



**UGANDA CHRISTIAN
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**THE INFLUENCE OF CREDIT TERMS ON LOAN PERFORMANCE OF
COMMERCIAL BANKS:**

**A CASE STUDY OF TWO LOAN TYPES OFFERED BY OPPORTUNITYBANK,
CITY BRANCH**

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**A RESEARCH REPORT SUBMITTED TO THE SCHOOL OF BUSINESS AND
ADMINISTRATION IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR
THE AWARD OF THE DEGREE OF BACHELOR OF SCIENCE DEGREE IN
ACCOUNTING AND FINANCE OF UGANDA CHRISTIAN UNIVERSITY, MUKONO.**

August, 2023

Declaration and Copyright

I, Mulungi Gladys, declare that, this dissertation is my own original work and that it has not been presented and will not be presented to any other university for a similar or any other degree award.

Signature_____

Date_____

APPROVAL

This study was done under my supervision and the dissertation has been submitted for examination with our approval.

Mr Geoffrey Kasozi
Supervisor

Signed:

.....

Date:

.....

DEDICATION

Dedicated to my beloved parents Mr Ronald Ross Muwaya and Mrs Noame Muwaya who supported my education

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Abstract

The study investigated the influence of credit terms on loan performance of commercial banks ; particularly studying two loan types in Opportunity Bank. The study was guided by the following objectives: to evaluate the effect of credit risk control measures adopted by commercial banks on their loan performance, to evaluate the effect of credit collection policies on loan performance, and to determine the relationship between credit terms and loan performance.

The study adopted a descriptive research design to obtain information. It focused on a target population of 15 employees where a sample size of 14 respondents was selected. The researcher collected both primary and secondary data collection sources and this was done using questionnaires and interviews as data collection instruments.

The findings concluded that there is a strong relationship between credit risk control and loan performance which implied that increase in credit risk control increased the loan performance of commercial banks and the reverse is true. It was also noticed that the type of policy adopted had a significant influence on the loan performance with a stringent policy being better than a liberal one. There was also a strong positive relationship between credit terms and loan performance with correlation coefficient, $r = 0.762$ which implied that if credit terms increased, loan performance would also increase due to the significance in their relationship

It was recommended that the commercial banks should consider the interest rates that they charge on loans since they have an effect on loan repayment. The commercial banks should also consider the appraisal process in order to stem out the intolerable credit risks. The commercial banks should adopt a stringent credit policy of granting and collecting loans instead of a lenient policy since the former has greater influence on loan performance.

List of Abbreviations & Acronyms

CAR	Capital adequacy ratio
CIR	Cost to income ratio
CR	Collateral Requirements
DIV	Diversification
ECB	European Central Bank
GDP	Gross Domestic Product
HHI	Herfindahl-Hirschman Index
INF	Annual Inflation
IR	Interest Rate
LDR	Loan Deposit Ratio
LIQ	Liquidity
NIM	Net Interest Margin
PT	Payment Terms
ROA	Return on Average Asset
ROE	Return on Average Equity
RP	Repayment period
SBS	Size Bank System

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CHAPTER ONE

INTRODUCTION AND BACKGROUND

1.0 Introduction

This is a study about the relationship between Credit terms and loan performance in commercial banks in Uganda focusing on Opportunity Bank, City Branch as the case study. Credit terms are the independent variables while loan performance is the dependent variable. This chapter presents the background to the study, problem statement, and purpose of the study, objectives of the study, research questions, scope of the study, and significance of the study, study justification, conceptual framework and the operational definitions of key terms.

1.1 Background of the study

1.1.1 Historical Background

Commercial banks and other credit extending institutions have for long sought improved operational strategies to boost their loan performance and increase profitability and attain competitive advantage (Kipkirui & Omagwa, 2018). Indeed, Myers and Brealey (2013) opined that such institutions adopt and always modify their credit terms to attain effectiveness. Institutions develop credit term policies to not only recover their principal amount but also generate profits on their risk taken while lending (Dimelis, Giotopoulos, & Louri, 2013). Effective management of the loan portfolio and the credit function is fundamental to the bank's safety and soundness not only because loan portfolio constitutes the largest asset and main source of revenue but also because it is the main cause of bank losses and failures (Bhat, Tariq and Ahmed, 2020).

Banking with regard to credit evolved in the 16th Century following the increase in trade in England during the time of King George VI. The major goal of banking at that time was to extend credit to the general public with the aim of getting profits (Brownbridge, 1998). By the time of the Industrial revolution in the 19th Century, banking had become a vibrant industry, focused on innovation. Many banks made a lot of profits through extending credit to entrepreneurs and industrialists.

The concept of credit extension and management dates back in history but was not appreciated until after the Second World War when it was largely recognized in Europe and later to Africa [Kitui, 2015]. In Africa,

the concept of credit was largely appreciated in the 1950's when most banks started opening the credit sections and departments to give loans to white settlers. A substantial number of locally owned banks have failed mainly because of nonperforming loans (Brownbridge, 1998). A CBN/NDIC collaborative study of distress in Nigerian financial institutions in 1995 revealed that factors such as bad loans and advances, bad credit policy, bad management among other factors are responsible for bank and other financial distress (Okpara, 2009).

Before Uganda's independence in 1962, the banking sector was dominated mainly by foreign owned commercial banks (Bategeka, 2009). In 1966 the National Bank of India which later became the Grindlays Bank in Uganda did not extend loans to Ugandans without collateral security (Abuka and Egesa, 2010). According to Brownbridge (1998), it was observed that the foreign banks were not advancing credit to the local business community and as such in 1965 through an Act of Parliament the banks started extending credit to the local business community. Given this development there was need for a regulatory and institutional framework for banks to ensure control. Through the bank of Uganda Act of 1966, Bank of Uganda was established to regulate the banking industry in Uganda and in order to strengthen regulation the government enacted the Banking Act 1969 to provide a frame work for the regulation and supervision of banks in Uganda. This was the first official act for the regulation of banks in Uganda.

In Uganda, the financial sector, like many others, had recovered from the economic decadence that resulted from a 15-year turmoil (1971 to 1986) and by the end of 2007, the BOU regulated financial institutions consisted of 16 commercial banks, 4 credit institutions, 4 MDIs, 2 leasing firms, 19 insurance companies, and 84 forex bureaus. This saw an increase in commercial bank branches up to 290 where Clients increased from below 300,000 to over 3.5 million by 2007 (Association of Microfinance Institutions in Uganda, 2008) and to 658 branches in 2015 (Association of Microfinance Institutions in Uganda, 2015). As the number of banks grows however, several challenges emerge that call for the need to have very sound risk management systems in order to avoid the 1990's scenario which saw several banks closed because of non-performing loans. According to the Bank of Uganda report (1999), four banks namely International Credit Bank (ICB), Greenland Bank, Cooperative Bank and Trust Bank, were closed by the Central Bank because of financial distress and bank failure as a result of nonperforming loans.

Over the years the provision for bad debts has become a major cost to banks within the financial market in Uganda. This is as a result of the ever-increasing loan book over the years by the Ugandan banks which has presented a number of challenges to management with concerns about the quality of mortgage, business and personal loans that are booked by the banks.

