ST. MARY'S UNIVERSITY

SCHOOL OF GRADUATE STUDIES

ASSESSMENT OF ASSET QUALITY MANAGEMENT PRACTICE: THE CASE OF BERHAN BANK

BY
AKLILU TADESSE

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ADDIS ABABA

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A THESIS SUBMITTED TO ST. MARY'S UNIVERSITY, SCHOOL OF GRADUATE STUDIES IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR MASTER OF BUSINESS ADMINISTRATION

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Dean, Graduate Studies	**Signature**
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Statement of Declaration

I hereby declare that this work entitled "Assessment of asset quality management practice: the case of Berhan bank." is my work. I have carried out the research work independently with the guidance and support of the research advisor. This study had not been submitted for any degree or diploma program in this or any other institution except where due acknowledgment has been made in the text.

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Signature

Endorsement

This thesis has been submitted to St.Mary's university, school of graduate studies for examination with my approval as a university advisor.

Research Advisor

Kiros Habtu (ASST.PROF)

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Signature and Date

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List of Acronyms

NBE	National Bank of Ethiopia
NPL	Non performing Loan
NPA	Nonperforming assets
RAD	Risk assessment and due diligence
ASQ	Asset quality
POU	Political Unrest
USL	Unsecured Loan
KYC	Knowing your customer
SPSS	Statistical Package for the Social Sciences

Abstract

This study was conducted to assess asset quality management practice of Berhan bank. The study used primary data using questioner. The study populations of 74 were from Berhan Bank employees who are directly involved in credit processing and administering loans in head office and Addis Ababa branch managers. The data collected using questionnaires were analyzed with descriptive statistics using SPSS 23. Descriptive analyses were used to analyze the data collected. The findings of the study revealed that majority respondents agree with the practice of weak risk assessment and due diligent has an impact on asset quality of the bank. Moreover, high lending interest rate, unsecured loans and political also have an impact on asset quality of the bank. Therefore, the study recommended that the bank should give more emphasis on its risk assessment and due diligence procedure before approval of loans and also lending interest rate should be reviewed and reduces to increase asset quality of the bank. In addition, the study recommended that unsecured loans are more risky than secured loans .Therefore; the bank should look for collateral when granting loans. Furthermore reduce and, if possible, eliminate all political influence involved in the giving of loans to specific political individuals and groups.

Key words: Asset quality, risk assessment and due diligence, unsecured loan, political unrest, Berhan Bank

CHAPTER ONE
INTRODUCTION

1.1 Background of the study

The banking sector plays a significant role in the economic growth as well as the development of any country. Banking has various functions like accepting deposits, granting loans and advances, and other financial services like international money transfers.

The main product of the bank is Loans and Advances. The price of a loan is determined by the cost to make the loan plus a profit or risk premium on it. Lending is the primary business of a bank and profit is one of a measure of its success. So, the main objective of lending is to earn a profit on loans for the ongoing sustainability of a bank. The performance of the banks is determined not only by operational results but also by the overall financial condition which consists of asset quality, management quality, efficiency, earning quality, liquidity, capital adequacy, and level of bank service (Kamande, 2016).

Lending is not an easy task for banks because it involves the risk of non-repayment which result in the loan being a non-performing loan. The reason given by different banks vary according to their less quality assets performed, but in common, there are internal and external factors that cause it (Oynaka, 2019).

Asset quality is defined as the overall risk attached to the various assets held by an institution. In the financial sector, the term asset quality and loan quality are used interchangeably. Asset quality is an important parameter for any banking institution, as the quality of its assets has a major role in the earning ability of that institution (Mekonnen, 2015).

In a political and economic crisis, asset quality takes a priority concern as many borrowers' defaults on their loans and the volume of non-performing loans increases. Banks must follow solid lending criteria, actively monitor asset quality and proactively tackle non-performing loans to mitigate losses and the impact on banks' soundness (Enria, 2020).

Non-performing assets indicate a loan and advance for which interest or repayment of principal or both remains overdue for 90 days or more. An advance/loan is treated as non-performing when it fails to satisfy its repayment obligations. As per the National Bank of Ethiopia directive, non-performing loans are defined as “Loans or Advances whose credit quality has deteriorated such that full collection of principal and/or interest under the contractual repayment terms of the loan or advances in question (National Bank of Ethiopia, 2008).

The causes of the impaired loan vary in different countries and have a multidimensional aspect both, in developing and developed nations. Depressed economic conditions, high real interest rates, inflation, lenient terms of credit, credit orientation, high credit growth, risk appetite, and poor monitoring among others are some of the reasons why loans fail to perform (Negera, 2012).

In Ethiopia, 30 private banks provide loans to investors. Berhan bank is one of the financial institutions in Ethiopia engaged in providing various loans and credit facilities since 2009. The bank's performance showed a decline as compared to previous periods represented by profitability levels and an increasing ratio of gross nonperforming assets to gross loans and advances (Berhan Bank, 2022). What causes a loan to be a non-performing loan? This study attempted to assess asset quality management practice of Berhan bank.

1.2 Background of the organization

Berhan Bank S.C was formed in accordance with Article 304 of the Commercial Code of Ethiopia with the objective of operating in the banking industry. The Bank was registered and licensed by the National Bank of Ethiopia on 27 June 2009 with a paid up capital of Birr 95.7 Million divided in to shares of Birr 1,000 and an authorized capital of Birr 300 Million.

Having been registered and licensed by the National Bank of Ethiopia on 27th June, 2009, Berhan Bank S.C started operation on October 30, 2009. Opening its first branch in Addis Ababa near Bole International Airport as ‘Berhan International Bank- Bole Branch’. With a branch network leapfrogging above 320, headquartered in Bole, Addis Ababa today, the bank operates in virtually all regional cities of Ethiopia and in their respective towns. The bank serves more than half a million customers across the nation.

The bank goal is to make banking stress free and efficient, and kept on investing in technology and innovations that enable customers to reach their goals as in saving, investment, business or efficient transaction. In addition to serving customers at networked branches, the bank offer electronic banking services such as Debit Cards allowing customers to access their accounts at any ATM machine nationwide, introduce Mobile and Internet Banking. Beyond local banking services, the bank have also partnered with international money transfer companies such as Western Union, Money Gram, Ria, Dahabshiil, Trans-Fast, Xpress Money and World Remit.

The Bank’s capital base has also kept on showing a steady growth. At the end of June 30, 2022, it’s paid up capital reached Birr 3.1 billion. Moreover, the number of shareholders has also significantly increased to over 14,879.

Vision, Mission and Values of the Bank [VMV]

Vision: To be a radiant and trustworthy Bank in excellence.

Mission: Provide diverse financial products by deploying motivated and qualified human resource as well as up-to-date technology with the highest ethical standard to create maximum value to stakeholders.

Values:

- Sustained business growth;
- Quality customer service;
- High ethical standards;
- Confidentiality;
- Corporate social responsibility;
- Conducive working environment for employees;
- Professionalism and team spirit; and
- Innovation and learning-organization.

1.3 Statement of the problem

Assets of a bank include cash, investments, fixed assets, loans, and others. Amongst all, loans and advances that it gives to borrowers take the lion's share and are the riskiest of all assets. In banking, any bank-owned asset whose value may change due to fluctuating interest rates, changes in credit quality, repayment risk, and other factors, is considered a risk asset.

The term asset quality refers to the quality of loans that a bank has lending to investors. A bank is said to have good-quality assets if loans are repaid as per the contract on time. This deterioration of asset quality affects not only its operating and financial performance but also the general soundness of the financial system. A sound financial system requires the maintenance of a low level of nonperforming assets which in turn facilitates the economic development of a country (Dr Abata, Matthew Adeolu, , 2014).

The level of non-performing loans (NPLs) is determined as a percentage of gross nonperforming assets to gross loans and advances were used as a proxy to measure asset quality. Non-performing loans affect the bank`s profitability and liquidity which are the main components of the overall efficiency of the bank. The level of loan default increase in the banking industry reduces the possibility of generating income to maximize the profitability of the banks. Therefore, the determinants of NPLs should be given due attention because of their effect on the survival of banks.

The principal objective of the study was to assess asset quality management practice of Berhan bank. Based on the audited financial statement of the bank the nonperforming (NPL) ratio of the bank is 8% and 9.5% as of 30 June 2022 and 30 June 2021 respectively which is above the National bank of Ethiopia requirement of 5% (Berhan Bank, 2022).

Many studies examined determinants of non-performing loans in commercial banking industries in Ethiopia and other countries are categorized the factors into a bank-specific and macro-economic variable. Government policy, inflation, currency fluctuations, and GDP are macroeconomic factors. Bank-specific factors include interest rates charged by banks, bank size, ownership (private and state owned), integrity issues, credit follow-up weaknesses, and other issues (Mileris, 2014).

Habtamu (2015) examined specific factors influencing the occurrence of non-performing loans in six private commercial banks in Ethiopia. Accordingly, the findings of the study indicated that weak credit assessment, poor loan follow-up, an underdeveloped credit culture, lenient credit terms and conditions, a lack of knowledge, compromised integrity, unfair competition among banks, fund diversion for unintended purposes, and shareholder influences were the main factors affecting NPLs.

Further more ,Tamiru, (2017) evaluated the impact of macroeconomic variables (deposit interest rate, exchange rate, and annual inflation rate), bank-specific factors (loan to deposit ratio, credit monitoring and follow-up, and loan growth rate), and business characteristic (business profit margin and nature of business) on the determinants of non-performing loan growth rate in Ethiopian commercial banks. The study used a mixed research approach that combines documentary analysis (a structured evaluation of documents) and in-depth interviews to span the years 2000 to 2015. According to the study's conclusions, there is a statistically significant correlation between a company's profit margin, deposit interest rate, loan growth rate, loan-to-deposit ratio, credit monitoring and follow-up, and the type of its business. The exchange rate and inflation rate, on the other hand, were discovered to be statistically not significant.

