CREDIT RISK MANAGEMENT AND FINANCIAL PERFORMANCE OF MICRO FINANCE INSTITUTIONS IN MASAKA DISTRICT

A CASE STUDY OF

PRIDE MICROFINANCE (MDI) MASAKA BRANCH

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DEDICATION

This is a dedication to my Loving parents; Mr. Bamulanzeki Fred (my father) and Ms. Namugera Prossy (my Mother) as well as my siblings for their support in doing my Bachelor of Business Administration and management Course.

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LIST OF ABBREVIATIONS

NPL Non Performing Loans

PMFI Pride Micro Finance Institution

MDI Microfinance Deposit Taking Institutions

CAMELS Capital adequacy, Asset quality, Management, Earnings, Liquidity and sensitivity

SACCOS Savings and Credit Corporative Societies

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ABSTRACT

The study intended to investigate the credit risk management and financial performance of microfinance institutions with pride microfinance Masaka branch as a case study in Masaka district.

The study was guided by three objectives; to establish the credit risk management indicators by pride microfinance Masaka branch, to establish the indicators of financial performance in pride microfinance in Masaka Brach and to establish whether credit risk management affects profitability of pride microfinance in Masaka branch.

The study was descriptive and analytical in nature employing both quantitative and qualitative approaches of data collection under a cross sectional case study research design. Questionnaire was the methods used in order to obtain data from a sample of 27 respondents of which 15 were male and 12 were female.

The study revealed that majority of employees in pride microfinance are male and the minorities are female this is shown in table 4.1. Majority of employees have worked in pride microfinance for a period of between one to five years and this is shown in table 4.4.

Therefore, the study recommended that the management of pride should identify risks as early as possible and make analysis at early stage to prevent the institution from facing credit risks.

CHAPTER ONE

GENERAL INTRODUCTION

1.0 Introduction

This study focused on credit risk management and financial performance of micro finance institutions in Masaka District where credit risk management is the independent variable and financial performance the dependent variable.

This chapter contains the background to the study, problem statement, general and specific objectives, research questions, scope of the study, significance of the study and conceptual framework, definition of terms and concepts.

1.1 Background to the study

Credit risk, according to Basel (2000) is the potential that a bank borrower or counterparty will fail to meet its obligations in accordance with agreed terms. It is a risk of borrower default, which occurs when counterparty defaults on repayment. The reasons for loan default / loan delinquency are when the obligor is in a financially stressed situation (Gestel and Baesens, 2008). Inadequate financial analysis, inadequate loan support according to Sheila (2011) are the causes of loan default. Credit risk management is the identification, measurement, monitoring and control of risk arising from the possibility of default from loan repayment (Early, 1966; Coyle, 2000). Credit risk management also refers to the systems, procedures and controls, which a company has in place to ensure the efficient collection of customer payments thereby minimizing the risk of non-payment (Mokogi, 2003).

Ditcher (2003) observes that banks in USA gave credit to customers with high interest rate which discouraged borrowing. As a result, the concept of credit did not become popular until

the economic boom in USA in1885 when banks had access to liquidity and wanted to lend excess cash.

In Africa, credit was largely appreciated in the 1950's when most of banks started opening the credit sections and departments to give loans to white settlers. Uganda is one of developing countries in Africa that has recently started to promote microfinance institutions. As a result, non-performing loans is on the increase thus lowering the level performance of microfinance institutions (MDI's). Available statistics from the Bank of Uganda annual supervision report, 2015 indicates high incidence of credit risk reflected by increasing non-performing loans (NPLs) by MDI's. The situation has adversely impacted on their profitability and overall asset quality has deteriorated. The NPL ratio (NPLs to total gross loans) increased from 3.2% in December 2011 to 5.3% December 2012 it decreased marginally in December 2013 to 3.4% and again rose to 4.2% in December 2014 and then rose to 6.6% in December.

Whitaker (1999) defines entry in financial distress as the first year in which cash flows are less than current maturities' long-term debt. The firm has enough to pay its creditors as long as the cash flows exceeds the current debt obligations. Wruck (1990) stated that firms enter into financial distress as a result of economic distress, declines in their performance and poor management especially on risks. Boritz (1991) depicts a process of a financial distress that begins with an incubation period characterized by a set of bad economic conditions and poor management which commits costly mistakes.

According to Boston Consulting Group (2001) credit risk is the oldest and important risk to which institutions are exposed. The importance of credit risk and credit risk management are Increasing with time because of some reasons like; economic crises and stagnation, company bankruptcies, infraction of rules in company accounting and audits, growth of off-balance

sheet derivatives, declining and volatile values of collateral, borrowing more easily of small firms, financial globalization and BIS risk-based capital requirements.

Greuning and Iqbal (2007) define credit risk as the risk of losses caused by the default of borrowers. Harrington (1999) posits that most organizations track interest rate risk closely. They measure and manage the firm's vulnerability to interest rate variation, even though they cannot do so perfectly. At the same time, international organizations with large currency positions closely monitor their foreign exchange risk and try to manage, as well as limit, their exposure to it. In a similar fashion, some institutions with significant investments in one commodity such as oil, through their lending activity or geographical franchise, concern themselves with commodity price risk.

According to Chen and Pan (2012), credit risk is the degree of value fluctuations in debt instruments and derivatives due to changes in the underlying credit quality of borrowers and counterparties.

Coyle (2000) defines credit risk as losses from the refusal or inability of credit customers to pay what is owed in full and on time. Credit risk is the exposure faced by banks when a borrower (customer) defaults in honoring debt obligations on due date or at maturity. There are different techniques of credit risk management that this study will focus on; they include credit risk identification, credit risk appraisal, and credit risk monitoring and credit risk mitigation participants and players in the industry need to align with. As earlier noted, it is a process which involves:

Risk identification: In order to properly manage risks, an institution must recognize and understand risks that may arise from both existing and new business initiatives; for example, risks inherent in lending activity include credit, liquidity, interest rate and operational risks.

Risk identification should be a continuing process, and should be understood at both the transaction and portfolio levels.

Risk Analysis: Once risks have been identified, they should be measured in order to determine their impact on the banking institution's profitability and capital. This can be done using various techniques ranging from simple to sophisticated models. Accurate and timely measurement of risk is essential to effective risk management systems.

Risk Mitigation: After measuring risk, an institution should establish and communicate risk limits through policies, standards, and procedures that define responsibility and authority. Institutions may also apply various mitigating tools in minimizing exposure to various risks. Institutions should have a process to authorize and document exceptions or changes to risk limits when warranted.

The objective of this study therefore, was to evaluate the relationship between credit risk management and financial performance of microfinance institutions Masaka. The study aimed at analyzing whether a relationship exists between credit risk identification, credit risk appraisal, credit risk mitigation and financial performance of microfinance institutions in Masaka District.

1.2 Statement of the problem

Credit risk is the exposure faced by banks when a borrower (customer) defaults in honoring debt obligations on due date or at maturity (Coyle, 2000). Kargi (2011) indicated that credit creation is the main income generating activity for the banks. As a result adequate management on loan processing is critical for the growth and survival of the banks otherwise the credit activity may lead to financial distress. The main purpose of a bank existence is to accept deposits as well as to grant credit facilities, therefore inevitably exposed to credit risk.

Credit risk is the most significant risk faced by banks and the success of their business depends on accurate measurement and efficient management of this risk than any other risks (Gieseche, 2004).

Credit risk is inherent in every commercial bank, but commercial banks that embed the right Credit risk management strategies into business planning and financial performance management are more likely to achieve their strategic and operational objectives. Taking credit risk management is core to the Bank's financial performance therefore to achieve an appropriate balance between risk and return to minimize potential adverse effects on its financial performance. This requires more dynamic and sound credit Risk Management methods to perform well in an ever dynamic and highly competitive banking industry, which will translate into having a competitive advantage and thus generate growth in profits. Some aspects of credit risks present opportunities through which firms can have a competitive edge over others and contribute to improvement of financial performance (Stulz, 1996).

