CREDIT RISK MANAGEMENT PRACTICES AND FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

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DECLARATION

Declaration by the Student

I declare that this project is my original work and has not been submitted for an award of a degree in any other University for examination purposes.

Signature.. Date..

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Declaration by the Supervisor

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DEDICATION

I happily dedicate this work to my wife.

ACKNOWLEDGEMENT

I like to thank my Supervisor Mr. Dominic Ngaba, for his undivided support during the writing of this project. His patience and understanding, he went a long way in ensuring I came up with a quality project. The support in guiding me step by step and assisting me to ensure that I finalize with the project in time, and his unlimited assistance is the reason I managed to come up with a final copy. Finally, I thank my wife for reading through the project page by page to ensure errors and omissions are minimized.

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OPERATIONAL DEFINITION OF TERMS

Credit Appraisal Practice This refers to the review of client's documents to ensure he/she is credit worthy.

Credit Collection Policies Credit collection policies refer to systems and procedures put in place by a bank to secure repayment of loans when they fall due

Credit Control Practices This refers to activities geared towards ensuring loans are granted adequately and used for the intended purpose.

Credit Risk This is the possibility of a loss resulting from a borrower failing to honor his contractual obligation of repayment as agreed

Credit Risk Management This refers to measures of curbing uncertainties associated with loans through assessment of risks and strategy developing

Credit terms and Conditions

It refers to requirements to be met before commercial banks issue out loans to clients

Non-Performing Loan This refers to a loan where payment of interests or repayments of principal are not being paid by the borrower and it may become a bad debt.

ABBREVIATION AND ACRONYMS

ABS	Asset Backed Securities
ANOVA	Analysis of Variance
CBK	Central Bank of Kenya
DFI	Development Finance Institution
MFI	Microfinance Institutions
ROE	Return on Equity
SACCO	Savings and Credit Cooperative
SSA	Sub-Saharan Africa

ABSTRACT

Commercial banks all over the world enhance the economic growth of nations by providing funds to customers of investments. The survival of commercial banks like every other financial institution depends largely on their profitability. However, the profitability of these banks is dependent on the risk management practices which they adopt. This is because granting of loans to borrowers is accompanied with its own risks. Credit risk is regarded as the most adamant risk faced by banks due to the nature of their activities. Studies relating to credit risk management practices were done in developed and other developing countries other than Kenya. Similarly, some of these studies focused on microfinance banks and Sacco societies. These studies among other findings have indicated a high default rates among commercial banks which in turn leads to their low performances. The current study sought to fill the conceptual and contextual gap in literature by focusing on credit risk management practices and commercial banks financial performance in Kenya. Therefore, the specific objectives of the study were to determine the effect of client appraisal, credit terms and conditions, credit collection policies and credit control practices commercial banks' financial performance in Kenya. Also, to assess the moderating influence of interest rates on the relationship between credit risk management practices and commercial banks' financial performance in Kenya. The research utilized descriptive research design and the sampling design was purposive sampling design. The research made use of a multiple regression model for the analysis. Findings of the study indicate that there exist a positive and significant effect of credit risk management practices that is, credit terms and conditions, client appraisal, credit practices and credit control practices on financial performance of commercial banks in Kenya. However, the study found an insignificant moderating effect of central bank rate on the relationship between credit risk management practices and financial performance of commercial banks in Kenya. The study recommends that credit managers should come up with efficient terms and conditions and client appraisal that will enhance credit control and collection. The study recommends that further studies on credit risk management practices and financial performance of banks should consider the moderation effect of bank specific interest rates.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The banking sector plays a vital role in the economic resource allocation of countries all over the world (Ongore, 2013). Banks promote a nation's economy by availing funds to borrowers for investments (Otuori, 2013). Notably, the profitability of Commercial banks has been very high in Sub-Saharan Africa (SSA), average returns on assets were about 2 percent over the last 10 years, which is significantly above the returns of banks in other parts of the world (Flamini, Valentina, McDonald, & Liliana, 2009). The high return as earmarked by Ongore (2013) is attributed to; investment in risky projects and the huge gap which exists between the demand and supply for services offered by banks. Implying that there exist few banks as compared to demand for bank services in SSA which results in high interest rates charge as a result of less competition.

Financial systems are the nerve centers of economic development across the globe. They provide intermediation services via bringing together savers and investors through channeling funds to investments that guarantee positive return. Financial institutions aid the diversification and pooling of risks, mobilization of savings and allocation of resources (Ongore, 2013; Arora & Kumar, 2014). However, in some developing countries, the banking sector has experienced several cases of collapses, these banks include Savannah Bank Plc in the 90's, Societe General Bank Ltd which occurred in early 2000's, and Alpha Merchant Bank Ltd, (for Nigeria). In the case of Kenya, notably the case of chase bank among others which have attracted the attention of stakeholders which include professionals and policy makers.

One of the core pillars of financial intermediation is lending which is accompanied with the risk of default which affects the performance of banks. McNaughton (1992) asserts that is a vital role of commercial banks, therefore, banks succeed when the risk management practices and appropriate. Anyanwu (2014) is of the view that for banks to ensure they survive the adherent lending risk and cater for the financial needs of the economy, they must relook at their bureaucratic tendencies. The bureaucratic tendencies can hinder loan applicants from obtaining credit at the right time, which in turn affects businesses.

1.1.1 Credit Risk Management Practices

According to Conford (2010), credit risk refers to the uncertainty that the actual return on achievement or loan extracted will deviate from expectations. This implies that credit risk is the losses from the inability or refusal of borrowers repay loans in full or on time. Therefore, credit risk management refers to the practice of mitigating against those losses associated with lending by commercial banks and other financial institutions. Waweru and Kalam(2010) identified volatile interests, inadequate organizational capacity, inappropriate laws and loan policies and poor management as the main causes of credit risks.

Credit terms and policies refer to the rules and guidelines under which commercial banks issue loans to customers. The period and interest rates of loans are indicated in the credit terms. The period of time in which loan is issued is known as credit period. The length of the credit period is often determined by the size of the account, collateral value, credit risk and the market compensation (Panday, 2008). Credit terms may also include discount terms offered to borrowers

as an incentive to prompt repayment or grace period before starting the repayment. However, the credit policies of banks often change with economic conditions (Kibor, Ngatu & Kwasira, 2015).

Loan appraisal is a request or application for funds, evaluated by financial institutions. The areas of interests in appraisal usually are: the client's purpose of borrowing, need genuineness, character of the borrower, repayment capacity of the borrower, quantum of loan and security (Boahene, Dasah & Agyei, 2012). Client appraisal is used to enhance loan performance. Gathering of relevant information from borrowers is a critical task in the effective screening of borrowers as indicated by Asymmetric Information theory. The first measure in addressing credit risk involves the client screening in order to ensure that borrowers are willing and capable of repayment of a loan. The 5Cs credit model is employed by banks in evaluating potential customers (borrowers) (Abedi, 2009). The model aids banks in enhancing performance by helping them know their customers better.

Credit collection policies refer to systems and procedures put in place by a bank to secure repayment of loans when they fall due. The systems are put in place to enquire about late loan payments through measures which include text messages, telephone calls, letters and personal visits (Arora & Kumar, 2014).Collection procedure is a recommended measure used to recover the amounts due from customers within the law. However, collection aspects might vary from one institution to another institution (Chepkoech, 2015). The procedures usually come in place only when the borrower's account becomes overdue (Waweru & Kalam, 2010).

1.1.2 Financial Performance

Bank performance is of great concern to all stakeholders, these stakeholders include the debtors, the owners, the managers of banks, the investors, the regulators, the creditors, the depositors and the government (Bentum, 2012). Bank performance serves as a guide for stakeholders in in their decision making. Bentum, (2012) asserts that performance provides debtors and investors with directions in decision making as to whether or not to invest money in an organization. Furthermore, it gives directions to bank management as whether to improve its financing and which method of financing.

The performance of Kenya commercial banks has been on a declining pattern as reported by World Bank (2016), their return on equity (ROE). The ROE stood at 25.98% as at 2010 which declined to 23.10% in 2011. Furthermore, the decline extended to 21.99% in 2012, 20.94% in 2013 and 20.88% in 2015. Similarly, the year 2015 saw the ROE further decline to 17.39%. Baba and Nasieku (2016) recommended that further studies in determining banks' financial performance should consider internal factors such as credit risk management practices among other factors. This study made use of ROE as an indicator for banks' performance.

1.1.3 Credit Risk and Financial Performance

Survival of most financial institutions lies on how successful their lending program is and repayments of loans made by the borrowers to them (Sindani, 2012). Therefore, this requires that an effective credit control system is installed in order to minimize unnecessary lending thus, improving on profitability of the banking sector (Kakuru, 2010). Credit management is solely an

executive task of ascertaining customer's credit ratings which forms part of credit control function.

