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IMPACT OF CREDIT MANAGEMENT ON BANK PERFORMANCE IN NIGERIA

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ABSTRACT

As with any financial institution, the biggest risk in bank is lending money and not getting it back. This study examined the impact of credit management and bank performance in Nigeria. The study adopted cross sectional survey design. The population of the study consisted of all management staffs of commercial banks operating in Nigeria. The sample sizes of eleven (11) select commercial banks were considered by systematic technique. The Purposive sampling technique was adopted; hence six respondents were administered questionnaire (Bank Manager and five senior staff) from each bank to make up a 66 respondents for the study. Multiple regression analysis was adopted for the study to determine the influence/impacts of credit management variables (Credit Appraisal, Credit Risk Control, and Collection policy) on bank performance. The study revealed that credit management has a significant impact on bank performance in Nigeria. The study also revealed that among the credit management variables considered, credit risk control has the highest driving force for bring about an effect financial performance of bank in Nigeria. It was recommended that financial institution should not only take credit management serious, but should recognised the role of credit risk section if they aim at increasing profitability.

Keywords: Bank Performance, Credit Management, Credit Appraisal, Credit Risk Control, and Collection policy, Financial Performance.

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Introduction

The strength of financial system has central role in the country (Das and Ghosh, 2007) as its failure can upset economic development of the country. Company's financial performance is the ability to create new resources, from day to day operation over a set period of time and being gauge by net income and cash from business (Abiola & Samuel, 2014).

Banks are profit-making organizations performing as intermediaries linking borrowers and lenders in bringing for the time being available resources from business and individual customers as well as providing loans for those in require of financial support (Drigă, 2012). Commercial Banks play a vital role in developing economies like Nigeria, Ghana, Egypt and Algeria. Bank lending is very vital for it make possible the financing of agricultural, industrial and commercial activities of the country (Uwuigbe, Olubukunola, & Babajide, 2015; Collins, Johnny, M-epbari and Barikui, 2017).

Credit is one of the many factors that can be used by a firm to impact demand for its products (Kagoyire & Shukla, 2016). According to Horne and Wachowicz

(1998), firms can only help from credit if the profitability generate from increased sales exceeds the added costs of receivables. Myers and Brealey (2003) define credit as a process whereby ownership of goods or services is allowed devoid of spot payment upon a contractual agreement for later payment.

A key requirement for efficient credit management is the ability to intelligently and resourcefully manage customer credit lines. In order to reduce exposure to bad debt, over-reserving and bankruptcies, companies must have greater insight into customer financial strength, credit score history and changing payment pattern. Credit management starts with the sale and does not stop until the complete and final payment has been received. It is as vital as part of the deal as closing the sale. In fact, a sale is in principle not a sale until the money has been collected. It follows that principles of goods lending shall be concerned with ensure, so far as possible that the borrower will be able to make scheduled payments with interest in full and within the required moment in time otherwise, the profit from interest earned is reduced or even wiped out by the bad debt when the customer eventually defaults. Credit management is concerned principally with managing debtors and financing debts. The objectives of credit management can be stated as safe guarding the company's investments in debtors and optimizing operational cash flows. Policies and procedures must be useful for granting credit to customers, collecting payment and limiting the risk of non-payments (Kagoyire & Shukla, 2016; Wadike, Abuba and Wokoma, 2017).

With the increase in bankruptcy rates, the probability of incurring losses has risen. Economic pressures and business practices are forcing organizations to slow payments while on the other hand resources for credit management are reduced in the face of the higher expectations. Therefore it is a necessity for credit professionals to seek for opportunities to implement proven top practices (Kagoyire & Shukla, 2016).

Sound credit management is a requirement for a financial institution‟s stability and continuing profitability, while worsening credit quality is the most frequent cause of poor financial performance and condition. Commercial banks are main players in the financial sector of every country's economy. The failure or success of these banks will to a large level affect the financial sector and the economy. Hence, firms must ensure that the management of receivables is efficient. Such delay on collecting cash from debtors has serious financial problems, increased bad debts and affects customer relations. If payment is made very late, then profitability is worn, and if payment is not made at all, then a full loss is incurred. On that basis, it is simply good business to put credit management at the front by running it strategically. In recent times some commercial banks in Nigeria have been wound up leaving customers to their fate. It is important to note that the chief cause of the winding up is their poor management of their finance and credit. Many of them were accumulating huge amounts of debt yearly. The rationale for the failure of these banks has sparked the attention of the researcher in conducting advance studies into the management of finance and credit in Nigerian banks. It is expedient to then ask; are there any impacts of Credit appraisal, Credit risk control, and collection policy on Bank Performance in Nigeria. It is in the light of the above, that this study examined the impact of credit management and bank performance in Nigeria.

