KWAME NKRUMAH UNIVERSITY OF SCIENCE AND TECHNOLOGY

SCHOOL OF BUSINESS

DEPARTMENT OF ACCOUNTING AND FINANCE

BANK SPECIFIC DETERMINANTS OF NON-PERFORMING LOANS AMONG SELECTED COMMERCIAL BANKS IN THE KUMASI METROPOLIS

A Thesis Submitted To School of Business, the Department Of Accounting and Finance, Kwame Nkrumah University of Science and Technology Kumasi in Partial Fulfillment Of The Requirement for the Award of Master of Business Administration (FINANCE OPTION), School of Business, College of Art and Social Sciences.

BY

FRANCIS AMPRATWUM

(PG9609313)

AUGUST 2015

DECLARATION

With the exception of the references which has duly acknowledge, I hereby do declare that that this thesis is exclusively my worn piece of work as a student of the Kwame Nkrumah University. I also do acknowledge that this piece of work has never been submitted, either in whole or part to any institution for the award of a degree. I am therefore fully accountable to any flaws associated with this work.

Francis Ampratwum	………………………..	……………………….
[PG9609313]	**Signature**	**Date**

Certified by;

Dr. Daniel Domeher	………………………..	……………………….
(Supervisor)	**Signature**	**Date**

Dr. K. O. Appiah	………………………..	……………………….
(**Head of Department)**	**Signature**	**Date**

DEDICATION

I dedicate this piece of work to Dr. K.K. Sarpong (Uncle), Yaw Sarpong (cousin), Yaw Adusei-Asomaning Obiri-Yeboah (Cousin), Alhaji Amponsah and my dear and lovely mom (Mrs. Naomi Boamah) and to all my love ones.

ACKNOWLEDGEMENT

I thank God for his abundant grace, mercies and protection throughout my two-year programme. Indeed God has been kind and faithful to me. I gratefully acknowledge and express deep appreciation to many wonderful people who made this thesis possible. To the management and staff of the Prudential Bank, Ecobank, Barclays Bank, Standard Charted Bank and Zenith Bank I say a big thank you for your maximum corporations in making this work a reality. God bless each and everyone and continue to bless these banks.

I would like to thank my supervisor Dr. Daniel Domeher for his time, patience and constructive criticisms, my family, my lecturers and my group members for their support throughout this course. Not forgetting my good friend and advisor through this project Mr. Appiah Karikari Michael for his guidance devotion and support during those difficult moments, It has been a roller coaster journey but thank God for his mercies. It was great meeting you all. May the lord bless us all.

ABSTRACT

The main aim of the study is to identify banks determinants of non-performing loans among selected banks in the Kumasi Metropolis (Prudential Bank, Ecobank, Barclays Bank, Standard Charted Bank and Zenith bank). For the purpose of this study a both purposive and convenient sampling technique was used to select 30 respondents. Responses from the respondents were analyzed using the Predictive Analytical Software (PASW) formerly known as Statistical Package for Social Sciences (SPSS). The finding indicated that the high interest rate is the major factor of nonperforming loan factors of selected commercial banks in Kumasi. The study revealed that majority of the workers was in support with the credit assessment and the occurrence of NPL. Simply because; know your customers policy bank leads to a high loan quality and good loan under writing ensures loan performance. Surprisingly, the study discovered that, collateralized loan perform well and helps to protect loan default, at the selected commercial banks in the Kumasi Metropolis. Also few of the workers had the perception that growth in bank size comes growth on NPL and bank great risk appetite is caused for NPL are the reasons for credit size and occurrence of NPL of selected commercial bank in the Kumasi. In sum, Nonperforming loans arise as a result of high interest rate of banks, banks great risk appetite, large number of borrowers, poor monitoring/follow up of loans given, the leniency of credit terms, poor risk assessment, and rapidity in growth of loan by banks and poor credit culture/orientation among others. The study

recommended that, Banks must initiate or if already in place strengthen their credit or loan policy in order to outline rigorous requirements that have to be met by borrowers before the issuance of loans. Also, Banks must have research department to carry out effective risk assessment in order to give the requisite advice on the issuance of loans to borrowers. Limitations of the study include constrains of time and finance.

TABLE OF CONTENTS

Content **Page**

LIST OF TABLES

LIST OF FIGURES

CHAPTER ONE

GENERAL INTRODUCTION

1.1 Background of the study

Hitherto, most nations had stabilized quality of credit and loan portfolios before the world economic meltdown in the 2007-2008. The recession witnessed by the world came with its attendant effect of decline in average bank asset quality and made regulators to place emphasis on issue of Non-Performing loans regardless of efforts aimed at regulating bank lending.

The IMF, World Bank and BIS stipulate that international strengths of banks in countries are examined by regulatory/supervisory bodies with the aid of non-performing loans aggregate rate. Variations exist in non-performing loan aggregate rates among world nations as for instance the aggregate values range between 0.2% and 26.5% respectively in Australia and Egypt from 2002-2006.

A preponderant of studies has declared that most bank outcomes such as performance and failures are mostly ligated to problem loans from external factors in external systems. Conversely, Salas et al. (2002) suggest that and problem loans have been examined as internal factors within a system.

In the aforementioned studies, the elucidation of non-performing loans was ligated to macroeconomic variable and banks' stipulated factors. The imperativeness of the contributory factors to non-performing loans stimulated several research on that facet and thus through that society is replete with data on problem loans. Breuer (2006) with the aid of bank scope assessed the sociological, economic, legal, political and institutional effects on problem loans.

Few banks and countries endowment of the detail bank scope data details on NPL made Breuer's work representatively prejudiced. Further, an assessment of the connections between various macroeconomic factors and financial strength variables (such as adequacy of capital, profitability and quality of organizations assets) based on the aggregate data of nations was methodologically carried out by Babihuga (2007).

According to Taylor (1993), banks' capital resources are afflicted by the losses of bad loans (NPLs) and this relatively stalls banks' business growth and development. Disclosure of the extent of these losses in its financial statements paves way for the banks' management to be impugned and also suffer low credit ratings. These will consequently lead to an increment in the banks' wholesale market borrowing cost and also exacerbate challenges in the banks' raising of capital. In the extreme mass withdrawals from the bank and loss of deposits ensue which culminates in unexpected liquidation (Taylor, 1993).

Thus NPL is among the tangible credit risks banks assume. Non-performing loan have consequence on banks' operations and the financial industry. Non-performing loans have historically being ligated to the occurrence of crises in the global banking industry as banks huge accrual of non-performing loans brings about impacts on banks' or financial institutions' total assets.

1.2 Statement of the problem

Many authors have studied the concept of loan default from so many angles. For instance, Bercoff et al (2002) examination of the fragile nature of Argentina's financial system and banks from 1993-96 posited that macroeconomic variables and banks'

specific factors had consequence on non-performing loans. The fragile nature of financial institutions or the sector was tied to the decline in the quality of banks' loan. González Hermosillo (1999) suggests that previous encounters or experiences suggest that the fast accumulation of bad loans impact on banks and causes crises in the sector. In Ghana series of studies have equally been conducted. Notably, credit risk emanates from circumstances where uncertainty counterparty's shoulder the ability to meet its obligations in uncertain environments. If the uncertainties materialize they would lead to deterioration of loan qualities. Decline in quality of banks' loans culminates in the

fragility of the financial institutions and the industry.

Previous encounters or experiences suggest that the fast accumulation of bad loans impact on banks and causes crises in the sector regardless, a comprehensive study focusing on different banks has least been explored. This is the intended gap the present study is aiming to fill. Subsequently, the above problem along with the knowledge gap in the literature stimulates an assessment of the determinants of non-performing loans among banks.

1.3 General Objective

The study's premise is to identify Kumasi commercial banks' non-performing loans specific determinants. Thus identifying determinants of nonperforming loans is very vital to minimize loan default.

1.3.1 Specific Objectives

1) To unearth banks specific non-performing loans determinants
2) To identify relationship between credit admittance policy, loan underwriting and risk assessment and level of nonperforming loans
3) To find out how credit monitoring and collateralized lending determine loan default

1.4 Research Questions

1) What are banks specific non-performing loans determinants?
2) What is the relationship between credit admittance policy, loan underwriting and risk assessment and level of nonperforming loans?
3) Does credit monitoring and collateralized lending determine loan default?

1.5 Justification of the study

The recent global economic meltdown globally led to defaults by households and firms and also impacted negatively on banks. Consequently, prudent and effective monitoring of quality of loans aided by preemptive systems or mechanisms to forewarn regulators of existing or prospective potential bank challenges and imminent crises will help ensure an indomitable and resilient financial sector globally.

Prudent risk management, with a special emphasis to credit risk is pivotal. The initiation of sound management of credit tools and the comprehension of contributory factors to occurrence of bad loan play is imperative.

A research like this would provide banks in Ghana with in-depth knowledge on the improvement of quality of loans as well as informing regulators on the re-examination of their policies in the facet of bank supervision and quality of banks’ assets.

The existing stock of literature on the determinants of nonperforming loans will be augmented by this thesis. Further, this research will stimulate further examination of Ghanaian Banking with emphasis on macroeconomic variables that determining nonperforming not captured by this research paper.

1.6 Scope of the Study

The study's context, geographical location and time influenced the work. The study was bent on identifying determinants of non-performing loans at Selected Commercial Banks, with the use of questionnaires to gather information.

Geographically, the study is limited to selected braches of Selected Commercial Banks in the Kumasi metropolis. The study area is informed by information accessibility and proximity to large population. The design scope is delimited to a cross-sectional descriptive survey approach. This is because of its cost effective and convenient features.

1.7 Limitation of the study

The study encountered challenges. The limitations or challenges included Design limitation i.e. cross-sectional descriptive survey was adopted by the researcher though longitudinal or time series will have been apt for the study. Hence data was collected at one point in time.

