AN ANALYSIS OF CREDIT MANAGEMENT IN THE BANKING INDUSTRY

(A CASE STUDY FIRST BANK OF NIGERIA PLC. ENUGU.)

BY

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BF/T/2010/146

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AUGUST 2013

TITLE PAGE

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BEING A PROJECT REPORT SUMBITTED TO THE DEPARTMENTOF BANKING AND FINANCE, FACULTY OF MANAGEMENT AND SOCIAL SCIENCES, CARITAS UNIVERSITY, IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE AWARD OF BACHELOR OF SCIENCE DEGREE (B.Sc) IN BANKING AND FINANCE.

APPROVAL PAGE

This research work was read and approved for meeting the requirements, is recommended for the award of Bachelor of Science (B.Sc) degree Banking and finance, Caritas University, Amorji-Nike, Emene, Enugu State.

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(Project Supervisor)

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Mr. I.G Okafor.

(Head of Department) Date

CERTIFICATION

I Akuw Obaje Fatima an under-graduate student of the department of Banking and Finance with registration number BF/T/2010/146 have submitted this project report for the award of the Degree of Bachelor of science (B,Sc) in Banking and Finance. The work embodied in the project report is my original work and has not been submitted in part or in full for any degree or diploma in this University or any other Institution.

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Akwu Obaje Fatima Date

We certify that this project report has successfully defended and accepted for the award of the degree of Bachelor of Science (B.Sc) in Banking and Finance.

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Dr Takon S.M. Date
(Project supervisor)

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Mr Okafor I.G Date
(Head of Department)

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External Examiner Date

DEDICATION

This work is dedicated to God Almighty my personal saviour. To my beloved Father Chief Akwu Obaje and the best mum in the world Mrs Ladi (Blessed memories)

ACKNOWLEGDEMENT

I begin with immeasurable gratitude to God Almighty, who has protected me and provided for me throughout my stay in Caritas University.

My special appreciation goes to my loving and caring parents Chief Akwu Obaje A., and late Mrs Ladi A. for their prayers, encouragement and their immeasurable support throughout my education so far. God will keep you to enjoy your labour.

I sincerely acknowledge the contribution of my project supervisor, Dr. Takon, S.M who stood by me to criticize my work in order for it to be successful and accepted. God bless you sir for your fatherly encouragement and advice.

To the principled man in our department, Mr. I.G. Okafor. H.O.D and the father of Banking and Finance department, I will never forget your pieces advice.

To my able and worthy lecturers, I will be ungrateful if I fail to show my appreciation to you all for your contribution and corporation towards my formation as a graduate of Banking and Finance. My thanks go to Prof. F.O. Okafor, Mr. Nwadiubu A., Mr. Ezeamama M. and Nsofor E.S. I pray for Gods' continuous guidance upon you all.

To the family of Mr and Mrs Mathew I. am grateful.

My next thanks also go to my siblings, Yusuf, Rabiu, Ahmed, and Seadatu, all for their prayers.

Finally to my beloved friend in the person of Sylvester E. I tank u so much. I am also grateful to Paul Audu, Mercy O., Chioma O., Faith I. and others

ABSTRACT

Credit extension is an essential function of banks and bank management strive to satisfy the legitimate credit needs of the community it tends to serve. This study is aimed at analysing the credit management in the banking industry in Nigeria with particular reference to first Bank of Nigeria PLC. The importance of credit in the economic growth and development of a country cannot be overemphasized. Despite the important role played by credit in the economy, it is associated with a catalogue of risks. The Nigeria banking industry witnessed some failures prior to the consolidation era due to imprudent lending that finally led to bad debt and some ethical facts. The issue of non- performance of asset and declaring of ficticious project has become the order of the day in our banking system as a result of poor credit management leading to bank distress in the industry. Three hypotheses were formulated and tested through use of chi-square on questionnaires administered to various respondents. From the data collected and the tested hypothesis, results showed that: (i) Inadequate feasibility study affects loan repayment in the banking industry, (ii) The diversion of bank loan to unprofitable ventures affects loan repayment and (iii) The problem of poor attention given to distribution of loan has negative effect on banks performance. Amongst several recommendations were the following: (a) Banks should establish sound and competent credit management unit and recruit well motivated staffs (b) Banks should ensure that the chief executive avoid approval in principle in the credit management, and (c) Banks should have a monitoring and control unit or department to carry out a sort of post- modern exercise by way of controlling and monitoring credit facilities and also ensuring completeness of all conditions precedent to draw down.

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CHAPTER ONE

1.0 INTRODUCTION

1.1 BACKGROUND OF THE STUDY

Credit management in our banking sector today has taken a different dimension from what it used to be. The banking industry has adopted a lot of strategies in checking credit management in order to stay in business. Thu the banking industry in Nigeria has lost large amount of money as a result of the turning source of credit exposure and taken interest rate position. Nigerian banks are being required in the market because of their competence to provide transaction efficiency, market knowledge and funding capability. To perform these roles, the banks act as the most important participants in their transaction process of which they use their own balance sheet to make it easier and making sure that their associated risk is absorbed.

Credit extension is essential function of banks and the bank management strive to satisfy the legitimate credit needs of the community it tends to serve. This credit advances by banks as a debtor to the depositor requires exercising prudence in handling the funds of depositors. The Central Bank of Nigeria established a credit act in 1990 which empowered banks to render returns to the credit risk management system in respect to its entire customers with aggregate outstanding debit balance of one million naira and above (Ijaiya G.T and Abdulraheem A (2000). This made Nigerian banks to universally embark on upgrading their control system and risk management because this coincidental activity is recognized as the industry physiological weakness to financial risk. The researcher, a New yolk-based, said that 40% of Nigerian banks that made up exchange rate value in west Africa, has reduced the operating lending as a result of bad debts which hit more than $10 billion in 2009 and this has led to a tied-up questioning asset that is holding almost half of Nigerian banks. The central bank of

Nigeria fired eight chief executive officers and set aside $ 4.1 billion in order to bail out almost 10 of the country's lenders. The reform which was introduced by Central Bank of Nigeria (CBN) in 2010 has made Nigerian banks resume lending supporting assets management companies and set up the requirement which will allow Nigerian banks make full provision for bad debts that will boost the market.

The banks identify the existence of destructive debtors in the banking system whose method involved responding to their debt obligations in some banks and tried to have contract of new debts in other banks. Banks are trying to make the database of credit risk management system more open for them to be more functional and recognized as to enable banks to enquire or render statutory returns on borrowers. There are some banking practices which increase the risks in the bank and cannot be easily changed. This result still leads to the question: what are the possible ways that will help make Nigerian banks manage their credit risks?

Credit risk management helps credit expert to know when to accept a credit applicant as to avoid destroying the banks reputation and making decision in order to explore unavoidable credit risk which gives more profit. Controlling a risk results in encouraging rewards that give internal audit more technical support service and customized training in banks or financial institutions. This research is presented to outline, find, investigate and report different state of techniques in risk management in the banking industry

1.2 STATEMENT OF THE PROBLEM

In the history of development of the Nigerian banking industry, it can be seen that most of the failures experienced in the industry prior to the consolidation era were results of imprudent lending that finally led to bad loans and some other unethical factors (Job, A.A Ogundepo A and Olanirul (2008)). Also the problem of poor attention given to distribution of loans has its effect on the bank’s performance. Most of the people collected loan from the banks and diverted the money to unprofitable ventures. Some bankers are not actually considering the necessary criteria for disbursement of loans to the customer. This work therefore intends to outline, explain these problems identify the causes and suggests lasting solutions to the problems associated with credit management and consequently banks debts.

1:3 OBJECTIVES OF THE STUDY

The objectives of this study is as follows

1. To examine how feasibility study affect loan repayment in the banking industry.
2. To highlight the extent in which diversion of bank loans to unprofitable ventures affect loan repayment.
3. To examine how distribution of loans affect banks performance if banks give proper attention.

1.4 RESEARCH QUESTIONS

Bank lending is said to be effective if it successfully achieves the banker’s obligation of maximum liquidity to the depositors. The questions here are

1. To what extent does feasibility study affect loan repayment in the banking industry?
2. To what extent does diversion of bank loans to unprofitable venture affect loan repayment?
3. Does distribution of loans have effect on banks performance if given proper attention?

1.5 STATEMENT OF HYPOTHESES

A reputable credit management system enhances good control on lending and proper keeping of credit account.

HYPOTHESES 1

Ho. Inadequate feasibility study does not affect loan repayment in banking industry.

Hi. Inadequate feasibility study affects loan repayment in banking industry.

HYPOTHESES 2

Ho. The diversion of bank loans to unprofitably ventures does not affect loan repayment.

Hi. The diversion of bank loans to unprofitably ventures affects loan repayment.

HYPOTHESES 3

Ho. The problem of poor attention given to distribution of loans does not have effect on banks performance.

Hi. The problem of poor attention given to distribution of loans has effect on banks performance.

16. SCOPE OF THE STUDY

This study is aimed at analysing the credit management in the banking industry in Nigeria with a particular reference to First Bank of Nigeria plc. The study intends to analyse the credit facilities in banking industry. It also reviews the various concepts procedures for efficient and effective credit management. It examines the success and failure (if any) as well as recommending corrective measure.

1.7 SIGNIFICANCE OF THE STUDY

This study will be useful to the executive and managers in the banking industry and other financial institutions. This is because it provides guidance which will enhance effect and efficient credit management aimed at attaining and boosting maximum profitability and liquidity in their banks. The depositor (public) on the other hand will be more enlightened on the need to be honest and fulfil the responsibilities in credit transaction with the banks so that they can look up to improve service from the banks. Finally to the researcher, this is an eye opener because as a potential manager it will guide one in future on how to manage credit facilities.

1.8 DEFINATION OF TERMS

Below are the major terms used in the course of this research work.

1) BANKRUPTCY: A state where a person or firm is unable to meet their financial obligations.
2) MANAGEMENT: management is the study of decision-makers from the supervisor and line managers at lower levels to the Board of Directors.
3) LOANS AND ADVANCES: These are credit facilities granted by banks to their customers. They could be short, medium or long term depending on the length of period of repayment
4) OVERDRAFT: A credit facility (usually short term) granted by banks to current account holders and it carries interest charges on daily basis
5) BANK: Section 61 of BOFIA 1991 Act defines a banking business as business of receiving deposits on current account or other similar account paying or collecting cheques drawn by or paid in by customers.
6) CUSTOMER: A person is a customer if he or she has account with the bank.

7) FINANCIAL RATIO: These are ratios usually expressed in mathematical terms to test the financial obligations.
8) FINANACIAL STATEMENT: They are firm balance sheets, profit and loss account and classified statement which show the financial state of affairs of the firm.
9) GUARANTOR: A person or group of persons who stand for bank customers for credit facilities.
10) COLLATERAL/ SECURITIES: is an asset presented by a customer to his bank to secure a credit facility granted to him by the bank.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

2.0 INTRODUCTION

The purpose of this chapter is to present a view of literature relating to credit management in banks on both theoretical and empirical grounds. Review of some of the studies carried out and suggestions extended by eminent authors on the subject have helped in formulating the theme meaningfully and to carry out the study in line with the objective and scope

2.1 THEORETICAL REVIEW

2.1.1 ORIGIN OF BANK CREDIT

The origin of bank credit could be traced to the medieval times, long before the advent of goldsmiths in the western civilization. As far back as 1850 BC, lending activities were recorded in the temple Samas in sipper of Babylon. The actual existence of the temple covered a century or two previously. During this period, lending was primarily for consumption and the imposition of interest was termed as exploitation. One of the earliest enactments on bank lending is Hebrew Law. Hebrew Law recognized lending but prohibited the taking of interest. Enrichment through lending with interest was frowned at and severe punishments were prescribed for such acts. This was later incorporated into Mosaic laws which prescribed thus, “You shall not lend upon interest to your brother”. About 1545, the mosaic laws were abolished and the taking of interest on loans was made legal. The Arabic civilization also recognized lending activities, but usury is condemned and prohibited as much as possible.

