

## **An Assessment of Challenges and Prospects of Credit Management Practice in The Case of Awash International Bank s.co**

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### ***Abstract***

*The study assesses the challenges and prospects of credit management in AIB Arada Giorgies branch. The research has been conducted mainly to find the major problems in credit management of the bank. The researcher used questionnaire and interview to obtain the attitudes, views and comments of borrowers and key personnel's from sample respondents which were selected using both judgmental and stratified random sampling technique by grouping loan types in each sector. Judgmental sampling is used to select senior staffs from Arada Giorgis branch, credit analysts at head office and employees who are related with the study. The data obtained were presented and analyzed by using descriptive statistical method. According to the result lack of proper financial statements submitted by borrowers in one side and a highly general, centralized, less flexible and not up to dated credit policy and procedure on the other are major problems identified which affects the quality of credit process, analysis and the decisions or recommendations of credit facilities. Moreover, irregular customer's business visiting, poor recognition for good borrowers and low the collateral value estimation are the flaws where as strictly reminding borrowers for repayment are the strong point of the bank. Generally, AIB should make the credit policies and procedures in a clearly defined, flexible and timely way and the credit procedures should include detail assessment of criteria for each credit products.*

## **Introduction**

Commercial Banks render a number of services such as provisions of different credit facilities, mobilizing savings, fixed time, demand deposits, local and foreign money transfers, transaction of currency, credit and debit cards and other related activities. The principal business line of commercial banks extends credit service to customers (Banking Business Proclamation No. 592/2008). The word credit which is also called loan is derived from the Latin word "Ceditum", which means to believe or trust. In economics, the term credit refers to a promise by one party to pay another for money borrowed or goods/services received. It is a medium of exchange to receive money or goods/ services on demand at some future date ( Thingan, 1997)

Bank advances credit ranging from single individual to a large corporation as well as projects as a means of income generating. However, the power or capacity of commercial banks to create credit facilities is not infinite or limitless. It depends on many factors such as the reserve requirement of central bank, unable to collectability of loans, credit policy etc. Within these and other limits, commercial banks should lend their money to those who repay the principal, interest and service charges. For this reason proper credit management is a crucial issue in any commercial bank<sup>1</sup>.

The process of credit management begins with accurately assessing the credit-worthiness of the customer base. This is particularly important if the bank 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

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<sup>1</sup> [www.awash-international-bank.com](http://www.awash-international-bank.com) accessed on Jan 21, 2014

of the evaluation process, credit management also calls for determining the total credit line that will be extended to a given customer (Ibid).

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. This includes 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 to protect the vendor from possible losses, but also protect the customer from creating more debt obligations that cannot be settled in a timely manner.

Being the major income bearing line of business, credit keeps any commercial bank alive, placing it in a profitable venture. In addition, it plays the role of stimulating economic growth and alleviating poverty by promoting investment and savings. Therefore, this paper will study about credit management by taking Awash International Bank S.C. as a representative of the real world.

Banking history in Ethiopia goes back to February 15, 1906 which marked the beginning of banking in Ethiopia when the first Bank of Abyssinia was inaugurated by Emperor Menelik II. It was a private bank whose shares were sold in Addis Ababa, New York, Paris, London, and Vienna. One of the first projects financed by the bank was the Franco-Ethiopian Railway which reached Addis Ababa in 1917. In 1931, Emperor Haile Selassie introduced reforms into the banking system. The Bank of Abyssinia was liquidated and the newly established Bank of Ethiopia, a fully government-owned bank, took over management, staff and premises of the ceased bank. The Bank of

Ethiopia provided central and commercial banking services to the country (NBE, 2014)<sup>2</sup>. On April 15, 1943, the State Bank of Ethiopia became the central bank and was active until 1963. In December 1963, by the bank proclamation separated the National Bank of Ethiopia and Commercial Bank of Ethiopia come into existence. Moreover the bank proclamation allowed foreign banks to operate in Ethiopia limiting their maximum ownership to be 49 percent while the remaining shares were owned by Ethiopians. During the Empire Haile Selasse there were private banks (Ibid)

Following the economic policy change of 1991 the financial sector reform took place in 1994. Thus monetary and banking proclamation No 83/1994 and the licensing and supervision of banking business No 84/1994 laid down the legal basis for investment in the banking sector. Consequently at time of the proclamation the first private bank, Awash International Bank S.C was established in November 10, 1994 by 486 shareholders with an authorized and subscribed capital of Birr 50 million and 30 million respectively. It started operation through five branches in February 13, 1995. It was named after the popular river “Awash” which is the most utilized river in the country especially for irrigation and hydro electric power production. Awash River plays a pivotal role in the economic development of the country<sup>3</sup>.

The number of shareholders and paid-up capital increased continuously and currently reached over 3000 and birr 1.2 billion respectively.