As per the knowledge of the researcher, there has not been much research which is conducted on assessment of asset quality management practice using the data after the year 2020 so the current impact of the determinants on NPLs is not studied. Moreover, social impact of the political unrest on asset quality is not addressed.

1.4. Research Questions

This study was intended to answer the following questions

1. Does risk assessment and due diligence practice affect asset quality of the bank?
2. Does lending interest rate affect asset quality of Berhan bank?
3. Does unsecured loan affect asset quality of Berhan bank?
4. To what extent political unrest affect asset quality of Berhan bank?

1.5 Objectives of the study

1.5.1 General Objective

The general objective of this study was to assess asset quality management practice of Berhan bank.

1.5.2 Specific Objectives

In line with the general objective, the researcher proposes to assess the following specific objectives;

I. To assess risk assessment and due diligence effect on asset quality of Berhan Bank
II. To identify the effect of lending interest rate on banks asset quality of Berhan Bank.
III. To assess the impact of unsecured loans on banks asset quality of Berhan Bank.
IV. To identify the impact of Political unrest on banks asset quality of Berhan Bank.

1.6 Significance of the study

Understanding the factors that reduce asset quality of the bank will have beneficial for bank management to give due emphasis on the management of these identified variables and provides them with understanding of activities that will enhance their loan performance. This is due to the fact that knowing the variables that determine the nonperforming loan will help the bank manager to concentrate on the quality of loan rather than its quantity.

Furthermore, the outcomes of the study may narrow the literature gap in the area of study particularly in Ethiopia and serve as a source of reference for other related research works in the future.

1.7 Scope of the Study

The geographical scope of the study was Berhan Bank S.C. located in Addis Ababa. The researcher selects this area of study due to the bank's head office being in Addis Ababa in terms of resource availability and the majority of loans concentrated on Addis Ababa branches. The study was restricted to Berhan bank head office employees and Addis Ababa branch managers who worked directly in loan administration as part of their daily operations. The data used in the study covered only the period 2018-2022.

1.8. Limitation of the Study

The study is limited to a single bank out of many commercial banks in Ethiopia. It would have better results if a study had been made on all commercial banks in the Ethiopian banking industry. However, the nature of the research title depends on the bank's risk appetite, lending culture differs from one bank to another. Moreover, only specific factors are included in the research due to the data availability and confidentiality nature of credit documents.

1.9. Operational Definition of Key Terms

Loans and Advances : means any financial assets of a bank arising from a direct or indirect advance or commitment to advance funds by a bank to a person that are conditioned on the obligation of the person to repay the funds, either on a specified date or on demand, usually with interest (National Bank of Ethiopia, 2008).

Nonperforming loans: loans or advances whose credit quality has deteriorated such that full collection of principal and/or interest in accordance with the contractual repayment terms of the loan or advances are in question; or when principal and/ or interest is due and uncollected consecutive days or more beyond the scheduled payment date or maturity (National Bank of Ethiopia, 2008).

Impaired Loan: A loan is considered to be impaired when it is probable that not all of the related principal and interest payments will be collected (KPMG, 2019).

Credit risk: it is the risk that a financial contract will not be concluded according to the agreement. It is the risk that the counterparty to an asset will default (KPMG, 2019).

1.10. Organization of the Study

The research is organized into five chapters. The first chapter deals with introduction of the study. The second chapter presents the theoretical and empirical review of the related literatures. The third chapter presents design and methodology of the study. The fourth chapter is concerned with summary of analysis and discussion of the result. Finally, the fifth chapter presents conclusions and recommendations of the study.

CHAPTER TWO

RELATED LITERATURE REVIEW

2.1 Introduction

This chapter highlights the existing literatures related to the research problem; different people at different country assess the practice of asset quality management on the overall economy. Furthermore, theoretical foundation of the study relating to asset quality is discussed. Following this, empirical studies are reviewed by focusing on factors that deteriorate asset quality are presented.

Literature has been argued that macro-economic variables are considered as external factor and bank specific variables considered as internal factors that deteriorates asset quality. (Saqib Muneer, 2017) State the reasons of internal factors are management improper decisions and lack of technologies. And also, external or macroeconomic factors are not controllable by management of banks and are caused by external matters like government policies and decisions.

2.2 Theoretical Concepts

Asset quality refers to level, distribution, trend and severity of asset classifications, the level, composition, and trend of past due, non-accrual, and non-performing loans, the adequacy of provisions for bad debts and the demonstrated ability to administer and collect problem credits and general economic environment (ChidoMakomeke, 2016).

2.2.1 Information Asymmetry Theory

Information Asymmetry Theory says to occur asymmetric information one party in a transactional relationship is more informed about the transaction than the other party. (Stiglitz, 2002) also reveals that information asymmetry occurs when people with different characteristics and goals knew various information at different levels. Asymmetric information literatures look at the impact of decisions based on the difference in the information available to both parties. Each individual carried out the decision-making process which requires information that is relevant to the problem they face. Information asymmetry occur when one party has more information than the others. The more enclosed the information is, the more difficult it is for other parties to know the existence of the information. Moreover, parties who only get limited information tend to find it difficult to make an accurate decision. In a banking sector, management as the creditor requires information relating to the debtor before signing the credit agreement (Stefano and Dewi, 2022). It is difficult to assess the creditworthiness of the borrower as lenders offering credit facilities to borrower's face uncertainty of loan repayment, as they cannot observe the characteristics and actions of the borrower (Ariccia, 1998). Subsequently, informational asymmetries cause adverse selection, also known as the "lemon Principle" and moral hazard problems (Akerlof, 1970).

2.2.2 Adverse Selection Theory

Martha (2017) shows that information sharing reduces adverse selection by improving banks information on credit applicants. The theory of asymmetric information states that it may be difficult to distinguish creditworthy from bad borrowers, which may result into adverse selection and moral hazards problems. The theory explains that in the market, the party that possesses more information on a specific item to be transacted (in this case the borrower) is in a position to negotiate optimal terms for the transaction than the other party (in this case, the lender). The party that knows less about the same specific item to be transacted is therefore in a position of making either right or wrong decision concerning the transaction. Adverse selection and moral hazards have led to significant accumulation of non-performing loans in banks.

This theory is related to this study and its helps this study in relation to providing appropriate information about borrowers, loan purpose and others and their adverse consequences. The idea underlying this model is that borrowers do not always provide the entire information required even if they do not all information will be correct. In general, borrowers have private (internal) information about their projects that are more accurate than the information possessed by lenders. In consequence, a lender could still be unclear about the default risk of a loan contract and has difficulties in assessing and controlling the nature and behaviour of the borrower. The adverse selection problem happens if lenders attempt to safeguard themselves against default risk by setting their contractual terms in a manner appropriate for the expected average quality of their loan applicants.

Normal interest rate charged to all borrowers to reflect pooled experience, if lenders cannot distinguish good from iniquitous borrowers (Evans, O., Leone, A. M., Gill, M., and Hilbers, P, 2000). Barron, J.M., and Staten, M.E., (2008) Pointed out that, if this rate is higher than good borrowers can afford, it will push some good borrowers out of the borrowing market, forcing banks to charge higher rates to the remaining unqualified borrowers. As a result, adverse selection leads high-quality borrowers are displaced by low-quality borrowers, which in the long run cause deterioration in the overall quality of bank loan portfolios and lead to accumulation of non-performing loans (Bofondi, M. and Gobbi, G., 2003). Consistent with adverse selection, bank managers also may lack the ability to underwrite, manage credit risk and manage operating costs; this phenomenon is linked to Bad Management Hypothesis.

2.2.3 Moral Hazard Theory

In the banking sector, moral hazard concept is variety of principal-agent problems. Bank managers undertake risky decision to gain an incentive because they stand to gain a large portion of upside risk (profits, bonuses, market share) and a small portion of downside risk on their part, but high downside risk to depositors and shareholders (Jensen, M. C., and Meckling, W. H., 1976). Bank managers facing capital burden tend to react to moral hazard incentives by disbursing high-risk loans at a high interest rate with the view of high interest rate will boost profits and raise capital. To the contrary, high level NPLs result from high-risk loans, as high interest rates may have similar adverse incentive to borrowers. Decision made by bank management for major change for balance sheet items like bank size, loan growth, asset growth, deposit growth and capital adequacy ratio which are linked to bank management behavior and moral (Kingu, 2018).

The theory holds that there can be problems with enforcement of the loan contract. This implies that borrowers may fail to repay their loans even when they have the capacity to do so. According to the theory, higher interest rates are likely to lead to the problem of debt burden. This theory suggests that lenders will stop from raising interest rates beyond a certain level. The theory also shows the aspect of collateral and borrower returns. It states that borrowers who have greater wealth to serve as collateral are bound to obtain credit at lower interest rates (Aghion, P., & Bolton, P., 1997). The theory holds that the interest rate is likely to be closely linked to borrower characteristics such as wealth or capacity to post collateral. It is further pointed out that the poor people cannot credibly abstain from morally hazardous behaviour as effectively as the wealth people (Dasgupta, P., & Ray, D., 1986).

Moral hazard theory can enable commercial banks to peg interest rates on loans that borrowers will not voluntarily default in loan repayment. The theory shows how practitioners can give borrowers incentives not to default in loan repayment by servicing their loans according to the agreed terms and conditions such as the period within which they are supposed to repay the loans advanced to them (Mwambia, 2016).

