

**Assessing Credit Management Practices in Savings & Loans
Companies: A Case Study of First Allied Savings & Loans Ltd, Ksi**

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ABSTRACT

This study assessed the credit management practices at First Allied Savings & Loans Ltd and their effect on performance. The main objectives of the study were to identify the credit management practices at First Allied Savings & Loans and their effect on performance. This was against the backdrop of the increasingly risky nature of the financial landscape and the high incidence of non-performing loans due to the lack of well diversified and efficient strategies for credit delivery which has crippled a lot of financial institutions and plunged them into crisis. The descriptive survey method was used for the study. The sample size comprised of 33 respondents who were purposively selected in order to obtain the kind of data that was required for the study. Questionnaires were distributed in order to gather the primary data together with an interview guide. Secondary data was obtained from financial statements of FASL from 2009 to 2014 in order to conduct a cross sectional survey to reveal performance trends over the period. The research revealed that one of the hallmarks of the credit management practices of FASL was the client appraisal adopted by the institution which allowed for a comprehensive assessment of clients as well as identify any inherent risks. It was also discovered that the institution had a credit management policy in place and that it was effective in managing the credit risk associated with the credit granting processes and that if strictly complied with, helped reduced non-performing loans as well as improve the quality of loan portfolio. One major recommendation that was made was for management to put in place measures that would ensure the strict compliance of credit management procedures by credit sectional heads and loan officers as this was identified as a major setback to the quality of loan portfolio and secondly the need for more training programmes to be organized to sensitize the credit staff on modern trends in the credit granting process.

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DEDICATION

I would like to dedicate this work to the Lord God Almighty for his grace, strength and wisdom. Lastly, I would also like to dedicate it to Deborah Korkor Cobbina, a very special friend whose encouragement, wisdom and motivation has inspired me to get to this point of my academic journey.

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LIST OF ABBREVIATIONS

FASL – First Allied Savings & Loans Limited

ROCE – Return On Capital Employed

BPP – Brierley Price Prior University

OCC – Office of the Controller of Currency

AgDM – Agriculture Decision Maker

BOG – Bank of Ghana

CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Credit management is a comprehensive process made up of the monitoring of loan facilities, extension of credit, distinguishing the market segments as well as delineating the returns generated. The policy on credit management comprises systems, guidelines and principles that serve as a blueprint for employees in the credit department in awarding loans and steering the total collection of credit facilities. The policy on credit management is described as a combination of principles devised to reduce expenditure connected with loan delivery while taking full advantage of the gains that can be generated from them (McNaughton, 1996). One critical prerequisite for being able to supervise credit delivery effectively is the capacity to astutely and competently administer the lines of credit to clients. To be able to reduce the vulnerabilities associated with uncollectable loans, companies must exercise a better understanding of economic capacity of clients, history of customers' credit rating and varying repayment arrangements. In order to make an intrusion into new markets as well as enroll more clients depends on the competence to rapidly and effortlessly make well-informed credit decisions and set appropriate lines of credit.

It is obvious that the primary functionality of a financial institution is the provision of loan facilities to deserving clients located in their sphere of jurisdiction. Banks are in business with the sole aim of making profits and so, they seek to generate profits through giving out loans and investment in other assets. Against this backdrop, loan supply and delivery are part of the core business activities of financial institutions because without giving out credit in the form of loans and advances to individuals and firms, their main objective for being in business would be

defeated. It will be a challenge to enact the most favourable credit policy as the best amalgamation of the variables of credit policy is quite arduous to acquire. An institution might decide to manipulate some of the variables within a period and observe the effect. It should be noted that the firm's loan guide is greatly influenced by economic conditions (Pandey, 2008). The guidelines of the firm on credit management may experience a shift as the prevailing conditions of the economy also metamorphose. The success of lending out credit depends on the methodology applied to evaluate and to award the credit (Ditcher, 2003) and therefore the credit decision should be based on a thorough evaluation of the risk conditions of the lending and the characteristics of the borrower.

First Allied Savings & Loans was established in September 1996 with the goal of providing innovative financial services to meet the needs of the micro, small and medium scale enterprises through the provision of tailor-made credit products designed to meet the needs of these stakeholders on a sustainable basis. Over the past eighteen (18) years, it has grown with a network of 23 branches providing the financing needs of many enterprises. However, dealing with the informal sector comes with a lot challenges especially in ensuring payment of credit facilities that are granted. It therefore becomes imperative to establish a credit management system that seeks to effectively mobilize surplus funds that go out to deficit units promptly to guarantee sustainability of the financial institution in the sector.

1.2 Statement of the Problem

Availability of credit management in banks could act as a catalyst for rapid development in their area of jurisdiction. By channeling available surplus funds to the immediate society, the operational policy of the banking system to a large extent will not only provide the space for

economic development in the locality but also the structure and direction of growth as well as income distribution.

According to the Bank of Ghana Supervision Report 2013, monetary growth as well as credit to the private sector generally moderated in the year 2013. Total outstanding loans given to public and private institutions grew by 30.2% compared with an increment of 39.3% in 2012. This was due to a reduction in economic activity in the Ghanaian economy as a result of the energy crisis coupled with declining commodity prices. This led to a decrease in the availability of credit to institutions which as established earlier is a major catalyst for growth. This has therefore made it imperative for financial institutions to come up with solid credit management tools that guarantee sustainability as well as availability of credit to support economic growth.

A non-performing loan is a loan granted by a bank or financial institution on which interest and principal repayments are not paid timely. According to the International Monetary Fund (IMF), a loan is termed as non-performing if it is 90 days (3 months) overdue. A loan can also be categorized as non-performing if it is less than 90 days behind schedule but installments are no longer expected. Repayment of principal and interest on loans create a stream of cash flows for the bank. Banks generate their profits from these interest payments. Therefore a high NPL portfolio leads to a reduction in the profitability and their ability to further perform the art of granting more credit to borrowers. This ultimately has a negative effect on the economy.

The issue of giving out credit especially to players within the informal sector comes with a lot of challenges as asymmetry of information is very high coupled with the lack of collateral to secure loans. The current blueprint for credit delivery are not well diversified or efficient, and therefore are not able to completely satisfy the differing demands of the market and different classes of

end-users within the savings and loans sector according to Asiamah & Osei (2007). This makes dealings in this area very risky and so it becomes important for financial institutions operating in this area to put in place effective credit management systems that seek to maximize value on loans giving out as risky assets to their clients. Since revenue or interest income is the live wire of financial institutions, it is imperative for them to institute measures that can guarantee a safety net in getting back their returns as well as the loans giving out and these are what this research work seeks to address. A lot of research has been done on credit models and credit risk management however there seems to be a gap in determining the extent to which credit management affects performance in financial institutions. A good quality loan is that which satisfies the bank's quest for maximizing returns and also has a low default risk. To achieve this, banks need effective credit management to avoid possible fold up. It is in this line that a study is being conducted to determine what an effective credit management is and its effect on performance in financial institutions.

1.3 Objective of the study

The overall objective of the study is to determine how credit management affects the performance of financial institutions specifically First Allied Savings & Loans.

1.3.1 Specific Objectives

- a) To identify the various credit management practices in First Allied Savings & Loans
- b) To determine how credit management practices and policies are applied in the selected institution in Ghana.
- c) To determine the strengths and weaknesses as well as challenges associated with the application of the credit management policies in the selected institution

d) To evaluate the effects of the credit management on the performance of the institution in terms of profitability and quality of loan portfolio.

1.4 Research questions

a) What are the credit management processes in First Allied Savings & Loans Ltd?

b) How are credit management processes and policies applied in the selected institution in Ghana?

c) What are the strengths and weaknesses as well as challenges associated with the credit management processes in the selected institution?

d) What is the effect of credit management on the performance of the institution in terms of loan targets, quality of loan portfolio, loan recovery and interest income?

1.5 Significance of the study

This research shall be of great relevance to the organization under study as well as other financial institutions. The non-financial business firms whether manufacturing or service centered shall also benefit from the research findings. This is because the results of the study shall enable the users especially banks to be able to assess and evaluate their credit policies and to review their operations critically for a more result oriented approach in dealing with their credit facilities. This study shall also be useful to all business enterprises involved in granting commercial credit and other users of the study. It will also be useful to government institutions that are directly involved with financial institutions as it will provide a source of knowledge into the core business of banks. Investors who are interested in investing strongly in financial intermediaries shall also benefit from this study as well.

1.6 Scope of the Study

This important research will concentrate on credit management in financial institutions in Ghana in general and First Allied Savings & Loans Ltd in particular. The study is limited to all the credit facilities of First Allied Savings & Loans Ltd which covered a period of five (5) years. Emphasis shall be placed on the effective credit management of loans and advances as well as the control measures put in place for recovery.

1.7 Limitations of the study

Budgetary expenses covering the printing, journeying to meet respondents and assistance were demanding. The researcher attempted to decrease expenses which might not have had a noteworthy effect on the study.

Feedback from staff respondents was also another constraint due to lack of time, resulting in the case of unanswered and semi-answered questionnaires. Most of the respondents had to interrupt their work in order to provide answers to the questionnaires making it a challenge.

With the issue of time restraint, the researcher had to be carrying out his thesis work while working on a fulltime job amid that brief time. This placed a restriction on the yearning to carry out a more in-depth analysis into the variables under study. The duration of the thesis was also short thereby preventing the researcher from doing an in-depth study of the research work.

1.8 Overview of the Methodology

A longitudinal study design was used to gather quantitative data spanning the period from January 2009 to December 2014 to establish the relationship between credit administration practices and performance. Questionnaires together with an interview guide were used to gather

primary data while the secondary data was obtained from financial statements of the institution from the year 2009 to 2014.

1.9 Organization of the Study

The research work is divided into five chapters. The first chapter centers on the introduction. It entails the background of the study, the statement of problem, objectives of the study; the research questions, the statement of the problem, the importance of the research work, the scope of the study, limitations of the study and a brief overview of the methodology employed in the research work.

The second chapter focuses on the review of literature relevant to the research work being conducted.

The third chapter focuses on the research methodology as well as the organization profile of FASL. The chapter consists of the population, the sampling size and the sampling method, the research instruments to be used for gathering relevant data and analyzing them as well as the profile of FASL. Chapter four presents an analysis of the data obtained from the research work as well as the discussion of the findings. Hence the data will be presented and analysed in graphical form to provide a greater comprehension of the findings.

The final chapter, the chapter five, deals mainly with the summary of findings, recommendations and conclusions made by the researcher.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter summarizes the information from the available literature in the same field of study. It will review theories of credit management as well as empirical studies on credit management and financial performance in Ghana and in other countries.

2.1 Credit Management

Credit management is one of the most essential activities in any company and cannot be neglected by any entity involved in the supply of credit lines no matter the nature of its business. It is the mechanism to ensure that customers will pay for the products delivered or the services rendered. Myers and Brealey (2003) consider it to be made up of techniques and strategies used by an enterprise to ensure that an optimal level of credit and its effective management are kept. This is one aspect of monetary administration including credit examination, credit assessment, credit scoring and credit reports. Nelson (2002) considers credit management as apparently the way by which an enterprise superintends over its credit sales in a manner that creates greater opportunities for making higher profits. This is a prerequisite for any business engaged in provision of lines of credit since it is not possible to completely eliminate credit risk default.

The higher the amount of accounts receivables together with a longer duration, the greater the monetary as well as opportunity costs incurred to sustain them. If these debts are not collected promptly and urgent cash needs surface, a firm may likely resort to borrowing and the opportunity cost translates into the interest expense paid. Nzotta (2004) opined that credit management greatly influences the success or demise of banks and other financial institutions.

This is because the failure of deposit banks is determined largely by the quality of credit decisions and thus the quality of the risky assets. He further notes that, credit management provides a leading indicator of the quality of deposit banks' credit portfolio. One important precondition for effective credit management is the ability to intelligently and efficiently manage customer credit lines. He continued by stating that to reduce over exposure to bad debts, overbooking and insolvency, financial institutions should have a better understanding of the financial strength of customers, credit account history and evolution of payment methods of clients.

According to Asiedu-Mante (2011) credit management involves the setting up of legal and formal systems and policies that will guarantee that the appropriately designated staff are well-positioned to grant credit, the facility goes to the people with the right credit history, the loan is given out for profitable activities or for businesses which have a strong financial and technical viability, the correct amount of credit is disbursed, the credit can be recovered and the flow of management information is sufficient within the organization to allow for effective monitoring of credit activity. He therefore viewed it as the putting in place of systems that act as a check right from the credit granting process to the point of collection.

Credit Management likewise alludes to the proficient mix of four noteworthy credit approach parameters to ensure convenient collection of advances conceded to clients and in the meantime build their trust in and devotion to the financial organization (Van Horne, 2007). The main variable is an evaluation of the nature of the client's record operation in the establishment. This takes into consideration the correct examination of the capacity of the clients to meet installments promptly. The second strategy variable is that of setting up the right credit period. In

this manner, the bank should give sufficient time to permit loyal customers the chance of deriving the full advantages of the credit. Such period should not be too long to put the bank in a distraught position. The third parameter is the rebate or the sweetener given to clients as a way of inspiring them to reimburse their credit facilities on time. Such sweeteners must be sufficiently appealing before the goal can be accomplished. The last variable looks at the level of expenditure that can be permitted in the recovering of debts. The inference here is that the bank should not give out credit where the cost to be spent on retrieving the obligation will probably surpass the obligation itself. To mix these variables into a proficient workable framework obliges the establishment of a watchful arrangement, controlling and coordination of all accessible human and material assets Van Horne (2007).

Office of the Controller of the Currency (2011) defined Loan portfolio management as the mechanism by which risks that are inherent in the credit granting process are controlled and effectively administered. It involves evaluating the steps taken by management of financial service providers of credit to identify and exercise adequate control over the element of risk throughout the credit delivery process. The evaluation centers on what management does to unveil the issues before they become problems. Office of the Controller of the Currency identified nine elements that ought to be part of the process of portfolio management. The nine components include:

1. Evaluation of the credit culture,
2. Objectives of the portfolio and risk tolerance limits,
3. Management of information systems,
4. Segmentation of portfolio and the diversification of risk objectives,
5. Analysis of loans originated by other lenders,

6. Aggregate policy and underwriting exception systems,
7. Stress testing analysis of portfolios,
8. Autonomous and effectual control functions,
9. Analysis of portfolio risk/reward trade-offs

Credit management starts with a sale or the granting of a facility as in the case of a bank and does not stop until the full and final payment has been made. Technically a transaction cannot be termed as complete until full payment has been made. Good lending therefore ensures that the borrower follows the repayment plan set up for him in a timely and prompt manner otherwise, this eventually leads to the total loss of interest that the institution could have earned due to the opportunity cost of the loan, the risk involved and time value of money. Credit management is primarily concerned with the effective management of debtors as well as judicious financing of receivables. The objectives of credit management can therefore be expressively stated as safeguarding the portfolio of the companies' investments in debtors and maximizing operational cash flows. Policies and practices ought to be rigorously enforced for granting credit facilities to customers, collection of repayments that are due and limiting the high risk factor of non-payments.

2.2 Credit Culture

Credit culture, according to Kamath et al (2010) can be defined as a bank's approach to all issues correlated to the administration of credit risk. He continued by stating that if it is to attain a healthy credit risk portfolio, it must be synchronized with the strategic direction and organizational culture of the financial institution. The culture must have the capacity to deliver the service required by the institution to meet the needs of its clients in a timely manner. It can

only do this if it is in harmony with the overall strategic direction of the financial institution and is pioneered by the top echelon of the financial institution. Because the credit culture ought to maintain a balance between assuming new risks and imposing limits on the amount of risk at the same time, it is bound to run into all of kinds of resistance. Top management is the only source that can ensure that the culture not only supports appropriate credit standards, but is also profitable enough not to cause the bank to lose out on good business.

Solid credit standards, according to Rouse (2002), will unavoidably cost the bank some business, which in retrospect would have been beneficial. However, when the decision is being contemplated on, hindsight is unavailable. Credit culture which is an integral part of credit management takes into consideration the fact that there is some business the bank has to be willing to lose and so it becomes imperative for an agreement to be sought and a consensus reached as to the yardstick to be applied in determining which business to do away with throughout the bank. This policy has to be established by management and should articulate the type and level of risk the bank is ready to accommodate and the return it expects from taking on stated risk levels, both at the customer and portfolio level.

In the view of Gallinger and Ifflander (2002), credit standards translate the culture into actions. They should consider the terrain of the bank's operations, its arrangement and the character and the level of preparedness of staff involved in credit decisions. This enables an effective credit management system to be implemented buoyed by a strong culture that is able to convert policies into proven results.

2.3 The Loan System

Before endorsing any credit facility, it behooves the bank to ensure that the debtor has a practical and viable proposal. However, the marketability of a loan proposition does not depend all together on the quantum of collateral provided by the borrower. The financial intermediary needs to establish the amount of credit risk latent in the credit proposal and within the boundaries of that risk, a decision has to be made whether to accept or reject the proposal. An effective credit management system provides the right framework for such decisions to be made Puri and Poli (2013)

For any provision of credit line within the retail sector for instance, a borrower must have a pre-existing capacity to repay the loan either from his/her salary or income from self-employed business or profession. But financing in the commercial sector is somewhat different. A borrower is not always required to have a pre-existing capacity to repay a working capital or a term loan that he or she seeks from the bank. The capacity to repay is built over the duration of the facility with the help of the bank loan. As the borrower's business expands, incremental cash flows are generated from which the debt can be serviced and repaid as per agreement. Growth of business in the right direction supported by the bank credit drives the cash flow of the business upwards. It is the assessment of incremental cash flows which helps the lender to determine the repayment capacity of the borrower to meet loan obligations in a timely manner (Poli and Puri, 2013)

Bank lending is premised on the assertion that the debtor has the willingness and capability to requite the loan at all stages in their business transactions with the bank. However, the capacity to pay back depends on future income streams and the disposition to repay has to be based on the

pre-existent commitment that has been undoubtedly demonstrated by the borrower. It is a statement of faith because the lender relies largely on the debtor's adroitness and competence despite business downturns to at least guarantee future cash flows and ensure the flow of regular payments.

The three conditions which should be in existence at the time the borrower seeks a loan from the bank to be able to strengthen for instance his line of business according to Poli and Puri (2013) are:

- i) Willingness or intention on the part of the borrower to repay the loan as per the agreement
- ii) The purpose for which the loan is requested or sought for by the borrower
- iii) The conditions which can set the trend for the future

The willingness or desire to pay back a facility granted is somewhat simple to establish for an existing borrower in practice. If a borrower happens to have a sound history of payment of loans including debt servicing, they are likely to continue making regular payments in the future as well. The only circumstance that could influence this pre-condition is an uncontrollable event such as fire outbreak or a major infrastructural destruction. This condition is strenuous to judge for anyone, much less to talk of a new borrower, if he has no previous business experience or skill.

