EFFECTS OF CREDIT RISK MANAGEMENT ON MICRO FINANCE INSTITUTIONS LOAN PORTFOLIO PERFORMANCE IN MPIGI DISTRICT

BY

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FEBRUARY, 2014

DECLARATION

I Racheal Violet Kayongo, solemnly declare that the information presented in this dissertation is my original work as a result of an independent investigation.

Signed ……………………………. Date……………….....................

APPROVAL

We certify that this dissertation satisfies the partial fulfilment of the requirements for the award of the degree of Master in Management Studies of the Uganda Management Institute.

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Sign..

Supervisor

Date..

2. Mr. Mugambe Paddy

Sign...

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DEDICATION

This work is dedicated to God Almighty, the one who has provided life and health to enable me complete this work.

Further, I dedicate this work to my parents Mr and Mrs Kayongo and to my sisters Olivia, Christine, Victoria and Juliet and my brothers Ronald and Charles who have been an immense source of inspiration and motivation to bring this work to a completion.

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ABSTRACT

This study analysed the effect of credit risk management on the performance of loan portfolio in UGAFOD Micro Finance Ltd, Mpigi Branch. Specifically, the study reviewed the effect of credit risk assessment on loan portfolio performance, the effect of credit monitoring on loan portfolio performance and the effect of credit risk control on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch. The study used a cross – sectional research design on a sample of 360 respondents got from a total population of 11,750 clients. Data was collected by use of questionnaire, interview guide, focus group discussions and observation and it was analysed both quantitatively and qualitatively. The study findings revealed that credit risk assessment affects the performance of the loan portfolio as it reduces the chances of loss by the bank. Credit monitoring affects loan portfolio performance however, this has to be continuous, the bank does not need to wait to begin monitoring when the client develops signs of inability to repay. In credit risk management, credit risk control affects loan portfolio performance since; administering the credit facility ensures orderly and full payment which helps the clients to be able to fulfil their repayment requirements. The study concludes that there is need to find away to improve service delivery through lower interest rates, extended payback period and flexing of the strict credit risk management conditionality, product differentiation, customer segmentation and improved information technology for more people to access the institutions services for improved living standards. The study recommends that; banks need to strictly assess their clients to eliminate Non Performing Assets. Credit monitoring should be vigilantly implemented for better performance of the loan portfolio. Credit risk control needs to be fully implemented such that clients do not forfeit their obligations to the banks.

CHAPTER ONE

INTRODUCTION

1.1 Introduction

Microfinance refers to a wide variety of financial services that are usually provided to people belonging to the low-income group, especially women. The majority of the clients of Micro Finance Institutions (MFIs) have low income and limited access to financial services. For such low income people, microfinance loans provide low level monetary benefits that help them boost their financial lives. The diversity of microfinance products implies that the financial needs of most individuals belonging to the low income group keeps on changing according to the financial lives.

From a historical point of view, internationally micro credit was initially promoted as a means of nurturing the entrepreneurial spirit of the poor to increase income generation opportunities. It turns out that the poor utilize micro loans in many other ways. For example, they utilize microcredit for business activity and to start new businesses for investment micro entrepreneurs. MFIs have evolved from mere self- help saving groups to well established institutions taking a semblance of the phenomenal world wide as Chaudhury (2002:16) points out:

Microfinance has evolved from the slow moving tortoise of the1990s to the nimble hare of the early “nineties” (Chaughury, 2002) and since then, into an over charged bull growing at 70-100% per annum in some markets. With the growth of loan portfolios of MFIs in Uganda, a number of services at micro-level involving deposit taking and loans insurances, among others have been rolled out. The Ugandan microfinance sector consists of a large number of competing

institutions of varying formality, commercial orientation, and professionalism. These range from multipurpose NGOs, cooperatives (SACCOs) and informal organizations; more formal commercially- oriented Microfinance Institutions; and increasingly, a number of registered lending institutions, which have identified a new market in urban microfinance.

However, the growth of the industry has inevitably led to a number of challenges. The large number of MFIs means that available human resources are spread thin and capacity building is a priority. Microfinance is concentrated in urban areas, although three quarters of Ugandans are rural; expansion into rural areas will mean that existing MFIs will need new products, delivery systems, and business models. These are taken over by the challenge of credit extension.

The study analyzed the impact of credit risk management on the borrowers, their enterprises and the lending microfinance institutions in Mpigi district. This chapter presents the background to the study, statement of the problem, purpose of the study, objectives of the study, research questions, hypotheses of the study, conceptual frame work, significance of the study, justification and operational definition of terms and concepts.

1.2 Background to the study

This study is an analysis of the effect of credit risk management on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch. In general terms, credit risk is the risk of loss due to a debtor's non-payment of a loan or other line of credit either the principal or interest coupon or both (Bonnevie, 2009). Credit risk arises from the potential that an obligor is either unwilling to perform on an obligation or its ability to perform such obligation is impaired resulting in

economic loss to the lending institution. Lending is the principal business activity for most a registered lending institutions. The loan portfolio performance is typically the largest asset and the predominant source of revenue. As such, it is one of the greatest sources of risk to a lending institution's safety and soundness. Whether due to lax credit standards, poor portfolio risk management, or weakness in the economy, loan portfolio performance problems have historically been the major cause of lending institution losses and failures (Cornett, 2009). The study looks at how the lending institution carries out credit risk management focussing on credit risk assessment, credit monitoring and credit risk control to maintain financial soundness.

1.2.1 Historical perspective

Historically, economic factors and the current economic and technological trends have greatly influenced the development of the micro finance systems and the micro small and medium enterprises. Micro finance interventions started to take root in the early 1980's mostly in Asia and Latin America and were replicated in Uganda. Best practice based microfinance in Uganda got a foot hold from the early 1990's. However, the growth of the micro finance industry in Uganda has come up with a number of challenges and most pronounced is credit risk management. This is a scenario where a client is having a number of loans servicing at one particular time.

The State of the Micro finance Sector Report, 2008 in Uganda estimates the extent of credit risk management as prevalent in 10% to 20% of MFI clients. However, actual incidence may be much higher, especially in mature markets or in markets where there are many MFIs competing for clients in the same area, such as the rural areas. Clients borrowing from different types of lenders to meet their diverse needs have created some concerns. This problem is complicated by

the limited capacity of MFIs to limit loan use to ‘productive’ purposes. Clients often use multiple loans for “non-productive” purposes, such as meeting emergency expenses which are often not budgeted for. Apparently, there are a number of MFIs in Uganda and the number continues to grow every year with mushrooming self- help organizations transforming into MFIs.

Brown (2008) reported that credit risk management is not a new thing; it is much older than writing. Hammurabi’s Code, which codified legal thinking from 4,000 years ago in Mesopotamia, did not outline the basic rules of borrowing and did not address concepts such as interest, collateral and default. These concepts appear to have been too well known to have required explanation. However, the Code did emphasise that failure to pay a debt is a crime that should be treated identically to theft and fraud. The Code also set some limits to penalties. For example, a defaulter could be seized by his creditors and sold into slavery. Similarly, the Bible records enslavement for debt without disapproval; for example, the story of Elisha and the widow’s oil concerns the threatened enslavement of two children because their father died without paying his debts (Brown, 2008).

Two men, Hermann Schulze-Delitzsch and Friedrich Wilhelm Raiffeisen (Credit Societies History Report: 1852-1864), were responsible for creating the first true credit unions in Germany in 1852 and 1864. During 1849, Raiffeisen founded a credit society in Flammersfeld, Germany, but it depended on the charity of wealthy men for its support. Raiffeisen remained committed to that concept until 1864, when he organized a new credit union along principles still fundamental today (Filene, 2010). The credit societies in Germany, and similar institutions founded by Luigi Luzzatti in Italy, were the forerunners of the large cooperative "lending institutions" that abound in Europe today. In 1871, credit union legislation was considered in Massachusetts. This attempt

and later efforts in the 19th century to start U.S. credit unions were not very successful. It was a Canadian who transplanted the credit union to the Western Hemisphere. In 1900, Alphonse Desjardins organized a credit union (caisse populaire) in Levis, Quebec. The reasons were the same as those in Germany 50 years before. People were poor, interest rates were financially crippling, and the credit union offered a way out.

That first Canadian credit union was small by modern standards. The first savings deposit was only 10 cents; the first collection from all the members totaled only $26. Even today, in some countries, credit unions start small. But Desjardins persevered and devoted a good part of his life to credit union development in North America. He founded other credit unions, including the first one in the United States, in 1909 in New Hampshire (Credit Societies History Report: 1852-1864).

The Grameen Lending institution -Bengali is a Nobel Peace Prize winning microfinance organization and community development lending institution started in Bangladesh that makes small loans (known as microcredit or "grameencredit") to the impoverished without requiring collateral. The name Grameen is derived from the word *gram* which means "rural" or "village" in the Bengali language. The system of this lending institution is based on the idea that the poor have skills that are under-utilized. A group-based credit approach is applied which utilizes the peer-pressure within the group to ensure the borrowers follow through and use caution in conducting their financial affairs with strict discipline, ensuring repayment eventually and allowing the borrowers to develop good credit standing. The lending institution also accepts deposits, provides other services, and runs several development-oriented businesses including

fabric, telephone and energy companies. Another distinctive feature of the lending institution's credit program is that the overwhelming majority (98%) of its borrowers are women.

The Lending institution today continues to expand across the nation and still provides small loans to the rural poor. By 2006, Grameen Lending institution branches numbered over 2,100. Its success has inspired similar projects in more than 40 countries around the world and has made World Lending institution to take an initiative to finance Grameen-type schemes. Grameen believes that charity is not an answer to poverty. It only helps poverty to continue as it creates dependency and takes away individual's initiative to break through the cycle of poverty, whereas loans offer people the opportunity to take initiatives in business or agriculture, providing earnings and enabling them to pay off the debt (Credit Societies History Report, 2009).

Grameen regards all human beings, including the poorest, as endowed with endless potential, and that unleashing the creativity in each individual should be the answer to poverty. Grameen has offered credit to many poor, women, illiterate and unemployed people. It created access to credit on reasonable terms such as the group lending system and weekly-installment payment with reasonably long term of loans, enabling the poor to build on their existing skill to earn a better income in each cycle of loans. Grameen’s objective has been to promote financial independence among the poor. It targets the poorest of the poor, with a particular emphasis on women, who receive 95 percent of the lending institution’s loans. Women represent a suitable clientele because, given that they have less access to alternatives, such as traditional credit lines and incomes, they are more likely to be credit constrained and they have an inequitable share of power in household decision making (Credit Societies History Report, 2009.

In Uganda, the Central Lending institution for effective credit management introduced the Credit Reference Bureau (CRB) Services through Compuscan Ltd. This is a legal entity established as a company that allows financial institutions to exchange information on their clients 'repayment history and debt profiles and which compiles a database that collects, stores, consolidates and processes information related to persons, companies and enterprises. According to Mutebile (2008), the Participating Institutions (PI's) were to submit both positive and negative information on a customer credit profile to the CRB. The CRB would create a comprehensive credit report, which would be available for use by PI's to support their lending function and risk management functions. In the absence of a National Identification System, it was also deemed necessary for the CRB provider to develop a Financial Card System (FCS) to uniquely identify borrowers using a biometric system.

1.2.2 Theoretical perspective

Theoretically, this study focused on the linkages between access to credit, savings and insurance services and household food security that has a reciprocating effect on the performance of UGAFOD Micro Finance Ltd. The study was based on the prosperity theory that explains the client behaviour that leads to credit risk management through widely applicable theories on behavioural finance 'Prospect Theory'. To achieve the objectives, the research is designed to explain the theory and then inference of the theory is drawn to understand the underlying causes prompting the risk seeking behaviour of the person that result into the situation of credit risk management. This theory was used by Tversky and Hahnemann (1992) and has provided one of the most influential accounts of how people make decisions under risk and these decisions affect loan portfolio performance. It is argued that managers whose firms experience performance declines evoke a loss context and seek out riskier alternatives, while those who experience

improved performance evoke a gain context and choose less risky alternatives (Gooding et al., 1996, p. 332). This can explain the phenomenon of credit risk management in Uganda's MFIs.

Risk management is a concept that has attracted the attention of many theorists. However, the theory that underpins this study is the risk management theory by Niu (2008). The theory points out that risk of credit industry consists of two major categories: credit risk and systemic risk. The credit risk in general is an estimate of the probability that a borrower will not repay all or a portion of a loan on time. Systemic risk is often used to describe the risk of a sudden, unexpected event that would harm the financial system to an extent that economy may suffer. Accordingly, the assessment of credit risk can be done in two stages in most cases: 1) loan application and underwriting, and 2) during the course of the loan payment. In the first case, the lender can only assess the credit risk by studying the borrower's credit history, while in the second case, the lender can not only continue to examine the credit history, but also monitor the current payment behaviour to better assess the credit risk. Commonly, lenders refer to the first stage as underwriting risk management, and the second stage as the portfolio risk management. Both credit risk and systemic risk are also tightly related to the regulatory environment. This theory shows how risks can be managed by lending institutions.

Credit worthiness of the borrower concerns integrity, moral character, management ability and debt repayment capacity of the customer while structuring the credits with the set policy guidelines focuses on quality and quantity of assets that can be pledged as collateral and quickly liquidated in the event of default, Inter-American Development Lending institution (2007). For

credit monitoring this involves among others, frequent contact with borrowers, observing the flow of the borrower's business through the lending institution's account; updating the borrower's credit files and periodically reviewing the borrower's rating assigned at the time the credit was granted, (Richard et, al 2008). With credit risk control, this is part of the overall credit extension process and follows the quantification and planning of credit risks, aiming to reduce credit risks to a level which, according to the stipulations from credit risk strategy is manageable for the lending institution; it is handled by portfolio management, ONB Report (2008).

1.2.3 Conceptual perspective

The concepts of the study are credit risk management and the performance of loan portfolio. Concerning credit risk management, this is the support, control systems, procedures, policies, principles and practices necessary to manage the outstanding risk in assets (advances/loans) repayment and to monitor business risks properly (Greuning et al,2009). Credit extension involves credit risk assessment, credit monitoring and credit risk control. Regarding Credit assessment, this focuses on assessing the credit worthiness of a prospective borrower and structuring the credits with the set policy guide lines.

This study focused on the concept of credit risk management and its influence on the performance of UGAFOD Micro Finance Ltd in Uganda. Micro-finance is not one of the tools for poverty alleviation as pointed out in one of the policy debates (for example the Micro-Credit Summit in February 1997 in Washington, D.C). Improved access to credit is seen as a potent means for increasing the poor's income. Credit risk management as a concept has a number of inter related concepts that affect it which include desire to strengthen the saving culture, guarantee life insurance, ensure food security and fighting poverty. This study seeks to assess

the role of microfinance for income and consumption smoothing by the poor and its reciprocating effect on the performance of UGAFOD Micro Finance Ltd.

UGAFOD Micro Finance Ltd Mpigi branch, serves the wide rural expanse including the whole of neighbouring Butambala and Gomba districts. The branch is composed of two departments namely; General Lending institutioning and the Loans departments. The branch when granting credit follows the UGAFOD Micro Finance Ltd Credit Policy. This policy provides the frame work for the entire credit management process and sets objective standards and parameters that guide the branch credit officers in granting credit and management of loan portfolio. In short, the practice of the credit officers before granting the credit facility to the loan applicant is that they first make credit risk assessment of the client, do credit documentation of the transaction, and the credit is advanced, after advancement of the credit they do credit monitoring.

1.2.4 Contextual perspective

This focused on the issue of credit risk management, relating it to the strategic behaviour of competing MFIs. It analyzed how credit risk management can affect borrowers and how this, in turn affects the MFIs portfolio performance. Technically, allowing borrowers to take out more than one loan is equivalent to assuming that MFIs cannot share information about the borrowers they are serving, and the borrowers do want to take multiple loans. The phenomena of credit risk management in microfinance clients are widely prevalent so much so that it has become a major cause of concern and challenge for the micro finance industry in Uganda.