Broll *et al*. (2002) asserts that credit risk is the oldest and usually the most common risk for lending institutions which has brought about innovations in order to curb this problem. The risk stems from the probability of a default on loan payments by clients, which ultimately jeopardizes the banks' capital. Therefore, considering the fact that asymmetric information is inherent among lenders and borrowers, banks must put in place mechanisms that minimizes and curbs information asymmetry problems which are moral hazards and moral hazards.

Repayment of loans is of high importance, therefore and effective system that will ensure borrowers repay loans is vital in addressing asymmetric information problems and in reducing loan default rates, thus ensuring the long-term stability of the banking sector. Credit risk management is an important ingredient in achieving optimum performance of lending institutions (Rukwaro, 2001). An effective credit risk management system put in place minimizes the risk of loan default.

1.1.4 Overview of Banking Sector in Kenya

Kenya banking industry is under the Banking Act, the Companies Act, the Central Bank of Kenya Act and the Central Bank prudential guidelines.1995 ion and lifting of exchange controls of the banking sector (Otuori, 2013). The Central Bank is responsible for formulation and implementation of monetary policies among other functions of fostering the liquidity of the financial system (Chepkoech, 2015). The reporting and publishing of information regarding Kenya's banking sector are one of the sole responsibilities of CBK (Otuori, 2013). Also, the

umbrella body for banking institutions in Kenya is known as Kenya Bankers Association which seeks to protect the interest of member institutions by addressing issues affecting banks.

The banking sector in Kenya comprises of 13 and 40 foreign owned and locally owned banks respectively (Central Bank of Kenya, 2015). Ongore (2013) put forward that in respect to asset holdings, 35% of banking assets is attributed to foreign banks as of the year 2011. The financial sector of Kenya is highly dominated by commercial banks, therefore, the stability of these banks is of utmost importance. This is attributed to the fact that the collapses in the banking sector may have multiplier effects on the country's economy as a whole (Ongore, 2013).

1.2 Statement of the Problem

Banks depend on their profitability in order to survive the dynamic nature of their environment. High banks' performance results in the growth and development of countries. Financial intermediation is the major role played by banks, however, this role comes with its own risk which is he risk of default. Kenya banking sector has been faced with many challenges which include low performance as a result nonperforming loans which have threatened the stability of banks (Chepkoech, 2015). The survival of commercial banks like every other financial institution depends largely on their profitability. However, the profitability of these banks is dependent on the risk management practices which they adopt. This is because granting of loans to borrowers is accompanied with its own risks. According to Ali (2015) Credit risk is the most significant risk faced by banks due to the nature of their activities.

The banking sector was at the center of the world's recent financial crisis. The fall in value of their asset portfolios, which was largely attributed to their poor credit management, formed one

of the major causes of this crisis. In Kenya, a number of banks have collapsed which include the Capital Finance Ltd and chase bank among others. Similarly, Njanike (2009) opined that the absence of effective credit risk management practices brought about the banking crises and the global financial crises at large. The seemingly trend poses a threat to commercial banks' sustainability and financial viability which could hinder the availability of loans to the rural unbanked areas.

Credit risk management and banks' performance have sparked the interests of many scholars. This is because poor credit management has led to the collapse of some banks which has caused panic in the society (Kiplimo and Kalio, 2012). Adekunle, Alalade, Agbatogun and Abimbola (2015) carried out a study how credit risk management affects financial performance of selected Commercial Banks in Nigeria and found that credit risk management has significant effect on financial performance of commercial banks. However, the study used cross-sectional research design. Mogga, Mwambia and Kithinji (2018) study focused on how credit risk management affects the financial performance of commercial banks in Juba city, South Sudan and established a positive and significant effect between credit risk management and financial performance. It is due to this regard that this study sought to investigate the effects of credit risk management practices on financial performance of commercial banks in Kenya.

1.3 Objectives of the Study

1.3.1 General Objective

The general objective of this study was to determine the effect of credit risk management practices on financial performance of commercial banks in Kenya.

1.3.2 Specific Objectives

The specific objectives of the study were:

i. Determine the effect of credit terms and conditions on commercial banks' financial in Kenya.

ii. Assess the effect of client appraisal on commercial banks' financial performance in Kenya.

iii. Determine the effect of credit control practices on commercial banks' financial performance in Kenya.

iv. Establish the effect of credit collection policies on commercial banks' financial performance in Kenya.

v. Assess the moderating impact of interest rates on the relationship between credit risk management practices and commercial banks' financial performance in Kenya.

1.4 Research Hypotheses

The following hypotheses guided the study:

H_{01}: Credit terms and conditions have no significant effect on commercial banks' financial performance in Kenya.

H_{02}: Client appraisal has no significant effect on commercial banks' financial performance in Kenya.

H_{03}: Credit control practices have no significant effect on commercial banks' financial performance in Kenya.

H_{04}: Credit collection policies have no significant effect on commercial banks' financial performance in Kenya.

H_{05}: Interest rates have no significant moderating impact on the relationship between credit risk management practices and commercial banks' financial performance in Kenya.

1.5 Significance of the Study

This study was of significance in various ways. First, the Government of Kenya would benefit from the study as it would help policy makers in policy formulation relating to the banking sector. Secondly, the study would educate members of the society on credit risk management practices and banks' performance. Furthermore, the study would form a basis for future researchers who wish to carry out more investigations in similar area of study.

1.6 Scope of the Study

The research focused on all commercial banks situated in Kenya for the period 2012 to 2016 thus, making it the time scope of the study. Thus, the study was centered on 43 commercial banks which existed during the study period. The research made use of a multiple regression model for the analysis of the study.

1.7 Limitation of the study

The most common limitation that a researcher encounters when using primary data is respondent's attitudes towards the questionnaire. Some of the respondents may be unwilling to reveal the true information needed for the study. This can be attributed largely to the fear of being blackmailed. However, the researcher addressed this challenge by convincing the respondents that their responses will strictly be used for the purposes of learning only.

1.8 Organization of the study

This study was organized in five chapters. Chapter one comprise of the background to the study, research problem, objectives of the study, purpose of the study, research questions, significance of the study, scope of the study, limitation of the study and assumptions of the study. Chapter two comprise of the theoretical review, empirical review, conceptual framework, knowledge gaps and summary of the literature review. Chapter three comprise of the research methodology, that is, research design, target population, sampling and sample size, data collection instruments, pilot study, data collection techniques, method of data analysis and ethical issues. Chapter four comprise of the research findings and discussion and finally, chapter five comprise of the summary of the findings, conclusion and recommendations.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

Chapter two comprises of the literature review of the study; the theoretical and literature review of the study are presented in this chapter.

2.2 Theoretical Review

Asymmetry Information theory, Modern Portfolio theory and 5 C's Model of Client Appraisal were used to provide more insight in the study.

2.2.1 Asymmetry Information Theory

In lending, information asymmetry exists when a client usually the borrower who applies for a loan usually poses superior knowledge on the potential risks and returns regarding the business or investments for which the loan is being applied for (Arora & Kumar, 2014). The lender usually doesn't have complete of information about the borrower and the intended project. In the context of financial institutions, information asymmetry problems are generally categorized into two, that is moral hazard and adverse selection (Rukwaro, 2001). Commercial banks encounter challenges in addressing these dominant problems because it is not rational to commit financial resources for monitoring and appraisal of small amounts of loans. This is because the data needed to screen applicants and monitor borrowers may have some costs attached to it (Ali, 2015). Therefore, commercial banks face a problem of information asymmetry in their operations.

Asymmetry theory relates to this study in that it explains how borrowers outsmart lenders by taking advantage of the superior knowledge which they have over them (commercial banks) by not making available all vital information. Particularly, information that may increase the rate of interest to be charge or that which will jeopardize the chances of securing a loan. The theory was associated to credit terms and conditions variable.

2.2.2 Modern Portfolio Theory Model

Modern portfolio theory introduced by Markowitz (1954) was refined and extended by the likes of Tobin (1918) and later Sharpe (1934), among other scholars in the subsequent years. This is a finance theory which seeks to maximize the expected returns of portfolio with consideration to specified amount of portfolio risk. In other words, it seeks to minimize risk as guided by a given rate of expected return, by choosing in the right proportions of various assets. The portfolio theory views diversification as a way of maximizing expected return of portfolios. It integrates the process of efficient portfolio formation to the pricing of individual assets. It is of the view that diversifications in this case holding an adequate combination of financial assets aids in the elimination of risk associated with individual assets (Bodie *et al.*, 1999).