The purpose for which the loan is sought should be carefully documented. The bank must make sure that the final application of the credit should be for the documented purpose only. The conditions which form the basis on which future trends can be mapped are the inherent business risks, performance history of the borrower in terms of financial positions/trends, credit referencing that shows past dealings with lenders and repayment records, and the experience and skills the borrower possesses in running his/her business Poli and Puri (2013). These factors are

necessary in carrying out an effective appraisal of the customer and provide the basis for making well-informed decisions as regards the credit granting process.

2.3.1 Principles of lending

Gaurav (2010) pinpointed certain criteria which are universally adhered to by most financial institutions in appraising credit propositions as follows:

- ❖ **Safety:** The banker must guarantee that the amount granted by him reaches the legitimate debtor and is appropriated in a manner that will make it secure at the time of giving as well as remain so throughout the period, and subsequent to fulfilling a valuable need in the business where it is utilized, is reimbursed with premium.
- ❖ **Liquidity:** The debtor ought to be in the capacity to make payments within a feasible time frame after a notice of repayment is sent. This is termed as the grace period and failure to meet it usually attracts a penalty.
- ❖ **Purpose;** The objective ought to be monetarily compensating so that the cash stays secured as well as provide an ensured wellspring of monetary streams to meet reimbursement plans.
- ❖ **Profitability:** the bank should be able to obtain some reasonable profit from the loan
- ❖ **Security;** Security is considered as a protection or a coverage to fall back upon in the event of a crisis
- ❖ **Spread;** ensuring that advances are spread across a broader spectrum of economic activities.

2.3.2 Credit appraisal techniques

Guidelines for Commercial Banks in Pakistan (2009) indicate that banks should as a matter of need operate within a sturdy and well accentuated criterion for new loan portfolios as well as the broadening of existing credit lines. Credit facilities should be expanded within targeted markets and as well as the ambits of the lending strategy of the institution. Before allowing a credit facility, the bank must carry out an assessment of risk profile of the customer/transaction. This may include:

- a) Credit analysis of the borrower's industry, and macro-economic factors.*
- b) The sole aim of the credit and source of repayment.*
- c) The performance / repayment history of borrower.*
- d) Assess/evaluate the repayment capability of debtor.*
- e) The Proposed terms and conditions as well as covenants.*
- f) Perfection and enforceability of collateral assignments*
- g) Approval from appropriate authority*

All these components aid in the easy identification of any inherent risks which can provide solid information that eventually facilitates the evaluation of the customer's application as well as provide the necessary platform for an effective profiling of clients.

Essentially, problems arise because lenders are not well informed about the peculiarities of would be debtors, and so it becomes impracticable, for financial institutions to know which customers are good and which ones are not (Fraser, 2012). According to Ahmad (2004) there is no system that can provide a hundred percent protection against bad loans as situations can sometimes overturn the best credit strategies of borrowers. This implies that no amount of credit management measures put in place to forestall delinquencies can ensure a zero default rate.

However, they can aid in ensuring that defaults are brought to the barest minimum thereby leading to a healthy loan portfolio.

2.3.3 Risk Associated with Lending

OCC (2011) identified elementary mechanisms of controlling credit risk as robust underwriting, extensive financial analysis, adequate appraisal techniques, credit documentation practices, and sound internal controls. These principles constitute a fundamental role in credit management as they help to ensure the sound management of credit portfolios in a manner that allows the financial institutions to maximize returns on loans granted as well as reduce economic losses from bad loans.

Kay (2002) considers lending risk as the spreading of economic losses because of unforeseen changes in the credit nature of counterparty in an economic arrangement. He likewise views it as the likelihood of default or any kind of inability to maintain a money related understanding. Credit risk forms a major component of credit management and so it becomes part of the credit management process. When unexpected situations arise that affect the credit worthiness of counterparties, it eventually leads to losses that affect both parties which in this case is made up of the bank and the customer. Credit management therefore seeks to provide strategies that can help limit such losses through the effective forecasting of such risks and the application of sound principles of credit management.

2.3.4 Credit Risk Control

Credit risk is the probability that the return supposed to be earned on an investment or risky asset extended will depart from that, which was expected. Coyle (2000) characterizes credit risk as debts emerging from the unwillingness or failure of loan clients to meet their commitment of

what is outstanding in full and on time. The major sources of credit risk include limitation in institutional capacities, unsuitable guidelines on loan management, high interest rates, lack of effective supervision of credit lines, unsuitable laws, low levels of capital & liquidity, poor loan underwriting, reckless lending, poor credit appraisal, poor practices of lending, interference by government and the inability to enforce oversight responsibility over financial institutions by the central bank. To reduce these risks, it is fundamental for the money related framework to have; all round strongly funded banks, provision of financial services to an expansive range of clients, sharing of credit data about borrowers through credit reference departments, adjustment of premium rates, decrease in non-performing advances, building of higher levels of deposits gathered by banks and expansion of credit to prospective clients. Advance defaults and nonperforming credits should be lessened (Bank Supervision Annual Report, 2006; Laker, 2007; Sandstorm, 2009).

2.3.5 Addressing Risks Associated With Credit Management

The risks associated with granting loans can result in insolvency issues, which in a compelling condition can lead to a bank encountering serious money related emergencies, resulting in the wiping off of capital, indebtedness and could bring a financial institution to its knees.

To distinguish and deal with the dangers connected with credit administration, the Basel Committee on Banking Supervision in its Publication No. 54 issued in September 2000 plotted the accompanying measures:

- Establishing a relevant credit risk environment
- Operating under a safe credit delivery process
- Maintaining an appropriate credit administration, measurement and monitoring process;

- Ensuring adequate controls over credit risk
- The role of supervisors.

The highlights of the measures raised by the Basel Committee on Banking Supervision (2000) as indicated above are as follows:

2.3.5.1 Establishing An Appropriate Credit Risk Environment

The Board of Directors ought to demonstrate the oversight supervision regarding endorsing and occasionally (in any event every year) critically appraise the credit hazard system and critical credit management strategies and controls of the bank. The outline ought to obviously reflect the bank's resilience for risk and the profit levels the firm expects for assuming different dimensions of risks involved in granting of loans. Top management must take responsibility for implementing the strategy for credit risk adopted by the Board and to develop policies and mechanisms to identify, measure, monitor and control credit risk. These policies and procedures must be able to cope with the credit risk in all activities of the bank.

Banks ought to distinguish and oversee credit exposures in all items and enterprise. Banks should guarantee that risks inherent in items and operations that are different to them are secured by adequate credit administration conventions and controls before they are presented or rolled out, and the proper endorsement sought for ahead of time from the Board or its suitable council.

(Basel Committee on Banking Supervision, 2000)

2.3.5.2 Operating Under A Sound Credit Granting Process

Banks must work within the ambient of a clear, well-laid out credit granting criteria. These criteria ought to give a reasonable distinguishing proof of the bank's biggest business and a

complete undertaking of the borrower or counter-party, and in addition the reason and nature of the loan facility, and its origin of reimbursement. Banks ought to set up a plainly characterized process with the sole aim for approving new credit and in addition the change, recommencement and re-funding of operational loan facilities. (Basel Committee on Banking Supervision, 2000)

2.3.5.3 Maintaining Appropriate Credit Administration Through Measurement And Monitoring Process

According to Signoriello and Vincent (1991), this process comprises the following:

Banks should exercise oversight responsibility over the management of their different credit risk bearing portfolios and establish a mechanism that allows them to monitor conditions of insufficient credits, including determining the level of adequacy of reserves as well as provisions. Banks are urged to deploy a system that has the capacity to supervise the administration of credit through the internal use of a risk categorization mechanism. The rating system should be in consonance with the character, structure and intricacies of a bank's operations.

Banks should be able to develop a data framework and diagnostic methods that furnish administration with the capacity to quantify the credit hazards inbound in all on-and-off activities found on the firm's statement of financial position. The administrative data framework deployed ought to have the capacity to give the fundamental data on the segments of the credit portfolio, including distinguishing varying concentration of risks.

Banks must also design a system that is able to monitor the total composition and health of the credit portfolios and to be able to consider any potential future variations in economic conditions when appraising credits given to individuals and to be able to carry out stress tests on inherent risks.

2.3.5.4 Ensuring Adequate Controls Over Credit Risk

Signoriello and Vincent J. (1991) stated that banks must have an autonomous framework that has the capacity to ensure a continuous evaluation of the firm's credit administration procedure and the outcomes of such audits should be specifically reported to the Board and senior administration for the necessary action to be taken when necessary. The credit granting function of banks must be properly managed and the credit exposures constantly evaluated to ensure that they are within levels that agree with prudential standards and internal limits that have been laid down. Furthermore, they ought to have a mechanism in place for early detection and swift corrective action on retrograding loan portfolios, handling problems and other comparable situations.

2.4 Standards

These incorporate elements, for example, the profundity of assessment required and how far this is adjusted to suit the economic needs and peculiarities of the debtor. There is an exchange off to be made between a wish to comprehend all the components of a loan proposal and expenses involved. How far loan amounts are to be standardized and the extent to which they are to be custom-made to address individual issues of clients are all important in creating sustainable credit standards. Moreover, Santomero (1995) says “structuring facilities to protect the bank should be done in such a way and as far as possible that benefits eventually accrues to the client as well.” An installment plan for a term loan should be designed based on a customer’s cash flow.

Setting standards additionally suggests the recognition of how far the sensibilities of customers will be adjusted against the bank's desire to shield itself against debt exposures. Case in point,

when a client's imperviousness to giving or enhancing security or giving data will be tolerated and considered, then there is the need to educate the customer adequately in order to build their capacity to be able to understand the issues at stake. In creating sound credit standards, it is imperative to include as a critical component, a proper degree of monitoring and control. The point of monitoring according to Hester and Pierce (2002) is to promptly identify deterioration of a loan portfolio and to take corrective measures. The efficiency of such a system depends not only on the ability to identify deterioration, but also the soundness and promptness of the response.

Credit principles should be maintained over the financial cycle and the status quo needs to be kept at all times. They ought not be relaxed in great economic times or over-fixed in awful times.

According to Dyer (2004), banks are confronted with a real dilemma in that if they decide to ignore the market forces and rigidly apply standards; they will avoid credit losses in the short term but will have to lose the good business and market share in the long term. This must be balanced against the need to meet shareholder aspirations. He further went on by stating that there are models of risk-adjusted capital that are widely utilized and the possibility of expected returns related to them. Shareholders do contribute a significant amount of cash capital and expect returns for that. It is therefore hard for banks to sit with a great deal of genuine capital and continue disregarding the need to capitalize on it to its advantage. A strong credit culture can help establish the right symmetry. In the event that the bank truly comprehends its clients and has the right kind of association with them, Adams (2002) supposes it can decide when to buckle

down on measures a little and when to stick to them, if conceivable, in the ambience of a solid client relationship to influence even the most troublesome of clients to see the bank's perspective.

Relationship banking according to Hollensen (2003) is a two way affair and customers would expect some level of support when they are in need of it. If a financial institution wants to get something out of its target business during the period of economic turbulence, it must be willing to give to return the favour when the customer is in a less solid situation. This is because, the ability to offer financial aid to customers during bad times can help build a solid relationship which they tend to reciprocate by providing banks with a lot of cheap deposits during the good times. Rouse (2004) admonishes that relationship banking does not provide a complete solution to bad debts, but it is likely to lessen the incidence of losses during periods of recession.

Credit management as a consequence allows for the right application of credit standards and helps to maintain that equilibrium between rigidly applying administrative procedures and relaxing them to suit the needs of different categories of customers as well as varied economic conditions. Credit management therefore incorporates the right credit standards that allow a financial institution to be able to achieve its strategic objectives through the application of an effective and well-adapted credit regime capable of safeguarding the interests of the firm and at the same time meeting the needs of prospective loan clients.

2.5 Credit Management Policy

It is defined as the tenets and systems set up by top administration that oversee the organization's credit division and investigates execution in the augmentation of credit benefits against set down procedures Jim Franklin (2010). It is essentially a situated composition of rules intended to minimize expenses connected with credit while expanding advantages from it (McNaughton,

1996). Credit administration arrangements involve the credit strategies, credit measures and credit terms. This policy becomes the blueprint which guides the conduct and expectations of all employees entrusted with the responsibility of granting credit and also acts as a benchmark by which performance can be measured against standards set.

2.5.1 Credit Procedures

To accomplish the great objectives of credit administration strategy, Franklin (2010) instructed the endorsement and utilization of credit strategies. To Franklin, credit methods are particular routes in which top administration imposes expectations on the credit division to accomplish the credit administration policies. The credit systems incorporate guidelines on what information to be utilized for credit examination and investigation procedure, provide information regarding procedure, account supervision and cases needing administration's notice. Such credit gathering endeavours incorporate the utilization of reminders, adoption of insurance, the application of legal procedures, the factoring of debtors and final write-offs as highlighted underneath:

2.5.1.1 Reminders

It involves dispatching a request note informing the debtor of the payment owed, and if there is no reply, processes are gradually intensified through more stringent mechanisms Pandey (2008). These other mechanisms include posting a letter of appeal to the client and if he fails to respond, then the customer is contacted by telephone or actually paying a visit to him or her as a way of creating awareness for the person and if it fails then the last resort will be gearing towards legal measures.

2.5.1.2 Insurance policy

This involves an entity seeking to provide coverage for every one of the obligations that are evaluated as non-performing. The firm ought to verify that every facility that has started to show signs of deterioration are completely guaranteed BPP (2002). Insurance agencies guarantee to repay the loan firm in the situation that the indebted person defaults on installment and as being what is indicated as the safety net, the provider will consent to such a course of action only when the financial organization has a viable credit administration framework established (Kakuru, 2001).

2.5.1.3 Factoring debtors

This comprises selling obligations to special financial organizations. The factoring of indebted individuals is a safety oriented measure meant for defending the organization's cash against losses. This the credit firm does by obtaining ahead of time monies locked up with debtors from the factor through an agreement that is reached. This leads to the firm incurring lesser expenses included with disbursement of loans Flouck (2001). Along these lines, the leaser is relieved off the recovery and other managerial expenses incurred in non-performing assets and different exposures included in handling such advances.

2.5.1.4 The use of litigation

This includes the commencement of legal activity against the client who defaults in his installments. This emerges when the loan facility is established as an uncollectible obligation after a significant disruption in the reimbursement plan is noted bringing about undue postponements in collection efforts thus giving the idea that lawful measures may be obliged to

enforce recovery (Kasozi 1998). This is turned to as the last measure and all the more so where the firm's association with the client has been mutually beneficial.

2.5.1.5 Final write off

This is the place in the books of the organization where the obligation is confirmed as irretrievable and thus, it is cancelled off as bad debt. If loan obligations are classified to be non-performing to the point that they can't be collected, it is then better to expunge them from the accounting books to give them a genuine and reasonable representation of the organization's money related position (BPP, 2000).

2.5.2 Credit Management Variables

Key Credit management variables include;

2.5.2.1 Client Appraisal

The initial phase in restricting the risk involved in granting a loan facility includes screening customers to guarantee that they have the readiness and capacity to reimburse the advance. A lot of financial institutions tend to utilize the 5Cs model of credit also known as credit standards to appraise a customer as a potential borrower (Abedi, 2000). The 5Cs act as a guide for financial institutions to improve loan portfolio, as they get to know their customers better. These 5Cs are: character, capacity, collateral, capital and condition.

2.5.2.2 Character

This assesses the client's qualities in order to examine the willingness of the prospective client to meet the credit commitments. Kakuru (2000) highlighted the accompanying variables to consider when investigating applicant's character. This is carried out by factoring the client's savings

conduct from the bank records, the level of training, mental status, occupation dependability, contact, connection to government offices and the past dealings with bank. The borrower who seeks to be a loan beneficiary of cash endowed to the bank by its depositors must be very honest- someone who will keep their word and who can be trusted.

Current trends in technology allow for credit investigation to be carried out helping to not just uncover past impressive and awful conduct in reimbursement of advances and handling of obligations but will likewise uncover the degree of a man's acquisition of credit limit. The higher the building up of a person's credit profile, the higher the response of the person to changes in interest rates or individual circumstances.

2.5.2.3 Capacity

This assesses the client's capacity to pay the obligation when given in the obliged time period. This is fundamental particularly for business, regardless of whether advances are included. This is determined by assessing the estimation of client's capital and resource offered as guarantee against the advance. The borrower must be, in any event, capable, if not a specialist at their employment or in their calling and should be able to produce strong evidence to support the viability or otherwise of the business.

2.5.2.4 Capital

This alludes to the general state of the organisation. "This is ascertained by the analysis of the financial statements with special emphasis on the risks and the debt-equity ratios and also evaluating the customer's firm working capital positions" according to Floucks (2001). The budgetary supervisor can likewise survey the accounting report to discover how much the

proprietor has put into the business as his own stake (BPP, 2000). A decent dependable guideline would be that a bank would not wish to put in more cash than the borrower.

2.5.2.5 Collateral

This alludes to properties like lands, houses, business and private bequests or whatever other property of quality offered as security of the estimation of the credit given out to the borrower (Kakuru, 2001). It is obtained by a lender as a claim on the borrower and on the asset that is secured, and provides a recourse that is available to a bank should the terms of the loan be breached by the borrower. The collateral ought to be secure, readily merchantable and that its quality ought to have the capacity to meet the obligation when sold off in the event that the borrower defaults in payment (Van Horne, 2007).

2.5.2.6 Conditions

These point to the predominant monetary and economic environment which may influence or be a hindrance to the borrower's capacity to pay the obligation and which may turn out to be unbeneficial to the creditor firm. Case in point, under inflationary inclinations, it is inappropriate to extend credit as the leaser is certain to incur forfeiture on the lent sum if not getting lower returns. The credit officer ought to carve a sensible judgment in regards to the possibilities of default and appraise the likelihood of losses under such conditions Pandey (2008). It is critical that the credit guidelines are situated based on individual applications, calling to attention the importance of gathering credit data, credit investigation and credit limits AgDM (2011 redesign).

2.5.3 Credit Risk Controls

Key Credit controls include loan product design, credit committees, and delinquency management. (Churchill and Coster, 2001)

2.5.3.1 Loan product design

Financial institutions can moderate a considerable segment of default risk by coming out with credit items that address customer issues. Credit product elements comprise the size of credit, interest rate and charges, reimbursement plan, guarantee necessities and some other peculiar terms. Loan products ought to be framed to address the particular reason for which it is being sought. (Churchill & Coster,2001)

2.5.3.2 Credit Committees

The establishment of a committee of persons to take decisions with regard to the granting of advances is a vital control in reducing credit (and misrepresentation) hazard. In the event that an individual has the ability to choose who will be loan beneficiaries, which advances will be written off or rescheduled, and the states of the advances, this level of influence can without much of a stretch be mishandled and concealed. While advance officers can serve on the credit board, no less than one other individual with more prominent power ought to likewise be included. The credit advisory group has the obligation for endorsing credit facilities, as well as for observing their advancement and, ought to get involved in delinquency management when borrowers start showing signs of non-repayment.

