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Evaluation of Credit Management and its Effect on Performance of Rural Banks in Ghana: A Case Study of Adansi Rural Bank Ltd. Fomena-Ashanti

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DECLARATION

I hereby declare that the submission of this thesis is my own work towards the award of Master of Business Administration (MBA) under the supervision of Dr. Kofi Poku. It contains no materials published previously by another person or material which has been accepted for the award of any other degree of the university, except where due acknowledgment has been made in the text.

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DEDICATION

This work is graciously dedicated to my lovely father and family, Ms. Patricia Owusu, Maxine Addai-Noughton, Mercy Boafo, Mr. Michael Asamani-Darko and the entire credit staff of Adansi Rural Bank Ltd.

ABSTRACT

The establishment of rural banks in Ghana in 1976 became crucial in response to make financial services and credits available to the majority of rural dwellers and hence, boost their economic activities. The sector has seen some improved banking operational performance, some new and dynamic innovations, and increases in efficiency to some extent in a way better than previously imagined and perceived by the Ghanaian populace. However, some rural banks are seen as the department of the banking industry that encounter all levels of credit and financial risks, due to poor credit management practices prevailing in the sector, hence, affecting their profitability and creating liquidity problems. The purpose of this study was to examine the credit management and its effect on performance of rural banks in Ghana, using Adansi Rural Bank Limited as a case study institution.

The study was conducted using both primary and secondary data. Primary data was collected through questionnaires from credit managers/officers of the bank. In addition, secondary data in the form of financial ratios of the bank was used to support the study. Descriptive statistics and regression analysis were the main data analysis techniques employed. The findings indicated 44.5% of the variations in the financial performance of Adansi Rural Bank Limited are explained by credit management practices such as credit appraisal, credit disbursement and credit and collection techniques and. Also, the F-statistics of 44.5 which is significant at 1% (sig≤0.01) indicated that credit management has significant impact on the performance of the bank. The study further revealed that the main factors causing loan default are laxity in loan monitoring, diversion of credit on the part of customers and customer business failure. The result also showed that the bank has been performing creditably well in the area of credit management through effective appraisal system and efficient recovery strategy.

The study recommends that the rural banks must improve their monitoring practices since the major cause of loan default is diversion of funds. Furthermore, the study recommends that the banks should provide non-financial services in the form of training and business advice to their customers. This will go a long way to improve their business performance and enhance their ability to repay their loans.

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LIST OF ABREVIATIONS

ARB-Apex	Association of Rural Banks-Apex
BoG	Bank of Ghana
Olem	Other Loans Exceptionally Mentioned
ROE	Return on Equity
ROA	Return on Assets
NPLR	Non-Performing Loans Ratio
LLP	Loan Loss Provisions
GLA	Gross Loans/Advances
CAR	Capital Adequacy Ratio
LDR	Loans to Deposits Ratio
CRDAPPR	Credit Appraisal
CRDDIB	Credit Disbursement
CRDMONCOL	Credit Monitoring and Collection

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CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The establishment of rural banks began in 1976 by the Central Bank of Ghana. The move was in response to make financial services and credits available to the majority of rural dwellers and hence, boost their economic activities.

Asiedu-Mante (2011) indicated that the main operators during that period it was only agencies of commercial bank, cooperative credit unions as well as informal financial operators. According to the author, a number of Ghanaian populace, especially non-literate and less affluent in the rural areas lost the courage to step foot in those building and in effect did not get access to institutional credit and other forms of financial services. These people were eventually, peasant farmers who largely depended on moneylenders with higher interest charges. Loans and other forms of credit facilities constitute the largest proportion of assets in rural banks. The interest incomes generated from these credit facilities form more than 50% of total income earned in every financial year (Bank of Ghana, 2004).

Credit can be an arrangement whereby an institution or an individual is required to undertake an obligation or to commit funds directly or indirectly to another party and the party to whom or whose behalf the funds have been given or the obligation has been undertaken is required to repay in accordance with agreed terms of arrangement with interest. Glen Bullivant (2012) underscored that the key issues of credit management control comprise guidance on credit policy, and management of credit functions, credit terms, credit risk management, debt collections and other relevant credit services. This means that good and appropriate measures in credit management eases banks to reduce the quantum of funds held by debtors, and also minimize credit risk or bad debts. The introduction of rural banking in Ghana became essential in promoting localities by extending credits to the rural folks to foster community and national development at large. Asiedu-Mantse (2011) indicated that credit management basically begins by establishing standard policies and procedures that will ensure that qualified authorities grant credit, the credit goes to the right people, the credit is granted for the productive activities or for businesses which are economically and technically viable, the appropriate size of credit is granted, the credit is recoverable and there is adequate flow of management information within the organization to monitor the credit activity.

1.2 Problem Statement

The banking activities had evolved rapidly over the years and particularly in the past decade. The rural banking sector has seen improved banking operational performance, new and some dynamic innovations, and increases in efficiency to some extent in a way better than previously imagined and perceived by the Ghanaian populace. Granting of loans and other forms of credit facilities requires huge commitment of funds. The rationale of good credit risk management is to minimize the probable losses and maximizing shareholders returns. Michael Asamani-Darko (Personal Communication), however, reveals that some rural banks are seen as the department of the banking industry that encounter all levels of credit and financial risks, due to poor credit management practices prevailing in the sector, hence, affecting their profitability and creating liquidity problems. Some of the rural banks lend to the people with virtually insufficient or without security against such credits. As noted, lending funds meant for depositors of the bank to potential customers with poor standing of credit history or cannot offer substantial security, can be dangerous, expensive and contains high credit risk to the lending bank. This research work therefore seeks to investigate how Adansi Rural Bank Limited is effectively managing its credit activities for maxim income generation.

1.3 Objective of the Study

The area of study seeks:

1. To assess credit management practices of Adansi Rural Bank Limited in the area of credits offered, loan appraisal processes, disbursement, etc
2. To assess the factors contributing to credit risks in rural banking system.
3. To investigate the performance of Adansi Rural Bank Ltd in the area of profitability and liquidity from 2010-2014
4. To investigate the effect of credit management on Rural Banks' performance.

1.4 Research Questions

Below questions were posed by the researcher to enhance achieving the set objectives:

1. What credit management practices prevail at Adansi Rural Bank Limited?
2. What are the factors of credit risk associated with Rural Banks?
3. What is the performance of Adansi Rural Bank Ltd in areas of profitability and liquidity? 4. What are the possible effects on credit risk management practices on Rural Banks performance?

1.5 Significance of the Study

This study would be beneficial to various stakeholders to ensure spearheading of effective credit risk management in Rural Banks. Since there is no difference in rural banking structure and operational system in the country, it is imperative that the study will provide an indication on how the credit risk management standards prevails in the banking sector, particularly, Rural Banks in Ghana. The research work will supplement stock of knowledge on credit risk management and its effect on performance of rural banks in Ghana.

Simultaneously, it will provide a guide for further studies for other researchers who may write similar topic in the industry.

1.6 Scope of the Study

The study focused on the last five years financial statements, credit reports and other disclosures contained in the credit policy of Adansi Rural Bank Limited since all rural banks in Ghana are under one umbrella and have the same structures and procedures. Other literatures and past research works similar to this work shall be consulted to give a fair knowledge on the study.

1.7 Brief Overview of the Research Methodology

The source of data shall be employed from both secondary and primary data. Secondary data will be obtained through a comprehensive review of documentations by other researchers, credit policy manual, the bank's credit books and other problem loans files. Primary data will be sourced from respondents (senior managers, credit manager, credit staff and customers). The instrument to be used shall mainly be interviews and questionnaires. The research design to be used in the study is descriptive survey. This is intended to analyze and report on the way things are done in the bank. The design will be used to describe the credit risk management practices of Adansi Rural Bank Ltd and to recommend some of the best practices to help improve the system.

1.8 Limitation of the Study

The major limitations that were encountered in undertaking this research work are that;

The case study as a research design had its limitation in using its findings for complete generalization since only one rural bank cannot be used to represent the sector as a whole. In this case the credit risk management and its effects on the performance of Adansi Rural Bank Limited, Fomena could not be used to generalize the risk management activities pertaining in all rural banks nationwide. To reduce this limitation, varied literature works were widely consulted as references to issues being discussed which are relevance to other rural banks across the country.

There was a constraint in accessing secondary data because of the confidentiality of financial information to both customers and researchers. However, the researcher's relationship as a staff of the bank and a written formal letter that served as evidence for academic purpose assisted in accessing the information. Finally, time and financial constraints posed a challenge for the researcher in completing this work. These were in the areas of money spent on telephone calls, printing questionnaire and works, travelling to head office, typewriters and other miscellaneous costs.

1.9 Organization of the Study

This study appears mainly in five (5) chapters. The first chapter comprises research background, problem statement, objectives of the study, research questions, significance of the study, scope and limitations, significance of the study and organization of the study. Chapter two discusses the existing literatures on the subject matter. It also includes other theoretical and relevant topical issues to the study. The chapter three focuses on methodology for assessing the bank, and this includes choice of population, sampling size and appropriate methods, research instruments to be used for collecting relevant data and major limitation posed in data collection. Chapter four of this research will analyze data obtained from the bank. Presentation in graphical and pictorial formats would aid in appreciation of the research. The chapter five is based on summary, proposed recommendations and conclusion based on the assessment done.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The major challenges in banking continue to exist between the lender and the borrower. However, a prudent effort in credit risk management has become vital catalyst of a detailed process to credit management and also ingredient to the long-term sustainability of any banking operation (Basle Committee on Banking Supervision, September 2000). The chapter seeks to review the literature on inherent risk in management of rural banks. It discusses issues on the aims and roles of rural banks establishment, credit types offered by rural banks, credit risk and its causes, effective credit risk practices and its effect on rural banking as well other relevant credit related issues essential to the study.

2.2 The Role of Rural Banks

The intermediation role of the banks is transforming savings received from households into credit for business firms and others in order to make investments in buildings, equipment and other assets (Rose, 1999).The establishment of Rural Banks in Ghana began since 1976 intended to provide banking services to the rural population, improving loans accessibility to the individual into small-scale farming and businesses whilst supporting other developmental projects in such areas. The first of its kind was in AgonaNyakrom in the Central Region of Ghana. Rural Banks are owned and managed by the local people in their respective communities. The supervision of Rural Banks lies under the authority of ARB Apex Bank as mandated by Bank of Ghana. (BoG)

Rural and Community Banks were created in the country to basically become main drivers for financial intermediation, sources of funds and means to retain rural community dwellers. The banks provide a mix of micro-finance and commercial banking products designed to stimulate satisfaction to the needs of rural population. The services these banks provide are mobilizing deposits and channeling such funds into credit facilities to cottage industry operators, farmers, fishermen and salaried employees of various organizations in their catchment areas. Today, the number of Rural Banks had increased to One-Hundred and Thirty-Seven (137) with over 650 branches across the country. (www.arbapexbank.com/rcbs).

In December 2006, rural banks had mobilized GH₵226.46million deposits from two (2) million customers which represented 7.6% of the total deposits in the banking industry in Ghana. In the same period, loans and advances granted were GH₵115.10 million. The loans to deposits ratio was 50.83 percent. (Ghana Market Watch, 2007)

2.3 Concepts of Credit Management in Banking

The activity of credit has become so imperative in today's banking environments and creates wealth provided it is well managed. If credit freezes, almost every activity in the banking operations, businesses and the economy as a whole are affected. The best way to utilize credit and get positive results is understand the credit practices and properly managing the risks involved. Small Business Development Corporation defined credit management as the process of controlling and collecting payments from customers (debtors). This means that a good credit administration and practice will help banks decrease the amount of funds held by debtors, and also minimize exposure of credit risk or bad debts. (www.smallbusiness.wa.gov.au)

The Institute of Credit Management established that credit management is comprehensive and it's a guide to improving organizational profits and cash flows through proper planning, motivation and control. Glen Bullivant (2012) underscored that the key issues of credit management control comprise guidance on credit policy, and management of credit functions, credit terms, credit risk management, debt collections and other relevant credit services.Asiedu-Mantse (2011) indicated that credit management basically begins by establishing standard policies and procedures that will ensure that qualified authorities grant credit, the credit goes to the right people, the credit is granted for the productive activities or for businesses which are economically and technically viable, the appropriate size of credit is granted, the credit is recoverable and there is adequate flow of management information within the organization to monitor the credit activity.

