THE EFFECT OF LOAN DEFAULT ON THE GROWTH OF COOPERATIVE SOCIETIES IN NIGERIA

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ABSTRACT

This study examined the effect of loan default on the growth of cooperative societies in Nigeria. Specifically, the study focused on establishing the association between loan management procedure, loan diversion and loan size and its association with the growth of cooperative societies in Nigeria. A total number of five (5) cooperatives were purposively selected for this study using the cross-sectional survey method of research design. Cooperative Society Growth is the dependent variable while Loan Management Procedure, Loan Diversion, and Loan Size as independent variables. The results affirmed that loan management procedure exerts positive insignificant effect on growth of cooperative societies in Ekiti State with coefficient estimate of 0. 619080 (p=0.0751>0.05); loan default exerts negative effect on growth of cooperative societies in Ekiti state with coefficient estimate of 0.479062 (p=0.0522=0.05); and loan size has positive insignificant relationship with growth of cooperative societies in Ekiti State given the coefficient estimate of 0.179562 (p=0.0802>0.05) and concluded that Loan default has remained a dominant issue that has discouraged most cooperative societies from granting loan to members while other cooperatives that has continuously disbursed loan to members have not performed soundly as they have remained stagnated per time. Therefore, recommended that Cooperative credit supervisor should evaluate records of credit officer to ascertain that loan policies are consistently observed; this would strongly establish loan procedures of cooperatives and enhance members commitment to loan repayment; Adequate training on financial management and business training should be carried out for members of cooperative towards aiding the profitability of their businesses and consequent payment of loan; Management of cooperative societies should ensure that loan requests are either declined or granted rather than approving an insignificant amount of loan application which encourages members to default; Loan approved should be based on the past record of the members; Creating channels that will make the loanee able to pay the loan at a convenient time before the exceeding period e.g Loan Applications for the members.

Keywords: Cooperative Society Growth, Loan Management Procedure, Loan Diversion Loan Size

INTRODUCTION

In the course of time, the increasing of poverty in most developing economies has necessitated the need for urgent intervention which primarily concerns the provision of huge and urgent financial alternatives for rapid and sustainable development aimed at improving the standard of living of individuals from different walks of life (Kassegn & Endris, 2020). Lending refers to the trust that gives one party a cause to provide resources to another party where the other party does not refund the money transferred immediately to the first party, but rather makes arrangement to pay the principal amount with interest (if applicable) at a pre-determined date (Nyaga, 2014). Cooperative societies have from the days of old to the present time have consistently encouraged development across the globe especially in emerging economies providing its members with the economic aids in the form of loan in the bid to cause improved standards and business prosperity for its members (Ajayi, Dada & Folorunsho, 2021). Adesina (1998) posits that cooperative society describes a set of people with the same mindsets and drive, whose passion is to cause the availability of the financial provisions that their members would find helpful. Contemporary researchers posited that it is an independent set of individuals who willingly joined force with other persons with similar interest to reach ordinary economic and social benefits through an organization jointly owned and managed democratically by a set organized member (Obasi, 2013). The usual failure of banks with regard to provision of loan to individuals either with or without adequate collateral security necessitated the need for social enterprise that ensures complete support for individuals with urgent economic and social needs; the basic intention was to amass economic resources of members and redistribute appropriately to members with extreme needs improving access of needy individuals to socioeconomic resources especially financial resources (Ajayi *et al*., 2021; Obasi, 2013). Notwithstanding these challenges and the adverse effect that it exerts on the operational performance and consequent prosperity of these organizations, the growth of cooperative society's remains measured with savings mobilization of the cooperative society (Abdullahi, 2016). Although, the issues of loan default are not solely caused by borrowers, lenders of financial resources play a crucial role in indulging borrowers as a result of not keeping proper records of loan disbursement and repayments. Bad loan management system has contributed significantly to the default issues thus making loan default unending with formal and most importantly informal financial institution (Baidoo, Yusif & Ayesu, 2020).

