

An Analysis of the Unpredictable Factors Influencing Loan Default in Small Scale Enterprises in the Port Loko Municipality in Sierra Leone using the Fish Bone Diagram

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Abstract

The study shows that there are unpredictable factors influencing loan default in small-scale enterprises in Port Loko Municipality. A fishbone diagram which is a cause and effect tool was used to determine these factors. A brainstorming activity was used to get the views of participants with regard to the Research Question. The research question was to respond to a research objective which was "Are there unpredicted factors influencing loan default in small scale enterprises in Port Loko Municipality in Sierra Leone?". Reviews of necessary literature were done to aid the study. In the review, matters relating to loan default and possible causes were addressed. It is unfolded that there are some loan defaults that are as a result of the borrowers' lapses and others that are lender-oriented causes. The population size of one hundred and a random sample size of sixty people were used as participants to carry out the brainstorming activity. The population is comprised of small-scale enterprise owners and workers of credit or Microfinance institutions in the Municipality. Brainstorming participants proved that the death of clients or borrowers, internal insecurity, outbreak of diseases (Pandemic), Natural Disasters, and accident all significantly influence loan default of small-scale enterprises.

Keywords: *Brainstorm, Fishbone diagram, Loan default, and Unpredictable factors.*

Introduction of the Study

A study presents that in business operation, there are challenges that are foreseeable and others that are unpredictable [1]. Researcher [1] added that if businesses are to be successful, they should be mindful of matters that have a material impact on their viability.

There are unpredictable factors that trigger loan default for which this research work is designed to investigate.

A review on loan default presents loan default as the failure to do repayment of principal and interest [2]. According to [2], such a payment should be done within a specified period. In addition, borrowers will default on the loan if they fail to comply with loan conditions.

Studies on loan default submits that a loan default happens when repayment for a loan is not made as agreed [3]. It was made evident from studies that bad debt can be recovered or not [3]. Such a situation can lead the organization to further cost of recovering the debt through credit agencies. Bad debts reduce the credit score of client and future denial of credit facilities [3]. There are however factors that may lead the credit organization to write off the debts.

A study presents that a bad debt cannot be collected and that it is a credit risk borne by the organization [4]. Such a debt is an expense to the organization that reduces its profitability.

There is risk in doing business and such a risk should be calculated. Therefore, Credit

agencies must ensure they administer loans, complying with administrative strategies that minimize the excessive risk of default. Therefore, staff knowledge and compliance with credit and ethical issues in loan administration should be strong. The closure of some credit agencies is as a result of their incompetence in dealing with credit matters. There are, however unpredictable factors that goes beyond the imaginations of the clients and credit agencies. In dealing with unpredictable and predictable factors, some credit agencies do provisions of bad and doubtful debts. These provisions are estimates made that a portion of debt shall not be recovered. If this provision is low compared to a prevailing circumstance in a year, then this is an additional expenditure on the side of the credit agency leading to a total reduction in profitability. On the contrary, if provision is high, compared to prevailing circumstances, then this is an additional gain to the business. These factors totally crumple both credit agencies and clients. This publication investigates the unpredictable factors that influence loan default in small-scale enterprises by making use of an old-aged tool that aims at efficiency known as the fishbone diagram.

Objective of the Studies

The following are the objectives of the study:

1. To use the fishbone diagram to analyze the unpredicted factors influencing loan default in small-scale enterprises in Port Loko municipality in Sierra Leone.
2. To give a possible recommendation to the study.

Research Questions

Are there unpredicted factors influencing loan default in small-scale enterprises in Port Loko Municipality in Sierra Leone?

Hypothesis of the Study

The study shall include hypotheses that there are unpredictable factors influencing loan

default in small scale enterprises in Port Loko Municipality in Sierra Leone.

Delimitation of the Study

Studies have been centered on the causes and effects of loan default without a thorough look at factors that gives rise to provision for bad debt for small scale enterprises. This study looks at the unpredictable factors that influences loan default in small scale enterprises in the Port Loko Municipality in Sierra Leone.

