ST.MARY'S UNIVERSITY

SCHOOL OF GRADUATE STUDIES

MASTER OF BUSINESS ADMINISTRATION

EFFECT OF CREDIT RISK MANAGEMENT ON QUALITY OF LOAN PORTFOLIO: THE CASE OF COMMERCIAL BANK OF ETHIOPIA BOLE DISTRICT

BY

MERON LULSEGED

ID:-SGS/0047/2015A

JUNE 2024

ADDIS ABABA, ETHIOPIA

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ST.MARY'S UNIVERSITY
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THE EFFET OF CREDIT RISK MANAGEMENT ON THE QUALITY OF LOAN PORTFOLIO

(THE CASE OF COMMERCIAL BANK OF ETHIOPIA BOLE DISTRICT)

By: Meron Lulseged

APPROVED BY BOARD OF EXAMINERS

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DECLARATION

I Meron Lulseged hereby declare that this thesis work is my original work towards the achievement of MBA in Business Administration at St. Mary's University, Department of Business Administration and has not been presented for a Degree in any other university, and all sources of material used for this thesis have been duly acknowledged.

Name: Meron Lulseged

Signature: _____________________

Date: ________________________

LETTER OF CERTIFICATION

This is to certify that the thesis entitled "EFFECT OF CREDIT RISK MANAGEMENT ON THE QUALITY OF LOAN PORTFOLIO THE CASE OF COMMERCIAL BANK OF ETHIOPIA BOLE DISTRICT submitted in partial fulfillment of the requirements for the Degree of **MBA** in **Business Administration,** the Graduate Program of the **School of Postgraduate Studies,** and has been carried out by Mrs. Meron Lulseged ID No_ SGS/0047/2015A under my supervision. Therefore I recommend that the student has fulfilled the requirements and hence hereby can submit the thesis to the department for defense.

Kiros Habtu (Asst. Prof.)

Signature ____________________

Date ________________________

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ACRONYMS

ACRE	Appropriate Credit risk environment
ANOVA	Analysis of Variance
APA	American Psychological Association
CIR	Cost Income Ratio
CBE	Commercial Bank of Ethiopia
CFI	Commercial Financial Institutions
LF/TA	Liquid Funds to Total Assets
LPM	Loan portfolio management
LLP/GLA)	Loan Loss Provision to Gross Loan Advances
KYC	Know Your Customers
LPP	Loan Portfolio Profitability
NBE	National Bank of Ethiopia
NPL	Non Performing Loan
RIMMP	Risk Identification, Measurement and Monitoring Process
RMSS	Risk Management System and Standard
SCGP	Operating under a sound Credit granting process
SPSS	Statistical Package for Social Sciences

ABSTRACT

The main objective of the thesis is to assess the effect of credit risk management on the quality of loans portfolio in the case of Commercial Bank of Ethiopia Bole District*. A sample of 82 respondents was drawn from the employees of the* Commercial Bank of Ethiopia Bole District *by using purposive sampling technique. Both primary and secondary data were used. Data related to loan portfolio and loan position is obtained from the* bank *whereas, primary data are collected using structured questioners from the employees of the* bank*. Descriptive and inferential statistics were used to conduct the research and Multiple Regression Analysis was run using SPSS Version 21.0 to analyze the data. With regard to credit risk management practices, the result show that* Commercial Bank of Ethiopia Bole District *has not satisfactory risk Management practice. Precisely, using score 1 (poor) to 5 (best), all the parameters of risk management practice assessment have a score value below 3.40, i.e. Credit Risk Granting and Portfolio Quality Control (3.40), Credit Risk System and Standard (3.20), Credit Risk and Portfolio Quality Control (3.17), Risk Identification, Measurement and Control (3.03), and Risk Environment (2.98). The* Bank`s *loan portfolio is also more vulnerable to various types of risks, such as to unpredictable risk, predictable, and controllable risks. The* bank's *NPL ratio was above 15% for the last five years. The regression result also showed that sound credit granting process and the existence of comprehensive risk management system and standards are the significant variables that affect loan portfolio quality of the* bank*. Credit risk management practice of the* bank *has insignificant effect on loan portfolio quality. Both in terms of Non-performing loan and concentration,* Commercial Bank of Ethiopia Bole District *has poor loan portfolio quality which is due to the* bank's *poor credit risk management practice. Therefore, there is a need to improve and enhance credit risk management practice of the* bank*, especially, by improving the credit granting process to have sound credit risk management, and by updating credit risk management system and standards so as to have strong credit management.*

Keywords: Credit Risk Management Practice; Loan Portfolio Quality; Credit Risk Management System and Standards

CHAPTER ONE

1. INTRODUCTION

This part of the paper presents an introduction to the study, which includes: Background of the study, description of the study, statement of the problem, the research questions that govern the study, the intended objectives, significance of the study, and scope of the study and organization of the research

1.1.Background of the study

Risk management is the continuing process to identify, analyze, evaluate and treat loss exposures and monitor risk control and financial resources to mitigate the adverse effects of loss. This is the core concept to financial sector because it has substantial effect not only on the behavior of financial institution, but also economy of a country as well as entire world. For that reason, the risk management issue is paid more and more attention in the every level of any organization over the world. In addition, as financial industry becoming more competitive as well as complex, bankers and financial managers have been shifted away from consideration on profit or spread towards to risk pricing. In other words it is not only insufficient to earn high return rate on an investment; but also earn return that compensates the banks properly for the risk assumed. Thus, the quantifying risk and finding optimal mix between taking risks, maximizing returns by creating own capital provisions are crucial for financial world (Togtokh, 2012).

Similarly, credit risk can be defined as- the possibility of losses associated with reduction in the credit quality of borrowers or counter parties. In a bank's credit portfolio, losses stem from outright default due to inability or unwillingness of a customer or counterparty to meet their commitments in relation to lending. Literature show that losses result from reduction in portfolio value is arising from actual or perceived deterioration in credit quality.

The idea of risk management is an exceptionally vital idea to numerous organizations as most financial choices spin around the corporate expense of holding risk on account of the critical risk it conveys regarding the survival of organizations. This issue is especially essential to banks since risk is a characteristic piece of their center business operations and activities. By it's extremely makeup, keeping money is an endeavor to deal with various and apparently restricting needs. Banks give liquidity on interest to investors through the present record and amplify acknowledge and in addition liquidity to their borrowers through lines of credit (Brown & Moles, 2014).

In developing countries, banks have emerged and evolved over time to play a similar role, namely providing long-term capital to support growth and economic transformation. That is, such banks are key in those countries embarking on accelerated economic growth and thus facing challenges in terms of financing for capital-intensive projects and maintaining institutions that can anticipate new needs, overcome technical and entrepreneurial limitations and help coordinate multiple investments taking place simultaneously.

When we came to Ethiopia case, the credit risk as the risk of loan repayment default by borrowers. Credit risk arises from poor lending discipline, quite often-inadequate attention to credit analysis, poor follow up and management of loans and too much reliance on collateral. As a result, asset prices decline and credit risk emerges. Loan default is a common feature of credit risk. It is the likelihood that a debtor to the bank will not meet obligation in accordance with agreed terms. Good loans are the most profitable assets for banks and are the base for their existence. Conversely, bad loans pose threats to the financial and institutional sustainability of banks. Credit risk is, therefore, understood as the critical problem in the financial industry that needs to receive management's priority attention and proper administration.

Like any financial institutions, credit risk is a major problem to the Commercial bank of Ethiopia. Looking at the portfolio, the size of non-performing loans has continued to rise from time to time and this has contributed to the deterioration of the portfolio quality in the bank.

To cope with the current looming threats, it is imperative to manage credit risk at bank level and ensure sustainability, which is critical to financial institutions. Credit risk management essentially means the process that assesses the qualitative and quantitative factors that support credit worthiness; mainly it focuses on evaluation of borrowers' creditworthiness, loan security and periodic valuation (IBID).

This research focus on credit risk identification, credit risk measurement, credit risk monitoring, and credit risk control. Thus, the research tries to lend empirical support issues on the effect of credit risk management on the quality of loan portfolio in CBE Bole District, Addis Ababa.

1.2.Statement of the Problem

Credit risk management involves the identification, assessment evaluation, control and management of a company's exposures to loss. It attempts to mitigate the occurrence of losses while initiating advance planning to assure that adequate funds will be available to cover those losses that occur (Yong, 2003). Credit risk is one of the most vital risks for banks. Credit risk arises from nonperformance by a borrower or may arise from either an inability or unwillingness to perform in the pre-commitment contracted manner. The credit risk adversely affects the bank's profitability, solvency, book value of a bank, and in severe case it cause crises. Poor credit risk management also affects the quality of its assets and increase loan losses and non-performing loan which may eventually lead to financial distress.

CBE has long history in financing Projects. However, this bank exhibit poor risk Management practice as compared to its long period practices in the industry. Despite employing credit risk management strategies responsible for managing risks related to lending, the bank is still experiencing a sharp rise in the level of NPL's. Lawer (2012) states that despite innovations in the financial services sector over the years, credit risk is still the major single cause of bank failures, for the reason that for "more than 80 percent of a bank's balance sheet generally relates to this aspect of risk management. Effective credit risk Management practice has a vital role in maintaining good Quality of Loans Portfolio. One of the concerns is quality of bank lending. Most significant challenge before banks is the maintenance of rigorous credit standards and system, especially in an environment of increased competition for new and existing clients.

Commercial Bank of Ethiopia, commonly known in providing short, medium, and long-term credits. Factors causing for poor quality of Loans Portfolio are deficiency in appraisal of loans proposals and in assessment of credit worthiness, inadequately defined lending policies and procedures, absence of credit concentration limits for various industries/business segments, liberal loans sanctioning powers for bank executives without checks and balances, lack of proper coordination between various departments of banks looking into credit functions, lack of well-defined organizational structure and clarity with regard to responsibilities, authorities and communication channels, lack of credit proper systems of credit risk rating quantifying and managing across geographical and product lines, lack of effectiveness of existing credit inspection and audit systems banks and slow progress in removal of deficiencies as revealed in inspection/audit of branches and controlling offices and absence of credit risk Management models. CFI's thus develop strategies to either eliminate or reduce this credit risk. In the management of this risk, banks are concerned about their Loans Portfolio Quality. However, despite the efforts made to address the poor credit risk management, financial institutions still have difficulties resulting from the credit risk management processes undertaken and changes in customer base leading to decreasing financial performance. To most banks, their credit risk management goal is to arrange the bank's financial affairs in such a way that however much borrowers fail to pay back the loan in the future, the effect on their return is diminished.

1.3.Objective of the study

The general objective of this study is to assess the effect of credit risk management on the quality of loans portfolio of a Commercial Bank of Ethiopia Bole District. Specifically, the study addressed the following objectives.