Nigeria has remained a low-income country where a good number of its citizens feed on less than US$1 per day with the generality of the populace living below the poverty line (Onafowokan, 2012). In fact, formal financial service providers have habitually shown preference to large and medium size businesses to the neglect of the teeming population of artisans, market men and women and small business operators. This has necessitated the need for the creation of cooperative societies that targets individuals with the same peculiarities and providing them with loans, which has become a viable option for aforementioned informal sector operators and salary earners (Ajayi et al., 2021). The causal factor has been attributed to several issues which have been affirmed severally in literature; managerial capacity of most cooperative societies remains a weakness that has marred its operations, this is evident in the poor loan processing and collection procedure that has contributed critically to loan default of cooperative members (Munyua, 2016). Again, members in their bid to fulfil other commitments different from the basic essence of obtaining the loan tend to use the loan obtained for another purpose which often include business opportunities that does not guarantee the realization of the principal amount invested or return on investment at least in the short term thus making default in repayment of the loan inevitable (Oluwakayode, Ogunmuyiwa, Aladegoroye, Akerele & Olabisi, 2020). Similarly, cooperative society indulge in multiple borrowing, that is, providing inadequate loan size to members giving less consideration to their prospect of paying back; consequently, this shoots up the number of loan defaulters which looking forward constrain the organization from achieving its basic objectives effectively which ultimately threatening its growth and survival (Munyua, 2016).

In fact, most of the loans disbursed by cooperative societies eventually become nonperforming loans which has per time affected the sustainability of cooperative institutions; this menace could be associated with loan management procedures which appears to be poor thus making loans incompetently managed and due diligence are almost not observed. Thus, has encouraged high loan default as members severally fail to repay their loans as and when due (Oluwakayode et al., 2020).

Also, loan disbursed to members to pursue productive investments are most likely directed to unproductive investments which may include residential building projects which guarantees no income generation; this makes poor repayment inevitable and further hinders the growth of cooperative societies in Nigeria (Zohair, 2013). In a similar way, cooperative societies appear to relatively low loanable funds compared to the mounting loan requests of members; in effect, the loan size disbursed to members often fall short of the amount requested. The implication is diversion of funds received to another cause thereby increasing loan default which drags down the performance
and growth of cooperative societies (Tundui & Tundui, 2013)

Considering the peculiarity of cooperative society and its contribution to the development of the economy, numerous studies have over time given focus to its growth and performance. Evidently, studies that established the association of loan default and the prosperity of cooperative society remains relatively low thus making this study worthwhile; again, effect of loan default on the growth of cooperative societies have not recently been considered as evident in the studies reviewed in this study; the growth of cooperative societies should be the basic concern of studies considering the significance of these organizations which qualifies them to grow on a consistent level so that their advantage can be fully harnessed. It is based on this premise that this study sets out to examine the effect of loan default on the growth of cooperative societies in Nigeria. The specific objective of this study is to evaluate the effect of loan management procedure on the growth of cooperative societies in Nigeria; examine the relationship between loan diversion and the growth of cooperative societies in Nigeria and investigate the effect loan size on the growth of cooperative societies in Nigeria.

LITERATURE REVIEW

Cooperatives Societies

Cooperative comes from the verb “operate” meaning to work and a prefix - Co‖ meaning together and merging the two gives the word Cooperative (Apata & Yusuf, 2020). In its broadest sense it means any two or more persons working together to achieve some aims. There exists no universally acceptable definition for cooperative societies as several meaning have been attached to the concept. Cooperative societies are self-regulated, self-funded microfinance institutions and often noticeable in communities as they are meant to service the local dwellers where the possibility to reach a formal banking system is almost impossible (Simkhada, 2004). Cooperatives are financial groups established and managed by members, providing savings and credit facilities to their members in the community (Sharma, et al., 2005). They are a kind of microfinance institutions owned by a set of people who are the members and they make available small scale financial services particularly savings and loans to their members. The concept of cooperatives differs completely from the formal microfinance institutions, for example microfinance banks (MFBs) in Nigeria which are focused on servicing the public (Oluyombo, 2012).

Basic Principles of Co-operative Societies

Cooperatives worldwide generally operate using the same principles as adopted in 1995 by the Intern Cooperative Alliance. The principles are part of a cooperative statement of identity, which also includes the definition of a cooperative as opine by Kareem, Arigbabu, Akintaro & Badmus (2012) includes: Voluntary and Open Membership, Democratic Member Control, Member Economic Participation, Autonomy and Independence, Education, Training and Information, Cooperation among Cooperatives and Concern for Community.