Problem Statement

Credit default is a major concern for credit agencies. The portfolio can be at total risk when debtors fail to meet their debt obligations. The terms of the loan are guiding tools for both the credit agency and the clients. Failure to comply with terms stages the issue of default. In accounting, debt that is not collected is known as a bad debt and this affects the profitability of the credit agency and the goodwill and going concern of the debtor. Unpredictable factors that influence loan default impact the credit agency and the debtor's enterprise in a very negative way. These factors render faithful debtors' default as they affect either the internal environment of the client or the external environment of the enterprise. These factors have violated the going concern principles of both credit agencies and the debtors or clients. Some Agencies close down because of the high rate of defaults from debtors. On the other hand, enterprises of clients close down because of total default and loss of properties to settle debts. For this reason, a study on these unpredictable factors is carried out to serve as a guide to both credit agencies and debtors of small-scale businesses.

Justification of the Study

There are factors that hinder loan repayment by clients. Some of these factors are the negligence of the Clients to pay and others caused by the credit agencies. Issues like loan

diversion, mismanagement of funds, and lack of business management techniques are all flaws on the part of the debtors or clients. On the other hand, bribe taken to administer loan to an unqualified client, poor screening, high cost of the loan is all flaw of the credit agencies.

The study on unpredicted factors influencing loan default in small-scale enterprises presents brainstorming feedback that will help credit agencies in doing an estimate for provisions for bad and doubtful debts. This will help them from business insolvency or closure as these forces can default a host of clients in a single day.

It will also alert loan debtors that there are probabilities of haven been default because of unpredictable factors. This may either lead to the closure of the enterprise and personal properties. The findings of this work will help other researchers in a similar field to adopt ideas for desired goals that may be individual or collective.

Literature Review

A study presents unemployment and poverty as the two main challenging factors affecting the world economy [5]. The researcher presents that both factors lead to financial crisis and hence reduces the overall purchasing capacity of a nation followed by an increase in debt [5]. In detail view, [5] revealed poverty as a financial condition where people are unable to maintain the minimum standard of living.

Job creation is a possible way to help minimize the high rate of unemployment and hence improve on the standard of living of people.

Studies revealed that entrepreneurs are known to be job creators and wage growers [6]. In the review of [6], it was explained that there are approaches of entrepreneurship of which self-employment is one. These self-employment activities are in small businesses.

In the work of [7], a small business is defined as a business that is independently owned and operated, not dominated in its field

of operation, and meets a certain standard of a number of employees and capital.

In a study on the role of the private sector, it was said that the private sector is the engine of growth and that Successful businesses drive growth, create jobs, and pay the taxes that finance services and investment [8].

Studies on the public and private sectors defined a private sector as one owned and managed by private people [9]. According to [9], such a business focuses on entrepreneurial activities, taking the risk to create jobs and generate profit.

It is now made evident that the private sector contributes immensely towards the reduction of the unemployed population by providing job opportunities and hence a booster of the nation's economy.

Studies of [10] submit that small and medium enterprises are driving forces towards economic growth but are constrained because access to finance is the major problem from banks because of rigid conditions for loan acquisition.

The Micro Finance Institutions and other credit Agencies aim at providing capital to empower borrowers for business ventures. This loan is at a designed condition that should be the terms and conditions of the lender. Loan default occurs when the borrower fails to comply with agreed terms and conditions.

Studies on loan default defined default as a situation where a debtor fails to meet his or her debt obligation [11]. Further, classifications of loan default were made as follows review on loan default as: sovereign default, orderly default, strategic default, consumer default, and sovereign strategic default [11]. Some debts become default because of a failure to pay the whole sum within a stipulated date. When a loan becomes the default, it is said to be a bad debt.

It is made known in a study that a debtor who cannot pay his or her debt is a bad debtor, and the debt owing is referred to as bad debt [12]. Credit agencies treat the default as bad

debts, and organizations usually make provisions for bad debts.

A study defines bad debts as debts not collectable or recoverable [12]. Further, doubtful debts were viewed [12] as debts that can be recoverable or cannot be ascertained at the date of preparing the financial statement. In simple words, doubtful debts are seen as debts which are doubtful to realize. Detail review on the Provision of bad debt makes it clear that provision for bad debt is a reserve made to an estimated percentage of total debt and doubtful debts that should be written off in a year [12]. According to [12], such a write-off is a loss as it appears as an expense in the Profit and Loss account during the year as provision.

