

Relationship Between Borrowers' Characteristics and Loan Default Among SMES in Eldoret City; The Moderating Role of Social Capital

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Abstract

Financing Small and Medium Enterprises (SMEs) in developing nations is gaining attention due to their vital role in job creation. Research has largely focused on access to finance, overlooking loan default issues and project execution challenges. Even with available funding, SME defaults remain prevalent. Social capital helps bridge information gaps, especially in micro-lending, where strong borrower-lender relationships are key. Therefore, the purpose of this study was to investigate whether social capital moderates the relationship between borrowers' characteristics and loan default among SMEs. The study was anchored on Social Capital Theory. The study targeted 2,485 SMEs in Eldoret City, with a sample size of 270 respondents determined using the Yamane formula. Data was collected using closed-ended questionnaires distributed to SME owners and managers. Cronbach alpha was used to determine the reliability and validity of questionnaires collected through pilot study in Iten town. Data was analyzed using descriptive and inferential statistics. The findings indicated that borrower's gender ($\beta_1 = 0.120, p < 0.05$), borrower's education ($\beta_2 = 0.240, p < 0.05$) and social capital ($\beta = 0.239, p < 0.05$) had a positive and significant effect on borrower's loan default. However, borrower's business experience had a negative and significant effect on loan default ($\beta_3 = -0.108, p < 0.05$), indicating that more experienced borrowers are less likely to default. Further, the moderating effect between borrower's gender and social capital ($\beta = 0.105, p < 0.05$), as well as borrower's education and social capital ($\beta = 0.101, p < 0.05$), showed a significant positive effect on loan default, suggesting that social capital amplifies the influence of these borrower characteristics on default risk. The findings provide both management and policy recommendations. Lenders should evaluate borrower characteristics during the loan evaluation process. Secondly, policy action is necessary to improve financial literacy among SMEs. Due to varying cultural, legal, and institutional contexts in developing countries, further research may explore alternative jurisdictions.

Keywords: Borrower's characteristics, social capital, loan default, SMEs

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Introduction

According to the World Bank (2019), Small and Medium Enterprises (SMEs) account for about 90% of businesses and over 50% of global employment, contributing up to 40% of GDP in developing countries. SMEs are widely recognized as key drivers of economic growth, employment generation and innovation across the globe (Surya, et al., 2021; Omowole et al., 2024). In Kenya, SMEs are the backbone of the economy, accounting for 98% of businesses and contributing significantly to GDP, innovation, and job creation. They employ over 14.9 million people across various sectors, with most operating informally. SMEs also are key in poverty reduction and economic development, as highlighted in Kenya's Vision 2030 (KEPSA (2024)). The success and overall sustainability of these SMEs largely depend on their ability to access and borrow funds from lending institutions. However, because of their limited operation capacity and scale coupled with low financial literacy skills, SMEs are more likely to default on their loans as compared to large established firms. As shared by Duarte, Gama and Gulamhussen (2018), fluctuation in sales

revenue creating liquidity shocks and constraints is a key feature of the SMEs that reduce the available cash flows for repayment of loans thus increasing the default rate. By June 2018, the default rate among Irish SMEs was 17.5% when weighted by loan size, down from 19.8% in December 2017. The accommodation and food sector experienced the highest default rate, nearing 30% (Irish Times, 2024).

There are two perspectives the loan default can be approached: the borrower and the lender. Loan default arises when a borrower is unable to repay the interest and the principal amount of the outstanding credit facility that was received from a lender (Santoso, Trinugroho & Risfandy, 2020). From the latter perspective, loan default is defined as the inability of the lender to recover the advances disbursed to borrowers as and when they fall due. Loan default can be viewed as bad loans on the side of the lender also called non-performing loan (NPL) (Uddin, 2019). Therefore, a defaulted loan is an advance that has not been honored on the basis of the established

terms and conditions between the borrowers and the lenders. Borrowers can default their loans either partially or fully. Borrowers can default on their loan obligations majorly due to unfavorable conditions that may come about which may have an adverse implication on borrower's ability to repay the loan amount (Ssekiziyivu, Bananuka, Nabeta & Tumwebaze, 2018).

Borrowers' characteristics like gender, education, and income and business experience have long been linked with loan default. According to World Bank (2007), gender of the borrowers is recognized as the factors influencing repayment of loans. This contradicts assertion of Jalloh, Appiah and Gyimah (2019) who held that female borrowers are positively but insignificantly associated with loan default. Beck, Behr and Guettler (2012) noted that there exists significant association between lower loan default rate and female borrowers. Godquin's (2004) failed to obtain adequate evidence to support the assertion of whether female borrowers outweigh the male counterparts when it comes to loan repayment. These views are similar with Bhatt and Tang (2002) as well as Adusei and Appiah (2011). On the contrary, D'Espallier et al., (2009) observed that unlike low educated borrowers, the highly educated counterparts are unlikely to default on their loans. The study by Nyahende (2013) focused on Tanzania and explored how the students' loans borrowers' characteristics impacted on default rate. It was shown that gender and age positively and significantly influence the default rate of student loan repayment. Bank employees frequently assume the responsibilities of village counselors, financial managers, and conflict mediators simultaneously (Ito, 2003). The beneficial elements of the social interactions that develop between bank employees and borrowers are now

