CREDIT RISK MANAGEMENT AND FINANCIAL PERFORMANCE IN FINANCE TRUST BANK, UGANDA

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A DISSERTATION SUBMITTED TO THE SCHOOL OF BUSINESS IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF BACHELOR OF SCIENCE IN ACCOUNTING AND FINANCE OF UGANDA CHRISTIAN UNIVERSITY

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DECLARATION

I, Nambuule Winnie Nkata, declare that this dissertation is my original work and has never been published or submitted for any award in any other institute or University.

Signed :..... Date: 15th/04/2026.

Nambuule Winnie Nkata

APPROVAL

This is to certify that the research report has been under my supervision and is now ready for submission to the school of business for the award of degree of bachelor of science in accounting and finance at Uganda Christian University. was done under our supervision, and the dissertation has been submitted for examination with our approval.

Signed: ..... Date: 15/04/2026

Mr. Ahabwe Alex

DEDICATION

I would like to dedicate this piece of writing to my beloved parents, friends and family for they have been supportive to my education from the start to now, lam highly indebted to give names to my loving Taata Eng Nkata Pascal and Mr muluya Robert who have tirelessly encouraged me with inspirational guidance and knowledge development. Thank you for your support and may the almighty God reward you abundantly.

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ABSTRACT

This study which examined credit management and the financial performance of financial institutions in Uganda was carried out at the Finance Trust Bank branch in Kampala.

This study examined the effect of credit risk management practices on the financial performance of Finance Trust Bank (FTB) in Uganda. The research specifically investigated the influence of credit risk identification, assessment, and control practices on key financial performance indicators, including profitability, revenue growth, return on assets, and overall financial sustainability.

The study concludes that effective credit risk management is critical for enhancing financial performance in Ugandan commercial banks. It recommends that FTB and other financial institutions continuously strengthen their risk identification, assessment, and control systems, including regular stress testing, collateral management, and use of advanced credit scoring models, to sustain profitability and minimize non-performing loans.

CHAPTER ONE

1.0 Introduction

The research will focus on credit risk management and its implications for the financial performance of commercial banks working in Uganda. In this respect, this chapter outlines the context of the inquiry, defines the problem statement, outlines the study objectives, formulates the research questions, and defines the study scope and the importance and justification of the study.

1.2 Background to the Study

Financial performance is the measure of success of any financial institution. The goal of such an institution is to maximise profits and increase shareholder returns on investment (Khan and Ahmed, 2022). The decision on whether a bank is sustainable as a going concern is arrived at as a result of profitability, an increase in revenue, liquidity stability, and general financial sustainability. When financial performance becomes poor, investor confidence reduces, operational capacity is compromised, and the future of the institution's survival is jeopardised. Therefore, maintaining healthy financial performance is front and centre of the banking activities globally.

However, the risk to financial performance in banks is extremely high. Risk is omnipresent in any company and has an impact on industries (Uryema and Deventer, 1993). Risk can take various forms in different industries, but it cannot be eliminated; it can be minimised to reasonable levels by using strategic management strategies. The effectiveness of risk management is only effective when it is aligned with the expectations of the stakeholders and organisational goals (Dickinson, 2002). The inability to adequately handle risks has in the past led to the downfall of large corporations across the globe. As an example, the Enron debacle added more arguments to the discussion of corporate governance and accountability (Bester, 1994). These were so disastrous that on 30 July 2002, the Sarbanes-Oxley Act was passed, which highlighted the importance of Enterprise Risk Management as a way of averting fraudulent reporting (Bester, 1994).

Out of the different types of risk that banks are vulnerable to, credit risk is the most significant type of risk since it directly threatens financial performance. Credit risk is the likelihood of losses to come about due to default or lack of ability by a borrower to repay loans in full and within the

prescribed time (Bofondi and Gobbi, 2003). The actual risk in credit is realised when a borrower is unable to pay or when his or her credit standing becomes worse (Bofondi and Gobbi, 2003). According to Coyle (2000), credit risk can only be properly managed by using a systematic credit-management programme that entails identification, measurement, monitoring, and control.

Traditionally, credit-risk management emerged as a leading agenda after the 1960s, after the economic shocks that had occurred after World War II. According to John (2021), credit-risk management was not developed in the 1990s, and many institutions did not have specific departments. But bad debts were accumulating, and the financial volatility encouraged the adoption of organised credit-risk-management functions. At the onset of the 2000s, credit-risk management emerged as a potent instrument of reducing credit risk, particularly in the context of a fluctuating financial market (Economic Intelligence Report, 2011; Gobbi, 2013). The significance of risk management was further enhanced by the events happening in the world, like the September 11 attacks and corporate scandals like Enron and WorldCom (Williams, Smith, and Young, 1998; Baranoff, 2004). In the modern banking industry, the credit risk has been on the rampage because of technological innovation, dependence on third-party information systems, high competition, and increased customer expectations (Hassan Al-Tamimi and Al-Mazrooei, 2007).

Poor credit-risk management has also compromised the performance of banks in Uganda. The failure of the Greenland Bank is a good illustration of what may happen due to weak risk management. The gross loan portfolio before it was closed was topped by insider loans exceeding 40 percent, and financial stability was considerably lost.

This theoretical study is based on the moral-hazard theory. According to Milton (2000), negative incentives can lead to risky lending practises by the bank owners and managers against the interest of depositors. According to this theory, there are three major processes of credit management, namely, loan approval, loan monitoring, and loan termination, that are intended to achieve effective credit-risk management. The moral-hazard theory thus emphasises proper credit-risk identification, measurement, and monitoring as a means of protecting the solvency of the banks and eventually improving financial performance.

There are three main components to credit risk management. Risk identification determines the possible organisational risk and areas where resources have been exposed (Williams, Smith and Young, 1998). In this paper, risk identification will include credit-risk origin and risk classification. The process of risk assessment entails the examination of risks that could make organisational goals unachievable (Holton, 2003). It entails the assessment of the financial statements of the borrowers, the industry trends, and the economic conditions to ascertain the quality of the credit. Risk control is the policies, procedures, and systems that maintain the risks within the appetite of the bank, such as risk mitigation and monitoring systems (Holton, 2003).

