EFFECT OF INTEREST RATE ON LOAN REPAYMENT IN MICROFINANCE BANKS IN NIGERIA

(A Case Study of Balogun Fulani Microfinance Bank Nig. Ltd.)

BY

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BEING A RESEARCH PROJECT SUBMITTED TO THE DEPARTMENT OF BANKING AND FINANCE, INSTITUTE OF FINANCE AND MANAGEMENT STUDIES, KWARA STATE POLYTECHNIC ILORIN KWARA STATE

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CERTIFICATION

This is to certify that this research study was conducted by **OGUNNIYI MERCY OLAOLUWA** with Matriculation Number **HND/23/BFN/FT/0192** and this work has been read and approved as meeting the requirement for the award of Higher National Diploma (HND) in Banking and Finance, Institute of Finance and Management Studies (IFMS), Kwara State Polytechnic.

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DEDICATION

This project is dedicated to the Almighty God, the author and finisher of my faith. His divine guidance, unending grace, and strength have sustained me throughout this academic journey. Without Him, this would not have been possible.

"To God be the glory, great things He has done."

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ABSTRACT

This study examined how microfinance banks' interest rate on loan affects repayment capability of borrowers in Balogun Fulani microfinance Bank. This study examined factors affecting loan repayment plan of borrowers; with a view on the impact of promptness of loan repayment on Micro Finance Institutions MFI loans; and find out measures put in place by MFsI to improve repayment plan of borrowers. Ballogun Fulani Microfinance Bank borrowers in Kwara state branch participated in the study. A sum total of 110 customers of Balogun Fulani microfinance bank participated in the study. A structured questionnaire adapted from previous studies and grounded literature review was used in collecting data. Findings from the study showed that: there is significant effect of high interest rate of MFI on the repayment plans of borrowers' loans, the frequency of loan repayment plan significantly has effect on borrowers' ability to payback loan, there is significant difference in the perception of borrowers on effect of high interest rate of MFI on the repayment plans of borrowers' loans based on gender and educational level. Also, the descriptive result showed that; Majority of the borrowers agreed that high interest rate affect loan repayment, it implied that Balogun Fulani and other microfinance bank interest rate on loan is higher compare to Deposit Money Banks. Majority of the participants believes that a single digit interest rate on loan could easy the paying back of loan. The study recommends that: Since default on loans is linked to high interest rate, MFIs should consider looking into their interest rates to encourage prompt payment. This may be weighed with interest rates of Deposit money banks and made relatively lower to encourage borrowers of MFIs.

Keywords: *microfinance banks, interest rate, loan repayment, borrowers*

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CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Interest rates can be classified as either short-term or long-term. For example, you can take out a home loan with the interest rate fixed for 20 years. This is considered a long-term interest rate. You make the same payments over these years, regardless of whether interest rates rise or fall. Alternatively, when you use your credit card or take out a personal loan you are borrowing money at an interest rate that can change in the short term. As a general rule, short-term interest rates tend to be higher than long-term interest rates.

A Microfinance Institution's main objective is to provide MFI and low income households with an affordable source of financial services. Interest charged on loans is the main source of income for these institutions, and because they incur huge costs, the rates are correspondingly high. Four key factors determine these rates: the cost of funds, the MFI's operating expenses, loan losses, and profits needed to expand their capital base and fund expected future growth (Ghatak, 1999).

Many policy makers question why microfinance interest rates remain high even when some MFIs receive concessional funds to finance lending. Although some microlenders receive loan funds at concessional rates, they must cost these funds at market rates when they make decisions about interest rates to ensure the sustainability of the institution's operations. Donors provide concessional funds for a particular usage only for a limited period, as do some governments. However, concessional funds cannot be considered a permanent source of funds for MFIs, and provision must be made through interest rates to sustain the lenders' operations (Ghatak, 1999).

Inflation adds to the cost of microfinance funds by eroding microlenders' equity. Thus, higher inflation rates contribute to higher nominal microcredit interest rates through their effect on the real value of equity. Microlenders have two kinds of operating costs: personnel and administrative. Because microlending is still a labor-intensive operation, personnel costs are high. Administrative costs consist mainly of rent, utility charges, transport, office supplies, and depreciation of fixed assets. Making and recovering small loans is costly on a per unit basis. Often loan recovery is executed by staffs who visit clients, increasing costs in time taken and transportation used. Poor physical infrastructure-inadequate road networks, transportation, and telecommunication systems-in many countries in which microlenders operate also increases administrative costs and adds significantly to the cost of microfinance operations. Inadequate law and order also contribute to high administrative costs as microcredit operations often involve cash transactions and the physical movement of cash (Pitt, and Khandker, 1998).

In many countries, the majority of microcredit is provided by a few leading institutions, and competition among them is mostly on non-price terms. This might not be the case in Ghana where Microfinance Institutions (MFIs) spring up every day. Today in Ghana the MFIs compete with traditional Banks in the cities as well as have dominance in the rural areas. Large-scale commercial banks with access to low-cost funds, low operating costs, extensive branch networks, and vast human and other resources to provide financial services efficiently are presently not significantly involved in microcredit. The lack of participation of such conventional financial institutions in the microcredit market also limits potential competition. Although it is widely recognized that microfinance alone will not end poverty, it is a vital step in that direction. Microfinance institutions, also known as MFIs, offer financial services to underserved, impoverished communities.

Previously, entrepreneurs seeking loans in impoverished communities had to provide collateral to borrow from unlicensed lenders at inequitably high interest rates. A number of factors, including high administrative costs relative to small loans and small returns, had kept banks from setting up branches in impoverished communities when surer profits were to be had elsewhere.

