

ST. MARY'S UNIVERSITY COLLEGE  
BUSINESS FACULTY  
DEPARTMENT OF MANAGEMENT

**EVALUATION OF CREDIT RISK MANAGEMENT  
PRACTICE: THE CASE OF DASHEN BANK S.C**

BY

NIGATUA TAFERE

JUNE 2011  
SMUC  
ADDIS ABABA

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PRACTICE THE CASE OF DASHEN BANK S.C**

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**By**

**Nigatua Tafere**

**JUNE 2011  
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**By**

**Nigatua Tafere**

**Faculty of Business  
Department of Management**

**Approved by the Committee of Examiners**

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**Chairperson**

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**Signature**

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**Advisor**

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**Signature**

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**Examiner**

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**Signature**

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**Examiner**

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**Signature**

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# **CHAPTER ONE**

## **INTRODUCTION**

### **1.1 BACKGROUND OF THE STUDY**

Credit risk management is exactly what it sounds like: monitoring risk within a company's or lender's operations. Credit risk management is an essential component of successful business ventures (especially in high finance), as it controls and guides a profitable business through transactions. Credit risk management has arguably existed since the beginning of banking. The underlying principle of banking is lending--and the underlying principle of lending is risk mitigation. Determining a borrower's ability and propensity to repay is essential to successful lending. As banking and finance have evolved, so has credit risk management (Jenkins, 2008:258).

Credit risk management is an important part of any business. A company assesses the investments and loans the company is committing to. The manager must think long-term and look critically at the soundness of each investment and loan as the company's financial health depends on safe, profitable investments. These credit risk managers not only look at the business's loans, they must also review and determine the soundness of the credit the company is extending to customers (Ibid).

With the development of sophisticated financial instruments--bonds, equity, swaps, futures--credit risk managers have had to evolve as well. These complex financial tools often involve many stakeholders--lenders, investors, shareholders. A successful credit risk manager is a savvy investor and money manager who can spot flaws in these instruments and determine the viability of a given transaction (Ibid).

## **1.2. Background of the Bank**

The bank is a privately owned company established in 1995 in accordance with the licensing and supervision of banking business Proclamation No. 84/1994 of the Ethiopia to undertake commercial banking activity. The bank obtained its license from the national bank of Ethiopia on 20 September 1995 and started normal business activities on 1 January 1996. It operates through its head office in Addis Ababa and 58 area banks established within and outside Addis Ababa, 5 foreign exchange Bureaus, 669 point of sale (POS) terminals and 55 automatic teller machines (ATM) installed at different places within and outside Addis Ababa (Annual report of the Bank, 2009).

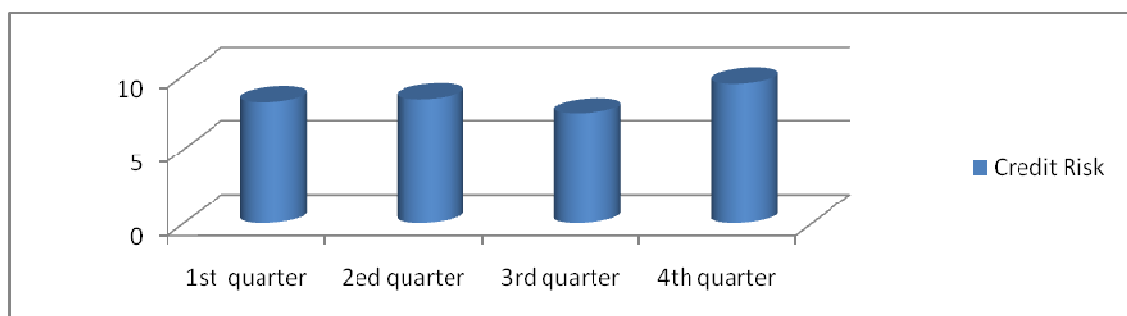
Dashen bank is “Ras Dashen”. It is the highest mountain of Ethiopia. It is also the habitat of rare wild animals, the Walia Ibex, the Gelada Baboon, and the Lammergeyer the beautiful bone breaker eagle. These unique characteristics of the mountain coincided with the interest of the founders of the Bank and prompted the founders to adopt this great name and epitomize their aspiration. Rightly, reaching the top of banking business in a dynamic and competitive business environment symbolized the highest peak, while the unique and efficient services the bank caters for the public through state-of-the-art computer technology and carefully selected and trained man-power equated with the rare wild animals (Ibid).

In cognizance of the fact that the bank’s sustainable growth is very much dependent on its human capital, it has been successful in providing various in-house and external trainings to a considerable number of staff, making good use of the educational assistance given by the bank, over 525 employees have been attending extension classes during the year. By the end of the fiscal year, the staff strength of the bank stood at 2,541 after having net addition of 292 employees (Ibid).

### 1.3 Statement of the Problem

If risks are improperly assessed prioritized and managed, time can be wasted in dealing with risk of losses that are not likely to occur. Spending too much time assessing and managing unlikely risks can divert resources that could be used more profitably. Unlikely events do occur but if the risk is unlikely enough to occur it may be better to simply retain the risk and deal with the result if the loss does in fact occur. The primary justification for a formal risk assessment process is legal and bureaucratic in most organizations. Prioritizing the risk management processes too highly could keep an organization from ever completing a project or even getting started. This is especially true if other work is suspended until the risk management process is considered complete.