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<sup>2</sup> <http://en.wikipedia.org/>

<sup>3</sup> [www.awash-international-bank.com](http://www.awash-international-bank.com) accessed on Jan 21, 2014

## **Statement of the Problem**

Commercial banks are the largest group of financial intermediaries, which play a major role in the business world by handling transaction that primarily deal with providing loans to business entities and individuals. As a means of earning their income, most banks provide credit service to various classes of customers and properly manage their credits. Credit management includes a number of activities ranging from credit investigation to sign of contract with borrowers, approval review, follow up, documentation, inspection recovery and written off. These activities require decision making skills. This can partly be developed though experience but partly it has to be learned externally.

The field of credit management is the critical activity that should be taken as a core point to meet the interest of the commercial bank and the need of borrowers. However, our pilot study shows that Awash International Banks face mainly the following problems: first and for most Awash International Bank customers has no practical experience of keeping proper financial records. This happened due to lack of reliable financial statements. As such, credit analysis on the basis of these statements lead to wrong decision. Therefore certain precaution must be taken to rectify the situation.

Secondly it takes time to respond to loan application in decision making. It also adds to fuel for money lent after the right time to be spent on unplanned purpose on the part of the customers. The remedy of to this failure is to use collateral position than project viability with lack of proper credit follow up system. These demands, the Banks to investigate their borrowers, the

practicality of their policies, procedures, and the method of evaluating the credit requests in respect with their collateral. Therefore, the main reason of this study was to assess the related problems in credit management mechanisms of Awash International Bank S.C in particular reference of Arada Giorgis Branch.

### **Research Question**

The proposed research seeks to investigate and answers the following specific questions concerned with credit management.

- What does the policies and procedures look like in credit granting decision of AIB?
- What are the major problems underlying in the credit management, before and after loan?
- What measures should be taken in order to give quality credit service in credit management of AIB?

### **Objective of the study**

#### **General Objective**

The main objective of the study is to assess the strengths and weaknesses of credit management system policies and procedures with its real practice at Awash International bank S.C.

#### **Specific Objective**

More specifically the objectives of the study are:

- To find out the main problems in connection with credit provision and collection.

- To examine the strength and weakness of the credit management system of AIB.
- To suggest possible solutions for underlying problems, in the credit management of the organization.

### **Delimitation of the study**

The research would be more comprehensive if it was conducted widely by including the credit management practices of other similar Banks. However, due to time and money constraints the study delimited itself to assess the problem only in one branch (Arada Giorgis) of Awash International Bank S.C credit department for the fiscal year of 2013/2014.

### **Significance of the study**

Experience shows that the awareness of using credit facilities is widely shown on banks and different financial institutions. On the other side, banks credit management show a poor credit management due to various reasons which was described in this research and the research team has realized that this topic is critical for both banks and their borrowers.

This study tries to, reasonably contribute the following comments:

- For the benefit of credit management of the case company, to shed light on the nature of the credit management problem and to propose the possible solutions to the problems.
- For other researchers, to use as a reference stone for a further studies on this matters.
- For other similar companies, to extend their frontiers of knowledge.

## **Limitation of the study**

In preparing this paper, the research team has faced problems like lack of information in certain aspects, time and finance constraints, to go through deeply all the activities of credit management and lack of transparency of the staff. As a result, only key management employees were interviewed, and a few key employees who were related to the credit operation and a few selected clients filled the questionnaires and only relevant documents were used.

## **Research Design and Methodology**

### **Research Design**

Descriptive research design was used to examine the credit extending and collection process of Awash International Bank S.C. Both qualitative and quantitative data type were collected from primary and secondary sources.

### **Population and Sampling Technique**

In selecting the sample respondents the research team has used both judgmental and stratified random sampling technique by grouping loan types in each sector. Judgmental sampling is used to select senior staffs from Arada Giorgis branch, credit analysts at head office and employees who are related with the study.

Types or classifications (based on the purpose of loan taken by borrowers, like Manufacturing production, domestic trade services, Export, Import, building & construction, personal loans and transport) of the loans have been distributed to the borrowers by using stratified random sampling method (A method of sampling that involves the division of a population into smaller groups known as strata. In stratified random sampling, the strata are formed based on members' shared attributes or characteristics. A random sample



from each stratum is taken in a number proportional to the stratum's size when compared to the population. These subsets of the strata are then pooled to form a random sample to get relevant information from all different types of loan users (borrowers).

### Sample size and Units

For the purpose of administering questionnaires, the respondents have been classified into two broad categories; staffs and clients (borrowers). A total of 14 staff respondents were selected purposively (1 Branch Manager, 1 Loan Officer, 5 Credit Analysts and 7 Engineers who have graduated in different engineering field like civil and mechanical who estimates any collateral in the market). And 82 client respondents were selected by determining the sample size 77% which is found using the formula of  $s = \frac{X^2 NP(1-P)}{d^2(N-1) + X^2 P(1-P)}$  of the target population (Arada Giorgis Branch borrowers) by using stratified random sampling method. The strata were the classification of the loans & Advances by sector. Thus the questionnaires were distributed as follows.