Cooperative Credit Facilities

A cooperative is simply an association of persons who pool their resources together on mutual basis to solve specific socio-economic problems, including income generating activities (Nwankwo, Ogbodo & Onwuchekwa, 2019). Cooperative societies constitute an avenue through which cheap credit is channeled to the rural areas and especially when it is supported by international donors and governments (Abdullahi, 2018). Kyazze, Nsereko and Nkote (2020), define credit as the power or ability to obtain goods or services in exchange for a promise to pay later. Credit, therefore, is the power or ability to obtain money by the borrowing process, in return for a promise to repay the obligation in the future (Katula & Kiriinya, 2018) Credit facility is a type of agreement that is made with the bank along with the person or organisation in terms of taking credit (Wasinda, 2019). Trade credit is the loan extended by one trader to another when the goods and services are bought on credit. Trade credit facilitates the purchase of supplies without immediate payment. Trade credit is commonly used by business organisations as a source of short-term financing (Lee, Wang & Ho, 2020).

Mobilization of savings by Cooperative Thrift and Loan Societies

Raising of venture capital is usually the responsibility of the owners of business while the employees render services and produce goods which are procured by the organization's customers. There are different sources of capital usually open to cooperatives including credit cooperative. These sources are grouped as owned and borrowed capital. Amahalu (2007) states that owned capital is obtained within the cooperative complex and borrowed capital is obtained outside the cooperative complex. Outside the cooperative complex is otherwise known as third party. Cooperative complex refers to the members of the cooperative and the cooperative business enterprise. Owned sources include; shares, reserves etc. sources of reserves include; retained annual shared capital, lapsed patronage grants and gifts, special earnings from assumption of member's liabilities to private outside lenders, manipulation of valuation etc. external sources of finance include borrowed fund from members of the cooperative, borrowed fund from the government, borrowed fund from financial institutions (commercial banks, micro fiancé banks, development banks etc) borrowed fund from other cooperative financial institutions, trade credit, etc. Ogbonna (2006) identified internal financing of cooperative to include entrance fee, share capital, savings deposit, admission fee and the external financing to include loans, deposits, overdraft, grants and aids.

Loan Default and Its Implication on Cooperative Growth

Default occurs when a debtor has not met his or her legal obligations according to the debt contract, e.g. has not made a scheduled payment, or has violated a loan covenant (condition) of the debt contract (Nicholas, 2010). A default is the failure to pay back a loan. Default may occur if the debtor is either unwilling or unable to pay his or her debt. This can occur with all debt obligations including bonds, mortgages, loans, and promissory notes. Defaulting on debt obligation can place a company or an individual in financial trouble. Loan repayment performance is an important concept for all the lending institutions. It is a measure of whether loans are settled up in full according to the loan contract or not. The higher loan repayment performance leads to the higher probability of the collecting interest revenues and lower loan losses in a lending institution (Kinyondo & Okurut, 2009). On the other hand, the poor loan repayments have a harmful impact on institutions capital, earning as well as in realizing its objectives and may even lead to a financial institution collapse. For instance, failure to manage loan repayment performance results in losses and high delinquency management costs (Ledgerwood, 2000). The higher expenses are for closer monitoring, more frequent portfolio and legal fees for pursuing seriously delinquent loans. Such costs adversely affect the generated income, and, in general, the operations of the lending institution, thus, the institution becomes unsustainable (Njanike, 2009).

RESEARCH METHOD

The model of Salaton, Gudda and Rukaria (2020) which explored the effect of loan default rate on financial performance of savings and credit cooperative societies Innarok, county Kenya was followed in this study. Notwithstanding that the study formed part of the few studies that established the association between loan default and performance of cooperative societies; it ignored the growth of cooperative societies which appears to be relatively significant. The need to ascertain the association between loan default and growth of cooperative has become necessary considering the role played by the organization; particularly the cause that they have taken which is to contribute noticeably to the development of the economy. However, the simple regression model of Salaton *et al* (2020) as provided in the study is demonstrated below:

$Y = \alpha + \beta_1 X_1 + e$ ………………………………………………………………….. 3.1

Where:

Y = A measure of Financial Performance based on ROA and ROE α = Constant term

β = Beta coefficient; X1 = Loan default rate (Amount of loan dispersed, amount of loan defaulted and default rate)

e = Error term.

