An Assessment of Credit Management Practices at Agricultural Development Bank (ADB) Branches in the Eastern Region of Ghana

By

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DECLARATION

I hereby declare that this submission is my own work towards the Commonwealth Executive Masters in Business Administration and that, to the best of my knowledge, it contains no material previously published by another person nor material which has been accepted for the award of any other degree of the university except where due acknowledgement has been made in the text.

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ABSTRACT

This study assessed credit management practices at ABD branches in the Eastern region of Ghana. This was carried out by analysing the process of accessing credits; credits control processes and credits collection strategies. This was done against the background that there was huge debts as a result of nonperforming loans affecting the financial status of the bank. The descriptive survey method was used for the study. Sample size of 81 members of staff was drawn from the 101 staff in all the six ADB braches in the Eastern region of Ghana. The cluster sampling method taking into consideration each branch as a cluster was used to identify individual sample units for the study.

Two main sources of data were used for the study namely the primary and secondary sources. Questionnaires were used as the main instrument to collect the primary data on access to credit, credit control processes and credit collection strategies.

Among the major findings of the study are; the main factors influencing access to credit are the stringent policy guidelines as well as the credit worthiness of the customers. A major credit control process was the process of ensuring compliance of internal guidelines. A major recommendation of the study was the need to adopt flexible policy which can improve access to credit.

DEDICATION

I sincerely dedicate this work to my entire family, especially my wife Emelia Ahiable (Mrs.) and my lovely children Theophilus Kwaku Ahiable and Jennifer Aku Ahiable who have given me the support, encouragement and permitted my long absence from home most of the time to enable me prepare this work.

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TABLE OF CONTENTS

CONTENT **PAGE**

LIST OF TABLES

KNUST

CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND OF THE STUDY

How long does it take business partners to pay their debts? Understanding the payment behavior of potential customers is vital in assessing credit management in every organization, since poor credit assessment can lead to major problems in financial planning (Atradius 2012).

According to Atradius (2011), payment delays and payment defaults continue to be major issues around the world. The study further found that as high as 30% of debts are paid late while 3% defaulted on and the primary reason for these is that the buyers have insufficient funds to pay.

Problems with loans are normally identified at the end of the credit channel (Katoh 2004). Before a loan becomes bad, it needs to be granted; moreover the poor quality of a loan is sometimes due to factors not attributable to the lending process such as adverse selection and moral hazards (Satiglitz and Weiss 1981) or any other external shock that may alter the borrower's ability to repay the loan (Minsky 1985).

Nevertheless, there are cases where the ways banks grant and monitor credits can be responsible for the bad loan portfolio. In other terms weak credit risk management systems can also be sources of problem loans (Nishinura 2001).

Credit Management processes can be summarised into three stages namely:

- Credit initiation
- Documentation and disbursement
- Credit administration.

In terms of credit initiation it is a process that starts from a market analysis and ends at the credit application approval (Katoh, 2004).

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

For most banks, loans are the largest and most obvious source of credit risk, however other sources of credit risk exist throughout the activities of a bank, including in the banking book and in the trading book and both on and off the balance sheet. Banks are increasingly facing credit risks in various financial instruments other than loans including acceptance, inter-bank transactions, trade financing, foreign exchange transactions, financial features, swaps, bonds, entities, options and in the extension of commitments and guarantees, and the settlements of transactions. (The Basel Committee 2011)

Since exposure to credit risks continues to be the leading source of problem in the bank worldwide, banks and their supervisors should be able to draw useful lessons from past experience. Banks should now have a keen awareness of the need to identify, measure, monitor and control risk as well as to determine that they hold adequate capital against these risks and that they are adequately compensated for risks incurred. (The Basel Committee 2011)

The Basel committee 2011 report on sound practices in risk management suggests the following:

i. Establishing an appropriate credit risk environment
ii. Operating under a sound credit granting process
iii. Maintaining an appropriate credit administration, measurement and monitoring processes and
iv. Ensuring adequate control over credit risk

1.2 STATEMENT OF THE PROBLEM

Credit risk continuous to remain the largest source of risk for Agricultural Development Bank (A.D.B) in Ghana, in general and specifically for the branches in Eastern Region (ADB Quarterly Report, 2010, and Annual Report & Financial Statement, 2011). For instance, according to the ADB Annual Report and Financial Statement (2011), the gross non-performing loan ratios for all ADB branches in Ghana in 2008 was 22.95 percent, this figure increased in 2009 to 23.63 percent. There was a slight fall 5.7 percent in 2010. This signifies that, most of the ADB profits are eroded annually due to the high risk associated with credit management practices. The details are presented in table 1.1 below

Table 1.1 Non-performing Loans at ADB

Year	Gross Non-Performing Loans Ratio in percentage (%)
2006	35.99
2007	30.99
2008	22.96
2009	23.63
2010	17.93

Source: Annual Report & Financial Statement, 2006-2010

The situation in Eastern Region is not different from the national problem. For instance, ADB Eastern Regional Annual Report (2010) indicated that, as at the end of the year, as high as 11.67 percent of the loans grated were declared irrecoverable.

Absence of effective management of such risk has resulted in significant losses to the institution. The consequences of such losses not only disrupt the intermediation functions of the institution but also impose large financial burden and profitability of the bank as shown in table 1.2.

Table 1.2 Impact of Bad Debt on Profit

Year	Operating Profit Before charge for Bad Debt	Charge for Bad Debt	Operating Profit after charge for Bad Debt	Ratio of Bad Debt to Operating Profit
2006	20,529,100.00	7,965,600.00	12,563,500.00	**38.80**
2007	13,141,345.00	7,336,574.00	5,804,771.00	**55.83**
2008	21,858,036.00	6,344,820.00	15,513,216.00	**29.03**
2009	29,230,579.00	15,696,800.00	13,533,779.00	**53.70**
2010	60,547,281.00	25,584,015.00	34,963,266.00	**42.25**
TOTAL	**145,306,341.00**	**62,927,809.00**	**82,378,532.00**	**43.31**

Source: ADB Annual Reports & Financial Statements, 2006-2010

Effective credit management is therefore vital to ensure that banks credit activities are conducted in a prudent manner and the risk of potential bank failures reduced.

This study therefore assesses the credit management processes in A.D.B Branches in Eastern Region and prescribes the best practices to ensure prudent conduct in the operations of the banks' credit granting activities.

1.3 OBJECTIVES OF THE STUDY

The general objective of the study is to explore how credits are managed in ADB branches in Eastern Region.

The specific objectives are to:

1. Determine the factors that influence access to credit in ADB branches in Eastern Region
2. Determine the credit control processes in ADB branches in Eastern Region.
3. Analyse the credit collection strategies in ADB branches in Eastern Region

1.4 RESEARCH QUESTIONS

1. What are the major factors influencing access to credit in ADB branches in Eastern Region?
2. What credit control processes are adapted in the management of credit in ADB branches in Eastern Region?
3. What credit collection strategies are adopted in the management of credit in ADB branches in Eastern Region?

1.5 SIGNIFICANCE OF THE STUDY

This study is significant because it deals with issues banks are facing and will continue to confront them in the future. According to the International Monetary Fund (IMF), the average level of Non-Performing Loans (NPLs) in Ghana is around 25% of the total loans. The IMF also highlighted that the definition of a non-performing loan in Ghana and the associated provisioning modalities were rather slack compared with other countries'. This signifies that NPLs have been a major problem to ADB in the study area. This study which seeks to address the problems associated with credit management would be part of the baseline data needed for effective planning and management of credit in the bank.

There is a high rate of NPLs in ADB in the study area and in Ghana general. This study would be of importance in that; it could serve as a reference material with documented best practices in reducing the incidence of NPLs.

This study is also found to be important because effective credit management lessens the burden on the Bank of Ghana in meeting its role of recapitalising the bank. This problem has been necessitated by the high rate of NPLs which has eventually reduced the liquidity of the bank, hence the need to fall on other sources for assistance.

1.6 LIMITATION OF THE STUDY

A major limitation of the study was the difficulty in getting information on NPLs in the bank. Even though the researcher sent introductory letter to management of the bank to grant him access for the study, management was skeptical in providing information on NPLs due to ethical reasons.

Another limitation of the study was the unwillingness of management to disclose the credit management processes as well as the best practices in credit management. Management was reluctant because it considered such processes and practices as trade secrets which should not be in the public domain for its competitors to take advantage of.

1.7 THE SCOPE OF THE STUDY

The study is limited to only credit management practices in ADB branches in Eastern Region. Other core functions of the bank are not considered for the study.