Again, geographical expanse of the study area, inadequate resources including financial and time constraints curtailed contacts with respondents. However purposive sampling, questionnaire piloting and careful scrutiny of the perceived parameters of measurement in the population and sample came to the researchers' rescue.

1.8 Organization of the study

The study would be organized in five (5) sections. Chapter one or the introductory chapter involve the background of the study, the problem statement, research questions, objectives of the study, justification of the study, scope and limitation of the study, research methodology and organization of the study. Chapter Two contains the Literature Review and summary of some related studies associated with credit risk, non performing loans and Profitability. Chapter Three also deals with the methodological or methods and procedures deployed in undertaking the research. Chapter Four involves the presentation of gathered data, its analysis and discussion represented tables, figures, graphs among others. Chapter Five encapsulates major study findings, conclusions inferred from the findings and recommendations for policy initiations and implementation.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

The section is a representation of the study's pertinent theoretical and conceptual underpinnings. This present study is tied with previous significant studies apropos the established objectives of the study. Hence, non-performing loans determinants were presented. Subsequently, macroeconomic variables that define nonperforming loans were examined. Again, existing studies on bank specific elements of nonperforming loans were assessed. The final subsection presents previous studies in the identification of knowledge gap.

2.1 Role of Banks

The banking sector makes a meaningful contribution to the economic growth of every country. Banks contribution to the growth lies in the role they play in mobilizing deposits and allocating the resources efficiently to the most productive uses investment in the real sector. Thus borrowers' contribution to the growth of economies hinges on the availability of credit available. Banks pool resources together for projects that are too large for individual shareholders to undertake (Bagehot, 1873). Thus banks are the principal sources of credit and facilitators of financial transactions in nations' economies (Rose, 2002).

Banks protect a nation's money embodied in deposits (Sinkey, 2002; Harris, 2003). Valdez et al. (2000) states that banks recent roles have been widened from the basic roles of taking deposits and credit provision to incorporate the creation of money; via deposit liabilities, managers of payment system; through cheque payment with the aid of Automatic Clearing Bureau (ABC) and give out loans to numerous borrowers for varied personal or business purposes (Saunders and Cornett, 2003). Banks ease credit payments, debit cards, automatic teller machines and cell/phone/internet banking. Again, banks create indirect financial securities through their hold of assets dependent on specific risks and these claims against risk are largely eliminated through diversification.

Banks also serves as information agents with their sound and concealed asymmetrical record of client information. Full general reports and bank codes are the means through which client information is shared with other banks. The gap created by capital markets' inability to create the needed business instruments are filled by banks. Banks also deal in foreign currency as they facilitate currency conversions, funds transfers and engage in foreign finance negotiations.

Nonetheless funds utilization of banks hinge on lending, which is deemed very important by the banks. Since a major portion of gross profit of the industry is earned from loans, effective loan management on banks' profitability (Wei-Shong et al. 2006).

2.1.1 Nonperforming Loans (NPL)

A non- performing loan involves a loan whose interest and principal payments pass the 90 days threshold for redemption or refinancing of interest (IMF 2009). Non- performing loans involve loans with uncertain cash flow streams unrecognized by banks until the receipt of cash and also loans with lower interest rate on the increase in its maturity (Machiraju, Undated). HR Machiraju expresses nonperforming loans as a leading indicator of credit quality. Non-Performing Loans (NPL) or bad loans arise in respect of the loans and advances which are given by banks to the whole range of different projects including but not exclusively retail or wholesale, personal or corporate or short, medium or long term projects. NPLs are a very sensitive element of a bank's operations.

Loans and advances constitute the primary source of income by banks. As any business establishment, a bank also seeks to maximize its profits through loans since loans entail profitability tendencies than any other assets, hence harbors the zeal to lend much funds in tandem with its capacity. Circumspection is however needed by banks apropos their lending advances (Radha *et al*. 1980). Bankers naturally try to balance the issue of maximizing profit by lending and at the same time manage risk of loan default as it would impair profit and thereby the very capital .Thus a bank needs to be cautious in advancing loans as there is a greater risk which follows it in a situation where the loan is defaulted. In other words loan loss or defaulted loans puts a bank in a difficult situation especially when they are in greatest amount. This emanates from the uncertainties regarding loan redemption or repayment regardless of banks hold of securities. Different scholar perspectives exist regarding non-performing loans. Paterson and Wadman (2004) saw non-performing loans as unprofitable or defaulted bank loans as they are not recovered within state laws stipulated time.

Historically, banking disasters are often ligated with massive accrual of non-performing loans (a substantial part of banks' total assets) of bankrupt or liquidated financial institutions or banks during crisis. The fragile nature of financial institutions or the sector was tied to the decline in the quality of banks' loan. González et al. (1999) suggest that previous encounters or experiences suggest that the fast accumulation of bad loans impact on banks and causes crisis in the sector. Generally, non-performing loans (NPLs) percentage reflects in global bank failures and financial crises.

Quantitative and qualitative norms or criteria differentiate good and bad loans.

Quantitatively the overdue schedule payments days are used and qualitatively, clients' financial status information availability and perspectives about future payments were used as distinguishing factors for good and bad loans. Accordingly, the Basel committee puts nonperforming loans as loans left unpaid for a period of 90 days as has been mentioned in the preceding paragraphs. The Ghana banking business directive views non-performing loans as "loans or advances whose credit quality has deteriorated such that full collection of principal and/or interest in accordance with the contractual repayment terms of the loan or advances in question (NBE, 2008)." It further provides that loans or advances with pre-established repayment programs become non-performing in the event the principal or interest is due and uncollected for 90 (ninety) consecutive days or beyond the payment date or maturity (NBE, 2008).

In addition to the above mentioned category of non- performing loans, loans and advances without pre-established repayment program become non-performing when the debt is outstanding or exceed the borrower's approved limit of 90 (ninety) consecutive days or beyond scheduled payment date/maturity, interest is due and uncollected for 90 (ninety) consecutive days and more. Overdrafts culminate in non-performing loans when borrower's accounts become inactive for 90 (ninety) consecutive days, the borrower's deposits are insufficient to match or cover interest capitalized during 90 (ninety) consecutive days and the borrower's account becomes unable to show the 20% of approved limit at least once a year prior to the date of loan review. This is in accordance with the Basel rules. If a loan is past due for 90 consecutive days, it will be regarded as non-performing. The criteria used in Ghana banking business to identify non- performing loan is a quantitative criteria based on the number of days passed from loan being due.

Generally, numerous facets of loan defaults exist in developing and underdeveloped countries. Researchers have attributed varied reasons for the default of loan.

Determinants of NPL are categorized by macroeconomic and bank specific factors according to literature.

George, (2004) suggest that several literature unearthed the linkage between business cycle phases and banking stability. Thus banks' foundation and stability have linkage with its nations' macroeconomic stability environment. Banking crisis is thus tied with the macroeconomic instability of the environment in which they operate. Literature connecting business cycle phase with banking stability has often examined the association between macro-economic environment and quality of loan. These researches postulate that nations' economies expansion feature relatively low number of NPLs, as firms and consumers benefit from inflow of sufficient income and revenues for their debt servicing. However, banks' uncalculated extension of credit to low quality debtors in times of economic booms backfires into NPL during recession or economic meltdowns (Geanakoplos, 2009).

Salas et al., (2002) suggest that GDP growth has substantial and negative concomitant effect on NPL ratio and subsequently attribute macroeconomic developments to economic agents' capacity to service their loans. Unemployment and interest rates culminate in NPL thus impacting on household and firms as they negatively influence household and firms' cash flow thereby exacerbating their debt burden.

2.2 Determinants of Nonperforming Loans

Sonali (2001) maintains that the investment climate is characterized by default as it has become an acceptable culture because do not care about being declared defaulters.

Largely, various facets of loan defaults exist in developing and underdeveloped countries. Researchers have attributed varied reasons for the default of loan.

Determinants of NPL centered on macroeconomic and bank specific factors.

Bercoff et al (2002) examination of the fragile nature of Argentina's financial system and banks from 1993-96 posited that macroeconomic variables and banks' specific factors had consequence on non-performing loans. The fragile nature of financial institutions or the sector was tied to the decline in the quality of banks' loan. González Hermosillo (1999) suggests that previous encounters or experiences suggest that the fast accumulation of bad loans impact on banks and causes crisis in the sector.

The recent global financial meltdown increased households' and firms' defaults, causing significant losses for banks. The below section discusses determinants of nonperforming loans starting with macroeconomic factors and then bank specific factors. In the following sub-section the details of the various determinants are discussed.

2.3 Macroeconomic Determinants of Nonperforming loans

The macroeconomic determinants of the quality of banks' loans have been area of various researchers during the past two decades. The literature on the major economies has confirmed that macroeconomic conditions matter for credit risk. These literatures among others have investigated the linkage between macroeconomic factors like GDP, inflation, real interest rates, unemployment etc. and loan performance. The paragraphs that follow critically review the existing literature on the major macroeconomic factors that have bearing on Non-performing loans (NPL).

George, (2004) suggest that several literature unearthed the linkage between business cycle phases and banking stability. Thus banks' foundation and stability have linkage with its nations' macroeconomic stability environment. Banking crisis is thus tied with the macroeconomic instability of the environment in which they operate. Literature connecting business cycle phase with banking stability has often examined the association between macro-economic environment and quality of loan. These researches postulate that nations' economies expansion feature relatively low number of NPLs, as firms and consumers benefit from inflow of sufficient income and revenues for their debt servicing. However, banks' uncalculated extension of credit to low quality debtors in times of economic booms backfires into NPL during recession or economic meltdowns (Geanakoplos, 2009).

Keeton and Morris (1987) attributed large portions of loan losses by banks in America to unfavorable economic environment or conditions and poor performances after their study of a sample of nearly 2,500 US commercial banks using simple linear regressions.