Applying to the case of the Housing Finance Bank (HFB), one of the 24 commercial banks in Uganda (Bank of Uganda Report, 2022), the bank is mostly engaged in mortgage and credit lending (Bank of Uganda Report, 2023). HFB has put in place a credit-risk-management unit and effective guidelines that are aimed at identifying, analysing, and curbing credit risks that could pose a threat to profitability and sales. Despite these, the bank is still witnessing increasing bad-loan portfolios, loan defaults, and write-offs. This tendency provokes some concerns related to its financial performance, which makes it necessary to investigate the connection between credit-risk management and financial performance at HFB.

1.3 Statement of the Problem

Proper identification, risk assessment, and risk control of credit risk should protect the financial performance of financial institutions and their sustainability (Hassan Al-Tamimi and Al-Mazrooei, 2007). Once such strategies are effective, the non-performing loans ought to decrease, bad debts ought to decrease, and profitability ought to increase. In Housing Finance Bank Uganda, the management has adopted different credit-risk-management techniques, which focus on the identification and assessment of risk and management of the risks (FTB Board of Directors Report, 2023). The strategies will be aimed at handling risks associated with the default of clients and thus safeguard the financial performance of the bank.

Nevertheless, despite these efforts, FTB is still facing growing rates of non-performing loans and bad debts. The non-performing loans grew to 1,000,427,882,842 in FY 2024 compared to 800,657,058 in FY 2023, and the bad debts grew to 100,025,649 in FY 2024 compared to 80,723,013 in FY 2023 (FTB Annual Report, FY 2024 This has resulted in a dwindling profitability where the profits have reduced to 95,235,760,000,000 in 2024 compared to

76,543,900,000,000 in 2023. This trend would possibly undermine the competitive edge of the bank, the confidence of the shareholders, the stability of the liquidity, and eventually the sustainability of the bank in the long run. Although current reports state that non-performing loans are on the increase, and profitability is on the decrease, the question that remains unclear is how the credit-risk-management practises (risk identification, risk assessment, and risk control) affect the financial performance of the bank. Consequently, the proposed research aims at analysing the correlation between credit-risk management and financial performance in banks in Uganda and, in particular, Finance Trust Bank.

1.4 Objectives of the study

1.4 .1General Objective of the Study

The general objective of this study was to examine the effect of credit risk management on the financial performance of FTB.

1.4.2 Specific objectives

The study will be guided by the following specific objectives.

1. To examine the effect of credit risk identification practices on the financial performance of Finance Trust Bank.
2. To analyze the effect of credit risk assessment practices on the financial performance of Finance Trust Bank.
3. To determine the effect of credit risk control practices on the financial performance of Finance Trust Bank.

1.5Research Questions

1. What is the effect of credit risk identification practices on the financial performance of Finance Trust Bank?
2. What is the effect of credit risk assessment practices on the financial performance of Finance Trust Bank?
3. What is the effect of credit risk control practices on the financial performance of Finance Trust Bank?

1.6 Significance of the Study

The results of the present study have substantial value to three main stakeholder groups, namely, FTB management, commercial bank management, and academia.

1.6.1 For FTB Management

This inquiry identifies major gaps in the credit risk management procedures of FTB, which include identification, evaluation, and control procedures. The supported recommendations provided below explain how to maximise the use of credit assets, strengthen risk-management approaches, and maintain a clean, highly profitable credit portfolio.

1.6.2 To the Commercial Bank Management.

The empirical findings provide practical information to managers in other commercial banks regarding credit-risk identification, evaluation, and management refinement. Using these findings, institutions will be able to increase the quality of decision-making, reduce future losses, and eventually improve the overall financial performance.

1.6.3 For Academia

The study adds to the body of strong empirical evidence about the nexus between credit-risk management practises and financial performance in commercial banks with a specific focus on a developing country setting like Uganda. It fills the existing gaps in the literature and provides a strong basis for further academic research on credit-risk management and banking performance.

1.7 Justification of the Study

The research is supported by a glaring gap in information with respect to credit risk management in the financial institutions, particularly in the FTB context. Although credit risk is a critical factor in the determination of financial performance, there is a dearth of empirical information on how the identification, assessment, and control of credit risk can be operationalised and how the inter-relationship between these functions determines the overall bank performance. These dynamics should be fully understood to make sure that banks effectively optimise their portfolio of credits and reduce the possible losses.

The study provides practical information that can be used by FTB as well as other trading banks to streamline their credit-risk management procedures. The results of the systematic examination of the processes of risk-identification, risk-assessment, and risk-control expose the spheres in which the efficiency levels can be increased, the strength of decision-making can be enhanced,

and the financial performance can be improved. This is particularly applicable to banks operating in the environment of developing countries, where resource limitations and regulatory requirements create the need to have more efficient risk-management techniques.

Moreover, the research contributes to the body of literature in that it covers areas that have not been well pursued in the literature on the relationship between credit-risk management practise and financial performance in commercial banks. It explains how risk management has a bearing on profitability and provides a sound basis for future research in similar institutional and developing countries. The lessons learnt can also be used as a practical guide to other financial institutions that would want to embrace the best practises in credit-risk management, and hence attain sustainable financial growth.

1.8 Scope of the study

1.8.1 Content Scope

The current investigation examines the effects of credit risk management on the financial performance of commercial banks, and especially on Finance Trust Bank. It explores the risk identification, risk assessment, and risk mitigation dimensions, questioning how the processes of risk identification, risk assessment, and risk mitigation can reveal possible defaults, gauge borrower credibility, and manage loan portfolios efficiently. The researchers use such financial performance indicators as profitability, return on assets, loan quality, and institutional stability. It can provide practical information on how to improve risk management to maximise performance, decision-making, and sustainability of banking institutions by defining the nexus between credit risk practises and financial outcomes.

1.8.2 Time Scope

The time frame of the study is between 2021 and 2025.