Literature on credit risk management suggests that firms with better credit risk management strategies tend to have better financial performance but the Empirical studies done have focused on: Assessment of credit risk management techniques adopted by microfinance institutions in Kenya (Mwirigi, 2006)

To the researchers best knowledge there is limited empirical evidence on the relationship between credit risk management and performance of commercial banks; thus this study seek to fill the existing research gap by answering the following research question, does there exist a relationship between credit risk management and financial performance of microfinance institutions? Taking a case study of Pride Micro Finance, in Masaka District

1.3 General objective

To ascertain the relationship between credit risk management and financial performance of microfinance institution in Masaka District

1.4 Specific objectives

i. To establish the credit risk management indicators in Pride Micro Finance, in Masaka District
ii. To establish indicators of banks' financial performance in Pride Micro Finance, in Masaka District
iii. To establish whether credit risk management affects Micro Finance profitability of Pride Micro Finance, in Masaka District.

1.5 Research questions

i. What are the indicators of the credit risk management?
ii. What are the indicators of Pride Micro Finance's financial performance (profitability)?
iii. Does credit risk management affect the Pride Micro Finance's financial performance (profitability)

1.6 Scope of the study

1.6.1 Content Scope

The study focused on Credit Risk Management as the independent variable and Financial Performance of Microfinance Institutions as the dependent variable. Therefore, the study focused on three study objectives which included; Credit risk Identification, Credit risk

Analysis, and Credit risk Mitigation to establish the relationship between Credit Risk Management and Financial Performance of Microfinance Institutions

1.6.2 Geographical Scope

The study was carried out from Pride Micro Finance, in Masaka District one of the MDI located in Masaka District, in Katwe Butego Division in Masaka Municipality.

The study was conducted from Pride Micro Finance, in Masaka District because it is one of the most prominent micro finance institution in the district with many clients to whom it offers the service of loans among others

1.6.3 Time Scope

The study covered a period of ten years from 2007 to 2017 because in this period there is information that is relevant to the study; and it is the period when the Micro finance has been operating and where a number of risks have been encountered.

The secondary data was obtained from secondary sources such as reports, books, internet sources and other related data records.

1.7 Justification of the study

Credit risk management is very important to banks as it is an integral part of the loan process. It maximizes bank risk, adjusted risk rate of return by maintaining credit risk exposure with view to shielding the bank from the adverse effects of credit risk A customer is happy and secure when he/she invests in a risk free business and wants to be equally happy on each further occasion. Therefore, risk management and profitability are closely related aspects and

need to be handled with extra emphasis if a business is to hit high profitability over a given period (Gizycki, 2001).

Hence, examining the relationship between credit risk management on financial performance of Micro Finance Institutions in Masaka is vital to check the situation in the industry as there is a very strong and direct involvement of risks associated in the day to day activities the Finance Institutions.

Understanding the relationship between credit risk management techniques and financial performance will benefit microfinance institutions and monetary authorities. Microfinance institutions, for example, will adopt appropriate credit risk management measures to avoid default from a borrower or counterparty to meet its obligations in accordance with agreed terms.

The study was carried out because it is a requirement for the student of Business Administration and Management that was lead her to the award of a bachelor's degree from Uganda Martyrs University.

1.8 Significance of the study

The study helps in improving of risks management standards for the micro finance institutions in Uganda.

The findings of the study give an insight into the current problem to improve on micro finance institutions performance and effectiveness; because it will enable institutions to come up with policies to manage risks associated with the sector so as to maximize profits.

The findings of the study enable micro finance institutions to prioritize risk management in their annual plans such that they do not lose a lot of funds in bad debts.

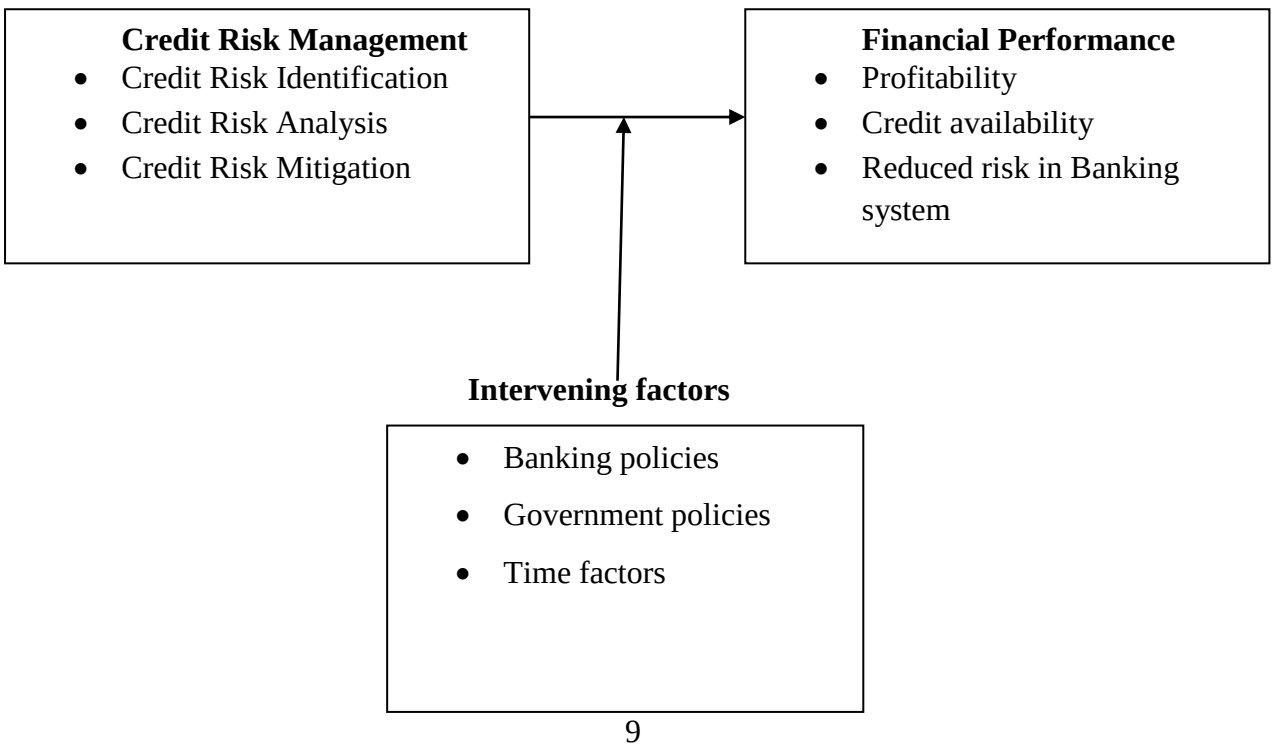
The study also acts as a basis for further research to other researchers in field of Risk management and financial Performance of Micro Finance institutions.

1.9 The conceptual framework

According to Mugenda and Mugenda (2003), a conceptual framework refers to conceptualization of the relationship between variables in the study and it is shown diagrammatically. Through the conceptual framework, the researcher was able to show the relationship between study variables. Previous studies have identified a number of factors that influence financial performance of micro finance institutions however; credit risk management as depicted below was identified as having major influence on financial performance of micro finance institutions.

The conceptual framework showing the possible relationship between Credit Risk Management and financial performance of micro finance institutions

Figure 1.1 The conceptual framework



Source: Developed by Researcher with help of Amin (2002)

The independent variable which is credit risk management with attributes including credit risk identification, credit risk analysis and the Credit risk mitigation, affect the dependent variable which is financial performance with attributes including profitability, credit availability and reduced risk in banking system this in one way play a great role in the performance of any microfinance institution. However, credit risk management and financial performance in microfinance institutions is affected by the intervening variables like banking policies, government policies, and time factors.

1.10 Definition of terms:

Credit:

Is as a probability or threat of damage, injury, liability, loss, or any other negative occurrence that is caused by external or internal vulnerabilities, and that may be avoided through preemptive action.