2.2.4 Management Behavior Theory.

Berger, A. N., & DeYoung, R., (1997) describe banking condition affected by the management behavior theory, mainly related to non-performing loans. The study produced four hypotheses: skimping hypothesis, bad luck hypothesis, bad management hypothesis, and moral hazard hypothesis. (Stefano and Dewi, 2022) explains that the skimping hypothesis, bad luck hypothesis, and bad management hypothesis represent the relationship between the efficiency of bank performance and nonperforming loans, while the moral hazard hypothesis represents the relationship between bank capital and non-performing loans. In the skimping hypothesis, banking companies that do savings tend to appear with good performance. In fact, these savings are only useful in short term, thus ignoring credit management in the long term (Khan, M. A., Siddique, A., & Sarwar, Z, 2020). The bad luck hypothesis explains that there are events outside of the bank that cause banking companies to spend more than they should, so that it has an impact on nonperforming loans. The bad management hypothesis describes a situation where a bank with poor management causes the supervision carried out on credit management to not be effectively conducted, thus triggering an indication of non-performing loans. (Berger, A. N., & DeYoung, R., 1997) points out that in responding to the increase in non-performing loans resulting from adverse selection, bank management tends to inject more resources into managing and monitoring bad loans, which in the long run results in an increase in operating expenses over the interest income. (Sarita, R., & Zubadi, H, 2018) explain that poor corporate governance performance and poorly organized management lead to greater credit risk.

2.2.5 Agency Theory

The relationship between principals and agents are described by agency theory. The agents receive a general authority to manage the company he owns where the agent is expected to achieve goals that are in line with the principal. (Jensen, M. C., and Meckling, W. H., 1976) describe that agency theory is characterized by the granting of authority from principal (shareholders) to the company's management as agent with the aim of emphasizing the relationship between the parties involved in order to prevent excessive agency costs and minimize asymmetric information. The company management as agent must strive as much as possible to achieve the company's goals, including maximizing shareholder's wealth while also increasing company value. In exchange, management receives compensation in the form of rewards for their completed work. Agency problem occur when mistakes made by agents might trigger losses in the company caused by differences in interest between agents and principals (Eisenhardt, 1989). When agency problem occurs, the company's overall performance will begin to slow down and eventually deteriorate due to poor management. Regarding the aspect of asset quality, the management of banking companies through credit management will analyze and evaluate prospective borrower before accepting credit applications and evaluate their compliance in fulfilling their future obligations. The financial condition and characteristics of the bank significantly affected by the performance of bank management (Prawira, R., & Wiryono, S. K., 2020).

2.2.6 Credit Assessment

The first stage in creating a solution specifically for the needs of the customer is credit assessment. To ensure that the supporting solution is a good fit for the customer's needs and capabilities, the assessment begins with an awareness of these factors. Credit assessment, which is regarded as a crucial component of credit risk management, is the most significant precaution to assure the underlying quality of the credit being issued (Cade, 1999).

The ability and willingness of the borrower to fulfill the obligations of the facility issued are often referred to as the exposure's credit quality. Additionally, default probability and expected recovery rate are included (Saunders A & Cornett MM, 2003). Thus, credit evaluation entails evaluating the financing risks and estimating the likelihood of default and recovery rate.

The credit official does a credit analysis to assess a borrower's character, capital, capacity, collateral, and the cyclical nature of the economy, or the "five C's" (Strischek, 2000). The next section goes into great detail on this model, which is also known as the "five C's."

The Five C’s of Credit

The traditional credit analysis procedure utilized by the early banks is not significantly different from the procedures used today (Caouette JB, Altman EI & Narayanan P, 1998). The five C's have been around for almost 50 years and are regarded as the foundational elements of successful lending. At first, just character, capital, and capacity were taken into account.

However, conditions and collateral were added over the course of the year. These gave rise to an even more thorough knowledge of the underlying risk and the ensuing lending decision (Sinkey, 2002).

(Murphey, 2004) contends that these guidelines ought to serve as the basis for all lending decisions. Following is a discussion of the five C's:

Character:

Character is the borrower's reputation and willingness to repay debts, respectively. The borrower's honesty, integrity, and dependability are considered when analyzing the appeal. Additionally assessed are the borrower's credit history and the owners' dedication (Rose P. , Commercial Bank Management, 5 th edition., 2002). The reputation of a business, specifically with regard to credit, is based on prior success. A borrower has established a solid reputation or credit history if previous obligations were met on time and were timely repaid (observed conduct). Character is seen as being the most significant and yet the most challenging to evaluate (Koch & MacDonald , 2003).

Bankers are aware of how crucial management is to a company's success. One method of evaluating character has been to critically analyze management quality. A company's history and management expertise are important considerations for determining its capacity to meet its financial responsibilities.

The reputation, honesty, qualifications, experience, and management skills of several business disciplines, such as finance, marketing, and labor relations, are taken into consideration when evaluating the quality of management in the particular organization (Sinkey, 2002).

If a banker views these qualities favorably, they can be viewed as risk mitigants. In actuality, effective leadership is largely responsible for its success. Businesses with strong and capable management teams typically endure economic downturns.

Contrarily, privately owned businesses are typically run by their proprietors. In this situation, succession planning is required because management is still essential to the survival of the business (Koch & MacDonald , 2003).

Capacity:

The term "capacity" describes a company's ability to bring in enough money to pay off its debt. The applicant's business plan, controlling accounts, and cash flow forecasts—which demonstrate the need for and ability to repay the commitments—will be examined in order to provide a good indication of the applicant's capacity to repay (Sinkey, 2002; Koch & MacDonald , 2003).

Evaluating the nature of the business and the sector in which it operates is essential for gaining a thorough grasp of a company's capacity. It is important because different internal and external factors have an impact on every industry. The following criteria serve as the foundation for this analysis: industry type, market share, product quality and life cycle, labor or capital intensity of the firm, present economic conditions, seasonal trends, bargaining power of buyers and sellers, competition, and legislative changes (Koch & MacDonald , 2003). These elements influence how the banker perceives the particular business and sector. If the banker has faith in the company and industry and believes that both have bright futures, he or she would view this as a possible risk to be mitigated.

Additionally, a crucial sign of a company's capability is its financial status. By analyzing the past and anticipated financial performance, the financial position of the company is analyzed. The audited financial statements of a corporation show its historical financial performance (Koch & MacDonald , 2003). Financial projections include predicted cash flows that show the facility's intended use and ability to be repaid (Sinkey, 2002). For data analysis, it is necessary to have balance sheets and income statements that have undergone an audit for at least three years. The study is performed using a financial spreadsheet.

The Moody's Risk Advisor is used by commercial banks to apply the monetary spread (i.e., audited financial statement analysis and ratio computations - DuPont). Additionally, the model compares itself to other models and determines the probability of default (Koch & MacDonald , 2003).

When evaluating a company's position, the following financial ratio evaluations are crucial (Koch & MacDonald, 2003):

- **Liquidity ratios** show how well a corporation can pay its immediate debts.
- **The current ratio** is determined by dividing current assets by current liabilities, according to (Conradie WM & Fourie CMW, 2002)
- **Activity ratios** show how effectively assets are utilised to produce sales.
- **Leverage ratios** show the company's financial mix of equity and debt as well as prospective earnings volatility. The likelihood that the borrower would be unable to make the interest and principal repayments rises when earnings volatility is at its highest.
- **Profitability ratios** provide data on the performance of the company's sales and earnings.

Once the ratio analysis has been assessed, it is necessary to perform the cash flow analysis. . The cash flow analysis allows the banker to distinguish between reported accounting profits and cash flow from operations. The cash flow from operations reveals how much money is produced by typical corporate operations. The cash flow generated must be enough to maintain the banking infrastructure (Sinkey, 2002; Koch & MacDonald, 2003). These assumptions are compared to the company's historical performance, industry averages, and anticipated economic developments (Nathenson, 2004).

A trend analysis should always be a part of a financial capacity assessment of a company. A good picture of the direction a corporation is moving in can be obtained by analyzing trends over a three to five-year period. Always compare ratio results to a peer group or an industry comparison. Is the company accumulating more quickly or more slowly than the rest of the sector? Is this business more successful than others that are similar to it? Making the most of ratios in this regard by contrasting the company with its competitors using accepted standards is crucial. A more realistic comparison is made when the company is compared to businesses in the same industry, region, and staff size.

The predictions also show what kind, how much, and for what purpose money is needed. Additionally, it reveals if the business can produce enough cash flow to pay its debts (Murphey, 2004; Nathenson, 2004). Banks must make sure that the form of funding matches the financing goal (Rose, 2000).

In order to ascertain whether an insolvent would be able to timely pay debts, analysis of the organization's financial capability should also be done. Its capacity to pay might be even more crucial. It is crucial to comprehend the distinction. Monitoring customer payment patterns over time is a great way to determine cash flow. It is crucial to examine bank and trade references, as well as any open legal cases or potential obligations. It is crucial to perform additional parent business relationship checks because a parent firm's guarantee can be accessible. Inter - company loans may have an impact on financial stability. Before concluding the investigation into a borrower's capacity, agency ratings that predict late payments or default should be conducted.

Capital:

Capital is the owner's percentage stake in the company (Sinkey, 2002). Banks prefer that owners shoulder a fair amount of the risk. Although there are no strict guidelines, a debt-to-equity ratio of 50:50 would be adequate to reduce the bank's risk when funding (unsecured) is dependent on the company's ability to pay back the funding (Harris, 2003).

Lenders favor notable equity (own investment), which shows an owner's dedication to and faith in the enterprise.

Conditions:

Conditions are uncontrollable events that may have an impact on a borrower's capacity to pay back the loan. Before making a choice, lenders consider the general economic and industry trends, as well as any regulatory, legal, and liability considerations (Sinkey, 2002). Once financing has been granted, it is typically subject to terms, covenants, and restrictions that are particularly relevant to the approved facility's compliance (Leply, 2003).

To safeguard the bank's interest, banks typically offer credit facilities subject to terms and agreements. Agreements' main purpose is to act as an early warning system (Nathenson, 2004). Before any money is provided, conditions often state that all of the collateral pertinent to the loan must be in order.

Collateral:

The assets that the borrower provides to the bank as collateral (also known as security) help the bank reduce its risk in the event of a default (Sinkey, 2002). It is a valuable item that the borrower pledges to the bank as security for their intention to pay back the loaned funds. (Rose and Hudgins , 2005) describe secured lending in banks as the activity when the secured loans have a promise of part of the borrower's property (such as home or automobiles) overdue as collateral that may have to be sold if the borrower defaults and has no other means of repaying the lender.