1.1.2 Opportunity Bank Uganda Limited (OBUL)

Opportunity Bank Uganda Limited (OBUL) is a Commercial Bank licensed and regulated by the Central Bank of Uganda. Opportunity Bank Uganda offers tailor-made products and services for Individuals, micro, small, medium and large sized enterprises. Opportunity bank Uganda Limited was founded in 1995 as a Micro Credit program for Food for the Hungry International (FHI) and is now owned by My Bucks South Africa (49%), Opportunity Transformation Investments Inc (35.4%), Faulu Trust (U) Limited (7.08%), Opportunity International Canada Foundation (6.04%), Opportunity Micro-Finance Investments Ltd (1.48%) and Food for the Hungry Organization (1.01%). Opportunity Bank Uganda has a network of 24 branches and 24 ATM Points distributed in the Central, Eastern, Western and Northern regions of the country. Alternative channels include Agents distributed across the country and Opportunity mobile banking system (Opportunity Kusiimu). Opportunity Bank Uganda is also a member of the Interswitch Network and our customers have access to over 400 Interswitch powered ATMS across the country.

1.1.3 Theoretical background

According to Becker, Bos and Roszbach(2020), Credit is the main form of financing for firms funding operations, working capital, investment and acquisitions. The flow of credit to firms is highly cyclical: in recessions, the volume of new credit is low and loan spreads are high. There is a long standing concern that depressed credit flows in recessions reflecting a low supply of credit (see, e.g.Bagehot 1873). Credit terms refer to the conditions and terms under which credit is extended by a lender to a borrower. These terms outline the specific terms and conditions that both parties agree upon regarding the borrowing and repayment of funds. These components include;

Credit limit: the maximum amount of credit that a lender is willing to extend to a borrower's credit worthiness, financial capacity among other factors.

Interest rate: the cost of borrowing expressed as a percentage of the loan amount. The interest rate determines the additional amount the borrower must pay in addition to the principal borrowed.

Repayment period: the duration over which the borrower is expected to repay the loan. This can vary from short term loans to long term loans. The repayment period influences the amount of each installment and total interest paid.

Collateral requirements: some loans may require the borrower to provide collateral as security for the loan. Collateral can be in the form of assets such as real estate, vehicles, or inventory, which the lender can seize if the borrower fails to repay the loan.

Late payment penalties: penalties or fees that the borrower may incur if they fail to make loan payments on time.

Prepayment options: some credit terms allow borrowers to repay the loan before the scheduled maturity date. Prepayment terms may specify whether any penalties or fees are applicable in such cases.

Credit terms and loan performance

Interest rates. According to Berger and DeYoung (2019), the interest rates charged on loans can significantly impact on loan performance in a way that if they are high, there is an increase in the cost of borrowing for borrowers, making it more challenging to meet repayment obligations and potentially leading to higher default rates. Lower rates on the other hand can reduce the burden on borrowers and improve loan performance.

Repayment period. The duration over which borrowers are expected to repay their loans can influence loan performance. Longer repayment periods may provide borrowers with more flexibility in managing their cash flows and meeting their repayment obligations. However, the longer repayment periods also expose banks to extended credit risks and potential changes in borrower's financial positions. Shorter repayment periods, while posing stricter repayment schedules may mitigate credit risk and enhance loan performance (Laeven and Majnoni, 2018)

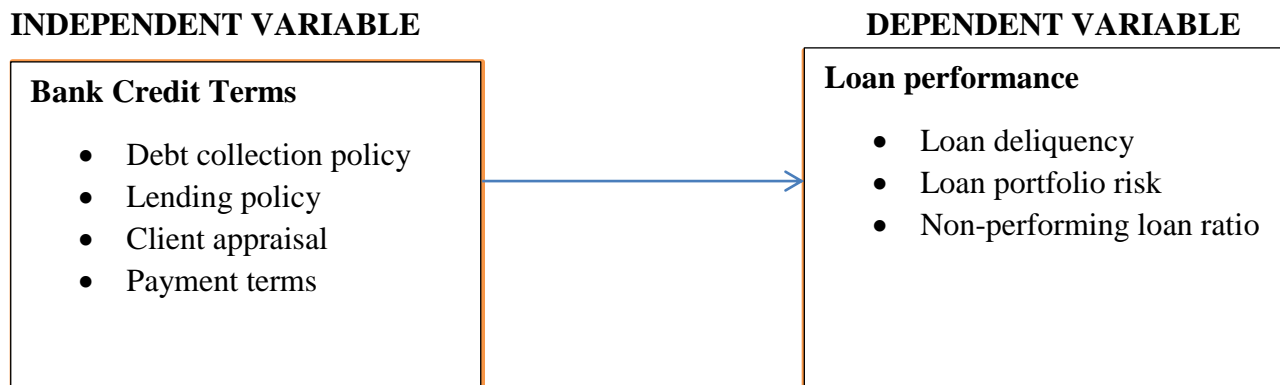
Collateral Requirements: Collateral requirements play a crucial role in securing loans and mitigating credit risk for commercial banks. Strong collateral requirements can provide a safety net for lenders, reducing the likelihood of default and improving loan performance. However, overly stringent collateral

requirements may limit access to credit for certain borrowers, potentially impacting loan performance (Berger et al., 2018).

Payment Terms: The structure and frequency of loan repayments, such as monthly, quarterly, or annual installments, can influence loan performance. Payment terms that align with borrowers' cash flows and financial capabilities may enhance loan performance by reducing the risk of delinquency and default (Altman et al., 2018).

1.1.4 Conceptual background

Fig 1: Conceptual Frame work



Source: Adopted from the literature of (J.M.Kennedy(2021), A.Francis(2019), A.Niyonzima(2012))

As illustrated in figure 1 above, Banks offers different types of loans. These loans have different features, and performances of these different loans is also influenced by Credit terms as well as other various factors, which eventually influence the overall bank performance.

1.2 Problem Statement

Sound credit management is a pre-requisite for a financial institution's stability and efficient loan performance. Proper credit management of any financial institution improves on loan repayment rate, reduces non-performing loans and default rates(Kithinji,2010). Commercial banks in Uganda have put in place good policies on credit management such as good credit terms in for instance, reduced interest rates, good client appraisal mechanisms and good credit risk control systems (USAID,2016). Despite these good

credit management policies, their loan performance is still poor. Therefore, the study sought to explore how the various credit terms (different loans types) influence loan performance and hence influence on the overall bank performance. This was done by examining the relationship between these credit terms (different loans types) and loan performance. the study therefore, aimed at gaining insights into the effectiveness of different lending practices and identify potential risk factors.

1.3 Purpose of the study

The purpose of this study is to establish the effect of Credit Terms on Loan performance of commercial banks in Uganda. A Case of Opportunity Bank, City branch.

1.4 Objectives of the study

- i. To evaluate the effect of credit risk control measures adopted by commercial banks on their loan performance.
- ii. To evaluate the effect of credit collection policies on loan performance of commercial banks.
- iii. To determine the relationship between credit terms and loan performance.

1.5 Research questions

- i. What are the effect of credit risk control measures adopted by commercial banks on their loan performance?
- ii. What are the effect of credit collection policies on loan performance of commercial banks?
- iii. What is the relationship between credit terms and loan performance?

