COLLATERAL SECURITY AND THE GROWTH OF SAVINGS AND CREDIT COOPERATIVE ORGANIZATIONS IN UGANDA

CASE STUDY: MORULEM SAVINGS AND CREDIT COOPERATIVE ORGANIZATION (MOSACCO)

OKULLO DENIS

REG. No. 2012-B021-10312

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Submitted By

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A DISSERTATION SUBMITTED TO THE FACULTY OF BUSINESS ADMINISTRATION AND MANAGEMENT IN PARTIAL FULFILLMENT OF THE REQUIREMENT FOR THE AWARD OF BACHELOR DEGREE OF BUSINESS ADMINISTRATION AND MANAGEMENT OF UGANDA MARTYRS UNIVERSITY

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DEDICATION

I dedicate this research work to my dear Mummy Mrs. Auma Albina through whose motherly advise and mentoring I have always achieved what I needed. I also dedicate this to FAWE-U through whose financial support I was able to accomplish this piece of work successfully, and to my Sister Aiello Josephine who also helped me financially during my time of study.

I further dedicate this to everyone who in one way or another helped me through the tough times I faced when compiling this research work.

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May the good Lord Bless you all!

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LIST OF ABBREVIATIONS

AMFIU	Association of Micro-Finance Institutions in Uganda
ASCAs	Accumulating Savings and Credit Associations
BAM	Business Administration and Management
BoU	Bank of Uganda
CCS	Cooperative Credit Scheme
CGAP	Consultative Group to Assist the Poorest
CUG	Credit Union of Ghana
DFID	Department For International Development
Findex	Financial Index
GDP	Gross Domestic Product
GFS	Global Financial Systems
GoU	Government of Uganda
MDIs	Micro-Credit Deposit taking Institutions
MOSACCO	Morulem Savings and Credit Cooperative Organization
MSC	Micro-Finance Support Center
NGOs	Non-Government Organizations

PAP	Poverty Alleviation-Action Plan
PFLS	Progressive Farmers' Loan Scheme
RDS	Rural Development Strategy
RFSs	Rural Farmers' Schemes
ROSCAs	Rotating Savings and Credit Associations
SACCOs	Savings and Credit cooperative Organizations
SMEs	Small and Medium Scale Enterprises
SPSS	Statistical Package for Social Scientists
U.S.A	United States of America
UCA	Uganda Cooperative Alliance
UCB	Uganda Commercial Bank
UCSCU	Uganda Credit and Savings Cooperative Union
VSLAs	Village Savings and Lending Associations

ABSTRACT

The study examines the role of collateral security on the performance of Savings and Credit Cooperative Organizations (SACCOs).

The dimensions of the independent variable include; Collateral eligibility, collateral valuation and collateral ownership whereas the dimensions of the dependent variable are; portfolio performance, interest income and the number of shareholders.

The objectives of the study of the study are;

i) To assess the relationship between collateral eligibility and the growth of Savings and Credit Cooperative Organizations.

ii) To find out the relationship between collateral valuation and the growth of Savings and Credit Cooperative Organizations.

iii) To assess the relationship between collateral ownership and the growth of Savings and Credit Cooperative Organizations.

The study employed a case study research design which and also adopted a quantitative approach for the study. The sample size was determined by the Krejcie and Moegan (1970) table which obtained a sample size of 76 respondents and closed ended questionnaires were used to collect data for the study.

The study findings revealed that collateral eligibility enhances secured borrowing and prevents counter party risks, collateral valuation helps to determine loan amount and quality of the loan and that collateral ownership prevents loan default and assures the SACCO about the safety of the loan.

The study concludes that there is a positive relationship between collateral security and the growth of SACCOs given that a majority of the respondents agreed that collateral eligibility prevent counter-party risks, collateral evaluation determines loan amount and collateral ownership assures the SACCO of the safety of money lent.

It can be recommended that the SACCO relax their loan pre-qualification policies to encourage more people to borrow as this will reduce incidence of reduce loan demand.

CHAPTER ONE

GENERAL INTRODUCTION

Secured lending by use of collateral security is one of the known ways by which micro-credit institutions like Savings and Credit Cooperative Organizations (SACCOs) maximize their returns alongside savings to enhance their growth.

According to (Kartik, 2003), collateral is a broadly used term to describe any asset that is used to secure borrowing from any financial institution and can take the form of property, cash, or Land which are the most likely securities. It is a form of guarantee that the cash borrowed by the counterparty would be returned back at the predefined time. In the event that the borrower fails to pay back the borrowed cash and any interest to the lender, the lender has the right to sell the collateral in order to raise the cash that was borrowed by the borrower.

Collateral refers to the borrower's pledge of his/her property to a lender to allow borrowing of a loan. The collateral serves as a security to the lender against the borrower's non-repayment of the principle and interest. If a borrower does not pay back the loan due to bankruptcy, the borrower surrenders the property given as collateral and the lender becomes the owner. Collateral is the only way a borrower's ability can be guaranteed and seems to be a monitoring tool to the borrowers, (Voordeckers, 2006) as cited in (Garreth ,1995).

1.1 Forms of collateral security accepted by micro-credit financial institutions

Usually Micro-credit institutions charge various forms of collateral, according to (Ledger wood, 1999) as cited by (Bukedeko, 2011), the institution lending the loan may require their clients to keep some balance usually stated as a portion of the loan. This portion of the loan is not to be withdrawn by their clients (Rogaly, 2004; cited by Bukedeko, 2011).

Collateral may perhaps take the form of asset security whose value is less that the market value of loan assets like land, cattle and other assets such as jewellery and sewing machines. (Rogaly, 2004 as cited in Bunkedeko, 2011) further states that in Bangladesh, after the asset is presented as security, the borrower is not allowed to use the asset anymore.

Collateral can also be in form of personal guarantee where by the person who applies for a loan should have some other person to act as security and in case he/she does not repay the principle and interest. At times, the lending institutions may consider the personal characteristics of the borrower whereby the credit officer of the institution go for appraisal to access information about the borrower prior to lending the loan, which delay the lending or quicken the lending procedure (Bunkedeko, 2011).

1.2 The basis of growth of SACCOs

The Savings and Credit Cooperative Organizations (SACCOs) system take into account a mutual membership organization involving pooling voluntary savings together from co-operators inform of shares. SACCOs are user-owned institutions with savings accumulated to act as the SACCO's wealth. The shareholders have a common bond based on a common area of interest or purpose, for example; place of origin, region, or other relationships. SACCOs mainly offer services like savings and credit but other services such as transfer of money, making payments, insurance services and member's growth are also available (Maina, 2007) as cited by (Ooko, 2011). According to (Branch, 2005), as cited in (Ooko, 2011), SACCOs have very important tasks to play on savings mobilization for the benefit of its clients. The major concern of a saving institution is to fabricate the financial force that would ensure continued service to members. Actually, the SACCOs' portfolio needs to be well managed for the achievement of the SACCOs' desired objectives.

1.3 Background of study

Savings and credit cooperative organizations (SACCOs) represent one of the most important sources of financing in developing countries and in the recent years, incredible growth has been seen in many SACCOs in many parts of the world with their performance gradually being recognized by scholars since they are also increasingly contributing an active task in the micro-credit market today (Akello, 2011).

1.4 Evolution of SACCOs in the world

Originating in Europe, the savings and credit cooperatives (SACCOs) model has been successfully transplanted to many developing countries. These cooperatives originated in Europe during the 19th century as mutual self-help organizations for people who are underprivileged. In England, the “Rochdale pioneers’’ initiated consumer cooperatives on principles (World Bank report, 2007). In the 1860’s, these first cooperatives formed the model of Agricultural cooperatives and savings and credit cooperatives enthused by the success of the consumer cooperatives’ formula in Great Britain and based on old traditions of solidarity aimed to meet the primary economics needs , which went unsatisfied.

The SACCOs helped Agricultural families to stop depending on money lenders and to find the credit necessary to modernize their Agricultural cooperatives (Mwakajumilo, 2011).

The cooperative model was first taken to the developing world when Sir Frederick Nicholson, the ‘Father of Indian cooperatives’ adapted the model to the Indian situation and many cooperatives sectors in developing countries followed (World Bank Report, 2007).

1.5 Evolution of SACCOs in Sub-Saharan Africa

In Africa, however, SACCOs were first introduced in the English speaking countries like Ghana, Nigeria, and Uganda. The idea was first introduce by John McNulty a catholic priest in Ghana in place called Jirapa in 1955.

He assisted the people to join a SACCO and assisted them to deal with their financial challenges which they could not handle individually and he trained about 60 natives who become the pioneers of SACCOs in Africa. The good performance and progress of this SACCO spread all over Ghana and by 1968, all SACCOs in Ghana merged to form the Credit Union of Ghana (CUG), which was set up to support and coordinate the activities of SACCOs in Ghana (Alila and Obado, 1990), as cited in (Mwakajumilo, 2011).

1.6 Growth of SACCOs in Uganda

According to Lubwama, 1995, as cited in Nuwagaba, 2011; the growth of SACCOs in Uganda had three main factors that led to the growth of SACCOs in Uganda which include; Campbell, the church and the government factors.

1.6.1 The Campbell Influence

Campbell planned Uganda's cooperative ordinance in 1946 with the rules and by-laws and started the formation of SACCOs. He began a departure from the general impression by the colonial government and opinion leaders that debt did not cause a serious problem. His persuasion led to the formation of the first SACCO in Uganda called 'The African Civil Servants of Thrift and Loan Society of Kampala.

1.6.2 The church Influence

The growth and swift development of SACCOs in Uganda was also by the efforts of the church, particularly the Roman Catholics who got involved in persuading their followers to actually take part in the program. The initiative was to help people institute lasting socio-economic structure and to encourage self-reliance and initiative (Kabuga and Batarinyebwa, 1995:232; as cited in Nuwagaba, 2011).

1.6.3 Government Influence

The government of Uganda promoted the growth of SACCOs when the department of cooperative development started the Agricultural scheme in 1961, in which concern was given to the introduction of the rural savings scheme. This was mainly on the rationale that credit without saving was of little importance to the members (Kabuga and Batarinyebwa, 1995:232; as cited in Nuwagaba, 2011).

The SACCOs in Uganda further took shift and more force in 2006 when the government initiated the 'Prosperity for all' program ('Bonabagagawale') which helped to institute at least one SACCO per Sub-county (AMFIU, 2010).

However, the researcher therefore attempts to investigate the relationship between collateral security and the growth of SACCOs in Uganda, by studying the relationship between collateral eligibility and the growth of SACCOs, collateral valuations and the growth of SACCOs, and the ownership of collateral and the growth of SACCOs.

1.7 Problem statement

Recently in 2006 under the program “prosperity for all” (Bonabagagawale), the government of Uganda initiated an idea of instituting a SACCO at every sub-county to support rural micro-credit groups in order to encourage savings, investment, and development (AMFIU, 2010), as cited in (Karuma, 2011).

In Kabarole district, poor management of SACCOs, embezzlement of SACCO funds, non-involvement of members in the decision making process and poor loan repayment rate by some members is pushing some members out of the SACCO groups which have led to a rapid decline in performance of SACCOs (Kajubu E. Uganda Radio Network, 8th February 2013) on-line.

Though the government has tried these initiatives, it is still reported that about 70% of rural SACCOs are at their formation or basic stage and about 30% are at their advanced stage (Kato, the New vision, 5th April 2011) on-line.

This therefore poses a question whether the use of collateral security to acquire loans has played a role in the growth of SACCOs in Uganda.

1.8 Broad objective

To examine the relationship between the role of collateral security and the growth of Savings and Credit Cooperative Organizations (SACCOs).

1.9 Specific objectives

1.9.1 To assess the relationship between collateral eligibility and the growth of Savings and Credit Cooperative Organizations.

1.9.2 To find out the relationship between collateral valuation and the growth of Savings and Credit Cooperative Organizations.

1.9.3 To assess the relationship between collateral ownership and the growth of Savings and Credit Cooperative Organizations.

1.10 Research questions

1.10.1 What is the relationship between collateral eligibility and the growth of Savings and Credit Cooperative Organizations?

1.10.2 What is the relationship between collateral valuation and the growth of Savings and Credit Cooperative Organizations?

1.10.3 What is the relationship between collateral ownership and the growth of Savings and Credit Cooperative Organizations?