By raising the likelihood that the lender will be able to recover the debts owed by the borrower, security serves to lower the risk of extending credit. Credit is more readily available and has better terms when there is security in place. The lender's willingness to lend is affected by the offer of security, which also alters the terms under which he is willing to do so. Typically, these modifications involve raising the loan amount, extending the loan's term, and subsequently lowering the interest rate (Norton, J & Andenans, M., 1997).

In the banking environment, security is necessary for the following three reasons, according to (De Lucia, R. & Peters, J, 1998):

- to ensure the borrower's full commitment to its operations;
- to provide safety should the borrower deviate from the planned course of action outlined at the time credit is extended;
- to provide insurance should the borrower default.

Based on the expected resale value of the item at the time of disposal, the security value of an asset is determined (McManus, 2000). For security reasons, the bank values the particular type of property to estimate its market value (Rose, 2002).

In addition to the actual collateral, a third party can guarantee the borrower's loan. The bank will then request payment from the surety if the borrower is unable to repay the debt (Koch & MacDonald, 2003). When money is loaned to a firm, it is standard banking procedure for the banks to demand surety ships from the owners and directors (Rose, 2002).

Commercial banks have created their own qualitative credit risk assessment models to determine whether they will accept to lend money to a particular company based on the C's, which are well-known byline assessment criteria (Sinkey, 2002).

Credit monitoring is carried out based on the borrower's credit information and credit assessment, which is done using a quantitative or qualitative model (using the five C's) or a combination of both. The section that follows discusses the credit approval process.

A person's or a company's credit history is tracked, and the credit office informs individuals who inquire about it about the company's credit history, leases, unrelated debts, financial-related public records, and questions about the individual's credit history.

Bank officers start the credit analysis or assessment process as soon as credit on the loan request is acquired.

Credit Analysis Process

The first step in creating a solution to match the customer's demands is credit analysis, which starts with analyzing the customer's wants and capabilities to determine whether there is a financing option. Credit assessment, which is regarded as a crucial component of credit risk management, is the most significant precaution to assure the underlying quality of the credit being issued (Goosen et al, 1999). Additionally, default probability and expected recovery rate are included (Saunders A & Cornett MM, 2003). Thus, credit evaluation entails evaluating the financing risks and estimating the probability of default and recovery rate.

Credit Approval process

Extending credit involves maintaining a precise balance between reducing risk and increasing profitability while preserving a competitive edge in a challenging, international market. The process of selecting whether or not to grant credit to a certain consumer is known as credit approval. A qualitative review of the borrower's request and a quantitative analysis of the financial information presented make up the credit analysis procedure.

The effectiveness of the credit approval procedure is demonstrated by the thorough disclosure of the risks involved in loan granting and an adequate assessment of these risks. There cannot be a standardized process to evaluate credit risks due to the vast variances in the characteristics of different borrowers and the assets to be funded, as well as the volume and complexity of products (Khemraj and Pasha, 2009).

The most accurate identification and assessment of the credit risk arising from a potential exposure determines the quality of the credit approval procedure from a risk standpoint. Saunders and Cornett ,(2003) state that the probability of default (PD), loss given default (LGD), and exposure at default (EAD) are the three risk factors that can be used to disperse the credit risk.

i) Probability of default (PD)

The probability that the company will stop making payments during the facility's term is known as the default probability. Examining a borrower's present and potential ability to meet its interest and principal repayment obligations essentially determines the borrower's probability of default.

ii) Loss given default (LGD)

The amount of exposure that might materialize in the case of a default is known as exposure at default. In the event of a default, it discusses what percentage of the exposure may be recovered through bankruptcy procedures or through another type of settlement. Both the collateralized portion and the cost of selling the collateral have an impact on the loss assuming default. Therefore, when creating the processes for approving loans, the calculated value and kind of collateral must also be considered.

iii) Exposure at default

The amount still owed to the institution is the exposure at default. As a result, in addition to the kind of claim, the amount of the claim is a crucial consideration in the credit approval process. Once the information is gathered, the business must make the difficult decision of whether to offer credit or not.

Loan Follow Up or Credit Monitoring Process

The decision to lend money is based on a careful examination of the credit risk and evaluation of the borrower's creditworthiness. A loan that was approved based on careful study could fail if the borrower failed to comply with the loan contract's terms and conditions. A loan that has been approved based on careful study could fail if the borrower fails to fulfill their commitments in accordance with the loan contract's terms and conditions. This makes adequate monitoring and follow-up absolutely necessary. Following up or monitoring focuses on the crucial elements listed below;

i) Ensuring that terms and conditions are followed;
ii) Monitoring the final use of funds allowed;
iii) Monitoring performance to ensure that operations continue to be viable;
iv) Finding deviations from the terms of the decision;
v) Periodically evaluating the health of the loans and advances using some of the key performance indicators, such as profitability, activity level, and management of the unit, and ensuring that the assets created are effectively used for productive purposes and are well maintained;

vi) Ensuring recovery of the principal and interest installments in the case of a term loan as per the schedule.

2.3 Empirical Literature review

- **Credit Growth**

The effects of credit growth range greatly and vary among banking industries. Because of its characteristics, it has both effects on banks. It is regarded as a reliable sign of the stability of the financial industry (Jakubik, Petr, and Bogdan Moinescu, 2015)

Various factors contribute for rapid growth of the credit. (Saqib Muneer, 2017) Cited as (Keeton, 1999; Klein, 2013) describe growth in credit implies increasing credit portfolio by banks that can determine the occurrence of NPAs. Reduced interest rate contributes for growth of credit and poor credit standard of loan lead to an increase of NPAs (Klein, 2013). As suggested by (Louzis, 2012), (Vatansever, M., &Hepsen, A., 2013) & (Ofori-Abebrese, et al, 2016) credit growth does not have significant impact on the occurrence of NPL. Other findings by (Yam, 2016) suggested that growth in credit negatively impact NPAs. It indicates that banks have better risk management procedures and technology and higher credit standards which may end up lower levels of NPAs. The findings also reveal that credit growth support by economic growth because of borrowers invest into profitable projects and can pay loan due to their sufficient earnings and hence decrease the levels of NPAs.

The variable discussed the growth of rate in different period of time and country, the study of (Keeton, 1999) shows relationship between loans and speedy credit growth. The author has used a vector auto regression model on commercial banks in United States for the periods 1982-1996. Empirical studies show that lenient credit terms is one of the factors which increases NPLs. To expand credit, banks have to ease the standards of credit terms, monitoring of borrowers and decrease the interest rates (Keeton, 1999). (Sarlija, N., & Harc, M., 2012) study indicates that in case of developed countries, lending is at a much rapid speed. A study by (Jimenez et al, 2006) points out that herd behavior, morale hazards, agency problems, and catastrophic shortsightedness are the underlying factors behind generous credit terms. In addition, they associated generous credit terms with bad debt. When the economy strengthens, bank management shows generosity in lending. This is because less credit expansion means less income, indicating poorer performance.

- **Loan Loss Provisions**

Banks use provisions to cover different kinds of loan losses like NPLs, customer bankruptcy, etc. However, its minimum portion is consumed in NPLs as the banks have significant NPLs each year (Makri Vasiliki, 2014). One of an indication of management inefficiency is described by higher loan loss provision. And it often is positively associated with actual losses. Banks with poor credit quality are exposed to higher risk in their loan portfolio that results higher NPLs (Beck et al, 2015).

- **Bank Diversification**

The two major sources of income in banks are classified as interest and non-interest income. Interest can be earned by different types of loans and investment securities, while non-interest earnings are from fee and commission-paying services. Income diversification from interest income to non-interest income is vital in the modern banking system (Chen, 2006).

Among various incomes excluding interest income and exerting effort to increase other banking services is referred to as income diversification (Stefano, 2022). (Ismail N. A., 2017) discovered that there is a positive relationship between non-performing loans and income diversification due to the more sources of income other than interest, finally, the bank does not fully concentrate on the credit sector, thereby increasing nonperforming loans. However, the research conducted by (Louzis, 2012) analyzed that income diversification harms non-performing loans. The researcher strengthens his analysis that banking that has high-income diversification are less vulnerable to risk-taking and have lower non-performing loans. The research conducted by (Rachman, 2018) states that income diversification does not affect nonperforming loans because the bank's efforts to earn profits by excluding interest income are not related to credit policies

- **Operating Efficiency**

Lending includes all lending-related activities such as sales, customer selection and screening, application and approval processes, repayment monitoring, default and portfolio management. It also relates to the institutional structure of the credit process. Loan quality is one of the most important determinants of a financial institution's efficiency, influence and profitability. Proper loan preparation and product mix is therefore one of the most difficult and challenging tasks for any financial institution (Nkusu, 2011). Average Gross Loan Portfolio (Samuel, 2015) found that the cost-to-income ratio coefficient, which provides information about firm efficiency in terms of cost to income, is negative and statistically significant at the 1% significance level (p-value = 0.0000). I found this variable is a key determinant of Ethiopian bank profitability. This shows that minimizing costs for commercial banks in Ethiopia will certainly improve their performance in general and their profitability in particular.

- **Bank Size**

Bank size is described by total assets. Bank asset is one of the factors that have been observed to be related with asset quality or NPAs. In the literature, this relationship is explained in terms of large banks with diversified loan portfolios and the ability to absorb non-performing loans (Dietrich, A., &Wanzenried, G., 2011). On the contrary, (Abid, L., Ouertani, M. N., &Zouari-Ghorbel, S, 2014) found that bank wealth positively affects NPA. (Alexandri, M. B., &Santoso, T. I., 2015) suggest that bank assets are not linked to the NPA.

