Journal of Economics and Sustainable Development www.iiste.org
ISSN 2222-1700 (Paper) ISSN 2222-2855 (Online)
Vol.6, No.2, 2015

Credit Management and Bank Performance of Listed Banks in Nigeria

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Abstract
The study critically assessed the effects of credit management on banks's performance in Nigeria. In achieving the objectives identified in this study, the audited corporate annual financial statement of listed banks covering the period 2007-2011 were analyzed. More so, a sum total of ten (10) listed banks were selected and analyzed for the study using the purposive sampling method. However, in an assessing the research postulations, the study adopted the use of both descriptive statistics and econometric analysis using the panel linear regression methodology consisting of periodic and cross sectional data in the estimation of the regression equation. Findings from the study revealed that while ratio of non-performing loans and bad debt do have a significant negative effect on the performance of banks in Nigeria, on the other hand, the relationship between secured and unsecured loan ratio and bank's performance was not significant. Hence, the study recommends that banks management should put in place or institute sound lending framework, adequate credit administration procedure and an effective and efficient machinery to monitor lending function with established rules.
Keywords: Credit Management, Non-performing loans and Bad debt, Bank performance

1.0 Introduction

Banks are profit-making organizations performing as intermediaries connecting borrowers and lenders in bringing temporarily available resources from business and individual customers as well as providing loans for those in need of financial support (Uwuigbe, 2013; Drigă, 2012). Commercial Banks play a vital role in developing economies like Nigeria, Ghana, Egypt and Algeria. Bank lending is very crucial for it make possible the financing of agricultural, industrial and commercial activities of the country.

Commercial Banks are entrusted with the funds of depositors. These funds are generally used by banks for their business. The fund belongs to the customers so a programme must exist for management of these funds. The programme must constantly address three basic objectives: liquidity, safety and income. Successful management calls for proper balancing of all these three. Liquidity enables the banks to meet loan demands of their valuable and long established customers who enjoy good credit standing. The second objective being safety is to avoid undue risk since banks meet responsibility of protecting the deposit entrusted to them. Proper and prudent management of banks create and hence customer confidence. The third being income/profitability which is aimed at growth and expansion to meet repayment of interest charges on debt, to achieve the objective of maximizing wealth of shareholders and to survive competition in the banking industry (Okwoli, 1996; Uwuigbe, 2011).

As a matter of fact a bank cannot remain in business if it neglects the credit function (Osayeme 2000). Of interest to this paper is the credit component of the banks' portfolio that contributes to the profit of the banks and which has lead to the problem of bad debts in Nigerian banks as a result of poor management. Credit as the name implies is described as the right to receive payments or the obligation to make payments on demand or at some future date on account of the immediate transfer of goods or money another (Uwuigbe, Uwalomwa and Ben-Caleb, 2012). It is based on the faith and confidence, which the creditor reposes in the ability and willingness of the debtor to fulfill his promise to pay. In a credit transaction the right to receive payment and the obligation to make payments originate at the same time.

The term debt is frequently used in reference to debtor's obligation to make payment. Debt and credit are therefore similar terms. Management of credit is simply the application of four management principles which are planning, organizing directing and controlling to credit concept. Commercial banks are major players in the financial sector of every country's economy. The failure or success of these banks will to a large extent affect the financial sector and the economy at large. In recent times some commercial banks have been wound up leaving customers to their fate. It is important to note that the major cause of the winding up of some of these banks is their poor management of their finance and credit. Many of them were writing off huge amounts of debt yearly and also reflected some going concern issues that related to their management of credit and finance. The reason for the failure of these banks has sparked the interest of the researcher in conducting further studies into the management of finance and credit in Nigerian banks. It is in the light of the above, that this study examined the relationship between credit management and bank performance in Nigeria.

In the light of the aforementioned discussion, the remaining part of this article is structured as follows. Following the introductory section is the review of relevant literature and hypotheses development. While section 3 focused on the research methodology adopted for the study; section 4 and 5 discusses the findings and conclusion of study.

