Internship Report

On

"The Relationship between Credit Risk Management and Financial Performance of Salaam Somali bank in Mogadishu-Somalia"

Supervised by

Prof. Dr. Mostafa Kamal
Faculty of Business and Economics
Daffodil International University

Pepared by

Hani Ahmed Iman
ID: 172-14-2399
Program: MBA
Major: Finance
Department of Business Administration
Faculty of Business and Economics
Daffodil International University

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LETTER OF TRANSMITTAL

Date: 19th May 2018

To: Dr. Mostafa Kamal

Professor

Department of Business Administration and

Department of Real Estate

Faculty of Business and Economics

Daffodil International University

Subject: - Submission of Thesis Paper

Dear Sir,

With due respect, I'm glad to summit my thesis paper entitled "The relationship between credit risk management and financial performance of salaam Somali bank in Mogadishu-Somalia" as a partial fulfillment of Master of Business Administration. It is an immense pleasure to complete this thesis within due time under your guidance and supervision. While conducting this research all instructions and guidelines were duly followed.

A sincere time was spent and all necessary effort was made to complete this research in a feasible and realistic way, with hope that this thesis will meet all the requirements and expectations.

Thank you

Yours Sincerely,

………………….

Hani Ahmed Iman

ID No : 172-14-2399

MBA Program (Finance)

Faculty of Business And Econmics

Daffodil International University

LETTER OF AUTHORIZATION

I hereby declare that this submission is my own work in completion of the program of Master of Business Administration, major in Finance, and that to the best of my knowledge, it's my work and it contains no material previously published by another person nor it has been accepted for the award of any other degree of the university, except where due acknowledgement has been made in the text.

Hani Ahmed Iman

ID: 172 – 14 - 2399

Signature ………….…..………

Date ………….….….…….……..…

LETTER OF ACCEPTANCE

I am very much pleased to certify that the thesis paper entitled "credit risk management and financial performance of salaam Somali bank in Mogadishu-Somalia**"** prepared by **Hani Ahmed Iman** ID No: **172-14-2399**, Department of Business Administration, Faculty of Business and Economics Daffodil International University under my supervision. The data and findings presented in this thesis paper seem to be authentic. Thus, the thesis paper has been approved for presentation.

I wish him every success in life.

……………………………………….

Date……………………………………………………………….

Dr. Mostafa Kamal

Professor**,** Department of Business Administration and

Advisor, Department of Real Estate

Faculty of Business and Economics

Daffodil International University

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ABSTRACT

The study sought to determine the relationship between credit risk management and the financial performance of salaam Somali bank Mogadishu-Somalia. And the study was conducted under three specific objectives which are; to know the relationship between client appraisal and financial performance in SSB, to evaluate the relationship between credit risk control and financial performance in SSB, to establish the relationship between credit collection practices and financial performance in SSB. The study adopted a correlational research design. The target population of study contained 113 staffs of Salaam Somali bank in different departments. And the sample size was 98 respondents. And Stratified sampling technique was used and Primary data was collected using questionnaires which were administered to the respondents by the researcher. And the data was analyzed by the means of descriptive statistics such as frequency and percentages and Pearson correlation was used to establish the relationship among the study variables. The correlations revealed that there is a moderate positive relationship between client appraisal and financial performance of Salaam Somali Bank($r = .431$, $P < 0.05$). And there is a strong positive relationship between credit risk control and financial performance of Salaam Somali Bank ($r = .641$, $P < 0.05$). And a strong positive relationship between credit collection practices and financial performance of Salaam Somali Bank ($r = .757$, $P < 0.05$). And the study recommends that there is need for Salaam Somali Bank to enhance its client appraisal, credit risk control and credit collection practices so as to improve its financial performance. Through client appraisal, credit risk control and credit collection practices the Salaam Somali bank managers may be able to know credit worth clients and thus reduce their non-performing loans and improve financial performance of the Bank. Further research is recommended on the effect of Credit policy on loan performance of salaam Somali bank. To see how the elements of credit policy influences and explains the loan performance of salaam Somali bank.

LIST OF ACRONYMS AND ABBREVIATIONS

REO	Return on equity
ROA	Return on asset
CVI	Content validity Index
SPSS	Statistical Package for Social Science
SSB	Salaam Somali Bank

TABLE OF CONTENT

LIST OF TABLES

CHAPTER ONE

1.0 Introduction

1.1 Background to the study

Credit risk management is a structured approach to managing uncertainties through risk assessment, developing strategies to manage it, and mitigation of risk using managerial resources. The strategies include transferring to another party, avoiding the risk, reducing the negative effects of the risk, and accepting some or all of the consequences of a particular risk. Some traditional risk managements focused on risk stemming from physical or legal causes such as natural disasters or fires, accidents, deaths and lawsuits (Huizinga &Demirgue, 2011).

Stoner (2003) as cited in Turyahebya (2013), defines financial performance as the ability to operate efficiently, profitably, survive, grow and react to the environmental opportunities and threats. . In agreement with this, Sollenberg and Anderson (1995) assert that, performance is measured by how efficient the enterprise is in use of resources in achieving its objectives.

Hempel (1994) focused on national banks that failed in the mid-1980s in the U.S.A found that the consistent element in the failures was the inadequacy of the bank's management system for controlling loan quality. It is strongly recommended that financial institutions should manage their credit risk to avoid exposing their organization to unnecessarily high levels of risk and subsequently a decline in returns.

Felix and Claudine (2008) investigated the relationship between bank performance and credit risk management. It could be inferred from their findings that return on equity (ROE) and return on assets (ROA) both measuring profitability were inversely related to the ratio of non-performing loan to total loan of financial institutions thereby leading to a decline in profitability.

In their study ‘Credit Risk management and Profitability in Commercial Banks in Sweden’ Juanjuann et al (2009) highlighted that credit risk management has effect on financial performance of the institution in order words on the profitability. The analysis further indicated that the impact of credit risk management on the financial performance is not the same of all commercial banks sampled. Further the results of the study were limited to banks sampled and were not generalized for all the commercial banks in Sweden.

According to Prakash and Poudel (2012) also state that credit risk management is an important predictor of bank financial performance. Thus success of bank financial performance depends on effectiveness of credit risk management which increases the bank growth.

Kurawa and Garba (2014) revealed that the credit risk management affects the banks financial performance. And their research improved on some of the existing studies, and investigated the overall effect of credit risk management and its indicators on financial performance of Jordanian commercial banks using certain individual indicators of credit risk management. Nawaz and Munir (2012) found that credit risk management effected on the banks’ financial performance and profitability, and they recommended that management should be cautious in setting up a credit policy that might not negatively affect profitability.

Kargi (2011) evaluated the relationship between credit risk management and financial performance of Nigerian banks. Financial ratios as measures of bank performance and credit risk were collected from the annual reports and accounts of sampled banks from 2004-2008 and analyzed using descriptive, correlation and regression techniques. The findings revealed that credit risk management has a significant impact on financial performance of Nigerian banks. It concluded that banks' profitability is inversely influenced by the levels of loans and advances, non-performing loans and deposits thereby exposing them to great risk of illiquidity and distress.

Kithinji (2010) assessed the effect of credit risk management on the profitability of commercial banks in Kenya. Data on the amount of credit, level of non-performing loans and profits were collected for the period 2004 to 2008. The findings revealed that the bulk of the profits of commercial banks are not influenced by the amount of credit and non-performing loans, therefore suggesting that other variables other than credit and non-performing loans impact on profits.

1.2 Salam Somali Bank

About Salam Somali Bank

Salaam Somali bank was established in October 2009 to answer the need for the community towards banking.

The banking sector in Somalia is showing a significant paradigm shift away from traditional means of money transfer. Salaam Somali Bank (SSB) bears the critical responsibility of leading the way forward in establishing a stable and dynamic banking system replete with dynamic and cutting-edge products and services.

SSB was established in October 2009 to answer to this need. Whether you are an individual or institutional client, SSB is there to help you as a partner in your success. It is committed to providing the highest level of personalized banking services. SSB promises to offer customized solutions that meet the unique needs of their clients through the right combination of traditional banking services and special features for the Somali community. Ultimately, SSB strive to make your success simple.

SSB believe in adding value to the customers' lives and business through dynamic and competitive products and services that fulfill their needs while conforming completely to the dictates of international standards. Run by a team of dedicated professionals you can rest assured that your finances are well taken care of.

1.3 Statement of the Problem

Credit risk management is essential for a financial institution's stability and continuing profitability, while failing credit quality is the most frequent cause of poor financial performance and the success of financial institutions largely depend on the effectiveness of their credit risk management systems because the institutions generate most of their income from interest and profit earned on loans extended to small and medium entrepreneurs (Scheufler, 2002).

Salaam Somali bank had established and implemented a credit risk management strategies to ensure that the credit management is efficient and effective in order to improve the bank's financial performance and avoid credit risks such as delays on collecting cash from debtors as they fall due which has serious financial problems. Despite all the efforts, to improve efficiency and effectiveness of the bank financial performance, there is a poor financial performance faced by the bank which affected the liquidity position of the bank, and there is a suspect that this poor financial performance caused by poor credit risk management (annual financial performance report 2015). And credit risk is the biggest threat to any bank financial performance which finally will cause bank failure. Therefore this study is aimed to explain the relationship between credit risk management and financial performance of salaam Somali bank.