However, as commerce developed and as the opportunities for transactions in money became abundant, secular practices went in the direction of lending with interest. Modern principles and practices of bank lending could be traced to the activities of goldsmiths who transacted business in benches and which formed the basis for formal banking business which started in 1587in Venice-Italy. In Nigeria, the origin of lending could be traced to the activities of traditional financial intermediaries, long before the advent of the colonial masters. These intermediaries developed as a consequence of the credit needs of the rural population. It is noteworthy that the basic occupation of the rural populace was peasant farming and crafts and these sustained the unformalized intermediation structures available at that time. These intermediaries consist of voluntary "ESUSU" groups, age grade associations, village rural development schemes, family fund pools, extended family cooperatives funds, social clubs etc. Essentially, people relied on these groups for their credit needs.

The traditional financial intermediaries constitute substantial source of credit for economic activities prior to the advent of commercial banks in Nigeria. It is not worthy that today, that role has not been entirely eliminated by the presence of organized banks. The impacts of these institutions are still felt in the rural and semi-urban centres. Basically they serve three functions: savings function, credit function and investment function.

2.1.2 THE CONCEPT OF CREDIT

According to Onyeagocha (2001), the term credit is used specifically to refer to the faith placed by a creditor (lender) in a debtor (borrower) by extending a loan usually in the form of money, goods or securities to debtors. Essentially, when a loan is made, the lender is said to have extended credit to the borrower and he automatically accepts the credit of the borrower.

Credit can therefore be defined as a transaction between two parties in which the creditor or lender supplies money, goods and services or securities in return for promised future payments by the debtor or borrower.

There are three major types of credit. These are commercial credit, consumer credit and investment credit.

Commercial credit can be bank credit such as overdraft, loans and advances; trade credit from suppliers; commercial papers (or note); invoice discounting; bill finance; hire purchase; factoring etc.

Consumer credit is a kind of permission granted to an individual or a household to purchase goods like refrigerator, television, car, electronic sets, which could not be paid for immediately but for which instalment payments are made over a period of time.

Investment credit allows a business concern such as corporate body, sole proprietorship or partnership to obtain credit for capital goods for expansion of factoring or procurement of machinery.

The tenor of a loan varies from short to medium, role to long term depending on the institution, nature and functions.

The importance of credit (and consequently the role of banks) in the economic growth and development of a country cannot be over-emphasize. The functions of credit are primarily two: it facilitate the transfer of capital or money to where it will be most effectively and efficiently used; and secondly, credit economizes the use of currency or coin money as granting of credit has a multiplier effect on the volume of currency or coin in circulation. Perhaps, we need to add here that the cost of credit (notable interest and discount rate) is one of essential tools to be used to control and regulate money by the central bank of Nigeria through its monetary policy.

Despite the important role played by credit in the economy, it is associated with a catalogue of risks. According to Obalemo (2004), credit risk is an assumed risk that a borrower won't pay back the lender as agreed.

The various types of credit risks include management risk, geographical risk, business risk, financial risk and industrial risk. The probable occurrence of partial or total default requires a thorough risk assessment prior to granting loans.

2.1.3 CREDIT MANAGEMENT

Every bank has to develop and implement comprehensive procedure and information systems to follow up the condition of individual credits. An effective loan monitoring system according to Odofuye (2007) will include measures to:

1) Monitor compliance with established covenants,

2) Assess, where applicable, collateral covenants, relative to creditor's current condition,

3) Identify contractual payment delinquencies and classify potential credits on a timely basis, and.

4) Direct actions at solving problems promptly for remedial management.

Loan monitoring which is the work of the relationship manager in most cases is not a choice, but an imperative for effective and efficient credit administration in banking sector. Problem loans can easily be spotted out. The banker's experience, knowledge of the customer business and above all, faith in the customer can be a guide in taking a decision to how far the customer can be supported before declaring the loan as bad.

In some occasions, the customer may be in need of more support. Any or a combination of the following strategies can then be employed:

(a) Alteration or waiver of some of the terms and condition of loan covenant in a way not to temper with the bank's interest. However, this must be communicated to the credit department

(b) Issue of additional collateral security, if available.

(c) Granting of additional funds, if borrower's circumstances and analysis require the need.

(d) Extension of loan repayment period supported by fresh cash flow statement.

2.1.4 TYPES OF BANK CREDIT

1. LOAN AND ADVANCES

A) OVERDRAFTS: These are the most common and simplest forms of credit facilities. They are usually granted for working capital purposes and the amount outstanding is expected to fluctuate over the life of the facilities, depending on the borrower's working capital financing needs, at any material time.

Overdrafts permit the borrower to use those amounts required on a day to day basis, thus saving unnecessary interest charges. In accordance with general banking practice, overdrafts are repayable on demand and can be cancelled at the bank's option without prior notice to the borrower. The overdraft limit is usually communicated to the customer and this limit serves as the bank's reference point in all drawings by the beneficiary.

B) ADVANCES: An advance is a short-term credit which is granted for a definite period, usually between 30 and 180 days. They are usually granted for specific purposes, for example, payment of various collections, refinancing of maturing loans, project bridging finance, refinancing of letters of credit for project equipment imported etc. The exact maturity date of an advance is normally determined at the onset and this makes it possible for the project to have a lower interest charge on the advance due to the reduced risk (money rate and credit risk).

Short-term loans are also used in financing seasonal increases in working capital and also in temporary accommodations of a project capital expenditure needs, and other long-term commitments, pending final negotiation of long-term loan. Most times, short term loans are usually renewed at maturity. Banks predominantly extend substantial amounts of short-term loans to farming, manufacturing, small-scale project etc. Short-term loans may be secured or unsecured. Banks extend secured loans to borrowers who have a high debt/equity ratio, or projects that have not established a record of satisfactory performance and stable earnings or generated enough sales revenue in relation to their capital. Large exposures are also often secured.

Unsecured loans, although disallowed by banking laws in Nigeria, are granted in exceptional cases to projects that are properly financed, have adequate capital and net worth, competent management, stable earnings, a record of prompt payment of obligations, and a bright future. Unsecured loans, however, often crystallize into bad debts in the Nigerian banking scene.

C) MEDIUM- TERM LOANS: These constitute important sources of intermediate funds for projects and businesses. Medium-term loans are usually granted for specific purposes such as investments, equipment financing, housing, share acquisitions, agricultural financing, construction etc.

A medium-terms loan is a facility with an original maturity of more than one year or a loan granted under a formal agreement (revolving credit or credits) on which the original maturity of the commitment is in excess of one year. Medium-term loans have maturities of between 1 and 5 years. They are negotiated between a borrower and a lender and are most prevalent in industrial projects characterized by heavy fixed capital requirements. Most of the loans however are made to small projects and businesses which rely on these sources, due to their limited access to the capital market.

Medium-term loans provide flexibility for the user and are amortized in fixed instalments on a monthly, quarterly, semi-annual or even annual basis, as the case may be. The interest rates on this type of loan amongst other factors depend on the general level of interest rates prevailing in the market, the amount and maturity of the loan and the credit standing of the borrower. Generally, the interest rates is higher than in ordinary advances or short-term loans due to higher money and credit risks and the fact that it is less liquid.

Medium-term loans are usually supported by a loan agreement between the bank and the borrower. This agreement outlines the terms and conditions of the loan, and other important features such as:

1) Preamble which contains the parties to the loan and the purpose of the loan
2) Amount of loan
3) Tenor. The maturity of the loan is usually well specified.
4) Repayment schedule; term loans generally specify that a repayment schedule be in the form of an annuity.
5) Interest rate- this is usually specified and may range from fixed rates to floating rates
6) Security/ guarantee. There are usually specifications for collateral.

   When a revolving credit agreement that does not require collaterals is converted into a term loan, the borrower may then have to secure the loan according to the conditions of the loan agreement.
7) Representations and warranties

8) Covenants of the borrower: This usually includes affirmative covenants, the negative covenant and other restrictive clauses. An example of a restrictive clause/negative clause are restrictions on the borrower from special actions such as increasing its dividend payments, making loans to its officers and /or directors and purchasing or leasing fixed assets etc.

9) Events of default/acceleration clause

10) Miscellaneous matters

Usually, a borrower is expected to execute series of promissory notes corresponding to each repayment date. Enforcement of repayment is thus facilitated and the parties tend to have a greater faith in the agreement

ADVANTAGES OF TERM LOANS

(i) Term loan affords the borrower the advantage of trading on its equity. This concept assumes that the profits on the borrowed funds exceed the cost of borrowing.

(ii) With a term loan, it is possible for the borrower to negotiate the provisions of the initial lending agreement directly with the lender.

D) LONG-TERM LOANS: Banks in Nigeria do not usually provide much of long-term loans. This is due to the nature of their deposit liabilities from where the loans are granted. Recently, however banks have been engaging in long-term lending through syndicated loan arrangements. Long-term loans are usually provided by investment banks, development banks and various international lending agencies.

Long-term loans are granted for periods exceeding five years, and are usually provided for fixed capital requirements. They are amortized in fixed instalments like medium-term loans.

The interest rate on this type of loan is tied to market rates and usually is higher than other rates in the market, due to the higher risk exposures.

(2) SPECIAL CREDITS

These are special types of credit facilities extended by banks in favour of various projects and businesses. They are usually non-fund based and are classified as credit since they entail some risks on the part of the bank/financial institution providing the facility

(1) Public Works Bond: these are three types of public works bond.

   (a) The Bid Bonds or Tender Bonds: The essence of bid bonds is to ensure that the party, to whom a project or contract has been awarded, will execute the contract successfully. The bid bond is called for the employer as soon as the contractor fails to accept the award. This is because failure to accept the terms of the contract may result in an additional cost of rewarding the contract to another contractor.

   (b) Advance Payment Guarantees: most times, a bank is required to issue a guarantee on an advanced payment made to a contractor by the employer, prior to the commencement of the contract. The guarantee is in terms of the contractor's financial and technical standing.

   (c) Performance bonds: banks issue this type of bond on behalf of their clients who have contracts. The bond provides a guarantee on the contractor's capability of handing the contract, his financial standing and credit rating.

(2) Customs and Excise Bonds: this type of bond is issued a by the bank to guarantee a third party (usually a government organ) with regards to an importer's capability of making payment of customs duties (for imports) and excise duties (for manufactured goods in Nigeria). As soon as the customer defaults, the bank would be held liable to pay the sum guaranteed.

(3) Bills of lading indemnities: A bill of lading is a quasi-negotiable document which confers title to goods. Banks usually issue a bill of lading indemnity to their customers, in cases where the goods imported into the country arrive before the importer (customer) receives the bill of lading. This indemnity issued will thus assist the customer in clearing the goods.

The bill of lading indemnifies the shipping company against any loss or subsequent claims on the ownership of the goods covered by the indemnity and usually the bank is primarily liable on the indemnity.