1.8 ORGANIZATION OF THE STUDY

This study was organized into five chapters. Chapter one which is the introduction considered the following sub-themes: Background of the study, Statement of the problem, Objectives of the problem, Research questions, Significance of the study, Limitation and scope of the study, The Scope of the Study.

The second chapter considered the review of literature while the third chapter also considered the methods used for the study.

Chapters four and five were devoted for data presentation and analysis as well as recommendations and conclusions of the study respectively.

CHAPTER TWO

REVIEW OF LITERATURE

2.0 INTRODUCTION

This chapter covers the review of literature on, definitions and concepts of credit management, types of credit and loan, functions of credit, causes of increasing debt, credit management practices and debt recovery strategies.

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2.1 DEFINITIONS, TYPES AND FUNCTIONS OF CREDIT

Credit, in commerce and finance, is a term used to denote transactions involving the transfer of money or other property on promise of repayment, usually at a fixed future date. The transferor thereby becomes a creditor, and the transferee, a debtor; hence credit and debt are simply terms describing the same operation viewed from opposite standpoints (Donald L. 2008).

The principal classes of credit are as follows (Donald L., 2009. and Redmond, W.A, 2008):

i. Mercantile or commercial credit, which merchants extend to one another to finance production and distribution of goods;
ii. Investment credit, used by business firms to finance the acquisition of plant and equipment and represented by corporate bonds, long-term notes, and other proofs of indebtedness;
iii. Bank credit, consisting of deposits, loans, and discounts of depository institutions;

iv. Consumer or personal credit, which comprises advances made to individuals to enable them to meet expenses or to purchase, on a deferred-payment basis, goods or service for personal consumption

v. Real-estate credit, composed of loans secured by land and buildings

vi. Public or government credit, represented by the bond issues of national, state, and municipal governments; and

vii. International credit, which is extended to particular governments by other governments, by the nationals of foreign countries, or by international banking institutions, such as the International Bank for Reconstruction and Development.

The principal function of credit is to transfer property from those who own it to those who wish to use it, as in the granting of loans by banks to individuals and corporate bodies who plan to initiate or expand their business ventures. The transfer is temporary and is made for a price, known as interest, which varies with the risk involved and also with the demand for, and supply of, credit, (Stiglitz and Weiss, 1981).

Credit transactions have been indispensable to the economic development of the modern world. Credit puts to use property that would otherwise lie idle, thus enabling the world to fully utilise its resources. One of the most significant differences between some nations of Africa, Asia, and South America and the advanced Western nations is the extent to which the use of credit permits the latter to keep their savings continuously at work. The presence of credit institutions rests on the readiness of people to trust one another and of courts to enforce business contracts. The lack of adequate credit facilities make it natural and necessary for inhabitants of developing countries to hoard their savings instead of putting them to productive and profitable use.

Without credit, the tremendous investments required for the development of the large-scale enterprise on which the high living standards of the West are based would have been impossible.

The use of credit also makes feasible the performance of the complex operations involved in modern business without the constant handling of money. Credit operations are carried out by means of documents known as credit instruments, which include bills of exchange, money orders, checks, drafts, promissory notes, and bonds. These instruments are usually negotiable; they may legally be transferred in the same way as money. When the party issuing the instrument desires to prevent its use by anyone other than the party to whom it is issued, he or she may do so by inscribing the words “not negotiable” on the instrument.

2.2 DEFINITION AND CONCEPTS OF CREDIT MANAGEMENT

Credit management is the process for controlling and collecting payments from your customers (Small business, 2011).

It is a term used to identify accounting functions usually conducted under the umbrella of Accounts Receivables (Wise-geek, 2010). Essentially, this collection of processes involves qualifying the extension of credit to a customer, monitors the reception and logging of payments on outstanding invoices, the initiation of collection procedures, and the resolution of disputes or queries regarding charges on a customer invoice. When functioning efficiently, credit management serves as an excellent way for the business to remain financially stable.

The process of credit management begins with accurately assessing the credit - worthiness of the customer base. This is particularly important if the company chooses to extend some type of credit line or revolving credit to certain customers. Proper credit management calls for setting specific criteria that a customer must meet before receiving this type of credit arrangement. As part of the evaluation process, credit management also calls for determining the total credit line that will be extended to a given customer.

According to Jabatan (2001) several factors are used as part of the credit management process to evaluate and qualify a customer for the receipt of some form of commercial credit. These factors include;

- Gathering data on the potential customer's current financial condition, including the current credit score.
- The current ratio between income and outstanding financial obligations will also be taken into consideration.
- Competent credit management seeks to not only protect the vendor from possible losses, but also protect the customer from creating more debt obligations that cannot be settled in a timely manner.

A good credit management system helps to reduce the amount of capital tied up with debtors (people who owe money) and minimise the exposure to bad debts. Good credit management is vital to your cash flow.

After establishing the credit limit for a customer, credit management focuses on providing the client with accurate and timely statements or invoices. The invoices must be delivered to the customer in a reasonable amount of time before the due date, thus providing the customer with a reasonable period to comply with the purchase terms.

When the process of credit management functions efficiently, everyone involved benefits from the effort. The vendor has a reasonable amount of assurance that invoices issued to a client will be paid within terms, or that regular minimum payments will be received on credit account balances. Customers have the opportunity to build a strong rapport with the vendor and thus create a solid credit (Bank Negara Malaysia, 2001).

2.3 CREDIT MANAGEMENT PROCESS

Problem loans are at the end of the credit channel. Before a loan becomes bad, it needs to be granted. Moreover, as we referred to so far, the poor quality of a loan is sometimes due to factors not attributable to the lending bank such as adverse selection and moral hazard (Stiglitz and Weiss (1981) or any other external shock that may alter the borrower's ability to repay the loan (Minsky, 1982 & 1985). Nevertheless, there are cases where the way banks grant and monitor credits can be responsible for the bad loan portfolio. In other terms, weak credit risk management systems can also be sources of problem loans (Nishimura and al, 2001).

For these last reasons, it was essential to overview the credit risk management process of Banks in order to capture the framework of the bad loans management.

Significant details related to the credit management processes are revealed here. Banks' credit management processes can be summarised in three main stages. These stages are:

i. Credit initiation

ii. Documentation and disbursement

iii. Credit administration

2.3.1 CREDIT INITIATION

The credit initiation is a process that starts from a market analysis and ends at the credit application approval. The steps involved in credit initiation processes are listed below:

- **Surveys and industry studies**: Relationship Officers scan the market and economic sectors to identify key players and potential business for the Bank. In the same vein, industries with high potential of growth that can be good business for the Bank are also listed.
- **Risk Asset Acceptance Criteria (RAAC)**: for each industry, criteria are designed to guide the relation with both industry and clients in order to limit the level of exposure at credit risk. Risk Asset Acceptance Criteria applied to industries include both quantitative and qualitative information such as net sales, net profit, years of experience in the business and the quality of corporate governance.
- **Prospect lists**: some prospects (companies and individual customers) identified as the main role players are short listed in accordance with the industry studies and the minimum risk criteria. This prospect list is ranked in order of preference.
- **Customer solicitation**: at that stage, although the primary source of target is the prospect list, the initiation of a credit comes either at the bank request in the frequent contact with existing customers or at the clients request if they have a need for financing.
- **Negotiation**: the relationship officer identifies the financing needs of the borrower and gathers background information such as the latest financial statements, project details, projections over the loan life. This information will allow the officer to check whether the risk is bearable by the Bank and its compliance with the bank's targets.

- **Presentation**: the conformity of information given with the market and industry analysis is the reliability of the information once again verified by consulting other sources. A draft of the credit application (CA) is prepared in conformity with the GCPPM and I consideration of the market and industry analysis by the account officer based on information collected.
- **Credit committee approval**: a copy of that CA is submitted to each member of the credit committee. The members review and approve submission of the final CA.
- **Control and reporting requirements**: the final CA package is submitted to the credit committee with highlights on the credit exposures of the bank.
- **Advice to customers**: once the credit is approved, the customer is advised in writing with details concerning the terms and conditions and with the statement that the credit can be subject to review, modification or cancellation at the Bank option.

2.3.2 DOCUMENTATION AND DISBURSEMENT

The documentation and disbursement refers to the compliance of documents provided with the law applicable and the requirements of the Bank's legal department. Documentation provided must satisfy the Bank's legal department and afford maximum protection to the Bank. The documentation is periodically reviewed to keep them in fine with ever-changing legal systems and practices.

The Legal department is consulted before making any compromises with the customer. Any amendments are done in consultancy with the legal department.