Modern Portfolio theory asserts that the selection of assets in an investment should not be selected individually with each on its own merits. But, when selecting assets in an investment what should be considered is the responses in prices of each asset in respect to the changes in prices of the other assets in the investment portfolio. In investments, a tradeoff lies between risk and expected return (Kargi, 2011). Therefore, the higher the risk involved, the higher the expected returns and vice versa. MPT provides ways of selecting a portfolio with the highest rate

of return possible, given an amount of risk. Similarly, given an expected rate of return, MPT provides ways of selecting a portfolio having the lowest possible risk. The theory explained the credit control practices variable.

2.2.3 The 5 C's Model of Client Appraisal

The 5Cs model is an instrument used by financial organizations in credit management in evaluating a potential customer (Abedi, 2009). The 5Cs include collateral, character, condition, capital and capacity. Character is used in estimating the credit worthiness of a customer, it is usually used in weighting values for the different characteristics of the customer (Njanike, 2009). Economic, cultural and personal factors are believed to influence a customer (Ouma, 2008; Migiri, 2012). Similarly, the psychological factor is not dependent on an individual's visible evidences of achievement but on his inner worth. These factors are considered by banks by enquiring and studying about the customer (Kibor *et al.*, 2015).

The 5 C's Model relates to this study as it explains that financial institutions' performance is enhanced by their loan performance of financial institutions. Client appraisal is used to minimize default which in turn enhances loan performance. The first step in curbing credit risk entails the screening of customers to ascertain their ability and willingness of loan repayment. The 5Cs model is employed by commercial banks in evaluating a potential customer (Abedi, 2009). These help banks in getting to know customers better and improve performance. 5Cs help banks to enhance the performance of loans, as it aids lenders to get to know their clients (borrowers) better (Waweru & Kalam, 2010). However, the 5 C's model of client appraisal is not considered on first time application. The theory was linked to client appraisal variable.

2.3 Empirical Review

This section looks at empirical studies relating to credit risk management practices and performance.

2.3.1 Credit Terms and Conditions on Financial Performance

Byaruhanga (2017) carried out a study on the relationship between Credit terms, credit accessibility and performance of agricultural cooperatives in Rwanda. A random sample of 196 active agricultural cooperatives was obtained from various districts in the southern province. Correlation and regression models were used. The findings revealed a positive and significant relationship between credit terms, credit accessibility and the performance of agricultural cooperatives.

Nyawera (2016) study examined the effect of credit policy on the financial performance of Deposit Taking Microfinance Institutions in Kenya. The researcher used a census approach for the six deposits taking micro finance organizations in Kenya. The findings indicated a positive significant relationship implying that credit policies affects the financial performance of deposit taking micro finance organization.

Chepkoech (2015) studies credit risk management and Micro Finance Institutions performance in Nairobi County. The target population of the study was all the 261 employees drawn from selected Micro-Finance Institutions in Nairobi County. The study adopted a multiple regression analysis. Empirical findings of the research show that credit terms and conditions have a significant positive effect on the performance of MFIs in Nairobi County. However, the study

was based on Micro Finance Institutions. The current research will fill this gap by focusing on commercial banks in Kenya.

Kithinji (2010) look at credit risk management impact on performance of commercial banks situated in Kenya. Data was collected on profits and non-performing loans of commercial banks from the period 2004 to 2008. The results of the study show that credit terms and conditions have a positive impact on the performance of commercial banks. However, the study did not consider the interest rates systems of the banks and their moderating impact on the relationship between credit risk management and banks' performance situated in Kenya.

2.3.2 Client Appraisal and Financial Performance

Njeru, Mohammed and Wachira (2017) study investigated the relationship between effectiveness of credit appraisal on loan performance of Commercial Banks in Kenya. Descriptive research design was used. Data was collected using a self-administered questionnaire. Credit appraisal was found to be very important in influencing performance of commercial banks. Findings also revealed that lending placed much reliance on use of past information and thus credit referencing and credit history were applied more in credit appraisal.

Chepkoech (2015) assessed credit risk management practices impact on Micro Finance Institutions' performance in Nairobi County. Target population of the study was all the 261 employees drawn from selected Micro-Finance Institutions in Nairobi County. The study analysis was done using a multiple regression model. Results of the study show that client appraisal has a significant positive effect on the performance of MFIs in Nairobi County. Notably, the study was based on Micro Finance Institutions

Gaitho (2010) studied credit risk management practices and Saccos' performance in Nairobi. The research showed that credit risk management is adopted by majority of the saccos in Nairobi. Empirical results indicate that client appraisal has a significant relationship with performance of saccos in Nairobi. However, this study was based on saccos, the current study was based on commercial banks situated in Kenya.

Korir (2011) carried an empirical analysis of credit risk management impact on Deposit Taking Microfinance institutions financial performance in Kenya. The research is of the view the credit risk management practices are adopted by Deposit taking microfinance institutions in Kenya to mitigate against the credit risks which they are exposed to. The results of the research show that client appraisal has a significant positive relationship with performance of deposit Taking Saccos. However, the study focused on Microfinance Institutions. The current study is centered on commercial banks situated in Kenya

2.3.3 Credit Control Practices and Financial Performance

Olabamiji and Michael (2016) carried out a study on how credit management practices affect bank performance: Evidence from First Bank. Data was collected using Purposive sampling technique. Both descriptive and inferential statistics were used to analyze data. The result revealed that credit management practices have a significant positive influence on the financial performance of First bank. The result concluded that client appraisal, credit risk control, and collection policy are major predictors of financial performance of First bank.

Chepkoech (2015) studied credit risk management practices and Micro Finance Institutions' performance in Nairobi County. Target population of the study was made up of all the 261

employees drawn from selected Micro-Finance Institutions in Nairobi County. The study adopted a multiple regression analysis. Results of the research show that credit control practices have a significant positive effect on the performance of MFIs in Nairobi County. However, the study was based on Micro Finance Institutions and the research failed to incorporate the moderating effect of interest rates on the relationship between credit risk management practices and performance of MFIs in Nairobi County.

Gaitho (2010) studied credit risk management practices and Saccos' performance in Nairobi. The research attributes credit control as a vital credit risk management practices. The research results indicate that credit control practices has a significant relationship with Saccos' performance in Nairobi. However, the study was based on Saccos, whereas commercial banks situated in Kenya was the focus of the current study.

2.3.4 Credit Collection Practices and Financial Performance

Wambugu (2017) study investigated on the effect of debt collection strategies on financial performance of local authorities in Kenya. Both a descriptive analysis and correlation and regression analysis was undertaken. Data was collected through the use of a questionnaire. The study found that the subcontracting of the debt collection to third parties and the enforcement strategies had a positive relationship with the level of debts while proactive debt collection strategies.

Chepkoech (2015) analyzed credit risk management practices and Micro Finance Institutions performance in Nairobi County. Target population of the study was all the 261 employees drawn from selected Micro-Finance Institutions in Nairobi County. The study adopted a multiple

regression analysis. The findings of the study indicate that credit collection policies have a significant positive effect on the performance of MFIs in Nairobi County. However, the study was based on Micro Finance Institutions. In filling the contextual gap, commercial banks situated in Kenya were the focus of the current research.

Kithinji (2010) studied credit risk management and performance of commercial banks situated in Kenya. Data was collected on profits and non-performing loans of commercial banks from the period 2004 to 2008. Findings indicated that credit collection policies positive impact on the performance of commercial banks. Notably, the study did not look at interest rates of the banks and their moderating impact on the relationship between credit collection policies and performance of commercial banks situated in Kenya.

Korir (2011) conducted a study on the impact of credit risk management practices on the financial performance of Deposit Taking Microfinance institutions in Kenya. The research concluded that credit risk management practices are adopted by Deposit taking microfinance institutions in Kenya to mitigate against the credit risks which they are exposed to. The findings of the study show thatcredit collection practices have a significant positive relationship with performance of deposit Taking Saccos. However, the study focused on Microfinance Institutions. Commercial banks situated in Kenya were the focus of this research.