UGAFOD Micro Finance Ltd was created as a finance institution to serve the economically disadvantaged people especially in rural areas and contribute to the overall economic development of the country. This has meant that this licensed and registered lending institution

has always focused on the provision of microfinance. This has been and will remain the focus of the MFI. However, to reduce business risk UGAFOD Micro Finance Institution has diversified her activities to include lending to small and medium enterprises and large corporations to reach the middle and higher-end markets in order to provide services to sectors that are complementary to our target market and customers, an aspect of credit extension by customers.

Concerning performance of the loan portfolio, this refers to the ratio of non performing advances/loans to the total loan portfolio performance of a registered lending institution. Total loan portfolio performance is a collection of all the lending institution's loans and advances. A non performing credit facility does not generate income and shall include substandard, doubtful and loss categories, Financial Institutions Regulations (2005). Greuning et al (2009) noted that the principal balance outstanding, rather than delinquent loan payments, is used to identify a non performing loan portfolio. This is because there is a high likelihood of default of the entire loan balance when one amortisation payment is missed. The non performing loan portfolio performances an indication of the quality of the total portfolio and ultimately that of the lending institution's lending decisions. The standard international measure of portfolio quality in lending institutioning is Portfolio at Risk (PAR) beyond a specified number of days:

$$PAR(x\ days) = \frac{\text{Outstanding principal balance of all loans past due more than x days}}{\text{Outstanding principal balance of all loans}} X\ 100$$

The number of days(x) used for this measurement varies. In micro finance, 30 days is a common breakeven point, while for Small medium enterprises and corporate loans 90 days are used. If the repayment schedule is other than monthly, then one repayment period (week, fortnight and quarter) could be used as an alternative. The higher the ratio, the lower is the quality of loan portfolio, and vice-versa. The international Portfolio at Risk standard is 5%. The level of

portfolio performance can be assessed by analyzing the Non Performing Asset Ratio, Loan loss provisions and Portfolio at Risk ratio.

1.3 Statement of the Problem

There is a general consensus between financial institutions managers and lending institution scholars that effective credit risk management is a prerequisite for effective loan portfolio performance (Jayamaha and Mula, 2011). This is the reason why credit risk management is emphasised in most financial institutions, of course, UGAFOD Micro Finance Ltd, Mpigi Branch not being exception. Credit risk management is done with an effort of improving loan portfolio performance in terms of reducing nonperforming assets, provision for loan losses in UGAFOD Micro Finance Institution balance sheet and minimizing the risk of loan default.

Despite such efforts the ratio of nonperforming loans to the total branch portfolio has been increasing year after year and the branch has not been able to achieve its set annual targets of the Non-performing Assets Ratio during the period under review that is 2008-2011 (UGAFOD Micro Finance Ltd, Mpigi Branch – Loan portfolio performance analysis and Performance Management Reports 2008-2011). Quarterly reports (2011) on loan performance indicate that over thirty loans were written off at the branch. UGAFOD Micro Finance Institution faces problems in recovering the loans issued to its borrowers. There are cases of accounts being abandoned because of loan attachment. The increase in provisions for bad loans and increasing non performing asset ratio threatens the soundness of branch. Therefore, it’s against this background that the researcher investigated the credit risk management practices at UGAFOD Micro Finance Ltd, Mpigi Branch to establish their effect on performance of loans.

1.4 Purpose of the study

The purpose of the study was to analyse the effect of credit risk management on MFIs loan portfolio performance in Mpigi district using UGAFOD Micro Finance Ltd, as a case.

1.5 Objectives of the Study

The study was guided by the following specific objectives;

(i) Examine the effect of credit risk assessment on loan portfolio performance in micro finance institutions.

(ii) Assess the effect of credit monitoring on loan portfolio performance in micro finance institutions.

(iii) Establish the effect of credit risk control on loan portfolio performance in microfinance institutions.

1.6 Research Questions

i. What is the effect of credit risk assessment on loan portfolio performance in micro finance institutions?

ii. What is the effect of credit monitoring on loan portfolio performance in micro finance institutions?

iii. What is the effect of credit risk control on loan portfolio performance in micro finance institutions?

1.7 Research hypotheses

i) The study was analysed along the following research hypotheses

ii) Credit risk assessment affects the performance of the loan portfolio performance in microfinance institutions.

iii) Credit monitoring affects the performance of the loan portfolio performance in microfinance institutions.

iv) Credit risk control affects the performance of the loan portfolio performance in micro finance institutions.

1.7 Scope of the Study

Consideration was focused on geographical, content and time with respect to the conducting of the study.

1.7.1 Geographical Scope

The study was carried out on UGAFOD Micro Finance Ltd, Mpigi Branch. The branch is composed of two departments namely: Retail Lending institutioning and Corporate Lending institutioning departments, all extending credit to the qualifying customers.

1.7.2 Content Scope

Broadly, this study was focused on analyzing the effect of credit extension on loan portfolio performance in UGAFOD Micro Finance Ltd-Mpigi branch. Particular emphasis was on credit risk assessment, credit monitoring and credit risk control on the loan portfolio performance and how they affect the performance of loans at UGAFOD Micro Finance Ltd, Mpigi Branch.

1.7.3 Time Scope

For the time scope, the study covered the years from 2008 to 2011. It is within these years that lending institution's loan portfolio performance increased after the introduction of SME/Commercial /corporate lending and other loan products like the Salary Loans, school fees Loans, Animal Traction Loans, DANIDA Investment Loans, Veterinary Loans and Home Improvement Loans (UGAFOD Report, 2011).

1.7 Significance of the study

The findings of the study are expected to be very useful to financial institutions when they are managing credit risk. The recommendations of the study will also be used by financial institutions to improve their credit extension tools/elements.

The findings of this study was used by financial institutions to reduce non performing loans and this will lead to low loan provisions, decline in loan losses and increased profitability.

The findings of the study will be useful for further research especially for those researchers carrying out studies on credit extension and non performing loans of financial institutions.

1.8 Justification of the study

MFIs have fallen in a trap of credit risk management leading to a problem of repayment crisis. This study examined the regulation procedures that govern the operations of the MFIs to improve their performance. The timing of this study is appropriate because the regulations governing Micro lending in MFIs is undergoing a process of streamlining operational procedures to promote the value for money principle. The study was meant to streamline the whole process,

multiple lending and borrowing of clients. This is the time when the Micro finance industry is facing a number of challenges and a number of MFIs are closing shops. Therefore the study will contribute to improved performance in the micro finance industry through introduction of measures to make the system compliant with internationally agreed norms for efficiency, transparency and accountability and through creation of professionals in the sector.

1.9 Conceptual Framework

The conceptual framework presents the relationship between credit risk management and loan portfolio performance.

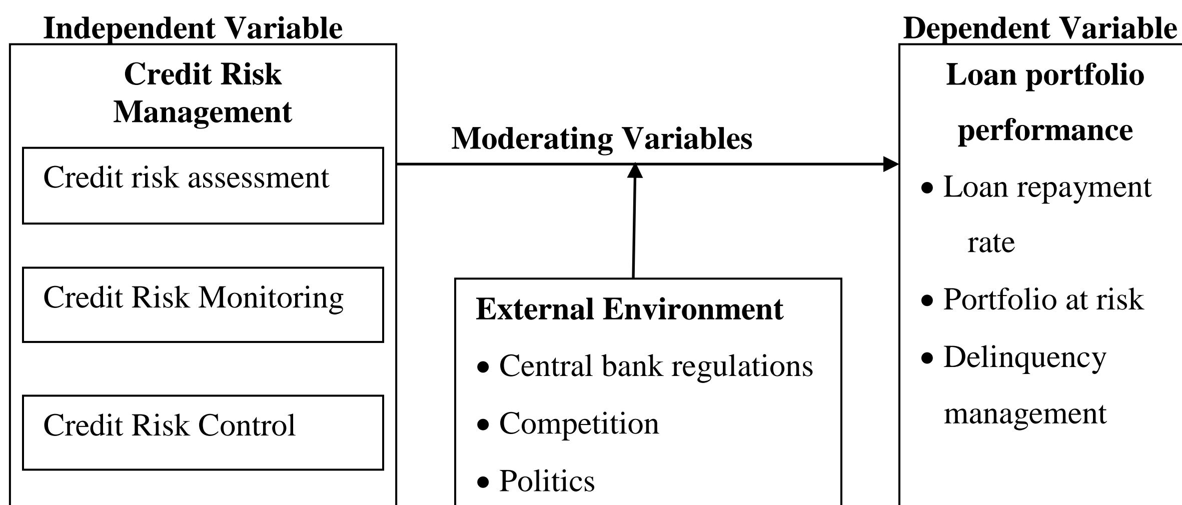

Figure I.1: Conceptual Framework showing the Relationship between credit risk management and Loan Portfolio Performance

Source: (Based on Risk Management Theory by Niu (2000) and adapted by Researcher, (2011).

In the conceptual framework, the independent variable is credit risk management while the dependent variable is loan portfolio performance. The moderating variables are: central lending

institution regulations, competition and politics. Accordingly credit risk management includes credit assessment, credit monitoring and credit control all that aim at proper loan portfolio performance, hence leading to loan repayment, proper use of the borrowed money and reduced cost of debt collection such that UGAFOD Micro Finance Institution is able to make profit and maintain liquidity.

This conceptual framework is derived from the risk management theory by Niu (2008). According to this theory, risks of credit industry consist of two major categories: credit risk and systemic risk. The credit risk in general is an estimate of the probability that a borrower will not repay all or a portion of a loan on time. Systemic risk is often used to describe the risk of a sudden, unexpected event that would harm the financial system to an extent that economy may suffer. The assessment of credit risk can be done in two stages in most cases: 1) loan application and underwriting, and 2) during the course of the loan payment. In the first case, the lender can only assess the credit risk by studying the borrower's credit history, while in the second case, the lender can not only continue to examine the credit history, but also monitor the current payment behaviour to better assess the credit risk.

Commonly, lenders refer to the first stage as underwriting risk management, and the second stage as the portfolio risk management. Both credit risk and systemic risk are also tightly related to the regulatory environment. This theory points out that there is need for assessment of the borrower at the borrowing time and through the payment process and this guided the study in establishing how it was done at UGAFOD Micro Finance Ltd, Mpigi branch and how it affected the loan portfolio performance.

1.10 Definition of terms

Credit risk

This refers to the risk that a borrower will default on any type of debt by failing to make payments obligated to do (Basel Committee on Lending institutioning, 1999).

Credit risk management

Concerning credit extension refers to the support, control systems, procedures, policies, principles and practices necessary to manage the outstanding risk in assets (advances/loans) repayment and to monitor business risks properly (Greuning et al, 2009).

Performance of the loan portfolio

This refers to the ratio of non performing advances/loans to the total loan portfolio performance of a registered lending institution (Financial Institutions Regulations, 2005).

Credit risk assessment

This is the process of analysing customer credit quality to facilitate loan approvals and ongoing credit compliance within the commercial lending book which helps UGAFOD Micro Finance Institution make better lending decisions (SunGard, 2012).

Credit monitoring

This is the keeping track of borrowers' compliance with credit terms, identifying early signs of irregularity, conducting periodic valuation of collateral and monitoring timely repayments (Boateng, 2008).

Credit risk control

This is the process of administering the credit facility to ensure orderly and full payment, monitoring of the credit facilities as well as the workout strategies in situations when credits actually deteriorate (McNaughton, 1996).

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter covers the theoretical review and then the review of the literature on the effect of credit risk assessment on loan portfolio performance, credit monitoring on loan portfolios performance and credit risk control on loan portfolios performance a registered lending institutions.

2.2 Theoretical Review

This has been organized in light of the study objectives that guided the study.

2.2.1 The effect of Credit Risk Assessment on Loan portfolio performance

Uganda's financial sector regulatory framework and reforms helps in credit extension. The Financial Institutions Act (FIA) 2008 governs the regulation and supervision of financial institutions (lending institutions and credit institutions). The regulatory framework for financial institutions is underpinned by 9 implementing regulations for Licensing, Capital Adequacy Requirements, Credit Classification and Provisioning, Limits on Credit Concentration and Large Exposures, Insider - Lending Limits, Liquidity, Corporate Governance, Ownership and Control and Credit Reference Bureaus gazetted in 2005. The credit policy demand prudential standards. That is rules that limit risk taking, intended to lower lending institution failures and are comprised of qualitative limits, provision of a buffer in case of need, re-enforcement of the incentives for the parent to manage and monitor the risk taken by UGAFOD Micro Finance

Institution (Egesa, 2008). In this literature review, it is indicted that lending institutioning institutions should limit risk. This helped in investigating how UGAFOD Micro Finance Institution toils to limit risk ensuring that a customer is in position to repay the loan.

Kabir et al (2010) reiterate that risk is inherent in all aspects of a commercial operation and so for lending institutions and financial institutions, credit risk is an essential factor that needs to be managed. This thus calls for credit risk assessment to; minimise bad loans by improving the risk/return profiles of the portfolio, price credit risk adequately or risk based pricing, maximise benefits from potential credit opportunities, setting of concentration and exposure limits, active portfolio management, adhere to credit policies and maintain a reliable database. Day (2006) emphasises that a lending institution should adopt and document a sound loan loss methodology, which addresses credit risk assessment policies, procedures and controls for assessing credit risk, identifying problem loans and determining loan provisions in a timely manner. In here, it is indicated that there is need for the credit risk assessment methodology. The study was thus attracted to establishing the credit risk assessment methodology of UGAFOD Micro Finance Institution and how it improves loans performance.

Kalimba (2005) explains that in credit risk assessment, there is credit investigation. The investigation has to look at borrowers; managerial aspect, that is; sincerity, honesty, integrity, educational background, experience of the borrower and ability of the management to run the project efficiently. Organisational aspect, that is; under what type of organisation the activities was undertaken. Whether it is sole proprietorship or partnership, private limited or public limited company; technical aspect: location of the business, land and building, machineries equipment,

requirements to be used like power, fuel, water, materials etc. Marketing aspect: marketability of the product to be produced projected sales volume, scope of market expansion, possible threat of competition etc. Financial aspect: total requirement of fund for the business activities and how much was required as loan from the lending institution, borrowers contributions in the business, cash inflow and out flow statement, sales forecast, balance sheet, profit and loss account etc. Economic aspect: contribution to gross commercial product (GCP), creation of employment, indirect benefit of the society.

Namyalo (2007) argued that there is also need for Preparation of Credit Report. A credit report contains: name and address of the client, nature of the firm and date of establishment, nature of business, investment in the business, subsidiary, net sales, annual net income, market reputation and means of finance particulars of lending institution account particulars of owner. And then considering the factors of selection of the borrower that include Five Cs: Character, Capacity, Capital/ Credit worthiness, Condition (Economic) and Collateral. According to the above literature, it is indicated that in credit assessment, there is need for investigation, preparation of credit report and considering factors of selection of the borrower. The study thus looked at how the staff of UGAFOD Micro Finance Institution carefully carried out investigation, prepared credit reports and considered factors of selection of the borrower to enable better loans performance.

Roy (2005) holds the contention that in credit risk assessment, there is need for a Credit Risk Grading system (CRGS). This is a collective definition based on the pre-specified scale and reflects the underlying credit-risk for a given exposure. A Credit Risk Grading System deploys a

number/ alphabet/ symbol as a primary summary indicator of risks associated with a credit exposure. Credit Risk Grading is the basic module for developing a credit extension system. Credit risk grading is an important tool for credit extension as it helps the Financial Institutions to understand various dimensions of risk involved in different credit transactions. The aggregation of such grading across the borrowers, activities and the lines of business can provide better assessment of the quality of credit portfolio of a Financial Institution (FI). Credit grading helps the sanctioning authority to decide whether to lend or not to lend, what should be the lending price, what should be the appropriate credit facility and what are the various risk mitigation tools to put a cap on the risk level. This literature points out that lending institutioning institutions need to establish a Credit Risk Grading System (CRGS). Basing on this literature, the study analysed the credit grading system of UGAFOD Micro Finance Institution and how it led to performance of loans (Roy, 2005 and Namyalo, 2007).