referred to as social capital. Studies have underscored the establishment and preservation of social capital between staff and borrowers is essential for: identifying and training borrowers; selecting and approving loan proposals; negotiating solutions when issues arise (e.g., the death of a group member, crop failure due to a cyclone, etc.); and countering criticism even hostility from skeptics, moneylenders, and certain religious leaders. Qian et al. (2010) examined the impact of external horizontal social networks, external vertical social networks, and internal vertical social networks on the growth of firms in China. The research utilizing data from the Pearl River Delta indicates that all three elements of social networks positively influence firm growth. Muthoni (2016) analyzed the business and borrowers factors that can cause default of microcredit in Kenya with emphasis on comparing the MFIs and financial intermediaries (FIs).

In Kenya, approximately 60.7% of small and medium enterprises (SMEs) in Kenya were reported to have defaulted on their loans as of June 2023. This figure reflects a significant increase from 42.8% in October 2022, indicating a growing challenge for these businesses in managing their loan repayments according to Business Daily (2023). In Eldoret City, a growing number of SMEs rely on bank loans and credit facilities to finance their operations. However, loan default rates have continued to rise, raising concerns among financial institutions, policymakers, and business owners. Therefore, this study examines the relationship between borrowers' characteristics and loan default among SMEs in Eldoret City, as well as the moderating role of social capital in this relationship.

Literature Review

Theoretical Framework

This study is grounded in Social Capital Theory (SCT), as articulated by Pierre Bourdieu in 1985. The theory posits that social capital is the aggregate of the actual or potential resources which are linked to possession of a durable network of more or less institutionalized relationships of mutual acquaintance or recognition (Gilbert, 2008; de Camargo Fiorini et al., 2018). Bourdieu's framework suggests that the benefits derived from social capital are not uniformly distributed but depend on one's position within the social hierarchy and the effort invested in cultivating these relationships (de Camargo Fiorini et al., 2018). Traditional lending institutions often perceive SMEs as high-risk due to limited collateral and financial histories (Peprah, 2016). However, robust social networks can mitigate these challenges by providing alternative mechanisms of trust and information flow. For instance, in Kenya, studies have shown that social capital enhances financial inclusion by increasing access to informal loans (Mwangi & Ouma, 2012; Wabwire, 2020). Networks characterized by trust and reciprocity enable members to share information about creditworthiness and enforce repayment norms, thereby reducing the perceived risk for lenders (Ullah et al., 2024). Applying SCT to the study of loan defaults among SMEs in Eldoret City involves examining how borrowers' social networks influence their financial behaviors and repayment patterns. Strong social ties may enhance loan repayment through mechanisms of peer monitoring and collective accountability. However, weak social capital could contribute to higher default rates due to a lack of communal oversight and support. Understanding these dynamics can inform the development of

credit models that incorporate social capital considerations, potentially leading to more effective lending practices and reduced default rates among SMEs.

Empirical Review

Relationship between borrower's characteristics and loan default

The nexus between borrowers' characteristics and loan default has been subject to several empirical studies. Santandreu, López Pascual and Cruz-Rambaud (2020) did a study in the United States of America on key issues that determine the repayment of loans considering the male and female borrowers from MFIs. The study established that there are no strong motivation and incentives that influence women to repay their loans better than male borrowers in USA. It emerged that MFIs existing in the USA needed to review their credit policies in regard to women.

Koride and Gurtoo (2019) sought to compare the borrowing and default behavior of both male and female borrowers. In total, 490 men and 349 women were sampled through systematic sampling from Andhra Pradesh. It was established that the disenfranchisement of women from property and income of the family means that women entirely dependent on their membership with self-help groups for borrowing. Jalloh, Appiah and Gyimah (2019) sought to resolve a big puzzle on whether gender affected the loan default utilizing the emerging market context. The specific focus of the study was on investigating if female borrowers were less risky in default of loan compared to male borrowers. The method used for analysis was logit and data set of 3,717 loan clients from big lending entities in Sierra Leone was utilized over 2007-2014. It emerged that female borrowers were

positively linked loan default but insignificant.

Zakaria, Rasyid, Mohamed, Daud and Ismail (2020) conducted a study on loan defaults among tertiary graduates. The study aims to investigate the factors of study loan default among Malaysia tertiary graduates. Questionnaires were distributed to 430 Universiti Teknologi MARA, Johor, Malaysia graduated respondents via online and 209 were returned. The result of this study revealed that the employment status, loan amount and education level are significant to study loan default among Malaysian tertiary graduates.