(3) DOCUMENTARY CREDITS

A documentary credit or letter of credit is a written commitment of one bank addressed to an identifiable party to pay the seller of goods or services, an agreed sum of money on condition that the seller produces documents evidencing that the goods have been shipped or that he has performed the services required of him. There are different types of documentary credits. These include: the revocable documentary credits, the irrevocable and confirmed credits. Others are revolving credits, red clause, 'bank to bank' credit and stand-by letters of credit. For our purpose we shall concentrate on the following types.

a) Revocable Documentary Credit
b) Irrevocable, Unconfirmed Documentary Credit
c) Irrevocable Confirmed Documentary credit.

i. Revocable Documentary Credit: A revocable documentary credit allows the issuing bank to amend or cancel the credit without notice to the beneficiary (the seller) before he is paid.

ii. Irrevocable, Unconfirmed Documentary Credits: this represents a commitment by the issuing bank (usually the buyer's bank) to pay the seller, if the terms of the credit are met and it is usually not amended or cancelled without the seller's consent.

iii. Irrevocable and confirmed documentary credit: this type of documentary credit offers the best security for payment to the seller assuming he fulfils his part of the contract. In the arrangement, another bank (the confirming bank) commits itself to paying the seller, if all the conditions of the credit are fulfilled.

Documentary credits could also be categorized according to the terms of payment. Here, we could distinguish between sight credit, acceptance credits, deferred payment credit, red clause' credit and revolving credits.

(i) Sight credit- this is a situation where the beneficiary receives payment on presentation and examination of the documents.

(ii) Acceptance credit- In this type of credit, the beneficiary draws a time draft either on the issuing or confirming bank or on the buyer or another bank, as specified in the documentary credit. As soon as it is accepted by any of the parties above, the issuing and confirming bank guarantee payment of the instrument at maturity to any confide holder.

(iii) Deferred credit- in this form of credit, the issuing or confirming bank issues a written promise to make payment on due date. This contrasts with the acceptance credit since in the latter case; a draft is accepted upon presentation of properly confirmed documents. Here, there is an obvious advantage since the draft being a negotiable instrument, could be easily discounted.

(iv) "Red- clause" credit- this is a special type of advance credit. It authorizes the advising bank to advance a part of the credit amount to the beneficiary to enable him mobilize the merchandise.

(v) Revolving credit- this form of payment, arises where a buyer intends to place orders in excess of his requirements. The revolving credit is established stipulating intervals of delivery and thus guaranteeing payment of each delivery, assuming the terms of the credit are maintained.

The process of establishing a documentary credit involves two banks and two parties: the importer and exporter. It should be noted that banks adopt normal credit evaluation methods in granting these special credits. The basic requirements, most time, are the same as in normal loans and advances.

The two banks involved in documentary credit transactions consists of, first, the importers' bank also known as the opening (establishing) bank. There is also the confirming or notifying bank that is the exporter's bank.

2.1.5 CLASSIFICATION OF LOANS AS TO PURPOSE (SELECTED CAUSE)

A) Agricultural Loans: as a result of the increased emphasis on increased agricultural output, government places a lot of emphasis on provision of loans by banks for agricultural projects. The essence is to establish, reactivate, expand or modernize all types of agricultural enterprises, which are considered economically feasible and desirable to the achievement of stated national economic goals of self-sufficiency in agricultural production, and commercially viable.

Agricultural project lending in Nigeria is enhanced by the agricultural credit Guarantee Scheme Fund operation by the Central Bank of Nigeria. According to the guideline of the scheme, the fund seeks to provide guarantee in respect of loans granted by any bank for agricultural purposes with the aim of increasing the level of credit to the agricultural sector.

Banks extend loans to agricultural project through two methods: direct lending and on-lending. Direct lending involves lending directly to farmers (individuals, groups or organizations). On-lending on the other hand, involves lending to farmers through intermediaries such as co-operative unions or a financing agency, agricultural corporations, state or federal ministries of Agriculture, River Basin Development Authorities and other relevant agricultural lending institutions and agencies. The latter method is practiced mainly by the Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB).

The criteria for this type of lending are the same as other types of lending and the security is the same, except that the ACGS requires personal guarantee. The interest rates are market-determined unlike previously when concessionary interest rates were charged by banks. Agricultural lending could be by way of overdraft, short-term loans, medium-term loans or long-term loans, depending on the purpose and gestation period of the project.

b) Export finance:

Banks have always been involved in the export business in Nigeria, even before the emergence of oil as the dominant source of earnings for the country. For example, during the era of commodity boards' involvement in the export trade, banks provided bridging finance to licensed buyers of commodities meant for export. However, following the deregulation in the Nigerian economy, banks are presently involved in export finance in the following areas.

(i) Short term financing of all aspects of non-oil export including storage, packaging, handling, transportation and delivery to the ultimate buyer.

(ii) Identification of the eligible non-oil export products, technical services and the identification of viable foreign markets etc.

(iii) Providing status reports on foreign buyers

(iv) Advising on modes of payments for the export trade.

(v) Enhancing the quality of documentations of the overall national export promotion strategies. There are basically two types of export finance- the pre-shipment finance scheme and the post-shipment finance schemes.

(a) Pre-shipment finance:

This could be classified broadly into two- the mobilization advance and the merchandize or produce advance. Pre-shipment finance is usually required by exporters to ease the production, processing and /or packaging of export goods, up to the point they are placed on board a ship or any other mode of transportation. Pre-shipment finance could be classified broadly into two:

(i) Mobilization Advance: this type of facility is similar to an overdraft. The only difference is that where as an overdraft may be cancelled without notice and is always current, a mobilization advance is liquidated at the end of its tenure or on completion of the particular export project or at the end of the operating cycle of the transaction. This financing scheme assists an exporter to obtain funds for purchasing produce from other sources-local buying agents or growers

(ii) Merchandize or produce advance: the merchandize or produce advance is a form of export finance provided by banks on the basis of ware house receipts. This presupposes that the exporter has purchased the produce and put them in an approved ware house and a ware house receipt is then issued by a reputable ware house agent. Here, loans are provided to the exporter and as a security for the finance, the exporter goods are controlled by placing them in the custody of a ware house company, who issues a warehouse receipt on them. When a loan is made on the security of warehouse receipt, there is a great reliance on the competence and integrity of the ware house company.

2.1.6 SYNDICATION CREDIT

Banks usually resort to loan syndications in an effort to spread risks, accommodate new and viable projects and enhance their earning potentials. They also resort to this approach whenever they find a viable project which one bank cannot finance single-handedly. Under the syndication arrangement, there is a lead bank and a consortium of other financial institutions (syndicates) comprising of banks, investment companies and insurance firms. Loans provided are usually large in nature and may be medium term or long-term in nature. The interest rate may be above the prime-lending rate and is usually payable annually or semi-annually or at any agreed period.

The increased cases of syndicated project financing in Nigeria can up to 1998 be explained by general trends in the economy. Rising project costs and increased risks of doing business in a recessed economy were crucial factors that gave rise to loan syndications. Increase restrictions on lending by the monetary authorities, the high demand for loans and the need for capital adequacy dictated that banks enter into consortium arrangements, to cater for the credit needs of large project concepts.

However, the increased level of distress in the financial system adversely affected syndications and thus there has been a lull in this area especially between 1998 and 2004

LOANS TO THE RURAL SECTOR

The limited nature of credit to the rural sector and the lopsided nature of bank branch expansion in favour of the urban segment motivated the federal Government to introduce the rural banking programme in 1977 and recently the community-banking scheme in 1991.

The rural sector could to a large extent be equated to the agricultural sector, since the predominant occupation of the residents of the area is peasant farming, limited credit facilities as a result of limited access to banks and poor banking habits, meant that this vital sector would be strangulated and growth would not be in the desired direction.

The monetary authorities during the era of direct control of bank credits prescribed minimum levels of loans for the rural sector in the monetary policy each year. This measure was aimed at compelling the banks to assist in the economic development of rural sector. It was also aimed at breaking the vicious circle of low productivity, low incomes, low savings and low growth that has been the bane of the rural sector. Under the present indirect system of credit control, these minimum credit prescriptions have been deemphasized. Banks however, are still expected to extend substantial volumes of credit to the rural sector, even with the phasing out of the rural banking programme.

LOANS TO SMALL AND MEDIUM SCALE ENTERPRISES

Banks are also required to grant loans to small and medium scale enterprises. SMES have the potentials of enhancing the level of development of the economy, in terms of increased output, creation of employment opportunities and the level of exports of the country. Over the years, banks did not substantially provide the necessary assistance to SMEs because of the high level of risks associated with lending to small businesses.

However, in 2001, the bankers committee agreed to set aside 10 per cent of the profile before taxes of each bank, for financing of SMEs. A small and medium scale enterprises equity and investment fund was set up for this purpose.

The monetary authorities also set up the national credit risk fund to provide additional guarantee for credit accommodation to small and medium enterprises. Available data show that the level of financial accommodation to SMEs has increased with the introduction of the equity investment fund.

2.1.7 ROLE OF BANK CREDIT IN THE ECONOMIC SYSTEM

It is generally accepted that bank credits influence positively the level of economic activities in any country. It influences what is to be produced, who produces it and how much is to be produced.

Bank credit affects and alters the level of money supply of a country. Thus the monetary authorities seek to influence the volume and cost of credit and thus moderate inflationary trends in the economy. This is premised on the fact that excessive credit expansion affects money support which ultimately affects the level of inflation and aggregate economic performance.

Also bank credit is the most important source of bank incomes. It affects a bank's profitability and long term growth prospects. It is also the most important aspect of bank's asset and in fact the largest portion of asset base. Bank credit also affects bank liquidity and non-performance credit is the major cause of bank distress and failure. It is noteworthy that the current distress in the financial system has its root in the large non-performing loans and advances granted by banks to various persons and the high level of credit abuses and inside dealings.

Credit also promotes the activities of bank and non-bank financial institutions and thus influences the level of growth of the financial system.

Finally, bank credit affects aggregate output and productivity, the pattern of production, the level of entrepreneurship, the realization of aggregate economic performance and economic growth. It could thus be concluded that credit is of crucial importance to banks, the monetary authorities and also the growth of the economy.

2.1.8 CREDIT RISK MANAGEMENT

Credit risk management greatly influences or prevent the failure of a bank. This is because the failure of a bank is influenced to a large extent by the quality of credit decisions and thus the quality of the risk assets. Credit risk management provides a leading indicator of the quality of banks credit portfolio. (McNaugton 1994)

The key element in an effective credit management includes:

- Well-developed credit policy framework and procedures
- Strong portfolio management
- Effective credit controls
- Well-trained human resource to implement system

Bank management must conduct a market definition as a starting point in credit risk management. This also includes the determination of the target markets. The credit policies are a necessary guide for the determination of the target market, and customers, and define the acceptable and unacceptable risks.

Credit origination usually is at the instance of the customer. The credit officer must identify the reasons when the borrower needs the loan and crosscheck all facts about the proposal and thus have all relevant information for evaluating the proposal. The credit officer should also evaluate the proposal as to the management and nature of business.

Thereafter the officer must be certain on the source of repayment, ascertain if the proposal fits into the banks objectives and the government policies in place, assess the government policies in place, assess the business risks that could inhibit repayment and then conduct a financial analysis. All the issues here are assessed under the credit analysis. In addition the collateral package is appraised.

Approval is then sought from the deciding authorities. Banks usually adopt either a committee or a sequential process of credit approval in the committee system, the ultimate approval of a credit proposal is done by a committee consisting of members of a senior management and sectional heads. It could also be a board committee made up of members of the board of directors. The sequential process is applied in smaller loans and consists of an approval chain of individual loan officers with ascending level of authority.

A deposit-banking firm like most financial institutions tend to hold little owner's capital relative to the aggregate value of its assets. The implication of this is that only a small percentage of total loans need to turn bad to push the entire credit portfolio to the brink of failure.

According to Peter and Sylvia (2008) the probability that a deposit banking institutions credit portfolio will decline in value and perhaps become worthless is known as credit risk while various attempts designed to control and protect banks against adversities associated with these risk exposure are referred to as credit risk management processes.