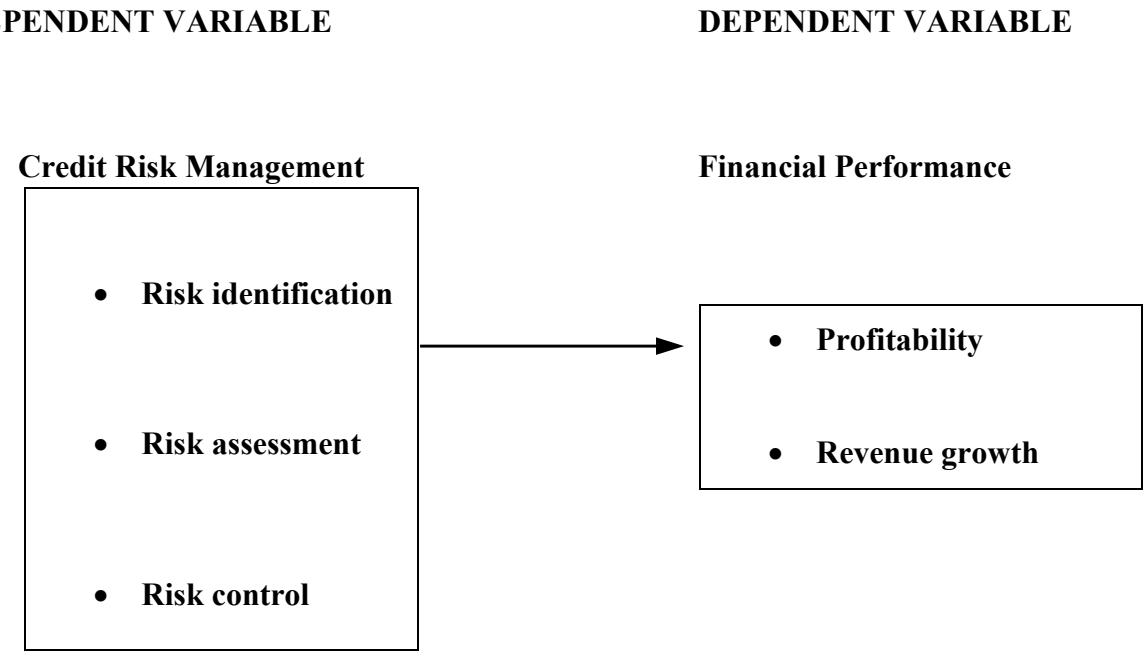
1.8.3 Geographical Scope

The scope of the geographical analysis is limited to the Finance Trust Bank location in Kampala, Uganda. This is a purposeful choice, which offers a proper environment to study the interdependence between the credit risk management practises and the financial performance of the bank.

1.9 Conceptual Framework

The conceptual framework outlines the relationship between the two main variables that are under consideration: credit risk management and financial performance. Based on this, the framework assumes that identification, assessment, and mitigation of credit risk processes directly and substantially impact the financial performance of the institution.

Figure 1: Conceptual framework



Source: *Adopted and modified from the works of* Vaubel (1983)

Figure 1 above shows the correlation between the independent variable, Credit Risk Management, and the dependent variable, Financial Performance of commercial banks, in reference to Finance Trust Bank. The operationalisation of the Credit Risk Management has three main dimensions, namely risk identification, risk assessment, and risk control, which collectively form the major mechanism through which a bank effectively deals with the exposure to credit-related losses that could be a result of borrower default. Risk assessment involves careful assessment and analysis of the risks that are identified with the use of the relevant risk data, financial information, and estimation methods to identify the probability and extent of possible losses. Risk control is a measure of the strategies and procedures used to reduce and oversee credit risk, such as risk-

reduction measures and constant control over the performance of loans. These dimensions combined effectively reflect the impact of the structured practises of credit risk on the exposure of a bank to non-performing loans and financial instability.

Financial Performance is a dependent variable that is manifested by quantifiable results in terms of profitability and an increase in revenues. Profitability refers to the capacity of the institution to make profits after expenses, and revenue growth is the growth in income earned through lending and other financial services. These pointers reflect the financial stability of the bank, its efficiency, and its ability to support shareholder value in a competitive banking environment.

The connection between credit-risk management and financial performance is based on the premise that by the successful identification, evaluation, and management of credit risk, loan defaults and bad debts are minimised, thus leading to increased profitability and growth of revenues. Effective risk identification allows identifying high-risk borrowers in early stages; risk-assessment instruments provide the ability to make informed lending decisions; and risk-control mechanisms restrict the exposure to financial losses. In contrast, inadequate credit-risk management is likely to contribute to higher non-performing loans, falling revenues, and decreased profitability despite the formal banking policies.

This means that the conceptual framework shows that the financial performance of the commercial banks, especially Finance Trust Bank, is directly dependent on the effectiveness of the credit-risk management practises adopted within the bank.

CHAPTER TWO
LITERATURE REVIEW

2.0 Introduction

This chapter is a systematic review of the available literature about credit risk management and its implications on the financial performance of banking institutions. It is divided into the following parts: introductory discussion, theoretical exegesis, critical survey of contemporary literature, and brief conclusion.

2.1 Theoretical Review

The current research is based on the Moral Hazard Theory, which is a variant of the more general Agency Theory. The Agency Theory, which is the expression of Michael C. Jensen and William H. Meckling (1976), questions the contractual nexus between principals and agents. It assumes that when decision-making power is delegated to the managers, it could create a conflict of interest because the agents might have their selfish interests at the expense of the principals, thus, the agency cost is incurred, especially in the absence of monitoring instruments.

In 1983, Roland Vaubel applied the moral-hazard theory to the banking industry, observing that banks, which are insured by deposit guarantees or government guarantees, can be tempted to take too much risk. Moral hazard is effective when a party is not at risk and therefore is not as constrained in its actions. Managers and shareholders in banks tend to take more risk in their lending positions since any losses may be vastly covered by depositors, regulators, or insurance programmes instead of the decision-makers themselves.

The theory has widely spread following the banking crisis of the 1980s and 1990s, which exposed weaknesses in loan screening and supervisory procedures. Indicatively, high levels of non-performing loans and institutional insolvency were associated with dubious credit evaluation procedures and lending decisions in most economies that were politically motivated. These events supported the hypothesis that a poor internal control environment and faulty incentives increase the exposure to credit risks. In reaction to such challenges, academic and regulatory bodies emphasised the need to have formalised credit-risk management systems. Timothy W. Koch and Scott S. MacDonald (2000) argued that proper risk governance begins with careful management of loans, including careful screening of borrowers and pricing of risky loans. They have highlighted that risk selection should be prudent as it is the only way to maintain the quality of the portfolio. Similarly, Comptroller Handbook (2000) recommended that the approval standards be

strict, constant monitoring and internal controls should be very strong to reduce the risk of default. Milton H. Spencer (2000) has defined the three critical processes in credit management: the approval process, the monitoring process, and the termination process; all of which jointly serve the purpose of assessing risks before credit is granted, managing risks throughout the life of the loan, and managing distress cases accordingly.