Wanjikub and Muturi (2015) did an assessment of financial literacy and its effect on loan repayment using a case of ecumenical churches loan fund. The results showed a negative relationship between independent variables and the probability of a respondent delaying in repayment. Magali (2013) also found that borrowers with more business experience are likely to manipulate around and default on their loans. Eresia-Eke (2016) did an assessment of the experience of the business manager and its contribution towards loan default. The author found that the experience of the owners and managers was significantly linked with the loan default. Muthoni (2016) did an assessment of business factors that explain default of loan in Kenya. This was a comparison of the financial intermediaries and the MFIs within the context of Subsaharan Africa. A sample of 106 MFIs and 40 FIs was used and the study found that business related factors had significant implication on loan default rate.

Moderating role of social capital

Studies have shown that vertical social capital, the nature of relationship between the lender and the borrower enhances loan repayment. For instance,

Gao, Liu, Yin and Zhang (2022) focused on mobile lending and explored how social capital, phone call activities and loan default were linked with each other. The study observed that phone call activities are a key component of social capital. Informed by the social capital theory, the study identified and studied two types of calling activities: income against outgoing calls as well as strong and weak ties. It emerged that an increase in incoming calls to the borrowers reduces the loan default probability. It also emerged that calling activities linked with strong socially established ties have more predictive power for loan default as compared to the activities linked with weak social ties.

Cassar et al., (2007) did a study focusing on social capital loan repayment in South Africa and Armenia. It was observed that individual trust between group members of the lending institution as well as social homogeneity are critical to loan repayment as compared to general societal trust. Dufhues et al., (2011) appraised the network based social capital and its implication on loan repayment performance at individual level using the context of Thailand. The findings revealed that social capital was significantly linked with repayment performance. Kangogo et al., (2013) did an analysis of social capital dimensions and their implication on ability of households to take part in loan repayment from, micro credit groups in Kenyan context. The study used a sample of 174 households. The authors observed existence of significant link between social capital and loan repayment. Kangogo, Lagat and Ithinji (2013) did an analysis of social capital dimensions and their implication on ability of households to take part in loan repayment from, micro credit groups in Kenyan context. The specific focus of the study was on Uasin Gishu County and a total of 174 households were selected through multi-stage sampling and

included in the study. Tobit regression models were adopted for analysis. The study observed existence of significant link between social capital and loan repayment.

Methodology

Population and sample

The target population for this study was 2485 registered SMEs operating within Eldoret Town as of January 2022. The sample for this study was determined using Yamane Taro (1967) formulae computed as follows;

$$n = \frac{N}{1 + N(e)^2}$$

Where

n = Desired sample size

N = Total Population under Study (In this case, there are 2485 registered self-help groups operating as small and medium enterprises (SMEs)

e = Signifies the margin of error in this case taken as 5%

Hence,

$$n = \frac{2,485}{1+2,485(0.05)^2}=270$$

Therefore, the study sample is approximately 270 SMEs.

Data collection

Data was collected using close ended questionnaires. The dependent variable (loan default) and the moderator social capital were measured on a five-point Likert scale. Loan default had 5 items borrowed from Owusu-Manu (2019). While social capital was measured using 6 items that were borrowed and modified from Iqbal and Rao (2023). The borrower’s characteristics were measured as follows:

$$LD_{it} = \beta_0 + \beta_1BG_{it} + \beta_2BE_{it} + \beta_3BBE_{it} \dots \dots \dots \text{Model 1}$$

$$LD_{it} = \beta_0 + \beta_1BG_{it} + \beta_2BE_{it} + \beta_3BBE_{it} + \beta_4SC_{it} + \varepsilon_{it} \dots \dots \dots \text{Model 2}$$

gender, “1” male otherwise “2”. No education (1), primary school education (2), secondary school education (3), diploma/degree (4) and postgraduate graduate (5). Business experience, less than 1 year experience (1), between 2-3 years of experience (2), more than 4 and 5 years of experience (3) and more than 5 years.

Content validity was checked by asking a range of inquiries regarding the tool or assessment and/or inquire the viewpoint from a specialist in the field, mainly the supervisors and peers. Construct validity was checked by this research study using Exploratory Factor Analysis (EFA) checking Bartlett's Sphericity and Kaiser-Meyer-Olkin (KMO) values. Validity and reliability were determined through Cronbach alpha with pilot data from Iten town where the value was 0.724 indicating reliable instruments.

In this study, both numerical and graphical methods was employed to present descriptive statistics. Measures of central tendency, such as the mean provide insights into the central position of the data set, while measures of dispersion, including standard deviation, skewness and kurtosis, offered information on the variability and distribution of the data.

Regression model

Hierarchical regression analysis was used to investigate the effect of borrower’s characteristics on loan defaults and whether social capital moderates the relationship.

The study tested the effect of the independent variables on the dependent variable as shown below.

The study tested the effect of the moderator variable on the dependent variable as shown below.