2.5.3.3 Delinquency Management

To minimize such delinquency, financial institutions can use the following delinquency management methods:

Institutional Culture: One critical way of dealing with delinquency is building an organization ethic that is completely intolerant to defaults and is able provide the avenue where defaulting customers can easily be tracked for repayment.

2.5.3.4 Staff Incentives

Opportunities ought to be created for staff to be actively involved in the loan management process through the establishment of an incentive system that rewards performance. Staff can for example be given commissions for the effort put in the recovery of bad debts as a way of motivating them and this goes a long way to improve productivity as well as the financial position of the organization.

2.5.3.5 Loan Rescheduling

Considering how volatile the target market can sometimes be, it is sometimes commonplace to find customers who might have the eagerness to pay but lack the capacity to do so due to the changing terrain of market conditions. This can lead to terrible losses for some of these customers and under such peculiar circumstances, a loan rescheduling can be considered as an alternative to repayment which is done by extending the duration of the loan as well as decreasing the size of installment payments.

2.5.3.6 Collection Policy

Organizations tend to adopt various policies that help in ensuring the viability of its credit administration. A debt collection policy happens to be one of the key elements utilized by management to achieve results. This policy is important because not all loan customers demonstrate the same level of commitment as some honour their obligations on time while others do not. Some customers are slow payers while some are non-payers. The goal of such a policy should be aimed towards fast tracking the collectibles from non-committed customers or slow payers whiles reducing losses that may arise from debts that might be going bad (Kariuki, 2010).

2.5.3.7 Credit information

This comprises the utilization of dependable and opportune data which becomes useful in dealing with the credit system. This is important in that it leads to a reduction of losses that may arise as a consequence of disbursing available funds to untrustworthy loan customers Kakuru (2001). Such data ought to incorporate; the clients' years in present business, the time spent at the present area of operation, monetary information, credit assessment with different merchants and credit scoring organizations, and data about the directors of the organization and other related intelligence. Information is so vital in the credit management process as it provides the basis for a sound credit granting process. When information becomes scanty, the probability of loss outcomes becomes increased since, it does not provide the platform to put in place mechanisms that can help forestall any known dangers associated with the credit disbursement and this sets the ground for inheriting huge losses which could have been avoided. The goal of the research work is to help establish the kind of information that is also vitally needed and utilized by financial institutions in the credit management process.

2.5.3.8 Credit analysis

It is important as a major component of credit management to determine the level of eagerness and capacity of clients to meet the credit commitments on a timely basis per the repayment agreement. The financial institution's credit examination ought to guarantee that the advances meet the organization's set credit guidelines McNaughton (1996), and that it ought to take after a general household procedure stream starting with information gathering and moving to activity watching AgDm (2011 overhauls). The credit investigation is a vital viewpoint in outlining a credit arrangement since it eventually climaxes into the seasons which determine the measure of advance to be given to the loan applicant. This means that an effective credit analysis helps to

know which period is appropriate for granting a certain category of loan based on economic factors as well as the capacity of customers premised on credit guidelines that have been outlined by a company in achieving set objectives.

2.5.3.9 Credit limit

This is the highest measure of credit which the firm can advance to clients at a particular point in time. The loan specialist's insight of the business sector and environment in which the client works is extremely crucial. In determining the extent of credit that can be disbursed, attention must be given to what it will take to augment profits in relation to customer's level of trade and furthermore the money related qualities of the client to determine whether he will have the capacity to pay the credit commitment. It is critical to also establish whether the borrower's cash flow forecast can adequately cater for regular repayments with interest. All the more along these lines, as far as possible the limit ought to be adaptable and revisable so frequently to suit the dynamisms and capitalize on the advantages that are available in the business sector of operation to generate optimal returns on the loan given out.

2.5.4 Credit Terms

Credit terms allude to the conditions which guide the firm or the bank organization in offering funds to prospective clients Pandey (2008). They refer to the stipulations under which a monetary organization stipends credit to its clients. In the event that a financial establishment disburses a loan to a client, then the credit terms will indicate the credit period and interest rates. This in this manner will have an impact on the execution of credits since it stipulates the season of advance reimbursements and subsequently establishing a platform where reimbursements can be made auspiciously thereby leading to a diminishing in default rate. Pandey prescribes the accompanying as the credit terms:

2.5.4.1 Credit period

This is the calendar of the interest installment and the last payment of the principal. It is duration between credit augmentation time and the time the client is relied upon to reimburse the loan.

2.5.4.2 Cash discount

This is a percentage decrease on the obligation to be required by the borrower. This serves as a motivating force to actuate the client to reimburse the credit commitment within the time frame of the loan facility. Cash discount as it goes is utilized as an instrument to help expedite installment payments from the clients and this helps the firm to rein in on the level of receivables and their related expenses (Reigner and Hill, 1997). “Once a credit decision has been made, the financial institution has to decide on the credit period, amount and period of the cash discount if any, and the credit instrument to be used” according to Tumuhinbise (1996).

2.6 Measures of Performance

There are certain performance measures that are used to evaluate the performance of financial institutions as a way of determining whether the institution is experiencing more growth through the making of gains or is retrogressing through the generation of losses and these include:

2.6.1 Profitability

Fundamentally, profitability is determined by the weighing of incomes against expenditure. Income is the returns generated from the various operations of the enterprise for instance, the interest revenue generated on advance commitments. Expense are the costs incurred in providing those operations carried out by the firm. Examples of some of the costs include the cost of deferred consumption on the loaned amount otherwise known as the opportunity costs since they

are locked up in the hands of debtors, the costs of recurring expenditure of credit activities, the expenses incurred in collecting non-performing debts and the costs involved in recovering bad loans (Leong, 2009).

Profitability can be defined in terms of accounting or economic profits. Accounting benefits is the surplus income left after derivation of all costs. For a financial organization to run, it must be making gains. Then again, a single non-benefit monetary year may not cause any significant loss to the institution, however when the firm continues posting misfortunes in resulting years, this may jeopardize the suitability of that business (Don, 2009).

Economic profit is computed by subtracting the opportunity cost from the net revenue (Graham, 1996). The opportunity cost includes the funds, the effort and the managerial resources directed towards the control and administration of credit processes AgDm (2011 updates). The essence of economic profits is to provide the business with a prospect in the long-term to superintend its continuous operation of activities. Some of the measures of profitability include return on capital employed (ROCE), Gross margins and net profit margins.

2.6.2 Default rates

Credit default refers to the lack of capacity of a borrower to meet his or her advance commitment at the agreed time as per the loan agreement. As noted by Baku and Smith (1998) the expenses incurred as a result of the failure to meet commitment imposed on the loan customer would be felt by both counterparties. The loan firm ends up acquiring costs produced as a result of non-payment situations, including wiped-off returns on risky assets, opportunity expense of primary, legal charges and related expenses. For the borrower, the choice to default is symmetry between

the relinquishments in lost reputation from default as against the opportunity cost of foregoing investments because of the repayment of the current credit facility. The borrower consequently needs to weigh the alternatives precisely and settle on the right choice that will support the circumstances in which he discovers himself. Defaults therefore ought to be managed in a manner that makes it difficult for such situations to arise through the establishment of prudent credit management processes that seek to safeguard loan assets against inherent default risks.

2.6.3 Interest-Income

It is generally a term used by companies on their income statements for reporting the interest accrued on cash temporarily held in savings accounts, certificates of deposits or other investments. Because the interest wasn't part of the original investment, they record it separately, as interest income. It is also the difference between the revenue that is generated from a bank's assets and the expenses associated with paying out its liabilities. A typical bank's assets are made up of all forms of personal and commercial loans, mortgages and securities. The liabilities are, of course, the customer deposits. The residual revenue that is generated from the spread between interest paid out on deposits and interest earned on assets is the net interest income.

2.6.4 Recovery-Rate

One critical element of a strong risk management system is a bank's ability to evaluate the potential losses on its investments. One factor that determines the extent of losses is the recovery rate on advances and securities that are in default. The recovery rate measures the extent to which the creditor recovers the principal and accumulated interest due on a defaulted obligation. While financial companies, their regulators, and researchers commonly assume that the recovery rate is constant, in practice, actual recovery rates vary significantly. The recovery rates are

inversely related to the default rates and this is due to the fact that both indicators are usually strongly influenced by the economic environment of a country

2.6.5 Relationship between Credit Management Policy and Profitability levels

The forwarding of credit to prospective customers suggests that the funds of a firm are locked up somewhere else whose installment will be some place within a reasonable time frame. Considering the way the future is characterized by an extraordinary level of uncertainty, the accessibility of credit is disproportionately related to profits on the grounds that it is hard to figure out if these obligations would be recuperated from customers, and so most often the organizations utilize the funds for sustainability rather than embarking on risky investments and expansion of scale of operations (Sharpele, 2000).

On the other hand, if the firm all the more so a bank chooses to restrict its credit lines, it causes a decrease on its level of profits (Don, 2009). This is on account of the fact that such monetary organizations generate returns singularly on the premiums that accrue based on the repayment of loans. These reduced gains may likewise be because of different components including lower levels of investments and misapplication of variable inputs (Brigham, 1997). In this manner, it is necessary to have a proficient credit administration strategy that decreases the expenses included in credit arrangements while at the same time expanding the profits from such endeavors.

In order to do achieve that, there has to be a way of determining how credit management and the various processes involved affect the performance in terms of not only profitability but loan portfolio quality, recovery rates and how these have a larger impact on the overall value of the

company in terms of the maximization of shareholders' wealth or value which is the real determinant of the value and performance of a company.

2.7 Credit Management In Ghana

Credit risk is still the biggest origin of risk for most monetary establishments around the globe (Credit Bank Negara Malaysia, 2001). A comprehensive credit administration is hence key to guaranteeing that credit centered operations of financial institutions are directed in a judicious way and the danger of potential insolvency is diminished. The achievement of banks (in the perspective of the analyst) depends on their capacity to deal with their credit lines successfully. Despite the fact that there are no entirely set down credit administrative processes, most monetary establishments follow the accompanying measures keeping in mind the end goal of expanding gains and in addition lessening credit hazards.

2.7.1 Lending

Lending is one of the central mainstays of financial intermediaries and so to that extent a major focal point in the operations of banks. It is however exceedingly unsafe. This is affirmed by McNaughton (1996), who underscored that risk taking is integral to the credit management process and banks are effective when the danger they take are sensibly controlled and within their budgetary limitations and credit skills. McNaughton was likewise of the perspective that to survive the various dangers associated with credit granting and to succeed, firms must reconsider their bureaucratic propensities with the end of goal of being able to satisfy the monetary exigencies identified within the economic system and help bridge these lapses. The bureaucratic inclinations could accordingly bring about loads of dissatisfactions from loan applicants due to

their inability to obtain their credit at the correct time and which may eventually hamper the accomplishment of such undertakings. This is a major setback in a lot of lending institutions in the country as customers have to wait painstakingly in order to get their facilities approved and with timing being a critical factor in loan application, the facility could end up bad since the period of need may have passed already

In the area of credit delivery, Rouse (2002) has declared that a bank lends out funds but does not give it away for free. He continues by stating that, there will dependably be some risk that the client will be not able to reimburse, and it is in evaluating this hazard that the loan specialist needs to show both ability and judgment. Credit delivery is seen as a craftsmanship in light of the fact that it includes creative ability and innovativeness. The credit administrator ought to possess skillful abilities and be able to carry out insightful monetary analysis, possess the mental attitude in deciding the apparent and circuitous expectations of the borrower, the kind of soil and climate as far as loans given to the agricultural sector are concerned and the apparent effect of the execution of credit lines on the firm Ahiabile (2012). A lot of Ghanaian banks are now beginning to embark on intensive training that will strengthen the creative ability and skill of their credit staff in the granting process as a way of ensuring that loan portfolios are greatly improved and strategic credit objectives are realized.

These circumstances make the operation of lending extremely difficult since any considerable critical mishap causes undesirable budgetary misfortunes that can have a debilitating impact on the fortunes of the financial institution. The lending environment in the country is riskier due to the lack of certain critical infrastructure that could enhance the lending process. This therefore makes it imperative in the view of the researcher for the right kind of persons who possess the

requisite skill and aptitude to be put in charge of the lending process especially in financial institutions in Ghana.

2.7.2 Cost Of Borrowing (Interest Rate)

Lending rates are always pegged against the risk of default therefore the higher the probability of default the higher the interest rates that are applied. Businesses which have a higher risk of becoming successful usually get credit facilities at higher rates. A typical example is the agricultural sector which is considered as highly risky due to the variable nature of the country's climatic patterns therefore lending to this sector comes at a higher cost than the commerce or retail industry which is considered as low risk. Lending to the agricultural sector and the commerce industry stood at 30.0 percent and 28.5 per cent respectively as at the end of December 2005 (Bank of Ghana, 2005). These circumstances have the potential to worsen the default risks since businesses tend to borrow at higher cost of capital and these additional cost increase their costs of production which is eventually passed onto the consumer through pricing. This eventually affects the purchase of their products which impacts on their cash flow thereby triggering the possibility of default.

Lending rates are also influenced by the supply of funds on the money market. When Government critically wants funding for infrastructural, they tend to offer higher Treasury bill rates which attract more investments thereby crowding out money supply to the private sector. Since most financial institutions peg their lending rates against government's risk free rates they are forced to offer credit facilities at higher interest rates (Bank of Ghana, 2000). Inflationary pressures have a direct bearing on interest rates as inflation affects the purchasing power of money. This means that the time value of money diminishes over time due to the rate of change

in the prices of goods and services. Banks therefore have to adjust their rates in order to accommodate these changes thereby leading to higher interest rates in a high inflationary environment like Ghana. Within the savings & loans industry, the rates are pegged higher due to the risky nature of the micro, small and medium scale sector.

2.7.3 Assessment Of Borrowers Credit Worthiness

Analyzing the credit worthiness includes the collection, screening and analysing of data on the credit applicant. A critical component of this information flow is the existence of credit rating. Credit rating is not a popular activity in Ghana due to the lack of technological and communication infrastructure as well as the lack of cooperation from firms in providing information that pertains to them as well as their customers. Credit reference bureaus have now began to mushroom up in the country and they having been sanctioned by the central bank are now operating with the financial institutions to facilitate the flow of credit information which becomes critical in determining the credit worthiness of a borrower.

2.7.4 The Industry

The Bank of Ghana promulgated a law, PNDC law 328 known as financial institutions (Non-Banking) law in order to regulate financial institutions whose activities did not fall directly under the operation of commercial banks. The motive was to instill sanity into the financial system as well as institutionalize the traditional/informal savings societies with the aim of achieving growth in the mobilization of deposits to support economic activities as a way of complementing the operations of commercial banks. The savings & loans sector therefore falls under the category of non-bank financial institutions.

Savings and Loans companies utilize microfinance strategies which are exceptionally innovative in reaching relatively poor clients with very small, short-term transactions but which remain both costly and risky GHAMFIN (2003). The lending rates of these institutions are therefore generally higher than the traditional banks. However clients place greater value on ready access to funds than interest charges. The modes of frequent small payments (weekly, fortnightly and monthly) make it easier for clients to meet the loan obligations. A culture of savings develops that provides a useful strategy which forms the basis for evaluation and selection of loan clients. Savings and Loans companies also as a requirement insist that potential clients save with them before applying for loans. This aids in the selection of clients with the discipline and capacity to meet loans repayments and to eliminate those who are unlikely to be able to bear the debt burden GHAMFIN (2003). The companies employ both individual and group lending strategies.

Generally, the credit management practices adopted by the savings and loans companies are also very similar in terms of their application to the commercial banks with the major difference being in the modes of payments where the savings & loans companies offer daily, weekly as well as monthly options compared to the commercial banks where the installment payment is mostly on a monthly basis.

2.8 The Essence of Sound Credit Management

If revenue is the energy that fuels a company, credit management is the engine that keeps it running. The credit management apparatus acts in the capacity as a dominant force that drives income and motivation to all aspects of the organization. As the credit management system metamorphoses into a more potent and effective mechanism, it has a direct impact on the business in terms of profits and productivity Atradius (2013)

According to Paul Brice, partner at KPMG, he stated that, “where you have important trading interconnections, it’s a good practice to regularly monitor financial performance by taking a comprehensive look at a broad range of financials and other information to establish the direction in which the company is moving towards and to identify its financing needs”.

Putting in place sound credit management, for example by scrutinizing both existing and new customers as well as consistent profiling and updating of customer data on an ongoing basis is a sensible strategy in any market, but especially in faltering economic conditions. (Atradius, 2011)

Credit management therefore ensures that the process of credit granting is effectively carried out by ensuring that the disbursed loan goes to the right people who possess the character and capacity to pay and also that optimal benefits are derived from the loaned funds through the regular payment of installments by customers to guarantee a solid revenue generating stream for the financial institution. It also allows for the identification of risks that are inherent within the credit process and to be able to make adequate provision for these risks through sound underwriting principles, effective appraisal systems as well as a solid monitoring system and guaranteeing a stable liability structure predominantly funded with deposits.

2.9 Empirical Review

Nagarajan (2001) in his study of risk management for financial institutions in Mozambique found that risk management is a changing process that could appropriately be advanced during normal times and tested in the event of risk. It requires careful planning and commitment on part of all stakeholders. It is encouraging to note that risks related losses can be minimized through strong management of portfolio and income streams, by establishing robust institutional

infrastructure with proficient human resources and instilling client discipline, through effective coordination of stakeholders.

Achou and Tenguh (2008) additionally directed an examination on the performance of financial institutions and credit risk administration and found that an essential relationship of huge significance existed between financial organizations performance (regarding profitability) and credit risk administration (with regards to credit effectiveness). Better credit risk administration brought about a more upbeat performance in financial institutions. Therefore, it is of fundamental importance that monetary establishments teach the propensity for reasonable credit hazard administration, protecting the resources of the organization and securing the interests of investment holders. This falls in line with one of the goals of the research work which is establish the relationship between credit management practices and institutional performance in credit granting institutions in Ghana with profitability being one of the performance measures to be utilized.

Soke Fun Ho and Yusoff (2009), in their study on credit risk management strategies of selected financial institutions in Malaysia pointed out that “losses incurred by majority of financial institutions and banks emanate from outright delinquency due to the customers’ inability to fulfill obligations relating to lending, trading, settlement and other financial transactions. Credit risk arises from a bank’s transactional activities with individuals, corporate, financial institutions or sovereign entities.” A bad loan portfolio can trigger serious liquidity as well as credit risk.