Once the credit application satisfies all these conditions, a thorough analysis is done and if the application complies with the Bank's conditions, instruction is given to the Credit administration for disbursement.

2.3.3 CREDIT ADMINISTRATION

The credit administration refers to the credit support, control systems and other practices necessary for the effective monitoring of credit risks taken by the Bank. Some of the important points of the credit administration are:

- Control of Credit files.
- Safekeeping of credit and documentation files.
- Follow-ups for expirations of essential documents like CA's and insurance.
- Control of credits and excesses over approved lines.
- Monitoring of collateral inspections, site visits and customer calls.
- Monitoring of repayments under term credits.
- Reporting: the portfolio is periodically reviewed to make sure that the names tiered are still complying with the risk acceptance criteria.

2.4 CREDIT MANAGEMENT PRACTICES

Credit risk continues to remain the largest source of risk for banking institutions in the world (Credit Bank Negara Malaysia, 2001). Effective credit management is therefore vital to ensure that a banking institution's credit activities are conducted in a prudent manner and the risk of potential bank failures reduced. The success of banks (in the view of the researcher) hinges on their ability to manage their credit effectively. Even though there are no strictly laid down credit management practices, most financial institutions practise the following in order to maximise profit as well as to reduce credit risk.

2.4.1 LENDING

Lending is one of the core pillars of financial intermediation and for that matter a significant activity in the operations of banks. It is at the same time highly risky. This is asserted by McNaughton (1992), who emphasised that risk taking is central to banking and banks are successful when the risk they take are reasonably controlled and within their financial reserves and credit competence. McNaughton was also of the view that to survive the numerous lending risks and to prosper, bankers must re-examine their bureaucratic tendencies in order to become responsible to the financial needs of the economy. The bureaucratic tendencies could thus cause lots of frustrations for loan applicants to obtain credit at the right time, which may hamper the success of projects.

In the area of credit delivery, Rouse (1989) has asserted that a lender 'lends' money and does not give it away. The lender needs to look into the future and asks; will the customer repay by the agreed date? Rouse contends that, there will always be some risk that the customer will be unable to repay, and it is in assessing this risk that the lender needs to demonstrate both skill and judgment. Lending is perceived as an art because it involves imagination and creativity (Rouse, 1989). It could be contended that credit management prescribes the guidelines to be followed and their religious adherence is very crucial for good credit management practices. The appropriate judgment depends on the skills, knowledge and foresight of the manager. This should embrace skills and knowledge in financial analysis, the performance of the sector receiving credit, the overall macroeconomic condition, the psychology in determining the perceived and indirect intentions of the borrower, the type of soil and climatic pattern in terms of agricultural loans and the perceived impact of the credit on the performance of the lending institution. In this vein, lending operations encompass various disciplines of economics, finance, law, accounting, geography, science, psychology, and culture among others. The situation makes lending activity very challenging since substantial significant slip causes undesirable financial losses and for that matter threatens the very existence of the lending institution. In this respect, persons with the right attitude, knowledge and skills devoid of all egoistic sentiments, are needed to superintend lending activities.

Olashore (1988) has identified four interested parties in bank lending and these are the depositor, the borrower, the lending bank and government. Whilst the depositor wants the highest possible interest on his deposits, the borrower cherishes lowest interest rate on lending; the bank wants the highest spread between lending and borrowing rates of interest, and the government places emphasis on the responsiveness of lending to the sectorial needs of the economy. In spite of these interest groups, the lending bank ensures that its interest supersedes that of the others. In a liberalised and deregulated economy, banks dictate both borrowing and lending interest rates and determine the direction of credit to sectors which are considered less risky and more profitable. Furthermore, in spite of agriculture being the mainstay of the Ghanaian economy, institutional credit to this sector has been low recording shares in total credit by banks of 9.2 percent, 9.2 percent and 7.6 percent respectively as at end December 2002, 2003 and 2004 (Bank of Ghana, 2004).

2.4.2 COST OF BORROWING (INTEREST RATE)

Stiglitz (1987) asserted that interest rates on lending would be higher if the probability of default is higher. In this regard ventures with high risk of success attract higher interest rates. For example lending to agriculture considered highly risky attracts higher interest rate than lending to commerce, which stood at 30.0 percent and 28.5 per cent respectively as at the end of December 2005 (Bank of Ghana, 2005). However, this situation rather tends to aggravate the risk of default, since the higher interest rates increase the cost of production, which may affect the expected patronage of the products concerned. This may be the reason why subsidies are provided to sustain production of basic essentials like agricultural products in some developed countries.

The level of lending interest rates is also influenced by the availability of loanable funds and the competing ends. In situations where Government needs to borrow substantially to support its business, high interest rates are offered to crowd out the private sector. This was the situation in 2000 where the Treasury bill rate reached a peak of 45.0 per cent per annum (Bank of Ghana, 2000). The level of inflation also affects interest rate since a higher regime bears direct relationship with interest rates. This view was advocated by Cox (1988), when he indicated that, interest rates were influenced by supply and demand for funds, risk premium, inflationary factors and amount of loan.

Before the liberalisation of the economy in 1990, the Bank of Ghana regulated interest rates. During the pre-liberalisation period, interest rates were fixed by the Bank of Ghana for the various sectors for which the banks were to comply. However, this system was abolished and banks were to determine their own interest rates according to the market forces and the dictates of the macroeconomic conditions. The Bank Rate of the Bank of Ghana seemingly becomes the benchmark but it takes time for the banks to adjust appropriately to it especially when there is downward revision of the rate.

2.4.3 ASSESSMENT OF BORROWERS CREDIT WORTHINESS

The assessment of the credit worthiness involves the gathering, processing and analysing of information on the loan applicant. An important aspect of information is by way of credit references and credit rating. Ghana is yet to have credit rating agencies, which will provide opinion on the credit standing of businesses in the system. The existence of such an agency would facilitate the credit decision process of banks.

According to Rose (1999) the question that must be dealt with before any other is whether or not the customer can service the loan – that is, pay out the credit when due, with a comfortable margin of interest. The factors underlying the assessment of pre-lending safeguards, in the opinion of Rose (1999) are; character, capacity, cash, collateral, conditions and control (i.e. the 6Cs). In another context, Rouse (1989) referred to mnemonics used as common checklist to review loan application as: CCCPPARTS (Character, Capital, Capability, Purpose, Person, Amount, Repayment, Terms and Security); PARSER (Person, Amount, Repayment, Security, Expediency, Remuneration); CAMPARI (Character, Ability, Margin, Purpose, Amount, Repayment, Insurance/Security).

The variation in the mnemonics relates to the basic principle of assessing the potential of having loans repaid. The dimension of each of the factors outlined by Rose (ibid) is as follows:

Character: Customer's past payment records; experience of other lenders with the customer; purpose of loan; customer's track record in forecasting business or personal income and credit rating.

Capacity: identity of customer and guarantors, description of history, legal structure owners, nature of operations, products and principal customers, suppliers for a business borrower and management quality.

Cash: take-home pay for an individual, the past earnings, dividends, and a less record for a business firm, adequacy of past and projected cash flow; availability of liquid reserves, turnover of payables, accounts receivable, and inventory; capital structure and leverage and expense controls.

Collateral: ownership of assets; vulnerability of assets to obsolescence and liquidation value of assets.

Conditions: Customer's current position in industry and expected market share; competitive climate for customer's products; sensitivity of customer and industry to business cycles and changes in technology.

Control: applicable banking laws and regulations regarding the character and quality of acceptable loans; adequate documentation for examiners who may review the loan.

Security: Securities for loans and overdrafts are to ensure recovery of the funds lent to the borrower in the event that the borrower becomes unwilling or incapable of meeting his commitments.

Dunkman (1996) outlined reasons for security as: safeguarding against some doubts about borrowers' repayment ability, basis for increasing amount of loans over and above existing facilities, and as a last resort to recover loan in the face of default. Agyeman (1987) expressed the view that even though security is necessary, its requirement by bankers must be adopted cautiously otherwise it is capable of being counterproductive. According to him, this can come about when bankable projects are funded solely because of availability of security. Stiglitz (1996) buttressed Agyeman's (1987) view that security has the unintended tendency for causing skewness of loans in favour of property owners. The researcher shares the view that if security becomes dominant factor in credit decision, bankable projects, which lack securities as support, may be starved of credit while those with adequate security support but not financially viable may rather have access to credit. This then serves as draw back in using financial intermediation as focus for meaningful economic development and growth. Banks are often confronted by instituting legal action against loan defaulters to take possession of assets pledged as collateral for foreclosure.