- Assesses the credit risk management practice of bank
- Assess the quality of loan portfolio of the bank
- To investigate the effect of credit risk management practice on loan portfolio quality of CBE.
- To assess the contributing factors for NPL in Commercial Bank of Ethiopia Bole District.
- To assess the level of NPL of the Banks in recent years.

1.4. Research questions

The study addressed the following research questions in the case of Commercial Bank of Ethiopia Bole District.

- What is the credit risk management practice of Commercial Bank of Ethiopia Bole District?
- To what extent Commercial Bank of Ethiopia Bole District perform loan portfolio quality?
- What is the relationship between credit risk management Practice and Loan quality Portfolio of Commercial Bank of Ethiopia Bole District?
- What are contributing factors for high NPL ratio in Commercial Bank of Ethiopia Bole District?
- To what extent Commercial Bank of Ethiopia Bole District experience NPL from loans provided for development projects?

1.5. Significance of the study

The principal findings of this research are expected to contribute a lot for different stakeholders and the country at large. The following are significance of this study:

Therefore, the outcome of the study is expected to generate pertinent insights for different stakeholders regarding the effects of Credit Risk Management on the quality of loans' portfolio. Furthermore, it is the belief of the writer that the study benefits the policy makers for their effort in policy formulation and implementation and recommending possible solution for the concerning body.

This study thus will help Commercial Bank of Ethiopia Bole District to get insight on what it takes to improve its loan qualities and the central bank (NBE) to examine its policy in bank supervision pertaining to ensuring asset quality banks maintain.

Finally the study contribute to the existing body of knowledge regarding the effects of credit risk management on quality of loans portfolio and motivate further research on Commercial Bank of Ethiopia Bole District and other Financial Institutions and more specifically on macroeconomic effects of credit risk management on the quality of loans portfolio which will not be studied under this research.

1.6. Scope of the Study

Since the term risk is a broad area of study, the paper was focus merely on the effect of credit risk management on the quality of loans portfolio in Commercial Bank of Ethiopia Bole District by ignoring other area of banks risks such as operational, interest rate, liquidity risks and the like. Even though, credit risk management is a concern of all Coops operating in the country, the paper is limited to cover Commercial Bank of Ethiopia Bole District credit risk management practice. On top of this, due to time and cost constraints, the study was focus only on respondents residing at Bole District of Commercial Bank of Ethiopia. The bole district of Commercial Bank of Ethiopia is selected due to the fact that huge amount of credit is given at this district.

Therefore, data analysis and interpretation and findings have been framed based on the Commercial Bank of Ethiopia Bole District current scenario.

1.7. Organization of the Paper

The research follows the logical steps of establishing the research questions, developing the methodology, gathering and analyzing data and drawing conclusions. Thus the study will be presented in 5 chapters.

Accordingly, the first chapter will present the background of the study, statement of the problem, research questions, objective of the study, significance of the study, scope of the study and methodology which on account to the introduction part.

The second chapter deeply deals with review of related literature on Credit Risk Management. It examines literatures and studies relevant to the study.

The third chapter incorporates brief description of methodology that is the population and sampling technique of the study; the sources of data; the data collection tools/instruments employed; the procedures of data collection; and the methods of data analysis. The fourth chapter will summarizes the results of the study and interpret the findings.

The fifth chapter is devoted to the summary of results, concluding remarks, recommendations and future research directions. More over the lists of bibliography and appendixes will be attached to the research work.

CHAPTER TWO

2. REVIEW OF RELATED LITRATURES

2.1.Introduction

This chapter presents what other scholars have written about the credit risk management and quality of loan portfolio of banks, it specifically looks at theoretical framework and empirical evidences. Finally, this section has present summary of the chapter.

2.2.Theoretical Literature Review

2.2.1. Definition of credit risk

There are various definitions of credit risk in literatures. Most common definition described by Basel Committee on Bank Supervision is credit risk is credit risk is the potential that a bank borrower or counterparty will fail to meet its obligations in accordance with agreed terms (BIS, 2000). Alternatively, credit risk is defined as the risk that unexpected change in a counter-party's creditworthiness may generate a corresponding unexpected change in the market value of the associated credit exposure (Andrea Resti & Andrea Sironi, 2016).

Credit risk is the most obvious risk of a bank by the nature of its activity. In terms of potential losses, it is typically the largest type of risk. The default of a small number of customers may result in a very large loss for the bank (Tony & Bart, 2008).

Credit risk is most simply defined as the potential that a bank borrower or counterparty will fail to meet its obligations in accordance with agreed terms. The goal of credit risk management is to maximize a bank's risk-adjusted rate of return by maintaining credit risk exposure within acceptable parameters. Banks need to manage the credit risk inherent in the entire portfolio as well as the risk in individual credits or transactions. Banks should also consider the relationships between credit risk and other risks. The effective management of credit risk is a critical component of a comprehensive approach to risk management and essential to the long-term success of any banking organization (Supervison, 2000).

2.2.1.1.Determinates Portfolio quality

Loan portfolio is the totality of all loans issued by a bank or other financial institution to its customer. The portfolio can consist of both safe and risky loans. Loan portfolio is the major asset of financial institution and predominate source of revenue. The determinants of quality of loan portfolio are stated below:

2.2.1.1.1. Credit Risk Identification

Risk identification is one of the vital actions financial sectors take to effectively manage risk. For effective credit risk management, financial sectors have to identify what risks they face. It is therefore important not to miss out any risk during risk identification. There exist a number of techniques that financial sectors can employ to identify the risk. The first step in establishing the operation of the risk administration function is to determine the crucial segments inside and outside the corporation. Units and the employees are given the responsibilities to identify the specific risk that might need attention (Kromcshdor F.& Luck C., 1998). (Al-Tamimi H., 2007) Established that commercial banks in United Arab Emirates were exposed to credit risk as the major risk further, the study established that the major methods used to identify credit risk posed by borrowers is inspection by credit managers and financial statements analysis.

The major practices used in risk management are institutionalizing credit standards, credit worthiness evaluation, credit scoring, assignment of risk rating and collateral. Credit risk identification has positive significance on credit risk management practices.

2.2.1.2. Risk Analysis and Assessment

Various conceptual studies have been made on risk analysis and assessment with focus to quantification and mitigation of risk. Organizations should classify the different risks the exposed to the ultimate potential of loss (Fuser,K.,Gleiner, W. and Meier, G., 1999).

The classification allows the management to clearly segregate the adverse risk that might affect banks going concern from those that can have slight impact. Normally, there exist an inverse relationship between the probable loss and its equivalent likelihood.

In a study conducted by, it was established that commercial banks in United Arab Emirates are more effective in examining and evaluating risk and there is a significant difference between UAE commercial bank and overseas banks that conduct lending risk analysis and evaluation.

Further, the study established that assessment and analysis of lending risk have bearing on credit risk management practices. (Drzik, 1995)Study established that big banks in the United States had made a considerable progress in development and institutionalizing of risk controls. The measures adopted by the United States have improved pricing and performance measurement as well as credit controls.

2.2.1.3. Credit risk Monitoring and control

Credit risk managers have responsibility of ensuring that there is a proper quantification, monitoring and control of risk arising from credit. Credit risk managers therefore have responsibilities of ensuring there is a proper unearthing of likely events or forthcoming fluctuations that could negatively compromise quality of loans portfolio and the banks potential to counter changes should they occur. Proper risk management requires banks to have in place an adequate structure for evaluation and reporting to ensure that credit risks are adequately identified and assessed and that controls are operational to mitigate the risk. The process of credit monitoring entails performing regular contact with borrowers, creation of an atmosphere and trust to borrowers so as banks can be considered as solution providers, creation of an organizational culture that provides support to borrowers during difficulties and assist the borrowers in any way possible to tackle the challenges, keen monitoring of the state of borrower’s business through their bank accounts, periodic re-examination of the borrower's reports as well as conducting borrower’s call backs and visits, keeping up to date credit files for borrowers and frequent reviewing of borrowers previous credit rating . Credit risk monitoring is vital tools that assist commercial banks to discover lapses and potential defaulters and at early stage and also to test if risk management practices are sound so as to reduce bank exposure to non-performing loans (Al-Tamimi H. , 2002).

Credit risk monitoring refers to incessant monitoring of individual credits inclusive of Off-Balance sheet exposures to obligors as well as overall credit portfolio of the bank. Banks need to enunciate a system that enables them to monitor quality of the credit portfolio on day-to-day basis and take remedial measures as and when any deterioration occurs. Such a system would enable a bank to ascertain whether loans are being serviced as per facility terms, the adequacy of provisions, the overall risk profile is within limits established by management and compliance of regulatory limits. Establishing an efficient and effective credit monitoring system would help senior management to monitor the overall quality of the total credit portfolio and its trends.

Consequently the management could fine tune or reassess its credit strategy /policy accordingly before encountering any major setback. The banks credit policy should explicitly provide procedural guideline relating to credit risk monitoring. At the minimum it should lay down procedure relating to the roles and responsibilities of individual's responsible for credit risk monitoring; the assessment procedures and analysis techniques (for individual loans & overall portfolio); the frequency of monitoring; the periodic examination of collaterals and loan covenants; the frequency of site visits; and he identification of any deterioration in any loan (SBP, 2012).

2.2.2. Loan Portfolio Theory

According to (Kurui, S. K. & Kalio, A, 2014) Loan portfolio theory relates to the sum total of money loaned out through various lending products to different borrowers. Loan portfolio encompasses salary loans, group bonded loans, individual loans and company loans (Murugu, 2010). Loan portfolio refers to number of bank customers with loans and the total amount loaned out (Crabb P. and Keller T., 2006). According to (Kurui, S. K. & Kalio, A, 2014), continued existence of most financial institutions depends entirely on successful lending program that revolves on funds and loan repayments made to them by the clients. This means a restrictive credit control policy should be adopted to act as a deterrent to unnecessary lending and in the process improve on profitability of the financial institutions (Kipchumba, 2015). Loan portfolio constitutes loans that have been made or bought and are being held for repayment. Loan portfolios are the major asset of Financial Institution. The value of the loan portfolio depends not only on the interest rates earned on loans but also on the likelihood that interest and principal will be paid (Jansson, 2002). 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 financial institution's safety and soundness. Whether due to lax credit standards, poor portfolio risk management, or weakness in the economy, loan portfolio problems have historically been the major cause of losses and failures. Effective management of the loan portfolio and the credit function is fundamental to financial institution'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 review of the LPM process is so important, it is a primary supervisory activity (Reilly F. K & Brown, K.C).