1.4 Objective of the study

General objective

The objective of this study is to examine the relationship between credit risk management and financial performance of salaam Somali bank Mogadishu- Somalia.

Specific objectives

i. To examine the relationship between client appraisal and financial performance.

ii. To evaluate the relationship between credit risk control and financial performance.

iii. To establish the relationship between credit collection practices and financial performance.

1.5 Research Questions

i. What is the relationship between client appraisal and financial performance?.

ii. What is the relationship between credit risk control and financial performance?

iii. What the relationship between credit collection practices and financial performance?

1.6 Hypothesis

i. There is no statistically significant relationship between client appraisal and financial performance.

ii. There is no statistically significant relationship between credit risk control and financial performance.

iii. There is no statistically significant relationship between credit collection practices and financial performance.

1.7 Scope of the study

1.7.1 Content scope

The study investigated the relationship between credit risk management and the financial performance of salaam Somali bank. Credit risk management involved Client appraisal, Credit risk control and Credit collection practices to find out how these elements relate and contribute the financial performance of Salaam Somali bank, Mogadishu, Somalia.

1.7.2 Geographical scope

The study was carried out in Mogadishu-Somalia and concerned the Salaam Somali bank to investigate the relationship between credit risk management and financial performance of salaam Somali bank.

1.7.3 Time scope

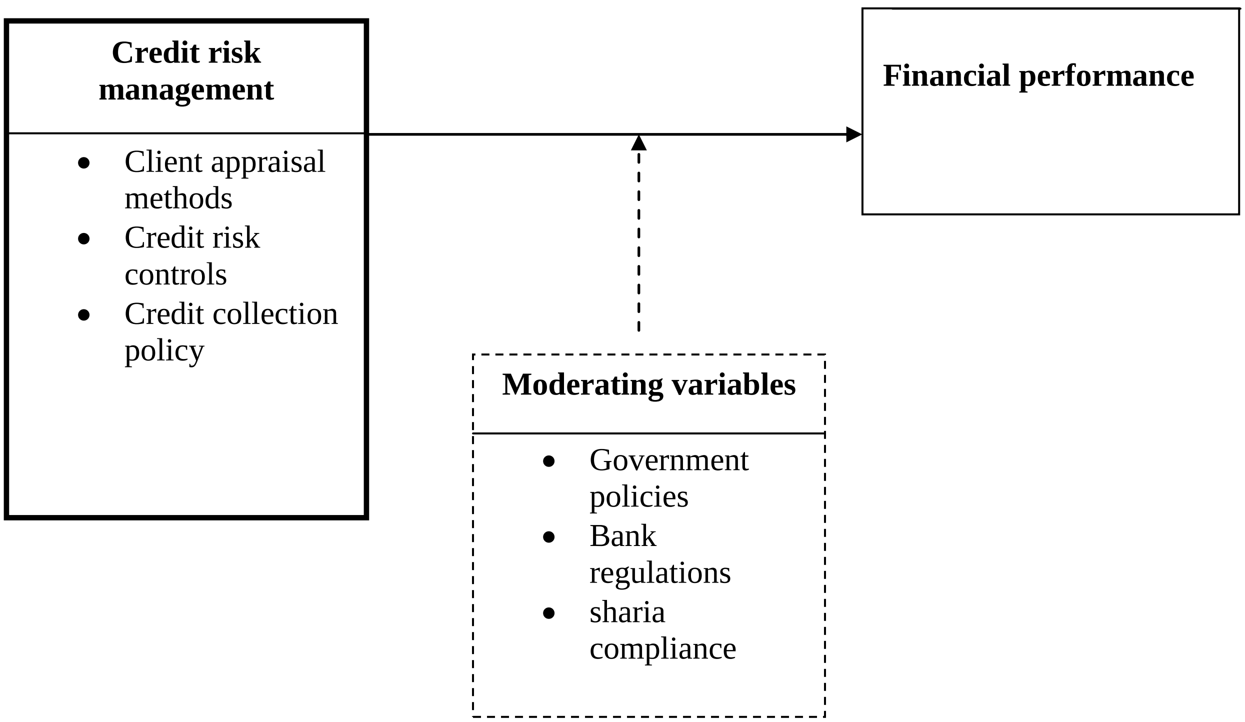
The study was limited to the period January to May.

1.8 Significance of the study

This study may be useful in the following ways; first, since the study identified how credit risk management affects the financial performance for salaam Somali. Thus, it may help a bank management to mitigate credit risk to maximize the shareholders' wealth as well to meet the shareholders' expectations. And also the study may be beneficial to the regulators and policy makers and provide the basis for regulatory policy framework to mitigate the financial system from financial crises and to better appreciate and quantify those credit risk exposures. The study may also be useful to the investors and help them to understand the factors that influence the returns on their investments. Finally the study may be beneficial to the commercial banks and provides an insight into the credit risk attributes which may need to be incorporated in their investment decision process

1.9 Conceptual Framework

Independent Variable **Dependent Variable**



*Source:*Kurawa and Garba (2014) as modified by the researcher.

The conceptual framework shows that the credit risk management influences the Financial Performance of Salaam Somali bank. In this framework, credit risk management is taken to involve client appraisal methods, credit risk controls and credit collection policy while Financial Performance involves the return on investment, liquidity and profitability. The figure hypothesizes that all methods of credit risk management (client appraisal methods, credit risk control and credit collection policy) have a relationship with Financial Performance of salaam Somali bank Mogadishu Somalia. However, the conceptual framework further describes that the moderating variables may hold back this relationship.

1.10 Operational definitions

Credit risk management: is a structured approach to managing uncertainties through risk assessment, developing strategies to manage it, and mitigation of risk using managerial resources (Demirgue, 2011).

Financial performance: is the ability to operate efficiently, profitably, survive, grow and react to the environmental opportunities and threats, (Stoner,2003) as cited in Turyahebya (2013).

Client appraisal: is an application and request for funds, evaluated by financial institution in order to assess the purpose of the client, need genuineness and repayment capacity of the borrower (Boldizzoni, 2008).

Credit risk control: is a procedure aimed to ensure that credit risk management is effectively practiced by banks (Javid, 2009).

Credit collection practice: is a systematic way required to recover the past due amount from clients within the lawful jurisdiction losses (Kariuki, 2010).

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter focuses on reviews of literature in relation to the credit risk management, and how it effects on business financial performance. And the review is conducted under the objective of the study and also this chapter identified the literature gab which this study fills.

2.1 The relationship between client appraisal and Financial Performance

Client appraisal is a procedure of evaluation of customer request for funds by financial institution. The aspects to be focused in appraisal includes: purpose of the client, need genuineness, repayment capacity of the borrower, quantum of loan and security. Loan appraisal plays important role to keep the loan losses to minimum level, hence if those officers appointed for loan appraisal are competent then there would be high chances of lending money to non-deserving customers (Boldizzoni, 2008).

Microfinance Institutions and other finance institutions must develop a credit policy to govern their credit management operations (Pandey, 2008) and since microfinance institutions generate their revenue from credit extended to low income individuals in the form of interest charged on the funds granted and the loan repayments may be uncertain (Pandey, 2008).

The success of lending out credit depends on the methodology applied to evaluate and to award the credit and therefore the credit decision should be based on a thorough evaluation of the risk conditions of the lending and the characteristics of the borrower (Ditcher, 2003). Numerous approaches have been developed in client appraisal process by financial institutions. They range from relatively simple methods, such as the use of subjective or informal approaches, to fairly complex ones, such as the use of computerized simulation models (Horne, 2007). Many lending decisions by Microfinance institutions are frequently based on their subjective feelings about the risk in relation to expected repayment by the borrower. Microfinance institutions commonly use this approach because it is both simple and inexpensive (Horne, 2007).

Client appraisal can be used to enhance loan performance; the first step in limiting credit risk involves screening clients to ensure that they have the willingness and ability to repay a loan. Microfinance Institutions use the 5Cs model of credit to evaluate a customer as a potential borrower so as to improve financial performance (Abedi, 2000).The 5Cs help microfinance institutions to increase loan performance, as they get to know their customers better. These 5Cs are: character, capacity, collateral, capital and condition.

Character - refers to the trustworthiness and integrity of the business owners, it is an indication of the applicant's willingness to repay and ability to run the enterprise. Character is the borrower's attitude towards credit obligation. Most credit managers considers character as the most important factor in predicting whether loan repayment will be made timely and ultimately. Character basically is a tool that provides weighting values for various characteristics of a credit applicant and the total weighted score of the applicant is used to estimate his credit worthiness.

Capacity- assesses whether the cash flow of the business (or household) can service loan repayments. Capacity is the borrower's ability to meet credit obligation. That is to make regular loan payment as scheduled in the credit agreement. The borrower's income and expenses are considered before credit approval.

Capital - Assets and liabilities of the business or household**.** Capital is also the borrower's assets or net worth. Generally the greater the capital, the greater the ability to repay a loan.