1.11 Research Hypothesis

There is a relationship between Collateral Security and the growth of SACCOs in Uganda.

1.12 Significance of the study

The research information will be helpful to policy makers especially at Abim district Local Government council, Morulem Sub-county as well as the ministry of finance who could use it to promote policies and by-laws that will enable Morulem Savings and Credit Cooperative Organization (MOSACCO) and other SACCOs to benefit from it as much as possible.

The study will act as a reference point for future scholars, practitioners, MOASCCO, stakeholders and the entire field of academic research and other researchers.

The findings from the study will help the researcher build more knowledge on SACCOs' growth, help the researcher find tentative solutions to problems that hinder the growth of SACCOs and as well help him attain a Bachelor degree of Business Administration and Management.

1.13 Justification of study

Many SACCOs lend to their clients on the basis of collateral security as platform for acquiring loans and has experienced no significant growth. However, there is limited or no access to information to explain such growth, coupled with illiteracy and low levels of education which makes most people have low self-esteem that leads them to fear joining or borrowing from SACCOs and opt to use informal groups (Kamuhanda, 2010).

The study therefore was intended to establish and develop a baseline data that would be used by scholars, management of MOSACCO and other Micro-credit institutions in Abim district to ascertain the role of collateral security on the growth of (SACCOs).

1.14 Scope of study

1.14.1 Geographical Scope

The study will be conducted in Morulem Sub-county, Abim district, Karamoja sub-region in North-Eastern Uganda 411.3 Kms away from Kampala.

1.14.2 Content Scope

The study will assess the relationship between collateral security and the growth of Savings and credit Cooperative Organization (SACCOs) at Morulem savings and Credit Cooperative Organization (MOSSACO) using the dimensions of collateral security such as; collateral eligibility, collateral valuation, and collateral ownership. However, there are other moderating variables in the conceptual frame work that will not be studied in this research.

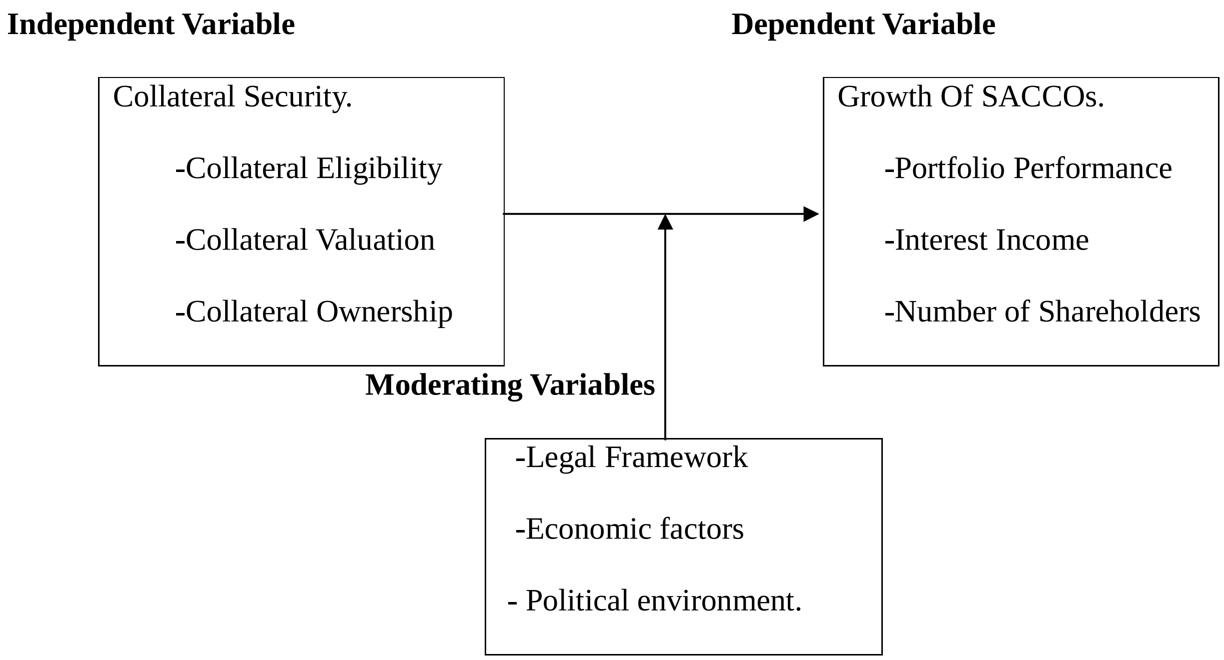
1.14.3 Time Scope

The essence of the study was to examine the role of collateral security on the growth of Savings and credit Cooperative Organizations (SACCOs) from the period 1990 to 2014.

1.15 Conceptual frame work

According to the literature reviewed, it is conceptualized that a change in collateral security variable like Collateral eligibility results into a change in the SACCOs growth like, change in portfolio performance. In general, a change in the independent variable will cause a resultant change in the dependent variables either positively or negatively (Inwon, 2002 and Luyirika, 2010).

Figure 1 conceptual framework



Source: *Developed from review of literature (Roslyn, 2007; Inwon, 2002; Luyirika, 2010).*

From the above conceptual framework, the study proposes that the growth of savings and Credit Cooperative Organizations (SACCOs) is determined by Collateral Eligibility, Collateral Valuation, and Collateral ownership. However, there are other variables which cannot be controlled by the SACCOs, but can also, in a way, determine their growth. They are the moderating variables which for this study include; the legal framework, Economic factors, and Political environment.

1.16 Definition of Operational terms

Collateral security

Collateral refers to any security or property pledged by a borrower to secure accessing a loan. If the borrower defaults paying back the loan, the lender may become the owner of the pledged collateral or property.

Collateral eligibility

Collateral eligibility refers to a condition that a given security pledged as collateral must meet before it is accepted by a lender as collateral as may be specified by the general framework or temporary framework of a particular financial institution European central bank.

Collateral valuation

This is the process of establishing the fair price of an asset that is being used as collateral through appraisal and evaluation by an expert to avoid loss incurred by counter-party and its value usually exceeds the loan value federal reserve bank.

Collateral ownership

This the legal right the borrower has over the asset or property pledged in order to secure loan form a given financial institution. This legal right can be transferred to the lender in case the borrower fails to repay the loan.

Savings and Credit Cooperative Organization (SACCO)

Savings and Credit cooperative Organizations (SACCOs) refer to institutions formed to provide financial support to the members; the institution accepts deposits from members and grants them loans at reasonable interest rates. Examples are Village Service Co-operatives and Urban Cooperative Banks.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This section discusses the literature presented by previous scholars related to collateral security and the growth of Savings and Credit Co-operative Organizations (SACCOs). It particularly focuses on literature on the dimensions of collateral security namely; Collateral Eligibility, Collateral Valuation, and Collateral ownership and their relationship with the growth of SACCOs.

2.1 Growth and performance of SACCOs in Uganda

Savings and Credit Cooperative Organizations (SACCOs) are voluntary and socially motivated financial institutions that provide loans to the underprivileged people who have no or less access to financial assistance from commercial financial institutions (Morduch and Haley, 2002) as cited in (Ssebaale, 2008). SACCOs' performance and development is looked in terms of wellbeing of the poor, financial sustainability and the number of clients of the SACCO (Donaghue, 2004) as cited in (Ssebaale, 2008).

SACOOs belong to and are managed by people who have a common bond who may be working together, same religion, or social group. SACCOs are legally registered registered under the Uganda Cooperative Statute of 1991 and Cooperative Societies Regulation of 1992. SACCO members always agree on how to use their money for the benefit of each member. Membership is open to any willing to join the group regardless of sex, gender, race religion, colour, or job status of a person and the minimum number of members to register a SACCO under the current law is 30 people, but for purposes of accessing external support, a minimum number of 300 people is probably better for selection. SACCO members always save their money together and lend to any member in need at convincingly lower rates of interest and the interests are mainly charged in order to cover the cost on savings and administration if necessary (UCSCU, 2014).

Cooperative Movements in Uganda began in 1913 when the first farmers' Association was formed by the African farmers. The motivation to form this Association was brought by a common voice, purpose and strong bargaining power against an economic system that did not meet their needs, which was seen to operate along racial lines, that is, the African farmers at the time. To enhance the formation of the cooperatives, the British Colonial Government endorsed a cooperative verdict which provided the legal framework for the operation of a number of farmers' associations that were formed in the 1920s and 1930s. This further stimulated the Uganda government to endorse the cooperative Act of 1962 after independence, focusing on the decree (Kyazze, 2010) and this was revised in 1991 to become the Cooperative Societies Act (GoU, 1991). Despite the rapid development of SACCOs in recent years, a very small portion of them have attained operational self sufficiency and their outreach remains very negligible compared to the potential demand by their members (AMFIU, 2009).

Uganda Cooperative Alliance (UCA) later established SACCOs to respond to government's call to provide affordable financial services to the economically poor people of the rural Uganda (UCA, 2004). Remarkable progress was made because the SACCO model was adopted and used effectively by the rural population who needed micro-finance services and several benefits were attained (UCA, 2005) as cited in (Mpiira et al, 2013).

The business replica of most SACCOs in Uganda is to mobilize saving deposits from its members and to intermediate them into loans which has enabled the poor and rural people to save and borrow loans as well. SACCO services are restricted to be used by members only because the law governing their operations in Uganda does not allow them to accept savings or give loans to the public. In order to encourage the formation of new SACCOs, the government has subsidized the formation of new SACCOs all over the country by giving them start-up capital from the government owned apex institution Micro-Finance Support Center (MSC) which also lends free interest loans to SACCOs or other forms of subsidized loans. The government further gives operational maintenance to the SACCOs in addition to grants and loans for example, paying salaries and rent for the first two years of operation (State House, 2007) as cited in (Markus and Schmidt, 2011).

The distinction of SACCOs from other financial institutions is that SACCOs are not regulated by the Bank of Uganda (BoU). Only Commercial banks and credit institutions are regulated through the Financial Institutions Act, whereas the Micro-credit Deposit taking Institutions (MDIs) are regulated through the MDI Act. SACCOs are instead regulated through the Cooperative Societies Act, although this Act is not sufficient for other financial institutions, hence, SACCOs are the only institutions that are mobilizing savings that are not regulated prudentially by the BoU (AMFIU, 2005).

2.2 The concept of Micro-finance/Micro-credit

The concepts Micro-Finance and Micro-Credit are closely correlated and some scholars tend to use them interchangeably, though they have different meanings. According to (Sandra, 2001) as cited in (Mugabi, 2010), Microfinance refers to providing of a wide variety of financial services to underprivileged households and micro-enterprises like voluntary savings, loans, insurance and money transfer. Micro-credit is however the provision of credit services to low income clients in form of small loans for the purpose of micro-enterprises and income earning activities. A micro-loan is a financial novelty which originated in low developed countries where it has successfully enabled extremely impoverished people start self-employment businesses that enables the poor and voiceless to earn income, build wealth and get rid of poverty. Micro-credit was initiated in Bangladesh during the famine of 1974, when Professor Yunus studied the behavior of 13 entrepreneurs in Bangladesh. Yunus started by lending to groups of women an amount of $30 to 42 basket weavers to aid them acquire bamboo. Upon the advice of financial institutions and government, he constantly gave out micro-loans and in 1983 started the Grameen Bank. The program confirmed that small loans could not only quickly improve lives of poor people, but were paid back with interest and on time, (Mugabi, 2010).

The diverse literatures obtainable on microfinance are unable to find a universally established definition. However, microfinance to many people refers to availing financial services to people who do not have access to prescribed financial organizations because of lack of wealth and societal difficulties. On the other hand, Yunus explained microfinance as the lending of small loans to the people who are unable to access conventional bank loans. So, it proved to be a practical and satisfactory determinant in the long-lasting endeavors against poverty.

The Association of Microfinance Institutions in Uganda (AMFIU) asserts that microfinance is a form of banking service that is given to underprivileged individuals or groups who would otherwise have no other ways of gaining financial services from formal financial institutions (Understanding the microfinance industry in Uganda, 2008:3), as cited in (Luyirika, 2010).

According to previous literature, the researcher therefore used the term ‘microfinance’ to mean small loans that are provided to the low income and or poor people mostly in the rural and sub-urban settings of developing countries.

