# THE EFFECT OF CREDIT POLICIES ON THE PERFORMANCE OF COMMERECIAL BANKS IN UGANDA

**CASE STUDY: KENYA COMMERCIAL BANK. KAMPALA**

**ROAD BRANCH**

**BY**

**JUAN SCOVIA**

**2013-BO21-10014**

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**AN UNDERGRADUATE DISSERTATION PRESENTED TO THE FACULTY OF**

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# DEDICATION

This thesis is dedicated to my beloved husband Jai Godfrey lokabang, Mother Guo Cilicia, my Sister Joggo Annet Giryang and brothers for their patience, endurance and understanding during my absence**.** Finally this thesis is dedicated to all members of the Family.

# ACKNOWLEDGEMENTS

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## LIST OF ABBREVIATIONS

| | |
|---|---|
| KCB | Kenya Commercial Bank |
| 5Cs | Character, Capacity, Collateral, Capital and Condition |
| CAR | Capital Adequacy Ratio |
| NPL | The Non-Performing Loans |
| ROE | Return On Equity |
| CPI | Consumer Price Index |
| BOU | Bank Of Uganda |
| SPSS | Statistical Package for Social Science |
| PQM | Portfolio Quality Management |
| STDDEV | Standard Deviation CVL- Coefficient of the Validity index. |

# ABSTRACT

This research examined the effect of credit policies on the performance of commercial banks in Uganda with Case study Kenya commercial bank (KCB). It looked at the objectives which are; To evaluate the effect of credit appraisal on the performance of Kenya Commercial Bank, To evaluate the effect of loan approval on the performance of Kenya Commercial Bank., To evaluate the effect of loan disbursement on the performance of Kenya Commercial Bank., To establish the relationship between loan recovery and the performance of Kenya commercial banks. A descriptive research design was used to collect the data from the field and a simple random sampling and Purposive sampling techniques were used to come up with a sample of 48 respondents. A questionnaire was used to collect data from 48 respondents in KCB. However only 48 questionnaires were returned. Both descriptive and inferential analysis was done. Analysis of Variance and regression analysis were used to test the hypothesis. The results showed that there is a positive relationship between Loan Recovery management and financial performance of commercial banks in Uganda.

The main motive for this research was to come up with policies such that KCB can recover loans from defaulters, bank can provide some advice to the borrower for repaying the loan. However from the findings of the research study, a strong positive relationship ($r = 0.755$) was revealed which implies that reasonable loan recovery values boosts financial performance of the financial institution. Therefore, the researcher recommended that there is need for commercial banks to enhance their customer's techniques so as to improve their financial performance. Through client appraisal techniques, the companies could be able to know credit worth customers and thus reduce default and enhance their collection procedures and policies by adapting a more policies for effective loan recovery.

# CHAPTER ONE

## 1.0 GENERAL INTRODUCTION

### 1.1 Introduction

This study investigated credit policies on the performance of commercial Banks. This chapter of the study presents the background of the study, statement of the problem, general objective, specific objectives, research questions, Scope of the study, significance, justification of the study and definition of key terms and the conceptual framework of the study.

### 1.2 Background to the study

The strength of any financial institutions lies in the hands of its ability to get a recommendable return from its outreach activities that involve release of credit to its esteemed customers and different business partners (Jun, S.G., (2003). Credit lending is the principle business activity for most commercial banks. The loan portfolio is typically the largest asset and the predominate source of revenue. As such, it is one of the great sources of risk to the bank's safety and soundness.

Credit policy is a set of policy actions designed to minimize costs associated with credit while maximizing the benefit from it (Kakuru, 2003). The objective of this policy is to have optimal recovery from debtors as a firm may follow a lenient or stringent credit policy. Credit terms are standards applied by commercial banks in determining the ability to repay loans. These terms help in assessing credit worthiness of borrowers and hedge against the risk of loss in case of non repayment decide the types of customers for purpose of extending credit such as capital adequacy and asset quality. They include collateral, interest rate and repayment period (Agarwal, 2006). Access to credit refers to the availability of a supply of reasonable quality financial

services at a reasonable rate .performance of commercial banks is the ability of the bank to contribute to job and wealth creation through business start up, survival and growth (Sandberg, 2002). Improved access to credit helps bank grow and advance their financial performance (Claessens, 2006 and Bamford, 1997). On the other hand acquisition of such credit has proved to be difficult due to credit terms that are perceived to be unfavorable. According to Kakuru (2008), in Uganda collateral is up to a tune of 150% of the loan, the repayment period is as short as 24 months, and interest rates range from 23% to 30% per month. Despite the important role that commercial banks are expected to play in the economy of Uganda, there are a number of constraints which act as barriers to the emergence and growth of a sustainable financial sector. The Ministry of Finance, Planning and Economic Development (2000), UNCTAD (2002) and Stevenson and St.Onge (2005) emphasize that the major constraints that the financial sector faces include: operations as an informal sector, the size of their operations is too small to enable enjoyment of economies of scale, poor production technology, limited access to markets, limited managerial skills, government bureaucracy and limited access to banking facilities.

The economic development of any country depends largely on the amount of investible funds available to her and the efficiency of her financial intermediaries to mobilize such funds from savers who have no immediate use of it and distribute to investors who need funds for productive purposes. One of the major intermediaries with this task is to increase the performance of commercial banks. (Ojo et. al, 1982).

Banking as a service industry is organized to make profit for the owners, (the shareholders), through the provision of banking services and supply of financial needs of individual and corporate bodies. According to Bidani et al, (2004), in a bid to maximize shareholders wealth and ensure safety of depositors fund, banks act as delegated monitors on behalf of lenders

(depositors) using various innovations, technologies and procedures to enforce credit contracts and asserts that these measures notwithstanding**,** banking operations are still exposed to some inherent risks including borrowers' outright default; unwillingness or inability to meet credit commitment due to the vagaries of business activities or other environment dynamics.

Regulators have always fostered an expectation that capital is what sustains banks in periods of stress and prevents them from failure and if it isn't capital, then it is the management culture which has embedded in its people and processes and this is through the incentives for individual compensation that balance risk and return with short-term self-interest and long-term stake holder goals together with the early warning system that highlight growing exposures to risk (Allan et al., 2011). In practical term, the essence of lending demands that, the lender temporarily parts with the possession and the use of what is lent whilst retaining the legal ownership of it, and due time, expects the resumption of the possessor and utility on the property lent out.

The importance of a credit policy is to maximize the value of a firm (Puxty and Dodds, 1991). An optimum credit policy is achieved through proper adjustment of credit standards, credit terms and collection efforts. Credit policy enhances credit administration, increases market share, retention of existing customers, acquisition of new ones, improves risk management and increases financial performance (Pandey, 2001). In Kenya, regulated banks have adopted credit policies and submit financial returns on monthly and quarterly intervals for offsite monitoring and Hence commercial banks manage depositors' funds with the hope of achieving the major objectives of liquidity, safety and profitability. Achieving this objective, while creating credits involves lot of risks, since the borrowers may not pay back as expected. This could lead to eventual liquidity crunch on the lending bank and therefore, loss of confidence in it by depositors (Adekanye 2010).As financial intermediaries, banks provide means by which funds can be

transferred from the surplus unit of the economy to the deficit unit. This role is performed primarily through the acceptance of deposits of different categories and characteristics for onward lending to the numerous customers by way of loan and advances. They seek to make themselves as attractive as debtors and as efficient as creditors that they earn a substantial gross income from the difference between the interest they charge as creditors and the interest they pay as debtors (Ayodele, 2014). In most cases, when banks grant loans, they expect the customers to repay the principal and interest on an agreed date. The non-performing loans (NPL) represent credits which the banks perceive as possible loss of funds due to loan defaults. They are further classified into substandard, doubtful or lost. Bank credit in lost category hinders banks **f**rom achieving their set targets (Kolapo et al, 2012).. To guide against negative consequences that may arise as a result of the above, banks need to map out clear policies and guidelines for efficient and effective credit operations.

Hence, the study tries to assess credit policies and management put in place by KCB to see how adequate they are in coping with the emerging threats in the Ugandan banking industry and proffers solutions in order to forestall another round of distress in the banking industry.

### 1.3 The Problem Statement

Credit policies are important in an organization because they maintain a good cash flow, reduce the risk of bad debts and minimize in the cost of granting credit hence, Commercial Banks need credit policy measures against inability clients and deliberate defaulters who willingly refuse to pay back the loan due to imprudent behaviors (AMFIU 2005).

Increasing amount of non-performing loans in the credit portfolio is inimical to banks in achieving their objectives and according to Ahmad and Ariff (2007).Kenya commercial bank

charges high interest rate thus leading to increase and persistent losses in the institution (Muzaale 2005). According to Bank of Uganda's annual supervision report (2012/2013), the Banking sector is facing some deterioration in terms of the quality of the loan portfolio due to arise in credit defaults attributed partly to the high interest rates that prevailed in 2012 where the Barclays bank made a profit of $10,104 in the financial year 2011/2012 and then a net loss of $129,709 in the financial year 2012/2013. Stanbic bank also stated a decline of shs28.9bn where the profits dropped from 130.7bn shillings in 2012 to 101.8bn shillings in 2013 due to risk exposures (Stanbic annual report 2012/2013). In addition to this, profitability in the banking sector declined largely due to non-performing assets which increased from 4% to 6.2% (budget speech, financial year 2014/2015). This therefore raises the need to know the extent to which commercial banks set their policies or strategies to manage such risks and how they relate or affect their financial performance.

### 1.4 Purpose or General Objective

The overall objective of the study is to assess credit policies on the performance of commercial Banks in Uganda

### 1.5 Specific objectives

- ❖ To evaluate the effect of credit appraisal on the performance of Kenya Commercial Bank.
- ❖ To evaluate the effect of loan approval on the performance of Kenya Commercial Bank.
- ❖ To evaluate the effect of loan disbursement on the performance of Kenya Commercial Bank.
- ❖ To established the relationship between loan recovery and the performance of Kenya commercial banks.

## 1.6 The Research Questions.

- What are the effect of credit appraisal on the performance of Kenya commercial bank?
- What is the effect of loan approval on the performance of Kenya commercial?
- What is the loan disbursement on the performance of Kenya commercial banks?
- What is the relationship between loan recovery and the performance of Kenya commercial bank?

## 1.7.0 The scope of the study

### 1.7.1 Geographical scope

The study was focus on Kenya commercial bank Uganda main branch on Kampala road in Kampala city.

### 1.7.2 Content scope

The study was focus on the effect of credit policies but emphasis was put on credit appraisal, loan approval, loan disbursement and loan recovery while focusing on the performance of commercial banks like Market share, Capital adequacy, and Profitability and Portfolio quality.

### 1.7.3 Time scope

The study covered a period of five years that is from 2012-2016 in order to capture previous and latest statistics.