The process of analysing credit risk, ranking and quantifying them constitute a substantial aspect of the framework and governance structures for most bank management. Among the reasons advanced for CRM include managerial self-interest and appraisal goal; high cost of financial distress and the existence of capital market imperfection. Other motivation for expending managerial resources on CRM according to Meyer (2000) is the need for insolvency avoidance, given the likelihood of poor credit risk management snowballing into financial crisis.

The process of sound CRM commences with identification of the existing and potential risk inherent in a bank's lending activities as well as designing appropriate policies to control them,. In the Nigerian banking system, individual bank management fashions out CRM system comprising polices that

I) Limits or reduce credit risk to certain industries, market or individuals (over-concentration)

II) Ensure adequacy of asset classification (asset classification rule)

III) Loan loss provisioning (prudential code)

IV) Stipulates borrower’s key performance indexes’ (conditionality rule)

V) Undertakes pre-lending assessment and post lending audit/monitoring.

In August 2009, the CBN issued guidelines for developing CRM framework for individual banks risk element in line with its supervisory model. The motivation for the guide line among other is the need to close the wide spread ‘’lacuna’’ in most codes and standards with respect to CRM of individual banks in the sector. Other goals have been identified to include strengthening the credit appraisal procedures, storage and dissemination of credit data, monitoring of over exposure to borrower’s, facilitating consistent credit classification and affording regulators first-hand information on customer’s global debt profile; (www.cinenbank.org (2010)).

By 2010 the CBN also floated an Asset Management Company (AMCON) specifically designed to relief ‘troubled banks’ of their ‘toxic’ assets. Lessons from recent bank crisis have however shown that removing assets from a bank balance sheet does not ultimately ensure that such bank will be risk free in its subsequent operations. Further evidence of this was provided by AMCON managing director, corporation lost about ₦226 billion in three nationalized banks (about 39.00 per cent of total shareholder’s fund) between 2009 and 2011.

2.1.9 CREDIT POLICY OF BANKS

Every bank puts in place a credit policy to guide its lending decisions, taking into consideration its overall corporate objectives Conceptually, a bank’s corporate objectives influence its overall banking operation including issues like:

-Liquidity management

-Profitability posture and earning capacity

-Bank portfolio management

-Service delivery and level efficiency

-Deposit mix and structure

-Credit management

-Capital adequacy

Credit management is the most important aspect of banking operations outside liquidity considerations, as it influences and ensures the survival and safety of a bank. Credit policies are thus the most important aspect of the various operational policies of a bank. Credit policy provides the framework for the entire credit management process.

The basic reason for policy is to ensure operational consistency and adherence to uniform and sound practices. A sound policy contributes to a bank's success by supporting prompt and good credit decisions. According to Robert Bench (1991) the scope of lending (credit) policies should include: who receive the credit; who grants it (and how); the pricing of the credit; the amount of credit and organisational structure for its distribution. Other issues like what kind of credit and under what circumstances they are granted, also come into this preview of credit policymaking. The above definition by Bench seeks to specify the scope of credit policy. However, the definition could be stretched further by pointing out the fact that credit policy influences and affects the administration and management of credits.

Credit policies are usually documented by banks in the form of credit manuals. The manuals specify the course of action, procedures and guides to sound lending. A properly articulated manual would usually consolidate and update all lending policies instructions, procedures and any relevant correspondence on credit matters and administration that would be evolved by top management from time to time, based on new exigencies, new developments in the industry, changes in environmental factors and other changes evolved by the monetary authorities as the need arise.

The absence of a properly articulated, formally written policy document coupled with the failure of credit officers, managers, and directors to monitor the implementation and administration of bank credits, are critical factors leading to unsuccessful bank lending or non-performing exposures and credits.

It must be emphasized here that putting sound policies into practice calls for the establishment of an effective organization and the adoption of appropriate procedures. Experience has however shown that most banks do not have a clearly spelt out and formalized policy framework, hence credit decision-making is adhoc and thus cumbersome, leading to loan losses and impairment of capital adequacy

2.1.10 THE PURPOSE OF CREDIT POLICY

Credit policy serves various purposes for banks. These include:

1) They provide bank credit officers, branch managers, credit controllers and financial analysts with basic guidelines and rules for efficient risk selection, credit analysis, credit administration and management.
2) They assist a bank in ensuring that it maintains high quality risk assets and also high level of performance assets.
3) They also assist a bank in meeting the legal and statutory requirements imposed by the monetary authorities, especially issues like capital adequacy, loan capital ratios, loan-deposit ratios, permissible credit expansion and legal requirements for granting credit to one individual.

4) Credit policy assists a bank in attaining the overall corporate mission and objectives, especially issues like achieving a high level of liquidity, profitability and earnings per share for the bank.
5) They provide a framework for the effective examination of the credit operations of a bank by both external and internal inspectors. This is because the availability of a codified policy easily yields grounds for an assessment of the performance of bank operators, assessing the deviation from the prescribed normal and the areas for possible normalization. It also provides a standard framework for predicting future trends in the credit operations of the bank based on available data and information.
6) They assist a bank in the training and retraining of credit officers, bank managers, credit controllers and most time the top management.
7) They are useful when a bank must adapt to a complex and rapidly changing economic environment and faces issues that formerly received little or no attention.
8) Finally, good credit policy ensures effective lending. According to Nwankwo(1980) lending is considered effective if it successfully reconciles the bankers obligation of maximum profitability to the shareholders and maximum liquidity to the depositors. This is done by ensuring that non-performing exposures are reduced and properly managed and hence ensures a high level of performing risk assets. This would ordinarily involve risk minimization measures. Risk minimization concerns and addresses statutory constraints or specific guidelines on risk exposures or risk concentration by a financial institution (bank) usually by relating such exposures to the total risk assets of the institution.

A bank's credit policy should encompass several elements: the regulatory environment, the availability of funds, the selection of risk, loan portfolio balance and the form structure of liabilities. It must be noted that the board of directors guides credit policy formulation, Good corporate governance demand that the board approves all policy thrusts and any changes thereof.

2.1.11 FACTORS AFFECTING CREDIT POLICY THRUSTS OF BANKS

A number of factors affect the loan policies of banks in Nigeria. These factors affect the quality of the exposure, the composition and size of the loan, the direction and use of the funds and the general circumstances under which it is appropriate to make a loan. These factors include:

(a) Risk and Yield/Profitability of a loan: Banks usually consider how profitable a prospect is to its earnings generally. It is generally accepted that banks with greater need for profitability will usually adopt more aggressive lending policies. On the other hand, banks with a high level of liquidity problems as is evident during the period of distress, would usually adopt very tight lending policies.

(b) Capital Position of Bank: the capital position of a bank and the nature of its capital adequacy needs influence the ability and willingness to extend further credits. It also influences the types and volume of the lending generally.

Usually, the capital structure of a bank serves as a cushion for the protection of depositor's funds and a cushion for loan losses or disappointing interest margins. The capital structure also influences the bank's growth prospects and potentials. Thus, banks with limited capital resources are constrained from engaging in large loan exposures and also long term lending generally. Preference in this case is given to self-liquidating loans and credit.

It is noteworthy that many banks in the Nigerian financial system up to 2004 have impairments on their capital resources. Thus, there are various restrictions as to the size of their loan portfolios and the nature of the loan exposure.

The capital structure of a bank will usually comprise of the issued and fully paid share capital, statutory reserves, (reserves from asset revaluation and share premiums), Long term debt issued either through public offers or private placements also provide a measure of support for the bank's lending activities. The issue of capital adequacy is crucial in the loan management policies of banks.

Also, the needs for liquidity usually influence the credit policy of a bank. Thus, there must be a trade-off between liquidity and profitability at all times.

(c) Structure of Deposit Liabilities: lending activities of banks are usually done with the deposits mobilized from the public. These deposits are of various types (savings, time and demand) and their stability varies in each case. The lending policy of bank is influenced by the volume of the deposit ratio and considerations relating to statutory and special reserve requirements.

(d) Economic Conditions: the economic conditions prevailing at each point in time also affect the credit polices of bank. In a recessionary period, the government usually adopts contractionary monetary and fiscal policies. Thus, banks are compelled to embark on restrictive lending practices due to the contraction of business opportunities and shortfalls in deposit mobilization. A stable economy encourages more liberal lending polices since opportunities exist for profitable lending.

(e) The Monetary and Fiscal Policy: the government usually adopt monetary and fiscal policies to ensure monetary stability, balance and even economic growth, full employment, self-reliance as tools for containing inflationary pressures. Monetary policy guideline regulates the cost, direction and quantity of credit facilities. These policy guidelines influence the pattern of growth of bank credit and by extension, the type of policies to be enunciated by banks.

(f) Legal Requirements: the banks and other financial institution Act 1991 as amended, specifies various safeguards to protect depositors from reckless lending by banks. These provision affect the lending practices of banks and hence the type of loan policies to be adopted at each point in time. The regulatory authorities specifies loan/deposits ratio, risk assets/ adjusted capital ratio and various prudential guidelines for banks, which seek to protect depositors funds and the investments of the shareholders.

(g) The Bank’s Human Resources: the quality of the human resource available to a bank, also affects its lending practices and policies. Lending to a large extent involve the interpretation of the financial data of the borrowing client, the determination of the liquidity and solvency of the project and the determination of the willingness and ability of the customer to service and repay the facility extended. It also involves a clear appreciation of the socio-economics and political developments in the country which may affect the project and thus the loan exposure. In cases where there are unqualified or inexperienced personnel, (especially credit officers) the bank may be reluctant to venture into some types of lending activities. An example is agricultural lending. This activity is associated with a lot of complexities and risk and calls for proper analysis, close monitoring and supervision. Thus, we undertake this type of lending, due principally to the associated problems and human resource limitations.

(h) Factors relating to the Borrower: most times, defects in the proposals by a potential borrower, might lead the lending bank in adopting a particular policy which subsequently may prove an error of judgement. A good proposal maybe badly presented and a bad one may be presented in such a way as to convey a false impression of the viability of the business, thereby resulting in a bad risk. As noted by Olashore,(1985) a proposal that on the face of it satisfies all the cannons of good lending, may turn out to be a bad risk because of sudden changes in tastes or fashion, or in the political situation. All these affect the lending policies of banks and the willingness to lend by a bank

(i) Expectations of the Community: the credit needs and expectations of the immediate community affect the lending policies of banks. These needs vary, depending on the predominant occupation of the population, the state of economic development and socioeconomic relations. Since banks are morally bound to extend credit to borrowers who present logical and viable proposals in a community, the policies to be adopted reflect the pattern of demand for loans and the needs of the customers.

2.1.12 CREDIT ANALYSIS

The essence of credit analysis is to determine the ability and willingness of a borrower to repay a loan in accordance with the terms of the loan contract. Banks attempt to assess the degree of risk it will be willing to exposure and the amount of funds that would be prudently extended in view of risk involved. The risks in lending stem from the various factors that can lead to non-payment of the loan obligation when it falls due. Read et al (1980) articulates the risks in lending thus:

Losses sometimes result from “acts of god” such as storm, drought, fires, earthquakes and floods. Changes in consumer demand or in technology of an industry may alter drastically the fortunes of a business firm and place a once profitable borrower to a loss position. A prolonged strike, competitive price cutting, or loss of key management personnel, can seriously impair a borrower’s ability to make loan repayments. The swings of the business cycle affect the profits of many who borrow from banks and influence the optimism and pessimism of business people as well as consumers. Some risks arise from personal factors that are difficult to explain.”