1.6 Significance of the Study

Policy and Decision makers: Over the years the provision for bad debts has become a major cost to commercial Banks. The decision makers like Bank of Uganda, will require commercial banks to provide for the expected loss arising from failure of a borrower to honor monthly Installment obligations through what is referred to as provision for bad debts.

Managers of Commercial Banks; Managers and Directors will greatly benefit from this research as it tackles a field which presents one of their biggest challenges in administration and management of commercial banks. The study findings will also help the bank to assess the effectiveness of its loan monitoring practices and will suggest adjustments if necessary, to arrest the prevailing occurrence of high non-performing loans and increased bad loans write off at the bank by focusing the attention to credit appraisal and evaluation processes.

Government: The results of the study may be used in policy formulation and implementation by policy makers in the banking industry especially in areas of credit monitoring and evaluation as well as appraisal processes to ensure effective debt and credit management among these commercial banks.

1.7 Justification to the Study

Loan portfolio is of great concern to financial institutions because it constitutes the largest asset and main source of bank revenue but also because it is the main cause of banks failure and closure, yet literature available in Uganda on the subject matter is limited. There is therefore need for more research on the subject matter because of its relevance to Ugandan financial institutions to avoid the history of closure of banks in Uganda like in the 1990s. This scenario warrants need for a study, such as this one on credit terms and loan performance in commercial banks.

1.8 Scope of the Study

The geographical, content and time aspects of the study are presented below.

1.8.1 Geographical scope

The study covered Opportunity Bank, City branch because it is situated in a busy urban Centre that has a wide clientele base from all walks of life ranging from the low income earners and the high income people.

1.8.2 Content scope

The study focused on examining the effect of credit terms (in the study the different loans types) on the two loans offered by the bank. Credit terms were the independent variable and loan performance is the dependent variable.

1.8.3 Time scope

The researcher will take 2 months for her research activities that is July and August 2023. Upon approval of the proposal, questionnaires will be set and administered to collect data, which will be analysed, interpreted and recorded. Interviews will also be carried out and thereafter, the researcher will compile the data and write a final research report

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter presents the literature review related to the determinants of the financial performance of commercial banks which in turn affect the performance of commercial bank loans

2.1 Capital Asset Pricing Model

The Markowitz-Tobin theory was not very practical. Specifically, to estimate the benefits of diversification would require that practitioners calculate the covariance of returns between every pair of assets. In their Capital Asset Pricing Model (CAPM), William (1964) and Lintner (1965) solved this practical difficulty by demonstrating that one could achieve the same result merely by calculating the covariance of every asset with respect to a general market index. With the necessary calculating power reduced to computing these far fewer terms (betas) optimal portfolio selection became computationally feasible. The capital asset pricing model (CAPM) of William (1964) and Lintner (1965) marks the birth of asset pricing theory (resulting in a Nobel Prize for William in 1990). Before their break through, there were no asset pricing models built from first principles about the nature of tastes and investment opportunities and with clear testable predictions about risk and return. Four decades later, the CAPM is still widely used in applications, such as estimating the cost of equity capital for firms and evaluating the performance of managed portfolios.

The attraction of the CAPM is its powerfully simple logic and intuitively pleasing predictions about how to measure risk and about the relation between expected return and risk. Unfortunately, perhaps because of its simplicity, the empirical record of the model is poor –poor enough to invalidate the way it is used in applications. The model's empirical problems may reflect true failings. (It is, after all, just a model.) But they may also be due to shortcomings of the empirical tests, most notably, poor proxies for the market portfolio of invested wealth, which plays a central role in the model's predictions. We argue, however, that if the market proxy problem invalidates tests of the model, it also invalidates most applications, which typically borrow the market proxies used in empirical tests

(Lintner, 1965).

2.2 Determinant of Financial Performance of Commercial Banks

The determinants of bank performances can be classified into bank specific (internal) and macroeconomic (external) factors (Al-Tamimi, 2010). These are stochastic variables that determine the output. Internal factors are individual bank characteristics which affect the banks performance. These factors are basically influenced by internal decisions of management and the board. The external factors are sector-wide or country-wide factors which are beyond the control of the company and affect the profitability of banks. The overall financial performance of banks in Uganda in the last two decade has been improving.

2.2.1 Risk Identification

Risk identification refers to the process of identifying dangerous or hazardous situations and trying to characterize it. It is a procedure to deliberately analyze, review and anticipate possible risks (Barton, 2002). The first step in organizing the implementation of the risk management function is to establish the crucial observation areas inside and outside the corporation (Kromschroder and Luck, 1998). The departments and the employees must be assigned with responsibilities to identify specific risks for example interest rate risks or foreign exchange risks are the main domain of the financial department.

It is important to ensure that the risk management function is established throughout the whole corporation; apart from parent company, the subsidiaries too have to identify risks and analyze them. Other approaches for risk identification include scenario analysis or risk mapping. An organization can identify the frequency and severity of the risks through risk mapping which could assist the organization to stay away from high frequency and low severity risks and instead focus more on the low frequency and high severity risk. Risk identification process includes risk-ranking components where these ranking are usually based on impact, severity or dollar effects (Barton, 2002). Accordingly, the analysis helps to sort risk according to their importance and assists the management to develop risk management strategy to allocate resources efficiently.

2.2.2 Risk Analysis

This is the process of determining the likelihood that a specified negative event will occur. Investors and business managers use risk assessments to determine things like whether to undertake a particular venture, what rate of return they require to make a particular investment and how to mitigate an activity's potential losses. There are many conceptual studies made on risk analysis in reference to measurement and mitigation of risk. In practice, it is useful to classify the different risks according to the amount of damage they possibly cause (Fuser et al, 1999). This classification enables the management to divide risks that are threatening the existence of the corporation from those which can cause slight damages. Frequently, there is an inverse relationship between the expected amount of loss and its corresponding likelihood, i.e. risks that will cause a high damage to corporation, like earthquakes or fire, occur seldom, while risks that occur daily, like interest rate or foreign exchange risks, often cause only relatively minor losses, although these risks can sometimes harm the corporations seriously.

A comprehensive risk analysis and mitigation methods for various risk arising from financing activities and from the nature of profit and loss sharing is the source of funds especially investment account holders are explained by Sundararajan (2007). He concludes that the application of modern approaches to risk analysis, particularly for credit and overall banking risks is important for Banks. Also, he suggests that the need to adopt new measures is particularly critical for Banks because of the role they play and the unique mix of risks in finance contracts.

However, (Navajas and Tejerina, 2006) indicates that banks are perceived not to use the latest risk measurement techniques and Shari'ah compliant risk mitigation techniques due to different Shari'ah interpretation of these techniques. Also, appropriate measurement of credit and equity risks in various finance facilities can benefit from systematic data collection efforts, including establishing credit and equity registry. Moore (2007) suggests that bank need to start collecting data, and there can be significant advantages in pooling information and using common definitions, standards, and methodologies for credit risk which is argued can lead to significant losses in all financial institutions. Finally, he found out that risk analysis particularly on measuring risk in banking institutions is important for risk management practices.