The lack of an efficient financial services industry has held back many would-be entrepreneurs with viable business plans from realizing their own potential. Women, in particular, have been excluded as loan candidates in developing communities. The lending practices of many emerging microfinance institutions have given people living in extreme poverty the opportunity to realize their potential in the business community (Rahman, 1999)

1.2 Statement of the Problem

Charging prices high enough to cover costs is essential for any business to survive in the marketplace. This is true for institutions providing microfinance services as it is for any other enterprise. Thus, it is not surprising that many successful microfinance institutions charge high interest rates to cover their high costs. However, despite the success of those institutions in expanding the supply of credit during the last two decades to an increasing number of poor and low-income households, most borrowers default in paying back those MFI loans.

The problem is compounded by the challenges faced by microfinance banks in managing credit risk, including loan defaults, late repayments, and non-performing loans, which could threaten their sustainability. Furthermore, there is a lack of consensus on the optimal interest rate structure that can ensure both borrower repayment and institutional stability.

This study seeks to examine how interest rates affect loan repayment in microfinance banks and explore strategies to align the interests of borrowers with the financial sustainability of microfinance banks.

1.3 Research Questions

Related to the problem, the research seeks to address four main questions outline below:

i. What is the relationship between interest rates and loan repayment behavior in microfinance banks in Nigeria?
ii. How do changes in interest rates affect the loan repayment performance of clients in Balogun Fulani MFB's Nig. LTD?
iii. What are the factors that influence the loan repayment behavior of clients in Balogun Fulani MFB's Nig. LTD?

1.4 Objectives of the Study

The objective of this study is to appraise the effect of interest rate on loan repayment using Balogun Fulani MFB's Nig. LTD in Nigeria as a case study

i. To examine the relationship between interest rates and loan repayment behavior in microfinance banks in Nigeria.
ii. To investigate the impact of changes in interest rates on the loan repayment performance of clients in Balogun Fulani MFB's Nig. LTD.
iii. To identify the factors that influence the loan repayment behavior of clients in Balogun Fulani MFB's Nig. LTD.

1.5 Research Hypothesis

Ho: There is no significant relationship between interest rate and loan repayment

Hi: There is a significant relationship between interest rate and loan repayment

1.6 Significance of the Study

The significance to be derived from the study includes:

Providing the management and other MFIs with an insight into the effect of interest rates on loan repayment and recommendations to make adjustments where necessary.

It will also assist MFIs to identify the other factors that also impact on loan repayment to enable them achieve a competitive edge in their respective businesses.

This study can be used as reference for further research. By conducting a research on a related subject, this study would serve as a platform to enhance their work. It will serve as a rich source of literature to other researchers, and the limitation of this research may be built on by others studying on the same topic. It is also hoped that findings from this research would confirm or refute the existing knowledge about the effect of interest rate on loan repayment.

1.7 Scope of the Study

The study was conducted within the framework of the effect of interest rate on loan repayment on Balogun Fulani Microfinance banks in Nigeria

1.8 Definition of Terms

Interest Rate: The percentage charged by a lender on the principal amount of a loan. It is typically expressed annually and determines how much interest the borrower will
pay on top of the loan amount.

Loan Repayment: The process by which a borrower repays a loan in installments or a lump sum, as per the terms and conditions set by the lender. In the context of microfinance, this refers to the timely or delayed payments made by borrowers to microfinance banks.

Microfinance Bank: A financial institution that provides financial services, including credit, savings, and insurance, to low-income individuals, small businesses, and rural communities. Microfinance banks aim to promote financial inclusion and provide access to credit for those excluded from traditional banking systems.

Non-Performing Loan (NPL): A loan in which the borrower has failed to make the scheduled repayments within a specified period, typically 90 days or more. NPLs are an indicator of loan default and a key challenge for microfinance institutions.

Financial Inclusion: The availability and accessibility of financial services, such as savings accounts, credit, and insurance, to individuals and businesses, especially those in underserved or low-income segments of society.

Default Rate: The percentage of loans that are not repaid according to the agreed-upon terms. A high default rate indicates that borrowers are failing to meet their repayment obligations.

Loan Restructuring: The process of modifying the terms of a loan, such as extending the repayment period or reducing the interest rate, to accommodate the borrower's financial situation and avoid default.

Central Bank of Nigeria (CBN): The apex financial institution in Nigeria, responsible for regulating and supervising the banking system, including microfinance institutions, to ensure their stability and protect depositors.

1.9 Plan of the Study

The research work is divided into five (5) chapters.