2.2.2 The effect of Credit Monitoring on Loan portfolio performance

Boateng (2008) supported the argument that every lending institution has to develop and implement comprehensive procedures and Information Systems to follow up the condition of individual credits. Accordingly, after a credit facility is approved and draw down allowed, the facility should be continuously watched over. This is keeping track of borrowers' compliance with credit terms, identifying early signs of irregularity, conducting periodic valuation of collateral and monitoring timely repayments. To minimise credit losses, monitoring procedures and systems should be in place that provide an early indication of the deteriorating financial health of a borrower. At a minimum, systems should be in place to report the following exceptions to relevant executives: past due principal or interest payments and breach of facility

covenants, non-receipts of financial statements on a regular basis and any covenant breaches or exceptions made, action not taken on time for findings of any internal, external or regulator inspection/audit. From the above literature, it emerged that there was need or constant watching over the borrowers. This literature helped the study in analysing if UGAFOD Micro Finance Institution had an effective loans management monitoring system and how it helped the performance of loans.

Kakuru (2006) explains that for a business to financially benefit from credit sales there must be in existence of a well organised credit monitoring and recovery process to minimise cases of default due to business solvency. The procedures range from sending reminders/delinquency letters informing the clients of the past due status of their accounts, making telephone calls, sending foreclosures and also employing a debt collection agency. However, as much as the above have been cited, slow paying customers need to be handled cautiously to avoid collection errors (Schumidt, 2009). This literature pointed out the need for the existence of well organised credit monitoring and recovery systems to minimise cases of default. This is through sending delinquent letters, telephone calls, sending foreclosures and employing debt collection agencies. The study explored how Micro Finance Institutions used these methods to monitor its clients and how it reduced loan default.

Mwisho (2008), envisages that credit monitoring involves, among others, frequent contact with borrowers, creating an environment that Micro Finance Institutions can be seen as a solver of problems and trusted adviser; develop the culture of being supportive to borrowers whenever they are recognised to be in difficulties and are striving to deal with the situation; monitoring the flow of borrower's business through the lending institution's account; regular review of the

borrower's reports as well as an on-site visit; updating borrowers credit files and periodically reviewing the borrowers rating assigned at the time the credit was granted. Richard (2006) further explains that the borrowers' respective activities, their performance, as well as behaviour are closely monitored, by both branches and corporate division on daily basis to establish whether there are any changes that need to be taken care of to protect non-repayment of credits. The study analysed how Micro Finance Institutions kept in contact with the customers and presented itself as a problem solver, such that it could be trusted and how this encouraged repayment of loans.

Derban et al (2005) expounded that credit monitoring involves keeping track of obligor's principal and interest repayments, account activity, as well as instances of excesses over credit limits. Attention is paid to the obligor's willingness and ability to provide timely margin top-up. The obligor's ability to adhere to negative pledges and financial covenants stated in the loan agreement are assessed and breaches detected trigger prompt action. According to Mlabwa (2008), the value of collateral should be updated periodically to account for changes in market conditions. For example, where the collateral is property or shares, an institution should undertake more frequent valuations in adverse market conditions.

If the facility is backed by an inventory or goods purportedly on the obligor's premises, appropriate inspections should be conducted to verify the existence and valuation of the collateral. This literature revealed that there should be constant attention to the obligor's repayment rate, adherence to covenant and the condition of collateral. The study analysed the Credit monitoring system of Micro Finance Institution of the borrowers' respective activities, their performance, as well as behaviour and it enables paying of the loans.

2.2.3 The effect of Credit Risk Control on Loan portfolio performance

This involves measuring and containing individual credit risk within strategic guidelines. It involves the administration of the credit facility to ensure orderly and full payment, monitoring of the credit facilities as well as the workout strategies in situations when credits actually deteriorate (McNaughton, 1996). Credit risk control assesses the likelihood that the credit was paid, if the loan proposed by Micro Finance Institutions is adequate, the quality of the collateral held and the ability of the borrower's business to generate necessary cash. It also involves asset classification whereby an asset is assigned a credit risk grade that is determined by the likelihood that the debt was serviced and then liquidated according to the contract terms.

Lending institutions should classify assets at origination and then reviewed and reclassified as necessary according to the degree of risk. It should consider the loan service repayment, borrower's financial conditions economic trends etc (Greuning et al, 2009). According to this literature, credit risk control is implemented both before and after loan signature. Its objective is to avoid making unsound loans from the outset and, subsequent to disbursement, to ensure that the value of the lending institution's loans is preserved, leading to the complete and timely recovery of all outstanding amounts. The study considered how Micro Finance Institutions monitored the value of collateral updating it periodically to account for changes in the market conditions ensuring the recovery of loans.

Richard (2006) contends that credit risk control involves the management of the client's financial situation, covenants, collateral and payments as well as credit review. It focuses on ensuring that credit worthiness of the clients earlier established is maintained. Once a loan is on the books of the lending institution, it must be managed actively to ensure that it does not deteriorate and it is

repaid. Good loan management can rarely overcome poor judgment but many good credits become problem loans because lending officials did not heed to the warnings that arose over time. This literature shows that credit risk control involves management of the clients' financial situation. This helped the study in establishing how Micro Finance Institutions manage the financial situation of clients and its effects on loan portfolio performance.

Richard et al (2008) holds the view that lending institutions use credit limits, inspection and review, rescheduling and different recovery procedures in controlling credit risk. Credit limits involve setting clearly defined levels of authority for credit approval to ensure that credit decisions are prudent and made within defined parameters. Credit limits also prevent the financial institution from being vulnerable to non performance on a few large loans. Modern prudential regulations usually stipulate that a lending institution not make investments, grant large loans, or extend other credit facilities to any individual entity or related group of entities in excess of an amount prescribed percentage of the lending institution's capital reserves, (Greuning et al, 2009).

Inspection and review involves an effective internal credit review system that is coupled with regular analysis and re-rating of credits by credit officers. During inspection credit officers check compliance with the covenants in the loan agreement, cross check the status of the collateral and obtain asymmetric information from customers. An observation made by Cope (1994) is that the monitoring and recovery process is one, which is simple, but at the same time very difficult to successfully implement. Accordingly, this process involves constant reconciliation by UGAFOD Micro Finance Institution of the customers' mortgage loan account (monitoring service trends)

with project site visit reports and exhibited customer cooperation. The idea is to constantly remind the client of the fact that funds in his hands belongs to somebody else and must be repaid back within a stipulated time (Fratantoni and Schuh, 2009).

Further in relation to the above, the Monetary Authority of Singapore (2006), states that an institution should perform regular credit reviews. The purpose of a credit review is to verify that credits are granted in accordance with the institution's credit policies and to provide an independent judgement of asset quality. The institution should conduct credit reviews with updated information on the obligor's financial and business conditions, as well as the conduct of the account. Exceptions noted should be evaluated for impact on the obligor's creditworthiness. Credit reviews should also be conducted on a consolidated group basis to factor in the business connections among related entities in a borrowing group. In the above literature, it emerged that lending institutions have risk controls like credit limits, inspection and review. The study explored how UGAFOD Micro Finance Institution uses these controls and how they affect the performance of the loan portfolio.

In conclusion, the emerging gap was that whereas there are many credit extension measures, it was not clear if there was better performance of loan portfolio. The study thus analysed the effect of; credit risk assessment, credit monitoring and credit risk control on loan portfolio performance in UGAFOD Micro Finance Ltd. This helped in establishing the effect of credit extension on performance of the loan portfolio, and how the moderating variables come in to affect the relationship between these two variables.

2.3 Summary of the Literature Review

The effect of credit risk assessment on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

The review reveals that risk is inherent in all aspects of a commercial operation and so for lending institutions and financial institutions, credit risk is an essential factor that needs to be managed. This thus calls for credit risk assessment to; minimise bad loans by improving the risk/return profiles of the portfolio, price credit risk adequately or risk based pricing, maximise benefits from potential credit opportunities, setting of concentration and exposure limits, active portfolio management, adhere to credit policies and maintain a reliable database. Day (2006) emphasises that a lending institution should adopt and document a sound loan loss methodology, which addresses credit risk assessment policies, procedures and controls for assessing credit risk, identifying problem loans and determining loan provisions in a timely manner. In here, it is indicated that there is need for the credit risk assessment methodology. The study was thus attracted to establishing the credit risk assessment methodology of UGAFOD Micro Finance Institution and how it improves loans performance.

Effect of Credit Monitoring on Loan Portfolio Performance in UGAFOD Micro Finance

In general, the literature reveals that for a business to financially benefit from credit sales there must be an existence of a well- organised credit monitoring and recovery process to minimise cases of default due to business solvency. However, there is possibility of mismanagement of the credit risk management procedures. The procedures range from sending reminders/delinquency letters informing the clients of the past due status of their accounts, making telephone calls, sending foreclosures and also employing a debt collection agency. However, as much as the

above have been cited, slow paying customers need to be handled cautiously to avoid collection errors. This literature pointed out the need for the existence of well organised credit monitoring and recovery to minimise cases of default.

Effects of credit risk control on loan portfolio Performance in UGAFOD Micro Finance

Credit risk control involves the rescheduling of loans. Rescheduled loans refer to loans that have been restructured and re-negotiated between authorised institutions and borrowers because of either deterioration in the financial position of the borrower or the inability of the borrower to meet the original repayment schedule and for which the revised repayment terms, either of interest or the repayment period, are non-commercial to the authorised institutions. Rescheduling of loans takes place when there is reasonable assurance that the borrowers was able to service all future principal and interest payments on the loans in accordance with the revised repayment terms.

This literature importantly guided the study in investigating how rescheduling of loans reduced the credit risk. Lending institutions also need to set limits, including operational limits, for the different trading desks and/or traders which may trade different products, instruments and in different markets, such as different industries and regions. Limits need to be clearly understood, and any changes clearly communicated to all relevant parties. Risk Taking Units must have procedures that monitor activity to ensure that they remain within approved limits at all times (State Lending institution of Pakistan, 2010). The study basing on this literature tried to establish the procedures that monitor activity to ensure that they remain within approved limits at all times in order to control risk.

CHAPTER THREE

METHODOLOGY

3.1 Introduction

This chapter presents the methodology used to collect data, population, sample size and selection, data collection method and instruments, validity and reliability of the instrument and data analysis.

3.2 Research Design

This used a cross-sectional survey design because Litze (2007) asserts that the design utilises different groups of people who differ in the variable of interest, but share other characteristics such as socioeconomic status, educational background and ethnicity. For this study the population of interest met the conditions. Both qualitative and quantitative data were used for purposes of thorough analysis and exploring the effects credit extension components on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch.

3.3 Study Population

This comprised 11,750 loan clients and the 38 credit staff of the loans department of UGAFOD Micro Finance Institution including the supervisors and the manager. UGAFOD Micro Finance Ltd has twelve credit products and these include: Commercial loans, Corporate loans, Salary loans, Agricultural loans, education loans, Home Improvement loans, Micro Business loans, Veterinary Loans, Animal Traction loans, Lending institution Overdrafts, Letters of Credit, DANIDA Investment Loan and lease loans.

3.4 Sample Size and Selection

The study used a total sample of 360 respondents, picked from a total of 11,788 using the Cranjie and Morgan table, that is 322 loan clients and 38 credit staff of the loans department of UGAFOD Micro Finance Institution including the supervisors and the manager determined using purposive and simple random sampling. However, 122 clients were studied and all the 38 staff of the lending institution.

3.5 Sampling Techniques

Different sampling techniques were used according to the category. The sample was selected using random sampling for the customers and purposive sampling for the staff of the lending institution. According to Burns (2009), random sampling is used because it helps to select respondents who are easily accessible in the place of the study. And for convenience sampling, this is used because the presence of targeted respondents is not easy to pre – determine. These techniques were used because it was not possible to predetermine the presence of every respondent. The customers could not be located in their areas of jurisdiction but from the lending institution. Purposive sampling was used aiming at selecting typical and useful people that would give relevant data. Purposeful sampling selects information rich cases for in – depth study. Size and specific cases depend on the study purpose (Onen, 2005).

Table 3.1 below, therefore shows the population and sample size basing on Morgan and Krejcie (1970) table.

Table 3.1: Showing the Population and the Sample size

Category	Population	Sample size	Sampling method
Manager	1	1	Purposive
Credit Administrators/ Supervisors	3	3	Purposive
Credit / Loans Officers	34	34	purposive
Clients/ borrowers	11,750	322	Convenience and proximity
Total	**11788**	360	

Source of Data: (*UGAFOD Micro Finance Ltd, Mpigi Branch Staff Attendance Register and Loan clients register, 2011*).

3.6 Data Collection Methods and Instruments

The methods used in data collection included: asking questions, observing, review and recording of collected information. Four basic instruments were used to collect data and these included questionnaire, interview schedules, and observation and focus group discussions. In line with works of Uma (2008), because almost all data from multi methods have biases associated with them, collecting data from multiple sources lends rigor to research. It is therefore significant to gather data from several sources and through multiple collection methods for data acquisition from a cross section of identified beneficiaries of UGAFOD Micro Finance Ltd-Mpigi Branch.

3.6.1 Interview Guide

Interview guides were employed to collect primary qualitative data from the respondents. According to Kakooza (2008: 6) an interview is a conversation in which the researcher tries to get information from the interviewee and records it by him/herself. Interviews were employed because they are easily adaptable and effective since they encourage probing for deeper information on part of the researcher (Bell; 2010; 135-136). Questions were prepared and set in form of a schedule followed in the interview process. The interviews were held with the respondents identified as crucial in the provision of information and explanations to the topic

under study. The interview guide was designed for UGAFOD Micro Finance Institution staff. In-depth Interview guide was designed and administered to different key in formants. In-depth interviews were used because they facilitate face to face verbal responses which help to obtain reliable and valid information behind participants' experiences (Creswell, 2010).

3.6.2 The Questionnaire

A questionnaire was administered to the identified sample of beneficiaries. The questionnaire was used because of its ability to produce data which deals with the topic in depth and detail (Amin, 2010). Semi structured and self-administered questionnaires were used to collect qualitative data from the respondents. Kothari (2010; 124) argued that a questionnaire is advantageous because it is free from bias of the interviewer since answers are in the respondent's own words and large samples can be used and thus the results can be more valid and Reliable. In this study, closed ended and open-ended questions were used for easy coding and facilitation of data collection on a wide range of opinions because the respondents are free to write their mind without limitations.

3.6.3 Focus Group Discussions

This instrument aided the researcher to equally gather primary qualitative data. In this regard, the respondents were gathered on appointment of the researcher to discuss issues concerning credit extension and loan portfolio performance in UGAFOD Micro Finance Ltd. According to Smith (2010; 67), a focus group discussion enhances the attainment of deep information since it encourages free interaction and probing of the respondents on spot. It therefore aided the researcher in eliciting necessary information.

3.6.4 Observation Checklist

This involved observing staff of UGAFOD as they served customers and projects that were the focus of the borrowed funds. This helped to find out under what conditions success is most likely, what individual staff members and borrowers do when they encounter difficulty, how interaction with others affects their activities and concentration, and what the affected persons need to put right in the process. Observations were both informal and highly structured, and incidental or scheduled over different periods of time in different activity contexts. Observation checklists allowed to record information quickly about how respondents perform in relation to specific outcomes from the program of credit extension and loan portfolio performance. Observation checklists were written in a yes/no format and used to assist in observing respondents' performance relative to specific criteria. They were also directed toward observations of an individual or group. These tools also included spaces for brief comments, which provided additional information not captured in the checklist.

3.7 Data Quality Control

Data quality control ensures that data collected is reliable and valid. These techniques included the Likert scale, use of variety of research instruments, validity and reliability measures, classification, tabulation and editing.

3.7.1 Validity

To ensure validity of data a set of questions were designed to collect same information but using questions para-phrased differently. Content and convergent validity were strictly adhered to which ensured quality of the data. Content validity in the questionnaire was monitored using the Content Validity Index (CVI). On the other hand, the questionnaire was pilot-tested on 10 of the

selected members of the sample on 20 from the two customer groups- personal and corporate lending institutioning. The content validity index model was used in ascertaining the validity of instruments used. CVI= (n-N/2) (N/2). Where; n= number of respondents indicating essential, N= total number of respondents. The study targeted a content validity index of at least 0.5 as a basis of ironing out the randomness within the factors considered in the instruments. In this study, the resultant validity index was 0.79, almost 0.8, rendering credibility to the use of the study instruments.