Literature Review

Empirical Review

As with any financial institution, the principal risk in bank is lending money and not getting it back. On this note, Kagoyire and Shukla (2016) studied effect of credit management on performance of commercial banks in Rwanda (A case study of Equity Bank Rwanda LTD). The study sought to determine the effect of credit management on the financial performance of commercial banks in Rwanda. The study adopts a descriptive survey design. The target population of study consisted of 57 employees of Equity bank in credit department. The entire population was used; giving a sample size of size of 57 employees. Purposive sampling technique was used where the entire population was included in the study. Primary data was collected using questionnaires which were administered to the respondents. Descriptive and inferential statistics were used to analyse data. The study found that client appraisal, credit risk control and collection policy had significant effect on financial performance of Equity bank. The study established that there was very strong relationship between financial performance of Equity bank and client appraisal, credit risk control and collection policy. The study also established that client appraisal, credit risk control and collection policy significantly influence financial performance of the bank. Collection policy was found to have a top effect on financial performance and that a stringent policy was more effective in debt recovery than a lenient policy. The study therefore recommends that Equity bank should enhance their collection policy by adapting a more stringent policy to a lenient policy for successful debt recovery.

In corroboration with Kagoyire and Shukla (2016), Uwuigbe, Olubukunola, & Babajide, (2015) carried out a study on credit management and bank performance of listed banks in Nigeria. The study aimed to examine the effects of credit management on banks's performance in Nigeria. In achieving the objectives recognized in this study, the audited corporate annual financial statement of the listed banks covering the period 2007-2011 were analysed. A sum total of ten listed banks were selected and analysed for the study by adopting the purposive sampling method. However, in assessing the research postulations, the study adopted the use of both descriptive statistics and econometric analysis, using the linear regression methodology consisting of periodic and cross sectional data in the estimation of the regression equation. Results from the study revealed that while ratio of non-performing loans and bad debt do have a significant negative effect on the performance of banks in Nigeria, on the other hand, relationship between secured and unsecured loan ratio and bank's performance was not significant. Hence, the study recommends that banks management should put in place or institute sound lending framework, adequate credit administration procedure, and an effectual and efficient apparatus to monitor lending function with an established rule.

Femi, Marshal, and Ayodele (2015) researched on credit risk management and bank performance in Nigeria. This study investigated the impact of credit risk on banks' performance in Nigeria. A panel estimation of six banks from 2000 to 2013 was done using the random model framework. Result from the study showed that credit risk is negatively and significantly linked to bank performance; measured via return on assets (ROA). This result suggests that an increased exposure to credit risk reduces bank profitability. It was also found that total loan has positive and significant impact on bank performance. Therefore, to shoot the cyclical nature of non-performing loans and increase their profits, the banks should implement an aggressive deposit mobilization to increase credit availability, and develop a trustworthy credit risk management strategy with adequate penalty for loan payment defaults.

In Kenya, Mutisya (2015) studied effect of mitigating credit management on performance of commercial banks in Kenya: A case of Chuka Town. The study aimed at investigating the effect of mitigating credit risk to the performance of commercial banks currently operating in Chuka Town in Tharaka Nithi County. The study was descriptive in nature. The study opted for both primary and secondary forms of data. The secondary data was collected from the documentations accessible from the banks, and the primary data from various banks using questionnaires. Data was analysed using descriptive statistics involving percentages. The study found out that the banks had policies and strategies of mitigating credit risk which has direct impact on their performance with the credit section being acknowledged as the most important sector in the banking section. This is owed to the fact that credit was the major investment that is being undertaken by commercial banks. Although all this are well-known by commercial banks still stress need to be put up for all credit risk policies to be observed carefully as still commercial banks experience risks that lead to heavy losses. Also it was found that there was a significant relationship between bank performance, and credit risk management (in terms of risk identification, monitoring and credit sanctions).