According to Weston and Eugene (1966), Capital is measured by the general financial position of the borrower as indicated by a financial ratio analysis, with special emphasis on tangible net worth of the borrower's business. Thus, capital is the money a borrower has personally invested in the business and is an indication of how much the borrower has at risk should the business fail.

Collateral -Access to an asset that the applicant is willing to cede in case of non-payment, or a guarantee by a respected person to repay a loan in default. Collateral is an asset that is used to pledge to obtain a loan. The asset is taken over if the borrower fails to honor the terms of agreement.

Conditions-A business plan that considers the level of competition and the market for the product or service, and the legal and economic environment. Conditions means the general economic conditions that can affect the ability to repay a loan. The questions focus on security of both the job and the firm that employs the borrower.

The 5Cs need to be included in the credit scoring model. The credit scoring model is a classification procedure in which data collected from application forms for new or extended credit line are used to assign credit applicants to good or bad credit risk classes (Constantinescu et al., 2010). Inkumbi (2009) notes that capital (equity contributions) and collateral (the security required by lenders) as major stumbling blocks for entrepreneurs trying to access capital. This is especially true for young entrepreneurs or entrepreneurs with no money to invest as equity; or with no assets they can offer as security for a loan. Any effort to improve access to finance has to address the challenges related to access to capital and collateral. One way to guarantee the recovery of loaned money is to take some sort of collateral on a loan. This is a straightforward way of dealing with the aspect of securing depositors' funds.

2.2 The relationship between Credit Risk Control and Financial Performance

Credit risk is an investor's risk of loss arising from a borrower who does not make payments as promised. Such an event is called a default. Another term for credit risk is default risk. Investor losses include lost principal and interest, decreased cash flow, and increased collection costs. Credit risk can be mitigated using credit risk controls, such as based pricing, covenants, credit insurance, tightening and diversification (Ross et al, 2008).

Credit risk control is a procedure aimed to ensure that credit risk management is effectively practiced by banks (Javid, 2009). Effective credit risk management involves the execution of a reporting and review structure to ensure that risks are properly identified and assessed as well as that appropriate control and responses are consequently put in place (ALARM, 2002).

The purpose of credit risk monitoring and control is to provide appropriate checks and balances to ensure that credits are made in accordance with bank policy and to provide an independent judgment of asset quality, uninfluenced by relationships with the borrower.

Effective credit risk monitoring and control not only helps to detect poorly underwritten credits, but also helps prevent weak credits from being granted, since credit officers are likely to be more diligent if they know their work will be subject to review. A common and very important problem among troubled banks in the early 1990s was their failure to monitor borrowers or collateral values. Many banks neglected to obtain periodic financial information from borrowers or real estate appraisals in order to evaluate the quality of loans on their books and the adequacy of collateral. As a result, many banks failed to recognize early signs that asset quality was deteriorating and missed opportunities to work with borrowers to stem their financial deterioration and to protect the bank's position. This lack of monitoring led to a costly process by senior management to determine the dimension and severity of the problem loans and resulted in large losses (WOCCU, 2011).

In the recent years, credit risk gained focal importance because of huge financial losses faced by big international financial organizations (Nikolaidou&Vogiazas, 2014). Since the financial crisis, financial organizations particularly commercial banking sector have taken special credit risk control measures to mitigate any forthcoming financial losses caused by mismanagement in loan allocations and credit recoveries. Credit risk control offers a viable solution to such challenges. Today, credit risk management constitutes a critical component of a comprehensive approach to risk management in banking sector (Arora& Kumar, 2014).

In some cases, the failure to perform adequate due diligence and financial analysis and to monitor the borrower can result in a breakdown of controls to detect credit-related challenges. For example, banks experiencing fraud-related losses have neglected to inspect collateral, such as goods in a warehouse or on a showroom floor, have not authenticated or valued financial assets presented as collateral, or have not required audited financial statements and carefully analyzed them. An effective credit review department and independent collateral appraisals are important protective measures, especially to ensure that credit officers and other insiders are not colluding with borrowers (Njoku, 2012). In addition to shortcomings in due diligence and credit analysis, bank credit problems reflect other recurring problems in credit-granting decisions. Some banks analyze credits and decide on appropriate non-price credit terms, but do not use risk-sensitive pricing. Banks that lack a sound pricing methodology and the discipline to follow consistently such a methodology will tend to attract a disproportionate share of under-priced risks. These banks will be increasingly disadvantaged relative to banks that have superior pricing skills (Anam et.al2012).

According to Basel committee (1999) on the management of credit risk, the following was observed:

Many credit problems reveal basic weaknesses in the credit granting and monitoring processes. While shortcomings in underwriting and management of market-related credit exposures represent important sources of losses at banks, many credit problems would have been avoided or mitigated by a strong credit control process. They noted too that many banks find carrying out a thorough credit assessment (or basic due diligence) a substantial challenge. For traditional bank lending, competitive pressures and the growth of loan syndication techniques create time constraints that interfere with basic due diligence. Globalization of credit markets increases the need for financial information based on sound accounting standards and timely macroeconomic and flow of funds data. When this information is not available or reliable, banks may dispense with financial and economic analysis and support credit decisions with simple indicators of credit quality, especially if they perceive a need to gain a competitive foothold in a rapidly growing foreign market. Finally, banks may need new types of information, such as credit risk measurements, and more frequent financial information, to assess relatively newer counterparties, such as institutional investors and highly leveraged institutions.

Proper credit risk control practices can be used to ensure that credit risk management practices which help the banks' management to uncover mistakes at an early stage are in place (Al-Tamimi, 2007). Moreover, it was discovered by the same study that there are significant differences between the conventional and Sharia compliant banks as far as credit risk monitoring and control is concerned. Pausenberger and Nassauer, (2002) are of the view that various controls have to be established at different levels since the control by the management board alone is insufficient to ensure the effective functioning of the credit risk control system. This is because the management board members do not have sufficient time to exercise extensive controls on the organization. Hence, the management board should appoint an independent unit which is responsible for internal supervision (Scholtens, 2013).

The main function of the risk manager is to monitor; measure and control credit risk. The Risk Manager's duty includes identification of possible events or future changes that could have a negative impact on the institution's credit portfolio and the bank's ability to withstand the changes. The areas to examine critically are: Economic or industry changes, Market risk events and Liquidity conditions. Effective credit risk management requires a reporting and review structure to ensure that credit risks are effectively identified and assessed and that appropriate controls and responses are in place, and credit risk control is the last step in the corporate credit risk management process (Pausenberger and Nassauer, 2002).

According to Parrenas, (2005) the shareholders of the institutions can use their rights to demand information in order to judge the efficiency of the risk management system. The director's report enables the shareholders to assess the status of the corporation knowledgeably and thoroughly.

Khan and Ahmad (2001) conducted a survey of credit risk management practices and found that there is direct relationship between UAE national and foreign banks financial performance and credit risk monitoring and control. Also, the UAE commercial banks have an efficient credit risk monitoring and controlling system and it has positive influence on risk management practices and profitability of the banks. Previous studies have noted that high credit risk controls (CRC) result in low chances of defaults and improve financial performance (Ross et al., 2008). Therefore, credit risk could be alleviated by utilizing danger based evaluating, contracts, credit protection, tightening and broadening (Ross et al., 2008).

Moti et al (2012) argue that intelligent and effective credit risk control is a key requirement for effective credit management and financial performance. Furthermore, to minimize the risk of bad debt and over-reserving, banks ought to have greater insight into important factors like, customer financial strength, credit score history and changing payment patterns (Moti et al., 2012).

According to (Churchill and Coster, 2001) Key Credit risk controls include loan product design, credit committees, and delinquency management.

Loan Product Design

Microfinance institutions can mitigate a significant portion of default risk by designing loan products that meet client needs. Loan product features include the loan size, interest rate and fees, repayment schedule, collateral requirements and any other special terms. Loan products should be designed to address the specific purpose for which the loan is intended.

Credit Committees

Establishing a committee of persons to make decisions regarding loans is an essential control in reducing credit (and fraud) risk. If an individual has the power to decide who will receive loans, which loans will be written off or rescheduled, and the conditions of the loans, this power can easily be abused and covered up. While loan officers can serve on the credit committee, at least one other individual with greater authority should also be involved. The credit committee has the responsibility not only for approving loans, but also for monitoring their progress and, should borrowers have repayment problems, getting involved in delinquency management.

Delinquency Management

To minimize such delinquency Micro-finance institutions can use the following delinquency management methods Institutional Culture: A critical delinquency management method involves cultivating an institutional culture that embraces zero tolerance of arrears and immediate follow up on all late payments. Micro-finance institutions can also remind clients who have had recent delinquency problems that their repayment day is approaching.

Client Orientation

A logical first step toward developing a zero-tolerance institutional culture is to communicate the clients about the credit, to each new client before he or she receives a loan.

Staff Incentives

Creating staff involvement in discouraging delinquency, through a staff incentives system, can be effective. Delinquency Penalties: Clients should be penalized for late payment. This could include delinquency fees pegged to the number of days late and limiting access to repeat loans based on repayment performance.

Loan Rescheduling

Given the vulnerability of the target market, it is common for borrowers to be willing but unable to repay. After carefully determining that this is indeed the case it may be appropriate to reschedule a limited number of loans. Only done under extreme circumstances, this may involve extending the loan term and/or reducing the installment size.

