St. Mary's University

School of Graduate Studies

ASSESSMENT OF CREDIT MANAGEMENT PRACTICE IN
COMMERCIAL BANK OF ETHIOPIA

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Addis Ababa - Ethiopia

January, 2016

ASSESSMENT OF CREDIT MANAGEMENT PRACTICE IN

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A Research Report Submitted to St. Mary's University,

School of Graduate Studies

In partial fulfillment of the requirements for the Degree Master's in

Business Administration

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ID. Number: SGS/0046/2006

January, 2016

ENDORSEMENT

This thesis has been submitted to St. Mary's University, School of Graduate Studies for examination with my approval as a university advisor.

Temesgen Belayneh (PhD, Assistance Professor)

Signature_____

Date_____

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DECLARATION

I hereby declare that this thesis is the result of my own research work towards the partial fulfillment of the requirements for the Degree of Masters in Business Administration in St. Mary's University. It contains neither material previously published by another person nor that has been accepted for the award of any other degree of the university, except where I have made explicit references to the work of others.

Chane Amare   ....

Signature   Date

APPROVAL

This is to certify that this research document has been submitted in partial fulfillment of the requirements for the Degree Master's in Business Administration with approved board of examiners.

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AKNOWLEDGEMENT

First of all I Thank Almighty God for his usual, continuous and unbroken support towards my entire carrier.

My sincere thanks go to my supervisor Dr. Abebaw Kassie for his unreserved suggestions, guidance and priorities at all his busiest time.

I would like to express my gratitude to my caring wife, Hiwot Amsalu for her continuous support , encouragement and taking care of all family matters during my study. My thanks also go to my beautiful daughters Mariyamawit and Yididya for creating conducive environment so that I can focus on my study and work at a time and to all my friends and family for their moral support.

ABSTRACT

This study intends to assess credit management practice of the Commercial Bank of Ethiopia based on three basic dimensions namely adequacy of credit policy content, compliance of the actual credit activities of the bank against the formulated policy and the overall existing credit control practice of the bank.

The research is designed as a case study on a single bank and a survey method was employed. Sources of both primary and secondary data were used. Questionnaire was used as a main instrument to collect primary data while secondary data were reviewed from different publications. Data was analyzed using SPSS 16.0 version and results are described based on statistical mean and standard deviation values.

The findings of the study revealed that CBE has adequate credit policy with a good content as per the examining statements provided. Similarly credit activities of the bank are complied with the stipulated credit policy document more than the average level. On the other hand the overall credit control activities of the bank are performing in an average level. This implies that the bank is expected to strengthen its credit controlling practice as one of the basic credit portfolio management tool so as to avoid associated risks with ongoing credit activities.

LIST OF TABLES

LIST OF ACRONYMS/ABBREVATIONS

ATM   Automatic Teller Machine

CA   Credit Administration

CBB   Construction and Business Bank

CBE   Commercial Bank of Ethiopia

CCA   Credit Control Activity

CM   Credit Management

CP   Credit Policy

CPU   Credit Processing Unit

DBE   Development Bank of Ethiopia

ETB   Ethiopian Birr

FDIC   Federal Deposit Insurance Corporation

L/C   Letter of Credit

LPM   Loan Portfolio Management

NBE   National Bank of Ethiopia

NPL   Non Performing Loan

O/D   Overdraft

POS   Point of Sale Service

RRO   Risk Return Optimization

SPSS   Statistical Package for Social Science

TLA   Total Loan and Advance

Contents

CHAPTER ONE

1. INTRODUCTION

Credit Management (CM) has grown as a discipline over the past decades in response to financial institutions continuing efforts to measure credit risk more accurately and to manage it more effectively across the firm. As it is well known, lending is the principal business activity for most commercial banks. The loan portfolio is typically the largest asset and the predominate source of revenue. As such, it is one of the greatest sources of risk to a bank's safety and soundness. Whether due to lax credit standards, poor portfolio and risk management, or weakness in the economy, loan portfolio problems have historically been the major cause of bank losses and failures (Comptroller's hand book, 2003)

Effective management of the loan and the credit function is fundamental to a bank's safety and soundness. Loan portfolio management (LPM) is the process by which risks that are inherent in the credit process are managed and controlled. Because assessing and reviewing of the credit process is so important and it is a primary managerial activity. Assessing credit management involves evaluating the steps bank management takes to identify and control risk throughout the credit process. (Comptroller's hand book 2003)

According to Boating (2011) good loan portfolio managers have concentrated most of their effort on prudently approving loans and carefully monitoring loan performance. And these activities continue to be main objectives of loan portfolio management. Credit managers expected to understand not only the comprehensive risk posed by each credit but also how the risks of individual loans and portfolios are interrelated.

Banks are merely custodians of the money they lend; hence interest must be paid to depositors and dividends to the investors Aug.et.al (2013). Credit management can be seen as an integral part of lending and as such in its absence, good loans can turn bad. It is expedient to note that the importance of credit management cannot be over-emphasized and good credit management requires the establishment of adherence to and of sound and efficient credit policies of government.

For banks to be successful, their corporate credit appraisal, disbursement, adequate monitoring and repayment must be assured. But experiences over the years have shown that inadequate credit analysis and sound judgment of loans application have resulted in nonperforming loans.

Provision of credits, which are in the form of loans and advances, are the total amount of money a given bank lends out to its customers at any given period of time. The bank usually charges the borrower interest for using its money. These loans and advances usually have maturity period. In providing credits for business ventures, banks should as a matter of importance take all necessary steps to ensure that advances are granted to those customers who can and will make judicious use of

loans so that repayment will not become a problem. Therefore credits must be made to people who are capable of utilizing it well and repaying the loan at its maturity.

The place of loans and advances in the affairs of banks can be explained by referring to the fact that "loans and advances are the largest item in the assets structures and income from loan and advance (interest income) is also one of the major income elements of commercial banks. Commercial bank of Ethiopia (CBE) as it is the leading bank in terms of market share, branch network, volume of asset and profitability, the year-end financial report of 2013 shows that the bank has an asset section loan and advance element of 69.7 billion and net interest income of 7.2 billion. Therefore it is justifiable for banks like CBE to give due consideration for proper credit management using appropriate policy and credit control mechanisms.

1.1. Background of the organization

1.1.1. Establishment of CBE

Sources of National Bank of Ethiopia (NBE, 2010) indicate that modern Banking in Ethiopia dates back to the year 1905 when the Bank of Abyssinia was established. Bank of Abyssinia was formed under a fifty year franchise agreement made with the National Bank of Egypt, which was owned by the British by then. To widen its reach in the country the Bank had expanded its branches to Dire Dawa, Gore and Dessie. It also had an agency and a transit office in Gambella and at the port of Djibouti respectively.

After its formal liquidation on August 29, 1931 the Bank of Abyssinia was replaced by the Bank of Ethiopia. According to NBE (2010) Bank of Ethiopia, which was also known as Banque National Ethiopienne, was a national bank and one of the first indigenous banks in Africa.

The Bank of Ethiopia operated until 1935 and ceased to function because of the Italian invasion. During the five years of the Italian occupation (1936-41), many branches of the Italian Banks such as Banco d-Italia, Banco di-Roma, Bancodi-Napoli and Banco Nazianalide Lavoro were operational in the main towns of Ethiopia.

After the Ethiopian-English victory over Fascist Italy, the new government established the State Bank of Ethiopia a proclamation issued in August 1942. State Bank of Ethiopia commenced full operations on 15 April 1943 with two branches and 43 staff. It served both as the Ethiopia's central bank with the power to issue bank notes and coins as the agent of the Ministry of Finance, and as the principal commercial bank in the country. In 1945 the Ethiopian government granted the bank the sole right of issuing currency. The first governor of the bank was an American, George Blowers. He inaugurated the new national currency, which owed its successful introduction to the United States. The United States provided the silver for 50 cent coins, whose intrinsic value ensured popular acceptance of the new paper money to a population used to the circulation of the silver Maria Theresa.

After evacuation of Italians, the State Bank of Ethiopia was established on November 30, 1943 with a capital of one million Marian Treasury of the Ministry of Finance. Pursuant to the Monetary and

Banking Law of 1963 the State Bank of Ethiopia that had served as both a central and a commercial bank was dissolved and split into the National Bank of Ethiopia and Commercial Bank of Ethiopia Share Company. Accordingly, the central banking functions and the commercial banking activities were transferred to the National Bank Ethiopia and the Commercial Bank of Ethiopia Share Company respectively.

The Ethiopian government merged Addis Bank into the Commercial Bank of Ethiopia in 1980 to make CBE the sole commercial bank in the country. The government had created Addis Bank from the merger of the newly nationalized Addis Ababa Bank, and the Ethiopian operations of the Bancodi Roma and Banco di Napoli. At the time of nationalization, Addis Ababa Bank had 26 branches. The merger of Addis Ababa Bank with made CBE the sole commercial bank in Ethiopia, with 128 branches and 3,633 employees

In 1991, when Eritrea achieved its independence, CBE lost its branches in Eritrea to nationalization. These branches formed the base for what became in 1994 the Commercial Bank of Eritrea. Also in 1994, the Ethiopian government reorganized and reestablished CBE.

1.1.2. Current state of the bank

CBE is the leading bank in terms of market share, branch network, volume of asset and profitability. After its establishment in 1942, CBE is a pioneer to introduce modern banking in the country having 939 branch outlets 2014/15 and a leading African bank with assets of 220.8 billion Birr as per the nine month progress report made on 2015.

In addition the bank currently mobilizes a total deposit of 27.5 billion from its total depositors of 10.1 million across the country. The bank also availed its customers with the 627 Automatic Teller Machine (ATM) and 1,162 Point of Sale Service (POS) machines at major business centers of the country. It also has about 145,000 mobile banking and 1,127 internet banking users. The new establish interest free banking also acquires around 70,000 customers so far.

The Commercial Bank of Ethiopia is going to build the first longest and huge skyscraper in Africa for its Head Quarter with a total number of 46 floors in the capital and construction contract is already concluded with the China State Construction Engineering and the construction is underway..

1.1.3. The mission statement and values of the Bank

Vision - becoming a world- class commercial bank by the year 2025.

Mission Statement - we are committed to best realize stakeholders' needs through enhanced financial intermediation globally and supporting national development priorities, by deploying highly motivated, skilled and disciplined employees as well as state-of-the-art technology. We strongly believe that winning the public confidence is the basis of our success.

Corporate citizenship

We value the importance of our role in national development endeavor and step-up for commitment.

We abide by the law of Ethiopia and other countries in which we do business.

We care about society's welfare and the environment.

Customer Satisfaction

We strive to excel in our business and satisfy our customers.

Quality Service

We are committed to offer quality service to our customers' and aspire to be branded with quality in the minds of our customers and the general public.

Innovation

We encourage new ideas that can improve customers' experience and the Bank's performance.

Teamwork

We recognize the importance of teamwork for our success.

We respect diversity of viewpoints.

Integrity

We are committed to the highest ideas of honor and integrity.

Employees

We recognize our employees as valuable organizational resources.

Public Confidence

We understand that the sustainability of our business depends on our ability to maintain and build up the public's confidence.

Keeping all these vision, mission and value statements, CBE currently is giving nearly a full furnished banking service for its national and international customers and it's a major player in the economic progress and development of the country. It has more than 10.1 million account holders, strong relationship with more than 50 well known foreign banks like Commerz Bank of Germany, Royal Bank of Canada, City and GP Morgan banks of USA and HSBC banks.