Credit Risk:

Refers to the probability of loss due to a borrower's failure to make payments on any type of debt

Credit Risk Management:

This is the practice of mitigating losses by understanding the adequacy of a bank's capital and loan loss reserves at any given time – a process that has long been a challenge for financial institutions

Credit Risk Identification:

Risk identification is the process of taking stock of an organization's risks and vulnerabilities and raising awareness of these risks in the organization

Credit Risk Analysis:

This is the process of defining and analyzing the dangers to credit posed by potential natural and human-caused adverse events

Credit Risk Mitigation:

This is the employment of various methods to reduce the risks to lenders, banks and other business which offer credit.

Financial Performance:

This is a subjective measure of how well a firm can use assets from its primary mode of business and generate revenues.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter reviews literature relating to the relationship between credit risk management and financial performance of microfinance institutions. The literature review has been organized in the following sections. First section covers the theoretical framework on credit risk management, and its impact on the microfinance financial performance. The second section covers the determinants of financial performance. The third section covers the empirical studies on the relationship between credit risk management and financial performance of micro finance institutions in Uganda, then the summary of the literature review including research gaps of the chapter.

2.1.1 Theoretical Review:

This study is to be based on the Finance Distress Theory as it seeks to determine the relationship between credit risk management and financial performance of microfinance institutions in Masaka.

2.1.2 Finance distress theory

Baldwin and Scott (1983) purported that when a firm's business deteriorates to the point where it cannot meet its financial obligation, the firm is said to have entered the state of financial distress. The first signals of financial distress are violations of debt payments and failure or reduction of dividends payouts. Whitaker (1999) defines entry in financial distress as the first year in which cash flows are less than current maturities' long-term debt. The firm has enough to pay its creditors as long as the cash flows exceeds the current debt obligations.

The key factor in identifying firms in financial distress is their inability to meet contractual debt obligations.

However, substantial financial distress effects are incurred well prior to default. Wruck (1990) stated that firms enter into financial distress as a result of economic distress, declines in their performance and poor management especially on risks. Boritz (1991) depicts a process of a financial distress that begins with an incubation period characterized by a set of bad economic conditions and poor management which commits costly mistakes. The relevance of the financial distress theory emanates from the liquidity and credit risk facing a firm. In the case of commercial banks, inability to provide cash to depositors and loans to borrowers as and when the demand may constitute a liquidity crisis. Other creditors also need to be taken into account when firms are putting in place risk management measures. Credit risks in banks also need to be addressed since it may lead to financial distress. Loan portfolio management is an important determinant of the firm's liquidity. The banks should manage the credit and liquidity risk in order to avoid the financial distress. The foregoing instigated the question as to what is the effect of the credit risks on the financial performance of microfinance institutions.

2.2 Credit Risk Management

Credit risk refers to the risk that a borrower will default on any type of debt by failing to make required payments. The risk is primarily to the lender and includes lost principal and interest, disruption to cash flows, and increased collection costs. The loss may be complete or partial and can arise in a number of circumstances. Risk management framework is important for commercial banks. The theory of asymmetric information argues that it may be impossible to distinguish good borrowers from bad borrowers (Auronen, 2003) which may result in adverse selection and moral hazards problems. Adverse selection and moral hazards

have led to substantial accumulation of non-performing accounts in the commercial banks (Bofondi and Gobbi, 2003).

Credit management is one of the most important activities in any company and cannot be overlooked by any economic enterprise engaged in credit irrespective of its business nature. It is the process to ensure that customers will pay for the products delivered or the services rendered. Myers and Brealey (2003) describe credit management as methods and strategies adopted by a firm to ensure that they maintain an optimal level of credit and its effective management. It is an aspect of financial management involving credit analysis, credit rating, credit classification and credit reporting. Nelson (2002) views credit management as simply the means by which an entity manages its credit sales. It is a prerequisite for any entity dealing with credit transactions since it is impossible to have a zero credit or default risk.

BCBS (2006) hold that risk management processes, require supervisors to be satisfied that the banks and their banking groups have in place a comprehensive risk management process. This would include the Board of senior management to identify, evaluate, monitor and control or mitigate all material risks and to assess their overall capital adequacy in relation to their risk profile. In addition, as suggested by Al-Tamimi (2002) in managing risk, commercial banks can follow comprehensive risk management process which includes eight steps: exposure identification; data gathering and risk quantification; management objectives; product and control guidelines; risk management evaluation; strategy development; implementation; and performance evaluation (Baldoni, 1998; Harrington and Niehaus, 1999).

The scope of internal auditing within an organization is broad and may involve topics such as an organization's governance, risk management and management controls over: efficiency/effectiveness of operations, the reliability of financial and management reporting, and compliance with laws and regulations. Internal auditing may also involve conducting

proactive fraud audits to identify potentially fraudulent acts; participating in fraud investigations under the direction of fraud investigation professionals, and conducting post investigation fraud audits to identify control breakdowns and establish financial loss. Internal auditors are responsible for the execution of company activities; they advise management and the Board of Directors (or similar oversight body) regarding how to better execute their responsibilities (Walker, 2002).

According to Boston Consulting Group (2001) credit risk is the oldest and important risk to which institutions are exposed. The importance of credit risk and credit risk management are increasing with time because of some reasons like; economic crises and stagnation, company bankruptcies, infraction of rules in company accounting and audits, growth of off-balance sheet derivatives, declining and volatile values of collateral, borrowing more easily of small firms, financial globalization and BIS risk-based capital requirements. Greuning and Iqbal (2007) define credit risk as the risk of losses caused by the default of borrowers. Default occurs when a borrower cannot meet his financial obligations. Credit risk can alternatively be defined as the risk that a borrower deteriorates in credit quality. This definition also includes the default of the borrower as the most extreme deterioration in credit quality. Credit risk is managed at both the transaction and portfolio levels. But, institutions increasingly measure and manage the credit risk on a portfolio basis instead of loan-by-loan basis.

Harrington (1999) posits that most organizations track interest rate risk closely. They measure and manage the firm's vulnerability to interest rate variation, even though they cannot do so perfectly. At the same time, international organizations with large currency positions closely monitor their foreign exchange risk and try to manage, as well as limit, their exposure to it. In a similar fashion, some institutions with significant investments in one commodity such as oil, through their lending activity or geographical franchise, concern

themselves with commodity price risk. Others with high single-industry concentrations may monitor specific industry concentration risk as well as the forces that affect the fortunes of the industry involved.

In the management of credit risk we thus have to deal with "true uncertainty" in the sense of Frank Knight (Voropaev**,** 2009) who was the first to distinguish between "risk" based on known probability measures and true uncertainty where the underlying statistical distributions are unknown. Knight's ideas have been further developed by several authors over the years and in particular by Ben-Haim (Ben-Haim, 2010) who has developed a quantitative formulation known as information-gap decision theory. Ben-Haim (2005), has recently applied this theory to the management of financial market risk.

Beresford-Smith & Thompson (2007) provides that the management of credit risk is now common place in most financial institutions where safeguards are needed to lower potential losses from defaults on loans and therefore quantitative methods for managing these and other risks are now required in most countries. Further, Al-Tamimi& Al Mazrooei (2007) stipulates that all banks in the present-day volatile environment are facing a large number of risks such as credit risk, liquidity risk, foreign exchange risk, market risk and interest rate risk, among others and such risks may threaten a bank's survival and success. In other words, banking is a business of risk and for this reason, efficient risk management is absolutely required. According to the consultative paper issued by the Basel committee on banking supervision (1999) (see Hassan & Sanchez (2009)); most banks' loans are the largest and most obvious sources of credit risk. Banks are increasingly facing credit risk in various financial instruments other than loans, including acceptances, interbank transactions, trade financing, foreign exchange transactions, financial futures, swaps, bonds, equities, options,

the extension of commitments and guarantees, and the settlement of transactions (Rosenberg, Gonzalez, and Narain, 2009).

2.3 Financial Performance

Financial performance is the measure of the results of the firm's policies and operations within a specified time period in monetary terms. The results are expressed inform of profit or losses. Financial performance of Micro finance institutions is the measure of the level Micro finance institutions profit or loses within a specified time. Several measures have been used to measure the financial performance of Micro finance institutions.