2.2.3. Credit Risk Theory

Management practices have been defined as the identification, measurement, monitoring and control of risk arising from the possibility of non-payment of loans advanced to various clients (Kithinji, A. M, 2010). Loans extended to bank's clients might have risks associated with non-repayment in circumstances the bank assumes that the loaners will faithfully pay back amounts borrowed; some borrowers usually don't repay resulting to decreases performance due to non-performing loans provisioning (Wang, 2013). Every Financial institutions experience a certain amount of uncertainty in instances where it loans funds to individual and corporate customers.

In such scenarios, the financial institution may end up with lending losses should some of the borrowers fail to clear loans as per agreements (Karugu and Ntoiti, 2015). Primarily, credit-risk of a banking institution is the chances that a loss resulting from default of interests and the principal, or the two of them, or in ability of the bank to sell the securities held against the loan (Kithinji, A. M, 2010).

Banks are required to use the Know Your Customer principle as a strategy aimed at minimizing and/or eliminating credit risk (Basel Committee on Banking,Supervision, 2006). Biased decisions made by banks management might result to insider leading or to individuals associated with the banker or individuals with poor financial background or to fulfill personal motives, which may include tying to be friend persons with higher status in the society. One of the solutions suggested is the use of well-known lending methods and especially quantitative ones as they filter out biasness (Abdifatah, 2010).

2.2.4. Credit Risk Management

According to (Tefera, 2011), the concept of credit risk management can be treated as the heart of any financial institutions. It plays the vital role in the performance of a financial institution as it analyzes credit worth ability of borrowers. (Kithinji, 2010), defined credit risk management has been defined as implementation of policies to limit insider lending and large exposures to related parties this is in addition to controlling risks stemming out of chances that a client may not repay the loan. Inadequate credit risk management practices and absence of care to variations in economy can be named as causes for poor financial performance by banking institutions (Tefera, 2011). The objective of credit risk management in banks is to achieve maximum risk-adjusted rate of return by retaining credit risk exposure within satisfactory limits (Wang, 2013). Indicatively credit risk management may be spell out methodical appliance of management strategies, processes and practices to the tasks of pinpointing, evaluating, gauging, treating and monitoring risk. Earnings due to banks will be exposed to risks of variations in returns and hence fluctuate if the financial institutions are not aware of the percentage of loans that will become delinquent. Loans extended to bank's clients might have risks associated with non-repayment in circumstances the bank assumes that the loaners will faithfully pay back amounts borrowed. A few of the clients ordinarily don't make the repayments resulting to decreased profits due to the need for provisioning and writing of the loans (Karugu and Ntoiti, 2015). Essentially, the credit risk of a bank is the likelihood of cost arising from non-repayment of interest and the initial loaned amount, or both, or failure to sell of securities pledged on the loan (Kithinji, A. M, 2010).

2.2.5. Portfolio Management

Effective management of the loan portfolio 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 review of the LPM process is so important, it is a primary supervisory activity. Assessing LPM involves evaluating the steps bank management takes to identify and control risk throughout the credit process. The assessment focuses on what management does to identify issues before they become problems. This booklet, written for the benefit of both examiners and bankers, discusses the elements of an effective LPM process. It emphasizes that the identification and management of risk among groups of loans may be at least as important as the risk inherent in individual loans (Chodechai, 2004) . For decades, good loan portfolio managers have concentrated most of their effort on prudently approving loans and carefully monitoring loan performance. Although these activities continue to be mainstays of loan portfolio management, analysis of past credit problems, such as those associated with oil and gas lending, agricultural lending, and commercial real estate lending in the 1980s, has made it clear that portfolio managers should do more. Traditional practices rely too much on trailing indicators of credit quality such as delinquency, non-accrual, and risk rating trends. Banks have found that these indicators do not provide sufficient lead time for corrective action when there is a systemic increase in risk (Sanchez, 2009). Now, many banks view the loan portfolio in its segments and as a whole and consider the relationships among portfolio segments as well as among loans. These practices provide management with a more complete picture of the bank's credit risk profile and with more tools to analyze and control the risk (Gonzalez-Paramo, J. M. , 2010).

2.2.6. Loan Portfolio Quality

Loan portfolio relates to the sum total of monies loaned out through various lending products to different borrowers (Kurui, S. K. & Kalio, A, 2014). Loan portfolio encompasses salary loans, group bonded loans, individual loans and company loans (Murugu, 2010). Loan portfolio refers to number of bank customers with loans and the total amount loaned out (Crabb P. and Keller T., 2006). According to (Kurui, S. K. & Kalio, A, 2014)continued existence of most financial institutions depends entirely on successful lending program that revolves on funds and loan repayments made to them by the clients. This means a restrictive credit control policy should be adopted to act as a deterrent to unnecessary lending and in the process improve on profitability of the financial institutions (Kipchumba, 2015). Credit management is the managerial responsibility through which customer's credit ratings are determined as part of the credit control function. Non-performing loans are used as a measure of the quality of loan portfolio. The portfolio is said to be of good quality if there are minimal or no non-performing assets (Onuko, L. K, 2015). According to (Onuko, L. K, 2015), should a loan remain unpaid for a period of time exceeding ninety days, then it is classified as non-performing loans and has limited chances of being serviced either partially or fully. Onuko (2015) suggests that unhealthy loan portfolio rather poor operating efficiency is the clearest sign of failed banks. A fall in loan portfolio quality impends on banks liquidity and hence its daily processes. Onuko (2015) posit that a healthy loan portfolio is very critical to the performance of the individual bank and also entire country's financial sector. The study concluded that poor loan portfolio tend to reflect on the total net worth of a bank.

2.2.7. Relationship between Credit Risk Management and Loan Portfolio

Loans being the major and most apparent source of credit risk to most banks means that credit management techniques needs to be applied (Abdifatah, 2010). Credit risk has been defined as the potential that a bank debtor and other counterparties will not meet their responsibilities occasioning to depressed earnings. Exposure to financial risk, in addition to direct financial loss should also be taken into consideration when it comes to credit risk. As it does not always happen in isolation, credit risk also exposes banks to other risks for instance liquidity risk with both affecting loan portfolio quality. The aim of credit risk management is to maximize banks risk adjusted rate of return by retaining credit risk exposure within acceptable levels (Hempel, G. H. & Simonson, D. G. , 1999). It is imperative for banks to ensure credit risk attached to loan portfolio is well managed in addition to that of individual client's credit transaction .The financial institutions must also put in mind the connection revolving among interest rates, credit and liquidity risk well-organized credit risk management is vital to the entire risk management structure and is vital to each financial institution profitability and eventually its own survival and growth in the long run (Karugu and Ntoiti, 2015). Comprehensive review risks involved lending decisions is of great significance and goes a long way in mitigating losses that would be occasioned should the loan book turn out to be bad. On the flip side, banks loan portfolio is directly related to the amounts of credits granted and hence strict credit management need to be put in place to lower the credit risk and hence prevent financial loss. Banks must consider and stabilize the two options in order to improve on profitability (Wang, 2013).

2.3.Empirical Literature Review

Several studies have been undertaken to understand the risk arising from credit operations as well as other underlying risks facing financial institutions.

A study by (Mohammad, 2008) did a study on risk management in Bangladesh Banking Sector. His main objective was to investigate the contribution of credit risk on non-performing loans. He found that, the core of the problem lies in the accumulation of high percentage of non-performing loans over a long period of time. As per him unless NPL ratio of the country can be lowered substantially they will lose competitive edge in the wave of globalization of the banking service that is taking place throughout the world. Since they have had a two-decade long experience in dealing with the NPLs problem and much is known about the causes and remedies of the problem, he concluded that it is very important for the lenders, borrowers and policy makers to learn from the past experience and act accordingly.

(Zewude, 2011), Conducted a study on credit risk administration and the profitability of commercial banks in Ethiopia. The motivation behind the investigation was to quantify the effect of credit chance administration on profitability of seven noteworthy business banks in Ethiopia. The researcher utilized relapse demonstrates, to examine the information which was gathered from the National Bank of Ethiopia and from seven business banks of the nation. The ROE was taken as the dependent variable while the free factors were the NPL proportion and the Auto. The examination uncovered that both nonperforming credit proportion and capital ampleness proportion negatively affects performance of banks in Ethiopia.

As studied by (Mehretu, 2015)on an assessment of credit appraisal and credit risk management practices on Commercial Bank of Ethiopia, was provide the following empirical evidences.

The main objective of the study was to evaluate the overall performance of CBE after the 1994 reform, to show whether the performance of BE is improving or deteriorating in various aspects. The study was a case study and it uses both qualitative and quantitative data from secondary sources, it also uses CBE’s financial statement as a primary source.

The study concludes in general as the performance of CBE has increased in all aspects except the fact that banks provision for doubtful loan increased which indicates deterioration in loan receivables.

A study was done on Brazilian National Development Bank (BNDES‟) by (Sergio G. Lazzarini,Aldo Musacchio,Rodrigo Bandeira-de-Mello and Rosilene Marcon , 2011) with the title "What do development banks do? Evidence from Brazil 2002-2009". It examines the selection/Appraisal process through which BNDES capital is allocated to firms. This study is a descriptive study and it started by setting a hypothesis of "Industrial policy and political view on the role of development banks" For this study data were collected from 286 publicly listed companies, between2002-2009, and secondary data were used from Brazilian National Development Bank (BNDES) on loans and equity allocation in the stated period. The findings of the study reveals that BNDES‟ apparently selects firms with good operational performance based on their capacity to repay their loan but, it also provided more capital to firms with political connection.

As shown below in figure there are four independent variables that compose credit risk management practices. The Dependent variable is the quality of Loans Portfolio as measured by Non-Performing Loans (NPL) to total loans. The four independent variables directly affect the quality of the Bank Loans Portfolio.