Return on Asset = Total Profit/Total Assets

Return on Equity = Total Profits/Total Equity

Loan default rate = Non-performing loan/total loan advance

This study based on established arguments modifies the model of Salaton *et al* (2020) to reflect loan management procedure, loan diversion and loan size as basic proxies of loan default and its effect on growth of cooperative societies. Hence, the modified model is presented below for clarity:
COSG = *f* (LMP, LOD, LOS)……..………………………………………………. 3.2

$$COSG = \alpha_0 + \alpha_1 LMP + \alpha_2 LOD + \alpha_3 LOS + \mu \quad \text{……………..…..…………………... 3.3}$$

Where:

OSG = Cooperative Society Growth

MGP = Loan Management Procedure

LOD = Loan Diversion

LOS = Loan Size

μ = Stochastic Error Term

$\alpha_0, \alpha_1, \alpha_2, \alpha_3$ are parameter estimates corresponding to constants term

RESULTS AND DISCUSSION

Descriptive Results

Table 1: Demographic Characteristics of Respondents

S/N	Demographics		Frequency	Percent	Valid Percent	Cumulative Percent
1	Sex	Male	64	64.0	64.0	64.0
		Female	36	36.0	36.0	100.0
		Total	100	100	100	
2	Age	21-30	57	57.0	57.0	57.0
		31-40	20	20.0	20.0	77.0
		41-50	12	12.0	12.0	89.0
		50 and Above	11	11.0	11.0	100.0
		Total	100	100	100	
3	Marital Status	Single	10	10.0	10.0	10.0
		Married	71	71.0	71.0	81.0
		Divorced	7	7.0	7.0	88.0
		Separated	12	12.0	12.0	100.0
		Total	100	100	100	

4	Education Qualification	First Degree	14	14.0	14.0	14.0
		Master Degree	73	73.0	73.0	87.0
		Doctorate Degree	13	13.0	13.0	100.0
		Total	100	100	100	
5	Period of Membership	Below 3 Years	30	30.0	30.0	30.0
		3-5 Years	39	39.0	39.0	69.0
		6 Years & Above	31	31.0	31.0	100.0
		Total	100	100	100	

Source: Author's Computation, 2022

The demographic details of the respondents selected across leading cooperative societies with sound operation in Ekiti State - the study area is reflected in the above Table 1. The table demonstrated that 64% of the participants of the study are male while 36% are female; this indicates that male dominate the respondents of the study and also suggests that there was no gender bias. Also, it is evident from the Table 1 that 57% of the respondents falls within the age range of 21-30 years, 20% are within the age bracket of 31-40 years; while 12% aged between 41-50 years, 11% ages 50 years and above. In addition, the distribution of respondents regarding marital status indicates that 10% of the respondents are single, 71% are married, 7% are divorced and 12% are separated. Again, the educational qualification distribution displayed above indicated that 14% of the participants of the study has a First Degree, 73% are Masters holders while others - 13 % has Doctorate Degree; we can establish that respondents who took part of this study has adequate level of education. Furthermore, from the result revealed in Table 4.1 above, it is ascertained that 30% of the study's respondents has been with their cooperative for 3 years' experience, 39% has spent 3-5 years' with their cooperatives while 31% has spent over 6 years' with their cooperatives; hence affirming that the respondents that participated in this study has gathered satisfactory experience in the course of time. This result also implies that the respondent's demographics satisfy the demographic qualities required by the researcher in eliciting useable information for the study.