## 1.8 Justification of the study

The main motive for this research was to come up with policies such that KCB can recover loans from defaulters

## 1.9 Significance of the study

- The study intends to help commercial bank to understand the effectiveness of credit policies that could be used to expand the loan recovery.
- The study intends to benefit management of Kenya commercial banks –Uganda by suggesting ways in which it can sustainably improve its credit policies.
- The study will help the researchers to satisfy the requirements that lead to the award of degree in Business Administration and Management.
- To the researchers, the study may act as a focal point in carrying out on similar problems.
- For students of a related course, it will form a basis of knowledge which will enlighten them on how credit policies like credit appraisal of the applicants, Loan approval, loan recovery and Loan disbursement influence performance of commercial Banks
- Finally the result of the findings will be of benefit to management of KCB on how best to improve their performance through credit policies.

### 1.10.0 Definition of key terms

**Credit policies;** set of principles a financial organization or business uses in deciding who it will loan money.

**Credit Appraisal**; this is the first step in limiting credit risk involves screening clients to ensure that they have the willingness and ability to repay a loan

**Loan Approval**; this is the last step in the credit initiation and analysis process in commercial banks.

**Loan recovery**; is the debt collection policy (recovery policy) of the bank is built around dignity and respect to customers.

**Loan disbursement**; this is the fourth element of the credit management process use in commercial banks.

**Market share**; this is the percentage of a market (defined in terms of either units or revenue) accounted for by a specific entity.

**Capital Adequacy**; this is the determination of the minimum capital amount required to satisfy a specified economic capital constraint.

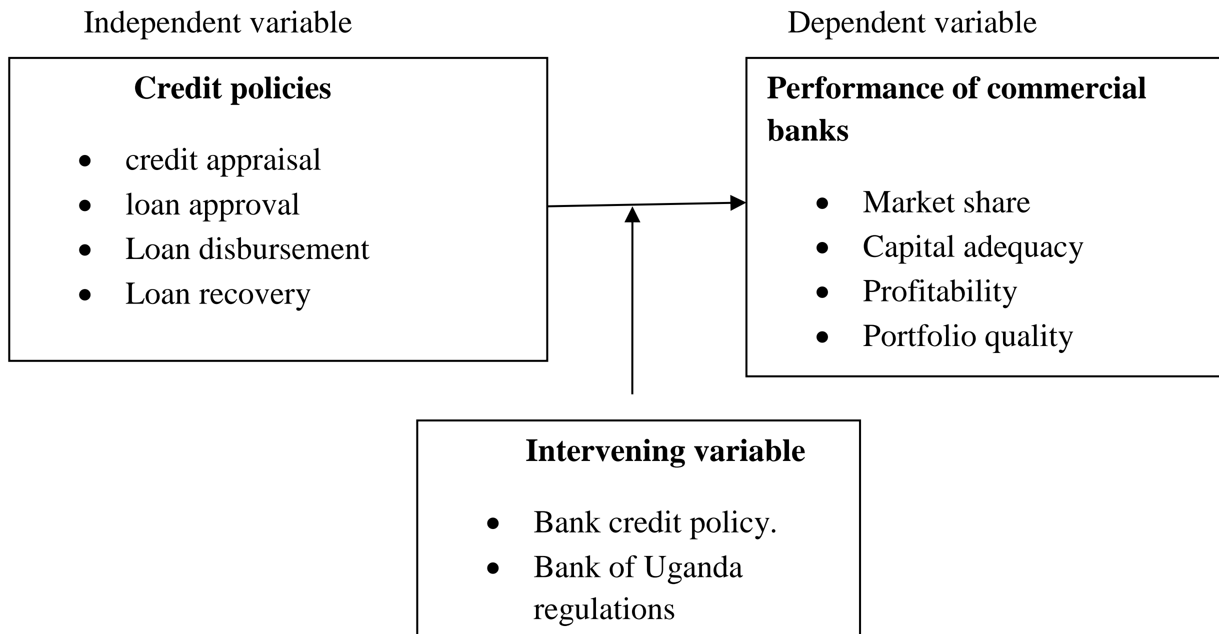
**Profitability**; in accounting sense profitability is the surplus of revenue over and above all point out costs including both manufacturing and overhead expenses.

**Portfolio Quality**; this is solvency of financial institutions which is typically at risk when their assets become impaired.

### 1.10.1 Conceptual framework

Onaolapo (2012) in his research highlights the different variables which make up the credit portfolio of a bank; bank internal loan policy; pre-lending assessment of borrower and past audit analysis of financed project constitute significant factors that shape the quality of a bank credit portfolio. Other sources of credit policies highlighted in some studies include deficient loan appraisal process, inadequately defined lending policies, high credit concentration, poor credit analysis skill of bank officials, as well as a mismatch between credit monitoring system and external operating environment (Bidani et al, 2004).

**Fig 1.10.2 Relationship between variables**




*Source: (Researcher 2015)*

The model fig 1.0 above reflects how the credit policies (Independent variable )and the dimensions; credit appraisal, Loan approval, Loan recovery, and Loan disbursement, if used appropriately can lead to good performance of commercial banks (Dependent variable) such as Market share, Capital adequacy, profitability and portfolio quality. Therefore the relationship is affected by Bank credit policy and Bank of Uganda policies which is the intervening variable. However for the purposes of this study the intervening variables will not be considered since they are macro factor beyond the scope of this study.

**1.11 Limitation of the study.**

- ❖ Due to the limited scope of the study, it may be challenging to apply the research findings of the Kenya Commercial Banks.
- ❖ The respondents selected as key informants such as the staff and management of banks are usually very busy, hence it was not easy to collect data from them. However, this was

addressed by making timely appointments with them and focusing on only important issues during the interview.

- In most cases banks prefer remaining discrete and privacy to information especially to matters that may appear negative for fear of scaring or creating a bad image that discourage public from doing business with them.
- This however addressed by creating a broad interview spectrum involving many players both at junior and management levels, by approaching individual informants and relating different information with the institute of bankers.

## 1.12 Conclusion

This chapter about the background its help me to find out more details of the financial institutions agencies which provides a range of financial services. Then commercial banks and financial Institutions that provides information to the economy and therefore, they also provides loans, advance and credit finance to the clients/citizens of this country.

# CHAPTER TWO

## 2.0 LITERATURE REVIEW

### 2.1 Introduction

A bank exists not only to accept deposits but also to grant credit facilities, therefore inevitably exposed to credit risk. Credit risk is by far the most significant risk faced by banks and the success of their business depends on accurate credit policies and efficient implementation of these policies to a greater extent than any other risks (Gieseche, 2004).However, banks generate profits from transaction fees on financial services and interest charges on lending, which correspond to two of their main functions as financial intermediary: brokerage and asset transformation. Apart from the above functions, banks also started providing services on top of deposit taking, lending, stock broking, money transactions and payments systems with the aim of making additional profits from cross-selling for example from insurance and investment products (Tony and Bart, 2008).

### 2.2 Theoretical Framework

#### 2.2.1 Portfolio Theory

Portfolio theory deals with the selection of portfolios that maximize expected returns consistent with the individual acceptable levels of risk. The theory provides a framework for specifying and measuring investment risk and to develop relationships between risk and expected returns. Its main basic assumption is that investors often want to maximize returns from their investments for a given level of risk. The full spectrum of investments must be considered because the returns from all these investments interact hence the relationship between the returns for assets in the portfolio is important (Reilly & Brown, 2011).

The basic portfolio model was developed by Harry Markowitz in the 1950s and early 1960s.

Markowitz is considered the father of modern portfolio theory since he originated the portfolio model that underlies modern portfolio theory. He derived the expected rate of return for a portfolio of assets and the expected risk measure.

Markowitz established that under reasonable assumptions, the variance of the expected rate of return was a meaningful measure of portfolio risk. From his model, the expected rate of return of a portfolio is the weighted average of the expected return for the individual assets in the portfolio.

### 2.2.2 Credit Risk Theory

Although people have been facing credit risk ever since early ages, credit risk has not been widely studied until recent 30 years. Early literature(before 1974) on credit uses traditional actuarial methods of credit risk ,whose major difficulty lies in their complete dependence on historical data. Up to now, there are three quantitative approaches of analyzing credit risk: structural approach, reduced form appraisal and incomplete information approach (crosbie et al,2003).Melton 1974 introduced the credit risk theory otherwise called the structural theory which is said the default event derives from a firm's asset evolution modeled by a diffusion process with constant parameters. Such models are commonly defined "structural model "and based on variables related a specific issuer. An evolution of this category is represented by asset of models where the loss conditional on default is exogenously specific. In these models, the default can happen throughout all the life of a corporate bond and not only in maturity (Longstaff and Schwartz.1995).

### 2.3.0 Actual Review (Objective by objective)

### 2.3.1 Credit appraisal.

Loan appraisal is an application/request for funds, evaluated by financial institution. The aspects to be focused in appraisal includes: purpose of the client, need genuineness, repayment capacity of the borrower, quantum of loan and security. Loan appraisal plays important role to keep the loan losses to minimum level, hence if loan officers appointed for loan appraisal are competent then there would be high chances of lending money to non-deserving customers (Boldizzoni, 2008).The purpose of credit appraised is to solicit enough information about the applicant in order to determine willingness and capability to serve the loan if granted, in accordance with the term of the loan agreement it enable bank to determine the degree of risk they are willing to assume and the amount of credit that can prudently be expected, given the risk involving and the term and condition for granting the loan. Financial Institutions use the 5Cs model of credit to evaluate a customer as a potential borrower (Abedi, 2011). The 5Cs help FIs to increase loan performance of Kenya commercial banks, as they get to know their customers better. These 5Cs are: character, capacity, collateral, capital and condition.

**Character:** This refers to the person or the entity borrowing the money. It relates to the borrower integrity, responsibility and credit worthiness based on past insure. One’s inherent character cannot be change overnight; hence this factor is very important in starting off a debt relationship (Ayodele, 2014).

**Capital:** This is essential in credit appraised as it represents the sales of the borrower in the business being financial with the borrower fund. The underling principal here is that, the higher the stake of the loan seeker in the venture for which assistance is though the greater in

commitment to the success of the venture. The loan portfolio of the leading bank should also be consideration (Ayodele, 2014).

**Capacity:** The past performances of customer will give an insight into whether he has technical and management capacity to execute the project for which credit is being requested. Establishing the capability of the loan seeker involves the credit officer's perception of the liability of the proposed project in mobilizing enough funds for repayment in establishing the possibility of the project being self-liquidation (Aremu, 2001; Obsessing, 2005)

**Collateral:** this is otherwise known as security. It is the right conference on a creditor to make him redeem in is loan obligation. A security base arrangement usually creates additional moral state on the side of the customer which results in a prudent and effective utilization of available resources. According to Osayameh (1986), securities are particularly relevant in our sit nation in this country, where banking education and habits are still relatively low. Loan should not be disabused until a customer has satisfied all security formalization and no disbursement should be granted again anticipatory approval.

**Condition:** this considers the external micro-environment and the attendant force over which the borrower has no control. This can render a good credit today bad in future if condition becomes in favorable to business. For example, government policy reversal, technological change, terrorist attack etc. can jeopardize the objective of taking loan.

**Duration:** this is the length of time for which the customer requires the loan. Bank is expected to be liquid on demand. This is the reason why some banks cannot afford to lend on long term. It is therefore very germane for any banking institution in performing its lending function to consider

liquidation, cost, profitability, convenience and confidence since all these serve as coeds with which customer are tied to their bankers.