2.3 The relationship between Credit collection Practices and Financial Performance

There are various policies that an organization should put in place to ensure that credit management is done effectively; one of these policies is a collection policy which is needed because all customers do not pay the firms bills in time. Some customers are slow payers while some are non-payers. The collection effort should, therefore aim at accelerating collections from slow payers and reducing bad debt losses (Kariuki, 2010).

McNaughton (2008) defines a collection policy as the procedure an institution follows to collect past due account. Collection policy refers to the procedures micro finance institutions use to collect due accounts. The collection process can be rather expensive in terms of both product expenditure and lost good will (Brighan, 2010).

Collection efforts may include attaching mandatory savings forcing guarantors to pay, attaching collateral assets, courts litigation (Myers, 2011).). Methods used by Micro finance institutions could include letters, demand letters, telephone calls, visits by the firm’s officials for face to face reminders to pay and legal enforcements. Dickerson et al, (1995) asserts that collection policy is a guide that ensures prompt payment and regular collections. The rationale is that not all clients meet their obligations, some just take it for granted, others simply forget while others just don’t have a culture of paying until persuaded to do so. According to Myers (2011) many micro finance institutions may send a letter to such individuals (borrowers) when say ten days elapse or phone calls and if payment is not received with in thirty days, it may turn over the account to a collection agency.

The credit collection policies adopted by microfinance institution had an effect on financial performance, stringent policy had a great impact on loan performance, and the lenient policy had an effect but was not as great as that of stringent policy (Kosmidou, 2008).

Credit collection policy is a systematic way required to recover the past due amount from clients within the lawful jurisdiction. The collection aspects may vary from institution but those should be complaint to existing laws such as third party collection agencies may involve in a collection process. It does not just involve in collection procedure details provided by the institution but also the procedure in which the lawful collection takes place (Latifee, 2006). Well administered collection is needed for better performance of the loan and financial performance. If financial institutions do not follow well administered collection procedures, this would results in loan defaults (Boldizzoni, 2008).

Credit Collection policy is required because some clients do not pay the loan in time some are slower while others never pay. Thus collection efforts aim at accelerating collections from slower payers to avoid bad debts. Prompt payments are aimed at increasing turn over while keeping low and bad debts within limits (Pandey, 1995).

Semukono, (2009) states that collection efforts are directed at accelerating recovery from slow payers and decreases bad debts losses .This therefore calls for vigorous collection efforts .The yardstick to measurement of the effectiveness of the collection policy is its slackness in arousing slow paying customers.According to Dawkin (2010) posited that prompt payments aimed at increasing turnover and keeping bad debts low. Collection efforts are directed at accelerating recovery from slow payers and decreases bad debt losses and increases profitability of the banking institution.

Previous studies indicated that microfinance institutions need to have strong and effective credit collection policies for ensuring consistent recoveries from clients (Frank et al., 2014).

For microfinance institutions, the main source of income is the credit, which is why they need to have strong policies for credit risk management. The advance reimbursements may be questionable and the accomplishment of giving out credit relies on the philosophy connected to assess and to grant the credit (Moti et al., 2012).

Firms that are efficient in credit risk management determine their optimal credit, which minimizes the total costs of granting credit and observed that An increase in the level of accounts receivables in a firm increases both the fund and the costs of holding and managing accounts receivables and both lead to a decrease in the value of the firm and financial performance. (Ross2008).

Studies by Lazaridis and Dimitrios (2005) found that firms who pursue increase in credit management to an optimal level increase their profitability.

Juan &Martinez (2002) emphasized that firms can create value by reducing their number of days of accounts receivable, thus confirmed the finding of Deloof (2003) who established that the length of credit collection period has a negative effect on a firm's financial performance and also affirmed that, putting in place a sound credit policy ensures proper debt collection procedures and is pivotal in improving efficiency in receivables management hence the performance of firms

According to Van Horne (1995) the firm's credit collection policies are the chief influences on the level of debtors, measuring the manager's position to invest optimally in its debtors and be able to trade profitably with increased revenue. And good credit collection policy will be able to maximize its investment revenue in debtors and this improves and promotes its financial standing and performance therefore a good credit policy decision is positively related to high financial performance.

2.4 Conclusion

The several literature reviews have expressed the relationship between credit risk management and financial performance in different context. And their studies related to specific population to the specific place and they provided different results on their studies toward the effect of credit risk management on firm's financial performance. However, the researcher did not find any previous studies and literature about the credit risk management and financial performance that have conducted in Somalia. And it's useful to investigate and find out the importance of credit risk management and its relationship with financial performance .And this study aimed investigate the relationship between credit risk management and financial performance of Salaam Somali Bank in the context of Mogadishu Somalia.

CHAPTER THREE

METHODOLOGY

3.0 Introduction

This chapter discusses the methodology of the study. The chapter was organized into four main parts. The First section presents research design method, while the second section focuses on research population including sample size and sampling procedure. The third section provides research instrument with the validity and reliability of the instrument. The Fourth section is discussing data analysis of the study.

3.1 Research Design

A correlational research design was used to establish the relationship between methods of credit risk management and financial performance of Salaam Somali bank Mogadishu-Somalia. Correlational studies aim at establishing whether an association exists between two or more variables (Keitany, 2000).

3.2 Study Population

The target population of the study consisted of the employees and management of the different department of salaam Somali bank branches in Mogadishu-Somalia. And the number of target population of the research was 113 employees. However, the researcher selected the respondents from the eight branches of salaam bank in Mogadishu Somalia.

3.3 Sample size

The sample size of the study was 98 respondents from all eight different branches of Salaam bank in Mogadishu Somalia. From the target population of 113 including top managers, accounting department, credit department and investment department. The sample of 98 respondents was selected based on a table of determining sample size by (Krejcie and Morgan, 1970). This table below shows the structure of the study population, sample size.

Table 3.1: Structure of the study population, sample size and sampling techniques

Category	Population	Sample	Sampling techniques
Top Managers	6	6	Census
Accounting department	42	36	Stratified sampling
Credit department	28	24	Stratified sampling
Investment department	37	32	Stratified sampling
Total	**113**	**98**	

3.4 Research Instrument

Research instrument is defined as the tools to be used for collecting data and how those tools are developed. The most common instruments for data collecting in educational research are questionnaires, interviews, observation, and document analysis (Soundrs et al, 2009). However, the researcher of this study used questionnaire instrument as main tool for collection data

3.5 Validity of the Instrument

Validity refers to the extent to which data collection method accurately measures what it was intended to measure (Oso&Onen, 2008). In this study, validity of the instrument was measured and calculated using the formula; CVI = (n / N) 100.

Where: n =items rated relevant (39) and N=Total numbers of items (42). In this case, a CVI of 92% was determined which implies that the instrument was valid as suggested by Amin (2005).

3.6 Reliability of the Instrument

Joppe (2000) defines reliability as the extent to which results are consistent over time and an accurate representation of the total population under study is referred to as reliability. Cronbanch's alpha for each value was established by the SPSS application and gauged against each other at a cut off value of 0.7 which is acceptable according to Cooper and Schindler (2008). According to table 3.2 all the values were above 0.7 which concludes that the data collection instrument was reliable.

Table 3.2: Reliability Coefficients

Cronbach's Alpha	N of Items
.855	39

Source: Primary data.

The researcher has measured the reliability of the four variable of the study, which are client appraisal, credit risk control, credit collection policy and financial performance. The Cronbach's Alpha of the client appraisal was 0.904, credit risk control 0.801, collection policy 0.904 and financial performance was 0.922. Therefore the Cronbach's Alpha Coefficient was above 0.7 and hence the scales used to measure the study variables were consistent and therefore reliable.

3.7 Data processing and analysis

Data processing involves translating the answers on a questionnaire into a form that can be manipulated to produce statistics. This involves coding, editing, data entry, and monitoring the whole data processing procedure. The data that was collected through questionnaires was tabulated and analyzed using the Statistical Package for the Social Sciences (SPSS) software package and the Respondents' responses were rated on a five Likert scale. Before processing the responses, the completed questionnaires were edited for completeness and consistency. The data was coded to enable the responses to be grouped into various categories. The study was used correlation to measure the relationship between credit risk management and financial performance of Salaam Somali Bank. And regression analysis was used to determine the contribution of credit risk management to the financial performance. The findings were presented using tables and percentages. Tables were used to summarize responses to facilitate comparison.

3.8 LIMITATION OF THE STUDY

This course of study has many limitations which may affected researchers across on its research procedure such limitations include: research instrument this study were used a questionnaire only rather than questionnaire with interview and other limitation of this study is that it adopted a questionnaire that had taken a time to make modifications. The geographical scope, the study limited only in Mogadishu, the study will be restricted to only a sample of 100 respondents of all small and medium business low level employees in Mogadishu and as well as limitation of the population, Potential researchers are expected to cover large samples in the future research.

CHAPTER FOUR

DISCUSSIONS AND FINDINGS

4.0 Introduction

This chapter involves the Presentation, Analysis and Interpretation of data collected from the respondents on issues regarding the relationship between credit risk management and financial performance for salaam Somali bank Mogadishu- Somalia. The data has been analyzed and presented according to the research objectives and hypothesis of the study. In the presentation of findings, tables and figures are constructed using frequencies and percentages to describe and analyze the findings of the study and to make conclusions.