According to the business dictionary financial performance involves measuring the results of a firm's policies and operations in monetary terms. These results are reflected in the firms return on investment, return on assets and value added. Stoner (2003) as cited in Turyahebya (2013), defines financial performance as the ability to operate efficiently, profitably, survive, grow and react to the environmental opportunities and threats. In agreement with this, Sollenberg and Anderson (1995) assert that, performance is measured by how efficient the enterprise is in use of resources in achieving its objectives. Hitt et al., (1996) believes that many firms' low performance is the result of poorly performing assets. Commercial banks earn financial revenue from loans and other financial services in the form of interest fees, penalties, and commissions. Financial revenue also includes income from other financial assets, such as investment income. Bank financial activities also generate various expenses, from general operating expenses and the cost of borrowing to provisioning for the potential loss from defaulted loans.

There are external factors that can cause bank failure which may include lack of information, deregulation (Mugenda, 2008) Some useful measures of financial performance are coined into what is referred to as CAMELS (Capital adequacy, Asset quality, Management,

Earnings, Liquidity and sensitivity) referring to the six components of a bank's conditions that are assessed. CAMELS' framework regulates the banking sector by giving a guide on governance. **(**Madhyam and Stichele 2010). Solvency level is a measures of degree at which debts are secured and obtained by computing debt to asset ratio. Asset quality; according to (Mugambe, 2008) the solvency of financial institutions typically is when their assets become impaired. So it's important to monitor indicator of quality, assets of financial institutions in Uganda in term of over exposure to specific risk trends in non- performing loan, the profitability and health of bank borrowers especially the corporate sector

Liquidity; initially solvent financial institution may be driven toward closure by poor management of short-term liquidity. Indicators should cover funding sources and capture large maturity mismatches. An unmatched position potentially enhances profitability but also increase the risk of losses **(**CBK, June 2001) the key dimensions of measuring financial performance in the commercial banks in Uganda are Capital adequacy, Asset quality, Earnings, Liquidity.

Financial performance of banks can be determined by several factors. These factors are divided in to two, the internal factors and the external factors. The internal factors include: Capital adequacy, Asset Quality, Management efficiency and liquidity management. It is important to note that these factors differ from one financial institution to another. External factors are the factors beyond the management's control. They include: political stability of a country, inflation rate, GDP growth rate, Interest rates and financial institution policies and a country (Naceur, 2003)

2.4 Credit Risk Identification

Risk identification refers to the process of identifying dangerous or hazardous situations and trying to characterize it. It is a procedure to deliberately analyze, review and anticipate

possible risks (Barton, 2002). The first step in organizing the implementation of the credit risk management function is to establish the crucial observation areas inside and outside the corporation (Kromschroder and Luck, 1998). The departments and the employees must be assigned with responsibilities to identify specific risks for example interest rate risks or foreign exchange risks are the main domain of the financial department.

It is important to ensure that the credit risk management function is established throughout the whole corporation; apart from parent company, the subsidiaries too have to identify risks and analyze them. Other approaches for risk identification include scenario analysis or risk mapping. An organization can identify the frequency and severity of the risks through risk mapping which could assist the organization to stay away from high frequency and low severity risks and instead focus more on the low frequency and high severity risk. Credit Risk identification process includes risk-ranking components where these ranking are usually based on impact, severity or dollar effects (Barton, 2002). Accordingly, the analysis helps to sort risk according to their importance and assists the management to develop risk management strategy to allocate resources efficiently.

2.5 Credit Risk Analysis and Mitigation

This is the process of determining the likelihood that a specified negative event will occur. Investors and business managers use risk assessments to determine things like whether to undertake a particular venture, what rate of return they require to make a particular investment and how to mitigate an activity's potential losses. There are many conceptual studies made on risk analysis in reference to measurement and mitigation of risk. In practice, it is useful to classify the different risks according to the amount of damage they possibly cause (Fuser et al, 1999). This classification enables the management to divide risks that are threatening the existence of the corporation from those which can cause slight damages.

Frequently, there is an inverse relationship between the expected amount of loss and its corresponding likelihood, i.e. risks that will cause a high damage to corporation, like earthquakes or fire, occur seldom, while risks that occur daily, like interest rate or foreign exchange risks, often cause only relatively minor losses, although these risks can sometimes harm the corporations seriously.

A comprehensive risk analysis and mitigation methods for various risk arising from financing activities and from the nature of profit and loss sharing is the source of funds especially investment account holders are explained by Sundararajan (2007). He concludes that the application of modern approaches to risk analysis, particularly for credit and overall banking risks is important for Banks. Also, he suggests that the need to adopt new measures is particularly critical for Banks because of the role they play and the unique mix of risks in finance contracts.

However, (Navajas and Tejerina, 2006) indicates that banks are perceived not to use the latest risk measurement techniques and Shari'ah compliant risk mitigation techniques due to different Shari'ah interpretation of these techniques. Also, appropriate measurement of credit and equity risks in various finance facilities can benefit from systematic data collection efforts, including establishing credit and equity registry. Moore (2007) suggests that bank need to start collecting data, and there can be significant advantages in pooling information and using common definitions, standards, and methodologies for credit risk which is argued can lead to significant losses in all financial institutions. Finally, he found out that risk analysis particularly on measuring risk in banking institutions is important for risk management practices.

2.6 Review of Empirical Literature

Financial institution performance is determined by so many factors with the main one being the risks. The risks include: credit risk, interest rate risk, political risk, operational risks, liquidity risks and market risk. These risks are either internal or external. Commercial banks have closed due to the poor performance of loans. This called for effective management of its asset (Naceur, 2003)

In the recent years banks have developed sophisticated systems of risk management. Many banks have been exposed to more risk of loan defaulting due to the increase of the amount of loans advanced. In addition to the system, management have had to up there game in securing there assets (Morsman, 1993). Commercial banks have policies which guide on the process of advancing credit. These policies define on who should access credit and the collaterals involved. In addition it guards its back through insurance. Once this is achieved the banks financial performance is expected to go up. For the past years, banks have reported increase in profits. The asset base of most banks has been increasing and the proportion of loans also has been on the growing trend (IFSB, 2005).

Various researches have analyzed the linkage between credit risk management and financial performance, and how effective credit risk management contributes to reduction of defaults by counterparty as well as restricting uncertainty of achieving the required financial performance. Otieno*et al.* (2016) evaluated the relationship between credit risk management and financial performance of microfinance banks in Kenya using Pearson correlation coefficient. The population of the study comprised of 12 licensed microfinance Banks. The study concluded that credit risk management impacts performance of MFBs. The study recommends that credit managers should operate under a sound credit granting process with well-defined credit-granting criteria detailing the MFB's target market, a thorough understanding of the borrower's purpose and source of repayment.

Justus *et al.* (2016) assessed the influence of credit risk management practices on loan delinquency in SACCOS in Meru County, Kenya. The study adopted a descriptive research design and the population consisted of all the 44 credit officers of SACCOs in Meru County. The study revealed that there exist a strong relationship between credit risk controls, collection policy and loan delinquency in SACCOs. Thus the study concludes that credit risk management practices significantly influenced loan delinquency in SACCOs in Meru County. The study recommends adoption of a more stringent policy on credit risk management practices in SACCOs for effective debt recovery

Kimotho and Gekara (2016) conducted a study on the effect of credit risk management and financial performance of commercial banks in Kenya. The purpose of study was to examine effect of credit risk management practices on financial performance of commercial Bank in Kenya. The study revealed that credit risk management procedures are used to influence profitability of the bank positively and also recommends the management of the banks to oversee facilitation of credit risk management as a substantial degree of standardization of process and documentation. The study recommended that the bank should consider risk identification as a process in credit risk management and focus on interest risks and foreign exchange risks to great extent in the risk identification map.