Generally, credit management in rural banks covers the diverse field of credit related areas, from receiving applications, granting loan requests to managing the credit options of businesses and individuals to monitoring and collection of delinquent debts.

2.3.1 Credit Application

The first and foremost step a potential client can assess credit in rural banks is to tender a loan application request. A credit application is usually made in writing by the potential borrower or by filling the bank's own standard application form. This must contain relevant information such as applicant's name, account number, amount of request, and purpose of the request, duration, source of repayment and others which should be duly signed or thumb printed by the applicant.

2.3.2 Credit Appraisal Processes

All credit applications are received by the manager of a branch and then referred to the credit officer of the branch. The credit officer then begins the appraisal process byscrutinizing the applications as to whether the applicants have the capacity to borrow or not from the bank. According to Asiedu-Mante (2011), the credit appraisal reveals the relationship of the borrower with the bank, financial and economic viability of the intended project. The Credit Officer then writes his/her appraisal report with recommendations to the Credit Manager for his comments. When the loan request is within the manager's limit, he approves it. If it is beyond his limit, the request is forwarded to other sanctioning authorities for approval and other higher amount of requests to the board of directors for approval at its meetings.

2.3.3 Credit Disbursement

Before a disbursement is initiated after approval, an offer and acceptance consent is written to the prospective borrower. The content of such letter contains areas as approved amount, the purpose of the credit, repayment period, interest rate and other charges, duration for credit repayment, security and post disbursement terms and conditions to the satisfaction of the customer. These approval letters are written by the Credit Manager at the credit department in line with Board's decision on the approved loan to be signed by two approving authorities. The letters are later released to the respective branch for the customer to read, understand and sign for his/her acceptance before disbursement is made by the branch credit officer.

2.3.4 Credit Monitoring and Collection Techniques

According to the Guidelines for Commercial Banks for Pakistan Banks, banks need to enunciate a system that enables them to monitor thequality of credit portfolio on day-to-day basis and take remedial measures as and when any deterioration occurs. Such a system would enable a bank to ascertain whether loans are being serviced as per facility terms, the adequacy of provisions, the overall risk profile is within limits established by management and compliance of regulatory limits.Asiedu-Mantse (2011) reveals that establishing an efficient and effective credit collection system would help senior management to monitor the overall quality of the total credit portfolio and its trends. Consequently the management could fine tune or reassess its credit strategy /policy accordingly before encounteringany major setback.

The author stressed that banks credit policy should explicitly provide procedural guideline relating to credit risk monitoring. At the minimum, it should lay down procedure relating to: the roles and responsibilities of individuals officers responsible for credit risk monitoring, assessment of procedures and techniques analysis for individual loans &overall portfolio, frequency of monitoring, the periodic examination of collaterals and loan covenants, the frequency of site visits to loan customers and the identification of any deterioration in loans, if any.

Asamani-Darko (personal communication) revealed that the monitoring of credit lies with the credit officers at the various branches. In addition, recovery officers are given additional responsibility to ensure that loans are well monitored and those are in default category. The information gathered on the monitoring process is further transferred to the credit manger of the branch. The credit manager reviews and evaluates the monthly portfolio reports and identifies non-performing loans and past dues for immediate attention.

2.4 Credits in Rural Banks

Ciby Joseph (2013) stressed that credit is seen as an exchange of transactions between two parties whereby one party (lender) grants funds in exchange for a promise for future payment by the other party (borrower). In his view, such transactions normally include the payment of interest together with principal to the lender.Asiedu – Mante (2011) also asserted that credit is an arrangement whereby an institution or an individual is required to undertake an obligation or to commit funds directly or indirectly to another party and the party to whom or whose behalf the funds have been given or the obligation has been undertaken is required to repay in accordance with agreed terms of arrangement with interest. The author underscored that credit facilities offered by the rural banks can be put under two broad headings, i.e.

Loans and Overdrafts.

2.4.1 Overdrafts

Overdraft is one of the means through which banks lend money to their respective customers. This occurs when a customer is allowed to withdraw in excess of funds from his or her account upon agreement with the Bank for a specific period of time. This type of credit is granted to commercial customers of the bank and it is granted on medium-term basis when the necessary arrangements between the authorities of the bank and the customer have been agreed upon. Interest could be charged on the facility by using the product approach or final debit balance standing in the account. The bank allows customers to provide security and this applies only to commercial applicants. An overdrawn account is subject to an interest charge depending on interest rate of the bank at a particular time.

The short-term overdraft which comes in the form of salary advance is another type of overdraft which is solely given to salary customers. Overdraft is given to only current account holders who qualify by satisfying all the necessary credit conditions. (Adansi Rural Bank Credit Policy Manual, 2014)

2.4.2 Loans

Asamani-Darko (Personal Communication) stressed that a bank loan is created when an agreed sum of amount has been credited to the applicant's account and debited to his loan account. This is done when an application for the loan has been appraised and approved by a higher authority when the necessary documents have been satisfied and the customer agreeing to the necessary credit conditions of the bank. Interest is paid on the amount granted and mostly repayment is on monthly basis. Repayment could be made semi-annually or the total amount and interest are paid at the end of the expiry period depending on the policy of the bank. Asiedu – Mantse (2011) indicated that loans offered by Rural Banks can be sub-divided into; Salary/Pension Loans, Susu Loans, Commercial Loans, School Fees Loans, Funeral Loans, Micro-Finance Loans, etc

2.5 Credit Risks Associated with Rural Banks

Credit is good if used and a prudentially by both parties. Nevertheless, several situations account for both lenders and borrowers suffering because of credit. These could be amounted to poor credit risk analysis and management of such risks. Sylvian et al (2013) defined credit risk as the probability of lender losing money due to the inability, unwillingness or nontimeliness of a counterparty to fulfill his financial obligations. The authors underscored that whenever there is a chance that the counterparty will not pay an amount of money owed, of fails to honor his financial commitment, there is credit risk. Ciby Joseph (2013) indicated that credit risk arise on the probability that the borrower (corporate or individual) may default on obligations. The author expressed that a borrower is responsible in the debt service obligations and should be aware of the consequences of the borrowing.

Casu et al (2006) also defines credit risk as the risk of reduction in the credit position of counterparty. The authors again spotted that credit risk is accompanied with traditional lending activities of banks and this can simply be deduced as loss of non-repayment either partly or wholly. They also stressed that loans and advances are the obvious sources of credit risk. The authors stressed that to reduce credit exposure; banks can limit the amount available to a certain class of borrowers. McNaughton (1999) explained that banks probably inherent Credit Risk immediately they act as intermediaries, and credit risk management lies at the heart of commercial banking. The author said; 'the business of banking is credit and credit is primarily the basis of which banks' quality and performance are judged'. She underscored that the ultimate harm in extending credits is that there is probability that the borrower may refuse to repay the loan when they fall due. She further stressed that credit risk has a negative effect on liquidity, and can bring about severe financial crisis, resulting in loss of capital, insolvency and liquidation of banks.

Marques (2010) also defines credit risk as the risk of probable default that may occur as a result of the inability of a business partner of a bank, known as counterparty to reimburse a loan when it is due. For instance, if a bank is expected a counterparty to reimburse

GH₵20,000.00 amount of loan on a specified date, and the counterparty fails to provide funds, the bank automatically incurs a risk of credit loss. He further stated that an effective credit risk practice or management helps put in place a bank's comprehensive and functional credit risk identification and reporting controls. In effect, this means that if payment is delayed or not made at all as stipulated it can adversely affect bank's profitability and also create liquidity problems. High credit risks continues to pertain in rural banks and amongst some contributing factors are further discussed below;

2.5.1 Cost of Borrowing

The Central Bank in early 1990's was the sole regulator of interest rates and, further fixed interest rate for banks which was to be complied by all banks. This system was later refuted prior to the pre-liberalization period and opened a door for the banks to determine their interest rates based on market forces and other macroeconomic conditions. Stiglits (1987) is of the view that interest rates on loans or credit facilities should be higher, if the probability of default is higher. The higher the risk of probable loss the higher the interest rate would attract. Businesses or banks whose operations increases risk of loan repayment therefore attract higher interest rates. This situation may be beneficial to the bank in the initial stage, however, in most cases tends to increase or intensify default rate, since charging higher rates increases cost of operations and eventually affect business sustainability.

2.5.2 Credit Worthiness of Borrowers

Rose (1999) indicated that the assessment tools of credit worthiness, which credit analysts respond to pre-lending safeguards, are – character, capacity, cash, collateral, conditions and controls. Ritter et al (2010) indicated that credit risk arises because some potential borrowers may not be able to pay back their loans due to the fact that they are unable to assess the risk of the borrower and where their performance is also difficult to monitor. Such loans are characterized by the nature of information asymmetry problems of adverse selection and moral hazards.

Aryeetey (1996) also expressed his opinion on measures to be taken before lending and stressed the importance for credit officers to ascertain time demand and false demand for credits. Whereas the former are applications for loans supported by bankable projects, the latter is without. The view of his report therefore calls for a proper and thorough appraisal of credit applications before credit decisions are taken. The comprehensive evaluation of credit worthiness compasses among others as gathering, processing and analyzing of information on potential applicants, and subjecting it to Credit Reference Bureau Scrutiny to ensure that clients fall within recommended credit ratings. For the past years, Rural Banks have not been able to access such data to enable them make quality credit decisions.

In April 2007, the government of Ghana, through the central bank had initiated a credit ratings and reference system to facilitate the credit worthiness of all existing and potential loan customers which is to be complied by all commercial and rural banks. However, Rural Banks have not fully complied with these directives and further have not been able to make credit references to thoroughly assessed credit worthiness of potential clients before loan approval (Bank of Ghana, 2007).

2.5.3 Poor Lending Behaviour

Rouse (1989) defines lending to be an art because it has an element of imagination and creativity. An effective credit practice enumerates the processes to be followed and this is imperative for good credit risk practices. The author stated that the lending activities encompass various disciplines of finance, economics, accounting, geography, law, science, psychology and culture among others. A sound credit decision relies on the knowledge, skills and foresight of the Credit Manager and other Officers in their various branches. McNaughton (1999) stressed that credits activities is one of the major of drivers of financial intermediation as such plays a significant role banking operations, whilst remaining highly risky at the same time. This situation makes lending activities very challenging to most rural banks in the country since a slight negligence can cause financial loss. Therefore, a person with the right attitude, skills and knowledge are to be charged to manage lending activities.

2.5.4 Insufficient Security

Security for credits is known to ensure that funds are recovered from the borrower at the time of his inability to fully meet his commitments or obligations of repayment. According to Dunkman (1996), the reason for security is to serve as a safeguard against some doubts about borrower's prepayment ability. The author reiterated that security serves as means for increasing loan request above existing facilities, and a secondary step to recover loans in event of default by the borrower. Agyeman (1987) was on his view that although collateral security serves as an important tool in credit decisions, banks should be cautious in setting security requirements as this can have an adverse effect on credit administration. It becomes a risk if bankable projects are solely financed on the availability of collateral security. The absence of reliable security in the rural communities was a major reasonable factor for the commercial banks not to extend credits to peasant farmers and small – scale businesses in such areas. The establishment of rural banks became essential for the fact that they do not rely on the rigidity of existence of security in extending credits to these farmers. The situation has created a serious turmoil for huge credit losses since most customers by virtue of their relationship with most stakeholders assess loans with insufficient security. It should be appreciated that the provision of adequate and perfected collateral security is essential in credit decision because it remains a secondary source of repayment of the loan in the event of default.