4.1 Demographic characteristics of respondents

This section provides detailed information about the composition of respondents by gender, work experience and the level of education.

4.1.1 Gender of respondents

Findings on the gender of respondents were considered and showed in the table below;

Table 4.1: Gender of Respondents

		Frequency	Percent	Cumulative Percent
Valid	male	74	75.5	75.5
	female	24	24.5	100.0
	Total	98	100.0	

Source: Primary Data

From table 4.1, indicates that 75.5 % (74) of the respondents were male, and 24.5% (24) were female. And this indicates that the majority of the respondents was male and also specifies that the responses include both sexes. And this supported by Mbabazi (2008) who argued that data collection that incorporates the responses from both sexes is reliable than a single sex sample size.

4.1.2 Number of years worked by respondents

The respondents were requested and asked to mention the time they spent working for the salaam Somali bank and can be evidenced in the table below.

Table 4 .2: The number of years worked by the respondents

		Frequency	Percent	Cumulative Percent
Valid	less than 1 year	14	14.3	14.3
	1-3 years	35	35.7	50.0
	3-5 years	33	33.7	83.7
	above 5 years	16	16.3	100.0
	Total	98	100.0	

Source: Primary data

The Table 4.2 presents the period in which participants have been working for the salaam Somali bank. 14.3% (14) of respondents have been working for salaam Somali bank less than one year. 35.7% (35) of respondents have worked for the company for 1-3 years. 33.7% (33) of respondents were working for 3-5 years, while 16.3% were working above 5 years. This specifies that respondents had experience relating to the study. Sine majority of the respondents have been working for the bank above one year therefore they may provide useful information to the study.. And this supported by Mbabazi (2008) who suggested that the period served by the respondents is useful to any study. Therefore since most of the respondents worked above one year for Bank the data is very useful and important to the study.

4.1.3 Educational level of the respondents

The respondents were asked the level of their education so as to find out the skills and knowledge they have which is important to the study. The responses were as shown below.

Table 4.3: Educational levels of the respondents

		Frequency	Percent	Cumulative Percent
Valid	Secondary	10	10.2	10.2
	Bachelor	48	49.0	59.2
	Master	36	36.7	95.9
	PhD	4	4.1	100.0
	Total	98	100.0	

Source: Primary data

According to the above table, 10.2% (10) respondents were secondary certificate holders, 49% (48) were bachelor Degree holders, 36% (36) respondents were master degree and 4.1% (4) were PhD holders. And this indicates that majority of the respondents had a bachelor degree and have the basic skills and knowledge to perform their work and capacity to answer questions in the questionnaire. This is in line with Uma (2000) who argued that it is important in social investigation research to involve people that have attained an acceptable level of literacy and numeracy in order to be in position to understand and interpreted content in the questionnaire

4.2 Client appraisal of Salaam Somali Bank

This objective desired to examine the relationship between client appraisal and financial performance of Salaam Somali bank Mogadishu-Somalia. Based on the five Likert scales (Strongly agree, Agree, Neutral, Disagree, and strongly disagree). And the findings on the Client appraisal were considered and showed in Tables below.

4.2.1 Client appraisal is a viable strategy for credit risk management

Findings on whether the client appraisal is a viable strategy for credit risk management are considered and have shown in the table below.

Table 4.4: Client appraisal is a viable strategy for credit risk management

		Frequency	Percent	Cumulative Percent
Valid	Disagree	2	2.0	2.0
	Neutral	6	6.1	8.2
	Agree	52	53.1	61.2
	strongly agree	38	38.8	100.0
	Total	98	100.0	

Source: Primary data

From table 4.4, 38.8 % (38) of the respondents strongly agreed that client appraisal is a viable strategy for credit risk management, 53.1 % (52) agreed, 6.1% (6) were not sure and 2.1% disagreed. And this indicates that client appraisal is viable strategy for credit risk management. And this is supported by (Ditcher, 2003) who suggested that credit appraisal is a viable and best strategy of credit risk management for commercial banks.

4.2.2Salaam bank has competent personnel for client appraisal

Findings on whether the salaam bank has the competent personnel for carrying out client appraisal were considered and evidenced in the table below.

Table 4.5: Salaam bank has competent personnel for carrying out client appraisal

		Frequency	Percent	Cumulative Percent
Valid	strongly disagree	1	1.1	1.1
	Disagree	4	4.1	5.2
	Neutral	12	10.2	17.4
	Agree	59	60.2	77..6
	strongly agree	22	22.4	100.0
	Total	98	100.0	

Source: Primary data

From table 4.5, 22.4 % (22) of the respondents strongly agreed that salaam Somali bank has competent personnel for carrying out client appraisal, 60.2% (59) agreed, 12.2% were not sure, and 1.1% (1) disagreed. This indicates that salaam bank has competent personnel for carrying out client appraisal. And this may allow the bank to have an effective client appraisal and credit risk management. Client appraisal considers the character of the customer seeking credit facilities. And this findings are consistent with (Kargi, 2011) who evaluated the relationship between credit risk management and financial performance of Nigerian banks and suggested that competent personnel for carrying out client appraisal is important for the commercial banks and thus may reduce credit risk.

4.2.3 Salaam Somali bank considers the character of the customers seeking credit

Findings on whether the client appraisal considers the character of the customers seeking credit facilities were reflected and are shown in the table below.

Table 4.6: Salaam Somali bank considers the character of the customers seeking credit

		Frequency	Percent	Cumulative Percent
Valid	strongly disagree	1	1.0	1.0
	Neutral	5	5.1	6.1
	Agree	54	55.1	61.2
	strongly agree	38	38.8	100.0
	Total	98	100.0	

Source: Primary data

From table 4.6, 38.8 % (38) of the respondents strongly agreed that client appraisal considers the character of the customers seeking credit facilities, 55.1% (54) agreed, 5.1% (5) were neutral, 1.1% (1) strongly disagreed. This indicates that client appraisal considers the character of the customers seeking credit facilities which is important for credit risk management. And this view is consistent with (Inkumbi (2009).who noted that client appraisal supports the applicant's willingness to repay and ability and prevent credit risk.

4.2.4 Aspects of collateral are considered while appraising clients

Findings on whether the aspects of collateral are considered while appraising clients of salaam Somali bank were considered are shown in the table below

Table 4.7: Aspects of collateral are considered while appraising clients

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	2.0	2.0	2.0
	Neutral	5	5.1	5.1	7.1
	Agree	58	59.2	59.2	66.3
	strongly agree	33	33.7	33.7	100.0
	Total	98	100.0	100.0	

Source: Primary data

From table 4.7, 33.7% (33) of the respondents strongly agreed that aspects of collateral are considered while appraising clients in the salaam Somali bank, 59.2% (58) agreed, 5.1 % were not sure and 2% (2) disagreed. In this case majority of the respondents agreed that the Salaam Somali Bank considers the aspects of collateral while appraising clients. This denotes that salaam Somali bank considers the collateral aspects while appraising the clients in order to improve loan performance and promotes credit risk management. And this finding is supported by (Abedi, 2000) who suggest that the aspects of collateral are important while appraising clients which may help microfinance institutions to increase loan performance.

Failure to asses customers capacity to repay results in loan defaults

The respondents were asked to specify whether the failure to assess the customers' capacity to repay results in loan defaults and their responses were shown in the table below.

Table 4.8: Failure to assess customers' capacity to repay results in loan defaults

		Frequency	Percent	Cumulative Percent
Valid	Disagree	4	4.1	4.1
	Neutral	10	10.2	14.3
	Agree	63	64.3	78.6
	strongly agree	21	21.4	100.0
	Total	98	100.0	

Source: Primary data

From table 4.8 above, the findings indicate that 21.4% (21) strongly agreed, 64.3% (63) agreed, 10.2% (10) were neutral and 4.1% (4) disagreed. Since the highest percentage of the respondents agreed, it indicates that the failure to assess customers' capacity to repay results in loan defaults which highly increase the credit risk. Therefore the bank has to assess the cash flow for the business (or household) which improves loan repayments.And this is supported by (Al-Tamimi, 2007) Who discovered that the failure to assess customers' capacity to repay results in loan defaults and leads credit risk to the commercial banks.

4.2.5 Salaam bank use client appraisal as best method of credit risk management

The participants were asked to indicate whether salaam bank use client appraisal as best method of credit risk management and are shown in the table below.

Table 4.9: Salaam bank use client appraisal as best method of credit risk management

		Frequency	Percent	Cumulative Percent
Valid	Disagree	10	10.2	10.2
	Neutral	7	7.1	17.3
	Agree	58	59.2	76.5
	strongly agree	23	23.5	100.0
	Total	98	100.0	

Source: Primary data

From table 4.9 above, 23.5%(23) of the respondents strongly agreed that salaam bank use client appraisal to best method of credit risk management, 59.2% (58) agreed, 7.1% (7)were not sure, and 10.2% (10) disagreed. This indicates that salaam bank uses client appraisal to best method of credit risk management so as to improve financial performance of the bank.