The study tested the effect of the first interaction between borrower’s gender and social capital on the dependent variable (Loan default) as shown below.

$$LD_{it} = \beta_0 + \beta_1BG_{it} + \beta_2BE_{it} + \beta_3BBE_{it} + \beta_4SC_{it} + \beta_5BG * SC_{it} + \varepsilon_{it} \dots \text{Model 3}$$

The study tested the effect of the second interaction between borrower’s education and social capital on the dependent variable (Loan default) as shown below.

$$LD_{it} = \beta_0 + \beta_1BG_{it} + \beta_2BE_{it} + \beta_3BBE_{it} + \beta_4SC_{it} + \beta_5BG * SC_{it} + \beta_6BE * SC_{it} + \varepsilon_{it} \dots \text{Model 4}$$

The study tested the effect of the third interaction between borrower’s experience and social capital on the dependent variable (Loan default) as shown below.

$$LD_{it} = \beta_0 + \beta_1BG_{it} + \beta_2BE_{it} + \beta_3BBE_{it} + \beta_4SC_{it} + \beta_5BG * SC_{it} + \beta_6BE * SC_{it} + \beta_7BBE * SC_{it} + \varepsilon_{it} \dots \text{Model 5}$$

Results and Discussion

Response rate

In this study, a total of 270 respondents were targeted by the study, and the researcher was able to obtain replies from 257 study participants. The results of this study are presented in Table 1 below. According to Mugenda and Mugenda (2003), this reflected a response rate of 95.0%, which was a good representation that would bring forth adequate reliability and validity of the responses from the study findings. This was said to be a good representation.

Where;

LD = Loan Default

β₀ = Constant

β₁- β₄ = Coefficients of the equations

Firm Size

BB=Borrower’s Gender

BE= Borrower’s Education

BBE= Borrower’s Experience

SC= Social Capital (Moderator)

X1 = Interaction term

t = Time

i = Firm

ε = error term

Table 1: Response rate

Response rate	Frequency	Percentage
Response	257	95.0
Non-Response	13	5.0
Total	270	100

Source: Field data (2024)

Reliability and validity

The questionnaire's reliability and validity in the study were assessed using Cronbach Alpha. Cronbach's Alpha is a commonly employed statistic in psychometrics that quantifies the internal consistency or reliability of a set of items inside a questionnaire. The Alpha value of an assessment instrument typically ranges from 0 to 1, with higher values indicating stronger internal consistency. A commonly

used guideline suggests that an Alpha value of 0.70 or higher is generally considered acceptable for research and practical purposes. This indicates that the items in the assessment instrument reliably measure the same underlying construct. Nevertheless, the particular circumstances and objectives of the research, along with the characteristics of the items, can impact the suitable criterion for establishing the acceptable degree of internal consistency

(Conelly, 2011). The test findings presented in Table 2 indicated that both

constructions met the recommended KMO and Bartlett's criteria of 0.5.

Table 2: Reliability statistics

Item	Cronbach's Alpha	KMO	N of Items
Loan default	.724	.762	5
Social capital	.669	.566	6

Source: Field data (2024)

The Cronbach's Alpha for the study variables according to table 1 indicates that the scale is above 0.7 and therefore there is high reliability and internal consistency in the data collected for all the study variables.

Descriptive statistics

The variable "Loan default" has 257 observations with values ranging from 2.6667 to 4.6667. The mean value is 3.6486, indicating that the average loan default score is moderately high. The standard deviation of 0.47174 suggests that the loan default scores are somewhat consistent, with moderate variability among borrowers. The skewness of -0.178 indicates a slight left skew in the distribution, meaning that the scores are slightly more concentrated on the higher end. The kurtosis value of 0.306 suggests that the distribution of loan default scores has tails that are slightly lighter than a normal distribution.

The "Borrowers gender" variable also consists of 257 observations and is coded as either 1 or 2. The mean value is 1.7375, showing that there are more borrowers coded as 2 than 1. The standard deviation is 0.4400, indicating some variability in the gender distribution, but with a higher concentration towards one of the genders. The skewness of -1.088 reflects a moderate left skew, meaning a higher proportion of the observations are closer to the upper end of the scale, potentially indicating a higher number of female borrowers. The kurtosis of -0.819

suggests a flatter distribution compared to a normal distribution, indicating less extreme values.

For "Borrower's education," there are 257 observations with education levels ranging from 1 to 4. The average education level is 3.4015, suggesting that the majority of borrowers have relatively high education levels. The standard deviation is 0.6870, pointing to moderate variability in education levels among the borrowers. The skewness of -0.864 indicates a moderate left skew, meaning that the distribution is slightly skewed towards higher education levels. A kurtosis value of 0.135 indicates that the distribution is close to normal, with tails that are neither too heavy nor too light.