Though Mutisya (2015) opined that better credit risk management results in better bank performance. This view does not deviate from positions of Femi, Marshal, and Ayodele (2015)., Shukla (2016)., and Uwuigbe, Olubukunola, & Babajide (2015). Thus, it is of crucial importance that banks practice prudent credit management and safeguarding the assets of the banks and protect the investors' interest.

Theoretical Framework

Information Assymetry Theory - Information asymmetry refers to a condition where business owners or manager know more about the forecast for, and risks facing their business, than do lenders (PWHC, 2002) cited in Eppy.I (2005). It describes a situation in which all parties involved in an undertaking do not know relevant information. In a debt market, information asymmetry arises when a borrower who takes a loan usually has improved information about the potential risks, and returns connected with investment projects for which the funds are earmarked. The lender on the other hand does not have adequate information concerning the borrower (Edwards and Turnbull, 1994).

Transaction Cost Theory - First developed by Schwartz (1974), this theory conjectures that suppliers may well have an advantage over traditional lenders in checking the real financial circumstances or the credit worthiness of their clients. Suppliers also have a healthier ability to monitor and compel repayment of the credit. All these superiorities may give suppliers a cost advantage when compare with financial institutions (Nduta, 2013).

There are three sources of cost advantage were classified by Petersen and Rajan (1997) as follows: information acquisition, controlling the buyer and salvaging value from existing assets. The first source of cost advantage can be explained by the verity that sellers can get information about buyers faster and at lower cost because it is obtained in the regular course of business. That is, the frequency and the amount of the buyer's orders offer suppliers an idea of the client's state of affairs; the buyer‟s rejection of discounts for early payment may provide to alert the supplier of a weakening in the credit-worthiness of the buyer, and sellers regularly visit customers more often than financial institutions do.

Methodology

The study adopted cross sectional survey design in which information were collected from only a fraction of the entire population selected so as to represent the whole. The population of the study consisted of all management staffs of commercial banks operating in Nigeria. The Central bank Nigeria (2017) reported that 22 banks are currently operating in Nigeria. The sample size of eleven (11) select commercial banks were considered. The eleven banks were systematically selected at an interval of two from the table of random numbers. Purposive sampling technique was adopted, hence six respondents were administered questionnaire (Bank Manager and five senior staff) from each bank to make up a 66 respondents for the study. Multiple regression analysis was adopted for the study to determine the influence/impacts of credit management variables (Credit Appraisal, Credit Risk Control, and Collection policy) on bank performance.

Results and Interpretations

To examine the extent to which credit management variables (Credit Appraisal, Credit Risk Control, and Collection Policy) influenced the Bank performance in the study area, multiple regression analysis was performed using SPSS version 20 and the result summarised in Table 1 and 2 respectively. Credit management variables were determined by summation of all the items in the questionnaire for all the select banks to achieve a composite index for each independent variable. The Overall Bank performance was determined by transforming all the composite indices of the variables to establish an overall index of performance for the study area using SPSS.

Hypothesis Testing

To test for the impact of credit management on bank performance in Nigeria, the following hypotheses were formulated

H2 = There is no significant impact of Credit management on bank peformance in Nigeria.

Table 1: ANOVA model of multiple regression analysis

Model		Sum of Squares	Df	Mean Square	F	Sig.
	Regression	6951.458	3	2317.153	13867.380	.000[b]

Residual	10.360	62	.167
Total	6961.818	65	

The result of the analysis showed that p<0.01 for crdeit management on bank performance was significant at 0.05 level of significance. Hence the null hypothesis was rejected, this implied that there is a significant impact of credit management on bank performance in Nigeria. The result from the analysis can also be further verified by the remarkable difference between the mean square exemplified by high value of the F-ratio. Since the F-ratio was greater than the table value, the null hypothesis was rejected at 0.05 level of significance.

The results presented in Table 2 showed that p<0.01for each of the credit management variables (Credit Appraisal, Credit Risk Control, and Collection policy) on the overall bank perrformance were significant at 0.05 level of significance. This therefore means that Credit Appraisal, Credit Risk Control, and Collection policy significantly influences the outcome of the bank performance in the study area.