Table 1: Questionnaire Distributions of Sample Borrowers

Types of Loans & Advance	No. of borrowers (100%)	Sample size (77%)
Manufacturing Production	10 X 77%	8
Domestic Trade Services	29 X 77%	22
Export	8 X 77%	6
Import	23 X 77%	18
Building & construction	11 X 77%	8
Personal Loans	7 X 77%	5
Transport	20 X 77%	15
<b>Total</b>	<b>108</b>	<b>82</b>

NB: Data Gathered at Dec 25, 2013 in Arada Giyorgis Branch (from active borrowers for the fiscal year of July 1, 2013 to June 30, 2014)

### **Data Sources, Data Collection Methods and Data Analysis Tools**

In our study we collected both primary and secondary data. The primary data were collected through personal interview and close and open ended questionnaire and secondary data were collected from loan files, annual report and other documents that were related to the topic under study. Different types of descriptive and frequency counts with percentages were the method of data analysis that the research team used. Finally, the collected data was analyzed and interpreted using tables.

### **Data Presentation, Analysis and Interpretation**

#### **Back ground of customer respondents**

Table 2: Characteristics of customer familiarity with AIB

Criteria	< 1 year	1-3 years	4-6 years	7-9 Years	>9 years	Total
Customer familiarity with AIB	9	15	33	10	7	74

Characteristics of customer by loan and advance

<u>Types of loan &amp; Advance</u>	<u>No of Respondent</u>
Manufacturing	8
Domestic	19
Export	6

Import	16
Building & Construction	7
Personal	5
Transport	<u>13</u>
<b>Total</b>	<b>74</b>

### **Back ground of staff respondents**

Table 3: Work experience in AIB

Criteria	1-3 years	3-5 years	5-7 years	>7 years	Total
Work experience In AIB	2	3	8	1	14

Table 4: Educational back ground of staffs

Criteria	Diploma	BA	MA	PHD	Total
Educational background	-	13	1	-	14

### Characteristics of staff respondent work position

Branch Manager	1
Loan officer	1
Credit analyst	5
Engineer	<u>7</u>
<b>Total</b>	<b>14</b>

### **Questionnaires for customers of AIB**

The primary data used for this study were collected from two types of respondents: from AIB staff working on loan area and from Arada Giyorgis branch borrowers. These two groups were selected because their opinion

gathered through practical evidences is believed to be relevant and meaningful to for this study furthermore; Questionnaires were developed and distributed to borrowers selected from different loan categories. Respondents were made aware of the objective of the study so that they could give genuine and relevant information.

### **Attitude Questions in Credit Management Process**

82 questionnaires were developed and distributed to Arada Giyorgis Branch’s different types of loan borrowers and 74 were properly filled out and returned.

Table 5: Adequately granting of loans for the intended purposes

Item	Service	Freq.	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
1	AIB grants a loan adequately for the predetermined purpose	No.	33	21	4	16	74
		%	44	28	6	22	100

As can be seen from table 5 respondents were asked about their attitude for the statement whether AIB grants a loan adequately for the predetermined purpose. 44% strongly agreed, 28% agree, 6% disagree, 22% strongly disagree. These percentages implies that majority of the respondents agreed with the statement. However, according to the bank's objectives and current situation of the country, with regarded to private banks competition, the percentages agreed with the statements are not much because still 22% of the respondents strongly disagreed with the statement.

Table 6: Timely approval of requested loans

Item	Service	Freq.	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
2	The requested loan is approved timely	No.	33	33	8	-	74
		%	44	44	12	0	100

As can be seen from table 6 respondents were asked about their attitude whether the requested loan is approved timely statement, and 44% of respondents strongly agree, 44% agree, 12% disagree, none strongly disagree. This shows that the credit approval and granting decision of the bank is timely managed. The final decision as to whether the loan request should be approved or rejected is reached by comparing the statements made by the applicant with the information derived through the investigation process and by analyzing various credit factors, such as capacity, capital, collateral, track record for repayments and other.

Table 7: Consideration of Market value for collateral estimation

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
3	The collateral estimation considers the current market value	No.	4	21	16	33	74
		%	6	28	22	44	100

We can learn from table 7 that, 6% of respondents strongly agree, 28% agree, 22% disagree, 44% strongly disagree that market value is considered in estimating collaterals. This implies bank's estimation is not good. Thus, we can learn from the percentages that majority of the respondents strongly disagree with the statements. Though one of the credit evaluation criteria is

collateral it has to be given immense emphasis for inspection, valuation and estimation of the property. In this case the collateral should neither estimate the exaggerated nor the underestimated, because while exaggerating it maximizes the risk of the Bank and while underestimating it minimizes the risk of the Bank and there by offends the client. This implies that the client loses the ability to pay and on the other hand it increases the uncollectable loan of the bank's risk.