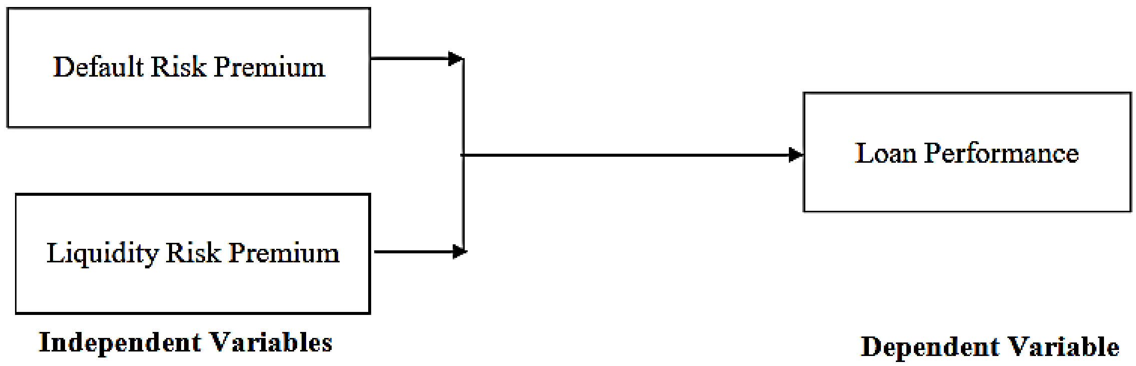
Chapter one, is dedicated to the introduction and research context. Further relevant sections have addresses the statement of the problem, research questions, and the objectives of the study, significance of the study, scope and limitation of the study. Chapter two, is devoted to literature review, various views from different authors were reviewed as regards the effect of interest on loan repayment on MFIs and definition of variables. Chapter three concentrates on the methodology of the research. Chapter four focuses on the Findings, Analysis and Discussions of Results. Chapter five covers the summary, conclusion and recommendations.

CHAPTER TWO

2.0 Literature Review

2.1Conceptual Framework

Figure 1: Conceptual Framework



Concept of Microfinance

Microfinance refers to the provision of financial services such as small loans, savings, and insurance to low-income individuals or households, often in rural or underserved urban areas. Microfinance banks are institutions that provide these services to help the poor engage in economic activities, thereby improving their living standards (Ledgerwood, 1999). Microfinance institutions are essential in promoting economic empowerment, especially among women and marginalized groups (Rhyne, 2001).

2.1.1 Interest Rates and Microfinance Lending

Interest rates are a key determinant of the profitability of microfinance banks. According to the World Bank (2004), microfinance institutions need to set interest rates that cover operational costs and ensure sustainability, while also considering the impact on borrowers' repayment abilities. Interest rates that are too high may burden borrowers, while rates that are too low might not be sustainable for the financial institution.

2.1.2 Effects of Interest Rates on Loan Repayment

Numerous studies have shown that interest rates can influence loan repayment behavior. In their study on microfinance in Nigeria, Olaitan (2006) found that high interest rates could lead to increased loan defaults as borrowers struggle to meet their repayment obligations. Similarly, Akinlo and Akinboade (2015) argued that excessively high rates might discourage borrowing and create a cycle of debt among borrowers, ultimately reducing repayment rates.

However, some scholars, such as Morduch (1999), have contended that interest rates are necessary to ensure the financial viability of microfinance banks, especially in developing countries where the cost of capital and operational expenses are high.

2.1.3 Factors Influencing Loan Repayment in Microfinance Banks

Several factors affect loan repayment in microfinance banks, including the size of the loan, the borrower's income level, and the socio-economic background of the borrower (Aghion & Morduch, 2005). Interest rates, while significant, are not the sole determinants of loan repayment. Other factors such as the financial literacy of borrowers, the effectiveness of monitoring systems, and the repayment terms (e.g., loan duration and installment frequency) also play crucial roles.

2.1.4 Role of Balogun Fulani Microfinance Banks in local Economic Development

The studies carried out according to what I confirmed that Balogun Fulani microfinance banks is assist to reduce and alleviate poverty and enhance economic development, particularly in developing economies. In Nigeria, they have accelerated the operation of poverty alleviation programmes of the Government and supported promising entrepreneurs while aiding new ones to emerge. The role of Balogun Fulani microfinance banks in the promotion of local economic development is entrenched in the objectives of the microfinance banking scheme in local that was formulated in line with the objectives of the Millennium Development Goals (MDGs), the local Economic Empowerment and Development Strategy (LEEDS) and the Vision 2020.

These roles include the promotion of rural development through financial intermediation, stimulation of productive activities in the rural sectors development of banking habits among rural dwellers, ensuring the development of an integrated local financial system and improving the economic status of small- scale producers in the rural and urban areas.

2.1.4.1 Deposit Mobilization and Promotion of Saving Culture

One of the requirements of Balogun Fulani microfinance clients is a safe place to keep their savings so that they can build up large sums of money to meet several needs- payment for shops, tools, accommodation, school fees, medical expenses, marriages, burials, etc. These needs are met by the savings mobilization activities of the MFBs. Most micro enterprises find it difficult to leave their shops and business premises for banking transactions. The convenience of this role is that the staff of the bank go to the customers at their houses, shops, etc. for daily collection of deposits and loan. Balogun Fulani microfinance banks usually pay interest on the amount saved. This role has helped to promote a healthy banking culture among the hitherto marginalized groups.

2.1.4.2 Credit Extension to Customers

Credit delivery is perhaps one of the most important roles of microfinance banks, as the loans extended are the main source of funds used to expand existing businesses and in some cases to start new ones. The credit delivery system in the microfinance banks exclusively focus on the poorest of the poor, organize borrowers into small homogenous groups, and give loans to meet diverse development needs of the poor without emphasis on tangible collaterals.

Many microfinance banks have a number of loans such as small business loans, small entrepreneur lending, loans for hardcore poor, partnership build up programmes, etc.

Governments also encourage co-operatives to partner with the Balogun Fulani microfinance banks to raise bulk loans for on-lending to the beneficiaries.

2.1.4.3 Employment Generation

MFBs also contribute immensely to job creation in the rural areas through the provision of skills acquisition and adult literacy programmes. It has therefore been acknowledged that the rural setting is an arena of many industries and self-employed micro-enterprises, which could be empowered to contribute significantly to the national economy. In some cases, the MFBs may pass on new skills and production techniques to a micro enterprise under a profit.