3.7.2 Reliability

This measure was used to ensure that the data collected was to a given magnitude error free or without bias across time and across various items in the instrument which made the data stable, consistent and therefore reliable. Here the Test-Retest reliability and inter item consistency reliability were employed hence data quality was controlled. Reliability on the study instruments was maintained using the Cronbach Coefficient. The Cronbach Score above 0.5 was considered effective, lending credence to rely on and use the study instruments. In this study, the Cronbach score was 0.77, and given that this was above 0.5, rendered reliability on the instruments used and the data collected and analyzed.

3.8 Data Processing and Analysis

The collected data was analysed depending on the nature of the data. For qualitative data, it was sorted by checking for any errors and analysed as postulated in the research objectives. Patterns and connections within and between categories were identified. It was interpreted by composing explanations and substantiating them using the respondents open responses. While analysing qualitative data, conclusions were made on how different themes/variables are related.

Quantitative data was processed and analysed using three processes; editing, coding and tabulation. It was entered and analysed using a Statistical Package for Social Scientists 13.0 (SPSS) program. Hypotheses were analysed with Pearson's correlation coefficient index using the computer. The index measures the degree and direction of the relationship between two variables X and Y; that is, the effect of credit extension on performance of loan portfolio performance in UGAFOD Micro Finance Ltd. For descriptive data, analysis involved use of frequency tables according to the variables under study.

Cross data validation was done to establish the relationship between the independent variable credit risk management and the dependent variable loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch. Thus, both quantitative and qualitative data was edited first and coded before analysis was done. Thereafter, data was summarized in form of tables, diagrams and other statistical forms suitable for presentation of findings. For qualitative data, authorities in research were contacted and helped in polishing the subject matter before conclusion, and recommendation for the way forward. Regression analysis was used to obtain results on how credit risk management has impacted on portfolio performance in UGAFOD Micro Finance Ltd. The relationship was generated using the linear regression model. Bajwa, *et al*., (2004) used the linear regression model to compare the different procedures for credit control in the Central Lending institution of Thailand. In this study,the multi-linear model was used to study the relationship between the dependent and independent variables. The model is estimated by:

$$Y = \beta_0 + \beta_1 X_1 + \ldots \beta_n X_n + e$$

Where; **Y** = independent variable (credit extension)

β_0 = Constant

β_1 = Coefficient

X_1 = Credit Risk Assessment

X_2 = Credit Monitoring

X_3 = Effect of credit risk control

e = independent error terms

Therefore: Credit risk management = **k** (Credit risk assessment + credit monitoring+ control effect).

3.9 Constraints

A number of constraints were encountered during the study. There were delays in return of the questionnaires but this was managed by making frequent telephone call reminders to the respondents and building a good rapport with the respondents. Some interview appointments were rescheduled according to the commitments of the respondents. Persistence and patience of the researcher was important to secure successful interviews from the respondents.

3.10 Ethical Considerations

The researcher secured a letter of introduction from Uganda Management Institute to proceed with the study after the proposal had been approved. Permission was sought from the Managing Director UGAFOD Micro Finance Ltd who gave the researcher permission to conduct the study in the lending institution. Anonymity was observed as not all the respondents wanted their names taken. The researcher observed extreme confidentiality while handling the responses. Information was availed to the respondents that the research would not endanger them directly or indirectly and that participation was voluntary.

CHAPTER FOUR

DATA PRESENTATION, INTERPRETATION AND ANALYSIS OF RESULTS

4.1 Introduction

This chapter is the presentation and analysis of the field findings of this study. The study focused on analysing the effect of credit extension on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch. The focus of the study was on the effect of credit risk assessment, credit monitoring and credit risk control on loan portfolio performance in UGAFOD Micro Finance Ltd.

4.2 Background Characteristics of the Respondents

The sample characteristics were analyzed taking three key consideration; the sex, age and education qualification. These are each presented and discussed below in turn. These were used to provide support for the responses from the identified respondents.

4.2.1 Gender Distribution of the Respondents

The study looked at the gender distribution of the respondents. This was looked at with the purpose of balancing the male and female respondents included in the study such that views representing both categories are obtained as this would help avoid biases of one gender. On top that women are universally accepted to hold different attitudes towards risk taking and management from men. Women are believed to higher standards of ethical behaviour and may be more concerned with the common good than men (Rivas, 2008). Therefore by including both male and females this was hoped to provide balanced views on credit extension at the lending institution. The statistics are in the Table 4.1.

Table 4.1: Gender of the respondents for different attitudes in the study

	Frequency	Percent
Male	138	52.2
Female	222	47.8
Total	360	100.0

Source: Primary Data

Table 4.1 above shows that there was an almost an equal number of the respondents number that is 52.2% male respondents and 47.8% females respondents. Though the males were slightly more than the females, the results indicate that both males and females equally participated in the study because the difference margin between those who participated was small at 4.4%. Therefore the views obtained by the study represent attitudes of both male and female staff and clients of the lending institution.

4.2.2 Education Level of the Respondents

The study then looked at the level of education of the respondents. This was aimed at establishing the accurateness of the responses as more highly learned people are likely to provide accurate information on most issues. Data was collected and is presented in Table 4.2 below:

Table 4.2: Education Levels of the respondents

Education Level	Frequency	Percent
Post graduate	40	5.6
Bachelors Degree	86	29.4
Diploma	55	20.8
Certificate	59	21.9
Secondary education	64	12.2
Primary education	56	10.0
Total	360	100.0

Source: Primary data

According to Table 4.2, those holding postgraduate qualifications were 5.6%, the higher number of respondents was of those with bachelors' degrees 29.4%, 20.8% held diplomas, 21.9% held certificates and 10.0% were holders' of primary education. The results indicate that the majority of the respondents had sufficient education with the majority of the respondents with diploma and above qualifications to enable them understand the credit extension. Their level of understanding and analysing credit risk assessment, credit monitoring and credit risk control by UGAFOD Micro Finance Institution was deemed high.

4.2.3 Role of the Respondent with the Lending institution

The study then looked at the role of the respondent in the operations of the lending institution. This aimed at establishing if the respondent was in position to understand the operations of UGAFOD Micro Finance Institution in credit risk management. The role of the respondent in the lending institution is summarised in table 4.3 below.

Table 4.3: Role of the Respondent with the Lending institution

Role with UGAFOD Micro Finance Institution	Frequency	Percent
Manager	1	.3
Credit administrators	3	.8
Credit officers	34	9.4
Client	322	89.4
Total	360	100.0

Source: Primary data

Table 4.3 shows that the majority of the respondents 89.4% were the clients and the remaining 10.6% were staff of the lending institution. However, to note is that the 10.6% respondents were all the staff of UGAFOD Micro Finance Institution involved in credit extension as these were all staff of the loans section. Then the clients these were people had loans with the lending

institution. This means that the staff would give accurate information about credit extension since they were in charge of credit risk control, while the clients would also give some necessary information because as borrowers, some of the credit extension measures had been applied on them.

4.2.4 The number of Years the Respondent had been involved in Working or Dealing with the Lending institution

This was looked at by asking the respondents to indicate the number of years they had spent working or dealing with the lending institution. This aimed at establishing if they had stayed with UGAFOD Micro Finance Institution for sufficient time, enough to understand the credit extension of UGAFOD Micro Finance Institution since it is universally presumed that the longer the time one spends with an institution means the higher the opportunities of knowing about its internal dynamics since one will have experienced some of its core practices. The statistics are presented in Table 4.4.

Table 4.4: Number of involved in Working or Dealing with the Lending institution

Number of Years with UGAFOD Micro Finance Institution	Frequency	Percent
1-5 years	90	25.0
6-10 years	181	50.3
11 years and above	89	24.7
Total	**360**	**100.0**

Source: Primary data

Table 4.4 indicates that the majority of the respondents 50.3% had been working or dealing with UGAFOD Micro Finance Institution for between 6 to 10 years; those above 11 years were 24.7% respondents and 25.0% had spent less than 5 years with the with the lending institution. Considering the statistics in the Table, majority of the respondents 75.0% had been involved with

UGAFOD Micro Finance Institution for more than six years. This means that the respondents had enough experience that enabled them to understand the credit extension practices of the lending institution. Therefore given their level of education and then the experience, it is worthwhile mentioning that the respondents were qualified to provide appropriate data.

4.3 Research Objective One: The effect of credit risk assessment on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

4.3.1 UGAFOD Micro Finance Institution trying to limit risk taking as it offers loans hence enabling good performance of loans

This item of the study correlated credit risk assessment on if UGAFOD Micro Finance Institution work to limit risk taking as it offers loans with item 16 on if the limiting of risk taking in the offering of loans enabled good performance of loans in the questionnaire. This aimed at if limiting risk taking prevented failure to pay the loans by the borrowers.

Table 4.5 UGAFOD Micro Finance tries to limit risk taking as it offers it offers loans

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	144	40.0	40.0	40.0
	Strongly agree	216	60.0	60.0	100.0
	Total	360	100.0	100.0	

Source: Primary data

According to the statistics on item one, the majority of the respondents 60.0% strongly agreed and 40.0% agreed. This means that lending institution made limiting risk a high priority as no single respondent disagreed. On whether this enabled good performance of loans**,** the results were largely in correlation.

Table 4.6: The limiting risk taking in the offering of loans enables good performance of loans

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	16	4.4	4.4	4.4
	Disagree	77	21.4	21.4	25.8
	Undecided	67	18.6	18.6	44.4
	Agree	126	35.0	35.0	79.4
	Strongly agree	74	20.6	20.6	100.0
	Total	360	100.0	100.0	

Source: Primary data

The larger number of the respondents 35.0% and 20.6% agreed and strongly agreed respectively. Those who were undecided were 18.6% while 21.4% disagreed and 4.4% strongly disagreed. These results indicate that limiting risk enables good performance of loans. However, limiting risk did not completely guarantee good performance as a sizeable number of the respondents 21.4% and 4.4% disagreed and strongly disagreed, respectively.

The results of the interviews were also in correlation with the test statistics results. All the respondents indicated that UGAFOD Micro Finance Institution trying to limit risk taking as it offers loans enabled good performance of loans. One staff of UGAFOD Micro Finance Institution stated:

"Limiting risk improved the overall asset quality of the lending institution." Another stated that "it reduced the chances of offering loans to clients likely to default hence good performance of the loan portfolio."

While another remarked that, "risk limiting reduced risk levels hence better loan portfolio."The staff pointed out that UGAFOD Micro Finance Institution uses the CAMPARI model which considers character, ability, margins, purpose, amount, repayment and insurance. The staff of

UGAFOD Micro Finance Institution carries out site visits and the client provides of records which are assessed to see whether the clients request conforms to UGAFOD Micro Finance Institution policy. These views were confirmed by the clients of the lending institution. One client stated:

"UGAFOD Micro Finance Institution credit application form requires the signatures of sureties confirming that the borrower was able to pay, the reason for which the money is borrowed and site visits are made to confirm the availability of collateral pledged as security for the loan. That when all these conditions are fulfilled to the satisfaction of the lending institution, that is when can obtain the loan".

Accordingly this helped in confirming to UGAFOD Micro Finance Institution that one was in position to repay the loan hence limiting risk.

The above finding that UGAFOD Micro Finance Institution tries to limit risk by ensuring that a customer is in position to repay the loan is in agreement with the views expressed by other scholars. Egesa (2008) states that, Uganda's financial sector regulatory framework and reforms helps in credit extension. Accordingly, the credit policy demand prudential standards. That is rules that limit risk taking, intended to lower lending institution failures. Kabir et al (2010) also indicate that risk is inherent in all aspects of a commercial operation and so for lending institutions and financial institutions, credit risk is an essential factor that needs to be managed. This thus calls for credit risk assessment to; minimise bad loans by improving the risk/return profiles of the portfolio. Therefore are with finding of the study, a registered lending institutions have to have measures that limit risk hence better performance of the loan portfolio.

4.3.2 UGAFOD Micro Finance Institution having the credit risk assessment methodology hence improving performance of loans

This item of the study correlated item 2 of the questionnaire on if UGAFOD Micro Finance Institution has established the credit risk assessment methodology with item 17 on if the establishment of the credit risk assessment methodology improved performance of loans. The statistics obtained from the respondents indicate that established a credit risk assessment methodology and this improved performance of loans.

Table 4.7 UGAFOD Micro Finance has established the credit risk assessment methodology

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	72	20.0	20.0	20.0
	Undecided	72	20.0	20.0	40.0
	Agree	144	40.0	40.0	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: Primary data

The majority of the respondents 40.0% and 20.0% agreed and strongly agreed that UGAFOD Micro Finance Institution had established a credit risk assessment methodology. Those who were undecided were 20.0% and 20.0% disagreed. However, the fact that a sizeable number of 40.0% of the respondents were undecided and disagreed, possibly this was due to the clients that did not understand the risk methodology assessment of the lending institution.

On whether the risk methodology assessment improved performance of the loan portfolio, the statistics correlated with the results of the test statistics.

Table 4.8: Establishment of the credit risk assessment methodology improved performance of loans

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	65	18.1	18.1	18.1
	Disagree	72	20.0	20.0	38.1
	Undecided	16	4.4	4.4	42.5
	Agree	125	34.7	34.7	77.2
	Strongly agree	82	22.8	22.8	100.0
	Total	360	100.0	100.0	

Source: Primary data

The larger number of the respondents 34.7% agreed, 22.8% strongly agreed while 4.4% were undecided. Those who disagreed were 20.0% and 18.1% strongly disagreed. This means that UGAFOD Micro Finance Institution having the credit risk assessment methodology improves performance of loans.

In the interviews the staff of the lending institution, they indicated that UGAFOD Micro Finance Institution employs several strategies of risk assessment methodology. These included the credit policy, risk grading, insurance and valuing collateral. There is also credit scoring and following of the financial models such as assessing market risk, liquidity risk, leverage, systemic risk and financial regulation. The respondents indicated that good assessment result into a high likelihood of quality loan portfolio performance and vice versa. Apparently, the risk assessment methodology of UGAFOD Micro Finance Ltd, Mpigi Branch worked because the Non – Performing Assets (NPA) were only at 3% with performing Assets (PA) at 97%. One respondent pointed out:

"Poor risk assessment methodology results in a greater proportion of the lending institutions entire portfolio becoming non – performing and ultimately being written off".

This directly reduces the lending institutions net earnings at the end of the reporting period."This means that a good risk assessment methodology improves performance of loans as indicated by the results of test statistics. The finding that a good risk assessment methodology improves performance of loans as is in agreement with opinions expressed by other scholars. Day (2006) emphasises that a lending institution should adopt and document a sound loan loss methodology, which addresses credit risk assessment policies, procedures and controls for assessing credit risk, identifying problem loans and determining loan provisions in a timely manner. This as with the finding of the study shows that a credit risk assessment methodology improves loans performance.

4.3.3 UGAFOD Micro Finance Institution staff carefully carrying out investigation, preparation of credit report and considering factors of selection of the borrower hence better loans performance.

This item of studied item 3 on if UGAFOD Micro Finance Institution staff carefully carried out investigations, preparation of credit report and considered factors of selection of the borrower. It was with item 18 on if UGAFOD Micro Finance Institution staff carefully carrying out investigation, preparation of credit report and considering factors of selection of the borrower helped to ensure better loans performance.

Table 4.9: UGAFOD Micro Finance staff carefully carries out investigation, preparation of credit report and considers factors of selection of the borrower at UGAFOD Micro Finance

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	8	2.2	2.2	2.2
	Disagree	72	20.0	20.0	22.2
	Undecided	10	2.8	2.8	25.0
	Agree	198	55.0	55.0	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: Primary data

For item 3, the majority of the respondents 55.0% agreed, 20.0% strongly greed and 2.8% were undecided. Those who disagreed were only 20.0% and 2.2% strongly disagreed.

Table 4.10: UGAFOD Micro Finance staff carefully carrying out investigation, preparation of credit report and consider factors of selection of the borrower have helped to ensure better loans performance.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	53	14.7	14.7	14.7
	Disagree	52	14.4	14.4	29.2
	Undecided	18	5.0	5.0	34.2
	Agree	165	45.8	45.8	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: primary data

For item 18, still the majority were in agreement with 45.8% agreeing, 20.0% strongly agreeing and only 5.0% being undecided. Those who disagreed were only 14.4% and 14.7% strongly disagreed. This means that UGAFOD Micro Finance Institution staff carefully carried out investigation, prepared credit reports and considered factors of selection of the borrower hence better loans performance.