Sinkey and Greenwalt (1991) in their examination of large US commercial banks from 1984 to 1987 with the aid of simple log-linear regression found depressed state/regional economic conditions as the cause of the banks' loss rate. Further, an association was found between increment in credit risk and adverse macroeconomic conditions considering asset-price of banks (Mueller et al. 2000). Similar findings were established by Kent and D'Arcy (2000) in their studies on Australian banks and Rajan and Dhal (2003) that examined similar association in Indian banks.

Mariucci and Quagliariello (2008) studied the Italian banking system by employing a reduced form value at risk (VAR) to examine the impact of business cycle conditions on the rate bank customers default from 1990–2004 and established that bank customers' rate of default follow a cyclical pattern i.e. defaults fall during macroeconomic expansions and increase during economic downturns. Salas and Saurina (2002) posit that GDP growth plays part in the NPL variation after they employed a dynamic model/ panel dataset to assess the determinants of problem loans of Spanish commercial and saving banks from 1985-1997. Rajan and Dhal (2003) found a relationship between GDP growth or favorable macroeconomic conditions and NPLs of commercial banks in India in their study of Indian commercial banks aided by panel regression analysis. Empirical studies corroborate the aforementioned link between the cycle's phase and credit

defaults.

According to Quagliarello (2007) business cycle influenced the NPL ratio of Italian banks from 1985 to 2002. Furthermore, Jimenez and Saurina (2005) found GDP growth and interest rates to be the determinants of NPL in Spanish banking sector from 1984 to 2003.

Salas and Saurina (2002) GDP growth had concurrent effect on the NPL ratio as macroeconomic developments translates to economic agents capacity to service their loans.

Furthermore, Cifter *et al* (2009), via neural network based wavelet decomposition established delayed industrial production effect on the quantity of non-performing loans in the Turkish financial system from January 2001 to November 2007. Bercoff et al. (2002) found that money multiplier, adequacy of reserve impact on NPLs after their analysis of Argentina's banking system via accelerated failure time model.

Moreover macroeconomic instability variables such as high inflation rate impact negatively on banks' loan appraisal because the uncertain economic climate makes the identification and viability of prospective borrowers difficult. Instability in the economy also makes asset prices high.

Martin Brownbrigde, (1998) sees future real value of security of loans as unpredictable. Banks poor performance is when their product and asset price, policy, inflation accelerates unpredictably and when inflation decelerates unpredictably unemployment increases, and/or aggregate output and income surprisingly decline. Unpredicted accelerations in inflation negative impact on banks that, on average, lend longer term at fixed-rates than they borrow because nominal interest rates will raise more than expected. This will increase their cost of deposits relative their revenues from loans.

An upsurge in unemployment rate negatively impact on the cash flow streams of households and their debt burden. Concerning firms, increases in unemployment may signal low productivity as a result of a drop in effective demand. This culminates in decrease in revenues and a fragile debt condition.

Studies carried out on several banks in various economies establish a correlation between macroeconomic factors like inflation, unemployment and interest rate and loan defaults.

Fuentes and Maquieira (2003) study on Chilean banks posit that interest rates had higher impacts on NPLs than business cycle. Also, exchange rate, unemployment, and asset and house prices are also determinants of NPL (IMF, 2006). Hogarth et al. (2005) from 1988–2004 employed quarterly data of the UK to assess the dynamics between banks' write off to loan ratio and several macroeconomic indicators discovered that banks' write off ratio also increases as retail price inflation and nominal interest rates increase.

Similarly, Babouček and Jančar (2005) analyzed the effects of macroeconomic shocks on the loan quality of the Czech banking sector for the period 1993– 2006 and found a positive correlation of non_performing loans with the unemployment rate and consumer price inflation. Gambera (2000) assessed the effect of state and nation wide macroeconomic variables on the quality of different types of loans (agricultural, commercial, industrial and residential) using US quarterly data for 1987–1999. He found out that unemployment rate, farm and non_farm incomes, bankruptcy filings and car sales, among various explanatory variables, were significant determinants of bank asset quality.

Filosa (2007), estimation of three distinct Value at Risk (VAR) models over the period 1990–

2005 with different indicators of banks' financial strength established a somewhat weaker connection between macroeconomic developments and banks' soundness. Conversely, he finds that decline in the quality of loans weakens real activity and

inflation.

Arpa et al. (2001) examination of the effects of macroeconomic developments on risk provisions of Austrian banks for the period 1990–1999 by the use of a single equation time series model stated that risk provisions ascend when real gross domestic product growth declines.

2.4 Bank Specific Factors causing Nonperforming Loans

Macroeconomic variables viewed as external/exogenous forces influencing the banking industry should not be sought exclusively in the determination of NPLs. Conversely, the banking sector's specific policy choices and their efforts to maximize efficiency and improve risk management exert vital influence on NPL revolution. Literatures on bank specific determinants of nonperforming loans are reviewed in the section that follows.

2.5 Rapid Loan Growth

Some studies suggest that loan delinquencies have connection with rapid credit growth. Keeton (1999) after using data from commercial banks in the United States (from 1982 to 1996) together with vector auto regression model, posit that there is a relationship between loan and rapid credit growth.

Similarly Weinberg (1995) after using data on the growth rate of total loans and loan charge-offs in the United States from 1950 to 1992 established a pattern where increases in lending precede increases in loan losses. He further hypothesized that risk-neutral lenders increase lending during periods of economic booms as they expect improvement on return of investments and subsequently, returns from all loan customers.

2.5.1 High Interest Rate

Banks with high interest rate charges comparatively face higher default rate or nonperforming loans. Sinkey and Greenwalt (1991), Rajan and Dhal (2003) and Waweru and Kalini (2009) in their respective studies in the US, India and Kenya on the commercial banks indicated that high interest rate charged by the banks is one of the internal factors that leads to incidence of non-performing loans.

2.6 Lenient Credit Terms

Credit sanctioning without due consideration to credit terms could potentially lead to occurrence of poor loan performance. Jimenez and Saurina (2005) study in Spain (1984 to 2003) stipulate that NPLs determination rely on lenient credit terms. Disaster shortsightedness, behavior, moral challenges and agency problems that enticed bank managers to take risk and lend excessively during economic boom periods are attributed to NPL occurrence.

Rajan (1994) postulates that bank managers' characteristic lack of foresight in decision making because of the strong influence public perceptions of their performance have on their reputation accounts for short-term earnings. Thus managers' reputations are impugned if they are unable to expand credit in tandem with banks and economic booms. This herd behavior culminates in loans going to customers with the likelihood of defaulting.

According to the Office of the Comptroller of the Currency (OCC, 1988) bank failure in the early 1980s was attributable to poor bank management and lax lending standards. FDIC (1997) found economic, legislative, managerial, and regulatory elements as the causes of the banking crises of the 1980s and early 1990s.

2.8 Bank Size

Cole et al. (2004) used data from the 1993 Federal Reserve National Survey of Small Business Finance, in their banks financial reports, suggest that smaller banks adopt small business loan underwriting practices riskier than those of larger banks. This is so because small banks prefer to lend to small firms that lack hard financial data to support the lending decision and riskier to the extent that the failure rates of small businesses are higher than those of larger, established firms. Rajan and Dhal (2003) in their study of commercial banks in India, by use of panel regression analysis indicates that banks size has impact on NPLs occurrence.

2.9 Cost Efficiency

Hughes et al. (1995) tied banks' assumption of risk to their efficiency. The argument is that risk-averse managers harbor the zeal to exchange reduced earnings for reduced risk, especially when their wealth hinges on their institution's performance. Increase in monitoring is the way they devise to improve loan quality which however increases their costs thereby impacting on the measure of operating efficiency.

2. 10 Ownership structure

Hu et al (2006) analyzed the connection between NPLs and ownership structure of commercial banks in Taiwan with a panel dataset covering the period 1996-1999. The study discovered that banks with higher government ownership recorded lower nonperforming loans. Walter and Werlang (1995) found that state-owned financial institutions underperform in their market, because their portfolios concentrate on the non-performing loans indebted by the state. Jang and Chou (1998) adopted the ratio of non-performing loans to total loan as the measure of risk by using 1986-1994 data of 13 Taiwanese banks for empirical study. The average risk-adjusted cost efficiency of the four provincial government-owned banks was the lowest among the sample banks.

2.11 Monitoring

A sound financial system hinges on regular monitoring of loan quality as it forewarns regulatory authorities on potential bank stress that could result in crisis (Agresti et al. 2008). Emphasis on borrower thus need not be overemphasized so as to ensure loan performance. Better attention of lenders to borrowers is reciprocated since some of the loans defaults are ascribed to lower level of attention given to borrowers (Mayers, undated).

Many banks losses are attributed to their poor monitoring their borrower's property as they fail to recognize early warning signs. The objective of supervising a loan is to confirm the prudency of the loan decision and ascertain whether the loan funds are being properly utilized for the purpose intended. Monitoring is also the means of knowing the borrower, loan repayment capacity, capital contribution, prevailing market conditions and the value of the collateral that was taken during loan approval time continues to remain the same (George G, 2004).

Periodic visits to the borrowers endow banks with the progress of the borrower's business activity and thereby give him/her advice as necessary. Constant monitoring increases the chance that the company will respond to a bank's concern and provide information more willingly. A bank which always closely follows a company's operations can detect danger or opportunities to the company, as well as quick agreement to request for credit. It thus establishes that monitoring is basically constructive, not a reactive or panic situation (Donaldson, undated)

A bank should have clearly defined continuous procedures for identifying potential bad and doubtful loans. These procedures should include regular independent reviews of the loan portfolio. Within this system, there should be formal procedures for the continuous review of all large loans and all areas of lending concentration. These reviews should place particular emphasis upon the borrower's continuing ability to service the loan. Failure to do these continuous reviews and monitoring will lead to loss to banks or increases the risk of such losses. From the regulatory point of view, Ghanaian banks are required to make continuous review of their loan and submit reports to the central bank.