- **Bank Profitability**

Hanafi, M. M., & Halim, A. ,(2018) explain that profitability through ROA analysis measures the company's ability to generate profits by using the total assets owned by the company after adjusting for the costs to fund these assets. Research conducted by (Lee, Y. Y., Yahya, M. H. D. H., Habibullah, M. S., & Ashhari, Z. M, 2020) revealed banks' profitability and non-performing loans have a positive relationship because of short-term reputation, banking companies tend to increase profitability by ignoring credit policies and changing current earnings. This will increase non-performing loans and have an impact on decreasing the company's performance in long term. on contrary, (Khan, M. A., Siddique, A., & Sarwar, Z, 2020) conducted research where profitability harms nonperforming loans because good bank performance and productive management lead to increased profits and will have an impact on decreasing non-performing loans. Ismail N. A., (2017) Shows that profitability does not affect non-performing loans. This is because although the increase in profitability indicates that the company has good performance efficiency in managing its assets, the bank's overall performance may experience a decline where income-generating capabilities do not have a strong influence on credit management.

- **Exchange Rate**

According to Castro, (2013), there is a positive and statistically significant relationship between exchange rates and NPAs. The loan payment capacity of export-oriented firms can be significantly affected by the appreciation in exchange rates (Fofack, 2005). Muneer, S., Ahmad, R. A.&Ali, A.,(2017) further strengths that it can also positively affect the loan payment capacity of those borrowers who borrow in foreign currency. On contrary, different findings point out that there is no relationship between exchange rate and NPAs because borrowers lend money in local currency so the exchange rate conversion between the local currency and US dollars does not affect the NPAs (Washington, 2014).

- **Gross domestic product (GDP) growth rate:**

Important empirical exhibit a significant of a negative correlation exists between real GDP growth and NPLs (Apan, M., & İslamoğlu, M., 2019). The main reason given in the literature for this correlation is that the significant positive GDP growth rate typically results in more revenue that increases the borrowers' repayment capacity, which in turn leads to lower NPLs. Contrarily, if the economy slows down and relatively low GDP growth, the level of NPLs is expected to rise.

Asset quality Management practice

- **Risk assessment and due diligence on banks NPLs.**

Non-performing loans arises from the loss of credit ratings and rating objectivity. The problem is worsened by vulnerabilities in accounting, disclosure and additional financing. Assessment of outstanding loan status does not take into account the borrower's creditworthiness and the market value of the collateral, making it difficult to identify non-performing loans (Patersson, 2004). Therefore, the deterioration of the quality of risk assessment leads to the occurrence of non-performing loans.

This hypothesis was created to ascertain the effect of bank efficiency on bad debt levels in the banking industry. The proposed justification behind this hypothesis is poor management with inadequate skills in credit evaluation, pledged collateral valuation, and borrower monitoring. Such bank managers do not follow standard credit monitoring, control and underwriting practices. Therefore, as "bad managers", they have poor credit evaluation, collateral evaluation, and credit monitoring and management skills. If managers are inefficient in managing current banking operations, this will lead to an increase in bad debts in the future (Berger, A. N., & DeYoung, R., 1997).

A study by (Ning, 2007) found that banks rely on personal experience to lend, rather than historical data, sophisticated loan portfolio management skills, and centralized information systems. Banks need access to their customers' credit information so that they can reduce their bad debts. In this regard, the bank's responsibilities should be clearly defined. Banks should ensure that they apply effective policies and appropriate risk management (Basel, 2001). A study by (Podpiera, J and Weill, L., 2008) empirically examines the relationship between poor credit risk management and non-performing loans. They conclude that there is strong evidence for the bad management hypothesis, suggesting that emerging market regulators should focus on management performance to improve financial system stability by reducing non-performing loans.

- **Lending interest rate on banks NPLs.**

The lending interest rate is one of the key terms in the financing structure and one of the crucial determinants of NPLs. Interest rate limits the ability to service debt, while an increase in interest rate repayments may increase the occurrence of NPLs (Atoi, 2018). Contrary to these findings, NPLs diminish by reducing interest rates that cause bank earnings also decrease. (Siddiqui, 2012) find that the volume of non-performing loans is determined by instability in interest rates in the Pakistani banking sector.

Bredl, (2018) identified lending rates as one of the factors that cause NPLs which is in line with a theory of adverse selection. Good borrowers are pushed out of the market due to raised interest rates, as they will not be willing to pay more than market rates. Commercial banks attract low-quality customers who are usually happy to pay higher interest rates on extremely risky loans, thereby raising the likelihood of default. Findings by (Kjosevski, J., & Petkovski, M., 2020) have shown a strong relationship between NPLs as well as the interest rate for lending. Loans at higher interest rates are costly for companies that result in profit margins for businesses are strained. Corporations may be financially at risk and default on their loans in such a situation. To overcome the interest payment burden on the company’s interest rate reduction is necessary, which leads to an expansion of their profit margins. As a result, businesses are becoming financially sound and are therefore more likely to pay back their loans on time.

- **Unsecured loans on banks NPLs.**

Nduruhu, (2016) describe unsecured loans affected the financial health of commercial banks. It was concluded that banks charged a higher interest rate on unsecured loans than on secured loans. Study of the financial statement of banks indicates that unsecured loans have a direct effect on asset quality and profitability of banks. This is because charge for loan provision is treated as expenses on the profit and loss account and as such impact negatively on the profit position of banks (Price Water-House Coopers, 2009).

- **Political unrest on banks NPL**

The political situation of a country is a critical factor affecting on NPLs and working of banking system. A number of studies, such as (Boudriga, 2009) have demonstrated that organizational climate and political uncertainty have a strong impact on non-performing loan ratios. Similarly, (Wheelock, D. C. and P. W. Wilson, 2000) pointed out that banking sector management, especially in developing countries, is influenced by a variety of social and political interest groups. In these situations, loans are granted on a political rather than performance basis. Ultimately, these loans are not used productively and are not properly repaid. (Crane et al. , 2006) examined various policy factors leading to non-performing loans in different countries. He said weak judicial power, bureaucracy, and poorly implemented credit policies were seen as the most important factors behind the rise in non-performing loans and a major cause of bank failures.

CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction

This chapter presented the research methodology that was used to carry out the study, which is broken down into the following main sections: research approaches, research designs, population and sampling.

3.2 Research approach

A qualitative research approach, according to Relacion (2017), uses qualitative data to study and characterize asocial phenomena, such as interviews, records, and questioners. A quantitative research approach, on the other hand, entails the process of gathering numerical data in a predetermined manner and utilizing statistical methods to draw conclusions from it (Apuke, 2021). The student researcher was ultimately persuaded by these elements to use the quantitative research strategy.

3.3 Research design

The research design, which also serves as the guide for gathering, measuring, and analyzing data, is the conceptual framework for research. Additionally, it represents the methods and arrangements made for gathering, analyzing, and interpreting data (Ebrary.net, 2014).

Three broad categories can be used to classify research designs. These three types of research design include exploratory, explanatory, and descriptive (Asenahabi, 2019). The student researcher used descriptive research design. Additionally, the study uses a cross-sectional (one-time) survey method that is carried out using written questionnaires. This approach is also preferred due to its quick data collecting and low cost.

3.4 Targeted population

The elements that belong to the target population are those that have the information needed by the researcher to support the study (Oso, W.Y., & Onen, D, 2005). However, the study's focus is on the population, which is each individual participant or entity being measured (Willie, 2022). According to (Cooper and Schindler , 2011), researchers can save a significant amount of time and money by using samples, and they can also obtain more specific information that would not be available otherwise. The study's population was concentrated on employees who directly handle credit processing, manage a portfolio of non-performing loans, and make decisions. Therefore, the total population is 74, which involves 36 employees from credit department, loan portfolio management department, finance department, and risk departments and the remaining 38 from Addis Ababa city branch managers were included.

3.5 Sampling technique

The major objectives of this research, as mentioned at the objectives section, were to assess asset quality management practice of Berhan bank. The seventy-four staff members were considered as the populations/universe of the study.

3.6 Sample size determination

One approach to determine a sample size is to use the entire population as the sample. Although cost considerations make this impossible for large populations, it will come in handy for the population of 200 or less. In this particular research, the student researcher used the entire population of study as a sample size.

The sample size will be;

$n = 74$

3.7 Data collection

This study was utilizing primary source to collect the data. It includes an available data, the researcher will refer the data which are already been collected and analyzed by someone else (Kothari, 2004). This study also used primary data by using structured questionnaire used to collect the data for obtaining information from respondents.

3.10 Data analysis methods and model

3.10.1 Data analysis and interpretation

After the collection of data through the primary data source, the student researcher was proceeding to the data analysis and interpretation. The collected data were encoded and processed with SPSS software after the raw data was well organized with a proper format. Using a table, the data were analyzed based on descriptive statistics by SPSS version 23 software.

3.11 Validity and reliability

Validity of research can be explained as an extent at which requirements of scientific research method have been followed during the process of generating research findings. (Oliver, 2006) considers validity to be a compulsory requirement for all types of studies. Reliability is a measure of the degree to which a research instrument yields consistent results or data after repeated trials (Mugenda & Mugenda, 2003).

3.11.1 Reliability test

According to Zikmund, Babin and Griffin (2010) scales with coefficient alpha, which determines the internal consistence reliability, is between 0.8 and 0.95 are considered to have very good quality, whereas, scales with coefficient alpha between 0.7 and 0.8 are considered to have good reliability, and finally, coefficient alpha between 0.6 and 0.7 indicates fair reliability.

The Cronbach alpha calculated for all the independent variable is summarized with the table below. Based on the rules stated above, it can be shown whether the measurement has an internal consistency or not.

No	Categories	No of item	Cronbach's Alpha	status
1	Risk assessment and due diligence	18	0.778	Good quality (Reliable)
2	Lending interest rate	4	0.827	Very good quality (Reliable)
3	Unsecured loans	9	0.743	Good quality (Reliable)
4	Political unrest	6	0.720	Good quality (Reliable)

TABLE 1. CRONBACH'S ALPHA OF THE VARIABLES -SPSS-OUTPUT

3.11.2 Validity

There are different forms of research validity and main ones are specified by Cohen et al (2007) as content validity, criterion-related validity, construct validity, internal validity, external validity, concurrent validity and face validity.

