was a banking institution-based descriptive cross-sectional study using Key-Informant Interview guide as a qualitative method of data collection. The study was conducted among the microfinance representatives. Primary data was collected from the bank representatives (bank managers, loan officers, compliance officers, account officers, marketing officers/managers or chief security officers) in the ten (10) micro-finance banks identified in Ibadan North Local Government, Ibadan Oyo State, Nigeria using Key-Informant guide as the study instrument. Key-Informant Interview (KII) guide was used for the data collection process and the KII guide was self developed based on the research objectives. The following research questions guided the conduct of the key-informant interview and this study:

1) What is the current status of loan recovery by MFBs in Ibadan North Local Government Area?
2) What are the major challenges facing MFBs in recovering their loans from customers in Ibadan North Local Government Area?
3) What are the factors responsible for loan defaulting among customers in Ibadan North Local Government Area?
4) What are the effects of loan defaults on MFBs sustainability in Ibadan North Local Government Area?

This study made use of the purposive sampling technique, which allowed the researcher to purposively select the MFBs that gave credit facilities to customers (MSMES). All recorded data from the interviews were fully transcribed verbatim; after transcription, it was typed and read so as to get familiar with the data; significant statements was underlined and extracted. ATLAS. ti version 8 was used for analysis.

4. Limitation of the Study

The limitation experienced in this study was the hoarding of information during the interview by banks' representatives, as they were doing everything within their power to protect their bank from negative publicity.

5. Result Analysis and Discussion

The findings were presented in key thematic areas with respect to the interview questions asked and study objectives. The thematic areas are presented in the finding's matrix table below:

Table 1. *Summary of the Analysis Result for Assessment of the Challenges Faced by Microfinance Banks in Recovering Loans from Customers in Ibadan North Local Government Area, Ibadan, Oyo State, Nigeria.*

1st Objective	Current status of loan recovery by MFBs in Ibadan North Local Government Area, Ibadan, Oyo State, Nigeria
Main Themes	1) Ineffective loan recovery system 2) Improvised loan recovery system
2nd Objective	Major challenges facing MFBs in recovering their loans from customers in Ibadan North Local Government Area, Ibadan, Oyo State, Nigeria
Main Themes	1) Documentation Challenges 2) MFBs Staff-related Challenges (Nonchalant attitude, corruption) 3) Customer related Challenges (Diversion of loan, network of loans, relocation) 4) Policies-related Challenges 5) Banking Operation-related Challenges
3rd Objective	Factors responsible for loan defaulting among customers in Ibadan North Local Government Area, Ibadan, Oyo State, Nigeria
Main Themes	1) Decline in Economy 2) COVID-19 Pandemic 3) Inflation
4th Objective	Effects of loan defaults on MFBs sustainability in Ibadan North Local Government Area, Ibadan, Oyo State, Nigeria
Main Themes	1) High risk portfolio 2) Reduction in shareholders 3) Reduction in target profit

5.1. Description of the Characteristics of the Microfinance Banks and Key-Informants Assessed

The microfinance banks assessed in this study were those that were functioning and operating in Ibadan North LGA. The staff strength of these MFBs ranged from ten to thirty (10-30) and majority of them had been operating for more than 5 years. The oldest among the MFBs assessed was licensed in 2012 which made it 9 years (as at this research was conducted) since it started operation. Most of the MFBs render loan service to three categories of customers, individual account holders, institutions and group lending. The key-informants interviewed, were representatives that the microfinance banks nominated to give information when permission to interview was applied for in their respective banking institutions. These representatives were loan officers, compliance officers, chief security officers, regional bank managers, head of loan departments and marketing managers who were believed to be knowledgeable and experienced in the process of loan disbursement and recovery.

5.2. Objective 1: The Current Status of Loan Recovery by Microfinance Banks in Ibadan North Local Government

Some of the participants were of the opinion that the current state of loan recovery in their respective banks was not as effective as they expected it but had improvised a new loan system in which customers were visited regularly to remind them of repayment.

The findings from this study also indicated that the current state of loan recovery is both complicated and worrisome. Despite a major pre-loan background check on the customer which was tagged Know Your Customers (KYC), at the end of the day the microfinance banks still go about chasing customers to pay back their loans. Also, COVID-19 pandemic was reported to have negatively impacted on economy and businesses in Nigeria as it disrupted day-to-day transactions during the compulsory lockdown [12] and by implication reduced remission rate. Before the COVID-19 compulsory lockdown, remission rate was ratio 6 to 10 but after lockdown it reduced to ratio 4 to 10. Some of the respondents said the micro-finance banks had to extend the loan term and also spread the loans to enable the customer pay back on weekly or daily basis. This aspect of the findings coincides with the study conducted by Gobbi, Palazzo and Segura (2020), where it was reported that it affected the loan repayments among major bank borrowers as they postponed the time of repayment. According to the respondents of this study, the END-SARS protest was another time extension was made on loans. The END-SARS protest resulted in shutdown of businesses and a halt in trading activities [14]. This aspect of the finding is not only prevalent in this study as it was also discovered in another study conducted by Ochi and Mark (2021) where it was reported that the END-SARS protest has left an indelible mark on the business activities of Nigerian people and as well as the national economy.