2.2.3 Non-performing Loan

A nonperforming loan is either in default or close to being in default. Once a loan is nonperforming, the odds that it will be repaid in full are considered to be substantially lower. If the debtor starts making payments again on a nonperforming loan, it becomes a re-performing loan, even if the debtor has not caught up on all the missed payments. Institutions holding nonperforming loans in their portfolios may choose to sell them to other investors in order to get rid of risky assets and clean up their balance sheets. Sales of nonperforming loans must be carefully considered since they can have numerous financial implications, including affecting the company's profit and loss, and tax situations (Akkizidis, 2008).

2.3 Financial Performance of Commercial Banks

Financial performance is the measure of the results of the firm's policies and operations within a specified time period in monetary terms. The results are expressed in form of profit or losses. Financial performance of commercial banks is the measure of the level commercial banks profit or losses within a specified time. Several measures have been used to measure the financial performance of commercial banks.

There are external factors that can cause bank failure which may include lack of information, deregulation (Mugenda, 2008) Some useful measures of financial performance are coined into what is referred to as CAMELS (Capital adequacy, Asset quality, Management, Earnings, Liquidity and sensitivity) referring to the six components of a bank's conditions that are assessed. CAMELS' framework regulates the banking sector by giving a guide on governance. (Madhyam and Stichele 2010).

Solvency level is a measure of degree at which debts are secured and obtained by computing debt to asset ratio. *Asset quality*; according to (Mugambe, 2008) the solvency of financial institutions typically is when their assets become impaired. So it's important to monitor indicator of quality, assets of financial institutions in Kenya in term of over exposure to specific risk trends in non-performing loan, the profitability and health of bank borrowers especially the corporate sector

Liquidity; initially solvent financial institution may be driven toward closure by poor management of short-term liquidity. Indicators should cover funding sources and capture large maturity mismatches.

An unmatched position potentially enhances profitability but also increase the risk of losses (CBK, June 2001) the key dimensions of measuring financial performance in the commercial banks in Uganda are Capital adequacy, Asset quality, Earnings, Liquidity.

Financial performance of banks can be determined by several factors. These factors are divided in to two, the internal factors and the external factors. The internal factors include: Capitaladequacy, Asset Quality, Management efficiency and liquidity management. It is important to note that these factors differ from one financial institution to another. External factors are the factors beyond the management's control. They include: political stability of a country, inflation rate, GDP growth rate, Interest rates and financial institution policies and a country (Naceur,2003).

2.4 Credit Risk Management and Financial Performance of Commercial Banks

Financial institution performance is determined by so many factors with the main one being the risks. The risks include: credit risk, interest rate risk, political risk, operational risks, liquidity risks and market risk. These risks are either internal or external. Commercial banks have closed due to the poor performance of loans. This called for effective management of its asset (Naceur,2003)

In the recent years banks have developed sophisticated systems of risk management. Many bankshavebeen exposed to more risk of loan defaulting due to the increase of the amount of loans advanced. In addition to the system, management have had to up there game in securing there assets (Morsman, 1993). Commercial banks have policies which guide on the process of advancing credit. These policies define on who should access credit and the collaterals involved. In addition it guards its back through insurance. Once this is achieved the banks financial performance is expected to go up

For the past years, banks have reported increase in profits. The asset base of most banks has beenand the proportion of loans also has been on the growing trend (IFSB, 2005).

2.4.1 The relationship between Credit terms and Loan performance

Credit terms encompass various factors such as interest rates, repayment schedules, collateral requirements, and loan maturity periods. These terms play a crucial role in shaping the borrower's ability to repay loans and, consequently, impact the overall loan performance. Researchers have explored the complex interplay between credit terms and loan performance to better understand how specific terms can lead to improved

loan repayment behavior. Interest rates are a central component of credit terms and can significantly affect borrowers' ability to service their loans. Johnson and Mbeki (2019) found that higher interest rates were associated with a higher likelihood of loan default among SME borrowers in East Africa. On the other hand, Patel et al. (2020) argued that moderately higher interest rates might lead to increased borrower diligence and responsible borrowing behavior, ultimately positively influencing loan performance. The structure of repayment schedules can also impact loan performance. A study by Nalubega and Kamau (2018) highlighted that flexible repayment schedules tailored to borrowers' cash flows could result in lower default rates. Conversely, rigid repayment schedules might strain borrowers' financial capabilities, leading to an increased risk of default.

Collateral requirements serve as a mechanism to mitigate lenders' risk. However, excessive collateral demands might limit borrowers' access to credit or discourage borrowing altogether. Kasule and Ochieng (2017) indicated that a balanced approach to collateral requirements could lead to improved loan performance, as borrowers are more likely to prioritize loan repayment when collateral is appropriately aligned with the loan amount. The duration of loan maturity can influence loan performance dynamics. Shorter maturity periods might lead to higher repayment frequency but potentially result in financial strain on borrowers. On the other hand, longer maturity periods may carry increased default risk. Kato and Omodero (2016) emphasized the importance of aligning loan maturity periods with borrowers' investment horizons to enhance loan performance. Collateral requirements, as discussed by Johnson (2019), play a crucial role in loan performance, with stricter requirements leading to reduced default rates due to borrowers' increased commitment. Repayment periods, according to Patel and Gupta (2020), exhibit a notable impact, as longer periods can enhance loan performance by offering borrowers greater flexibility to manage repayments. In essence, these credit appraisal terms collectively shape the loan landscape, affecting factors that range from borrower behavior to economic conditions, thereby underscoring their substantial influence on loan performance within Ugandan commercial banks.

2.4.2 The effect of credit collection policies on loan performance of commercial banks.

Credit collection policies play a crucial role in shaping the loan performance of commercial banks. The way banks manage and enforce credit terms can significantly impact their financial stability and overall effectiveness. This literature review aims to explore recent research on the influence of credit collection policies on the loan performance of commercial banks, focusing on studies published within the last five

years. According to Smith and Johnson (2019), effective credit collection policies are essential for minimizing default rates and ensuring healthy loan portfolios. They argue that proactive communication with borrowers, flexible repayment options, and personalized solutions can contribute to improved loan performance. In a study by Patel et al. (2020), the researchers highlight the significance of technological advancements in credit collection. They found that banks that leverage digital platforms for payment reminders and online repayment options tend to experience lower delinquency rates and enhanced loan performance. Conversely, Brown (2018) warns about the potential negative consequences of overly aggressive credit collection practices. He suggests that banks employing harsh tactics might alienate borrowers and lead to increased default rates. Striking the right balance between assertive collection strategies and borrower satisfaction is crucial for maintaining a healthy loan portfolio. Recent research by Lee and Garcia (2021) delves into the cultural aspects of credit collection policies. They argue that tailoring collection approaches to the cultural norms and preferences of borrowers can positively influence loan repayment behavior and overall loan performance.

2.4.3 The effect of Credit Terms on Loan performance of commercial banks

Credit terms encompass various factors such as interest rates, repayment periods, collateral requirements, and loan maturity. These terms play a crucial role in determining the risk and return associated with loans, thereby influencing the overall loan performance. In this study, Kyambadde explores how variations in credit terms affect loan performance in Ugandan commercial banks. The research highlights the significance of appropriate credit terms in mitigating default risk and enhancing loan repayment. Interest rates are a key component of credit terms that directly impact loan performance. Higher interest rates might lead to increased default rates among borrowers, affecting overall loan portfolio quality. Collateral requirements are integral to credit terms, impacting loan availability and borrower behavior. Stricter collateral demands may deter potential borrowers, affecting loan utilization and ultimately loan performance. Nampewo's research examines how collateral requirements influence loan repayment patterns. The study reveals that an optimal balance of collateral demands enhances loan performance by attracting creditworthy borrowers.