The proficient administration of credit risk is a fundamental aspect of the entire administration framework of risks which is vital to every bank and in the end the survival of every monetary

establishment. It is subsequently imperative that credit choices are made by solid investigations of hazards involved to avoid the eroding of profits. An effective credit administration is a vital part of a far reaching strategy to an enterprise risk administration framework and basic to the growth of every financial institution in the long-term.

CHAPTER THREE

RESEARCH METHODOLOGY & ORGANIZATIONAL PROFILE OF FASL

3.0 Introduction

To guarantee that the study is appropriately adapted to the targets set, careful consideration has been taken in drawing up the research plan. This section highlights target populace and additionally the tools used to gather data keeping in mind the end goal of obtaining useful data for the investigation. This segment is a general plan or structure arranged to help the researcher in providing answers to the research questions asked. This stage unveils how the research was executed and the approach used in identifying and sourcing information from respondents, and in addition how the research work was finished. It examines the population, sample size, sampling procedure and sources of data. This chapter consequently identifies the procedures and techniques that were used in the collection, processing and analysis of data. Specifically the following subsections are included; research design, population, sampling procedure and size data collection instruments, data collection procedures, data analysis and finally an organization profile of FASL

3.1 Research Design

The study adopted a descriptive survey design. The object of descriptive research is to gain an accurate profile of events, persons or situations. It helps in obtaining information concerning the current status of a situation to describe what exists with respect to variables or conditions in the situation under investigation. This technique was appropriate as it involved a careful and in-depth analysis of the effect of credit management on the performance of financial institutions. What's more, information gathered utilizing the survey method can be utilized to recommend

conceivable purposes behind specific connections in the middle of variables and to deliver models of these connections (Saunders et al, 2012).

A case study method which explores a research topic or phenomenon within its context or within a number of real-life contexts was employed in the research. Yin (2009) highlighted the importance of context, adding that, within a case study, the boundaries between the phenomenon being studied and the context within which it is being studied are not always apparent. This is a potential favorable position of the contextual investigation procedure. The contextual investigation technique will be pertinent in the event that you wish to pick up a rich comprehension of the connection of the research and the procedures being utilized (Eisenhardt and Graebner 2007).

A mixed method involving both qualitative and quantitative designs was used as a means of providing a contextual background to give a better understanding of the research problem. The characteristics that help to define mixed methods research (stage, level of integration, timing and relative status) highlight how quantitative and qualitative methods may be combined in a number of ways to provide you with better opportunities to answer your research question according to Tashakkori and Teddlie (2010).

3.2 Population

The population for the study was made up of all staff of First Allied Savings & Loans Ltd. The study was done on 33 respondents who were staff drawn from the credit department, the finance department, and the risk department.

3.3 Sampling Procedure & Sample Size

Persons were selected into a sample population by judgmental or purposive sampling from the population of employees due to the specific needs of the topic which required people who were directly involved in the credit administration and procedures of the company and who were also available at the time of carrying out the research work

Table 3.1 Sample Population and Size

POPULATION	SIZE
Staff (finance department)	4
Staff (credit department)	25
Staff (risk department)	4
Total	33

3.4 Sources of Data

Data was obtained from primary sources through the use of questionnaires and interview guide. This was to help ascertain views and opinions pertaining to the topic under investigation. Secondary sources of data were gathered from the financial statement of accounts of FASL from 2009 to 2014 in order to carry a trend analysis to help provide a more comprehensive assessment of credit management practices and their impact on performance over a period of time.

3.5 Data Collection

Data was collected using a combination of both quantitative and qualitative methods. Quantitative data was primarily collected from the financial statements of the First Allied Savings & Loans. The questionnaires formed the basis for generating the primary data. Qualitative data was collected using questionnaires and interviews which were done purposively.

Secondary data was collected from annual reports of portfolio size, loan recovery rates, loan performance as well as interest income from 2009 to 2014. Questionnaires were administered to each respondent in the study and they had both open and close ended questions.

The close ended questions were used to collect opinion variables as well as test the rating of various attributes. Opinion variables record how respondents feel about something or what they think or believe is true or false. The open-ended questions provided additional information that may not have been captured in the close-ended questions.

3.5.1 Data Validity and Reliability

Internal validity in connection to data alludes to the capacity of your survey questions to quantify what you plan it to gauge. It alludes to the concern that what the researcher finds with the survey is a fair representation of what is being measured (Saunders et al, 2012). The survey questions were deliberately composed and tried with a couple of individuals from the populace for further upgrades. This was done with a specific end goal to improve the legitimacy and precision of the data that was being gathered for investigation and further analysis as well as ensure validity of data.

Reliability refers to consistency. It measures the level of variance of actual results from expected results from the research tool that has been adopted. The tendency towards consistency found in repeated measurements is referred to as reliability. One method of testing for reliability is the internal consistency method. Internal consistency involves correlating the responses to questions in the questionnaire with each other. (Saunders et al, 2012).

3.6 Data Analysis

The data that was collected through questionnaires were presented in tables for further examination through the use of the Statistical Package for the Social Sciences (SPSS) software package. Descriptive statistics was used to analyze data. Furthermore, descriptions were made based on the results of the tables. Before processing the responses, the completed questionnaires were edited for completeness and consistency. The data was coded to enable the responses to be grouped into various categories for easier analysis. The findings were presented using percentages, graphs and tabulations. Tables and graphs were used to summarize responses for further analysis and facilitate comparison.

3.7 Profile Of First Allied Savings & Loans Limited

3.7.1 History

First Allied was licensed by the Bank of Ghana under PNDC Law 328 (1993) to provide banking services. It started operations on 25th September, 1996 beginning its operations from its office located in Adum, Kumasi where its Head Office is now situated. The strategic objective behind the establishment of the institution was to accept deposits from the public as well as provide credit to business units in need of them through the provision of customized products and services that meet the overarching needs of its target market

3.7.2 About FASL

First Allied is a leading Savings & Loans Company in Ghana, with a mission to provide convenient access to efficient innovative and responsive financial services to the Small and Micro Enterprise Sector on a sustainable basis for the mutual benefit of all stakeholders.

With 19 years of providing excellent banking services, First Allied has been consistent in building a differentiating brand through its superior services and irresistible customer support. As a customer-centered institution, First Allied cherishes the service of providing a broad range of accessible financial solutions to its customers in a timely manner and at optimum convenience.

The institution has earned its current enviable status as a leading Savings and Loans company in Ghana through its relentless pursuit of customer-centered services and the continuous introduction of innovative products which have become lifelines to many SMEs and individuals who hitherto were marginalized by the formal financial system. First Allied has created financial inclusion for these marginalized SMEs through the introduction of the SUSU concept into mainstream banking. This innovation caught the attention of the World Bank which conferred on First Allied the Most Innovative Product Award in 2002.

3.7.3 Products

First Allied Savings & Loans offers the following products:

Allied Supersave Account

The Allied Supersave Account is an exciting savings product which offers client convenience and great opportunity to secure their future. This new product also offers flexibility, great reward, transparency and above all an expectation of good returns on savings.

Current Account

This is specially designed for customers who require unlimited access to their money.

Savings Account

The Savings Account is available to customers who desire to make regular deposits and build on

them to meet their future needs, to do so profitably.

Fixed Deposit

Fixed Deposit is an investment account that is offered for a fixed term or on rollover basis. The very high interest rates associated with this product may be negotiated or fixed at the time of investment.

First Allied also offers carefully designed loan products to meet specific needs of their customers. These include:

Travel Credit

This facility allows customers and non customers alike to buy air-tickets on credit from our selected travel agents. It is granted for short term at a competitive interest rate.

Clearance Loan

This is a short term facility, specially designed to enable importers to clear their goods with ease. The facility is available to both customers and non-customers at a very competitive rate. It can be granted within twenty-four hours.

Commercial Loan

The facility is targeted at individuals and businesses who wish to expand their businesses and may be utilized to meet cash flow needs. It is available to anybody with existing account relationship with First Allied. It offers substantial loan sizes at a very competitive interest rate.

Salary Credit

The facility exists for employees who receive their salaries through First Allied. This facility also enables beneficiaries to access substantial loan amounts with monthly repayments, done through deductions from their salaries. Request from salary earners who are not customers of First Allied may be considered for this facility.

Gospel Loan

Gospel loan is meant to aid churches in their development projects. This facility may be accessed by church for the purpose of building churches, procuring equipment, furnishing, etc.

The facility also carries a very attractive and flexible repayment terms.

Consumer Credit

This is a hire purchase scheme run with selected shops. The facility is available to both customer and non- customers who desire to buy consumer durables from any of these shops.

Beneficiaries of this facility are only required to make minimum deposit, with balance of the cost paid through flexible monthly installment arrangements.

Community Lending

Community lending programme is an outreach programme intended to reach out to prospective customers outside the metropolis.

Equipment Lending

The facility exists to meet medium range equipment needs of joineries, machinist, etc.

Under this scheme customers are encourage to save up to an agreed minimum while FASL finances the cost of the equipment in question. Customers are then given flexible terms of repayment. Under this scheme loans are given out at a very competitive rate.

3.7.4 Management

First Allied Savings & Loans has a management team made up of the Chief Operating Officer (COO) who superintends over all activities of the company as well as exercise oversight responsibility over the various departments of the institution. He is assisted by 9 departmental heads (HODs) who assist him in the day-to-day running of business in the institution. These HODs are assisted by branch managers and sectional heads who exercise oversight responsibility

over the various branches and departments and report to the heads of departments. This is the current management structure that has been adopted by FASL to help expand its presence as well as maintain its competitive advantage within the Savings & Loans industry in order to achieve its strategic objectives. The Credit Management process is coordinated by the Head of Credits who oversees and supervises all the various applications that come from various departments and branches. He does it in conjunction with a credit committee that goes through and vets all credit applications presented for approval. He together with the committee update the credit management policy on a regular basis and reports to management concerning the updated policies and provides a report on portfolio of the institution as submitted by the various branches. This allows for management to be abreast with current happenings and to be able to report to board which has ultimate oversight responsibility over the credit management and risk control policy of the institution.

CHAPTER FOUR

DATA PRESENTATION, ANALYSIS AND DISCUSSION OF FINDINGS

4.0 Introduction

The chapter comprises the presentation and discussion of the findings in view of the research questions raised in the first chapter of this research work. Primary and secondary sources of data were used to collate the findings. The data were analyzed using SPSS and presented using, tables, percentages and graphs that were used to draw relationships as well as make inferences from the variables under investigation

4.1 Access to credit

Without creating the platform necessary for customers to access credits, it will be impossible for management to control and manage credits since nothing will be there to manage. Based on this, the researcher was interested in determining the factors that influenced access to credits and what management was doing to enhance access to credits and broaden the portfolio of the institution. The details of the factors influencing access to credits are presented in the graph below.

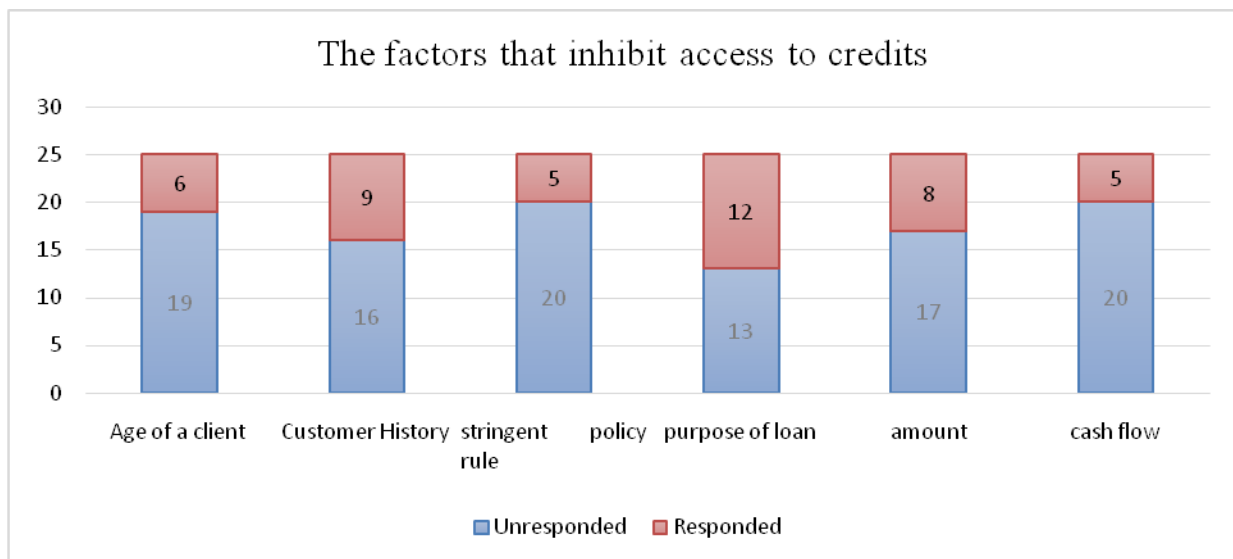


Fig 4.1

From the figure above, the researcher assessed the response on the factors that inhibit access to credit, and the result showed the purpose of a loan was a factor that prevented access to credit as indicated by twelve (12) of the respondents. The purpose of accessing the credits (i.e. according to 48% of respondents) was seen as measure of determining whether the loan should be granted or not since one of the main elements in the credit application process is the purpose of the loan. This implies that, the purpose for which the loan is being accessed should first and foremost be legal. This was in agreement with Poli and Puri (2013) who stated that the purpose of the loan should be documented carefully. They went ahead to state that the bank should ensure that the end-use of the credit should be for the documented purpose only. The study further found that the institution granted loans meant for specific activities such as overdraft, commercial loan, salary loan and asset finance. Limits are set on each of these, making it easier for anyone who falls within such limits to access the loan without difficulties.

Another major factor influencing access to credit was the critical examination of customer's history. Nine (9) of the responses constituting 36 percent (%) of the respondents indicated the customer's history as another major factor. The researcher found that it was the duty of the credit officers to research into the history of customers based on their past credit performance and repayment history. If a customer was found to have demonstrated commitment with the bank by paying his indebtedness on schedule, then the credit officer would assume that all things being equal, the customer could pay the new facility he/she wanted to access based on his previous records. Based on their background, customers with good credits history could easily access credit facilities at even reduced rates from the institution. On the other hand, if a customer was blacklisted because of his past records such as difficulty in repayment, such a customer was either given a reduced amount or denied completely. The study found that credits officers were

able to categorize the customers into those who are credit worthy and those who are not based upon a credit grading system which had been adopted by the institution. Each of these categories was treated on its own merit based on conditionalities that had been set.

Another factor influencing access to credits was the amount to be accessed as indicated by eight of the respondents (32%). It was found that when the amount to be accessed was in line with the purpose and the business activity of the customer, all things being equal, the likelihood of the loan being granted was higher than a customer whose request was not realistic or did not match the purpose for which the loan was being requested. Usually, the amount being granted should match and suffice the purpose of the loan, which will enable the customer utilise the amount to generate enough revenue for the business in question and subsequent repayment of the loan. Insufficient amount means under financing of the business project and the client will run into liquidity problems. When this happens, the debtor will be unable to effectively utilize the facility granted, making it very difficult to repay the loan, hence the risk of default. Other factors such as age of a client, cash flow, and stringent policy rule were also considered as factors that hindered the access to credits.

In addition to the factors that hinder access to funds above, high interest rate, months of being a customer and others were also highlighted by the respondents.

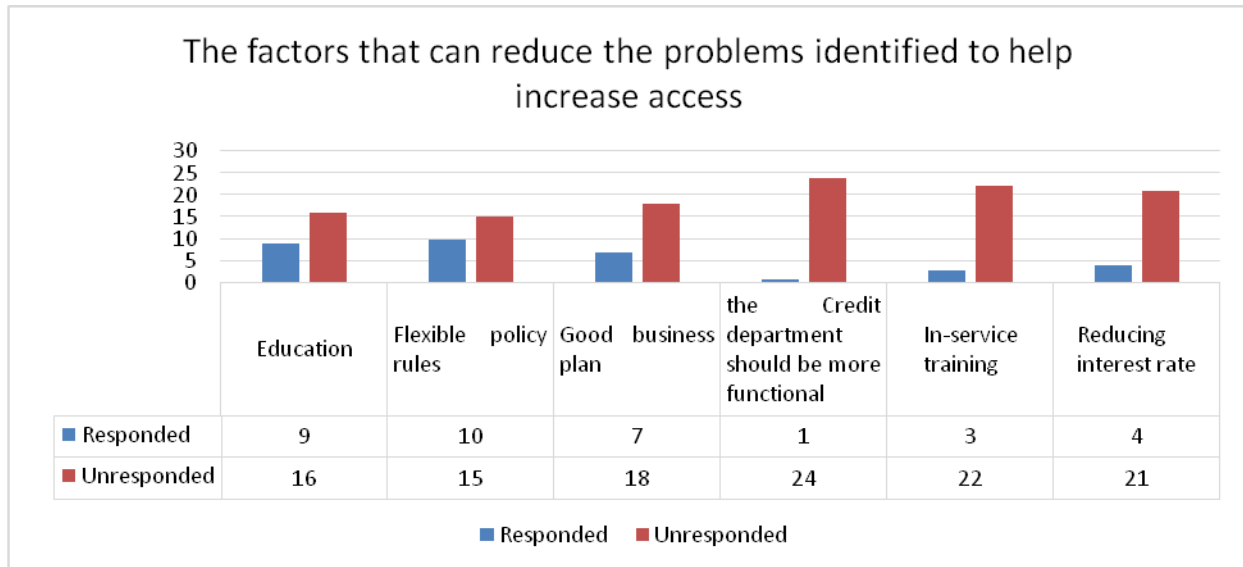


Fig 4.2

The figure above reveals that flexible policy rules followed by education, good business plan and the reduced interest rate can help improve access to credit facilities. Majority of the respondents i.e. ten of the staff respondents (40%) were of the opinion that if some of the requirements of the credit granting process could be made flexible, it would help create more avenues for people to access loans. Stringent policy rules are sometimes established as a way of helping to ensure effective control of the credit management process however, due to changing nature of the environment coupled with intense competition from other players in the industry, it becomes imperative for some of these rules to be relaxed in order to allow more people to access credit facilities. This reinforced Adams' (2002) position that the presence of a strong credit culture allowed a bank to establish the right kind of relationship with its customers which allowed them to determine when to flex standards a little and when to tighten them. Education was also indicated as one of the factors that could help improve access to credit. It was discovered that a lot of clients were not educated well enough on the benefits and requirements of the credit granting process thereby leading to them being misinformed and sometimes scared away from accessing credit facilities. Nine of the respondents (36%) were of the opinion that if clients were

educated well enough on the benefits and the intricacies of lending, it could lead to more clients accessing loans thereby generating more income for the institution. This was a clear vindication of Ahlin and Townsend (2005) who found that the most productive group of customers in terms of education have a better repayment performance. Fewer respondents said considering in-service training and the functionality of the credit department can help reduce the problem.