2.4 Summary of Literature Review and Research Gaps

Table 2.1: Summary of the Literature Reviewed and Research Gaps

Author and Year	Title	Findings	Gaps	Focus of current study
Byaruhanga (2017)	Relationship between Credit terms, credit accessibility and performance	A positive and significant relationship between credit terms, credit accessibility and the performance of agricultural cooperatives.	Focused on performance of agricultural cooperatives	Focused on financial performance of commercial banks
Nyawera (2016)	credit policy on the financial performance	positive significant relationship implying that credit policies affects the financial performance	Deposit Taking Microfinance Institutions in Kenya study context	commercial banks study context
Njeru *et al.* (2016)	relationship between effectiveness of credit appraisal on loan performance	lending placed much reliance on use of past information and thus credit referencing and credit history were applied more in credit appraisal	Qualitative data	Quantitative data
Chepkoech (2015)	credit risk management practices impact on Micro Finance Institutions' performance in Nairobi County	client appraisal has a significant positive effect on the performance	Focused on MFIs	Focused on Commercial banks
Olabamiji and Michael	credit management practices and bank	credit management practices have a	Cross-sectional	Descriptive

(2016)	performance	significant positive influence on the financial performance of First bank	research design	research design
Chepkoech (2015)	credit risk management practices and Micro Finance Institutions' performance in Nairobi County	credit control practices have a significant positive effect on the performance of MFIs	Focused on MFIs	Focused on Commercial banks
Wambugu (2017)	debt collection strategies on financial performance of local authorities in Kenya	subcontracting of the debt collection to third parties and the enforcement strategies had a positive relationship with the level of debts	Qualitative data	Quantitative data
Chepkoech (2015)	Credit risk management practices and Micro Finance Institutions performance in Nairobi County.	credit collection policies have a significant positive effect on the performance	Focused on performance of MFIs	Focused on financial performance Commercial banks

Source: Researcher (2018) and Literature Reviewed

2.5 Conceptual Framework

A conceptual framework is a diagrammatic presentation of the relationship of the study variables. The current research seeks to ascertain the effect of credit management practices on commercial banks' financial performance in Kenya. Therefore, the independent variables for the study constitute the credit management practices, the moderating variable is the interest rates and the dependent variable is commercial banks' financial performance.

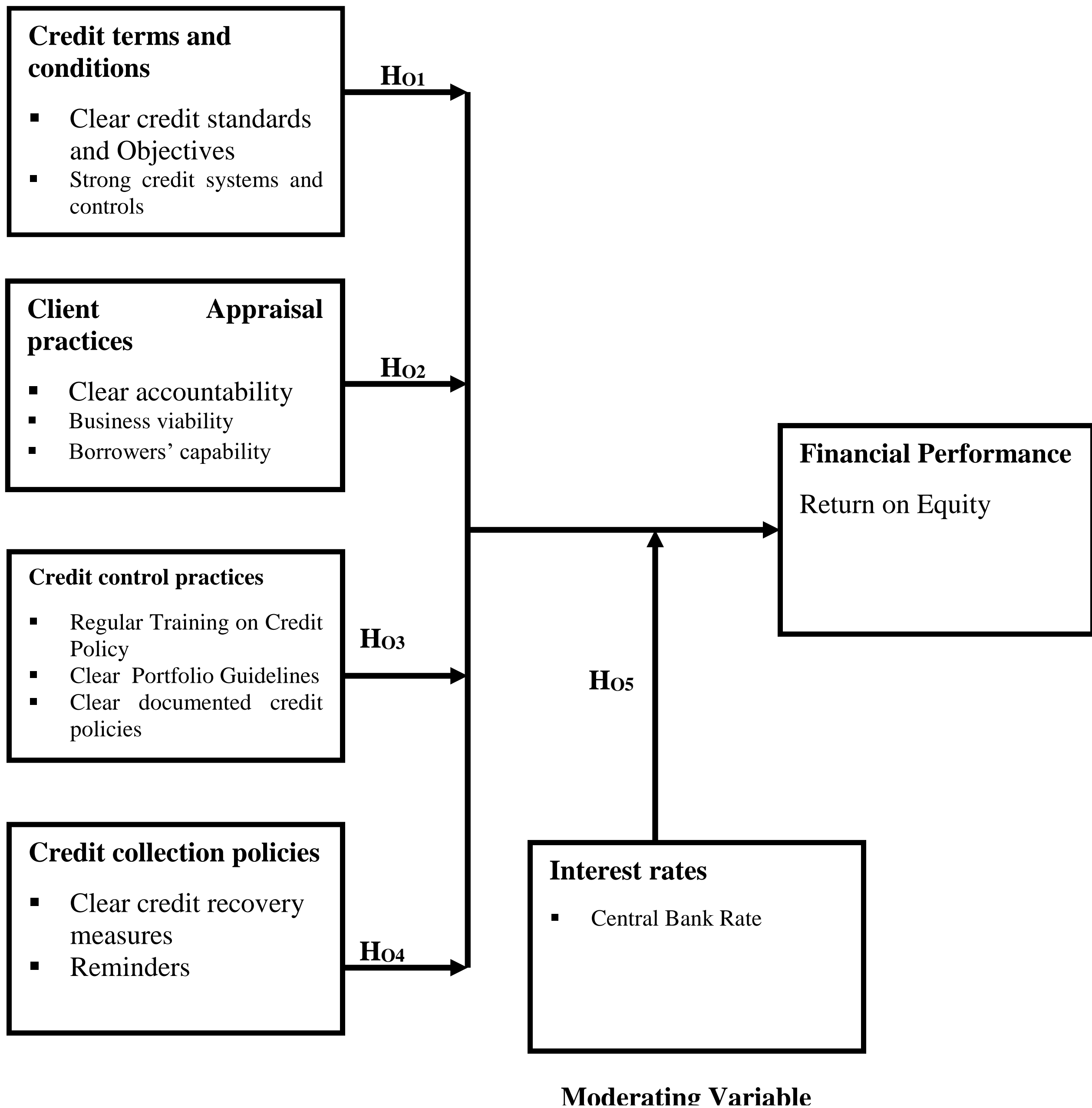


Figure 2.1: Conceptual Framework

Source: Researcher (2018)

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The current chapter provides insight on the study proposed methodology. It provides insight on the research population, instruments of data collection, research design and data analysis of the study.

3.2 Research Design

Cooper and Schindler (2009) are of the view that research design forms the basis for the collection, measurement and analysis of research data. Research design refers to an outline plan which is adopted in a study by a researcher to generate answers to research questions (Mugenda & Mugenda, 2003). The study adopted descriptive research design. Descriptive studies provide description of the general characteristics of the study population and also give description of the characteristics of the research variables (Cooper and Schindler, 2009).

3.3 Target Population

The 44 commercial banks situated in Kenya between the years 2012 to 2016 was the focus of this study, thus constituting the target population of the study. Similarly, the audited financial statements of the banks formed the unit of observation of the research.

3.4 Sampling Design and Sample Size

The study made use of purposive sampling design as it was based on all the 44 bank situated in Kenya. Mugenda and Mugenda (2003) assert that purposive sampling allows the researcher to

use his judgements to choose the respondents of the study. Similarly, the respondents of the study will be the compliance managers, risk managers and collection managers of the 44 commercial banks situated in Kenya. Therefore, making the total number of respondents was 129.

3.5 Data Collection instruments

This research utilized both secondary and primary data. Primary data was gathered with the use of questionnaire. Questionnaire is a method of data collection whereby the respondents provide written answers to written questions. The choice of questionnaire as a method of data collection for this study is attributed to the fact that questionnaires are cost effective when compared to face-to-face interviews. In addition, questionnaires are easy to analyze. Moreover, questionnaires are familiar to most people as it is the most common method of data collection in a research.

Questionnaires reduce biasness since there is uniformity in the presentation of questions. Also, the choice of a questionnaire in this study is also influenced by the fact that questionnaires are less intrusive than telephone or face-to-face surveys. In this study, the researcher made use of closed ended questionnaire. Closed questionnaire provides uniformity in answering the questions by allowing respondents to provide their personal and unbiased views. Furthermore, secondary data on performance indicator that is, ROE was sourced from the websites of the 43 banks that was considered in the study.

3.5.1 Validity of instruments

The research instruments had validity tests. In ensuring content validity, the research questionnaires were given to experts in the field of accounting and finance to give their

suggestions and opinions for improving the research questionnaire. Also, construct validity was achieved by reviewing various theoretical and empirical literature which provided more insight on the relevant concepts of the study. Thus, the research instrument items were constructed based on existing studies. The research supervisor was highly involved in ensuring validity of the research instruments.

3.5.2 Reliability of instruments

Reliability relates to a measure of the extent to which instruments used in a research yield consistent results (Mugenda & Mugenda, 2003). The research instruments are required to be consistent. A pre-test wasbe conducted. The respondents were taken through the questionnaire which is the tool for collecting data collection. The pre-test was conducted by the researcher to ensure correct, accurate and meaningful data is captured by the research questionnaire. The Cronbach's α coefficient of reliability ranges from 0 to 1 in providing this overall assessment of a measure's reliability A minimum α coefficient between 0.65 and 0.8 is recommended; α coefficient, that are below 0.5 are generally not acceptable, particularly for scales that are one dimensional (Meeker &Escobar, 2014).The study adopted cronbach test at α coefficient of 0.70.