Correlation Analysis

Table 2: Correlation Matrix

	COSG	LMP	LOD	LOS
COSG	1.0000			
LMP	0.3155	1.000000		
LOD	0.5602	0.4821	1.0000	
LOS	0.4102	0.2052	0.4163	1.0000

Source: *Field Survey (2022)*

Table 2 presents correlation coefficient for pairs of variables adopted in the study. Specifically, the table reported correlation statistics of 0.3155, 0.5602 and 0.4102 for COSG and LMP, COSG and

LOD, COSG and LOS respectively. The result shows that there is positive relationship between pairs of variables used in the study. The correlation result connotes that loan management procedure, loan diversion and loan size move in the same direction with cooperative society growth as reported in the table above. This gives a reflection of the interconnection between the pairs of variables adopted in the model of the study.

Multicollinearity Test

The presence of strongly correlated variables in a model tends to create a multicollinearity problem. Therefore, the Variance Inflation Factor (VIF) test can be used to confirm the existence of multicollinearity among the explanatory variables of loan default amongst cooperative societies. Based on the rule of thumb, the VIF must be less than 10 to confirm that the estimates of the regression would not be biased due to the presence of multicollinearity.

Table 3 Result of Multicollinearity Test

Variable	VIF
LMP	1.302
LOD	1.509
LOS	1.209

Sources: Author's Computation, (2022)

Table 3 shows that all the variables have a VIF value of less than 10, thus implying that there is no strong evidence of collinearity among the explanatory variables of loan default amongst cooperative societies in Ekiti State.

Regression Analysis

Table 4: Regression Estimation Result

Influencing Variable: COSG

Variable	**Coefficient**	**Std Error**	**t-statistics**	**Prob.**
C	5.589366	5.226325	1.069464	0.2970
LMP	0.619080	0.213860	0.289477	0.0751
LOD	-0.479062	0.232817	2.057679	0.0522
LOS	0.179562	0.162003	1.108389	0.0802

R-Squared=0.8543

Adjusted R-Square=0.7621

F-statistics=3.84

Prob (F-statistics) = 0.0244

Result of the regression estimate in table 4 revealed the coefficient estimate of 0.619080, 0.479062 and 0.179562 for loan management procedure, loan diversion and loan size respectively. The result of the analysis shows that loan management procedure of cooperative societies in Ekiti State exerts positive insignificant effect on growth of cooperative societies; loan diversion exerts negative and insignificant impact growth of cooperative societies while health loan size exerts positive insignificant effect on growth of cooperative societies. In specific terms, improved loan management procedure of cooperative societies would command noticeable increase in growth of cooperative societies; result also established that reduction in loan diversion would lead to increased growth cooperative societies in Ekiti State. Evidence further obtained from the result that demonstrated that loan size maintains positive relationship with growth of cooperative societies which suggests that increasing loan size will culminate into an increase the growth of cooperative societies.

Specific estimates and probability values reveals that loan management procedure of cooperative societies in Ekiti State has a positive significant relationship with growth of cooperative societies with coefficient estimate of 0. 619080 ($p=0.0751>0.05$), loan diversion of members of cooperative societies in Ekiti State maintains negative insignificant relationship with growth of cooperative societies with coefficient estimate of -0.479062 ($p=0.0522=0.05$) while loan size disbursed by cooperative societies in Ekiti State has positive significant relationship with growth of cooperative societies given the coefficient estimate of 0.179562 ($p=0.0802>0.05$). R-square statistics reported in table 4.3 stood at 0.7621 which connotes that about 76% of the systematic variation in the growth of cooperative societies in Ekiti State can be significantly explained by loan management procedure, loan diversion and loan size. F-statistics and probability values reported in table 4.3 reflect that the model is a good fit, with the probability value of the reported statistics less than 0.05.

Post Estimation Test

Post estimation test conducted in the study include linearity test Normality test (using JarqueBera test) and heteroscedasticity test (using Breusch-Pagan Godfrey test). Summary of the aforementioned post estimations are presented in table 4.5 below:

Table 5: Post Estimation Test Result

Normality Test		
Statistics	*Values*	*Probability*
Jarque-Bera Stat	22.5164	0.0000
Heterogeneity Test		
Statistics	*Values*	*Probability*
F-statistic	0.3691	0.7760

Source: *Field Survey (2022)*

The estimates Jarque-bera statistics and probability values of the estimation conducted in the study reflect a coefficient estimate of 22.5164 and probability value of 0.0000. This estimate indicates that alternative hypothesis is well demonstrated and following the probability being less than 0.05 ($0.0000<0.05$), we affirm the normal distribution of the error term of the study's model.