The collateral security a bank takes to back an advance is a cushion to fall back upon in case of need. But it is not always correct to presume that an advance should be granted purely on the basis of security offered. A bank would not ordinarily like to recover the advance from sale of the security, but from normal business sources otherwise the consequence might be scarce for the bank's future lending quality. The importance of adequate and acceptable security, however, cannot be ruled out.

Table 8: Convenience loan repayment schedule procedure

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
4	The loan repayment scheduling procedure is convenient	No.	24	50	-	-	74
		%	33	67	0	0	100

When we look through table 8 from the respondents 33% were found to be strongly agree, 67% agree. This implies that all of the respondents agreed with the statement which means the Bank loan repayment scheduling procedure are good and desired by customers.

Table 9: Friendly Credit follow-up system

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
5	AIB's credit follow-up system is friendly and encouraging to do business with the bank	No.	49	21	4	-	74
		%	66	28	6	0	100

As shown in table 9 respondents were asked about their attitude whether AIB's credit follow-up system is friendly and encouraging to do business with the bank. The finding shows that 66% of respondent strongly agree, 28% agree, 6% disagree. Almost all respondents agreed with the statements. This indicates that the Bank utilizes friendly follow-up system.

Table 10: Bank assistance for adverse effect of granted loans

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
6	If an adverse effect happened to repay the loan granted, the Bank helps the borrower aggressively	No.	21	42	7	4	74
		%	28	56	10	6	100

As we can learn from table 10 respondents were asked their attitude whether the Bank helps the borrower aggressively if an adverse effect happened to repay the loan granted, 28% of the respondents strongly agree, 56% agree, 10% disagree and 6% strongly disagree. Here also the majority of the respondents agree. However, there are still respondents who disagreed and

strongly disagreed with the statement even though the percentage is small. Thus, there is a little bit inconvenience procedure in terms of bank's assistance towards the non - performing loans.

Table 11: Grace period's procedure for new loans considers borrowers Paying Ability

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
7	AIB's grace period procedure for new loans recognize the Borrower's paying ability	No.	16	35	23	-	74
		%	22	47	31	0	100

As shown from table 11 respondents were asked to express their attitude towards AIB's grace period procedure on new loans recognize the Borrower's paying ability and 22% of the respondents strongly agree, 47% agree, 31% disagree and none one strongly disagree. We can observed from the percentage, majority of the respondents were agreed. However there are still large percentages of respondents which disagreed with the statement. It implies that the Bank's grace period doesn't perfectly consider the borrowers paying ability for the new business lines (credit beginners). This also might frustrate the new credit applicants for projects and new business lines. Similarly if the proper grace period is not arranged to the borrowers the loan may not be repayable and will categorized to undesired account (NPL) due to inappropriate time scheduling.



Lending is to extend credit facility of affecting an advance to business on the basis of certain rules, regulation and under prearranged set of conditions entered between the parties concerned; the bank and the borrower. Procedures are a series of steps followed in a regular definite order. Lending has its own disciplines that are to be strictly followed by all who deal with bank credit matter. Properly implemented procedures in a bank credit are good indicators for loans to be repaid without any problem. Step by step follow ups of procedures are the basis to a credit facility to be healthy throughout its term of repayment. (AIB's Credit Policy and Lending Principle, 2012).

Based on the above main points, respondents were asked to rate the following different Bank's Credit Management Services.

### **Attitude Questions in Credit Management Service**

Table 12: Borrowers attitude for bank's Credit Services Management

Item No.	Credit Service	Freq	Excellent	Very Good	Good	Fair	Poor	Very Poor	Total
1	Types of loan by the bank compared to the client's desire	No	4	22	28	8	8	4	74
		%	6	28	38	11	11	6	100
2	Handling of special mentioned loans	No	8	25	4	4	33	-	74
		%	11	33	6	6	44	-	100
3	Handling of doubtful loans	No	8	13	8	-	45	-	74
		%	11	17	11	-	61	-	100
4	Criteria and credit standards set by the bank	No	50	16	4	-	4	-	74
		%	66	22	6		6	-	100
5	Accessibility of staffs	No	70	-	4	-	-	-	74

	for borrowers discussion	%	94	-	6	-	-	-	100
6	Willingness of managers for borrowers discussion	No	58	8	8	-	-	-	74
		%	78	11	11	-	-	-	100
7	Technical/Professional advise	No	21	49	-	4	-	-	74
		%	28	66	-	6	-	-	100
8	Visiting customers business	No	4	8	4	4	12	42	74
		%	6	10	6	6	16	56	100
9	Reminding for repayments	No	33	33	4	4	-	-	74
		%	44	44	6	6	-	-	100
10	Recognizing good borrowers	No	8	12	4	4	30	16	74
		%	11	16	6	6	39	22	100
11	AIB grants a loan adequately for the predetermined purpose	No	62	9	3	-	-	-	74
		%	84	12	4	-	-	-	100

When we go through table 12 we can observe the following rates including their interpretation for different types of Credit Management;

**Item No. 1** Credit management is rated as 6% Excellent, 28% Very Good, 38% Good, 11% Fair, 11% Poor and 6% Very poor. Still 6% of the respondents ranked Very poor, meaning that the types of product (credit) are not much suitable for the borrowers. The bank should have to research for other new products based on the customers demand to increase customers satisfaction.