A pilot study was conducted to determine the reliability and validity and the results are presented in the table below;

Table 3.1 Reliability and validity test

Variable	Cronbach's Alpha	No of Items	Comment
Credit terms and conditions	0.856	5	Reliable
Client appraisal practice	0.821	5	Reliable
Credit control practices	0.934	6	Reliable
Credit Collection policies	0.754	5	Reliable
Financial Peformance	0.857	4	Reliable
Overall Reliability coefficient	**0.844**	**25**	**Reliable**

Source: Survey data (2018)

Table 3.1 indicate an overall cronbach alpha score test of 0.81 which implies a good reliability since this value is higher than the acceptable threshold of 0.70

3.6 Data Analysis and Presentation

Drop and pick later method was adopted in administering the questionnaire. After the questionnaires have been filled and collected, the researcher went through the data and thoroughly checked for errors in responses, exaggerations or omissions. The study adopted descriptive analysis and inferential analysis where the study data was analyzed, presented and interpreted based on the study objectives. Descriptive statistics aim at providing the pattern of the responses and their consistency in each of the hypothesized variables. Inferential statistics provided more insight into the research findings. The research findings are presented using tables and charts.

3.6.1 Empirical Model

The study made use of multiple regression model. Multiple regression model is used in a study where there is more than one independent variable. Thus, the study expressed performance of Commercial banks as a function of Credit terms and conditions, Client Appraisal practices, Credit Control Practices and Credit collection policies

$Y = \beta 0 + \beta 1X1 + \beta 2X2 + \beta 3X3+ \beta 4X4+ \epsilon$ …………………………………………..3.1

Where:

Y- Financial Performance of commercial banks in Kenya.

$\beta 0$ - Constant

X1 – Credit terms and conditions

X2 – Client Appraisal practices

X3 – Credit Control Practices

X4 – Credit collection policies.

$\beta1 - \beta4$= Coefficients of regression

Є= Error term

Two models were used to test the moderation of interest rate on zero-order correlation between credit risk management practices and performance of Commercial banks situated in Kenya:

$Y = \beta0 + \beta1 X + \varepsilon$……...3.2

$Y = \beta0 + \beta1 X + \beta2M0 + \beta3 X * M0 + \varepsilon$..3.3

Where; Y = Financial Performance

X = Credit Risk Management Practices

M0 = Moderating Variable (Interest Rate)

X * M0 = Interaction term

$\beta1$, $\beta2$, and $\beta3$ = Coefficients of Beta

ε = Error term

In such a case there is an overall effect to be moderated, the moderation test will be centered on ascertaining if the coefficient of the interaction term is statistically different from zero (Ndiangui, 2016).

3.7 Research ethics

Research ethics refer to procedures and norms that are observed in a study. Ethical considerations regarding research in Kenyatta University and Kenya at large were adhered to. These considerations include but not limited to avoidance of fabrication, plagiarism, fabrication

and falsification. Also, respondents and their responses were handled with maximum confidentiality.

CHAPTER FOUR

DATA ANALYSIS AND PRESENTATION

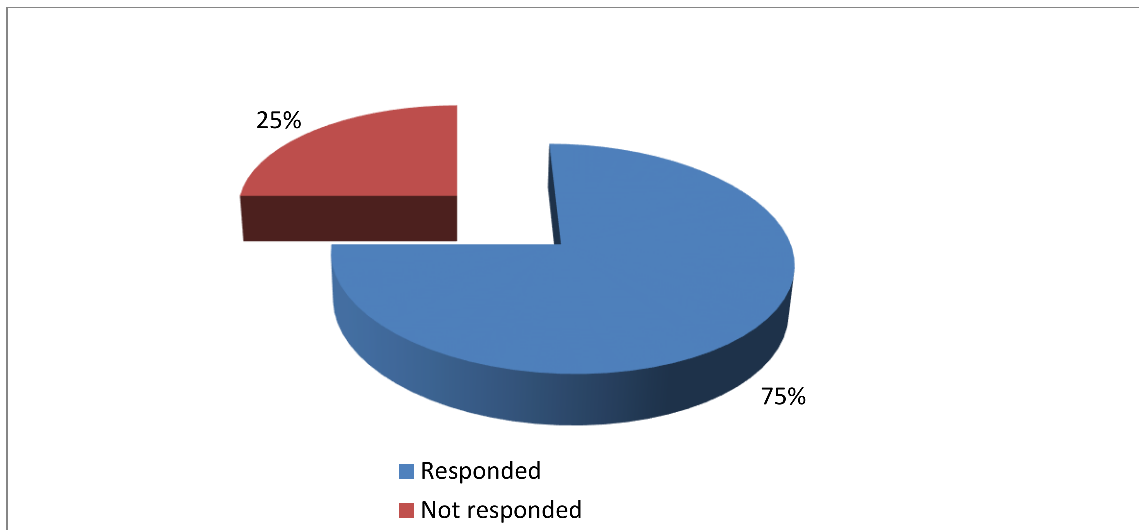
4.1 Introduction

This chapter represents the analysis of descriptive and inferential statistics deriving the findings obtained from the analysis of the primary data using regression, correlation, and analysis of variance. It further presents the results of analysis, interpretation and discussion of the findings with the reference to the theoretical and empirical literature review

4.2 Response rate

The response rate was analyzed on the basis of the proportion of the questionnaires that were duly filled and returned as presented in Figure 4.1 below.

Figure 4.1: Response rate



Source: Survey Data (2018)

The results in Figure 4.1 shows the response rate was 75% which was good and representative. This is consistent with Mugenda and Mugenda (2012) that a response rate of 50% and above is adequate for analysis and drawing conclusion.

4.3 Background information

The study sought to determine the background characteristics of the respondents in terms of the gender, age and education level.

4.3.1 Gender

The table 4.1 below indicates the demographic characteristic based on the gender

Table 4.1: Gender of the respondents

	Frequency	Percent
Female	29	33.0
male	59	67.0
Total	**88**	**100.0**

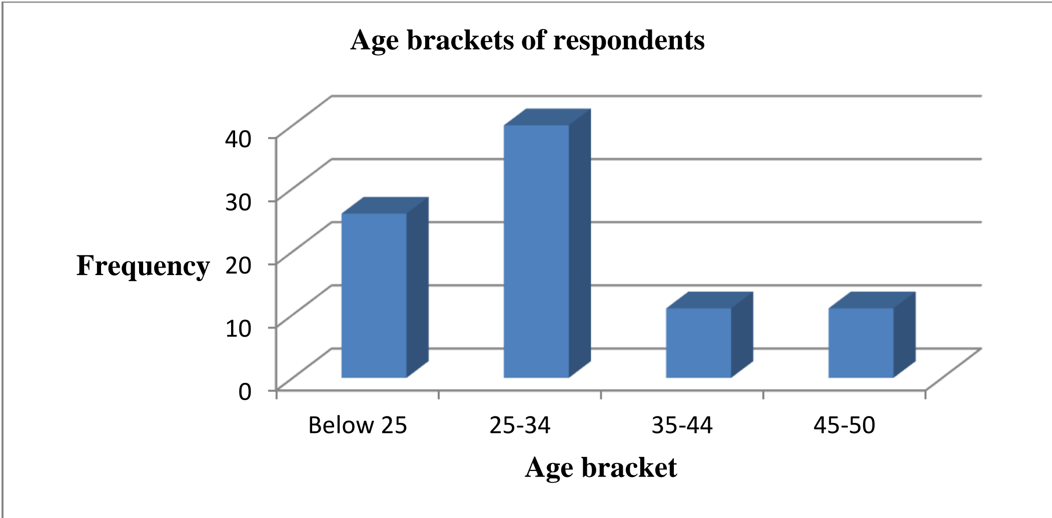
Source: Survey Data (2018)

According to the findings, majority of the respondents were male at 67% while female constituted 33%. However the two types of gender were fairly represented in the study.

4.3.2 Age bracket

The study also sought to determine the age brackets of the respondents. The results are presented in figure 4.2 below;

Figure 4.2: Age brackets of the respondents



Source: Survey Data (2018)

From the findings, majority of the respondents were between the age of 25-34 years at frequency 40, followed by those below the age of 25 years at 26, then those between the age of 35-44 years and 45-50 years at 11 each.

4.3.3 Level of education

The study sought to determine the levels of education for the respondents and the results presented in table 4.2 below;

Table 4.2: Levels of Education.

	Frequency	Percent
Diploma/certificate	23	26.1
Graduates	32	36.4
Masters	22	25.0
Phd	11	12.5
Total	**88**	**100.0**

Source: Survey Data (2018)

From the findings, the graduates were the majority of respondents at 36%, followed by diploma at 26%, masters at 25% and Phd at 12.5%.