4.2 Credit control processes

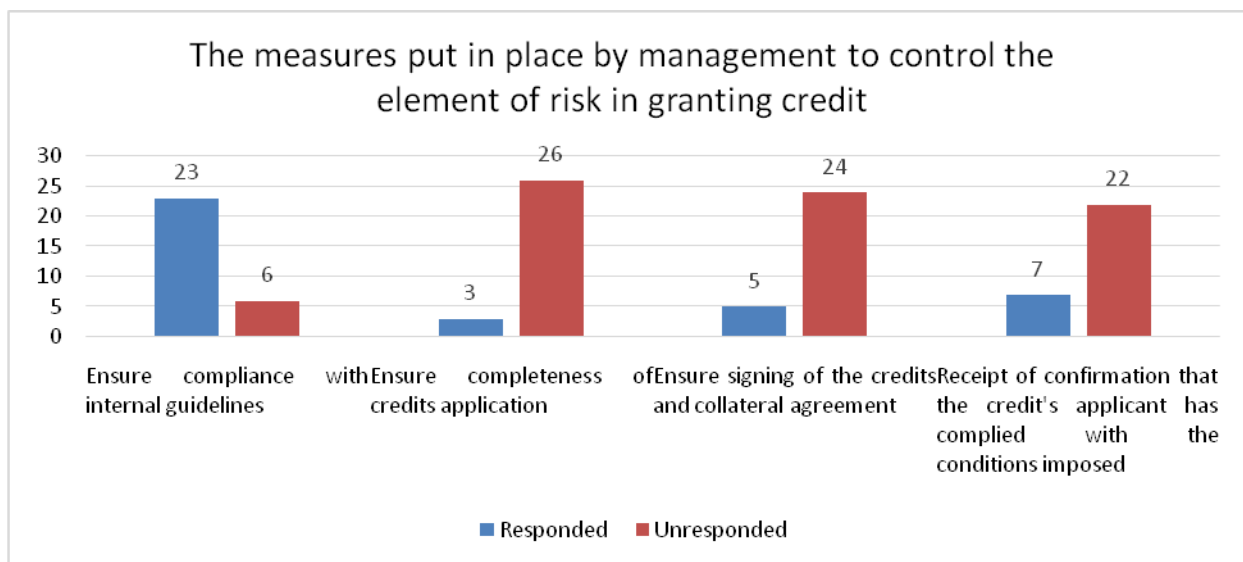


Fig 4.3

In controlling the element of risk in granting credit, most of the respondents agreed that ensuring compliance with internal guidelines can help as depicted in the graph above. Twenty-three respondents (i.e. 92%) indicated that the main credits control process they follow is to ensure that they comply with the guidelines set in granting credits. It was found that the first guideline in granting approval to credits was to ensure that all information is correctly provided on the credit application form. This was confirmed by McNaughton (1996) who stated that the firm's credit analysis should ensure that the loans meet the company's set credit standards, and that it should follow a typical domestic process flow beginning with data collecting and moving to action observing. Once the credit officer is satisfied that there is no error on the form, the next

guideline is to carry out a comprehensive appraisal of the customer to determine the line of customer's business, customer's cash flow as well as estimated net income of business based on transparent and comprehensive presentation of the risks when granting the loan on one hand, and adequate assessments of these risks on the other. Another guideline is to be able to determine and value the type of collateral needs and sources of cash flows.

Another credit control measure that was identified was ensuring that the client has complied with all the conditions set. To do this all the conditions associated with granting of credits should be made known to the customers, so that in the course of his application he/she ensures that all the terms and conditions given him/her are met. When this is done, the main duty of the credit officers is to examine the application form and submit it with recommendations to management for approval. This is also a critical factor as failure to meet any of the conditions could easily lead to a client being turned down even at the last stage which is the signing of the loan agreement. This helped to ensure that loans being disbursed were not diverted for other purposes by clients.

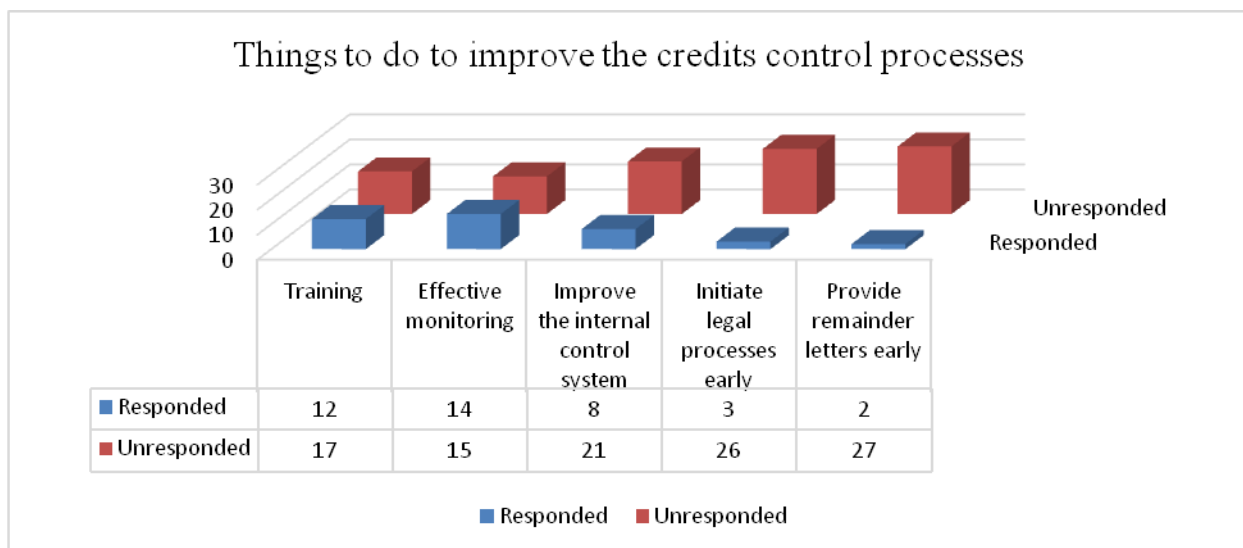


Fig 4.4

From the figure above, effective monitoring was identified as the major factor that could help improve the credits control process. Fourteen respondents constituting about 48% indicated that effective monitoring was one of the things that could be done to improve credit control. This was also found as the first guideline in the credit control process of the institution. According to Hester and Pierce (2002), in creating sound credit standards, it is important to include a proper degree of monitoring and control. The point of monitoring according to them is to identify deterioration as soon as possible and to take constructive remedial action affirming what the respondents said. Effective monitoring helps to ensure that loans disbursed are being carefully tracked to ensure prompt payment of installments (i.e. principal and interest) so as to be able to easily track any case of default or non-performance. This helps guarantee that bad loans are reduced to the barest minimum and that the institution derives maximum benefits from loanable funds. There was an admission that a lack of effective monitoring accounted for the huge debts that were incurred by customers to the institution from responses gathered by the researcher.

Another factor that was highlighted by respondents was training. This was found to be another critical factor as indicated by twelve of the respondents (41%) due to level of risks involved in the credit management process as well as the changing nature of the economic environment making these risks more significant. Training is therefore important to in order to keep them abreast with current issues under credit management and to provide them the leverage to be able easily identify risks as well as be able to measure the probability of default by high risk customers. Improvement in the internal control system was also chosen by eight of the respondents (i.e.29%) as the things to do to improve the credits control processes. In addition, all the respondents agreed that their institution has a definite laid down credit policy.

4.3 Credit management policy and practices

Table 4.1 Responses on Credit management policy and practices

Variable	Frequency	Percent
How often is definite laid down credit policy reviewed		
Quarterly	3	10.3
Semi-Annually	3	10.3
Annually	12	41.4
Others	11	38.0
Who is responsible for the establishing of or created policy in the institution		
The managing director	3	10.3
The chief operating officer	7	24.2
The board	19	65.5
Are you acquainted with the credit policy of the institution		
Very well acquainted	10	34.5
Well acquainted	11	38.0
Acquainted	7	24.1
Not acquainted at all	1	3.4
To what extent does the policy have an impact of the credit granting decisions of FASL		
Impact is very strong	14	48.3

Impact is strong	12	41.4
Impact is moderate	3	10.3
Are you familiar with the credit management processes of FASL		
Very familiar	18	62.1
Moderately familiar	5	17.2
Familiar	6	20.7
If yes which credit period do you consider most appropriate		
Short	13	52.0
Optimum	8	32.0
Long	4	16.0
To what extent does FASL use credit risk control in Credit Management		
Very great extent	3	12.0
Great extent	12	48.0
Moderate extent	7	28.0
Low extent	3	12.0

From the above table, twelve of the respondents (48%) said that the definite laid down credit policies are reviewed every year. The researcher discovered that this was due to the fact that management used the performance of the year together with the strategic objectives of the institution as benchmarks in reviewing the credit policy.

The board and the chief operating officer of the institution are responsible for establishing or creating policies in the institutions as indicated by twenty six (i.e. 89.7%) of the respondents. The researcher found this to be in line with BOG regulations as well as the Basel Committee on Banking Supervision (2000) which posited that The Board of Directors should exercise the oversight responsibility for sanctioning and periodically (at least annually) critically appraise the credit risk strategy and significant credit risk policies and controls of the bank. The board is supposed to exercise an oversight responsibility over all credit management policy and practices and ensure that they are in line with laid down standards. Twenty-one (72.5%) of the respondents indicated that they were well-acquainted while twenty-three (79.3%) respondents indicated their familiarity with the credit management processes of the institutions. This was critical as it was these officers who had an interaction with the customers hence the necessity in being familiar with processes and procedures in credit management.

From the responses above, it is evident that the policies have a strong impact on the credit granting decisions of FASL as indicated by twenty-six staff constituting 89% of respondents. Most of the respondents also were very familiar with the credit management processes of FASL, and they preferred short credit periods to longer ones. Moreover, FASL appeared to use the credit control to a great extent.

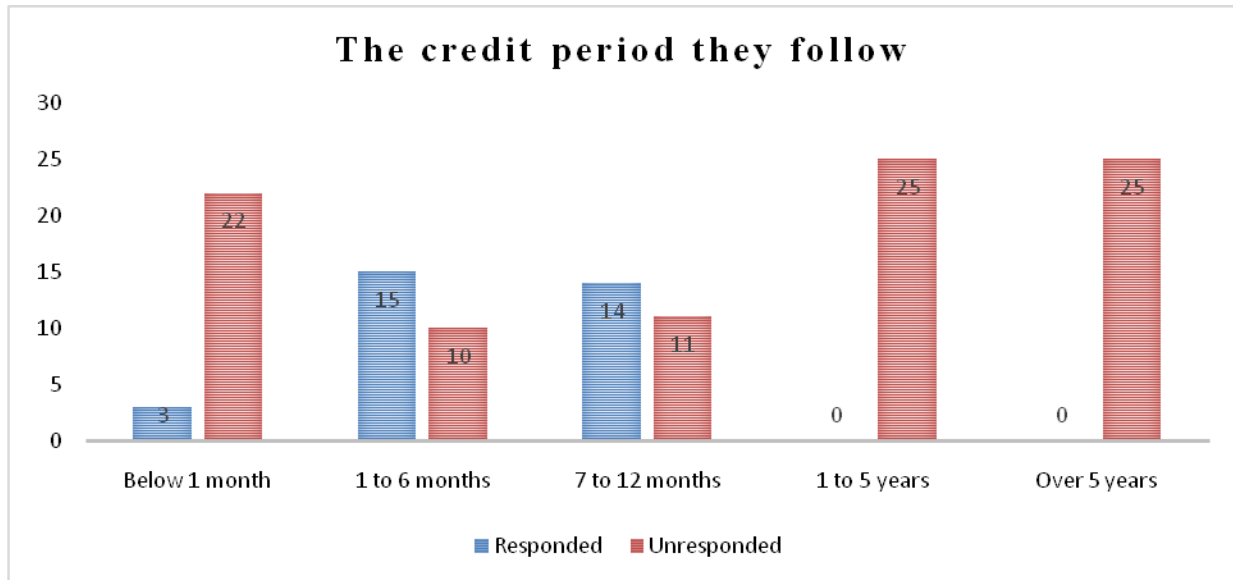


Fig 4.5

Most of the respondents agreed that they follow credit periods such as one to six months and seven to twelve months periods as indicated by fifteen respondents (60%) and fourteen respondents (56%) respectively. These were the major credits periods that were identified from the findings of the research. Credit period refers to the period of time in which the credit is granted according to Ross, Westerfield & Jordan (2008). They posited that the length of the credit period is influenced by collateral value, credit risk, the size of the account and market competition thereby affirming the fact that customers were given varying credit periods as gathered from the staff respondents. This also substantiated Van Horne's view (2007) that one of the noteworthy strategies to ensure an effective collection of advances includes the setting up of the right credit period. He continued by stating that in this manner, the bank should give sufficient time to permit loyal customers the chance of deriving the full advantages of the credit. Such period should however not be too long to put the bank in a distraught position. All respondents said they had loyal customers.

Table 4.2 Responses on Credit Granting Period

Variable	Frequency	Percent
Do you have a standard credit period for all customers		
Yes	6	24.0
No	19	76.0
Do you offer cash discounts to customers who pay in the time period		
Yes	19	76.0
No	6	24.0
Do you consider the time an applicant has been dealing with you before granting credit		
Yes	19	76.0
No	6	24.0
Is the credit period by the applicants of major consideration in the granting credit		
Yes	18	72.0
No	7	28.0

The results from the table above show that standard credit period are not set for all customers as indicated by nineteen (i.e.76%) of respondents and this is due to the different categories of customers they have. Customers with good repayment history are given longer periods as well as

cash discounts on early repayment as indicated by nineteen (76%) of the respondents confirming what was stated by Reigner and Hill (1997) that cash discount acts as a tool to accelerate credit collections from the customers and this helps the firm reduce on the level of receivables and their associated costs. This serves as a way of rewarding loyal and committed customers which also allows them to access bigger loan amounts. The length of time and history of customers play a strong role in granting them credit as indicated by nineteen respondents (76%) and eighteen respondents (72%) respectively. This was a clear vindication of Kakuru's (2001) position that credit information is critical in the sense that it helps minimize losses resulting from investing in unreliable credit clients and that such information included customer's years in present business, financial data coupled with loan repayment history as well as credit rating.

4.3.1 Client Appraisal

Table 4.3 The agreement on the statements relating to client appraisal in FASL

Variable	Frequency	Percent
Client appraisal is a viable strategy for credit management		
Strongly Agree	15	60.0
Agree	10	40.0
The institution has competent personnel for carrying out client appraisal		
Strongly Agree	12	48.0
Agree	12	48.0
Neutral	1	4.0
Client appraisal considers the character of the		

customers seeking credit facilities		
Strongly Agree	11	44.0
Agree	10	40.0
Neutral	4	16.0
Aspects of collateral are considered while appraising clients	6	24.0
Strongly Agree	16	64.0
Agree	3	12.0
Neutral		
Failure to assess customers capacity to repay results in loan defaults	17	68.0
Strongly Agree	8	32.0
Agree		

All the respondents agreed that client appraisal was a viable strategy for credit management as well as having competent personnel for performing client appraisal. The appraisal process was identified as a critical component of the credit management process as it allowed credit officers the chance to diligently and painstakingly assess customers as well as identify any credit risk that might be present. A good appraisal was seen as important in reducing the probability of default by prospective customers. This was found to be in line with the guidelines for commercial banks (2009) which stated that banks should as a matter of need operate within a sturdy and well accentuated criteria for new loan portfolios as well as the broadening of existing credit lines through the assessment of risk profile of customers which forms the basis for an effective client appraisal. Twenty-one of the respondents (84%) also agreed on the character of the customers

seeking credit facilities as also key in granting credit though they admitted that it was difficult to completely determine the character of customers. This reconciled with the views of Poli and Puri (2013) who opined that the capacity of a customer to pay back a loan facility depends on future income streams and the disposition to repay has to be based on the pre-existent commitment that has been undoubtedly demonstrated by the borrower. However, a very good credit appraisal and assessment helped in discovering certain characteristics of their customers which aided them in the credit granting decision process. Aspects of collateral were also considered in appraising clients as indicated by twenty-two (88%) of the respondents. In granting credit, the value of the collateral needed to be sufficient to cover the loan amount requested for. The nature of the collateral was also considered as very important in granting credit as some collateral were considered to be more marketable and therefore easier to sell off than others. This in the view of the researcher was found to be in line with one of the guidelines for commercial banks (2009) which is the perfection and enforceability of collateral assignments. This is very important especially in cases where loan facilities granted begin to deteriorate into delinquency. The perfection of collateral allows such debts to be recovered in an easier fashion. Van Horne (2007) also reemphasized it by stating that the collateral should be safe, easily marketed and that its value should be able to cover up the debt when sold in case the borrower defaults on repayment. Moreover, assessment of clients seeking credit facilities are carried out to prevent loan defaults as indicated by all the respondents. The capacity of the customers was determined through the assessment of the customer's cash flow, line of business as well as the credit turnover of the customer's account operation. These were the main credit management procedures that were followed in assessing the capacity of a customer in accessing a loan facility.

4.3.2 Credit Risk Control

Table 4.4 The agreement on the statements relating to credit risk control in FASL

Variable	Frequency	Percent
Imposing loan size limits is a viable strategy in credit management		
Strongly Agree	8	27.6
Agree	13	44.8
Neutral	5	17.2
Disagree	2	6.9
Strongly Disagree	1	3.4
Flexible repayment periods improve loan repayment		
Strongly Agree	17	58.6
Agree	12	41.4
Penalty of late payment enhances customers' commitment to loan repayment		
Strongly Agree	6	20.7
Agree	13	44.8
Neutral	6	20.7
Disagree	4	13.8
The use of customer credit application forms improves monitoring and credit management		
Strongly Agree	14	48.3
Agree	11	37.9

Neutral	1	3.4
Disagree	3	10.3
Credit committees involvement in making decisions regarding loans are essential in reducing default risk		
Strongly Agree	15	51.7
Agree	11	37.9
Neutral	3	10.3
Interest rate charged affect loan performance in FASL		
Strongly Agree	8	27.6
Agree	7	24.1
Neutral	7	24.1
Disagree	6	20.7
Strongly Disagree	1	3.4

On credit risk control, imposition of loan size limits was found to be a viable strategy in credit management as indicated by twenty-one respondents (72.4%). This affirmed Barusa's (2011) view that in setting up the credit limit, considerations must be taken to maximize the returns in terms of the sales and also the financial strengths of the customer to ascertain whether he will be able to pay the credit obligation. He went ahead to further state that, the credit limit should be flexible and revisable so often to suit the dynamisms and take advantage of the opportunities in the market.