During the interviews with the staff of UGAFOD Micro Finance Institution and the clients, they all confirmed that UGAFOD Micro Finance Institution staff carefully carried out investigation, prepared credit reports and considered factors of selection of the borrower and this ensured better loans performance. Generally the respondents indicated that loan officers visited the sites of the borrowers to verify the businesses, collateral and made reports which are forwarded to UGAFOD Micro Finance Institution management for approval of the loan. It was pointed out not all people who put forward their loan requests were considered. The capacity of the client to repay has to first be critically established. From the reports of the branch it was established that between January 2010 and December 2010, UGAFOD Micro Finance Ltd rejected 660 loan applications because the capacity of the clients to repay could not be easily ascertained. Therefore UGAFOD Micro Finance Institution staff carefully carried out investigation, prepared credit reports and considered factors of selection of the borrower and this ensured better loans performance.

Nassali (2005) in a study on the Loan Assessment System for Centenary Rural Development Lending institution diagrammatically presents the credit assessment procedure of UGAFOD Micro Finance Ltd that confirms that centenary has a credit assessment system. This is presented in Figure 2 here.

The finding that UGAFOD Micro Finance Institution staff carefully are carrying out investigation, preparing credit reports and considering factors of selection of the borrower ensures better loans performance is agreed to by Kalimba (2005) explains that in credit risk assessment, there is credit investigation. The investigation has to look at borrowers; managerial aspect, that is; sincerity, honesty, integrity, educational background, experience of the borrower

and ability of the management to run the project efficiently. Organisational aspect, that is; under what type of organisation the activities was undertaken.

Whether it is sole proprietorship or partnership, private limited or public limited company; technical aspect: location of the business, land and building, machineries equipment, requirements to be used like power, fuel, water, materials etc. Marketing aspect: marketability of the product to be produced projected sales volume, scope of market expansion, possible threat of competition etc. Financial aspect: total requirement of fund for the business activities and how much was required as loan from the lending institution, borrowers contributions in the business, cash inflow and out flow statement, sales forecast, balance sheet, profit and loss account etc. Economic aspect: contribution to gross commercial product (GCP), creation of employment, indirect benefit of the society.

Namyalo (2007) also in agreement indicates that there is also need for Preparation of Credit Report. A credit report contains: name and address of the client, nature of the firm and date of establishment, nature of business, investment in the business, subsidiary, net sales, annual net income, market reputation and means of finance particulars of lending institution account particulars of owner. And then considering the factors of selection of the borrower that include Five Cs: Character, Capacity, Capital/ Credit worthiness, Condition (Economic) and Collateral. According to the above literature, it is indicated that in credit assessment, there is need for investigation, preparation of credit report and considering factors of selection of the borrower. However, with high levels of corruption lending institutions staff may not be carrying out proper investigation and true preparation of credit report and considering factors of selection of the

borrower. This thus as with the finding of the study show that the process of investigation, preparation of credit report and considering factors of selection of the borrower at UGAFOD Micro Finance Institution ensures better performance of the loan portfolio.

4.3.4 UGAFOD Micro Finance Institution having a credit grading system which enables easy recovery of loans

This item aimed at establishing the grading system that they considered for each individual before offering the loan such that UGAFOD Micro Finance Institution is certain the borrower according to his/her grade gets the loan that he/she was able to repay.

Table 4.11: Banks have a credit grading system

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	72	20.0	20.0	20.0
	Undecided	10	2.8	2.8	22.8
	Agree	88	24.4	24.4	47.2
	Strongly agree	190	52.8	52.8	100.0
	Total	360	100.0	100.0	

Source: Primary data

To that item seeking to establish if UGAFOD Micro Finance Institution had a credit grading system, the majority of the respondents 52.8% strongly agreed followed by 24.4% who agreed. Those who were undecided were 2.8% and 20.0% disagreed. This indicates that UGAFOD Micro Finance Institution had a credit grading system.

Table 4.12: The credit grading system of UGAFOD Micro Finance enables easy recovery of loans

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	41	11.4	11.4	11.4
	Disagree	97	26.9	26.9	38.3
	Undecided	48	13.3	13.3	51.7
	Agree	100	27.8	27.8	79.4
	Strongly agree	74	20.6	20.6	100.0
	Total	360	100.0	100.0	

Source: Primary data

As to whether this credit grading system enabled easy recovery of loans, still the larger majority of the respondents were in agreement with 27.8% and 20.6% agreeing and strongly agreeing and 13.3% being undecided. Those who disagreed were 26.9% and 11.4% strongly disagreed. These results show that to some extent the credit grading system enabled the recovery of loans.

When asked if the loan offered depended on the grading system, the results were still in agreement.

Table 4.13: The loan credited depends on the individual's credit grade

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	14	3.9	3.9	3.9
	Disagree	124	34.4	34.4	38.3
	Undecided	8	2.2	2.2	40.6
	Agree	142	39.4	39.4	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: Primary data

The larger number of the respondents 39.4% and 20.0% agreed and strongly agreed respectively. Those who were undecided were 2.2% and 34.4% and 3.9% disagreed and strongly disagreed respectively.

Table 4.14: Offering loans depending on the individual's credit grade has helped in loans management

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	16	4.4	4.4	4.4
	Disagree	69	19.2	19.2	23.6
	Undecided	31	8.6	8.6	32.2
	Agree	173	48.1	48.1	80.3
	Strongly agree	71	19.7	19.7	100.0
	Total	360	100.0	100.0	

Source: Primary data

To the item, seeking to establish if offering loans depending on the individual's credit grade has helped in loans management, still the respondents were in agreement. The majority of 48.1% and 19.7% agreed and strongly agreed respectively. Only 8.6 were undecided, 19.2% disagreed and 4.4% strongly disagreed. This means that the credit grading system enabled easy management of the loans hence loans recovery.

A review of secondary data from UGAFOD Micro Finance Ltd, Mpigi Branch confirms the existence of the grading system. The credit policies and procedures of UGAFOD Micro Finance Ltd (December, 2010) outlines that the branch committee has to agree with the grading of the various loans before a loan is approved. The grading system of UGAFOD Micro Finance Institution is presented here under in Table 4.6.

During the interviews, the staffs of UGAFOD Micro Finance Institution were to tell asked to tell what the importance of the credit grading system was. One respondent stated that, "it is the basis on which the decision to offer a loan or deny is based. High scores indicate a limited risk." Another stated that, "it helps in the levying interest rates. Low scores which indicate high credit risk attract higher interest rates and vice versa. This reduces the chances of loss by the lending institution." This indicates that the credit grading system enables the recovery of loans.

The finding that the credit grading system enables the recovery of loans is in agreement with the Roy (2005) who indicates that in credit risk assessment; there is need for a Credit Risk Grading system (CRGS). Roy explains that a Credit Risk Grading is the basic module for developing a Credit extension system. Credit risk grading is an important tool for credit extension as it helps the Financial Institutions to understand various dimensions of risk involved in different credit transactions. The aggregation of such grading across the borrowers, activities and the lines of business can provide better assessment of the quality of credit portfolio of a Financial Institution (FI). Credit grading helps the sanctioning authority to decide whether to lend or not to lend, what should be the lending price, what should be the appropriate credit facility and what are the various risk mitigation tools to put a cap on the risk level. This thus helps in the recovery of lent out funds.

4.3.5 Research Hypothesis One Testing: Credit risk assessment affects the performance of the loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

This hypothesis was obtained from objective one of the study that sought to examine the effect of credit risk assessment on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch. The test was carried out on the Null Hypothesis (Ho) which stated that there is no relationship between credit risk assessment and performance of loan portfolio.

This hypothesis analysed items 1 – 5 of the questionnaire that were correlated with items 16 –20. The items of study included UGAFOD Micro Finance Institution trying to limit risk taking as it offers loans, establishing the credit risk assessment methodology, carefully carried out investigation, prepared credits report and considered factors of selection of the borrower, if UGAFOD Micro Finance Institution had a credit grading system and if the loan credited

depended on the individual's credit grade. These were studied in relation with enabling of good performance of loans, improvement performance of loans, ensuring of better performance of loans, enabling easy loans recovery and helping in loans management. The results of this hypothesis are presented using Pearson correlation co – efficient between the index of credit risk assessment and performance of loan portfolio as illustrated in Table 4.5 below.

Table 4.15: The Correlation between Credit Risk Assessment and Performance of Loan Portfolio

		Credit risk assessment	Performance of loan portfolio
credit risk assessment	Pearson Correlation	1	.590
	Sig. (2-tailed)	.	.000
	N	360	360
Performance of loan portfolio	Pearson Correlation	.590	1
	Sig. (2-tailed)	.000	.
	N	360	360

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

Table 4.15 shows that the value of the co – efficient equals to .590. This value is positive and it means that there is a strong positive relationship between credit risk assessment and performance of loan portfolio. The sig. value for the correlation was equal to .000 which was less than the level of significance (.05) which led to the rejection of the null hypothesis that there is no relationship between credit risk assessment and performance of loan portfolio. Thus the results indicate that there is a significant relationship between credit risk assessment and performance of loan portfolio.

4.4 Research Objective Two: The effect of credit monitoring on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch.

4.4.1 Existence of an effective loans management monitoring system and performance of loans

This item aimed at establishing if UGAFOD Micro Finance Institution had an effective loans management monitoring system and if this helped the performance of loans.

Table 4.16: UGAFOD Micro Finance has an affective loans management monitoring system

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	18	5.0	5.0	5.0
	Disagree	121	33.6	33.6	38.6
	Undecided	11	3.1	3.1	41.7
	Agree	138	38.3	38.3	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: Primary data

When the respondents were asked to tell if UGAFOD Micro Finance Institution had an effective loan monitoring system, a slight majority of 38.3% agreed, 20.0% strongly agreed and 3.1% were undecided. Those who disagreed were 33.6% and 5.0% strongly agreed.

Table 4.17: UGAFOD Micro Finance's loans management monitoring system helps in the performance of loans

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	24	6.7	6.7	6.7
	Disagree	79	21.9	21.9	28.6
	Undecided	64	17.8	17.8	46.4
	Agree	122	33.9	33.9	80.3
	Strongly agree	71	19.7	19.7	100.0
	Total	360	100.0	100.0	

Source: Primary data

As to whether the lending institution's loans management monitoring system helps in the performance of loans, the larger number of the respondents 33.9% agreed, 19.7% strongly agreed and 17.8% were undecided. Those who disagreed were 21.9% and 6.7% strongly disagreed.

A scrutiny of the Credit Policies and Procedures December 2010 of UGAFOD Micro Finance Ltd shows a clearly outlined system of the credit monitoring. It outlines that; as a general rule, loans should be approved to borrowers living within reasonable distance from the branch that would allow regular visits and monitoring by the loan officers. Exception can be made for valuable customers with strong collaterals. (Strong collaterals are defined as those which are located in urban areas, well developed and easily realizable in case of default). All microfinance loans shall be charged a fixed rate of interest and a monthly monitoring fee for the entire loan period. All outstanding loans in the portfolio shall be closely monitored with the aid of the computer system. Reports generated by the system on a daily, weekly, and monthly basis was used by the branch management and Head office for monitoring and control of the arrears rate, and general quality of the lending business. The branch loan committees shall hold recovery meetings at least twice a month to review all loans in arrears on each loan officer’s portfolio. The details for each meeting shall be recorded by the Credit Administrator and filed for reference in subsequent meetings.

The Credit Policies and Procedures December 2010 further outlines that a Loan Officer is fully responsible for the follow up and recovery of all loans in his or her own portfolio. Loans in arrears are to be recovered before they are more than 30 days in arrears. All loans in the commercial portfolio shall be continuously monitored to ensure that portfolio quality does not deteriorate. Loan officers should monitor the performance of borrowers primarily to reassure

themselves that a borrower will continue to be in position to honour the terms of the loan and that the quality of our loan portfolio performance is within acceptable parameters. Monitoring was done by Commercial Loan Officers together with Credit Administrator and Credit Analysts as follows:

1. In-house continuous monitoring:

   The loan officers are required to:

   - Review loan monitoring reports generated by the system on a monthly basis;
   - Ensure proper payments of interest and principal every month;
   - Ensure proper maintenance of credit files, complete with required updates information
   - On a monthly basis, the Head Office Credit Supervisor will provide senior management with a performance report for the loan portfolio performance (amounts approved, disbursed, outstanding, arrears,); any significant changes in the quality of the portfolio must be analyzed in detail.
   - On a monthly basis, the GM Credit will provide senior management and the Board with a performance report for the loan portfolio performance similar to the above one.

2. Customers' contact monitoring:

   The loan officers are required to:

   - Visit customers at least once every quarter;
   - Maintain contact with customers in person;
   - Obtain stock statements (for merchandising and manufacturing businesses) on a monthly basis;
   - Each visit was supported by written visit report to be properly kept in files;

3. Non-performing loans:

- In case the loan becomes non-performing, in-house monitoring and contact with customers was performed on a weekly basis (daily if needed);
- Each visit was supported by a written visit report to be properly kept on file.

The existence of credit monitoring system and its ability to help in loan portfolio performance was confirmed during the interviews. One staff stated:

"UGAFOD Micro Finance Institution monitors borrowers' compliance with credit term to avoid funds diversion and default".

And as to whether this helped the performance of loan, one lending institution staff member remarked:

"The monitoring system helps loans officers to keep tabs on its customers ensuring agreed schedules are adhered to."

Another stated:

"The *credit terms are usually imposed to ensure the loaned monies are actually put to use for the purposes (facilities) they are requested for".*

However, during interaction with the clients, it was found out that some aspects of the monitoring system were merely on paper and UGAFOD Micro Finance Institution staff did not carry out the monitoring as required. One client pointed out that "UGAFOD Micro Finance Institution staff does not ensure that the borrowed money is put the actual use and even monitor the progress of the projects." Another client indicated that, "the monitoring of UGAFOD Micro

Finance Institution only begins when one has started to default."However, generally all the clients agreed that being monitored by UGAFOD Micro Finance Institution staff made them feel reminded hence fulfilling their loans obligations. Therefore monitoring helps in the performance of the loan portfolio.

The finding that monitoring of clients by UGAFOD Micro Finance Institution helps the performance of the loan portfolio is supported by other scholars. According to Boateng (2008), every lending institution has to develop and implement comprehensive procedures and Information Systems to follow up the condition of individual credits. After a credit facility is approved and draw down allowed, the facility should be continuously watched over. This is keeping track of borrowers' compliance with credit terms, identifying early signs of irregularity, conducting periodic valuation of collateral and monitoring timely repayments. To minimise credit losses, monitoring procedures and systems should be in place that provide an early indication of the deteriorating financial health of a borrower. At a minimum, systems should be in place to report the following exceptions to relevant executives: past due principal or interest payments and breach of facility covenants, non-receipts of financial statements on a regular basis and any covenant breaches or exceptions made, action not taken on time for findings of any internal, external or regulator inspection/audit. Thus, as with the finding of the study, constant watching over the borrowers helps in the performance of loans.

4.4.2 Debt Collection Methods and Reduction Loans Default

This item looked at the debt collection methods and how these helped in reducing default. On this item, the respondents were asked to tell if UGAFOD Micro Finance Institutions ends delinquent letters, made telephone calls, foreclosures and employed debt collection agencies.

Table 4.18: UGAFOD Micro Finance sends delinquent letters, telephone calls, foreclosures and employs debt collection agencies

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	.6	.6	.6
	Undecided	71	19.7	19.7	20.3
	Agree	158	43.9	43.9	64.2
	Strongly agree	129	35.8	35.8	100.0
	Total	360	100.0	100.0	

Source: Primary data

To this item, the majority of the respondents the majority of 43.9% and 35.8% agreed and strongly agreed respectively. Only 19.7% were undecided and 0.6% disagreed.