4.4 Descriptive Analysis

The researcher used mean and standard deviation to present the summary measures of the sample that was observed. Analysis of descriptive statistics was conducted on the basis of the data collected on the variables that were at the core of this study. The basic feature of the observed sample formed the basis for quantitative data analysis for this study.

4.4.1 Credit terms and conditions

The researcher analyzed the data collected on the measures of credit terms and conditions used by commercial banks in Kenya and presented the results in Table 4.3.

Table 4.3: Descriptive Statistics on credit terms and conditions

	N	Minimum	Maximum	Mean	Std. Deviation
The bank has an internal credit rating system	88	3.00	5.00	4.2386	.67797
The organization has clear credit standards and objectives	88	3.00	5.00	3.9886	.66944
We have strong credit systems and controls	88	1.00	5.00	4.1477	.86489
There is clear credit information disclosure	88	1.00	5.00	3.9091	.68877
Management capacity of the loan applicants is rated	88	1.00	5.00	3.4432	.98094
Average scores				**3.9455**	**.77640**

Source: Survey Data (2018)

The results in Table 4.3 show that the respondents agreed that credit terms and conditions used by commercial banks in Kenya influenced their financial performance as shown by the aggregate mean of 3.9455 with a significance variance of .77640. Moreover, the mean values on individual items ranges between 3.4432 on the lower side and 4.2386 on the upper side. This indicates that the activities that have been adopted as the measures of credit terms and conditions are practiced in commercial banks and are thus considered crucial for financial performance of the organization. Byaruhanga (2017) study revealed a positive and significant relationship between credit terms, credit accessibility and the performance of agricultural cooperatives. Nyawera (2016) study indicated a positive significant relationship implying that credit policies affects the financial performance of deposit taking micro finance organization.

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4.4.2 Client appraisal practice

The researcher conducted the analysis of the data collected on the descriptive statistics of the client appraisal practices and displayed the results in Table 4.4;

Table 4.4: Descriptive Statistics on Client appraisal practice.

	N	Minimum	Maximum	Mean	Std. Deviation
Business plan is analyzed in order to identify risk exposure	88	3.00	5.00	4.3182	.70377
Cash flow projections of the projects are considered before financing	88	3.00	5.00	4.5682	.52073
Borrowers capability is considered before giving loan	88	3.00	5.00	4.3864	.53459
Long term business viability and clients trustworthiness of every loan applicant	88	2.00	5.00	3.9886	1.18898
We look at the collateral as a secondary source of repayment	88	3.00	5.00	4.5341	.54560
Average scores				**4.3591**	**.69873**

Source: Survey Data (2018)

The results in Table 4.4 show that the respondents strongly agreed that client appraisal practices used by commercial banks in Kenya influenced their financial performance as shown by the aggregate mean of 4.3591 with a significance variance of .69873. Moreover, the mean values on individual items ranges between 3.9886 on the lower side and 4.5682 on the upper side. This indicates that the activities that have been adopted as the measures of client appraisal practices are practiced in commercial banks and are thus considered crucial for financial performance of the organization. Njeru *et al.* (2017) study revealed that lending placed much reliance on use of past information and thus credit referencing and credit history were applied more in credit

appraisal. Chepkoech (2015) study shows that client appraisal has a significant positive effect on the performance of MFIs in Nairobi County. Notably, the study was based on Micro Finance Institutions.

4.4.3 Credit control practices

The researcher analyzed the data collected on the measures of credit control practices and presented the results in Table 4.5.

Table 4.5: Descriptive Statistics on Credit control practices.

	N	Minimum	Maximum	Mean	Std. Deviation
The institution has regular training on credit policy	88	1.00	5.00	3.0341	1.22661
We have clear portfolio guidelines	88	2.00	5.00	3.5000	.88409
There are clear documented credit policies	88	3.00	5.00	4.2273	.82667
Efficient data management	88	3.00	5.00	4.0114	.78043
The institution has sufficient risk tools	88	2.00	5.00	3.8750	.81385
Clients are requested to provide financial guarantees	88	3.00	5.00	4.4545	.72570
Average scores				**3.8504**	**0.87623**

Source: Survey Data (2018)

The results in Table 4.5 show that the respondents agreed that credit control practices used by commercial banks in Kenya influenced their financial performance as shown by the aggregate mean of 3.8504 with a significance variance of 0.87623. Moreover, the mean values on individual items ranges between 3.0341 on the lower side and 4.4545 on the upper side. This

indicates that the activities that have been adopted as the measures of credit control practices are practiced in commercial banks and are thus considered crucial for financial performance of the organization. Olabamiji and Michael (2016) study revealed that credit management practices have a significant positive influence on the financial performance of First bank. Chepkoech (2015) study show that credit control practices have a significant positive effect on the performance of MFIs in Nairobi County.

4.4.4 Credit collection policies

The researcher analyzed the data collected on the measures of credit collection policies and presented the results in Table 4.6.

Table 4.6: Descriptive Statistics on Credit collection policies

	N	Minimum	Maximum	Mean	Std. Deviation
Debtors are reminded before the repayment falls due	88	2.00	5.00	3.7273	.69028
Defaulters are followed up	88	2.00	5.00	3.8068	.78576
Clients are given grace period when repayment falls due	88	2.00	5.00	3.5341	.89634
Retaining of collateral is the last option when debtors are unable to repay the loans	88	2.00	5.00	4.1591	.60432
Collection procedures are made clear to clients before granting of any loans	88	2.00	5.00	3.2159	1.04440
Average scores				**3.6886**	**0.80422**

Source: Survey Data (2018)

The results in Table 4.6 show that the respondents agreed that credit collection policies used by commercial banks in Kenya influenced their financial performance as shown by the aggregate mean of 3.6886 with a significance variance of 0.80422. Moreover, the mean values on individual items ranges between 3.0341 on the lower side and 4.4545 on the upper side. This indicates that the activities that have been adopted as the measures of credit collection policies are practiced in commercial banks and are thus considered crucial for financial performance of the organization. Wambugu (2017) study found that the subcontracting of the debt collection to third parties and the enforcement strategies had a positive relationship with the level of debts while pro active debt collection strategies.

4.5 Inferential Analysis

This section focused on the Correlation test, model summary, ANOVA, and multiple regression analysis on the effect of credit risk management practices (credit terms and conditions, client appraisal practice, credit control practices and credit collection policies) on the performance of commercial banks.

4.5.1 Correlation test

The correlation test was also carried out to determine how strongly a pair of variable is correlated. The results are presented in table 4.7 below;

Table 4.7: Correlation test

		Performance	Credit terms and conditions	Client appraisal	Credit control	Credit collection	Central bank rates
Performance	Pearson Correlation	1					
	Sig. (2-tailed)						
Credit terms and conditions	Pearson Correlation	.544**	1				
	Sig. (2-tailed)	.000					
Client appraisal	Pearson Correlation	.788**	.173	1			
	Sig. (2-tailed)	.000	.107				
Credit control	Pearson Correlation	.719**	.209	-.130	1		
	Sig. (2-tailed)	.000	.051	.229			
Credit collection	Pearson Correlation	.514**	-.029	.173	.274**	1	
	Sig. (2-tailed)	.000	.785	.107	.010		
Central bank rates	Pearson Correlation	-.130	-.024	-.064	-.144	-.029	1
	Sig. (2-tailed)	.229	.822	.555	.180	.785	

**. Correlation is significant at the 0.01 level (2-tailed).

Source: Survey Data (2018)

From table 4.8 above, there is a significant positive relationship between the credit terms and conditions and the performance of commercial banks (r=-0.544, p value 0.000). There is a significant positive correlation between client appraisal and performance (r=0.788, p-value 0.000). There is also a significant association between the credit control practices and performance (r=0.719, p value 0.000). There is also a significant association between the credit

collection practices and performance (r=0.514, p value 0.000). Kithinji (2010) study show that credit terms and conditions have a positive impact on the performance of commercial banks.

There was a non significant correlation between central bank rates and performance of (r=-0.130, p-value 0.229). According to Green, (2008), if a pair of variable has a correlation of 0.8 or -0.8 (i.e. r2 of 64% or more), then the pair is strongly correlated and this means that multicollinearity exists. From the table, none of the pair of association has r of more than 0.8 (64%) hence the data has no multicollinearity problem. Korir (2011) study results show that client appraisal has a significant positive relationship with performance of deposit Taking Saccos.

4.5.2 Analysis of Variance (ANOVA)

This study made use of the ANOVA statistics to find out the significance of the association between the financial performance of commercial banks in Kenya and the independent variables.