2.5.5 Poor Loan Monitoring

Huppi and Feder (1990) stressed that loan monitoring plays a significant role in ensuring the success of the project and, hence boost loan repayments on time. The authors emphasized that regular monitoring of loans lead to higher recovery rates by giving early possible dangers of delinquencies and diversion of loan funds by the borrower. The authors stressed that monitoring of credits should be seen as a catalyst to ensuring repayments at early signs of delinquencies either on interest or principal. Regular monitoring the borrower of the obligations of loan repayment as scheduled to the lending bank. However, most Rural Banks have not been able to take advantage to reduce the high rate of their loan defaulters.

Casu et al. (2006) indicated that banks must thoroughly assess the state of borrowers' ability to honor repayment of loans before, during and after the facilities had been granted. AsamaniDarko, (Personal Communication) revealed that monitoring is a vital step towards recovery because it gives firsthand information on situations that may eventually lead to arrears and subsequent default. One of the major causes of loan default in most Rural Banks is poor monitoring and control. Monitoring and control of all loans and the entire portfolio management is the responsibility of the Head of Credits and the credit teams at each branch of the bank.

For poor performing loans, credit officers may need to pay regular visits to customers to ascertain reasons for late payment, poor payment and non-payment. Nevertheless, good loans should also be monitored regularly to avoid degeneration of delinquent and hardcore loans. He advised that, monitoring could be done by visiting or calling of client by the Officer and through the liaising agents of the bank and the customer.

2.5.6 Weak Regulatory Control

Rural Banks are the expected in the course of operations protect their depositors' money which is the life blood to them. The essence of quality loans portfolio of banks provide security for deposits. The regulatory controls in credit management in most rural banks in Ghana have been highly weak leading to income leakages, loan defaults and affecting performances. Section 29 of the Banking Act, 2004 (ACT 673) mandates the Bank of Ghana to direct and regulate the maintenance of liquid assets by a bank as a certain percentage of its
total liabilities.

The assets to liabilities should not be more that 50% in Rural Banks. (Adansi Rural Bank

Credit Manual) .Credit risk continues to be a major problem in most of the rural banks in Ghana. The board, management and other supervising authorities must appreciate the compliance of those provisions. These provisions in The Banking Act, 2004 (ACT 673) outlines the need to adopt and comply by all banks to help establish good credit management practices in order to minimize default rates and maintain good loan portfolio to maximize shareholders returns.

2.6 Effective Credit Management Practices

The most effective form of portfolio management is at the point of origination of the credit (ARB - Apex Bank Manual, 2014). This part of the work stresses on key principles of effective credit risk management practices.

2.6.1 The Basle Committee on Banking Supervision Model

According to the Basle Committee on Banking Supervision as cited by Casu et al (2006), the common aim of managing credit management is to increase a bank's risk- adjusted rate of return by maintaining the credit risk exposure within acceptable parameters.The Basle Committee on Banking Supervision Report (2000) had outlined the following measures in order for banks, especially rural banks to address their credit risk exposures:

I. Establishment of Standardized Credit Environment

- ✓ The Board of Directors should have the oversight role of sanctioning and continuously reviewing their credit risk policies for their respective banks.
- ✓ Senior Management should have responsibility for implementing the credit risk policies and strategies as approved by the Board. They should therefore make policies and structures to help identify and keep watch of their credit risk measures.
- ✓ Banks should identify and manage credit risk associated with all loan products and activities.

II. Operating Under Sound Process of Granting Credits

- ✓ Banks should operate within well-defined criteria in granting credits to customers. The requirement should clearly indicate the target customers and a full analysis of the borrower, as well as purpose and structure of the credit, and its source of repayment.
- ✓ Banks should establish an overall credit limits at all levels of individual borrowers and counter-parties.

III. Measurement and Monitoring in Credit Procedures

- ✓ Banks should develop a system for the ongoing administration of their respective credit risk bearing portfolios.
- ✓ Banks should have a mechanism for monitoring conditions of adequate credits, by determining the adequacy of provisions and reserves.
- ✓ Banks should make it a habit of using the rating system in managing their credit risk. The rating system should be consistent in nature, size and complexity of a bank's credit activities.
- ✓ Banks should have a system in place for monitoring the overall composition and quality of their respective credit portfolios.

IV. Supervisor's Role

- ✓ Credit supervisors should ensure that effective credit system has been put in place in identification, measuring, monitoring and controlling credit risk as part of total approach to credit risk management.
- ✓ Supervisors should conduct an independent evaluation of the bank's credit policies, strategies and practices related to credit granting and management of portfolios.
- ✓ The role of supervisors to ensuring a good credit management practices is enforceable in Section IV, The Banking Act, 2004 (ACT 673)

2.6.2 Collateral/Security Requirements

Misklin (2006) stated that security which is a property promises the lending bank as compensation if the borrower default, it serves as secondary source of repayment and therefore, reduces the lender's losses in the event of default. McNaughton (1999) claims that collateral reduces bank's risk, reduces costs in terms of documentation and monitoring. She further stressed that the value of collateral should remain stable during the currency of the loan. According to Asiedu-Mante (2011), stated that the issue of security was crucial in the establishment of rural banks since the commercial banks were stressing on taking building and land as securities which were beyond the reach of rural dwellers. He further stated that the set-up of rural banks were to address the credit needs of rural dweller, and all obstacles that prevented financial intermediation in rural areas, which security was one of those obstacles. The author claimed that security against a loan is only a fallback position to a lender. He stated that today, most banks will rather lend on the strength of the balance sheet of a business or on the viability of a project. The author outlines the following as some of the items accepted by rural banks as security for loans;

- ✓ Cash/Credit balances on accounts
- ✓ Government debt instruments such as Treasury Bills and Notes, Bonds and Stocks
- ✓ Life Insurances Policies
- ✓ Fixed Deposits
- ✓ Pledges
- ✓ Security assignment
- ✓ Fixed/Floating Charges
- ✓ Mortgage on immovable Property

The general requirements of a good security is that, it should be easily realizable, easy to value, stable over an appreciable length of time , and that the title should be easily transferable. These have become an effective tool for decreasing borrower's risk of default.

2.6.3 Credit Rationing

Misklin (2006) simply define credit rationing as the intention of a bank to make credits unavailable, even though borrowers are willing to pay the stated interest rate or even a higher rate. The author stressed that the lender deliberately refuses to make loan of any amount to a borrower, even if the borrower may have the capacity and willingness to pay a higher interest rate or when a lender is willing to make a loan available but restricts the size of the loan to less than the borrower would desire. According to the author, credit rationing is essential because the larger the loan, the greater the moral hazard associated to it.Casu et al (2006) stated that credit rationing is an attempt to minimize the problem of adverse selection in the loan market. The authors stressed that bank can limit the amount available to a particular or class of borrowers in order to reduce credit risk exposures.

2.6.4 Credit Policy

A Credit policy is a document which guides the senior management and the Board in their lending activities. The policy calls for standards and prescribed culture in credits which are to be observed and comply. It is also a statement of the Bank's basic credit philosophy. Credit Policy is also viewed to provide a framework for achieving asset quality in a manner which is consistent with the strategic objectives of the bank.

Credit policies vary from one financial institution to the other. However they all seek to achieve effective credit administration or management. Asamani-Darko (Personal Communication) underscored that one of the objectives of a bank's credit policy is to improve access to financial services through timely and efficient credit delivery to a larger and wider client population with a total portfolio health of not less than 95%.

2.7 Loan Classification and Provisions

Section 53 of The Banking Act, 2004 (ACT 673) categorically classified loans into Current, Other Loans Exceptionally Mentioned (OLEM), Sub-Standard, Doubtful and Loss. These classifications give an indication of the level of provisions the banks are required to make to qualify the quality of their loan portfolios as indicated below;

a. Current	-	Up to 30 days	-	1%
b. OLEM	-	31 days – 90 days	-	10%
c. Substandard	-	91 days – 180 days	-	25%
d. Doubtful	-	181 days – 365 days	-	50%
e. Loss	-	365 days and above	-	100%

Source: Banking Act, 2004/Adansi Rural Bank Credit Policy Manual

These classification also segment credits into performing and non-performing loans in line with banking regulations. The performing loans comprise the current and Olem category whereas the non-performing loans are in the brackets of substandard to loss. Rural Banks are to ensure that loans granted to customers are fully secured to mitigate these risks of default.

2.8 Concepts of Organizational Performance in Banking

The drive for organizational performance has always been the priority of most organizations especially in the banking industry. Amstrong (2006) stressed that organizational performance management is seen as a systematic process for improving organization's performance by getting better results from the organization, teams and individuals within the framework of planned goals, standard and competent requirement. In view of that, a real organizational performance is noted to improve financial performance by enhancing greater profit, better cash flows, and among others.

According to American Management Association (2007), an organization must hold to its strategies that are closely related with its philosophies and beliefs to achieve a high performance. Khademfar and Amiri (2013) proposed five models a high performance organization maintains as Strategic, Customer, Leadership, Processes and Structure, and Beliefs and Values. The authors believe that these components are linked to each other, since a change to one affects others. Bounds (2005) suggested that the common measure of organizational performance is effectiveness and efficiency. These measures might look synonymous, yet each of these has its distinct meaning.

2.8.1 Effectiveness

Zheng et al. (2010) underscored that effective oriented organizations are concerned with output, sales, quality, creation of value added, innovation, and cost reduction. It usually measures the propensity to which a business achieves its goals or the way outputs interact with the economic and social environment. The author stressed that effectiveness determines the policy objectives of the organization or the degree to which an organization realizes its own goals. The effectiveness of most banks, particularly, rural banks in meeting clients expectations through quality loan products and good lending practices should be a major concern in fulfillment of its organizational goals.

2.8.2 Efficiency

Pinprayong and Siengthai (2012) categorized efficiency into business efficiency and organizational efficiency. According to the authors, business efficiency reveals the performance of input and output ratio, while organizational efficiency reflects the improvement of internal processes of the organization, such as organizational structure, culture and community. The authors suggest that the Return on Assets (ROA) is a suitable measure of overall company or banks performance, since it reveals how profitable organizations assets are in generating revenues. Rural banks could improve their level of effectiveness and efficiency by adopting sound credit management practices to enhance quality loan portfolios and operational maximize their profitability.

Organizational performance = effectiveness x efficiency

2.8.3 Measures of Banks Performance

Kumbirai and Webb (2010) stated that one of the several approaches used to measure banks performance is the accounting (financial ratios). These financial ratios have over the years been employed by financial institutions for assessing their performance. Artrill and McLaney (2011) expressed that financial ratios provide a quick and relatively simple means of assessing financial strength of a bank. The authors further stated that through the applications of financial ratios, banks are able to examine various aspects of their financial position and performance.