Table 4.19: Has the sending of delinquent letters, telephone calls, sending foreclosures and employing debt collection agencies help in reducing loans default.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	23	6.4	6.4	6.4
	Disagree	24	6.7	6.7	13.1
	Undecided	10	2.8	2.8	15.8
	Agree	187	51.9	51.9	67.8
	Strongly agree	116	32.2	32.2	100.0
	Total	360	100.0	100.0	

Source: Primary data

As to whether the sending of delinquent letters, making telephone calls, foreclosures and employing debt collection agencies helped in reducing loans default, the majority of the respondents 51.9% agreed, 32.2% strongly agreed and only 2.8% were undecided. Those who disagreed were 6.4% and 6.7% strongly disagreed. This means that the sending of delinquent letters, making telephone calls, foreclosures and employing debt collection agencies reduced loans default.

Data collected from the interviews agrees with the descriptive statistics presented above. All the respondents agreed that UGAFOD Micro Finance Institution employed the sending of delinquent letters, made telephone calls, foreclosures and employed debt collection agencies. One staff of UGAFOD Micro Finance Institution indicted that, "these ensure that clients conform to the agreements signed to avoid default." Another staff of UGAFOD Micro Finance Institution indicated that, "Yes it does, because the customers are made aware that UGAFOD Micro Finance Institution will take the necessary precautions to ensure that the loaned funds are recovered at all cost. This in turn motivates them to pay outstanding monies or make efforts to pay loans." This was also agreed to by the clients. One client indicated that, "any warning from UGAFOD Micro Finance Institution scares me into looking for the lending institution's money such that I am not embarrassed by attachment of my property." Another respondent indicated, "I try as much as possible to fulfil obligations to UGAFOD Micro Finance Institution such that I am not embarrassed by warnings from the lending institution. This means that sending of delinquent letters, making telephone calls, foreclosures and employing debt collection agencies helps in reducing default.

4.4.3 Frequent contact with borrowers and creating conducive environment as a solver of problems and loans repayment

On this item, the respondents were asked to tell if the staff of UGAFOD Micro Finance Institution carried out frequent contact with borrowers, created an environment that UGAFOD Micro Finance Institution could be seen as a solver of problems and trusted adviser.

Table 4.20: Does the staff of UGAFOD Micro Finance carry out frequent contact with borrowers, creating an environment that UGAFOD Micro Finance can be seen as a solver of problems and trusted adviser

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	12	3.3	3.3	3.3
	Disagree	124	34.4	34.4	37.8
	Undecided	31	8.6	8.6	46.4
	Agree	121	33.6	33.6	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: Primary data

The statistics on indicate that 33.65 agreed, 20.0% strongly agreed while 8.6% were undecided. Those who disagreed were 34.4% and 3.3%. This results show a large number of the respondents disagreeing with the item though they were not an absolute majority.

Table 4.21: UGAFOD Micro Finance being supportive to clients finding difficulty in loans repayments encourages them to repay

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	52	14.4	14.4	14.4
	Disagree	53	14.7	14.7	29.2
	Undecided	42	11.7	11.7	40.8
	Agree	143	39.7	39.7	80.6
	Strongly agree	70	19.4	19.4	100.0
	Total	360	100.0	100.0	

Source: Primary data

As to whether UGAFOD Micro Finance Institution being supportive to clients finding difficulty in loans repayments encouraged them to repay, the larger number of the respondents, 39.75 agreed, 19.4% strongly agreed and those who were undecided were 11.7%. Still a sizeable number of the respondents 14.7% and 14.4% disagreed and strongly disagreed respectively.

When this question was put the clients in the interviews, the respondents indicated that whereas UGAFOD Micro Finance Institution made contact with borrowers, it largely did not create an environment that UGAFOD Micro Finance Institution could be seen as a solver of problems and trusted adviser. One respondent stated that, "most of the loan officers are proud and do not give a hearing the customer. They do not listen and only scares you into avoiding going to UGAFOD Micro Finance Institution and switching off your phone when you have a repayment problem." Another respondent indicated that, "my loans officer is a nightmare and only gets in touch with me to scare me."

However, there were those clients who indicated that some loans officers and especially top managers create an environment that UGAFOD Micro Finance Institution could be seen as a solver of problems and trusted adviser. One respondent stated, "When I went to the loans manager after being threatened by my loans officers, he understood and we rescheduled my date of payment and gave me more time to find the money and I was able to fulfil my obligations." Another respondent indicated that, "my loans officer understands and always counsels me on how to pay whenever I have repayment problems and go to her." This means that if UGAFOD Micro Finance Institution keeps in contact with the customers and presents itself as a problem solver, it can be trusted hence encouraging repayment.

Generally on this item, the views of the staff of UGAFOD Micro Finance Institution were almost the same. They indicated that UGAFOD Micro Finance Institution maintains a standard relationship management practice which requires account managers to keep in touch with their clients making sure they understand the customers' needs and take step to or provide lasting

/sustainable solutions to repayment issues. One staff of UGAFOD Micro Finance Institution stated that, “UGAFOD Micro Finance Institution is not a real state dealer, thus it creates conducive atmosphere for repayment such that it avoids selling property pledged as security not to tarnish its image in the public who may fear to borrow in future.” Generally, the views expressed here indicate that if the staff of UGAFOD Micro Finance Institution carry out frequent contact with borrowers, create an environment that UGAFOD Micro Finance Institution can be seen as a solver of problems and trusted adviser, this encourages clients’ repayment of loans.

The finding that if the staff of UGAFOD Micro Finance Institution carries out frequent contact with borrowers create an environment that UGAFOD Micro Finance Institution can be seen as a solver of problems and trusted adviser, it encourages clients’ repayment of loans concurs with the views of Mwisho (2008). He states that monitoring involves, among others, frequent contact with borrowers, creating an environment that UGAFOD Micro Finance Institution can be seen as a solver of problems and trusted adviser; develop the culture of being supportive to borrowers whenever they are recognised to be in difficulties and are striving to deal with the situation. This as with the finding of the study shows that UGAFOD Micro Finance Institution has to create an environment where it can be seen as a solver of problems and trusted adviser like hence encouraging repayment.

4.4.4 Closely monitoring the borrowers’ respective activities, their performance, as well as behaviour and loans recovery

This item aimed at establishing if UGAFOD Micro Finance Institution closely monitored the borrowers’ respective activities, their performance, as well as behaviour and is this enabled

recovery of loans. Regarding if UGAFOD Micro Finance Institution closely monitored the borrowers' respective activities, their performance, as well as behaviour, larger number of the respondents were in agreement.

Table 4.22: The borrowers' respective activities, their performance, as well as behaviour are closely monitored

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	38	10.6	10.6	10.6
	Disagree	99	27.5	27.5	38.1
	Undecided	24	6.7	6.7	44.7
	Agree	127	35.3	35.3	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: Primary data

Those who agreed were 35.3%, those strongly agreeing 20.0% and 6.7% were undecided. Those who disagreed were 27.5% and 10.6% strongly disagreed.

Table 4.23: The monitoring of the borrowers' respective activities, their performance, as well as behaviour enables loans recovery

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	38	10.6	10.6	10.6
	Disagree	97	26.9	26.9	37.5
	Undecided	22	6.1	6.1	43.6
	Agree	131	36.4	36.4	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: Primary data

As to whether the monitoring of the borrowers' respective activities, their performance, as well as behaviour enabled loans recovery, the larger number of the respondents 36% agreed, 20.0% strongly agreed and 6.1% were undecided. Those who disagreed were 26.9% and 10.6% strongly

disagreed. Generally this means that UGAFOD Micro Finance Institution closely monitors the borrowers' respective activities, their performance, as well as behaviour enabling loans recovery. During interviews, the staff and clients agreed that UGAFOD Micro Finance Institution closely monitored the borrowers' respective activities, their performance, as well as behaviour enabling loans recovery. When the staff of UGAFOD Micro Finance Institution was asked to tell why did UGAFOD Micro Finance Institution monitor the borrower's respective activities, performance as well as behaviour, several views were presented. One staff of UGAFOD Micro Finance Institution stated that, "to ensure that the borrower will continue to pay the debt owed to UGAFOD Micro Finance Institution and also provide professional advice while recovering the loan." Another staff of UGAFOD Micro Finance Institution stated that, "to ensure that the customer is on track and also as an avenue for collecting feedback that may harbour worrying signs of looming failure. This also builds confidence in the customer that UGAFOD Micro Finance Institution is very interested in their progress/success and the development thus propelling them to do the right thing and stick to agreed terms/confidence." For the customers, they generally all agreed that if they are closely monitored, they feel obliged to pay their loans. Therefore, this means that if UGAFOD Micro Finance Institution closely monitors the borrowers' respective activities, their performance, as well as behaviour, it enables paying of the loans

The finding that if UGAFOD Micro Finance Institution closely monitors the borrowers' respective activities, their performance, as well as behaviour, it enables paying of the loans agrees with the views expressed by other scholars. Richard (2006) explains that the lending institutions needs to monitor borrowers' respective activities, their performance, as well as

behaviour by both branches and corporate division on daily basis to establish whether there are any changes that need to be taken care of to protect non-repayment of credits. This means that there is need for closely monitoring the borrowers' respective activities, their performance, as well as behaviour to enable them to pay their loans.

4.4.5 Ensuring the value of collateral is updated periodically and loan recovery

This item sought to establish if UGAFOD Micro Finance Institution ensures the value of collateral is updated periodically to account for changes in market conditions such that there is certainty that the customer will still be in position to repay the loan with the existing circumstances hence loan recovery.

Table 4.24: UGAFOD Micro Finance ensures the value of collateral is updated periodically to account for changes in market conditions

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	9	2.5	2.5	2.5
	Disagree	135	37.5	37.5	40.0
	Undecided	3	.8	.8	40.8
	Agree	141	39.2	39.2	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: Primary data

Concerning if UGAFOD Micro Finance Institution ensures the value of collateral is updated periodically to account for changes in market conditions, 39.2% of the respondents agreed, 20.0% strongly agreed and 0.8% were undecided. However, there was a big number of 37.5% and 2.5% who disagreed and strongly disagreed respectively.

Table 4.25: UGAFOD Micro Finance ensuring the value of collateral is updated periodically to account for changes in market ensures loan recovery

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	72	20.0	20.0	20.0
	Undecided	48	13.3	13.3	33.3
	Agree	169	46.9	46.9	80.3
	Strongly agree	71	19.7	19.7	100.0
	Total	360	100.0	100.0	

Source: primary data

As to whether, UGAFOD Micro Finance Institution ensuring the value of collateral is updated periodically to account for changes in market ensures loan recovery, the larger number of the respondents 46.9% agreed, 19.7% strongly agreed, 13.3 were undecided and 20.0% disagreed. This generally means that UGAFOD Micro Finance Institution monitoring the value of collateral is updated periodically to account for changes in market conditions ensures the recovery of loans.

When during the interviews the staff of UGAFOD Micro Finance Institution were asked to tell why UGAFOD Micro Finance Institution periodically updated the value of collateral for changes in the market conditions, several responses were given. These included, “to ensure that UGAFOD Micro Finance Institution is properly/sufficiently covered in terms of security, since it the secondary source of repayment.” “To ascertain the trend of the borrowers businesses and this case, UGAFOD Micro Finance Institution is able to identify the need that might need to be met.” And “this allows UGAFOD Micro Finance Institution to ensure that the total exposure towards customers is sufficiently, secured as property rates have the ability to change in either direction.”

However, during interviews with the respondents, they generally indicated that UGAFOD Micro Finance Institution did periodically update the value of collateral for changes in the market conditions because staff does not visit the customer after offering the loan except when the customer is failing to fulfil their repayment obligations. This means that UGAFOD Micro Finance Institution does not visit the clients. One customer indicated that, "even one can manage to sell the security if say its Kibanja land (unregistered land) because UGAFOD Micro Finance Institution ceases to make visits to the customer when there are no repayment problems. One other customer said that, "except for properties like vehicles for which UGAFOD Micro Finance Institution keeps the log books which one cannot withdraw before completing repayment, otherwise UGAFOD Micro Finance Institution does not monitor the clients as long as they are repaying the loans properly." However, they all indicated that UGAFOD Micro Finance Institution visiting them to assess the performance of their business when repayment is not going well puts pressure on them and make them work hard to repay. This means that if UGAFOD Micro Finance Institution periodically updates the value of collateral for changes in the market condition, it helps in the recovery of loans.

The finding that if UGAFOD Micro Finance Institution periodically updates the value of collateral for changes in the market condition, it helps in the recovery of loans is agreed by other scholars. Derban et al (2005) expound that credit monitoring involves keeping track of obligor's principal and interest repayments, account activity, as well as instances of excesses over credit limits. He further explains that attention is paid to the obligor's willingness and ability to provide timely margin top-up. The obligor's ability to adhere to negative pledges and financial covenants stated in the loan agreement are assessed and breaches detected trigger prompt action.

Indeed, Mlabwa (2008) adds that the value of collateral should be updated periodically to account for changes in market conditions. That where the collateral is property or shares, an institution should undertake more frequent valuations in adverse market conditions. If the facility is backed by an inventory or goods purportedly on the obligor's premises, appropriate inspections should be conducted to verify the existence and valuation of the collateral. This means that if UGAFOD Micro Finance Institution periodically updates the value of collateral for changes in the market condition, it helps in the recovery of loans.

4.4.6 Research Hypothesis Two Testing: Credit monitoring affects the performance of the loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

This hypothesis was obtained from objective two of the study that sought to assess the effect of credit monitoring on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch. The test was carried out on the Null Hypothesis (Ho) which stated that credit monitoring has no effect on the performance of the loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch.

This hypothesis analysed items 6 – 10 of the questionnaire that were correlated with items 21 – 25. The items of study included UGAFOD Micro Finance Institution had an affective loans management monitoring system, implemented the system of tracking of borrowers' compliance with credit terms, sent delinquent letters, telephone calls, foreclosures and employs debt collection agencies, staff of UGAFOD Micro Finance Institution carried out frequent contact with borrowers, creating an environment that UGAFOD Micro Finance Institution can be seen as a solver of problems and trusted adviser, borrowers' respective activities, their performance, as well as behaviour are closely monitored. These were looked at on how the monitoring system

helps in the performance of loans, sending of delinquent letters, telephone calls, sending foreclosures and employing debt collection agencies helped in reducing loans default, being supportive to clients finding difficulty in loans repayments encouraged them to repay, monitoring of the borrowers' respective activities, their performance, as well as behaviour enabled loans recovery and ensuring the value of collateral is updated periodically to account for changes in market ensured loan recovery. The results of this hypothesis are presented using Pearson correlation co – efficient between the index of credit monitoring and performance of loan portfolio.

Table 4.26: The Correlation between Credit Monitoring and the Performance of the Loan portfolio performance

		effect of credit monitoring	Loan portfolio performance
effect of credit monitoring	Pearson Correlation	1	.864
	Sig. (2-tailed)	.	.000
	N	360	360
Loan portfolio performance	Pearson Correlation	.864	1
	Sig. (2-tailed)	.000	.
	N	360	360

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

Table 4.26 shows that the value of the co – efficient equals to .864. This value is positive and it means that there is a significant positive relationship between credit risk assessment and performance of loan portfolio. The sig. value for the correlation was equal to .000 which was less than the level of significance (.05) which led to the rejection of the null hypothesis that the credit

monitoring has no effect on the performance of the loan portfolio. Thus the results indicate that credit monitoring significantly affects the performance of the loan portfolio.

4.5 Research Objective The effect of credit risk control on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

4.5.1 Administering the credit facility to ensure orderly and full payment and loan recovery

This item of the aimed at establishing if UGAFOD Micro Finance Institution administered the credit facility to ensure orderly and full payment.

Table 4.27: UGAFOD Micro Finance administers the credit facility to ensure orderly and full payment

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	72	20.0	20.0	20.0
	Undecided	11	3.1	3.1	23.1
	Agree	205	56.9	56.9	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: primary data

The statistics on this indicate that UGAFOD Micro Finance Institution administers the credit facility to ensure orderly and full payment. This is because the majority of the respondents 56.9% agreed 20.0% strongly, 3.1% were undecided and 20.0% disagreed.