This historical trajectory demonstrates how the Moral Hazard Theory has been transformed since its initial, strictly theoretical, formulation to a practical application, which defines the current credit-risk practises. The relationship between credit-risk management and financial performance is supported by empirical studies. Research always proves that weak identification and monitoring processes bloat non-performing loans, hence killing profitability and halting revenue growth. On the other hand, effective credit appraisal systems and good internal controls improve the quality of assets and financial stability.

In the Finance Trust Bank context, the Moral Hazard Theory provides a theoretical tool to analyse the relationship between institutional performance and risk-management practises. If the theory threatens that credit-risk identification, appraisal, and oversight systems fail to do their job satisfactorily, the loan officers might be tempted to focus on quantity over quality, where performance incentive schemes tie compensation to disbursement targets. This kind of behaviour increases default risk and reduces profitability. Through enacting stringent screening policies, methodical appraisal processes, and exemplary monitoring measures, the bank will be in a position to reduce the negative incentives, enhance the portfolio quality, and strengthen the general financial health.

Therefore, not only does the Moral Hazard Theory explain the causes of too much risk aversion in banks, but it also explains why structured risk-management regimes are needed, which directly underpins the exploratory aim of the given study.

2.3 Empirical literature review

2.3.1 Credit Risk Identification and Financial Performance

Risk identification is generally considered the key component of the risk-management continuum (Kleindorfer and Saad, 2005). Mitigation efforts cannot be resident without prior identification of the presence of risk. Buhman, Kekre, and Singhal (2005) continue that a holistic approach to identification is essential to the identification of all the salient risks before the deployment of

assessment and control mechanisms. All these scholars confirm that antecedent judgment plays a crucial role in deciding whether a risk should be further explored.

Craighead, Blackhurst, Rungtusanatham, and Handfield (2007) build on this argument and argue that the level of disruption depends on how fast an organisation becomes aware of being exposed to risk. They concur that early prediction and environmental scanning are central to helping in timely mitigation efforts. Combined, these studies may indicate that successful identification breeds organisational readiness and reduces the chances of disastrous financial turbulence. However, the empirical support of the theoretical significance of risk identification in the literature is strong, but there is little empirical research on the relationship between structured credit-risk identification practises and current financial performance in Ugandan commercial banks. Such scarcity creates doubt as to how far the early detection can be converted into quantifiable profitability and revenue increase in the Ugandan banking landscape. In this regard, this study aims to empirically question this relationship in Finance Trust Bank.

2.3.2 Identification of Credit Risk Origin and Financial Performance

Brownbridge (1998) argues that insider lending is the largest contributor to the deleveraging crisis of many of the failed African banks. The research identifies that insider lending constituted a high proportion of non-performing portfolios and was frequently allocated to speculative projects, such as real-estate development projects, hospitality projects, and shopping complexes, thus surpassing exposure limits and creating maturity mismatches. This fact highlights how disastrous a poorly recognised credit-risk source could be to the performance of the banks. Brownbridge goes on to hypothesize that in Uganda, high lending rates were charged on borrowers in high-risk groups of the credit market. The practise led to adverse selection in which many borrowers had failed to meet the tough foreign-bank creditworthiness requirements in the past. The coincidental lack of specialised screening experience and weak internal credit procedures contributed to the further decline in the quality of loan portfolios, which supports the thesis that ineffective identification of the origins of credit risks undermines financial stability.

Llewellyn (2008) demonstrates that unsustainable business models and a lack of supervisory controls initiate high default rates and subsequent insolvency. Paul (2007) notes that credit decisions are co-determined by macro-economic conditions, capital supply, and industry characteristics. Credit-risk exposures are amplified by seasonal business ventures and companies

that work during recessions, which require higher credit due to fluctuating cash flows. Mazumder and Ahmad (2010) also indicate that inadequate regulation of excessive risk-taking, particularly in economic exuberance, spreads real estate and systemic distress. As such, the corpus of literature agrees that credit-risk arises as a result of a group of internal and external factors- such as insider lending, adverse selection, speculative investments, weak supervision, and macro-economic volatility. However, these studies are descriptive and lack an empirical understanding of how the modern process of identifying certain sources of credit risk may affect the financial performance of the Ugandan commercial banks. Therefore, there exists a significant contextual gap in relation to the impact of the identification of the origins of credit risk on the profitability and revenue trend in Housing Finance Bank. Our study attempts to fill this gap through a systematic examination of the nexus between the identification of credit-risk origins and economic performance in the banking sector of Uganda.

2.3.4 Credit Risk Classification and Financial Performance

The risk classification after the identification identifies the way the identified risks are classified and prioritised (Berg, Knudsen, and Norrman, 2008). According to Kleindorfer and Saad (2005), identification is the pre-step process, and thereafter, the appraisal efficacy solely depends on the quality of initial classification. Therefore, risks that are identified and classified appropriately can only be assessed and managed, and this means that classification actively defines risk-response architecture.

Llewellyn (2008) opines that loans constitute the major cause of credit risk among banks, but off-balance-sheet exposures can also play a role. He also argues that credit risk should not be viewed in the context of direct accounting loss to include opportunity costs and transaction costs associated with non-performing assets. This expanded outlook embraces the economic exposure aspects. In line with this argument, Paul & Boden (2008) observe that the expansion of trade credit allows firms to accumulate financial information of the customers in terms of payment behaviour, thus narrowing down risk classification. Marrison and White (2002) further explain that good credit-risk governance will bring competitive advantage and minimise the incidence of defaults, and poor classification and administration of credit tenets will usually lead to the failure of banks.