Table 4.8: Analysis of variance (ANOVA)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	16151.109	4	4037.777	271.502	.000[b]
	Residual	1234.376	83	14.872		
	Total	17385.485	87			

a. Dependent Variable: Financial performance

b. Predictors: (Constant), Credit collection policies, Credit terms and conditions, Credit Client appraisal practices

Source (Survey data, 2018)

From the findings, the model was significant with a p-value of 0.000 which implies that the model was good for estimation.

4.5.3 Model summary

The study also determined the percentage of variation in the dependent variable as a result of a percentage change in the predictor variables. The results are presented in table 4.9 below

4.9: Model summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.964[a]	.929	.926	3.8564231

a. Predictors :(Constant), Credit terms and conditions, Client appraisal, Credit control practices, Credit collection policies

Source (Survey data, 2018)

The model had an adjusted R-square value of 0.926. The R-square value of 0.926 implies that the predictor variables explain 92.6% of the changes in the financial performance of commercial banks in Kenya.

4.5.4 Regression Analysis

This study further sought to determine the multiple regression effect of credit risk management practices on the financial performance of commercial banks in Kenya. Table 4.10 exhibits the regression analysis results.

Table 4.10: Multiple Regression Analysis without the moderating variable

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B	
	B	Std. Error	Beta			Lower Bound	Upper Bound
1 (Constant)	1.090	.231		4.724	.000	.631	1.549
X1	9.998	1.180	.288	8.471	.000	7.651	12.346
X2	15.412	1.398	.413	11.022	.000	12.631	18.193
X3	14.954	1.398	.365	10.699	.000	12.174	17.734
X4	13.907	1.195	0.359	11.636	.000	11.529	16.284

a. Dependent Variable: Financial performance

Source: Survey Data (2018)

The regression model that was estimated through the results of regression analysis is presented below.

$$Y=1.090+9.998X_1+15.412X_2+14.954X_3+13.907X_4+\varepsilon$$

Without the inclusion of the predictor variables, the performance increases by 1.090 times. A unit increase in credit terms and conditions (X1) results in the increase in the financial performance of Banks by 9.998 times. Secondly, a unit increases in client appraisal practices (X2) other factors held constant, results in an increase in performance of Banks by 15.412 times. Thirdly, a one unit increase in credit control practices (X3) other things held constant, results in an increase in the performance by 14.954 times. Lastly for a unit increase in the credit collection practices there is an increase in financial performance of commercial banks by 13.907 other factors held constant. The p values also indicate that all the variables, are significant at 0.05 level of significance with p values of 0.000.

Table 4.11: Multiple regression with the inclusion of the moderating variable.

Model		Unstandardized Coefficients		Standardized Coefficients			95.0% Confidence Interval for B	
		B	Std. Error	Beta	t	Sig.	Lower Bound	Upper Bound
1	(Constant)	1.073	.181	.481	5.939	.000	.715	1.431
	X1	10.006	1.178	.288	8.494	.000	7.663	12.350
	X2	15.414	1.396	.413	11.045	.000	12.638	18.191
	X3	14.746	1.407	.360	10.482	.000	11.948	17.545
	X4	13.922	1.193	.359	11.670	.000	11.549	16.295
	X5	-.383	.334	-.034	-1.148	.254	-1.046	.281

a. Dependent Variable: Financial performance

Source: Survey Data (2018)

The regression model that was estimated through the results of regression analysis is presented below.

$$Y=1.073+10.006X_1+15.414X_2+14.746X_3+13.922X_4-0.383X_5+\varepsilon$$

With the inclusion of the predictor variables, the performance increases by 1.073 times. A unit increase in credit terms and conditions (X1) results in the increase in the financial performance of Banks by 10.006 times other things held constant. Secondly, a unit increases in client appraisal practices (X2) other factors held constant, results in an increase in performance of Banks by 15.414 times. Thirdly, a one unit increase in credit control practices (X3) other things held constant, results in an increase in the performance by 14.746 times. Lastly for a unit increase in the credit collection practices there is an increase in financial performance of

commercial banks by 13.922 other factors held constant. A unit increase in the central bank rates (X5) there is decrease in financial performance of commercial banks by 0.383 other factors held constant. The p values also indicate that all the variables, are significant at 0.05 level of significance with p values of 0.000. However, the moderating variable is not significant at 0.05 since the p value is 0.254.

4.6 Interpretation of the findings

The study sought to achieve the following objectives;

4.6.1 Specific Objective One

The researcher sought to establish the effect of credit terms and conditions on financial performance of commercial banks in Kenya. The results of regression analysis in Table 4.12 demonstrate that Without the inclusion of the predictor variables, a unit increase in credit terms and conditions (X1) results in the increase in the financial performance of Banks by 9.998 times. With the inclusion of the moderating variable, the financial performance increases by 10.006 times. The p values also indicate that the credit terms and condition was significant at 0.05 level of significance with p values of 0.000.

The findings of the study in respect to the effect of credit terms and conditions is in line with that of Ben-Naceur and Omran (2008) who found that that credit terms and conditions have a significant positive effect on the performance of banks. Similarly, the findings concur with those of Korir (2011) and Chepkoech (2015) who found a positive and significant effect of credit terms and conditions on financial performance for Deposit Taking Saccos and MFIs respectively.

4.6.2 Specific Objective Two

The researcher sought to establish the effect of client appraisal on financial performance of commercial banks in Kenya. The results of regression analysis in Table 4.12 demonstrate that without the inclusion of the predictor variables, a unit increase in client appraisal (X2) results in the increase in the financial performance of Banks by 15.412 times. With the inclusion of the moderating variable, the financial performance increases by 15.414 times. The p values also indicate that the client appraisal was significant at 0.05 level of significance with p values of 0.000.

The findings of the study with regards to the effect of client appraisal on financial performance are in agreement with that of Gaitho (2010), Korir (2011) and Chepkoech (2015) who found a positive and significant effect of client appraisal on performance. This can be attributed to the fact that client appraisal leads to issuing of loans to credit worthy customers. Therefore, the more efficient the appraisal of customers is, the better the financial performance of banks.

4.6.3 Specific Objective Three

The researcher sought to establish the effect of credit control practices on financial performance of commercial banks in Kenya. The results of regression analysis in Table 4.12 demonstrate that Without the inclusion of the predictor variables, a unit increase in credit control practices (X3) results in the increase in the financial performance of Banks by 14.954 times. With the inclusion of the moderating variable, the financial performance increases by 14.756 times. The p values also indicate that the credit control practices were significant at 0.05 level of significance with p values of 0.000.

The findings on credit control practices concur with those of Ben-Naceur and Omran (2008), Gaitho (2010) and Chepkoech (2015) who found credit control practices to have a positive and significant effect on financial performance. The positive and significant effect of control practice on financial performance can be attributed to the fact that credit control practices minimize the risk of credit default which in turn maximizes financial performance of banks.

4.6.4 Specific Objective Four

The researcher sought to establish the effect of credit collection policies on financial performance of the commercial banks in Kenya. The results of regression analysis in Table 4.12 demonstrate that Without the inclusion of the predictor variables, a unit increase in credit collection policies (X4) results in the increase in the financial performance of Banks by 14.954 times. With the inclusion of the moderating variable, the financial performance increases by 14.756 times. The p values also indicate that the credit control practices were significant at 0.05 level of significance with p values of 0.000.

Similarly, the study findings on the effect of credit collection policies on financial performance are in agreement with those of Felix and Claudine (2008), Juanjuann*et al*. (2009), Kithinji (2010) and Korir (2011) where their respective studies also indicated a positive and significant effect of credit collection policies on performance. This is in view of the fact that efficient collection policies will bring about high level of loan repayments and thus, higher financial performance of banks.

4.6.5 Specific Objective Five

The researcher sought to establish the moderating effect of central bank rate on the relationship between credit risk management practices and financial performance of the commercial banks in Kenya. The results of regression analysis in Table 4.13 demonstrate that a unit increase in Central Bank Rate leads to a 0.383 decrease in financial performance of commercial banks. The p values 0.254 therefore, implying that central bank rate has an insignificant effect on the relationship between credit risk management practices and financial performance of commercial banks in Kenya. Therefore, the performance of commercial banks as predicted by credit risk management practices is not influenced by central bank rate.

CHAPTER FIVE

SUMMARY CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

Chapter five consists of the summary of the study, conclusion, recommendations and suggestions for further research.