This function of banks has a legal as well as contractual base. But the detail as to the frequency of visiting the borrower's premises, verifying the use of the loan and other related circumstances is the discretion of individual banks. The legal base for banks to do the review is provided under Article 5 of Directive No.SBB/43/2008.

2.12 Poor Risk Assessment

Loans are associated with risk. Regardless of how secured a loan and the pedigree of the borrower, loans have the potential to generate loss for the lender. Loans risk susceptibility and loss probability on the side of lenders is what varies (Brown, 1993).

Banks consider the quality of a borrower in, inter alia, its past and projected profit performance, the strength of its balance sheet, market for his/her product, economic and political conditions in the country before deciding to lend or not. Banks knowledge of the intended purpose of loan and its validity, the payment of interest and how the repayment of capital will be regenerated is necessary.

Strategy to mitigate non- performing loans (*The Five C's of Credit)*

There were several ways and strategy to mitigate non-performing loans. According to (Rose, 2002) the conventional ways of dealing with credit do not differ much from the modern approach. She considered the five Cs as the most efficient and effective ways of handling and dealing with credit default related issues. This was opposes to the initially system of resorting to character, capacity and capital approaches. According to Murphey (2004a), in an attempt to successfully deal with loan defaults the collateral and conditions were added to ensure total effectiveness. As these approaches provide the comprehensive and clearer approaches to the problem. These must serve as the leading principles and a cornerstone of every lending decision.

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 Introduction

The methods and study setting adopted for this study are discussed in this chapter. In this regards, the following had been raised and discussed. Notably: the study design, population, sampling size and sampling techniques, sources of data for the study, data collection instruments, data analysis techniques and ethical consideration.

3.1 Research Design

There are various kinds of research design available for scientific research study. Notably among them are quantitative, qualitative and mixed method designs. However, upon consideration and deliberation of issues, the researcher adopted the mixed method design. This is because it's blend the two other research approaches. Moreover, it prevents possibility of errors due to the complementary role of the two. In this approach the survey strategy was used to reach out to the respondents. Survey in this study is defined as the process of pulling answers from different people using same questions whiles making inference to the large population in which the sample were drawn from.

3.2 Population

The population is the universe from which samples are chosen. It defines elements with same and similar characteristics. Population is the entire number of people or element available for a study. From the survey the target population for this study comprises of management and staff of Selected Commercial Banks Kumasi Metropolis. Target population shall comprise of loan officers and managers in the following banks:

Prudential Bank, Ecobank, Barclays Bank, Standard Charted Bank and Zenith Bank

3.3 Sample Size and Sampling Procedure

Sampling defines the process of using part to represent a whole. In the normal parlance, the larger the sampling the more representative the outcome and the vice visa. However, when the given population is small the study must factor in a relatively larger sampling. This enables the researchers to draw accurate conclusion and make prediction quite easier. Non-probability sampling technique convenient was used to select the five (5) banks and also the 30 respondents for the study. Five respondents each are selected from Prudential

Bank, Ecobank, Barclays Bank, Standard Charted and Zenith Bank. This is due to time, finance and information readiness.

3.4 Sources of Data

Basically, there are two main sources of obtaining research information. Either through the primary source or the secondary sources. In this study the primary information were obtained through questionnaires distribution and interview guide. The secondary information were predominately from the literature review through the search engines.
Notably: Google scholar.

3.5 Data Collection Instruments

In an attempt to collect and gather meaningful information for the study, the researcher resorted to the use of questionnaires. This was partially due to the nature of the questionnaires and secondly questionnaire enables the pulling of large data from diverse population within the shortest time period and relatively lower cost. The questionnaires were in two folds. Namely: open and close ended questions. The open ended questions were aimed to allow for the respondents opinion whiles the closed ended give force option to choose from. The combination of the two in this study allowed more quality and valid information to be obtained. The responses were then reviewed and coded for data analysis.

3.6 Data Analysis

Upon the completion of all the data collection activities, the researcher adopted
Predictive Analytic Software (PASW) version 20.0 formerly Statistical Packages For Social Scientist (SPSS) for the data analysis. This was due to the fact that it is the most recommended statistical software package in the KNUST Business School. Beside it is

easy and convenient to use. The version twenty in particular has newly added feature that makes it different from the preceding versions.

3.7 Ethical Considerations

The main respondents were informed before participating to indicate their willingness. This was done to ensure the right protection of the respondents. Respondents who formed the focus of the study were asked to indicate their willingness to participate in the study. Moreover during the primary data collection, the information was duly handled to ensure rights to privacy of respondents. Both anonymity and confidentiality were ensured throughout the study. This includes the use of hypothetical names in the study just to disguise the actual identity of the respondents.

CHAPTER FOUR

PRESENTATION OF DATA AND ANALYSIS

4.0 Introduction

This chapter presents analysis of findings of the primary and secondary data of field survey to investigate into factors that determine non-performing loans at Selected Commercial Banks Ghana (Prudential Bank, Ecobank, Barclays Bank, Standard Charted Bank and Zenith Bank) with particular reference to the responses received as well as variables identified from literature. The findings of the study were captured in the forms of tables in line with the established objectives. Before analyzing the data, the questionnaires were cleaned up to remove possible errors to ensure accuracy, consistency, uniformity and completeness. The data gathered were analyzed quantitatively.

4.1 Background Information

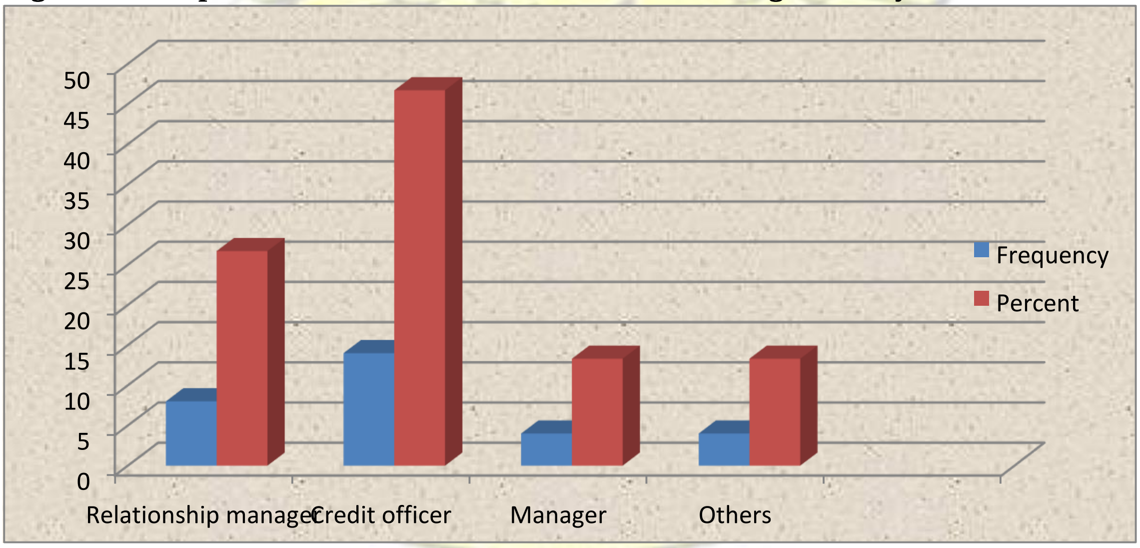
Table 4.1.1 Respondents Current Position In The Banking Industry

Variables	Frequency	Percent	Cumulative Percent
Relationship manager	8	26.7	26.7
Credit officer	14	46.7	73.4
Manager	4	13.3	86.7
Others	4	13.3	100.0
Total	30	100.0	

Source: Field Survey, 2015

The Table 4.1.1 reveals the current position workers in the Selected Commercial Banks (Kumasi Metropolis). Workers who are relationship managers are 26.7, 26.7% of them are credit officers. Workers who are manager are 13.3% and workers who are holding other positions are 13.3%. The results shows that majority of the workers are relationship managers. The figure 4.1 gives a pictorial view of the results in the table 4.1.1

Figure 4.1 Respondents Current Position In The Banking Industry



Source: Field Survey, 2015

Table 4.1.2 Respondents Experience In The Banking Industry

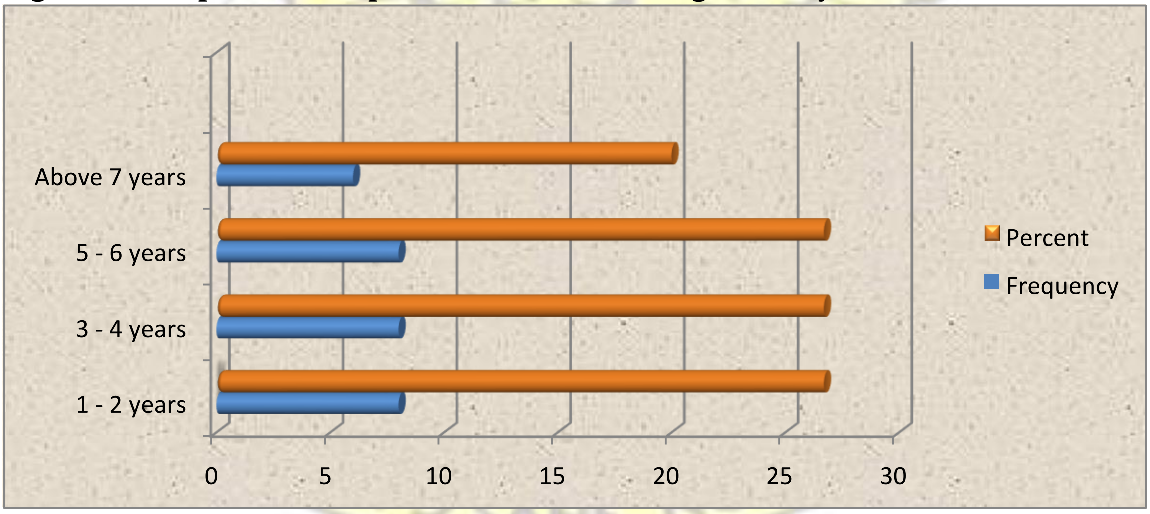
Variables	Frequency	Percent	Cumulative Percent
1 - 2 years	8	26.7	26.7

3 - 4 years	8	26.7	53.3
5 - 6 years	8	26.7	80.0
Above 7 years	6	20.0	100.0
Total	30	100.0	

Source: Field Survey, 2015

The Table 4.1.2 identifies the banking experience of the worker in the banking industry. Workers with 1-2 years banking experience are 26.7%, workers with 3-4 years banking experience are 26.7% and workers with 5-6 years banking experience are 26.7%. Finally, 20.0% of the workers are having more than 7 years banking experience. This implies that majority of the workers in the Selected Commercial Banks in the Kumasi Metropolis are having below 6 years working experience. The figure 4.2 further enhances the results in the table 4.1.2.