This allowed credit officers to easily determine the loan amounts different categories of customers qualified for and also aided them in grading customers and graduating those who had

shown greater commitment in terms of the repayment of their facilities. Flexible repayment period was also found to be another factor that aided in loan repayment as indicated by all respondents. This was due to the different economic cycles of customers and so having flexible repayment terms allowed them the opportunity to structure the timing of their cash flows to their repayment. Penalty for late payment which carried a charge of 2% p.a. was identified as helping to improve loan repayment by customers as indicated by nineteen of the respondents (65.5%). This helped act as a check against default since customers were informed of the risk of incurring a higher cost for their loan if they risked defaulting on their commitment. Twenty-five respondents (86.2%) admitted that the use of credit application form was also effective as a credit risk control measure as it allowed them the ability to effectively appraise customers and do a proper customer profiling. Credit committee's involvement in credit granting decisions was also found to be helpful in managing credit risk as indicated by twenty-six (89.6%) of the respondents. As part of the credit control policy of the institution it was discovered that loan amounts up to GH¢10,000 could be authorized by branch managers however beyond such amounts, they were forwarded to the head office for authorization by the credit committee who reviewed the loan files as a way of double checking and ensuring the authenticity of information provided. This therefore helped to a large extent in reducing default risks. Credit risk control measures in FASL such as use of customer credit application forms, Credit committee's involvement in making decisions regarding loans and interest rate charges affect monitoring and credit management thereby reducing default risk leading to improvement in loan performance in FASL.

Table 4.5 Rating of Firm's Policy & Practices in Credit Mgt

Variable	Frequency	Percent
In your opinion how do you rate the firm's credit management policy and practices		
Very effective	17	58.6
Effective	10	34.5
Ineffective	1	3.4
How do you see the institution's credit policy and procedure in terms of its application		
Rigid	4	13.8
Flexible	24	82.8
Average	1	3.4
How do you rate the credit analysis and procedure followed by the bank in extending credit		
Excellent	6	20.7
Very Good	18	62.1
Good	5	17.2

Majority of the respondents (58.6%) i.e. seventeen respondents rated the firm's credit management policy and practices as very effective followed by ten respondents (34.5%) who considered it as effective. The credit management practices of the FASL were seen as generally effective and yielded very good results when applied assiduously by credit staff. In terms of its application twenty-four of the respondents (82.8%) considered it as flexible and accommodating. Most of the respondents indicated the credit practices of the institution as generally flexible in

terms of its approach and application to clients. This was due to the cash discounts that customers received as well as the raising of the credit amount at which collateral was required. This therefore allowed more customers who did not have a solid security the opportunity to access loans validating the view held by Adams (2002) that if the bank genuinely understand its customers and has the right sort of relationship with them, it can choose when to bend standards a little and when to adhere to them, if possible, in the context of a strong customer relationship. Six (20.7%) and eighteen respondents (62.1%) ranked the credit analysis and procedure laid down by the institution as excellent and very good respectively. Most of the respondents were of the opinion that the credit management procedures that were laid down were very effective once they were adhered to and helped reduce the element of risk in the credit granting process. This was found to be a validation of Ahiabile's (2012) position that credit management generally prescribed the guidelines to be followed and their religious adherence was seen as very crucial for good the effective implementation of sound credit management practices. Once the laid down mechanisms were properly implemented, the institution was found to benefit substantially from it through the generation of greater interest incomes and charges. This therefore meant that effective supervision was very important in ensuring that policies and procedures put in place are dutifully carried out by credit officers as gathered by the researcher from the respondents. A lack of supervision according to the respondents resulted in a breakdown of communication as well as procedures and protocols leading to the higher loan delinquencies and non-performing loan portfolios.

4.3.3 Credit collection strategies

The credit collection strategies that management adopt in retrieving credit

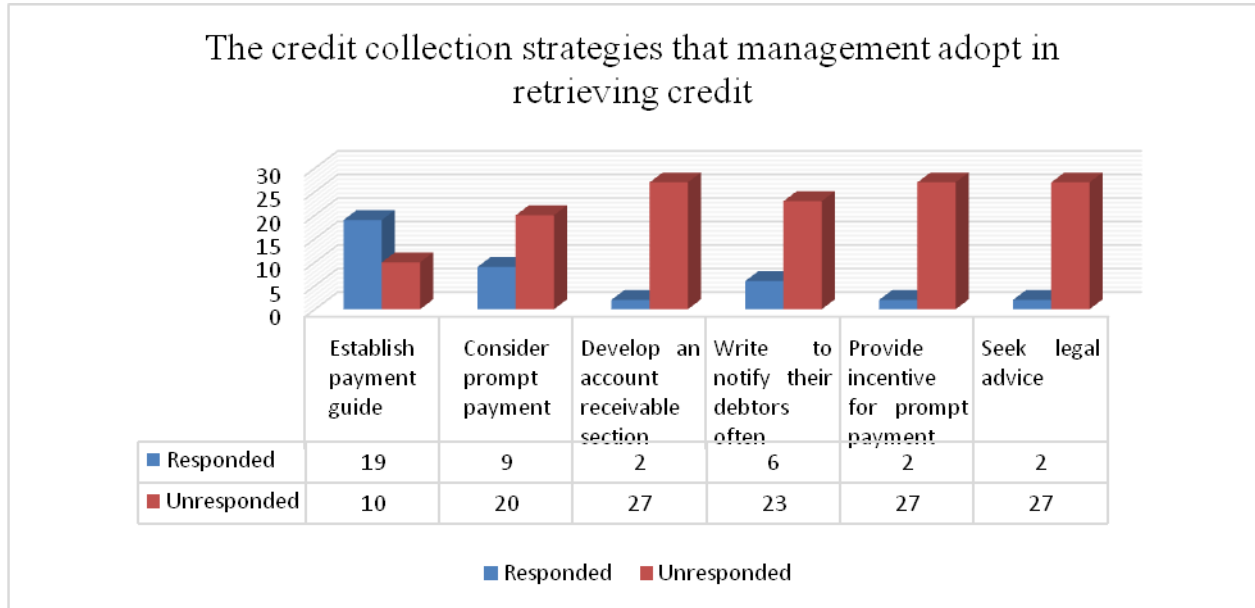


Fig 4.6

From the figure above, establishing a payment guide was the major credit collection strategy identified as indicated by nineteen of the respondents (65%). The establishment of the payment guidelines would give a clear indication as to when and how loans would be paid. To be able to establish effective policy guidelines, there is the need to create a tracking system that would alert debt collectors of all overdue payments; so that immediate action could be taken to collect all outstanding debts. It is also important to follow strict protocols for missed payment. This is possible if the tracking system is put in place. Considering prompt payment and writing to notify the debtors often were also regarded as the main strategies that the management had adopted in recovering credit as indicated by nine (31%) and six respondents (20%) respectively.

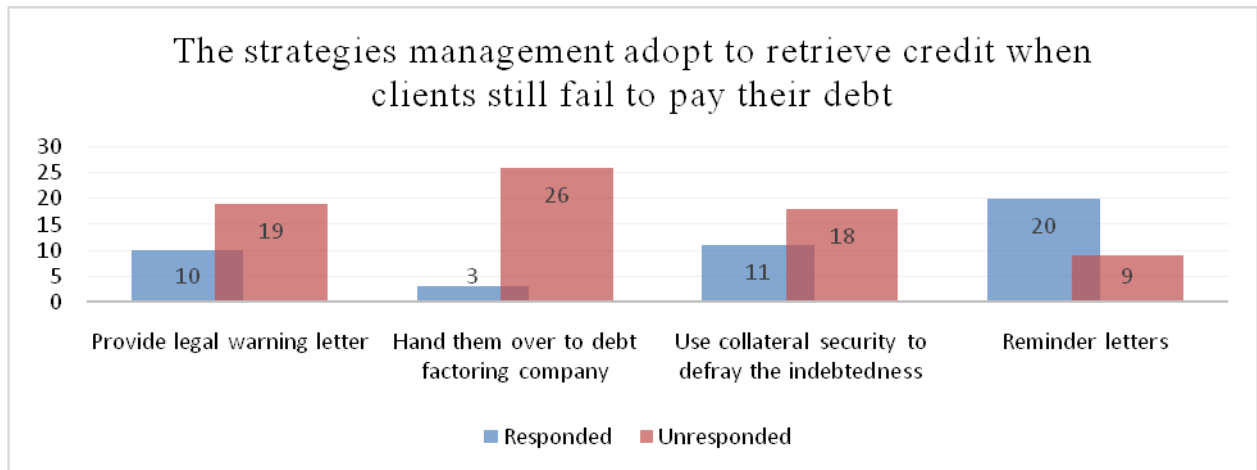


Fig 4.7

In situations where the clients still fail to pay their debt, twenty respondents (68%) considered sending reminder letters as the major action taken to help retrieve non performing loans. Clients whose facilities were going bad were usually written to as a way of reminding them. This affirmed the view posited by Franklin (2010) that credit collection efforts including the usage of reminders should be adopted as part of credit procedures. Eleven respondents (37%) identified the usage of collateral to defray indebtedness as another major strategy. This validated the opinion of Kakuru (2001) that collateral is obtained by a lender as a claim on the borrower and on the asset that is secured, and provides a recourse that is available to a bank should the terms of the loan be breached by the borrower. This position was also reinforced by Van Horne (2007) who opined that the collateral should be safe, easily marketed and that its value should be able to cover up the debt when sold in case the borrower defaults in payment.

The staff respondents however conceded that this was usually a last resort if other strategies such as issuing of legal warning letters and reminder letters had failed to yield the desired results.

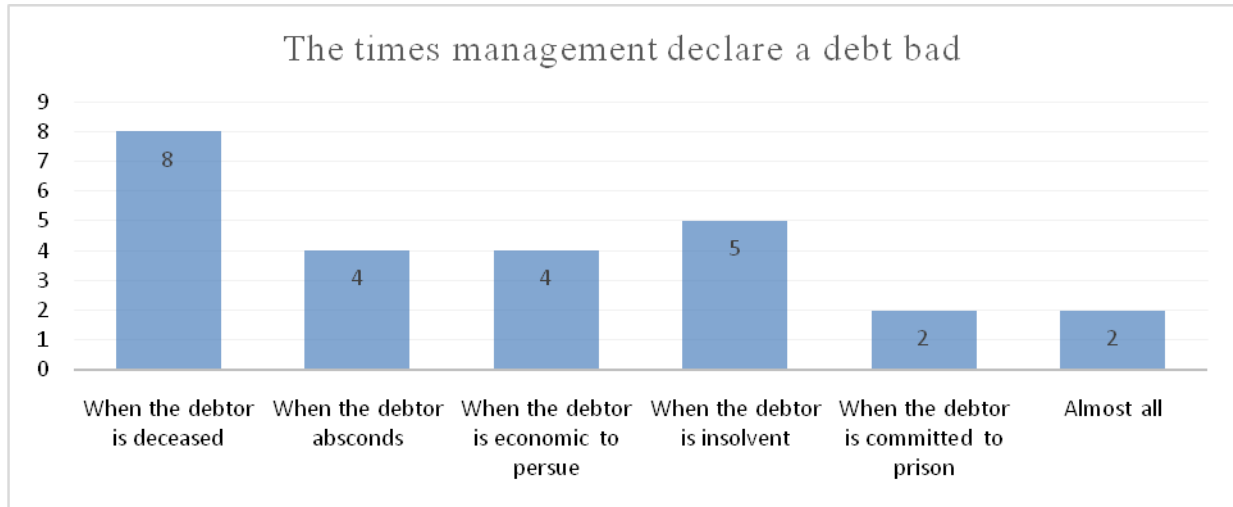


Fig 4.8

Out of the total number of respondents, eight (32%) agreed that the time management declared a debt bad was when the debtor is deceased, followed by when the debtor is insolvent as indicated by five respondents (20%). Majority of the respondents admitted that once a debtor is deceased or insolvent, it became extremely difficult for debts to be reclaimed. This was found by the researcher to be in line with the policy of other financial institutions from the respondents. Four out of the respondents (16%) indicated that debts are declared bad when the debtor absconds as well as when the debtor is difficult economically to pursue. This validated the position of Van Horne (2007) who stated that the level of expenditure that can be permitted in the recovering of debts should be considered as part of the strategy in retrieving loans giving out to customers. He furthermore stated that inferentially, the bank should not give out credit where the cost to be spent on retrieving the obligation will probably surpass the obligation itself.

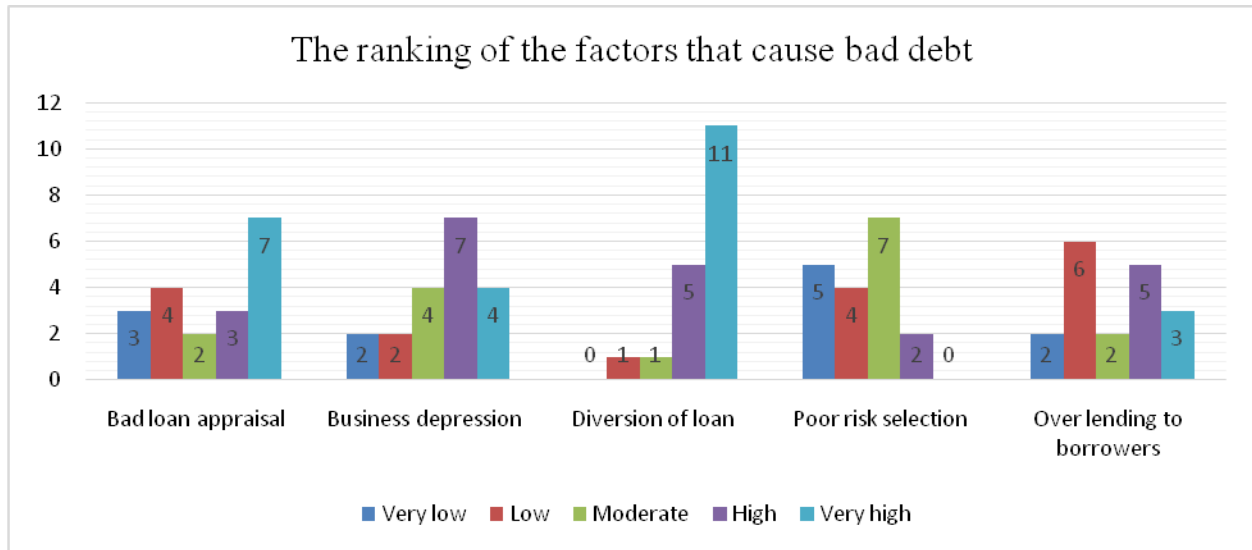


Fig 4.9

Considering the factors that cause bad debt, diversion of loan was ranked the highest (eleven of the respondents representing 44%) followed by bad loan appraisal which was identified by seven staff respondents (28%). Loan diversion was identified as the major factor that causes bad debts since quite a number of customers upon securing the facility utilized it for a purpose different from what was indicated earlier in the credit application form. When this happens, the loans most often ended up going bad due to the unfamiliar nature of those businesses which the customers have diverted the funds to. Bad loan appraisal was also identified by seven respondents (28%) as another major factor as it resulted in the inability to identify any inherent risk that might be present. Other factors such as business depression and over lending were ranked high for contributing to bad debt.

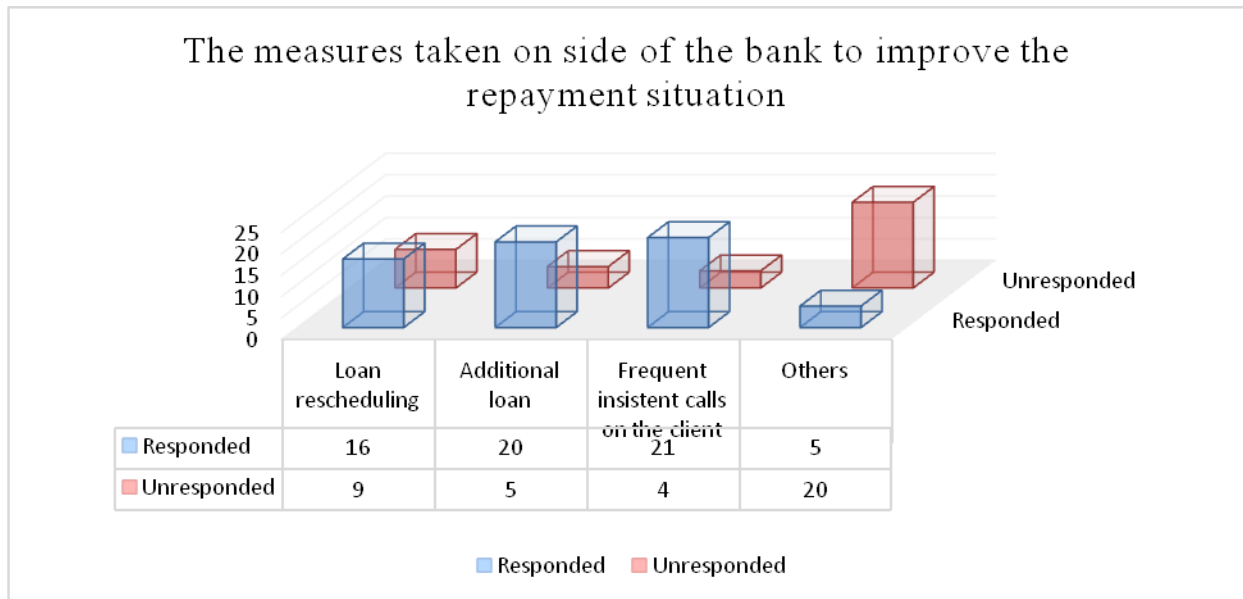


Fig 4.10

Frequent insistent calls on the client, additional loan and loan rescheduling were the measures taken by the bank to improve the credit repayment. Constant reminder of defaulting clients was seen as a measure that helped to a large extent in improving repayment as customers saw it as a bother thereby pushing them to settle their indebtedness as indicated by twenty-one respondents (84%). Another measure that was identified by the researcher was loan rescheduling which helped in allowing customers the chance of repayment due to more flexible terms that were offered to them as indicated by sixteen respondents (64%). This was seen as a risk control measure in allowing customers to avoid the possibility of default on loan facilities granted. These measures are said to have improved the repayment situation as 92% of the respondents agreed.