Independent Variable   Dependent Variable

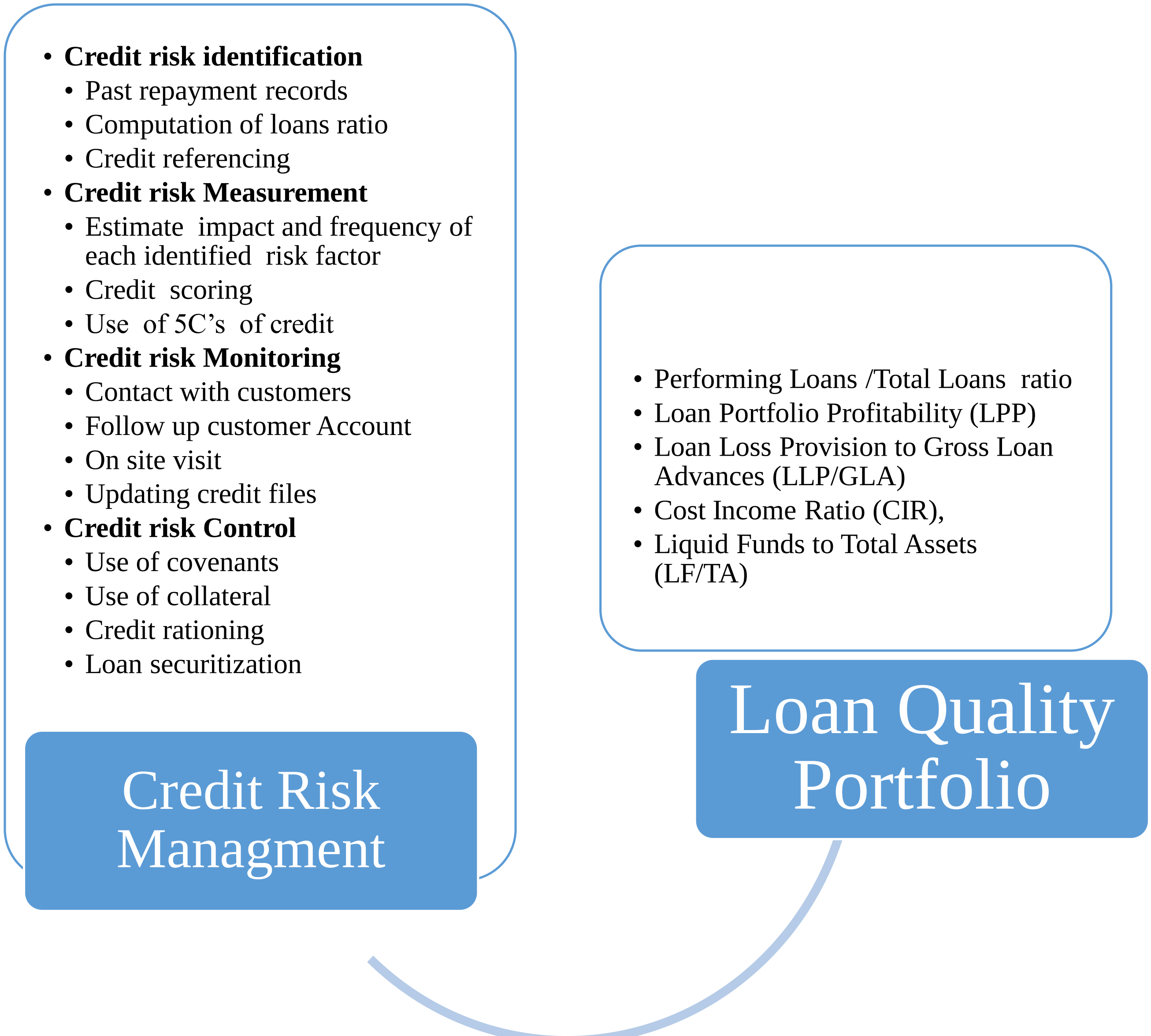

Figure 1: Conceptual Framework

CHAPTER THREE

3. METHODOLOGY OF THE STUDY

3.1.Introduction

This chapter presents the research design and methodology. Specifically it presents research design and approach, data source and collection tools, sample and sampling techniques, sample size selection, data analysis techniques, model specification and ethical considerations.

3.2. Research Design and Approach

Research designs are plans and the procedures for research that span the decisions from broad assumptions to detailed methods of data collection and analysis. It involves the intersection of philosophical assumptions, strategies of inquiry, and specific methods (Creswell, 2009).

There are three type of research approach; quantitative, qualitative, and mixed research. Quantitative research as defined by Creswell (2009) is a means of testing objective theories by examining the relationship among variables. These variables in turn can be measured, typically on instruments, so that the numbered date can be analyzed using statistical data. Qualitative research examines why and how of decision-making using words or figures. This type of research is more descriptive in nature. Mixed research has the characteristics of both quantitative and qualitative research.

The research was undertaken to evaluate the relationship between credit risk management practice and the quality of loans Portfolio of Commercial Bank of Ethiopia at Bole District. Both descriptive and inferential methods of analysis were employed to investigate the relationships. The researcher used this mixed approach to investigate the cause and effect relationships between the dependent and the independent variables. Thus, it would help understand and explain the pattern of relationship between the variables.

3.3.Data Sources and collection Tools

Primary and secondary data sources were used for the thesis. The primary data was collected through structured questionnaire from sample selected respondents in the bank, who had expertise knowledge about credit risk management. The questioner was designed in such a way that it would have three main parts. Part 1 contains information regarding the respondent's demographic features which include gender, age, educational qualification, work experience and job position. Part 2 of the questionnaire consists of structured five point Likert scale questions related to Credit Risk Management Practices. And also Part 3 Credit risk Management and portfolio loan quality (relationship) which deal with level of effectiveness of risk identification, risk analysis and assessment, risk monitoring and risk mitigation. Each statements were measured by assigning scores of 1 to 5 likert scale of strongly disagrees to strongly agrees. Regarding the sample respondents, Directors, Managers and officers who had a direct and indirect relationship with risk management activities of the bank were considered.

The secondary sources of data were annual reports of the bank, Credit Policy documents, Strategic Planning document and loan portfolio data of the bank were used.

3.4.Validity and Reliability of Research Instruments

It is the degree to which the data captured by the research instruments represents accurately the theoretical concepts and measurements required for the variables.

Internal reliability of the instrument was checked by using Cronbach's alpha. The standard value of reliability is 0.7 and results indicate the value of 0.905 which is well above of the standard value 0.7 and thus is reliable.

Cronbach's Alpha

Cronbach's Alpha	N of Items
.905	82

3.5. Sampling and Sampling Techniques

A study population generally refers to the totality of items under investigation. The target population for this study was all employees of the bank who have direct and indirect link with credit risk management practice of the bank. There were five working units: Credit Risk and Compliance Management Directorate, Customer relationship Management Directorate, Loan Portfolio and Data Management, Project Appraisal Directorate and Project Rehabilitation & Loan Recovery Directorate at district level which is the scope of the study for the thesis. 52 52

According to data obtained from the bank`s Human Resource Management there are Two Hundred Sixty four (264) employee in these five working units: Director (1), managers (29), officers (234).

The researcher used purposive sampling technique which is categorized under the non-probability sampling techniques where the researcher confined to specific types of people who provided the required information. The purposive sampling technique was chosen because of the fact that the employees do have heterogeneous knowledge about the risk management practice. Directors have better knowledge than managers and managers have better knowledge than officers. As a result, as compared to respective number of employees in each category, respondents of more proportion were taken from directors, managers and officers respectively.

3.6. Sample Size Determination and Selection

A sample design is a definite plan for obtaining a sample from a given population. It refers to the technique or the procedure the researcher would adopt in selecting items for the sample. Sample design may as well lay down the number of items to be included in the sample i.e., the size of the sample. Sample design was determined before data are collected (Kothari, 2004, pp.55-56).

Assuming that, Director will have more information on the issue 100% of them were taken, then 40% of the managers were taken as respondents and 30 percent of the respondents were taken purposively. The logic is that employees at higher position have relatively better knowledge about the credit risk management and should be given more chance to capture more information. The other thing is that, employees at lower position are large in number and they have almost homogenous knowledge about the issue under investigation and it is possible to get adequate information from small proportion as of the survey considering the cost, time and sufficiency of information trade off.

Table 3-1 Sample size Determination

Category	**Population size**	**Sample Size**
Directors	1	1
Managers	29	13
Credit Officers	234	56
Total	**264**	**70**

3.7. Data Analysis Techniques

Data analysis is the process in the form of summarizing (condensation) of meanings; categorization (grouping) of meanings; Structuring (ordering) of meanings using narrative are groups in analysis process. (Saunders et al., 2009)

After collecting the raw data of questionnaire, the data was entered into computer spreadsheet, SPSS program. Therefore, IBM Statistical Package for Social Sciences (SPSS) computer program version 21.0 was used to summarize and categorize the respondents view.

More specifically, after all the data is coded and entered, the result was analyzed using descriptive method. Descriptive statistics helped the researcher to summarize and present the data in statistical arrangement. In view of that, statistical techniques such as frequencies, charts and percentages were used to analyze the profile of respondents, Credit risk management practices of Commercial Bank of Ethiopia Bole District, Credit risk management practice and loan portfolio relationship and interpret the results accordingly.

The research was used descriptive and inferential statistics. Frequency count, percentage, and standard deviation were employed to analyze the responses of the respondents on the variables that influence the quality of loans portfolio. On the other hand, inferential statistical tools such as t-test and correlation were used to critically scrutinize the relationship of different variables with Loans Portfolio and the differences in views of the respondents.

3.7.1. Model Specification

The effect of credit risk management practice on the loan portfolio quality of the bank was analyzed through a regression model; loan portfolio quality (LPQ) as dependent variable and credit risk management practices as independent variables. Credit risk management practices incorporates variable according to the Basel principle these are:Establishing an Appropriate Credit risk environment (ACRE), Operating under a sound Credit granting process(SCGP), Maintaining an Appropriate risk identification, measurement, Measurement and monitoring process(RIMMP), Having developed risk management system and standards(RMSS).

$$\text{Loan Portfolio Quality} = \text{f(Credit Risk Management Practices)}$$

$$\text{LPQ} = \text{f(ACRE, SCGP, RIMMP, RMSS)}$$

$$\text{LPQ}_i = \beta_0 + \beta_1 ACRE_i + \beta_2 SCGP_i + \beta_3 RIMM_i + \beta_4 RMSS_i + \varepsilon_\text{i}$$

LPQ is the outcome variable (dependent variable), $\beta_{i`s}$are the coefficient of predictors (ACRE, SCGP,RIMMP, RMSS) and e_i is the error terms.

3.8. Ethical Considerations

The researcher ensures the quality and integrity of this thesis work. The respondents pursued consent for participation with full awareness of what it is. The confidentiality and anonymity of the voluntary respondents were guaranteed. This independent and impartial thesis work considered not to cause harm to respondents in what so ever way. Accordingly, the researcher optimal considers all the ethical perspectives.

The researcher used proper citation to avoid plagiarism work of different authors and researchers used in the research paper was acknowledged using APA style of citation ; and analysis of data techniques so that the research was not raising any ethical anxiety.

CHAPTER FOUR

4. DATA ANALYSIS AND RESULT DISCUSSION

This Section of the thesis deals with data presentation, analysis and interpretation. These data are presented and analyzed based on data collected through structured questionnaires, and secondary data obtained from Commercial Bank of Ethiopia Bole District related to loan portfolio and risk management practices. The primary data were obtained from the employees of the bank in one Directorate which are supposed to have direct relationship with the credit process and credit risk management practices. The questionnaires were distributed to 82 employees but 70 of them are responded.

4.1 The General Background of the Respondents

In this section, the demographic information of respondents is presented. These include the sex, age category, work experience, and educational qualification and job position of respondents. There were a total of 70 respondents, of these, 62 (88.7%) were male and 8 (11.3%) were female (See Table 4-1 below).