A study presents provision for doubtful debt as the estimated amount of bad debt that will arise from accounts receivable that have been issued but not yet collected [13]. Further disclosure shows that the accrual basis accounts for provisions for bad and doubtful debts [13].

An International Accounting Standard Board lists two assumptions that must be applied to meet their objectives [14]. These Assumptions are the accrual basis or accrual concept and the going concern concept [14].

Our concern in this study is the accrual basis or accrual concept. Studies explain that in the accrual basis, the effects of transactions and other events are recognized when they occur. They are recorded in the books and reported in the financial statement of the period to which they relate [15]. In summary, [15], opinion about the accrual basis is that all income and charges relating to the financial period to which the financial statement relates should be taken into account with regard to the date of receipt or payment. Provisions for bad debts and other provisions should be noted in the calculation of accounting profit [15].

Under a favorable economic climate, where conditions are favorable, and clients are willing to do their payments as they fall due, there will be less default, and the organization will actualize an increase in revenue. But in adverse

economic conditions, clients will struggle to do repayment, and hence many will fall into default. This, in turn, will reduce profit-making.

A study disclosed that loan default could be as a result of the socio-economic factors of borrowers [16]. These factors included: family size and family living expenses [16]. Further review [16] showed that defaults can be as a result of poor management procedure, loan diversion, and unwillingness of the clients to repay. The following were reported to be the possible cause from the side of management that may lead to default [16]:

1. Interest rate ceilings are usually imposed by the government.
2. Monopoly power in credit markets often exercised by informal lenders.
3. Large transaction costs incurred by borrowers in applying for loans.
4. Moral hazard problems.

Various researchers have used diverse research tools to investigate what the causes of loan defaults are. Some of these causes are predictable causes during business operations. This research work is to investigate the unpredictable causes of loan default using a fishbone diagram.

A study defines the fishbone diagram as a cause-and-effect diagram that is also known as the Ishikawa diagram that shows potential causes of a specific event [17]. Researcher [17] highlighted the common use of the cause-and-effect diagram. Common product design and quality defect prevention were used to identify potential factors causing an overall effect [17].

Delved in the study of the fish bone diagram, it was explained that each cause or reason for imperfection is a source of variation, and these Causes are grouped to identify and classify these sources of variation [17].

From the submission above, it is clear that a fishbone diagram is a problem-finding tool. Such a tool is useful in organizations as solutions to problems can only be seen when

emanating problems or causes are identified.

Below is a diagram depicting a fishbone.

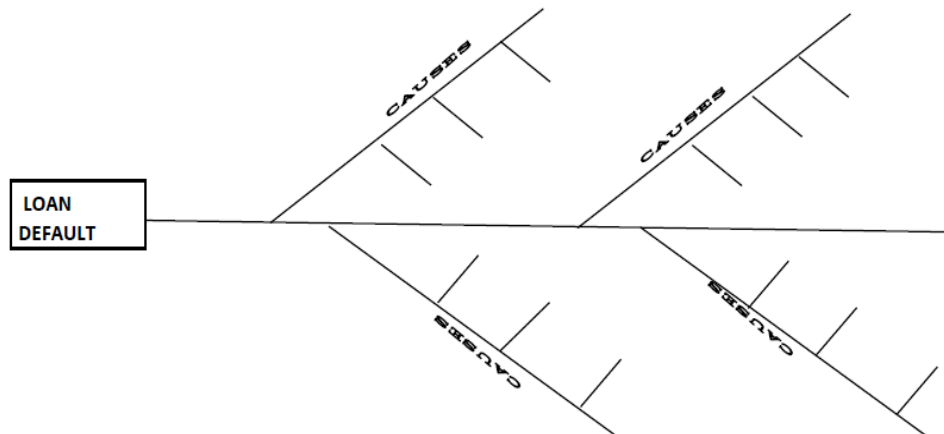


Figure 1. A Fishbone Diagram

Fishbone Diagram

The above diagram depicts a fishbone diagram. The diagram shows the head of the fish, which is seen as the effect, and the bones showing the causes. Some causes have root causes. This tool is a brainstorming tool that is very effective in problem solving and identification. Therefore, such a tool will be used to know and analyze the unpredictable factors influencing loan default in small-scale enterprises in Port Loko Municipality in Sierra Leone, West Africa.