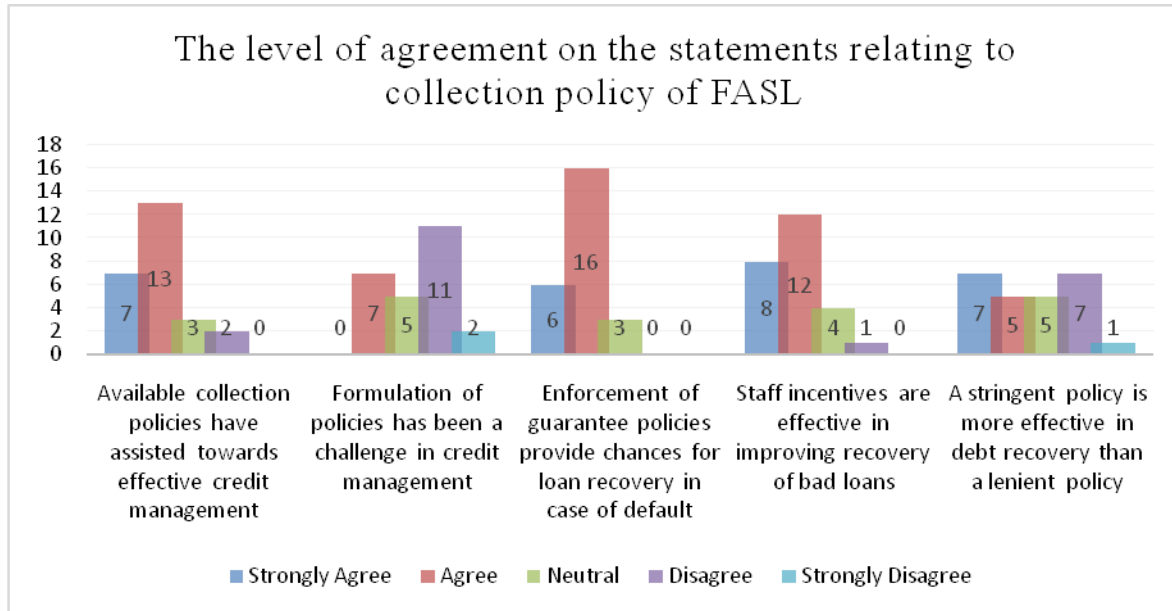


Fig 4.11

From the graph above, twenty respondents i.e. 80% agreed that available collection policies had assisted towards effective credit management of the firm. This was found to be in agreement with Nishimura et al, (2001) who stated that debt collection is an endless challenge that must be tackled with care. Twenty-two respondents (88%) also indicated that enforcement of guarantee policies as part of the collection policy also helped to reduce the incidence of bad debts as it allowed the institution to at least recoup loan amounts that had become delinquent. Staff incentives were also seen as effective in improving recovery of bad loans and it was discovered that management had introduced a commission of 15% on any bad loan that could be reclaimed by a staff. This was seen as a big motivation in allowing staff to go after bad loans. This was found to be in consonance with the general perception that motivation of employees enhances credit management performance in terms of retrieving bad debts. Most of the respondents (eighteen representing 72%) however disagreed that formulation of policies had been a challenge in credit management. Most of them actually admitted that credit management practices were

being updated on a routine basis and were communicated promptly to credit officers as a way of keeping up with the credit management standards of the institution as well as that of the central bank and improving the quality of loan portfolios.

4.4 Impact on Performance

Table 4.6 Impact on performance

Variable	Frequency	Percent
To what extent has the credit management processes had on the quality of loan portfolio of the institution		
Very strong	13	39.4
Strong	16	48.5
Moderate	3	9.1
Small	1	3.0
How far reaching has been the effect of credit management policy on the loan recovery rates		
Very strong	3	9.1
Strong	22	66.7
Moderate	7	21.2
Small	1	3.0
What has been the effect of credit management practices on interest income over the years		
Very strong	11	33.3
Strong	16	48.5
Moderate	5	15.2

Small	1	3.0
What has been the effect of credit management policies and practices on the profitability of the institution		
Very strong	10	30.3
Strong	19	57.6
Moderate	1	3.0
Small	3	9.1
To what extent has the credit management practices in FASL affected loan default rates		
Very strong	4	12.1
Strong	13	39.4
Moderate	7	21.2
Small	7	21.2
Not at all	2	6.1

Credit management processes according to the respondents had a strong effect on the quality of loan portfolio of the institution as indicated by twenty-nine people i.e. 87% of the respondents. Once the right credit management processes were followed, bad debts were reduced substantially as well as non-performing loans which helped improve loan portfolio. The effect of credit management policy on the loan recovery rates was also considered to be strong according to twenty-five (75%) of respondents. The researcher gathered from the respondents that once a

solid credit policy was being implemented, it helped to strongly improve loan recovery rates thereby leading to higher revenues for the institution.

The effects of credit management practices on interest income over the years as well as the effect of credit management policies and practices on the profitability of the institution was ranked as high as indicated by twenty-seven (81%) and twenty-nine respondents (87%) respectively. This clearly epitomizes the view of Achou and Tenguh (2008) who conducted an investigation on bank performance and credit risk management and discovered that an important relationship of huge significance existed between financial institutions performance (in terms of profitability) and credit risk management (in terms of loan performance). Better credit risk management resulted in a more improved performance. The effect of credit management practices in FASL on loan default rates were all considered to be high by the respondents.

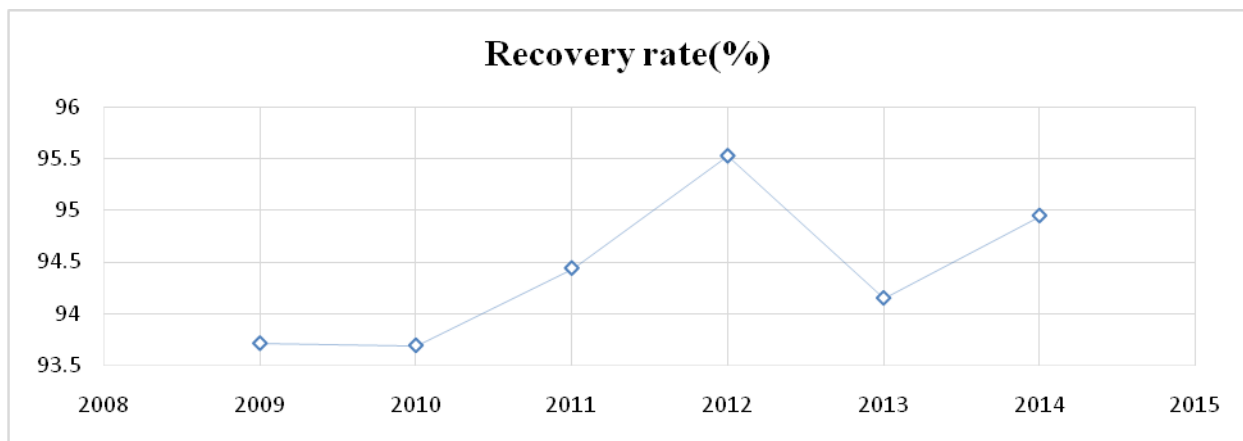


Fig 4.12

One factor that determines the extent of losses is the recovery rate on advances and securities that are in default. The recovery rate measures the extent to which the creditor recovers the principal and accumulated interest due on a defaulted obligation. The recovery rate from 2009 to 2012 witnessed an increasing trend even though the rate was almost the same for 2009 and 2010.

The year 2012 recorded the highest recovery rate of 95.5% followed by a sharp reduction in 2013. It then improved considerably in 2014. 75% of the respondents indicated that credit management processes had an impact on recovery rates. The high recovery rate in 2012 was due to the strong implementation of credit policies by officers however when these practices were relaxed, the institution witnessed a huge decline in recovery rates before seeing a gradual increase in 2014 due to the strict compliance that was initiated by the Head of Credits together with the credit committee.

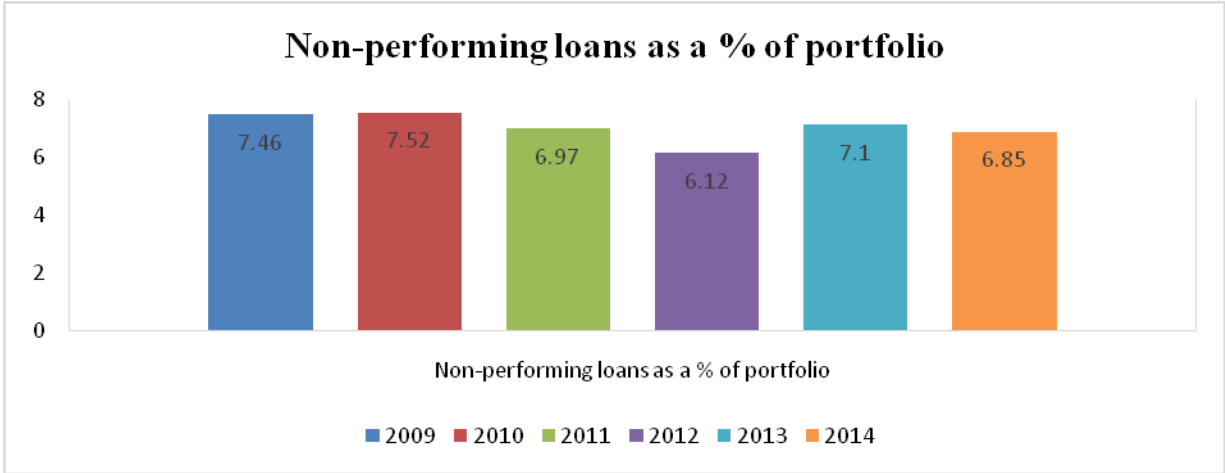


Fig 4.13

A non-performing loan is a loan granted by a bank or financial institution on which interest and principal repayments are not paid timely. Non-performing loans are a measure of the quality of the total loan portfolio of a financial institution. From the figure above, 2010 followed by 2009 reported the highest non-performing loans. Non-performing loans for 2012 was the least and from that point, there was an increase in 2013 and a little decrease in 2014. The year 2012 had the best performance in terms of non-performing loans due to the marked improvement in the recovery rates that year as seen in the earlier figure. This was indeed a confirmation that the two variables are inversely correlated; once the right credit management practices are being implemented, the institution records higher recovery rates and once they increase, non-

performing loans are largely reduced. There was a sharp rise in the year 2013 followed by a slight dip in the following year due to harsh macro economic factors that affected the capacity of businesses to meet loan repayments on time as cash flows were not forthcoming. This had a huge impact on the loan portfolio of the institution which therefore necessitates the adoption of well-diversified and more strategic credit management processes that are able to accommodate such conditions and be able deliver the right results.

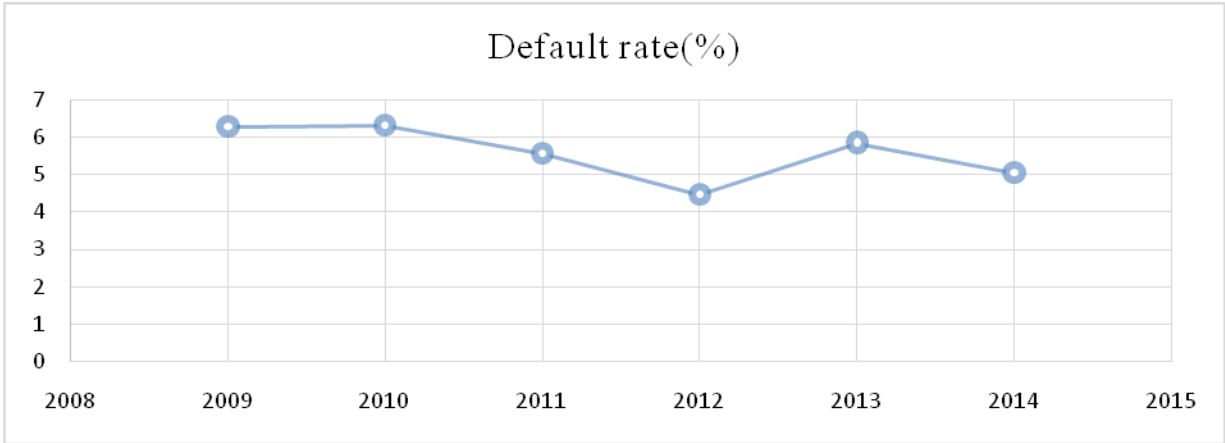


Fig 4.14

The default rate was decreasing from 2009 to 2012 and then increased in 2013 and then a decrease in 2014. Looking at the non-performing loans above and the default rate, we can see a relationship between the two. The year 2012 which had the lowest non-performing loans also reported a better default rate as against the other years. The recovery rates and default rates were also identified as having an inverse correlation; once recovery rates were high, default rates were as witnessed in the year 2012. This means that with a reduced default rate, more loans are performing well and so the institution stands to benefit immensely from such improved performance as long as the credit management systems are strictly monitored and enforced.

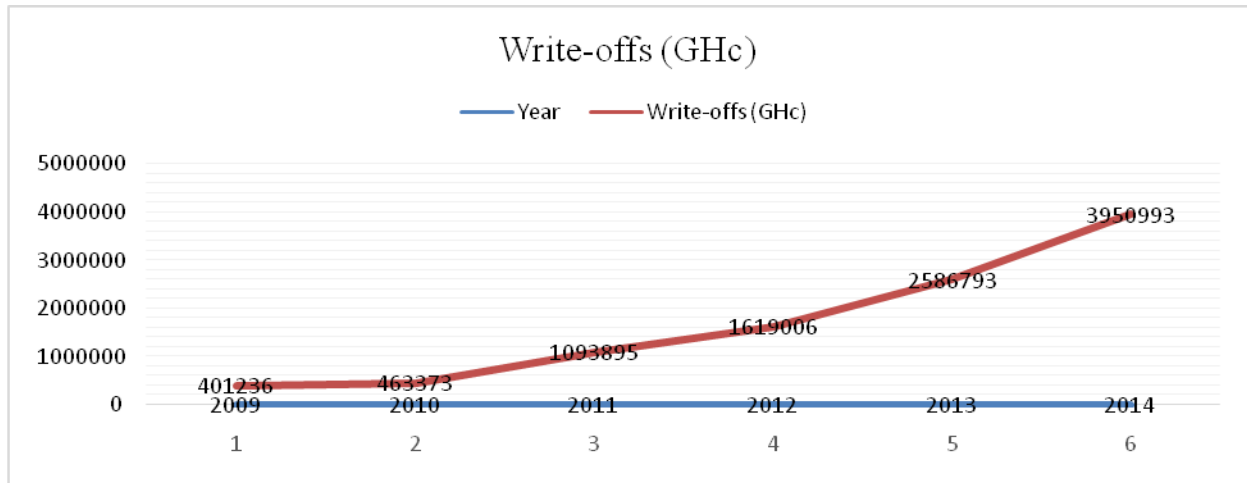


Fig 4.15

Write-offs generally deal with debts that are declared as uncollectible and hence expunged from the balance books to give a true and fairer picture of the financial position of an organization. The write-offs of FASL have been increasing from 2009 to 2014, and this might be because of the inability to recover the bad debts. The trend has been increasing at a faster rate which is not good for the institution since write-offs are an expense to the institution. This means a percentage of the profits are used in writing off loans and with the increasing trend, the institution is losing more in terms of profits. Write-offs generally arise as a result of non-performing loans which deteriorate into bad debts. Non-performing loans arise when credit management protocols that govern the credit granting process are not followed prudently. These eventually lead to poor profiling of prospective loan customers as well as insufficient assessment of inherent risks which ultimately affects the quality of loan portfolios. Critical measures therefore have to be put in place to ensure the enforceability of laid credit procedures as they have a big impact on the institution in terms of profitability.

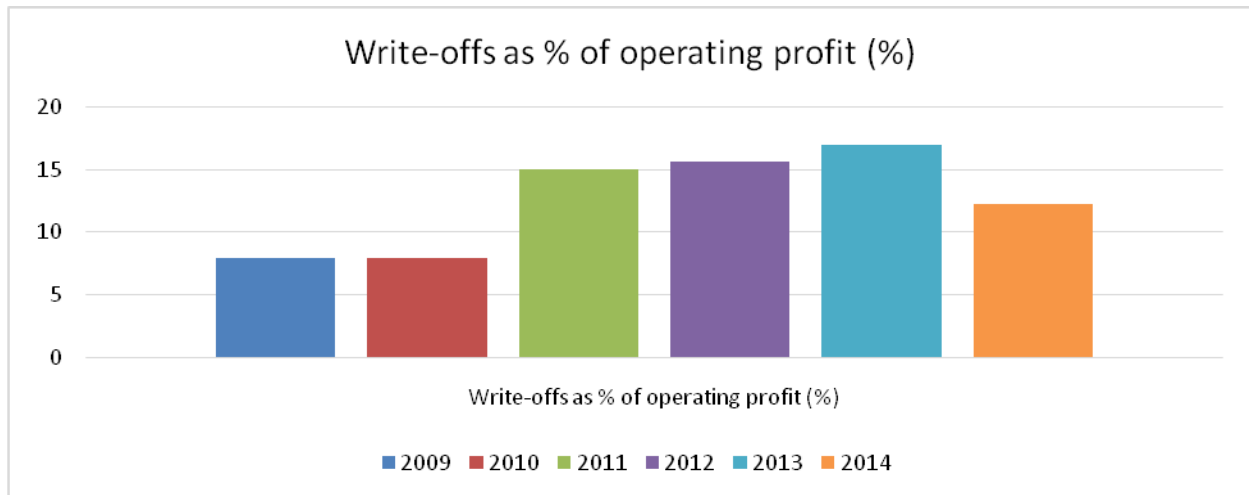


Fig 4.16

From the figure above, it is evident that the write-offs as a percentage of operating profit has witnessed an increasing trend from 2009 to 2013. This goes a long way to affect the profit of the institution as a sizeable portion is expended in writing off bad loans. The trend has not been impressive with a generally increasing trend from 2009 to 2013 followed by a slight decrease in 2014. This means that more measures such as robust underwriting, extensive financial analysis and adequate appraisal techniques ought to be put in place to check the increasing rate of write-offs by ensuring that non-performing loans are reduced to the minimum validating the point spelt out by OCC (2011). If not checked, it could have debilitating consequences on the institution in terms of profits as well as leading to serious liquidity issues since a lot of debts would have become irrecoverable. This will eventually affect the capital structure of the institution in the long-term leading to serious under-capitalization and the ability of the institution to meet its capital adequacy ratios as required by the central bank.