This view is in line with (Boldizzoni, 2008) who highlighted that Credit appraisal plays important role to keep the loan losses to minimum level, hence if those officers appointed for client appraisal are competent then there would be high chances of lending money to the deserving customers.

Hypothesis one

To test the null hypothesis the researcher used Pearson correlation coefficient and the hypothesis one stated that, there is no statistical significant relationship between client appraisal and financial performance of Salaam Somali Bank and the findings of the correlation were summarized in the table 4.10 below:

Table (4.10): Correlation between Client appraisal and financial performance

		Client appraisal	Financial performance
Client appraisal	Pearson Correlation	1	.431**
	Sig. (2-tailed)		.000
	N	98	98
Financial performance	Pearson Correlation	.431**	1
	Sig. (2-tailed)	.000	
	N	98	98

**. Correlation is significant at the 0.05 level (2-tailed).

The above correlation coefficient indicates that (r= .431, P = 0.000 < 0.05) meaning that there is a positive moderate and significant relationship between client appraisal and financial performance. On the basis on the above findings, therefore, we reject the null hypothesis and accept the alternative hypothesis and that there is a positive significant relationship between client appraisal and financial performance of Salaam Somali Bank. This implied that client appraisal positively and moderately influenced financial performance of salaam Somali bank. And the findings of the study Consistent with the findings of Gitman (2011) who found a significant relationship between Client appraisal and financial performance since the computed p- value (0.000) was less than 0.005 at 95% confidence level. Salaam Somali Bank therefore should evaluate the collateral used as security when appraising the clients; this is because in case of any default the bank will recover the collateral in order service the loan.

4.3 Credit risk control of Salaam Somali Bank

This objective wanted to discover the relationship between credit risk control and financial performance of salaam Somali bank Mogadishu-Somali. And the participants were requested to specify level of agreement on the following statements relating to credit risk control in salaam Somali bank.

4.3.1 Imposing loan size limits is a viable strategy in credit risk management

The participants were asked to specify whether imposing loan size limits is a viable strategy in credit risk management and the findings were shown in the table below.

Table 4.11: Imposing loan size limits is a viable strategy in credit risk management

		Frequency	Percent	Cumulative Percent
Valid	Disagree	2	2.0	2.0
	Neutral	5	5.1	7.1
	Agree	58	59.2	66.3
	strongly agree	33	33.7	100.0
	Total	98	100.0	

Source: Primary data

From the table 4.11, findings show that 33.7 %(33) strongly agreed, 59.2% (58) agreed, 5.1% (5) not sure and 2% (2) disagreed. And this identifies that the highest percentage agreed, denoting that imposing loan size limits is a viable strategy in credit risk management which supports to reach the financial targets of the bank. And this is a line with the suggestion by (Javid, 2009) that setting a loan size limit is a good strategy for credit risk management and aimed to ensure that credit risk is effectively protected by the banks.

4.3.2 The use of credit checks on regular basis enhances credit risk management

Findings on whether the use of credit checks on regular basis enhances credit risk management were evidenced in the table below;

Table 4.12: The use of credit checks on regular basis enhances credit risk management

		Frequency	Percent	Cumulative Percent
Valid	strongly disagree	1	1.0	1.0
	Disagree	7	7.1	8.2
	Neutral	10	10.2	18.4
	Agree	43	43.9	62.2
	strongly agree	37	37.8	100.0
	Total	98	100.0	

Source: Primary data

From the table 4.12 above, the findings indicate that 37.8%(37) strongly agreed, 43.9%(43) agreed, 10.2 %(10) were not sure, 7.1%(7) disagreed and also 1%(1) also strongly disagreed. This clearly shown that the highest percentage agreed, therefore the salaam bank should use credit checks on regular basis in order to manage credit risk and enhance financial performance. And the findings are supported by

(ALARM, 2002). Who argue that credit checks and review structure is essential to ensure that risks are properly identified and assessed as well as that appropriate control and responses are consequently put in place.

4.3.3 Flexible repayment periods improve loan performance

The respondents were asked to specify whether the use of flexible repayment periods improve loan performance and the findings were evidenced in the table below;

Table 4.13: Flexible repayment periods improve loan performance

		Frequency	Percent	Cumulative Percent
Valid	Disagree	3	3.1	3.1
	Neutral	3	3.1	6.1
	Agree	58	59.2	65.3
	strongly agree	34	34.7	100.0
	Total	98	100.0	

Source: Primary data

From the table 4.13, the findings indicate that 34.7 %(34) strongly agreed, 59.2% (58) agreed, 3.1% (3) not sure, and also 3.1% (3) disagreed. It is obviously shown that the highest percentage agreed, and the use of flexible repayment periods improves loan performance. And the salaam bank should maintain this because it improves financial performance. And also the findings are consistent with the suggestion of (Myers, 2011) who asserted that flexible period repayment ensures prompt payment and full collections. The rationale is that not all clients meet their obligations, some just take it for granted, others simply forget while others just don’t have a culture of paying until persuaded.

4.3.4 Penalty for late payment enhances customer commitment to loan repayment

The respondents were asked to specify whether the use of penalty for late payment enhances customer commitment to loan repayment and the findings were shown in the table below;

Table 4.14: Penalty for late payment enhances customer commitment to loan repayment

		Frequency	Percent	T	Cumulative Percent
Valid	Disagree	1	1.0		1.0
	Neutral	3	3.1		4.1
	Agree	59	60.2		64.3
	strongly agree	35	35.7		100.0
	Total	98	100.0		

Source: Primary data

From table 4.14 above, 35.7% (35) strongly agreed, 60.2% (59) agreed, 3.1% (3) not sure, and1% (1) disagreed. This indicates that the respondents were agreed that the penalty for late payment enhances customer commitment to loan repayment, therefore the managers of salaam Somali bank must implement this in order to avoid credit risk and increase financial performance for the salaam Somali bank. And this finding is supported by (Javid, 2009) who argued that penalty for late payment enhances the commitment of the loan repayment and reduces credit risk of commercial banks.

4.3.5 The use of credit application forms improves credit risk management

The respondents were asked to state whether the use of credit application forms improves monitoring and credit risk management and the findings were revealed in the table below;

Table 4.15: The use of credit application forms improves credit risk management

		Frequency	Percent	Cumulative Percent
Valid	strongly disagree	1	1.0	1.0
	Neutral	5	5.1	6.1
	Agree	54	55.1	61.2
	strongly agree	38	38.8	100.0
	Total	98	100.0	

Source: Primary data

From table 4.15 above, 38.8%(38) of the respondents strongly agreed that profit charged affect performance of loans for salaam Somali bank, 54.5% (54) agreed, 5.1% (50) not sure and 1% strongly disagreed. This specify that the use of credit application forms improves credit risk management and enhance financial performance, therefore the salaam Somali bank managers has to use the credit application forms so as to avoid the credit risks.This view is in line with (Boldizzoni, 2008) who found that the use the credit application forms improve credit risk management of the commercial banks.

4.3.6 Profit charged affect performance of loans for salaam Somali bank

The respondents were asked to state whether the profit charged affect performance of loans for salaam Somali bank and the findings were revealed in the table below;

Table 4.16: Profit charged affect performance of loans of the bank

		Frequency	Percent	Cumulative Percent
Valid	strongly disagree	1	1.0	1.0
	Disagree	4	4.1	5.1
	Neutral	12	12.2	17.3
	Agree	59	60.2	77.6
	strongly agree	22	22.4	100.0
	Total	98	100.0	

Source: Primary data

From table 4.16 above, 22.4% (22) of the respondents strongly agreed that profit charged affect performance of loans for salaam Somali bank, 60.2% (59) agreed, 12.2% (12) not sure, 4.1 % (4) disagreed, and 1% strongly disagreed. This indicates that the profit charged affect performance of loans for salaam Somali bank, and the bank should adopt this strategy in order to achieve financial targets. And this is supported by (Al-Tamimi, 2007), Who discovered that the profit charged by the Islamic Sharia compliant banks has an effect of loan performance and prompt payment since the clients are happy and satisfied the profit that are charged by the banks. Therefore, the profits charged by the banks have influences on loan performance.

Hypothesis Two

To test the null hypothesis the researcher used Pearson correlation coefficient and the hypothesis two stated that, there is no statistical significant relationship between Credit risk control and financial performance of Salaam Somali Bank and the findings of the correlation were summarized in the table 4.10 below:

Table 4.17: Correlation between Credit risk control and Financial Performance

		Credit risk control	Financial performance
Credit risk control	Pearson Correlation	1	.641**
	Sig. (2-tailed)		.000
	N	98	98
Financial performance	Pearson Correlation	.641**	1
	Sig. (2-tailed)	.000	
	N	98	98

**. Correlation is significant at the 0.05 level (2-tailed).

The above correlation coefficient indicates that (r= .641, P = 0.000 < 0.05) meaning that there is a strong positive significant relationship between credit risk control and financial performance of Salaam Somali Bank. On the basis on the above findings, therefore, we reject the null hypothesis and accept the alternative hypothesis and that there is a positive significant relationship between credits risk control and financial performance of Salaam Somali Bank. And the findings of the study are consistent with those of (Brighan, 2010), who found that credit risk control has a main influence of financial performance of micro financial institution and suggested that microfinance institutions should improve the credit risk control to avoid loan defaults

4.4 Credit collection practices of Salaam Somali Bank

This objective sought to find out the relationship between credit collection practices and financial performance of salaam Somali bank Mogadishu-Somali. And the participants were requested identify their levels of agreement on the statements relating to credit collection policy for salaam bank.