Alshatti (2015) examined the effect of credit risk management on financial performance of the Jordanian commercial banks during the period 2005 to 2013. Thirteen commercial banks were chosen to express on the whole Jordanian commercial banks. The research revealed that the credit risk management affects financial performance of the Jordanian commercial banks as measured by ROA and ROE. Based on findings, the researcher recommends amongst others that banks should improve their credit risk management to achieve more profits, banks should take into consideration the indicators of non-performing loans/gross loans, and that

banks should establish adequate credit risk management policies by imposing strict credit estimation before granting loans to customers.

Lagat*et al.* (2013) analyzed the effect of credit risk management practices on lending portfolio among savings and credit cooperatives in Kenya using data on risk identification, risk analysis, risk monitoring, risk evaluation and risk mitigation obtained from 59 SACCOs in Nakuru County. The study applied regression models in the analysis, and the results indicate significant effect of all the risk management practices on loan portfolio except risk evaluation which did not register significant effect on the lending portfolio of the SACCOs. The findings further showed almost all (99%) the respondents who participated in the study noted that monitoring was part of their credit management activities and it was influencing their lending portfolio to a great extent. From the findings of the study it was concluded that majority of the SACCOs have adopted largely risk management practices as a means of managing their portfolio.

Moti*et al.* (2012) examined the effectiveness of credit management system on loan performance of microfinance institutions. Specifically it sought to establish the effect of credit terms, client appraisal, credit risk control measures and credit collection policies on loan performance. The researchers adopted a descriptive research design. The respondents were the credit officers of the MFIs in Meru town. The results show that the credit management system variables have significant impact on loan performance of microfinance institutions. It also reports that collection policy has a higher effect on loan repayment at 5% significance level. The study recommends that microfinance institutions should consider credit insurance, signing of covenants, credit rating, reports on financial condition, and diversification in granting loans.

Mulondo (2011) investigated the relationship between credit risk management and loan performance of two development finance institutions in Uganda. The study found that loan appraisal showed a very strong significant relationship as compared to other risk management techniques such as risk transfer and risk diversification. The study recommends that considering that there is a significant positive relationship between loan appraisal and loan performance, it is important for the bank to formulate appraisal process/procedures, format that details ways of capturing all the credit risk. The appraisal process should identify and analyze all loss exposures, and measure such loss exposures. The appraisal process should capture key issues like capital adequacy, capacity of applicant, value of collateral, and repayment history.

Mutangili (2011) analyzed the relationship between credit risk management practices and the level of non-performing loans for commercial banks in Kenya. The study documented evidence of negative linkage between the level of non-performing loans and credit risk management practices in banks. He concludes that level of non-performing loans is inversely related to credit risk management practices. He therefore recommends that commercial banks should adopt various credit risk management practices to reduce the level of non-performing loans. In addition, he further recommends that sustainable and reliable credit database should be established for availability of credit information needed by banks.

Ochola (2009) evaluated the relationship between credit risk management and non-performing loans. The study show that a combination of intensive credit risk management by the banks coupled with close supervision by central bank has greatly enhanced the decline of non-performing loans ratio in the banking sector. Analyzing the asset quality of financial sector for 2003 to 2008, the ratio of gross non-performing loans to gross loans declined from

a high 35% in 2003 to a low of 9.23 in 2008. This decline supports evidence of close relationship of nonperforming loans and credit risk management.

2.7 Summary of Literature Review

Generally, from almost all surveys reviewed in the literature, it is evident that credit risk management is essential in optimizing the performance of micro financial institutions. In addition, an effective credit risk management involves establishing an appropriate credit risk environment, operating under a sound credit granting process, maintaining appropriate credit administration that involves the identification, analysis and monitoring process as well as adequate controls over credit risk.

According to Parrenas (2005), organizations have long viewed the problem of risk management as the need to control risks which make up most, if not all, of their risk exposure, credit, interest rate, foreign exchange and liquidity risk. While they recognize counterparty and legal risks, they view them as less central to their concerns. Where counterparty risk is significant, it is evaluated using standard credit risk procedures, and often within the credit department itself. Likewise, most micro financial institutions would view legal risks as arising from their credit decisions or, more likely, proper process not employed in financial contracting.

Research gaps exist since none of the studies address in detail the relationship between credit risk management and financial performance of commercial banks. In addition, majority of the studies were either done on credit risk management systems or on operational risk in banks. Research gaps also exist as this research will provide more literature for examining the theories reviewed. In addition, the majority of the studies were done in developed economies hence leaving scarce literature in developing economies.

This study sought to fill the existing research gap by answering the following research question, does there exist a relationship between credit risk management and financial performance of microfinance institutions in Masaka Municipality? The above chapter reviews the various theories that inform credit risk management and financial performance. In addition, an empirical review is conducted where past studies both global and local is reviewed in line with the following criteria, title, scope, methodology resulting into a critique. It is from these critiques that the research gap is identified.

2.8 Conclusion

The aim of the above literature review is to analyze the studies carried out on credit risk management on financial performance of micro finance institutions. In relation to the above discussion, the studies and theories have established the value of, credit risk management on financial performance of micro finance institutions. They, however, fail to highlight in clear terms the role of credit risk management on financial performance of micro finance institutions Therefore, the study attempted to establish the relationship between credit risk management and financial performance of micro finance institutions in Masaka Municipality.

CHAPTER THREE

METHODOLOGY

3.1 Introduction

This chapter gives the analysis of the particular methods that were used in the study and their rationale. It describes the research design, population size and sample frame, sampling procedures, data collection methods, data collection instruments, measurement of variables, data processing and analysis procedures. The chapter as well points at the limitations and constraints that were faced during the study process.

3.2 Research design

Burns and Grove (2003:195) define a research design as a blueprint for conducting a study with maximum control over factors that may interfere with the validity of the findings. Parahoo (1997:142) describes a research design as a plan that describes how, when and where data are to be collected and analyzed.

The researcher used a cross sectional case study design involving use of both qualitative and quantitative approaches. Oso and Onen (2009) defined a case study as a descriptive, exploratory or explanatory analysis of a person, a group or event and since the research design will use qualitative and quantitative methods, it is obvious that a case study was appropriate because case studies base on a mix of qualitative and quantitative evidence.

This is because the study concentrated on one financial institution as a case study and looked at all its credit risk management systems analytically with necessary descriptions.

3.3 Study population

According to Borg and Gall (1989), a target population is defined as all members of the real set of people, events or objects to which a research wishes to generalize the results of the study. The population study included staff from Pride Microfinance i.e. Credit Officer, Clients, Branch Supervisors and Manager. The number in the study population considered was 35.

Table 3.1 showing the study population

EMPLOYEE CATEGORY	**POPULATION**	**SAMPLE SIZE**
Manager	2	1
Supervisors	4	3
Credit officers	7	6
Clients	16	15
Others	7	7
TOTAL	**35**	**32**

3.4 Area of the study

The study was carried out from Pride Microfinance (M D I) which is a Private Microfinance Institution located in Masaka District, in Katwe Butego division, Masaka Municipality on

Kampala road. The institution serves Greater Masaka Region with districts including; Masaka, Kalangala, Lyantonde, Rakai, Ssembabule, Kalaungu, Lwengo and Bukomansimbi.

3.5 Sample size and selection

Sampling is the process of selecting a number where individuals or objects from a population such that the selected group contains elements representative of the characteristics found in the entire group (Orodho and Kombo, 2002)

The sample size for the study was 32 staff of the 35 staff were considered in the study population in the institution. The number of sample size was selected because according to Robert V. Krejcie (1960), for every 35 respondents at least 32 people should be sampled to get the appropriate study findings of a given study topic.

The researcher used simple random sampling technique because it ensures that each member of the target population has an equal and independent chance of being included in a sample and avoids biasness. This applied to both the employees and customers. Purposive sampling was used according to their positions because they are assumed to have the desired information in relation to the topic of study and to get reliable information.

3.7 Methods of data collection and instruments

These are the tools the researcher employed during the process of data collection in the area of study for efficient and effective data collection. The researcher used questionnaires as a method of data collection. The research instrument was well-designed, edited and pre-tested questionnaire before administering it to ensure its quality, reliability and validity. The questionnaire contained both open and closed ended questions and statements, was self-administered in a way that each respondent had the opportunity to fill in the questionnaire

and where assistance required it was offered. This gave chance to the respondent to tick the appropriate answers and fill in answers of their choice.