The "Borrower's business experience" variable includes 257 observations, with experience levels ranging from 1 to 4. The mean value is 3.3475, indicating that borrowers generally have considerable business experience. The standard deviation of 0.8891 suggests a relatively high variability in business experience among borrowers. The skewness of -1.242 reflects a significant left skew, meaning a greater concentration of borrowers have higher business experience levels. The kurtosis of 0.606 indicates a distribution with tails slightly heavier than a normal distribution, implying a few more extreme values than would be expected in a normal distribution. The "Social capital" variable consists of 257 observations, with values ranging from 2.5000 to 5.0000. The mean social capital score is 3.7964, indicating that on average,

borrowers have a high level of social capital. The standard deviation of 0.5403 shows moderate variability in social capital among borrowers. The skewness of 0.147 suggests a slight right skew in the distribution, meaning the scores are

marginally more concentrated towards the lower end. The kurtosis of 0.552 indicates that the distribution has slightly heavier tails than a normal distribution, implying the presence of a few more extreme values than expected.

Table 3: Descriptive statistics results

Variables	Number of observations	Minimum	Maximum	Mean	Standard deviation	Skewness	Kurtosis
Loan default	257	2.6667	4.6667	3.6486	.47174	-.178	.306
Borrowers gender	257	1.0000	2.00	1.7375	.4400	-1.088	-.819
Borrower’s educations	257	1.0000	4.0000	3.4015	.6870	-.864	.135
Borrower’s business experience	257	1.0000	4.0000	3.3475	.8891	-1.242	.606
Social capital	257	2.5000	5.0000	3.7964	.5403	.147	.552

Source: Field data (2024)

Correlation analysis

Results from the table 4 indicate that loan default is positively related with borrower’s gender ($r = 0.277, p < 0.05$). The higher the borrower’s gender the higher the loan default. The results also indicate that borrower’s education is positively related with loan default ($r = 0.438, p <$

0.05). Consequently, the higher the borrower’s education, the higher the loan default. Results further show that borrowers business experience is positively and insignificantly related with loan default ($r = 0.008, p > 0.05$). Therefore, the higher the borrower’s business experience, the higher the loan default.

Table 4: Correlation analysis results

Variables	LD	BG	BE	BBE	SC
Loan default (LD)	1.0000				
Borrowers gender (BG)	0.277**	1.0000			
Borrower’s educations (BE)	0.438**	-0.003	1.0000		
Borrower’s business experience (BBE)	0.008	0.070	0.273**	1.0000	
Social capital (SC)	0.390**	-0.185**	0.237**	-0.006	1.0000

** . Correlation is significant at the 0.05 level (2-tailed).

Source: Field data (2024)

Results indicate that the social capital is positively related to loan default ($r = 0.390, p < 0.05$). Consequently, the higher social capital, the higher the loan

default. There was a weak, negative and insignificant relationship between borrower’s educations and borrower’s gender ($r = -.003, p > 0.05$). There was a weak, positive and insignificantly

relationship between borrower's business experience and borrower's gender ($r = .070^{**}$, $p > 0.05$). There was a negative and significant correlation between social capital and business gender ($r = -.185^{**}$, $p < 0.05$). There was a weak and positive relationship between borrower's business experience and borrower's education ($r = .273^{**}$, $p < 0.05$). The correlation between social capital and borrower's education was positive and significant ($r = .237^{**}$, $p < 0.05$). There was a negative insignificant relationship between social capital and borrower's business experience ($r = -.006^{**}$, $p < 0.05$).

Regression Analysis

After conducting correlation analysis, where it was established that each of the independent variables in the study had a positively significant relationship with the dependent variable, there was need to assess how all the independent variables jointly affect the dependent variable.

R square is used to determine the extent the predictor variable explain the change in the outcome variable. The regression model explains 29.1% of the changes borrower's loan default among micro medium and small enterprises in Uasin Gishu County, as explained by borrower's characteristics. The moderate explanatory power is an indicator that there may be more determinants of performance of borrower's loan default among micro medium and small enterprises in Uasin Gishu County not captured in this study.

Testing Direct Hypothesis

Hypothesis 1 (H_{01}) stated that borrower's gender has no significant effect on borrower's loan default among micro medium and small enterprises in Uasin Gishu County. The findings in Table 5 indicate that

borrower's gender had a positive and significant impact on borrower's loan default ($\beta_1 = 0.120$, $p < 0.05$): hence H_{01} is rejected and it is concluded that borrower's gender has significant influence on borrower's loan default among micro medium and small enterprises in Uasin Gishu County. The findings are supported by empirical literature done by Kimaiyo (2016) who investigated the challenges SMEs face in accessing credit within Uasin Gishu County and found that male entrepreneurs had higher chances of securing credit facilities compared to their female counterparts. This disparity was attributed to factors such as complex application procedures, high interest rates, insufficient collateral, and poor record-keeping. Cheluget (2013) examined the challenges women entrepreneurs encounter in accessing financial credit in Kapseret Constituency, Uasin Gishu County. The study identified several challenges, including lower educational levels, high interest rates, low business income, and socio-cultural constraints. These factors not only affect women's ability to obtain credit but may also impact their capacity to repay loans, potentially influencing default rates among female borrowers. Tangut (2012) also explored how access to business credit affects gender relations in rural households within Uasin Gishu County. The study revealed that while microenterprise financing empowered women economically, it also led to increased workloads and responsibilities. The pressure of balancing business obligations with domestic duties could influence women's loan repayment behaviors, potentially affecting default rates.