Micro lending or micro-loan is the provision of finances to the poor through activities leading to generation of income to the borrowers, frequently attached with additional financial services including savings and insurance. Its focus is to lend without any condition of collateral. The difference between micro-credit and microfinance is that micro-credit deals with clients loan and credit needs and microfinance deals with financial services generating a broad range of success opportunities, (Umara et al, 2001).

The so called ‘new world’ of micro-finance is not the first endeavor to formalize the qualities of traditional methods of intermediation with a social rather than a business motive. Friedrich Raiffeisen started the first formal cooperative savings and credit organizations and these early and genuine cooperative banking institutions grew up as smaller local groups came together to pool their funds and their capability, and assist intermediation between savers and borrowers beyond the local community. Cooperatives and Credit unions have in some places continued both to grow and serve the poor, and in many countries, and districts, they are the most important and successful financial institutions. Elsewhere however, and particularly in the poorer countries, cooperatives have been ‘hijacked’ by the less poor, the land owners, and by allied political interest.

Government first became involved because of the need to protect the poor people from corrupt or unskilled promoters, except that this very poor concern has often been corrupted by politicians’ desire to protect and promote their own interest, (Harper, 2001).

The concept of microfinance began gaining importance in the 1980s. These programs were introduced in various developing economies during the past ten years. Well-known examples include a bank in Bangladesh by the name of Grameen Bank, Banco Sol in Bolivia and an Indonesian bank, Bank Rakyat.

Recently, policy makers and scholars paid a lot of concentration to the theory of microfinance. It is considered as a successful approach for development and has a considerable policy proposition concerning reduction. The idea of giving loan to the poor was believed to be unreasonable. However, financial services were required by a lot of underprivileged households as they were concerned with savings maximization, decreased risk and to have a shelter due to doubtful situations often motivated by financial crisis, sickness and tragedies. Their investment was in business run at smaller scale, children education services, health facilities, purchased assets and improved their living standard. The appropriate financial intermediaries like commercial banks usually were less beneficial for these households because at the first place, their business models were commonly inappropriate for a micro-finance business. Secondly, conventional lending is offered by them based on collateral requirement and high appraisal and monitoring costs. Moreover, it is unfairly believed that the households are unwilling or unable of paying back the loans. Unavailability of credit was one of the main reasons for the people to remain poor in developing countries. The financial services have been used as a development tool since the last 25 years. Such services have several forms such as microfinance organizations lending to mainly female micro-entrepreneurs, rural credit schemes providing to subsidize loans to poor farmers and a number of organizations offering a range of monetary services like offering loans, savings and facilities of insurance, in order to help the poor, maximize their earnings as well as decreasing exposure to variations in income (Umara et al, 2011).

Amazingly more than 3,000,000,000 poor people hunt for access to basic financial services worldwide (Helms, 2006, ix) as cited in (Guntz, 2011), and were ignored by commercial banks for a very long time. For commercial banks the poor were regarded as “unbankable” for decades because they cannot present collateral. It is also predictable that about 90% of the people in developing countries have no access to institutional financial services (Robinson, 2001; 9) as cited in (Guntz 2011). Microfinance gives financial services to those who are not served by the traditional financial sector. Therefore it was one of the most important tools to help solve this problem and bridge the gap for the poor, even if it is not a magic solution that cures all poverty among the poor (Guntz, 2011).

2.3 Classification of financial institutions in Uganda

Microfinance institutions in Uganda consist of; money lenders, microfinance agencies, Non Government Organizations (NGOs), Rural Farmers’ Schemes (RFSs) and Small and Medium-scale Enterprises (SMEs). These lent to individuals or groups who have found difficulty in accessing loans from formal financial institutions. They provide a range of activities which comprise; deposit taking, saving schemes, small scale entrepreneurship, giving advice on entrepreneurship, agriculture, real estate, group lending, retail financial services, giving advice on financial matters and training in business management. According to the Financial Institutions Act 2004, microfinance institutions in Uganda are categorized according to their respective levels of development (Bunkeddeko, 2011).

i. Formal banks regulated by the Central Bank – Tier 1-3

This constitutes financial institutions that are directly supervised and regulated by the Central Bank of Uganda (BoU) and they include: commercial banks, credit institutions and Microfinance Deposit taking Institutions (MDIs) (Fin Scope Uganda, 2013).

ii. Non-bank formal financial institutions

These include Savings and Credit Cooperative Organizations (SACCOs) and other microfinance institutions (MFIs), insurance companies and the non-banking financial institutions like foreign exchange bureau, money transfer services like Western Union, and cell phone money services (Fin Scope Uganda, 2013).

iii. Informal financial institutions

These encompass among others money lenders, Rotating Savings and Credit Associations (ROSCAs), Accumulating Savings and Credit Associations (ASCAs), Village Savings and Lending Associations (VSLAs), Non-governmental Organizations (NGOs), Investment Clubs, Saving Clubs, services by employers and other village groups like burial societies and welfare funds (Fin Scope Uganda, 2013).

iv. Financially excluded institutions/persons

These comprise of people who do not use either the formal banks, non-bank formal or informal institutions. Products and services under financially excluded groups include saving in secret places, friends' shops, borrowing from friends or relatives, or transfer of money through individuals (Fin Scope Uganda, 2013).

2.4 Credit Schemes provided by Micro-finance institutions (SACCOs)

There are two major types of credit schemes which are universally used by Micro-finance institutions and other money lenders when advancing loans and/or lending money to their clients.

2.4.1 Secured credit

Money is lent against the value of an asset the borrower owns which acts as security against the money borrowed. If the borrower defaults payments, the lender takes legal action to sell off the collateral pledged in order to recover back the money lent. As lenders know that they will recover the money lent in one way or another with a secured loan, they often charge less interest. A mortgage is one of the major used forms of secured credit, although specialist brokers will advance money against a broad range of valuables, from stocks and shares to antiques and art.
Other examples of secured credit that money lenders and financial institutions consider may include among others the following;

i). Pawnbroker loans, where the item is stored by the pawnbroker and will only be returned when the loan and interest are paid back in full within an agreed period. If the loan and interest are not paid back, the item is forfeited and sold by the pawnbroker to recover the lent money.

ii). Pension loans, where a loan is made against future pension income. This can either be used by government or private sector employers to give financial support to their employees and in future deduct from their pension income to recompense the loan and interest.

iii). Endowment loans; this is where the loan is made against an endowment guiding principle with a guaranteed value.

2.4.2 Unsecured credit

This is a situation in which the financial institution lends money to the borrower without any security placed against the money lent. It is risky for lenders because they do not have any security that could be taken and sold in case the borrower defaults payment of the money lent.

As an alternative, the lender estimates the amount that the borrower can unfailingly repay after a given agreed period. Lenders generally charge higher rates of interest for unsecured credit compared to secured credit because they probably can lose money if anything goes wrong and the borrower cannot pay back what they owe. For example loans to loans are a noticeable exception, since they attract comparatively small interest charges and can be paid back over several years (Better Money Skills) On-line.

2.5 The concept of Savings in Uganda

According to (Ledgerwood, 2000), savings mobilization has long been a contentious issue in Micro-finance. In recent years, policy makers and practitioners have been raising awareness that there are immense numbers of informal savings schemes and MFIs around the world, particularly, credit union organizations have been very successful in mobilizing savings from their clients. The developments confirm the fact that low income clients can and do save. The World Bank’s worldwide inventory of micro-finance Institutions established that many of the largest, most sustainable institutions in micro-finance depend heavily on savings mobilization.

The government of Uganda through the Cooperatives inspectorate has started programs to promote saving especially among the rural people. Uganda’s rural poor are interested in savings even with the country’s low formal savings rate. Most of them make at least some attempt to set aside money, often hiding it in mattresses or burying it in the garden.

The public awareness drive has shown that the rural populace can be motivated to move their savings into the formal sector. Saving is the best technique for meeting daily requirements and achieving future goals. The recent DFID study designated that many rural Ugandans are accessing and borrowing, mainly from informal sources, domestic consumption, school requirements and other emergencies. Saving is nonetheless a far more cost-effective way to finance these daily needs of the rural people in Uganda (Nuwagaba, 2012).

Further, a survey of 2012 reveals that Uganda's savings to Gross Domestic Product (GDP) ratio of about 11.8% is one of the lowest in Sub-Saharan Africa and its continuing to decline in the latest few years. Hindrances to organized savings are among others, high interest rates, high minimum deposits and long distance from banking institutions. According to the World Bank Financial Inclusion index (Findex, 2011), maintaining a checking account in Uganda costs the comparable amount of 25% of GDP per capita annually, and about 54% of non-account holders cite cost as a cause for not having an account. These costs are still high and there is a range for lowering them (Kasekende, 2013).

2.6 Types of Savings

Savings mobilization should be backed by sufficient institutional capital which guarantees permanency, provide cushion to absorb losses and impairment of members' savings (Evans, 2001) as cited in Olando et al (2012). The institutional capital, which comprises the core investment and less share capital, is mainly collected from appropriation of the surpluses. This therefore means that SACCOs should endeavor to maximize on the earnings to build the institutional capital (Branch & Cifunentes, 2001; Ombado, 2010) as cited in Olando et al (2012).

This institutional capital guarantees the permanence and development of the SACCOs even in unstable economic periods (Evans, 2001). To back up the above statements, Gijselinckx & Devetere assert that savings in fact help the SACCOs to grow and remain economically and financially feasible, (Gijselinckx & Devetere, 2007) as cited in **(**Olando et al. 2012).

Micro-finance institutions have been tasked to mainly lend to the financially excluded people in the past, while savings have been neglected but in the recent years, this has been under looked promoted mainly by a micro-finance calamity which took place in India and other low income countries (CGAP, 2010a) as cited in (Markus and Schmidt, 2011). Many scholars therefore argue that it would be good if the poor save first and later invest the money (CGAP, 2010b) as cited in (Markus and Schmidt, 2011). This calls for safe and reliable saving opportunities to be the central significant objective for the poor and the MFIs. In Uganda, SACCOs act as financial intermediaries which channel savings into loans, while providing saving opportunities to mainly the poor in the rural areas. Nevertheless, further improvements are needed to make their services more resourceful and sustainable. Research shows that poor people have always looked for opportunities to save their surplus income in case of emergencies despite the fact that this has been on a minimal scale or to open up larger investments in the future without going for loans (CGAP, 2006) as cited in (Markus and Schmidt, 2011). This affirms that there is a high potential to mobilize savings among the poor in Uganda.

(Ledgerwood, 2000) asserts that, savings schemes are majorly of two kinds which most financial institutions use and also applies to Uganda's financial institutions.

i). Compulsory Savings

Compulsory savings are funds that must be collected by borrowers as a condition of receiving a loan, sometimes as a proportion of the loan, or as a nominal amount. Compulsory savings can be considered to form a higher proportion of a loan product rather than an actual savings product, since they are so closely tied to receiving and paying loans. However, compulsory savings are alleged by borrowers as a "fee" they must pay to partake and gain access to credit.

Normally, compulsory savings cannot be withdrawn by members while they have unpaid loans. In this way therefore, savings act as collateral. Clients are thus not being able to use their savings until they pay back the loan. In some instances, compulsory savings cannot be withdrawn until the borrower actually ceases membership from the MFI. These sometimes make clients borrow loan amounts that are in fact less than their accumulated savings. However, many MFIs are now beginning to recognize the weaknesses of this practice and are allowing their clients/members to withdraw their compulsory savings if they do not have a loan outstanding or if a certain amount is still held by the institution (Ledgerwood, 2000).

ii). Voluntary Savings

Voluntary savings are not mandatory for accessing loans and credit services. Voluntary savings are provided to borrowers and non borrowers who can deposit or withdraw according to their needs. Interest rates paid range from comparatively low to a little higher than those offered by formal financial institutions. The prerequisite of compulsory savings and the mobilization of voluntary savings reflect two very different viewpoints (CGAP, 1997) as cited in Ledgerwood (2000). The former presupposes that the poor must be trained to save and that they need to discover financial discipline and the latter emphasizes that the working poor already save and that what is required are institutions and services suitable to their needs. Micro-finance clients may not feel contented putting voluntary savings in compulsory savings accounts or even other accounts in the same MFI. For the reason that often they cannot withdraw their compulsory savings until their loan is repaid, they fear that they may also not have easy access to their voluntary savings. As a result, MFIs should always clearly differentiate between compulsory and voluntary savings services (Ledgerwood, 2000).