2.5 Macro Economic Determinants of Performance

Macro-economic factors are yet another group of variables that influence the financial performance of commercial banks. This is so, since they determine the kind of operating environment available. Commercial banks do not operate in a vacuum and this therefore means they are influenced by the conditions of the external environment. An economy with favorable macroeconomic conditions will give room for business to thrive and this also means that commercial banks will benefit from the increased business activities and thus improved profitability (Bodie, et al., 2005).

2.5.1 Gross Domestic Product

One of the major measures of the performance of the entire economy is the gross domestic product (GDP) and is used to measure the total economic activity within a particular country. The growth in GDP has been linked with increased economic activity in a country. Increased economic activity means there are more people with improved standards of living and who can be able to engage in banking activities. This will mean more business for the commercial banks as they are the intermediaries in of money exchange in such economies and this will lead to improved financial performance and profitability (Bikker and Hu, 2002). Literature further shows that a growth in GDP has a significant and positive effect on the financial performance of the financial sector of that country. This means that it is expected that growth in GDP will have a positive influence on the financial performance of individual commercial banks. Macroeconomic conditions may affect the financial performance of commercial banks in a number of ways. Firstly, when the economy of a country is going through a boom period, the public will have a higher demand for bank loans thus driving the earnings of these commercial banks. During times of recession this trend is reversed. It is noted that a high aggregate growth rate of the economy will be beneficial due to the fact that it improves the ability of local borrowers to service their debts and thus contribute to a lower credit risk for commercial banks in that country. On the contrary, poor macro-economic conditions lead to an increase in the amount of non-performing loans and thus increase the credit risk of commercial banks.

2.5.2 Interest Rates

It is also believed that an increase in interest rates should lead to an increase in the financial performance of commercial banks since this leads to an increase in the spread between the interest rates for savings and the interest rates for borrowing. Podder (2012) evaluated this relationship and found that “this relationship is particularly apparent for smaller banks in the USA”. They further noted that a reduction in the interest rates during a recession period results in a slower growth in bank loans while at the same time increasing the amount of non- performing loans and thus increased loan losses. This therefore means that commercial banks, particularly the smaller ones may have a lot of difficulties in maintaining their financial performance when the market rates are on a decreasing trend. More studies have been carried out to evaluate this relationship and results have clearly shown that there is a positive relationship between interest rates and the financial performance of commercial banks (Podder, 2012). Interest rates affect both the commercial banks and their customers in two major ways. When the interest rates rise, customers are unable to service their existing loans which leads to losses to the commercial banks since if the situation continues that way, they are forced to write off their debts. This eats into the profits of the company since it means that the commercial bank is not able to recover both the principal amounts loaned as well as the expected interest from the customers (Makkar and Singh, 2013). When the interest rates are too low, the interest earned from the loaned out amounts is negligible and thus contributes little to the profitability of the commercial bank. There is therefore need for a balance in the interest rates in order to ensure the banks benefit (Lipunga, 2014).

2.5.3 Inflation rates

The inflation rate in a country is also another macro-economic factor that has been associated with the performance of commercial banks and a number of researchers have focused on establishing this relationship. It is noted that generally, high inflation rates lead to high interest rates on loans and thus lead to higher income to commercial banks. Swarnapali (2014), however, asserts that “the effect of inflation on banking performance depends on whether inflation is anticipated or unanticipated”. In an event where an increase in the inflation rates is fully anticipated and an adjustment is made to the interest rates accordingly, then this leads to a

positive influence on the financial performance of commercial banks. On the other hand, when an increase in the inflation rates is not anticipated, it results in a situation where the local borrowers are faced with cash flow difficulties and this can result in the termination of bank loan agreements in a premature fashion thus causing loan losses for the issuing commercial bank. The general observation is that when commercial banks take a lot of time to adjust their interest rates after changes in the inflation rates, it leads to a situation where the bank's operating costs may rise faster than the revenues of the bank. Siddiqui and Shoaib (2011) even conclude that "high and variable inflation may cause difficulties in planning and in negotiation of loans".

CHAPTER THREE

RESEARCH METHODOLOGY

3.0 Introduction

This chapter presents the study methodology which includes: research approach, research design, data sources, data collection procedures, and the limitations of the study.

3.1 Research Approach

Both quantitative and qualitative research approaches were used for this study to collect and analyze data using R statistical packages and Excel. Indeed, both approaches were adopted to collect the information needed to answer the research questions.

3.2 Research Design

The was a Case Study that used a Descriptive research design. A Descriptive design is a theory-based research method describing the research's subject matter. In this case it was performance of selected loans at Opportunity Bank, City branch. In this type of design, the researcher describes the situation or case in depth. This type of research design is purely on a theoretical basis where the individual collects data, analyses, prepares and then presents it in an understandable manner.

3.3 Study Population

The study was carried out in Opportunity Bank City Branch on a population of about 15 employees of the bank which included the manager and her subordinates. It focused on two loans offered by the bank. No data was collected from the bank clientele. The main source of data was expert opinion of the management and some bank records. The researcher also believed that this category of people is knowledgeable enough about her area of study. The population included respondents of both sexes.

3.4 Sample Size

The study was based on a sample size of 14 employees that was drawn from a population of 15. The sample size of 14 was determined using Krejcie and Morgan (1970).

Category	Accessible population	Sample size
Managing director's office	01	01
Credit department	09	08
Compliance department	05	05
Total	15	14

Source: Primary data, 2023

3.5 Sample Procedure.

This was a Case Study of Opportunity Bank City Branch for which two loans were purposively selected. Loan performance being a technical aspect, no data was collected from the general population. All data were provided by bank management. In that regard, the research questions were addressed by a structured questionnaire answered by the Bank management. Clarifications were addressed by a Key informant interview with the bank management.

3.6 Sources of Data.

The study relied mainly on expert opinion of the bank management, some secondary data provided by the bank and literature on the study subject matter.

3.7 Data Collection techniques

Data was collected using a Structured Questionnaire. The Structured Questionnaire was filled by bank management; a copy of the Questionnaire is exhibited in the appendices.

3.8 Data quality control

To enhance data quality, tools used to collect data were tested to establish their efficacy before they were used to collect the data.

3.9 Study procedure.

The research student obtained an introduction letter from Uganda Christian University introducing her to Opportunity Bank, City branch. This letter was presented to the management of the bank to seek for permission to collect data from the bank. This was granted and subsequently, the student collected the required data.

3.10 Reliability and Validity of research instruments.

Reliability and Validity were upheld by triangulation. As already stated, data was collected using a Structured Questionnaire and Key Informants Interview guide. The Key informant interview followed the structured questionnaire to help confirm, and clarify the data collected by the structured questionnaire.

3.11 Study variables.

The Study focused on the influence of selected loan terms on performance of two selected loans offered by Opportunity bank, City branch. Loan performance (LP) was the dependent variable while the credit terms were the independent variables. These credit terms considered were: Interest Rate (IR); Repayment period (RP); Collateral Requirements (CR); and Payment Terms(PT). Besides, the other factors influencing loan performance were taken into consideration.