Figure 4.2 Respondents Experience In The Banking Industry



Source: Field Survey, 2015

Table 4.1.3 Respondents Experience In Bank Credit Processes

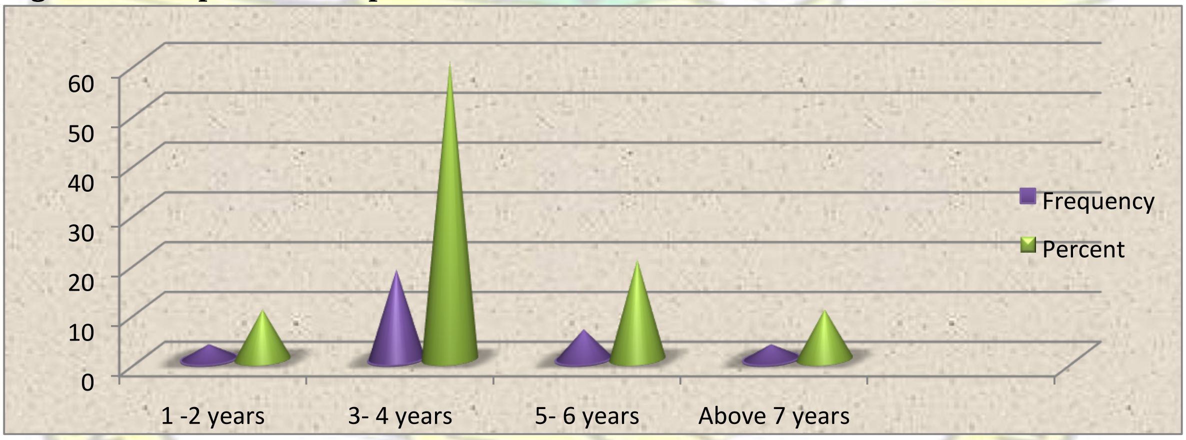
Variables	Frequency	Percent	Cumulative Percent
1 -2 years	3	10.0	10.0
3- 4 years	18	60.0	70.0

5- 6 years	6	20.0	90.0
Above 7 years	3	10.0	100.0
Total	30	100.0	

Source: Field Survey, 2015

The Table explores the workers experience in bank credit processes in the Selected Commercial Banks in the Kumasi Metropolis. Workers who have 3-4 years in bank credit processes are 60.0% and 20.0% of the workers are having 5-6 years of experience in bank credit processes. Also, with respect to bank credit processes 10.0% of the workers are having 1-2 years and above 7 years in the Selected Commercial Banks (Kumasi Metropolis). The results confirm that most of the workers are 3-4 years of experience in bank credit processes. The figure 4.3 gives an illustration of the results in the table 4.1.3

Figure 4.3 Respondents Experience In Bank Credit Processes



Source: Field Survey, 2015

Table 4.1.4 Ownership Of The Bank

Variables	Frequency	Percent	Cumulative Percent
Private	30	100.0	100.0

Source: Field Survey, 2015

The Table 4.1.4 confirms that all the working places of the workers in the Selected Commercial Banks (Kumasi Metropolis) are privately owned.

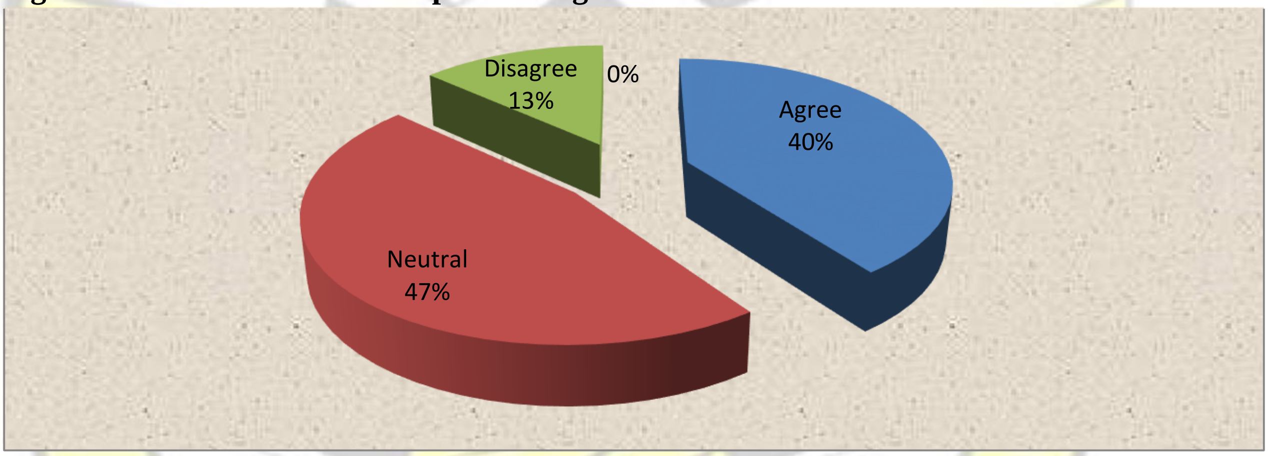
Table 4.1.5 Determinant Of Nonperforming Loans Are Obvious

Variables	Frequency	Percent	Cumulative Percent
Agree	12	40.0	40.0
Neutral	14	46.7	86.7
Disagree	4	13.3	100.0
Total	30	100.0	

Source: Field Survey, 2015

The Table 4.1.5 declares that 46.7% of the workers did not specify whether obviously there are determinant of nonperformance loans. Workers who agreed that there is nonperformance of loans in the Selected Commercial Banks in the Kumasi Metropolis are 40.0% and 13.3% of them also disagreed. The study implies that obviously there is no determinant of nonperforming loans in the Selected Commercial Banks in the Kumasi Metropolis. A picture of the results in the table 4.1.5 is in the figure 4.4 below.

Figure 4.4 Determinant Of Nonperforming Loans Are Obvious



Source: Field Survey, 2015

4.2: Answering Research Objective One

In answering research objective one the study assessed the determinants of nonperforming loans with eight factors to identify which one is the major NPL determinants and one which is the least

4.2.1: Non-Performing Loan Factors (Determinants of Non-Performing Loans)

Table 4.2.1: Non-Performing Loan Factors (Determinants of Non-Performing Loans)

ITEMS	RANK (X)
High interest rate	1.7333
Poor monitoring / Follow	1.6000
Lenient credit term	1.5000
Others, please specify	1.4000
Rapid loan growth by banks	1.4000
Size of the Bank	1.3000
credit culture/ Orientation	1.3000
Poor risk assessment	1.0667
Ownership type of Bank	1.0000
N	30

Source: Field Survey, 2015

The Table 4.2.1.1 examines the nonperforming factors of Selected Commercial Banks in the Kumasi Metropolis. High interest rate (X=1.73), poor monitoring/follows (X=1.60), lenient credit team (X=1.50), others (X=1.40), rapid loan growth by banks (X=1.400), size of the bank (X=1.30), credit culture/orientation (X=1.30), poor risk assessment (1.06%), ownership type of bank (X=1.00).

The finding indicates that all the aforementioned are factors of nonperforming loan factors of Selected Commercial Banks in Kumasi. It was found that high interest rate is the major factor of the Selected Commercial Banks in the Kumasi Metropolis. The remaining factors are also issues bordering the nonperformance of the bank.

4.3: Answering Research Objective Two

In answering the study's objective two the study assessed the response rate on the: credit assessments and the occurrence of NPL; borrower's orientation and the occurrence of NPL and credit size and the occurrence of NPL

4.3.1: Credit Assessments And The Occurrence Of NPL (*Answering Research Objective two*)

With the help of Likert scale 1-5 (where a mean of 5 indicated strongly agree, 4 agreed, 3 neutral, 2 disagree and 1 indicated strongly disagree), the study tasked the respondents to rate their agreement or disagreement with the factors enumerated in the table 4.

Table 4.2.2.1 Credit Assessments And The Occurrence Of NPL

Variables	Mean	Std. Deviation
Good loan under writing ensures loan performance	4.1667	.53067
Know your customers (KYC) policy of Banks lead to high loan quality	4.1667	.94989
Easy admitted borrowers usually default	4.1333	.73030
Poor risk assessment would lead to loan default	3.9667	.88992
N	30	

Source: Field Survey, 2015

The Table 4.2.2.1 explores the credit assessment and the occurrences of NPL. Good loan under writing ensures loan performance (X=4.16, STD=.53), easy admitted borrowers usually default (X=4.13, STD=7.3), Poor risk assessment would lead to loan default (X=3.96, STD=.88) and know your customers (KYC) policy of Banks lead to high loan quality (X=4.16, STD=.94).

The study reveals that majority of the workers strongly agreed with the credit assessment and the occurrence of NPL simply because; know your customers policy bank leads to a high loan quality and good loan under writing ensures loan performance. Subsequently, a few of the workers also confirmed that they support the credit assessment and the occurrence of NPL because, poor risk assessment will lead to high loan quality.