Research Methodology

Research Methodology is presented as the practical how of any given piece of research [18]. Further view submits that it is how a researcher systematically designs a study to ensure valid and reliable results that address the research aims and objectives [18].

Simply, research methodology refers to the ways adopted to systematically collect data and analyzing methods that will enable valid conclusions and recommendations. This includes the design of research, sources of data collection, and framework of analysis.

Study Area

Port Loko City is the district headquarter town of the Port Loko District. It has eleven chiefdoms. The district administrative activities are done in Port Loko City. The town is large in Population. The inhabitants are mainly of the Themne tribe, although there are other tribes inhabiting the town. Occupationally, the people are petty traders and some of the agriculture sector. Some are in other services, but all contribute towards the development of the district. There are schools and institutions of higher learning. The people belong to a different faith and socially interact with themselves.

Study Population

This population relates to owners of small-scale businesses in Sierra Leone with respect to the Port Loko Municipality. It shall entail both men and women present and those out of business. Also, some administrative staff of Micro Finance Institution shall be part of the study.

Population Size

The population size shall be a one hundred brainstorming participants.

Sampling Method

The sampling method is the random sampling method. Samples of existing and former clients will be selected randomly. The sample size shall be 60 small-scale business owners' inclusive staff members of Micro Finance Institutions.

Data Collection Method

Primary Research

Data will be collected that be via a brainstorming activity where participants will respond to the research question of the study. The fishbone diagram shall be used to know

unpredictable factors that influence loan default in small-scale enterprises.

Secondary Research

This involves the use of what others have done similar to the study to be carried out. It is the review of work from textbooks and electronic source.

Data Analysis

Data will be analyzed using a table and a fishbone diagram also, qualitative presentations were done reflecting the views of participants with a regards research question.

Results

A brainstorming activity was carried out to know the unpredictable causes of loan default in small-scale enterprises in Port Loko Municipality. The table below shows the sex distribution of participants in the discussion.

Table 1. The Sex Distribution of Brainstorming Participants

No	Sex	Number of Participants
1	Female	40
2	Male	20
Total		60

Source: Self Designed 2021

Four brainstorming activities were carried out. There were a total number of fifteen participants per group.

From brainstorming activities, the participant brought the following as unpredictable causes of loan default in small scale enterprises in Port Loko Municipality in Sierra Leone:

Finding One – the Death of the Client

This is one of the causes that is discussed in the brainstorming activity with regard Research objective. It was discussed in the fishbone diagram that the death of a borrower is an unpredictable cause of loan default. Some members said that this can only be a default, provided it is a single loan. For a group loan, the death of a group member does not mean a

loan default as other group members are liable to do the repayment.

Finding Two – the Outbreak of Diseases

The outbreak of pandemic diseases is another cause of loan default discussed among brainstorming participants. Sierra Leone has experienced two solid outbreaks of the pandemic that greatly disturbed the nation. Businesses were greatly affected. Ebola and Covid 19 are serious pandemics that gravely disturbed the business sector and the other sectors of the country.

Finding Three – Internal Insecurity

Issues of security matters were brainstormed that have led to the default of some borrowers. This is also an unpredictable factor for loan default. Port Loko Municipality is greatly

disturbed by the activities of thieves. The breaking of houses, killing, and looting of properties is still an issue of concern. A forceful default takes place when thieves break shops and loot properties.

Finding Four - Accident

Accidents of all sorts disturb businesses. Accidents are unpredictable factors that influence loan default. A fire accident burnt down over ten business sites in Port Loko. It was reported that over twenty businessmen and women were involved. The majority of these small-scale business owners were clients of Microfinance Institutions. This was a forceful default as all their shops and belongings were burnt down.

Finding Five - Natural Disaster

Sierra Leone as a country has experienced landslide and flooding as natural disasters. Many parts of the country experienced flooding, including the Port Loko district. Therefore, flooded areas with the operations of Microfinance should expect they lost of properties and lives. Therefore, loan default becomes possible.

Discussions

A Study presents those risks are always part of businesses and that business risks implies uncertainties in profit or danger or loss and the events that could pose a risk due to some unforeseen events in the future which causes business failure [19].