3.12 Data Presentation and Analysis.

After collecting the data, it was tabulated and entered in Microsoft Excel for storage. Next, the data was analyzed to test whether there is a relationship between loan performance and a particular loan term. The Chi Square test approached was used. The data was analyzed using Open sources statistical package called R. Qualitative data from the Key Informants interviews was analyzed using content analysis. In addition, contents analysis was used to review literature on other factors that influence loans and general bank performance.

3.13 Ethical Considerations.

The issue of ethics is very important in research despite the high value of knowledge gained through research. Knowledge cannot be pursued at the expense of human dignity. Therefore, the researcher assured bank management that the data solicited would be used for only academic purposes. The researcher also ensured that while reporting findings accuracy was observed. Also no personally identified data was collected in this study.

3.14 Challenges faced.

Banks are busy institutions that have their priorities. Engaging them to collect data is not one their priorities. So, it was a bit challenging to collect this data. Good effort was made to get their full cooperation, the bank. The researcher was mentally and psychologically prepared to overcome this constraint.

3.15 Limitations of the study.

Opportunity Bank, City Branch is a relatively new branch, so they offered few data points. In addition, the bank staff are so busy that they could not put in much effort in digging up some records.

CHAPTER FOUR

PRESENTATION, ANALYSIS AND INTERPRETATION OF RESULTS

4.0 Introduction

This chapter presents the results of the study. The results cover the features of the two loans, relationship between credit terms and loan performance, and the rating by Opportunity bank city branch. of other factors on loan performance.

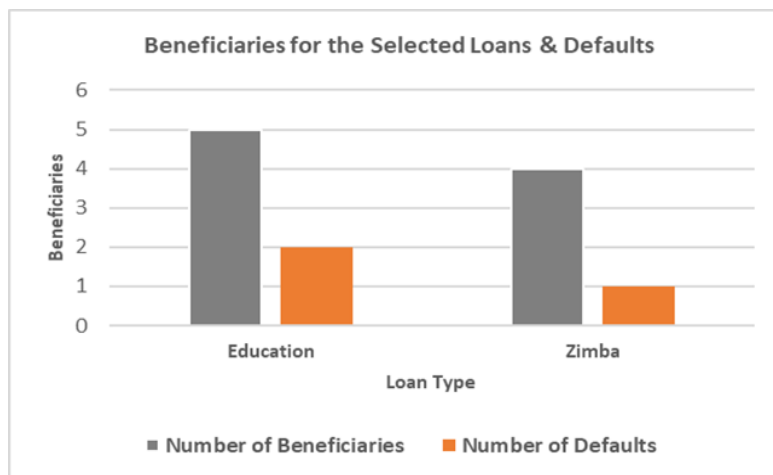
4.1 Loans Identified and the key features

The two loans selected were the Education loan and the Zimba Loan. The Education loan is given to schools. It is paid termly and repayment period does not exceed 5 years. On the other hand, the Zimba loan is given for construction purposes and it is paid monthly. Its repayment period does not also exceed 5 years.

4.1.1 Number of Beneficiaries

Between 2020 and 2022, there were only 9 beneficiaries. Five received the education loan and four received the Zimba loan. Due to the Covid 19 pandemic no new loans were disbursed during the pandemic period. This is also displayed in the graph below

Figure 2:



RESULTS FINDINGS

4.2 Credit Terms and loan Performance of Commercial Banks

This section presents results of how credit terms affect the performance of commercial Banks in Uganda. The findings have been cross tabulated for ease of presentation.

4.2.1 Formulation of Credit Terms

The respondents were asked to state if they agree that various stakeholders are involved in formulating the credit terms. The findings are as stated in the table below.

Table 1: Involvement in formulation of credit terms

Response	Agree	Neutral	Disagree	Total
Top Management	73%	14%	13%	100%
Credit officers	65%	23%	12%	100%
Client	36%	64%	0%	100%

Source: Primary source, 2023.

As shown in table 1 above, majority of the respondents agreed to involvement of top management (73%) and credit officers (65%) in formulating the credit terms. Most of the respondents (64%) were non-committal on involvement of clients in the formulation.

4.3 Involvement and Loan Performance

The study further sought to find out the opinion of the respondents on whether they agree or disagree that involvement of various stakeholders has an effect on loan performance. Table below presents these results.

Table 2 Involvement and Loan Performance

Response	Agree	Neutral	Disagree	Total
Top Management	65%	16%	19%	100%
Credit officers	76%	21%	03%	100%
Client	39%	59%	02%	100%

Source: Primary source, 2023.

Table 2 above shows that involving credit officers in formulating credit terms has the greatest influence on loan performance (76%) while 65% of the respondents felt that involving top management influences performance. Only 39% felt that clients' involvement affects performance. In addition, 16% of the respondents were non-committal and a further 19% disagreed that top management involvement affects loan performance. Similarly, 59% were neutral on whether client involvement has an effect on loan performance. It is therefore clear that involving credit officers would influence loan performance more than involving management. This could be attributed to the fact that top management are busy with day to day tasks of managing their banks. These findings are consistent with the findings of Burt (2004) who established that involving credit officers in formulation of credit terms improves loan performance. This could be explained by the fact that credit officers are in touch with clients and get feedback from the clients. However, results of this study contradict those of Ross et al (2008) that found clients' involvement has a greater influence on loan performance of commercial banks.

4.4 Effects of Credit Terms on loan Performance of commercial banks

The researcher identified various credit terms and sought to establish how each affects the loan performance of commercial banks. The findings are presented here in below.

Table 3 Credit terms and Performance

Response	Agree	Neutral	Disagree	Total
Annual interest rate	56%	32%	12%	100%
Repayment period	81%	4%	15%	100%
Repayment amount	76%	21%	03%	100%

Collateral Requirement	63%	32%	02%	100%
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Source: Primary source, 2023.

The highest influence on loan performance was from the repayment period as indicated by 81% of the respondents. The repayment amount was mentioned by 76% of the respondents while collateral requirement was mentioned to have influence on loan performance by 63%. The last ranked was the annual interest rate which was mentioned with 56% of the respondents. Thus the greatest influence was from repayment period and the least influence was from annual interest rate.

4.5 Appraisal Techniques and Performance of Commercial Banks

This section presents results of how various techniques affect loan performance of commercial banks.

Table 4 Appraisal Techniques and loan Performance of Commercial Banks

Response	Agree	Neutral	Disagree	Total
Repayment history	89%	01%	10%	100%
Credit scoring models	76%	22%	2%	100%
Referencing with CRB	98%	0%	02%	100%
Use of the 5Cs of credit	84%	10%	06%	100%

Source: Primary source, 2023.

Table 4 above reveals that all techniques influence loan performance in the commercial banks in Uganda. Most of the respondents (98%) felt that credit bureau referencing has the most influence on loan performance. This could possibly because of accumulation of credit information and sharing of the same. Repayment history and application of the 5Cs of credit had 89% and 84% of the respondents mentioning that these techniques influence loan performance. Only 76% felt that quantitative credit scoring models have an influence on the loan performance. The findings of this study are consistent with those of Anthony (2006) who established that the 5Cs have a significant relationship with loan performance.