Akakpo (1994) suggested that the view that security should always be the last consideration in any loan proposition and one should not lend purely because security is offered. Any loan proposition should stand on its own with the security only providing a cushion should things go wrong.

Rouse (1989) however, held the view that no advances should be made until security procedures have been completed or at least at a stage where completion can take place without the need to involve the borrower any further. This suggests that the provision of adequate perfected security should be paramount in taking a credit decision. The rigidity in total secured collateral before disbursement of credit facilities needs to be relaxed in order not to delay the financing, which invariably impedes the success of projects.

It should be also noted that the provision of security just provides secondary source of repayment and therefore to ensure sustained relations with customers in their business endeavours, it is pertinent to consider the viability of the project being financed to generate sufficient cash flows to liquidate the credit facility. Furthermore the foreclosure of immovable property pledged as security goes through a long legal tussle, which could not easily bring prompt liquidity relief to a bank. It is therefore very essential for banks to lay much premium on the viability of a project as a paramount consideration for lending financial support.

2.4.4 REGULATORY CONTROLS OF CREDIT

One of the basic objectives of banking supervision is to protect depositors' interest, the source of the bulk of working funds for banks. The existence of good quality loan asset portfolio of a bank provides guarantee for safety of deposits.

Section 2(1) of the Banking Act, 2004 (Act 673) empowers the Bank of Ghana to have an overall supervisory and regulatory authority in all matters relating to banking business and be also responsible for promoting an effective banking among others. To this end, Act 673 provides restrictions to regulate lending and investment activities and some of the specific provisions include:

i. prohibition for a bank to grant credit facilities against the security of its own shares and those of its related parties;
ii. limit unsecured exposure and secured exposure to one person or group of persons to not more than 10.0 per cent and 25.0 per cent of a bank's net own funds respectively;

iii. a bank shall not take unsecured financial exposure in respect of any of its directors or significant shareholders and related parties;

iv. the board of the bank shall be the only authority to approve or sanction any financial exposures of the bank to any of its directors or significant shareholders or related parties;

v. the financial exposure of a bank shall not be written-off or waived fully or partially, without the sanction of the bank's board and the prior approval in writing of the Bank of Ghana; and

vi. a bank shall not grant to any of its officers and employees any unsecured advances or credit facilities, the aggregate amount of which exceeds two years' salary of the officer or employee.

The above-entrenched provisions of the law are to ensure that risk posed by financial exposures to customers and related parties are regulated and minimised and to make sure the bank's credit is well managed. The Bank of Ghana enforces these provisions through its off-site surveillance and on-site examination systems.

The researcher considers the legal provisions appropriate in controlling credit risk and also instilling sanity into writing-off non performing facilities. Another controlling tool of the Bank of Ghana in regulating the quantum of credit to the public is the maintenance of liquid assets. Section 29 of the Banking Act, 2004 (Act 673) empowers the Bank of Ghana to prescribe the maintenance of liquid assets by a bank at a certain percentage of its deposit liabilities. In this respect the higher the prescribed ratio the lower the funds at the disposal of a bank to grant as credit facilities and vice versa.

Before July 2005 the Bank of Ghana required major banks to maintain Primary Reserve Ratio of 9.0 per cent and Secondary Reserve of 35.0 per cent both on deposit liabilities thus making available 56.0 per cent of deposits available for credit facilities. However, from July 2005 the Secondary Reserve Ratio was reduced to 15.0 per cent while the Primary Reserve Ratio remained intact at 9.0 per cent. The situation therefore allows major banks to utilise 76.0 per cent of deposits available for credit. The mandatory maintenance of secondary reserve for major banks was abolished in July 2006 whilst that for rural banks was conditionally abolished in July 2008.

Another constraint on lending by banks is imposed by Section 23(1) of the Banking Act, 2004 (Act 673) which requires banks, while in operation, to maintain a minimum capital adequacy ratio of 10.0 per cent. What this implies is that a bank should provide a capital cushion of 10.0 per cent for risk assets (invariably loan portfolio) maintained. Capital adequacy ratio of below 10.0 per cent would debar a bank for making further credit.

A bank may have loanable funds but its inability to maintain the prescribed minimum capital adequacy ratio of 10.0 per cent persistently, would prevent such a bank from extending credit facilities. In the view of the researcher, the compliance with capital adequacy ratio is dependent to a greater extent on efficient credit management, which mitigates high loan loss provision arising from the existence of good loan portfolio quality.

2.4.5 CLASSIFICATION OF LOANS AND PROVISIONING

The outstanding credit facilities granted by banks are classified to assess the quality and determine the required loan loss provision level. The classification of loans and advances by the

ADB is based on guidelines issued by the Bank of Ghana. The classifications are based on five categories, determined by the extent of duration of default and other incidental circumstances (i.e. a facility not due for repayment but beneficiary is deceased and with no collateral provided).

These five categories of loans according to Bank of Ghana (2008) are; Current, other loans especially mentioned (OLEM), substandard, doubtful and loss. The classifications indicate the level of provisions banks are required to make to reflect the quality of their loan portfolio. Indeed the various classifications clearly group loans into performing and nonperforming, in line with banking regulations. These categories further help banks to know the structure of their loan portfolio and for that matter their assets quality.

In Ghana, a major factor considered in making loans is the ability of the borrower to repay the loan. However, to mitigate the risk of default, banks ensure that loans are well secured. Though advances shall be granted on the basis of the borrower's ability to pay back the advance and not on the basis to pledge sufficient assets to cover the advance in case of default, it is highly desirable for all advances made to customers and staff to be well secured. This means that in the event of default the bank shall fall on the collateral used in securing the facility to mitigate the effect of loss of principal and interest (Banking Act, 2004).

The provision rate is applied on the total balance on the "Current" category whilst in the case of the other four categories, it relates to the balances net of prescribed realisable collateral pledged (i.e. cash, treasury bills, lien on deposits).

Provisions for Bad and Doubtful Debts are made in anticipation of non-repayment of credit facilities granted when they fall due. The provisions are made in relations to the guidelines

KNUST

issued by the Bank of Ghana. The provisioning mechanism provides yardstick as to the strength of the credit management practice of a bank. The higher the provisioning figure and its sustainable increasing trend, the weaker the credit management and the reverse holds true.

Thus, the provisioning mechanism is highly subjective especially if the period of overdue does not constitute the main yardstick and this should therefore be approached with due circumspect and compromise between the Bank of Ghana and the banks. The misapplication of the principle could bring distortions in the profitability profile and loan asset quality of a bank. The general provision of 1.0 per cent on 'Current' classified balances without recourse to netting off allowable collateral as in the case of the other classifications brings inconsistency into the application of the principle.

In view of the above, banks take into account the assets used in securing the facility to determine the level of provision to be made. Bank of Ghana regulations indicate that certain amount of provisions are made on the aggregate outstanding balance of all current advances, and aggregate net unsecured balance of all other categories as shown in the table below.

Table 2.1 Categories of Loans and their Provisions

	Category	Provision (Percentage)	No. of Days of Delinquency
1	Current	1%	0 - less than 30
2	OLEM	10%	30 - less than 90
3	Substandard	25%	90 - less than 180
4	Doubtful	50%	180 - less than 360
5	Loss	100%	360 and above

Source: Section 53(1) of Banking Act 2004

The review of the above literature on classifications and provisioning implies that the higher the non-performing loan category the higher the provisions and charges for such bad loans. For example in December, 2008, the total banking industry loan classification depicted an increase in the nonperforming categories which were 85.97%, 78.47% and 63.73% for substandard, doubtful and loss respectively. This led to an increase in the total non-performing loans which increased from 6.37% in 2007 to 7.68% in 2008 (Bank of Ghana, 2008).

2.5 IMPLICATIONS OF LOANS ON BANKING INSTITUTIONS

Loans generate huge interest for banks which contribute immensely to the financial performance of banks. However, when loans go bad they have some adverse effects on the financial health of banks. This is because in line with banking regulations, banks make adequate provisions and charges for bad debts which impact negatively on their performance. Bank of Ghana regulations on loan provisioning indicate that loans in the non-performing categories that is loans that are at least ninety days overdue in default of repayment will attract minimum provisions of 25%, 50% and 100% for substandard, doubtful and loss, respectively (Bank of Ghana Act, 2004).

According to Bloem and Gorter, (2001), though issues relating to non-performing loans may affect all sectors, the most serious impact is on financial institutions such as commercial banks and mortgage financing institutions which tend to have large loan portfolios. Besides, the large bad loans portfolios will affect the ability of banks to provide credit. Huge non-performing loans could result in loss of confidence on the part of depositors and foreign investors who may start a run on banks, leading to liquidity problems.