As far as this study is concerned, some of the various financial ratios adopted to examine the performance of rural banks specifically, Return on Equity (ROE); Return on Assets (ROA); Loans to Deposit Ratio (LDR); Capital Adequacy Ratio (CAR); and Non-Performing Loan Ratio.

a. Return on Equity (ROE)

Watson and Head (2008) underscored that return on equity measures how much institutions are performing after each Ghana Cedi invested in the shareholders' equity of the company. Islam and Salim (2011) also revealed that ROE measures banks' efficiency at generating profits from every cedi or pesewa of shareholders' equity.

b. Return on Assets (ROA)

The Return on Assets (ROA) is an indicator that measures how much a bank is earning after each cedi or pesewa invested in the assets of the institution. According to Van Horne (2005), return on assets indicates the profitability on banks assets after all expenses and taxes. Pinprayong and Siengthai (2012) indicated that the Return on Assets (ROA) is a suitable measure of overall company or banks performance, since it reveals how profitable organizations assets are generating revenues for the bank.

c. Loans to Deposits Ratio (LDR)

One important ratio used to measure the liquid condition of a bank is the Loans to Deposits Ratio. Moin (2013) indicated that banks with high LDR seem to have excessive liquidity, but with potential danger of reducing profits and in effect, less risk as compared to banks with high LDR. However, banks with high LDR are usually noted in engaging in financial stress as a result of granting excessive loans and have high risk of meeting depositors' claims.

d. Capital Adequacy Ratio (CAR)

Capital Adequacy Ratio (CAR) measures a bank's strength from a regulator's perspective. According to Asiedu-Mantse (2011) rural banks with strong capital adequacy ratio usually have good profitability and are able to absorb their possible bad loans and also escape the danger of bankruptcy, insolvent and collapse. The author further indicated that rural banks in the country are set with a minimum of 10% CAR and any ratio below this benchmark is unsatisfactory which needs immediate attention.

e. Non-performing Loans Ratio

Non-performing loans ratio (NPLR) are used to measure the fitness of credit risk management of a bank. Hosna et al 2009 indicated that non-performing loans ratio indicates how banks manage their credit risks because it defines the proportion of loan losses amount in relation to the total loan portfolio. Nair and Fissha (2010) indicated that Non-performing Loans (NPL) fairly affect profitability of banks and this is as a result of shifting cost of loan default to other customers and this poses a threat to the industry. Asamani - Darko (personal communication) revealed that non-performing loans are either in default or past due brackets, and include any unpaid loan amounts for at least 90 days. Ideally, non-performing loans are expected to have an inverse relationship with rural banks performance.

2.9 Effect of Credit Management on Banking Performance

Credit risk management in rural banking has raised many concerns not because of the financial crisis it can pose but also determines the bank's profitability and growth. This section reviews the effect credit management can pose to banks' performance in the area of profitability, being the key factor in banking performance; and liquidity.

2.9.1 Profitability

Primarily, organizations operate to make profits and shareholders expect to be paid dividends at the end of every year. Therefore, profitability measures are required to inform management, potential investors, shareholders, general public and other stakeholders about how the institution is performing. Artrill and McLaney (2011) defined profitability as the ability in the case of a bank to generate more revenues than its expenses, and that banks generally exist with the primary purpose of creating wealth for their owners. Rouse (1989) indicated that the core implication on granting credits is the probability that the borrower will not repay the facility that will lead to low interest income of a bank. The author stressed that high credit risk affects the profitability of banks, thereby eroding the shareholders' wealth.

Cooper et al. (2003) stated that the variations in banks profitability are mostly as a result of variations in credit risk, since increased exposure to credit risk usually associated with decreased profitability of a bank. Credits granted by the banking and non-banking institutions are expected to be the major source of generating income and are expected to have positive impact on profitability. All other things being equal, effective credit management and the higher the amount of credits granted, the higher would be the profitability level for the banks. Naceur and Goaid (2009) claimed that credits granted by banking institutions have a significant positive relationship with profitability. Achou andTenguh (2007) on a research conducted on bank performance and credit risk management found that there is a significant relationship between financial institutions performance (in terms of profitability) and credit risk management (in terms of loan performance). Better credit management results in better performance. Thus, it is of crucial importance that financial institutions practice prudent credit management techniques and safeguarding the assets of the institutions and protect the investors interests.. Nduta (2013) established that credit management practices have a strong relationship with financial performance in terms of profitability. She underscored that credit appraisal, credit risk control and collection policy to a great extent enhance the financial performance of Micro-Finance Institutions in Kenya. This is also true for rural banking institutions in Ghana

2.9.2 Liquidity

Liquidity is the ability to meet financial obligations as they fall due. Asiedu-Mantse (2011) indicated that very low deposits and high default rates have plunged some rural banks into serious liquidation problems, leading to the erosion of the general public confidence in rural banks in Ghana. He further stressed that improper lending culture and ineffective monitoring and recovery of credit facilities to customers have contributed to high credit risk and pose liquidity risk in most rural banks. In the year 1999 for example, the Bank of Ghana withdrew the banking licenses of 23 rural banks which were in distressed in the year 1999 due to unacceptable credit behavior and practices which eventually had serious bearing on their liquidity. McNaughton (1999) stated that credit risk has a negative effect on liquidity risk, and if it fails to receive the necessary attention can extremely lead to serious financial crisis of a bank, resulting in the loss of capital, insolvency and the collapse of a bank.

Generally, it is noted that the high risk of loan portfolios in most rural banks was a result of poor credit management practices, and this requires collaborative interventions to find ways of ensuring improvement. The adaption of effective credit management techniques has become a significant tool in enhancing profitability, enhancing liquidity, and maximizing shareholders wealth as well as deepening financial intermediation whilst bringing risk on return to its minimum to stimulate economic growth and development in rural areas. Since profitability is the major driver of organizational performance as measured by return on equity (ROE) would be used as a dependent variable for the purpose of the study and credit appraisal, credit disbursement and credit collection techniques as independent variables for credit management practices.

CHAPTER THREE

RESEARCH METHODOLOGY AND ORGANIZATIONAL PROFILE

3.1 Introduction

The previous chapter examined the theoretical and empirical literature on credit management practices in the rural banking industry. This chapter explains the methodology adopted to empirically analyze the result. The main issues considered in this chapter include the research design, study population, sample size and technique, data collection procedure, sources and type of data, as well as data analysis technique. Finally, the chapter provides a brief profile of the organization being used as a case study.

3.2 Organizational Profile

Adansi Rural Bank is a limited liability company established in the year 1980 in line with the Companies Code 1963, (ACT 137) and operates within the framework provided for in the Banking Act 2004, (ACT 673). The bank has its headquarters at Fomena in the Ashanti Region on the Kumasi – Cape Coast Highway. One of the reasons of its inception was to help stimulate savings culture and offer the needed assistance to alleviate rural poverty by granting credits. Today, the bank has eight (8) branches and poised to be the most preferred, efficient and effective Rural and Community Bank within its competitive environment. The bank is focused on income generating activities by extending different loan packages to its customers.

3.3 Research Design

According to Saunders et al. (2009), a research design encompasses the overall view of the method adopted for the study and the reasons underpinning those methods. He proposes three broad issues that make up a research design. These are research approach, research purpose and research strategy. The research purpose looks at the fundamental purpose of the research; whether it is descriptive, exploratory or explanatory. While descriptive research basically generates detailed description of issues, events and phenomena, explanatory/causal studies examines cause-and-effect relationship between variables (Saunders et al. 2009). Exploratory studies typically explore issues that have not been explored in detail. For the purposes of this study, descriptive design is adopted. The descriptive design allows the researcher to use financial data and questionnaire from Adansi Rural Bank Ltd to describe in detail the credit management practices pertaining in the bank and how it is affecting its financial performance. As far as the description and explanation of phenomena are concerned, quantitative research focuses on analyzing numerical data whereas qualitative research deals with meanings, examining the attitudes, feelings and motivations of people (Babbie, 2004). Based on the nature of data employed in the study, a quantitative research approach is adopted. Financial data and questionnaire will be quantitatively presented using percentages, means, standard deviations and graphs.

According to Yin (2004), five major research strategies can be identified. These are surveys, case studies, archival studies, histories and experiments. The study employs the case study strategy since the researcher is considering one rural bank but not all rural banks in Ghana.

3.4 Study Population

A study population encompasses person or objects having at least one common characteristic. As far as this study is concerned, the population of the study consists of Credit Officers and Managers of Adansi Rural Bank Limited in the Ashanti Region. Based on information available to the researcher, the number of Credit Officers and Managers of the bank currently stands at 21. The breakdown of the population based on the bank's 8 branches and its Head Office is presented in Table 3.1 below.

Table 3.1 Population of respondents from selected branches

Branch/Agency	Number of Risk Officers/Managers
AdanseFomena	2
New Edubiase	2
Obuase	2

Akrokerri	1
Kotwi	2
Kaase	2
Atonsu	2
Dunkirk Head Office	2 6
Total	**21**

Source: Field Data, June 2015

3.5 Sample Size and Technique

The subset of the population relied on by the researcher to gather relevant information is described as a study sample (Saunders et al. 2012). Using the entire population is the best since all individuals and objects are given the opportunity to offer their contribution. However, due to time and other resource constraint, researchers are forced to choose a part of the population to represent the entire population. However, Saunders et al. (2009) explained that when the study population is not too large, the entire population can be studied. Since the population of credit officers/managers of Adansi Rural Bank Limited is just twenty-one (21), the entire population will be considered in this study.

3.6 Data Collection

Research data can be sourced from either primary or secondary sources. According to Saunders et al. (2012), primary data constitutes new data collected specifically for a study, while secondary data constitutes data previously collected for some other purpose. As far as this study is concerned, the purposes of this study on both primary and secondary data were employed. Section 3.6.1 and 3.6.2 provides detailed explanation of the various sources of data. The questionnaires were administered to credit officers of all the eight (8) branches of the bank in the Ashanti region. The head of credits was also interviewed to gain more insight into the subject matter. These officers and managers were considered because they pose the right kind of knowledge and expertise needed to enrich the quality of the researcher's findings.

3.6.1 Primary Sources of Data

Primary data was obtained through questionnaire and interview conducted by the researcher. The responses obtained from respondents formed the primary data used in the analysis. In order to capture relevant information from respondents, the interview guide and the structured questionnaires were well-designed. The content of the questionnaire and interview guide were based on the theoretical and empirical studies reviewed by the researcher.

3.6.2 Secondary Sources of Data

The main secondary data employed in the study is the financial data of the bank on quarterly basis from 2009 - 2014. Specifically, financial records in the form of Return on Equity (ROE), Return on Assets (ROA), Non-Performing Loans (NPL) and profitability figures were used. Also, the credit management policies and strategies of the bank were used to support the financial data. In addition to the above mentioned sources of secondary data, other sources such as journals, books articles, newsletters and other internet sources were used.

3.7 Design of Research Instrument

As indicated earlier, questionnaire and interview guide were designed to solicit the views of credit risk officers and managers of Adansi Rural Bank Limited on issues relating to credit management in rural banks at large. Based on the kind of information required by the researcher, these research instruments were deemed appropriate. The research instruments were designed to ensure that all relevant information is captured to improve the validity of the research findings. As far as the questionnaire is concerned, both close and open ended questions were asked. The closed ended questions provided several options for the respondents to make a choice. The open ended questions gave respondents the opportunity to write their own answers to the questions asked. This was done to ensure that detailed information that could not be captured by the close ended questions is obtained.

The interview guide was designed to obtain in-debt information on the knowledge management practices of the bank and the entire rural banking sector at large. The head of credit risk management was interviewed to solicit more information to compliment the responses obtained from credit officers/managers. A semi-structured interview guide was designed for this purpose. This structure was adopted because the researcher was convinced it was the best structure to use based on the objectives of the study.

3.8 Questionnaire Administration

Before the questionnaires were administered, the respondents were informed by the researcher about the study. The questionnaires had brief preamble explaining the purpose of the study, those responsible for the study, and a statement guaranteeing the confidentiality of respondents. To ensure that respondents understood each question asked, the researcher personally administered them.

3.9 Interview guide Administration

As indicated earlier, the head of credits of Adansi Rural Bank was interviewed to ascertain the opinion of management on credit management of the bank. Before the interview process, the researcher informed him about the purpose of the study. The researcher personally interviewed the head of risk management of the bank, using a semi-structured interview guide. To ensure that all information provided were captured, the researcher sought the permission of the interviewee to record the conversation. The result of the interview process was synthesized and presented in a table form.

3.10 Ethical considerations

Ethics is critical for the success of any research project. According to Saunders et al. (2012), research ethics relates to issues concerning how the research topic is formulated and clarified, data collection procedure, data processing and storage, and how the data is presented and analyzed. The researcher ensured that the research was conducted in a morally responsible manner. In order to ensure that the research does not violate any ethical standards, a number of issues were considered. Firstly, the researcher tried as much as possible to avoid plagiarism. Secondly, the literature was competently reviewed in order to obtain high quality research. Thirdly, the researcher avoided shading the results of the research. Fourthly, the researcher informed interviewees about the research and avoided coercing respondents to participate in the study. Finally, the interviewees' right to privacy was very well protected by keeping the information provided as confidential as possible.