To address the credit of the business society banks have different classification of loans. However, each classification of the loan is granted to

deserving business, so as to match the need of the business to the type of facility. Though there are many, the major loan products (credit facilities) practiced in AIB are Manufacturing Production, Merchandising, Agriculture, Domestic and Trade Service, Import, Export, Transport, Building Construction and Personal (Consumption) loans.

**Item No. 2** Credit management is rated as 11% Excellent, 33% Very Good, 6% Good, 6% Fair, 44% Poor, no one rate this item as Very poor. Here large percentages of respondents rated item no.2 as poor, meaning they may not face a problem to pay back the loan granted.

**Item No. 3** Credit management is rated as 11% Excellent, 17% Very Good, 11% Good, none Fair, 61% Poor and none Very poor. Here the majority of the respondents are poor the service like Item No. 2. Both Special mentioned and doubtful loans should have to be handled tactfully before they are getting bad loans.

**Item No. 4** Credit management is rated as 66% Excellent, 22% Very Good, 6% Good, none Fair, 6% Poor and none Very poor. The percentages indicate that the Bank makes good communication with the borrowers. This motivates the client to borrow again and further to plan for other new business by doing with bank for their financial assistances.

**Item No. 5** Credit management is rated as 94% Excellent, 6% Good no one rate item no.5 as Very Good, Fair, Poor or Very poor. In these days of free competition it is the banker who has to go extra miles to please its customers and to make life easy for the customers in his/her dealings with the Bank. With this regard, the bank is doing properly as per the manual, almost all respondents ranked above Excellent.

**Item No. 6** Credit management is rated as 78% Excellent, 11% Very Good, 11% Good, none Fair, Poor and Very poor. Here we can observe that the bank managers are willing for borrowers' discussion.

**Item No. 7** Credit management is ranked as 28% Excellent, 66% Very Good, none Good, 6% Fair, none Poor and Very poor. Usually it is observed that either the borrower will come to the Bank seeking for a loan, or the Branch Manager initiates the customer to take out a loan for his business because a customer may not always know how to obtain credit from a Bank especially if he is a new one as a borrower or as a business man. The latter is usually emphasized. Accordingly, as the percentage shows the majority of respondents rated the service as very good and all are rated above fair which implies the Bank has emphasized to technical advises to its borrowers.

**Item No. 8** Credit management is rated as 6% Excellent, 10% Very Good, 6% Good, 6% Fair, 16% Poor, 56% Very poor. We can observe from the percentage majority of the respondents rated the service as very poor. It is remarkable, because it contradicts with the Bank's manual. If the borrower business is not visited regularly the granted amount might not be spent for the intended purposes.

Site visit is necessary for a more detailed business assessment. Site visits are useful: to become more familiar with the customers, to review changes that are taking place when customers have been granted a continuing line of credit, to review such changes when a significant new loan is to be considered, to assess the business in general a visit has to be arranged informal to witness the actual existence of inventory, work in progress finished goods and other relevant assessment, to witness the actual progress of the project from own and to get overview of the location and status of collateral proposed. (AIB's Credit Policy and Lending Principle, 2002)

**Item No. 9** Credit management is rated as 44% Excellent, 44% Very Good, 6% Good, 6% Fair, none Poor and Very poor. Here we can learn from the ranks almost all respondents ranked above fair meaning that the Bank strictly remind borrowers for repayment.

**Item No. 10** Credit management is rated as 11% Excellent, 16% Very Good, 6% Good, 6% Fair, 39% Poor, 22% Very poor. Large percentages rated poor and very poorly. The Bank should have to be keep its prominent credit record and award for those top performed; this encourages peoples to do more with the bank.

**Item No. 11** Credit management is rated as 84% Excellent, 12% Very Good, 4% Good, none Fair, Poor and Very poor.

### **Questionnaires for Credit Managements of AIB**

#### **Attitude Questions in Credit Management Process**

Fourteen questionnaires were developed and distributed to different credit management staffs at AIB and all of them were properly filled out and returned.