2.1.5 Effects of microfinance on entrepreneurial development.

Balogun Fulani Microfinance bank is vital to the development of entrepreneurship activities in local area, People have access to capital for entrepreneurship development in local area through microfinance. Balogun Fulani Microfinance has affected entrepreneurship in the country positively.

The major contribution of Balogun Fulani Microfinance bank to the developing economy like that of Nigeria is its role in promoting entrepreneurship development in the nation. One of the goals of entrepreneurship routed by successful kwara state government has been the reduction of unemployment and poverty alleviation. A cordial thrust in public policy for the achievement of indigenous entrepreneurship through the provision of long term loans and equity capital by banks for enterprise. Given the gap between savings and invertible funds, the short fall is provided by credit delivery. Many newly developed and developing countries have therefore made credit delivery an endurable strategy in the development of entrepreneurship in both industry and agriculture.

The Balogun Fulani microfinance is evident tools for entrepreneurship development due to the various services they offer and the role they performs towards the development of the local economy. Balogun Fulani Microfinance bank is identified to be one of the key players in the financial industry that have positively affected individuals, business organizations, other financial institutions, the government and the economy at large through the services they offer and the functions they perform in the economy. It is expected that with the current reforms put in place by the Federal Government through its regulatory authorities, microfinance bank in Balogun Fulani will be able to compete favourably in the local market and gainfully increase entrepreneurship development in local government.

Balogun Fulani Microfinance bank have positive relationship with the Nigerian economy

represented by expanded GDP. Although, interest rate is not significantly influential, the results of findings of this study can still be summarized that the microfinance banks and their activities go a long way in the determination of the pattern and level of economic activities and development in the local economic.

2.2 Theoretical Framework

In this section, the Fisher's theory of interest rates and the stakeholder theory are reviewed and discussed in the context of interest rates and loan performance of MFIs.

2.2.1 Fisher's Theory of Interest

The Fisher's theory was invented by Irving Fisher in 1930 but has been advanced and criticized by various theorists and scholars ever since (Harrod, 1971; Fisher, 1974; Tymoigne, 2006). The theory base its argument on that, individuals are impatient to spend income and opportunity to spend it. It is stated that the nature of capital and income was primarily supposed to serve as a basis for the interest rate which immediately followed it. It is stated that the link between income and capital is the rate of interest. In other words, the theory defines the interest rate as the per cent of premium paid on money at a particular date in terms of money to be paid one year later. Theoretically, it is argued that money can be substituted with other sorts of goods. However, practically, it is only money that is traded between present and future, the foregoing argument justifies why the rate of interest is at times referred to as price of money and the market in which present and future money are traded for that price or premium is referred to as money market (Fisher, 1974).

It is opined that Fisher's real rate of interest framework is essential for the inflation-targeting framework. This is due to the reasoning that it rationalizes the notion that monetary policy ought to be concerned mainly with managing inflation expectations so as to keep interest rates at a stable level that enhances saving and investment (Cottrell, 1994; Smithin, 2003). In tandem with the interest rates and MFIs' loan performance, the Fisher's theory could be employed to explain the implication of inflation risk premium as a component of interest rates on the loan financial performance.

2.2.2 Stakeholder Theory

Stakeholder theory was the brainchild of Freeman (1984). The theory which is argued to exist in tension suggests that, firms have stakeholders whom they should pay attention to. Philips (2003) asserted that firms that diligently seek to serve the interests of a broad group of stakeholders are bound to create more value over time. Yet, it is averred that there are so many and various interpretations of basic stakeholder ideas that theory development has been difficult (Scherer & Patzer, 2011).

Freeman, Harrison, Wicks, Parmar and de Colle (2010) supported the argument of the existence of a positive relationship between stakeholder-oriented management and the performance of a firm. The firm's performance according to Choi and Wang (2009) is more often than not measured in terms of financial returns. In other words, financial performance is the most relevant measure of the value created by a firm. More so, loan performance depicts financial performance of MFIs to a great extent given that these financial institutions rely on the interest accruing from loans advanced to borrowers. In the context of MFIs, stakeholder theory can be employed to illustrate how those firms advance the interests of the stakeholder thorough enhancement of loan performance.

2.3 Empirical Review

Empirical review of the effects of interest rates on loan repayment in microfinance banks (MFBs) in Nigeria would involve examining existing studies, data, and findings on how interest rate levels impact borrowers' ability to repay loans. Microfinance banks in Nigeria play a crucial role in providing financial services to individuals, small businesses, and rural populations who typically do not have access to conventional banking services. However, the interest rates charged by these banks have been a subject of debate, particularly in relation to their effect on loan repayment.

The influence of unforeseen events, such as public health crises, environmental disasters, and economic downturns, on borrower's ability to repay a loan has been widely documented in the literature. Collier et al. (2024) used data from the U.S. Census Bureau and Business Credit reports that firms that applied for a government-provided recovery loan following a natural disaster. The study found that for borrowers with limited social safety nets, such events can negatively affect household finances, therefore causing borrowers to focus on immediate survival needs and thus delay in loan repayment (see also Lesego, 2020).

Group lending models was designed to expand access to microcredit programme and mitigate risk through shared responsibility, may also encounter repayment challenges due to group dynamics (Kodongo & Kendi, 2013; Muchnick & Kollamparambil, 2015). Ahlin and Debrah (2023) conducted a field experiment with group lending models in Ghana. The findings suggested that peer pressure and social collateral within group lending arrangements can influence repayment patterns both positively and negatively. A cohesive group can encourage timely repayments, but a default by one member can erode trust within the group lending leading to increased defaults. More specifically, Muchnick and Kollamparambil (2015) studied the impact of group homogeneity on repayment performance. Their findings indicated that large group sizes and mixed-gender groups (as opposed to groups with only females) were more likely have a negative impact, while more homogeneous groups showed better repayment performance.