Table 4-1: Sex Respondents

Sex	Frequency	Percent	Cumulative Percent
Male	62	88.7	88.7
Female	8	11.3	100.0
Total	70	100.0	

In terms of age category, majority of the respondents 51(73.2%) respondents are between 25 and 35 years of age, 14(19.7%) respondents are in the category of 36 and 45 years of age while the remaining 5(7%) respondents are 46 and above years of age.

Table 4-2: Age Category of Respondents

Age Category	Frequency	Percent	Cumulative Percent
25-35	51	73.2	73.2
36-45	14	19.7	93.0
≥46	5	7.0	100.0
Total	*70*	*100.0*	

Majority of the respondents have masters education level (See Table 4-3). From 70 respondents 40 of them have level masters of education, 29 of them have bachelor degree and 1 respondent has third degree. The implication is that CBE has staffs in terms of level of education if possibly inferred to the whole.

Table 4-3: Respondents` Level of Education

Education	Frequency	Percent	Cumulative Percent
BA/BSC	29	40.8	40.8
Masters	40	57.7	98.6
PhD	1	1.4	100.0
Total	70	100.0	

Table 4-4 also describes the years of experience at work for the respondents. About 35 percent of the respondents (24 of 70) have 6-10 years of experience followed by 21 respondents with years of experience from1 up to 5 years. A quarter of the respondents (18 of 70) have also 10 to 15 years of experience and 7 respondents have also above 15 years of experience at work.

Table 4-4: Respondents` years of Experience

Experience	Frequency	Percent	Cumulative Percent
1-5 years	21	29.6	29.6
6-10 years	24	35.2	64.8

10-15 years	18	25.4	90.1
Above 15 years	7	9.9	100.0
Total	70	100.0	

The data collected in terms of the position of the respondents were from four categories: senior credit officers, credit officers, managers and those at director and above director position level. Senior credit officers are about 56 percent of the respondents (39 of 70), Credit officers are about 22 percent of the total respondents, managers are about 15 percent of the respondents and about 6 percent of the respondents have director position level (See Table 4-5).

Table 4-5: Respondents` level of Position

Position	Frequency	Percent	Cumulative Percent
Credit Officer	16	22.5	22.5
Senior Credit officer	39	56.3	78.9
Manager	14	15.5	94.4
Director	1	5.6	100.0
Total	70	100.0	

4.2 Credit Risk Management Practice of CBE

Credit risk management practice in a given bank can be evaluated from the perspectives of the presence of well-established and appropriate collection amount to be in line with the amount of actual loan outstanding that the Bank has. This is a signal that the working units have given less weight for collection efforts as compared to the disbursement process. The loan recovery rate both the plan and the actual has been declining while the planed and actual NPLs has shown increments. The study has undergone a study to assess the loan quality portfolio of the Bank both through secondary data and primary data analysis. The loan portfolio quality in one or another way is related to its exposure for different type of risks.

Table 4-16 showed that the loan portfolio of Commercial Bank of Ethiopia Bole District is relatively more exposed to unpredictable and uncontrollable risks. More than 25 percent of the respondents have stated that such risks are frequently encountered in CBE. Data on these five parameters were collected from 70 respondents using 5 Likert scale structured questionnaire, each parameter has a set of indicator variables ranging from 8 to 20 items. The frequency analysis on the assessment of the level of risk management practice in CBE has been presented from Table 4.6 to table 4. 10. The level of agreement of respondent on the set of statements that best describes each parameter has been presented in these tables. Finally, a score analysis has been presented to make a comparison on their relative importance on the risk assessment situation of CBE.

Table 4-6: Presence appropriate credit risk environment

Sr.No	Statement	No. Of Respondents with Positive Agreement	Percentage (Positive Agreement)	No. Of Respondents with Negative Agreement	Percentage (Negative Agreement)
1	The bank's staffs take the necessary precaution against default risk and effectively work to the implementation of credit risk management policies, strategies and procedures	33	46.48	21	29.58
2	Credit Risk management strategy, Policies and Procedures are consistently applied in all Credit product and activities of the bank.	28	39.44	23	32.39
3	Authority and Responsibility of Risk Management are clearly set out and understood throughout the bank.	28	39.44	23	32.39
4	There is proper identification of Credit Risk inherent in all products and activities of our bank.	28	39.44	27	38.03
5	Bank's Credit risk strategies and policies are regularly reviewed/ updated	25	35.21	26	36.62
6	Bank's Credit provision and risk identification procedures are regularly reviewed/updated	24	33.80	26	36.62

7	Boards of Directors and Senior Managers closely monitor the major Credit Risk exposure of the bank and implementation of credit risk policies, strategies and procedures	21	29.58	22	30.99
8	There is common understanding about Credit Risk Management Strategy, Policy and Procedures across the bank.	21	29.58	38	53.52
9	Senior managements are fully dedicated to improve the bank's credit risk management practices	18	25.35	34	47.89
	Average		***35.37***		***37.56***

Table 4-6: shows that establishment of appropriate credit risk environment in CBE. The table shows that out of 70 respondents, 35.37% of the respondents indicated that CBE has well establishment and appropriate credit risk management environment the remaining 37.56% respondents has negative response on CBE establishment of appropriate credit risk management environment.

Table 4-7: Presence of appropriate Portfolio loan and Credit granting process

Sr.No	Statements	No. Of Respondents with Positive Agreement	Percentage (Positive Agreement)	No. Of Respondents with Negative Agreement	Percentage (Negative Agreement)
1	It is too risky to invest our bank's funds in one specific sector of the economy.	64	90.14	5	7.04
2	The bank uses well defined Credit-granting Criteria for assessing credibility of each loan applicants.	43	60.56	19	26.76
3	The Bank conducts comprehensive Credit worthiness analysis properly before granting loan.	36	50.70	20	28.17
4	The bank has established comprehensive Credit limit for the main categories of risk factors in all types of credit facilities.	34	47.89	18	25.35
5	The Bank undertakes Credit granting process based on a reliable and substantial amount of data related to macroeconomic and borrower specific factors.	34	47.89	18	25.35
6	The Bank optimally diversifies its credit exposure to different economic sectors and geographical area.	33	46.48	23	32.39
7	The bank critically follows Sound Credit granting process for approving new credits	32	45.07	24	33.80

	as well as amending, renewing and re-financing existing credits.				
8	Adequacy, marketability and enforceability of collateral requirement is properly evaluated and measured by professional personnel or expertise	28	39.44	24	33.80
	Average		***53.52***		***26.58***

The above Table 4-7shows that Out of 70 respondents, 53.52% of the respondents agreed that CBE has appropriate portfolio and credit granting process and the remaining 26.58% of the respondents were disagree and strongly disagree with the above statement. Based on the above response it is confident to say that CBE has good credit granting process and loan portfolio.

Table 4-8: Credit risk identification, Measurement and Monitoring process

Sr.No	Statements	No. Of Respondents with Positive Agreement	Percentage (Positive Agreement)	No. Of Respondents with Negative Agreement	Percentage (Negative Agreement)
1	The bank strictly monitors loan terms and conditions that have been stipulated at the time of loan approval.	38	53.52	18	25.35
2	The bank regularly reviews and monitors the performance of Credit quality at individual and portfolio level.	35	49.30	26	36.62
3	The bank quantify its credit risk at individual and portfolio level	32	45.07	24	33.80

4	The bank has developed its own internal risk rating system and applying in credit risk management process effectively.	28	39.44	23	32.39
5	There is effective system and practice of reporting and communicating risk data/ information among relevant staffs of our bank	28	39.44	26	36.62
6	There is a complete, neatly organized and regularly updated credit file in our bank.	25	35.21	27	38.03
7	There is effective Credit monitoring system and procedures.	24	33.80	26	36.62
8	The bank's Credit risk management system and practice has been integrated with appropriate Management Information Systems.	19	26.76	37	52.11
	Average		**40.32**		**36.44**

From table 4.8 the result maintaining Credit risk identification, Measurement and Monitoring process exhibited that 40.32% of the respondents strongly agree and agree which means the credit risk identification, measurement and monitoring process is to much lower than the minimum of 50 % while the percentage of negative respondents strongly disagree and disagree respondents' result shows that 36.4% which is relatively similar to strongly agree and disagree results. Which means the respondent of the bank employees did not satisfied with the credit risk identification, Measurement and Monitoring process of CBE. In the other way from the eight statements the higher score gained statements are 1, 2, &3 while the lowest score scored statements are 6, 7& 8.

Generally, Credit risk identification, Measurement and Monitoring process of CBE is too much poor and it needs serious of improvements accordingly the given specifications.

Table 4-9 : existence of well-established risk management system and standards

Sr.No	Statements	No. Of Respondents with Positive Agreement	Percentage (Positive Agreement)	No. Of Respondents with Negative Agreement	Percentage (Negative Agreement)
1	Success and failure of the bank is mostly depends on the effectiveness of Credit Risk Management System and Practice.	62	87.32	3	4.23
2	Establishing and Practicing effective Credit Risk Management system is one of the main objectives of my bank.	53	74.65	10	14.08
3	The bank has established Sound Credit Risk Management System in line with NBE's risk management guideline and directives.	35	49.3	13	18.31
4	The bank has well-documented Credit Risk Management Strategy, Policy and Procedures that guide the staffs in their daily activities of managing credit risks.	32	45.07	21	29.58

5	The bank gives adequate and effective Risk Management training for staffs	26	36.62	30	42.25
6	There is suitable Organizational structure that enables me to undertake effective Risk Management System and practice.	24	33.8	31	43.66
7	This bank has adequate and qualified risk management staffs and expertise	23	32.39	23	32.39
8	There is adequate Deposit mobilization and fund utilization in this bank.	23	32.39	26	36.62
9	Overall, I consider the level of Credit Risk Management system and Practices of the bank is to be excellent.	16	22.54	35	49.3
	Average		***46.01***		***30.05***

From the above table of 4.9 results of the indicted that strongly agrees and agrees holds 46.01% of the total respondents. This is lower than 50% of the minimum average of score. This indicated that the bank has no well-established risk management system and standards are poor .while the percentage of strongly dis-agree and disagree are scored 30.05%. This indicated that the CBE existence of well-established risk management system and standards shallow and it need maximum replacement and detailed review the bank's risk management system and standards.

In the other ways from nine statements of risk management system and standards statement 1, and 2 scores the highest percentage respectively and the lowest score statements are 8, & 9 respectively. The bank should revise its risk management system and standards based on the above results accordingly.