CBE also has a SWIFT bilateral arrangement with 700 other banks across the world. The bank currently has more than 23,000 permanent workers in the country and its oversea branches abroad in

South Sudan. As it is a first bank to introduce Western Union Money Transfer in Ethiopia, these days it's working with other 20 money transfer agents like: Money Gram, Atlantic International (Bole), Blue Nile, Dihabshiil, Money Transit, Xpress Money, Golden Money Transfer, Tran Fast, Turbo Cash and other agents.

Online internet banking service also given by the bank to enable customers carries out transactions comfortably from their home or office. The online services include:

Viewing account balances and transactions.

Making fund transfers between customers' own current accounts and savings accounts.

Effecting payments to the third parties, including bill payments pre-defined CBE customers within Ethiopia.

Viewing and downloading current and saving account statements.

Requesting for stop payment on cheques etc.

Applying for a Letter of Credit.

Other than Saving Account, Current Account, Money Transfer, Cheque Clearance and payment services, the bank extends different types of credit facilities to its customers in short term, medium term and long term credit categories.

1.2. Statement of the problem

Asper Comptroller's Handbook of loan portfolio management (1998), the primary activity of commercial banks is lending, and therefore the loan portfolio represents one of the largest assets and a predominant source of revenue. This would also be a great source risk to banks if it is not properly managed. As it is large part of the total banks asset, its failure will necessarily be big for the entire bank. Whether due to credit standards, poor credit management and control or weaknesses in the economy, credit problems have historically been the major cause of bank losses and failures. Therefore it is mandatory for banks to implement a sound practice of credit management so as to stay healthy and profitable in the commercial banking business.

The credit volume of commercial banks in Ethiopia is increasing through time as their market share increase in the industry. According to CBE's bilingual magazine of "*Mudaye-Neway*" 2014 edition, a statistical report of 12 years that shows yearly deposit and loan of banks, an average of 69% of the total deposit of banks are extended for loans where deposit is a huge portion of the bank's total liability section of the balance sheet.   For instance, out of the total liability of CBE in 2013, about 83% is the customer's deposit and deposit due by other banks. Likewise major portion of the banks' profit also resulted from their lending activities.

Provision is usually held for anticipated loan losses which arise from different reasons like insufficient credit managements, low quality lending activities, inadequacy of integrated credit policy and procedure, inconsistent execution of credit activity against the existing policy and procedure, as

well as weak control over credit. It is a kind of cash reserve set aside from the bank's profits in order to recover expected loss from particular credit portfolio, Eliana et al (2013). For instance, total provision held by the Commercial bank of Ethiopia has increased from ETB 1.4 billion in 2012 to ETB 2.9 billion in the first quarter of the current business year (2015) where the credit volume increased from 58 billion 2011 to 96 billion in the first quarters of 2015. This clearly shows that there is a high anticipation of possible loan loss through time as a credit volume increases despite the rate of an increase in credit volume is still less than the rate of increase in provision.

In addition as per loan classification and provision report made annually to the governing bank (bank supervision directorate of NBE), the bank's Nonperforming Loan (NPL) amount was also increasing during the last consecutive years. For example based on the bank's annual report, NPL amount of Birr 300 million in 2011, 316 million in 2012, 1.46 billion in 2013and 1.56 billion in 2014 was reported.

According to NBE's (National Bank Of Ethiopia, 2008) the commercial bank of Ethiopia is the giant and leading bank in Ethiopian banking industry in all aspects of banking operations like huge capital ownership, wider branch networks, deposit mobilization, credit service, foreign exchange collection as well as annual income. Based on *Mudaye-Neway*, a bilingual magazine published by CBE Vol. 3 No. 4 2014, the three public banks that are CBE, CBB and DBE provide more than half of the credit volume in Ethiopia while, CBE alone contributes over 50% of total loans and advance (TLA) that are provided by all public banks in the industry (Commercial Bank Of Ethiopia, 2014). This implies that if a sound credit management activities are not employed and if the bank's lending activities are not healthy, it leads not only to the erosion of huge part of the bank's profit but also affects large amount of the credit requirements of the economy. Despite all these facts and the sensitive nature of the sector, to the extent of the researcher's knowledge, no comprehensive research has been undertaken so far which has evaluated the credit management activities of the commercial bank of Ethiopia.

Not only on CBE, but also to the extent of researchers investigations made in the area no empirical research has found that looks in to and evaluate credit management practice of commercial banks in Ethiopian banking industry except with the very single case study made on Wegagen Bank Sc. Tigray Region published in 2010. This is also one of the main reasons that the researcher initiate to make the credit management evaluation practice in CBE and to deliver the first initial reference document for those who are interested in carrying on similar study on this bank or other banks and credit institutes in the industry.

Commercial banks should be strong and determining to protect themselves from loss arising from their credit activities. Maintain sound credit management practice by making timely evaluation and frequent examination of their level of credit management is one basic way of banks to keep their entire loan healthy and well performing. Based on the facts mentioned above like increasing nature of nonperforming loans, annual increasing volume of provision for anticipated loan loss and furthermore no assessment has made so far to evaluate the strength of the credit management practice of the bank despite loan is a huge portion of the bank's asset (193 billion out of total asset of 249 billion in 2014)the researcher was interested in and has found justified to look into to what extent credit management is being practiced in commercial bank of Ethiopia based on some basic credit

management dimensions so as evaluate and identify areas that need further enhancement to carry on sound and healthy credit activities.

1.3.   Objectives of the study

General Objective

The main objective of this study is basically to assess the aspects of credit management in commercial bank of Ethiopia.

Specifically, the study has objectives of:

Specific objectives

1. To asses adequacy of the bank's credit policy to guide all its loan activities
2. To examine compliance of the actual lending activities of the bank to its established policies
3. Assessing the current credit control practice of the bank

1.4.   Research Questions

1. Did the bank established adequate credit policy with sufficient content to guide the lending activities?
2. Does the bank consistently comply with its credit policy on its loan performing activities?
3. How are the current credit control activities of the bank on its credit management process?

1.5.   Significance of the study

This study contributes to the financial services literature as it is one of the very few that examine credit management application in the Ethiopian banking sector. More specifically, the study has the following potential contribution for commercial bank of Ethiopia.

This study would be significant in assessing the currently existing level of credit management practice in the commercial bank of Ethiopia and point out strength and weakness based on the research output.

It serves as a background material to further assessment of its level of credit management application of the bank in different dimensions.

It enables the bank to identify the areas of the credit management that needs further enhancements so as to benefit from Its application properly and at full scale.

This research paper can also be used as an initial reference for those who are intended to make further research in the area as may be very few or none is written so far in the area.

1.6.   Limitation of the Study

This study emphasis only on a single bank out of many commercial banks that believed to carried on credit management practice as one of their basic functions. Had such study been made on all commercial banks in Ethiopian banking industry, it would have better results. However due to the vast nature of the topic (since credit management is wide principle), because of credit management function is different for different banks (depends on their complexity, lending culture, risk appetite etc.), because of confidentiality nature of credit documents, due to time and financial constraints of the researcher, it is limited to this specific bank.

1.7.   Organization of the Study

The research is organized into five chapters. The first chapter introduces the background of the study, background of the organization, the research objectives and questions, significance of the study, limitation of the study and organization of the study. The second chapter presents theoretical and empirical review of the related literatures while the third chapter deals with methodology of the study. The fourth chapter is concerned with summary of analysis as results and discussions. Finally the fifth chapter presents the conclusion and recommendations drawn from the findings.

CHAPTER TW

2. RELATED LITRATURE REVIW

The purpose of this chapter is to present a view of literature relating to credit management in banks on both theoretical and empirical grounds. Review of some of the studies carried out and suggestions extended by those authors on the subject have helped to carry out the study in line with the objective and scope.

2.1. THEORETICAL REVIEW

2.1.1. Origins of Credit

The origin of bank credit could be traced to the medieval times, long before the advent of goldsmiths in the western civilization. As far back to 1850 BC, lending activities were recorded in the temple in Babylon. The actual existence of the temple covered a century or two previously. During this period, lending was primarily for consumption and the imposition of interest was termed as exploitation. One of the earliest enactments on bank lending is Hebrew Law. Hebrew Law recognized lending but prohibited the taking of interest. Enrichment through lending with interest was forbidden and severe punishments were prescribed for such acts. This was later incorporated into Mosaic laws which prescribed thus, "You shall not lend upon interest to your brother". About 1545, the mosaic laws were abolished and the taking of interest on loans was made legal. The Arabic civilization also recognized lending activities, but usury is condemned and prohibited as much as possible. (FATIMA, 2013)

In Ethiopia, the origin of lending did not clearly traced, but could be estimated with the emerging of activities of traditional barters long before the advent of the formal market. No research has done or no literature has found that indicate specific time about the starting of lending in Ethiopia. But traditional financial activities (traditional saving and lending) believed to be emerging with the philosophy of traditional "Edir" and" Ekub" in rural and semi urban Ethiopia. "Edir" involves offering assistance of financial and labor mainly stand for performing burial and condolence ceremony when death is occurred among the family members in a traditional society which has an implication of early contribution and saving. Whereas "Ekub" is financial form of traditional cooperative formed voluntarily based on rotating saving and credit type association whose members make regular contribution to revolving trend. It somehow requires guarantee by the payee when he takes the money from the members to minimize risk of failure.

Many people used these forms of cooperation as a means of financial solution to their economic problems. "Ekub" is somewhat similar to modern saving and credit cooperative Verakumaran (2013).

With the emergence of formal and informal trading exchange activities and growth of urban and rural society searching for financial source has come in place. Therefore families, relatives, friends and traditional money lender like "*arata-abedari*" were used as informal financial source to fill the gap of financial demand till the coming of modern financial service in Ethiopia, Solomon (2007)

2.1.2. The Concept of Credit Management

According to Onyeagocha (2001), the term credit is used specifically to refer to the faith placed by a creditor (lender) in a debtor (borrower) by extending a loan usually in the form of money, goods or securities to debtors. Essentially, when a loan is made, the lender is said to have extended credit to the borrower and he automatically accepts the credit of the borrower. Credit can therefore be defined as a transaction between two parties in which the creditor or lender supplies money, goods and services or securities in return for promised future payments by the debtor or borrower.

Credit Management refers to the efficient blend of four major credit policy variables to ensure prompt collection of loans granted to customers and at the same time boost their confidence in and loyalty to the bank (Ankrah, 2011). The first variable is the assessment of the quality of the customer account. This examines the ability of the customers to repay on time. The second policy variable is that of setting the credit period. In so doing, the bank ought to give (agu Osmud Chigozie, 2012)enough time to allow the customers derive the full benefits of the credit. Such period must not be too long to put the bank at a disadvantage. The third variable is the discount or the enticement to credit beneficiaries to repay credit on time. Such enticement must be motivating enough before the aim can be achieved. The last variable considers the expenditure level that could be incurred in the collection exercise. This implies that the bank must not grant credit where the amount to be expended on collecting the debt will likely be greater than the debt itself. To blend these variables into an efficient workable system requires careful planning in controlling.

According to Obaje (2010) that there are three major types of credit and two types of credit functions. These are commercial credit, consumer credit and investment credit.)

Commercial credit can be bank credit such as overdraft, loans and advances; trade credit from suppliers; commercial papers (or notes); invoice discounting; bill finance; hire purchase; factoring etc.

Consumer credit is a kind of permission granted to an individual or a household to purchase goods like refrigerator, television, car, electronic sets, which could not be paid for immediately but for which installment payments are made over a period of time.