4.4.1 Available collection have assisted effective credit risk management

The respondents were asked to identify whether the available collection policies have assisted towards effective credit risk management and the findings were revealed in the table below;

Table 4.18: Available collection policies have assisted effective credit risk management of salaam Somali bank

	Frequency	Percent	Cumulative Percent
Disagree	3	3.1	3.1
Neutral	13	3.1	6.2
Agree	58	59.2	65.4
strongly agree	34	34.6	100.0
Total	98	100.0	

Source: Primary data

From table 14.18above, 34.6% (34) strongly agreed, 59.2% (58) Agreed, 3.1 %(3) neither agree nor disagree, and 3.1 %(3) disagreed. This shows that the majority of the respondents have agreed that available collection policies have assisted towards effective credit risk management of salaam Somali bank. This identify that salaam bank has a credit collection policy which helps the bank to prevent the credit risk. And this supported by (Latifee, 2006) who said that credit collection practices in commercial Banks have a great extent of the credit risk management in the commercial banks. Therefore, the available collection policies of Salaam Bank have an effective credit risk management of salaam Somali bank have been a challenge in credit management

4.4.2 Staff incentives are effective in improving recovery of delinquent loans

Findings on whether staff incentives are effective in improving recovery of delinquent loans can be evidenced in the table below.

Table 4.19: Staff incentives are effective in improving recovery loans

		Frequency	Percent	Cumulative Percent
Valid	strongly disagree	3	3.1	3.1
	Disagree	4	4.1	7.1
	Neutral	16	16.3	23.5
	Agree	54	55.1	78.6
	strongly agree	21	21.4	100.0
	Total	98	100.0	

Source: Primary data

From the table 4.19 above, the findings indicate that 21.4% (21) strongly agreed, 55.1% (54) agreed, 16.3% (16) were neither agree nor disagree, 4.1%(4) disagreed and 3.1% (3) also strongly disagreed. This clearly shows that the highest percentage agreed that staff incentives are effective in improving recovery of delinquent loans which helps the bank to achieve its financial objectives. Creating staff involvement in discouraging delinquency, through a staff incentives system can be effective. And this is Consistent with the findings of Gitman (2011) we found that staff incentives are effectives have an influence in improving recovery loans and preventing credit risk. Therefore the staff incentives maybe an effective tool of recovering credit from the clients.

4.4.3 A stringent policy is more effective in debt recovery than a lenient policy

The respondents were asked to identify whether the a stringent policy is more effective in debt recovery than a lenient policy and the findings were shown in the table below;

Table 4.20: **Stringent policy is more effective in debt recovery than a lenient policy**
Source: Primary data

From table 4.20 above, 38.8% (38) strongly agreed, 55.1% (54) agreed, 5.1% (5) were not sure, and 1% (1) strongly disagreed. This shows that the majority of the participants were agreed that stringent policy is more effective in debt recovery than a lenient policy and salaam Somali bank should adopt stringent policy than the a lenient policy. Stringent policy had a great impact on loan performance, and the lenient policy had an effect but was not as great as that of stringent policy (Kosmidou,, 2008).

4.4.4 The length of credit collection period has a negative effect on a financial performance

The respondents were asked to state whether the length of credit collection period has a negative effect on a financial performance and the findings were shown in the table below;

Table 4.21: The length of credit collection period has a negative effect on a financial performance

		Frequency	Percent	Cumulative Percent
Valid	Neutral	6	6.1	6.1
	Agree	51	52	58.2
	strongly agree	41	41.8	100.0
	Total	98	100.0	

Source: Primary data

The tables 4.21 above, the findings indicate that 41.8% (41) strongly agreed, 52 %(51) have agreed, and 6.1 % (6) were not sure. It is clearly shown that the highest percentage agreed that the length of credit collection period has a negative effect on a financial performance, therefore the salaam Somali bank has reduce the period of credit they offer to its clients. And this confirmed the finding of (Moti et al., 2012), who established that the length of credit collection period has a negative effect on a firm's financial performance.

4.4.5 The credit collection practices adopted by the bank has an effect on financial performance

The respondents were asked to indicate whether the credit collection practices adopted by salaam Somali bank has an effect on financial performance and the findings were shown in the table below;

Table 4.22: The credit collection practices adopted by the bank has an effect on a financial performance

		Frequency	Percent	Cumulative Percent
Valid	strongly disagree	1	1.0	1.0
	Disagree	4	4.1	5.1
	Neutral	12	12.2	17.3
	Agree	59	60.2	77.6
	strongly agree	22	22.4	100.0
	Total	98	100.0	

Source: Primary data

From table 4.22, 22.4% (22) of the respondents strongly agreed that the credit collection practices adopted by the salaam Somali bank has an effect on a financial performance, 60.2%

(59) agreed, 12.2% (12) were not sure, 4.1 %(4) disagreed, and 1% (1) strongly disagreed. This indicates that majority of the respondents have agreed that the credit collection practices adopted by salaam Somali bank has an effect on financial performance. The above view is in consistent with (Frank et al., 2014) who argue that the microfinance institutions need to have strong and effective credit collection practices for ensuring consistent recoveries from clients and enhance financial performance.

4.4.6 Effective credit collection policy reduces credit risk

The respondents were asked to specify whether the effective credit collection policyreduces credit risk and the findings were shown in the table below;

Table 4.23: Effective credit collection policy reduces credit risk

		Frequency	Percent	Cumulative Percent
Valid	strongly disagree	1	1.0	1.0
	Neutral	5	5.1	6.1
	Agree	54	55.1	61.2
	strongly agree	38	38.8	100.0
	Total	98	100.0	

Source: Primary data

From table 23 above, the findings show that 38.8 %(38) strongly agreed, 55.1 %(54) agreed, 5.1% (5) were neither agree nor disagree and 1% (1) strongly disagreed. It is clearly revealed that the highest percentage agreed, and this supports that credit collection policy reduces credit risk.

Credit collection policy establishes a set of procedures used to collect accounts receivables which was getting overdue .Methods used could include letters, telephone calls, visits by the firms' officials for face to face reminders to pay and legal enforcements (Van Horne, 2007.

Hypothesis Three

Hypothesis three stated that, there is no statistical significant relationship between credit collection practices and financial performance of Salaam Somali Bank. To test the null hypothesis the researcher used Pearson correlation coefficient and the findings of the correlation were summarized in the table 4.24 below:

Table 4.24Correlation between credit collection practices and financial performance

		Credit collection policy	Financial performance
Credit collection policy	Pearson Correlation	1	.757**
	Sig. (2-tailed)		.000
	N	98	98
Financial performance	Pearson Correlation	.757**	1
	Sig. (2-tailed)	.000	
	N	98	98

**. Correlation is significant at the 0.05 level (2-tailed).

According to the above correlation co-efficient indicates that (r= .757, P = 0.000 < 0.005) meaning that there is a strong positive significant relationship between credit collection practices and financial performance of Salaam Somali Bank. Therefore, the researcher rejected the null hypothesis and accepted the alternate hypothesis since the correlation showed a strong positive relationship between credit collection practices and financial performance of salaam Somali Bank.

4.5 Multiple Regression Coefficients

The researcher conducted a linear multiple regression analysis to test the most important predictor variables to the financial performance. The researcher applied the statistical package for social sciences (SPSS) to code, enter and compute the measurements of the multiple regressions for the study.

Multiple regression coefficients were also used to predict the extents of the variance in the financial performance in salaam Somali bank explained by credit risk management elements and the results revealed and presented in the table (4.23) below:

Table (4.25): Multiple Regression Coefficients.

Model	Standardized Coefficients Beta	T	Sig.	R Square	Adjusted R Square	F	Sig
(Constant)	7.408	3.107	.002	.681	.671	66.960	.000
Client appraisal	.008	.119	.003				
Credit risk control	.368	5.344	.000s				
Credit collection practices	.583	8.476	.000				

Dependent Variable: Financial Performance

From the data in the above table, the established regression equation was Y = 7.408+ 0.008X1 + 0.368 X2 + 0.583X3 From the above regression equation, was revealed that holding client appraisal , credit risk control and collection practices to a constant zero , financial performance of salaam Somali bank would be 7.408, a unit increase in Client appraisal would lead to increase the financial performance of salaam Somali bank by a factor of 0.008, a unit increase in credit risk control would lead to increase the financial performance of salaam Somali bank by a factor of 0.368 and also unit increase in collection practices would lead to increase the financial performance of salaam Somali bank by a factor of 0.583.

Credit collection policy contributed and related to the financial performance more than other variables of credit risk management. Therefore this shows that the elements of credit risk management influenced and positively related to the financial performance of salaam Somali bank.