Hypothesis 2 (H_{02}) stated that borrower's education has no significant effect on borrower's loan default among Micro medium and small enterprises in Uasin Gishu

County. The findings in Table 5 indicate that borrower's education had a positive and significant impact on borrower's loan default ($\beta_2 = 0.240, p < 0.05$): hence H_{01} is rejected and it is concluded that borrower's education has significant influence on borrower's loan default. Empirically, a percentage change in borrower's education led to a 0.240 unit increase in borrower's loan default among micro medium and small enterprises in Uasin Gishu County.

The findings are supported by empirical literature done by Wamalwa (2016) who conducted a study to identify factors influencing loan repayment among borrowers in micro-financial institutions in Nakuru County and found that education level, income level and age were significant determinants of loan repayment.

Specifically, higher education levels were associated with better repayment performance, suggesting that educated borrowers possess better financial management skills and understanding of loan obligations. Mwaniki, Makori and Irungu (2024) also investigated the effect of borrower characteristics on the repayment of individual loans provided by the Youth Enterprise Development Fund (YEDF) in Embu County. The findings indicated that borrower characteristics, including education level, had a positive effect on loan repayment. However, the study concluded that these characteristics did not have a statistically significant impact on repayment, suggesting that other factors may play a more critical role in influencing loan default rates.

Table 5: Direct hypothesis results

	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	.453	.017		26.068	.000
Predictor Variables					
Borrowers gender	.120	.021	.277	5.800	.000
Borrower's educations	.240	.028	.412	8.581	.000
Borrower's business experience	-.108	.014	-.383	-7.989	.000
Model Summary					
R	.651				
R Square	.424				
Adjusted R Square	.417				
Std. Error of estimate	.0439				

a. Dependent Variable: Borrower's loan default

Source: Field data (2024)

Hypothesis 3 (H_{03}) stated that borrower's business experience has no significant effect on borrower's loan default among Micro medium and small enterprises in Uasin Gishu County. The findings in Table 5 indicate that borrower's business experience had a negative and significant

impact on borrower's loan default ($\beta_3 = -0.108, p < 0.05$): hence H_{01} is rejected and it is concluded that borrower's business experience has significant influence on borrower's loan default. Empirically, a percentage change in borrower's business experience led to a 0.108 unit decrease in borrower's loan

default among Micro medium and small enterprises in Uasin Gishu County.

The findings are supported by empirical literature done by M'Muruku, Kingori, and Mwirigi (2023) who analyzed how socio-economic factors affect loan default rates among agribusiness borrowers in Mount Kenya Region. The research found that farming experience was significant at the 10% level, indicating that borrowers with more farming experience were less likely to default on loans. This suggests that practical experience in the agricultural sector enhances financial management and repayment capabilities. Further, the findings of the study concur with those of Njoroge (2014) who while investigating behavioral factors linked to high default rates among SME borrowers in Kenya concluded that business experience significantly affects loan repayment, with

more experienced business owners demonstrating better repayment behavior. This implies that seasoned entrepreneurs possess enhanced financial management skills, leading to lower default rates.

Testing the effect of the moderation variable

After testing the effect of the independent variables, the study further examined the effect of the moderator on the outcome variable as suggested by Baron and Kenny (1986). The results presented in table 6 confirmed that social capital had a positive and significant effect on borrower's loan default among Micro medium and small enterprises in Uasin Gishu County ($\beta = 0.239, p < 0.05$). Social capital has a positive and significant influence on borrower's loan default among Micro medium and small enterprises in Uasin Gishu County.

Table 6: Moderator Hypothesis Results

Regression results for the mediator

	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	.316	.031		10.082	.000
Predictor Variables					
Borrowers gender	.142	.020	.327	7.027	.000
Borrower's educations	.210	.027	.360	7.690	.000
Borrower's business experience	-.083	.014	-.295	-6.040	.000
Social capital	.239	.046	.262	5.156	.000
Model Summary					
R	.692				
R Square	.479				
Adjusted R Square	.470				
Std. Error of estimate	.0418				

a. Dependent Variable: Borrower's loan default

Source: Field data (2024)

According to Kimani et al. (2023), strong social networks allow entrepreneurs

to share knowledge about market opportunities, financial strategies, and best

practices. This exchange of information helps business owners make more informed decisions, thereby reducing the risk of financial mismanagement and loan default. Additionally, social networks can offer emotional support and encouragement, which are crucial for maintaining resilience in the face of business challenges.