2.7 Access to Credit Finance in Uganda

The financial sector in Uganda is highly dualistic as it is in other African states and other developing countries, consisting of both formal and informal financial institutions, with the later controlling a big percentage of the market in rural areas. With the emerging micro-finance and other rural financial institutions, a new sector, the semiformal financial sector, is rapidly developing in Uganda. Evidence from previous scholars on the relative importance of formal and informal financial sectors confirms that the latter plays a very fundamental role in the provision of financial services to the rural poor. In terms of coverage and amounts received, rural smallholder farmers and traders rely on informal financial institutions as their major source of credit, (Mpuga, 2004).

Among the main distinctiveness of rural financial markets in the developing countries are informational limitations and therefore limited access to institutional or formal credit, segmentation, lack of specialization and inter-linkage, for example the village money lender may at the same time do other businesses, interest rate changes, rationing, exceptionality, and a high degree of absorption of the loan portfolios of informal financial institutions (Ray, 1998) as cited in (Mpuga, 2004).

The result of this is that only a small fraction of the total number of rural households and firms receive credit from the formal sector. Again among those with access to the institutional credit, a very small group, predominantly the rich and the elites in the village receive a very large share of the total amount distributed.

Credit programs in Uganda can be traced to the early 1960s when two credit schemes that is, the Cooperatives Credit Scheme (CCS) in 1961 and the Progressive Farmers' Loan Scheme (PFLS) in 1964 respectively were formed, with a focus of changing farmers from subsistence to commercial practitioners and as an approach to reduce poverty. Another state directed credit programme, the Rural Farmer's Scheme (RFS) was initiated under the support of the Uganda Commercial Bank (UCB) in April 1988 also with similar objectives as the two credit programs mentioned above. All the above three credit programs botched and were suspended due to high default rates and their failure was accredited to outcomes such as inaccurate mechanisms used to choose credit beneficiaries, cumbersome evaluation procedures which resulted in delayed disbursement, lack of sufficient staff to monitor the credit given, and the nonexistence of readily available market for farmers' produce. Other reasons for the collapse of these credit programs included; bureaucracies, questionable integrity of loan officers, poor disbursement policies, high transaction costs, lack of collateral security for the loans and political interference (Muhumuza, 2007) as cited in (Karuma, (2011).

Furthermore in the last 20 years, the government of Uganda has started, executed and supported various micro credit plans aimed at fighting poverty in the country with a focus of creating rotating funds for Micro-credit institutions (SACCOs) to households at the grass roots. Such initiatives include the South-western Smallholder's Rehabilitation Project, ECS and Poverty Alleviation Action Plan (PAP). However, some of these efforts have had modest success and inadequate impact on addressing the needs of the targeted people due to design flaws, and management insufficiencies, (Micro-finance Support Centre Limited Report, 2007). Out of the above mentioned government directed credit programs, only PAP registered some success like a recovery rate of 93%, training of intermediary agencies and clients in group dynamics, enterprise management and book keeping, generating material and social benefits for its beneficiaries, increased co-operation between group members, enrichment of beneficiaries' interests and formation of social networks. The PFA programme, which was designed to be achieved through the Rural Development Strategy (RDS) emphasized the need to enhance production, competitiveness and commercialization of the economy .This was to be achieved through increased production and productivity, promoting value addition and marketing, improved access to information and increased access to reasonable financial services (Microfinance support centre limited report, 2007) as cited in (Karuma 2011). In the implementation of PFA, the Government of Uganda (GoU) developed a plan for RFSP aimed at developing a financial infrastructure that was to reach every sub- county in Uganda. The infrastructure was a channel for encouraging savings mobilization throughout the country.

Uganda's Vision 2040 states the lack of access to finance as one of the obstacles affecting the competitiveness of the economy. There is inadequate access to credit and most individuals and firms access credit from informal sources mostly. One of the reasons for the limited access to credit is the low level of incomes and accordingly domestic savings which affect the capacity of institutions to offer long term finance. As such, the government plans to increase gross national savings from the level of 14.5% (2013 estimate) to about 35% of GDP by 2040, as a means to hasten structural transformation (Fin scope Uganda, 2013).

The financial access statistics (2013 estimates) reports that only 38% of Ugandans received financial services from both formal and informal sectors and of this, only 20% used formal sector financial institutions that is, commercial banks (Tier 1), credit institutions (Tier 2), and microfinance Deposit Taking Institutions (MDIs) (Tier 3). This therefore explains that nationwide, 62% of Ugandans were not served by any financial institution or groups whether formal, semiformal or informal. Further, the inequality between urban and rural access to financial services was so wide with urban access at 48% compared to rural access at 35%.

This would imply that more than 12,000,000 adult Ugandans in rural areas did not have access to financial services. However, the number of adults having saving accounts with SACCOs increased by about five times that is, from 128,000 in 2009 to 622,000 by 2013. Geographically, the share of adults operating an account varied from 9% in Northern region to 42% among adult residents in Kampala. So, definitely there is a lot of work to be done if the financial sector is to reach the more than 12,000,000 rural adult populations. However in overall, there has been a significant improvement in financial access in Uganda from 70 % in 2009 to 85% in 2013. The number of the adult population accessing formal institutions increased by almost two times from 28% in 2009 to 54% in 2013, which growth was motivated by the increase in the non-bank formal sector from 20% in 2009 to 52% in 2013. Partly due to the presence of SACCOs, the rural population is more likely to access credit finance through non-bank formal institutions compared to their counterparts in urban areas. Western region leads in terms of access to credit from non-bank formal financial institutions with 7% of the people accessing credit from this particular source compared to 5% for Central region and only 2% for Northern region (Kasekende, 2013).

2.8 Loan Collateral

Collateral is a term used to describe any asset that is used to secure borrowing from any financial institution and can take the form of property, cash, or Land. It is a form of assurance that the money borrowed would be returned back at the predefined time. In the event that the borrower defaults payment back, the lender has the right to sell off the collateral in order to raise the money that was borrowed, (Kartik, 2003).

Generally, MFIs and SACCOs lend to low income borrowers who often have very few assets to be pledged as collateral. Consequently, traditional collateral such as property, land, machinery, and other capital assets is time and again not available. Various innovative means of reducing the risk of loan loss have been developed including collateral substitutes and alternative collateral.

Generally Micro-credit institutions charge a variety of collateral (Ledger wood, 1999) as cited in (Bunkedeko 2011), MFIs may necessitate their clients to hold a balance usually stated as a proportion of eth loan. These proportions are not available for withdrawal by their clients as (Rogaly, 2004) notes, cited in (Bunkedeko, 2011). Collateral may also be in the form of assets pledged at less than the real market value of loan assets like land, cattle and other physical assets. (Rogaly, 2004) states that similar to the practice in Bangladesh, a borrower after pledging the assets might be limited from using the assets pledged.

Collateral may also be in form of personal security, usually a person, the underwriter is required by the lending institutions to act as security incase the borrower defaults payment of the loan.

At times a loan demanded may depend on the personality of the borrower, here preceding advancing the loan, the credit officer visits the client and finds out information about the client’s personality and this could be the reason why lenders usually give loans quickly to borrowers from large institutions because of the wide information available about their character (Bunkedeko, 2011).

2.9 Collateral Eligibility and the growth of SACCOs

European Central Bank report (Euro system) (2013) states that assets to be eligible as collateral for financial institution's operation need to accomplish certain criteria and requirements to guarantee sufficient quality, and protect the financial institution from counter-party credit risk.

The capacity to pool eligible collateral assets to raise secured borrowing and lending can be viewed as a liquidity buffer to be used in times of financial market stress. This provides the motivation for the micro-credit financial institutions to issue unsecured debt in normal times.

In times of financial strain when risk appetite falls sharply due to increased counter-party risk, adjustments in the use eligible collateral for secured and unsecured lending becomes more costly or even unavailable owing to lending uncertainty about the true level of risk. Similarly access to secured lenders can be negatively affected if collaterized instruments have difficult structures that call for standard criteria for evaluating the eligibility of the collateral in question. These dynamics were observed during the sub-prime mortgage crisis in the United States of America (U.S.A), resulting in to the disintegration of large parts of the lending market (Banks for International Settlement, 2013).

However, one important question is also whether loans with eligible collateral are riskier or not than those without. The assumption forecasts that riskier borrowers are more likely to pledge collateral when the quality of the borrower is observable for the lender and there is moral hazard (Berger and Udell, (1990), and (Boot, Thakor and Udell, 1991), as cited in (Yaron, 2008).

On the other hand, if the quality of the borrower is not evident, then the lender will use the collateral eligibility to self-select the borrowers according to their perceived risk and, in the balancing solution, high quality borrowers will prefer loans with high eligible collateral and lower interest rates (Bester, 1985; Basenko and Thakor, 1987 and Berger and Udell, 1990) as quoted in Yaron, 2008). To find out which of the effects win through, preceding work has regressed the risk of premium in the interest rate of the loan on the presence of eligible collateral in the same loan (Berger and Udell, 1990), and (Degryse and Caryseel, 2000), the interest rate and the same use of collateral are mutually determined so therefore, the two are endogenous variables in the growth of micro-credit financial institutions.

(Chailloux, Gray and McCoughrin, 2008), stated that the collateral eligibility criteria for micro-credit institutions (SACCOs) loans should include loans that protect the SACCOs from losses, while still providing on collective basis a significant expansion of collateral availability.

Too stringent criteria would deny the counter-party of the benefit of accessing additional liquidity while too loosely defined collateral eligibility criteria may shift excessive risks to the micro-credit institution (SACCOs).

On the other hand, (Roslyn 2007), as cited in (Ooko, 2011), conducted a study which found the facts that encouraged the repayment of loans in SACCOs were the nature of collateral, control recovery measures and the type of loans that the SACCO society has in place to check on defaulters. The study recommended that there was need for SACCOs to implement sound collateral eligibility management and loan recovery measures to improve the growth of SACCOs. Roslyn's study showed that the growth of SACCOs' wealth was linked to the control of loan default by use of sound collateral eligibility criteria. This did not explain how growth of SACCOs' wealth would be achieved.

2.10 Collateral Valuation and the growth of SACCOs

Once the bank has established the eligibility of the collateral offered and set the relevant haircut, it continues to examine the value of the collateral throughout the life of the transaction on a daily basis. The financial institution will re-value all the collateral it is holding using the latest available source.

Where prices are not available, the financial institution will use model based techniques including using discounted cash flow valuation for fixed income collateral security and historical performance data for asset backed collateral security, (Garreth, 1995).

In addition, determining a suitable collateral value is a common problem when provisioning for losses on impaired loans. If the collateral is assigned too high a value, the provision will be inadequate. However, although collateral is ideally marketable, banks and other financial institutions and to some extent, supervisors may undervalue or even ignore the obstacles caused by weak legal systems and cultural factors in the effective of sale of the collateral (Alain and Majnoni, 2002).

Countries take varying techniques to the management of collateral and other guarantees in the classification process. Several influences for instance, from Czech Republic, France, Spain, and West African Monetary Union do not take collateral and guarantees into account for classification purposes. As a result, classifications reflect the quality of loans irrespective of the purpose for recovery derived from collateral. Far more, countries clearly factor in the value of collateral, in a variety of ways, when classifying loans. The focus looks to be on establishing the amount of recovery. In Australia, loans with interest or principal 90 days past due must be recorded as non-accrual if the market value of the collateral is not enough to cover payment of principal and accrued interest. When the market value is adequate, the loan is classified as past due.

In Mexico, the initial credit rating must be higher than that of the debtor and in Singapore, the secured percentage of a non-performing loan is considered substandard, while the unsecured percentage is graded as doubtful or loss, while in China, the declining value of collateral and the deterioration of the guarantor's financial condition is a trigger point that results in normal loans being downgraded, and different portions of a loan with an eligible guarantee can be classified differently based on the extent of protection that the primary guarantee provides. Similarly in Japan, only assets secured by the safest collateral will not be reclassified, even when customers experience problems, on the hypothesis that banks are unlikely to incur any loss. In many countries, collateral and guarantors are evaluated and considered in making loan provisions. This is relevant to the extent that financial institutions are able to seize and sell off collateral within a reasonable period. It is not unusual, however, for a collateral value to be used devoid of any discount being applied over time-even when the results of the financial institution's attempts are uncertain (Alain and Majnoni, 2002).