2.0 Literature Review and Hypotheses Development

Basically, banks are in place not only to accept deposits but also to grant credit facilities, hence they are exposed to credit risk. Credit risk is by far the most important risk faced by banks and the accomplishment of their business depends on accurate measurement and efficient management of this risk to a greater extent than any other risks (Gieseche, 2004 as cited in Kargi, 2011).While financial institutions have been bedeviled with series of problems over the years for a large number of reasons, the main cause of this problems continues to be directly related to lax credit standards for borrowers and counterparties, poor portfolio risk management, or a lack of attention to changes in economic or other situation that can lead to a deterioration in the credit standing of a bank's. This occurrence is common in emerging economies such as Nigeria, Ghana, Egypt etc. However, despite the series challenges that have bedeviled the industry, the banking industry have continued to play a crucial role in the economic development of economies (e.g. Nigeria). This is because, it contributes to the real productivity of the economy and to the overall standard of living, since banks are able to simultaneously satisfy the needs and preferences of both surplus and deficit units (Owojori, 2011).

It is universally acknowledged that the banking industry plays a catalytic role in the process of economic growth and development (Uwuigbe, Uwuigbe and Daramola, 2014). This acknowledgement is reinforced by contemporary conceptualization to the effect that banks are veritable vehicles for mobilizing resources (funds) from surplus units and channeling them to deficit units. These resources belong to customers so a programme must exist for the management of these funds. The programme must constantly address three basic objectives which are liquidity, safety and income. In meeting the three basic objectives, it requires establishing a schedule of actual priorities, because the most fundamental obligation of commercial banks is to meet all the demands for withdrawal of funds. Furthermore, since banks also have an obligation to satisfy the legitimate credit requirements of their depositors and the community and to meet the aspiration of profit making of the shareholders. These objective needs must also consider loans demand. Every commercial bank is under simultaneous pressure from depositors and shareholders. Customers deposit funds with those banks that meet their request for credit; Shareholders look for growth and profit of the banks which cannot be achieved without granting credits. It therefore requires a higher degree of management skill to reconcile the two. Bad credit management has lead to so many problems; most prominent is bad debt with a devastating effect on the banks and the entire economy. It is in the light of the above that the researcher looked at what ingredients are required in credit management of commercial banks and what result if they are not adequately put in place.

Prior studies suggests that a good credit risk architecture, policies and structure of credit risk management, credit rating system, monitoring and control contributes to the success of credit risk management system Bagchi (2003). Similarly, Muninarayanappa and Nirmala (2004) in a related study opined that the success of credit risk management require maintenance of proper credit risk environment, credit strategy and policies. Thus the ultimate aim should be to protect and improve the loan quality. In the same vein, findings from Salas and Saurina (2002) revealed that growth in GDP, rapid credit expansion, bank size and capital ratio had a significant impact on the non-performing loans.

Felix and Claudine (2008) examined the association between the performance of banks and credit risk management. As part of their findings, they observed that return on equity and return on assets both measuring profitability were inversely related to the ratio of non-performing loan to total loan of financial institutions thereby leading to a decline in profitability. Also, Hosna, et al. (2009) in their study opined that credit risk has a significant positive effect on the profitability of commercial banks in Sweden. Correspondingly, Kithinji (2010) examined the effects of credit risk management on commercial banks profitability in Kenya. They observed that the level of credit was high in the early years of the implementation of Basle II but decreased significantly in

2007 and 2008, probably when the Basle II was implemented by commercial banks. The findings revealed that the bulk of the profits of commercial banks are not influenced by the amount of credit and non-performing loans suggesting that other variables other than credit and non-performing loans impact on profits. Funso and et al., (2012) investigates the quantitative effect of credit risk on the performance of commercial banks in Nigeria for the period 2000-2010. Findings from their study showed that the effect of credit risk on bank performance measured by the return on assets of banks is cross sectional invariant.

In Nigeria, Kargi (2011) examined the impact of credit risk on the profitability of Nigerian banks. Findings from the study revealed that credit risk management has a significant impact on the profitability of Nigerian banks. Hence, they opined that banks' profitability is inversely influenced by the levels of loans and advances, non-performing loans and deposits thereby exposing them to great risk of illiquidity and distress. Although, some considerable amount of literature exists on the interaction between finance and credit management on banks liquidity position, however, the same is not true in developing economies like Nigeria where there is a relatively dearth in literature in this area, coupled with the huge institutional differences between Nigeria and other developed economies. Hence this study examined the relationship between credit management and bank performance in Nigeria.