The issue of validity was addressed through the review of literature and adapting instruments used in previous research works (Vithessonthi & Schwaninger, 2008). In this research, Criterion-related validity was undertaken using statistical analysis such as correlation.

3.12 Ethical consideration

Selected participants have been informed of the study's objectives, whether or not it is appropriate for them to participate, any potential advantages of doing so, and any privacy and confidentiality concerns. They were also told that taking part in the study was entirely optional. All of the data were handled with the utmost confidentiality in accordance with research ethics to protect the respondents' right to privacy.

CHAPTER FOUR
DATA PRESENTATION, ANALYSIS AND INTERPRETATION

4.1 Introduction

This chapter captures the presentation, analysis and discussions of the result of the research work. The objective of the study was to assess asset quality management practice of Berhan bank. The chapter presents the results and findings of the study which was to establish to assess asset quality management practice of Berhan bank. The data was analyzed using descriptive analysis, were computed using the statistical software SPSS 23.

4.2 Descriptive analysis of the variables

In this section the student researcher discussed the descriptive relationship between the demography of the respondent and all the variables including the dependent variable and the independent variables.

4.2.1 Summary of questionnaire responses

All of the issued questionnaires were correctly completed and fully collected. All of the responses were useful and pertinent for carrying out the research. The total number of observations for each variable was seventy-four (74) of which 67.6% of the respondents participated in the opinion survey were found to have worked more than five years. From the respondents 20.3% have worked 3-5years and the rest 12.2% worked on the bank between one and three years. This is also an indication that the respondents have actually spent enough time in the banking sector to give proper response for the questionnaire.

Experience				
	Frequency	**Percent**	**Valid Percent**	**Cumulative Percent**
1-3 Years	9	11.5	12.2	12.2
3-5 years	15	19.2	20.3	32.4
5-10 Years	38	48.7	51.4	83.8
above 10 years	12	15.4	16.2	100
Total	**74**	**94.9**	**100**	

TABLE 2. EXPERIENCE QUESTIONNAIRE RESPONSES

The breakdown of the result is as indicated in the tables below shown 42.3% were branch managers and the rest 57.7 were credit experts and directors. Desaleg, (2015) on his research the impact of bank specific factors on non-performing loans state about his respondents that 47.7% of the respondents were branch managers and the remaining 52.3% of the respondents were credit workout officers, follow-up officers and credit analyst. This implies the respondents have high exposure on loan and credit facilities.

Position

	Frequency	**Percent**	**Valid Percent**	**Cumulative Percent**
Loan Officer	16	20.5	21.6	21.6
Credit Analyst	8	10.3	10.8	32.4
Credit Manager	2	2.6	2.7	35.1
Director	6	7.7	8.1	43.2
Monitoring/Follow up Officer	9	11.5	12.2	55.4
Branch Manager	33	42.3	44.6	100
Total	**74**	**94.9**	**100**	

TABLE 3. POSITION QUESTIONNAIRE RESPONSES

In considering gender composition of the bank, 56.4% were male and 38.5% were female. Even if majority of staff who work on credit related are male, females also have working on credit process in Berhan bank. On contrary, (Abdeta, 2015) describe on his research that majority of Development bank of Ethiopia staff on processing credits are 85.4% are males. These results indicate that respondent’s gender was not significantly affecting the result.

Gender				
	Frequency	Percent	Valid Percent	Cumulative Percent
Male	44	56.4	59.5	59.5
Female	30	38.5	40.5	100
Total	**74**	**94.9**	**100**	

TABLE 4 GENDER QUESTIONNAIRE RESPONSES

In terms of educational qualification as show in the table below indicate that 56% of respondents have first degree and the rest of respondents have second degree. This implies majority of the bank staff who involves in credit processing are highly qualified.

Education

	Frequency	Percent	Valid Percent	Cumulative Percent
Bachelor Degree	44	56.4	59.5	59.5
Second degree	30	38.5	40.5	100
Total	**74**	**94.9**	**100**	

TABLE 5 EDUCATION QUESTIONNAIRE RESPONSES

4.3 Descriptive Statistics for the research Variables

The descriptive statistics for dependent and independent variables are presented and their results are discussed below. The study uses mean and standard deviation as the optimal measurements for analysis, in light of the mean range created by (Al-Sayaad, J., Rabea, A., Samrah, 2006) of the following table.

No	Mean range option	Response option
1	1.00-1.80	Strongly agree
2	1.80-2.60	Agree
3	2.60-3.40	Neutral
4	3.40-4.20	Disagree
5	4.20-5.00	Strongly disagree

TABLE 6 MEAN RANGE (AL-SAYAAD, RABEA, & SAMRAH, 2006)

In statistics and probability theory, the standard deviation is a commonly used indicator of variety or diversity. The difference or "dispersion" from the mean (or expected value) is demonstrated. The sample mean demonstrates that the majority of responders are the most accurate population predictions.

4.3.1 Risk assessment and due diligence practice of the Bank

As per the question presented under table 8 (Q1) improper/poor clients selection and due diligence assessment (KYC) has a mean value of 1.67, shows that most of the respondent strongly agreed on the fact that improper/poor client selection and due diligence assessment were the main reasons for loan defaults. The standard deviation of 0.66 also indicated that that improper/poor client selection and due diligence assessment of the bank is close to the mean value of 1.67 on average by 0.66. This implies that client section and due diligence practice of the bank are poor and the main cause of loan default.

Description	Mean	SD
1. One of the main reasons for loan defaults and NPLs in the bank is improper/poor client selection and due diligence assessment (KYC).	1.67	0.66
2. The banks credit granting and approval process establish accountability to decision makers	3.27	1.09
3. There are situations when directors, senior managers, or other powerful bank employees may have an impact on the credit decisions and oversight of applicants.	2.16	0.88
4. The bank handles credit-processing tasks apart from the appraisal.	3.34	1.04
5. Customer make multiple borrowing in different banks	2.08	0.72
6. To identify risk exposure, the bank requires all clients to submit a business plan.	2.72	1.16
7. A poor assessment of the credit risk would result in loan default and NPL.	1.63	0.69
8. Projects that are under or over-financed will experience Loan default and NPL.	2.27	0.98
9. The bank takes applicants' prior repayment history into account.	1.96	0.76
10 Great risk appetite is the cause for NPL in the Bank	2.12	0.87

11. Quality loans are made possible by enhancing or introducing effective risk assessment mechanism.	1.99	0.82
12. No serious action will be taken against borrowers not to repay the loan	2.62	1.27
13. Borrowers default because they do not understand the credit terms well	3.45	1
14. Loan follow up is directly related to occurrence of nonperforming loans	2.24	0.89
15. Poor credit analysis is one of the major causes for loan Default/NPLs in the Bank.	1.80	1
16. Lack of contact with borrowers within the lending period.	2.31	0.89
17. Poor credit monitoring and credit collection technique is major causes for loan Default/NPLs in the Bank.	2.11	0.93
18. Weakness in credit risk assessment procedure is the cause of loan default	2.17	0.96

TABLE 7 RISK ASSESSMENT AND DUE DILIGENCE

From the above table, it can be observed that the banks credit granting and approval process establish accountability to decision makers (Q2) has a mean value of 3.27 and Standard deviation of 1.08. The result indicates that most of respondents were neutral about accountability for granting and approval practice of the bank.

The respondents asked on the situations when directors, senior managers, or other powerful bank employees may have an impact on the credit decisions and oversight of applicants. The result indicates the respondents agree with the stated situation with the mean value of 2.16. The standard deviation of 0.88 also indicated the situations when directors, senior managers, or other powerful bank employees may have an impact on the credit decisions and oversight of applicants is close to the mean value of 2.16 on average by 0.88.

The bank handles credit-processing tasks apart from the appraisal raised on Q4 has a mean value of 3.34 indicates that respondents are neutral.

As the findings indicated table 7 in Q5, the study sought to determine customer make multiple borrowing in different banks that impact asset quality of the bank. The result mean value of 2.08 shows majority of respondents agree on customer make multiple borrowing in different banks that impact asset quality of the bank. The standard deviation of 0.72 also indicated that that customer make multiple borrowing in different banks is close to the mean value of 2.08 on average by 072.

Based on the above table 7 (Q6), it can be revealed that to identify risk exposure, the bank requires all clients to submit a business plan as shown by mean 2.72 and SD 0.98.The result indicated that respondents were neutral on all clients to submit a business plan to identify risk exposure.

As shown on table 7 (Q7) respondents with 1.63 mean and SD 0.69 strongly agreed on the statement that a poor assessment of the credit risk would result in loan default and NPL. This indicates that there is poor credit assessment practice that causes loan default and NPL.

The above table shows that in Q8 respondents agree with projects that are under or over-financed will experience Loan default and NPL with the mean value of 2.27 and Standard deviation of 0.98.

The respondents asked on the practice of the bank that takes applicants' prior repayment history into account (Q9) .The finding reveal that respondents agree on the practice of the bank on taking prior repayment history with the mean value of 1.96. The standard deviation of 0.76 also indicated that bank that takes applicants' prior repayment history into account is close to the mean value of 1.96 on average by 0.76.

Great risk appetite of the bank (Q10) has mean value of 2.12 and standard deviation 0.87. This result tells us respondents agree that great risk appetite is the cause for NPL in the Bank.

The respondents asked on the situations that Quality loans are made possible by enhancing or introducing effective risk assessment mechanism in Q11. The result indicated that respondents agree with the mean value of 1.99. The standard deviation of 0.82 also indicated that quality loans are made possible by enhancing or introducing effective risk assessment mechanism is close to the mean value of 1.99 on average by 0.82.

Question 12 indicates about the responses generated for describing no serious action will be taken against borrowers not to repay the loan. The result indicated that respondents were neutral with the mean value of 2.62 on no serious action will be taken against borrowers not to repay the loan.

On assessing borrowers default because they do not understand the credit terms well (Q13) has a mean value of 3.45 and SD of 1. The result implies majority of respondent's disagree with the statement borrower's default because they do not understand the credit terms.