Amato and Remolona (2003) provide a more complex perspective by noting how hard it is to attain diversification when there is skewness in bond yields; their analysis of collateralised debt

obligations (CDO) proves that potential diversification is limited even where incentives are present. According to Bevan and Garzarelli (2000), the yield spreads are related to GDP growth, and Bewley, Rees, and Berg (2004) did not find such a relationship in Australia. Longstaff, Mithal, and Neis (2005) find that most credit spreads have been attributed to the default risk, whereas Chen, Lesmond, and Wei (2007) claim that the liquidity factor has been credited with the change in credit spreads, especially in speculative grade bonds. These combined results depict that the credit-risk classification is intertwined with the macro-economic variables and liquidity variables in intricate aspects. Although these scholars show a large coverage of the classification dimensions, they do not give much empirical information on the impact of practises of classification within the Ugandan commercial banks on the current financial performance. Therefore, it is not yet definite whether structured credit-risk classification will increase profitability and revenue growth in Finance Trust Bank. This research undertaking purposefully fills this research gap.

2.3.5 Credit Risk Evaluation and Financial Performance.

The risk assessment involves the identification, measurement, monitoring, and management of exposures on a wider institutional ecosystem (Tomlin, 2006). Zsidisin, Ellram, Carter, and Cavinato (2004) argue that the main aim of assessment is to create detailed information needed to prevent or alleviate risk. Kleindorfer and Saad (2005) also emphasise the necessity of evaluating the risk and events that are interrelated. Collectively, these studies are in agreement that the strength of assessment enhances risk-response mechanisms. The importance of policy guidelines that outline the process of credit allocation and portfolio management is emphasised by Basel (1999), Greuning and Bratanovic (2003), and Pricewaterhouse (1994). Heffernan (1996) concurs with this and says that transparent credit-approval procedures are key to the management of credit risk. According to Cole, Glenn, and Brent (2005), accurate credit evaluation filters out high-risk borrowers and matches risk-return expectations and portfolio limitations. The same is also highlighted by Ralston and Wright (2003), who stress systematic identification and modification of the lending terms before approval. There are two main methods of assessing creditworthiness that are proposed by Abdou and Pointon (2009): repayment capacity appraisal and asset-backed lending. They maintain that institutions should examine the integrity of borrowers, the competence of the managers, as well as the quality of collateral. Nevertheless, the expert-based approach can fail because of a lack of training, bureaucracy, and over-concentration of portfolios.

Basel II, through an internal ratings-based approach (Jacobson, Linde and Roszbach, 2006), attempts to match the capital requirements with risk exposure. Haber (2007) observes that the majority of banks prefer this more sophisticated method even though the approach has a potential effect on the cost of borrowing by small and medium enterprises (Esperance, Ana, and Mohamed, 2003).

Banco de Portugal (2010) established that reduced lending volume was a result of the reduced lending criteria. Blumberg and Letterie (2008), Berger and Black (2011), and Berger and Udell (2002) point out that the information asymmetry among SMEs is a problem that makes it difficult to determine the risks accurately. Though the literature is emphatic in support of rigorous credit-risk appraisal as a key to good banking, there is still uncertainty on how the use of credit-risk data and estimation practises, in particular, affects the financial performance in the Ugandan commercial banks. Thus, this research examines how the credit-risk evaluation procedures affect the profitability and revenue-generating in Finance Trust Bank.

CHAPTER THREE
METHODOLOGY

3.0 Introduction

The chapter gives an outline of the methodological framework that will be used to analyse credit risk management practises and the accompanying effect they have on the financial performance of Housing Finance Bank. It describes the research methodology, research design, research setting, population, sample size, sampling methods, data collection tools, validity and reliability measures, methods of data analysis, ethical considerations, and constraints of the study. The framework is well-developed to maintain the utmost standards of academic rigour, plausibility, and systematic investigation of the interrelation between credit risk management and financial performance.

3.1 Research Approach

The research methodology used was a mixed paradigm of investigation that incorporated both quantitative and qualitative research methods. The quantitative strand enabled the empirical quantification of the associations among the components of credit risk management, which include risk identification, risk assessment, and risk control, and key performance measures, including profitability and growth in revenues, by using numerical data. The qualitative strand supplemented the quantitative results by instilling deep insights of the key informants on the institutional credit policies, mitigation of risks, and practical challenges that encroach on financial performance. The intersection of these techniques increased triangulation, strengthened validity, and provided a subtle insight into the causal processes by which management of credit risks affects financial performance.

3.2 Research Design

The research design is a systematic plan that will assist in data collection, measurement, and analysis in an organised manner. Based on this, a cross-sectional and simultaneous mixed-method design was employed. In this design, the quantitative and qualitative data were collected simultaneously at one time, analysed independently, and then combined during the interpretation process. The cross-sectional design enabled effective data collection without the necessity of repetitive observations, which makes it time-pragmatic in assessing the current credit risk management practises. The quantitative element allowed hypothesis testing about the interrelations among the risk identification, risk assessment, risk control, and financial performance. The qualitative aspect provided the explanatory background of the policies in terms

of policy implementation, loan monitoring, and internal control structures. This parallel mixed-method design is considered appropriate because credit risk management represents both a technical and a managerial aspect, which requires quantifiable indicators and experience.

3.3 Study Area and Population

The field study was within the Head Office of Finance Trust Bank, based in Kololo, Kampala. The institution is a controlled financial institution providing mortgage and retail banking services in Uganda. The sample size included 70 employees who were selected in the Credit and Finance Departments and included eight Senior Managers, two Loan Pricing Officers, and sixty Retail Credit Officers. These participants were chosen because of their personal experiences in credit appraisal, loan pricing, monitoring, risk management, and financial reporting, which makes them the right respondents in an in-depth examination of credit risk management practices and financial performance.

3.4 Sample Size Determination

The size of the sample in the quantitative component was determined by the Krejcie and Morgan (1970) table at the 95 percent confidence level. To establish a statistically sufficient sample of respondents, there was a calculation of 62 respondents out of a population of 70 employees. The qualitative aspect was based on purposive selection of key informants who were selected on the basis of their strategic positions in credit risk management and financial management.

3.5 Sampling Techniques and Procedures.

Both non-probability and probability sampling methods were used to support the mixed-methods design.