2.1 Development of Hypotheses

Drawing from the literature, the hypotheses to be tested in this study are stated below in their null forms:

1) *H_1: There is no significant relationship between non-performing loans and the performance of banks in Nigeria.*
2) *H_2: There is no significant relationship between secured and unsecured loan and performance of banks in Nigeria.*

3) *H_3: There is no significant relationship between bad debt and performance of banks in Nigeria.*

3.0 Methodology

In achieving the objectives of this study, the audited annual financial statement of listed banks covering the period 2007-2011 were analyzed. The choice of these periods arises based on the fact that it was plagued with a number of corporate frauds arising from poor corporate governance practice and institutional failures. However, a total of 10 listed banks in Nigeria were selected and analyzed for the study using the purposive sampling method. Nevertheless, in analyzing the research hypotheses, the study adopted the use of both descriptive statistics and econometric analysis using the Panel linear regression methodology consisting of periodic and cross sectional data in the estimation of the regression equation.

3.1 Specifications of the Econometric Model

The data are to be analyzed using the regression analysis which could be termed to be a statistical technique used to find relationships between variables for the purpose of predicting future values. Using the formula;

Y=F(x)

Where;

Y is the Independent Variable (Credit Management)

X is the dependent variable (Bank performance measured as profit after tax)

$X = X_1, X_2, X_3$

X_1 = Non performing loans

X_2 = Bad debt

X_3 = Secured and Unsecured loans

A general panel data regression model is stated as;

$$Y_{it} = a + \beta x_{it} + e_{it}$$

Adapting the model provided in (Takang, 2008; Uwuigbe, Jimoh and Ajayi, 2012 and Uwuigbe, 2013) the association between bank performance and credit management in this study is stated in the following functional form as:

$$P_{it} = f(NPLR_{it}, BD_{it}, SLR_{it}) \quad (1)$$

In an explicit form this equation can model can be written as:

$$P_{it} = \beta_0 + B_1 NPLR_{it} + B_2 BD_{it} + B_3 SLR_{it} + e_{it} \quad (2)$$

Where;

P_{it} = Performance (P) here is measured with Profit after tax for the period

NPLR = Non performing loans to Total Loans (Non performing loans Ratios)

BD = BD here represents Bad Debt (BD)

SLR = Secured loans to unsecured loans (Secured Loan Ratio)

i = 10 banks sample

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e = *Stochastic or disturbance term.*
t = *Time dimension of the Variables*
β_0 = *Constant or Intercept.*
$B_{1\text{-}3}$ = *Coefficients to be estimated or the Coefficients of slope parameters.*
The expected signs of the coefficients (a priori expectations) are such that $\beta_1, \beta_2, \beta_3 < 0$.

4.0 Discussion of Findings

Summary of descriptive statistics results for all the variables as used in the study is presented in table 1.

Table (1) ***Descriptive Statistics of Variable***

Variable	*Obs*	*Mean*	*Std. Dev.*	*Min*	*Max*
PAT	*50*	*6.62e+09*	*1.87e+10*	*-7.11E+10*	*4.65E+10*
NPLR	*50*	*.1774161*	*.2119421*	*.0078467*	*1.122426*
SLR	*50*	*4488.627*	*16569.92*	*0*	*87503.01*
BD	*50*	*1.23e+10*	*1.83e+10*	*4784000*	*1.08E+11*

Results from our descriptive statistics as shown in table 1, present a mean profit after tax of about 6.62 for the period under consideration. Correspondingly; the independent variables in this study proxied as (NPLR, SLR and BD) maintains an averaged mean distribution value of about .177, .449.0 and 1.23 respectively for the sampled firms. Also, findings from the Pearson correlation analysis as depicted in table 2 indicates that both non-performing loans (NPLR) and bad debt (BD) have a negative association with the profit after tax of the sampled banks and it is significant at 1% probability level with a correlation coefficient (r) of about 0.018. This outcome basically implies that there is an inverse relationship between the two non-performing loan (proxied by NPLR) and profit after tax (proxied by PAT). In the same vein, the study also observed that a negative association does exist between secured loans ratio (proxied by SLR) and profit after tax of the sampled banks. However, this association is not significant.