Generally, banks do not knowingly extend poor loans and advance. It is what happens after a loan has been made, that causes it to deteriorate in quality. Such adverse circumstance may be foreseen, as when obvious credit weaknesses are over looked or ignored. Many are, however, unforeseen.

Aside from the risks enumerated above, a prominent feature of lending risks in Nigeria is the outright and deliberate disregard to financial obligations. In Nigeria, loans from the bank are often thought of as funds that are not meant to be repaid. Evidence show that before the advent of the failed banks and financial malpractices Decree 1994, and recently the Economic and financial Crimes Act 2001 a Nigerian who obtains a loan from the bank is not looked upon as one who has increased his liability, but as a clever man who has successfully attracted public funds that need be repaid. Most times, the intending borrower does not disclose fully why the loans are wanted and as soon as approval is received, there is a diversion to other unproductive uses, e.g. marrying more wives or buying a new car. Also, most borrowers under estimate their needs, due to various reasons ranging from ignorance, lack of a proper feasibility study and the fear of contracting huge debts. As a result, as soon as the amount asked for is approved, the venture is abandoned half way, making the chance of repayment very remote.

Risk taking is central to banking. Banks are successful when the risks they take are reasonable, controlled and within their financial resources and credit competence. Protection against the risks of lending consists mainly of maintaining high credit standards, appropriate diversification, intimate knowledge of the borrowers' affairs and alert collection procedures.

Also in the process of lending, banks seek to investigate the factors that may lead to default in the repayment of loan. This investigation is called credit analysis. Nwankwo,(1980), views credit analysis as involving a combination of all activities connected with the collation of both qualitative and quantitative data and information. The main objective of credit analysis is to increase the certainty level of lending by carefully assessing the parameters surrounding the economic, financial and social status of the applicant. In credit analysis, an attempt is made to determine the conditions and terms under which the loan will be granted, the factors that will affect the ability to repay including financial projections, economic forecasting, environmental analysis and the history and reputation of the borrower. It may include the collection of information that will have a bearing on credit evaluation and the preparation of the information collected.

2.1.13 THE CANNONS OF LENDING

A number of factors are considered by banks in assessing a loan request. Reed et al (1980) views these factors as the ingredients that determine the lending officer's faith in the debtor's ability and willingness to pay the obligations in accordance with the terms of the loan agreement. Many authors like Adekaye (1986), Fatemi and Fooladi(2006) and Onyiriuba (2004) call these factors the criteria for creditworthiness. Some authors call them the "six Cs" of lending, consisting of character, capacity, capital, condition, connection and collateral. For our purpose, we shall call them the five cannons of lending.

(a) Character: this is considered as the most important factor in bank lending. It refers to the integrity, honesty, reliability, morality and the level of responsibility of the customer. It influences the willingness to repay debts and the strong desire to settle all obligations within the terms of the contract.

In credit analysis, the character of an individual could be obtained from his past operation of the account, his previous loan service behaviour, his social class, nature of occupation and spending patterns. For incorporated bodies or registered businesses, the character of its principal officers, its past loan-service and repayment record are analysed in assessing its corporate character. It is also important to obtain a status report from banks where the customer maintained an account in the past

(b) Capacity to borrow: this refers to the legal capacity to borrow. A bank is interested not only in the ability of a borrower to repay but also in the legal capacity. Banks would usually not lend to a minor except the contract is co-signed by a parent or guardian and even at that, it must be used for essential purposes.

In lending to a partnership, all members of the firm must sign for the loan or those signing must have legal authority to sign for the rest. Furthermore, the partnership agreement must specify the way and manner the loan could be contracted.

For an incorporated body, the lending officer must be satisfied that the articles and memorandum of association of the company, empowers the directors to borrow on behalf of the company. The bank would in most cases insist in ascertaining that the purposes for which the loan is required, agrees with the object's clause in the memorandum of association.

It is also important to note that lending to a company may be perfectly in order, for an activity or a set of activities, but restrictions may be placed as to the amount and, or conditions of borrowing by the board of the company. In this case, it is only the board that could ratify the loan.

(c) Capital: this refers to the financial position of the customer as depicted in its financial history. It could also be reduced to the not worth of the business or the residual equity that is available for the repayment of the debt. Credit is usually not granted to a business unless capital resource of the business is one of the measures of its financial strength and reflects the prudence and resources tend to show a high ability to repay outstanding obligations

(d) Collateral: This represents forms of assets pledged by the borrower as security for the loan. Banks often ask for and take adequate collateral securities as a manifestation of the customer's confidence in his own project and as something upon which the banker can fall on if things go wrong and expected results are not achieved.

The type of collateral securities demanded by a bank and the valuation placed on it depends on the nature and circumstances of the loan and the character of the customer. Collateral is often referred to as the 'second way out' and is usually taken, in case the customer cannot repay from his own resources.

Banks usually consider the following factors in assessing collaterals for bank lending:

(i) The collateral is usually obtained before disbursement of funds. This is because most customers become uncooperative in the performance of the security, where they have already received the money.

(ii) Banks usually insist on holding a first charge on collateral. No charge is taken without a search to ascertain a previous charge.

(iii) Collaterals taken should be such that it will maintain or preferably increases its valve over time.

(iv) A realistic valuation of the security is done to ascertain its forced sale value, which is lower than the normal market value. The essence is to determine a realizable value for the collateral

(v) Economic conditions: banks usually consider the impact of socio-economic trends on the activities of the customer, economic condition affect the ability of the borrower to repay financial obligations. Usually, these conditions are beyond the control of the borrower and the banker. Economic conditions are the environment under which businesses operate.

A loan proposal may satisfy all the requirements of a good exposure, but economic conditions may render the extension of the credit unwise. Hence, banks try to do some forecasting of economic trends. The essence is to determine those factors in the economic environment that might, in future, affect the projections of the borrower and hence make the ability to repay impossible. It is important to note that the longer the maturity of the loan, the more the need for economic forecasting.

Apart from the cannons of lending as enunciated above, banks also consider the following factors in their lending decision, According to Mather (1962).

(a) Safety: banks normally would have to convince themselves about the certainty of repayment. The lending officer would want to find out the sources of repayment of the facility granted and whether the borrower can service and repay the loan from profits and revenues generated by the business.

(b) Suitability: banks also satisfy themselves that the loan purpose is not in conflict with the lending regulations in force or with existing regulations. These regulations include those that affect business, investments and contracts generally. The loan must not conflict with public policy or affect the establishment of contractual relationships.

(c) Profitability: banks exist as business ventures with profit motives. Also, the funds used in making advances are generated from customers, which usually attract a cost to the bank. As a result, banks would naturally build in all the attendant costs to make the lending exercise a profitable venture. These costs include the cost of doing business, the cost of lost opportunities and the cost of funds.

It is important for the bank to ascertain whether the project to be funded will be viable enough to enable them recover all these costs and make a profit.

(d) Purpose of loan: as noted earlier, the purpose of the loan request must be clear and very well-articulated. Banks insist on this since very high risk ventures bothering on gambling and betting are usually not considered.

(e) Amount of the loan: the borrower is expected to articulate fairly well his financial requirements. This is usually done in a financial plan/cash budget, prepared alongside a feasibility study for corporate clients. For a small business/individual, this is usually done less elaborately. The borrower's stake in the venture must also be well specified.

2.1.14 SECURITIES FOR BANK CREDIT

Securities are usually described as a 'second way out' for bank lending. Banks usually realize the securities if the customer fails or is unable to repay his loan. A security also enables the bank to exert a better control on his customer's financial commitments. Taking adequate security infuses necessary responsibility on the borrower.

A collateral security is defined as "some right or interest in a property given to a creditor by a debtor so that in the event of the debtor failing to pay his dents as at when due, the creditor may reimburse himself for the debt out of the property charged". Securities are also defined in the widest sense by the Union Bank of Switzerland as “documents giving title to property or claims on income which may be lodged, e.g. as securities for bank loan” it goes further to say that securities may take the form of a pledge of securities, as assignment, a guarantee, a surety, or real or personal collaterals.

Four types of securities for bank lending are easily discernable. These include liens, pledges, mortgage, and assignments. These could be expanded to be setoffs, guarantees, etc.

(1) MORTGAGE AS SECURITY:

A mortgage could be said to be the conveyance of land or an assignment of chattels as a security for the payment of a debt or the discharge of any other obligation for which it is given. It also consists of the conveyance of a legal or equitable interest in real or personal property as security for a debt. These are two types of mortgages, viz

(a) Legal mortgages

(b) Equitable mortgages

(A) Legal mortgage: the essential features of a legal mortgage in Nigeria are as follows:

(i) The right to sell is automatically conferred on the banker in addition to a right over the asset.

(ii) All legal mortgage must be executed under seal

(iii) The customer has a right of redemption, i.e. a right of conveyance on repayment of the monies borrowed through a deed of release.

(B) Equitable mortgage: this is simply a deposit of a title deed by a borrower and has the following features:

(i) It could be affected with or without a memorandum of deposit.

(ii) It could also be affected with or without a letter of undertaking.

Generally, banks prefer a legal mortgage to an equitable mortgage. This is because an equitable mortgage only gives the bank a right on the asset mortgaged but not the right of sale in the event of a default by a borrower, except by an order of the court.

An equitable mortgage, however, could be converted to a legal mortgage in the following ways:

(1) By obtaining a court order for specific performance of the undertaking as contained in the equitable charge.

(2) If a customer refuses to execute a legal mortgage in compliance with the court order, or cannot be found, a legal mortgage will then be executed by a court official on behalf of the mortgagor.

Presently, as a result of the provisions of the land use Act of 1976, the customer is required to produce a certificate of occupancy and a consent to mortgage from the state Governor before a legal mortgage is executed.

Banks generally consider the forced sale value of a mortgage in granting a facility. The value of the facility usually does not exceed the forced sale value of the mortgage. Note that the remedies available to banks in a legal mortgage include a right of sale, a remedy of fore closure, suing for the debt, right to enter into possession, and the appointment of a receiver/manager.

(2) GUARANTEES AS SECURITY

A guarantee is an undertaking by one person (guarantor) to attend to the debt owned by a debtor to the bank in case the debtor defaults. The bank usually relies on the agreement of the guarantor to offset the debts of the principal debtor in the case of default. A guarantee is only as reliable as the guarantor's ability and willingness to repay. Thus, it is important to conduct a financial analysis of the credit worthiness of the guarantor at all times.

A guarantor is usually not enforceable by action unless it is evidenced by a written memorandum of agreement signed by the party sought to be made liable under it. The essential features of a bank guarantee are as follows:

(a) There must be a consideration

(b) The guarantee must be for the whole debt on any account or in any manner whatsoever due from the principal debtor, either banking charges including legal costs and expenses.

(c) Guarantees may be specific or continuing.

(d) Guarantee containing definite time limit are not usually acceptable except the bank reserves the right to withdraw future advance within the specified period.

(e) The guarantor is normally required to give a notice of determination of the guarantee in writing to enable the bank have sufficient time to communicate the amount of his liability at the expiration of his notice.

(f) The guarantee also makes provisions for the surrender of the guarantor common law rights.

(g) The guarantee may be supported by a cash deposit.

(3) LIEN AS SECURITY: Here the borrower remains the owner of the property. The bank usually has no right to dispose of the property. Banks take lien over credit balances and with stipulated balance to be retained in a blocked account. A letter of set-off is attached to this lien to enable the bank recover the debt in the event of default.

(4) ASSIGNMENT AS SECURITY: An assignment transfers rights under a contract, especially in a contract of life assurance. In this case, the insured has a right to receive the sum assured at maturity or at death. This right may be assigned by the insured as security for loan. The valid value for the assignment is the current surrender value duly obtained from the insurance company and with the bank's interest noted therein.