From the above table, it can be observed that loan follow up is directly related to occurrence of nonperforming loans (Q14) has a mean value of 2.24 and Standard deviation of 0.89. The result indicates that most of respondents agree about the relationship of loan follow-up and the occurrence of nonperforming loans.

The respondents asked on credit analysis practice of the bank in Q16.is the result indicated that majority of respondents strongly agree on poor credit analysis is one of the major causes for loan default/NPLs in the Bank with the mean value of 1.80 and SD of 1.

The practice of the bank contacting with borrowers within the lending period raised under Q16 has a mean value of 2.31 and SD of 0.89. The result showed that respondents agree on the lack of contact with borrowers within the lending period contributes for the occurrence of loan default.

From the results deduced from the above Q17, it can be observed that poor credit monitoring and credit collection technique is major causes for loan default in the Bank has a mean value of 2.11 and SD of 0.93. This implies that majority of respondents agree that one of the major cause for loan default in the bank is poor credit monitoring and credit collection technique.

At last weakness in credit risk assessment procedure has a mean value of 2.17 and SD of 0.86 indicated that respondents agree that one of the causes of loan default were weakness in credit risk assessment procedure of the bank. And the given that most of the SD value is low it could be considered the data collected is not widely spread out and could be used as a representative of most of the population.

4.3.2 Lending Interest rate practice of the Bank

Description	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree	Mean	SD
	%	%	%	%	%		
19. Loans with high interest rate tend to turn to NPL	18.9	51.4	18.9	10.8	-	2.22	0.88
20. Charging high interest rate leads to loan default	21.6	41.9	20.3	14.9	1.4	2.32	1.02
21. Customers can't afford to pay the interest rate for borrowing.	6.8	59.5	10.8	23		2.5	0.93
22. Customers unable to pay the penalty fees upon defaulted loan amount.	12.2	51.4	12.2	21.6	2.7	2.51	1.05

TABLE 8 ASSESSMENT OF LENDING INTEREST RATE

Table 9 shows whether Loans with high interest rate tend to turn to NPL in Q19. From the study finding, the respondents agreed that loans with high interest rate tend to turn to NPL as shown by mean of 2.22 and standard deviation of 0.88.

On the other hand respondents asked on the situation of charging high interest rate leads to loan default on Q20. The result indicated that respondents agree that one of the reasons for loan default is charging high interest rate which has a mean value of 2.32 and SD of 1.02.

The above table shows that in Q21 respondents agree with Customers can't afford to pay the interest rate for borrowing with the mean value of 2.5 and Standard deviation of 0.93.

At last respondents asked about customers unable to pay the penalty fees upon defaulted loan amount. The result mean value of 2.51 and 1.05 indicated that respondents were agreeing on customers unable to pay the penalty fees upon defaulted loan amount. And the given that most of the SD value is low it could be considered the data collected is not widely spread out and could be used as a representative of most of the population.

4.3.3 Unsecured Loans practice of the Bank

As indicated in the table 10, 81.1% of respondents with the mean value of 1.94 and Standard deviation 0.77 agreed that providing collateralized loans reduces the chances of loan defaults.

The respondents asked on the practice of the bank on client with good repayment records need not to provide physical collateral. The result indicated that majority of the respondents disagree on the statement that state client with good repayment records need not to provide physical collateral which has a mean value of 3.45 and Standard deviation of 1.24.

And also 35.1 %(mean of 3.16 and standard deviation of 1.49) of the respondents disagree on the practice of the bank set the minimum amount that a client can apply without collateral.

This study showed that 52.7% respondents agreed that most of the time non collateralized loans are defaulted with mean value of 2.63 and standard deviation of 1.18.

Description	**Strongly Agree**	**Agree**	**Neutral**	**Disagree**	**Strongly Disagree**	**Mean**	**SD**
	%	**%**	**%**	**%**	**%**		
23. Providing collateralized loans reduces the chances of loan defaults.	28.4	52.7	14.9	4.1	-	1.94	0.77
24. Client with good repayment records need not to provide physical collateral	10.8	20.3	14.9	40.5	13.5	3.45	1.24
25. The bank has set the minimum amount that a client can apply without collateral	12.2	21.6	21.6	35.1	8.1	3.16	1.49
26. Most of the time non collateralized loans are defaulted	17.6	35.1	18.9	23	5.4	2.63	1.18

27. Collateralizing loans help protect loan default	28.4	44.6	14.9	12.2		2.11	0.96
28. Unsecured loans are charged higher interest rates than secured loans	18.9	44.6	14.9	20.3	1.4	2.4	1.05
29. Collateralized loans perform well	24.3	36.5	16.2	18.9	4.1	2.41	1.17
30. High cost of collateralization hinders loan take by clients	10.8	41.9	17.6	-	-	2.66	1.02
31. The bank look at collateral whenever granting any loan	5.4	94.6	-	-	-	1.95	0.23

TABLE 9 ASSESSMENT OF UNSECURED LOANS

On the other hand respondents asked on the situation of collateralizing loans help protect loan default. The result indicated that respondents agree on collateral that help the loan not to be defaulted which has a mean value of 2.11 and SD of 0.96.

Based on the above table 10, it can be revealed that unsecured loans are charged higher interest rates than secured loans as shown by mean 2.4 and SD 1.05.The result indicated that respondents agree on unsecured loans are charged higher interest which increases the occurrence of loan default.

The survey results showed that 60.8% of the respondents agreed that collateralized loans perform well with the mean value of 2.41 and standard deviation 1.17.

The respondents asked about high cost of collateralization hinders loan take by clients. The result reveals that respondents agree with the mean value of 2.66 and standard devation of 1.02 that high cost of collateralization hinders loan take by clients.

At last respondents requested on the practice of the bank on looking collateral whenever granting any loan. The result indicated that the respondents agree on the bank look at collateral whenever granting any loan with the mean value of 1.95 and Standard deviation of 0.23. And the given that most of the SD value is low it could be considered the data collected is not widely spread out and could be used as a representative of most of the population.

4.3.4 The impact of Political unrest on asset quality

The above table shows that 90.6% of respondents (mean 1.72 and standard deviation 0.67) strongly agree that Customers who operate in conflict areas in Ethiopia unable to repay the loan. In addition 43.2% of respondents were neutral that disbursement of loans to politicians under political pressure is causing NPLs.

The above table shows that 86.5% of respondents (mean 1.74 and standard deviation 0.68) agree that Political unrest also have a strong impact on various customers out of conflict areas which can turn a loan into NPLs whereas 78.4% of respondents agree on majority of loans taken by the conflict regions are defaulted with the mean value of 1.89 and standard deviation 0.77.

Description	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree	Mean	SD
	%	%	%	%	%		
32. Customers who operate in conflict areas unable to repay the loan	39.2	51.4	8.1	1.4	-	1.72	0.67
33. Disbursement of loans to politicians under political pressure is causing NPLs	28.4	28.4	43.2	-	-	2.72	0.84
34. Political unrest also have a strong impact on various customers out of conflict areas	39.2	47.3	13.5	-	-	1.74	0.68
35. Majority of loans taken by the conflict regions are defaulted	33.8	44.6	20.3	1.4	-	1.89	0.77

36. NPL caused by political unrest considered as bad luck	24.3	45.9	23	6.8	-	2.12	0.86
37. Political uncertainty have a strong impact on ratio of NPLs	43.2	48.6	8.1	-	-	1.65	0.63

TABLE 10 ASSESSMENT OF POLITICAL UNREST

The above table shows that 90.6% of respondents (mean 1.72 and standard deviation 0.67) strongly agree that Customers who operate in conflict areas in Ethiopia unable to repay the loan. In addition 43.2% of respondents were neutral that disbursement of loans to politicians under political pressure is causing NPLs.

The above table shows that 86.5% of respondents (mean 1.74 and standard deviation 0.68) agree that Political unrest also have a strong impact on various customers out of conflict areas which can turn a loan into NPLs whereas 78.4% of respondents agree on majority of loans taken by the conflict regions are defaulted with the mean value of 1.89 and standard deviation 0.77.

This study showed that 70.2% respondents agreed that NPL caused by political unrest considered as bad luck which has a mean value of 2.12 and standard deviation of 0.86.

Lastly respondents asked about political uncertainty have a strong impact on ratio of NPLs. The result indicated that 91.8% of respondents were strongly agree with the mean value of 1.65 and Standard deviation of 0.63 on political uncertainty have a strong impact on ratio of NPLs. And the given that most of the SD value is low it could be considered the data collected is not widely spread out and could be used as a representative of most of the population.

4.3.5 Ranking the determinant of Asset quality of Berhan Bank

Regarding ranking factors affecting asset quality of the bank, poor risk assessment and due diligent, unsecured loans, lending interest rate, and political unrest were rated as critical factors.

As shown from the table below 94.9% of respondents agree on risk assessment and due diligence considered as a strong factor for deteriorating asset quality of the bank followed by unsecured loans (37.2%), lending interest rate (87.2), and political unrest (17.9%).

This indicates that risk assessment and due diligence have higher impact as compare to other variables or factors that determine asset quality of the bank.

	Percentage			
	Risk Assessments and Due diligences	**Lending Interest Rate**	**Unsecured Loans**	**Political Unrest**
Strong	94.90%	30.80%	37.20%	17.90%
Some what		56.40%	55.10%	48.70%
Neutral			1.30%	15.40%
Weak		7.70%	1.30%	10.30%
Insignificant				2.60%

TABLE 11 RANKING FACTORS AFFECTING ASSET QUALITY

CHAPTER FIVE
SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

This research paper is conducted as assessment of asset quality management practice of Berhan bank, in an endeavor to assess the relationship of risk assessment and due diligence, lending interest rate, unsecured loans and political unrest. In so doing, primary data were collected through structured questionnaire.

5.1 Summary

The study indicated that the bank week risk assessment and due diligence ,charged high interest rates on loans and disbursing unsecured loans contribute for the deterioration of asset quality. It was further indicated that political unrest was a factor that reduce asset quality of the bank.