Nevertheless, Dashen Bank has its own risk management department which is responsible for handling of credit risk which occurs in during service delivery operation of the bank. This department couldn't make assessment of different risks as per their potential severity of loss and to the probability of occurrence. This makes the credit risk management practice of the bank complicated and result maximum rate of risk of loss especially credit risk, perhaps it is also due to improper identification of risk and absence of appropriate risk management plan in different type of risks. The following chart indicates the NPL's position of the bank's during the last four quarters (1<sup>st</sup> quarter-8.4, 2<sup>nd</sup> quarter-8.6, 3<sup>rd</sup> quarter-7.2 and 4<sup>th</sup> quarter 9.4)



Thus, this study is to evaluate and investigate credit risk management practice of Dashen Bank and confirm the magnitude and /or significance of the problem.

## **1.4 Basic Research Questions**

To address the problem mentioned, this study answer the following basic research questions:

- Dose the bank has appropriate credit risk management policies and procedure?
- What kinds of mechanisms are used by the bank to handle credit risk?
- What kind of credit risk management orientation is followed by the bank?
- What are the factors affecting proper credit risk management of the bank?

## **1.5 Objectives of the Study**

### **1.5.1 General Objective**

The general objective of the study is to evaluate credit risk management practice of Dashen Bank. So to recommend, on how problems related to the subject can improved.

### **1.5.2 Specific Objective**

- To identify whether the bank has appropriate credit risk management policies and procedure or not.
- To examine the mechanisms used by the bank to handle credit risk.
- To identify the kind of credit risk management orientation followed by the bank.
- To examine factors affecting proper credit risk management of the bank.

## **1.6 Significance of the Study**

This study has a great contribution in providing important feedback to Dashen Bank regarding their credit risk management practice. Moreover, the study can be the source of information for some other study conducted under similar or related area. It can also provide an experience for the researcher future carrier.

## **1.7 Delimitation or Scope of the Study**

This study was conducted only the Head office of the Bank particularly risks management and credit department which is located around Bekelobet in Addis Ababa. Since it is difficult to address all employees in the head office, the study delimit itself only sample respondents. Moreover, the study collect, analyze and interpret data form 2009 to 2010.

## **1.8 Research Design and Methodology**

### **1.8.1. Research Design**

The research is designed and accordingly conducted using survey methodology and it is descriptive in its nature.

### **1.8.2 Population and Sampling Technique**

Employees in the head office department of risk management were considered as population of the study. Since the number of employees in the departments is manageable i.e. 39 the study were use all of employees as respondents. And also 20 credit customers were taken as sample respondents using accidental sampling technique.

### **1.8.3 Type Of Data used**

The study was used both primary and secondary data to undertake the research. The primary data source is selected to get clear and effective first hand information from the employees and managers. Secondary data source include various books, magazines document of the bank such as quarterly credit management reports and other relevant written documents.

#### **1.8.4 Method of Data Collection**

In order to gather the required data, questionnaire and interview were used. Questionnaire was used because it helps in saving money and time for both the researcher and the workers; it also helps to gather vast information within limited period of time. On the other hand, Interview was made with the risk management bodies (Risk Department Manager & Credit Department Deputy Manager) that are responsible to oversee the topic under study.

#### **1.8.5. Method of Data Analysis**

To conduct the study, qualitative and quantitative research method were used. Qualitatively method used to describe qualitative data in logical manner where as in quantitative term express in number like table and percent were used to present, analyze and interpret the information obtained from respondents.

### **1.9 Limitation of the Study**

During conducting the study, some difficulties encountered in to the student researcher such as:

- Obtaining the required data from managers due to over crowded agenda.
- Time constraint is also pass serious problem over the study effectiveness

### **1.10 Organization of the Study**

The main body of the paper organized in to four chapters. Chapter one contains, introductory part such as, background of the study , statement of the problem, objectives of the study, research questions , significance of the study, delimitation of the study, the research design and methodology, and organization of the study. Chapter two, deals with review of related literatures. Data analysis and interpretation arranged in chapter three. The last chapter contains summary, conclusions and recommendations.

## **CHAPTER TWO**

### **REVIEW OF RELATED LITERATURE**

#### **2.1 WHAT'S "RISK MANAGEMENT"**

Risk management is attempting to identify and then manage threats that could severely impact or bring down the organization. Generally, this involves reviewing operations of the organization, identifying potential threats to the organization and the likelihood of their occurrence, and then taking appropriate actions to address the most likely threats (Gustavson S. 1998:21).

Traditionally, risk management was thought of as mostly a matter of getting the right insurance. Insurance coverage usually came in rather standard packages, so people tended to not take risk management seriously. However, this impression of risk management has changed dramatically. With the recent increase in rules and regulations, employee-related lawsuits and reliance on key resources, risk management is becoming a management practice that is every bit as important as financial or facilities management.

There are several basic activities which a nonprofit organization can conduct to dramatically reduce its chances of experiencing a catastrophic event that ruins or severely impairs the organization (Ibid).