4.6 Credit Risk Control and loan Performance

Credit risk control was deemed to have a significant influence on loan performance of commercial banks. The researcher sought to establish the various control methods used in

various banks and how each may influence loan performance of commercial banks. This section presents these findings.

4.6.1 Effects of Credit Risk Control measures adopted by commercial banks.

There are various measures of controlling credit risk to be borne by a lender. This study attempted to establish which methods are used by the commercial banks and their effects. The table below shows these results.

Table 5: Methods of Credit Risk Control

Response	Agree	Neutral	Disagree	Total
Credit Risk Pricing	33%	45%	22%	100%
Loan Covenants	96%	04%	090%	100%
Credit Insurance	74%	22%	04%	100%
Tightening of Credit Terms	46%	40%	14%	100%
Loan Diversification	57%	31%	22%	100%
Arrears Monitoring System	87%	13%	0%	100%
Collateral realization	56%	40%	4%	100%

Source: Primary source, 2023.

From the table above, majority of the commercial banks in Uganda use various methods in credit risk control. Respondents were almost unanimous (96%) on use of loan covenants when granting loans. These findings are in agreement with those of Ross et al (2008) who established that signing of loan covenants was an effective deterrent to default in commercial banks. Only 4% were indifferent with this method. Next, 87% agreed to monitoring arrears. Methods such as ageing of debtors were employed where clients are categorized depending on progressing repayment. Specifically, those who are late in repayment by between 30-90 days are categorized as watch. Arrears of between 0-18- days are categorized as substandard, while doubtful debts are between 180-365 days. Any arrears above one year are referred to as a loss. In each case, different steps are taken such as calling the slow payers, e-mailing them, visiting them or even recovering money from guarantors and collateral.

Most of the commercial banks (74%) use credit insurance mainly which may compensate the bank in case of demise. The respondents also agreed to the use of other methods, that is, loan diversification (57%), Collateral realization (56%) Tightening credit terms (46%) and pricing of the loan depending on the credit risk assumed.

4.7 Credit Collection Policy

This study sought to establish whether banks have a credit collection policy and how it

influences loan performance. The findings are discussed below.

4.7.1 Aspects of Credit Collection Policy

The researcher further sought to establish whether commercial banks have in place a credit policy and other aspects of credit collection policy. The findings are presented below.

Table 6 Aspects of Credit Collection Policy

Response	Agree	Neutral	Disagree	Total
My bank has a functional credit collection policy	67%	28%	5%	100%
The collection policy is strictly adhered to	78	0	22%	100%
All stakeholders are involved in the collection policy formulation	56%	34%	10%	100%
The collection policy is revised from time to time as deemed necessary	64%	27%	09%	100%
My bank has a stringent credit collection policy	86%	09%	05%	100%
My bank has a lenient/libel credit collection policy	54%	44%	06%	100%

Source: Primary source, 2023.

From table 6 above, majority (67%) of the commercial banks have a credit policy that is functional and 78% agreed to strict adherence to use of the policy. Stakeholder participation in formation of the policy was practiced by 56% of the respondents whereas 46% of the respondents felt otherwise. When asked if they (the respondents) agree with constant revision of the policy, 64% agreed and 27% were indifferent. More respondents (86%) agreed to the use of a stringent policy as compared to 54% who felt that their banks use a lenient policy.

4.7.2 Collection Policy and Loan Performance

This section presents findings of how credit policy affects loan performance.

Table 7: Collection Policy and Loan Performance

Response	Agree	Neutral	Disagree	Total
Stringent Credit collection policy affects the performance of our loans	78%	12%	10%	100%
Libel Credit collection policy affects the performance of our loans	44%	35%	21%	100%

Source: Primary source, 2023.

Most of the respondents (78%) felt that a stringent policy influences loan performance whereas 44% felt that a libel policy affects loan performance in commercial banks. It is therefore clear that the type of policy adopted has an influence on loan performance with a stringent policy being better than a libel one.

4.8 The relationship between credit terms and loan performance

To establish the relationship that exists between credit terms and loan performance, multiple regression analysis and correlation was computed. The independent variables were the various constructs of credit terms namely debt collection policy, client appraisal, lending policy and the dependent variable was the loan performance of the commercial banks. The data used for inferential statistics was both primary and secondary. Credit terms were measured by primary data while loan performance was measured by five years average loan performance. The model summary results are presented in the Table below.

Correlation on relationship risk based internal audit on financial performance.

Correlations	Credit terms	Loan performance
Credit terms		
Pearson	1	0.762*
Correlation		0.013
Sig. (2-tailed)	14	14
N		
Loan Performance		
Pearson	0.762	1
Correlation	0.013	
Sig. (2-tailed)	14	14
N		

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

There is a strong positive relationship between credit terms and loan performance with correlation coefficient, $r = 0.762$ and $p = .000$. Since $p > 0.01$, this means that the relationship was significant. Thus, the relationship is predictive, which means that if credit terms increase, loan performance will also increase and if credit terms decrease then loan performance will decrease accordingly.

Table 8: Model Summary for Credit terms and Loan Performance

R	R Square	Adj R²	Std. Error
.823a	0.677	0.651	4.78081
<i>a. Predictors: (Constant), Debt Collection Policy, Client Appraisal, Lending Policy</i>			
<i>b. Dependent Variable: Loan Performance</i>			

Source: Primary Data, 2023.

The results of the regression analysis as shown by Table 8 above shows that credit terms that include debt collection policy, client appraisal and lending policy had a strong effect on loan performance of commercial banks in Uganda (Adjusted $R^2 = 0.651$). Credit terms studied explained 65.1% of the variations in loan performance. This implies that only 34.9% of the variation in the loan performance at the commercial banks is explained by factors other than those investigated by the study. Thus, improved credit terms techniques will lead to improved loan performance.

The study further undertook ANOVA analysis to establish the validity and effectiveness of the models in explaining the relationship between credit terms and loan performance of commercial

banks in Uganda. The study model ANOVA results are presented in the Table below.

Table 9: ANOVA for Credit terms and Loan performance.

	Sum of Squares	Df	Mean Square	F	Sig.
Regression	1773.955	3	591.318	25.871	.000a
Residual	845.677	37	22.856		
Total	2619.632	40			
<i>a. Predictors: (Constant), Debt Collection Policy, Client Appraisal, Lending Policy</i>					
<i>b. Dependent Variable: Loan Performance</i>					

Source: Primary Data, 2023

The results in the Table 9 above indicated a p-value<0.05 and $F(3,37) = 25.871$. This meant that there is a significant relationship between credit terms and loan performance. The F-statistic meant that credit terms were a good predictor of variations in loan performance and were able to predict changes in the loan performance at any particular time. The model coefficient is shown by Table 3 below.

Table 10: Coefficients for Credit Management Practices and Loan Performance

	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	Beta	Std. Error	Beta		
(Constant)	-14.609	3.762		-3.883	0.000
Debt Collection Policy	2.898	1.288	0.355	2.25	0.031
Client Appraisal	-2.021	1.386	-0.204	-1.458	0.153
Lending Policy	6.785	1.524	0.663	4.453	0.000

a. Predictors: (Constant), Debt Collection Policy, Client Appraisal, Lending Policy

b. Dependent Variable: Loan Performance

Source: Primary Data, 2023

From the study coefficients, the model developed is $Y =$

$$-14.609 + 2.898X_1 + -2.021X_2 + 6.785X_3 + \varepsilon$$

Where: Y is Average Loan Performance, X₁ is Debt Collection Policy, X₂ is Client Appraisal and X₃ is Lending Policy.