3.5.1 Stratified and Simple Random Sampling.

The first stratification of the population was conducted based on three groups, namely Senior Management, Loan Pricing Officers, and Retail Credit Staff, so that there must be a proportional representation of the three categories. Retail Credit Officers were then chosen using simple random sampling, so the selection bias was reduced and the representativeness was increased. All the members of this stratum had the same chance to be selected.

3.5.2 Purposive Sampling

Key informants such as Senior Managers, Loan Pricing Officers, the Risk Manager, and the Internal Auditor were identified using purposive sampling. These people were chosen due to their

specialised knowledge and involvement in credit risk policies, financial reporting, and internal control, and hence depth of information and contextual understanding.

3.6 Data Collection Methods and Instruments

A mix of both quantitative and qualitative data collection tools was used in the study.

3.6.1 Questionnaire

The main data-collection instrument was a structured questionnaire, which is a systematic set of items that are aimed at gathering standardised quantitative data. It helped to obtain primary data in a relatively large cohort in a rather efficient and objective manner. The tool consisted of five parts, which include: demographic characteristics; credit risk identification; credit risk assessment; credit risk control; and financial performance indicators (sales revenue and profitability). The answers were taken on a five-point Likert scale as Strongly Disagree (1), Strongly Agree (5). The questionnaire was self-administered, and the respondents were given an opportunity to provide knowledgeable responses based on their work experience. It was designed in such a way that it facilitated statistical analysis, reduced the bias of the interviewer, standardised responses, and increased the validity and reliability of the results.

3.7 Instrument validity and reliability.

Strict measures were implemented to ensure the quality and credibility of instruments.

3.7.1 Content Validity

An expert appraisal was done to establish content validity. The research supervisor and academic experts examined the instruments to identify their relevance, clarity, and completeness with respect to the constructs of credit risk management and financial performance.

3.7.2 Construct Validity

Construct validity was assessed using Exploratory Factor Analysis (EFA). Adequacy was tested by the Kaiser Meyer Olkin (KMO) measure and the Bartlett Test of Sphericity. The products with factor loading of 0.50 or more were carried forward to further analysis.

3.8 Data Collection Procedure

The management of the Finance Trust Bank was approached with a letter of introduction, which was obtained by way of the School of Business, requesting that the management approve the study.

Questionnaires were sent to the selected respondents via mail and collected after being filled out and sent back to the researcher upon approval. Interviews were arranged when the key informants found it convenient. The researcher made sure that all the participants understood the purpose of the study before engaging them.

3.9.2 Qualitative Data Analysis

Interpretations of qualitative data in the form of interviews were analysed using thematic analysis. Coding of the transcripts was done to reveal patterns, themes, and categories that were relevant to credit risk implementation and its impact on financial performance. Quotations that were selected were included to support emergent themes and triangulate quantitative findings.

3.9.3 Integration of Findings

The quantitative and qualitative strands' results were synthesised in the interpretation phase, which provided an in-depth explanation of the role of credit risk management practises in the financial performance.

3.10 Ethical Considerations

There were strict ethical standards that were observed during the investigation. The authorities of the university and the management of Finance Trust Bank were shown formal permission. The study was voluntary, and informed consent was received from all the respondents. Anonymity and confidentiality were ensured by not including identifiers in the questionnaires and interview transcripts. The data were utilised for academic purposes and kept safely to avoid unauthorised access. The researcher ensured that there was no harm inflicted on the participants, either psychologically, professionally, or socially.

3.11 Limitations of the Study

The preliminary reluctance of the respondents due to the consideration of confidentiality was reduced with the help of reassurance and the issuance of formal authorisation letters. There were other challenges that were faced in the form of financial constraints and time pressures, but they were well planned and scheduled, limiting their effects. Follow-up reminders were used to solve the problem of delayed questionnaire returns, which guaranteed a sufficient response rate.

CHAPTER FOUR

DATA PRESENTATION, ANALYSIS AND INTERPRETATION

4.0 Introduction

This chapter presents, analyses, and interprets the study findings on credit risk management and financial performance in FTB. It specifically presents the response rate, Demographics of the respondents, description of variables, and findings of the study objective.

4.1 Response Rate

A total of 62 questionnaires were issued, and 54 were returned, as shown in Table 4.1 below.

Table 4.1: Response Rate

Category	Questionnaires issued	Questionnaires returned	Response rate (%)
Senior Managers	8	7	87.5
Loan Pricing Officers	2	2	100
Retail Credit Officers	52	45	86.5
Overall response rate	**62**	**54**	**87.1**

Source: Primary data 2025

Table 4.1 above shows an overall response rate of 87.1%, which was high and suggests that the survey results were representative. Fincham (2008) contends that a response rate of 50% is representative enough and acceptable for a survey.

4.2 Demographics of the Respondents

This section reflects the distribution of respondents by sex, age, position in the bank, and years of experience, as shown in Table 4.2.

Table 4.2: Background Information on the Respondents

	Details	Frequency	Percentage
Gender of the respondent	Male	38	70.4
	Female	16	29.6
	Total	**54**	**100**
Age of the respondent	Between 25 – 30	6	11.1

	Between 31 – 35	14	25.9
	Between 36 – 40	18	33.3
	Between 41 – 45	9	16.7
	Between 46 – 50	5	9.3
	Above 50	2	3.7
	Total	**54**	**100**
Position of the respondent	Senior Manager	7	13.0
	Loan Pricing Officer	2	3.7
	Retail Credit Officer	45	83.3
	Total	**54**	**100**
Years of experience	1 – 5 years	19	35.2
	6 – 10 years	22	40.7
	11 – 15 years	9	16.7
	Above 15 years	4	7.4
	Total	**54**	**100**

Source: Primary Data 2025

According to Table 4.2, males contributed more to the sample with 70.4% of the respondents compared to the females who contributed 29.6%. This suggests that the majority of the staff in the Credit and Finance Departments of Finance Trust Bank are male.

Table 4.2 also shows that the category of 36 – 40 years dominated the sample by contributing 33.3% of the respondents. This was followed by 31 – 35 years (25.9%). This suggests that the majority of the staff are in their mid-career stage.