Table 13: Credit Management Policy is Practical and Effective

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
1	AIB's credit management policy is practical	No.	9	5	-	-	14
		%	67	33	-	-	100
2	AIB's credit management policy is effective	No.	9	5	-	-	14
		%	67	33	-	-	100

As can be seen from table 13 respondents were asked their attitude for the statement and 67% of the respondents strongly agree, 33% agree, none disagree and strongly disagree. These percentages implies that majority of the respondents agreed with AIB’s credit management policy practicality. Therefore there is no doubt for the practicality of the policy and procedure at AIB in the management perspective.

Although there is no hard and fast rule in the techniques of lending, which essentially is an art, it is however necessary that a defined procedure has to be followed by a banker to properly address the credit needs of its customers. AIB's customers must also have a feel of what the Bank's requirements are as regards to procedures and documentation necessary to obtain credit facility from the Bank. Besides, it is quite important that customers perceive the Bank as transparent and fair in its dealings and lending operation.

Table 14: Promotes its credit management effectively

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
3	AIB promotes its credit management program effectively	No.	6	5	3	-	14
		%	43	36	21	-	100

As can be seen from table 14 employees were asked their attitude for the statement that AIB promotes its credit management program effectively and 43% of respondents strongly agree, 36% agree, 21% disagree and none strongly disagreed. Here we observed that the credit management agrees the promotion of its credit management program.

The successful and quality management of a commercial bank's funds requires careful consideration and when a bank lends, it must be certain that the advances will be repaid. To this end, the character, capacity, capital and collateral of the borrower must be evaluated in advance. Character is important because it determines the borrower's willingness to repay the loan. The capital and capacity of the borrower to run his business successfully also determines the capabilities to repay. Collateral provides cushion against unfavorable events in the business.

Along with a written loan application, the following and other documents should be submitted as may be demanded by the Bank:

- ✚ Trade licenses, registration certificate, investment certificate from the appropriate ministry or bureau,
- ✚ Financial statements (preferably audited and reflecting the current year's position), including cash flow statement, especially if the borrower runs a sizable business.
- ✚ Feasibility study, where applicable (ordinarily for project loans extending beyond two years). This also calls for projected financial statements to judge whether the plans are financially viable or not.
- ✚ Memorandum and articles of association, where appropriate, and
- ✚ Other documents that may justify the need for the loan as may be required by the Bank on the merit of each application.

It is absolutely necessary that the branch manager requests the submission of all documents necessary to process the loan request.

Table 15: Developed a well defined system of screening customers

Item	Service	Freq	Strongly	Agree	Disagree	Strongly	Total
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			Agree			Disagree	
4	AIB has developed	No.	5	9	-	-	14
	a well defined system of screening applicants	%	33	67	-	-	100

Table 15 asked respondents whether the bank has developed a well defined system of screening customers and 33% of the respondents strongly agree, 67% agree, none disagree and strongly disagree. This indicates that identifying each client for credit needs is well defined by the bank and we can learn from the percentages majority of the respondents disagree with the statements. Despite the basic importance of the three key principles (Safety, liquidity and profitability), they are inherently conflicting, when viewed individually, because one cannot be achieved without sacrificing the others. Therefore, skilful balancing of these diverse objectives is always of prime importance. And other things that should be considered are Purpose of the loan, Diversification concerned with the industry, and security offered for the loan request.

Table 16: Convenience loan collection procedure

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
5	The loan collection procedure of AIB is convenient	No.	5	9	-	-	14
		%	34	66	-	-	100



When we look through table 16 for the statement 34% of the respondents strongly agree, 66% agree and none disagree and strongly disagree. This implies that all of the respondents are agreed with the statement which means the Bank loan collection procedure is good and desired by customers.

Table 17: Relevancy of credit information for managing loans

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
6	Collecting credit information is relevant for managing loan	No.	14	-	-	-	14
		%	100	-	-	-	100

The above Table shows respondents attitude with the statement 100% the credit management staff strongly agreed with the statement. Whether the applicant is new or not to the Bank, it is particularly necessary to obtain as much information as possible. Such information may usually be related to his honesty, ability, stability, managerial capacity, operational efficiency of the firm, financial history, etc. The information can be gathered from various sources, including banks, trade partners, suppliers and the like. Credit information from banks must be requested at the earliest possible time, while other lending formalities continue, to avert unnecessary delays in processing the loan application.

Credit information should be obtained on behalf of the customer spouse, mortgager, company and its general manager and major shareholders from credit information center maintained at National Bank of Ethiopia.

Table 18: Credit Granting Decision is Worthy

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
7	AIB's credit granting decision is worthy for customers	No.	6	8	-	-	-
		%	44	56	-	-	-

As shown in table 18 respondents were asked their attitude for the statement of " AIB's credit granting decision is worthy for customers" and 44% of them strongly agree, 56% agree, none disagree and strongly disagree. This is very interesting; almost all respondents agreed with the statements, it indicates that the Bank's credit decision is worthy.