Investment credit allows a business concern such as corporate body, sole proprietorship or partnership to obtain credit for capital goods for expansion of factoring or procurement of machinery. The tenor of a loan varies from short to medium, role to long term depending on the institution, nature and functions.

Whereas functions of credit are primarily two: it facilitate the transfer of capital or money to where it will be most effectively and efficiently used; and secondly, credit economizes the use of currency or coin money as granting of credit has a multiplier effect on the volume of currency or coin in circulation despite the cost of credit like interest and discount rate is one of essential tools to be used to control and regulate money by the central banks through their monetary policy.

2.1.3. Definition of Credit Management

There are many definitions given for credit management (CM) by different scholars. Among them, some are provided as follows:

According to (Nath, 2013) Credit management in a bank is a dynamic sector where a certain standard of long-range planning is needed to allocate the fund in diverse field and to minimize the risk and maximizing the return on the invested fund. The objective of the credit management is to maximize the performing asset and the minimization of the non-performing asset as well as ensuring the optimal point of loan and advance and their efficient management

Credit management is implementing and maintaining a set of policies and procedures to minimize the amount of capital tied up in debtors and to minimize the exposure of the business to bad debts (Mirach, 2010). When it functions efficiently, credit management serves as an excellent instrument for the business to remain financially stable and profitable. Credit management is also the process of controlling and collecting payments from customers. This is the function within a bank or company to control credit policies that will improve revenues and reduce financial risks.

Wise Geek (2014) describe credit management as the process of building a series of investments based upon credit relationships and managing the risks involved with these investments. Therefore, credit management encompasses assessing the risk involved with each loan and then analyzing the total amount of risks for all loans. The major objective of credit management is to reduce the amount of loans default. Banks reduce the loan portfolio default risk by considering the credits repayment history of both individuals and groups applying for loans. Myers and Brealey (2003) describe credit management as methods and strategies adopted by a firm to ensure that they maintain an optimal level of credit and its effective management. (T.R, 1997)Nelson (2002) also views credit management as simply the means by which an entity manages its credit extension. It is a prerequisite for any entity dealing with credit transactions since it is impossible to have a zero credit or default risk.

2.1.4. Features of Credit Management

Credit management is one of the most important activities in any company and cannot be overlooked by any economic enterprise engaged in credit irrespective of its business nature. It is the process to ensure that customers will pay for the products delivered or the services rendered. It is an aspect of financial management involving credit analysis, credit rating, and credit classification and credit reporting. The higher the amount of accounts receivables and their age, the higher the finance costs incurred to maintain them. If these receivables are not collectible on time and urgent cash needs arise, a firm may result to borrowing and the opportunity cost is the interest expense paid.

Nzotta (2004) opined that credit management greatly influences the success or failure of commercial banks and other financial institutions. This is because the failure of deposit banks is influenced to a large extent 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. A key requirement for effective credit management is the ability to intelligently and efficiently manage customer credit lines. In order to minimize exposure to bad debt, over-reserving and

bankruptcies, companies must have greater insight into customer financial strength, credit score history and changing payment patterns.

According to Rosemary 2011, credit management starts with the sale and does not stop until the full and final payment has been received. It is as important as part of the deal as closing the sale. In fact, a sale is technically not a sale until the money has been collected. It follows that principles of goods lending shall be concerned with ensuring, so far as possible that the borrower will be able to make scheduled payments with interest in full and within the required time period otherwise, the profit from an interest earned is reduced or even wiped out by the bad debt when the customer eventually defaults. Credit management is concerned primarily with managing debtors and financing debts. The objectives of credit management can be stated as safe guarding the companies' investments in debtors and optimizing operational cash flows.

Policies and procedures must be applied for granting credit to customers, collecting payment and limiting the risk of non-payments. Accordingly every bank has to develop and implement comprehensive procedure and information systems to follow up the condition of individual credit (Odofuye (2007).

2.1.5. Importance of Credit Management

Credit management always has huge importance and play major role in organization especially in banks' lending business by enabling them:

Reduce credit concentration risk, reflecting various factors, including the financial institution's marketing policies, to make business base and lending practices, to make better diversification

(Credit may concentrated in certain areas or business sectors and/or individual companies) etc. In addition, credit management enables commercial banks and financial institutions to:

Reduce credit risk - (economic capital)- CM is effective not only in reducing credit concentration risk as seen above, but also in ensuring that capital is adequate vis-à-vis credit risk. Even when current credit risk is judged not to be excessive, CM can be broadly applied to adjusting the risk profile by taking steps to reduce credit risk as part of protective preparations against potential stress situations, such as the next downturn.

Risk/return optimization(RRO)- in cases where management is also conscious of the need to optimize shareholder value, CM's direct objectives will be to reduce risk while improving returns as a means of improving the balance between the two. In this case, the primary aim is to ensure that the risk/return relationship is optimized at all times by dynamically replacing credits that bear a poor risk/return profile with credits that bear a better one.

Controlling bad debt exposure and expenses through the direct management of credit terms on the company's ledgers.

Maintaining strong cash flows through efficient collections. The efficiency of cash flow is measured using various methods.

Monitoring the accounts receivable portfolio for trends and warning signs.

Determine credit ceilings.

Setting credit-rating criteria.

Setting and ensuring compliance with a corporate credit policy.

Obtaining security interests where it is necessary.

Initiating legal or other recovery actions against customers who are delinquent.

2.1.6. Types of Credit Management

Based on (Study Group on Credit Portfolio Management, May 2007) released report of the Credit Management Study Group of Japanese Financial Institutes, CM takes various forms depending on the development status of the credit market, the features of the credit portfolio (level of credit concentration, etc.), the importance of long-term relationships with customers, relationships with a broader range of stakeholders, and management strategies that take such factors into account. To simplify this group indicate that it is useful to set up credit management in to two categories: risk-hedge-oriented CM, and enhanced return-oriented CM.

Risk-hedge-oriented CM focuses more on reducing risk in the credit portfolio than on increasing returns, and typically aims to free up economic (or regulatory) capital by correcting credit concentration. Based on this report currently, major European banks have basically adopted this type of CM which for example, involves reducing selling off loan assets when large loans exceed internal credit limits.

On the other hand, enhanced return-oriented CM aims to improve the risk/return balance by not only reducing risk, but also raising returns. More specifically, the intention behind this type of CM is not simply to release economic capital, but also to make effective use of it, and it is normally used in the credit market for flexible rebalancing of credit portfolios (risk hedging and risk taking).

2.1.7. Basic Tools of Sound Credit Management

According to Ankrah(2011) credit management involves establishing formal legitimate policies and procedures that will ensure: the proper authorities grant credit, the credit goes to the right people, the credit is granted for the productive activities or for businesses which are economically and technically viable, the appropriate size of credit is granted, the credit is recoverable and there is adequate flow of management information within the organization to monitor the credit activity.

Credit Management refers to the efficient blend of major credit policy variables to ensure prompt collection of loans granted to customers and at the same time boost their confidence in and loyalty to the bank.

After the loan is approved and draw down consistently with the established loan policies and procedures, the loan should be properly controlled. These include reviewing loans in timely manner, keeping track of borrowers' compliance with credit terms, identifying early signs of irregularity,

conducting periodic valuation of collateral and monitoring timely repayments. As described above, granting credit using policy guidelines is one thing but controlling the performance of loans using better loan controlling tools is another vital matter.

2.1.8. The Credit Policy

Every bank puts in place a credit policy to guide its lending decisions, taking this into consideration its overall corporate objectives conceptually, a bank's corporate objectives influence its overall banking operation (Obaje, 2010).

The loan policy is the primary means by which senior management and the board guide lending activities. Although the policy primarily imposes standards, it also is a statement of the bank's basic credit philosophy. It provides a framework for achieving asset quality and earnings objectives, sets risk tolerance levels, and guides the bank's lending activities in a manner consistent with the bank's strategic direction. Loan policy sets standards for credit portfolio composition, individual credit decisions, fair lending, and compliance management. The credit policy should be clearly defined, consistent with prudent banking practices and relevant regulatory requirements, and adequate for the nature and complexity of the banking institution's activities Puan (2001)

According to Comptroller's Handbook portfolio management (1998) Loan policies vary in length, organization, degree of detail, and breadth of topics there is no ideal format. Frequently, the bank's general lending policy will be supplemented by more detailed underwriting standards, guidelines, and procedures. Within the same banking company, certain aspects of the policy may vary because of factors such as geographic location, economic conditions, personnel, or portfolio objectives. The policy should provide a realistic description of where the bank wants to position itself on the risk/reward spectrum.

It needs to provide sufficient latitude for a bank to respond to good business opportunities while concurrently controlling credit risk. Loan Policy provides a general rule to guide decisions concerning credit management.

Loan policies provide a framework for credit management process. They set standards and parameters to guide managers and credit officers in evaluating, granting and loan monitoring and follow up actions. They provide Directors, regulators, auditors with a basis for evaluating performance McNaughton (1992). Credit policy involves three decision variables namely credit terms (interest charge, loan size, loan period, collateral requirement and eligibility criteria) credit standards and collection effort.

For the policy to be an effective risk management tool, it must clearly establish the responsibilities of those involved in the lending process. For example, who is authorized to approve a covenant violation, who arbitrates risk rating differences, can a credit-scored decision be overridden? Lenders must know what is expected of them. When policy is vague or too broad, credit standards may be unclear and virtually nothing may be regarded as an exception. If the policy states that a bank will extend credit to established businesses, almost any company would qualify.

When policy is too prescriptive and particular, exceptions to policy will become the rule and meaningless exception data will mask meaningful trends, thereby diminishing the effectiveness of the policy. Because exceptions are so important, the policy should address them specifically; it should state when they are acceptable and how they should be identified, mitigated, and documented. Some lending standards, such as those that implement legal requirements or those whose violation quickly translates into losses, have greater significance than others. More substantive exceptions should have heightened reporting requirements to senior management and the board. Failure to comply with the provisions of loan policy concerning exceptions is generally regarded as a material weakness. Significant numbers of material exceptions should be a factor in a lender's performance evaluation.

Policies should be periodically reviewed and revised to accommodate changes in the bank's strategic direction, risk tolerance, or market conditions. Policy review should consider the organizational structure, breadth and complexity of lending activities, capabilities and skills of lending personnel, and strategic portfolio quality and earnings objectives. Changes in regulations and business conditions also need to be considered. In addition to providing an opportunity for change, the review should evaluate how well the policy has guided lending decisions.

For example, a high volume of exceptions indicates that many loan decisions are being made outside the policy. This could mean that the bank is assuming more risk than is desirable or that the policy is too restrictive. If the bank's policy is too restrictive, easing it could increase business opportunities without unduly increasing risk. Conversely, the absence of exceptions may indicate that the policy is too vague, and a tightening of the policy could strengthen the controls on loan quality. All policy reviews should include the organizational unit responsible for assessing compliance with policy.

2.1.9. Loan Policy Components

The form and contents of loan policies and procedures will vary from bank to bank; however, many literatures indicate that there are some common elements that the loan policy should include: loan authorities, limits on aggregate loans, and commitments, distribution by loan category and product, geographic limits, types of loans, underwriting criteria, collateral and structure requirements, pricing guidelines, documentation standards, collections, reporting requirements, and guidelines for loan participations are some of them.