Table (2) ***Correlations Matrix for Sampled firms***

	PAT	*NPLR*	*SLR*	*BD*
PAT	*1*			
NPLR	*-.469**	*1*		
SLR	*-.043*	*-.034*	*1*	
BD	*-.681***	*.580***	*-.047*	*1*

** Correlation is significant at the 0.05 level (2-tailed).*
***. Correlation is significant at the 0.01 level (2-tailed)*

Table (3) ***Anova***

Source	*SS*	*DF*	*MS*
Model	*6.5793e+21*	*3*	*2.1931e+21*
Residual	*1.0512e+22*	*46*	*2.2852e+20*
Total	*1.7091e+22*	*49*	*3.4880e+20*

Table (4) ***Regression Analysis***

DAC	*Coefficient*	*Std. Err.t*	*P > t*		*[95% Conf.*	*Interval]*
NPLR	*-2.78e+10*	*1.05e+10*	*-2.64*	*0.011*	*-4.90e+10*	*-6.63e+09*
SLR	*-121020.2*	*130701.9*	*-0.93*	*0.359*	*-384109.5*	*142069.1*
BD	*-121020.2*	*0.121934*	*-3.79*	*0.000*	*-0.7076533*	*-.2167727*
_Cons	*1.78e+10*	*3.04e+09*	*5.84*	*0.000*	*1.17e+10*	*2.39e+10*

No. of Obs	*50*
F (3, 46)	*9.60*
Prob. F	*0.0000*
R-squared	*0.3850*
Adj. R-squared	*0.3448*
Root MSE	*1.5e+10*

Findings from the regression result for the selected banks as depicted in table 4 suggest that the model is capable of explaining about 38% of the variability of banks' performance (measured as Profit after tax). Hence, this result suggests that simultaneously the explanatory variables are significantly associated with the dependent variable. The use of multivariate hypothesis test is based on the assumption of no significant multicollinearity between the explanatory variables. Non-existence of multicollinearity between the independent variables was confirmed when computing the variance inflation factors (VIFs) for each of the explanatory variables used in the study.

Interestingly, empirical evidence from the study suggest that consistent with our initially stated a priori expectations (i.e. $\beta_{1,}\ \beta_{2,}\ \beta_3 < 0$), a significant negative relationship was observed between non-performing loans and banks performance (measured as profit after tax) for the sampled banks. This is evident in the probability and t-statistics values of (P >|t| = 0.011 and -2.64, suggesting a rejection of the null hypothesis and the acceptance of the alternate proposition. This outcome implies that there is an inverse relationship between the ratio of non-performing loans and the performance of banks. This outcome supports the methodological juxtaposition of Kolapo et al (2012) where they opined that an increase in non-performing loan would eventually lead to a decrease in profitability.

Secondly, consistent with our a priori expectation, findings for the second hypothesis suggest that there is a negative association between secured and unsecured loan and performance of banks in Nigeria. However, this relationship is not significant as depicted in the P>|t| (Prob) value of (0.359 and -0.93) for secured and unsecured loan. Hence the null hypothesis is accepted.

This result thus corroborates the findings provided in Acquaah (2012 as cited in Shafiq and Nasr (2010).

Finally, consistent with the stated a priori expectation, findings provided in table (4) show that there is a significant negative relationship between bad debt and the performance of the sampled banks in Nigeria. This is evident in the probability and t-statistics values of (P >|t| = 0.000and -3.79). This outcome basically suggests that suggests that there is an inverse relationship between banks bad debt and the performance of commercial banks in Nigeria. In essence, the higher the bad debts written off from the profit, the lower the net profit and performance of banks thus leading to a decline in the amount of dividends to be distributed to shareholders and also the amount ploughed back into the business to enhance its future revenue earning capacity. Interestingly, this outcome is in tandem with the findings provided in Kargi (2011), Kithinji (2010), Felix and Claudine (2008).

5.0 Conclusion

This study examined the relationship between credit management and bank performance in Nigeria. Findings from our determination test indicate that about 38% of the variability in banks' performance (measured as Profit after tax) can be explained by the attributes of the credit management. Interestingly, the study observed that a negative relationship exist between secured and unsecured loan and performance of banks in Nigeria. However, this relationship is not significant. In addition, based on the hypotheses tested, findings from the study further provided evidence to support the arguments that ratio of non-performing loans and bad debt do have a significant negative effect on the performance of banks in Nigeria. This outcome corroborate the suggestion that the higher the bad debts written off from the profit of the bank, the lower the net profit and, therefore, the amount available for distribution as dividends to shareholders and, in fact, the amount ploughed back into the business to enhance its future revenue earning capacity. Hence, nothing the fact that bad debts destroy banks loan which are banks earning assets, the study concludes that banks management should establish sound lending policies, adequate credit administration procedure and an effective and efficient machinery to monitor lending function with established guidelines.

A salient limitation of this paper is the period for which the data is sampled. The sample horizon for this research is short compared to other related studies in the literature. To address this limitation, future research can increase the sample size and also examine the effect of other credit management variables on the financial performance of banks.

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