Table 19: Management of credit authorization scheme is strong

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
8	The credit authorization scheme is strongly managed by AIB	No.	14	-	-	-	14
		%	100	-	-	-	100

As we can learn from table 19 respondent attitudes for the statement "The credit authorization scheme is strongly managed by AIB" 100% of the respondents strongly agree with the statement. As per the banks Lines of credit limit communication to ensure the timely dissemination of credit risk management policies and other credit risk management information to all bodies involved in the process, it has the following Discretionary Lending Limits of loan approval.

Management Party  
Limits (DLL)

Discretionary Lending

Board of directors .....	More than 18 million
President of Bank .....	500,000 up to 18 million
Head office loan committee beyond branch.....	30,000 up to 500,000
Branch Manager .....	< 30,000 Birr

Table 20: Significance of identifying potential customers for credit management

Item	Service	Freq	Strongly Agree	Agree	Disagree	Strongly Disagree	Total
9	Identification of potential customer is significant for proper credit management	No.	5	9	-	-	14
		%	33	67	-	-	100

As shown from table 20 respondents attitude for the statements 33% were found to be strongly agreed, 67% agree, none disagree and strongly disagree. We can observe from the percentage, majority of the respondents were agreed with its significance. Either the bank will go to the customer and initiates the customer to take loan for his business or the borrower will come to the bank seeking for a loan. Whichever is the case, we have to cheerfully greet our customer respectfully and explain in clear term to him/her the credit processes and alternatively listen to his side of query.

To assess the borrower’s credit needs. If branch Manager is not sure about loan requested, it is advisable to consult credit department and provided appropriate reply. During discussion one can obtain information such as his credit history with banks, purpose of loan required previous repayment habit

and more and it is necessary that a defined procedure has to be followed by a banker to properly address the credit needs of its customers.

### **Attitude Questions in Credit Management service**

Table 21: Credit staff attitude for bank's Credit Services Management

Item No.	Credit Service	Freq	Excellent	Very Good	Good	Fair	Poor	Very Poor	Total
1	Classification of the loan	No.	12	2	-	-	-	-	14
		%	89	11	-	-	-	-	100
2	Handling of special mentioned loans	No.	5	9	-	-	-	-	14
		%	33	67	-	-	-	-	100
3	Handling of doubtful loans	No.	3	11	-	-	-	-	14
		%	22	78	-	-	-	-	100
4	Criteria and credit standards set by bank	No.	8	5	1	-	-	-	14
		%	56	33	11	-	-	-	100
5	Accessibility of staffs for borrowers' discussion	No.	12	2	-	-	-	-	14
		%	89	11	-	-	-	-	100
6	Willingness of managers for borrowers discussion	No.	11	3	-	-	-	-	14
		%	78	22	-	-	-	-	100
7	Technical/Professional advise	No.	3	8	3	-	-	-	14
		%	22	56	22	-	-	-	100
8	Visiting customers business	No.	5	9	-	-	-	-	14
		%	33	67	-	-	-	-	100
9	Reminding for repayments	No.	11	3	-	-	-	-	14
		%	78	22	-	-	-	-	100

10	Recognizing good borrowers	No.	12	2	-	-	-	-	14
		%	89	11	-	-	-	-	100
11	AIB grants a loan adequately for the predetermined purpose	No.	8	6	-	-	-	-	14
		%	55	45	-	-	-	-	100

When we go through the above Table, we can observe the following rates including their interpretation for different types of Credit Management

**Item No. 1** Credit management is rated as 89% Excellent, 11% Very Good, and none for the rest. Means majority of the respondents rated Excellent for loan classifications.

**Item No. 2** Credit management is rated as 33% Excellent, 67% Very Good, and none for the rest. These means the bank strictly handles special mentioned loans. High NPLs are a sign of weaknesses in loan administration or it is a lack of good credit risk management. However, as lending is a risky business, an acceptable level of loss is always expected. Special mention loans are Loans & Advances within 1-3 months in arrears (no repayments were made for three consecutive months). (AIB's Credit Policy and Lending Principle, 2012)

**Item No. 3** Credit management is rated as 22% Excellent, 78% Very Good and none for the rest. Here the large percentages of respondents are agreed in handling doubtful loans (no repayments were made from four to six consecutive months).

**Item No. 4** Credit management is rated as 56% Excellent, 33% Very Good, 11% Good, none Fair, Poor and Very poor. Here also the majority of the

respondents agreed that criteria and credit standards set by the bank is excellent.

**Item No. 5** Credit management is rated as 89% Excellent, 11% Very Good and none for the rest. As we have seen on the clients' response the percentages indicate the Bank makes good communication with the borrowers. This motivates the client to borrow again and further to plan for other new business by doing with bank for their financial assistances.

**Item No. 6** Credit management is rated as 78% Excellent, 22% Very Good and none for the rest also, therefore we can observe that the bank managers are willing for borrowers' discussion.