#### **2.2 CONDUCTING A RISK MANAGEMENT ASSESSMENT**

Organizations should regularly undertake comprehensive, focused assessment of potential risks to the organization. This focused assessment should occur at least twice a year by a team of staff members representing all the major functions of the organization. The assessment should be carefully planned, documented and methodically carried out.

The most common risks are typically of the types listed below. Comprehensive checklists help a great deal to quickly review a wide range of organizational aspects. Other aspects require more careful review.

## **2.3 BEST PROTECTION: GOOD MANAGEMENT, PERSONNEL POLICIES AND INSURANCE**

### **Good Management:**

Efforts undertaken to manage an organization well also contribute to sound risk management. For example, a fully attentive board with a wide range of skills may be the most important guard against major threats to an organization. Careful strategic planning and effective supervision helps ensure organizational resources are closely aligned to accomplishing the organization's mission, and that staff and volunteers are treated fairly and comply with rules and regulations.

### **Up-to-date, Reviewed Personnel Policies:**

Every organization must have up-to-date policies which guide the relationships between staff and management. There has been a noticeable increase in lawsuits regarding wrongful termination, harassment and discrimination, disagreements about promotions or salary actions, etc. Parties to lawsuits include the organization, management and/or board members. Therefore, personnel policies must be reviewed at least once a year by an outside advisor who is an expert about all of the employee-related laws and regulations. Be sure that management is well versed about the policies. Typically, courts will interpret actions by organizational personnel as representative of the organization's preferred course of action and superseding related, documented policies.

### **Well-designed Insurance Coverage:**

For a broad and basic overview of insurance, you might first review this information and then invite an insurance agent (or better yet, an insurance broker) to visit your organization to provide you an overview of the types of



insurance typically sold to nonprofits. Note that many insurance professionals might not understand the nature of nonprofits. Therefore, you might first ask a few people from fellow nonprofits for references. As dreadful as it may sound, you must schedule two hours sometime during the year to close your door and study your insurance policies. Note *any* questions and pose them to your insurance professional. Ask him or her to provide you a written, clear description regarding any ambiguities and to do so on company letterhead with his or her signature.

Note that Directors and Officers Insurance (D & O, and covered in the above "Insurance against Liabilities" section) is increasingly considered because of the increasing number of lawsuits. In addition, D & O insurance helps attract highly experienced board members. Be sure your D & O insurance covers "insured vs. insured" which covers employee-related lawsuits and also covers ongoing costs to address a lawsuit (rather than paying only when the outcome of a lawsuit has been decided).

## **2.4 CLASSIFICATION OF RISK**

Risks may be classified in many ways; however there are certain distinctions that are particularly important to our purpose. The major categories of risk are: pure and speculative risks, fundamental and particular risks, static and dynamic risks, objectives and subjective risks (Gustavson S. 1998:5).

### **2.4.1 Pure and Speculative Risk**

Pure risk- is type of risk that exists when there is a chance of loss but not chance of gain. For instance the owner of a car faces a risk of collision loss, if collision occurs; he will suffer a financial loss. If there is no collision he will not be benefited. But speculative risk- is a type of risk that exists when there is a chance of gain as well as a chance of loss. Pure risks are always distasteful but speculative risk possesses some alternative features. It exists when there is uncertainty about an event that could produce either a profit or loss. In a situation involving speculative risk the society may be benefited even though the individual is hurt.

### **2.4.2 Fundamental and Particular Risks**

A fundamental risk is a risk affects the entire economy, or large number of persons or groups within the economy. It involves on losses that the impersonal in origin and consequences and they are group risks mostly caused by economic, social and political phenomena. On the other hand particular risk is a risk that affects only individuals and not the entire community. It involves loss that arises out individual events and is felt by a single individual rather than by the entire group (Gustavson S. 1998:7)

### **2.4.3 Static and Dynamic Risks**

Static risks are those risks, which would occur even if there were no changes in the economy these risks include losses caused by the regulations of the forces of nature or human errors. On the other hand, dynamic risks are those risks resulting from changes in the economy. The agreement is, changes in the price level, consumer tastes, income and outputs, and technology may cause financial losses to member of the economy. These are risks related with changes in human wants although these dynamic risks may affect a large number of individuals, they are generally considered less predictable than static risks, since they do not occur with any precise degree of regularity (Sonja B., 2003:4)

### **2.4.4 Objective and Subjective Risk**

Subjective risk refers to the mental state of an individual who experiences, uncertainty doubt or worry as to the outcome of a given event. It is essentially the psychological uncertainty that arises from an individual's state of mind. On the other hand objectives risks are defined as the relative variation of actual from expected losses. It is manly applicable to group of objective exposed to losses.

Objective risk can be statistically measured by some measure of dispersion, such as the standard deviation or coefficient of variation; it is an extremely useful concept for an insurer or a corporate risk manager (Ibid).

## **2.5 TYPES OF FINANCIAL RISK**

Financial risks, which this study specifically deals with, in turn comprise two types of risks. Pure risk including liquidity, credit and solvency risks- can result in loss for a Bank if they are not properly managed. Speculative risks, based on financial arbitrage, can result in a profit, if the arbitrage is correct or a loss if it is incorrect. Financial risks are subject to complex interdependencies that may significantly increase is normally exposed to currency risks, but also be exposed additionally to liquidity risk are interest rate, currency and market price risk (Sonja B.,2003:4).