The policy may also address insider transactions, affiliate transactions, conflicts of interest, the code of ethics, community support, appraisal requirements, environmental assessment requirements, relevant accounting issues such as, nonperforming loans and debt restructuring), and the allowance for loan and lease losses. Any administrative requirements for granting loans should be covered in the policy. Policies and procedures should also ensure compliance with laws and regulations.

2.1.10. Exceptions to Policy

Lending exceptions generally either relate to documentation or underwriting. Banks should have systems to analyze and control both types of exceptions. While it is advisable to identify, mitigate, and monitor all exceptions, the level of attention and reporting should correspond with the materiality of the exception. A missing title can be handled satisfactorily at the administrative level, but a breach

of the house lending limit should be brought to the attention of senior management and the board. Institutions making "low documentation" small business and farm loans are exempt from exception tracking for the qualifying loans.

2.1.11. Policy and Documentation

"Loan documentation" refers broadly to the documents needed to legally enforce the loan agreement and properly analyze the borrower's financial capacity. When a document is missing, stale, or improperly executed, it becomes an exception.

Common loan documents are promissory notes, note guarantees, financial statements, collateral agreements, and appraisals. The promissory note, guarantee, and financial statement must be properly prepared and signed; the financial statement must be received and analyzed in a timely manner by the bank; and the collateral agreement must be recorded in the appropriate jurisdiction. A bank should systematically identify document exceptions, initiate timely resolution, and ensure that documentation remains current and valid throughout the loan term.

2.1.12. Policy and Underwriting

Policy and underwriting exceptions are conditions in approved loans that violate the loan policy or underwriting guidelines. Because underwriting guidelines are the primary means by which the bank steers lending decisions toward planned strategic objectives and maintains desired levels of risk within the portfolio, deviations from these guidelines should be well documented and justified

It is obvious that banks serve a broad constituency. In order to meet the legitimate credit needs of their communities and service creditworthy borrowers, banks will occasionally approve loans outside established guidelines. Loans with approved exceptions are often acceptable risks and should not be criticized solely because of their exceptions. However, these credits often warrant closer-than-normal supervision.

Loan Portfolio Management Comptroller's Handbook (1998) Identifying and approving exceptions is part of effective portfolio risk management. The loan approval document should clearly identify exceptions and provide mitigates that justify the decision to underwrite. This information should be kept in the permanent loan file.

2.1.13. Credit Control

According to O. Fatima (2010) credit control is concerned with the post approval and monitoring of the credit facility, to ensure that each credit remains qualitatively satisfactory during the tenure of the credit. It is very important to monitor (control) the facility after it has been approved to ensure that:

(I) the borrower complies with the stipulated conditions

(II) the facilities are utilized with the purpose for which they were approved

(III) any deterioration or negative trends in the customers" business or prospects is determined and corrective actions taken.

Credit controls also entail making some basic credit returns as required by the Banking Act for the purpose of monitoring the banks total commitments to clients in a particular period. Based on David T.R's statement made on the Hong Kong Monetary Authority's Quarterly Bulletin of 1997 edition, poor asset quality attributable to over-concentration and poor risk selection remains main causes of problems in banks.

In maintaining sound credit controls, a clear credit philosophy, and ongoing management of credit portfolio with a view to identifying early warning signals of deteriorating asset quality helpful.

The bank identifies three main causes of these asset quality problems, some of which were present in more than one case. One could be over concentration, where the failure of one loan places the bank in jeopardy. Another was specialization, where there was a concentration of loan book in one sector, region, or group of individuals. The third one may be poor risk selection, where the bank extends loan without correctly price a risk.

2.1.14. Credit Control Functions

Office of the Comptroller of Credit Portfolio Management (1998) states that besides the loan policy, the primary controls over a bank's lending activity is its credit administration, loan review, and audit functions. Independent credit administration, loan review, and audit functions are necessary to ensure that the bank's risk management process, management information systems, and internal and accounting controls are reliable and effective. The bank's control functions can also provide senior management and the board with a periodical assessment of how the bank's employees understand its credit culture and whether their behaviors conform to the bank's standards and values.

2.1.15. Independence

Independence is the ability to provide an objective report of facts and to form impartial opinions. Without independence, the effectiveness of control units may be jeopardized. Independence generally requires a separation of duties and reporting lines. However, it should not be assumed that the independence of a control function is solely a function of reporting lines. Independence also depends heavily on the corporate culture's valuing and promoting objective oversight and constructive criticism. No individual or group should be expected to preserve its independence on its own; instead, senior management, the board, the credit culture, and the organizational framework should all support the independence of control units.

Budget constraints can compromise the independence and ultimately the effectiveness of control functions. Control areas are easy targets for expense reduction efforts because they do not generate revenue. But the costs of control functions are relatively small compared with the much greater costs that historically have resulted from their absence. Before reducing staffing levels, coverage, or review cycles for control units, management should carefully assess the risks to the institution. If management and the board choose to make such reductions, they should be prepared to support them in their overall corporate strategic plan.

2.1.16. Credit Policy Administration

Credit policy administration is responsible for the day-to-day supervision of the loan policy. The unit decides whether the policy provides adequate guidance for lending activities, determines whether employees are following loan policy, reports policy violations, and administers policy and underwriting exceptions. If policy needs to be supplemented or modified, credit policy administration drafts the changes. This unit may also assist the account officers with routine account maintenance such as monitoring covenant compliance and ensuring that financial statements are received, spread, and analyzed in a timely manner. Credit policy administration is responsible for the body of written documents —loan policy, loan procedures, and policy-related credit memorandums —that govern the credit process. The unit should establish a formal process for developing, implementing and reviewing policy directives.

2.1.17. Loan Review

Loan review is a mainstay of internal control of the loan portfolio. Periodic objective reviews of credit risk levels and risk management processes are essential to effective portfolio management. Welsh (2010) underlines that the loss generated from loans that are written-off is one of the biggest costs of a financial institution. In view of this timely review of the performance of loans is as crucial as thorough appraisal of the original loan application.

To ensure the independence of loan review, the unit should report administratively and functionally to the board of directors or a standing committee with audit responsibilities. The board or committee approves the unit's operating budget, prepares the performance evaluation for the division's head, approves the unit's strategic and operating plans, acts on the unit's findings, and ratifies administrative matters.

Weaknesses in loan review hamper the entire portfolio management process and may signal the need for more extensive testing during an examination. Assessment of the loan review function should also include evaluation of its role in assuring the effectiveness of the loan portfolio management process. The loan review function should go beyond transactional testing to include evaluation of how well individual departments perform. Sound credit review standards provides that a bank should establish a system of independent, ongoing credit review and the results of the credit reviews should be communicated to management and the board of directors.

2.1.18. Audit

Audit activities in lending departments usually focus on the accounting controls in the administrative support functions. While loan review has primary responsibility for evaluating credit risk management controls, audit will generally be responsible for validating the lending-related models (e.g., loan pricing models, funds transfer pricing, financial analysis software, credit scoring). The logical structure and assumptions, as well as the data and mathematical algorithms used by the models, must be accurate. Audits should be done at least annually and whenever models are revised or replaced.

2.1.19. Administrative and Documentation Controls

The responsibilities of credit administration (CA) will vary widely from bank to bank. CA is the operations arm of the lending function. CA includes the backroom functions of loan disbursement, loan processing and billing, lien perfection, and credit and collateral documentation. CA is an important control mechanism. In fact, the backroom processing functions are often the first line of defense. Weaknesses in credit administration can pose significant safety and soundness issues for the bank. CA is normally reviewed periodically by audit, loan review, or both.

When money is lent against some security of assets, the document must be executed in order to give the bank a legal and binding charge against those assets. Documents contain the precise terms of granting loans and these serve as important evidences in the law courts if the circumstances so desire. That's why proper documentation must be completed prior to the disbursement of the facilities.

2.1.20. Concluding framework of the literature

Different literatures confirmed that sound credit management critically involves formally established legitimate policy and procedure that guides the whole crudities of the bank and that can outline authority and responsibilities of credit performers as well as customers.

Ensuring the adequacy of the policy in content and level of details one vital matter and following up whether the credit activity is as per the policy guideline is also another, Ankrah (2011). Loans and advances that are extended as per the stipulated policy guideline should be controlled properly using different tools that enable the approved credit remain productive and qualitatively satisfactory during the tenure of the credit Fatima (2010)**.**

2.2. EMPERICAL REVIEW

This part of the proposal paper takes a closer look on empirical studies on the subject matter mainly on sub share Africa region.

Rana-Al Musharafa (2013), on his study of "*Credit Assessment Practices of commercial banks in Bangladesh* " has investigate some of the Bangladesh commercial banks to evaluate credit assessment activities and to forward possible suggestions. Up on his study the researcher used both primary and secondary data sources and both qualitative and quantitative data analysis methods to evaluate the banks credit assessment using banks loan and advance growth, income from loan, sector credit allocation and credit risk management and nonperforming loan status of the bank as measuring parameters. The research has found that growth of loan and advances are sustainable, better sector allocation of loans, better risk management and income from loan and advances are increasing despite some banks need to improve their general loan policy.

Haron, Justo, Nabat and Mary from four different universities and public authority locations in Kenya- on their paper of *"Efficiency of credit management on loan performance: Empirical evidence*

from Micro Finance sector in Kenya" to asses credit management system on loan performance of micro finance institutes and to establish the effect of credit term, client appraisal, credit risk control and credit collection policies on loan performance of the institute. The researcher use primary data source and quantitative research design to test the relationships of theses selected variables.

These researchers has found that credit term formulated by MFI has an effect on loan performance, involvement of client on credit term formulation affects loan performance, interest rate charged has a reverse effect on loan performance, credit risk controls adopted by MFI has an effect on loan performance and collection policies of the institutes have high effect on loan repayment performances. Therefore the research concludes that all the above mentioned variables have relationship with loan performance and hence lenders should make their loan extension in considerations of these factors.

Omoijiode (Chief), 2014) Leeds Metropolitan university has made a comparative research under the topic "*Critical Assessment of Credit Management in Nigerian Bank Sector"*. This comparative study had made between Union and Zenith banks of Nigeria for the objective of establish level of Union bank and Zenith bank advance and provision against doubtful debts, to evaluation of Union bank net competitive advantage or disadvantage on credit management and to establish if United bank net competitive advantage or disadvantage against Zenith bank of Nigeria in their credit management. The researcher used secondary data collected from Nigerian Union and Zenith banks financial reports of 2005/200, united bank's loan and advance.

The researcher also employed qualitative analysis techniques and evaluate the two banks loan and advances (using balance score card map), financial perspective, loan and advance mix (O/D and loans against doubtful accounts provision), customer perspectives (customer service capability and geographic coverage), internal perspective(relationship management and credit monitoring), and learn and growth perspective(knowledge, innovation technology and reward system) to-compare loan and advance of the two banks, against their provision for bad debts, to evaluate responsible for increasing NPL for Union bank and to analyze competitive strength of the two banks using some success factors.

The research findings show that there is an inverse relationship between Union bank's loan portfolios against provision i.e. loan and advance of union bank is lower than Zenith bank's but the provision for union bank is higher (due to failure to monitor loan and advance efficiently). Success factor evaluation shows Zenith bank is much better than Union bank of Nigeria.

Afroz (2013) under his study of *"Credit Portfolio management Bangladesh Kirishi Bank"* the researcher tried to specify and estimate necessity credit portfolio management of Bangladesh Kirishi Bank and describe present credit management practice of the bank along with his suggestions. The study used primary and secondary data sources with descriptive data analysis techniques. The research has found that: the framework of the bank's function is not clear, agro business financing is risky for the bank, very few activities on L/C and other purchase type financing has been made, poverty alleviation credit program of the bank is successful but very little portion of the total portfolio (only 3%-4%).