Table 4.28: UGAFOD Micro Finance administering the credit facility to ensure orderly and full payment

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	38	10.6	10.6	10.6
	Disagree	73	20.3	20.3	30.8
	Undecided	59	16.4	16.4	47.2
	Agree	120	33.3	33.3	80.6
	Strongly agree	70	19.4	19.4	100.0
	Total	360	100.0	100.0	

Source: primary data

As to whether UGAFOD Micro Finance Institution ensured the value of collateral is updated periodically to account for changes in market ensures loan recovery, the larger number of the respondents 46.9% agreed, 19.7% strongly agreed, 13.3% were un decided and 20.0% disagreed. This means that UGAFOD Micro Finance Institution administers the credit facility to ensure orderly and full payment and this helps in recovery of the loans.

During the interviews, the staff of UGAFOD Micro Finance Institution explained that UGAFOD Micro Finance Institution administers the credit facility to ensure orderly and full payment through the making of daily reports. This helps in ensuring that there is compliance with the credit policy and facilitates security perfection. The administering of the credit facilities ensures all terms or covenants are adhered to from the onset of disbursement. This enables UGAFOD Micro Finance Institution to take appropriate action in case early warning signs of delinquency are observed. The ultimate result is better quality asset book for the lending institution. In case of the client begins to show signs of failure to repay, he or she can be easily followed up hence enabling recovery of the money.

Finding that UGAFOD Micro Finance Institution administering the credit facility to ensure orderly and full payment helps in the recovery of lent out money agrees with the views presented by other scholars. McNaughton (1996) explains that credit risk control involves measuring and containing individual credit risk within strategic guidelines. It involves the administration of the credit facility to ensure orderly and full payment, monitoring of the credit facilities as well as the workout strategies in situations when credits actually deteriorate. This means that credit facility administration helps in the recovery loans.

4.5.2 Monitoring the financial situation of clients and loan repayment

On this item, the respondents were asked to tell if UGAFOD Micro Finance Institution monitored the financial situation of clients and UGAFOD Micro Finance Institution monitoring of the financial situation of clients made them repay.

Table 4.29: UGAFOD Micro Finance monitors the financial situation of clients

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	31	8.6	8.6	8.6
	Disagree	166	46.1	46.1	54.7
	Undecided	25	6.9	6.9	61.7
	Agree	52	14.4	14.4	76.1
	Strongly agree	86	23.9	23.9	100.0
	Total	360	100.0	100.0	

Source: primary data

Regarding UGAFOD Micro Finance Institution monitoring the financial situation of clients, the larger number of the respondents 46.1% disagreed, 8.6% strongly disagreed and 6.9% were undecided. The remaining 23.9% and 14.4% strongly agreed and agreed respectively.

Table 4.30: UGAFOD Micro Finance monitoring the financial situation of clients makes them repay

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	23	6.4	6.4	6.4
	Disagree	132	36.7	36.7	43.1
	Undecided	60	16.7	16.7	59.7
	Agree	85	23.6	23.6	83.3
	Strongly agree	60	16.7	16.7	100.0
	Total	360	100.0	100.0	

Source: Primary data

On whether UGAFOD Micro Finance Institution monitoring the financial situation of clients made them repay, still the larger number of the respondents 36.7% disagreed, 6.4% strongly disagreed and 16.7% were undecided. Those who agreed were 23.6% and 16.7% strongly agreed. These statistics mean that UGAFOD Micro Finance Institution did not monitor the financial situation of clients and UGAFOD Micro Finance Institution monitoring of the financial situation of clients and so this was not a guarantee for repayment.

However, whereas during the interviews the clients indicated that UGAFOD Micro Finance Institution did not monitor their financial situation except when they start to fail to deposit the monthly instalments, the staff of lending institution gave views that differed from those of the clients. When the staff of UGAFOD Micro Finance Institution was asked to tell how they monitored the financial situation of the clients, they generally indicated that this is done by requesting for management and audited accounts for a given period. As to how this helped in the repayment of loans, it was indicated that monitoring of financial situation of clients enables UGAFOD Micro Finance Institution to keep to tabs on the clients ability to repay the loan and is also a source of information to show progress made.

The monitoring process also reveals whether the credit facility was utilised for the indeed purpose. However, during the interviews with the clients, it was generally pointed out that whereas monitoring their financial situation would be good to keep them on their toes, UGAFOD Micro Finance Institution staff only monitors them when there are repayment problems. Otherwise as long as one is still able to fulfil their loan obligations, they are not monitored. This means that there was poor monitoring of the financial situations of the clients but if it was perfected, it would help in the repayment of the loans.

The finding that monitoring the financial situation of clients helps in the repayment of the loans concurs with the views of other scholars. According to Richard (2006), credit risk control involves the management of the client's financial situation, covenants, collateral and payments as well as credit review. It focuses on ensuring that credit worthiness of the clients earlier established is maintained. Once a loan is on the books of the lending institution, it must be managed actively to ensure that it does not deteriorate and it is repaid. Good loan management can rarely overcome poor judgment but many good credits become problem loans because lending officials did not heed to the warnings that arose over time. This as with the finding of the study reveals that administering the financial situation of the clients helps in repayment of the loans.

4.5.3 Regular inspection of the activities of the clients and Repayment

This item sought to establish if UGAFOD Micro Finance Institution carry out regular inspection of the activities of the clients.

Table 4.31: UGAFOD Micro Finance carries out regular inspection of the activities of the clients

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	36	10.0	10.0	10.0
	Disagree	162	45.0	45.0	55.0
	Undecided	12	3.3	3.3	58.3
	Agree	72	20.0	20.0	78.3
	Strongly agree	78	21.7	21.7	100.0
	Total	360	100.0	100.0	

Source: Primary data

On this, the larger number of the respondents 45.0% disagreed, 10.0% strongly disagreed and 3.3% were undecided. Those who agreed 20.0% and 21.7% strongly agreed.

Table 4.32: UGAFOD Micro Finances carrying out regular inspection of the activities of the clients makes them pay

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	57	15.8	15.8	15.8
	Disagree	83	23.1	23.1	38.9
	Undecided	32	8.9	8.9	47.8
	Agree	116	32.2	32.2	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: Primary data

As to whether the lending institutions carrying out regular inspection of the activities of the clients made them pay, the larger number of the respondents 32.2% agreed, 20.0% strongly agreed and 8.9% were undecided. Those who disagreed 23.1% and 15.8% strongly disagreed. Whereas the respondents to a large extent disagreed that UGAFOD Micro Finance Institution did not carried out regular inspection of the activities of the clients, it is clear according to these statistics that these customers believe that if there is regular inspection would be encouraged to repay their loans.

The need for regular inspection of the clients is supported by other scholars. Greuning et al, (2009) outlines that importance of inspection of the clients. He indicates that during inspection credit officers check compliance with the covenants in the loan agreement, cross check the status of the collateral and obtain asymmetric information from customers. Further Cope (1994) explains that t the monitoring and recovery process is one, which is simple, but at the same time very difficult to successfully implement. Accordingly, this process involves constant reconciliation by UGAFOD Micro Finance Institution of the customers' mortgage loan account (monitoring service trends) with project site visit reports and exhibited customer cooperation. The idea is to constantly remind the client of the fact that funds in his hands belongs to somebody else and must be repaid back within a stipulated time (Fratantoni and Schuh, 2009). This thus encourages repayment of the loans.

4.5.4 Rescheduling of loans and easy repayment of loans

This item sought to establish if UGAFOD Micro Finance Institution controlled credit risk through rescheduling of the loans to make it easy for the customers to repay. Concerning the rescheduling of loans, all the respondents agreed that it existed.

Table 4.33: There is rescheduling of loans

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	216	60.0	60.0	60.0
	Strongly agree	144	40.0	40.0	100.0
	Total	360	100.0	100.0	

Source: primary data

The majority of 60.0% agreed and the remaining 40% strongly agreed.

Table 4.34: Rescheduling of loans makes it easy for debtors to repay their loans

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	23	6.4	6.4	6.4
	Disagree	58	16.1	16.1	22.5
	Undecided	44	12.2	12.2	34.7
	Agree	161	44.7	44.7	79.4
	Strongly agree	74	20.6	20.6	100.0
	Total	360	100.0	100.0	

Source: primary data

As to whether the rescheduling of loans makes it easy for debtors to repay their loans, still the respondents were in agreement. The majority of 44.7% agreed, 20.6% strongly agreed, 16.1% were undecided and only 6.4% were undecided. This means that there is the rescheduling of loans and this makes it easy for debtors to repay their loans.

During the interviews, the respondents indicated that rescheduling of loans is carried when the client applies for rescheduling and provides genuine reasons backed with documentary evidence and UGAFOD Micro Finance Institution is comfortable, the loan is rescheduled. The importance of rescheduling accordingly is that it gives a breather to the client to be able to stabilise and pay the loan on newly agreed time. Accordingly, this grants the customer the opportunity to realise or to save some money off repayments in cases of financial stress. This flexibility enables customers to repay.

The finding that rescheduling of loans grants the customer the opportunity to realise or to save some money off repayments in cases of financial stress and be able to repay is agreed to by other scholars. The Lending institutioning Policy Department (2009) outlines that rescheduled loans" refer to loans that have been restructured and re-negotiated between authorised institutions and borrowers because of deterioration in the financial position of the borrower or of the inability of

the borrower to meet the original repayment schedule. Accordingly, rescheduling of loans takes place when there is reasonable assurance that the borrowers was able to service all future principal and interest payments on the loans in accordance with the revised repayment terms. The fact that rescheduling of takes place when there is reasonable assurance that the borrowers was able to service all future principal and interest payments on the loans in accordance with the revised repayment terms indicates that rescheduling helps in controlling credit risk.

4.5.5 Strict to regulations in granting loans and recovery of loans

This item aimed at establishing if the staff is keen to the rules such that risk is controlled.

Table 4.35: UGAFOD Micro Finance is strict to regulations in granting loans

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	72	20.0	20.0	20.0
	Agree	216	60.0	60.0	80.0
	Strongly agree	72	20.0	20.0	100.0
	Total	360	100.0	100.0	

Source: primary data

To the question that lending institution is strict to regulations in granting loans, the majority of the respondents 60.0% agreed, 20.0% strongly agreed and only 20.0% disagreed.

Table 4.36: UGAFOD Micro Finance being strict to regulations in granting loans ensures recovery

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	45	12.5	12.5	12.5
	Disagree	89	24.7	24.7	37.2
	Undecided	12	3.3	3.3	40.6
	Agree	118	32.8	32.8	73.3
	Strongly agree	96	26.7	26.7	100.0
	Total	360	100.0	100.0	

Source: primary data

As to whether UGAFOD Micro Finance Institution being strict to regulations in granting loans ensures recovery, still the majority of the respondents were in agreement with 32.8% and 26.7% agreeing and strongly agreeing respectively. Only 3.3% the respondents were undecided, 24.7% disagreed and only 12.5% strongly disagreed. These results mean that UGAFOD Micro Finance Institution is strict in adherence to the regulations in granting loans and this enabled the recovery of loans.

In the interviews, the staff of UGAFOD Micro Finance Institution was asked to tell the regulations UGAFOD Micro Finance Institution followed in granting loans. They pointed out that UGAFOD Micro Finance Institution follows the credit policy, Lending institution of Uganda regulations, Financial Institutions Act and the Mortgage Act and other statutory instruments issued from time to time such as the recent Consumer Protection Act. Apparently, the importance of strictly following regulations in the granting of loans is that it safeguards depositors' funds and prevents lending institution closures. Ensures compliance with the law to avoid penalties imposed by the regulator, minimise litigation and encourage corporate governance. And it also ensures security perfection such that UGAFOD Micro Finance Institution is sure that the customer was able to fulfil his or repayment requirements. This means that strictly following the regulations in the granting of loans helps in the recovery of loans as there is security perfection.

The finding that following the regulations in the granting of loans helps in the recovery of loans agrees with the Guidelines for A registered lending institutions of the State lending institution of Pakistan (2010). Accordingly, lending institutions need to set limits, including operational limits, for the different trading desks and/or traders which may trade different products, instruments and

in different markets, such as different industries and regions. Limits need to be clearly understood, and any changes clearly communicated to all relevant parties. Risk Taking Units must have procedures that monitor activity to ensure that they remain within approved limits at all times. This means that strictly following the procedures that monitor activity to ensure that they remain within approved limits at all times help in control risk hence recovery of loans.

4.5.6 Research Hypothesis Three Testing: Credit risk control affects the performance of the loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

This hypothesis was obtained from objective two of the study that sought to establish the effect of credit risk control on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch. The test was carried out on the Null Hypothesis (Ho) which stated that credit risk controls have no effect on the performance of the loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch.

This hypothesis analysed items 11 – 15 of the questionnaire that were correlated with items 26 – 30. The items of study included if UGAFOD Micro Finance Institution administers the credit facility to ensure orderly and full payment, lending institution monitors the financial situation of clients, carries out regular inspection of the activities of the clients, rescheduling of loans and is strict to regulations in granting loans. These were analysed in correlation with ensuring orderly and full payment, making it easy for debtors to repay their loans and ensuring recovery.

Table 4.37: The Correlation between Credit Risk Controls and the Performance of the Loan Portfolio

		the effect of credit risk control	loan portfolio performance
The effect of credit risk control	Pearson Correlation	1	.725
	Sig. (2-tailed)	.	.000
	N	360	360
Loan portfolio performance	Pearson Correlation	.725	1
	Sig. (2-tailed)	.000	.
	N	360	360

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

Table 4.7 shows that the value of the co – efficient equals to .725. This value is positive and it means that there is a strong positive relationship between credit risk controls and the performance of the loan portfolio. The sig. value for the correlation was equal to .000 which was less than the level of significance (.05) which led to the rejection of the null hypothesis that credit risk controls have no effect on the performance of the loan portfolio. Thus the results indicate that credit risk controls significantly affects the performance of the loan portfolio.

4.5.7 Discussion of Results

The general objectives of the study was to establish the impact of credit extension on loan portfolio performance of UGAFOD and specific objectives were to establish impact of credit assessment, implementation and risk control on loan portfolio performance. The result of the study showed d that credit extension is an important predictor of loan portfolio performance thus success of financial institutions performance depends largely on the level of credit extension management.

The study results also showed that default rate as one of the risk management indictors is a major predictor of the loan portfolio performance to the extent of 56% and followed by capital adequacy ratio at 25%. Credit risk management is crucial on the lending institution performance since it have a significant relationship with lending institution performance and contributes up to 22.6% of the lending institution performance. Among the risk management indicators, default rate management is the single most important predictor of the lending institution performance whereas cost per loan assets is not significant predictors of lending institution performance.

Since risk management in general has very significant contribution to lending institution performance, the lending institutions are advised to put more emphasis on risk management. In order to reduce risk on loans and achieve maximum performance the lending institutions need to allocate more funds to default rate management and try to maintain just optimum level of capital adequacy. Based on the study other factors not studied in this research has a very significant contribution of 77.4% to lending institution performance therefore require further research to efficiently manage the credit risk hence improve loan portfolio performance.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents the findings or research outcomes, the recommendations and suggested areas of further research. The conclusions reached and recommendations suggested by the study are drawn in alignment with the objectives and research questions/hypotheses.

5.2 Summary of Findings

5.2.1 Objective One: The effect of credit risk assessment on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

The study findings revealed that through credit assessment measures like character, ability, margins, purpose, amount repayment and insurance, UGAFOD Micro Finance Institution limits risk. This helps in confirming to UGAFOD Micro Finance Institution that one is in position to repay the loan hence limiting risk. Also, when UGAFOD Micro Finance Institution has a credit risk assessment methodology there is improvement the performance of loans. Strategies of risk assessment methodology that help UGAFOD Micro Finance Institution include the credit policy, risk grading, insurance, valuing collateral, credit scoring and the financial models such as assessing market risk, Value-at-Risk, validation, liquidity risk, leverage, systemic risk and financial regulation. Good assessment results into a high likelihood of quality loan portfolio performance and vice versa. The risk assessment methodology of UGAFOD Micro Finance Ltd worked because the Non – Performing Assets (NPA) were only at 2% with performing Assets

(PA) at 98%. UGAFOD Micro Finance Institution carefully carrying out investigation, preparation of credit report and considering factors of selection of the borrower ensures better loans performance**.**

5.2.2 Objective Two: The effect of credit monitoring on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

Credit monitoring affects loan portfolio performance. The existence of an effective loans management monitoring system promotes good performance of loans. This involves monitoring borrowers' compliance with credit terms to avoid funds diversion and default. The monitoring system helps loans officers to keep tabs on its customers ensuring agreed schedules are adhered to. Monitoring methods of debt collection like sending delinquent letters, making telephone calls, foreclosures and employing debt collection agencies reduce loans default. These make the customers aware that UGAFOD Micro Finance Institution will take the necessary precautions to ensure that the loaned funds are recovered at all cost. This motivates them to pay outstanding monies or make efforts to pay loans. Warnings from UGAFOD Micro Finance Institution scare clients into looking for the lending institution's money such that they are embarrassed by attachment of my property. Frequent contact with borrowers and creating conducive environment as a solver of problems ensures loans repayment. Counsel from loans managers and some loan officers present them as problem solvers winning trust of the clients hence repayment.