This method was convenient because it provided the respondents with ample time to think and respond to the questions hence respondents were assumed to be free and unbiased during the provision of sensitive information.

3.8 Data management and analysis

The information was gathered, recorded and edited for completeness, legibility, consistency and clarification, uniformity and easy comprehension in preparation for analysis.

The researcher used two approaches to analyze data, these include; qualitative and quantitative analysis. Raw data was grouped, edited and coded where necessary and entered manually into the computer for processing and for quantitative data; descriptive statistics were used in form of tables

3.9 Quality control methods

3.9.1 Validity

Validity is the extent to which the data collection instruments that were used in the study actually measure what they are intended to measure. Validity is concerned with whether the findings are really about what they appear to be (Kombo, 2006).

In order to ensure validity of information which was to be collected, the researcher used pre-tested questionnaires so as to determine whether the instruments used will give the best results. To ensure external validity, the researcher considered all genders, departments and age so as to avoid getting biased results.

3.9.2 Reliability

Reliability is the consistency of measurement or the degree to which an instrument measures the same way each time used repeatedly. Reliability was used by consulting skilled people concerning phrasing of statements in the questionnaires and approved by the supervisor, pilot study and testing were done by the researcher to determine the reliability and validity.

This helped the researcher to get information that was necessary for the study as well as obtaining respondent's compliance depending on the questionnaires.

3.10 Ethical considerations

The researcher observed confidentiality of the information that was given on questionnaires in a way that from the individual from whom data was collected was referred to as anonymous where by the names and any form of identification was excluded.

The respondent's information was not passed on to a third party and the researcher avoided any form of plagiarism and sought respondents consent before administering the questionnaires.

The researcher conducted himself in an honest and respectful manner to all the respondents and trust worthy when presenting the findings about the study.

A letter of introduction was obtained from the administration of Uganda Martyrs University after approval of the proposal by the supervisor and the research committee. The letter was then taken to the management of pride microofinance for introduction.

Respondents were informed about the purpose of the study, freedom of participating or withdrawal at any stage, and their consent was obtained before inclusion in the study and they

were informed that the information provided would only be used for research purpose and responses given would not affect the quality of care offered.

3.11 Limitations

1. Time; the time given to complete the study was so fixed and therefore there was a need for the researcher to overcome this by working very hard to finish on time.
2. Heavy schedule; the respondents had a busy schedule thus being unreliable for researcher to seek for their participation since they are working in a health public institution where they need not to neglect the patients.
3. Some of the respondents never felt free to reveal some information for fear of being victimized. This was overcome by explaining to them that confidentiality would be involved in the study and no names would be revealed during the study.
4. There researcher faced a challenge of financial constraints during the process of carrying out the study; but he tried to minimize costs by carrying out the research himself.
5. The researcher focused only on one public institution due to lack of funds and limited time and so the study results could not be generalized since the research was only done in only one public organization hence may not give a true picture of the state of procurement planning in all public organizations.

3.12 Delimitations

The study was limited to only one financial institution that is pride microfinance masaka which is a branch of pride microfinance found in kampala with a primary purpose of providing financial services among Ugandans.

3.13 Conclusion

This chapter has defined the different methods that were used in the study. For every method identified was taken as independent so as to arrive at the expected objectives of the study and the results was accessed during data findings and discussions before conclusions are made about the study.

CHAPTER FOUR

PRESENTATION, ANALYSIS AND DISCUSSIN OF FINDINGS

4.1 Introduction

This chapter was devoted to the analysis of data, interpretation and discussion of major findings based on the topic under study. Respondents were made up of Credit Officers, manager, and clients. The main credibility characteristics in this study were the respondents' professional background, Gender, level of Education and years worked in the position.

A total of 32 questionnaires were distributed to the respondents who constituted the study population and 27 questionnaires were collected back having been filled completely however the 5 questionnaires were not returned by the respondents. This constituted a response rate of 84% which according to Mugenda and Mugenda (1993) a response rate of more than 80% is sufficient for a study.

Data was analyzed using qualitative and quantitative approaches. Raw data was grouped, edited, coded and entered manually into the computer for processing; descriptive statistics were used in form of tables and pie charts for qualitative data. The results are presented in tables and figures to highlight the major findings for quantitative data to depict clearly the results in the institution.

4.2 Respondents Background Information

4.2.1 Demographic Characteristics

This section sought to establish the information on the respondents employed in the study with regards to the gender, their level of education, profession and duration of service. These

bio data points at the respondents' appropriateness in responding to the study questions required for the study to be complete.

4.2.2 Gender of the respondents

The respondents were asked to tick against their gender; this was to guide the researcher on making logical conclusions regarding the degree of congruence of responses with the gender characteristics on the services in pride microfinance. The results of the study are presented in the table and figure below:

Table4. 1 Shows the respondents' gender

Gender	Frequency	Percent
Male	15	55.6
Female	12	44.4
Total	27	100.0

Source: Primary Data (2018)

The results as shown in the table 1 show that majority of the respondent were male at 55.6% while female were 44.4%. The results indicate that majority of the respondents were male, who are employees and clients of Pride Micro Finance

.

4.2.3 Level of education:

This helped the researcher understand the level of education of the employees and clients of Pride Micro Finance. The results of the study are presented in figure below:

Table 4.2 Shows the Respondents' Level of Education

	Frequency	Percent
bachelors	5	18.5
postgraduate	8	29.6
diploma	9	33.3
others	5	18.5
Total	27	100.0

Source: Primary Data (2018)

The study findings indicate that 29.6% of the respondents are first degree graduates, 18.5% are post graduate degree holders, 33% had Diplomas and 18% had other study qualifications like Certificates. All employees and clients of Pride Micro Finance were found to be degree, diploma and at least certificate holders therefore, they provided information based on the academic knowledge they have gained in microfinance institutions.

4.2.4 Occupation held in the organization

The respondents were asked to indicate the profession/ occupation that they held in the organization. This was expected to help the researcher know the kind of work the employees and clients had and how effective they would be able to give information about the topic of

study. The results are shown in the figure below as by categorization of the researcher's choice

Table 4.3 Shows the respondents' Occupation

	Frequency	Percent
Manager	1	3.7
credit officer	3	11.1
branch supervisor	2	7.4
Client	15	55.6
Others	6	22.2
Total	27	100.0

Source: Primary Data (2018)

From Table 4.3, 55.6% which is majority of the respondents were clients to Pride Microfinance who obtain Loans and credits from the institutions and utilize them, 11.1% of the respondents are Loan Officers who issue loans to clients as well as overseeing them to ensure proper usage including paying the loan on time, while 7.4% work as Supervisors and 22.2% others including Tellers at the Branch Respectively, 3.7% are the Branch Managers at PMFI who authorizes most of the activities including insurance of loans to clients.

The findings therefore indicated that majority of the Respondents in PMFI are clients who apply for loans and manage them by using them for intended purposes as well as paying them back on time thus they are familiar about the credit management activities and how they influence financial performance of PMFI.

4.2.5 Period served in the organization

The respondents were asked to indicate the number of years they had worked in the organization. This was expected to help the researcher to gauge how effective and reliable the information given by the respondents is to the topic of study depending on their experience in the organization. The results are shown in figure below:

Table 4.4 Shows the Respondents' Period Served in the Organization

	Frequency	Percent
less than 1 year	5	18.5
1-5 years	14	51.9
6-10 years	5	18.5
over 10 years	3	11.1
Total	27	100.0

Source: Primary Data (2018)

From Figure 4, 18.5% of the respondents have been in the institution for less than 1 year, majority of the respondents 51.9% had worked in the institution between 1 and 5 years, while

18% had worked between 6 and 10 years and 11.1% have been in the institution for over 10 years.

The findings therefore indicated that majority of the employees and clients in PMFI had worked planning and service delivery in PMFI.