Another strand of the literature has examined how behavioural and psychological traits of borrowers predict the credit default. Goel and Rastogi (2023) confirmed that certain non-financial factors can be assessed when granting a loan to a borrower. These factors can be used to develop a subjective credit scoring model that can quantify and verify the soft information, such as character and reliability of debtors. Friedetzky et. al., (2024) found that aligning repayment schedules with borrowers' unpredictable income patterns can significantly improve repayment rates.

2.3.1 Default Risk Premium and Loan Performance

A study on the trade-off between sustainability and outreach as experienced by microfinance institutions (Milson, 2013), and a global analysis of leading microbanks in respect of financial performance and outreach (Cull, Demirguc-Kunt & Morduch, 2007) revealed some common observations. The two studies indicated that the real gross portfolio yield is a proxy for interest rates charged by MFIs. In addition, they argued that the depth of outreach-viability controversy determines whether or not to subsidize interest rates. The authors gave a contextual and practical analysis involving the poor, interest rates charged and loan repayment default. It was exemplified in the event the interest rate prevailing in the market cannot be afforded by poor people and these people continue borrowing loans aware they would default in repayment, and if the loss from such interest rate induced default is outweighs the revenue gain from higher interest rates, then real yield is anticipated to negate operational self-sufficiency (OSS). The study observed that, the repayment rates amongst MFIs are part of their success stories which interpretatively implies that these firms have managed to keep the default risk sufficiently low. The authors further opined that, they are is a great belief that borrowers of credit from MFIs are able and willing to pay commercial interest rates. On the part of these institutions, low default rates are reported.

Notably, the MFIs are less efficient and often charge higher interest rates on loans and also have a shorter repayment plan. It is vital to note that, practically, wealthy clients barely subscribe to MFIs; however, clients who seek huge loans are likely to be those planning to default, thus the occurrence of high credit risks. This is justified by the argument that MFIs are unable to compete with deposit money banks in providing huge loans to wealth and creditworthy clients.

2.3.2 Interest Rate Sensitivity and Loan Repayment

A large body of research suggests that interest rates have a direct effect on borrowers' repayment behavior. High interest rates could increase the financial burden on borrowers, making it more difficult for them to meet repayment schedules. Conversely, lower rates might facilitate easier loan servicing and reduce default rates. In the context of Nigerian MFBs, interest rates are often set high to cover the costs of lending, but excessive rates might lead to loan defaults or late repayments, particularly among low-income borrowers. Studies have shown that borrowers in Nigeria tend to struggle with repayment when interest rates exceed certain thresholds, as their income levels do not grow proportionally with the loan amount or repayment terms.

Example: A study by Obamuyi (2013) examined the impact of microcredit on loan repayment behavior in Nigerian microfinance banks. The research found that high interest rates led to an increase in loan defaults, as borrowers faced difficulties repaying the loans due to insufficient cash flow.

2.3.3 Interest Rate, Loan Size, and Repayment Patterns

Another theme that frequently emerges is the relationship between the size of the loan and the repayment terms. When interest rates are high, smaller loans tend to have higher default rates because the interest component becomes a significant burden on borrowers. Larger loans might be more manageable, but the terms of repayment (including interest rates) might be more stringent. Studies have shown that borrowers may prefer smaller loans with lower interest rates, as the repayment is easier to manage. However, microfinance banks in Nigeria often charge higher rates for smaller loans to offset the risk of lending to high-risk, low-income clients. This creates a paradox where the poor borrower faces greater difficulty repaying smaller loans with high-interest rates.

Example: A research study by Osei-Assibey (2013) found that loan size, coupled with interest rate structures, had a significant impact on the repayment capacity of borrowers. Higher interest rates on smaller loans were found to have a negative effect on the timely repayment of loans.

Similarly, Sangwan (2023) noted that flexible repayment terms are beneficial as they accommodate income fluctuations, leading to better repayment outcomes, while rigid repayment schedules increase the risk of default. The advancement of technology has also revolutionized the way MFIs disburse and manage loan repayment performance. Millan et. al., (2023) for example, explored the implications of mobile banking technologies on the loan performance of DT SACCOS in Mombasa. The study found that the incorporation of digital payment systems and mobile banking significantly improves repayment efficiency by lowering transaction costs and enabling borrowers to experience convenient payment plans. However, Rozzani et. al. (2015) who examined the implementation of technology in the disbursement and repayment of MFIs from the clients' perspectives, reported that while clients were fairly satisfied with the disbursement process through a mobile solution, the same conclusion could not be drawn for the repayment process. It can therefore be safely concluded that while technology is acknowledged to have a positive impact, its benefits in management may vary between different aspects of the loan process.

2.4 Gap in Literature

The evidence of this study will contribute to the understanding of the impact of interest rates on loan repayment in the Nigerian microfinance sector. By examining the specific context of microfinance banks, this study will investigate how socio-economic factors, such as income, education, and occupation, influence loan repayment behavior in response to interest rate changes. it will contribute to the understanding of the current state of the microfinance sector in Nigeria, reflecting recent changes in regulations, technologies, and market conditions.