5.2 Summary of the Study

The survival of commercial banks like every other financial institution depends largely on their credit risk management practices. This is because granting of loans to borrowers is accompanied with its own risks. Credit risk is regarded as the most adamant risk faced by banks due to the nature of their activities. Studies relating to credit risk management practices were done in developed and other developing countries other than Kenya. They sought to examine the effect of credit risk management practices on commercial banks financial performance in Kenya. Consequently, the specific objectives of the study were to determine the effect of client appraisal, credit terms and conditions, credit collection policies and credit control practices commercial banks' financial performance in Kenya. Asymmetry Information theory, Modern Portfolio theory and 5 C's Model of Client Appraisal were used to provide more insight in the study.

The research utilized descriptive research design and purposive sampling design as it was based on all the 43 bank situated in Kenya. Similarly, the respondents of the study were the compliance managers, risk managers and collection managers of the 43 commercial banks situated in Kenya. Therefore, making the total number of respondents to be 129.This research utilized both secondary and primary data. Primary data was gathered with the use of questionnaire. The

secondary data was sourced from the financial statements of banks. The study had a response rate was 75% which was good and representative.

The research made use of a descriptive analysis and multiple regression analysis. Reliability and validity of research instruments were tested. On the effect of credit terms and conditions on financial performance of commercial banks in Kenya, the study revealed that a credit terms and conditions has a positive and significant effect on the financial performance of Banks. Similarly, with regards to the effect of client appraisal on financial performance of commercial banks in Kenya. The results provided a positive and significant effect of client appraisal on the financial performance of Banks.

Also, regarding the effect of credit control practices on financial performance of commercial banks in Kenya. The findings reveal a positive and significant effect of credit control practices on the financial performance of commercial banks in Kenya. Furthermore, the study found a positive and significant effect of credit collection policies on financial performance of banks. Lastly, the study found the moderation effect of central bank rate on the relationship between credit risk management practices and financial performance of commercial banks to be insignificant.

5.3 Conclusions

The conclusions of the study are based on the findings of the study. The first objective of the study was to establish the effect of credit terms and conditions on financial performance of commercial banks in Kenya. Findings of the study show that credit terms and conditions have positive and significant effect on financial performance of commercial banks in Kenya. This is

an indication that the financial performance of commercial banks in Kenya has a direct relationship with credit terms and conditions.

The second objective of the study was to examine the effect of client appraisal on financial performance of commercial banks in Kenya. The study concluded that client appraisal on financial performance of commercial banks in Kenya. Implying that the more effective the appraisal of customers before issuing out loans to them the better the financial performance of commercial banks in Kenya.

The third objective of the study was to determine the effect of credit control practices on financial performance of commercial banks in Kenya. Findings of the study reveal that credit control practices have positive and significant effect on financial performance of commercial banks in Kenya. Therefore, the study concluded that financial performance of commercial banks in Kenya is highly determined by credit control practices. The more efficient the control practices are in the bank, the higher the performance of commercial banks.

The fourth objective of the study was to investigate the effect of credit collection policies on financial performance of the commercial banks in Kenya. Research findings showed that credit collection policies has a positive and significant effect on financial performance of the commercial banks in Kenya. Based on these findings, the study concluded that credit collection policiesare significant determinants of financial performance of commercial banks in Kenya. Therefore, effective credit collection policies bring about higher profitability of commercial banks and vice versa.

Lastly, the fifth objective of the study was to investigate the moderating effect of Central Bank Rate on the relationship between credit risk management practices and financial performance of commercial banks in Kenya. In line with the findings of the study, the study concluded that CBR has a negative and insignificant effect on the relationship between credit risk management and financial performance of commercial banks in Kenya.

5.4 Recommendations for Policy and Practice

The policy recommendations of this research are in view of the conclusions of the study. Similarly, the policy recommendations are based on the variables that significantly affect financial performance of commercial banks in Kenya. In respect to effect of credit terms and conditions on financial performance of commercial banks in Kenya. The study concluded that credit terms and conditions have positive and significant effect on financial performance of commercial banks in Kenya. Therefore, the management of commercial banks should ensure and enhance effective terms and conditions regarding the lending habit of banks.

Secondly, with respect to client appraisal and financial performance of commercial banks in Kenya. The study concluded that client appraisal significantly impacts on financial performance of commercial banks in Kenya. In view of this, the study recommends that the credit managers should put in place a sound and effective appraisal system which will ensure the proper appraisal of customers before any loans and advances are issued.

Thirdly, based on the findings of the study, the study concluded that there is a positive and significant effect of credit control practices on financial performance of commercial banks in Kenya. Consequently, the study recommends that bank management adopt control policies that

will monitor and stabilize bank credit to customers. This in turn will bring about greater financial performance of commercial banks in Kenya.

Lastly, the study sought to establish the effect of credit collection policies on financial performance of commercial banks in Kenya. Based on the research findings, the study concluded that credit terms and conditions have positive and significant effect on financial performance of commercial banks in Kenya. The study recommends that credit managers should adopt measures that will improve credit collection as this significantly determines bank performance.

5.5 Suggestions for Further Research

The suggestions for further research of this study are in line with the last objectives of the study which is the moderation effect of interest rates on the relationship between credit risk management practices and financial performance of commercial banks. The study utilized the central bank rate and found an insignificant moderation effect. Therefore, further studies on credit risk management practices and financial performance of banks should consider bank specific interest rates as this could provide a different result from that of this study.

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APPENDICES

APPENDIX I: QUESTIONNAIRE

Introduction

This questionnaire seeks to gather information on credit risk management practices and financial performance of commercial banks situated in Kenya. Your responses will only be used for academic purposes. You are highly encouraged to provide answers to the questions in the best way known to you according to your experience and knowledge.

SECTION I: Demographic Information

1. Indicate your gender?

   Female [ ] Male [ ]

2. Indicate your highest educational level.

PhD [ ] Masters [ ] Undergraduate degree [ ] Diploma/Certificate [ ]

3. Indicate your age bracket?

Below25 [ ]

25-34[ ]

35-44[ ]

45-50 [ ]

Above 51[ ]

Key: 5 – Strongly agree, 4 – agree, 3 – Don’t Know, 2 – disagree and 1 – Strongly disagree

SECTION II: CREDIT TERMS AND CONDITIONS

a) *Please answer the following questions by ticking the degree to which you agree or disagree on each item.*

	Statement	**5**	**4**	**3**	**2**	**1**
1	The bank has an internal credit rating system.					
3	The organization has clear credit standards and Objectives.					
4	We have strong credit systems and controls in the institution.					
5	There are clear credit information disclosures					
6	Management capacity of loan applicants is rated.					

SECTION III: CLIENT APPRAISAL PRACTICE

b) *Please answer the following questions by ticking the degree to which you agree or disagree on each item.*

	Statement	**5**	**4**	**3**	**2**	**1**
1	Business plan are analyzed in order to identify risk exposure					
2	Cash flow projections of projects are considered before financing					
3	Borrowers' capability are considered before giving loan.					

4	We look at the long term business viability and clients' trustworthiness of every loan applicant.					
5	We look at collateral as secondary source of repayment.					

SECTION IV: CREDIT CONTROL PRACTICES

c) *Please answer the following questions by ticking the degree to which you agree or disagree on each item.*

	Statements	**5**	**4**	**3**	**2**	**1**
1	The institution has regular training on credit policy.					
2	We have clear portfolio guidelines.					
3	There are clear documented credit policies.					
4	We have efficient data management.					
5	The institution has sufficient risk tools.					
6	Clients are requested to provide financial guarantees					

SECTION V: CREDIT COLLECTION POLICIES

d) *Please answer the following questions by ticking the degree to which you agree or disagree on each item.*

	Statements	**5**	**4**	**3**	**2**	**1**
1	We remind debtors before the repayment falls due					
2	We follow up on debtors who have defaulted					
3	Debtors are given few days/weeks of grace when repayment date falls due					
4	Retaining of collateral is the last option when debtors are unable to repay loans					
5	Collection procedures are made clear to clients before granting of any loans					

Thanks for your Time and Cooperation.

Appendix II: Research Study Work Plan

Month	**Activity**
May	**Writing of proposal**
June	
July	**Estimated period for defence.**
October	**Defence corrections and field work**
November	**Analysis of data and its Interpretation.**
December	**Writing of project and its submission**

Appendix III: Study Budget.

Item	**Quantity**	**Per Unit Cost**	**Total Cost**
Buying of Laptop.	1	65,500	65,500
Purchase of a Modem	1	4,500	4,500
Modems Monthly Charges	12	3,000	36,000
Charges for Internet	9,000		
Transportation	14,000		
Charges for Printing	26,000		
Miscellaneous Expenses	11,500		
Stationery Expenses:			
Plain writing sheets	1 ream.	500	500
Writing Pens		2	100
Staple Pins and Stapler	1	250	250
Total			**167,350**