The 5Cs need to be included in the credit scoring model. The credit scoring model is a classification procedure in which data collected from application forms for new or extended credit line are used to assign credit applicants to good or bad credit risk classes (Inkumbi, 2009). He notes that capital and collateral security are major stumbling blocks for entrepreneurs trying to access capital. This is especially true for young entrepreneurs or entrepreneurs with no money to invest as equity; or with no assets they can offer as security for a loan. Any effort to improve access to finance has to address the challenges related to access to capital and collateral. One way to guarantee the recovery of loaned money is to take some sort of collateral on a loan. This is a straightforward way of dealing with the aspect of securing depositors funds.

### 2.3 .2 The Loan Approval.

The aim of the bank loan process management is to minimize the credit risk since these risks emerges in all cases as a result of the bank's loan approval or issuance of the credit instrument, such as a guarantee or a letter of credit, on the client's behalf (Petrovic and Davidovic, 2011) . There are no risk-free loans. The risk simply means the possibility that the client, who takes the loan or requires the bank to issue a letter of credit/guarantee on his behalf, will not be capable to fulfill its commitments to the bank within the due dates on the basis of the principal repayment and payment of installments/fees and at the same time, the risk implies combination of threats and possibilities: the threat of default and possibility of regular loan payment along with the respective interest (Ivanović, 2008).

Approval authorities sanctioned by the board of directors are prudent credit practitioner who cover new credit approvals, renewals of existing credits, and changes in terms and conditions of previously approved credits, particularly credit restructuring, all of which should be fully documented and recorded (Chilukuri and Rao, 2014). Approval authorities of individuals have to be commensurate to their positions within management ranks as well as their expertise. The approval process has to be based on a system of checks and balances. The credit risk may be minimized through the careful analysis of all loan applications before the final decision of the credit reference agency as well as sound management of the loan repayment process. The principal aim of these activities is the bank's profit orientation in terms of income made as an interest margin increased by the fees calculated by the bank on the basis of the risk undertaken (Vunjak, 2008).Therefore, it is very important that the bank, in the process of the loan approval, establishes the client's credit rating by means of credit analysis.

To achieve this Šarlija, (2009), stress that the client's credit rating includes fulfillment of commitments to the bank on the basis of the principal repayment and payment of interests and fees within due dates. Despite the financial market sophistication, a loan is still dominant form of the bank placement. As a result, loan placements may also be regarded as the most significant source of a bank's profitability (Gakure et al, 2012).Considering that the profitability is ultimate business performance since bank loans are source of interest income, the loan approval process management is of imperative importance (Vunjak, 2008). The loan approval process follows adequate methodological guidelines as a set of mechanisms and procedures to which relevant credit documentation is being subject. Koch & MacDonald, (2009), note that, formalization of the loan approval process improves efficiency in gathering and processing of credit documentation, but also facilitates the process of evaluation of the gathered data with a view to

efficient making of credit decisions. Additionally, Bjelica (2005), Points out that the documentation flow is burdened with specific check points within which the data relevant for the loan approval are filtered. One of the most important check points refers to the assessment of the credit-worthiness of the loan applicant.

According to Chilukuri and Rao, (2014), the assessment of credit-worthiness includes identification of financial capacity of a future debtor as a source of depreciation of approved loan By means of credit analysis the client's financial standing and financial structure are examined and its character, capacity, collateral, capital and other relevant debtor's parameters assessed with a view to efficiently assessing the degree of placement risk (Petrovic and Davidovic, 2011). In the context of parameter analysis of the credit rating, the financial indicators have a significant role. As a set of ratios derived from the relation of specific elements of the balance sheet and income statement, these financial indicators are of great analytical and informative significance (Alešević Vranjković, 2007). By comparing them with boundary (desirable) values, the loan repayment capacity is the determined. Beside the financial parameters, as referential factors to assess creditworthiness, the credit analyst gives special attention to the assessment of other relevant parameters such as: the situation in a business activity concerned, economic trends at regional level, and projections with regard to economic activity trends in the forthcoming period (Sunitha and Raju, 2013).

Depending on the size of the financial institution, it has to develop a corps of credit risk specialists who have high level expertise and experience and demonstrated judgment in assessing, approving and managing credit risk(Singh, 2013). An accountability regime should be established for the decision-making process, accompanied by a clear audit trail of decisions taken, with proper identification of individuals/committees involved and all this must be properly

documented. Clear established processes of approving new creditors and extending the existing credits has been observed to be very important while managing credit risks in commercial Banks. Credit unions must have in place written guidelines on credit approval processes and approval authorities' .The board of directors should always monitor loans, approval authorities will cover new credit approvals, renewal of existing credit changes in terms and conditions of previously approved credits particularly credit restructuring which should be fully documented and recorded. Prudent credit practice requires that persons empowered with the credit approval authority should have customer relationship responsibility. Approval authorities of individuals should be commensurate to their positions within the management ranks as well as their expertise (Mwisho, 2001).

### 2.3.3 Loan Disbursement.

Commercial Banks performs all types of banking activities by its various sections to achieve and fulfill its objectives of earning profit, economic development as well as to strengthen its position. The advance reimbursements may be questionable and the accomplishment of giving out credit relies on the philosophy connected to assess and to grant the credit (Moti et al., 2012). Subsequently the credit choice ought to be focused around a careful assessment of the danger states of the loaning and the qualities of the borrower. Various approaches have been created in customer evaluation preparation by budgetary establishments which run from generally straightforward techniques, for example, the utilization of subjective or casual methodologies, to reasonably mind boggling ones, for example, the utilization of mechanized reproduction models (Horcher, 2005; Horne, 2007).

Once the credit is approved, the customer should be advised of the terms and conditions of the credit by way of a letter of offer. The duplicate of this letter is duly signed and returned to the

bank by the customer. The Disbursement should be effected only after completion of covenants, and receipt of collateral holdings, insurance cover in the institution's favor and the vetting of documents by a legal expert. In case of exceptions funds are to be released after prior approval from competent authorities to compliance with pre-disbursement conditions and approval by the relevant authorities in the financial institution.

### 2.3.4 The Relationship between Loan Recovery and the Performance of Commercial Banks

Chilukuri and Rao, (2014), emphasize that a financial institution's credit policy gives solution how problem credits are to be managed by shouldering the responsibility to various credit operations department. It forms part of the credit monitoring section of the credit department called the credit workout unit. The workout unit follows all aspects of the problem credit, including rehabilitation of the borrower, restructuring of credit, monitoring the value of applicable collateral, scrutiny of legal documents, and dealing with receiver/manager until the recovery matters are finalized (Sunitha andRaju, 2013). Financial institutions have to put in place systems to ensure that management is kept advised on a regular basis on all developments in the recovery process, may that emanate from the credit workout unit or other parts of the credit department.

It is the duty of the Bank to recover the landed fund within the stipulated time and if the borrower fails to repay the money within the period Bank will declare him as a defaulter and recover the fund by selling the securities given by the borrower or by freezing his account or make a suit against the borrower (Ullah, 2014). Collection procedure is a systematic way required to recover the past due amount from clients within the lawful jurisdiction (Gakure et al, 2012). The collection aspects may vary from institution but those should be complaint to existing laws such as third party collection agencies may involve in a collection process. It does not just

involve in collection procedure details lawful collection takes place (Latifee, 2006). Well administered collection is needed for better performance of the loan. If financial institutions do not follow well administered collection procedures, this would results in loan defaults (Boldizzoni, 2008). Previous studies indicate that financial institutions need to have strong and effective credit policies for ensuring consistent recovery of loans from clients (Frank et al, 2014).According to Ullah, (2014)recovery of loan can be made in the following 3 methods:1) Persuasive, 2) Voluntarily and 3) Legally

**1) Persuasive recovery:**

If the borrower didn't paid the due amount of loan in time then the first step of bank is private communication with him. It creates a mental pressure on borrower to repay the loan amount. In this case bank can provide some advice to the borrower for repaying the loan.

**2) Voluntarily recovery:**

In this method, some steps are followed for recovering loan. This are; Building Task Force, Arranging seminar, Loan rescheduling policy and Waiver of interest rate.

**3) Legal recovery:**

When all steps fails to keep an account regular and the borrower does not pay the installments and interests then bank take necessary legal steps against the borrower for realization of its dues.

Investors may lose interest and principal as a consequence of credit risk which further leads to increased cost of collection and decreased cash flows (Moti et al, 2012).Previous studies have noted that high Credit Recovery Controls result has low chances of defaults and therefore it has to be alleviated utilizing danger based evaluating, contracts, credit protection, tightening and

broadening techniques (Ross et al, 2008).There can be multiple aspects and arrangements by which an organization can set specific policies for collecting money from borrowers (Moti et al, 2012)

Ezaz et al, 92006), in their study revealed that loan default is quite enormous in the banking sector. They analyzed the issues governing the recovery rate and procedure with respect to Islamic Banking while comparing with the conventional baking principles amongst other Banks. It has been threatening the existence of the banking system. Though it is argued that upswings and downswings of the economic development had impacts on the performances of the banks on the while, the reasons for widespread loan defaults and recovery rate of loans in the banking sector were inherent in the characteristics of the operational systems/mechanisms of the banks(Gakure et al, 2012).Nevertheless, loan default in banks has special significance because extending credit is almost the exclusive business of banking institutions (Alam and Jahan, 1999).

Keeping into focus that few clients are moderate their credit obligations while some are non-payers. The accumulation exertion ought to, subsequently go for quickening accumulations from moderate payers and lessening awful obligation misfortunes (Loona&Zhong, 2014).Chilukuri and Rao, (2014) assert that Banks should maintain the list delinquent customer including any legal steps initiated to realize on the collateral. In case of any delay the banks in the liquidation of collateral or other credit recovery processes, the rationale is administered properly by authentic documented and anticipated actions recorded, and taking into account any revised plans submitted by the borrower. The accountability and responsibility of the staff should be reviewed in checking the credit. Olomola (2002) found that repayment performance is significantly affected by borrower’s characteristics, lenders characteristics and loan characteristics. Repayment problems can be in form of loan delinquency and default. Whatever

the form however, the borrowers alone cannot be held responsible wherever problems arise, it is important to examine the extent to which both borrowers and lenders comply with the loan contract as well as the nature and duties, responsibilities and obligations of both parties as reflected in the design of the credit program rather than heaping blames only on the borrowers.

### 2.3.5.0 Other factors that affect the Performance of Commercial Banks include the following

#### 2.3.5.1 Market Share

Market share is said to be a key indicator of market competitiveness against competitors. This metric, supplemented by changes in sales revenue, helps managers evaluate both primary and selective demand in their market. That is, it enables them to judge not only total market growth or decline but also trends in customers' selections among competitors (David and Reibstin, 2010). Generally, sales growth resulting from primary demand (total market growth) is less costly and more profitable than that achieved by capturing share from competitors. Conversely, losses in market share can signal serious long-term problems that require strategic adjustments. Firms with market shares below a certain level may not be viable. Similarly, within a firm's product line, market share trends for individual products are considered early indicators of future opportunities or problems (David and Reibstin, 2010).