(5) PLEDGES AS SECURITY: in a pledge, the pledgee is entitled to the exclusive possession of the property until the debt is paid whereas the ownership still rests with the

pledge subject to the pledge's rights. The pledge reserves the right to sell the property in certain circumstances.

(6) OTHER SECURITIES:

(a) Quoted share/bonds: Quoted share and bonds could also be used as security for a loan. In this case, the bank can take either a legal or equitable charge. In either case, the bank gets the customer to execute a memorandum or letter of deposit. The memorandum is taken in order to establish the nature of the transaction, and so prevent a customer from subsequently alleging that he entrusted the security to the in a bail-bailee relationship, so that the bank would not have either an equitable charge by deposit or even a lien on them. The share certificates are usually deposited in the bank together with black share transfer forms and consent to sell addressed to the respective registrars. Banks only lend up to 90 per cent of the market value of the share. The reason is to allow a suitable margin over the market value for fluctuation purposes.

(b) Treasury Bills/Certificates: these could also be used as security for a loan, depending on the maturity date and other instructions noted therein.

(c) Fixed and Floating Charge: most times, a bank may take out a charge on all or any assets of company as security for a loan. This is usually done by way of a debenture. A debenture is an acknowledgement of debt incorporating a charge over the assets of the borrower and usually given by incorporated companies under seal. It should be noted that debentures are equitable charges only and a bank cannot get any of the remedies of a legal mortgage other than the power to appoint a receiver in the event of the company going into bankruptcy.

Debentures are drawn in favour of bank and expressed to be payable on demand and interest is stipulated to be at fixed or determinable rate. Banks usually make reference to the board resolution of the company or of the directors, authorizing the debenture.

2.1.15 CREDIT ADMINISTRATION AND CONTROL

(a) Credit Administration: this is concerned with the implementation of credit decisions as authorized by the bank's top management of credit and involves the day-to-day follow up of the credit, including documentations, credit files, interest payments and loan repayments, according to the terms of the approvals.

Credit administration commences from the time an application is received from a customer to the processing and approval, advice of facilities granted to the customer (including terms and conditions of approval), opening of credit files, perfection of securities, a follow up of the credit (including correspondence on irregularities observed on the account) and finally, the repayment of the facility granted.

(b)CREDIT CONTROL: Credit control is concerned with the post approval and monitoring of the credit facility, to ensure that each credit remains qualitatively satisfactory during the tenure of the credit. It is very important to monitor (control) the facility after it has been approved to ensure that:

(I) The borrower complies with the stipulated conditions

(II) The facilities are utilized with the purpose for which they were approved

(III) Any deterioration or negative trends in the customers' business or prospects is determined and corrective actions taken

Credit controls also entail making some basic credit returns as required by the Banking Act for the purpose of monitoring the banks total commitments to clients in a particular period.

(c) Credit Reviews: Credit reviews could be said to be a periodic appraisal of the credit portfolio of a bank to identify accounts which are operating in an unsatisfactory manner with a view of taking necessary corrective measures. Banks periodically review their credit portfolio to determine the performing and nonperforming credits. Here, the causes of non performing credits are investigated and reported upon and prompt action is then taken to effect recovery through persuasion, receivership, litigation measures etc.

Credit monitoring is an important aspect of credit reviews. The machinery of credit monitoring entail constant and periodic discussions with the borrower to better appreciate their problems and future prospects, the level of activity and the potentials of the borrower. The historical financial records are also closely reviewed to find out the performances of the borrower and the causes of any deviations from the earlier projections.

Credit reviews according to Agene (1995), also involves the increase or decrease in the approved limit and expiry date, a change in the terms and conditions of the credit, the mode of repayment and the spread amongst other factors depending on past performances and future plans and prospects. Credit reviews also seek to examine the financial data of the customer to determine any deterioration or negative trends in the customer's credit history including the state of the securities pledged as collateral. The determination of non-performing accounts and the appropriate provisions is a key consideration in the review. The prudential Guidelines (1990) specify the ways and methods of providing for non performing account, including the methods of reserving interests and provision for the capital sum.

The policy areas relating to non-performing accounts would include:

- Basic premise for detecting a difficult and non-performing account;
- The system or method for detection of such accounts;
- The actions to be taken for the detection of such accounts;
- The responsibility for decision making and managing of such accounts;
- The rules for classifying banks 'other asset' as well as treatment of off-balance sheet items.
- The minimum amount of provision to be made for each category of loan commitment;

- The conditions and methods for treating interest recognition for non-performing accounts; and

- The measures for full or partial recovery of provisioned bad and doubtful debts.

Thus credit reviews try to determine whether the level of facility granted is justified and are within the customer’s ability to repay, or whether the funds have been deployed properly for the purposes intended and whether the securities pledged have been perfected and are adequate, suitable, and realizable in case of need.

Usually, banks are able to reclassify their loan portfolio from the credit reviews into satisfactory and unsatisfactory classes. The unsatisfactory accounts are further broken down into sub-standard accounts, doubtful accounts, and bad or irrecoverable accounts.

(a) Sub-standard Account: These are account that possess some deficiencies in terms of security offered being unsuitable, inadequate, non-existent or of dubious value. It may also be because they operate in excess of the authorized limit.

(b) Doubtful Accounts: these are unsatisfactory account, the full recovery of which is considered improbable, considering the operation and general circumstances of the accounts. Banks usually make provisions for these from its capital reverses or by a charge against its annual profits.

(c) Bad or Irrecoverable Accounts: These accounts are considered bad and irrecoverable by reason of the customer becoming totally bankrupt or holds no security or the outstanding amount ‘represents the residual balance of original indebtedness after the bank has set-off the amount realized from the sale of the underlying securities, or in the opinion of the bank. It would be too burdensome and unprofitable to continue to chase the debtors for payment.”

2.1.16. BAD AND DOUBTFUL DEBTS: bad and doubtful debts are part of inherent risks in bank lending. Bad and doubtful debt is usually associated with the total loss of both interest and capital (principal amount of loan). Olashore (1988) summarized the causal factors thus:

(i) Lack of proper appraisal of the customers need; credit worthiness and business experience.

(ii) Indiscriminate acceptance of securities as collateral for credit facilities without regard to their suitability, worth and the ease of realization, in cause of need.

(iii) Failure to obtain and review periodically the financial statements of borrowing customers and determine the conduct and volume of their business.

(iv) Absence of information on credit records and other commitment of borrowing customers.

(v) Excessive zeal on the part of borrowing customers to expand their businesses beyond their capacity, considering various other factors.

(vi) The conscious actions of unscrupulous customers to defraud the bank.

(vii) The usual vicissitudes of business life.

(viii) Failure of bank officials to observe the banks own credit policy"

The above causal factors could be expanded further to include the following:

(a) Natural phenomena

(b) Changes in government policy (political instability

(c) Bad management (by the customer)

(d) Sudden change in fashion (resulting in change in consumer preference and change in technology, which all lead to loss of business for customer)

Banks thus evolve different strategies in all attempts to recover these debts. The need for recovery is principally due to the fact that bad debts affect the banks aggregate earnings and also its capital funds and consequently affect the dividends payable to shareholders of the bank. Huge bad and doubtful debts also affect depositor's confidence in the bank in particular, and the banking system in general. Invariably, excessive bad loan may lead to distress and capital reconstruction. In view of these factors, banks adopt two strategies:

1. Evolve measures to avoid the incidence of bad and doubtful dents.

2. Evolve strategies to fully or partially recover provisioned bad and doubtful debts.

The major factors responsible for the deficiencies in the credit risks management also include:

(a)The absence of written polices,

(b)The absence of portfolio concentration limits

(c) Excessive centralization or decentralization of lending authority

(d) Poor industry analysis

(e) A cursory financial analysis of borrowers

(f) An excessive reliance on collateral

(g)Infrequent customer contact

(h)Inadequate checks and balance in the credit process.

(i) The absence of loan supervision

(j) A failure to improve collateral position as credits deteriorates.

(k) Poor controls on loan documentation

(l) Excessive overdraft lending

(m) Incomplete credit files

(n) The absence of asset classification and loan loss provisioning standards

(o) A failure to control and audit the credit process effectively.

The issues above lead to credit weaknesses and poor risk selection. The obvious effects are non-performing credits illiquidity of the bank insolvency

2.1.17 MEASURES TO AVOID BAD AND DOUBTFUL DEBTS:

Banks credit analysts ensure that the principles of sound lending are set in motion to achieve a healthy loans and advances portfolio. This entails the establishment of comprehensive lending policies, proper credit analysis which includes analysis of financial history, viability analysis, feasibility studies, case flow projections, ratio analysis and a proper assessment of the borrower using the basic cannons of lending as discussed earlier, and yield calculations including profitability considerations.

It is generally agreed that credit monitoring and controls assist in early detection of bad loans and determination of deteriorating accounts. In this case, the following indicators are usually considered.

1. Increased facility not resulting in increased turnover
2. Fall in credit turnover indicating a reduced sale volume
3. Fall in debit turnover with or without increase in average utilization of facilities.
4. Failure to meet all commitments as they fall due
5. Failure to meet loan repayments/interests as they mature
6. Cross-firing or kite flying
7. Frequent excesses over approved limits
8. Development of hard core-failure to revert to credit or low debit figures when the overdraft is expected to be fluctuating
9. Deterioration of balance sheet or liquidity

A deterioration of the account should sound a warning to the lending banker to put corrective measures into effect.

2.1.18 RECOVERY/REACTIVATION OF BAD ACCOUNT:

Many banks do not rush to realize the security offered by the customer as soon as a facility goes bad. This is because of the adverse publicity this gives especially if this occurs frequently. Realization of the asset occurs as a last resort, in many cases. Banks, however, resort to recovery efforts geared at ensuring that the accounts are reactivated and fresh repayment proposals put into effect for the customer. This essentially involves rescheduling, restructuring or refinancing. All these are with a view to ease the burden of the borrower.

Furthermore every bank has to develop and implement comprehensive procedures and information systems to follow up the condition of individual credits. An effective loan monitoring system according to Odufuye (2007), will include measures to:

- Monitor compliance with established covenants,
- Assess, where applicable, collateral coverage. Relative to creditor's current condition;
- Identify contractual payment delinquencies and classify potential credits on a timely basis, and,
- Direct actions at solving problems promptly for remedial management.

Loan monitoring which is the work of the relationship manager in most cases is not a choice, but an imperative for effective and efficient credit administration in the banking sector. Problem loans can easily be spotted out. The banker's experience, knowledge of the customer can be a guide in taking a decision as to how far the customer can be supported before declaring the loan as bad.

In some occasions, the customer may be in need of more support. Any or a combination of the following strategies can then be employed:

a) Alteration or waiver of some of the terms and condition of loan covenant in a way not to tamper with the bank interest. However, this must be communicated to the credit department.

b) Issues of additional collateral security, if available.

c) Granting of additional funds. If borrower's circumstances and analysis require the need.

d) Extension of loan repayment period supported by fresh cash flow statement.

2.2 EMPERICAL REVIEWS

Kargi (2011) evaluated the impact of credit risk on the profitability of Nigerian banks. Financial ratios as measures of bank performance and credit risks were collected from the annual reports and account of sampled banks from 2004-2008 and analysed using descriptive, correlation and regression techniques. The findings revealed that credit risk management has a significant impact on the profitability of Nigerian banks. The findings revealed that bank's 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.

Epure and Lafuente (2012) examined bank performance in the presence of risk for Costa-Rican banking industry during 1998-2007. The results showed that performance improvements follow regulatory changes and that risk explains differences in banks, and non-performing loans negatively affect efficiency and return on assets while the capital adequacy ratio has a positive impact on the net interest margin.