Table 4-10: loan portfolio quality and credit risk control

sr. No	Statements	No. Of Respondents with Positive Agreement	Percentage (Positive Agreement)	No. Of Respondents with Negative Agreement	Percentage (Negative Agreement)
1	The performance of the bank is enhanced by using regularly credit checks	56	78.87	5	7.04
2	To reduce default and credit risk, it's important to in involve Credit committees in reaching decisions.	50	70.42	8	11.27
3	Repayment of loans can be improved by having flexible plans for repayment	46	64.79	16	22.54
4	Clients' commitment to pay back their loan is enhanced by having penalties for lateness.	36	50.70	19	26.76
5	The performance of the bank can be improved by setting limits on size of loan.	35	49.30	20	28.17
6	The performance of the bank is affected by loans' rates interest.	29	40.85	23	32.39
7	There is an early identification of Credit default sign with immediate corrective action	29	40.85	33	46.48
8	Monitoring and management of credit is enhanced by using clients' loan application form.	27	38.03	22	30.99

9	The Bank carry out regular independent internal Credit quality reviews accurately.	22	30.99	33	46.48
10	Appropriate and timely policy measures have been taken for resolving loan recovery problem during the last three years.	21	29.58	32	45.07
11	The bank's top managements have strong commitment toward controlling default risk	12	16.90	41	57.75
	Average		***46.48***		***32.27***

From the above table 4.10 result of the effect of credit risk control on loan portfolio quality exhibited that 46.48% the total respondents were strongly agree and agree while 32.27 % the respondents were strongly disagree and disagree on the given alternatives. This indicated that the bank credit risk control mechanism on loan portfolio quality is very poor and did not continuously improve its loan portfolio quality. This leads to the bank to inter to NPLS which is more than 40% of the total loan portfolio of the bank however, the international and NBE standards allowed up to 5% to 15% respectively. From the above alternative statements the respondent give more scores to statement 1, and 2 and the lowest scores from the respondent was 10 and 11 statements respectively. So, the bank's top managements have strong commitment toward controlling default risks statement the respondents are ranked the highest negative score among the other alternative statements. This means the bank top executive management has no commitment to work strongly to improve the bank loan portfolio quality.

The frequency analysis in the previous five tables shows how credit risk assessment based on each of the parameters looks like in CBE. However, it would be difficult to make a comparison among these parameters to deduce that, CBE is worse in some parameters and best in others.

Table 4-11: Credit Risk Management Practice assessment Parameters score in CBE

Credit Risk Management Practice Parameters	***N***	***Minimum***	***Maximum***	***Mean***	***Std. Deviation***
Credit Risk Granting and Portfolio Quality Control	70	1.25	4.63	3.35	0.64103
Credit Risk System and Standard	70	1.67	4.67	3.20	0.64322
Credit Risk and Portfolio Quality Control	70	1	4.36	3.17	0.5852
Risk Identification, Measurement and Control	70	1.75	4.13	3.03	0.67709
Risk Environment	70	1.22	4.56	2.98	0.67924

As it can be depicted from Table 4-11, credit risk management practice in CBE is not highly satisfactory. From a score of 5 the highest in CBE case is 3.34, which is for Credit granting process and portfolio management. CBE is relatively good in establishing appropriate credit granting process and managing its loan portfolio to have a lesser risk exposure. The score for the existence of appropriate credit risk system and standards in place is 3.20 and for that of Credit Risk and Portfolio quality control is 3.17. The Bank has relatively poor score in establishment of appropriate risk environment (score 2.90) and having appropriate risk identification, measurement and control mechanism (3.03). The results on these parameters meant to asses risk management practice of the Bank revealed that, CBE if not worst, not very good at its risk management practice, especially, in the mechanisms to identify, measure and control its credit risks. As a result, improvements are needed in creating appropriate risk environment, in the way how it identify, measure and control credit risks, credit risk and portfolio quality controlling mechanisms. The Bank should also further enhance its system and standards of risk control as well as the credit granting and portfolio management process.

Table 4-12: CBE credit risk Management practice in evaluating the client’s credit worthiness capacity for Loan Portfolio

CBE credit risk management practices in evaluating the client’s credit worthiness capacity for loan portfolio		Frequency	Percent
	Poor	24	33.8

Satisfactory	17	23.9
Good	27	39.4
Very good	2	2.8
Total	70	100.0

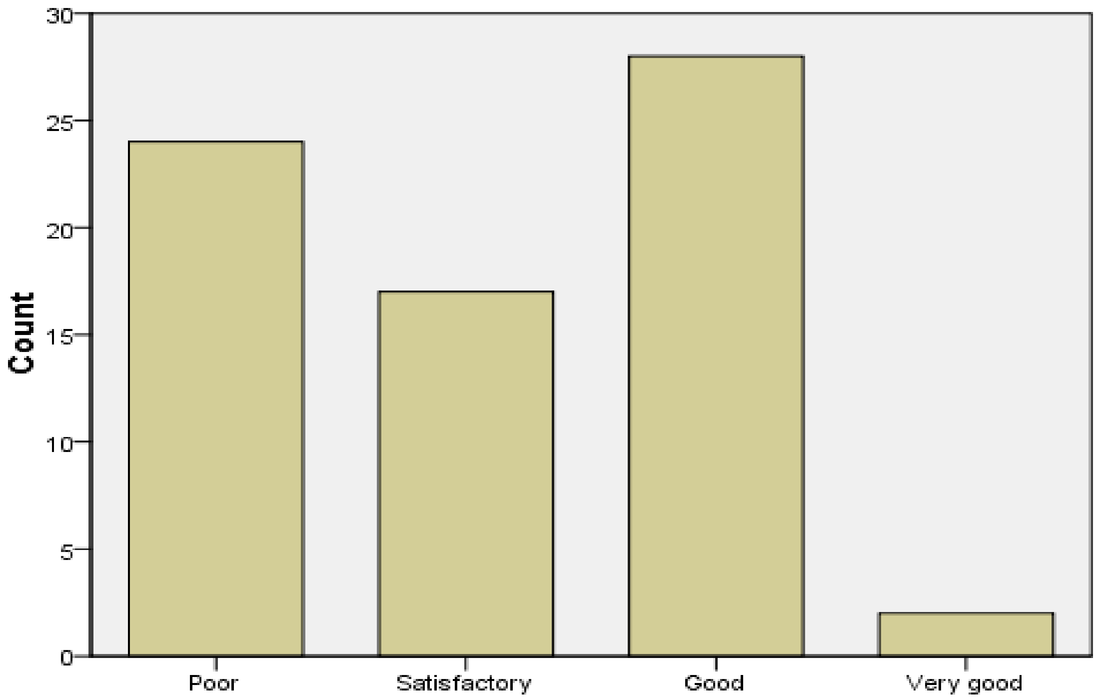

Figure 2: Clint Credit worthiness assessment Capacity

Table 4-12 and Figure 3 showed that about 33% of the respondents have a perception that the coop has poor capacity in evaluation client’s credit worthiness. Of course, about 42 % and 23% of the respondents` has a perception that the coop has good and satisfactory capacity in this regard. However; majority of the respondent`s being in the credit process, 33% negative response is an indication that the coop has week capacity in assessing the credit worthiness of its clients.

Table 4-13: Effectiveness of credit risk management practices

Sr.No	Statements	No. Of Respondents with Positive Agreement	Percentage (Positive Agreement)	No. Of Respondents with Negative Agreements	Percentage (Negative Agreements)
1	Risk identification	42	60.56	28	39.44
2	Risk Analysis and assessment	40	57.75	30	42.25
3	Risk monitoring	39	56.34	31	43.66
4	Risk mitigation	38	54.93	32	45.07
Average			***57.39***		***42.61***

The study assessed the effectiveness of credit risk management practices (risk identification, risk analysis and assessment, risk monitoring and risk mitigation) with regard to their effect on the loan portfolio quality. From the above table and figure regarding to the effectiveness of CBE credit risk identification, risk analysis and assessment, monitoring and mitigation from the total respondents 57.39% have positive agreement (effective, more effective and very effective) while 42.61% of the respondents have negative(not effective and less effective) response on the current CBE credit risk management practice . The implication is that CBE has to improve the risk management practices, especially, in devising mitigation and control mechanisms for risk.

4.3 Loan Portfolio Quality Assessment of CBE

4.3.1 Trend of outstanding loan by number of clients and loan amount

Commercial bank of Ethiopia has been giving its project and lease financing service to customers in selected priority areas selected by the government to spur the economic development agenda of the country. These priority areas are Commercial Agriculture; Agro processing, manufacturing and Extractive Industries, preferably export focused. The Bank has been providing its financial and technical support to priority sectors of the economy. **Error! Reference source not found.**3 showed that majority of the clients for the Bank are rom the agriculture, manufacturing and financial service (Lease financing and credit to Microfinance Institutions). Following GTP II, the number of clients from these sectors has shown increment. The withdrawal of the Bank from financing service sector projects is the reason for the decline in the number of clients for the service sector.

However in terms of amount, outstanding loan given to the Manufacturing sector is by far exceeds the other sectors which is followed by the agriculture sector and the financial services. The loan outstanding for CBE in recent years is highly concentrated to the manufacturing sector.

The concentration of loan per client is the highest in the manufacturing sector followed by the mining and extractive sector; the financial service sector and the agriculture sector

4.3.2 The Agriculture sub-sector loan outstanding Assessment

CBE gives loan to the agriculture sector for production of oil crops, fibber crops, Horticulture, cereal & pulses, coffee and others. It gives credit for Agro service purpose too. The numbers of clients for the bank are more concentrated in the oil crops production sub-sector followed by fibber crops and agro-service. The number of clients in the oil crops sub sector is increasing while clients in the coffee and other sub-sectors are declining.

However, in terms of loan amount the fibber crops (Mainly Sisal and Cotton Production) production sector took the leading share followed by the oil crops, horticulture, cereal and pulses and other sub sectors respectively. The loan concentration per client is the highest in the fibber crops sub-sector too. It is followed by the horticulture, the livestock and oil crops sub-sectors respectively.

Figure 8: Loan amount Concentration per client by sub-sectors

4.3.3 The Manufacturing sub Sector loan Assessment

To support the country's economic development through the manufacturing sector growth following the Growth and transformation plan of the country, it gives loan to the cottage industry, food processing, agro processing, manufacturing of liquor and beverage, metallic and non-metallic products, textile and garments, chemical & plastic products, wood and paper products etc.

Manufacturing of Textile and garments takes the leading share of the Bank`s outstanding loan followed by integrated agro processing, manufacturing of non-metallic products, production of household appliance, rubber and communication equipments and apparatus production , manufacturing of plastic and chemical products and the food processing sub-sectors respectively.

Based on the number of clients having outstanding loan, the food processing and the integrated agro-processing, manufacturing of chemicals & plastics sector, and the manufacturing of textile and garments sub sectors are dominating respectively. The loan amount per client is higher in the agro processing sub sector followed by the manufacturing of textile and garments.