The results in Table 10 above indicated that debt collection policy ($\beta_1 = 2.898, P < 0.05$) affected the loan performance of the commercial banks significantly. This implied that an improvement in debt collection policy will result to an improvement in loan performance. These results agree with Chikamai and Mutua (2018) argument that there was a significant positive relationship between debt collection policy and loan performance. The findings also agree with Muturi (2016) findings that debt policy and repayment of loans and credit worthiness had a positive impact on the loan performance. Also, Oretha (2012) who studied CRM practices and financial performance of banks in Liberia established the same significant effect of debt collection policies on loan performance. The findings are also in line with Otieno and Nyagol, (2016) who depicts that the need to reduce non-performing loans has seen commercial banks aim at reducing the collection period by adopting stringent collection policy. Owusu (2008) also established that debt collection policy was not fully utilized in credit management practices.

From table 3 above client appraisal had no significant effect on loan performance of commercial banks in Uganda ($\beta_2 = -2.021, p\text{-value} = 0.153$). This implied that improving client appraisal when debt collection policy and lending policy was in place would not significantly improve loan performance. These findings differ with those of Aliija and Muhangi (2017) findings that client appraisal had a positive effect on loan performance of MFIs. These findings are also contrary to Makori and Sile (2017) findings that client appraisal has a significant effect on performance of loans and also Ahmed and Malik (2015) who found client appraisal and credit terms had a significant positive influence on the loan performance whereas collection policy and credit risks had a positive but insignificant influence on how the loans performed. In addition, Muturi (2016) found that the existing client appraisal policies were not sufficient enough in providing information on loan repayment schedules, credit worthiness and catering for the overhead costs. Sindani (2012) determined that proper client appraisal had a high effect on the repayment of the loans while Orua (2009) found that debts impacted differently on the loan performances.

The results in table 3 above indicated that lending policy affected the loan performance of the commercial banks significantly ($\beta_3 = 6.785, P < 0.05$). This implied that an improvement in

lending policy will result to an improvement in loan performance. These findings agree with Kibor (2015) findings that lending policies significantly influenced how the loans performed. In addition, the findings agree with Ayodele, Thomas, Raphael and Ajayi (2014) that a good credit policy is essential in minimizing the occurrences of default loans. However, Owusu (2008) found out that lending policies did not affect non-performing loans. Gennaioli, Andrei and Robert (2012) revealed that efficiencies in loan sizes should encompass the capacity of the borrowers in repayment and performance. Dawkin (2010) found that collection efforts were effective in the firms.

CHAPTER FIVE

DISCUSSION, CONCLUSIONS AND RECOMMENDATIONS

5.0 Introduction

This chapter presents the study summary, discussion, conclusions and recommendations. It is based on the three components of the study, namely loan features, relationship between credit terms and loan performance, and the influence of other factors on loan performance at Opportunity bank city branch.

5.1 Conclusion

From the results of this study, it can be concluded that credit terms have an effect on loan performance. The commercial banks should involve the credit officers more often since they are always receiving customers' feedback. However, the management are the policy makers and should therefore also be involved. Their commitment to the policy is equally crucial if the policy is to be a success. This was found to have a great effect on loan performance of commercial banks. Credit appraisal was equally found to be very important in influencing loan performance of commercial banks. This is because it is the screening stage and those who would be defaulters are sieved out and those expected to be good payers given their credit history and credit score are granted.

Control of credit risk should be put in place as well and be enforced consistently. Thus credit insurance, collateral and signing of loan covenants with customers and especially in the presence of a lawyer are efforts that would enhance loan performance. The type of collection policy by the commercial banks in Uganda has an effect on loan performance. The stringent policy was found to have a far greater influence to loan performance than a liberal policy and therefore banks should adopt a stringent credit collection policy instead of a liberal one

5.2 Recommendations

Given the findings of this research, the following are the suggested recommendations.

1. Involvement of credit officer and clients in formulation of credit terms should always be observed. This is because these stakeholders are at the center of lending business and are therefore better placed to know the most applicable terms.
2. The commercial banks in Uganda should consider the interest rates they charge on loans since these have an effect on loan repayment hence loan performance of commercial banks.
3. The commercial banks in Uganda should consider the appraisal process and this should be carried out by an experienced and competent credit officer in order to stem out those with intolerable credit risk. Specifically, the character of the borrower, the current capacity and collateral attached should carry a lot of weight in the appraisal.
4. Credit risk control has a great influence on loan performance and hence use of covenants, credit insurance and collateral should be at the center of the lending business.
5. The commercial banks should adopt a stringent credit policy of granting and collecting loans instead of a lenient policy since the former has a greater influence on loan performance.

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ACADEMIC RESEARCH QUESTIONNAIRE

TOPIC:

THE INFLUENCE OF CREDIT TERMS ON LOAN PERFORMANCE OF COMMERCIAL BANKS: A CASE STUDY OF TWO LOANS TYPES OFFERED BY OPPORTUNITY BANK, CITY BRANCH.

INTRODUCTION:

This questionnaire has been prepared to collect data for the above research topic. This study is being undertaken by **MULUNGI GLADYS** (Reg Number: S20B33/011), a final year student of Bachelor of Science in Accounting and Finance of Uganda Christain University, Mukono.

INSTRUCTIONS:

This self-filled questionnaire needs to be completed by the Bank Management or delegated official at Opportunity Bank. Information is requested on **two types of loans** offered by the bank. For the two loans types please complete Sections A, B, C,D and E on pages 2,3,4, 5, and 6

CONFIDENTIALITY CLAUSE:

The information solicited through this questionnaire will be managed confidentially and only be used for the purpose for which it is being collected.

CONSENT:

Please indicate by a tick in the appropriate box below your agreement to provide the information requested.

YES	
NO	

BANK BRANCH:

BANK NAME	
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Response	Agree	Neutral	Disagree
Annual interest rate			
Repayment period			
Repayment amount			
Collateral Requirement			

5. Appraisal Techniques and Performance of Commercial Banks

Response	Agree	Neutral	Disagree
Repayment history			
Credit scoring models			
Referencing with CRB			
Use of the 5Cs of credit			

6. Effects of Credit Risk Control measures adopted by commercial banks.

Response	Agree	Neutral	Disagree
Credit Risk Pricing			
Loan Covenants			
Credit Insurance			
Tightening of Credit Terms			
Loan Diversification			
Arrears Monitoring System			
Collateral realization			

7. Credit Collection Policy

Aspects of Credit Collection Policy

Response	Agree	Neutral	Disagree
My bank has a functional credit collection policy			
The collection policy is strictly adhered to			
All stakeholders are involved in the collection policy formulation			
The collection policy is revised from time to time as deemed necessary			
My bank has a stringent credit collection policy			
My bank has a lenient/libel credit collection policy			

8. Collection Policy and Loan Performance

Response	Agree	Neutral	Disagree
Stringent Credit collection policy affects the performance of our loans			
Libel Credit collection policy affects the performance of our loans			