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-preforming loan and profit were collected for the period 2004 to 2008. The finding revealed that the bulk of 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.

Chen and Pan (2012) examined the credit risk efficiency of 34Taiwanese commercial banks over the period 2005-2008. Their study used financial ratio to assess the credit risk and was analysed using Data Envelopment analysis (DEA). The credit risk parameters were credit risk technical efficiency (CR-TE), credit risk allocative efficiency (CR-AE) and risk cost efficiency (CR-CE). The result indicated that only one bank is efficient in all types of efficiencies over the evaluated periods. Overall, the DEA results show relatively low average efficiency levels in CR-TE, CR-CE and CR-CE in 2008.

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 (ROA) both measuring profitability were inversely related to the ratio of non-performing loan to total loan of financial institutions thereby leading to decline in profitability.

Ahmad and Ariff (2007) examined the key determinants of credit risk of commercial banks on emerging economy banking systems compared with the developed economies. The study found that regulation is important for banking systems that offer multi-products and services; management quality is critical in the case of loan-dominant banks in emerging economics. An increase in loan loss provision is also considered to be a significant determinant of potential credit risk. The study further highlighted that credit risk in emerging economy banks is higher than that in developed economies.

Al-Khouri (2011) assessed the impact of bank's specific risk characteristics, and the overall banking environment on the performance of 43 commercial banks operating in 6 of the Gulf Cooperation Council (GCC) countries over the period 1998-2008. Using fixed effect regression analysis, result showed that credit risk, liquidity risk and capital risk are the major factors that affect profitability is measured by return on assets while the only risk that affects profitability when measured by return on equity id liquidity risk.

Ben-Naceur and Omran (2008) in attempt to examine the influence of bank regulations, concentration, financial and institutional development on commercial banks margin and profitability in Middle East and North Africa (MENA) countries from 1989-2005 found that bank capitalization and credit risk have positive and significant impact on banks' net interest margin, cost efficiency and profitability.

Ahmed, Takeda and Shawn (1998) in their study found that loan loss provision has a significant positive influence on non-performing loans. Therefore, an increase in loan loss provision indicate an increase in credit risk and deterioration in the quality of loans consequently affecting bank performance adversely

Onyiriuba (2009), provided some empirical evidence on how poor stock returns emanating from underperforming Nigerian bank credit portfolio fuelled negative volatilities in foreign exchange, substantial reduction in the aggregate value of capital market and contagions in other sectors of the Nigerian economy.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 INTRODUCTION

The process of this research is to analyse the credit management in the banking industry in Nigeria. A research according to Balsley and Clover (1982:2), “is the answers to significant and pertinent question by use of the scientific method of gathering and interpreting information”. On the other hand, methodology simply means method used in certain process of study. Research methodology therefore is a laid down process adopted in a scientific investigation to discover facts.

The methodology used is descriptive and analytic in nature to permit easy combination of ideas, facilitation of understanding as well as making it congruence to the research methodology.

This chapter in strict adherence to the above definitions attempts the methods with which this research intends to adopt in finding out facts on the subjects. This research shall be based on scientific method since it will enable the researcher to systematically conduct this study in such a manner that could be scientifically verified.

3.2 RESEARCH DESIGN

Nachmais and Nachmais (cited in Baridam 1995:49) posit that research design could be seen as the framework or plan that is used as a guide in collecting and analysing data for a study. It is knowledge of proof that allows the researcher draw inferences concerning causal relationship among the variables under investigation.

This study is made up of Quasi-experimental research otherwise called surveys. This is due to the complex relationship that exists among the variables. According to Baridam (1995:50) “in Quasa-experimental research, the various elements of the design are not under control of the researcher" This type of design is special suited to descriptive studies, which implies natural observation of the characteristics of the research subjects without manipulation of the research.

3.3 SOURCES AND TECHNIQUES OF DATA COLLECTION

Both primary and secondary data is to be used in this study. The main instrument or tool to be used in the collection of primary data is the questionnaire while the secondary data will be obtained from the works of other researchers.

The primary data was obtained by the researcher from the senior and other staff of the bank where the research was focused on, through the administration of questionnaire. The secondary data was collected through the library of The Central Bank of Nigeria, Enugu..

3.4 DESCRIPTI0N OF POPULATION AND SAMPLE PROCEDURE

The population of the study refers to the Banks. But since the researcher does not intend to study the population in this case, she has resorted to use sample size of forty (40). This is because it is only the people who are knowledgeable and also have the ability to influence decision in respect to the banking business that information may be obtained.

Consequently, a sample size of forty (40) persons was drawn from the population using a simple random sampling method. Apart from that, questions relating to the subject of the study were asked. Respondents were required to tick right against the letters they feel is correct and to give opinions where it is required. Out of forty (40) questionnaires distributed, only thirty six were completed and returned. However, this is a fair figure representing 90% of the total sample size. This percentage is acceptable because the researcher expected at least 75% in her assumption. Thus certain generalisations are made in the study.

3.5 METHOD OF DATA ANALYSIS

A frequency count of all responses obtained from the questionnaire in the question for testing are made using chi-square method. The responses are tallied under the following variables:

(i) Yes

(ii) No

(iii) No idea

A scientific method of data analysis was carried out and the data collected was presented in a table and the necessary computation carried out. The chi-square statistical method used was to aid the researcher to explain the data on the questionnaire. The questionnaire scale is based on the research hypothesis.

The chi-square denoted by the Greek letter X^2 is frequently used in testing a hypothesis concerning the difference between a set of observed frequencies. A chi-square is a simple statistics (Osuala 1982:72). It is computed as follows:

$X^2=\sum(fo - fe)/^2fe$, where the parameters are:

X^2=chi-square

Fo= observed frequency

Fe =expected frequency

Chi-square test is non-parametric statistical tool which can be conveniently used in testing hypothesis when dealing with discrete data, (that is, the data are not measured in testing hypothesis or ratio scale) and it is not possible to estimate a population parameter from the sample statistics using hypothesis.

In other words, the chi-square test deals with the application of data that is not on continuous scale of measurement. This implies that the sample data is the count for each category and is thus discrete data. The chi-square is particularly important in analysing data presented in the form of contingency tables of more than two categories as in the study.

3:6 DETERMINATIONS OF CRITICAL VALUES

In determining the critical values or table value, the appropriate number is given or compiled to be able to check up the corresponding value in chi-square using appropriate level of significance.

The degree of freedom is an important feature of the x^2 distribution for the contingency test used. This is given as df=(r-1)(c-1)

Where r = the number of row;

C = the number of column.

The degree of freedom for data arranged in series where "n" is the number of observations. In this case, the observations made are:

1. Yes
2. NO

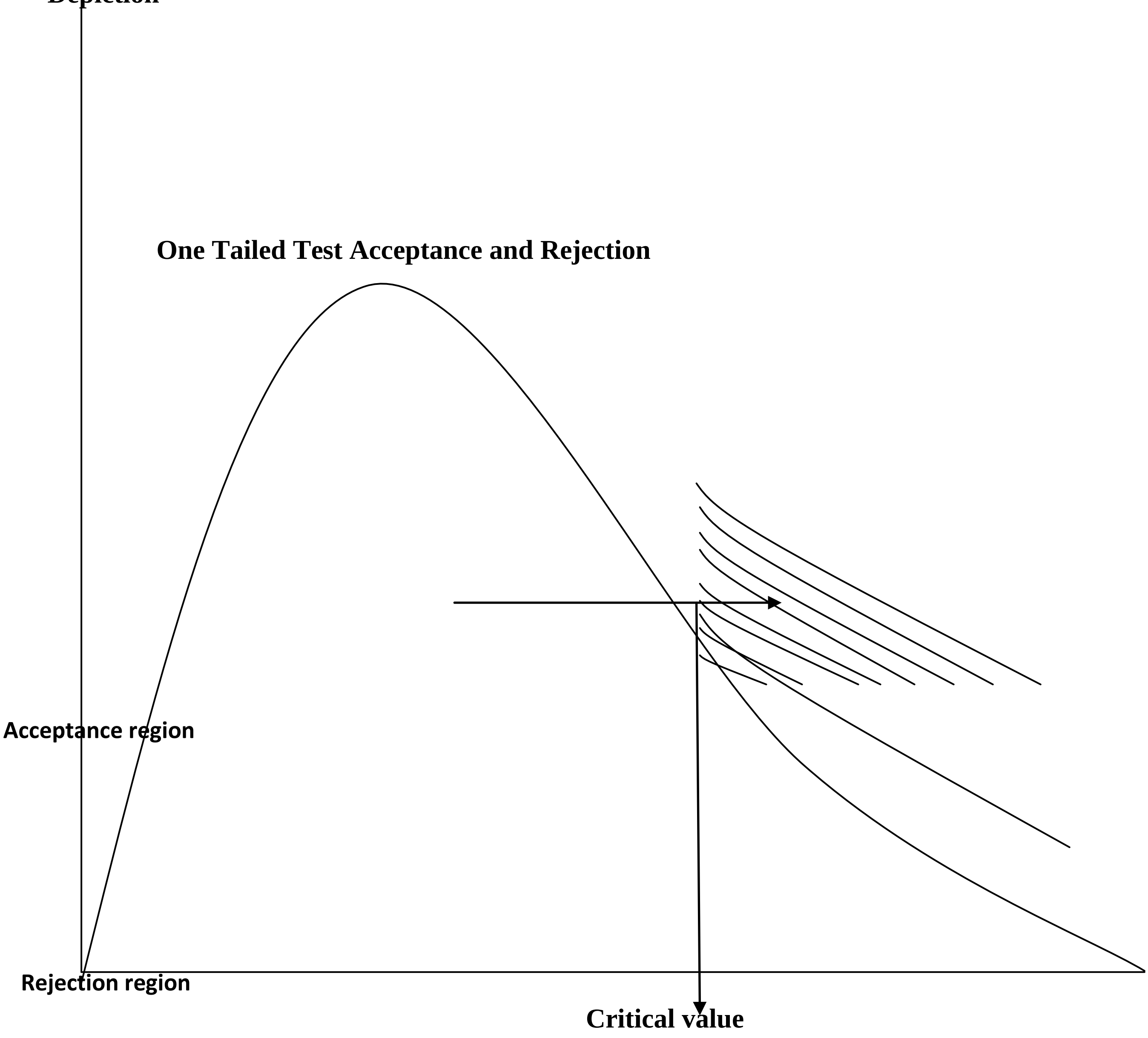
The decisions criteria for accepting or rejecting the null hypothesis have the following characteristics.

The smallest possible number of x^2 is zero. This will only occur when the observed frequencies are equal to the expected frequencies (that is fo-fe=0).

Therefore in all cause, x^2 will have a positive value which increases as the difference between fo and fe increases.

Although, fo must be whole number, fe under chi-square(x2) must not be applied to percentage in analysis of any cause. The x^2 test is always a one tailed test with distribution as shown in the diagram below

Depiction



SOURCES: (Groebner and Schannon 1981:387)

If a 50% or 0.5 significance level is closed in designing a test of hypothesis, what is mean is that we have a chance of five out of hundred that will reject the hypothesis where it should be accepted. In other words we are about 95% confident that we have made the right decision. In this case, we say that the hypothesis has been rejected at 0.05 level of significance; that is we can be wrong with a probability of 0.05.

In determining the acceptance or rejection of the null research hypothesis, the computed chi-square is composed with the table value (under a given significance level) and degree of freedom on which the value depends on the decision rule:

(a) The null hypothesis is accepted if the computed x02 is less than the table value (Accept H0 if $x0^2 < xe^2$).