R square is used to determine the co-efficient of determination which indicates the extent to which the model can be used to predict the changes in the dependent variable. The regression model is strong since it only explains 47.9% of the changes in loan default. It indicates that majority of the factors that affect loan default among were captured in the model as the model could only explain 47.9%.

Results of the interaction effect of social capital

(H_{04a}) social capital does not significantly moderate the relationship borrower’s gender and borrower’s loan default among Micro medium and small enterprises in Uasin Gishu County. The findings of the study revealed that interaction term of borrower’s gender and social capital had a positive and significant effect on borrower’s loan default ($\beta= 0.105, \rho<0.05$). Therefore, H04a was rejected and the study concluded that social capital moderates the relationship between borrower’s gender and borrower’s loan default among Micro medium and small enterprises. The moderating effect of social capital is further shown by the aid of a modgraph figure 1.

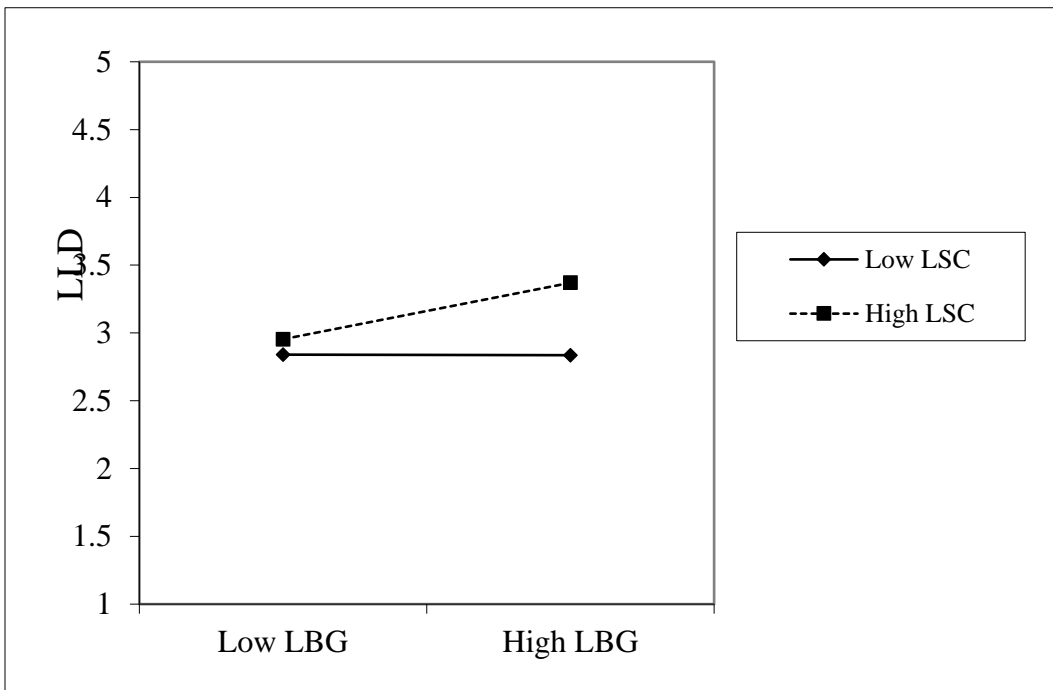


Figure 1: Modgraph for social capital on LBG and LLD

Source: Field data (2024)

The modgraph shows that borrower’s loan default is low when social capital is low and when there are more women borrowing. This means that when there are more women borrowing than men whose social

capital is low then there’s less likelihood of loan default among micro and small enterprises. Women are less likely to leverage their social networks to maintain their reputation and fulfill their financial

obligations, thus reducing the likelihood of loan default. Muia et al. (2018) explored how women small-scale traders in Nairobi's informal settlements utilize social capital. The study found that these women form groups such as "chamas" and savings and credit cooperatives (SACCOs) to access financial resources and social support. These networks serve as guarantors for loans, reducing reliance on spouses and formal financial institutions. This suggests that social capital enhances women's financial autonomy and potentially improves loan repayment behaviors. Further, Muthee and Maina (2023) investigated the influence of entrepreneurial social capital on the performance of MSMEs in Mombasa County. The study concluded that dimensions of social capital structural, relational, and cognitive positively and significantly impact MSME performance. Although the study did not focus explicitly

on gender or loan default, the findings imply that robust social networks can enhance business performance, which may correlate with improved loan repayment behaviors.

(H_{04b}) social capital does not significantly moderate the relationship borrower's education and borrower's loan default among micro medium and small enterprises in Uasin Gishu County. The findings of the study revealed that interaction term of borrower's education and social capital had a positive and significant effect on borrower's loan default ($\beta= 0.101, p<0.05$). Therefore, H_{04b} was rejected and the study concluded that social capital moderates the relationship between borrower's education and borrower's loan default among Micro medium and small enterprises. The moderating effect of social capital is further shown by the aid of a modgraph figure 2.