Loan Collection Performance

4.4.1 The nexus of NPL and Collections in CBE

The NPL amount for the bank has showed a sharp increment. The level of increment in the level of loan collection has not shown much progress. Loan outstanding has shown average growth rate of 18% while actual collection amount and planed collection amount registered average growth rate of 12% and 7% respectively.

Table 4-14: Loan collection plan & actual, outstanding loan and NPLs in Million Birr

Year	*Collection plan*	*Collection Actual*	*Loan outstanding*	*NPLs*
2016	8,151.93	2,539.95	17,465.40	1,595.03
2017	7,424.41	3,053.55	21,160.87	6,505.84
2018	9,685.52	4,087.32	25,291.47	4,035.50
2019	11,836.50	4,109.07	29,622.89	6,507.50
2020	2,078.94	4,560.09	32,627.14	10,453.99
2021	13,119.16	4,842.18	37,129.45	15,219.95
2022	11,882.79	4,936.00	47,740.60	19,083.37
Average Growth	**7%**	**12%**	**18%**	**77%**

The prevailing gap between actual and plan collection of loan on one hand and the increasing level of loan outstanding and Non-performing loan on the other hand is an indicator of the bank has also exerted less effort for collection of its loans. At least the bank should increase the collection in terms of plan so that it can match with its loan outstanding (See Table 4-14).

4.3.4 Collection Trend and Performance for the Last Five Years

Under this section, the last five years' CBE's loan collection trends and performances have been addressed. In order to see the past loan collection trends of the Bank, the researchers considered the total loan collection plan and actual total loan collection of the Bank for the last five fiscal years. Besides this, Loan Outstanding Position, Non-Performing Loan Ratio, and Loan Recovery Rate of the Bank have been considered. So as to see the performances of the Bank on these issues, five fiscal years periods have been taken into account commencing from 2017/18-2021/22. Accordingly, the plan and actual performances of the Bank on the loan collection, Loan outstanding position, NPL Ratio and loan recovery rate of the Bank for the last five years have been stated on the table below;

Table 4-15 Loan Collection, Loan Outstanding, NPL Ratio and Loan Recovery Rate Performance of the Bank for the Last Five Years "in Million Birr"

Credit Operations	2017/18 F.Y Performance			2018/19 F.Y Performance			2019/20 F.Y Performance			2020/21 F.Y Performance			2021/22* F.Y Performance		
	Plan	**Actual**	**%**	**Plan**	**Actual**	**%**	**Plan**	**Actual**	**%**	**Plan**	**Actual**	**%**	**Plan**	**Actual**	**%**
Loan Collection	3.90	4.09	105%	5.78	4.11	71%	6.00	4.56	76%	6.09	4.84	79%	6.93	4.99	72%
Loan outstanding	32.15	27.36	85%	38.61	31.63	82%	42.46	33.82	80%	40.54	39.15	97%	41.78	47.58	114%
NPL ratio	5.27%	12.54%	42%	9.45%	17.71%	53%	9.16%	24.98%	46%	16.97%	39.43%	43%	15.76%	33.92%	46%
Loan Recovery Rate	63%	47%	75%	57%	53%	93%	67%	50%	75%	58%	40%	69%	55%	50.09%	91%

Source: CBE Annual Report of 2017/18- 2021/22

The above table indicates that actual loan outstanding has been increasing steadily and it has also surpassed the plan that the working units has set. On the other hand, the amount of actual loan collection has not shown a progress that should have been matched with the Bank`s actual loan outstanding. Unlike our loan outstanding the amount of planned loan collection has been above the actual loan collection amount in the previous three years. The implication is that the loan processing units should take care of disbursing the planed loan amount so that it would have no impact on our loan collection. They should also plan and make efforts to match their collection plan and hence the actual loan collection amount to be in line with the amount of actual loan outstanding that the Bank has. This is a signal that the working units have given less weight for collection efforts as compared to the disbursement process. The loan recovery rate both the plan and the actual has been declining while the planed and actual NPLs has shown increments.

The study has undergone a study to assess the loan quality portfolio of the Bank both through secondary data and primary data analysis. The loan portfolio quality in one or another way is related to its exposure for different type of risks.

Table 4-16 showed that the loan portfolio of Commercial Bank of Ethiopia Bole District is relatively more exposed to unpredictable and uncontrollable risks. More than 25 percent of the respondents have stated that such risks are frequently encountered in CBE.

Table 4-16: Level of risk for loan portfolio encountered

sr. No	Statements	Not encountered	Rarely encountered	Moderately encountered	Frequently encountered	Most frequently encountered	No. Of Respondents with High frequency of occurrence	Percentage (Positive Agreement)	No. Of Respondents with low frequency of occurrence	Percentage (Negative Agreement)
1	Unpredictable risks	3	14	29	23	2	23	32.39	17	23.94
2	Uncontrollable risks	4	12	23	21	11	21	29.58	16	22.54
3	Predictable risks	11	22	22	15	1	15	21.13	33	46.48
4	Controllable risks	9	21	28	12	0	12	16.90	30	42.25
	Average							***25.00***		***33.80***

From table 4.16 we have understand that level of risk for loan portfolio encountered result indicates 25% of the respondents were positively agree while 33.80% the respondents were negatively agree on the above statements. This indicated that levels of risk for loan portfolio encountered are negative. On the other way Unpredictable risks and Uncontrollable risks are high frequency of occurrence on level of risk for loan portfolio while Predictable risks and Controllable risks are lower frequency of occurrence. The bank mostly affected by the un controllable and unpredictable factors (uncertain factors).

4.4 Credit risk management practice and loan portfolio quality in CBE

Theoretically, in vast literatures it has been noted that credit risk management practice has its own impact on the quality of loan portfolio that creditors will have. In this section of the thesis the relationship that credit risk management has with loan portfolio quality and those factors that lead to poor loan portfolio quality has been discussed thoroughly.

Table 4-17: Existence of relationship between Credit Risk Management practices and Loans portfolio quality?

	Frequency	Percent	Valid Percent
Yes	70	98.6	98.6
No	1	1.4	1.4
Total	71	100.0	100.0

Respondents were to either confirm if there is any effect between the Credit Risk Management practices of the bank and its Loans portfolio quality by answering either yes or not. The result is presented shows in table 4.17, almost of the respondents 98.6 % indicated that there is relationship between credit risk management practice and loan portfolio Quality. Based on the response it is confident to say that there is credit risk management and portfolio loan quality (relationship). That means the existence of good credit risk management practice could be increase the Bank loans Portfolio quality. Whereas poor credit risk management practice leads to rising of nonperforming loans and deteriorate the quality of loans portfolio

Table 4-18: Credit risk management practice effect on Loan Portfolio Quality

Credit risk management practice level of effect on Loan Portfolio Quality	Frequency	Percent	Valid Percent
No effect	1	1.4	1.4
Moderate effect	19	26.8	26.8
Major effect	50	71.8	71.8

	Total	70	100.0	100.0

Based on the data presented in Table 4-18, majority of the respondents (71.8%) o have a thought that credit risk management practice has major effect on loan portfolio quality. Some 26.8% of the respondents felt that credit risk management practice has moderate effect on loan portfolio quality and only one respondent felt that credit risk management practice has no effect on loan portfolio quality.

Table 4-19: Contributing factors for the existence of banks NPLS in CBE

sr. No	Statements	No. Of Respondents with Positive Agreement	Percentage (Positive Agreement)	No. Of Respondents with Negative Agreement	Percentage (Negative Agreement)
1	Poor risk assessment prior to loan approval	64	90.14	3	4.23
2	Lack of aggressive credit collection methods	60	84.51	5	7.04
3	Inadequate use of the KYC policy by staff when assessing quality of borrowers	58	81.69	8	11.27
4	Poor monitoring / follow up by credit officers	57	80.28	8	11.27
5	Staff inexperience in credit allocation. May need more training.	54	76.06	12	16.90
6	Insider lending and pressure from senior managers, board members and politicians to approve some loans.	53	74.65	3	4.23

7	Poor market research done on the loan products offered by CBE.	50	70.42	13	18.31
8	Lack of sound financial management advice provided to clients by bank staff	47	66.20	10	14.08
9	Use of Credit standards like the 5c's e.g. collateral, capital, condition, character and capacity.	47	66.20	14	19.72
10	Fraudulent approval of loans	41	57.75	11	15.49
11	Credit procedure of approving facility	40	56.34	11	15.49
12	Collateral offered was inadequate or less than loan amount advanced	40	56.34	16	22.54
13	CBE's use of specific lending and project appraisal techniques	40	56.34	17	23.94
14	Sector of economy to which the loan was allocated	39	54.93	15	21.13
15	All information regarding clients cannot be kept on the computer e.g. signed contracts, proof of collateral,	38	53.52	21	29.58
16	Inadequate number of staff in some departments	37	52.11	16	22.54
17	Loan size / amount disbursed	32	45.07	25	35.21
18	CBE uses an out-dated credit policy	30	42.25	26	36.62
19	Short repayment period	24	33.80	32	45.07
20	Very high number of clients issued loans leads to more NPLs	23	32.39	23	32.39
	Average		***61.55***		***20.35***

From the above table of 4.19 understands that the contributing factors for the existence of banks NPLS in CBE presented statements result showed that 61.55% the respondents have positive response while 20.35% of respondents were negative response on the given statements. This indicated that the majority of the respondents agreed that the above statements are major contributing factor for high none performing loan and low quality loan portfolio and it results more than 40 % of the bank's loan is at risk in general. On the other hand from statement 1 up to 6 the respondents responded 90.14%,84.51%,81.69%,80.28%,76.06%,74.65%, and 70.42% respectively .which means more than 90-70% of the respondents strongly agree and agree about the contributing factors for the existence of banks NPLS .while the remaining respondents responded that 4.23 %,to 36.62 % were strongly disagree and agree . This compared to the respondents of strongly agree and agree very much lower. So, the bank's contributing factors for the existence of NPLS is higher. .

CHAPTER FIVE

5. SUMMARY, RECOMMENDATIONS AND CONCLUSION

5.1 Summary of Findings

The thesis has sought to attain the main objectives of assessing the effect of credit risk management on the quality of loans portfolio of Commercial Bank of Ethiopia Bole District. Both primary and secondary data were used. The secondary data with regard to loan portfolio and loan position of the bank as has been used. And the primary data were collected from the professional employees of the bank through structured questionnaire.

The main finding with regard to the assessment of the credit risk management practice of the bank revealed that, Commercial Bank of Ethiopia Bole District has not satisfactory risk management practice. The score from 1 poor to 5 best, all the parameters of risk management practice assessment have a score value below 3.40, i.e., Credit Risk Granting and Portfolio Quality Control (3.40), Credit Risk System and Standard (3.20), Credit Risk and Portfolio Quality Control (3.17), Risk Identification, Measurement and Control (3.03), and Risk Environment (2.98).