### **2.5.1 Liquidity Risk**

Liquidity risk is a condition of an individual or business where in a high percentage of the assets can be quickly converted into cash without involving any considerable loss by accepting sacrifice prices. Liquidity implies a high degree of currentness and solvency in the equality sense; the ability of current assets will be able to meet current liabilities as they mature. Liquidity risk can also be defined as uncertain future outcomes that either improve or worsen the present liquidity position of the company. It may mean that holding idle cash on the hand or failure to meet financial commitments when they are due on the other.

Fund mobilization, fund application, quality service, branch expansion, and application of new technology are the critical issues that can be emphasised by management in minimizing liquidity risk. Fund raising is not limited to deposit mobilization. Borrowing and equity contribution are other sources of fund raising (Williams J. 1998:15).

## **2.5.2 Credit Risk**

Loan is the thing that is lent, specially a sum of money, the action lending something or the state of being lent". For each lender a loan is an investment comparable to bonds, stocks or other assets. On the other hand, for each borrower, a loan is a debt, an obligation to repay the borrowed money plus interest.

Banks grant loans to borrowers assuming that they will pay the agreed interest and principal amount according to their contractual agreement. However, the borrower may fail to do so. This results in non performing loans (NPL). Non- performing loans are those loans which are past their due dates. According Williams J. (1998:15) they are classified into three categories as shown below:

- 1. Sub-Standard:-** Non-performing loans or advances past due 90 days or more but less than 180 days shall at minimum be classified sub-standard.
- 2. Doubtful:** - Non –performing loans or advances past due 180 days or more but less than 360 days will be referred as doubtful.
- 3. Loss:** - Non-performing loans or advances past due 360 days or more will be classified as loss.

## **Causes of Credit Risk**

A bank is successful when the risks it takes are reasonable, controlled with in its financial resources and credit competence. The vital issues for preservation of the quality of loans are; existence of a well developed policies and procedures, strong portfolio of management, effective credit controls and well trained staff that is qualified to implement the system. Conversely, absence of adequate guidelines to monitor administration of the lending function pave the way for the occurrence of substantial amount of problem on loans there are many causes for the occurrence of credit risk. Some of these are the above listed factors and several others, which are sources of

failures in loans, entail financial losses, which impede growth of the Bank (Dashen Bank, 2003:4).

### **2.5.3. Foreign Exchange Risk**

The term foreign exchange refers to the simultaneous purchase of one currency and selling of another as currencies are traded in pair. Foreign exchange risk results from changes in exchange rates between a Bank's domestic currency and other currencies. It is a risk of volatility due to a mismatch and may cause a Bank to experience losses as a result of adverse exchange rate movements (Sonja B., 2003:6).

There are a number of factors that affect a foreign exchange market influencing the value of currencies. Some of these are: changes in interest rates of a currency affects the value of currencies in that the rise in interest rates of inflation that is the higher the rate of inflation, in the economy of a country, the lower will be the demand for the currency to result in decrease of the value. The country's economic and political stability have also an impact with the demand and supply of currency there by affecting the value. The more stable the political and economic condition of a country, the local currency will be strong, National Bank intervention in interest rates or exchange rates has an impact on value of currencies depending on the position taken by such bank, the larger the market orders for commodities, services or currencies which prevail in a given country, the more volatile will be foreign exchange rates depending on the level of supply.

### **2.5.4 Interest rate Risk**

According to Sonja B., (2003:6) Gardner interest rate risk refers to the exposure of an economic unit to movements in the market rates of interest. It is an important part of balance sheet management system, which is concerned with making the corporate trade-offs, striking the correct balance between profitability, liquidity and capital adequacy (solvency).

All financial institutions face interest rate risk. When interest rates fluctuate, a Bank's earnings and expenses, as well as the economic value of its assets, liabilities and balance sheet positions also change. This risk is by its nature a speculative type of risk since its consequences may result in a profit or loss.

## **2.6 Theoretical Models of Credit Risk Management**

Credit risk management can be a very analytical and statistical process. Theoretical models used to measure and manage credit risk are often complex and highly quantitative. Well before credit risk can be managed, it first must be measured. Detailed and accurate analytical work needs to be done by companies that have large numbers of credit counterparties and large dollar values of exposure. This kind of work is not limited to banks. Attempts to manage credit risk will fail if the analysis and models used to quantify the risk are executed poorly.

Models that measure and manage credit risk serve three main functions. First, these models are used to estimate the likelihood that counterparty will default, or fail to pay what it owes. Second, the models need to be able to measure the dollar amount that might be lost if a counterparty defaults. Third, the models should have the capability to measure the correlation of default risk across the entire credit exposure portfolio.

Statistical and market approaches are used to build credit risk models. Statistical approaches rely on data compiled over many years that show how often companies at different credit rating levels default. The most common credit ratings referred to are those provided by Standard & Poor's, Moody's and Fitch. Market approaches use actively traded information, such as that provided by the prices of credit default swaps, to estimate the potential for a particular company to default. If a company that is being evaluated is not large enough to have its own credit rating, then similar or comparable companies that do have ratings or credit default swaps priced in the open

market can be used to make an estimate. Correlation models are also used to test the likelihood of several counterparties defaulting at the same time.