3.11 Validity and Reliability of the study

According to Saunders et al (2009), the credibility of a study, to a large extent, hinges on the validity and reliability of the study process. Validity refers to the extent to which a measure reflects the concept it intends to measure. According to Trochim (2005), if a study actually measure what they claim to, and if there are no logical errors when drawing conclusions from the data, the study is said to be valid. On the other hand, reliability refers to the extent to which studies can be replicated. In order to attain a high level of validity, much attention was given by the researcher to the design of the questionnaire and the interview guide. The researcher ensured that the instruments measured what they proposed to measure. To ensure the validity of the instruments, the questionnaire was validated by a research supervisor of KNUST Business School before they were administered. Secondly, a pre-test was undertaken to ensure that inconsistencies in the research instruments were corrected.

3.12 Data Analysis

Saunders et al. (2009) describe data analysis as breaking down data into units for understanding. The data collected for the study made it possible for both quantitative and qualitative analysis to be conducted. The quantitative techniques adopted for the study include descriptive statistics, correlation analysis and regression analysis. The analysis was made possible by the use of Statistical Package for the Social Sciences (SPSS). The data obtained from the interview was analyzed based on the approach of Miles and Huberman (1994).

CHAPTER FOUR

DATA ANALYSIS AND PRESENTATION OF RESULTS

4.1 Introduction

The chapter three of this study examined the methodology and sources of data for analysis. In this chapter, the data collected is analyzed and presented. The result obtained is further discussed and compared with existing literature on the subject. The study has four main specific objectives. The first is to assess the credit management practices of Adansi Rural Bank Limited in the Ashanti region of Ghana. The second objective looks at the factors accounting for credit risks (defaults) in the rural bank. The third objective looks at the performance of the bank. The final objective looks at the effect of credit management on the performance of the bank.

In order to meet the objectives of the study, both primary and secondary data were used. The primary data involved information solicited from the risk management department of the bank. The secondary data comprised of financial ratios such as Return on Equity (ROE), Loan Loss Provision to Gross Loan Advances (LLP/GLA) and capital adequacy Ratio (CAR).A total of twenty-one (21) Credit Officers and Managers selected from all the 8 branches of the bank were served with questionnaires to complete. Out of this number, nineteen (19) representing a response rate of 90.5 percent successfully completed and submitted their questionnaires.

4.2 General Background of Respondents

As indicated in the chapter three of this study, twenty-one (21) Credit Officers and Managers selected from all the 8 branches of the bank were served with questionnaires to complete. Out of this number, nineteen (19) representing a response rate of 90.5 percent successfully completed and submitted their questionnaires. Out of the nineteen (19) respondents, 7 (36.8%) were Credit/Branch managers, 1(5.3%) was Credit Risk Manager, while 11(57.9) of the respondents were Credit Officers. The result also indicates that the respondents have varying degree of experience in the banking sector in general and risk management in particular. For instance, it can be observed from the result in Table 4.1 that eleven (11) of the respondents, representing 57.9 percent of the total sample has served the bank for between one to five years, while the remaining 42.1percent have been working with the bank for over five years. The result from the background characteristics of the respondents gives credence to the fact that the respondents possess valuable information that helped to enhance the validity of the study.

Table 4.1 General Background of respondents (N=19)

Variable	Classification	Frequency	Percentage

Position	Branch/Credit mangers	7	36.8
	Chief Credit Managers	1	5.3
	Credit officers	11	57.9
Banking experience	1-5 years	11	57.9
	6-10years	6	31.6
	Above10 years	2	10.5
Risk management Experience	Under 1 year	1	5.3
	1-5 years	10	52.6
	6-10 years	5	26.3
	Above10 years	3	15.8

Source: Field Data, June 2015

4.3 Credit Management Practices of Adansi Rural Bank Ltd.

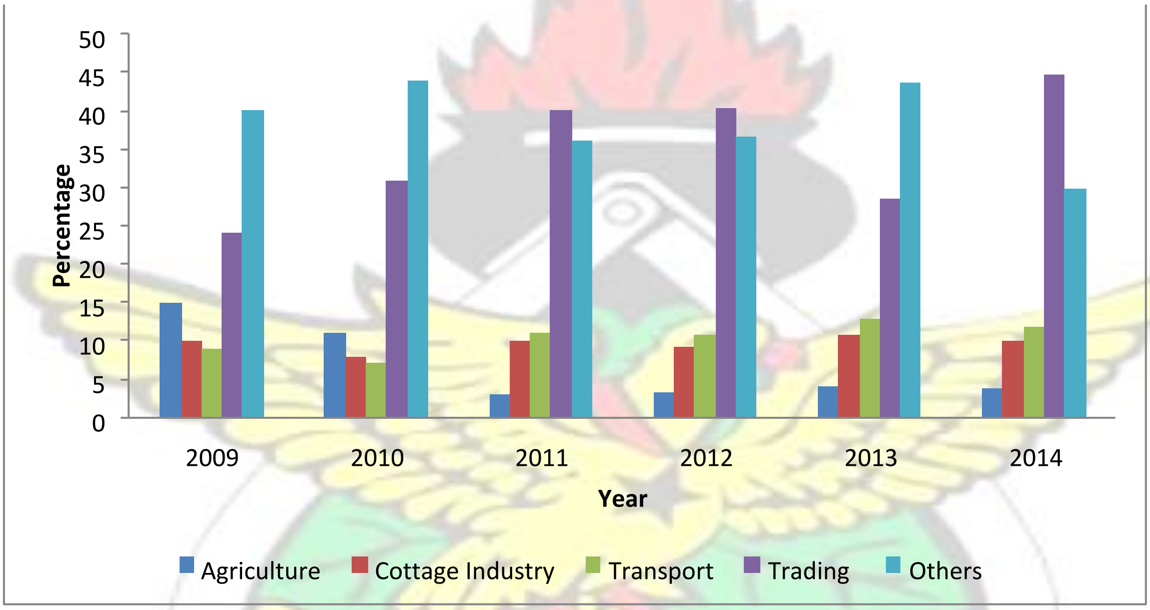
Managing credit is one of the most important aspects of businesses, especially banking business. The extent to which credit is managed goes a long way to determine the financial performance of banks, particularly, rural banks in Ghana. Against this backdrop, the first objective of the study was to examine the credit management practices of Adansi Rural Bank Ltd. The areas examined include the nature of credit offered, the effectiveness of the credit appraisal system and credit recovery trend within the period considered.

4.3.1 Target customers

Providing credit for rural dwellers to improve the rural economy of Ghana is one of main reasons for the setting up of the rural banking industry. However, an effective credit management demands that rural banks target customers who are credit worthy and are able to repay their credit and associated interest. Rural banks usually have sectors they concentrate on when it comes to credit disbursement.

Information obtained from Adansi Rural Bank indicates that the bank provides credit to the agriculture sector, cottage industry, transport and trading. These sectors, however, do not receive the same amount of credit. The credit is disbursed to the sectors based on their risk exposure and credit worthiness. Figure 4.1 provides a summary of the percentages of total loans received by the various sectors from 2009 to 2014.

Figure 4.1 Graphical Picture of Sectoral Credit Coverage of Adansi Rural Bank Ltd. from 2009 to 2014



Source: Analysis of secondary data from Adansi Rural Bank Ltd, 2009-2014

Figure 4.1 compares the percentage of the total loans received by the various sectors. Trading has been enjoying high percentage of the total credit offered by the bank. Though many factors are considered when granting credit to the various sectors of the economy, banks usually place much emphasis on risk. For instance, the agriculture sector has received less support compared to other sectors for the period considered. For instance the percentage of total loans for the agriculture sector was 3.91% compared to 10.85% for the cottage industry for the same period in 2013. The result is not different from 2011, 2012 and 2014. Though the rural banking industry was establish to promote the rural economy and agriculture, most rural banks are shying away from this role because of the risky nature of the sector.

The agriculture sector is considered risky by the bank and therefore is unwilling to invest in it compared to other sectors of the economy. Revenue received by farmers is less stable and most of the farmers do not have the needed collateral security to guarantee for their loans. This, among other reasons may be accounting for the dwindling fortunes of the sector as far as credit disbursement is concerned.

4.3.2 Application and Credit Appraisal Process

Effective credit management requires that loan granting procedures are followed. Every bank is expected to appraise customers, be it individual or corporate, before granting of credit. Basel (1999) indicates that credit must be granted based on a number of considerations such as the borrower's ability to amortize the debt, the character of the customer in term of credit worthiness, the customers' ability to provide collateral security, among others. The study sought to examine how credits granting procedures are followed by Adansi Rural Bank Ltd.

On a scale of 1 to 4, the respondents were asked rank the individual and company factors considered before granting loans. The factors considered include character, security, ability to pay, borrowers repayment history, profit and loss statement, cash flow statement, future prospects of the of the borrower, among others. The result is presented in Table 4.3 The result indicate that the most important factor considered before granting loans to customers is the ability of the customer to pay back the credit facility. This factor has the highest mean rank of 3.89 and a standard deviation of 0.315. The low standard deviation value indicates that credit officers unanimously agree that ability to pay is a critical factor considered in the credit management practices of the bank. The second most important factor considered is Character of the customer. This factor has mean of 3.88 and a standard deviation of 0.315. The third most important factor is security (Mean=3.79; S.D=0.419). Other important factors examined include borrowers repayment history (Mean=3.47;

S.D=0.513); Profitability (Mean=3.53; S.D=0.612) and Cash flow Statement (Mean=3.26; S.D=0.806). The result obtained indicates that the bank does not grant credits without following the main credit appraisal system.

Table 4.2 Descriptive Statistics of the credit appraisal system of Adansi Rural Bank Ltd.

Variable	N	Minimum	Maximum	Mean	Std. Deviation
Character	19	3	4	3.89	0.315
Security	19	3	4	3.79	0.419
Ability to pay	19	3	4	3.89	0.315
Borrower's repayment history	19	3	4	3.47	0.513
Profit and loss statement	19	2	4	2.84	0.688
Future prospects of the business	19	2	4	3.26	0.562
Cash flow statement	19	2	4	3.26	0.806
Experience with credit utilization	19	1	4	3.00	0.745
Profitability	19	2	4	3.53	0.612
Financial/capital structure	19	1	4	2.68	0.885
Skills and expertise of management	19	1	4	2.89	0.809

Source: Field Data, June 2015

The result shows that the bank follows the credit appraisal process stipulated by Basel (1999). For effective credit management, the character of the customer in terms of past credit history needs be examined. Also, the credit worthiness and ability of the customer to repay the loan needs to be examined as well. In addition, the profitability of the customers' business and cash flow statements needs to be examined. The response obtained from the population suggests that the bank is doing well when it comes to credit appraisal.