Research has also shown that market share is a desired asset among competing firms. Experts discourage making market share an objective and criterion upon which to base economic policies (Kesten,2010). The aforementioned usage of market share as a basis for gauging the performance of competing firms has fostered a system in which firms make decisions with regard to their operation with careful consideration of the impact of each decision on the market share of their

competitors. It is generally necessary to commission market research to determine. Sometimes, though, one can use primary research to estimate the total market size and a company's market share include some of the construction (David.j, Reibstin; 2010.).Market share can be decomposed into three components, namely: penetration share, share of customer, and usage index. These three underlying metrics can then be used to help the brand identify market share growth opportunities. With the preliminaries the managers are now in a position to explore further the relationship of a bank's market shares with its marketing activities. For the time being managers shall assume that a relevant industry is defined and industry sales are measured. Kotler, (1984), posits that a firm's market share is proportional to the marketing effort of its product.

#### 2.3.5.2 Capital Adequacy

Capital is one of the bank specific factors that influence the level of bank profitability. Capital is the amount of own fund available to support the bank's business and act as a buffer in case of adverse situation (Athanasoglou et al. 2005). Banks capital creates liquidity for the bank due to the fact that deposits are most fragile and prone to bank runs. Moreover, greater bank capital reduces the chance of distress (Diamond, 2000). However, it is not without drawbacks that it induce weak demand for liability, the cheapest sources of fund Capital adequacy is the level of capital required by the banks to enable them withstand the risks such as credit, market and operational risks they are exposed to in order to absorb the potential loses and protect the bank's debtors. According to Dang (2011), the adequacy of capital is judged on the basis of capital adequacy ratio (CAR). Capital adequacy ratio shows the internal strength of the bank to withstand losses during crisis. Capital adequacy ratio is directly proportional to the resilience of the bank to crisis situations. It has also a direct effect on the profitability of banks by determining

its expansion to risky but profitable ventures or areas (Sangmi and Nazir, 2010).Capital adequacy measured by EA has a significant negative impact on bank performance measured by return on equity (ROE).

The finding contradicts with previous study Herrero et al., (2009) showed a positive impact of capital on bank profitability. The new empirical evidence from Uganda suggests that higher capital ratios may lead to lower profitability. Consequently setting up high regulatory capital has negative impact on profitability and ultimately bank performance in Uganda. This implies that domestic commercial banks are operating over-cautiously by avoiding potential profitable ventures. The new findings indicate that, setting up high capital regulatory requirement has a negative impact on commercial banks" performance if not counteracted by increased investments. Loan loss provision to total loans has a highly significant impact on ROE over the period of the study. It indicates that, the quality of loans for domestic commercial banks have led to greater credit risk which eventually impacted negatively on bank performance.

Net interest margin to total assets has a positive and statistically significant impact on returns on equity for domestic commercial banks in Uganda. This implies that, domestic commercial banks in Uganda rely mostly on interest income as their main source of business income. Inflation measured by has a positive significant impact on return on equity for domestic commercial banks in Uganda, The results are consistent with the findings of Davydenko, (2011) and Sehrish et al., (2011who indicated a strong positive impact of inflation on bank profitability. The results suggest that, bank income increased more than bank costs. The implication is consumer price index (CPI) that domestic commercial banks management predicted correctly the trend of inflation and adjusted interest rates accordingly to earn more profits or bank customers never predicted the inflation correctly.

### 2.3.5.3 Profitability.

There are two important concepts that figure in Bank decision that is economic profits and accounting profits (Dwivedi 1996). In accounting sense profitability is the surplus of revenue over and above all point out costs including both manufacturing and overhead expenses. On the other hand, profitability accounting to economists takes into account the implicit or imputed cost; the implicit cost is the opportunity cost. Opportunity cost is defined as the payment that would be necessary to draw forth the factors of production from their most remunerative alternative employment. That is opportunity cost is income foregone which a businessman could expect from the second best alternative use of his resources. Profitability is stated as the ability to provide a reasonable and adequate return on capital employed in existing business, new areas and internal control operations so as to fulfill the objectives of the organization (Pandey 1996). Primary objectives of every business are solvency and profitability (Herman 1987).

Solvency is the ability to pay debts as they become due while profitability is the ability to generate income. Unless a business can produce satisfactory income and pay its debts as they come due, other objectives that firm may have will never be realized, simply because the business will not survive. Profitability of a firm both to shareholders and managers is summarized in the valuation of that firm (Glautier 1992). In deed the basic objective of measurement of profitability is to provide valuation of the firm which will be a critical assessment of its worth as investment. In effect, the value of a firm may be stated as being the present value of its future income. Generally, profitability is regarded as an income accruing to the equity holders in the same way wages accruing to the labour, rent accrues to the owners of rental assets and interest to the money lenders.

#### 2.3.5.4 Portfolio Quality

The solvency of financial institutions is typically at risk when their assets become impaired, so it is important to monitor indicators of the quality of their assets in terms of over exposure to specific risks trends in non-performing loans and the health and Profitability of bank borrowers. Credit risk is inherent in lending which is the major Banking business. It arises when a borrower defaults on the loan payment agreement. A financial institution whose borrower defaults on their payment may face cash flow Problems, which eventually affects its liquidity position. Ultimately, this negatively impacts on the profitability and capital through extra specific provisions for bad debts (BOU, 2002). All banks need to have basic loan portfolio management principles in place in some form. This includes determining whether the risks associated with the bank's lending activities are accurately identified and appropriately communicated to senior management and the board of directors, and, when necessary, whether appropriate corrective action is taken (Comptroller's hand book, 1998).

Portfolio quality management (PQM) is the process by which risks that are inherent in the credit process are managed and controlled. Because review of the portfolio quality management process is so important, it is a primary supervisory activity. Assessing PQM involves evaluating the steps bank management takes to identify and control risk throughout the credit process. The assessment should focus on what management does to identify issues before they become problems (Comptroller's Hand Book, 1989:1). Specific measurable goals for the portfolio are established by portfolio quality objectives. They are an outgrowth of the credit culture and risk profile (Comptroller's Hand Book, 1989:13). The board of directors must ensure that loans are made with the following three basic objectives in mind: (1) To grant loans on a sound and

collectible basis. (2) To invest the bank's funs profitably for the benefit of shareholders and the protection of depositors. (3) To serve the legitimate credit of their communities.

Banks require that senior management and the board of directors to develop medium- and long-term strategic plans to meet objectives for the portfolio quality. These strategies should be consistent with the strategic direction and risk tolerance of the institution. They should be developed with a clear understanding of their risk/reward consequences. They should be reviewed periodically and modified as appropriate. Portfolio quality performance, on the other hand, refers to the rate of profitability or rate or return of an investment in various loan products thus broadly, it looks at the number of clients applying for loans, how much they are borrowing, timely payment of installments, security pledged against the borrowed funds, rate of arrears recovery and the number of loan products on the chain. The loan products may comprise of; Salary loans, Group guaranteed loans, Individual loans and corporate loan (Puxty et al, 1991).

Since one of the main tasks of commercial banks is to offer loans and their main source of risk is credit risk, that is, the uncertainty associated with borrowers' repayment of these loans. A non-performing loan (NPL) may be defined as a loan that has been unpaid for ninety days or more (Greenidge and Grosvenor, 2010).

Such loans unpaid affect the bank portfolio quality performance. For effective portfolio quality performance banks should pay attention to several factors when providing loans in order to curtail the level of impaired loans. Specifically, commercial banks need to consider the international competitiveness of the domestic economy since this may impair the ability of borrowers form the key export oriented sectors to repay their loans which in turn would result in higher nonperforming loans. These lending institutions should also take the performance of the real economy into account when extending loans given the reality that loan delinquencies are

likely to be higher during periods of economic downturn. Finally, banks should constantly review the interest rates on loans since loan delinquencies are higher for banks which increase their real interest rates.

## 2.4 Conclusion.

In as much as a lot of researchers have been done on the effect of credit appraisal on the

Performance of commercial banks, most of the local studies i have learned heavily towards the various tools and techniques of credit appraisal and performance, practices and strategies used by various institutions. The studies did not establish a clear relationship between credit appraisal and performance of Kenya commercial banks. In addition, and to the best knowledge of their searcher, no other research has used credit appraisal as an independent variable. Therefore, this briefs the gap between the performances of commercial banks (Wanjira, 2010).

## CHAPTER THREE

## 3.0 RESEARCH METHODOLOGY

### 3.1 Introduction

Each research problem is in some form unique and thus requires a custom-made research procedure. In this chapter, the researcher discusses the methodology of the study including the source of data, sample and sampling technique, data instrument, pilot testing of instrument, data distribution and collection as well as data management and analysis are described in this section. To be able to accomplish the task at hand, there is a need to gather adequate and comprehensive data on KCB. This chapter seeks to explain the research instruments used in collecting data, the population of the research, sampling procedure, the type of data collected and the difficulties encountered during the research.

### 3.2 Research design

The study used a case study design. The study focused on quantitative and qualitative approaches for data collection analysis and interpretations. The quantitative data focused on quantifiable data which possesses descriptive statistics presentation and using standard mean deviation which enabled the researcher to establish the relationship between credit policies and financial performance of KCB. The study was a cross sectional time dimension and since it is conducted for a single period, the researcher conducts the study and carries out the reporting in a single period.

### 3.3 Study population

The research population is a group of individuals, objects, or items from which the items are taken for measurement (Kumar 2005). The target population of the study was the Managers, accountants, loan officers, and employees. The target population of this study is comprised of 55 respondents from which information was to be obtained. The target study population of the researcher is heterogeneous comprising of staff members who work in the loan department plus the managers of the branch and some reference made from the annual financial report 2013/2014.

### 3.4 Area of the study.

The study was conducted at KCB. The bank is located at on Kampala road. The area of study was sufficient for the researcher since it's one of the biggest and busiest branches of KCB in Uganda hence it enable the researcher to identify the gaps in relation to the research topic.

### 3.5 Sample size and Selection

The clear sample size of the study population was 48 employees and this was based on the statistical model of Krejice and Morgan (1970) table to establish the sample size since the population is quite small. The researcher cannot sample it thus studied the entire population of employees in KCB, main branch since it was sufficient enough for the research.

Table 3.5.1Category of samples

| Category | Number of population | Number of Respondents |
|---|---|---|
| Managers | 5 | 3 |
| Loan officers | 5 | 2 |
| Accountants | 30 | 25 |
| Sales department | 8 | 5 |
| 0ther employees | 15 | 13 |
| **Total** | **55** | **48** |

**Source:** *The Researcher (2016)*

### 3.6 Sampling techniques

The purpose of this study, the Random sampling was used and subjects were selected because of their convenient accessibility to the researcher. The researcher was also using purposive sampling because some elements were chosen purposely for the study. The subject was chosen simply because they are the easiest to obtain for the study and it was used because it is easy, fast and usually the least expensive.

#### 3.6.1 Sampling procedures.

Sampling is a procedure of selecting a part of population on which research can be conducted, which ensures that conclusions from the study can be generalized to the entire population. According to Mugenda et al, (2003) a sample size of between10% and 30% is a good representative of the target population. Researchers have developed a number of techniques

where only a small portion of the total population is sampled, and attempts to generalize the results and conclusion for the entire population.