According to (Inwon, 2002), collateral needs to be appraised periodically, considering legal credentials and various other applicable factors such as viability of timely foreclosure. Collateral should be conservatively valued by the reliable, independent and consistent experts of the SACCO. When collateral is provided, management of the micro-credit institution (SACCO) should set up a mechanism periodically monitoring and appraising the worth of the collateral and little value should be attributed to enhance proper growth mechanisms.

(Foss, 2013) further states that it would be preferable to use an item that has a set value as collateral. Aside from eliminating any uncertainty between the parties, the lender appreciates the worth and re-sale ability of such asset in the event of default. It also leaves either party in no doubt as to the value of such collateral and hence the amount of loans it can collaterize.

Lenders would cherish collateral whose market values are not likely to devalue significantly during the life of the loan for instance, Agricultural products compared to buildings. Financial institutions also prefer assets with ready secondary markets as collateral. Assets that are highly susceptible to rapid obsolescence render older models less valuable.

However, Blazy and Weil disagree that high value collateral can induce Micro-credit institutions (SACCOs) to become lazy and therefore to undertake unsatisfactory screening of the borrowers when the loan is granted, and even if borrowers are fully sincere, they may suffer from excessive optimism making them undervalue their possibility of default consequently, they would be willing to provide any requested amount of collateral as they under-value the cost of collateral they present as cited in (Manova and Padilla, 2001).

(Inwon, 2002), further contends that during banking crises, collateral values drop sharply. Collateral is illiquid, difficult to value during periods of financial distress, and costly, (in terms of both time and expenses) to realize through foreclosure or other legal means. Another concern is that a large number of concurrent “fire sale” would amplify the fall in asset value. In addition, the reliability of measures to realize collateral value depends on a competent, swift, and transparent legal process. He further states that collateral plays an important role in many countries, collateral can be used to solve various economic questions, but in the practical world, particularly in new markets, it provides only little benefit to micro-credit financial institutions (SACCOs) even in good times, because of the complexity in evaluating and realizing collateral value.

2.11 Collateral ownership and the growth of SACCOs

Collateral ownership plays an important role in accessing credit from the Micro-credit institutions (SACCOs) since it gives guarantee to the Micro-credit institutions regarding the safety of the borrowed funds. Formal institutions have deprived the rural poor access to credit due to non-ownership of collateral (Ajay, 2009) and (Chiqudu, 1991) as cited in Blazy and Weil. Collateral assist in determining credit worthiness of the clients and also reduces the enforcement problem. In practice, households apply for credit but the lenders determine how credit is allocated to them basing on the insight of the household's credit worthiness and ownership of collateral security (Blazy and Weil). Collateral can reduce the problem of moral hazard after the borrower has obtained the loan by sinking the incentives of the borrower to invest in riskier businesses or to minimize efforts to ensure the success of the project from which loan has been granted. Indeed, the micro-credit institution (SACCO) can bring into line the borrower's interest with his collateral, as it imposes a greater loss on the borrower in case of default (Boot, Thakor and Udell, 1991) as quoted by (Blazy and Weil, 2010).

As also reported by the Banks for international settlements committee on Global Financial Systems (GFS, 2013), commercial banks and other formal financial institutions fall short of catering for credits of Small holders (rural poor), however, mainly due to their lending conditions which the rural poor do not meet. It is generally the rules of the formal financial institutions that have created the understanding that the rural poor are not bankable since they do not afford or own the required collateral, so they are considered un credit worthy as cited in (Adera,1995) by (GFS, 2013).

According to the study held in Bangladesh, the credit in SACCOs is targeted to assetless borrowers, the moderately poor or extremely poor. The borrowers are placed in groups of 10-20 people which meet frequently with the loan officer of .the micro-credit institution (SACCO) program. It is further explained that these groups of borrowers substitute for collateral and take over the role of securing for the loan. This is because each borrower in the group accepts to be held liable for debts incurred by any member of the group. In the event that a borrower does not pay, the other members of the group are required to make up the amount not paid (Meade, 2001:2), as cited by (Luyirika, 2010). Therefore, today if these rural poor did not afford any collateral security, they can unite as a group and have access to credit from the SACCOs as the group members will represent the collateral required.

(Businge, 2009) further supports the above statement stating that, an institution's success in mobilizing the prospective borrower to form groups and start saving makes accessibility to credit easy since the savings and members in the group can substitute collateral required as cited in (Anna, 2005 and Ledgerwood, 2000). From the lender's viewpoint, improved credit worthiness of the borrowers will reduce the danger of loan default, improve profitability, institutional development and financial sustainability of the micro-credit institution (SACCO) as cited in (Okurut, 2004).

Ha and Rong also contend that small and informal firms in developing counties who operate in the service sector are less likely to own assets for collateral and as a result, they potentially have to depend on other means such as their reputation or owners' personal connections to substitute for the formal collateral. On the other hand, firms in developed economies could potentially also borrow without collateral for different reasons. For example, developed countries with high levels of financial growth could allow financial institutions to track a firm's record of payments and defaults. In this case, financial institutions are more likely to know the category firms they give loans and therefore, firms are less likely required to posses some kind of collateral when borrowing.

2.12 Portfolio performance in savings

Loan portfolio theory describes the selection of portfolios that take full advantage of expected returns consistent with the individual suitable levels of risks in a given financial institution. The assumption gives a structure that specifies and measures investment risk to come up with a relationship between risk and expected returns. It further states that the full range of investments must be considered because the proceeds that accrue from all these investments interact thus; the relationship between the returns for assets in the portfolio should not be overlooked (Brown and Reilly, 2011 as cited in Lagat et al, 2013).

Modern portfolio theory is mainly concerned with finding the most favorable risks/return tradeoffs from financial assets. The loan portfolio is one of the most significant part of the whole portfolio of a given financial institution but regrettably, loan portfolio adjustments cannot happen immediately as it is in other asset categories and this happens due to market situations such as transaction costs and the illiquidity of loans arising from for example, informational asymmetries between the lender and the borrower. Arguments supporting loan portfolio risk concentration are mainly determined by loan market forces such as asymmetry information for instance, when a financial institution specialize its portfolio composition, it will always have to spend new resources to evaluate the particular industry but analyzing a financial institution’s portfolio structure might not disclose their intention unconcealed since the outstanding loan volumes as well as their composition result, among others from an interaction between supply and demand of loans including global economic development (Pfingsten and Kai, 2002).

The basic loan portfolio model was first developed by Harry Markowitz in the 1950s and early 1960s and he is considered the father of modern portfolio theory since he came up with the portfolio model that describes modern portfolio theory in which he derived the expected rate of return for a portfolio of assets and the expected risk measure. Markowitz established that under reasonable assumptions, the variance or standard deviation of the expected rate of return was a significant measure of portfolio risk. From this model therefore; the expected rate of return of a portfolio is the weighted average of the expected return for the individual assets in the portfolio.

He therefore asserted that the standard deviation is a function of;

i) The standard deviation for individual assets in the portfolio

ii) The covariance between the rates of return for all paired assets in the portfolio and further derived the following formulas for computing the expected return and the variance of a portfolio.

Expected rate of return for a portfolio:

$$ERp = \Sigma\ Wi\ ERi$$

The variance and standard deviation:

$$\delta p = \Sigma\ Wi\ \delta i + \Sigma\ Wi\ Wj\ COVi\ j$$

Where; $i \neq j$

From the above formulas, Markowitz determined how to diversify effectively and the importance of diversification of investments in order to reduce total risk of portfolio. The theory further asserts that the risk of portfolio returns is determined by three factors namely;

The risks or standard deviation of individual securities that constitute the portfolio.

The proportions of individual securities in the portfolio.

Coordination of returns between the securities in the portfolio (Brown and Reilly, 2011) as cited in (Lagat et al, 2013).

2.13 Interest income

Accounting dictionary defines interest income as the amount of interest that has been earned during a specific period which might have been in cash or it might have been accrued that is, it has been earned but the payment has not yet been made. The accrued interest income should only be recorded after receiving cash and if the amount to be received can be calculated. It is only investments that pay interest that earn interest income for a given financial institution and such investments may include savings account or a certificate of deposit. It may also be earned for penalty charges levied on the financial institution's clients for instance, overdue accounts, since the payments are based on the financial institution's funds by the clients but some financial institutions may instead call it penalty income and commercial banks may refer to it as the excess amount earned on investments over the amount paid out for deposits and is recorded within the interest income account in the general ledger (Accounting tools, On-line).

Net interest income on the other hand is the cash flow financial institutions receive from loans and investment in securities less interest payments on savings deposits and other forms debt that are present. Cash inflows and outflows depend directly on the interest rates a given financial institution charges on loans, earns on securities and pays on deposits as well as other debt instruments, and on the structure of its asset and liabilities. The growth of community banks and other micro credit institutions ultimately therefore depend on their ability to earn adequate returns on lending which therefore give the importance of community banks to the local economies and the lack of recovery in community banks is largely a legitimate worry (Morris and Regehr, 2014).

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 Introduction

This chapter presents and describes in detail the strategies used by the researcher in conducting the research which included; The research design, study population, study area, sample size, sampling techniques, data sources, methods of data collection, data analysis and presentation, quality control, measurement of variables, ethical considerations and the limitations encountered during the study.

3.1 Research design

3.1.1 Study design

The researcher employed a case study design to collect the required data with reference to Morulem Savings and Credit Cooperative Organization (MOSACCO) as the representative study organization. The researcher selected a case study design because it is good for studying rare phenomena where large samples of similar characteristics are not available and also challenges theoretical assumptions.

In order to ensure that the objectives of the study were attained, the researcher used majorly and quantitative data collection approach.

It majorly relies on random sampling and structured data collection instruments that fit diverse experiences into predetermined response categories and they produce results that are easy to summarized, compare and generalize.

Quantitative research was used because it is more reliable and objective and uses statistics to generalize findings.

The use of the quantitative data collection method was aimed at obtaining extensive, reliable, valid and logical conclusions to the research findings.

The researcher used cross sectional study approach to collect data because this was a short term study meant to produce only one report which made it more reliable to use this approach in order to meet the objectives of the study it is also quick and easy to use in order to come up with the findings of research.

3.2 Study population

The researcher used Morulem Savings and Credit Cooperative Organization (MOSACCO) as his study organization.

The researcher obtained data mainly from the members of Morulem Savings and Credit Cooperative Organization (MOSACCO), the management and staff particularly those in the loans section.

3.3 Area of study

The study was conducted in Morulem Sub-County, Abim District, and Karamoja sub-region in North-eastern Uganda a distance of 418.3 km from Kampala City by road.

3.4 Sample size

The researcher employed (Krejcie and Morgan, 1970) table to determine the sample size from the study population.

It was from the large group of people who constitute the study population that a sample population was selected to compose the respondents for the study. This particular sample size was selected because it was easier to manage and it was enough to generate findings as well as to generalize the findings to a bigger population. The sample size also took into account the fact that the respondents were only management, staff and members/borrowers of Morulem Savings and Credit Cooperative Organization (MOSACCO).

Table 3.1 Population and Sample size of Respondents

Description	Population Size	Sample Size
Managers/Staff	6	6
Members/Borrowers	85	70
Total	**91**	**76**

Source; primary data, 2015

The respondents to the study constitute 6 staff / mangers and 85 members/borrowers form which a sample of 70 respondents were selected to constitutes the sample size of respondents to the study. The total population size was 91 and the total sample size was 76 respondents.

3.5 Sampling techniques

The researcher used probability sampling technique under which he employed simple random method to select from among the study population the respondents. Here, the researcher selected respondents randomly without considering any characteristic or features and it enabled every sampling unit to have a chance of being chosen. The researcher also applied purposive sampling technique majorly in selecting staff because there was need to specifically get information from those members of staff who deal directly with loans advancement and verification.

3.6 Data sources

The researcher used primary, secondary and tertiary data sources to help him collect a more elaborate and extensive data.

The primary data helped the researcher get original and direct information from the respondents.

The researcher used secondary data sources that helped him get access to records of previous performance of the organization and other external sources which are established by other scholars and academicians about the variables under study through use of tertiary data sources.