The assessment of the loan collection performance relative to disbursements is poor. Disbursements are above plan and steadily growing. But collections are below plan and showed no progress. The bank`s loan portfolio is also more vulnerable to various types of risks such as to unpredictable risk, unpredictable risks as well as predictable and controllable risks. Majority of the respondents perceived that credit risk management practice has major effect on the loan portfolio quality of the bank (More than 70%). The quality of portfolio is also poor. It has NPL ratio of above 15% which is the maximum set by international standards. The most important contributing factors as perceived by the respondents are poor risk assessment prior to loan approval, lack of aggressive credit collection methods, inadequate use of the KYC policy by staff when assessing quality of borrowers, Poor monitoring / follow up by credit officers, staff inexperience in credit allocation, insider lending and pressure from senior managers, board members and politicians to approve some loans, and poor market research done on the loan products offered by Commercial Bank of Ethiopia Bole District..

5.2 Conclusion

Based on the finding s of the study the following conclusions have been drawn with regard to the set specific objectives. First, credit risk management practice of the bank is not that much satisfactory. The scores related to Credit Risk Granting and Portfolio Quality Control(3.40), Credit Risk System and Standard(3.20), Credit Risk and Portfolio Quality Control(3.17), Risk Identification, Measurement and Control(3.03), and Risk Environment are average and below average. Therefore, there is a need to improve and enhance credit risk management practice of the bank. Second, both in terms of Nonperforming loan and concentration, Commercial Bank of Ethiopia Bole District has poor loan portfolio quality. The poor loan portfolio quality of the bank is associated with poor credit risk management practice. As a result it is important to improve the credit risk management practice to improve the loan portfolio quality. Especially, standards of risk management have significant impact on loan portfolio quality.

5.3 Recommendation

The following recommendations are forwarded based on the findings, so as to enhance loan portfolio quality of Commercial Bank of Ethiopia Bole District:

- Improve the Risk management practice of the bank
- Improve the credit granting process to have sound Credit risk management
- Up-to- date Credit risk management System and standards so as to have strong credit management
- Strengthen client credit worthiness assessment to minimize credit risk
- Follow aggressive credit loan collection strategies to improve loan portfolio quality
- Enhance the capacity of employees related to risk management practice
- Have explicit exposure limit on credit by sector and Geographic location

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APPENDIX

St.Mary UNIVERSITY

POST GRADUATE STUDIES

DEPARTMENT OF MANAGEMENT

Dear Respondents,

The aim of the questionnaire is to gather data on the Effect of credit risk management on the quality of loan portfolio the case of Commercial Bank of Ethiopia and to assess the effect of credit risk management practice on the quality of loans portfolio of Commercial Bank of Ethiopia for the partial fulfillment of the requirements for the Degree of Masters of Business Administration.

You are kindly requested to assist the successful completion of the study by providing the necessary information. Your participation is entirely voluntary and the questionnaire is completely anonymous. I assure you that the information you share will stay confidential and only used for the aforementioned academic purpose.

Thank you in advance for your kind cooperation.

Part I: Biographical Information

1. Gender: Male ☐ Female ☐
2. Age: less than 25 ☐25 -35 ☐36-45 ☐ ≥46 ☐
3. Educational Background: Diploma☐BA/BSC☐Masters ☐PhD ☐
4. Work experience : Less than 1 year ☐1-5 Years ☐6-10 Years☐

   10-15 Years ☐ above 15Years☐
5. What is your current position in the bank?

   Credit officer ☐

   Senior credit officer ☐

   Credit Manager ☐

Credit Director

Part II: Credit Risk Management Practices

6. Rate the extent to which you agree with the following statements which are related to the establishment of appropriate credit risk environment in your organization.

Please put tick mark **(√)** in the box corresponding to the option that identifies your level of agreement.

1= strongly disagree 2= disagree 3= neutral 4= agree 5= strongly agree)

Statements	**Strongly Agree**	**Agree**	**Neutral**	**Disagree**	**Strongly Disagree**
Bank's Credit risk ***strategies and policies*** are regularly reviewed/ updated					
Bank's Credit provision and risk identification ***procedures*** are regularly reviewed/updated					
Senior managements are fully dedicated to improve the bank's credit risk management practices					
Boards of Directors and Senior Managers closely monitor the major Credit Risk exposure of the Bank and implementation of credit risk policies, strategies and procedures					
The banks' staffs take the necessary precaution against default risk and effectively work to the implementation of credit risk management policies, strategies and procedures					
Credit Risk management strategy, Policies and Procedures are consistently applied in all Credit product and activities of the bank.					
Authority and Responsibility of Risk Management are clearly set out and understood throughout the bank.					
There is proper identification of Credit Risk inherent in all products and activities of our Bank.					
There is common understanding about Credit Risk Management Strategy, Policy and Procedures across the Bank.					

7. Portfolio loan and Credit granting process

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
It is too risky to invest our bank's funds in one specific sector of the economy.					
Adequacy, marketability and enforceability of collateral requirement is properly evaluated and measured by professional personnel or expertise					
The Bank conducts comprehensive Credit worthiness analysis properly before granting loan.					
The Bank uses well defined Credit-granting Criteria for assessing credibility of each loan applicants.					
The bank critically follows Sound Credit granting process for approving new credits as well as amending, renewing and re-financing existing credits.					
The bank has established comprehensive Credit limit for the main categories of risk factors in all types of credit facilities.					
The Bank optimally diversifies its credit exposure to different economic sectors and geographical area.					
The Bank undertakes Credit granting process based on a reliable and substantial amount of data related to macroeconomic and borrower specific factors.					

8. Maintaining an appropriate Credit risk identification, Measurement and Monitoring process

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
The bank strictly monitors loan terms and conditions that have been stipulated at the time of loan approval.					
The bank regularly reviews and monitors the performance of Credit quality at individual and portfolio level.					
There is a complete, neatly organized and regularly updated credit file in our bank.					
The bank has developed its own internal risk rating system and applying in credit risk management process effectively.					
There is effective Credit monitoring system and procedures.					

The bank quantify its credit risk at individual and portfolio level					
There is effective system and practice of reporting and communicating risk data/ information among relevant staffs of our bank.					
The bank's Credit risk management system and practice has been integrated with appropriate Management Information Systems.					

9. Credit risk management practice

Existence of well-established Risk management system and standards

Statements	**Strongly Agree**	**Agree**	**Neutral**	**Disagree**	**Strongly Disagree**
Establishing and Practicing effective Credit Risk Management system is one of the main objectives of my bank.					
Success and failure of the bank is mostly depends on the effectiveness of Credit Risk Management System and Practice.					
The bank has well-documented Credit Risk Management Strategy, Policy and Procedures that guide the staffs in their daily activities of managing credit risks.					
The bank has established Sound Credit Risk Management System in line with NBE's risk management guideline and directives.					
There is suitable Organizational structure that enables me to undertake effective Risk Management System and practice.					
This Bank has adequate and qualified risk management staffs and expertise					
There is adequate Deposit mobilization and fund utilization in this bank.					
The bank gives adequate and effective Risk Management training for staffs					
Overall, I consider the level of Credit Risk Management system and Practices of the Bank is to be excellent.					

10. ***Portfolio loan quality and Credit Risk Control:*** Please indicate your opinion about the statements on effect of credit risk control on loan quality portfolio of Commercial Bank of Ethiopia.

Statements	**Strongly Agree**	**Agree**	**Neutral**	**Disagree**	**Strongly Disagree**
The performance of the bank can be improved by setting limits on size of loan.					
The performance of the bank is enhanced by using regularly credit checks					
Repayment of loans can be improved by having flexible plans for repayment					
Clients' commitment to pay back their loan is enhanced by having penalties for lateness.					
Monitoring and management of credit is enhanced by using clients' loan application form.					
To reduce default and credit risk, it's important to in involve Credit committees in reaching decisions.					
The performance of the bank is affected by loans' rates interest.					
There is an early identification of Credit default sign with immediate corrective action					
The Bank carry out regular independent internal Credit quality reviews accurately.					
Appropriate and timely policy measures have been taken for resolving loan recovery problem during the last three years.					
The bank's top managements have strong commitment toward controlling default risk					

11. ***Portfolio loan, NPL and Credit risk management practice:*** Please indicate your level of agreement on the statement below regarding contributing factors for the existence of Banks non-performing loans in CBE?

Statements	**Strongly Agree**	**Agree**	**Neutral**	**Disagree**	**Strongly Disagree**
Poor monitoring / follow up by credit officers					
Lack of aggressive credit collection methods					
Poor risk assessment prior to loan approval					
Inadequate use of the KYC policy by staff when assessing quality of borrowers					
Lack of sound financial management advice provided to clients by bank staff					
Fraudulent approval of loans					
Insider lending and pressure from senior managers, board members and politicians to approve some loans.					
Inadequate number of staff in some departments					
Staff inexperience in credit allocation. May need more training.					
CBE uses an outdated credit policy					
Credit procedure of approving facility					
Use of Credit standards like the 5c's e.g. collateral, capital, condition, character and capacity.					
Short repayment period					
Collateral offered was inadequate or less than loan amount advanced					
Sector of economy to which the loan was allocated					
Loan size / amount disbursed					

Very high number of clients issued loans leads to more NPLs					
Poor market research done on the loan products offered by CBE.					
CBE's use of non -specific lending and project appraisal techniques					
All information regarding clients cannot be kept on the computer e.g. signed contracts, proof of collateral,					

12. Based on the bank's experience, please indicate the level of risk for portfolio loan encountered.

	Not encountered	Rarely encountered	Moderately encountered	Frequently encountered	Most frequently encountered
Predictable risks					
Unpredictable risks					
Controllable risks					
Uncontrollable risks					

Part III: Credit risk Management and portfolio loan quality (relationship)

13. Do you think there is any effect between the Credit Risk Management practices of the bank and its Loans portfolio quality?

Yes ☐ No ☐

14. If your response is 'yes' to the above question, please indicate the level of the effect of credit risk management on portfolio quality.

No effect □ minor effect □ moderate effect □ major effect □

15. Improper preparation of credit risk grading score sheet leads to high non-performing portfolio loan in CBE.

Strongly disagree□ Disagree □ Moderately agree □ Agree □ Strongly agree □

16. Based on the overall average, how do you rate the bank's credit risk management practices in evaluating the client's credit worthiness capacity for portfolio loans?

Poor □ Satisfactory □ Good □ Very good □ Excellent □

17. Kindly rate the effectiveness of the following credit management practices with regard to their effect on the loan portfolio quality.

	not effective	less effective	effective	more effective	very effective
Risk Identification					
Risk Analysis and assessment					
Risk monitoring					
Risk mitigation					