CHAPTER THREE

3.0 Research Methodology

3.1 Introduction

Balogun Fulani Microfinance is a banking service provided for low-income individuals or groups who otherwise would have no other access to financial services. Microfinance allows people to take a reasonable small business loans safely, in a manner that is consistent with ethical lending practices. The majority of microfinancing operations occur in developing nations, particularly Balogun Fulani Microfinance bank, Balogun Gambari, Ajikobi micro finance bank among others. Like conventional lenders, microfinanciers charge interest on loans and institute specific repayment plans.

3.2 Research Design

Research utilised a qualitative approach to ensure effective understanding of successful microloan repayments, challenges, and processes. Creswell (2009) said that this design enables the researcher to go further into the responder’s experiences, point of view and ideas concerning the factors affecting loan repayment mechanisms. As for obtaining more detailed insights about the processes and issues related to stable micro-loan repayment, this survey employed a qualitative methodology as the research method.

3.3 Population of the Study

The population of this study consisted of all loan clients of Balogun Fulani Microfinance Bank Ilorin, Kwara State, Nigeria. The bank has a total of 5,000 active loan clients.

3.4 Sample Size and Sampling Techniques

A sample size of 150 loan clients were selected for this study using the Taro Yamane formula for sample size determination. The study will employed a stratified random sampling technique to select the sample. The loan clients were stratified based on their loan repayment status (i.e., regular repayments, irregular repayments, and defaulters). A random sample of 150 loan clients were then selected from each stratum.

3.5 Methods of Data Collection

A structured questionnaire was designed and administered to the selected sample of loan clients to collect data on their demographic characteristics, loan repayment behaviour, and perceptions of interest rates. The bank's records and reports were reviewed to collect data on loan repayment performance, interest rates, and other relevant financial data.

Interviews were conducted with the use of a semi-structured interviews guide. This was to understand the loan repayment behaviour and the challenges that borrowers face. Open ended questions were used to allow researchers to gain a deep understanding of the elements contributing to borrowers' capacity to fulfill their financial obligations, as suggested by Creswell (2009).

Informed agreement before the interviews was mandatory in the participants. Interviews were conducted either in person or remotely (remote option being considered based on logistical considerations). To ensure accurate analysis and transcription, they were audio recorded. Interview sessions with participants took between 30 to 45 minutes, during which participants shared their perception and viewpoint of loan repayment practice. This methodology refers to Creswell (2009) in the design of interviews; hence participants can freely express their opinions which can be used for data collection.

3.6 Methods of Data Analysis

Regression analysis was used to examine the relationship between interest rates and loan repayment behavior. Chi-square analysis was used to test the significance of the relationships between interest rates and loan repayment behaviour.

3.7 Limitation to the Methodology

The study's findings may not be generalizable to other microfinance banks in Nigeria or other countries due to differences in institutional characteristics and environmental factors.

The study's sample may not be representative of the entire population of loan clients due to the use of a stratified random sampling technique. The study's findings may be influenced by measurement errors in the data collection instruments or procedures. The study focused on the effect of interest rates on loan repayment behaviour and did not examine other factors that may influence loan repayment behaviour.

CHAPTER FOUR

4.0 Data Presentation, Analysis and Interpretation

4.1 Data Presentation

According to the CBN, there are 916 microfinance banks in Nigeria as at October 2020. The broad objective focused on in this study was to examine the effect of interest rate on loan repayment capability of borrowers in MFBs. The study adopted the survey research design using a well structured questionnaire as research instrument to elicit primary data from borrowers of Balogun Fulani Microfinance Bank in Ilorin Kwara State, Nigeria.

The population of the study was some selected staff and customers of the microfinance bank. From the questionnaire issued out a total of 108 questionnaires were returned and considered usable for this research. In the questionnaire the respondents were required to rank each item in other of importance, A 5 point likert scale was used to indicate importance. Section A of the questionnaire was used to obtain demographic statistics of respondents. While section B was divided into 4 parts containing a total of 20 questions to obtain information from respondents on the interest rate that applies to loans, factors that affect loan repayment and method of collection of loan due for repayment.

Table 4.1 Demographic Statistics

		Freq.*(n=108)*	%
Gender	Female	65	60.2
	Male	43	39.8
	Total	108	100.0
Age	31-35 years	14	13.0
	36-40 years	28	25.9
	41-45 years	50	46.3
	46-50	16	14.8
	Total	108	100.0
Marital Status	Married	62	57.4
	Single	39	12.2
	Others	7	
	Total	108	100.0
Qualification	No formal Education	4	3.7
	Primary Education	5	4.6
	Secondary Education	44	40.7
	Tertiary Education	55	50.9
	Total	108	100.0
Occupation	Employed	40	37.0
	Self employed	61	56.5
	Others	7	6.5
	Total	108	100.0

Field Survey, 2021

RESULT AND DISCUSSION

For the purpose of this study a total the 110 copies of questionnaire were prepared, only 108 were returned and found usable for analysis, which is approximately 98%.

It is important to state that the questionnaire was ethically administered and that some respondents did not respond to all questions, leaving the total in some questions less than 110. Descriptive statistics were used to analyse date. The hypothesis formulated was analysed using chisquare. This was done to examine the infuence of interest rates charged by MFBs on loan repayment capability. 39.8% of the respondents were male while 60.2% were female. The results indicated that majority of the respondents were between the age bracket of 31-45 years of age. 13% of the respondents were ages between 31-35 years, 25.9% were ages between 36-40years, 46.3% were ages between 41-45 years, and 14.8% were ages between 46-50 years. Over half of the respondents had up to a tertiary education and almost half with up to secondary education. 57.4% of the respondents were married, 36.1%were single and 6.5% were others. This result implies that majority of the borrowers were married. In addition, over 50% of the respondents were self employed; 37% of the respondents were employed, 56.5% were self-employed while 6.5% were neither employed nor self employed.