3.7 Methods of data collection

3.7.1 Questionnaires

These were self-administered by the researcher and they contained questions divided into sections that is, Staff/management section, and members/borrowers' section. Sproul (1998), states that a self administered questionnaire is the only way to elicit self report on people's opinion, attitudes, beliefs and values. This was used by the researcher to collect primary data and it contained both open and closed ended questions. A 5-point likert scale was used to construct the closed ended questions with five (5) intervals which ranged from; 1-Strongly Disagree, 2-Disagree, 3-Not Sure, 4-Agree and 5-Strongly Agree. The closed ended questions assisted the researcher to collect quantitative data. The questions were delivered direct to the respondents and the respondents filled the questionnaires in writing.

3.8 Data analysis and presentation

3.8.1 Quantitative data

Majorly, quantitative approach of data analysis was used to analyze data. After data collection and gathering, it was examined to detect errors, omissions, contradicting and unreasonable information to establish how and when collateral security influences SACCO's performance. This was done to ensure accuracy, consistency, uniformity and meaningful information for analysis. Quantitative data from the questionnaire will be coded and entered into the computer for computation of descriptive statistics. The Statistical Package for Social Scientists (SPSS 16.0) was used to run descriptive statistics such as frequency and percentages to present the quantitative data in form of tables and graphs based on the major research questions.

3.9 Quality control

3.9.1 Reliability

According to (Mugenda and Mugenda, 1999), an instrument is reliable when it can measure a variable accurately and obtain the consistent results over a period of time. However, reliability in research may be affected by random errors, the pre-test of the research tools helped the researcher in identifying the most likely source of errors and hence respond to before the actual study was carried out. Test re-test method was used to pilot the questionnaires, which did not form sample of the study.

3.9.2 Validity

(Mugenda and Mugenda, 1999) state that, for a data collection instrument to be considered valid, the content selected and included must be relevant to the need or gap established. Before the actual study, the instruments were discussed with the supervisor and research experts. The feedback and recommendations from the supervisor and research experts helped in modifying the instruments. The research instrument was validated in terms of content and face validity. The content related technique measures the degree to which the questionnaire items reflected the specific areas covered.

3.10 Measurement of variables

The research variables were measured using a questionnaire for both the managers/staff and the members/borrowers of MOSACCO.

The researcher used the 5-point likert scale with respondent's answers ranging from "Strongly agree" to "Strongly disagree" to collect information that was used to measure the variables. This scale was formulated by Dane Bertram.

Collateral security which is the independent variable for this study was measured in respect to its dimensions like; Collateral valuation, Collateral eligibility and ownership (Kababiito, 2013).

3.11 Ethical issues

Before data collection commenced, the researcher sought permission to collect data from the appropriate authorities. He secured a letter of introduction from Uganda Martyrs University, Faculty of Business Administration and Management (BAM) which he presented to the manager Morulem Savings and Credit Cooperative Organization (MOSACCO) to let him inform his members and staff about the study.

The researcher ensured confidentiality and security of the data collected from the respondents by not allowing them fill the questionnaires anonymously to avoid exposure of who gave what information.

The researcher ensured that he did not force the responded to participate in providing response to his questions but rather sought for voluntary response from the respondents.

The researcher acknowledged all the sources of information he has used to compile this study information by sighting them appropriately.

3.12 Study limitations

The study was conducted in Morulem Sub-County, Abim District using only Morulem Savings and Credit Cooperative Organization (MOSACCO) as a case study. This implied that the study had geographical limitations. However, the researcher used both qualitative and quantitative data collections approaches to collect enough data.

The study was limited by time and other logical issues to use the data collection tools adequately to get complete information. However, he used a cross sectional study to mitigate this limitation.

The study was a cross sectional study which implied a short term study and may have lead to making wrong conclusions on the findings of the study on how the variables behave. The researcher used the multi data collection techniques to mitigate making wrong conclusions.

The researcher used sampling technique to collect data from which thus, not all respondents were contacted and so some important information may have been left out which might have led to errors in the findings by the researcher. This was also mitigated by use of multi data collection techniques by the researcher.

CHAPTER FOUR

PRESENTATION, ANALYSIS AND DISCUSSION OF FINDINGS

4.0 Introduction

The study findings and analysis are presented in this chapter. The purpose of the study was to establish the role of collateral on the growth of Savings and Credit Cooperative Organizations (SACCOs) in Uganda-Abim district. The analysis is based on the data collected using questionnaires which were answered by the staff/management and members/borrowers of MOSACCO.

The presentation of findings is arranged in accordance with the questionnaire questions. 76 questionnaires were designed for the study which were responded to by the Managers/Staff and Members/borrowers of MOSACCO. This meant that all the questionnaires were responded to duly during the study.

4.1 Background Information of respondents

In this section, the researcher aimed at establishing the personal characteristics of the respondents to the study. These included information like; Gender, age group, education level and the duration of membership or duration worked at Morulem Savings and Credit Cooperative Organization (MOSACCO).

Table 4.2 Frequency Distribution for Gender of Respondents

Gender	Frequency	Percent
Male	31	40.8
Female	45	59.2
Total	**76**	**100.0**

Source; *Primary data, 2015*

Results in table 4.2 reveal that there were more females than males who participated in the study. Females constituted 59.2% of the respondents while males made up 40.8% of the total respondents.

Table 4.3 Frequency Distribution for Age group of respondents

Age Group	Frequency	Percent
18-24	13	17.1
25-30	20	26.3
31-34	12	15.8
35-40	11	14.5
41 and above	20	26.3
Total	**76**	**100.0**

Source; *Primary data, 2015*

Results in table 4.3 above reveals that respondents of different age groups ranging from 18 years to 41 years and above participated in the study. From the table it is noted that respondents of age group of 25-30 years and 41 years each with a percentage of 26.3%, while the age group 18-24 followed with a percentage of 17.1% and the age group31-34 had 15.8% and 35-40 had the least percentage of 14.5.

Table 4.4 Frequency Distribution for Education level of respondents

Education level	Frequency	Percent
Certificate or Diploma	28	36.8
Degree	15	19.7
Postgraduate	10	13.2
Others (P.L.E, U.C.E, U.A.C.E)	23	30.3
Total	**76**	**100.0**

Source; *Primary data, 2015*

From table 4.4 above, it is noted that the qualification of respondents include; Certificate or diploma, degree, postgraduate and other levels of education which included Primary Leaving Examination (P.L.E), Uganda Certificate of Education (U.C.E) and Uganda Advanced Certificate of Education (U.A.C.E).

The results show that Certificate or Diploma holders formed a majority of the study respondents with 36.8%, others (P.L.E, U.C.E and U.A.C.E) constituted 30.3%, Degree 19.7% and Postgraduate had the least percentage of 13.2% of the total respondents.

Table 4.5 Frequency Distribution for duration of respondents

Duration	Frequency	Percent
Less than a year	14	18.4
1-2 years	21	27.6
Over three years	41	53.9
Total	**76**	**100.0**

Source; *Primary data, 2015*

Results shown in table 4.5 reveal that a majority of the respondents (41) (53.9%) have worked or have been members in MOSACCO for over three years, 21 respondents (27.6%) 1-2 years and 14 respondents (18.4%) have worked or have been in MOSACCO for less than a year.

4.2 Collateral Eligibility and growth of SACCOs

One of the objectives of the study was to examine the relationship between collateral eligibility and the growth of SACCOs. European Central Bank Report (Euro system) (2013), states that assets to be eligible as collateral for financial institution's operation need to fulfill certain criteria and requirements to ensure sufficient quality and protect the financial institution from counter-party credit risk. The capacity to pool eligible collateral assets to raise secured borrowing and lending can be viewed as a liquidity buffer to be used in times of financial market stress.

As indicated in the methodology (Chapter three) of the study, the questionnaire which was used to generate data was designed on a five-point likert scale with different levels of agreement for each statement that is, 1-Strongly disagree, 2-Disgree, 3-Not sure, 4-Agree and 5-Strongly agree. This therefore shows that all responses averaging 3.0 and above accounted for “Agree” whereas all responses averaging below 3.0 accounted for “Disagree”.

4.2.1 Descriptive statistics on the eligibility of collateral

The eligibility of collateral considered by MOSACCO was examined by computing the mean and standard deviation from statements categorized under; lending policy, collateral eligibility, counter-party risk, loans without eligible collateral, self-selecting borrowers, nature of loans and recovery measures forms of collateral. The analysis is provided in the table below.

Table 4.6 Mean and standard deviation for Collateral eligibility

Collateral eligibility	N	Min	Max	Mean	Std. Dev
Lending policy	76	1	5	4.05	1.232
Collateral Eligibility	76	1	5	3.99	1.160
Counter-party risks	76	2	5	4.28	0.826
Loans without Eligible Collateral	76	1	5	3.93	1.087
Self-selecting borrowers	76	1	5	3.96	1.216
Nature of loan and recovery measures	76	1	5	4.05	1.142
Forms of collateral	76	1	5	4.11	1.206

Source; *Primary data, 2015*

4.2.1.1 Lending policy

As viewed from table 4.6 above, majority of the respondents agree that it is the lending policy of MOSACCO to require collateral before advancing loans with mean, 4.05 and a standard deviation of 1.232. This seems to agree with the study done by (Roslyn 2007), as quoted in (Ooko, 2011) who found out that SACCOs always require collateral to be presented by their clients as a policy so that they access loans.

4.2.1.2 Collateral eligibility

Notably from table 4.6 above, majority of the respondents agreed that collateral eligibility is considered before giving loans to the clients with a mean of 3.99 although some of the respondents had different views as shown by the standard deviation of 1.160. This response seems to be in agreement with the study conducted by European Central Bank report (Euro system, 2013), which reveals that the capacity to pool eligible collateral assets to raise secured borrowing and lending can be viewed as a liquidity buffer to be used in times of financial market stress. Despite the agreement with this study, there was still variation in the response meaning that the respondents did not have the same view about collateral eligibility considered by SACCOs.

4.2.1.3 Counter-party risk

Table 4.6 above shows that majority of the respondents agreed that collateral protects MOSACCO from counter-party risks that may occur in the process of the transaction with a mean of 4.28 however, some of the respondents had different views as shown by the standard deviation value of 0.826. This agreement is further supported by a study from European Central Bank report (Euro system, 2013) which stated that assets to be eligible as collateral for financial institution's operation need to fulfill certain criteria and requirements to ensure sufficient quality, and protect the financial institution from counter-party credit risk.

4.2.1.4 Loans without eligible collateral

Results in table 4.6 shows that respondents agreed that loans without eligible collateral are riskier than those without with mean 3.93 although some of the respondents had different views as shown by the standard deviation of 1.087. This seems to answer the question posed by, (Berger and Udell, 1990), and (Boot, Thakor and Udell, 1991), as cited in (Yaron, 2008) who said that, one important question is also whether loans with eligible collateral are riskier or not than those without. Their theory predicts that riskier borrowers are more likely to pledge collateral when the quality of the borrower is observable for the lender and there is moral hazard hence loans without eligible collateral are riskier than those without.

4.2.1.5 Self selecting borrowers

Study results in table 4.6 shows that respondents agree that MOSACCO uses Collateral eligibility to self-select borrowers according to their perceived risks with a mean of 3.96 although some of the respondents had different views as shown by the standard deviation of 1.216. Their agreement seems to be supported by (Bester, 1985), (Basenko and Thakor, 1987) and (Berger and Udell, 1990) as cited in Yaron (2008) who say that, if the quality of the borrower is not observable that is, hidden information and adverse selection, then the lender will use the collateral eligibility to self-select the borrowers according to their perceived risk and, in the equilibrium solution, high quality borrowers will choose loans with high eligible collateral and lower interest rates.

4.2.1.6 Nature of loan and recovery measures

As noted from table 4.6, results show that the respondents agree that Collateral obtained determines the nature of the loan and the measures of recovery with a mean value of 4.05 however, some of the respondents had different views as shown by the standard deviation of 1.142. (Roslyn, 2007), as quoted in (Ooko, 2011) conducted a study which found the facts that influenced the repayment of loans in SACCOs were the nature of collateral, control recovery measures and the nature of loans that the SACCO society has in place to check on defaulters. Her study recommended that there was need for SACCOs to implement sound collateral eligibility management and loan recovery measures to enhance the growth of SACCOs. (Roslyn's 2007) study further showed that the growth of SACCOs' wealth was related to the control of loan default by use of sound collateral eligibility criteria. This did not however explain how growth of SACCOs' wealth would be achieved. This study therefore seems to support the views provided by the respondents.