### 3.7.0 Data collection methods and instruments

### 3.7.1 Questionnaire

Kumar, (2005) defines a questionnaire as a written list of questions, the answers to which are recorded by the respondents. It is a device for gathering information consisting of a list of questions or statements calling for information from the respondents. Usually the respondent writes in the spaces provided on the form as guided by the researcher. Self-administered questionnaires covering all the aspects of the study variables and accompanied with a five-point Likert scale response continuum, that is 5 = strongly agree,4 = agree, 3 = undecided, 2 = disagree and 1= strongly disagree, was used for this study to collect data respondents

### 3.7.2 Document review

The secondary data was collected using document review through viewing the bank's annual financial report since there was limited time to conduct the study and collect all the required data especially information in regard to credit policy is very vital and cannot easily be fully disclosed by most banks thus this instrument will enable the researcher acquire adequate and relevant information needed for the research.

### 3.7.3 Interview guide

These are in forms of face to face meeting, where the researcher interacts with the respondents by asking them questions and recording their feedback. They are normally of two types i.e. telephone interviews and face to face interviews.

The researchers use face to face interviews because it is cheaper to conduct and the researcher could observe the conducts of respondents to note their reactions.

### 3.8 Data management and Analysis.

Presentation of findings was done using tables, graphs. This is done by the help of computer programs SPSS version 16 and micro-soft word. These were used to present the data collected in tabulation form in order to identify the similarities and differences between the variables and finally use of inferential statistics to derive conclusion.

#### 3.8.1 Data analysis

There are two types of analyses were conducted and there are quantitative and qualitative analyses. The following subsections explain the analyses in detail.

#### 3.8.2 Qualitative Data Analysis

Qualitatively the data were sought into themes, categories and patterns. These enable the researcher to make general statements in terms of the observed attributes hence conceptualization according to (Saunders, 2009).

#### 3.8.3 Quantitative Data Analysis

Data from questionnaires was summarized, coded, tabulated and analyzed. Editing was done to improve the quality of data for coding. Coded data were then being fed into the statistical package for social sciences (SPSS) version 16. This version of SPSS were selected for analysis since it offers a more user friendly interface and can easily be linked with Microsoft office utility programs. Descriptive statistics was employed to analyze the data. According to (Cooper et al, 2001) descriptive statistics reveal characteristics of an array of data and enable the researcher to use few indices or statistics to meaningfully describe the phenomena under investigation.

Descriptive statistics such as mean scores, standard deviation, correlation analysis and regression was used to analyze the data and the results were presented in tables and graphs.

### 3.9.1 Data validity

Data validity was ensured through subjecting the drafted tools such as the questionnaire questions to be reviewed by experts to ensure that the right questions for research study are asked. The questionnaire was reviewed by the supervisor before being granted permission to go and collect data. The researcher also ensures that right questions for the study are asked basing on the objectives.

### 3.9. 2 Data reliability

To ensure data reliability, the researcher administered different forms of data collection instruments that included "questionnaires and there results were compared. The instrument was modified on the basis of the pilot test before administering it to the study respondents. In this study, quality control will be done by carrying out a pretest of the questionnaire on the respondents to test the reliability using Chronbach's alpha coefficient. A coefficient of 0.7 and above shows high reliability of data (Saunders, 2009).

## 3.10 Ethical issues / Consideration.

The researcher cited all the sources she or he used in the study either in the literature or appendices and also accessed data through official channels by getting an introductory letter from the person in charge which is presented to the manager of KCB, main branch for permission to conduct the study. The researcher also secured voluntary participation from the respondents in providing responses to the tools and ensured confidentiality and conditions of anonymity of respondents' identity and revelations during and after collecting the data and

finally informed the officials about the accomplishment of the study and thereafter requested for their addresses incase of any inquiries.

### 3.11 Study Limitations

- The issue of finances also limits the research in that the researcher does not have enough funds to facilitate various activities like printing, transportation for various trips to the study area and this will be minimized by the use of soft copies via E-mail.
- Again the outcomes are based on the information solicited from the respondents and therefore subjected to human errors, omissions and possible misstatements. However, in spite of the above, the researchers ensured that the research meets all the relevant requirements for a scientific research and thereby reducing errors to the barest minimum if not to eradicate it completely.
- There is a problem with the sample size of respondents which is quite small as regards to my topic thus giving rise to high levels of error in the data to be collected and this was minimized through studying the entire population of KCB alongside making references to the bank's annual report 2013/2014. There are limitation on the structural formation of institutions as it is different in regard to case study design thus each institution uses different credit policies to improve on the non-performing loans though the researcher will minimize it by mainly focusing on the credit policies used by KCB.

### 3.12 Conclusion

This chapter gives a researcher an understanding of how data was collected and analyzed during the study. These include understanding the population and the sample size which should be sampled during the research. Therefore through these methods, the researcher believes the information to be presented in a required result that is valid and reliable.

# CHAPTER FOUR

# DATA PRESENTATION, ANALYSIS, AND DISCUSSION OF FINDINGS

## 4.0 Introduction

This chapter presents the research findings that were captured from the field of the study. The chapter presents, interprets and discusses the findings of the study ***"The Effect of Credit Policies on the Performance of Commercial Banks in Uganda"*** The chapter is organized in that the background information of the respondents is presented first, and then the findings relating to the research questions are presented next. The presentation of findings is arranged in accordance with questions in the questionnaire which were prepared for the research. Therefore 48 questionnaires were designed for the studies which were responded to by the respondents. This therefore this meant that all the questionnaires were responded to duly during the study.

## 4.1Background Information of the Respondents

In this section, efforts are made to document the background information of the respondents such as gender, education qualification and duration in the organization.

### 4.1.1 Gender of the Respondents

The research study sought to establish the gender of the respondents who participated in the study. The figure below presents the findings of the study.

**Table 4.1 showing gender of respondents**

| | Detail | Frequency | Percentage |
|---|---|---|---|
| Valid | Female | 30 | 62.5 |
| | Male | 18 | 37.5 |
| | Total | 48 | 100.0 |

**Source:** *Primary Data (2016)*

Table 4.1, indicates that there were more female respondents than the male respondents. This is shown by the female having a percentage of 62.5%, while the male are shown by a percentage of 37.5%. This therefore implies that during the research most of the employees were women since there is always need for recruiting more males to have gender balance.

### 4.1.2 Respondents' level of Education

The researcher had interest in knowing the academic qualification of the people employed so that he could establish whether the people operating and managing credit are technically skilled and also whether they have acquired formal education

**Table 4.2: showing the Level of Education**

| | | Frequency | Percentage |
|---|---|---|---|
| Valid | Certificate | 2 | 4.2 |
| | Diploma | 5 | 10.4 |
| | Degree | 29 | 60.4 |
| | masters and above | 9 | 18.8 |
| | Others | 3 | 6.2 |
| | Total | 48 | 100.0 |

**Source:** *Primary data, (2016)*

Results from table 4.3 above indicate that majority of the respondents (60.4%) had attained degrees, (18.8%) had attained masters and above, the 10.4% had diplomas, 6.2 others and the minority (4.2%) had certificates. This implies that the majorities of the employees in KCB have a

good educational background and fully understand the concept of credit policies and performance of commercial banks.

### 4.1.3 Duration spend in the organization

**Table 4.3: Showing Duration spend in the organization**

| | | Frequency | Percentage |
|---|---|---|---|
| Valid | 0-5 years | 33 | 68.8 |
| | 6-10 years | 11 | 22.9 |
| | 10 years above | 4 | 8.3 |
| | Total | 48 | 100.0 |

**Source:** *Primary data, (2016)*

Results shown in table 4.3 reveal that a majority of the respondents 68.8% have worked with KCB for over a period of 0-5 years, 22.9% respondents for a period of 6-10 years and 8.3% for 10 years and above. This implies they had much knowledge about credit policies and basing on their duration in the organization, there response based on experience and how credit policies have helped the Bank.

## 4.2 Descriptive Statistics basing on study objectives.

Analysis based on study objectives and results were presented on the objective questions. As stated in Chapter three, the questionnaire used to generate data was designed in Likert scale with different levels of agreement for each statement that is, 1-Strongly disagree, 2-Disagree, 3-Newton ,4-Agree and 5-Strongly agree. Therefore the mean level of agreement was computed as (5+4+3+2+1)/5= 3.0. This therefore implies that all responses averaging 3.0 and above amounted

for "Agree" whereas all responses averaging below 3.0 accounted for "Disagree". The researcher interviewed none of the workers.

### 4.2.1 Credit appraisal

**Table 4.4 showing Descriptive statistics on credit appraisal**

| Details | N | Min | Max | Mean | Std. Deviation |
|---|---|---|---|---|---|
| KCB borrowers have integrity, responsibility and credit worthiness | 48 | 2 | 5 | 4.04 | .683 |
| Firm has credit policy in place | 48 | 2 | 5 | 4.02 | .785 |
| The past performance of customer gives an insight for which is being requested | 48 | 2 | 5 | 4.06 | .810 |
| Clients appraisal is done following the credit policy of the organization | 48 | 2 | 5 | 3.98 | .785 |
| All loan applications are subjected to the credit appraisal | 48 | 2 | 5 | 4.00 | .772 |
| The loan portfolio of the lending Bank is put under consideration | 48 | 2 | 5 | 4.00 | .744 |

**Source:** *Primary Research Data, (2016)*

#### 4.2.1.1 KCB borrowers have integrity, responsibility and credit worthiness

From the table 4.4 shows that the majority of the respondents agreed to the statement that KCB borrowers have integrity, responsibility and credit worthiness with a mean value of 4.04. This is

in line with Ayodele, (2014) who affirm that the borrower integrity, responsibility and credit worthiness bases on past insured. One's inherent character cannot be changed overnight; hence this factor is very important in starting off a debt relationship. However there was a deviation in respondent's opinion with a standard deviation value of 0.683which implies that responses varied from one respondent to another though it's minimal. This implies that for credit to be given to clients, the bank assess the level of integrity, worthiness and how the client is responsible

#### 4.2.1.2 Firm has Credit Policy in place

Table 4.4 shows that the majority of the respondents agreed that Firm has credit policy in place with the mean value of 4.02. Hence Frank et al, (2014) agrees that financial institutions need to have strong and effective credit policies for ensuring consistent recovery of loans from clients. However the respondent's deviation according to their opinion with the standard deviation of value 0.785which implies that KCB to recover loans from clients, it has to have policies in place which guide the process of loan recovery

#### 4.2.1.3 The Past Performance of Customer gives an insight for which is being requested

From the research findings in table 4.4 it can be noted that majority of the respondents agreed to the statement, that past performance of customer gives an insight for which is being requested with the mean value of 4.06and this is in line with Aremu, (2001) who stressed that the past performances of customer will give an insight into whether he has technical and management capacity to execute the project for which credit is being requested. However it should be noted that there was a deviation among the respondents with a standard deviation of 0.810 thus implying that management has to assess the technical and capacity of a client basing on past performance.

#### 4.2.1.4 Client's Appraisal is done following the credit policy of the organization

Table 4.4 shows that the majority of the respondents agreed that Clients appraisal is done following the credit policy of the organization with the mean value of 3.98. Hence, Abedi, (2011) emphasize that financial Institutions use the 5Cs model of credit to evaluate a customer as a potential borrower The 5Cs help FIs to increase loan performance of Kenya commercial banks, as they get to know their customers better. These 5Cs are: character, capacity, collateral, capital and condition. However the respondent's deviation according to their opinion with the standard deviation of value 0.785which implies that clients applying for loan are evaluated before loans are issued to them to avoid cases of defaults.