The total amount of money owed at a given time by a counterparty is the potential loss amount, and this number should be tracked on a daily basis by the credit risk model. Good credit risk models benefit banks and corporations by allowing senior financial leaders to always have a clear snapshot of how much money is at risk from credit defaults and the likelihood at a given time that defaults might occur (George E. Rejda, 2003:54).

## **2.7 Importance of Credit Risk Management Practices**

Businesses face various types' credit risks every day in their business operations. Managers will create a risk management program to mitigate their company's potential susceptibility and financial liability associated with credit risk. Business credit risks include creating open accounts that allow vendors or customers to purchase goods on credit, loaning money to businesses or individuals with poor repayment history or ability, and borrowing excessive amounts of money from outside lenders. While operating a business with acceptable levels of loaning or using credit is common, failing to assess the risk involved with the credit may lead to dangerous cash flow problems (Ibid).

Companies should develop written standards regarding the amount of credit extended to vendors and customers or borrowed from lenders. Using risk management software may help managers automate their credit risk management process, allowing for real-time management policies. Properly managed credit risk enhances a company's operational cash flow, resulting in quicker expansion of business operations. Strong financial credit history also allows companies a higher potential for outside investments. Managers may consult with public accounting firms or lawyers when developing their credit risk management policies. This ensures that the company's credit risk management policies address all pertinent financial and legal issues.

## **2.8 Credit Risk Solutions**

If you own or are starting a business and extend credit to your customers or plan to, managing credit risk is very important. It can mean the difference between good profitability and marginal profitability, or at worst, the failure of your business. The ability to evaluate your customer's creditworthiness is essential. Fortunately, the management of credit risk has evolved into something of a science, and there are many good tools now available to manage both consumer and business credit risk (James T. and Sandra G., 1998:410).

### **Initial Application**

A thorough and effective credit application should be obtained before extending credit. A good credit application should contain several sections that will enable you to collect and evaluate pertinent information, before you make a decision to extend credit and decide how much credit should be extended. At a minimum, credit applications should include the name, address, phone number and SSN of the applicant, their income, occupation and employer. More extensive applications often ask for details on the applicant's current obligations, such as the amount of their housing payment and other outstanding debts. A credit application may also ask for credit references and the name, address and phone number of a personal reference who is unrelated to the applicant (Ibid).

### **Credit Reports**

Credit reports are available for a modest fee from three major credit reporting companies, Equifax, Experian and Trans Union. It is also possible to obtain a consolidated credit report that shows the information on file at all three firms. A credit report should be obtained and evaluated before any decision to extend credit is made. The credit report will show the names of the applicant's current and past creditor, the date the credit was originally



extended, and the amount of credit that was granted. It will also show the applicants current balance with the creditor. Most importantly, the credit report will show the manner in which account has been maintained, its current status, and whether the person to whom the credit was granted has ever been delinquent in the past. Credit reports also include public record information such as suit, liens, and judgments (James T. and Sandra G., 1998:451).

## **Scoring Systems**

Credit scoring is an important tool that has been developed to aid credit granters in making a decision to extend credit and deciding how much credit is appropriate to extend. Credit scoring is a multivariate statistical technique that combines a number of various factors and is considered superior to a strict set of judgmental rules since it allows lower ratings on one factor to be compensated for by higher ratings in another. Several credit scores are already available from credit bureaus, including the well known FICO score, which is the one most widely used by consumer credit granters. Alternatively, a credit granter may choose to develop their own credit score, based on an analysis of the past credit behavior of their current and previous customers (Ibid).

## **Debt Burden Analysis**

Many credit granters perform a "debt burden analysis" before extending credit and in deciding what amount of credit is appropriate to extend. In the type of analysis, the credit granter computes the minimum payment amount that will be necessary to service the credit line the applicant has requested. They then take the applicant's income, subtract their taxes, housing payments, and the monthly amount necessary to meet the applicant's existing credit obligations, and determine whether there will be sufficient funds left over to service the new credit line that the applicant has requested. If not, the credit granter reduces the proposed line until the minimum payment can be supported with the income that remains.

## **Account Monitoring Systems**

Once credit has been granted, it is useful to monitor a creditor's payment behavior with other organizations. Several credit bureaus now offer account monitoring systems for this purpose, which can supply an "early warning" of impending credit problems. To use these systems, creditors supply the bureau with a list of accounts they would like to be monitored. The bureau then notifies the creditor whenever that account shows a delinquency at another organization on the bureau's files. This allows the creditor to respond quickly, before their own account is affected.

## **2.9 The Best Practices in Credit Risk Management**

Credit risk management protects an organization's financial assets. Credit risk management means protecting an organization from finance-associated risks. These risks can include loan repayment and debt recovery. Credit risk management employs several practices, each aimed at reducing the financial risk to a company. They include credit policies and procedures, credit analysis and credit review, all of which help prevent poor lending decisions and protect company investments (Jim, 2010:170).