2.5.1 PERFORMING LOANS

Legally, a loan or credit facility refers to a contractual promise between two parties where one party, the creditor agrees to provide a sum of money to a debtor, who promises to return the said amount to the creditor either in one lump sum or in installments over a specified period of time. The agreement may include provision of additional payments of rental charges on the funds advanced to the borrower for the time the funds are in the hands of the debtor (Wikipedia, 2011). The additional payments that are in the form of interest charges, processing fees, commissions, monitoring fees among others, are usually paid in addition to the principal amount lent. Indeed these additional payments when made in accordance with the loan contract constitute income to the lender or the creditor. A loan may therefore be considered as performing if payments of both principal and interest charges are up to date as agreed between the creditor and debtor.

Bank of Ghana classifications of loans indicates that loans that are current are those for which the borrower is up to date in respect of payments of both principal and interest. It further shows that an overdraft would be considered as current or performing if there were regular activity on the account with no sign of a hardcore of debt building up (Bank of Ghana, 2008).

The foregoing reveals that loans that are up to date in terms of principal and interest payments are described as performing facilities. These types of loans constitute quality asset portfolio for banks in view of the interest income generated by such assets.

2.5.2 NON-PERFORMING LOANS

The term ‘’bad loans’’ as described by Basu (1998), is used interchangeably with non-performing and impaired loans as identified in Fofack (2005). Berger and De Young, (1997) also considers these types of loans as “problem loans”. Thus these descriptions are used interchangeably throughout the study.

Generally, loans that are outstanding in both principal and interest for a long time contrary to the terms and conditions contained in the loan contract are considered as non-performing loans. This is because going by the description of performing loans above, it follows that any loan facility that is not up to date in terms of payment of both principal and interest contrary to the terms of the loan agreement, is nonperforming.

Available literature gives different descriptions of bad loans. Some researchers noted that certain countries use quantitative criteria for example number of days overdue scheduled payments while other countries rely on qualitative norms like information about the customer's financial status and management judgment about future payments (Bloem and Gorter, 2001).

Alton and Hazen (2001) described non-performing loans as loans that are ninety days or more past due or no longer accruing interest. Caprio and Klingebiel (1990), cited in Fofack (2005), consider non-performing loans as loans which for a relatively long period of time do not generate income, that is the principal and or interest on these loans have been left unpaid for at least ninety days.

A non-performing loan may also refer to one that is not earning income and full payment of principal and interest is no longer anticipated, principal or interest is ninety days or more delinquent or the maturity date has passed and payment in full has not been made (Teach Me Finance, 2009).

A critical appraisal of the foregoing definitions of bad loans points to the fact that loans for which both principal and interest have not been paid for at least ninety days are considered non-performing. A classification of advances of the banking industry in December, 2008 showed that out of the total loan portfolio of GH¢5,966,804,133.00 in Ghana, 7.68% was non-performing. This included loans captured within substandard, doubtful and loss categories. Loans in these groups have exceeded ninety days in terms of repayment (Bank of Ghana, 2008).

2.6 DEBT RECOVERY STRATEGIES

It is inevitable that any business owner, big or small, is going to encounter clients that are just not willing to pay. This is especially prominent in the banking industry, as services are ongoing processes and not a one-time product purchase. It is no surprise that many small businesses do not survive the first two years, and the inabilities to collect from nonpaying clients are likely a large contributor of this failure. Debt collection is an endless challenge that must be tackled with care (Nishimura and al, 2001).

The following strategies are recommended (www.peligotraining.com).

2.6.1 MONITORING

Monitoring of credit facilities granted to customers is a significant function in ensuring the success of the project for which repayment is made. Huppi and Feder (1990) revealed that effective monitoring leads to higher recovery of loans by exposing possible dangers (like loan diversions) and reminding borrowers of their obligations to the lending bank (i.e. calling for redoubling of efforts towards loan repayments).

Monitoring of credit facilities has been concentrated typically on ensuring repayment when there are signs of defaults for either payment of interest or principal repayment by installments. Such practice, in the view of the researcher, fails to achieve desirable loan repayments since the facility might have already gone bad. The researcher believes that monitoring of loans should be total by following events right from the disbursement of the facility, ascertaining the deployment of funds on the intended project, following up and reviewing progress of the project, identifying shortcomings for possible advice through field visits and discussions, ensuring prompt repayment of proceeds from the project and advising on further expansion or re-direction of the project among others. 'Armed-chair' monitoring invariably becomes a factor for non-repayment of credit facilities. Effective monitoring should be instituted by a lending institution and apprise management of the state of affairs of each project

2.6.2 COLLATERAL

The granting of credit facilities is underpinned by the risk of being repaid when due. Williams and Heins (1985) indicated that risk identification is the process by which a business systematically and continuously identifies property, liability, and personnel exposures as soon as or before they emerge. The first step in business risk management in their view is to identify the various types of potential losses confronting the firm, and secondly, to measure these potential losses with respect to such matters as their likelihood of occurrence and their probable severity. It is therefore pertinent to assess the inherent risk of a credit facility, the existing operational management to mitigating the risk and determining the underlying actual risk. This assessment gives the idea of intended quality of the credit facility.

The unlikelihood that there will be a loss arising from default at repayment of a credit facility granted is referred to as credit or default risk. The primary danger in granting credit is the chance that the borrower will not repay the loan. Rouse (1989) buttressed this by stating that a lender 'lends' money and does not give it away and there will always be some risk that the customer will be unable to repay. This therefore calls for critical assessment of any credit request with reasonable assurance that repayment would not be of much problem. A bank further covers the uncertainty of the repayment by demanding collateral.

2.6.3 FREQUENT CONTACT

A lack of continued contact is a common mistake in bank debt recovery. While initial contact brings the debt to the attention of the delinquent client, without continuous, friendly reminders, you lose the benefit of the first courtesy call. Frequent contact is the key to assuring successful bank debt recovery efforts. At the same time, all contact should be hospitable. When keeping in touch with delinquent debtors, you want to remain on good terms, which require a careful, gentle approach. You'll find that, if you are speaking to the client as often as every three days, having a good attitude will assist in more success at bank debt recovery. Even once the debtor makes a commitment to pay, continued contact and follow-up is necessary to assure the payment is actually recovered. Many clients will make such promises in an effort to stop collection calls, while others become so overwhelmed with paying several debts that one can slip through the cracks unless the bank debt recovery agent follows up as a reminder (Business blog, 2011).

2.7 ADDRESSING RISK ASSOCIATED WITH CREDIT MANAGEMENT

Credit risk has the repercussion of liquidity risk, which in the extreme instance can lead a bank to severe financial crisis, resulting in erosion of capital, insolvency and could ruin the bank.

To identify and address risk associated with credit management, the Basel Committee on Banking Supervision in its Publication No. 54 issued in September 2000 outlined the following measures:

- Establishing an appropriate credit risk environment
- Operating under a sound credit granting process
- Maintaining an appropriate credit administration, measurement and monitoring process;
- Ensuring adequate controls over credit risk
- The role of supervisors.

The highlights of the above issues raised by the Basel Committee on Banking Supervision (2000) are as follows:

2.7.1 ESTABLISHING AN APPROPRIATE CREDIT RISK ENVIRONMENT

The Board of Directors should have responsibility for approving and periodically (at least annually) review the credit risk strategy and significant credit risk policies of the bank. The strategy should reflect the bank's tolerance for risk and level of profitability the bank expects for incurring various credit risks.

Senior Management should have responsibility for implementing the credit risk strategy approved by the Board of Directors and for developing policies and procedures for identifying, measuring, monitoring and controlling credit risk. Such policies and procedures should address credit risk in all of the bank's activities and at both the individual credit and portfolio levels.

Banks should identify and manage credit risk inherent in all products and activities. Banks should ensure that risks of products and activities new to them are subject to adequate risk management procedures and controls before being introduced or undertaken, and approval in advance by the Board of Directors or its appropriate committee.

2.7.2 OPERATING UNDER A SOUND CREDIT GRANTING PROCESS

Banks must operate within sound, well-defined credit granting criteria. These criteria should include a clear indication of the bank's largest market and a thorough undertaking of the borrower or counter-party, as well as purpose and structure of the credit, and its source of payment;

Banks should establish overall credit limits at the level of individual borrowers and counter-parties, and groups of connected counter-parties that aggregate in comparable and meaningful manner different types of exposures, both in banking and trading book and on and off balance sheet;

Banks should have a clearly established process in place for approving new credit as well as the amendment, renewal and re-financing of existing credits

All extension of credit must be made on an arm-length basis. In particular, credit to related companies and individuals must be authorised on an exceptional basis, monitored with particular care and other appropriate steps taken to control or mitigate the risk of non-arm's length lending.