Table 4.2

Descriptive result of effect of high interest rate of MFI on the repayment of borrowers' loans.

ITEMS	SD N(%)	D N(%)	U N(%)	A N(%)	SA N(%)	Total N(%)	Mean	Std Dev
The interest rate of microfinance banks is high compare to Deposit Money Banks	8 (7.4%)	7 (6.5%)	4 (3.7%)	9 (8.3%)	80 (74.1%)	108 (100.0%)	4.35	1.263
Not requesting for collateral influences the high interest rate charged by microfinance bank loans	12 (11.1%)	14 (13.0%)	14 (13.0%)	47 (43.5%)	21 (19.4)	108 (100.0%)	3.47	1.256
Borrowers default in paying back loans because of the high interest rate	0 (0.0%)	6 (5.6%)	21 (19.4%)	22 (20.4%)	59 (54.6%)	108 (100.0%)	4.24	.956
High interest rate could result in delayed repayment of loans	0 (0.0%)	14 (13.0%)	0 (0.0%)	42 (38.9%)	52 (48.1%)	108 (100.0%)	4.22	.980
If the interest rate on loan is single digit (less than 10%), it may make paying back easy for borrowers	3 (2.8%)	10 (9.3%)	5 (4.6%)	17 (15.7%)	73 (67.6%)	108 (100.0%)	4.36	1.106

Field Survey:2025

Test of Hypothesis

There is a significant effect of high interest rate of MFI on the repayment plans of borrowers' loans.

Table 4.3: Chi square result of effect of high interest rate of MFI on the repayment plans of borrowers' loans

Variable	Mean	Std. Deviation	N	Chi Square	Asymp. Sig.
Questionnaire items 1-5	21.67	1.82915	108	118.556	.000

Source: *Field Survey 2025*

Table 4.3 presents chi square result of effect of high interest rate of MFI on the repayment plans of borrowers' loans. The mean value (M = 21.67) indicates an average score of items 1- 5. The standard deviation (SD = 1.8294) result obtained indicate that individual score obtained does not differ from mean. Which indicate that the data is normally distributed. From the table, the chi square value obtained at 118.56 is statistically significant at 5%. Therefore, the null hypothesis which states that there is no significant effect of high interest rate of MFI on the repayment plans of borrowers' loans is hereby rejected and it is concluded that high interest rate of MFI significantly affects repayment of loans by borrowers.

Table 4.4: *Analysis of the impact of Interest rate on loan and business performance in Balogun Fulani Microfinance Bank in Ilorin Kwara State, Nigeria.*

Response	**Frequency**	**Percentage**
Strongly agree	12	20
Agree	34	57
Strongly disagree	4	7
Disagree	10	16
Total	**60**	**100**

Source: *Field Survey 2025*

According to table 4.4 23% of the respondents expressed a disagreement that micro-credit loans have helped their business grow. These respondents, in an interview explained that the bank charges high interest on loans and it is this high interest rate that have significantly affected their business operations and other claimed that, this effect have been witnessed with their profit margins hence making repayment difficult and the end result is closure of businesses. On the other hand, 77% proved with agreement that micro credit loans have helped their business grow however, many respondents accused the bank of charging high interest rates, which they claimed might affect their repayment with time if not revised.

Basing on these study findings, it was found out that though some customers have had their enterprises achieve some levels of growth, virtually all respondents complained about high interest rate and proved its effect on their repayment of loans. It was further found out that many micro-credit customers have pulled out using loans any more while others are planning to stop seeking for loans once their current running loans are fully repaid if, the bank does not revise its interest charged on loans.

But according to one Equity Bank supervisor in the loan department, some claims were true as he claims, “many businesses have grown from the small size capital to large capital as a result of loans;” however, different respondents criticized the method of lending as being uneasy. The criticism mainly was on the previous Micro-credit group lending method that in many cases it affects other parties who properly service their loans yet there are others who have intentions of defaulting or fail as a result of their business failure. It can therefore be inferred that though micro credit loans have caused business growth in the study area, the high interest rates on loans have affected their repayment and might continue to affect more as well as business failure to increased premium and inability to repay back

Table 4.5: Analysis of the proposed factors leading to loan defaulting in Balogun Fulani Microfinance Bank Ilorin Kwara State Nigeria.

Response	***Frequency***	***Percentage***
High interest rates	26	43.3
Short repayment period	3	5
Small loans	11	18.3
Fiscal policy (taxation)	-	-
Social problems (domestic)	4	6.7
Lack of entrepreneurship skills	16	26.7
Total	**60**	**100**

Field Survey 2025

From Table 4.5, results of micro credit problems affecting loan repayment in Balogun Fulani Microfinance Bank Ilorin Kwara State were analyzed. The researcher analyzed respondents‟ views on some limitations that affect loan repayment such as high interest rates, short repayment period, the government fiscal policy (tax) remuneration, size of capital (loan), social problems, lack business skills. In this Table 4.7, interest rates and small loans offered featured more frequently. Respondents in this research who criticized the high interest rate and lack of entrepreneurship skills as factors behind loan repayment and affecting their business growth and performance accounted to 43.3% and 26.7% respectively of the total number of respondents and this was followed by those who criticized the small size of loans offered (18.3%). Criticisms against short repayment period were 5%, social problems and domestic problems experienced with the business owners were 6.7%, while none of the respondents attributed loan repayment to taxation.