#### 4.2.1.5 All loan applications are subjected to the Credit Appraisal

Table 4.4 shows that the majority of the respondents agreed that all loan applications are subjected to the credit appraisal with the mean value of 4.00. This is in line with Boldizzoni, (2008) who elaborated that loan appraisal for funds are evaluated by financial institution. The aspects focused in appraisal includes: purpose of the client, need genuineness, repayment capacity of the borrower, quantum of loan and security. Loan appraisal plays important role to keep the loan losses to minimum level, hence if loan officers appointed for loan appraisal are competent then there would be high chances of lending money to non-deserving customers however with a standard deviation of value 0.772 thus implying loan applications are appraised first before clients get loans.

#### 4.2.1.6 The Loan Portfolio of the Lending Bank is put under consideration

From the findings of the research study in table 4.4, it can be noted that the loan portfolio of the lending Bank is put under consideration thus the majority of the respondent agreed with the statement with a mean value of 4.00 which is in line with Ayodele, (2014) who postulated that is

essential in credit appraised as it represents the sales of the borrower in the business being financial with the borrower fund and the underling principal here is that, the higher the stake of the loan seeker in the venture for which assistance is though the greater in commitment to the success of the venture hence the loan portfolio of the leading bank should also be in consideration.. However there was a standard deviation with values of 0.744 which indicates that portfolio management has to be considered to avoid defaults.

### 4.2.2 Descriptive Statistics on loan approval

**Table 4.5 showing descriptive statistics loan approval**

| Details | N | Min | Max | Mean | Std. Deviation |
|---|---|---|---|---|---|
| The board of directors always monitor loans | 48 | 2 | 5 | 4.04 | .743 |
| The credit risks are minimized through careful analysis of all loan application | 48 | 2 | 5 | 4.02 | .729 |
| The approval process is based on a system of check and balances | 48 | 2 | 5 | 4.02 | .699 |
| Loans are only approved after they meet all the requirements as per the credit policy | 48 | 2 | 5 | 4.06 | .697 |
| The loan approval process follows adequate guidelines relevant to credit documentation | 48 | 2 | 5 | 4.04 | .798 |
| Loan approval process improves efficiency in gathering and processing of credit documentation | 48 | 2 | 5 | 4.04 | .798 |

**Source:** *Primary Research Data, (2016)*

#### 4.2.2.1 The board of directors always monitor loans

From the findings of the research study in table 4.5 above, it can be noted that. The board of directors always monitor loans where the majority of the respondents agreed with mean value of 4.04 which is in line with Chilukuri and Rao, (2014) who cited that approval authorities

sanctioned by the board of directors are prudent credit practitioner who cover new credit approvals, renewals of existing credits, and changes in terms and conditions of previously approved credits, particularly credit restructuring, all of which should be fully documented and recorded However from the findings of the research study, it was also revealed there was a standard deviation with the value of 0.743 which implies that director monitor loans frequently

#### 4.2.2.2 The credit risks are minimized through careful analysis of all loan application

From the findings of the research study in table 4.5, it can be noted that credit risks are minimized through careful analysis of all loan application with the majority of respondents agreeingto the statement with a mean value of 4.02which is in line with Vunjak, (2008) who stress that the credit risk may be minimized through the careful analysis of all loan applications before the final decision of the credit reference agency as well as sound management of the loan repayment process. However from the findings, there was a deviation of 0.729thus implying that analysis of loan application helps to minimize credit risks in the bank.

#### 4.2.2.3 The approval process is based on a system of check and balances

From the findings of the research study in table 4.5 it can be noted that The approval process is based on a system of check and balances this was in respect to the majority of respondents who agreed with the mean value of 4.02 which is in line with Vunjak, (2008) who affirm that approval authorities of individuals have to be commensurate to their positions within management ranks as well as their expertise and therefore approval process has to be based on a system of checks and balances. However from the findings of the research study, also revealed that there was a standard deviation of values 0.699 which implies that checks and balances determine loan approval

#### 4.2.2.4 Loans are only approved after they meet all the requirements as per the credit policy

From the findings of the research study in table 4.5 above, it can be noted that Loans are only approved after they meet all the requirements as per the credit policy since majority of the respondent agreed with the mean value of 4.06 which is in line with the outcome of an interview with Jonathan (2016) who stressed that the bank has credit policies that customers have to meet before loan request is approved and this ranges from collateral, capital, character and other of a customer. However from there was a deviation too with the standard deviation of values of 0.697 this implies that before loans are approved, customers have to meet the credit requirement of the bank.

#### 4.2.2.5 The loan approval process follows adequate guidelines relevant to credit documentation

From the findings of the research study in table 4.5 it can be noted that the majority of respondents claimed that The loan approval process follows adequate guidelines relevant to credit documentation with the mean value of 4.04 which is in line Šarlija, (2009) who noted that the loan approval process follows adequate methodological guidelines as a set of mechanisms and procedures to which relevant credit documentation is being subject. However from the findings of the study, it was also revealed that there was a standard deviation with values of 0.798which is a minimal implying that guidelines followed to approve a loan under credit documentation

#### 4.2.2.6 Loan approval process improves efficiency in gathering and processing of credit documentation

From the findings of the research study in table 4.5 it can be noted Loan approval process improves efficiency in gathering and processing of credit documentation this was in respect to the agreement mean value of 4.08 which is in line with Koch & MacDonald, (2009) who noted that, formalization of the loan approval process improves efficiency in gathering and processing of credit documentation, but also facilitates the process of evaluation of the gathered data with a view to efficient making of credit decisions. However from the findings of the research study, also revealed a standard deviation of values 0.798which implies that gathering and processing credit documents, loan approval process aids and improves efficiency in the process.

### 4.2.3 Descriptive Statistics on loan disbursement

**Table 4.6 showing the descriptive statistics loan disbursement**

| **Details** | **N** | **Min** | **Max** | **Mean** | **Std. Deviation** |
|---|---|---|---|---|---|
| Commercial banks perform all types of banking activities by its various sections to achieve and fulfil its objectives | 48 | 2 | 5 | 3.98 | .699 |
| KCB creates customer evaluation forms | 48 | 2 | 5 | 3.96 | .683 |
| KCB customers are advised of the terms and conditions of the credit by a way of a letter of offer | 48 | 2 | 5 | 4.04 | .743 |
| The disbursement is effected after completion of convents and receipt of collateral holdings as insurance cover | 48 | 2 | 5 | 4.02 | .729 |
| Credit choice focuses on a careful assessment of the danger states of the loaning and qualities of borrower | 48 | 2 | 5 | 4.00 | .744 |

***Source: Primary Research Data, (2015)***

#### 4.2.3.1 Commercial banks perform all types of banking activities by its various sections to achieve and fulfill its objectives

From the findings of the research study in table 4.7, it can be noted that Commercial banks perform all types of banking activities by its various sections to achieve and fulfill its objectives where the majority of respondents agreed to the statement with a mean value of 3.98 which is in line with Horcher, (2005)who reviewed that Commercial Banks performs all types of banking activities by its various sections to achieve and fulfill its objectives of earning profit, economic development as well as to strengthen its position. Though there was a minimal deviation with the standard deviation values of 0.699 thus implying that for banks to achieve their objectives, they should perform all types of banking

#### 4.2.3.2 KCB creates customer evaluation forms

From the findings of the research study in table 4.7, it can be noted that the majority of the respondents agreed that KCB creates customer evaluation forms with the mean value of 3.96which is in line with Horne, (2007) who noted that various approaches have been created in customer evaluation form preparation by budgetary establishments which run from generally straightforward techniques, for example, the utilization of subjective or casual methodologies, to reasonably mind boggling ones, for example, the utilization of mechanized reproduction models. Though there were some respondents who deviated with the standard deviation of 0.683 though minimal thus implying that evaluation forms are created by KCB.

#### 4.2.3.3 KCB customers are advised of the terms and conditions of the credit by a way of a letter of offer

From the findings of the research study in table 4.7, it can be noted that KCB customers are advised of the terms and conditions of the credit by a way of a letter of offer where the majority of respondents agreed to the statement with a mean value of 4.04 which is in line with Moti et al, (2012) who emphasized that once the credit is approved, the customer should be advised of the terms and conditions of the credit by way of a letter of offer. However from the findings of the study, it was also revealed that some respondent deviated though minimal with the standard deviation of value 0.743 thus implying that customers know the terms and conditions of the loan since they are advised.

#### 4.2.3.4 The disbursement is effected after completion of covenants and receipt of collateral holdings as insurance cover

From the findings of the research study in table 4.7 above, it can be noted that the disbursement is effected after completion of convents and receipt of collateral holdings as insurance cover where majority of respondents agreed with the statement with the mean value of 4.02 which is in line with Ullah, (2014) who stressed that the Disbursement should be effected only after completion of covenants, and receipt of collateral holdings, insurance cover in the institution's favour and the vetting of documents by a legal expert. However there was a minimal deviation of 0.729. This therefore implies that before loans are disbursed to customers, they have to complete covenants and have receipts

#### 4.2.3.5 Credit choice focuses on a careful assessment of the danger states of the loaning and qualities of borrower

From the findings of the research study in table 4.7, it can be noted that Credit choice focuses on a careful assessment of the danger states of the loaning and qualities of borrower with the majority of respondents in agreement to the statement with a mean value of 4.00 which is in line with Horne, (2007) who affirm that the credit choice ought to be focused around a careful assessment of the danger states of the loaning and the qualities of the borrower. However from the findings of the study, it was also revealed that some respondents deviated though minimal with a standard deviation values of 0.744 thus implying that danger state are assessed before making credit choices.

### 4.2.4 Descriptive Statistics on loan recovery

**Table 4.7 showing descriptive statistics loan recovery**

**Descriptive Statistics**

| Details | N | Min | Max | Mean | Std. Deviation |
|---|---|---|---|---|---|
| KCB collection procedures have a systematic way required to recover the past due amount from clients | 48 | 2 | 5 | 4.13 | .733 |
| The bank carries out private communication with clients when they fail to repay loan dues | 48 | 2 | 5 | 4.04 | .713 |
| KCB takes necessary legal steps against the borrower for realization of dues in case of default | 48 | 2 | 5 | 4.15 | .743 |
| Records are kept on loans recovered by the bank | 48 | 2 | 5 | 4.00 | .684 |
| The accountability and responsibility of the staffs are reviewed in checking the credit | 48 | 2 | 5 | 4.08 | .710 |

***Source:*** *Primary Research Data, (2016)*

#### 4.2.4.1 KCB collection procedures have a systematic way required to recover the past due amount from clients

From the findings of the research study in table 4.6 above, it can be noted KCB collection procedures have a systematic way required to recover the past due amount from clients thus the majority of respondent acknowledged and agreed with a mean value of 4.13 which qualifies with

Gakure et al, (2012) that collection procedure is a systematic way required to recover the past due amount from clients within the lawful jurisdiction.

However from the findings of the study, it was also revealed that there was a standard deviation with the values of 0.733 which implies there are systematic procedures to collect dues.