4.3.2: Borrower's Orientation And The Occurrence Of NPL (*answering Research Objective Two*)

With the help of Likert scale 1-5 (where a mean of 5 indicated strongly agree, 4 agreed, 3 neutral, 2 disagree and 1 indicated strongly disagree), the study tasked the respondents to rate their agreement or disagreement with the factors enumerated in the table.

Table 4.3.2 Descriptive Statistics On Borrower's Orientation And The Occurrence Of NPL

Variables	Mean	Std. Deviation
loan price affect loan performance	4.6000	1.03724
There is a relationship between loan default and borrower's culture	4.2667	.58329
Charging big intrest rate leads to loan default	4.1000	.54772
Borrower's orrientation / culture is related to loan performance	4.0667	.25371
Lenient / lax credit term cause loan default	4.0667	1.14269
Society's cultural development leads to good loans performance	4.0333	.92786
Default in some ares is ascribed to the culture of the borrower's	4.0333	.61495
poorly negotiated credit terms lead to loan nonperformance	3.8333	.98553
Borrowers default because they don't understand credit terms well	3.6667	1.09334
Loans with intrest rate tends to turn to NPL	3.3000	1.11880
N	30	

Source: Field Survey, 2015

The Table 4.3.2 measures the borrower's orientation and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis. The following variables are; borrowers default because they don't understand credit terms well (X=3.66, STD=1.11), loan price affect loan performance (X=4.60, STD=1.03), there is a relationship between loan default and borrower's culture (X=4.26, STD=.58), loans with interest rate tends to turn to NPL (X=3.30, STD=1.11), charging big interest rate leads to loan default (X=4.10, STD=.54), poorly negotiated credit terms lead to loan nonperformance (X=3.83, STD=.98), borrower's orientation / culture is related to loan performance (X=4.06, STD=.25), default in some areas is ascribed to the culture of the borrower's (X=4.03, STD=.92) and lenient / lax credit term cause loan default (X=4.06, STD=1.14).

The study shows that loan price affect loan performance, charging big interest rate leads to loan default, default in some areas is ascribed to the culture of the borrower's and there is a relationship between loan default and borrower's culture are some of the factors why majority of the workers came into strongly agreement with borrower’s orientation and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis.

However, poorly negotiated credit terms lead to loan nonperformance, loans with interest rate tends to turn to NPL and borrowers default because they don't understand credit terms well are also factors which few of the workers mentioned as the reasons borrower’s orientation and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis.

4.3.4: Credit Size And The Occurrence Of NPL (*Answering Research Objective Two*)

With the help of Likert scale 1-5 (where a mean of 5 indicated strongly agree, 4 agreed, 3 neutral, 2 disagree and 1 indicated strongly disagree), the study tasked the respondents to rate their agreement or disagreement with the factors enumerated in the table.

Table 4.3.4 Descriptive Statistic Credit Size And The Occurrence Of NPL

Variables	Mean	Std. Deviation
With growth in Bank size comes growth on NPL	4.2000	1.18613
BAnks great risk appetite is caused for NPL	4.0000	1.20344
Banks who credit growth is rapid experience huge NPL level	3.9667	.88992
Having large number of borrowers cause loan default	3.9000	1.47040

Loan default is not related banks ownership type (private / state owned)	3.7000	.74971
Loans default rate is directly related to Bank's size	3.7000	1.36836
Aggresive lending leads to large NPL volume / ratio	3.4667	1.47936
Compromised intergrity in lending leads to loan default	3.4333	1.16511
N	30	

Source: Field Survey, 2015

The Table 4.2.4 discloses the credit size and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis. The following are the factors stated; banks who credit growth is rapid experience huge NPL level (X=3.9, STD=.88), with growth in Bank size comes growth on NPL (X=4.20, STD=1.18), bank great risk appetite is caused for NPL (X=4.00, STD=1.20), compromised intergrityin lending leads to loan default (X=3.43, STD=1.16), aggressive lending leads to large NPL volume / ratio (X=3.46, STD=1.47), having large number of borrowers cause loan default (X=3.90, STD=1.47), loan default is not related banks ownership type (private / state owned) (X=3.70, STD=.74) and loans default rate is directly related to Bank's size (X=3.70, STD=1.36). This indicates that few of the workers strongly agreed that growth in bank size comes growth on NPL and bank great risk appetite is caused for NPL are the reasons for credit size and occurrence of NPL.

Subsequently, majority of the workers also mentioned some factors as the reasons for credit size and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis. Notably are; loans default rate is directly related to Bank's size, having large number of borrowers cause loan default, compromised intergrityin lending leads to loan default, banks who credit growth is rapid experience huge NPL level and aggressive lending leads to large NPL volume / ratio.

4.4 Answering Research Objective Three

In answering research objective three the study assessed how credit monitoring determine loan defaults in selected commercial banks in the Kumasi metropolis.

4.4.1: Credit Monitoring and the Occurrence of NPL (A*nswering Research Objective three*)

With the help of Likert scale 1-5 (where a mean of 5 indicated strongly agree, 4 agreed, 3 neutral, 2 disagree and 1 indicated strongly disagree), the study tasked the respondents to rate their agreement or disagreement with the factors enumerated in the table.

Table 4.4.1 Descriptive Statistics On Credit Monitoring And The Occurrence Of NPL

Variables	Mean (X)	Std. Deviation
Poorly assessed and advanced loan may perform well if properly monitored	4.2667	.58329
Strict monitoring ensures loan performance	4.0667	.25371
loan follow up is directly related to occurence of nonperforming loans	3.7667	.67891
Banks with higher budget for loan monitoring have lower nonperforming loans	3.5667	1.00630
N	30	

Source: Field Survey, 2015

The Table 4.4.1 explores the credit monitoring and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis. The variables are stated below; banks with higher budget for loan monitoring have lower nonperforming loans (X=3.56, STD=1.00), poorly assessed and advanced loan may perform well if properly monitored (X=4.26, STD=.58), strict monitoring ensures loan performance (X=4.06, STD=.25) and loan follow up is directly related to occurrence of nonperforming loans (X=3.76, STD=.67).

This implies that half of the workers came into agreement that strict monitoring ensures loan performance and poorly assessed and advanced loan may perform well if properly monitored as factors to credit monitoring and the occurrence of NPL of Selected Commercial Banks in Kumasi. Again, the other half of the workers also pointed that loan follow up is directly related to occurrence of nonperforming loans and banks with higher budget for loan monitoring have lower nonperforming loans as their supporting factors for credit monitoring and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis.

4.4.2: Collateral And the Occurrence of NPL

With the help of Likert scale 1-5 (where a mean of 5 indicated strongly agree, 4 agreed, 3 neutral, 2 disagree and 1 indicated strongly disagree), the study tasked the respondents to rate their agreement or disagreement with the factors enumerated in the table.

Table 4.2.4.1 Descriptive Statistics on Collateral And The Occurrence Of NPL

Variables	Mean	Std. Deviation
Most of the time no collateralized loans are defaulted	4.1667	.37905
Collateralizing loans helps to protect loan default	4.0667	1.14269
Collateralized loan perform well	4.0333	.80872
N	30	

Source: Field Survey, 2015

The Table 4.4.2 discloses the collateral and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis. Most of the time no collateralized loans are defaulted (X=4.16, STD=.37) Collateralizing loans helps to protect loan default (X=4.06, STD=1.14) and collateralized loan perform well (X=4.03, STD=.80).

Surprisingly, all the workers are with one accord that most of the time no collateralized loans are defaulted, collateralized loan perform well and collateralizing loans helps to protect loan default are their reasons for collateral and the occurrence of NPL of Selected

Commercial Banks the Kumasi Metropolis.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.0 Introduction

This chapter presents major findings regarding the investigating into factors that determine non-performing loans at the Selected Commercial Banks Ghana namely

Prudential Bank, Ecobank, Barclays Bank, Standard Charted Bank and Zenith Bank. From the data interpreted from the preceding chapter, a conclusion inferred from the major findings and a recommendation to serve as a policy action for the bank.

5.1 Major Findings

5.1.1Background Information

The study found that majority of the workers with 46.7% were relationship managers whilst, 13.3% of them were managers, only 20.0% of the workers were having more than 7 years banking experience. However, 60.0% of the workers were having 3-4 years of experience when it comes to bank credit processes. Surprisingly, all the workers working places were privately owned.

5.1.2 Nonperforming loan

The finding indicated that the high interest rate is the major factor of nonperforming loan factors of Selected Commercial Banks in the Kumasi Metropolis. The remaining factors like; poor monitoring/follows, lenient credit team, rapid loan growth by banks, size of the bank, credit culture/orientation, poor risk assessment and ownership type of bank are also minor factors bordering the nonperformance of the bank.

5.1.3 Credit assessment and the occurrence of NPL

The study revealed that majority of the workers was in support with the credit assessment and the occurrence of NPL. Simply because; know your customers policy bank leads to a high loan quality and good loan under writing ensures loan performance. Subsequently, a few of the workers also confirmed that they support the credit assessment and the occurrence of NPL because, poor risk assessment will lead to high loan quality.

5.1.4 Borrower's orientation and the occurrence of NPL

The study showed that loan price affect loan performance, charging big interest rate leads to loan default, default in some areas is ascribed to the culture of the borrower's and there is a relationship between loan default and borrower's culture, are some of the factors why majority of the workers came into support with borrower's orientation and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis.

However, poorly negotiated credit terms lead to loan nonperformance, loans with interest rate tends to turn to NPL and borrowers default because they don't understand credit terms well are also factors which few of the workers mentioned as the reasons for borrower's orientation and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis.

5.1.5 Credit size and the occurrence of NPL

This declared that few of the workers had the perception that growth in bank size comes growth on NPL and bank great risk appetite is caused for NPL are the reasons for credit size and occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis.