The coefficient of determination (R^2) was 0.999 while the adjusted R^2 was 0.998 which showed that 99% of the variation in achieving effective bank performance was explained by combined changes in the predicting variables (Appraisal, Credit Risk Control, and Collection policy). The analysis also shows that the overall fit of the regression model was good given the ANOVA F-value of 13867.380 and significance at 0.05 critical level. The Durbin Watson was 0.638. This is an indication that there is autocorrelation among the successive values of the variables in the model. Hence, linear relationship exists between the dependent and the independent variables.

Table 2: Summary of multiple regression analysis credit management variables

Variables	Beta Estimate	t	Sig.	Remark
Credit Appraisal	.309	14.236	.000	Reject Ho
Credit Risk Control	.417	10.946	.000	Reject Ho
Collection Policy	.281	8.464	.000	Reject Ho
R	.999			
R^2	.999			
Adjusted. R^2	.998			
Standard Error	.40877			
D-Watson	.638			
F Value	13867.380			

Source: Fieldwork, 2017

To determine the contribution of each independent variable on bank performance in Nigeria, through evaluation of each independent variables, the absolute value of the Beta estimate (β) was used. Table 2 shows that the three credit management variables were good predictors of bank performance in Nigeria. At 0.05 level of significance, Credit Appraisal (β = 0.309; t = 14.236; p<0.01) made a significant contribution (30.9%) towards predicting bank performance in the study area. Credit Risk Control has the highest contribution of (41.7%) with (β = 0.417; t = 310.946; p<0.01), and Collection policy (28.1%) with (β = 0.281; t = 8.464; p<0.01). This means that given one standard deviation increase in Credit Appraisal, bank performance will increase by 0.309 standard deviation, and given one standard deviation increase in Credit Risk Control, Bank performance will increase by 0.417 standard deviation. Also, given one standard deviation increase in Collection policy, Bank performance will increase by 0.281 standard deviation
Based on the result Table 1&2 respecively, the general linear regression model estimator of Bank performance was shown mathematically as follows:

$$BF = a + \beta_1 CA + \beta_2 CRC + \beta_3 CP + e$$

$$\text{Bank Performance (BP)} = a + \mathbf{0.309}CA + \mathbf{0.417}CRC + \mathbf{0.281}CP + e$$

Where: a = Constant

β_1, β_2 and β_3 are the regression coefficients.

CA = Credit Appraisal

CRC = Credit Risk Control

CP = Collection Policy

e = Error term

Discussion of Findings

Multiple Regression Analysis revealed that at 0.05 level of significance, Credit Appraisal ($\beta = 0.309$; $t = 14.236$; $p<0.01$), Credit Risk Control ($\beta = 0.417$; $t = 310.946$; $p<0.01$), and Collection policy ($\beta = 0.281$; $t = 8.464$; $p<0.01$) influences overall bank Performance in Nigeria. Because β_2 is higher than β_1 & $\beta_{2,}$ it was concluded that Credit Risk Management was more important than Credit Appraisal and Collection Policy in driving the variation in Bank Performance in the study area. These results corroborated with the findings of Kagoyire and Shukla (2016) on impact of credit management on bank performance, but differ in some other ways. While the author opined that collection policy has the highest driving force in bringing about bank performance, the result of this study revealed that credit risk control as one of credit management variables is important in driving bank performance in the study area. The aforementioned finding is supported by Femi *et al*. (2015) in that the authors opined that the increase exposure to credit risk may significantly reduce bank profitability, hence, financial institutions should develop a well reliable credit risk management strategy. This idea does not deviate from the idea of Mutisya (2015) whose work suggested that bank policies credit risk has influences on bank. Therefore, credit section should be recognised as one of the most important section in the banking section.

Conclusion and Recommendation

The study found out that credit management variables (Credit appraisal, credit risk control and collection policy) had significant effects on financial performance of commercial banks in Nigeria. But above all, credit risk control which a very significant effect on bank performance should be taken very seriously if any financial institutions aim to survive in the ever changing and competitive banking sector. The study also recommended that further study should critically examine the effect of credit risk control on financial performance of commercial banks in Nigeria, by using different data collection methods, increase sample size in order to improve accuracy of results.

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