Analysis of Loan Repayment and Interest rates

Table 4.6 : Interest Rate charges

Response	Frequency	Percentage
Strongly agree	13	21.7
Agree	29	48.3
Not Sure	5	8.3
Disagree	9	15.0
Strongly Disagree	4	6.7
Total	**60**	**100.0**

Source: *Field Survey 2025*

The responses in Table 4.6 were given towards the statement that "the interest rate charged is high." About 70% of the respondents were in agreement with the statement. They claimed that other banks provided friendly interest rates but dealt with Equity bank due to the ease with which they could access the loans. However, all the 10 Equity bank officials disagreed with the statement as it would contradict with their operations.

Table 4.7 : Loan Repayment process

Response	Frequency	Percentage
Strongly agree	4	6.7
Agree	8	13.3
Not Sure	5	8.3
Disagree	28	46.7
Strongly Disagree	15	25.0
Total	**60**	**100.0**

Source: *Field Survey 2025*

The responses in Table 4.7 were given towards the statement that "Loan repayment is a smooth process." About 75% of the respondents were in disagreement with the statement with all the bank officials (10) disagreeing or strongly disagreeing. Bank officials said that majority of the people default due to various reasons above and recovering the money from them is not an easy process.

Table 4.8 : Relationship between Interest rate and Loan repayment

Correlations

		High Interest rate charged	*Loan Repayment is a smooth process*
High Interest rate charged	Pearson Correlation	1.000	-.246
	Sig. (2-tailed)	.	.690
	N	5	5
Loan Repayment is a smooth process	Pearson Correlation	-.246	1.000
	Sig. (2-tailed)	.690	.
	N	5	5

Source: Field Survey 2025

Data in the tables 4.8 and 4.9 was correlated. Pearson Correlation r equals -0.246 at 0.690 significance level. This indicates a negative correlation between high interest rate charged and the loan repayment being a smooth process. This implied that as the interest rate charged increases, loan repayment becomes a difficult process both on the side of the borrowers and the bank.

CHAPTER FIVE

5.0 Summary, Conclusion and Recommendation

5.1 Summary of Findings

This chapter is a synthesis of the earlier discussions. The main objective of the study was to examine the effect of interest rates on loan repayment, a case study of Balogun Fulani Microfinance Bank, Ilorin Branch, Kwara State, Nigeria.

The specific objectives of the study were; to investigate the effect of interest ceiling on loan repayment, to analyze the impact of interest rates fluctuation on loan repayment and to analyze the effects of interest rate on the supply of loans. Existing literature on the subject under study was reviewed. The study used questionnaires and interviews as data collection instruments/methods.

This study clearly showed that there is great close relationship between interest rates and loan repayment in conjunction with business growth and performance. High interest rates, coupled with lack of entrepreneurial skills were seen as the major factors that have a direct bearing with the loan repayment among Equity Bank loan customers. Literature available clearly shows that however much loans have great role in business growth and development and therefore performance, the level of interest rates has a significant effect in premium repayment thus one claim that a loan may not necessarily be solely the paramount factor, the self-efficiency theory clearly shows that enterprise growth and performance is dependent on entrepreneurship skills, which in many cases are equally districted to every person therefore giving loans to people who lack skills to effectively and efficiently invest it is a waste of time.

5.2 Conclusion

Microfinance banks play a critical role in making money available at the grassroots to reduce the level of poverty as such MFBs providing microfinance would provide for sustainable development. Thus the availability of the microfinance is necessary and should be not ne hampered by high interest rates. The study concluded that microfinance bank's interest rate is higher than Deposit Money Banks with a shorter repayment period which invariable could lead to default in repayment. The rate of interest on loans charges leads to failure to pay in time. Also, the most preferred repayment frequency is monthly compared to other available scheduled payment plan.

Furthermore, the key indicator of financial execution and proficiency of business banks is the spread between loaning and deposit rates. On the off chance that this spread is large, it fills in as an obstacle to the extension and improvement of financial intermediation. This is on the grounds that it disheartens potential savers because of low profits for stores and therefore restricts financing for potential borrowers. This has the far-reaching impact of decreasing achievable speculation openings and subsequently restricting future development potential.

Finally, it is concluded based on this study findings that loan size borrowed by Balogun Fulani Microfinance bank's client, the interest rate, and type of repayment schedule for the loan have effect on borrower's ability to repay loan.

5.3 Recommendations

Based on this study findings, it is recommended that since default on loans is linked to high interest rate

i. Balogun Fulani Microfinance bank and other microfinance banks should charge a fair and reasonable rate which the short-term borrowers can afford and the same time avoid risk of default in the long-run.

ii. Balogun Fulani Microfinance bank and other microfinance banks should partner with credit reference bureau such as Aset Manangement Company of Nigeria (AMCON) or Central bank in ensuring that information is communicated and shared on the loan defaulters in all financial institutions in the country.

iii. Balogun Fulani Microfinance bank and other microfinance bank should not only give loan based on borrowers presented collateral but should scrutinize the borrowers' credit history. The size of loan to be given to a borrower should be based on the borrowers' cash flow and financial aptitude.

iv. Effective monitoring of loan utilization should be done by Balogun Fulani Microfinance bank follow-up team to avoid diversion of the loan by the borrowers. This study focused on the effect of Microfinance banks' interest rate on loan repayment capability of borrowers using Balogun Fulani Microfinance bank as a case study. Others studies should encompass other microfinance banks to determine the relationship between interest rate and the loan repayment capability of borrowers.

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