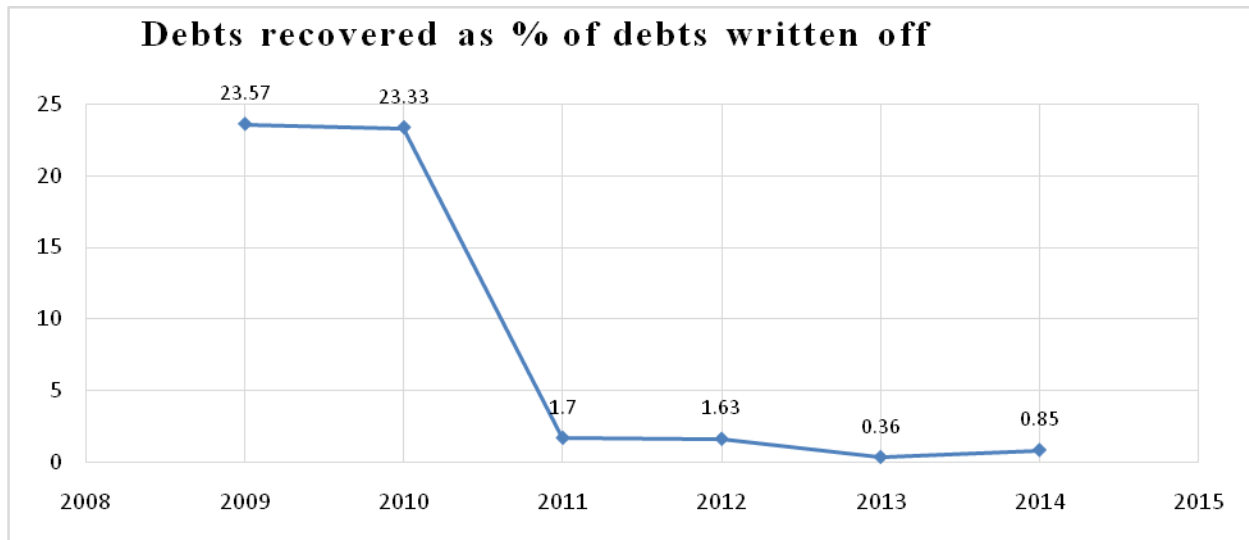


Fig 4.17

From the figure above, we realize that debt recovered by the firm as a percentage of debt written off shows a decreasing trend, and between 2010 and 2011 we witness the sharpest decrease from 23.33% to 1.7%. This implies that less and less of the debts are being recovered as against more and more of the debts being written off. From the data gathered, it was identified that performance in terms of recovery of bad debts had decreased sharply from 2009-2014 which did not augur well for the institution. This might have been due to a lack of coordinated approach that involved all the various departments in recovering such debts as gathered by the researcher from respondents. One of the ways of improving profitability levels is to be able to recover more bad debts and this is essential for institutional performance. A critical delinquency management method involves cultivating an institutional culture that embraces zero tolerance of arrears and immediate follow up on all late payments. If more debts are going bad, it means that more funds are getting locked up in the hands of debtors which can have an effect on the capitalization of the institution and lead to more serious liquidity concerns.

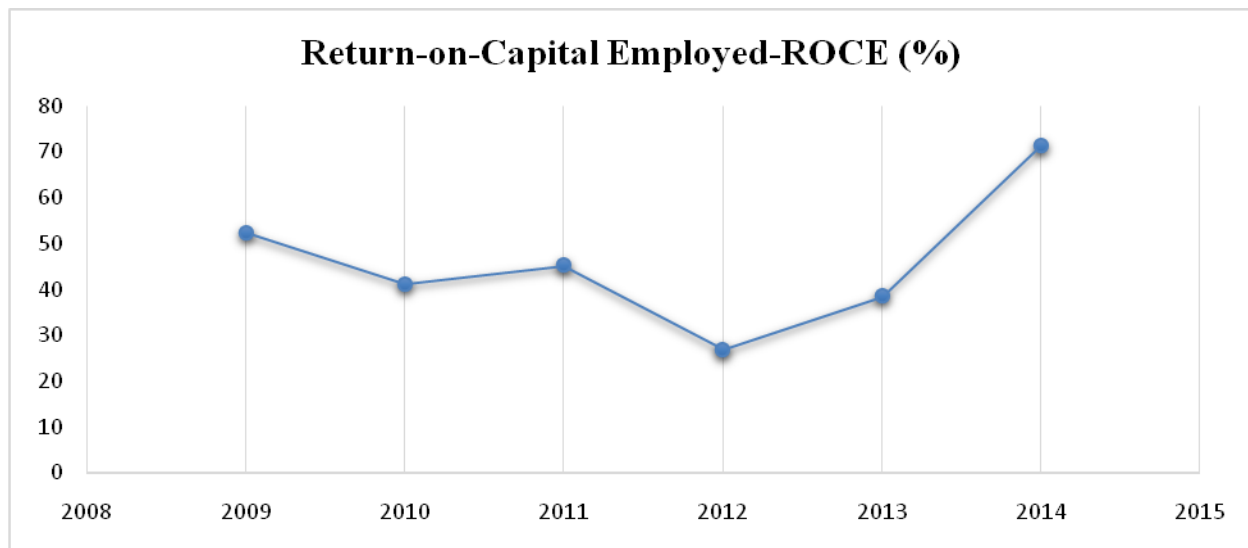


Fig 4.18

The Return-On-Capital-Employed shows how well an institution has been able to use its capital to efficiently generate revenue or income and this is a measure of the profitability of a business enterprise. The graph for the profit measure above, shows that the ROCE of FASL decreased from 2009 to 2010 and then showed a slight increase in 2011, which was then followed by a greater decrease in profit in the year 2011-2012. However, the graph shows a better performance from 2012 to 2014, reporting a sharp increase in profit. This may have been as a result of a reduction in the default rate due to strict enforcement of credit management procedures leading to the record of higher performing loans as well as flexibility in loan requirements thereby allowing more customers to access loan facilities. The rise in ROCE apparently was as a result of the significant increase in the interest income generated during that year. This means that clearly the company has been performing well in terms of being able to derive maximum benefits in terms of revenue from its capital (assets).

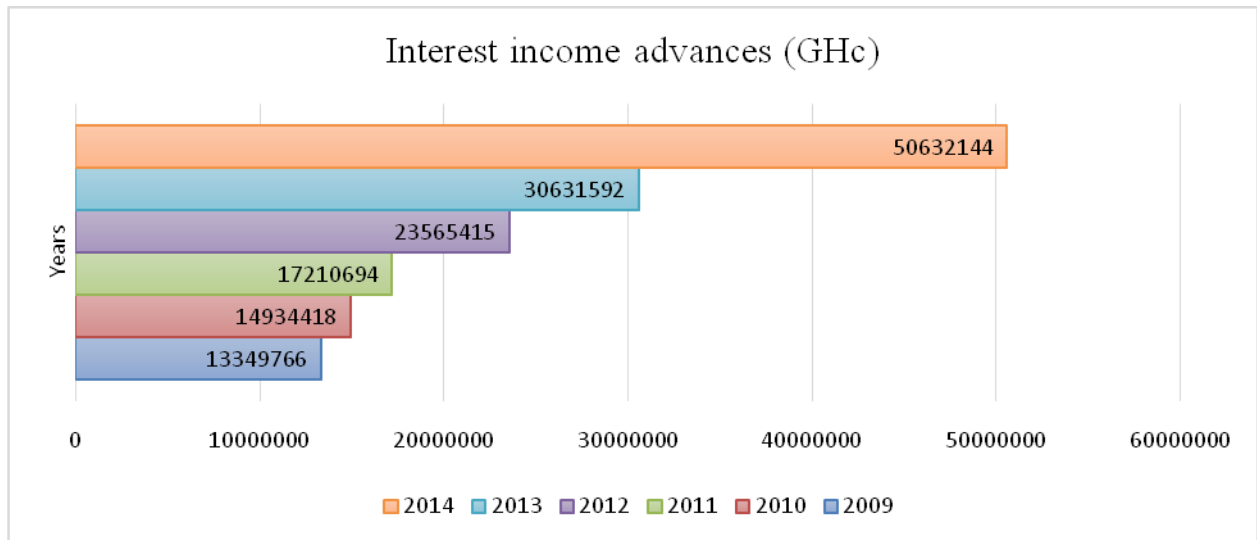


Fig 4.19

Interest income is generally a term used by companies on their income statements for reporting the interest accrued on cash temporarily held in savings accounts, certificates of deposits or other investments including loans. The above figure shows that interest income advances have been increasing from 2009 to 2014, with the business period 2013-2014 showing the highest increase. This was attributed to broadening of the loan customer base of the institution due to the flexibility that was adopted in the credit management procedures thereby allowing more customers to have access to loans as well as improved credit management procedures such as the introduction of micro-insurance on loan facilities granted as a way of insuring them against natural disasters and unforeseen circumstances. Once credit management practices are being strictly enforced and updated, it directly has an impact on revenue since interest income is generated from loans disbursed to customers so once the loans are performing, interest income shows a significant increase as can be seen from the graph in 2014.



Fig 4.20

Profit before tax in the graph above shows that there has been a smooth increase in profit before tax for the years 2009 to 2014. However, the increase has been marginal relative to the number of years under review. This means that if credit management procedures are improved, more revenue can be generated from increased interest income leading to higher profits since interest income are generated directly from performing loans. If more loans are performing, it means the institution can generate more interest income from a healthy loan portfolio.

4.5 Additional credit management processes that have been currently adopted by the institution

First and foremost, additional credit management processes that are adopted currently by the institution include: the background check for full disclosure of information for appraisal purposes, granting of concessionary rate to good customers, extension of loan duration from 12 to 24 months, pre and post disbursement monitoring, insurance of loan products, quarterly recovery and monitoring as gathered by the researcher from respondents

Others include, reduction in processing fees and days of contribution as a procedure for accessing susu loan products, taking cash collateral for all loan facilities, inspection of businesses/homes of would be borrowers, policies on loan graduation based on client's loan

repayment performance, using the risk department to recover bad loans and expired loans, inter branch monitoring and recovery teams formed to make loan recovering effective. These were all obtained by the researcher from staff respondents.

4.6 Strengths/Advantages of the firm's credit management policy

The advantages of the firm's credit management policy according to respondents included cash collateral which provide a cushion during default; usage of loan history which facilitates the process of loan graduation; increased monitoring of clients, customers accessing loans at shorter period, good recovery rate, ensuring the granting of higher performing loans and the introduction of micro-insurance which reduces the risk of default. Another important strength that was noted was the use of legal and risk departments in coordinating debt recovery. It was also noted that the credit management policy provided a solid guide for credit officers in granting loans as well as helping improve loan portfolio quality. Furthermore it also serves as a solid road map for all credit activities; helps in decision making processes and serve as performance indicator to measure growth. Again, it also helps prevent bad loans through the provision of a solid monitoring system, and helps make more loans available to SMEs and individuals; it helps to reduce the risk of loan default, and it improves commitment to loan repayment. Others identified the credit procedures as being customer friendly, flexible, and responsive to the needs of customers, aiding in the reduction in errors and major risks in appraisal and disbursement processes as well as reduction of fraud perpetrated by credit officers. Last but not the least, respondents also stated that the credit management practices also helped in reducing potential defaulters and also aided in the easy determination of cash flows due to the comprehensive nature of client appraisal forms which were updated regularly to meet modern trends in credit

management. These were gathered from open questions that were posed by the researcher to respondents

4.7 Weaknesses and challenges of the credit management procedures

Weaknesses identified in the credit management procedures by respondents were enumerated as follows: huge amounts of paper work that were involved in the credit granting process making it prolonged, poor perfection of security, cash collateral requirements and rigorous client appraisals that drove some customers away, high interest rate as compared to traditional banks and ineffective implementation of credit policy. Others included a lack of supervision, lack of communication, failure to enforce loan provisions when customers defaulted and rigidity of certain provisions which prevented customers from accessing loan facilities. Not being able to use the collateral secured to settle debts due to nature of collateral as well as lack of enforcement of provisions in loan contracts, poor documentation coupled with inadequate information provided by the customers, and more bad debts that were written off as part of policy were also identified as some weaknesses of the credit management procedures.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATION

5.0 Introduction

This chapter summarizes and briefly discusses the findings of the study. The study was conducted with a set of research objectives as a guide. It draws conclusions on the entire work and makes recommendations for the study.

5.1 Summary

This study assessed the effect of credit management practices on the performance of First Allied Savings & Loans Ltd. This was carried out by analysing the process of accessing credits; credits control processes and credits collection strategies. The descriptive survey method was used for the study. Sample size of 33 members of staff was drawn from all staff in all the four FASL branches in the Kumasi.

Two main sources of data were used for the study namely, the primary and secondary sources of data. Questionnaires were used as the main instrument to collect the primary data on access to credit, credit control processes and credit collection strategies.

The following findings were identified;

5.1.1 Credit Management Practices and their application in FASL.

The study revealed that FASL used client appraisal in Credit Management to a great extent. Further, it was established that client appraisal was a viable strategy for credit; aspects of collateral were considered while appraising clients; failure to assess customer's capacity to repay resulted in loan defaults; client appraisal considered the character of the customers seeking credit facilities and that FASL had competent personnel for carrying out client appraisal.

The study established that FASL used credit risk control in Credit Management to a great extent. It was also further established that interest rates charged did not affect performance of loans in the institution. Credit committees involvement in making decisions regarding loans were essential in reducing default/credit risk; the use of credit checks on regular basis enhanced credit management; penalty for late payment enhanced customers commitment to loan repayment; the use of customer credit application forms improved monitoring and credit management, flexible repayment periods improved loan repayment and also that the use of credit checks on regular basis enhanced credit management. The study revealed that FASL used collection policy in Credit Management to a great extent. Formulation of collection policies had not been a challenge in credit management whiles enforcement of guarantee policies provided chances for loan recovery in case of loan defaults. Staff incentives were seen as effective in improving recovery of delinquent loans, a stringent policy was more effective in debt recovery than a lenient policy, regular reviews had been done on collection policies to improve state of credit management, and finally that available collection policies had assisted towards effective credit management.

5.1.2 The Strengths and Weaknesses of Credit Management practices in FASL

It was discovered from the respondents that the credit management practices and policy of FASL had assisted in the reduction of bad loans in the books of the institution as well as allowing loan officers to follow an effective process in appraising loans due to its comprehensive nature. This facilitated the reduction of errors and major risks associated with appraisal and disbursement. Other strengths identified included lower charges on loan processing, lower interest rates as compared to other Savings & Loans companies as well as a lower savings period required before granting of loans. Again, taking of cash collateral (known as guarantee fund) helped to provide a cushion for the institution in case of default and the usage of loan graduations based on client's

loan history ensured that high-risk customers do not have access to huge facilities whilst low risk and dependable customers could access higher amounts whenever necessary.

Some of the weaknesses of the credit management practices that were enumerated included the strict nature of some of the requirements which resulted in a lot of people not qualifying for a loan. This ended up driving away a lot of potentially good customers. Requirements such as the provision of a cash collateral ended up pushing a lot of customers away since they considered it as a reduction in the total amount they were requesting for and therefore unable to fully meet their working capital demands. Again one challenge that was identified was that the credit granting process involved a lot of paper work and procedures making it very long and cumbersome for both the credit officers and the customers. This was found to be a disincentive as it prolonged the time it took for people to access loans thereby leading to higher default rate sometimes.

5.1.3 Impact on Performance

It was established that the credit management processes had a strong effect on the quality of loan portfolio of the institution. The effect of credit management policy on the loan recovery rates was also considered to be strong according to the findings.

Credit management practices were also established to have a high impact on interest income over the years as well as the profitability of the institution and finally the effect of credit management practices in FASL on loan default rates was also considered to be high by the respondents. The graphs as well as the longitudinal survey that was done between 2009 and 2014 also helped established the fact that credit management practices had a strong impact on institutional performance and helped to establish the facts that better credit management practices helped

ensure lower default rates, higher recovery rates, lesser non-performing loans, more revenue from interest income as well as higher profits for the institution.

5.2 Conclusion

The researcher established that the institution had a comprehensive credit appraisal system which considered the character of customers seeking credit facilities, the nature of the collateral, the capacity of the customer to repay as well as being able to effectively identify and access any inherent risks. Again the researcher established that credit risk control was considered as a major strategy in the credit management process which included compliance with internal guidelines and procedures as well as ensuring that all pre-disbursement conditions were met by customers.

Another major finding that was identified by the researcher as part of the credit management process was a strong credit collection policy. The major strategy that was employed as part of the credit collection policy of the institution was the establishment of the payment guidelines that would give a clear indication as to when and how loans would be paid.

It was also established from the study that the credit management policy of the institution was very effective in controlling the element of credit risk and impacting on the overall credit granting process; a firm application of the credit management processes helped reduce non-performing loans and the incidence of bad debts and improved recovery rates. The major weakness that was identified was the lack of effective monitoring as well as compliance with credit management procedures which affected the quality of the loan portfolio.

Finally it was established that credit management practices had an effect on recovery rates, default rates, interest income and the overall profitability of the institution. The graphs showed

that even though the institution had been performing satisfactorily in terms of profitability, a lot of work needed to be done in the area of default rates as well as write-offs and the incidence of bad debts as the data showed an increasing trend over the years which was quite significant. The researcher is of the opinion that when the right measures are put in place to supervise the credit management process, the institution can generate huge profits that can spiral remarkable growth over the years ahead.

5.3 Recommendations

One of the strong recommendations that has been presented is that management needs to put in place measures to ensure that credit officers comply fully with the credit delivery policies of the institution. One major weakness that was identified earlier from the findings was the lack of effective monitoring of loans given out by credit officers due to a lack of supervision. It is therefore imperative for a mechanism to be put in place by management to ensure that credit officers effectively monitor all loans disbursed as a way of reducing the risk of default.

Secondly, it is also recommended that a moratorium be permitted on some category of loans as a way of given customers enough space to be able to meet commitments. It was discovered from the findings that some customers found it hard to meet their repayments due to unexpected seasonal changes in their business cycles. Loan repayments were found to have a strict installment policy which sometimes made it difficult for customers to meet commitments when unexpected situations arise. It was therefore necessary, that a moratorium be made available under such circumstances in order to prevent customers from defaulting on their commitments.

Thirdly, more training programmes need to be organized for credit staff on modern methods of managing loans and credits delivery process. This was also clearly identified in the findings

concerning ways to improve the credit delivery process. The risks inherent in credit delivery keep increasing and becoming more complex over time and so it is important for credit staff to be fully abreast with current trends within the financial industry to enable them be fully equipped to deal with the challenges and risks within the credit management process.

Again, in order to reduce write-offs due to the incidence of bad debts, FASL should consider outsourcing these bad debts to debt recovery or factoring companies. This will allow them the opportunity to recover a huge amount of these bad debts and help reduce the huge write-offs that have been increasing tremendously over the years. A reduction in these write-offs will help generate more profits for the institution as it will reduce their expenditure tremendously.

Last but not the least, it is recommended that requirements such as the provision of cash collaterals should not be strictly enforced for all customers as this was identified as a major setback to customers accessing loans from the institution. Customers who have demonstrated a lot of commitment in terms of loan repayment should be excluded from such strict requirements as a way of acting as a huge incentive for them to access bigger loans and to also motivate prospective customers to meet their repayments in a timely manner in order to allow them the opportunity to access such incentives. This will be a huge step in allowing the institution to broaden its loan customer base as well as its loan portfolio leading to the generation of more interest income for the institution as well as significant increase in profits.

Finally, the researcher would like to recommend that further research be conducted into the effect of credit management on the capital structure of financial institutions.

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