#### 4.2.4.2 The bank carries out private communication with clients when they fail to repay loan dues

From the findings of the research study in table 4.6 it can be noted that The bank carries out private communication with clients when they fail to repay loan dues this is because majority of respondents agreed with mean value of 4.04 which is in line with what Ullah, (2014) stressed that if the borrower didn't paid the due amount of loan in time then the first step of bank is private communication with him. It creates a mental pressure on borrower to repay the loan amount. In this case bank can provide some advice to the borrower for repaying the loan. However from the findings of the research study, it was also revealed a standard deviation of 0.713which is a minimal implying that the bank communicates privately with client in case of failure to pay their dues.

#### 4.2.4.3 KCB takes necessary legal steps against the borrower for realization of dues in case of default

From the findings of the research study in table 4.6 above, it can be noted KCB takes necessary legal steps against the borrower for realization of dues in case of default where the majority of respondent agreed to the statement with the mean value of 4.15 which is in line with Moti et al, (2012) who stated that when all steps fails to keep an account regular and the borrower does not pay the installments and interests then bank take necessary legal steps against the borrower for

realization of its dues because investors may lose interest and principal as a consequence of credit risk which further leads to increased cost of collection and decreased cash flows. However there was yet a deviation with a value of 0.743it is a minimal deviation thus banks takes legal steps to recover loan dues.

#### 4.2.4.4 Records are kept on loans recovered by the bank

From the findings of the research study in table 4.6 it can be noted that this is because majority of respondents agreed Records are kept on loans recovered by the bank with mean value of 4.00 which is in line with an interview held with Jonathan (2016). Who affirmed that loans which are recovered are well recorded and documented to avoid loss of data about the recovered loans. However from the findings of the research study, it was also revealed a standard deviation of 0.684which is a minimal implying that the bank records recovered loans from clients.

#### 4.2.4.5 The accountability and responsibility of the staffs are reviewed in checking the credit

From the findings of the research study in table 4.6 above, it can be noted The accountability and responsibility of the staffs are reviewed in checking the credit with the majority of respondents agreeing with a mean value of 4.08 as observed by Chilukuri and Rao, (2014) who stressed that the accountability and responsibility of the staff should be reviewed in checking the credit. However there was a deviation with the standard deviation with values of 0.710 thus implying that there are accountability and responsibility review of staff

#### 4.2.5.1 KCB has a surplus of revenue over cost

From the findings of the research study in table 4.8, it can be noted that KCB has a surplus of revenue over cost where the majority of respondents agreed to the statement with a mean value

of 3.98 which is in line with Pandey (2010) who stress that profitability in the bank means the surplus of revenue over and above all point out costs including both manufacturing and overhead expenses Though there was a minimal deviation with the standard deviation values of 0.729thus implying that KCB has surplus revenue.

#### 4.2.5.2 KCB provides reasonable and adequate return on capital employed

From the findings of the research study in table 4.8, it can be noted that the majority of the respondents agreed that KCB provides reasonable and adequate return on capital employed with the mean value of 4.00which is in line with Pandey (1996) who emphasized that profitability represents the ability to provide a reasonable and adequate return on capital employed in existing business, new areas and internal control operations so as to fulfill the objectives of the organization. Though there were some respondents who deviated with the standard deviation of 0.825 though minimal thus implying that there is an adequate and reasonable return on capital employed in KCB.

#### 4.2.5.3 KCB produces satisfactory income and pays its debts as they come due

From the findings of the research study in table 4.7, it can be noted that KCB produces satisfactory income and pay its debts as they come due where the majority of respondents agreed to the statement with a mean value of 3.96 which is in line with Dang, (2011) who elaborated that unless a business can produce satisfactory income and pay its debts as they come due, other objectives that firm may have will never be realized, simply because the business will not survive. However from the findings of the study, it was also revealed that some respondent deviated though minimal with the standard deviation of value 0.798 thus implying that KCB pays its debts as come due as a result of production of satisfactory income.

#### 4.2.5.4 KCB monitors indicators of the quality of their assets

From the findings of the research study in table 4.8 above, it can be noted that KCB monitor indicators of the quality of their assets where majority of respondents agreed with the statement with the mean value of 3.94 which is in line with Puxty et al, (1991) who treed that the solvency of financial institutions is typically at risk when their assets become impaired, so it is important to monitor indicators of the quality of their assets in terms of over exposure to specific risks trends in non-performing loans and the health and Profitability of bank borrowers. However there was a minimal deviation of 0.783. This therefore implies that KCB monitors its asset quality.

#### 4.2.5.5 KCB has loan portfolio management principles in place

From the findings of the research study in table 4.8, it can be noted that KCB has loan portfolio management principles in place with the majority of respondents in agreement to the statement with a mean value of 3.94which is in line with Comptroller's hand book, (1998) which affirm that all banks need to have basic loan portfolio management principles in place in some form and this includes determining whether the risks associated with the bank's lending activities are accurately identified and appropriately communicated to senior management and the board of directors, and, when necessary, whether appropriate corrective action is taken. However from the findings of the study, it was also revealed that some respondents deviated though minimal with a standard deviation values of 0.755thus implying that danger state are assessed before making credit choices.

#### 4.2.5.6 Banks require management to develop strategic plans to meet objective of portfolio quality

From the findings of the research study in table 4.8 above, it can be noted that Banks require management to develop strategic plans to meet objective of portfolio quality where majority of respondents agreed with the statement with the mean value of 4.06which is in line with Greenidge and Grosvenor, (2010) who noted that Banks require that senior management and the board of directors to develop medium- and long- term strategic plans to meet objectives for the portfolio quality. However there was a minimal deviation of 0.727. This therefore implies that management is required to develop strategic plans to meet the objectives of portfolio quality in order to perform well.

### 4.3 Correlation analysis

In order to determine the effect that credit appraisal, loan approval, loan recovery and loan disbursement have on financial performance, the researcher conducted correlation analysis and the following were the results;

### 4.3.1 Correlation analysis between credit appraisal and financial performance

**Table 4.8: Correlation results of credit appraisal and financial performance**

| Details | | Credit appraisal | Financial performance |
|---|---|---|---|
| Credit appraisal | Pearson Correlation | 1 | .721** |
| | Sig. (2-tailed) | | .000 |
| | N | 48 | 48 |
| Financial performance | Pearson Correlation | .721** | 1 |
| | Sig. (2-tailed) | .000 | |
| | N | 48 | 48 |

**. Correlation is significant at the 0.01 level (2-tailed).

***Source:*** *Primary data (2016)*

The study sought to determine the effect of credit appraisal on financial performance. This was done with the support of the Pearson correlation product moment technique. From the table 4.9 above, correlation value ($r = 0.721^{**}$ $p < 0.01$) revealed that there is a positive and a significant relationship between credit appraisal and financial performance. This meant that credit appraisal leads to an improvement in financial performance. The value of 0.721 meant that credit appraisal has a 72.1% effect on financial performance which is in line with Boldizzoni, (2008) who noticed that loan appraisal plays important role to keep the loan losses to minimum level, hence if loan officers appointed for loan appraisal are competent then there would be high chances of lending money to non-deserving customers.

### 4.3.2 Correlation between loan approval and financial performance

**Table 4.9: Correlation results of loan approval and financial performance**

| Details | | Loan approval | Financial performance |
|---|---|---|---|
| Loan approval | Pearson Correlation | 1 | .495** |
| | Sig. (2-tailed) | | .000 |
| | N | 48 | 48 |
| Financial performance | Pearson Correlation | .495** | 1 |
| | Sig. (2-tailed) | .000 | |
| | N | 48 | 48 |

**. Correlation is significant at the 0.01 level (2-tailed).

***Source:*** *Primary Data (2016)*

The study sought to determine the effect of loan approval on financial performance. This was done with the support of the Pearson correlation product moment technique. From the table 4.10 above, correlation value ($r = 0.495^{**} p < 0.01$) revealed that there is a positive and a significant relationship between loan approval and financial performance. This meant that loan approval leads to an improvement in financial performance. The value of 0.495 meant that credit appraisal has a 49.5% effect on financial performance which is in line with Petrovic and Davidovic, (2011) who stressed that the aim of the bank loan process management is to minimize the credit risk since these risks emerges in all cases as a result of the bank's loan approval or issuance of the credit instrument, such as a guarantee or a letter of credit, on the client's behalf.

### 4.3.3 Correlation between loan disbursement and financial performance

**Table 4.10: Correlation results of loan disbursement and financial performance**

| Details | | Loan disbursement | Financial performance |
|---|---|---|---|
| Loan disbursement | Pearson Correlation | 1 | .863** |
| | Sig. (2-tailed) | | .000 |
| | N | 48 | 48 |
| Financial performance | Pearson Correlation | .863** | 1 |
| | Sig. (2-tailed) | .000 | |
| | N | 48 | 48 |

**. Correlation is significant at the 0.01 level (2-tailed).

***Source:*** *Primary Data (2016)*

From the table 4.11above, correlation showed that there is a positive and a significant relationship ($r = 0.863^{**}$, $p < 0.01$) between loan disbursement and financial performance with values 0.863. This introduces a fact that critical emphasis on loan disbursements procedures to clients enhances better financial performance of the institution with a rate of 86.3 % which is in line with Moti et al, (2012) who emphasize that the advance of reimbursements may be questionable and the accomplishment of giving out credit relies on the philosophy connected to assess and to grant the credit to clients.

#### 4.3.4 Correlation between loan recovery and financial performance

**Table 4.12: Correlation results of loan recovery and financial performance**

| Details | | Loan recovery | Financial performance |
|---|---|---|---|
| Loan recovery | Pearson Correlation | 1 | .755** |
| | Sig. (2-tailed) | | .000 |
| | N | 48 | 48 |
| Financial performance | Pearson Correlation | .755** | 1 |
| | Sig. (2-tailed) | .000 | |
| | N | 48 | 48 |

**. Correlation is significant at the 0.01 level (2-tailed).

***Source: Primary Data (2016)***

From the table 4.11above, correlation showed that there is a positive and a significant relationship ($r = 0.755^{**}$, $p < 0.01$) between loan recovery and financial performance with values 0.755. This introduces a fact that an emphasis on loan recovery fosters business performance at 75.5 % which is in line with Ullah, (2014) who stated that financial institutions have to put in place systems to ensure that management is kept advised on a regular basis on all developments in the recovery process, may that emanate from the credit workout unit or other parts of the credit department.

### 4.4 Conclusion

The analysis of the primary data indicates that the independent variables through the predictor variables; credit appraisal, loan approval, Loan disbursement and Loan recovery on the performance as it has been seen in the findings of the study in this chapter four regardless of how much or greater the influence is. Therefore this facilitated the findings as discussed and presented in the above chapter.

# CHAPTER FIVE.

# SUMMARY, CONCLUSION AND RECOMMENDATIONS

## 5.1. Introduction

This chapter refers to the organized, presented and analyzed data in the preceding chapters. The Summary and Conclusions plus recommendations are drawn from the discussed findings, in line with the objectives of the study.

## 5.2. Summary

The main purpose of the study was to establish the relationship between credit policies on the Performance of commercial banks in Uganda. The research was mainly qualitative and quantitative in nature. The sample size was 48. The main instrument used for data collection was Questionnaire. Descriptive correlation research design was used to analyze data and test the Hypothesis.