4.2.1.7 Forms of collateral

Table 4.6 further revealed that majority respondents agree that various forms of collateral are accepted by Morulem Savings and Credit Cooperative Organization from their clients with mean value of 4.11 however, some of the respondents had different vies as shown by the standard deviation value of 1.206.

4.3 Collateral Valuation and growth of SACCOs

Another objective of the study was to examine the relationship between collateral valuation and the growth of SACCOs. This was examined using the statements under; loan amount, monitoring collateral value, latest available source for valuing, loan quality, market value of collateral, reliable and independent expert valuers, worth and resale value of collateral and screening of the borrowers.

Table 4.7 Mean and standard deviation of Collateral valuation

Collateral valuation	N	Min	Max	Mean	Std. Dev
Loan amount	76	1	5	4.05	1.299
Monitoring collateral value	76	2	5	3.99	.974
Latest available source for valuing	76	1	5	4.28	1.076
Quality of the loan	76	1	5	3.93	1.154
Market value of Collateral	76	1	5	3.96	1.381
Reliable, independent experts	76	2	5	4.05	5.778
Worth and resale value	76	1	5	4.11	.978
Screening of borrowers	76	1	5	3.13	1.708

Source; *Primary data, 2015*

4.3.1 Loan amount

It is noted from table 4.7 that respondents agree that Collateral value is considered to determine the loan amount that is to be given to the clients with a mean value of 4.05 although some of the respondents had different vies as shown by the standard deviation of 1.299. The respondents' agreement seem to be of the same mind with Alain and (Majnoni, 2002) who stated that, if the collateral is assigned too high a value, the provision for the loan will be insufficient.

4.3.2 Monitoring collateral value

Results presented in table 4.7 shows that the respondents agree with the statement that the value of Collateral is monitored throughout the life of the transaction with a mean value of 3.99 although some respondents had different views as shown by the standard deviation of value 0.974. Their response seems to be in agreement with (Garreth, 1995), who states that once the bank has accepted the eligibility of the collateral offered and set the relevant haircut, it continues to monitor the value of the collateral throughout the life of the transaction on a daily basis. (Inwon, 2002), further seem to support this statement stating that, collateral needs to be appraised periodically, considering legal documentation and various other relevant factors such as feasibility of timely foreclosure. He states that this helps the SACCO in this case to be acquainted with the change in value of the collateral presented so that adjustments are made where necessary.

4.3.3 Latest available source for valuing collateral

As study results in table 4.7 shows, the respondents agree that Collateral is valued using the latest available source or the historical performance of the Collateral presented by the respondents having a mean value of 4.28 however, some respondents had different views as shown by the standard deviation value of 1.076.

The respondents therefore seem to be in agreement with the study of (Garreth, 1995), who found out that the financial institution will re-value all the collateral it is holding using the latest available source and where prices are not available, the financial institution will use model based techniques including using discounted cash flow valuation for fixed income collateral security and historical performance data for asset backed collateral security.

However, (Alain and Majnoni, 2002) contend that although collateral is potentially marketable, banks and other financial institutions and to some extent, supervisors may underestimate or ignore the obstacles caused by weak legal systems and cultural factors in the effective disposal of the collateral.

4.3.4 Quality of the loan

As viewed from table 4.7 above, respondents agree that Collateral is valued depending on the quality of the loan to be given to the clients with a mean value of 3.93 although some respondents had different views as shown by the standard deviation value of 1.154. A study by (Alain and Majnoni, 2002) reveals that countries take varying approaches to the treatment of collateral and other guarantees in the classification process. Several jurisdictions for instance, from Czech Republic, France, Spain, and West African Monetary Union do not take collateral and guarantees into account for classification purposes.

As a result, classifications reflect the quality of loans regardless of the purpose for recovery derived from collateral. Far more countries explicitly factor in the value of collateral, in various ways, when classifying loans. This seems to be in agreement with the respondents as regard loan quality.

4.3.5 Market value of Collateral

The results in table 4.7 above notes that respondents agree that the market value of Collateral should be able to cover payment of the principle and accrued interest of the loan given by MOSACCO having a mean value of 3.96 however, some respondents had different vies as shown by the standard deviation of 1.381. They seem to be in agreement with Alain and (Majnoni, 2002) who carried out a study in Australia and the findings were that loans with interest or principal 90 days past due must be recorded as non-accrual if the market value of the collateral is insufficient to cover payment of principal and accrued interest. When the market value is sufficient, the loan is classified as past due. (Foss, 2013) further states that lenders would cherish collateral whose market values are not likely to depreciate significantly during the life of the loan for instance, Agricultural products compared to buildings.

4.3.6 Reliable, independent experts

As presented in table 4.7 above, study results show that respondents agree to the statement that Collateral is valued by reliable, independent experts of MOSACCO with a response mean value of 4.05 although some respondents had different views as shown by the standard deviation of 5.778. According to (Inwon, 2002), collateral needs to be appraised periodically, considering legal documentation and various other relevant factors such as feasibility of timely foreclosure.

Collateral should be conservatively valued by the reliable, independent experts of the SACCO/financial institution. This appears to be in agreement with the view of the respondents that MOSACCO uses reliable, independent experts to value collateral prior to loan acquisition.

4.3.7 Worth and resale value

Basing on the results in table 4.7 above, the respondents agree with the statement that the worth and resale value of the Collateral is considered when advancing loans to clients with a mean value of 4.11 although some respondents had different views as shown by the standard deviation of 0.978. (Foss, 2013) asserts that, aside from eliminating any ambiguity between the parties, the lender appreciates the worth and re-sale ability of such asset in the event of default and that it also leaves neither party in doubt as to the value of such collateral and hence the amount of loans it can collaterize. His findings therefore seem to be in agreement with the views of the respondents of the study.

4.3.8 Screening of borrowers

Study results in table 4.7 shows that respondents agree that highly valued Collateral may make MOSACCO management/staff become lazy to undertake sufficient screening of borrowers before the loan is granted. This has a mean value of 3.13 however, some respondents had different views as shown by the standard deviation of 1.708. This seems to concur with a study by (Blazy and Weil) as cited in (Manova and Padilla, 2001) who stated that high value collateral can induce Micro-credit institutions (SACCOs) to become lazy and therefore to undertake insufficient screening of the borrowers when the loan is granted, and even if borrowers are fully sincere, they may suffer from excessive optimism making them underestimate their probability of default consequently, they would be willing to provide any requested amount of collateral as they under-value the cost of collateral they present.

4.4 Collateral Ownership and growth of SACCOs

This section gives findings to objective three of the study. This was achieved through examining data collected under the variable collateral ownership and the performance of SACCOs. Collateral ownership was measured using statements including; client must own the collateral, safety assurance, credit worthiness, group borrowing, saving deposits, borrowers' past history and reputations, and problems encountered from requirement of collateral.

Table 4.8 Mean and standard deviation of Collateral ownership

Collateral Ownership	N	Min	Max	Mean	Std. Dev
Client must own the Collateral	76	1	5	4.03	1.275
Assurance	76	2	5	4.12	.993
Credit worthiness	76	2	5	3.95	.831
Group borrowing	76	1	5	3.61	1.234
Savings deposits	76	1	5	3.87	1.087
Borrowers' past history and reputations	76	2	5	3.99	.931
Encounters some problems	76	1	5	3.86	1.430

Source; *Primary data, 2015*

4.4.1 The client must own the collateral

As viewed from table 4.8, respondents agree that the client must own the Collateral presented to MOSACCO in order to access the loan with a mean value of 4.03 however, some respondents had different views as shown by the standard deviation rate of 1.275. Their view seem to be in agreement with the study by (Ajay, 2009 and Chiqudu, 1991) as cited in (Blazy and Weil, 2010) who stated that formal institutions have denied the rural poor access to credit due to lack of collateral ownership. However, Ha and Rong argue that small and informal firms or individuals in developing countries who operate in the service sector are less likely to own assets for collateral and as a result, they potentially have to rely on other means such as their reputation or owners' personal connections to substitute for the formal collateral. On the other hand, firms and individuals in developed economies could potentially also borrow without collateral for different reasons. For example, developed countries with high levels of financial development could allow financial institutions to track a firm's or individual’s history of payments and defaults.

In this case, financial institutions are more likely to know the type of firms and individuals they give loans and therefore, firms or individuals are less likely required to posses some kind of collateral when borrowing.

4.4.2 Assurance

As presented by the results in table 4.8, respondents to the study agreed that Collateral ownership gives assurance to MOSACCO regarding the safety of the loan given out to the clients having a mean value of 4.12 although some respondents had different views as shown by the standard deviation rate of 0.993. (Ajay, 2009 and Chiqudu, 1991) as cited in (Blazy and Weil, 2010) carried out their study and found that, collateral ownership plays an important role in accessing credit from the Micro-credit institutions (SACCOs) since it gives assurance to the Micro-credit institutions regarding the safety of the borrowed funds. This therefore seems to correspond with the views obtained from the respondents that collateral gives assurance to the financial institution as regard safety of the loan borrowed out.

4.4.3 Credit worthiness

Basing on the results in table 4.8, respondents agree that Collateral ownership helps to determine credit worthiness of the borrowers and also reduce enforcement problems with a mean of 3.95 although some respondents had different views as shown by the standard deviation value of 0.831. (Blazy and Weil, 2010) in their study noted that Collateral assist in determining credit worthiness of the borrowers and also reduces the enforcement problem. In practice, households apply for credit but the lenders determine how credit is allocated to them basing on the perception of the household's credit worthiness and ownership of collateral security that they present.

Further, (GFS, 2013) as cited in (Adera, 1995) report that, it is generally the rules of the formal financial institutions that have created the myth that the rural poor are not bankable, since they do not afford or own the required collateral and so they are considered uncredit worthy. This study therefore seems to agree with the view obtained from the respondents during the study.

4.4.4 Group borrowing

Results in table 4.8 above show that respondents agree that borrowers who do not own Collateral are put in groups so as to access loans from MOSACCO with a mean of 3.61 however, some respondents had different views as shown by the standard deviation of 1.234. According to the study carried out in Bangladesh by (Meade, 2001:2) as cited by (Luyirika 2010), the credit in SACCOs is targeted to the landless or asset-less borrowers, the moderately poor or extremely poor. The borrowers are placed in groups of 10-20 people which meet regularly with the loan officer of the micro-credit institution (SACCO) program.

It is further explained that these groups of borrowers substitute for collateral and take over the role of securing for the loan and each borrower in the group agrees to be held liable for debts incurred by any member of the group. In the event that a borrower defaults, the other members of the group are required to make up the amount in default.

(Businge, 2009) as cited in (Anna, 2005), and (Ledgerwood, 2000) further supports the above statement stating that, an institution's success in mobilizing the potential borrower to form groups and start saving makes accessibility to credit by the borrowers easy since the savings and members in the group can substitute collateral needed. Therefore, today if these rural poor did not own any collateral security, they can join a group and have access to credit from the SACCOs as the group members will represent the collateral needed. The researchers above seem to agree with the views obtained from the respondents.

4.4.5 Savings deposits

Study results presented in table 4.8 above indicate that respondents agree that savings deposits and members in the group substitute the Collateral needed by MOSACCO in order to give out loans (mean, 3.87) although some respondents had different views as shown by the standard deviation of 1.087. This shows that views of the respondents varied from one respondent to another. The respondents’ views seem to correspond with the study by (Businge, 2009) as cited in (Anna, 2005), and (Ledgerwood, 2000) who stated that an institution's success in mobilizing the potential borrower to form groups and start saving makes accessibility to credit by the borrowers easy since the savings and members in the group can substitute collateral needed.

4.4.6 Borrowers' past history and reputations

Study results in table 4.8 above indicate that respondents agree to the statement that the borrowers' past history, reputations and the owners' personal connections are considered in case there is no Collateral presented with a mean value of 3.99 although some respondents had different views as shown by the standard deviation of 0.931. The standard deviation shows that the borrowers had approximately uniform views as to whether the borrowers’ past history and reputation is considered if there is no collateral.

This seems to be in agreement with Ha and Rong’s study which state that small and informal firms and individuals in developing counties who operate in the service sector are less likely to own assets for collateral and as a result, they potentially have to rely on other means such as their reputation or owners' personal connections to substitute for the formal collateral. On the other hand, firms or individuals in developed economies could potentially also borrow without collateral for different reasons.