(b) The null hypothesis is rejected if the computed xo2 is greater than the table value (Reject Ho if $x0^2 > xe^2$)

CHAPTER FOUR

DATA PRESENTATION, ANALYSIS AND INTERPRETATION.

4.1 INTRODUCTION

The chapter is devoted to the presentation of data collected, analysed and interpreted. The research hypothesis are presented in order in which they are stated and data from questionnaires relating to them are analysed in order to give a constructive validation of null hypothesis (Ho)

The objectives of this study as stated earlier are to analyse how credit management affects the banking industry in Nigeria specifically:

- To examine how feasibility study affect loan repayment in banking industry.
- To highlight the extent in which diversion of bank loan to unprofitable ventures affect loan repayment
- To examine how distribution of loans affect banks performance if given proper attention and
- To make recommendation where necessary.

4.2 PRESENTATION OF DATA

To ensure the acquisition of the necessary data needed for the study, forty (40) questionnaires were distributed to selected respondent at the main branch of First bank of Nigeria PLC in Enugu municipality. However thirty six (36) were returned and subsequently used in the study, the number returned represented 90 of the total number.

4.3 ANALYSIS AND INTERPRETATION OF DATA

In this section, the null hypothesis will be to ascertain their validity or non-validity using the chi-square

HYPOTHESIS ONE

H0: Inadequate feasibility study does not affect loan repayment in the banking industry.

Hi: Inadequate feasibility study affects loan repayment in the banking industry.

TABLE 4 .1

Calculation of chi-square (x02) for hypothesis one

Response option	Fo	Fe	Fo-fe	$(fo-fe)^2$	$\sum(fo-fe)^2/fe$
Yes	22	12	10	100	8.33
No	10	12	-2	4	0.33
No idea	4	12	-0	64	5.33
Total	36	36	0	168	13.99

SOURCE: researcher computation

Chi-square computed value ($x0^2$) = 13.99,Fe

At 0.05 level of significance

Degree of freedom (df) = (3-1) (2-1) = 2

From the table: critical value =5.99

Chi-square = 13.99

RESULT ANALYSIS AND INTERPRETATION

From the above table 4, xo^2 computed value,

13.99> critical value 5.99, Therefore, the null hypothesis (Ho) is rejected while the alternative hypothesis (Hi) is accepted which states that adequate feasibility study affects loan repayment in the banking industry.

HYOPTHESIS TWO

HO: The diversion of bank loans to unprofitable ventures doesn’t affect loan repayment.

Hi: The diversion of the bank loan to unprofitable ventures affects loan repayment.

TABLE 4.2

CALCULATION OF CHI SQUARE XO2 FOR HYPOTHESIS TWO

Response option	fo	fe	Fo-fe	$(fo\text{-}fe)^2$	$\sum(fo\text{-}fe)^2/fe$
Yes	10	12	-2	4	0.33
No	24	12	12	144	12.0
No idea	2	12	-10	100	8.33
Total	36	36	0	248	20.66

SOURCE: Researcher's computation

Chi-square computed value $(x0^2)$ = 20.66

At 0.05 level of significance

Degree of freedom (df) (3-1) (2-1) = 2

From the table: critical value xo^2 = 5.99

RESULT ANALYSIS AND INTERPRETATION

From the table 4.2, xo^2 computed value

20.66 critical value 5.99.therefore, the null hypothesis (HO) is rejected while the alternative hypothesis (Hi) is accepted which states that the diversion of bank loan to unprofitable ventures affects loan repayment.

HYPOTHESIS THREE

H0: The problem of poor attention given to distribution of loans has effect on bank's performance.

Hi: The problem of poor attention given to distribution of loans has no effect on bank's performance.

TABLE 4.3

CALCULATION OF CHI-SQUARE (X02) FOT HYPOTHESIS THREE

Response option	Fo	fe	Fo-fe	$(fo\text{-}fe)^2$	$\sum(fo\text{-}fe)^2/fe$
Yes	16	12	4	16	1.33
No	14	12	2	4	0.33
No idea	6	12	-6	36	3.0
Total	36	36	0	56	4.66

SOURCE: Researcher computed

Chi-square computed value ($X0^2$) = 4.66

At 0.05 level of significance

Degree of freedom (df) (3-1) (2-1) = 2

From the table: critical value ($X0^2$) = 5.99

RESULT ANALYSIS AND INTERPRETATION

From the table 4.3 $X0^2$ computed value 4.66 <critical value 5.99 therefore, the null hypothesis (Ho) is accepted while the alternative hypothesis (Hi) is rejected. We can then say that the problem of poor attention given to distribution of loan has effect on bank's performance.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1) INTRODUCTION

This chapter is divided into three distinct parts. The first part is concerned with the summary of the whole study from the beginning to the end. The second part deals with the conclusion where inferences and generalization were made or drawn from. Findings in the analysis of the study formed the recommendation section which brought the research to an end.

5.2 SUMMARY OF FINDINGS

This study was directed towards perhaps the most sensitive problem on credit management in the banking industry in Nigeria.

The study was organized with five chapters. Chapter one introduced research topic under the background of the study, the chapter also stated the problems, objectives, significance of the study, limitations and as well as definition of relevant terms used in the study.

Chapter two focused on the review of literature related to the topic, while chapter three shows the research methodology used in gathering the relevant information needed, the decision and the administration of the questionnaire, and equally the parameters used for the analysis of the questionnaire.

Chapter four focused on the presentation, analysis and interpretation of data collection from the bank used. Finally the fifth chapter draws conclusion and also makes recommendation, which if adhered to, can enable banks manage their loans, recover their loans and make higher profits.

From the findings on hypothesis tested (under chapter four), the result showed the following:

That inadequate feasibility study affects loan repayment in the banking industry, That the diversion of bank loan to unprofitable ventures affect loan repayment; and

That the problem of poor attention given to distribution of loan has negative effect on banks performance.

5.2 CONCLUSION

The issue of non-performance of assets and declaration of fictitious projects has become the order of the day in our banking system. This is a result of poor credit management in the sector causing many banks to have become distressed. The study therefore, focused on credit management in banks with particular references to Frist Bank of Nigeria. Plc. Data collected and hypothesis tested revealed that inadequate feasibility study affects loan repayment; the diversion of bank loan to unprofitable ventures affects loan repayment and the problem of poor attention given to distribution of loan has negative effect on banks performance in the economy.

5.4 RECOMMENDATION

Taking cognizance of the problem of the study together with researcher’s personal observations, it is believed that if they are strictly adhered to, some of the problems surrounding credit management which banks are encountering will be a thing of the past. The recommendations are as follow:

Banks should establish sound and competent credit management units and recruit well-motivated staff. Credit officers are the cutting edge of credit programmes. They perform a range of functions from project appraisal through credit disbursement and deposit mobilization to loan collection. Issues restraining to their selection, training, placement, job evaluation, reward and discipline need to be tackled effectively.

Proper loan appraisal and follow-up, including very careful loan screening procedure and timely disbursement of approved loan should be undertaken by credit officers to reduce delinquencies and default.

Precaution in credit administration is important in reducing credit risk and can be achieved through (i) demand for appropriate collateral security before granting loans, and (ii) Effective loan supervision and monitoring by credit officers.

Banks in Nigeria should enhance their capacity in credit analysis and loan administration while the regulatory authority should pay more attention to bank compliance to relevant provisions of the Bank and other Financial Institution Act (1999) and prudential guidelines.

There should be credit manual, which should be strictly adhered to at every stage of the credit process when credits are administered and managed in accordance with laid down policies and procedures, the occurrence of reckless un-suitable credits and poor loan administration will be drastically reduced or eliminated.

Banks should ensure that the chief executive avoids ‘approval in principle in the credit process. Approval in principle is anticipating approval given by chairman in time of exigency and it is expected to ratify by the board of directors even when the outcome of the transaction is unknown and unfavourable. This has caused some banks’ chief executives their job in the past. It is advisable to adhere to laid down credit process/procedure.

Bankers are advised to imbibe the spirit of ‘’after-sales-services ‘’. They should monitor the credit process as to prevent possible diversion of funds. There is a great danger in not monitoring a customer for it can lead to bad loan.

Banks should have a monitoring and control units or department to carry out a sort of post-mortem exercise by way of controlling and monitoring credit facilities and also ensuring completeness of all conditions precedent to draw down.

They should put in place proper credit documentation which serves as the official documentation verifying the existence of a credit facility and contains information relating to the credit. This will aid banks in recovery when the loan goes bad

Credits should also be extended within the target nerves and lending strategy of the institution. Identifying to the key feature of credit origination to be the assessment of the risk profile of the customer /transaction, banks should develop procedure that adequately capture salient issues regarding the borrower's industry, macro-economic factors, purpose of the credit, source of repayment, track record and repayment history of the borrower, repayment capacity of the borrower, the proposed terms and conditions, adequacy and enforceability of collaterals and appropriate authorization for the borrowing.

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APPENDIX

Department of Banking and Finance
Caritas University
Amorji-Nike,
Enugu State.
30/07/2013.

Dear respondent,

RESQUEST FOR THE FILLING OF QUESTIONNARE

I am a final year student of the above mentioned department and University. As part of the requirements for the Award of degree in the university, I am carrying out a research project on Analysis of credit management in the Banking Industry.

I therefore request you to please supply the information being sought for as stated in the attached questionnaire so as to assist the researcher to arrive at rational conclusion.

Your identity will not be revealed in any form so feel free to complete the questionnaire with objective and independent judgment. Thanks

Yours faithfully,

Akwu Obaje Fatima

QUESTIONNAIRE

Please tick (√) as appropriate in the box provided after each question and comment where necessary

SECTION A

NAME.…………………….

SEX.....…………………….

AGE.................................

NATIONALITY………......

DESTINATION.……........

Which of the following age rank do you belong? (20-34) (35-49) (50-64) (60 and above)

SECTION B

What is the objective of credit management in commercial bank?

To increase profitability in the banking sector.

To aid the country's economic growth and development.

All of the above.

Does first Bank of Nigeria plc. Check on the credit stand of their customers before granting loan facility?

a. yes

b. No.

What types of credit facilities does your bank render to its customers?

A) Short term loans

B) Medium term loans

C) Long term loans

D) Overdraft

E) All of the above

9. Which of these credit facilities rendered by your bank to customer requires collateral securities?

a) Agriculture

b) Housing loans

c) Industrial loan

d) Vehicle loans

e) All of the above

10. Does inadequate feasibility study affect loan repayment in the banking industry?

(a) Yes (b) No(c) No idea

11. The diversion of bank loans to unprofitable venture does not affect loan repayment.

(a) Yes (b) No(c) No idea

12. The problem of poor attention given to the distribution of loans affected bank performance.

(a) Yes (b) No(c) No idea

13. What are the acceptable securities for your bank's credit facilities?

Building (b) Plot of land with certificate(c) A reputable guarantor (d) all of the above

14. What measures has been most effective to your bank in recovery of bad debt from its customers?

(a) Communication (b) personal follow-up(c) court action (d) accounting of collateral securities

15. Do you usually have default in payment of loan?

(a) Yes (b) No

16. Do you charge interest on over-due account?

(a) Yes (b) No

17. Which of the following is the cause of default on the part of the customer's?

(a) Failure of project (b) diversion of fund(c) government action (d) all of the above

18. Has adhering of strict guideline by your staff in loan appraisal increased the rate of default?

(a) Yes (b) No(c) No idea

19. Does your bank go into proper feasibility studies of customer's business or project before granting loan?

(a) Yes (b) No

20. Does improper feasibility studies affect your bank negatively?

(a) Yes (b) No

21. Are banks really aware of the need for collateral securities?

(a) Yes (b) No