**Item No. 7** Credit management is rated as 22% are Excellent, 56% Very Good, 22% Good, none Fair, Poor and Very poor. Here also we can observe that the bank managers give technical and professional advice for their customers.

**Item No. 8** Credit management is ranked 33% are Excellent, 67% Very Good and none for the rests. This percentage indicates that the management of AIB makes visit their businesses.

**Item No. 9** Credit management is rated as 78% are Excellent, 22% Very Good and none for the rest. Here we can learn from the ranks almost all respondents ranked above fair meaning that the Bank is strictly remind borrowers for repayment.

**Item No. 10** Credit management is rated as 89% are Excellent, 11% Very Good and none for the rest. The percentage indicates that the bank is recognizing its good borrowers' future good credit awareness on those clients.

**Item No. 11** Credit management is rated 55% are Excellent, 45% Very Good and none for the rest. The percentage indicates that customer of the bank is the loan adequately used for pre-determined purpose.

## **Conclusions and Recommendations**

### **Conclusions**

The following conclusions are raised based on the findings of the study

- In the credit facility request approval process, the manual doesn't include detail assessment and it is done in a conservative way. Though the credit approval process is said on time by borrower's respondents. In contrary said lengthy by staff personnel's. Obviously, the staff response is acceptable because it is practically justified. As per the discretionary lending limit all loan requests above Birr 30,000 go to head office credit department from all 120 Branches and wait their order for approval. These affect the quality of the service and dissatisfied loyal customers because one of the determinants factor of quality is time.
- Lowering the collateral value resulted in inadequate financing. This makes a borrower in shifting the loan for unintended purposes, also it create customers dissatisfaction.
- Though emphasizing on collateral for credit approval minimizes a bank's risk in case of an adverse effect, it doesn't give a chance for new idea promoters who don't have collateral. By the same token it affects innovation and development.
- Considering other factors rather than collateral like, Assessments of borrower's credit history, analysis of financial statement and repayment

capacity are essential. It allows the credit management decision to give a right credit, to the right borrower for the right purpose.

- In credit follow-up activities if the relationship between borrowers and the Bank is friendly and if the Bank remind borrowers to repay on time, the collection procedure will be smooth. This decreases Bank's NPL.
- If an adverse effect happens in borrowers business to pay back the loan and if the Bank doesn't aggressively support a borrower, it leads to non-performing loan.
- Irregular customer's business visiting is observed. This will lead the borrower to divert the granted loan for other purposes.
- The Bank doesn't give recognition for good borrowers. This discourages good borrowers to do more with the bank.
- Lack of proper financial statements submitted by borrowers affects the quality of credit process, analysis and decisions or recommendations of credit facilities.
- Even though credit policy and procedure is carefully formulated, it is highly general, centralized by top management less flexible and not up to dated. The Credit manual depict the Discretionary Lending Limits how much the decision is centralized and not flexible for a better credit Management.

### **Recommendations**

Based on the conclusions presented in above, the following suggestions are recommending to Awash International Bank S.C management and other concerned parties.

- AIB should make the credit policies and procedures in a clearly defined, flexible and timely way.



- The credit procedures should include detail assessment of criteria for each credit products. The loan request approval decision has to be done in a rational way and transparent with lower level of managements. The bank must try to upgrade the discretionary lending limit at all level thereby organizing a credit committee at branch level and up grading the branch manager limit to entertain the request within a branch.
- The Bank's engineer service should make comparable or market oriented estimation, by forming competent measurement of building evaluation factors to give reasonable property estimation services.
- Prioritization for feasibility study than collateral based, the bank should carefully investigate new borrowers loan request through their business plan (feasibility study) and to allow credit for new idea promoters, by strengthening Bank's project analysts to provide project loan widely.
- The Bank should support borrowers when an adverse effect happens on their credit by arranging recovery means like, re-rescheduling, extension of due dates and even allowing additional credit necessary to reinforce the borrower's capacity.
- The Bank should establish criteria that can effectively and regularly evaluate borrower's performance and based on the evaluation, borrowers should be given recognition. This should be done by providing customers day (Exporters, Importers day) and giving a prize for best performers in front of participants. It encourages doing more for the existing customers and also attracting others.
- To give quality service the bank should carefully investigate background of the borrower depending on the loan request. Unreliable sources like un-audited financial statement, while evaluating and selecting customers among applicants, will lead the bank in poor

selection of customers. This poor selection also has an impact on future collection of loan. So that, the bank should try maintain limitation of Birr, loan request to require an audited financial statements, which will alleviate this problem.

- Finally, AIB has to give due attention to the internal factors those affecting fast and timely decisions. Like hiring a necessary workforce for each level in the loan area starting from branch up to head office credit department and giving continuous credit operation training for the existing staffs to maximize their performance and to reduce shortage of human power. In addition hiring additional engineers for engineering department to get short appointment for customer's collateral inspection & estimation.

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