Agu and Basil 2013, Federal university of Nigeria, on their study of ' Credit Management and Bad Debts in Nigerian Commercial banks, in order to determine major causes of bad debts in Nigerian banks using both primary and secondary data like interview, questionnaires other sources . The researchers also used both qualitative and quantitative data analysis using time series and regression data analysis tools to identify nature and causes of bad debts in Nigeria. Accordingly the researchers had found an overall inefficiency of the banks due to inadequate monitoring of borrowers on their borrowed fund utilization, an increase in lending rate, and failure in appropriate follow-ups, poor credit policy and weak credit administration practices.

Based on the research made by Joseph John Mangali (2014),Dongabei University of China, on the 'Effectiveness of loan portfolio management in Rural Saving and Credit Cooperatives in Tanzania, the researcher has used both primary data in the form of questionnaire on seventy microfinance officers in fourteen microfinance institutes, using multi regressive and descriptive data analysis tools to identify factors that affect Credit Portfolio qualities, the finding has revealed that quality of loan portfolio has strictly influenced by loan size, gender(Female has better repayment history than men), loan type, borrower's location, and insurance coverage and status of the loan.

Another research also has made by Hagos Mirach, at University of Mekelle, Ethiopia, (2010), which is a case study on "Credit Management Practice of the Wogagen Bank in Tigray Region" using both primary and secondary data and qualitative and quantitative data analysis tools, has found that the bank was managing its credit good in many aspects in this specific region. However the researcher has also indicate that very long loan processes, in adequate credit policy in terms of customers aspect discouraging credit customers, The researcher has also only short term credit facility resulted in repayment burden on the client within a short period that leads the customers to termination.

Empirical reviews that I made so far, which included in this research paper or not, show and emphasize on loan management practices of some African and Asian commercial banks and other microfinance institutes. To the extents of my reviews of related research materials, did not find any general or specific study that made on the assessment of credit management practice in commercial bank of Ethiopia. Therefore it is the researcher's belief that it is appropriate to carry on the research on the established topic.

CHAPTER THREE

3. METHODLOGY

Introduction

This chapter deals with the methodology of the study whereby the research design, sampling, data collection instruments, data collection procedures and the method of data analysis will be discussed.

3.1. Research Design

A research design is the frame work or blue print of conducting research. This research has used descriptive research based on survey method. It is a case study of specific bank and survey method enables the researcher to have a designed data. According to Trochin (1999), survey methods are used for non- experimental but descriptive research methods. Descriptive research is basically used to ascertain and describe the characteristics of variables of interest in some situation and subject of study. This research design enables the researcher to describe the phenomenon of interest from individual or organizational perspectives. In addition this study is fundamental to add knowledge about a subject by describing a shape or nature of a phenomenon by answering vital research questions like "what is going on" about a situation. Accordingly this study has found this research design appropriate to collects data from sources and then analyzes it in order to asses and describes the present condition of credit management in commercial bank of Ethiopia.

3.2. Study Area

This case study is emphasized on the Commercial Bank of Ethiopia (CBE) to assess its credit management practice. The study focuses on central credit processing unit of the bank's head office where almost all of the bank's credit processing, disbursing and management jobs have carried on.

3.3. Participants of the study

All credit performing employees of the bank at the central head office who have direct relationship with the bank's credit in all aspects were involved in the research. Based on the bank's credit employee set up all employees in credit team, that are: credit relationship managers, credit appraisal experts and analysts, credit portfolio management officers, credit relationship officers, workout loan and recovery officers, credit advisors and credit approving committee, as well as credit audit unit of the bank were involved.

3.4. Sampling Procedure

The total population for this study will be the total Credit Performing Unit (CPU) of the Commercial Bank of Ethiopia. The credit structural set up of the bank arranged in a way that the total credit of the bank is processed and managed in a central credit processing center of the bank's head office. Therefore a total population (all credit performing staff) has taken as an input for the designed

research. Hence, this enables the researcher not only to cover total area of credit management of the bank but also make the findings more concrete.

Table .3.1 Credit performers of the bank in each credit unit

S.N	Credit Performing Employees	Total Number
1	Credit Relationship Managers	30
2	Credit relationship Officers	40
3	Credit Analysts & Credit Appraisal Experts	36
4	Credit Advisors and Approving Committee	9
5	Credit Portfolio Management Officers	10
6	Work out loan (Loan Recovery Officers)	12
7	Internal Credit Audit team	8
Total Central Credit Performing Employees		*145*

3.5. Data Collection Instruments

Questionnaires is developed and adopt to undertake this study which contains statements that are specifically designed to measure credit management practice of the bank based on credit policy, credit policy application and credit control dimensions. In the process of conducting the research, primary data are used. The primary data is collected using structured questionnaires which intended to collect participant's opinion on the statements which stated to measure the overall existing credit management practice of the bank based on the designed parameters. Questionnaires are adopted from previous researches made in the area that asses credit management practices.

For instance "assessment of credit management practice in agricultural development bank of Ghana-2012, assessment of financial institutions loan portfolio management in Uganda-2003,

Credit management in Wogagen bank Tigray Region-2010 and other international credit management review standards like loan portfolio management and review examination module of the (FDIC) of the United States (Federal Deposit Insurance Corporation of USA , 2000)based on their appropriateness and relevance for the research objectives.

Questionnaires are re-designed and arranged based on the relationship for the specific evaluation parameter in the research question and in the way that enable respondents to answer questions accordingly. Hence, the first part (section) of the questionnaire designed to collect the participants' background information. The second part of the questionnaire also emphasized on evaluating adequacy and capability of the bank's policy to manage its credit practice. The third part related to

the level of compliance of credit activities against its guiding policy while the last part emphasized on the credit control practice of the bank.

3.6. Data Collection Procedure

Primary data is collected using self-administered questionnaires which are to be drop and pick method to and from credit performers of the bank at the central head office by the researcher. Questionnaire is used as an instrument to collect primary data from the respondents about their opinion at every question that designed to evaluate the credit management practice of the bank.

3.7. Validity and reliability

Validity and reliability of the research measurement instruments influence, first the extent that one can learn from the phenomena of the study. Second the probability that one will obtain statistical significance in data analysis and third the extent to which one can bring meaningful conclusion from the collected data.

Most ethical issues in research fall into one of the four categories: protection from harm, informal consent, right to privacy and honesty with professional colleagues (Leedy and Ormrod, 2005)

3.7.1. Validity

According to Leedy et al (2005), validity is the ability of an instrument used to measure what it is intended to measure or how truthful the research results are. These issues are addressed by the content validity, internal validity and external validity.

Content validity

It is the extent to which the measuring instrument provides adequate coverage of the investigative questions and the degree to which it measure. In order to check content validity for the descriptive survey studies, sources of evidence chain evidence and having key informants reviewing draft of the study report is vital Leedy et al (2005). In this case to ensure content validity the target groups included were those who know better about the issue being assessed. In addition the questionnaire has carefully designed and tested with a few members of participants for further improvement. Accordingly feedback has collected about clarity of a sentence, correctness of a language and grammar, as well as whether the designed instrument can fully assess the research topic prior to administering the survey.

Internal validity

The internal validity of a research study is the extent to which its design and the data it yields allow the researcher to draw accurate conclusions about the relationships within the data. In this case, it's less likely that there will be a Hawthorne effect (process where human subjects of an experiment change their behavior, simply because they are being studied) since the respondents have professional background , knowledge about bank lending and credit management, they are not expected to change their behavior. They were also asked to give their consent and they were given all the right not to answer any questions if they did not wish to.

External validity

External validity is related to the extent to which the findings from one research can be applied to other similar situations. In other words, how the conclusions drawn can be generalized to other contexts. An external validity depends on how well the sample used can be extrapolated to a population as a whole. It evaluates whether the sample population represents the entire population, and also whether the sampling method is acceptable. There would be no problems in this case since the researcher includes all the population in the study by using census method.

3.7.2. Reliability

According to Leedy and Ormrod (2005) reliability of a measurement instrument is the extent to which it yields consistent results when the characteristic being measured has not been changed.

Furthermore, Cameron et al., (2007) states that in order to increase reliability, the researcher should use the same template as far as possible and use static methods. To ensure the reliability of measurement instrument the researcher performed first standardize the instrument from one person or situation to another.

Besides, the researcher also believed that this study is reliable since the respondents were selected based on their past experience on credit management and their answers were expected to be credible. Given the credibility of selected respondents, the same answers would probably be given to another independent researcher. Keeping all these facts the researcher has made reliability analysis using Cronbach`s coefficient alpha for the entire set of statements and found to be 0.883, which is much higher than the threshold value of 0.65.The reliability result for the three categories of the research topics are also presented below which confirms the scale is considered to be reliable.

Table 3.2 Reliability results

Research topic	Number of Items	Cronbach's Alpha
Credit Policy Assessments of the bank	27	0.855
Credit Activities Compliance Assessment	17	0.747
Credit Controlling Activity Assessment	17	0.841

3.8.   Data Analysis

In order to evaluate the credit management practice of commercial bank of Ethiopia both qualitative and quantitative analyses are employed so as to address the gap in practice. Since survey is designed to solicit to what degree credit management has applied by the bank based on the selected dimensions, data collected from survey questionnaires are analyzed by using the Statistical Package for Social Science (SPSS) spreadsheet version 16.0. This software has been widely used by researchers as a data analysis technique (Zikmund, 2003).

Mean score and standard deviations are used from the measure of central tendencies to interpret the questionnaire. Mean is basically used in order to measure the average opinion that the respondents give on subject provided by the questioner and SD is also used to show how the value obtained by participants opinion dispersed (spread) from the mean. They are widely used measurements of population opinions on survey provided by Likert scale.

3.9. Ethical Consideration

Due consideration was given to obtain consent from each participant about their participation in the study in the first place, and it was strictly conducted on voluntary basis. The researcher tried to respect participants' right and privacy. The findings of the research were presented without any deviation from the outcome of the research. In addition, the researcher gave full acknowledgements to all the reference materials used in the study

CHAPTER FOUR

4. RESULTS AND DISCUSIONS

The previous chapters presented orientation of the study, theoretical foundations, literature review and the research methods adopted in the study. This chapter presents the results. As discussed in the preceding chapter this study aimed to explore and evaluate credit management practices of the commercial bank of Ethiopia based on three basic parameters. Accordingly this chapter tries to analyzed, summarized and present the results of the collected data from the credit employees of the bank.

Based on this the first part of this chapter describes the respondents profile as per their sex, age group, educational qualification and experience in the bank job and in the credit areas of the bank, while the second part presented results of respondents opinion on adequacy of credit policy of the bank, credit activity compliance against the existing credit policy and the credit control activity of the bank in the summary of tables along with their description

4.1. Survey results

The questionnaire was distributed to credit related professionals including customer relationship managers, credit analysts and appraisal experts, recovery officers, credit portfolio management officers, credit officers, credit approving committee and credit audit teams of the bank.

The questionnaire was physically distributed to 145 employees (whose positions are related to credit activities as indicated above). Out of 145 questionnaires 137 were completed and collected. As the result the response rate was 94.48 percent. In light of the poor response culture in Ethiopia this is impressive and much time has been devoted by the researcher to increase response rate as much as possible.