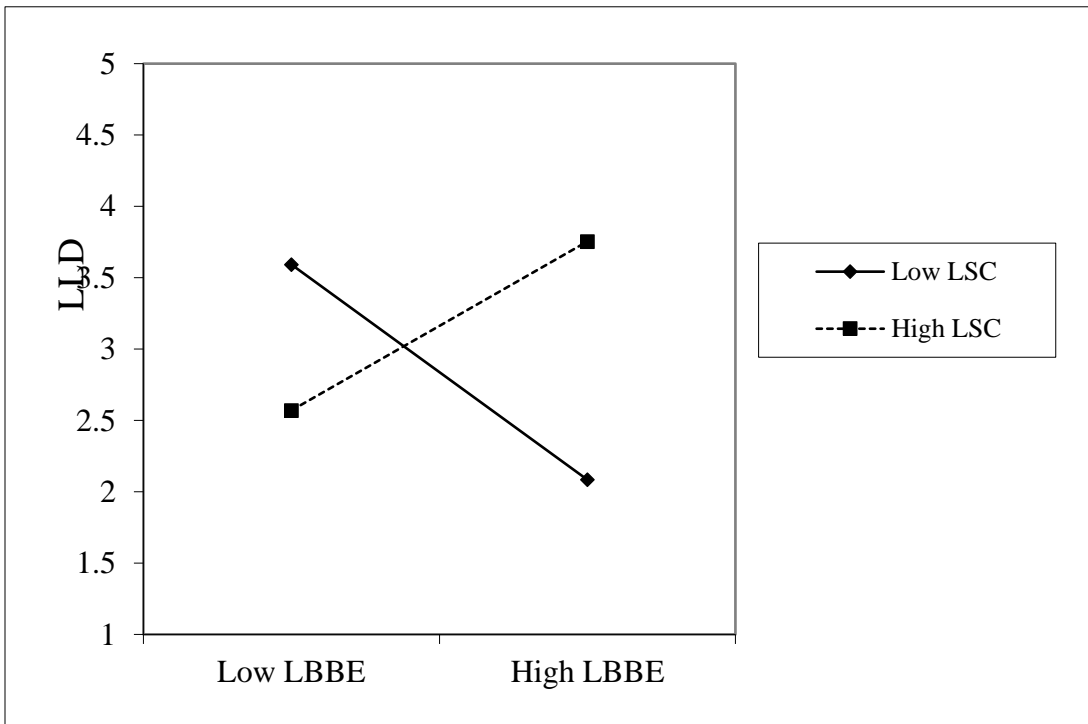


Figure 3: Modgraph for social capital on LBG and LBBE

Source: Field data (2024)

The modgraph shows that borrower's loan default is low when social capital is low and borrower's education is low. This means that when the borrower's education is low and their social capital is low then there's less likelihood of loan default among micro and small enterprises. Borrowers that are less educated and have low social capital might also be more motivated to establish a positive credit history to compensate for the lack of support networks and lack of education, making them more conscientious about fulfilling their loan obligations. These findings concur with those of Gathige (2010) who investigated the causes of loan default among off-farm borrowers in Nairobi's microfinance programs and identified both borrower-related factors (such as education level) and institutional factors as contributors to loan default. Further, Ochieng (2015) analyzed various factors influencing loan default among MSMEs in a Kenyan financial institution. The study found that variables such as net income, loan repayment period, interest rate, and repayment amount were significant predictors of default. While education level was considered, its direct impact was not found to be significant.

Conclusion

The findings of this study indicate that borrower characteristics such as gender, education and business experience play a significant role in influencing loan default rates among SMEs in Uasin Gishu County. The results show that female borrowers and those with higher levels of education tend to have higher default rates, which may be attributed to socio-economic challenges and difficulties in financial management. On the other hand, increased business experience is linked to lower default rates, pointing out the key role of entrepreneurial expertise in reducing financial risks. Additionally, social

capital was found to positively and significantly moderate loan default by facilitating access to resources and information, although it may also lead to an over-reliance on informal financial support.

Recommendations

Based on the study's findings, it is recommended that Uasin Gishu County government as well as other policymakers should implement gender-sensitive financial products, grants and mentorship programs to support women entrepreneurs, alongside awareness campaigns promoting gender diversity in business for equitable financial access. Recognizing the importance of business experience in reducing loan defaults, policies should focus on continuous professional development through subsidized training and mentorship opportunities. Comprehensive business education is essential and funding should prioritize initiatives that equip entrepreneurs with vital skills, including integrating business management courses into local curricula and providing access to online learning resources. Additionally, promoting social capital through networking events and support systems can enhance business sustainability. To proactively address loan defaults, robust monitoring and evaluation frameworks should be established to track the financial health of businesses, while ensuring access to diverse funding options and simplifying the loan application process will create a more favorable financial ecosystem for SMEs.

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