### **Establishing Credit Policies and Procedures**

A necessary practice of credit risk management is establishing credit policies and procedures. Credit policy consists of guidelines and rules related to an organization's lending activities. This may include qualification requirements, loan amounts, and types of customers, interest rates, collateral and other mandates. Credit procedures instruct the credit department on how to achieve the organization's credit policies. These instructions can include specifics on the type of data used for the credit investigation and analysis process. They can also provide information for the credit approval process, account suspension and instances requiring

management's approval. By employing credit policies and procedures, ambiguity is reduced and the credit department functions more efficiently.

## **Analyzing Credit**

Credit analysis determines the degree of risk involved with lending to a business or individual. This practice uses information from credit applications, public records and credit reports. Credit applications are documents that require an applicant to provide basic information about them. The applications allow research into an applicant's financial background, and they allow the credit department to access public records to research judgments, liens, business registration and other legal information. Credit bureaus or agencies sell credit reports, which reveal financial and legal information that is vital to determining lending risk. The information includes previous and existing credit lines; payment history, bankruptcies and judgments filed and credit scores. Obtaining this information allows an organization to better identify who it is lending to and assess the risk versus the reward (Jim, 2010:172).

## **Reviewing Credit**

Credit review relates to established clients and their present situation. Financial difficulties may become obvious through actions such as late payments and partial payments, but a business closure or immediate default may not provide any warning signs. Reviewing accounts and their history allows an organization to stay familiar with the current credit situation of its clients. This practice allows for preemptive actions such as adjusting credit limits. Reviewing credit accounts also can ensure all required credit paperwork is in house (signed credit application or personal guaranty).

## **2.10 Credit Risk Management Structure**

Credit risk ratings help companies differentiate good business partners from less creditworthy ones. Credit is a pivotal tool in modern economic activities because individuals, nonprofits, government agencies and businesses may need loans for operational or consumption needs. Credit risk management is a business practice that helps a lender evaluate a borrower's creditworthiness and ability to repay a loan or a line of credit when it becomes due (Marquis, 2010:412).

**Definition:** Credit risk is the risk of loss originating from a business partner's failure to repay a loan or meet other financial commitments when they become due. A business partner (also known as counterparty) may default because of bankruptcy or temporary economic difficulties. For example, a retail store lends \$10,000 to a major customer, with repayment due after five years. If the customer files for bankruptcy after nine months, the store may incur credit losses if it is unable to recover any amount in court.

**Rating Methodology:** A corporation applies three procedures to rate risks. First, top management requires department heads to document credit risk policies and rate those risks as "high," "medium" or "low" based on loss expectations. Department managers' typically record risk and control information in a risk and control self-assessment (RCSA) report. Second, a corporation's internal audit department performs periodic reviews and may rank risks perceived in business transactions as "tier 1," "tier 2" or "tier 3" based on expected losses. Third, financial auditors also rate risks and controls in financial reporting mechanisms as part of the annual external audit (Ibid).

**High Risk:** High risk control problems can cause a corporation significant losses. Accordingly, top management typically ensures that department

heads provide proper solutions to these problems. For example, an investment bank has five branches in the U.S., but the New York branch contributes 70 percent to the company's total profits. The New York branch's consumer information processing database is dysfunctional. This problem is a high risk, and the bank may incur significant losses if it does not resolve the problem quickly.

**Medium Risk:** Medium risk problems are also known as significant deficiencies. Department heads generally partner with segment managers to resolve these deficiencies. To illustrate, if the investment bank's Colorado branch contributes 20 percent to corporate total revenues and has a similar computer information systems breakdown, top management may rate the problem as medium risk because losses are not significant. An information technology (IT) manager may partner with the branch supervisor to fix the breakdown.

**Low Risk:** A low risk control deficiency may be an occasional breakdown in a segment's procedures. Segment employees typically provide solutions to this type of deficiency under the direction of a senior manager. The investment bank may have low risk control deficiencies, such as occasional computer glitches, in its New York branch's customer service department. A manager or a supervisor in that department can provide solutions to such problems.

## **2.11 PRINCIPLES OF RISK MANAGEMENT**

The International Organization for Standardization (ISO) identifies the following principles of risk management: Risk management should:

- create value
- be an integral part of organizational processes
- be part of decision making

- explicitly address uncertainty
- be systematic and structured
- be based on the best available information
- be tailored
- take into account human factors
- be transparent and inclusive
- be dynamic, iterative and responsive to change

## **2.12 POTENTIAL RISK TREATMENTS**

According to Sonja B., (2003:211) once risks have been identified and assessed, all techniques to manage the risk fall into one or more of these four major categories

- **Avoidance** (eliminate, withdraw from or not become involved)
- **Reduction** (optimize - mitigate)
- **Sharing** (transfer - outsource or insure)
- **Retention** (accept and budget)

Ideal use of these strategies may not be possible. Some of them may involve trade-offs that are not acceptable to the organization or person making the risk management decisions. Another source, from the US Department of Defense, Defense Acquisition University, calls these categories **ACAT**, for Avoid, Control, Accept, or Transfer. This use of the ACAT acronym is reminiscent of another ACAT (for Acquisition Category) used in US Defense industry procurements, in which Risk Management figures prominently in decision making and planning(Ibid).