4.3.3 Monitoring and Collection Techniques

An effective credit risk management does not end with the granting of advances or loans. The ability to recover loans in a timely manner is an important component of credit management. To verify the extent to which credit risk management of Adansi Rural Bank has helped to reduce loan default rate, financial data of the bank was analyzed. The data collected spans from 2009 to 2014 as depicted in Figure 4.2 below:

Figure 4.2 Trend of Loan Recovery Rate, 2009-2014

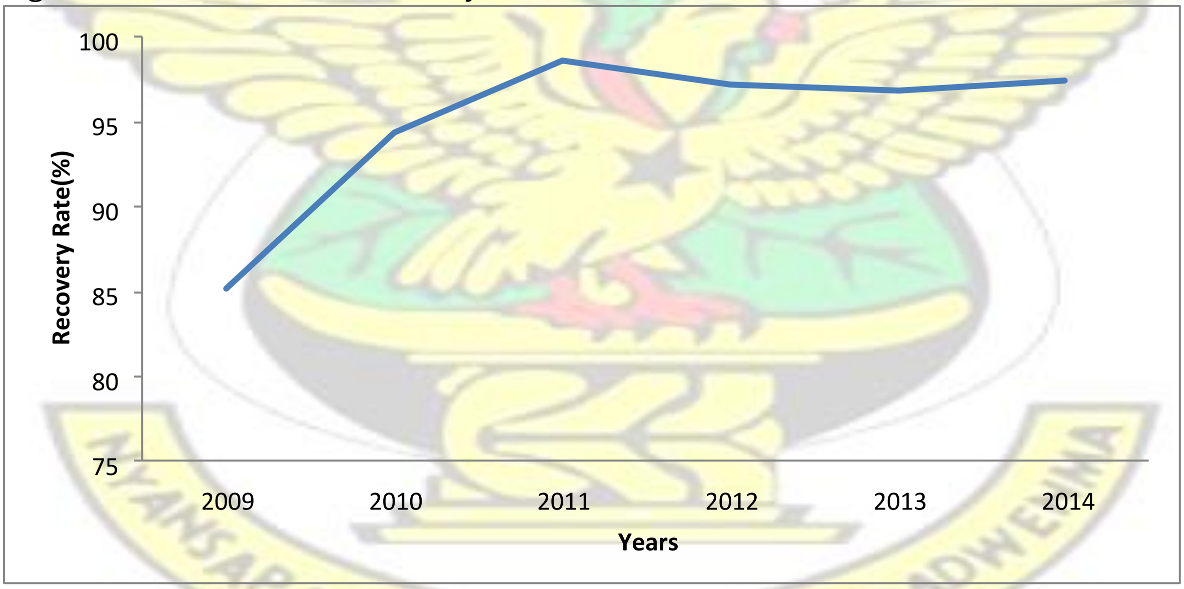


Figure 4.2 shows that loan recovery rate of the bank has improved considerably over the period under review. For instance in 2009, the bank was able to collect 85.2 percent of the total portfolio of loan granted. This means that the default rate was as high as 4.8 percent. However, in 2010, 2011 and 2012, the bank had recovery rates of 94.4 percent, 98.6 percent and 97.2 percent respectively. Though the recovery rate fell to 96.9 in 2013, it rose again to

97.4% in 2014.

The result clearly shows that the bank is performing well when it comes to loan recovery. The implication of this impressive result may be attributed to the prudent credit risk management techniques being practiced by the bank. This shows that the healthy portfolio report approximately 95% which is above the industry benchmark of 85%. The bank in the year 2013 was adjudged the best loan financing rural bank of the year. However, the result should encourage the bank to do more to reduce credit default to the barest minimum. This can be achieved by effective monitoring, efficient credit appraisal system, training of credit officers and effective and efficient credit recovery strategy.

4.4 Factors Contributing to Credit Risk (Default)

In spite of the effort by rural banks to reduce the rate of default, the problem of credit risk still persists. The study sought to examine the factors accounting for credit risk (default) at Adansi Rural Bank. Credit officers/managers selected from all the eight (8) branches of the bank were interviewed. A number of factors were identified and respondents were asked to rank these cases on a scale of 1 to 3; with 3 indicating highest cause and 1 representing the lowest cause. The responses were presented using descriptive statistics in Table 4.4. The result indicated that diversion of loan by customers constitute the major cause of credit risk by customers (Mean=2.58, s.d=0.607). The low standard deviation value means that majority of the credit officers identified diversion of credit as a major cause of loan default. The second most important cause of credit default at the bank was identified as customer business failure (Mean=2.26, S.d=0.653). Poor monitoring of credit customers was also identified as the third major cause of loan default at the bank (Mean=2.21, s.d=0.787).

The result implies that the bank must do more to educate customers who secure loan facility from its outfit. Rural banks must also continuously monitor the customers to ensure that they are using the credit for the intended purposes. Diverting the credit to unproductive ventures makes it difficult for such ventures to generate enough cash flow to amortize the debt. A monitoring team should therefore be instituted by the bank to monitor the activities of loan clients frequently.

Identifying business failure as one of the major causes of loan default means that when the business of the loan clients fails, they are unable to generate enough profit to service the debt they have procured. It is therefore important for rural banks to provide non-financial services to the customers. For instance, the bank should educate customers on basic business principles and basic accounting concepts to enable them maintain proper financial records. Poor monitoring of credit was also identified the third major cause of credit default.

Monitoring is crucial if a bank seeks to reduce its default rate. Having a technology to monitor customers' account can help the bank reduce its credit default to the barest minimum. The findings are in agreement with the findings of Ahmad (1997), who identified the main causes of credit default as lack of willingness to pay loans coupled with diversion of funds by borrowers; willful poor business practice is yet another cause. In this study, the findings indicate that business failure of customers is one of the major causes of loan default. This findings also corroborate the findings of Kasozi (1998) who found customer business failure as a major cause of loan default. The reason for this phenomenon, he argue, is due to poor business management practices on loan customers. Many borrowers lack the technical skills like keeping records and checking on the business performance until the time of paying back the loan. This is usually hard because they never plough back the profits leading to loan default in the long run.

Table 4.3 Descriptive Statistics of the Causes of Credit Risk (Default)

	N	Min	Max	Mean	Rank	Std. dev.
Poor appraisal system	19	1	2	1.39	6TH	0.502
Poor monitoring mechanism	19	1	3	2.21	3RD	0.787
Staff influence	19	1	2	1.21	7TH	0.419

Inadequate collateral security	19	1	3	2.05	4TH	0.848
Diversion of loan	19	1	3	2.58	1ST	0.607
Customer business failure	19	1	3	2.26	2ND	0.653
Inadequate credit officers	19	1	3	1.63	5TH	0.597

Source: Field Data, 2015

4.5 Analysis of the Performance of Adansi Rural Bank in terms of Profitability and Liquidity

Profitability and liquidity are important to the sustainability of the rural banking system in Ghana. One of the objectives of this study is to examine how Adansi Rural Bank Limited has been performing in terms of profitability and liquidity for the past five years (2010-2014).

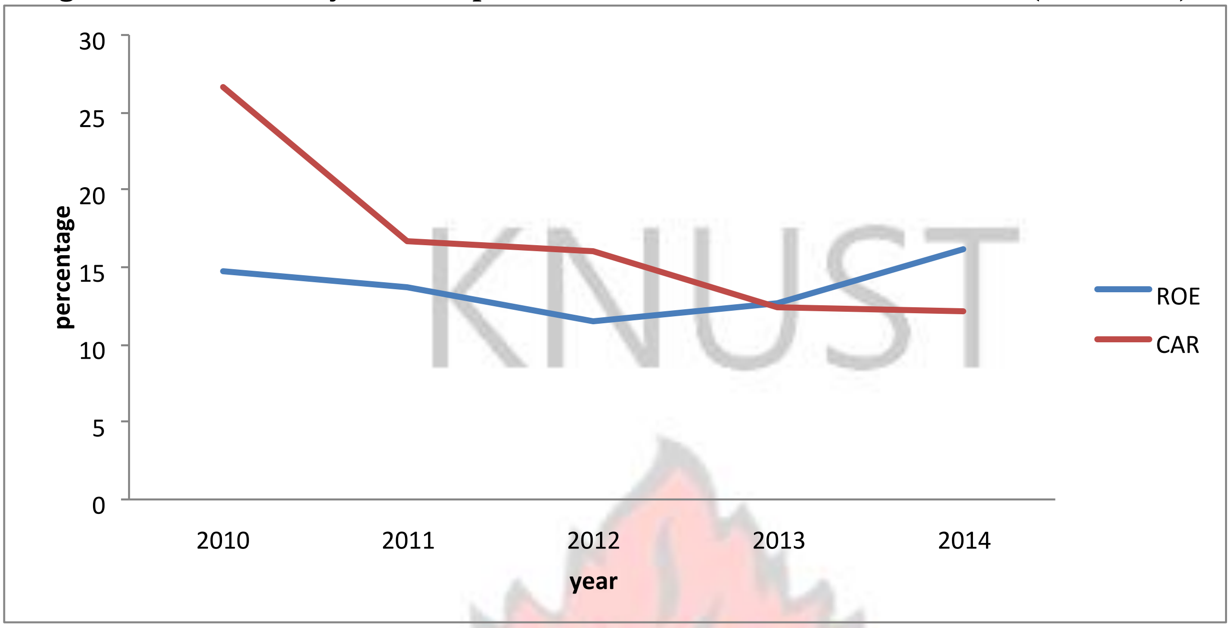
Return on Equity (ROE) was used as a proxy for profitability of the bank while Capital Adequacy Ratio (CAR) was designated as the proxy for liquidity.

The descriptive statistics of the performance variables were illustrated in the Table 4.4 and Figure 4.3 below:

Table 4.4 Descriptive Statistics of the Performance variables (ROE and CAR)

Performance variables	Minimum	Maximum	Mean	Std. Deviation
ROE	11.5	16.2	13.78	5.14
CAR	12.2	26.7	18.98	7.48

Figure 4.3 Trend analysis of the performance of Adansi Rural Bank Ltd. (2010-2014)



Source: Financial Data from Apex Bank, 2015

The descriptive statistics showed that within the period considered, the average return on equity (ROE) was 13.78%. This indicates a moderate return on equity to investors. This means that the bank generates 13.78% on every cedi invested shareholders. However, it must be emphasized that reporting high profit figures does not necessarily imply that the bank in performing exceptionally well in its financial management. It is highly possible that huge amount of its profit are as a result of debtors. Also, the capital adequacy ratio within the period averages 18.98%, which is relatively high compared to the industry average of 15%. The higher CAR indicated that the bank is more liquid and reliable. Banks having good capital requirement will be in the position to absorb loans that have gone bad.

Figure 4.3 shows that both CAR and ROE of the bank have been declining. Though the decline is not significant, the bank must take steps to improve its liquidity and profitability. The improvement of liquidity and profitability, according to Asiedu-Mante (2002) will enable the bank to advance more credit to improve its profitability in the form of interest and charges. Also, improving the CAR will enable the bank to be more liquid and absorb shocks emanating from credit default.

Table 4.7 The Effect of Credit Management on Rural Banks Performance.

The final objective of the study was to examine the effect of credit management on the performance of rural banks in Ghana using financial data from Adansi Rural Bank. The performance of the bank within the period was measured by its Return on Equity (ROE). Thus, ROE was designated as the dependent variable whiles CAR and NPLR were used to represent the independent variables in the descriptive and correlation analysis.

However, the credit management practices of the bank were used as independent variables in the regression analysis over the ROE as dependent variable to determine their impact on rural banking performance as far as profitability is concerned as the key performance indicator. Credit management components such as credit appraisal (CRDAPPR), Credit Disbursement (CRDDISB) and Credit Monitoring and Collection (CRDMON) were regressed on the dependent variables. Descriptive, correlation and regression analysis using Statistical Package for Social Sciences (SPSS) was performed. The results were presented in Table 4.5, 4.6, 4.7, 4.8 and 4.9 below:

Table 4.5: Descriptive Statistics of Dependent and Independent Variables

Study Variables	N	Minimum	Maximum	Mean	Std. Deviation
ROE	24	4.99	324.79	105.1535	85.52336
CAR	24	6.46	22.50	16.6025	3.60718
NPLR	24	4.26	20.22	7.8777	3.60823

Source: Field Data, 2015

The descriptive statistics shows that within the period considered, the average return on equity (ROE) was 105.15%. This indicates a very high return on equity to investors. This means that every shareholder's equity invested in the bank generates twice its value. This indicates that over the years, the bank has been doing well in improving profitability. Also, the capital adequacy ratio within the period averages 22.5%, which is relatively high compared to the

industry average of 15%. The higher CAR indicates that the bank is more liquid and reliable. Rural banks having good capital requirement will be in the position to absorb loans that have gone bad. Also, the non-performing loan ratio within the period was
7.8%, which is also high, albeit within a manageable level.