Table 4.1 Survey response rate

Sample size	145
Completed and returned questionnaires	137
Response rate	**94.48**

Source: Survey outcome and own computation

4.2. Respondents' profile

This section present profile of respondents in relation to their sex, ages group, educational level, service year and current positions as well as exposure in the credit area of the bank. As shown in table 5.1 male respondents constitute the largest share of the gender composition representing 83.21% of the respondents while 16.79% were female employees.

Table 4.2 Gender composition of respondents

Gender	Categories	Frequency
Male	114	83.21
Female	23	16.79
Total	**137**	**100**

Source: own survey result

Concerning age category of respondents major number of them are found in the age range of 30-49 which constitute around 82 percent of whom 50 percent (69) are found under age range of 30-39.

Table 4.3Age Category of respondents

Age Category	Frequency	Percentage
20-29 Years	12	8.76
30-39 Years	69	50.36
40-49 Years	43	31.39
50 and more	13	9.49
Total	**137**	**100**

Source: own survey result

As shown below in table 4.4 all the respondents have a qualification of first degree and a master's degree only and more than 89 percent of them intact are bachelors' degree holders. This indicates that respondents are academically qualified to quality of the survey.

Table 4.4 Academic background of respondents

Educational level	Frequency	Percentage
Diploma	0	0
Bachelors'	122	89.05
Masters	15	10.95
PhD	0	0
Total	**137**	**100**

Source: own survey result

As indicated in table 4.5 below more than 50 per cent of total respondents have a service of 11-20 years while less than 5 year and more than 21 years of service respondents account only about quarter of the total.This clearly depicts that respondents had rich experience in providing response that naturally contributed to the data quality of the survey.

Table 4.5Respondents experience in bank

Year of service in banks	Frequency	Percentage
1-5 years	17	12.41
6-10 years	24	17.52
11-15 years	42	30.66
16-20 years	33	24.09
21-25 years	17	12.41
Above 25	4	2.92
Total	**137**	**100**

Source: own survey result

Regarding respondents' service year in credit area of the bank, more than 60 percent of them has found under the range of 6 to 15 years, which contributes much to know deeply about the job. Five percent of them are very rich in credit experience while 18 percent are less than five year of stay in credit operations.

Table 4.6 Years of service in credit area

Year of service in credit	Frequency	Percentage
0-5 years	25	18.25
6-10 years	56	40.87
11-15 years	31	22.63
16-20 years	18	13.14
21-25 years	7	5.11
Above 25	0	0.00
Total	**137**	**100**

Source: own survey result

According to Table 4.7 below all the respondents of the survey are currently credit performers of the bank at different levels or at least to the credit related jobs of the bank. Out of them more than seventy per cent of the positions are maintained by credit relationship managers, credit relationship officers and credit appraisal expert staff. This helped capture a good quality of data.

Table 4.7 Current position of respondents

Credit Performing Employees	Frequency	Percentage
Credit Relationship Managers	29	21.17
Credit relationship Officers	38	27.74
Credit Analysts & Appraisal Experts	34	24.82
Credit Advisors and Approving Committee	8	5.84
Credit Portfolio Management Officers	10	7.30
Work out loan (Loan Recovery Officers)	11	8.03
Internal Credit Audit team	7	5.11
Total	**137**	**100**

Source: own survey result

4.3. Assessing the bank's credit management practice

The study tried to assess the credit management practice of the commercial bank of Ethiopia using three basic parameters namely, credit policy, compliance of actual credit activity with the existing established credit policy and the existing credit control practice of the bank.

4.3.1. Assessment of the loan policy

One major objective was to assess how appropriate and sufficient the existing credit policy of the Bank. Rating was made whether the bank's credit policy has included the listed credit policy component statements sufficiently. Accordingly opinion results are considered using a likert scale.

Based on S. Rick Fernandez., (2013) the scale 5 was used to represent "No at all", 4 represented "Little extent" 3 represented "Moderate extent", 2 represented "Great extent" and 1 represented "Very great extent". The score "very great extent" was taken to be equivalent to mean score ranging from 1 to 1.80," great extent" represented mean score ranging from 1.81 to 2.60, "Moderate extent" represented mean score ranging from 2.61 to 3.40, "Little extent" represented mean score of 3.41 to 4.20 and "Not at all" represented mean score of ranging from 4.21 to 5. In addition standard deviation of greater than one (>1) represent a significant difference (dispersion) in the response given.

Table 4.8Loan policy adequacy assessment

Evaluating Statements	Very great extent (1)	Great extent (2)	Moderate extent (3)	Little extent (4)	Not at all (5)	Mean	Standard deviation
Credit customer recruitment guideline	67	35	24	11	0	1.85	1.20
Eligibility criteria for loans	63	38	36	0	0	1.80	0.83

Credit document requirements	76	50	11	0	0	1.53	0.64
Loan appraisal standards	87	39	11	0	0	1.45	0.64
Loan approving authority	61	64	12	0	0	1.64	0.63
Loan approving limits of credit performers	45	79	13	0	0	1.77	0.61
Combinations of loan approving teams	59	53	25	0	0	1.75	0.75
Loan pricing standards of the bank	32	48	57	0	0	2.18	0.79
Credit monitoring and follow up processes	13	24	76	13	11	2.89	0.98
Aggregate geographical credit limit	0	12	58	43	24	3.58	1.06
Credit limit by economic sector	0	26	21	46	44	3.79	1.09
Credit limit by loan product types	14	79	19	12	13	2.50	1.10
Collateral requirement standards for loans	47	45	45	0	0	1.99	0.82
Insurance coverage requirements for loans	73	56	8	0	0	1.53	1.78
Maximum loan amortization period	53	61	23	0	0	1.78	0.71
Loan review procedures	24	35	24	11	0	2.25	0.84
Criteria for exceptionally approved loans	0	38	36	43	35	3.77	0.90
Limit for exceptionally approved loans	0	50	11	42	34	3.72	0.98
Credit risk grading standards	24	39	11	19	0	2.45	0.94
Risk tolerance limit of the bank	0	64	12	0	0	2.66	0.48
Credit risk management guideline	0	79	13	13	0	2.58	0.66

Action to be taken by credit performers	21	53	25	11	0	2.10	0.78
Credit reporting hierarchy of credit performers	16	48	57	0	0	2.49	0.70
Size of loan against total deposit	0	24	76	53	22	3.61	0.87
Size of loan against other balance sheet items	14	12	58	10	0	2.40	0.78
Skill required for each lending activities	26	26	21	12	0	2.38	0.89
Number of staff for each credit activities	0	79	19	46	24	3.47	0.96
Mean average						**2.44**	

Regarding the level of credit customer recruitment guideline, it is believed to be adequately included in the policy as per the respondents reveal scale of great extent, with the mean score value of 1.85 and standard dilation of 1.20.Responding for illegibility criteria for loans, respondents rate very great extent with a mean value of 1.80and standard deviation of 0.83. The result shows that points that make the customer (credit requester) illegible for the loan is very explicitly presented in the policy.

Credit document requirement rated the same way by respondents scaling it very great extent with a mean and standard deviation of 1.53 and 0.64 respectively, which shows that it's sufficiently presented in the policy document.

The same strong positive response was given for the statement that concerns loan appraisal standards set for credit appraisal experts of the bank has presented with a very sufficient manner evidenced by a mean of 1.45, and standard deviation of 0.64respectively.

On the other hand loan approving authority of credit approving teams of the bank has rated to present in a very great extent in the policy document as it responded with a mean score of 1.65 and minimum dispersion score of 0.63.

In the same way loan approving limit of credit approving teams of the bank has also has explicitly presented in the credit policy document with a mean and dispersion score of 1.77 and 0.61 respectively.

Regarding loan approving team composition respondents believed that it included in a very great extent in the policy document with a mean score value of 1.75 and SD of 0.75.Which implies that

credit approving team members are combined from different positions with in the same credit center that enables to make a quality decision on every credit request.

Respondents rating on loan pricing standards for every loan approved are greatly added to the policy document as evidenced by the mean score of 2.18, SD 0.79.

Credit monitoring and follow up process guideline is included in the credit policy of the bank in average detailed manner as showed by its mean value of 2.89 and standard deviation of 0.98.

In relation to aggregate geographical credit limit allowed along the nation has also rated with the mean and SD of 3.58 and 1.06 respectively. That reveals it is presented in the policy document with a little detailed manner.

Similarly the degree of credit limit set for every economic sector included in the policy with little extent as the previous statement as it evidenced by the mean score of 3.79 and dispersion of response is 1.09 which can be said it is somehow spread response.

Respondents believe that credit limit by the loan product type (for different loan titles that the bank served so far) is moderately included in the policy document by the response mean score of 2.5 and SD of 1.1 where regarding to collateral requirement for loans and advances approved to customers rated as explicitly included in the policy document as per the mean score of 1.99 and SD of 0.82.

Concerning insurance coverage requirement for every loan and loan amortization period, respondent's rate that they are included in the policy document with a very great and great extent as evidence by the mean of 1.53 and 1.78, and SD of 1.78 which is highly dispersed opinion for the first statement and 0.71 for the second statement.

In respect to loan review process guideline the bank has sufficiently included in its policy statement as evidenced by mean value and SD value of 2.25 and 0.84 respectively.

As per the responses on criteria set to exceptionally approved loan and exceptionally approved loan limit have rated with a similar nearest mean score of 3.77 and 3.72 and nearest SD value of 0.90 and 0.98 which indicate that these stamens are presented in the policy document of the bank with little manner not in an explicit way.

Credit risk grading standards process and credit risk tolerance limit of the bank are evaluated by the respondents as they are greatly and moderately added to the policy evidenced by their mean and SD score of 2.45 and 2.66 and SD of 0.94 and 0.48 respectively.

The response shows credit risk management guideline put in the policy in a strongly explicit way as a mean and standard deviation scores confirmed with a value of 2.58 and 0.66 respectively.

Respondents also believe that an action to be taken when the credit customer failed to pay his loan as per the agreement, has very sufficiently presented in the credit policy document with the mean and SD of 2.10 and 0.78.

Concerning the credit reporting hierarchy of credit performers respondents have believed that it is strongly added to the policy respectively with the mean value of 2.49 and SD of 0.78 where as in relation to the size of loan disbursed against a total deposit available in the bank, respondents believe that it presented in the policy inadequately as indicated by mean score of 3.61and SD value of 9.78. However size of total loan disbursed against other balance sheet items has added in a policy in great extent with a mean value of 2.40 and SD of 0.78

Skill required for the lending activity also is believed to be presented in the policy strongly by the response mean score of 2.38. Number of staff required to each credit activity section of the bank has presented in the policy in a little detailed way as evidenced by its mean value of 3.47 and SD of 0.91.

In general in the literature part of the paper credit policy is the means by which the management of the bank guides lending activities. It sets standards on every activities of lending like appropriate credit composition, individual credit performers discretion, economic sector and geographical credit concentration and other important fair lending principles. Accordingly based on the assessment result of how adequate them, CBE currently has a good credit policy with a good content and details as evidenced by the overall mean of 2.44 and this enables the bank to guide all its credit portfolio sufficiently.

4.3.2. Credit policy compliance assessment

Another objective was to assess whether the actual credit activity of the bank comply with the stipulated credit policy and procedure. In this respect respondents required to rate the extent of compliance of the credit activities of the bank to the existing policy document. The table below shows respondents' response rate.