2.7.3 MAINTAINING APPROPRIATE CREDIT ADMINISTRATION THROUGH MEASUREMENT AND MONITORING PROCESS

According to Signoriello and Vincent (1991), this process entails the following:

Banks should have in place a system for the ongoing administration of their various credit risk bearing portfolios and a system for monitoring conditions of inadequate credits, including determining the adequacy of provisions and reserves.

Banks are encouraged to develop and utilise an internal risk rating system in managing credit. The rating system should be consistent with the nature, size and complexity of a bank's activities.

Banks must have information system and analytical techniques that enable management to measure the credit risk inherent in all on-and-off balance sheet activities. The management information should provide adequate information on the composition of the credit portfolio, including identification of any concentration of risk;

Banks must have in place a system for monitoring the overall composition and quality of the credit portfolios and take into consideration potential future changes in economic conditions when assessing individual credits and their stressful conditions.

2.7.4 ENSURING ADEQUATE CONTROLS OVER CREDIT RISK

Signoriello and Vincent J. (1991) stated that banks must establish a system of independent, on-going assessment of the bank's credit risk management process and the results of such reviews should be communicated directly to the Board of Directors and senior management.

Banks must ensure that the credit granting function being properly managed and the credit exposures are within levels consistent with prudential standards and internal limits; and must further have a system in place for early remedial action on deteriorating credit, managing problem and similar workout situations.

2.7.5 THE ROLE OF SUPERVISORS

On the role of supervisors, the Basel Committee (2000) advised that supervisors should require that banks have an effective system in place to identify measure, monitor and control credit risk as part of an overall approach to risk management. The Basel Committee (2000) further stressed that supervisors should conduct an independent evaluation of a bank's strategies, policies, procedures and practices related to the granting of the credit and the ongoing management of the portfolio. In addition, supervisors should consider setting prudential limits to restrict bank exposures to single borrowers or groups of connected counter-parties.

The issues raised in the Basel Committee Publications No. 54 (2000) are very relevant and pertinent credit risk management. The Board of Directors should approve and periodically review credit risk strategy whilst senior management should ensure its effective implementation. A sound credit management process provides the basis for assessing the credit worthiness of beneficiaries and creates facilities to be followed through. This ensures the utilisation of the credit for the intended purpose and also unveils any bottlenecks, which may arise for appropriate remedial action to be enforced. This mitigates the risk of the facility not achieving the intended purpose and generating sufficient cash flows to service as well as liquidate the principal amount. Projects with high-risk profile should be given close and continuous monitoring to ensure being managed efficiently.

The role of supervisors in ensuring good credit management practices has been in force. The single borrower exposure limits, insider lending (as stipulated in Part VI of the Banking Act, 2004 (Act 673)) and stringent provisioning rules are strictly enforced by the Central Bank. Recently the Central Bank has requested all banks to nominate risk officers to coordinate the various measures instituted to control the risks confronting them.

The researcher considers the issues raised by the Basel Committee as very relevant and pertinent to manage credit risk and comments as follows:

i) The Board of Directors should approve and periodically review credit risk strategy whilst senior management should ensure its effective implementation. This would ensure that the Board of Directors exercises effective oversight over the credit management within the context of good corporate governance.

ii) The institution of sound credit management ensures the utilisation of the credit facilities for the intended purposes and also unveils any bottlenecks which may arise for appropriate remedial action to be enforced. Sound credit management processes mitigate the risk of the facility not achieving the intended purpose and generating sufficient cash flows to service as well as liquidate the principal amount. Project with high-risk profile should be given close and continuous monitoring to ensure being managed efficiently.

iii) The Bank of Ghana through regulations and the implementation of the Banking Act, 2004 (Act 673) ensures that banks adopt good credit management practices. The single borrower exposure limits and insider lending (as stipulated in Part VI of the Banking Act, 2004) and stringent provisioning rules (specified in the Guide for Reporting Institutions, Bank of Ghana, 2005) are strictly enforced by the Bank of Ghana. The Bank of Ghana recently requested all banks to nominate risk officers to coordinate the various measures instituted to control the risks confronting them.

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CHAPTER THREE

METHODOLOGY

3.0 INTRODUCTION

The following methods were adopted for the study; Research design, sources of data, sampling procedures, instruments for data collection, methods of data presentation and analysis.

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3.1 **RESEARCH DESIGN**

This study used the survey methods by employing quantitative instruments for data collection and analysis. The survey methods were used because the variables involved in the analysis were quantitative in nature. According to Trochin (1999), survey methods are used for non-experimental and descriptive research methods. He further indicated that, survey can be useful when a researcher wants to collect data on phenomena that cannot be directly observed. Based on Trochin's assertion, the researcher adopted the survey method for his study.

3.2 SOURCES OF DATA

Primary and secondary sources of data were used for the study. The main primary source of data was through the use of questionnaires. The questionnaires were both open- and close ended. The open-ended questions offered the respondents the opportunity to freely express themselves on the issues under consideration while the close-ended questions restricted the respondents on the options provided.

In the case of the secondary source of data, reports and journals, of the bank were analyzed. These reports and journals contain best practices and risk management adopted by the bank.

3.3 STUDY POPULATION

The study units were limited to members of staff and management of the branches of ADB in Eastern Region.

3.4 INSTRUMENTS OF DATA COLLECTION

Structured questionnaires were used for the collection of data. As indicated earlier these questions were both open and close-ended and were based on factors influencing access to credits, strategies for improving access to credits, credit control processes and credit collection strategies.

3.5 SAMPLING PROCEDURES

Cluster sampling method was used to group all the members of staff of the branches in the study area, dealing in various types of credit portfolio (exposure) after which simple random sampling method was used to select sampling unit from each group. This was carried out after the number of workers in each branch has been determined.

3.6 SAMPLE SIZE DETERMINATION

The Yamane's (1967) simplified formula corrected to proportions were used and it is defined as

$$n = \frac{N}{1 + N\left(e\right)^2}$$

where

N = Population

n = Sample size

e = Precision

There were about a total of 101 workers in the study area. Therefore, our sample size was computed as follows;

$$n = \frac{101}{1+101(0.05)^2}$$

$$= 81$$

The table below gives the breakdown of the population and the selected samples in the various branches of the study area.

Table 3.1 Branches with their population and selected samples in the study area

Branch	**Total Members of staff**	**Sample size**
Koforidua	22	19
Suhum	15	12
Nkawkaw	16	13
Juapong	17	14
Asiakwa	15	12
Kade	16	11
Total	**101**	**81**

3.7 METHODS OF DATA PRESENTATION AND ANALYSIS

The quantitative data collected were summarized and presented by means of tables and charts. This offered a pictorial presentation to enhance the understanding of the data. The data presented was also analysed using percentages.

CHAPTER FOUR

DATA PRESENTATION AND ANALYSIS

4.0 INTRODUCTION

This chapter presents the finding and discussions of the study. It starts with the socio – demographic analysis on the respondents after which factors influencing access to credits, credits control practices and credits collection strategies are analysed.

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4.1. SOCIO – DEMOGRAPHIC CHARACTERISTICS OF RESPONDENTS

The following socio – demographic characteristics of respondents were analysed, sex, age, level of education and years of experience.

4.1.1 SEX OF RESPONDENTS

Out of the 81 respondents used for the study, 55.6% were males whiles 44.4% were females. This signifies that, there are more males employees in the ADB branches in the Eastern Region of Ghana. The details are presented in table 4.1 below

Table 4.1 Sex of Respondents

Sex of respondents	Frequency	Percentage
Male	45	55.6
Female	36	44.4
TOTAL	**81**	**100**

Source: field work (2012)

4.1.2 AGE OF RESPONDENTS

It was found that, staffs in the age cohort of 30 – 34 years are more dominant in the Bank (42.0%). This is followed by those aged between 20 – 29 years (32.1%). The age with least representation in the bank is between 50 – 59 years a (9.9%). This means that most of the workers in the bank are young adults. The details are found in Table 4.2

Table 4.2 Ages of Respondents

Age of Respondents	Frequency	Percent
20 – 29	26	32.1
30 – 34	34	42.0
40 – 49	13	16.0
50 – 59	8	9.9
Total	**81**	**100**

Source: field work (2012)

4.1.3 LEVEL OF EDUCATION

The analysis on the level of education indicated that, over 46.9% of the respondents have bachelors' degree whiles 21.0% have diploma, 19.8% masters' degree and 12.3% senior high school level certificate. The details are found in table 4.3 below**.**

Table 4.3 Level of Education

Level of Education	**Frequency**	**Percent**
SHS level	10	12.3
Vocational/Technical	0	0
Diploma	17	21.0
Bachelor	38	46.9
Masters	16	19.8
Total	**81**	**100**

Source: field work (2012)

4.1.4 YEARS OF SERVICE

The study found that, 3.7 % of the respondents have served the organization for over 20 years. Staff who have served the organization for less than 1 year represents 11.5%, whiles majority (36.1%) have served the organization between 1 – 4 years. The details are presented in the table 4.4 below.