Table 4.6 Pearson's Correlation Coefficient Result

Correlations

		ROE	CAR	NPLR
ROE	Pearson Correlation	1		
	Sig. (2-tailed)			
CAR	Pearson Correlation	.505*	1	
	Sig. (2-tailed)	.012		
NPLR	Pearson Correlation	-.420*	-.474*	1
	Sig. (2-tailed)	.041	.019	
	N	24	24	24

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

Source: Field Data, June 2015

REGRESSION ANALYSIS

Credit management components such as credit appraisal (CRDAPPR), Credit Disbursement (CRDDISB) and Credit Monitoring and Collection (CRDMON) were regressed on the dependent variable Return on Equity (ROE), which is a measure of performance.

Table 4.7 Summary of the Regression Model

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate

1	.667[a]	.447	.362	68.30420

F-statistic = 4.447, Probability value of f-statistics (0.007)

Source: Research Findings

Table 4.8 Regression Result

Coefficients[a]						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	177.992	62.142		2.864	.010
	CRDAPPR	4.632	19.339	5.32	2.226	.024
	CRDDISB	57.978	18.095	6.43	3.204	.0.04
	CRDMONCOL	31.070	62.142	4.53	1.962	0.48
a. Dependent Variable: Return on Equity (ROE)						

Source: Research findings ***KEY:***
CRDAPPR - Credit Appraisal CRDDISB - Credit Disbursement
CRDMONCOLL - Credit Monitoring and Collection

The result of the regression analysis (See table 4.8) showed that Credit Disbursement (CRDDISB) recorded the highest 'B' value of 57.978 and greatly affect the profitability of rural banks (β=0.04, sig<0.05). This means that quality improvement in disbursement of credits to customers would improve the profitability of the banks. Credit Monitoring and Collection (CRDMONCOL) recorded the second 'B' values highest of 31.070 but less significant to profitability (β=0.48, sig<0.05). The third factor is Credit Appraisal (CRDAPPR) with 'B' value of 4.632 which significantly also affect the performance of the banks. All the 'B' values and 'β' values are positive indicating a strong relationship of the credit management variables with the dependent variable. The F-statistics of 44.5 9 (See table

4.7) which is significant at 1% (sig≤0.01) also indicates that credit management has significant impact on the performance of the banks. The result above is in agreement with a number of previous studies. For instance, Basel (1999) explains that effective credit appraisal and monitoring enhances the credit recovery process and hence improves the financial performance of banks. A similar study conducted by Nduta (2013) that credit management practices have a strong relationship with financial performance on MFI institutions in Kenya. The result obtained in this study confirms the theory that good credit management leads to high performance and profitability of rural banks in Ghana.

Table 4.9 The Predictive Power of the Model

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	74918.73	3	24972.791	5.353	.007[b]
	Residual	93309.274	20	4665.464		
	Total	168227.648	23			

a. Dependent Variable: ROE

b. Predictors: (Constant), CRDAPPR, CRDDIB, CRDMONCOL

Source; Field Data, June 2015

The predictive power of the model was tested using F-statistics (See Table 4.9). The rule of them is that when the overall probability (P) value (Prob>F) is between 0 and 0.05 then the model is strong and has high predictive power and that significant results will be achieved when used in other studies. The model used for the analysis of this study has a high predictive power of 0.007(i.e. Prob>F = 0.05). Thus, this model can be used in similar studies to predict the relationship between credit management and rural banks financial performance. The result means that credit management has significant impact on the performance of rural banks.

4.7 Analysis of Interview with Credit Risk Manager

To ascertain additional information that is essential for the understanding of credit risk management practices of the bank, an interview with the Chief Credit Manager of the bank was conducted. The researcher personally, organized the interview session using face-to-face approach. The responses were captured based on the questions asked by the researcher.

- ***The Level of Expertise of Employees in the Credit Department of Adansi Rural Bank Ltd.***

The interview with the chief risk manager revealed that most of the employees lack the skills and experience needed for effective credit risk management. He explained that, this has made it incumbent on the bank to constantly train credit officers to improve on their delivery. He further disclosed that it will take more than two years to train employees to appreciate the risk aspect of their work.

This finding corroborated with those findings obtained from the credit officers who stated that lack of expertise in the area of credit risk management is affecting the smooth administration of risk management at the bank. The result implies that the bank must do more to recruit more experts in the area of risk management to reduce credit default and improve its profitability.

- ***Credit Management Framework and Policies of your Bank over the years*** In responding to this question, the interviewee explained that the approval of limits and authorities are vested in the directors of the bank who approve loans with little or no interference from management. This, he explained, is a strategy to ensure that managers do not use their influence to compromise on good credit risk management practices. He indicated that a new policy is been drafted that will ensure among other things that loan forms are updated to capture relevant information from borrowers. The credit policy of the bank, he explained, does not set a limit on the quantum of loans to be granted to customers. He indicated that the credit is granted on the clients ability to repay based on credit appraisal. He was however quick to explain that the bank has a policy not to grant loans exceeding 70 percent of its total deposits.

- ***Credit Management Strategy Adopted by the Bank***

The head of credits of the bank explained that two main strategies have been adopted to manage risk, especially credit risk in the bank. The first is that the bank has a system to verify information received from loan applicants from credit reference systems and bureaus. The reason for this strategy, he disclosed that this strategy was designed to ensure that customers who have bad credit history are barred from receiving credit from the bank.

The responses given by the Chief Credit Manager relates to the general views expressed by the Credit Officers that the bank has a risk management framework to ensure that that the credit appraisal system is followed based on laid down procedure. It is therefore not surprising that the bank has been able to improve its loan recovery rate over the years.

- ***Credit Management Effectiveness of Adansi Rural Bank Ltd.***

The interview revealed that the bank has been quite successful in managing its credit risk. It was for instance, revealed that out of over GH¢ 18 million credit portfolio balance, less than GH¢ 1 million are in past due bracket. This shows that the healthy portfolio report approximately 95% which is above the industry benchmark of 85%. The bank in the year 2013 was adjudged the best short-term loan financing rural bank of the year.

As far as credit monitoring is concerned, he stated that the monitoring of credit lies with the credit officers at the various branches. In addition, recovery officers are given additional responsibility to ensure that loans are well monitored. The information gathered on the monitoring process is further transferred to the credit manager of the branch. The credit manager reviews and evaluates the monthly portfolio reports and identifies non-performing loans and past dues for immediate attention.

The finding obtained from the interview is in tandem with the responses provided by the risk officers of the bank to the extent that the bank effectively manages is credit risk. This is also evidence from the analysis of the secondary data obtained from the bank which shows that the bank is effectively managing its credit risk.

- ***Challenges in Managing Credit Risk at the Bank***

Some of the challenges revealed by the interviewee include the following; the first is staff competence to handle credit portfolio of the branch. Secondly, lack of functional credit policy to guide the overall credit administration of the bank. Thirdly, poor attitude of staff towards credit recovery was identified as a major challenge militating against credit risk management of the bank. Finally, lack of proper filling and archival system to manage loan data was identified as a challenge. These challenges identified by the chief risk officer are similar to those expressed by the credit officers. The interview further revealed that the challenges enumerated above are having some form of negative impact on the overall performance of the bank. For instance, the chief risk officer explained that credit administration of the bank has become difficult as a result of some of these challenges. He also indicated that as a result of these challenges, the bank is not able to achieve the highest recovery rate of 99% it hopes to.

- ***Management of the Challenges***

As part of the comprehensive risk policy being embarked upon by the bank, the credit manager has instituted a proper filing system to manage loan forms for easy reference. Further, the bank has instituted training programs for credit staff to sharpen their skills on credit risk management at their respective branches.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

In chapter four of this study, the primary and secondary data were subjected to statistical analysis with the aid SPSS software. This chapter provides a summary of the key findings based on the analysis. Also, the chapter provides conclusions of the entire study as well as recommendations for key stakeholders.

5.2 Summary of Findings

The study had three specific objectives. The findings of these objectives are summarized as follows:

5.2.1 Credit management Practices of Adansi Rural Bank Ltd.

The findings of the study indicated that the bank has good credit management practice. This is evidenced by low non-performing ratio and high capital adequacy ratio in its portfolios. The result clearly shows that the bank is performing well when it comes to loan recovery. The bank has a healthy portfolio report of approximately 95% which is above the industry benchmark of 85%. The result further shows that the bank follows all the credit appraisal processes stipulated by Basel (1999). For instance the study discovered that due diligence is done by the bank before selecting customers to benefit from credit facilities. Due diligence is done in the area of the customer's ability to pay, character, business performance and borrower's credit history.

5.2.2 Causes of Credit Risk (Default) in Rural Banks.

The second objective of the study was to examine the main causes of credit risk (default) within rural banks using Adansi Rural Bank Limited as a case study. The result indicated that diversion of loan by customers constitute the major cause of credit default by customers (Mean=2.58, s.d=0.607). The low standard deviation value means that majority of the credit officers identified diversion of credit as a major cause of loan default. The second major cause of credit default at the bank was identified as customer business failure (Mean=2.26, s.d=0.653). Poor monitoring of credit customers was also identified as the third major cause of loan default at the bank (Mean=2.21, s.d=0.0.787).

5.2.3 Effect of credit risk Management on Performance of Rural Banks

The descriptive statistics shows that within the period considered, the average return on equity (ROE) was 105.15%. This indicates a very high return on equity to investors. This means that each shareholder's equity invested in the bank generates twice its value. This indicates that over the years, the bank has been doing well in improving profitability. Also, the capital adequacy ratio within the period averages 22.5%, which is relatively high compared to the industry average of 15%. The higher CAR indicates that the bank is more liquid and reliable

The result of the correlation analysis shows a positive relationship between ROE and CAR, Meaning that an increase in CAR leads to an increase in ROE, and vice-versa. However, the negative relationship between NPLR and ROE indicates that an increase in NPLR leads to a decrease in ROE. The regression result (See table 4.8) indicates that credit management has significant impact on the performance of the banks. This means that if rural banks prioritize their credit management practices it will positively improve their profitability.

The study found that the predictive power of the regression model was quite high (i.e. Prob>F = 0.05). Thus, this model can be used in similar studies to predict the relationship between credit risk management and rural banks financial performance. The result means that credit management has significant impact on the performance of rural banks. The R-square value of 0.4445 indicates that 44.5% of the variations in performance (ROE) were explained by credit management. This means that 55.5% of variations in the bank's performance were as a result of other factors such as managerial competence, liquidity management and marketing skills.

5.3 Conclusion

Most rural banks are unable to stay in business because of their inability to manage credit risk effectively. For instance, Asiedu-Mante (2011) reported that most rural banks are unable to compete with commercial banks because of their poor credit management practices. Against this backdrop, the study evaluated the credit management of rural banks using Adansi Rural Bank as a case study. The bank was selected for the study because of its impressive financial performance over the years. Both primary and secondary data were collected for the purpose of meeting the objectives of the study.

The primary data was collected mainly from credit officers of the rural banks whiles the secondary data in the form of Return on Equity, Capital Adequacy Ratio, and Nonperforming loan ratio was collected from 2009 to 2014. The credit appraisal, credit disbursement and credit monitoring and collection were analyzed per the questionnaire. The result indicated that the bank's credit management practice is satisfactory since it follows the key appraisal system. Also the bank has been able to reduce its loan default rate below the benchmark set for rural banks. The study further established that the main causes of loan default in the bank are loan diversion, customer's business failure and poor monitoring practices of the bank. The study also found that, credit management has significant impact on the performance of rural banks in Ghana.

5.4 Recommendation

Top management must ensure, in managing credit risk, that all guidelines are properly communicated throughout the organization and that everybody involved in credit risk management understands what is required of him/her. Sound credit risk management system (which include risk identification, measurement, assessment, monitoring and control) should strictly be guided as policies and strategies which clearly outline the purview and allocation of a bank credit facilities and the way in which credit portfolio is managed; that is, how loans were originated, appraised, supervised and collected.