4.3 Indicators of Credit Risk Management and Financial Performance

Risk identification refers to the process of identifying dangerous or hazardous situations and trying to characterize it. It is a procedure to deliberately analyze, review and anticipate possible risks (Barton, 2002). Credit Risk Analysis and Mitigation. This is the process of determining the likelihood that a specified negative event will occur. Investors and business managers use risk assessments to determine things like whether to undertake a particular venture, what rate of return they require to make a particular investment and how to mitigate an activity's potential losses

Table 4.5 showing statistics of indicators of credit risk management and financial performance

Statements	Mean	SD
Credit risk identification is one of the credit risk management indicators in micro finance institutions.	3.93	1.439
Credit risk analysis is one of the credit risk management indicators in micro finance institutions	3.22	1.396
Credit risk mitigation is one of the credit risk management indicators in microfinance institutions.	3.00	1.664

Source: primary data (2018)

From table4. 5, majority of the respondents agreed respectively that credit risk identification is one of the indicators of credit risk management with a mean of (3.93), however some respondents were not agreeing with the statement with the standard deviation of (1.439). Therefore, the majority respondents agreed with (Kromschroder and Luck, 1998) who according to his study concluded that the first step in organizing the implementation of the credit risk management function is to establish the crucial risk observation areas inside and outside the corporation.

From the research findings, majority respondents agreed that credit risk analysis is one of the indicators of credit risk management with a mean of (3.22), and a standard deviation of (1.396). The majority respondents agree with Moore (2007) who found out in his study that risk analysis particularly on measuring risk in banking institutions is important for risk management practices

The respondents were asked whether credit risk mitigation is an indicator of credit risk management, the respondents views were presented with a mean of (3.00) and a standard deviation of (1.664). Majority of the respondents agree with Fuser et al, 1999 who noted that in practice, it is useful to classify the different risks according to the amount of damage they possibly cause so as to make it easier to develop a comprehensive plan for mitigating them.

4.4 Indicators of Financial Performance on the profitability

Table 4.6 showing statistics of indicators of financial performance on the profitability.

Statements	Mean	SD
Profitability of pride microfinance indicates its financial performance.	3.41	1.448
Credit availability to clients indicates the financial performance of pride microfinance	3.41	1.500
Reduced risk in the banking system indicate the financial performance of pride microfinance	3.52	1.533

Source: primary data (2018)

From the table above, majority of the respondents agreed that profitability of pride microfinance indicates the financial performance with a mean of (3.41) and a standard deviation of (1.448).Thus this indicates that the majority respondents agree with Stoner (2003) as cited in Turyahebya (2013), who defines financial performance as the ability to operate efficiently, profitably, survive, grow and react to the environmental opportunities and threats.

From the research findings, majority respondents agreed that the availability of credit to clients indicates the profitability of pride microfinance with a mean of (3.41) and a standard deviation of (1.500). According to majority respondents they agree with Mugenda, 2008 who noted Some useful measures of financial performance that he coined into what is referred to

as CAMELS (Capital adequacy, Asset quality, Management, Earnings, Liquidity and sensitivity) referring to the six components of a bank's conditions that are assessed.

The respondents agreed that reduced risk in the banking system of Pride Microfinance improves on its performance this was presented with a mean of (3.52) and a standard deviation of (1.533). According to the majority respondents it indicates that reduced risk in the banking system banking improves on its financial performance thus conquering with Al-Tamimi& Al Mazrooei (2007) who stipulates that all banks in the present-day volatile environment are facing a large number of risks such as credit risk, liquidity risk, foreign exchange risk, market risk and interest rate risk, among others and such risks may threaten a bank's survival and success and thus banking is a business of risk and for this reason, efficient risk management is absolutely required to improve on its performance.

4.5 Credit risk management and financial performance.

Table 4.7 statistics of credit risk management and financial performance.

Statements	Mean	SD
Credit risk identification affects profitability of pride microfinance.	3.56	1.368
Credit risk analysis affects the profitability of pride microfinance	3.41	1.500
Credit risk mitigation affects the profitability of pride microfinance	3.15	1.610

Source: primary data (2018)

From table above, majority of the respondents agreed that credit risk identification affects profitability of pride microfinance with a mean of (3.56) and a standard deviation of (1.368).Basing on the majority respondents who agreed that credit risk identification affects

the profitability of microfinance institutions, thus agreeing with Al-Tamimi (2002) who suggested that in managing risk, commercial banks can follow comprehensive risk management process which includes eight steps: of which one of them is risk identification; data gathering and risk quantification; management objectives; product and control guidelines; risk management evaluation; strategy development; implementation; and performance evaluation.

The respondents agreed that credit risk analysis affects profitability of pride microfinance institution, Basing on the majority respondents who agreed it indicates that credit risk identification affects the profitability of microfinance institutions, thus agreeing with Al-Tamimi (2002) who suggested that in managing risk, commercial banks can follow comprehensive risk management process which includes eight steps: of which one of them is data gathering and risk quantification and performance evaluation thus indicating that credit analysis affects the profitability of PMF.

Majority respondents agreed respectively that credit risk mitigation affects profitability of pride microfinance with a mean of (3.15) and a standard deviation of (1.610). From the majority point of view Basing on the majority respondents who agreed it indicates that credit risk mitigation affects the profitability of microfinance institutions, thus agreeing with Al-Tamimi (2002) who suggested in his study that to improve on the financial performance of banking institutions there should be management objectives; risk control guidelines; risk management evaluation; strategy development; implementation; and performance evaluation.s

Table 4.8: shows relationship between profitability and credit risk.

		profitability indicates the financial performance	reduced risk indicates the financial performance
profitability indicates the financial performance	Pearson Correlation	1	.0621
	N	27	27
reduced risk indicates the financial performance	Pearson Correlation	.0621	1
	N	27	27

Source: primary data (2018)

From the table above, there was a strong positive relationship between profitability and reduced risk showed by r= 0.621. This implied that reduced risk in the banking system affects the profitability

Table 4.9: relationship between credit risk identification and credit risk analysis

		credit risk identification is an indicator of CRM	credit risk analysis is an indicator of CRM
credit risk identification is an indicator of CRM	Pearson Correlation	1	.012
	N	27	27
credit risk analysis is an indicator of CRM	Pearson Correlation	.012	1
	N	27	27

From the table above, the pearson's correlation coefficient was 0.012. This implies that there is a very weak positive relationship between credit risk identification and credit risk analysis.

Table 4.10s. Relationship between credit risk identification and credit risk mitigation.

		credit risk identification affects profitability	credit risk mitigation affects profitability
credit risk identification affects profitability	Pearson Correlation	1	.046
	N	27	27
credit risk mitigation affects profitability	Pearson Correlation	.046	1
	N	27	27

From the table above, the pearson's correlation coefficient was 0.046. This means there is a very weak positive relationship between credit risk identification and credit risk mitigation.

Conclusion

The findings of this study concur with studies by (Afriyie*et al*. 2011; Hosna*et al*., 2009; Ogboi and Unuafe, 2013; Marshal and Onyekachi, 2014) explained that there exist a significant negative association between credit risk management components and financial performance. Duca and McLaughlin (1990) conclude that variations in bank profitability are largely attributable to variations in credit risk management components, since increased exposure to credit risk is normally associated with decreased firm profitability. These triggers a discussion concerning commercial banks that are exposed to highrisk loans tend to have higher the accumulation of unpaid loans and the lower the profitability. From the study a

conclusion can be made that credit risk management components affect the performance (performance) of microfinance institutions.