Table 4.4 Years of Service

Types Of Service	Frequency	Percentage
Less than 1	9	11.1
1 – 4	29	35.8
5 – 9	19	23.5
10 – 11	9	11.1
15 – 19	7	8.6
20 – 25	5	6.2
25+	3	3.7
Total	**81**	**100**

Source: field work (2012)

4.2 FACTORS INFLUENCING ACCESS TO CREDITS

Without creating the platform necessary for customers to access credits, it will be impossible for management to control and manage credits since nothing will be there to manage. Based on this, the researcher is interested determining the factors influencing access to credits and what management is doing to increase access to credits. The details of the factors influencing access to credits are presented in table 4.5 below.

Table 4.5 Factors Influencing Access to Credits

Factors	Frequency	Percentage
Age of client	4	5.0
Client history	21	25.9
Stringent policies	26	32.1
Purpose of loan	7	8.6
Amount of loan	6	7.4
Cash flow of client	17	21.0
Others	0	0
Total	**81**	**100**

Source: field work (2012)

The way credit is controlled in the bank is among the major strategies in managing credits since poor credit control can increase the level of credit risk in the bank Kotoh (2004). This study found that, as high as 32.1 percent (%) of the respondents considered the use of stringent policy rules as a major factor in controlling credit.

It was found that, management has established policy rules that, the Bank shall not grant unsecured financial exposure in respect of any of its directors or significant shareholders and related parties. The board of the bank shall be the only authority to approve or sanction any financial exposure of the bank to any of its directors or significant shareholders or related parties.

Another major factor influencing access to credit is critical examination of customers' history. This constitutes 25.9 percent (%) of the respondents. The study found that it is the duty of the credit officers to delve into the history of customers based on their past credits performance. If a customer is found to have kept fit with the bank by paying his indebtedness on schedule, then the credit officer would assume that all things been equal the customer could pay the new credits he/she wants to access based on his previous records. Based on their background, customers with good credits history easily get credits from the bank.

On the other hand, if a customer is blacklisted because of his past records such as difficulty in repaying credits, such a customer is either given small amounts or denied completely. The study found that credits officers are able to categories the customers into those who are credit worthy and those who are not. Each of these categories is treated on its own merit.

The purpose of accessing the credits (8.6%) was seen as measure of determining whether the loan should be granted or not. No bank will ever give a loan to support illegal activities. This implies that, the purpose for which the loan is being accessed should first and for most be on legal activities. The study further found that, banks grant loans meant for specific activities such as overdraft, agricultural loan, personal loan, asset finance and construction. Limits are set on each of these, making it easier for anyone who falls within such limits to access the loan without difficulties.

Another factor influencing access to credits is the amount to be accessed (7.4%). It was found that when the amount to be accessed is in line with the purpose and the business activity of the customer, all things been equal, the likelihood of the loan being granted is higher than a customer whose request is not realistic or does not much the purpose for which the loan is being requested. Usually, the amount being granted should match and suffice the purpose of the loan, which will enable the customer utilise the amount to generate enough revenue for the business in question and subsequent repayment of the loan. Insufficient amount means under financing of the business project and the client will run into liquidity problems. When this happens, the debtor will be unable to execute the project successfully, making it very difficult to repay the loan, hence the risk of default.

The 'cash flows of a customer' (21.0%) is also used as a measure to grant credits to customers. It is a requirement in the bank that every loan request should be supported with cash flow system. The statement of a business's cash flows is often used by analysts to gauge financial performance. Companies with ample cash on hand are able to invest the cash back into the business in order to generate more cash and profit. Cash flows therefore indicate how much the customer can pay at a time as well as how long it will take the customer to pay the loan. When the cash flows indicates that, a customer can pay the amount within the agreed time, all things been equal, such a customer will not have any difficulty in accessing the loans as compared to customers with negative cash flows. This is due to the fact that, every company has to be able to generate positive cash flows in the long run. Businesses with permanently negative cash flows will face liquidity constraints; hence will be unable to repay the loans if granted.

The age of a Client (5.0%) is another factor taken into consideration when granting credits to customers. Persons under 18years cannot access credits from any bank because they are considered as minors. The study found that the bank is cautious when granting loan to the aged. It was also found that, most often huge loan granted to the aged should be supported with adequate collateral security. This suggests that it is quite easier for young and middle age customers to access loans from the banks than the aged could do.

Notwithstanding the established policy guidelines on access to credits, there is the need for customers to meet certain conditions such as cash flows, purpose of loan, amount, age of client and security in other to enhance access to the loan request.

4.3 CREDITS CONTROL PROCESS

A major credit management function is to be able to control the process of credits. Based on this the researcher explored from management and the credits officer how they control the credits process and the responses are found in table 4.6

Table 4.6: Credit Control Processes

Control Measures	Frequency	Percentage
Ensure completeness of internal guideline	46	56.8
Ensure completeness of credit application	26	32.1
Ensure signing / collateral agreement	6	7.4
Confirmation of applicant compliance with conditions	3	3.7
Total	**81**	**100**

Source: field work (2012)

Majority of the respondents (56.8%) indicated that the main credits control process they follow is to ensure that they comply with the guidelines set in granting credits.

It was found that the first guideline in granting approval to credits is to look out for all possible errors in the application form. This is to ensure that the applicant provides the right information. Once the credit officer is satisfied that there is no error on the form, the next guideline is to segment the applications based on economic and illegal situations as well as the relevant environmental factors. After the segmentation, the applications are appraised based on transparent and comprehensive presentation of the risks when granting the loan on one hand, and adequate assessments of these risks on the other. Another major guideline after the segmentation is to be able to account for the risk aspects for the credits being granted. This involves the ability to account for probability of defaults on maturity. Another guideline is to be able to determine and value the type of collateral needs and sources of cash flows.

Another major credits control process identified by 32.1 percent (%) of the respondents is to ensure the completeness of the loan application. The study found that, it is the duty of the loan officers to ensure that all the major fields on the credit assessment forms are filled and duly singed by the applicant. The study further found that the credit application is considered incomplete if either the date of application or the full name of the applicant is omitted. The purpose to which the credit is being accessed, cash flow analysis and the security intended to support the application are all necessary ingredients needed to make the application complete. Until this information is provided in full, an assessment cannot be made on the applicant request to determine whether the credits will be granted or not.

A small percentage (7.4%) of the respondents said that, the main process in credits management is to ensure that the credit application is signed and is supported by substantial collateral. It was found that once these two prerequisite are met the credit officers' duty of evaluating the credit must begin. These categories of respondents were of the view that, it is not obligatory for the applicant to provide every information required. But it is the duty of the credit officers to assess every piece of information the customer provides in other to take a decision on whether to provide the credit or not.

Receipts of confirmation that the credit applicant has complied with the terms and conditions on loan request, is another process the credit officers examines. This constituted 3.7% of the responses. To do this all the conditions associated with granting of credits should be made known to the customers, so that in the course of his application he/she ensures that all the terms and conditions given him/her are meet. When this is met the main duty of the credit officers is to examine the application form and submit it with recommendations to management for approval.

There are many control processes management use in credit administration. The main control practices are to ensure that credit applications are in line with the credit policy guidelines of the bank and to ensure the completeness of the application forms.