Subsequently, majority of the workers also mentioned some factors as the reasons for credit size and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis. Notably are; loans default rate is directly related to Bank's size, having large number of borrowers cause loan default, compromised integrity in lending leads to loan default, banks who credit growth is rapid experience huge NPL level and aggressive lending leads to large NPL volume / ratio.

5.1.6 Credit monitoring and the occurrence of NPL

The study explored that half of the workers mentioned strict monitoring ensures loan performance and poorly assessed and advanced loan may perform well if properly monitored as factors to credit monitoring and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis.

Again, the other half of the workers also pointed that loan follow up is directly related to occurrence of nonperforming loans and banks with higher budget for loan monitoring have lower nonperforming loans as their supporting factors for credit monitoring and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis.

5.1.7 Collateral and the occurrence of NPL

Surprisingly, all the workers were with one accord that most of the time no collateralized loans are defaulted, collateralized loan perform well and collateralizing loans helps to protect loan default, are their reasons for collateral and the occurrence of NPL of Selected Commercial Banks in the Kumasi Metropolis.

5.2 Conclusion

In sum, Non-performing loans arise as a result of high interest rate of banks, banks great risk appetite, large number of borrowers, poor monitoring/follow up of loans given, the leniency of credit terms, poor risk assessment, and rapidity in growth of loan by banks and poor credit culture/orientation among others.

Respondents viewed credit assessment factors such as bank staff knowing their customers (KYC) policy, creditors knowing that easily admitted borrowers usually default and ensuring good loan underwriting will culminate in loan performance and also avert the occurrence of NPL.

Again, proper monitoring and the use of collateral before the issuance of credit or loans will ensure the prevention of non-performing loan.

5.3 Recommendation

Banks must initiate or if already in place strengthen their credit or loan policy in order to outline rigorous requirements that have to be met by borrowers before the issuance of loans.

Banks must have research department to carry out effective risk assessment in order to give the requisite advice on the issuance of loans to borrowers.

Banks must adequately train staff in charge of credit in loan matters to enhance their credit issuance skills and also give orientation to prospective borrowers on strategic sectors to channel the loan so that its repayment will be fruitful.

Interest or charges on loans must be reduced by banks in order to facilitate repayment by borrowers.

Effective monitoring of borrowers to ascertain the progress of loan given in order to avert the instance of loans becoming non-performing.

Banks need to institute a collateral regime where loans to borrowers would be collateralized in order to have alternative repayment scheme.

5.4 Recommended areas for further studies

In line with the recommendations posited above, the following elements are relevant recommended areas for further study;

Though the study used the a survey method design which blended two research approaches, taking care of possible errors, further study should consider time series data aimed at arriving at bringing out consequential features and indicators of the data.

Furthermore, future studies can either decrease or increase the study scope to measure the dynamisms as such. Alternatively, a comparative study between two or more banks can be embarked on where the researcher will elevate from the current point of exploratory case studies to a more advanced level of general theoretical models, invariances, such as causality or evolution.

Further studies should assess the correlation that exists between macro-economic determinants of non-performing loans and bank's specific determinants of non-performing loans.

In summary, the favorable considerations of these recommended areas of studies will go a long way to help curb the challenge of non-repayment of loans in the Ghanaian banking industry.

REFERENCES

Abrams, R. K. and Taylor, M.W., (2003). ‘*Assessing the Case for United Sector Supervision’*, Working Paper, Risk Management and Insurance International Conference.

Agresti, A. M., P. Baudino & P. Poloni. (2008). The ECB and IMF indicators for the MacroSelected Commercial Banks analysis of the banking sector: a comparison of the two approaches. *ECB Occasional Paper no. 99.*

Anderson R. &S. Sundaresan, (2000). A comparative study of structural models of corporate bond yields: an explanatory investigation. *Journal of Banking and Finance*, 24: 69-255.

Arpa M., I. Giulini, A. Ittner, & F. Pauer.2001. The influence of macroeconomic developments on Austrian banks: *implications for banking supervision.BIS Paper 1: 91-116.*

Babihuga, R., (2007). ‘Macroeconomic and _nancial soundness indicators: An empirical investigation’, *IMF working paper, no.115,*

Babouček, I. and M. Jančar, (2005). Effects of Macroeconomic Shock to the Quality of the Aggregate Loan Portfolio. Czech National Bank, *Working Paper Series, 1:1–62.*

Bagehot, Walter, (1962). *Lombard Street, Homewood*; IL: Richard D. Irwin. Reprint of the 1873 edition.

Barrickman, J.R. (1990). Successful commercial lending from the ground up. *Bottom line, 7(2): 12-14.*

Beckman TN & Bartels R. (1955). *Credits and Collections in Theory and Practice.* 6th edition. New York: McGraw-Hill.

Bercoff, Jose J., Julian di, Giovanni & Franque Grimard, (2002). *Argentinean Banks, Credit Growth and the Tequila Crisis:* A Duration Analysis" (Unpublished).

Berger A. N. and R. De Young. (1997). Problem loans and cost efficiency in commercial banks .*Journal of Banking and Finance*, 21: 849_870.

Bikker, J. A. & H. Hu, (2002). Cyclical patterns in profits, provisioning and lending of banks and procyclicality of the new Basel capital requirements.*BNL Quarterly Review*, 55: 143_75.

Bluhm, Overbeck & Wagner, (2003). *National bank Credit Approval Process and Credit Risk Management.*

Breuer, J.B, 'Problem bank loans, con_icts of interest, and institutions', *Journal of _nancial stability, Vol. 2, 2006, pp. 266-285.*

Brownbrigde, Martin, (1998). The Causes of financial distress in local banks in Africa and implication for Selected Commercial Banks policy, *UNCTAD/OSG/DP/132.*

C. Brown, D.J. Mallet &M.G. Taylor, (1993). *Banks: an Industrial Accounting and Auditing Guide*. Great Britain: Page Bros Ltd.

Cifter, A., Yilmazer, S. & Cifter, E., (2009). Analysis of sectoral credit default cycle dependency with wavelet networks: evidence from Turkey. *Economic Modeling 26, 1382–1388.*

Cole, R. A., Goldberg, L. G., & White, L. J., (2004). Cookie-cutter versus character: The micro structure of small business lending by large and small banks. *Journal of Financial and Quantitative Analysis*, 39(2), 227–251.

Collin-Dufresne, P., and R. Goldstein, (2001). "Do Credit Spreads Reflect Stationary Leverage Ratios?" *Journal of Finance*, Vol. LVI, pp. 1929–1957.

Creswell, J.W., (2007), *Research design: Qualitative, Quantitative and Mixed Method approach*, third edition, U.S: SAGE publication, Inc.

De Lucia, R. & Peters, J. (1998). *Commercial Bank Management.* 4th Edition. Sydney, Country: LBC Information Services.

Demirgüç-Kunt A. & E. Detragiache, (1998). The Determinants of Banking Crises: Evidence from Developed and Developing Countries. *IMF Staff papers, Vol. 45, No. 1.*

Federal Deposit Insurance Corporation, (1997*). History of the eighties, lessons for the future, vol. 1: An examination of the banking crises of the 1980s and early 1990s*.
Washington, DC:
Federal Deposit Insurance Corporation

Fofack, Hippolyte, (2009). Non-performing loans in sub-Saharan Africa: Causal Analysis and Macroeconomic Implications. *World Bank Policy Research Working Paper No. 3769,*
November
Fourie LJ, Falkena HB & Kok WJ. 1998: *The South African Financial System*, 2nd edition. Johannesburg: Thomson Publishing.

Filosa R., (2007). Stress Testing of the Stability of the Italian Banking System: a VAR Approach. *Heterogeneity and Monetary Policy, no. 703, pp. 1–46.*

Fisher I., (1933). The Debt Deflation Theory of Great Depressions. *Econometrics* 1, 337-57.

Fuentes, R., & C. Maquieira, (2003), *Institutional arrangements, credit market development and loan repayment in Chile, School of Business and Economics*, Universidad de Chile.

Gambera M., (2000). *Simple Forecasts of Bank Loan Quality in the Business Cycle. Emerging Issues Series*, Federal Reserve Bank of Chicago.

Geanakoplos, J., (2009). The Leverage Cycle. *Cowles Foundation Discussion Paper No. 1715*.

George G. Kaufman, (2004). Macroeconomic stability, Bank soundness, and Design Optimum Regulatory Structures, *Multinational Finance Journal*, 1/30/04.

González-Hermosillo, B., (1999). Determinants of ex- ante banking system distress: A macro empirical exploration of some recent episodes. *IMF Working Paper*, *33.*

Harris P., (2003): *A banker's view of BEE. Briefing to Business Map Foundation members,* Johannesburg, July 25, 2003.http://www.businessmap.co.za accessed on 2011/03/09

Hoggarth G., S. Sorensen & L. Zicchino., (2005). Stress Tests of UK Banks Using a VAR Approach. *Bank of England Working Paper, no. 282.*

Hu, Jin-Li, Yang Li & Yung-Ho, Chiu., (2006). *Ownership and Non-performing Loans: Evidence from Taiwan's Banks. Developing Economies.*

International Monetary Fund., (2007a). *Initial lessons of the crisis. IMF Staff Paper 09/37.* International Monetary Fund, Washington, DC.

International Monetary Fund., (2006). Spain: *Financial Sector Assessment Program–Technical Note–Stress Testing Methodology and Results,* IMF Country Report No.06/216, (Washington DC: International Monetary Fund).

Jimenez G. & J. Saurina., (2005). Credit Cycles, Credit Risk, and Financial Regulation. *International Journal of Central Banking*, vol. 2, pp 65-98.

Keeton W. & C. S. Morris, (1987). Why Do Banks' Loan Losses Differ? Federal Reserve Bank of Kansas City, *Economic Review*, May, pp. 3-21.

Kent, C., & P. D'Arcy., (2000). Cyclical prudence - credit cycles in Australia, *Bank for International Settlements Working Paper No 1*.