The summary of the findings is summarized below in relation to the objectives

The findings in the table 4.2 above revealed that, in relation to the level of education of the respondents, it was reviled that, out of 48 (100%), Majority 29 (60.4%) were degree level ,majority 9 (18.8%) were masters and above, the 10.4% had diploma,6.2% other and majority 4.2% had certificate. This implies that the majorities of the employees in KCB have a good educational background and understand the concept of credit polices and performance of Kenya Commercial Bank. The first objective was to examine the types of credit appraisal experienced in the banking sector.

Findings of this objective revealed that, type's credit appraisal experienced in the banking sector had a (grand mean of 3.98) the scale indicated that the types of credit appraisal experienced in the Banking sector were high.

The second objective was to examine the loan approval on the performance of commercial banks in Uganda. Findings on this objective indicated that, the performance of banks in Uganda was high at (grand mean 4.04)

The third objective was to examine the loan disbursement on the performance of commercial banks in Uganda. The finding on this objective indicated that, the performance of banks in Uganda was high at (4.6). The fourth objective was to establish the relationship between loan recovery and performance of commercial banks in Uganda. To attain this objective, Pearson correlation was used. And Findings on the relationship revealed that there is a strong positive relationship between loan recovery and performance of commercial banks at a p-value of 75.5% which is above 0.775 two tailed. This implies that the relationship between loan recovery and performance of commercial banks is highly positive; meaning that when loan recovery increases, the performance will go up. When loan recovery decreases, the performance will decrease. Correlation is significant at the 0.01 level (2-tailed) at the performance of commercial banks in Uganda.

**5.3. Conclusion**

From the findings, the study found that credit appraisal, loan approval, loan disbursement and loan recovery have an effect on the performance of commercial banks in Uganda. The study established that there was strong relationship between credit appraisal and performance of commercial banks. The study revealed that credit appraisal would lead to increase in

performance of commercial banks in Uganda; this is an indication that there was positive relationship between credit appraisal and performance of commercial banks in Uganda, An increase in loan appraisal would lead to increase in financial performance of commercial banks in Uganda, which shows that there was a positive relationship between performance of commercial banks and loan approval and a unit in loan disbursement had effect on performance of Commercial banks. The study established that there was strong relationship between performance of Commercial banks and credit appraisal, loan approval, loan disbursement and loan recovery.

The study revealed that an increase in credit appraisal, would lead to an increase in performance of Commercial banks in Uganda; this is an indication that there was positive relationship between credit appraisal and performance of commercial banks, an increase in loan approval would lead to increase in performance of Commercial banks in Uganda, which shows that there was positive relationship between performance of commercial banks and loan approval and an increase in loan disbursement and loan recovery would lead to increase in performance;

this is an indication that there was a positive relationship between performance of Commercial banks and loan disbursement and loan recovery. Credit appraisal, loan approval, loan disbursement and loan recovery significantly influence performance of Commercial banks in Uganda.

## 5.4 Recommendations.

Management should always update their web page with the current information from the bank to make their clients up to date. In case of any changes in the borrowing rates or information

regarding the accounts, system break down should always be communicated to the clients in order avoid inconvenience.

When making the communication, the banks should ensure clarity in the message being passed. The banks should look for more ways of capturing their customers, for instance trying to listen and respond positively to complaints forwarded by clients, giving them the right information in light of improving their profits.

The management should strive at cutting unnecessary costs incurred when passing on information. The study confirmed a positive relationship between loan recovery and performance of commercial banks. Strong recommendation is made to management of KCB Bank to critically evaluate the channels it uses to pass information and manage information that will increase the company's profits.

There is a positive relationship between loan recovery and performance of commercial banks in Uganda therefore commercial banks should strongly emphasize on loan recovery from the clients during their time of operations.

There is need for commercial banks to enhance their customer's credit appraisal techniques so as to improve their financial performance. Through client appraisal techniques, the companies will be able to know credit worth customers and thus reduce default and enhance their collection procedures and policies by adapting a more policies for effective loan recovery.

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# APPENDICES

## APPENDIX I : QUESTIONNAIRE

Dear respondent,

I am **JUAN SCOVIA**, a third year student of Uganda Martyrs University pursuing a Bachelor's degree in Business Administration and Management. As part of my academic requirement, I am carrying out research on a topic "**The effect of credit policies on the performance of commercial banks in Uganda,** with a case study KCB. You have therefore been purposively identified as a resourceful person in providing the required information. The purpose of this research is purely academic and the information you give will be anonymously treated with confidentiality.

**Thanks you for your precious time**

**SECTION A**: Background Information.

1. Department…………………………………………………………………..

2. Sex: a) Male ☐ b) Female ☐

3. Level of academic qualification

a) Certificate ☐ b) Diploma ☐

c) Degree ☐ d) Masters and above ☐ e) other levels ☐

4. Years worked in the organization

a) 0-5 years ☐ b) 6-10 years ☐ c) 10 years and above ☐

**Tick in the appropriate box basing on this scale.**

| **Scale** | **5** | **4** | **3** | **2** | **1** |
|---|---|---|---|---|---|
| Particulars | Strongly agree **(S.A)** | Agree **(A)** | Neutral **(N)** | Disagree **(D)** | Strongly disagree **(S.D)** |

**SECTION B: Credit appraisal**

| | **Details** | **5(S.A)** | **4(A)** | **3(N)** | **2(D)** | **1(S.D)** |
|---|---|---|---|---|---|---|
| C 1 | In Kenya commercial bank borrowers have integrity, responsibility and credit worthiness. | | | | | |
| C 2 | The firm has a credit policy in place. | | | | | |
| C 3 | The past performance of customer gives an insight for which credit is being requested. | | | | | |
| C 4 | Client's appraisal is done following the credit policy of the organization. | | | | | |
| C 5 | All loan applications are subjected to the credit appraisal. | | | | | |
| C 6 | The loan portfolio of the lending bank is put under consideration. | | | | | |

Are there any challenges faced while carrying out credit appraisal in commercial banks? If yes, state them

…………………………………………………………………………………………………

…………………………………………………………………………………………………

**SECTION C: loan approval.**

| | Details | 5(S.A) | 4(A) | 3(N) | 2(D) | 1(S.D) |
|---|---|---|---|---|---|---|
| L1 | The board of directors always monitors loans. | | | | | |
| L2 | The credit risks are minimized through the careful analysis of all loan applications. | | | | | |
| L3 | The approval process is being based on a system of checks and balances. | | | | | |
| L4 | Loans are only approved after they meet all the requirements as per the credit policy. | | | | | |
| L5 | The loan approval process follows adequate guidelines relevant to credit documentation. | | | | | |
| L6 | Loan approval process improves efficiency in gathering and processing of credit documentation. | | | | | |

How best can loan approval process be improved?

…………………………………………………………………………………………………

…………………………………………………………………………………………………

…………………………………………………………………………………………………

**SECTION D: loan disbursement.**

| | Details | 5(S.A) | 4(A) | 3(N) | 2(D) | 1(S.D) |
|---|---|---|---|---|---|---|
| D1 | Commercial Banks performs all types of banking activities by its various sections to achieve and fulfill its objectives. | | | | | |
| D2 | KCB creates customer evaluation forms. | | | | | |
| D3 | In KCB bank customers are advised of the terms and conditions of the credit by the way of a letter of offer. | | | | | |
| D4 | The disbursement is effected only after completion of covenants and receipt of collateral holdings as insurance cover. | | | | | |
| D5 | Credit choice focuses on a careful assessment of the danger states of the loaning and the qualities of the borrower. | | | | | |

How does loan disbursement improved the performance of commercial bank?

…………………………………………………………………………………………………

…………………………………………………………………………………………………

**SECTION E: Loan Recovery.**

| | Details | 5(S.A) | 4(A) | 3(N) | 2(D) | 1(S.D) |
|---|---|---|---|---|---|---|
| R1 | In KCB collection procedures have a systematic way required to recover the past due amount from clients? | | | | | |
| R2 | The bank carries out private communication with clients when they fail to repay loan dues? | | | | | |
| R3 | KCB takes necessary legal steps against the borrower for realization of dues in case of default? | | | | | |
| R4 | Records are kept on loans recovered by the bank? | | | | | |
| R5 | The accountability and responsibility of the staffs are reviewed in checking the credit. | | | | | |

How does loan recovery increase financial performance of the KCB?

……………………………………………………………………………………………......................

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**FINANCIAL PERFORMANCE OF COMMERCIAL BANKS**

| | DETAILS | 5(S.A) | 4(A) | 3(N) | 2(D) | 1(S.D) |
|---|---|---|---|---|---|---|
| P1 | KCB have surplus of revenue over cost. | | | | | |
| P2 | KCB provides a reasonable and adequate return on capital employed. | | | | | |
| P3 | KCB produces satisfactory income and pay its debts as they fall due | | | | | |
| P4 | KCB monitor indicators of the quality of their assets. | | | | | |
| P5 | KCB have loan portfolio management principles in place. | | | | | |
| P6 | Banks require management to develop medium- and long term strategic plans to meet objectives of portfolio quality. | | | | | |

What are other indictors of financial performance in KCB?

……………………………………………………………………………………………………

……………………………………………………………………………………………………

……………………………………………………………………………………………………

***Thanks for your participation, May the Almighty Reward you abundantly.***

## APPENDIX : II

**Morgan and Krejcie Table**

TABLE FOR DETERMINING SAMPLE SIZE FROM A GIVEN 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 | 246 |
| 25 | 24 | 130 | 97 | 320 | 175 | 950 | 274 | 4000 | 351 |
| 30 | 28 | 140 | 103 | 340 | 181 | 1000 | 278 | 4500 | 351 |
| 35 | 32 | 150 | 108 | 360 | 186 | 1100 | 285 | 5000 | 357 |
| 40 | 36 | 160 | 113 | 380 | 181 | 1200 | 291 | 6000 | 361 |
| 45 | 40 | 180 | 118 | 400 | 196 | 1300 | 297 | 7000 | 364 |
| 50 | 44 | 190 | 123 | 420 | 201 | 1400 | 302 | 8000 | 367 |
| 55 | 48 | 200 | 127 | 440 | 205 | 1500 | 306 | 9000 | 368 |
| 60 | 52 | 210 | 132 | 460 | 210 | 1600 | 310 | 10000 | 373 |
| 65 | 56 | 220 | 136 | 480 | 214 | 1700 | 313 | 15000 | 375 |
| 70 | 59 | 230 | 140 | 500 | 217 | 1800 | 317 | 20000 | 377 |
| 75 | 63 | 240 | 144 | 550 | 225 | 1900 | 320 | 30000 | 379 |
| 80 | 66 | 250 | 148 | 600 | 234 | 2000 | 322 | 40000 | 380 |
| 85 | 70 | 260 | 152 | 650 | 242 | 2200 | 327 | 50000 | 381 |
| 90 | 73 | 270 | 155 | 700 | 248 | 2400 | 331 | 75000 | 382 |
| 95 | 76 | 270 | 159 | 750 | 256 | 2600 | 335 | 10000 | 384 |

“N” is population size

“S” is sample size.