5.3. Objective 2: Major Challenges Facing Microfinance Banks in Recovering Loans from Customers in Ibadan North LG

Some of the major challenges identified in this study facing microfinance banks in recovering their loans from customers are documentation errors which may include wrong house address, wrong phone number, wrong amount of loan received by customers etc, and it poses a serious challenge when the loan is due for payment and the customer could no longer be contacted, or the customer had remitted all his loans and the micro-finance bank keeps contacting the customer. Another challenge highlighted by this study is staff related challenges, this include nonchalant attitude of staffs on loan recovery, and this is when the staffs only sit in office without doing proper follow up on loans. Corruption of staff members is also a challenge identified in this study, this happens when some staffs extend the period of the loan unofficially because they have been bribed by customers who are defaulting. By implication, this results to late remission of loans. The study of Nkamnebe and Idemobi (2011), also reported similar findings of corrupt staff and weak skill. Also, Nawai and Shariff (2013) in their study also reported similar results about customers' attitude to loan repayment, diversion of funds, and the burden of other debt as major challenges in loan recovery. Another challenge faced by MFBs during loan recovery is customer related challenges, the common challenges identified in this study includes diversion of loans, relocation of shops/business places and homes without notifying the MFB and network of loans, this occurs when a customer gets loan from one MFB to pay up loan in another MFB. This aspect of findings is similar to the ones reported in the study conducted by Nawai and Shariff (2013); Asongo, Idama and Ngutor (2014), where borrowers' wrong attitude to credit repayment were reported as an important cause of loan default.

Policies by the Central Bank Nigeria (CBN) and National Deposit Insurance Corporation (NDIC) as well as National Association of Microfinance Banks (NAMB) also pose some challenges on loan recovery as these financial regulation bodies do not permit microfinance banks to use extreme force or violence in the recovery of loans, no matter how much your customer is defaulting. The use of loan collectors is also not encouraged. These policies were there to ensure that customers are respected and treated rightly with utmost respect. This becomes more challenging when customers fail to reciprocate these values and morals in the CBN policies as discussed earlier [19]. Furthermore, another challenge reported was that law enforcement cannot be afforded by most microfinance banks during loan recovery as it is bad for business and most of the time the funds for lawsuits was always substantial and it takes longer time before the banks recover from the expenses. These describe the state of loan recovery by MFBs.

The lack of proper interpretation of interest rates by customers charged on loans also possess its own challenge, when customers are in dire need of loans, they do not bother to properly interpret what the interest on the loan really means. It is at the time of repayment that they feel the interest rate is too high; which by implication results in delay of loan payments.

5.4. Objective 3: Factors Responsible for Loan Defaulting among Customers in Ibadan North Local Government

The participants assessed were of the opinion that many of the factors responsible for loan defaulting were influenced by several external factors triggered by the decline in national economy (recession, inconsistence and weak value of national currency "Naira"), impact of COVID-19 pandemic on the economy and resultant inflation, these factors have contributed to loan default among customers, lot of businesses were not flourishing and some folded up and by implication resulted to loan default. According to this study, some customers want to pay back loans but cannot because of these factors affecting them.

5.5. Objective 4: Effects of Loan Default on MFBs Sustainability in Ibadan North Local Government

The findings from this study revealed that the effects loan defaults were on all the stakeholders including the staff, shareholders, external investors, branch operations and expected profits. In a nutshell, this study identifies high-risk portfolio, reduction in shareholder and reduction in target profit as the effects of loan defaults on the sustainability of microfinance banks in Ibadan North Local Government Area, Ibadan, Oyo State, Nigeria.

6. Conclusion

This study was set out to assess the current state, challenges and factors associated with loan recovery by MFBs. The current state of loan recovery as revealed in this study is not totally all bad, as a fair repayment rate was reported. The challenges highlighted in this study shows that both the banks and the customers have their own share of the problem, ranging from documentation errors, diversion of loans to network of loans etc. The factors responsible include the poor economic condition of the country and bad attitude of customers to loan repayment. Also MFBs sustainability will be affected immensely if the rate of bad loans are not brought to the minimal, they risk losing shareholders and investors, and they also will result to giving out loans with high interest rate.

7. Recommendations

Based on the findings from this study, the following recommendations were made:

1) MFBs should try as much as possible to ensure that due processes are followed in their loan processing in order to reduce the risk associated with documentation.
2) MFBs should also endeavour to make flexible policies that take the economic context of the nation into account in setting up of their loan terms and conditions.
3) The regulatory bodies like the CBN, NDIC and NAMB should endeavour to strengthen the regulatory policies in order to cut the excesses of loan shark MFBs that set outrageous interest rates making it difficult for the customers to pay back on time.
4) MFBs should try as much as possible to create a legal unit in the bank which will be responsible for any legal matter and in return reduce cost of lawsuits for the banks compared to if they were to contract it to external legal/enforcement bodies.
5) MFBs should communicate the performance-based rewards and consequences to staff at the time of appointment in order to improve their effectiveness in discharging their duties.

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