From the research findings of objective one, loans improved the financial performance of medium scale enterprise. Medium scale enterprises which took long term loans recorded improved financial performance in their operations. Short term loans contributed to the profitability of such businesses. The data collected from the field, 14.3% of respondents disagreed that short term loan interest rate charges were fair.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.0 Introduction

This chapter presents the summary of findings, conclusion and recommendations that were presented objective by objective. The presentation was guided by three objective which guided the entire data collection and analysis

5.1 Summary of findings

5.1.1 Summary of Background Findings

This study was conducted on 27 respondents of whom 55.6% were male and 44.4% were female, their level of education included 18.5% who had attained a bachelors' degree, 29.6% postgraduate qualifications, 33.3% and 18.5% had attained diploma and other relevant study qualifications respectively. Among the respondents 3.7% work as managers of PMF, 7.4% work as branch supervisors, 11.1% work as credit officers in the institution, 22.2% work as tellers and 55.6% of the respondents were clients.18.5% of the respondents had worked in the institution for less than 1 year, 51.9% served the institution between 1-5 years, 18.5% had worked with pride for the period between 6-10 years, and 11.1% had worked with pride for over 10 years respectively.

5.1.2 Summary of indicators of credit risk management and financial performance.

from the findings the analysis revealed that there was a very weak positive relationship between credit risk identification and credit risk analysis with a correlation coefficient showed by r= 0.012. According to his study concluded that the first step in organizing the implementation of the credit risk management function is to establish the crucial risk observation areas inside and outside the corporation.

The study found out that indicator of credit risk management highly contributes to the financial performance of pride microfinance as many of the respondents agreed in table 5

As well the respondents agreed that credit risk analysis is one of the indicators of financial performance of pride microfinance in table 5, and many of the respondents agreed in table 5 that credit risk mitigation is one of the credit risk management indicators in microfinance institutions.

5.1.3 Summary of financial performance on the profitability.

The study found out that to some extent indicators of credit risk management contributes to financial performance of pride microfinance; this is shown in table 6 where many of the respondents agreed, in table 6 many of the respondents agreed that credit availability to clients indicates the financial performance of pride microfinance,. However in table 6, many respondents agreed that the reduced risk in the banking system indicates and improves the financial performance of pride microfinance.

5.1.4 Summary of credit risk management and financial performance

The study found out that credit risk management affects financial performance of pride microfinance. This is shown in table 7 where many of the respondents agreed that credit risk identification affects the profitability of pride microfinance. As well in figure 7, many of the respondents agreed the credit risk analysis affects the profitability of pride. However, in table 7 many of the respondents agreed that credit risk mitigation affects the profitability of pride microfinance.

5.2 Conclusions.

5.2.1 Summary of indicators of credit risk management and financial performance.

The researcher concludes by saying the pearson's correlation coefficient was 0.012. This implies that there is a very weak positive relationship between credit risk identification and credit risk analysis.

5.2.2 Summary of financial performance on the profitability.

The researcher concludes that, there was a strong positive relationship between profitability and reduced risk showed by r= 0.621. This implied that reduced risk in the banking system affects the profitability.

5.2.3 Summary of credit risk management and financial performance

The pearson's correlation coefficient was 0.046. This means there is a very weak positive relationship between credit risk identification and credit risk mitigation.

5.3 Recommendations of the study

5.3.1 Indicators of credit risk management and financial performance.

From the analysis, the management should identify the risk at early stage to enable the institution from facing over increasing risks. They should also make policies that will govern borrowers on returns. The loan officers should provide credit to clients on time to enable them use loans at the time they are needed. This will increase the number of borrowers hence increase in the level of financial position of the institution.

5.3.2 Financial performance on the profitability

The management should measure the results of the firm's policies and operations within a specified period of time in monetary terms. The results should be expressed in form of profits or losses.

5.3.3 Credit risk management and financial performance

The management should know how effective credit risk management contributes to reduction of defaults by counterparty as well as restricting uncertainty of achieving the required financial performance.

5.4 Suggestions for further research

The introduction of comp scan in Uganda was intended to help on the issue of having and organized credit industry in Uganda and also fighting fraudsters and defaulters. Therefore, for further research, a study to analyze the impact and effectiveness of the credit s bureau in controlling credit risk in MDIs can be undertaken.

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APPENDIX I

QUESTIONNAIRE FOR RESPONDENTS

Dear respondent,

The researcher is **Nassolo Janefer** a student of Uganda Martyrs University, as part of completion requirements for the ward of Bachelors' Degree in Business Administration and Management, the student is undertaking a research by using your Institution as a case study on the topic:

"Credit risk management and financial performance" a case study of pride microfinance

Please be assured that this is purely an academic exercise and thus the information you provide will be treated with the utmost confidentiality and will not be linked to you in any way. It would therefore be most appreciated if your answers to the following questions are as candid as possible.

SECTION A: RESPONDENT BACKGROUND INFORMATION

Gender of respondent

Male ☐ Female ☐

Highest level of education

Bachelors' Degree (including honors) ☐

Postgraduate (MA/MSc/MPhil/PhD) ☐

Diploma ☐

Other (please specify)……. ☐

☐

Occupation

Manager ☐

Credit officer ☐

Client ☐

Others (please specify)…… ☐

How long have you worked in your current position?

Less than 1 year ☐ 6-10 years ☐

1-5 years ☐ Over 10 years ☐

SECTION B: INDICATORS OF CREDIT RISK MANAGEMENT AND FINANCIAL PERFORMANCE

SA: Strongly Agree, **A:** Agree, **N:** Not Sure, **DA:** Disagree, SD: Strongly disagree

Statements	**SD**	**DA**	**N**	**A**	**SA**
Credit risk identification is one of the credit risk management indicators in micro finance institutions.					
Credit risk analysis is one of the credit risk management indicators in micro finance institutions					
Credit risk mitigation is one of the credit risk management indicators in microfinance institutions.					

SECTION C: INDICATORS FINANCIAL PERFORMANCE ON THE PROFITABILITY

SA: Strongly Agree, **A:** Agree, **N:** Not Sure, **DA:** Disagree, SD: Strongly disagree

Statements	**SD**	**DA**	**N**	**A**	**SA**
Profitability of pride microfinance indicates its financial performance.					
Credit availability to clients indicates the financial performance of pride microfinance					
Reduced risk in the banking system indicate the financial performance of pride microfinance					

SECTION D; CREDIT RISK MANAGEMENT AND FINANCIAL PERFORMANCE

SA: Strongly Agree, **A:** Agree, **N:** Not Sure, **DA:** Disagree, SD: Strongly disagree

Statements	**SD**	**DA**	**N**	**A**	**SA**
Credit risk identification affects profitability of pride microfinance.					
Credit risk analysis affects the profitability of pride microfinance					
Credit risk mitigation affects the profitability of pride microfinance					

THANK YOU

APPENDIX II: RESEARCH PROJECT BUDGET

NO	ITEM	TOTAL COST (UGX)
1	Stationary	50,500
2	Transport	20,000
3	Printing	110,000
4	Photocopying	30,000
5	Data	15,000
6	Binding	10,000
7	Airtime	5,000
8	Compact disk	15,000
9	Others	30,000
	TOTAL	**285,500**

APPENDIX III:

MORGAN TABLE FOR DETERMINING SAMPLE SIZE

Table for determining sample size from a given population.

Table 3.1

Table for Determining Sample Size of a Known Population

N	S	N	S	N	S	N	S	N	S
10	10	100	80	280	162	800	260	2800	338
15	14	110	86	290	165	850	265	3000	341
20	19	120	92	300	169	900	269	3500	346
25	24	130	97	320	175	950	274	4000	351
30	28	140	103	340	181	1000	278	4500	354
35	32	150	108	360	186	1100	285	5000	357
40	36	160	113	380	191	1200	291	6000	361
45	40	170	118	400	196	1300	297	7000	364
50	44	180	123	420	201	1400	302	8000	367
55	48	190	127	440	205	1500	306	9000	368
60	52	200	132	460	210	1600	310	10000	370
65	56	210	136	480	214	1700	313	15000	375
70	59	220	140	500	217	1800	317	20000	377
75	63	230	144	550	226	1900	320	30000	379
80	66	240	148	600	234	2000	322	40000	380
85	70	250	152	650	242	2200	327	50000	381
90	73	260	155	700	248	2400	331	75000	382
95	76	270	159	750	254	2600	335	1000000	384

Note: N is Population Size; S is Sample Size *Source: Krejcie & Morgan, 1970*

APPENDIX IV:

INTRODUCTION LETTER