Retail Credit Officers dominated the sample (83.3%), which reflects the relative staffing structure in the credit function. Staff with 6 – 10 years of experience formed the largest group (40.7%), indicating a good mix of experience and institutional knowledge.

4.3 Description of the Dependent Variable: Financial Performance of FTB

The dependent variable, financial performance of FTB, was conceptualised through perceptual indicators of profitability and revenue growth. It comprised 6 quantitative items measured on a five-point Likert scale (1 = Strongly Disagree, 2 = Disagree, 3 = Not Sure, 4 = Agree, 5 = Strongly Agree) as shown in Table 4.3.

Table 4.3: Statistics for Respondents' Self-Rating on Financial Performance

Financial Performance Indicator	N	Mean	SD
1. Profitability has improved significantly in the last three years	18	4.0000	0.912
2. Revenue growth from lending activities has been strong	15	3.9815	0.845
3. Non-performing loans have reduced noticeably	12	3.7222	1.021
4. Return on assets has shown a positive trend	14	3.8704	0.938
5. Shareholder returns have increased	11	3.6481	1.078
6. Overall financial sustainability of the bank has strengthened	16	3.9815	0.891

Source: Primary Data 2025

Table 4.3 reveals that profitability has improved significantly (Mean = 4.0000; SD = 0.912) and revenue growth from lending has been strong (Mean = 3.9815; SD = 0.845). Overall financial sustainability also scored highly (Mean = 3.9815). These emerged as the key indicators of financial performance.

4.4 Credit Risk Identification Practices and Financial Performance of FTB

The first objective was to examine the effect of credit risk identification practices on financial performance in Trust Finance Bank. The findings on credit risk assessment and financial performance were gathered from a questionnaire, and the interview guide construct was measured using 5 items on the same five-point Likert scale ranging from 5= strongly agree,4=agree,3= not sure,2=disagree, and 1=strongly disagree.

Table 4.4: Descriptive Results for mean and standard deviation of credit risk assessment in FTB.

Response	N	Mean	SD
1. The bank has clear policies to identify potential credit risks early	22	4.1852	0.823
2. Regular scanning for insider lending and related-party risks is done	19	4.1111	0.856
3. Macro-economic factors are routinely assessed before lending	14	3.9444	0.912
4. Borrower credit history and collateral are thoroughly screened	21	4.1481	0.801
5. Risk classification and prioritisation are done systematically	18	4.0926	0.845

Source: Primary Data 2025

The bank has clear policies to identify risks early (Mean = 4.1852) and thorough screening of borrower history (Mean = 4.1481). These scored the highest means and emerged as the strongest identification practices.

4.5 Credit Risk Assessment Practices and Financial Performance of Financial Institutions

With respect to the second objective, we examined credit risk assessment practices. The findings were tabulated as follows using a 5-point Likert scale, the means, and standard deviation.

Table 4.5: Descriptive Results for Credit Risk Assessment Practices

Assessment Practice	N	Mean	SD
1. Financial statements of borrowers are rigorously analysed	20	4.1296	0.867
2. Credit scoring models and rating systems are used effectively	17	4.0926	0.823

3. Industry and economic trends are incorporated in assessments	15	3.9444	0.938
4. Collateral valuation is updated regularly	19	4.0370	0.912
5. Stress testing of loan portfolios is conducted periodically	16	4.0000	0.856

Source: Primary Data 2025

From the research findings of financial statements (Mean = 4.1296) and effective use of credit scoring models (Mean = 4.0926) emerged as the key assessment practices.

4.6 Credit Risk Control Practices and Financial Performance

The third objective examined credit risk control practices on the financial performance of financial institutions. The findings were tabulated below using a 5-point Likert scale.

Table 4.6: Descriptive Results for Credit Risk Control Practices

Control Practice	N	Mean	SD
1. Loan monitoring and follow-up systems are robust	23	4.2407	0.801
2. Limits on exposure and concentration risk are strictly enforced	21	4.1852	0.823

3. Early warning signals for default are acted upon promptly	19	4.1111	0.845
4. Collateral and guarantees are enforced when needed	18	4.0926	0.856
5. Regular review and restructuring of problem loans occur	20	4.1296	0.912

Source: Primary Data 2025

Robust loan monitoring (Mean = 4.2407) and strict enforcement of exposure limits (Mean = 4.1852) scored the highest and emerged as the dominant control practices.

Conclusion

This chapter presented and interpreted the results in line with the study objectives, which included assessing the effect of credit risk assessment on the financial performance of financial institutions in Uganda, analyzing the influence of credit policies on the financial performance of financial institutions, and examining the effect of credit risk control practices on the financial performance of financial institutions.

CHAPTER FIVE
SUMMARY,DISCUSSION, CONCLUSION, AND RECOMMENDATIONS

5.0 Introduction

This chapter discusses the study findings in relation to the research objectives. It also consists of a general conclusion and recommendations of the research report.

5.1 Discussion of key research Findings

5.1.1 Credit Risk Identification Practices and Financial Performance of FTB

The study found a positive relationship between credit risk identification practices and the financial performance of financial institutions examined the effect of credit risk identification practices on financial performance. Respondents rated identification practices highly (means 3.94–4.19), with strong emphasis on clear early-risk policies (M=4.1852), thorough borrower screening (M=4.1481), and regular scanning for insider/related-party risks (M=4.1111). Financial performance indicators were also positively perceived (profitability M=4.0000; revenue growth M=3.9815; overall sustainability M=3.9815).

These positive perceptions align with moral hazard theory (Vaubel, 1983), which stresses proactive identification to counter incentives for risky lending. Effective early detection reduces information asymmetry and moral hazard, preventing defaults that erode profitability.

The findings support empirical literature indicating that structured risk identification enhances portfolio quality and reduces NPLs (Brown Bridge, 1998; Klerksdorp & Saad, 2005). In FTB's context, strong identification likely contributed to controlled NPL growth (from ~4.3% in 2023 to ~3.7% gross NPL ratio in 2024 per bank reports) amid 22% loan book expansion and 178% profit surge in 2024. This suggests identification practices have supported resilience despite sector-wide credit pressures.

5.1.2 Credit Risk Assessment Practices and Financial Performance of FTB

The research findings analysed credit risk assessment practices and financial performance of financial institutions, which implied that respondents strongly endorsed rigorous analysis of borrower financial statements (M=4.1296), effective credit scoring models (M=4.0926), and regular collateral updates/stress testing (M=4.0370–4.0000).