4.4 CREDIT COLLECTION STRATEGIES

Credit collection is a key component of the credit management life cycle and the impact of getting it right can have a significant influence in reducing the risk associated with credit management (Benoit 2009). Based on Benoit assertions, the researcher determined the credit collection strategies adopted as a credit management process of ADB branches in Eastern region. The details are presented in Table 4.7

Table 4.7 Credit Collection Strategies

Credit Collection Strategies	Frequency	Percentage
Establish payment guidelines	25	30.9
Consider prompt payment	4	4.9
Develop collection section	30	37.0
Write to notify customers	16	19.8
Provide incentives for prompt payment	6	7.4
Total	**81**	**100**

Source: field work (2012)

From table 4.7, it was found that the main strategy adopted for collection is the establishment of credit collection section in the credit management department and this constituted 37.0 % from the respondents. The main task of the credit collection section is to devise strategies for collecting debts and to ensure that debts owed have been tracked and every effort made for the payment even if it includes initiating legal actions. As part of the function of the credit collection section, they are to submit monitoring report on all customers with loan portfolios for management decision.

Another credit collection strategy identified is to establish payment guidelines on credit collection (30.9%). The establishment of the payment guidelines would give clear indication as to when and how loans would be paid. To be able to establish effective policy guidelines, there is the need to create a tracking system that would alert debt collectors of all overdue payments; so that immediate action could be taken to collect all outstanding debts. It is also important to follow strict protocols for missed payment. This is possible if the tracking system is put in place.

There is also the need to conduct credit checks. When working with new clients, it will be prudent to conduct a thorough credit and background checks to determine the credit worthiness for the clients. After all these standard policy guidelines have been set, there should be a payment guideline.

The study found that strict payment guidelines often help, for instances the debt collection officers should avoid extended payment terms, that is, not to extend payment beyond 30 days when the economy is tight. The offer of multiple payment option is another payment guideline that can facilitate debt collection. This helps in the prompt collection of payment. The payment option can be through cash, checks, credits and fleet cards. The ability to offer flexible payment guidelines is a way of enhancing debt collection.

Sending of letters of notification to debtors (19.8%) was seen as a strategy in debt collections. The study found that one of the initial steps taken in debt collection is to write to notify the debtors a well as to remind them of their indebtedness. After a month of notification another letter of reminder (demand notice) is sent indicating the principal and the interest accrued, and an opportunity to reschedule the repayment of their indebtedness. When the second reminder letter does not yield intended results, then a third and a final warning letter is issued indicating the next line of action to be taken, that is, either to sublet the indebtedness to a debt collection agency or initiate legal action. The study found that letters of reminder to debtors most often prompt debtors to honour their obligations to the bank.

The provision of incentives for prompt payments (7.4%) was also seen as a strategy management adopts in collecting credits. It was found that management often reduces the interest amounts for customers who wants to pay their indebtedness upfront and especially in one installment before the expiration of the deadline for payment.

Debt collection policy which considers prompt payments (4.9%) was seen as another credits collection strategy. The study found that, as part of the payment guideline, an option is provided for customers to pay for the credits before the deadline. Customers who are able to offer prompt payments are classified as creditworthy. As such, the bank is willing to transact business with such customers at all times.

Credit collection strategies are important component of credit management practices and the key credit collection strategies in the study area are to develop collection sections and the establishment of payment guidelines.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 SUMMARY

This study assessed credit management practices at ADB branches in Eastern region of Ghana. This was carried out by analysing the process of accessing credits; credits control processes and credits collection strategies. This was done against the background that there was huge debts as a result of nonperforming loans affecting the financial status of the bank.

The descriptive survey method was used for the study. Sample size of 81 members of staff was drawn from the 101 staff in all the six ADB braches in the Eastern region of Ghana. The cluster sampling method taking into consideration each branch as a cluster was used to identify individual sample units for the study.

Two main sources of data were used for the study namely, the primary and secondary sources of data. Questionnaires were used as the main instrument to collect the primary data on access to credit, credit control processes and credit collection strategies.

5.2 CONCLUSION

The following findings were made in line with the conclusion drawn;

1. There are more male workers involved in credits management process in the bank than females.

2. The age of most of the bank officials involved in credits management are between 30 – 39 years with a small percentage aged between 50 – 59 years.
3. The level of education of most officials involved in credits management is high with majority having first degree.
4. Majority of the credit collection staff have worked between 1 – 4 years in the organization.
5. The main factors influencing access to credits are stringent policies or guideline, clients' history and cash flows of clients.
6. Process management adopts to control credits includes ensuring compliance with internal guidelines and completeness of credits applications forms.
7. The main credit collection strategies used in managing credits in the bank includes establishment collection section in the credits management department and establishment of payment guidelines.
8. Minor credit collections strategies adopted in the bank include providing incentive for prompt payment and consideration of prompt payment in the credit policy.

Based on the findings, the following conclusions were drawn. Notwithstanding the establishment of guidelines in access to credits, customers who want to access credits must meet certain conditions in terms of cash flows, purpose of the loan, amount, age of client and the provision of security in order to enhance access to loans.

There are many credit control processes used by management and the main processes are ensuring that credits applications are in line with credits guidelines and that the forms are fully completed.

The key credit collection strategies adopted in the study area are to develop credits collection section in the credit management department and to establish payment guidelines.

5.3 RECOMMENDATION

1. The study found that the main factors influencing access to credits are stringent policies, client history and cash flows of clients. It is therefore recommended that the policy of access should be flexible so that customers can easily access credits. In addition, management should not rely on only client history and cash flows but should look at the variability of business plan and the past financial statement to take a decision on the variability of credit worthiness.
2. The study found that minor processes such as receipts of confirmation of applicant compliance with condition of credits and ensuring that collateral agreement are signed, were considered as minor processes in credit management practices. It is recommended that all processes of managing credits should be considered as important factors in the credit management process to ensure efficiency in credits delivery.
3. The study found that one of the main credit collection strategies is to establish a credit collection department. The study also found that the credit collection section is under resourced in fulfilling its mandate of credit collection. It is recommended that the credit collection section should be provided with the logistics needed to carry out its main task of debt collections.

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APPENDIX

KWAME NKRUMAH UNIVERSITY OF SCIENCE AND TECHNOLOGY

INSTITUTE OF DISTANCE LEARNING

QUESTIONNAIRE

This questionnaire is designed to help assess the credit management practices among selected Agricultural Development Bank (ADB) branches in Eastern Region.

All pieces of information provided in this questionnaire are strictly confidential and will only be used for the purpose of this research.

Thank you for your time and contribution to this important research.

HOW TO COMPLETE THE QUESTIONNAIRE

Please tick the box that corresponds to the most appropriate response/Answer in each question.

You may also write your response in the spaces provided where applicable.

Thank you for your contribution towards this all important research.

Section A: Social Demographic Profile of Respondents

1. What is your sex?

   ☐ Male

   ☐ Female

2. In which age group do you belong

   ☐ 20 – 29

   ☐ 30 – 39

40 – 49

50 – 79

3. Which level of education are you?

SHS/Secondary

Vocational/Commercial/Technical

Diploma

Bachelors'

Masters'

Others (Specify)………………..........................

4. Which year of service are you in the bank?

Less than 1 year

1 – 4 years

5 – 9 years

10 – 14 years

14 – 19 years

20 – 24 years

25+

Section B: Access to Credits

1. What are the factors that inhibited access to credits?

Age of client

Customer History

Stringer Policy rule

- [ ] Purpose of Loan
- [ ] Amount
- [ ] Cash Flow
- [ ] Others (Specify)………….........................

2. How can the problem identified be reduced to help increase access?

- [ ] Education
- [ ] Flexible policy rules
- [ ] Good business plan
- [ ] The credits department should be more functional
- [ ] In – service training
- [ ] Reducing interest rate

Section C: Credits Control Process

1. What measures are put in place by management to control the element of risk in granting credit?

- [ ] Ensure compliance with internal guidelines
- [ ] Ensure completeness of the credits application
- [ ] Ensure signing of the credits and collateral agreement
- [ ] Receipt of confirmation that the credits applicant has complied with the conditions imposed.

2. How can the credits control processes be improved?

- [ ] Training
- [ ] Effective Monitoring

☐ Improve Internal Control System

☐ Initiate Legal Processes Early

☐ Provide remainder letters early

Section D: Credits Collection Strategies

1. What credits collection strategies does management adopt in retrieving credit?

☐ Establish payment guideline

☐ Consider prompt payment

☐ Develop an account receivable section

☐ Write to notify your debtors often

☐ Provide incentive for prompt payment

☐ Seek legal advice

2. What strategies do management adopt when clients till fail to pay their debt?

☐ Provide legal warring letter

☐ Hand them over to debt factoring company

☐ Use the collateral security to defray the indebtedness

☐ Reminder letters

3. When does management declare a debt bad?

☐ When the debtors is deceased

☐ When the debtor absconds

☐ When the debt is economic to pursue

☐ When the debtor is in solvent

☐ When the debtor is committed to prison