Also, the heteroskedasticity test which assessed the heterogeneity of the variables reported fstatistics and probability values of 0.3691 and 0.7760 also describes that there is no justification to rejecting the null hypothesis of constant variance of the error term (homoscedasticity). Therefore, the test determined the lack of issue as regards heteroscedasticity in the error term of the models demonstrated in the study.

Discussion of Findings

The most consistent and efficient estimation result shown in table 4 suggests that loan management procedure exerts positive insignificant effect on growth of cooperative societies in Ekiti State thus implying that as loan management procedures improves, growth of cooperative societies also heightens. The series of approach adopted by management of cooperative societies to control the loan from the point of disbursement to the point when the loan has been completely paid (Agada, Iheanacho & Ogbanje, 2018; Gebeyehu, 2002; Kinyondo & Okurut, 2009; Njanike, 2009; Nsengiyumva, & Harelimana, 2020). At every stage of loan management cycle, adequate management is expected; peculiar approach is adopted from the pre-qualification stage to the loan disbursement stage thus guaranteeing the selection of members that would stay committed to the repayment of disbursed loan. This in effect ascertains that the cooperative would sustainably possess the resource required to persistent in providing loan to members; this consequently gives members a cause to remain active thus enhancing its growth of the society.

Again, the height of economic uncertainties across all states in Nigeria including Ekiti State, and the effect it has on the wealth of individuals and households significantly contributes to the failure of business projects and other ventures where funds are pooled by cooperative members towards making profit. Most times, the failure of these ventures or the uncompletion of other projects are envisaged by cooperative members thus causing the diversion of loan obtained to other ventures which may hinder the repayment of such loan as most of these ventures may not guarantee return on investment in the shortest time as promised by cooperative members; this contributes to the increased height of loan default which consequently drags down the growth of cooperative societies in Ekiti state. This results of loan diversion which could lead to loan default and it conforms to Baidoo, *et-al* findings (2020).

Lastly, loan size has positive insignificant relationship with growth of cooperative societies in Ekiti State which implies that as loan size increases, growth of cooperative societies also increases. Cooperative societies generates interest income from loan disbursed to members which suggests that the disbursement of relatively large loan which gives the society the chance of maintaining higher revenue which is deployed to financing of projects which includes building projects, business ventures amongst other economic activities that the organization embarks on. Although the disbursement of loan in large sizes may contribute to loan default, but it bolsters the earning capacity of the society; in fact, part of the interest income are retained and distributed to members thereby providing them with funds to execute other smaller projects, this influences rate of cooperative membership which translates to the growth of the society. This conforms with the study of Kassegn and Endris (2020).

SUMMARY AND RECOMMENDATIONS

Loan default has remained a dominant issue that has discouraged most cooperative societies from granting loan to members while other cooperatives that has continuously disbursed loan to members have not performed soundly as they have remained stagnated per time. In establishing the cause for the menace, the results obtained in this study revealed that loan default has an association with growth of cooperative societies in Nigeria. Specifically, the study established that loan management procedure exerts positive insignificant effect on growth of cooperative societies in Ekiti State, hence we conclude that loan management procedure of cooperative societies in Ekiti State appears ineffective and has contributed to relatively low growth of cooperatives in the state. Loan default exerts negative effect on growth of cooperative societies in Ekiti state thus we conclude that cooperative members have increasingly defaulted loan terms and this has dragged cooperative growth in Ekiti State. Loan size has positive insignificant relationship with growth of cooperative societies in Ekiti State, hence we establish that loan size exerts noticeable effect on the growth of cooperative societies in Nigeria.

Based on these findings, it is thereby urgent that the following suggestions be made:

i Cooperative credit supervisor should evaluate records of credit officer to ascertain that loan policies are consistently observed; this would strongly establish loan procedures of cooperatives and enhance members commitment to loan repayment

ii Adequate training on financial management and business training should be carried out for members of cooperative towards aiding the profitability of their businesses and consequent payment of loan.

Iii Management of cooperative societies should ensure that loan requests are either declined or granted rather than approving an insignificant amount of loan application which encourages members to default.

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