Koch TW & Scott MacDonald S., (2003). *Bank Management*, 5th edition. Ohio: South-Western
Thompson Learning.

Leply W. H., (2003). Bankers, Betas… and the Cs of credit. *The RMA Journal*, 86(4): 62-65.

Marcucci J. & M. Quagliariello., (2008). Is Bank Portfolio Risk Procyclical? Evidence from Italy Using a Vector Auto regression. *Journal of International Financial Markets, Institutions and Money*, vol. 18, pp. 46-63.

M. Quagliariello, (2007). "Banks' riskiness over the business cycle: a panel analysis on Italian intermediaries," *Applied Financial Economics, Taylor and Francis Journals*, vol. 17(2), pages 119-138.

Mueller, C., (2000). *A simple multi-factor model of corporate bond prices, Doctoral Dissertation*, University of Wisconsin-Madison.

Murphey L. B., (2004a). Focusing on the Fundamentals (Again). *The RMA Journal*, 86(8): 18- 19.

Nathenson J. L., (2004). A Primer on Deals for Middle-Market Bankers. *The RMA Journal*, 86(8): 46-54.

NBE, (2008). Asset classification and Provisioning Directive No. SBB/43/2008.*National Bank of Ethiopia*, Addis Ababa Ethiopia

Ning Guo, Causes and Solutions of non-performing Loans in Chinese Commercial Banks, *Chinese Business Review, ISSN1537-1506, Vol. 6, No, 6, 2007*.

Norton, J., & Andenans, M., (1988). *Emerging Financial Markets and Secured Transactions*, Kluwer Law International, London.

Office of the Comptroller of the Currency, (1988). *Bank failure: An evaluation of the factors contributing to the failure of national banks.* Washington, DC: Office of the Comptroller of the Currency.

Pain D., (2003). The Provisioning Experience of the Major UK banks: A Small Panel Investigation. *Bank of England Working Paper, no. 177.*

Patersson, Jessica & Isac Wadman, (2004). *Non- Performing Loans-The markets of Italy and Sweden, Uppsala University thesis, Department of Business Studies.*

Radha, M & SV. Vasudevan, (1980). *A Text Book of Banking: Law, Practice and Theory of banking,* S, Chand &Co. Ltd: New Delhi.

Rajan, R. G., (1994). Why bank credit policies fluctuate: A theory and some evidence. *Quarterly Journal of Economics, 109(2), 399–441.*

Rajan, Rajiv & Sarat C. Dhal, (2003). Non-performing Loans and Terms of Credit of Public Sector Banks in India: An Empirical Assessment. *Occasional Papers, 24:3, pp. 81-121, Reserve Bank of India.*

Reed EW, Cotter RV, Gill EK & Smith R. K., (1976). *Commercial Banking*, 1st edition. New Jersey: Prentice-Hall.

Rose P. S., (2002). *Commercial Bank Management,* 5 th edition. New York: McGrawHill/Irwin.

Ross, Westerfield & Jaffe, (1999). *Corporate Finance.* 5 th edition. Irwin/McGraw-Hill.

Salas, Vincente & Jesus Saurina, (2002). Credit Risk in Two Institutional Regimes: Spanish Commercial and Savings Banks. *Journal of Financial Services Research, 22:3, pp. 203-224.*

Saunders A & Cornett M. M., (2003). *Financial Institution Management*, 4 th edition. New York: McGraw-Hill/Irwin.

Shofiqul Islam, Mohammed, Nikhil Shil & Mannan Abdul, (2011). *Non-performing Loans: Its causes, consequence and some learning*, *American International University*, Bangladesh, East West University, Stamford University.

Sinkey J. F. (2002). *Commercial Bank Financial Management in the Financial-Services Industry*, 6 th edition. New Jersey: Prentice Hall.

Sinkey, J. F. and Greenawlat, M.B., (1991). 'Loan-Loss Experience and Risk-taking Behaviour at Large Commercial Banks', *Journal of Finan- cial Services Research, Vol. 5, no. 1, pp. 43-59.*

Sonali Abeyratne, (2001). .*Banking and Debt Recovery in Emerging Markets*: *The law reform Context*, England: Dartmouth publishing Company.

V. Salas and J. Saurina, (2000). "Credit risk in two institutional regimes: Spanish commercial and savings banks", *Journal of Financial Services Research, Volume 22, Number 3, 203-224, 2002.*

Valdez S., (2000)*: An Introduction to Global Financial Markets,* 3rd edition. London: Macmillan Press Ltd.

Walter, N. and Werlang, S. (1995). Inflationary Bias and State-owned Financial Institutions. *Journal of Development Economics*, 47, 135-54

Waweru, N.M. & Kalani, V. M. (2009). Commercial banking crises in Kenya: causes and remedies, *African Journal of Accounting, Economic Economics, Finance and banking research, 4(4): 12-32*

Weinberg, J. A., (1995). Cycles in lending standards? Economic Quarterly, *Federal Reserve Bank of Richmond, 81(3), 1–18.*

Wei-Shong ,Lin Peter, Mei Albert Kuo-Chung. 2006 The internal performance measures of bank lending: a value-added approach, Benchmarking: *An International Journal, 13(3).272 - 289*

APPENDIX

QUESTIONNAIRES

This questionnaire is intended to solicit for information that will enable the researcher to investigate into factors that determine non-performing loans at Selected Commercial Banks Ghana. The exercise is for academic purpose only in partial fulfillment for the degree of Masters of business administration with option in finance. Whatever information you give will be kept confidential. (Please tick appropriate boxes)

SECTION ONE – BACKGROUND INFORMATION 1. Your current position in the Banking industry

a. Loan Officer
b. Relationship manager
c. Credit analyst
d. Recovery/ monitoring officer
e. Credit Officer
f. Manager
g. Other, please specify ______________________

2. Indicate your experience in the banking industry

a. 1-2years
b. 3-4years
c. 5-6years
d. Above 7years

3. Indicate your experience in bank credit processes

a. 1-2years
b. 3-4years
c. 5-6years
d. Above 7years

4. Indicate ownership of the Bank you work for

a. Private
b. State owned

5. Determinants of nonperforming loans are obvious.

a. Agree
b. Neutral
c. Disagree

SECTION TWO – DETERMINANTS OF NON PERFORMING LOANS 6. What bank specific factors do you think are causing the occurrence of Nonperforming loans at Selected Commercial Banks

7. Please rank the factors that cause occurrence of nonperforming loans in your Bank. N.B Rank the factors in order of their importance in contributing to the occurrence of nonperforming loans from 1-8

Nonperforming Loan Factors	**Rank 1=highest ……8=lowest**
Rapid Loan growth by banks	
High interest rate	
Lenient credit terms	
Credit culture / Orientation	
Size of the Bank	
Poor monitoring/follow	
Ownership type of bank	
Poor risk assessment	
Others, Please specify_	

Please indicate your degree of agreement or disagreement to the statements pertaining to credit assessment and the occurrence of NPL. Please use the following 5 point likert scale to answer the questions where 1. Strongly Agree 2. Agree 3. Neutral 4. Disagree 5. Strongly Disagree

8. Easily admitted borrowers usually default	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
9. Know Your Customer (KYC) policy of banks lead to high loans quality	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
10. Good loan underwriting ensures loan performance	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
11. Poor risk assessment would lead to loan default	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**

Please indicate your degree of agreement or disagreement to the statements pertaining to credit monitoring and the occurrence of NPL. Please use the following 5 point likert scale to answer the questions where 1. Strongly Agree
2. Agree 3. Neutral 4. Disagree 5. Strongly Disagree

11 Strict monitoring ensures loan performance	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
12 Poorly assessed and advanced loans may perform well if properly monitored	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
13 Loan follow up is directly related to occurrence of nonperforming loans	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
14 Banks with higher budget for loan monitoring have lower non performing loans	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**

Please indicate your degree of agreement or disagreement to the statements pertaining to Collateral and the occurrence of NPL. Please use the following 5 point likert scale to answer the questions where 1. Strongly Agree
2. Agree 3. Neutral 4. Disagree 5. Strongly Disagree

15 Collateralized loans perform well	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
16 Collateralizing loans help protect loan default	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
17 Most of the time non collateralized loans are Defaulted	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**

Please indicate your degree of agreement or disagreement to the statements pertaining to borrower's orientation and the occurrence of NPL

18 Borrower's orientation/culture is related to loan performance	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
19 There is a relationship between loan default and borrower's culture	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
20 Default in some area is ascribed to the culture of the borrowers	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
21 Society's cultural development leads to good loan performance	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
22 Loans with big interest rate tend to turn to NPL	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
23 Charging big interest rate leads to loan default	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
24 Loan price affects loan performance	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
25 Lenient / lax credit term cause loan default	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
26 Borrowers default because they don't understand credit terms well	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**

27 Poorly negotiated credit terms lead to loan non performance	**(1) (2) (3) (4) (5)**

Please indicate your degree of agreement or disagreement to the statements pertaining to Credit size and the occurrence of NPL

28 Aggressive lending leads to large NPL volume/ratio	**(1) (2) (3) (4) (5)**
29 Banks whose credit growth is rapid experience huge NPL level	**(1) (2) (3) (4) (5)**
30 Bank's great risk appetite is cause for NPL	**(1) (2) (3) (4) (5)**
31 Compromised integrity in lending leads to loan default	**(1) (2) (3) (4) (5)**
32 Having large number of borrowers causes loan default	**(1) (2) (3) (4) (5)**
33 Loans default rate is directly related to banks' Size	**(1) (2) (3) (4) (5)**
34 With growth in banks size comes growth on NPL	**(1) (2) (3) (4) (5)**
35 Loan default is not related banks ownership type (private/state owned	**(1) (2) (3) (4) (5)**

36. If you have further comments on the bank specific factors affecting nonperforming loans of your bank please use the space below

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

End of the questionnaire

Thank you for your participation