These practices mitigate adverse selection and moral hazard by enabling informed lending decisions (Basel Committee, 1999; Abdou & Pointon, 2009). The high ratings correlate with perceived improvements in profitability, ROA trends, and sustainability.

Literature supports that rigorous assessment reduces default probability and enhances asset quality (Cole et al., 2005; Ralston & Wright, 2003). In FTB, effective assessment likely aided the bank's ability to grow loans (Shs291bn to Shs356bn) while containing provisions for bad debts and achieving strong after-tax profit growth. This counters Ugandan trends of rising NPLs in

5.1.3 Credit Risk Control Practices on Financial Performance of weaker institutions, highlighting assessment as a key driver of performance.

FTB

The third objective determined the effect of credit risk control practices. Highest ratings went to robust loan monitoring/follow-up (M=4.2407), strict exposure limits (M=4.1852), and prompt action on early warnings (M=4.1111).

Control mechanisms address post-disbursement moral hazard through ongoing oversight (Milton, 2000; Comptroller Handbook, 2000). Strong control perceptions align with improved NPL management and financial sustainability.

This supports studies showing effective monitoring/restructuring reduces losses and boosts profitability (Holton, 2003; Serwadda, 2018). FTB's practices appear to have supported recovery (e.g., bad debts written off declined in 2024 vs. prior years), contributing to enhanced revenue growth and shareholder returns despite macroeconomic challenges.

Overall, the three credit risk management dimensions positively influence financial performance at FTB, consistent with the conceptual framework and moral hazard theory. High perceptual scores suggest effective implementation, correlating with actual 2024 improvements (profit after tax ~UGX 10.36 billion, up significantly).

5.2 Conclusion

From the research findings, according to the main and specific objectives, the results showed that credit policies were vital to financial performance analysis. Therefore, proper and well-designed credit policies should be well implemented while offering credit services to customers, thus improving the financial performance of the financial institutions.

5.4 Recommendations

Based on the research findings, credit policies boost improved financial performances; therefore, financial institutions have to put on better analysis measures to improve their credit risk management policies to reduce non-performing loans, thus improving financial performance.

Financial Institutions in Uganda and worldwide are still affected by credit risk; therefore, to achieve the desired sales revenue and profitability, the management of FTB should review and strengthen its credit mitigation factors related to credit limits, interest, the credit review committee, and collateral.

From the research findings. Credit risk control measures should upgrade the information systems capability to provide reliable data for action on deteriorating loans through benchmarking industry management information systems.

5.5 Limitations of the study

During the research study, some of the staff members were hesitant to share information due to fear of losing their jobs, while others had busy schedules and were unwilling to fill out the questionnaire in time.

Furthermore, financial constraints were also due to movements that were made while taking the questionnaire and picking it, which made the whole exercise costly.

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UGANDA CHRISTIAN UNIVERSITY

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APPENDIX

RESEARCH QUESTIONNAIRE

I am Nambuule Winnie Nkata, a student of Uganda Christian University conducting research on credit risk management and financial performance of financial institution in Uganda as requirement for the award of a Bachelors of Science in Accounting and Finance at Uganda Christian University, Mukono.

I am kindly requesting you to assist me in the study by answering the following questions. I assure you that your information will be treated with utmost confidentiality.

SECTION A: Demographic Data

Please tick (✓) the most appropriate box as the most agreed answer to the following statements.

1. Gender of the respondent.

   [ ] [ ]

   Male Female
2. Age group of the respondent
3. [ ] 25 [ ] 31 – 35 years [ ] 36 – 40 years [ ] 41 – 45 years [ ] 46 – 50 years [ ] Above 50 years
4. Current position in the bank [ ] Senior Manager [ ] Loan Pricing Officer [ ] Retail Credit Officer [ ] Other (specify): _____
5. Years of experience in banking/credit-related work [ ] 1 – 5 years [ ] 6 – 10 years [ ] 11 – 15 years [ ] Above 15 years

SECTION B:

Please indicate the extent to which you agree with the following statements regarding credit risk identification practices at Finance Trust Bank. (Use the scale: 1 = Strongly Disagree, 2 = Disagree, 3 = Not Sure, 4 = Agree, 5 = Strongly Agree)

No	Statement	1	2	3	4	5
1	The bank has clear policies to identify potential credit risks early.					
2	Regular scanning for insider lending and related-party risks is conducted.					

3	Macro-economic factors are routinely assessed before approving loans.					
4	Borrower credit history and collateral are thoroughly screened.					
5	Risk classification and prioritisation are done systematically.					

SECTION C: CREDIT RISK ASSESSMENT PRACTICES

No	Statement	1	2	3	4	5
1	Financial statements of borrowers are rigorously analysed.					
2	Credit scoring models and internal rating systems are used effectively.					
3	Industry trends and economic conditions are incorporated in credit risk assessments.					
4	Collateral valuation is updated regularly and independently.					
5	Stress testing of loan portfolios is conducted periodically.					

SECTION D: CREDIT RISK CONTROL PRACTICES

No	Statement	1	2	3	4	5
1	Loan monitoring and follow-up systems are robust and effective.					
2	Limits on single-borrower exposure and sector concentration risk are strictly enforced.					
3	Early warning signals of potential default are identified and acted upon promptly.					
4	Collateral and guarantees are enforced effectively when borrowers default.					
5	Regular review and restructuring/rehabilitation of problem loans is carried out.					

SECTION E: FINANCIAL PERFORMANCE OF FINANCE TRUST BANK

Please indicate the extent to which you agree with the following statements regarding the financial performance of Finance Trust Bank in recent years.

No	Statement	1	2	3	4	5
1	Profitability of the bank has improved significantly in the last three years.					
2	Revenue growth from lending and other core activities has been strong.					
3	The level of non-performing loans has reduced noticeably.					
4	Return on assets (ROA) has shown a positive trend.					
5	Returns to shareholders/investors have increased.					
6	Overall, the financial sustainability and stability of the bank have strengthened.					

Thank you very much for your time and valuable contribution.

Nambuule Winnie Nkata

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