From the findings above, one can note that there are unpredictable factors that cause loan default. Though organizations make provisions for doubtful debts, which will eventually reduce their profitability, enormous defaults threatened their going concern it is unprecedented. Factors like death leaves a business closed when it has no succession plan. Pandemic and other natural causes are also issues discussed that lead to loan default.

The Government should have plans to strengthen this sector. Training programs and financial subsidies can aid in the crisis period.

Summary, Recommendations and Conclusions

Summary

The research work focused on analyzing the unpredictable factors that influence loan default in small-scale enterprises in Port Loko Municipality in Sierra Leone. A fishbone diagram was used to do the cause-and-effect studies. The fishbone diagram uses a brainstorming technique to know the views of participants with regard to the research question. From the study, the hypothesis of the study was confirmed that there are unpredictable factors influencing loan default in small-scale enterprises in Sierra Leone. The following were the derived factors.

1. The death of the client
2. The outbreak of diseases as in the case of Ebola and Covid 19
3. Internal Insecurity – thievery
4. Accident
5. Natural Disaster

Recommendations

The following recommendations were reached for the studies:

1. The Death of a Client – The loan is seen to be the default when it is a personal loan, but group loans will not be default as other members of the group are obliged to do the repayment upon the death of one. It was therefore recommended that since death is an unpredictable default factor, Micro Finance Institutions should promote group businesses to avoid default upon the death of one client. The issue of Partnership should be promoted as there are many limitations of the sole trader type of business.
2. The outbreak of the Pandemic – this is a crucial issue as it occurs in human history.

The issue of the pandemic has claimed the lives of many people, including business people. Ebola claimed the lives of many in Sierra Leone. Covid 19 has also claimed lives, slowed down, and even closed down some businesses. As this cause is beyond human thinking and control, Lenders should make provisions for bad and doubtful debts. Also, there should be a bailout strategy by the national Government like the Munafa Fund in Sierra Leone. This can help those affected by the pandemic to continue their businesses.

3. Internal Insecurity is an issue with the Municipality of Port Loko. The use of guns and harmful weapons are rampant with the community. Some business persons damaged and others lost of a huge sum of working capital. A death case is reported to the regional division, and many grabbing of bikes and properties of citizens and of businessmen. This is a very serious problem prompts the default of the loan. The government should be aware that the crime rate within the district is at an increase, and therefore, measures should be in place to protect the inhabitants of the community. There should be a correct policing and legal system within the municipality to address robbery and burglary as they arise.
4. A natural disaster like flooding is common in Sierra Leone. For the study area, this is not so common. However, Measures that prevent happens of some of these disasters should be in place by businessmen to avoid loss of life and properties.
5. Accidents – Accidents either by road, sea, or fire are all unpredictable causes of loan default. In the brainstorming activity, it was revealed by a participant that a fire accident destroyed shops and many commodities of small-scale retailers. It is therefore recommended that for unseen circumstances, small-scale retailer should cover their businesses through insurance.

Massive sensitization should be done to educate business owners about the importance of insurance.

Work on uncertainties reveals that there are many uncertainties of which businesses require cover [20]. Further, [20] noted of the outbreak of diseases and other unpredictable causes. In addition, the relevance of insurance was presented by the researcher as a risk management technique that ensures an optimal risk-return relation through a variety of available risk management methods [20].

From this, we can see that insurance can play a very vital role towards uncertainties.

Conclusion

Research work has made it evident that there are unpredictable factors that influence loan default in small-scale enterprises in Port Loko Municipality. All these causes stand significant in influencing loan default. However, precautionary measures can be used to prevent or combat a fire accident when it arises. Also, insurance cover can help restore a businessman when in a condition that was insured for. Finally, we should be aware that these causes are beyond human control from occurrence, and therefore, organizations should do provisions to embrace loan defaults when they arise because of these unpredictable factors.

Conflict of Interest

The financial acquisition is a problem to many in Sierra Leone. Therefore, to raise capital for a business venture is truly a problem. Many want to have access to the facilities of formal banks but do not want to do savings with these banks. So having control of their finances and at the same time have interest in the facilities of these banks is conflicting. On the other hand, clients want their finances secured but do not want to save their monies in the banks nor be part of insurance companies.

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