5.1.1 **Summary of risk assessment and due diligence**

- Majority of respondents agree with Improper/poor client selection and due diligence assessment were the main reasons for loan defaults.
- Most of respondents were neutral about accountability for granting and approval practice of the bank and on the bank handles credit-processing tasks apart from the appraisal
- Respondents agree on the situations when directors, senior managers, or other powerful bank employees may have an impact on the credit decisions and oversight of applicants.
- Customers make multiple borrowing in different banks that impact asset quality of the bank was agree by majority of the respondents.
- Respondents are neutral on the practice of the bank on requesting all clients to submit a business plan to identify risk exposure.
- Majority of respondents strongly agreed on the statement that a poor assessment of the credit risk would result in loan default and NPL.
- Respondents agree with projects that are under or over-financed will experience Loan default and NPL.
- Respondents agree on the practice of the bank on taking prior repayment history.
- Respondents agree that great risk appetite is the cause for NPL in the Bank

- quality loans are made possible by enhancing or introducing effective risk assessment mechanism
- The result indicated that respondents were neutral on no serious action will be taken against borrowers not to repay the loan.
- Respondents disagree with the statement borrower's default because they do not understand the credit terms.
- Most of respondents agree about the relationship of loan follow-up and the occurrence of nonperforming loans.
- Majority of respondents strongly agree on poor credit analysis is one of the major causes for loan default/NPLs in the Bank.
- Respondents agree on the lack of contact with borrowers within the lending period contributes for the occurrence of loan default.
- Majority of respondents agree that one of the major causes for loan default in the bank is poor credit monitoring and credit collection technique.
- Respondents agree that one of the causes of loan default were weakness in credit risk assessment procedure of the bank.

5.1.2 **Summary of lending interest rate and asset quality**

- Respondents agreed that loans with high interest rate tend to turn to NPL.
- Respondents agree that one of the reasons for loan default is charging high interest rate.
- Respondents agree with Customers can't afford to pay the interest rate for borrowing.
- Respondents were agreeing on customers unable to pay the penalty fees upon defaulted loan amount.

5.1.3 **Summary of unsecured loan practice of the bank**

- Most of respondents agreed that providing collateralized loans reduces the chances of loan defaults.
- Majority of the respondents disagree on the statement that state client with good repayment records need not to provide physical collateral

- Respondents disagree on the practice of the bank set the minimum amount that a client can apply without collateral.
- Respondents agreed that most of the time non collateralized loans are defaulted.
- Respondents agree on collateral that help the loan not to be defaulted.
- Respondents agree on unsecured loans are charged higher interest which increases the occurrence of loan default.
- Respondents agreed that collateralized loans perform well.
- Respondents agree that high cost of collateralization hinders loan take by clients.
- The respondents agree on the bank look at collateral whenever granting any loan.

5.1.4 **Summary on the impact of political unrest and asset quality of the bank**

- Respondents strongly agree that Customers who operate in conflict areas in Ethiopia unable to repay the loan. However, respondents were neutral that disbursement of loans to politicians under political pressure is causing NPLs.
- Respondents agree that Political unrest also have a strong impact on various customers out of conflict areas which can turn a loan into NPLs.
- Respondents agreed that NPL caused by political unrest considered as bad luck.
- Respondents were strongly agreed with political uncertainty have a strong impact on ratio of NPLs.

5.1.5 Summary of ranking the determinant of Asset quality of Berhan Bank

94.9% of respondents agree on the practice of weak risk assessment and due diligence considered as a strong factor for deteriorating asset quality of the bank followed by unsecured loans (37.2%), lending interest rate (87.2), and political unrest (17.9%).

5.2 CONCLUSIONS

The basic objective of this research has been to assessment of asset quality management practice of Berhan bank. On the basis of the broad objective the study is to obtain empirical evidence on risk assessment and due diligence practice affect asset quality of the bank, lending interest rate affect asset quality of Berhan bank, unsecured loan affect asset quality of Berhan bank and the impact of political unrest affect asset quality of Berhan bank.

The study indicated that the practice of week credit assessment and due diligence was the cause for reducing asset quality of the bank. The result of assessment also shows charging high interest rate on loans contributing for reducing asset quality of the bank. Furthermore, collateral that helps the loan not to be defaulted. Furthermore, the study indicated that political unrest in the county was one of the challenges in asset quality management.

5.3 Recommendation

Based on the findings of the study the following possible recommendations were forwarded:

- For asset quality banks need to improve their processes of screening credit customers and monitoring of credit risk. Therefore, management of the bank should revisit lending policy and highly observe the risk assessment and due diligence before giving any loans.
- Before approving any loans appropriate credit analysis in detail shall be applied.
- Build the professional capacity loan officers and managers.
- Lending interest rate should be reviewed and reduce to increase asset quality.
- Unsecured loans are more risky than secured loans .Therefore; the bank should look for collateral when granting loans.
- Reduce and, if possible, eliminate all political influence involved in the giving of loans to specific political individuals and groups.

5.4. Recommendation of future Studies

To better understand the fluctuations in non-performing assets, the researcher propose that further studies should be undertaken by different loan categories (agriculture, construction and building, Manufacture, domestic trade and service, import and export) which significantly affect asset quality of the bank.

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Questionnaire on 'Assessment of asset quality management practice'

Dear Respondents:

- This study is a requirement for the partial fulfillment for the degree of Master of Business Administration (MBA). The purpose of this research is to **assess asset quality management practice of Berhan bank**. Please note that any information you give will be treated with confidentiality and at no instance will it be used for any other purpose other than for this project. Your assistance will be highly appreciated.
- Note: Please put a „√" mark on your choice on the space provided and No need of writing your name

Thank You for your Collaboration!

Part I: Demographic Information

1. Age: ☐ 18-25 ☐ 26-35 Years ☐ 36-45 Years ☐ 46 and above
2. Gender: ☐ Male ☐ Female
3. Educational Level:

   ☐ College Diploma ☐ Second Degree (MA/MSc/MBA)

   ☐ Bachelor Degree ☐ Others___________________
4. How many years did you work in Berhan Bank?

   ☐ 1-3 years ☐ 6-10 years

   ☐ 3-5 years ☐ above 10 years

5. Your current position in Berhan Bank?

Loan officer:	☐	Director	☐
Credit Analyst	☐	Monitoring/Follow-up Officer	☐
Credit manager	☐	Branch Manager	☐

Part II Questions regarding Assessment of asset quality management practice in Berhan Bank

Please indicate the degree of your agreement/disagreement with the following statements associated with the **four** Dimensions' of risk assessments and due diligence, Lending interest rate, political unrest and unsecured loans in Berhan Bank **(put** "√" **the Alternative Number That Best Describes Your View)**

Description	Strongly Agree(1)	Agree (2)	Neutral (3)	Disagree (4)	Strongly Disagree (5)
Statements related to Risk assessment and due diligence					
1. One of the main reasons for loan defaults and NPLs in the bank is improper/poor client selection and due diligence assessment (KYC).					
2. The banks credit granting and approval process establish accountability to decision makers					
3. There are situations when directors, senior managers, or other powerful bank employees may have an impact on the credit decisions and oversight of applicants.					
4. The bank handles credit-processing tasks apart from the appraisal.					
5. Customer make multiple borrowing in different banks					
6. To identify risk exposure, the bank requires all clients to submit a business plan.					
7. A poor assessment of the credit risk would result in loan default and NPL.					
8. Projects that are under or over-financed will experience Loan default and NPL.					
9. The bank takes applicants' prior repayment history into account.					
10 Great risk appetite is the cause for NPL in the Bank					
11. Quality loans are made possible by enhancing or introducing effective risk assessment mechanism.					
12. No serious action will be taken against borrowers not to repay the loan					
13. Borrowers default because they do not understand the credit terms well					
14. Loan follow up is directly related to occurrence of nonperforming loans					
15. Poor credit analysis is one of the major causes for loan Default/NPLs in the Bank.					
16. Lack of contact with borrowers within the lending period.					
17. Poor credit monitoring and credit collection technique.					
18. Weakness in credit risk assessment procedure.					

Description	Strongly Agree(1)	Agree (2)	Neutral (3)	Disagree (4)	Strongly Disagree (5)
Statements related to Lending interest rate					
19. Loans with high interest rate tend to turn to NPL					
20. Charging high interest rate leads to loan default					
21. Customers can’t afford to pay the interest rate for borrowing.					
22. Customers unable to pay the penalty fees upon defaulted loan amount.					
Statements related to Unsecured Loan					
23. Providing collateralized loans reduces the chances of loan defaults.					
24. Client with good repayment records need not to provide physical collateral					
25. The bank has set the minimum amount that a client can apply without collateral					
26. Most of the time non collateralized loans are defaulted					
27. Collateralizing loans help protect loan default					
28. Unsecured loans are charged higher interest rates than secured loans					
29. Collateralized loans perform well					
30. High cost of collateralization hinders loan take by clients					
31. The bank look at collateral whenever granting any loan					
Statements related to political unrest					
32. Customers who operate in conflict areas unable to repay the loan					
33. Disbursement of loans to politicians under political pressure is causing NPLs					
34. Political unrest also have a strong impact on various customers out of conflict areas					
35. Majority of loans taken by the conflict regions are defaulted					
36. NPL caused by political unrest considered as bad luck					
37. Political uncertainty have a strong impact on ratio of NPLs					

38. How do you the factor stated below affect asset quality?

1. Strong, 2 somewhat 3, neutral, 4 Weak and 5 insignificant

Factors	Rate
Risk assessment and due diligence	
Lending interest rate	
Unsecured Loan	
political unrest	

Part II Open ended Questions

39. What steps should be taken, in your opinion, to help the bank lower its high NPL portfolio and default rates in light of internal factors? Give more details in your reply.

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____

40. If you have further comments on the bank specific factors affecting asset quality of bank please specify in the space provided.

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End of questionnaire

Thank You