### **Risk avoidance**

This includes not performing an activity that could carry risk. An example would be not buying a property or business in order to not take on the legal liability that comes with it. Another would be not flying in order not to take the risk that the airplane were to be hijacked. Avoidance may seem the answer to all risks, but avoiding risks also means losing out on the potential

gain that accepting (retaining) the risk may have allowed. Not entering a business to avoid the risk of loss also avoids the possibility of earning profits (Ibid).

**Hazard Prevention:** Hazard prevention refers to the prevention of risks in an emergency. The first and most effective stage of hazard prevention is the elimination of hazards. If this takes too long, is too costly, or is otherwise impractical, the second stage is mitigation.

### **Risk reduction**

Risk reduction or "optimization" involves reducing the severity of the loss or the likelihood of the loss from occurring. For example, sprinklers are designed to put out a fire to reduce the risk of loss by fire. This method may cause a greater loss by water damage and therefore may not be suitable. Halon fire suppression systems may mitigate that risk, but the cost may be prohibitive as a strategy. Acknowledging that risks can be positive or negative, optimizing risks means finding a balance between negative risk and the benefit of the operation or activity; and between risk reduction and effort applied. By an offshore drilling contractor effectively applying HSE Management in its organization, it can optimize risk to achieve levels of residual risk that are tolerable (Sonja B., 2003:2113).

Modern software development methodologies reduce risk by developing and delivering software incrementally. Early methodologies suffered from the fact that they only delivered software in the final phase of development; any problems encountered in earlier phases meant costly rework and often jeopardized the whole project. By developing in iterations, software projects can limit effort wasted to a single iteration.

Outsourcing could be an example of risk reduction if the outsourcer can demonstrate higher capability at managing or reducing risks. For example, a company may outsource only its software development, the manufacturing of hard goods, or customer support needs to another company, while

handling the business management itself. This way, the company can concentrate more on business development without having to worry as much about the manufacturing process, managing the development team, or finding a physical location for a call center.

## **Risk sharing**

Briefly defined as "sharing with another party the burden of loss or the benefit of gain, from a risk, and the measures to reduce a risk." The term of 'risk transfer' is often used in place of risk sharing in the mistaken belief that you can transfer a risk to a third party through insurance or outsourcing. In practice if the insurance company or contractor go bankrupt or end up in court, the original risk is likely to still revert to the first party. As such in the terminology of practitioners and scholars alike, the purchase of an insurance contract is often described as a "transfer of risk."

However, technically speaking, the buyer of the contract generally retains legal responsibility for the losses "transferred", meaning that insurance may be described more accurately as a post-event compensatory mechanism. For example, a personal injuries insurance policy does not transfer the risk of a car accident to the insurance company. The risk still lays with the policy holder namely the person who has been in the accident. The insurance policy simply provides that if an accident (the event) occurs involving the policy holder then some compensation may be payable to the policy holder that is commensurate to the suffering/damage. Some ways of managing risk fall into multiple categories. Risk retention pools are technically retaining the risk for the group, but spreading it over the whole group involves transfer among individual members of the group. This is different from traditional insurance, in that no premium is exchanged between members of the group up front, but instead losses are assessed to all members of the group.



## **Risk retention**

Involves accepting the loss, or benefit of gain, from a risk when it occurs. True self insurance falls in this category. Risk retention is a viable strategy for small risks where the cost of insuring against the risk would be greater over time than the total losses sustained. All risks that are not avoided or transferred are retained by default. This includes risks that are so large or catastrophic that they either cannot be insured against or the premiums would be infeasible. War is an example since most property and risks are not insured against war, so the loss attributed by war is retained by the insured. Also any amounts of potential loss (risk) over the amount insured are retained risk. This may also be acceptable if the chance of a very large loss is small or if the cost to insure for greater coverage amounts is so great it would hinder the goals of the organization too much (Sonja B., 2003:219).

## **2.13 RISK FINANCING TECHNIQUES**

After exists whenever the future is unknown because adverse effect of risk plagued mankind since the beginning of time. As a result accidental losses each day had threaten the survival of some businesses. Causing their earnings to drop below acceptable levels, interrupt their operations or slow their growth. All businesses face the threat of losses that may never occur. Worrying about these possibilities does more than make life less pleasant' it conducts its operations. Proper risk management enables a business to handle its exposures to accidental losses in the most economic and effective way (Williams J., 1998:3).

The purpose of risk management is to minimize the risk of losses at a minimums cost and its contribution to the business can also be categorized as follows.

- Risk management may take the differences between survival and failure that means it can contribute directly to business profits for business organization and increase efficiency for nonprofit making organizations because profits can be improved by reducing exposures as well as increasing income.
- If a business has successfully managed its pure risks, the peace of mind and confidence permits its managers to investigate and assume attractive speculative risks that they might otherwise seek to avoid.

## **2.14 LIMITATIONS**

If risks are improperly assessed and prioritized, time can be wasted in dealing with risk of losses that are not likely to occur. Spending too much time assessing and managing unlikely risks can divert resources that could be used more profitably. Unlikely events do occur but if the risk is unlikely enough to occur it may be better to simply retain the risk and deal with the result if the loss does in fact occur. Qualitative risk assessment is subjective and lacks consistency. The primary justification for a formal risk assessment process is legal and bureaucratic.