The adjusted R2 is the coefficient of determination. This value explains how financial performance varied with client appraisal, credit risk management and credit collection policy. The three independent variables that were studied, explain 68.1% of the financial performance as represented by the R2. This therefore means that other factors not studied in this research contribute 31.9% of the financial performance giving room for further research to investigate the other factors (31.9%) that influence financial performance implementation. And the findings of the regression are consistent with (Abedi,2000) who found that client appraisal, credit risk control and credit collection practices have influences and explain the financial performance of commercial Banks. While further indicated that credit collection practices is the main predictor of financial performance

CHAPTER FIVE

RECOMMENDATION AND CONCLUSION

5.1 Recommendations

Based on the findings of the study objectives, the researcher made recommendations to the Salaam Somali Bank Mogadishu-Somalia.

Based on the findings of the study, there was a moderate positive relationship between client appraisal and financial performance of salaam Somali bank. And this situation the researcher recommends that there is need for Salaam Somali Bank to enhance its client appraisal so as to improve its financial performance. Through client appraisal, the Salaam Somali bank managers may be able to know credit worth clients and thus reduce their non-performing loans and improve financial performance of the Bank.

The researcher found that there is a strong positive relationship between credit risk control and financial performance. In this circumstance the researcher recommends that there is also need for salaam Somali bank to boost its credit risk control, and this may help in decreasing default levels as well as its non-performing loans as well it may attract the current and potential investors of the bank.

The study also found that, there is a strong positive relationship between credit collection practices and financial performance of Salaam Somali Bank. Therefore the researcher recommends that Salaam Somali Bank management should enhance their collection practices by adapting a more stringent policy to a lenient policy for effective debt recovery and finally may improve financial performance of the bank.

Areas for future Research

The study sought to determine the relationship between credit risk management and the financial performance of financial performance. To this end therefore a further study should be carried on the salaam Somali bank to see whether the same results also hold by testing the variables in this study, Such as the effect of moral hazard on credit risk management. Moral hazard in credit mainly arises from information asymmetry. If information asymmetry is not checked, it will lead to obtaining of improper information that subsequently leads to wrong credit decisions.

This study could be further developed by including more independent variables to the regression model and increasing the sample size. The variables would help improve the results of the study since it would include all the other factors that affect the profitability of the banks. The increased sample size would give a better representation of the bank.

- ✓ Further research is recommended on the effect of Credit policy on loan performance of salaam Somali bank. To see how the elements of credit policy influences and explains the loan performance of salaam Somali bank.

5.2 Conclusion

The major conclusions of the study were drawn from the specific objectives of the study.

Relationship between Client Appraisal and Financial Performance of Salaam Somali Bank

The study found that there is apositive relationship between Client appraisal and financial performance of salaam Somali bank. From the correlation table, it clearly shown that there is a significant positive relationship between client appraisal and financial performance. This implied that client appraisal positively and moderately influenced financial performance of salaam Somali Bank, therefore the null hypothesis was rejected and the alternate hypothesis was accepted and that is; there is a moderate relationship between the client appraisal and financial performance of salaam Somali bank. On other hand, Client appraisal adopted by Salaam Somali Bankhas an influence to the financial performance of the Bank. And a unit increase in Client appraisal would lead to increase the financial performance of salaam Somali bank.Therefore client appraisal is important method of reducing and managing credit risk faced by the bank. If the client appraisal is not maintained or adopted it may lead poor financial performance of Salaam Somali Bank.

Relationship between Credit risk Control and Financial Performance of Salaam Somali Bank

The findings of study revealed that there is a significant positive relationship between Credit risk control and Financial Performance of Salaam Somali bank. From the results of the correlation showed that a strong positive relationship exists between credit risk control and financial performance and therefore the null hypothesis was rejected and the alternate hypothesis was accepted because of the strong positive relationship between credit risk control and financial performance of Salaam Somali bank. This means that credit risk control is a good strategy of preventing and managing credit risk. Another hand if the company doesn’t implement credit risk control it may cause nonperforming loans which leads poor financial performance.

Relationship between Credit Collection Practices and Financial Performance of Salaam Somali bank

As regards of the relationship between credit collection practices and financial performance, the findings of the study revealed that there is a significant positive relationship between Credit collection practice and financial Performance of salaam Somali bank. And this means that if good credit collection practices are adopted it may lead and improve financial performance, but if it is not adopted it may lead poor financial performance of the Bank. Therefore the null hypothesis was rejected and the alternate hypothesis was accepted because of the strong positive relationship between credit collection practices and financial performance of Salaam Somali bank. And Credit collection practices contribute and relate the financial performance more than other variables of credit risk management.

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APPENDICES

APPENDIX I

RESEARCH QUESTIONNAIRE

Dear Sir/Madam,

I am Hani Ahmed Iman, a student at Daffodil International University a Master of Business Administration, and I am currently carrying out a postgraduate research project on the relationship between credit risk management and the financial performance for salaam Somali bank in Mogadishu Somalia. You have been selected to participate in this study because you have useful information. I request you to respond with truthfulness and honesty for the success of this study. Remember that the information you provide will be treated with maximum confidentiality.

Thank you in advance

SECTION A: DEMOGRAPHIC CHARACTERISTICS (Please tick in the appropriate box provided).

1. **Sex of respondent: (1)**Male ☐ **(2)**Female ☐
2. **Work experience of respondent:**

   (1) Less than 1 year ☐ **(2)** 1-3 years ☐ **(3)** 3-5 years ☐

   (4)Above 5 years ☐
3. **Level of education**

   (**1)**Secondary ☐ **(2)** Bachelor degree ☐ **(3)** Master degree ☐

   (4) PhD ☐

SECTION B: CREDIT RISK MANAGEMENT PRACTICE

1) CLIENT APPRAISAL

What is your level of agreement on the following statements relating to client appraisal for Salaam Somali bank?

No.	Statement	Strongly agree(5)	Agree (4)	Neutral (3)	Disagree (2)	Strongly disagree (1)
1.	Client appraisal is a viable strategy for credit risk management of Salaam Somali bank.					
2.	Salaam bank has competent personnel for carrying out client appraisal at Salaam Somali bank.					
3.	Client appraisal considers the character of the customers seeking credit facilities.					
4.	Aspects of collateral are considered while appraising clients at Salaam Somali Bank.					
5.	Failure to assess customers' capacity to repay results in loan defaults at Salaam Somali Bank.					
6.	Salaam bank use client appraisal to best method of Credit risk Management.					
7.	An appropriate appraising and accurately evaluating the borrower's financial capacity contribute financial performance					
8.	Effective client appraisal provides effective credit risk management					
9.	Credit appraisal guarantees the recovery of loaned money					
10	Capital is measured by the general financial position of the borrower and enhance loan performance					

2) CREDIT RISK CONTROL

What is your level of agreement on the following statements relating to credit risk control in salaam Somali bank?

No.	Statement	Strongly agree(5)	Agree(4)	Neutral (3)	Disagree (2)	Strongly disagree(1)
1	Imposing loan size limits is a viable strategy in credit management					
2	The use of credit checks on regular basis enhances credit management.					
3	Flexible repayment periods improve loan repayment.					
4	Penalty for late payment enhances customers commitment to loan repayment					
5	The use of customer credit application forms improves monitoring and credit management as well					
6	Profit charged affect performance of loans for salaam Somali bank					
7	Credit committees involvement in making decisions regarding loans are essential in reducing default/credit risk					
8	The integrated credit risk controls practiced by salaam Somali bank improve financial performance.					
9	An effective credit risk control provides effective credit risk management and financial performance					
10	Product loan design mitigates a significant portion of default risk that meet client needs					

3) CREDIT COLLECTION PRACTICES

What is your level of agreement on the following statements relating to credit collection practices for salaam bank?

No.	Statement	Strongly agree(5)	agree (4)	Neutral (3)	disagree(2)	Strongly disagree(1)
	Available collection policies have assisted towards effective credit management.					
	Formulation of collection policies have been a challenge in credit management.					
	Enforcement of guarantee policies provides chances for loan recovery in case of loan defaults					
	Staff incentives are effective in improving recovery of delinquent loans.					
	Regular reviews have been done on collection policies to improve state of credit management.					
	A stringent policy is more effective in debt recovery than a lenient policy.					
	Effective credit collection policy reduces credit risk					
	Good credit collection policy enables to maximize investment revenue in debtor and promotes financial standing position					
	The length of credit collection period has a negative effect on a firm's financial performance.					
10	The credit collection practices adopted by salaam Somali bank has an effect on financial performance					

SECTION C: FINANCIAL PERFORMANCE

What is your level of agreement on the following statements relating to the financial performance of salaam bank?

		Strongly agree(5)	agree (4)	Neutral (3)	Disagree(2)	Strongly Disagree(1)
1	The profitability of Salaam bank is constantly increasing					
2	Salaam bank has a good return on investment (ROI)					
3	The bank makes sufficient profits to cover all its operational costs					
4	Salaam bank often pays its creditors on time					
5	The bank always achieves its financial targets within the budgeted period.					
6	Salaam bank has attained a good current ration liquidity performance standard					
7	The bank' s cost efficiency level is adequate					
8	Salaam bank has adequate working capital					
9	Salaam bank generates enough revenue to meet its obligations as they fall due					

END
Thank you for your cooperation