However, proud loan officers that do not give a hearing to the customers scare them into avoiding going to UGAFOD Micro Finance Institution and switching off their phones when they have repayment problems. When UGAFOD Micro Finance Institution closely monitors the borrowers' respective activities, their performance, as well as behaviour it enables loans

recovery. This helps in ensuring that the borrower will continue to pay the debt owed to UGAFOD Micro Finance Institution and also provide professional advice while recovering the loan. UGAFOD Micro Finance Institution ensuring that the value of collateral is updated periodically ensures loan recovery. Monitoring helps to ensure that UGAFOD Micro Finance Institution is properly/sufficiently covered in terms of security, since it the secondary source of repayment. UGAFOD Micro Finance Institution thus does not need to wait to begin monitoring when the client is beginning signs of inability to repay.

5.2.3 Objective Three: The effect of credit risk control on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

Credit risk control affects loan portfolio performance. This is because, administering the credit facility to ensure orderly and full payment helps in recovery of the loans. It ensures that there is compliance with the credit policy and facilitates security perfection. The ultimate result is better quality asset book for the lending institution. In case the client begins to show signs of failure to repay, he or she can be easily followed up hence enabling recovery of the money. When UGAFOD Micro Finance Institution monitors the financial situation of clients, it helps in the repayment of the loans. The lending institutions by requesting for management and audited accounts for a given period of their customers they are able to control risk. Lending institutions do no need to wait to monitor the financial situation of the clients when they start to fail to deposit the monthly instalments.

Regular inspection of the activities of the clients by UGAFOD Micro Finance Institution helps in repayment. Also as a risk control measure, rescheduling of loans makes easy repayment of

loans. The rescheduling gives a breather to the clients to be able to stabilise and pay the loan on newly agreed time. It grants the customer the opportunity to realise or to save some money off repayments in cases of financial stress. And when UGAFOD Micro Finance Institution is strict in adherence to the regulations in granting loans, it enables the recovery of loans. This involves the adherence to the credit policy, Lending institution of Uganda regulations, Financial Institutions Act and the Mortgage Act and other statutory instruments issued from time to time such as the recent Consumer Protection Act. These safeguards depositors' funds preventing lending institution closures and ensure security perfection such that UGAFOD Micro Finance Institution is sure that the customer was able to fulfil his or repayment requirements.

5.3 Conclusions

The study focused on analyzing the effect of credit extension on loan portfolio performance in micro credit institutions, using UGAFOD Micro Finance Institution- Mpigi branch as the case study. The results indicated that though there are some problems faced by both the microfinance managers and the overall intended beneficiaries, these have not been prohibitive enough to do away with UGAFOD microfinance services.

What is actually needed, the researcher believes is to find a way to improve service delivery through lower interest rates, extended pay back period and flexing of the strict credit extension conditionality, product differentiation, customer segmentation, and improved information technology. When all this is done, more people may be in position to access UGAFOD micro finance services for better living standards.

To sum up, the performance of loans in UGAFOD portfolios has improved significantly, albeit unevenly, since the end of the 2009-12 recession. Differences in performance across major loan

categories reflect key features of the recession itself, in particular the central role played by the collapse in real estate prices and fall in personal consumption. In the future, the tighter underwriting standards applied to more recent loan cohorts would suggest that the fraction of nonperforming loans may continue to fall over time, as earlier loan vintages become a progressively smaller share of bank portfolios. As in recent history, however, macroeconomic and financial market conditions are likely to be the main determinant of bank loan performance going forward.

5.4 Recommendations

The study makes the following important recommendations from the findings of the study in relation to the observations made from the findings of the study;

5.4.1 Objective One: Examine the effect of credit risk assessment on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

Lending institutions need to strictly assess their clients to c eliminate Non Performing Assets. Risk assessment measures limits risk, risk assessment methodologies like the credit policy, risk grading, insurance, valuing collateral, credit scoring and the financial models such as assessing market risk, Value-at-Risk, validation, liquidity risk, leverage, systemic risk and financial regulation result into a high likelihood of quality loan portfolio performance and vice versa. Lending institutions should carefully carry out investigation, preparation of credit report and considering factors of selection of the borrower. Carefully carrying out investigations, preparing credit reports and considering factors of selection of the borrower ensures better loans performance. This is because customers can be easily graded and helps in the levying interest rates reducing chances of loss by the lending institution.

5.4.2 Objective Two: Assess the effect of credit monitoring on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

Credit monitoring should be vigilantly implemented for better performance of the loan portfolio. Some aspects of the monitoring system were merely on paper and staff of UGAFOD Micro Finance Institution did not carry out the monitoring as required. The staff of UGAFOD Micro Finance Institution did not ensure that the borrowed money is put the actual use and even monitor the progress of the projects. Monitoring of UGAFOD Micro Finance Institution only begins when one has started to default. The staff of UGAFOD Micro Finance Institution also needs to create an environment that UGAFOD Micro Finance Institution can be seen as a solver of problems and trusted adviser this is because some of the loan officers were proud and did not give a hearing to the customers. When UGAFOD Micro Finance Institutionkeeps in contact with the customers and presents itself as a problem solver, it can be trusted hence encouraging repayment.

5.4.3 Objective Three: Establish the effect of credit risk control on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch

Credit risk control needs to be fully implemented. Credit risk control affects loan portfolio performance. Administering the credit facility to ensure orderly and full payment helps in recovery of the loans. It ensures that there is compliance with the credit policy and facilitates security perfection. When UGAFOD Micro Finance Institution monitors the financial situation of clients, it is able to keep them on track. Lending institutions do no need to wait to monitor the financial situation of the clients when they start to fail to deposit the monthly instalments.

5.5 Suggested Areas of further Research

The study only analysed the effect of credit extension on loan portfolio performance in UGAFOD Micro Finance Ltd, Mpigi Branch. There are many more areas which may be studied and these include: internal control and performance of a registered lending institution, factors affecting implementation of internal controls in fraud prevention, Auditing procedures and control systems and Productivity and competitiveness.

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APPENDICES

APPENDIX I: QUESTIONNAIRE FOR THE RESPONDENTS

Uganda Management Institute
P.O. Box 20131
Kampala

Dear Respondent;

I am currently undertaking research on the topic "Analysis of the Effect of credit risk management on loan portfolio performance in micro finance institutions in Mpigi district, using a case study of UGAFOD Micro Finance institution – Mpigi Branch for the award of Master of Management Studies of Uganda Management Institute.

You have been selected to participate in this study because you have necessary information and knowledge related to the study. The information sought is required only for academic purposes. Participation is entirely out of your free will and necessary for the success of this work. Information provided will be treated with maximum confidentiality.

………………..

Kayongo Rachael Violet
MMS- UMI

RESPONSES TO THE QUESTIONNAIRE

SECTION (A): Background

Tick or write in the space provided the alternative of your choice.

1. Gender: Male ☐ Female ☐
2. Level of education: a. Masters Degree ☐ b. Bachelors Degree ☐
   c. Diploma in Education ☐
   Others specify......................... ....
3. Role with UGAFOD Micro Finance
   a. Top management level ☐ b. Middle Management Level ☐
   c. Lower Management Level ☐ d. Client ☐
4. Duration with UGAFOD Micro Finance
   a. 1 – 5 years ☐ b. 6 – 10 years ☐
   c. 11 – years ☐

SECTION B: Tick in the spaces provided according to your feeling about the Item

I Strongly Disagree	I Disagree	I am Undecided	I Agree	I Strongly Agree
1	2	3	4	5

S.No	**Items**	**1**	**2**	**3**	**4**	**5**
	The Independent Variables					
1	UGAFOD Micro Finance tries to limit risk taking as it offers it offers loans					
2	UGAFOD Micro Finance has established the credit risk assessment methodology					
3	UGAFOD Micro Finance staff carefully carry out investigation, preparation of credit report and consider factors of selection of the borrower at UGAFOD Micro Finance					
4	Banks have a credit grading system					
5	The loan credited depends on the individual's credit grade					
6	UGAFOD Micro Finance has an affective loans management monitoring system					
7	UGAFOD Micro Finance sends delinquent letters, telephone calls, foreclosures and employs debt collection agencies					
8	Does the staff of UGAFOD Micro Finance carry out frequent contact with borrowers, creating an environment that UGAFOD Micro Finance can be seen as a solver of problems and trusted adviser					
9	The borrowers' respective activities, their performance, as well as behaviour are closely monitored					
10	UGAFOD Micro Finance ensures the value of collateral is updated periodically to account for changes in market conditions					
11	UGAFOD Micro Finance administers the credit facility to ensure orderly and full payment					
12	UGAFOD Micro Finance monitors the financial situation of clients					
13	UGAFOD Micro Finances carries out regular inspection of the activities of the clients					

14	There is rescheduling of loans					
15	UGAFOD Micro Finance is strict to regulations in granting loans					
	Dependent Variables					
16	The limiting risk taking in the offering of loans enables good loans performance					
17	Establishment of the credit risk assessment methodology improved performance of loans					
18	UGAFOD Micro Finance staff carefully carrying out investigation, preparation of credit report and consider factors of selection of the borrower have helped to ensure better loans performance.					
19	The credit grading system of UGAFOD Micro Finance enables easy recovery of loans					
20	Offering loans depending on the individual's credit grade has helped in loans management					
21	UGAFOD Micro Finance's loans management monitoring system helps in the performance of loans					
22	Has the sending of delinquent letters, telephone calls, sending foreclosures and employing debt collection agencies help in reducing loans default.					
23	UGAFOD Micro Finance being supportive to clients finding difficulty in loans repayments encourages them to repay					
24	The monitoring of the borrowers' respective activities, their performance, as well as behaviour enables loans recovery					
25	UGAFOD Micro Finance ensuring the value of collateral is updated periodically to account for changes in market ensures loan recovery					
26	UGAFOD Micro Finance administering the credit facility to ensures orderly and full payment					
27	UGAFOD Micro Finance monitoring the financial situation of clients makes them repay					
28	UGAFOD Micro Finances carrying out regular inspection of the activities of the clients makes them pay					
29	Rescheduling of loans makes it easy for debtors to repay their loans					
30	UGAFOD Micro Finance being strict to regulations in granting loans ensures recovery					

APPENDIX II: INTERVIEW GUIDE

1. What is the impact of limiting risk performance on loan performance?
2. What is the credit risk assessment methodology of UGAFOD Micro Finance?
3. How does the credit risk assessment methodology of UGAFOD Micro Finance affect the performance of the loan portfolio?
4. What is the performance and non-performance rate of loans at UGAFOD Micro Finance?
5. How is use of a grading system in the offering of loans important in the performance of loan portfolio?
6. Does UGAFOD Micro Finance's loans management monitoring system help in the performance of loans?
7. Does the system of tracking of borrowers' compliance with credit terms promote better loan portfolios performance?
8. Does UGAFOD Micro Finance's sending of delinquent letters, telephone calls, foreclosures and employing debt collection agencies help in reducing default on loans?
9. Is UGAFOD Micro Finance carrying out frequent contacts with borrowers, creating an environment that UGAFOD Micro Finance is a solver of problems and trusted adviser which helps in loans repayment?
10. Why does UGAFOD Micro Finance monitor the borrowers' respective activities, performance, as well as behaviour?
11. Why does UGAFOD Micro Finance periodically update the value of collateral to account for changes in market conditions?
12. How does the administering of credit facility help in ensuring orderly and full loan repayment?
13. How does monitoring the financial situation of clients help in the repayment of loans?
14. What is the importance of carrying out loan rescheduling?
15. What regulations does that bank follow in the granting of loans?
16. What is the importance of strictly following regulations in the granting of loans?

APPENDIX III: R E L I A B I L I T Y   A N A L Y S I S - S C A L E (A L P H A)

	Mean	Std Dev	Cases
Q1	4.6000	.5071	15.0
Q2	3.6000	1.0556	15.0
Q3	3.2000	1.0142	15.0
Q4	4.2000	1.2071	15.0
Q5	3.4000	1.2421	15.0
Q6	3.1333	1.5976	15.0
Q7	3.8000	.9411	15.0
Q8	3.2667	1.4376	15.0
Q9	3.6000	1.0556	15.0
Q10	3.0000	1.7321	15.0
Q11	3.6667	1.0465	15.0
Q12	2.2000	1.5213	15.0
Q13	3.0000	1.3093	15.0
Q14	4.4000	.0142	15.0
Q16	3.7333	1.1629	15.0
Q17	3.6000	1.8048	15.0
Q18	2.4000	1.4041	15.0
Q19	3.2667	1.0328	15.0
Q20	2.4667	1.7674	15.0
Q21	2.4667	1.4075	15.0
Q22	3.0667	1.5337	15.0
Q23	3.3333	1.3452	15.0
Q24	2.7333	1.5796	15.0
Q25	3.3333	1.0465	15.0
Q26	2.2000	1.3202	15.0
Q27	3.4000	1.4041	15.0
Q28	3.2667	1.2228	15.0
Q29	3.0667	1.5337	15.0
Q30	3.3333	1.4960	15.0

R E L I A B I L I T Y   A N A L Y S I S - S C A L E (A L P H A)

N of Cases = 15.0

Item Means	Mean	Minimum	Maximum	Range	Max/Min	Variance
	3.2844	2.2000	4.6000	2.4000	2.0909	.3479

Item Variances	Mean	Minimum	Maximum	Range	Max/Min	Variance
	1.7244	.2571	3.2571	3.0000	12.6667	.5920

Inter-item

Correlations	Mean	Minimum	Maximum	Range	Max/Min	Variance
.3093	-.8807	.9932	1.8739	-1.1277	.1264	

Reliability Coefficients 30 items

Alpha = .9257 Standardized item alpha = .9307

APPENDIX IV: VALIDITY OF THE QUESTIONNAIRE

Judges	Relevant	Irrelevant
Judge 1	27	5
Judge 2	29	3
32		

CVI = 27+29 = 58 ÷2 = 29

29÷ 32 = 0.906

APPENDIX V: VALIDITY OF THE INTERVIEW GUIDE

Judges	Relevant	Irrelevant
Judge 1	14	3
Judge 2	13	4
17		

CVI = 14+13= 27 ÷2 = 13.5

13.5 ÷ 17 = 0.794

APPENDIX VI: DETERMINING SAMPLE SIZE FROM A GIVEN POPULATION

Table 3.2 : Small Sample Technique for Selection of Sample

N	*S*	*N*	*S*	*N*	*S*
10	10	220	140	1200	291
15	14	230	144	1300	297
20	19	240	148	1400	302
25	24	250	152	1500	306
30	28	260	155	1600	310
35	32	270	159	1700	313
40	36	280	162	1800	317
45	40	290	165	1900	320
50	44	300	169	2000	322
55	48	320	175	2200	327
60	52	340	181	2400	331
65	56	360	186	2600	335
70	59	380	191	2800	338
75	63	400	196	3000	341
80	66	420	201	3500	346
85	70	440	205	4000	351
90	73	460	210	4500	354
95	76	480	214	5000	357
100	80	500	217	6000	361
110	86	550	226	7000	364
120	92	600	234	8000	367
130	97	650	242	9000	368
140	103	700	248	10000	370
150	108	750	254	15000	375
160	113	800	260	20000	377
170	118	850	265	30000	379
180	123	900	269	40000	380
190	127	950	274	50000	381
200	132	1000	278	75000	382
210	136	1100	285	1000000	384

Note.—*N* is population size.