Second, the bank must improve its monitoring practices since the major cause of loan default is diversion of funds. This can be done by setting a monitoring and recovery team in place to visit loan customers to ensure that the loans are applied for the intended purpose. If there is a recovery unit already in place, then the team of officers should be adequately resourced to ease and improve the efficiency of their work. Also, the bank should improve its information technology system to electronically monitor the accounts of loan customers at various branches to be abreast with how they are amortizing their debt.

Thirdly, the study recommends that the banks should provide non-financial services in the form of training and business advice to their customers. This will go a long way to improve their business performance and enhance their ability to repay their loans.

Furthermore, the findings revealed that almost a third (44.5%) of the variations in performance (ROE) of the bank is explained by credit management. This means that the bank must prioritize its credit management since it has significant impact on its performance. Finally, since the bank has a very high Capital Adequacy Ratio (CAR) the study recommends that the bank should advance more loans to support the rural economy. This will enable the bank to earn more interest and therefore record better profitability.

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APPENDIX

Appendice A: Questionnaire

Kwame Nkrumah University of Science and Technology

KNUST School of Business

<u>(Questionnaire for credit officers and managers)</u>

Dear Respondent,

I am a student of Kwame Nkrumah University of Science and Technology (KNUST), studying for a Master of Business Administration (MBA) degree. An academic work is been conducted to examine credit management practices of a rural banks. Your bank has been chosen for this purpose. I would be very grateful if you could spare me few minutes of your time to respondent to questions in this instrument. All information provided will be used solely for academic purposes and will be treated with utmost confidentiality.

Please answer the questions by ticking the appropriate boxes or writing in the spaces provided.

Thank you.

Section A: Professional Background of Respondents

1. Your Current position: (Please tick)

Risk Manager [ ]Credit risk manager [ ] Credit risk officer [ ]

2. Banking experience

1-5 years [ ] 6-10 years [ ] 11-15 year [ ] More than 15 years [ ]

3. Your experience in credit field:

Under 1 year [ ]

1 – 5 years [ ]

Over 5 years – 10 years [ ]

Over 10 years [ ]

Section B. Credit management practices

The questions under this section seek your opinion on the credit management practices of Adansi Rural Bank Ltd.

4. Which categories of loan customers do you deal with? Tick as many as applicable

Agric [ ] Mining [ ] Trading [ ] Small scale entrepreneur [ ] Contractors [ ] Salaried Workers [ ] Manufacturing [ ]

5. How do you rate the following factors before granting loans? Please circle your choice

Factors	**Very high(4)**	**High(3)**	**Moderate(2)**	**Low(1)**
Character	4	3	2	1
Security	4	3	2	1
Ability to pay	4	3	2	1
Borrower repayment history	4	3	2	1
Profit and Loss statement	4	3	2	1
Future prospects of the business	4	3	2	1
Cash flow statement	4	3	2	1
Experience of credit utilization	4	3	2	1
Profitability	4	3	2	1
Financial/Capital Structure	4	3	2	1
Skills and expertise a of management	4	3	2	1

6. How often do you monitor the loan portfolio?

Monthly basis [ ]   Yearly [ ]   When there is default [ ]

7. Who are those in charge of loan monitoring?

Credit officers [ ]   All workers [ ]   Branch Managers [ ]   Special Personnel [ ]

8. Will you say that your loan monitoring process is helping the bank to control credit default?

Yes [ ]   No [ ]   Don't know [ ]

9. What type of loans do you grant? Tick as many as applicable

Short Term Loan [ ] Medium Term Loan [ ] Long Term Loan [ ]

Other (Specify) ---

10 Please indicate the extent to which you agree or disagree with the following

Statement by ticking the appropriate boxes.

Where: strongly agree=5, Agree=4, Neutral=3, Disagree=2, Strongly disagree

ID	**STATEMENT**	**1**	**2**	**3**	**4**	**5**
1	Workers are regularly trained on credit risk					
	management					
2	The training courses are effective					
3	The bank calls for your opinion when credit risk management needs adjustment					
4	The bank follows the lending principles to evaluate the credit worthiness of customers before granting credit.					
5	There is regular credit review at the bank					
6	The bank effectively monitor customers who have been offered loans					
7	Credit customers are given expert advice on how to effectively utilize the credit granted					
8	Credit is granted based on merit					
9	There is no political interference in the profit granting process					

10	There is a comprehensive and effective credit risk strategy and policies					
11	There is an appropriate Credit Administration and measurement.					

9. Has the implementation of Credit Risk Management helped to minimize bad debts in your firm?

Yes [ ]   No [ ]

<u>Section C: Challenges of credit risk management Practices</u>

Do you encounter problems in your Credit risk management practices? Yes [ ] No [ ]

13. Rank the challenges below by circling the appropriate answers: Where 3=**major challenge,2=moderate challenge,** 1=**Minor challenge**

Factors	**Major**	**Moderate**	**Minor**
Inadequate appraisal	3	2	1
Inadequate monitoring mechanisms	3	2	1
Board imposition	3	2	1
Staff influence	3	2	1
Inadequate security	3	2	1
Diversion of loans	3	2	1
Customer business failure	3	2	1
Inadequate credit staff	3	2	1

Appendice B: Interview Guide

Kwame Nkrumah University of Science and Technology

KNUST School of Business

(Interview Guide for Chief Credit Manager)

Dear Respondent,

I am a student of Kwame Nkrumah University of Science and Technology (KNUST), studying for a Master of Business Administration (MBA) degree. An academic work is been conducted to examine credit management practices of a rural banks. Your bank has been chosen for this purpose. I would be very grateful if you could spare me few minutes of your time to respondent to questions in this instrument. All information provided will be used solely for academic purposes and will be treated with utmost confidentiality.

Thank you.

Q1. How will you assess the level of expertise of employees in the Risk Management Department of Adansi Rural Bank?

--- ------

Q2. How will you describe the risk management framework and policies of your bank over the years? ---

----

-- ------

Q3 What Risk Management Strategy is adopted by the bank?

-- ------

Q4. What does the risk Policy say about the quantum of loans (credit) that should be granted to customers?

-- -----

-- **Q5.**

What are the Risk Monitoring and Supervision mechanisms of the bank?

………………………………………………………………………………………………………

………………………………………………………………………………………………………

………………………………………………………………………………………………………

…………………………………………………………

Q7. In your view, has the bank been successful in managing its risk exposure? Please elaborate on your answer?

-- ------

Q8. What are the challenges you face in managing risk in your bank?

-- **Q9.**

Are these challenges affecting the risk management process of the bank in a serious manner?

-- ------

--- ------

Q10. How are these challenges being managed in the bank?

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Appendice C: Other Relevant data

SUMMARY OF REGIONAL RCB's DISTRIBUTION – 2014

	REGION	**NUMBER**
1.	ASHANTI	25
2.	CENTRAL	21
3.	EASTERN	22
4.	BRONG AHAFO	20

5.	WESTERN	14
6.	VOLTA	12
7.	GREATER ACCRA	7
8.	UPPER EAST	5
9.	UPPER WEST	4
10.	NORTHERN	7
	TOTAL	**137**

Source: ARB-Apex Annual Rural Banks Distribution Reports

ADANSI RURAL BANK LIMITED
STATEMENT OF INCOME
FOR THE YEAR ENDED DECEMBER 31, 2014

		2014	2013
		GH¢	GH¢
Interest Income	3	8,312,008	5,825,927
Interest Expense	4	(1,061,090)	(742,923)
Net Interest Income		**7,250,918**	**5,083,004**
Commissions and Fees	5	1,110,439	730,798
Other Operating Income	6	116,720	50,551
Total Income		**8,478,077**	**5,864,353**
Operating Expenses	7	(6,312,679)	(4,609,185)
Loan Impairment Charge		(171,972)	(221,851)
Net Profit before Taxation		**1,993,426**	**1,033,317**
Provision for Taxation	8	(167,515)	(107,463)
Profit After Taxation		**1,825,911**	**925,854**
Other comprehensive income			
Changes in fair value of shares		28,260	7,482
Total comprehensive income for the year		**1,854,171**	**933,336**

Notes 1 - 19 form an integral part of the financial statements.

ADANSI RURAL BANK LIMITED
STATEMENT OF CASH FLOW
FOR THE YEAR ENDED DECEMBER 31, 2014

	2014	2013
Cash Flow from Operating Activities	GH¢	GH¢
Profit for the year	1,993,426	1,033,317
Adjustment for:		
Depreciation	286,067	292,187
Development Fund applied	(6,310)	(43,856)
Changes in Fair values of shares	(28,260)	0
Staff Fund Applied	(19,572)	0
Prior Year Adjustment	281,270	0
	2,506,621	**1,281,648**
Change in Advances to Customers	(3,407,381)	(3,428,098)
Change in Other Assets Accounts	(1,999,878)	88,272
Change in Deposits	7,814,753	2,443,716
Change in Creditors and Accruals	855,128	1,267,260
	5,769,243	**1,652,798**
Tax Paid	(48,678)	(75,116)
Net Cash from operating Activities	**5,720,565**	**1,577,682**
Cash Flow from Investing Activities		
Purchase of Fixed Assets	(970,578)	(400,001)
Increase in Long Term Investments	28,259	0
Increase in Short Term Investments	(3,150,000)	(1,080,000)
Net Cash from Investing Activities	**(4,092,319)**	**(1,480,001)**
Cash Flow from financing Activities		
Issued of shares	149,296	388,038
Decrease in Long Term Loans	(690,112)	699,445
Dividend Paid	(321,730)	(176,273)
Net Cash from financing Activities	**(862,546)**	**911,210**
Net Increase in Cash and Cash Equivalents	765,700	1,008,891
Cash and Cash Equivalent at 1st January	3,938,142	2,929,251
Cash and Cash Equivalent at 31st December	**4,703,842**	**3,938,142**
ANALYSIS OF CASH AND CASH EQUIVALENTS AS SHOWN IN THE STATEMENT OF FINANCIAL POSITION		
Cash on Hand	1,183,255	786,593
Other Banks	120,253	1,128,156
Apex Bank Clearing Account	2,148,548	1,192,726
Apex Bank Deposit Account	1,251,786	830,667
	4,703,842	**3,938,142**

Notes 1 - 19 form an integral part of the financial statements.

ADANSI RURAL BANK LIMITED
STATEMENT OF FINANCIAL POSITION
AS AT DECEMBER 31, 2014

	NOTES	2014	2013
		GH¢	GH¢
ASSETS			
Cash and Short-Term Funds	9	4,703,842	3,938,142
Short Term Investments	10	10,720,000	7,570,000
Long Term Investments	11	41,404	13,145
Loans and Advances	12	16,257,403	12,850,022
Other Assets	13	4,900,184	2,900,306
Property, Plant & Equipment	14	2,561,538	1,877,027
Total Assets		**39,184,371**	**29,148,642**
LIABILITIES			
Deposits	15	28,613,774	20,799,023
Taxation	8	165,540	46,704
Creditors and Accruals	16	4,171,499	3,316,371
Total Liabilities		**32,950,813**	**24,162,098**
NON- CURRENT LIABILITY			
Long Term Loans	17	**501,239**	**1,191,351**
Total Liabilities		**33,452,052**	**25,353,449**
EQUITY			
Stated Capital	18	828,273	678,977
Statutory Reserve	19	777,036	548,797
Income Surplus		3,548,735	2,265,410
Development Fund	19	145,938	60,952
Staff Fund	19	392,932	229,913
Capital Surplus	19	39,404	11,144
Total Shareholders Funds		**5,732,318**	**3,795,193**
Total Liabilities and Equity		**39,184,371**	**29,148,642**

Notes 1 - 19 form an integral part of the financial statements.

The financial statements were approved on 27/04/ 2015 and signed on behalf of the Board by

DIRECTOR DIRECTOR