For instance, developed countries with high levels of financial development could allow financial institutions to track a firm's history of payments and defaults. This study therefore seems to agree with the views presented by the respondents of the study.

4.4.7 Problems encountered from the requirement of collateral

Basing on the results shown in table 4.8, it can be noted that respondents agree that MOSACCO encounters some problems from the requirement of Collateral from their clients to access loan and their agreement had a mean value of 3.86 however, some respondents had varying views as shown by the standard deviation of 1.430. This shows there was variation in the views of the respondents during the study. As reported by the Banks for international settlements committee on Global Financial Systems (GFS, 2013), commercial banks and other formal financial institutions fail to cater for credits of Small holders (rural poor), however, mainly due to their lending terms and conditions which the rural poor do not meet like the requirement of collateral which pose a problem of a few clients demanding for loans and this seems to be in agreement with the views of the respondents.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.0 Introduction

This chapter presents the summary, conclusions and recommendations on Collateral Security and Growth of Savings and Credit Cooperative Organizations (SACCOs) basing on the findings from the study. The findings, conclusions and recommendations were to examine how Collateral security influences the performance of SACCOs in terms of collateral eligibility, collateral valuation and collateral ownership.

The data were analyzed inform of tables which were used to test the relationship between the independent variable (Collateral security) and the dependent variable (growth of SACCOs).

5.1 Summary of findings

5.1.1 Collateral Eligibility and the growth of SACCOs

While assessing collateral eligibility, the researcher used various qualities of collateral eligibility like; lending policy, collateral eligibility, counter-party risk, loans without eligible collateral, self-selecting borrowers, nature of loans and recovery measures forms of collateral.

Findings from the study revealed that a majority of the respondents agreed that collateral security enhances the growth of SACCOS by for example acting as a liquidity buffer, protecting counter-party risks, providing proper measures of recovery to check on loan defaulters and appropriate selection of its borrowers.

5.1.2 Collateral Valuation and the growth of SACCOs

Assessment of Collateral valuation was measured using the variables of; loan amount, monitoring collateral value, latest available source for valuing, loan quality, market value of collateral, reliable and independent expert valuers, worth and resale value of collateral and screening of the borrowers.

Study findings revealed that a majority of the respondents assented to the view that collateral valuation leads to the growth of SACCOs by; helping to determine the loan amount to be granted in respect to collateral value, acquaintance with the change in value of the collateral presented so that adjustments are made where necessary, enabling valuation to be carried out by reliable, independent experts and proper screening of borrowers before the loan is granted.

5.1.3 Collateral Ownership and the growth of SACCOs

While assessing Collateral ownership it was measured using the variables under; client must own the collateral, safety assurance, credit worthiness, group borrowing, saving deposits, borrowers' past history and reputations, and problems encountered from requirement of collateral.

Study findings disclosed that a majority of the respondents agreed that collateral ownership enhances growth of SACCOs through; giving assurance regarding the safety of the loan given out to the clients, clients did not default paying back the loans, improved credit worthiness of the borrowers and also reduced enforcement problems, members who did not own collateral accessed loans through group borrowing and that there were a few clients demanding for loans due to the requirement of collateral.

5.2 Conclusions

The study was set to assess the role of Collateral on the growth of SACCOs in Uganda taking Morulem Savings and Credit Cooperative Organization (MOSACCO), in Abim district-Karamoja Sub region as the case study organization.

Following the results of the study presented in chapter 4, the researcher was able to make conclusions on the role of collateral security on the performance of SACCOs as under;

Collateral eligibility enhances secured borrowing, protects both the SACCO and the borrowers from counter-party risks, and helps the SACCO select clients to be granted what type and nature of loan demanded as well as the measures of loan recovery and that various forms of collateral are accepted by MOSACCO. This is evidenced by the different responses summarized on the qualities such as; lending policy, collateral eligibility, counter-party risk, loans without eligible collateral, self-selecting borrowers, nature of loans and recovery measures.

Collateral valuation helps MOSACCO to determine the nature of loans to be granted, helps them monitor any changes in the value of asset pledged as collateral, value collateral using the latest market value, match the right collateral amount with the right loan quality, enables the SACCO set a value that will cover both the principle and interest accrued, enables them use reliable, independent expert to value collateral and as well measure the worth and resale value of the collateral. It is also found that highly valued collateral may make the SACCO undertake insufficient screening of borrowers which in turn may cause losses to the SACCO.

Collateral ownership helps the SACCO ensure that the borrower owns the collateral pledged for the loan, assures the SACCO about the safety of the loan lent to the borrower, and helps determine the credit worthiness of the client.

The borrowers also can access loans through forming groups since the groups substitute collateral, and that other traits like past credit history is considered when there is no collateral. Collateral security also posed some problems to the SACCO like reduced demand for loans thus, reducing growth potentials of the SACCO.

This is the general objective of the study and it was measured using the variable like; collateral eligibility, collateral valuation and collateral ownership. As observed from the evaluation of these variables, collateral security enhances the growth of SACCOs since through its demand, there is reduced loan default, prevents counter-party risks and enhances better recovery measures for the SACCOs thus reduces risks of losses that might occur in case of unsecured loans.

5.3 Recommendations

Basing on the findings of the study, the researcher found it prudent to make a few recommendations which are deemed important to guide the readers and policy makers as they use this research work and in order that Morulem Savings and Credit Cooperative Organization (MOSACCO) may use it to achieve potential growth through the demand of collateral security when it lends its members/borrowers.

From the study findings, it is pertinent that collateral should be given adequate attention as a prerequisite of lending since it protects the lending institution from anomalies like loan default which is currently rampant with most borrowers.

Collateral should not be seen as tool to mount pressure on the borrowers but rather as a monitoring tool that will help the borrowers use the borrowed funds adequately and efficiently so that they able to repay both the principle and accrued interest in time.

The study findings revealed that some problems were encountered from the demand for collateral security like reduced loans demand. MOSACCO should therefore relax their loan prequalification policies in order that more borrowers can access loans from the SACCO. This can be curbed by constantly reviewing their credit policies that will enhance adequate evaluation of borrowers even in the absence of collateral.

The researcher also recommends that a strong audit committee be instituted in MOSACCO to regularly and consistently check on the internal control systems of the SACCO. This will help the organization perform better since it will act as a watchdog on the activities on the organization.

5.4 Suggested Areas for further research

Loan recovery policies and the performance of Savings and Credit Cooperative Organizations in Uganda.

Information technology and the performance of Savings and Credit Cooperative Organizations in Uganda.

The role of Auditing on the Performance Savings and Credit Cooperative Organizations in Uganda.

The role of Capital structure methods on the growth of Performance Savings and Credit Cooperative Organizations in Uganda.

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APPENDIX

APPENDIX I: QUESTIONNAIRE

Dear sir/ madam;

I am Okullo Denis, student of Uganda Martyrs University pursuing Bachelor of Business Administration and Management.

This is purely an academic research aimed at establishing the role of Collateral Security on the growth of Savings and Credit Cooperative Organizations (SACCOs). You have been chosen as a respondent because you are a member/staff/part of management of Morulem Savings and Credit Cooperative Organization. I therefore request that you spare your valuable time and answer these questions. I promise as a researcher that the information you provide will be treated with utmost confidentiality and anonymity.

SECTION A: Background Information and the Growth of SACCO

1. Gender

a) Male ☐ b) Female ☐

2. Age group (years)

a) 18 -24 ☐ b) 25-30 ☐ c) 31-34 ☐

d) 35-40 ☐ e) 41 and above ☐

3. Education level

a) Certificate or Diploma ☐ **b)** Degree ☐

c) Postgraduate ☐ **d)** Others, specify ☐

4. Duration you have been in Morulem Savings and Credit Cooperative Organization (MOSACCO)

a) Less than a year ☐ b) 1-2years ☐ d) over 3 years ☐

SECTION B: Collateral Eligibility and the Growth of SACCO

Please tick your appropriate choice in the space provided using the keys given below;

1. S.D- Strongly Disagree **2. D-** Disagree **3. N.S-** Not Sure **4. A-** Agree **5. S.A-** Strongly Agree

Statement	**S.D**	D	**N.S**	A	**S.A**
1. It is the lending policy of MOSACCO to require collateral before advancing loans to borrowers					
2. Collateral eligibility is cindered before the loan is advanced					
3. The Collateral we obtain protects our SACCO from counter-party risk					
4. Loans without eligible Collateral are riskier than those without					
5. Our SACCO uses collateral eligibility to self-select the borrowers according to their perceived risks					
6. The eligibility of the Collateral obtained determines the nature of the loan and the measures of recovery					
7. Various forms of collateral are accepted by our SACCO					

SECTION C: Collateral Valuation and the Growth of SACCOs

Statement	**S.D**	D	**N.S**	A	**S.A**
1. Collateral value is considered to determine the loan amount					
2. The value of Collateral is monitored throughout the life of the transaction					
3. Collateral is valued using the latest available source or the historical performance of the collateral					
4. Collateral is valued depending on the quality of the loan					
5. The market value of collateral should be able to cover payment of the principle and accrued interest					
6. The collateral is valued by reliable, independent experts					
7. The worth and resale value of the collateral is considered					
8. Highly valued Collateral may make our SACCO become lazy to undertake sufficient screening of the borrowers					

SECTION D: Collateral Ownership and the Growth of SACCOs

Statement	S.D	D	N.S	A	S.A
1.The client must own the collateral presented to our SACCO					
2. Collateral ownership gives assurance to our SACCO regarding the safety of the loan given out					
3. Collateral ownership helps us to determine credit worthiness of the borrowers and also reduces the enforcement problems					
4. Borrowers who do not own Collateral are put in groups so as to access loan from our SACCO					
5. Savings deposits and members in the group substitute the Collateral needed by our SACCO					
6. The borrowers' past history, reputations and the owners' personal connections are considered in case there is no Collateral presented					
7. We encounter some problems from the requirement of Collateral to access loan					

Thank you for your cooperation.

APPENDIX II: KREJCIE AND MORGAN TABLE

N	S	N	S	N	S	N	S	N	S
10	10	100	80	280	162	800	260	2800	338
15	14	110	86	290	165	850	265	3000	341
20	19	120	92	300	169	900	269	3500	246
25	24	130	97	320	175	950	274	4000	351
30	28	140	103	340	181	1000	278	4500	351
35	32	150	108	360	186	1100	285	5000	357
40	36	160	113	380	181	1200	291	6000	361
45	40	180	118	400	196	1300	297	7000	364
50	44	190	123	420	201	1400	302	8000	367
55	48	200	127	440	205	1500	306	9000	368
60	52	210	132	460	210	1600	310	10000	373
65	56	220	136	480	214	1700	313	15000	375
70	59	230	140	500	217	1800	317	20000	377
75	63	240	144	550	225	1900	320	30000	379
80	66	250	148	600	234	2000	322	40000	380
85	70	260	152	650	242	2200	327	50000	381
90	73	270	155	700	248	2400	331	75000	382
95	76	270	159	750	256	2600	335	100000	384

Note: "N" is population size

"S" is sample size.

From : Krejcie, Robert V., Morgan, Daryle W., "Determining Sample Size for Research Activities", Educational and Psychological Measurement, 1970.

APPENDIX III: LETTER OF INTRODUCTION

Uganda
Martyrs
University

VIRTUTE ET SAPIENTIA
DUC MUNDUM
UGANDA MARTYRS UNIVERSITY

making a difference

Office of the Dean
Faculty of Business Administration and Management

Your ref.:
Our ref.:

Nkozi, 6th January, 2015

To Whom it may Concern

Dear Sir/Madam,

Re: Assistance for Research:

Greetings and best wishes from Uganda Martyrs University.

This is to introduce to you OKULLO DENIS who is a student of Uganda Martyrs University. As part of the requirements for the award of the Degree of Bachelor of Business Administration and Management of the University, the student is required to submit a dissertation which involves a field research on a selected case study such as a firm, governmental or non governmental organization, financial or other institutions.

The purpose of this letter is to request you permit and facilitate the student in this survey. Your support will be greatly appreciated.

Thank you in advance.

UGANDA MARTYRS UNIVERSITY
OFFICE OF THE DEAN
06 JAN 2015
FACULTY OF BUSINESS ADMINISTRATION & MANAGEMENT
SIGN:..........

Yours Sincerely,

Moses Kibrai
Dean

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