Table 4.9 Credit policy compliance assessment

Evaluating Statements	Very great extent (1)	Great extent (2)	Neutral (3)	Little extent (4)	Not at all (5)	Mean	Standard deviation
Authority and responsibility of all credit performers	37	69	31	0	0	1.96	0.71
Eligibility require for loans and advances	24	82	31	0	0	2.05	0.63
Credit document requirements from loan applicants	38	63	36	0	0	1.99	0.74
Loan processing and appraisal activities	35	67	35	0	0	2.00	0.72
Credit risk assessment practices	19	43	61	14	0	2.51	0.81
Collateral requirement from	41	73	23	0	0		

borrowers						1.87	0.68
Credit decision making process	13	60	44	12	8	2.58	1.03
Loan pricing processes of the bank	25	22	69	13	8	2.69	1.12
Loan disbursement processes of the bank	27	44	66	0	0	2.28	0.78
Credit monitoring and follow up processes	0	29	32	68	8	3.40	0.89
Loan collection activities of the bank	12	74	40	11	0	2.36	0.73
Credit control process of the bank	2	14	42	70	9	3.51	0.97
Credit approval by exception of the credit guidelines	28	41	53	15	0	2.40	0.75
Credit amortization period for loans	38	53	46	0	0	2.06	0.78
Problem loan management processes	8	68	61	0	0	2.39	0.6
Risk tolerance limit of the bank	0	50	47	27	0	3.02	0.97
Credit staff requirement for the credit activities.	0	26	36	59	0	3.47	1.15
Mean average						**2.50**	

The response reveal that authority and responsibility of credit performers is applied in a great extent as per set by the credit policy with the response mean score of 1.96 and a deviation less than one (0.71) Regarding eligibility requirements for loans and advances also believed to apply strictly as per the policy in a great extent with the mean and SD value of 2.05 and 0.63. Similarly document requirements to process the requested loan is also believed to be carried on greatly as per the policy guideline as response mean value and SD of 1.99 and 0.74 respectively.

Concerning loan processing and appraisal activities, they are responded in the same scale category of applying in great extent evidenced with mean and SD of 2.0 and 0.72.Credit risk assessment practice is also believed to be applied in the same way with the previous statement in a great extent level as the mean indicates 2.51 and SD 0.81.

As per the respondents rating value, collateral requirement from borrowers a very greatly complied with a total mean score of 1.87 while credit decision making process comply with the policy with great extent as the mean value is 2.58.

Majority of respondents believe that loan pricing practices is moderately applied statement with mean 2.69 and SD 1.12 whereas loan disbursement process has complied in a great way as evidenced by mean and SD score of 2.28 and 0.78 respectively.

Response on compliance of on the credit monitoring and follow up process reveal it is moderately comply as set in the policy document of the bank with mean value of 3.4 and dispersion of 0.89.

In respect to loan collection activities of the bank is done as per the policy statement with the mean and SD value of 2.36 0.73 respectively on the other hand credit control activity of the bank applied in the little far away from the stipulated policy document as response reveal with a mean value and SD of 3.51and 0.97 respectively.

As per the response rate credit approval with exception to the policy, credit amortization period for the approved loan and problem loan management has rated similarly with greatly comply with the policy with the mean value of 2.4, 2.06 and 2.39 and SD of 0.75, 0.78 and 0.60 respectively.

Risk tolerance limit set by the bank also comply in average level with mean of 3.02 whereas credit staff requirement for the loan activity it is neither sufficiently presented in the policy in a detailed way nor comply with the policy even to its existence level as evidenced by its mean and SD of 3.47 and 1.15 respectively.

Inconsistency of credit practice of banks against the existing credit policy and procedural guidelines resulted in compliance problem. As the level of violation increases, the risk of failure of loans and advances also increase. As a result the expectation of future loan loss will increase and so do the credit provisions. In addition as credit decisions made in deviation from the existing credit guidelines, it poses the risk of building up non-performing loans by affecting credit portfolio compositions, sartorial and geographical credit allocations and other soundness principles.

Despite all these facts, the findings from the assessment of the level compliance of actual credit performing activities of the Commercial Bank of Ethiopia against the stipulated credit policy prove that going in a complied manner as evidenced by the overall mean average score of 2.50. However some individual assessment figures in the table tell us there are still inconsistencies of activities like credit follow up, credit monitoring, risk limit considerations and manpower requirements to the unit against the existing credit policy of the bank and this further implies that efforts should be made on these points in order to alleviate compliance problems and to increase the strength and soundness of the whole credit portfolios.

4.3.3. Assessment of existing credit control practice of the bank

Other objective of the research is to assess the existing credit control activities of the bank. Accordingly the respondents asked to express their level of agreement or disagreement as per the

established scale for the statements that provide to evaluate these activities. Table 5.10 below summarizes the respondents' response.

Table 4.10 existing credit control practice of the bank

Evaluating Statements	Strongly agree (1)	Agree (2)	Neutral (3)	Dis-agree (4)	Strongly disagree (5)	Mean	Standard deviation
Periodical loan review is performed	36	90	11	0	0	1.82	0.56
Adequate credit follow-up is done regularly	0	11	38	81	7	3.61	0.98
Sufficient credit audit is done periodically	0	24	72	28	13	3.22	0.95
Strong credit inspection is performed timely	22	78	37	0	0	2.11	0.91
The loan review practice address all or majority of loans	5	23	37	72	0	3.28	0.89
Adequate control is made on credit concentrations	27	79	15	12	3	2.14	0.85
The existing credit control enables to classify loans based on their weakness level	32	44	48	12	0	2.28	0.95
The existing credit control enable to maintain provision for possible loan loss	63	38	36	0	0	1.80	0.78
Credit control activity of the bank is sufficient to prevent all credit risk	4	20	43	54	16	3.42	0.95
The existing credit control activity enable to confirm if loan is utilized only for approved purpose	24	57	42	14	0	2.34	0.89
Credit control activity determines trend of customers business	0	79	23	22	13	2.77	1.04

Close review of borrowers' financial records to evaluate performance	21	47	66	3	0	2.37	0.75
Credit control of the bank enable early identification of problem loans	0	30	63	23	21	3.26	0.98
Credit control staff have adequate skill and expertise to carry on controlling activities	13	60	24	39	0	2.64	1
Credit control jobs are independently carried on	0	71	42	24	0	2.66	0.76
Credit control unit of the bank sufficiently staffed	11	38	56	19	13	2.89	1.06
Loan monitoring and controlling reports published regularly	30	33	50	24	0	2.50	1.02
Mean average						*2.65*	

As per the respondent's response on the question that requires if adequate periodical loan review is made, majority of them very strongly agreed with little variance as indicated by mean and SD of 1.82 and 0.56 respectively.

The respondent believed that there is an insufficient credit follows up practiced for the question that requires whether sufficient credit follow up is made regularly as they disagree with a mean 3.61and SD0.98

On the other hand respondents opinion if adequate credit audit is made periodically, majority of the respondents were in different with the mean 3.22 whereas the response on if strong credit inspection is made in timely bases many of them were agreed with a mean and SD of 2.11 and 0.91.

Majority of respondents also feel neutral for the statement that states if loan review practice addresses the majority of loans and advances delivered by the bank with the mean and standard deviation of 3.28, and 0.89 respectively.

Respondents strongly agree on the statement that requests if adequate control is made on credit concentration of the bank, more than fifty percent of them total agree with a mean and SD of 2.14 and 0.85 respectively. In addition the statement that requests whether the existing credit control of the bank enable to classify the loans based on their weakness levels they agreed as per the mean score of 2.28 degree of dispersion from the mean is 0.95.

Regarding the question if credit control activities of the bank enable to prevent all credit risks, most of the respondents disagree with a mean of 3.42 while they are strongly agree for the statement which states that the existing credit control enable to maintain provision early for possible future loan loss with mean and SD of 1.80 and 0.78 respectively.

Responses has agreed for the statement that states the existing credit control practice enable to confirm the utilization of approved loan for approval purpose as evidenced by the mean of 2.34 and SD of 0.89 whereas opinion whether the existing credit control practice enable to determine the trend of customers business, majority of them feel neutral with mean of 2.77 and SD of 1.04.

In respect to the request if close review of borrowers' financial records is made to evaluate the business performance of the customer, respondents are in different with a mean 2.37 and SD 0.75. Similarly the result on the statement that states existing credit control activities enable to early identify problem loans majority of respondents neutral with mean and SD of 3.26 and 0.98.

Regarding the skill of the staff in processing credit control respondents were indifferent with the mean and SD of 2.64 and 1.00 respectively. Similarly for the question that requests if credit control is independently carried on also responded neutral with the nearest mean to the previous one (2.66).

Respondents rate whether credit control job is staffed sufficiently and loan monitoring and controlling activity reports published regularly, they have a neutral feeling as per their opinion mean score of 2.89 and 2.50 and with nearest SD of 1.06 and 1.02 respectively.

Based on the research made on major reasons that increase NPL in the Commercial Bank of Zimbabwe in 1993, Credit Control problems take the first place. Credit control problem include weak credit analysis, lack of strong supervision, poor portfolio composition, poor credit risk management,

Weak follow up to identify early signals of credit failure are some reasons other than external uncontrollable macro-economic problems like natural disaster. Lack of appropriate credit control resulted in malfunction of loans and possible failure. As unhealthy loans increase provision to cover possible loan loss also increase which in turn affects the profitable performance of the bank.

Where anticipations of credit losses increase, provision is held from the net income of the bank to cover them up. This affects strength of the bank for future business expansion. In addition as loss arises from credit control problems, the financial source of the bank is used to cover up the defect and this also leads to insufficient supply of finance in the form of loans and advances either to the deficit sector of the economy or the general economy as a whole other than deteriorating of the bank's capital.

Accordingly the existing credit control activities of the Commercial Bank of Ethiopia is very average level as evidenced by the overall average mean of 2.65. This can be one main indicator for an increase in credit provision and non-performing loans of the bank. If the trend continued in such a way, it will affect not only the profitability of the bank but also the lending capacity of the bank for priority sectors of the economy as well as the financial need of the general economy.

CHAPTER FIVE

5. SUMMARY OF CONCLUSION AND RECOMMENDATIONS

The previous chapter presented the result of the analyzed data. In this section of the paper the findings based on each response will be presented in informative and summarized manner. The study analyzed each point that is believed to be weight and measure the overall credit management activities of the bank.

5.1. Findings on credit policy adequacy assessment

First assessment was made to evaluate the adequacy and the level of sufficiency of the credit policy of the bank to outline and guide credit processes undertaking in the bank. Accordingly the numbers of adequacy measuring statements were presented so that respondents can evaluate using five scales about how adequately and the state of detail these points are included in the credit policy document of the bank.

Consequently respondents gave their positive responses for majority of statements in agreeing that these statements are sufficiently included in the credit policy of the bank as evidenced by average mean of 2.44for the entire table.

Statements that respondents believed to be presented in policy statement to the very great and great extent includes: credit customer recruitment guideline, eligibility criteria for loans, credit document requirements, loan appraisal standards, loan approving team establishment, credit insurance and collateral requirements, loan approving authority, credit approving limit of performers, loan amortization period, loan pricing standards, loan review procedure and credit risk management guidelines.

As per the respondents scale of evaluation statements that describe credit monitoring and follow up process and risk tolerance limit of the bank were evaluated as moderately presented in the policy document in an average extent of details. On the other hand some statements were agreed by the respondents to be presented and described in the policy document in a little extent and in insufficient manner despite their importance if included in the policy.

These include: aggregate geographical credit limit, criteria and limit for exceptionally approved loans, credit limit by economic sector, size of loan against total deposit and the number of staff needed for each credit activities.

5.2.   Findings on credit policy compliance assessment

As the table shows that the level of alignment and compliance of the formulated credit policy of the bank against the actual credit activities performed in the ground accordingly. In this respect the respondents' feedback majority of statements included in the policy are believed to be performed strictly in a great extent as per the policy guideline revealed by the average mean value of 2.50.

Statements believed to be included in the policy to a very great and great extent includes: authority of credit performers, eligibility requirements for loan, document requirements, loan appraisal activities, collateral requirement, credit decision making processes, loan collection, credit amortization period, problem loan management, credit risk assessment practices, loan disbursement processes and credit approved in exception of the credit guidelines.

Respondent feel neutral and confirmed that on the level of inclusion of credit monitoring and follow up processes, and risk tolerance limit of the bank and loan pricing activities of the bank in the bank's credit policy document.

Whereas the existing credit control activities of the bank and credit staff requirements are complied with the stipulated policy in a little or poor manner. This indicates that the mentioned activities are performed in deviation from the policy guideline.

Concerning the credit staff requirement of each credit processing unit, it is noticed in both adequacy evaluation and compliance evaluation that it is neither presented sufficiently in the policy document nor at least applied to the extent and state of its presentation in the policy document. This farther indicates that if insufficient and inappropriate number of staff assigned to the credit job, with no doubt negatively affects the process and activities of lending at each step and resulted in overall credit management problem.

5.3.   Findings on assessment of existing credit control activities

Based on the responses majority of participants were indifferent between agreement and disagreement about the existing credit controlling activities of the bank as shown by the average mean value of 2.65.

Respondents were strongly agreed and agreed on statements including strong credit inspection performed timely, adequate control is made on credit concentration, loan utilization control, follow up of the credit customer's business trend, the existing credit control is activities enable to maintain provision for possible loan loss of the bank, the existing credit control practice enable to classify loans in their weakness level and the existing credit control is activities enable to maintain provision for possible loan loss of the bank.

Respondents feel neutral on statements that stated skill of credit control staff, independency of credit control jobs, sufficient credit audit is made timely, the existing credit review addresses all majority of

loans, close reviews of borrower's financial record to evaluate their performance, the credit control practice of the bank enable to early identify problem loans and credit control unit of the bank is adequately staffed. This reveals that the credit control activities of the bank are carried on neither in a strong level nor in a poor manner, rather in the middle of them.

Finally respondents were completely disagree on statements which states adequate follow up is done regularly, loans and credit control activity of the bank is sufficient to prevent all credit risks that the bank faced. This suggests that though credit controlling is one of the major activities in credit management practices, the bank failed to practice that to extent of its importance.

5.4. Conclusion

The broad objective of the research was to assess the credit management practice of Commercial Bank of Ethiopia. Based on these broad objectives basic research questions were developed and survey was made on the bank's credit performing employees.

The research assesses the credit management of the bank using three basic parametrical dimensions namely credit policy contents, credit policy application and credit control practices. As per the premises and the forgoing findings the following conclusions are drawn.

Based on assessment on the adequacy and the sufficient manner of the bank credit policy document, it can be concluded that the existing credit policy of the bank is adequate and sufficiently addresses majority of the credit policy statements that should be included and presented in detail. In fact there are very few issues that the policy did not include in a sufficient manner like economic sector credit limit, size of loan against total deposit of the bank, criteria and limit s of exceptionally approved loan as well as staff requirements of each lending activities.

Concerning the compliance level of the credit activities against the credit policy guidelines, similar conclusion is drawn as the previous one. More than the average level from the total credit activities performed in the bank was done in accordance with the formulated credit policy guideline of the bank. However credit monitoring and controlling jobs were applied in deviation from the stipulated policy.

On the other hand existing credit control activity dimensions of the bank can be confidently concluded as performing in an average level as confirmed by value of mean average whereas no adequate follow up is done regularly and the existing credit control practice is not to control risks raised from credit activities. This provides support to sum up that credit control is not strongly exercised in full scale rather in a half way between them.

5.5.   Recommendations

Based on the findings of the study, the following recommendations are forwarded for the Commercial Bank of Ethiopia in order to contribute for the overall sound credit management of the bank.

The bank should put in place and present in its credit policy document that appropriate credit limit for each economic sector to prevent possible risks raise from credit concentrations. It is obvious that concentration risk created as the bank place loans and advances in a single economic sector, region or group of individual. Therefore, explicit criteria and limit should be set for loans approved in an exception (deviation) of the existing loan policy and the policy should also be revised by considering the existing economic realities.

The bank should also set in its policy document the size of loan in alignment with its total deposit amount presented in its liability accounts. The bank should strictly apply its credit monitoring and follow up processes as it is set in the policy document in order to make timely identification of weakness in availed loans, to detect emerging risk and to give possible supervision and corrective actions.

Credit control function should also be strictly comply with the stipulated policy guidelines so as to improve credit risk management process and insure sound lending practices

The bank should perform periodic loan review which addresses all or at least majority of loans that are currently outstanding this activity is the main internal control which enable the bank to know the credit risk level of the total loan and to increase the effectiveness of loan portfolio management.

Credit staff should be assigned in required number and skill for each credit unit of the bank. This enables the bank to timely process the loan until the disbursement phase, which in the way helps to satisfy customers and to make adequate follow up process afterwards. This further helps to carry on sound and healthy credit management practice in general.

5.6.   Recommendations for further studies

5.6.1.   Credit Management Practices of the Ethiopian Banking Industry

The focus of this study was the credit management practice of the Commercial Bank of Ethiopia; therefore it is recommended that a similar study be conducted on the overall banking industry in the country.

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St. Mary's University

School of Graduate Studies

Letter of Introduction

Dear Sir/Madam,

RE: QUESTIONNAIRE

My name is Chane Amare, a student at the St. Mary's University undertaking a Master of Business Administration. Currently I am doing a postgraduate research project on **"Assessing Credit Management Practices of Commercial Bank of Ethiopia"** as a partial fulfillment of the requirements of degree of masters. I would appreciate your favorable consideration in completing the enclosed questionnaire and assisting me in the research endeavor. All pieces of information provided in this questionnaire are strictly confidential and will only be used for the purpose of this research.

Thank you in advance for your time

HOW TO COMPLETE THE QUESTIONNAIRE

Please answer the questions by either (**√**)the appropriate box or whichever the mark that best describes your situation that corresponds to the most appropriate response/answer in each point. You may also write if any additional points in the spaces provided at the end of every section.

In case you have any questions please call 0911 444927 or email chaneamare@gmail.com

Thank you again for your contribution towards this important research

Section A: **Social Demographic Profile of Respondents**

1. A. **What is your sex?**

Male ☐ Female ☐

2. A. In which age group do you belong?

☐

20 – 29   30 – 39 ☐   40 – 49 ☐ above 50 ☐

3. A. Your level of education

Diploma ☐ Bachelors' ☐ asters' Ot☐ ☐

4. A. Which year of service are you in the bank?

1 – 5 years ☐   11 – 15 years ☐   21 – 25 years ☐

6 – 10 years ☐ 20 years   above 25 ☐ ☐

5. A. Indicate your experience in bank credit processes

Less than one year ☐ 6 -10 years ☐

1-5 years ☐   11-15 years   above 15 years

6. A. Your current position in the Banking industry

Credit Director ☐ ustomer Relationship Officer ☐ her Relationship manager ☐

Credit analyst ☐ edit Recovery Officer   Cred ving committee ☐

Credit Portfolio Management Officer ☐ edit Appraisal Expert   Cred t ☐

Section B: **Adequacy Examination of Credit Policy of the Bank**

To what extent the following credit processes components included in the bank's credit policy documents?

Statements		Very great extent	Great extent	Moderate extent	Little extent	Not at all
7.B	Credit customer recruitment guideline					
8.B	Eligibility criteria for loans					
9.B	Credit document requirements					
10.B	Loan appraisal standards					
11.B	Loan approving authority					
12.B	Loan approving limits of credit performers					
13.B	Combinations of loan approving teams					
14.B	Loan pricing standards					
15.B	Credit monitoring and follow up processes					
16.B	Aggregate geographical credit limit					
17.B	Credit limit by economic sector					
18.B	Credit limit by loan product types					
19.B	Collateral requirement standards for loans					
20.B	Insurance coverage requirements for loans					
21.B	Maximum loan amortization period					
22.B	Loan review procedures					
23.B	Criteria for exceptionally approved loans					
24.B	Limit for exceptionally approved loans					
25.B	Credit risk grading standards					
26.B	Risk tolerance limit of the bank					
27.B	Credit risk management guideline					
28.B	Action to be taken by credit performers at each stage when borrowers unable to perform as per the contract					
29.B	Credit reporting hierarchy of credit performers					

30.B	Size of loan against total deposit					
31.B	Size of loan against other balance sheet items					
32.B	Skill required for each lending activities					
33.B	Number of staff for each credit activities					

Do you think the existing credit policy and procedure of the bank is **adequate** to guide credit activities of the bank?

Yes, ☐   No, ☐

If your answer is no, please specify the gap--

Section C: **Examination for Compliance of Actual Credit Activity of the Bank against the Existing Policy and Procedure**

Do you think the actual credit activities of the bank strictly comply with (performed as per) the stipulated credit policy and procedure of the bank?

Statements		Very great extent	Great extent	Moderate extent	Little extent	Not at all
34.C	Authority and responsibility of all credit performers					
35.C	Eligibility require for loans and advances					
36.C	Credit document requirements from loan applicants					
37.C	Loan processing and appraisal activities					
38.C	Credit risk assessment practices					
39.C	Collateral requirement from borrowers					
40.C	Credit decision making process					

41.C	Loan pricing processes of the bank					
42.C	Loan disbursement processes of the bank					
43.C	Credit monitoring and follow up processes					
44.C	Loan collection activities					
45.C	Credit control process of the bank					
46.C	Credit approval by exception of the credit guidelines					
47.C	Credit amortization period for loans					
48.C	Problem loan management processes					
49.C	Risk tolerance limit of the bank					
50.C	Credit staff requirement of for loan activity					

Is there any **compliance** problem of the actual credit activities of the bank against its existing credit policy and procedure other than included in the above list?

Yes, ☐   No, ☐

If yes, please specify---

Section D: **Examination of the Existing Credit Control Practice the Bank**

Please indicate your degree of agreement or disagreementto the statements pertaining to the existing credit control practice of the bank?

Statements		Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
51.D	Periodical loan review is performed					
52.D	Adequate credit follow-up is done regularly					
53.D	Sufficient credit audit is done periodically					
54.D	Strong credit inspection is performed timely					
55.D	The loan review practice address all or majority of loans					
56.D	Adequate control is made on credit concentrations					

57.D	The existing credit control enables to classify loans based on their weakness level					
58.D	The existing credit control enable to maintain provision for possible loan loss					
59.D	Credit control activity of the bank is sufficient to prevent credit risk					
60.D	The existing credit control activity enable to confirm if loan is utilized only for approved purpose					
61.D	Credit control activity determines trend of customers business					
62.D	Close review of borrowers' financial records to evaluate performance					
63.D	Credit control activity of the bank enable early identification of problem loans					
64.D	Credit control staff have adequate skill and expertise to carry on controlling activities					
65.D	Credit control jobs are independently carried on					
66.D	Credit control unit of the bank sufficiently staffed					
67.D	Loan monitoring and controlling reports published regularly					

Do you think the current/existing credit control practice of the bank is **sufficient** to insure credit remains qualitatively satisfactory during all the tenure of the loan?

Yes, ☐   No, ☐