Prioritizing the *risk management processes* too highly could keep an organization from ever completing a project or even getting started. This is especially true if other work is suspended until the risk management process is considered complete (Smith and Others, 1998:199).

## CHAPTER THREE

### DATA PRESENTATION, ANALYSIS AND INTERPRETATION

This chapter deals with presentation, analysis and interpretation of data obtained from respondents through administration of questionnaire and interview.

Out of 59 questionnaires (39 to employees and 20 to customers) distributed to the respondents, 54(92%) of them were properly filled and returned only 5 customers are reluctant to return the questionnaire. And interview provided to management bodies of the bank.

Accordingly, all the data gathered were presented, analyzed and interpreted in the up coming chapter.

#### 3.1 GENERAL CHARACTERISTICS OF RESPONDENTS

Table 1 below shows, the general characteristic of respondent in terms of their sex distribution, educational background and work experience.

**Table 1 Sex distribution, educational and duration of service on current position**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
Sex	Male	29	76
	female	10	34
	<b>Total</b>	<b>39</b>	<b>100</b>
Educational Background	Diploma	14	35
	1 <sup>st</sup> degree	21	55
	MA/MSC	4	10
	<b>Total</b>	<b>39</b>	<b>100</b>
Work Experience	Below 5 years	12	30
	5-10 years	20	52
	10-15 years	7	18
	<b>Total</b>	<b>39</b>	<b>100</b>

As can be observed in table 1, majority of the respondents i.e. 29(76%) are male. While the rest 10(34%) of them are female. This indicates that, the study can address both genders.

Item 2 of the same table indicated that, majority of the respondents i.e. 21(55%) of them replied that they are 1<sup>st</sup> degree holders. While the remaining 14(35%) and 4(10%) of them categorized as diploma holders and MA/MSC respectively. This shows that, respondents are matured to express their view concerning the credit risk.

Item 3 of the same table signifies that, 20(52%), 12(30%) and 7(18%) them respondents have work experience of 5-10 years, below 5 years, and 10-15 years respectively. Form this one can understand that, respondents are well informed about the operation and/or practice of the bank.

### 3.2 MATTERS OF DIRECT RELEVANCE OF THE SUBJECT OF STUDY

**Table 2 Risk Management Practice**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
Do you think that the bank possibly have well organized risk management practice?	Yes	14	35
	No	25	65
	<b>Total</b>	<b>39</b>	<b>100</b>

As can be seen in table 2 above, 25(65%) of the respondents i.e. majority replied that No there is no organized risk management practice with in the bank. while the rest 14(35%) of them said yes there is organized risk management practice with in the bank. Form this one can easily understand that, the risk management practice of the bank somehow doubtful.

Regarding, policies and procedures with in the bank are in line with the over all strategy of the bank, the researcher asks the respondents, accordingly the responses presented as follows.

**Table 3 the Compliance between the Bank's Policy, Practices and Strategy**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
Do you believe that credit risk management polices and practices are in line with the overall strategy of the bank?	Yes	25	64
	No	14	36
	<b>Total</b>	<b>39</b>	<b>100</b>

As can be seen in table 3 majority of the respondent's i.e. 25(64%) replied that Yes risk management polices and practice in line with the overall strategy of the bank. However the remaining 14(36%) said No, but there are some similarity. Beside this, data obtained from the management evidenced that the policy and practice of credit risk management are relatively as similar as the overall strategy. From this on can infer, the bank polices and practice of credit risk management in line with overall strategy.

**Table 4 Participation of Employees on Risk Management Process**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
At the best of your understanding can we say risk management practice of the bank is participative?	Yes	35	91
	No	4	9
	<b>Total</b>	<b>39</b>	<b>100</b>
If your answer for the above question is Yes what type of risk management activity are conducted by the bank?	Credit risk management	24	70
	Liquidity risk management	7	20
	Interest rate & foreign exchange	4	10
	Other	-	-
	<b>Total</b>	<b>35</b>	<b>100</b>

As can be seen item 1 of table 4 above, majority of the respondents i.e. 35(91%) of them replied that, they do have the opportunity to involve or participate in the risk management activities. While the rest 4(9%) of them said no they are not participating in the risk management process of the bank.

Item 2 of the same table above, 24 (70%) and 7(20%) of them have to participate in credit risk and liquidity risk management activities. While the rest 4(10%) of them said they involve interest rate risk management. From this one can conclude that, employees are active participants in credit risk management. Moreover, the words obtained from the management evidenced that, relatively active involvement of employees in the overall risk management activity presented in the bank manual, however due to various unforeseen reasons their application is rare.

**Table 5 Effectiveness of Risk Management**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
Are you satisfied with the effectiveness of credit risk Management system adopted by Dashen Bank?	Yes	16	40
	No	23	60
	<b>Total</b>	<b>39</b>	<b>100</b>

As can be seen in table 5 above, 23(60%) of the respondents i.e. majority said they are not satisfied by the quality of credit risk management system of the bank, because, the system could not consider possible factors that should incorporate; while the remaining 16(40) said yes they are satisfied. This implies that, the management of the bank have some inconsistency in regard to quality of credit risk assessment.

**Table 6 Credit Risk Identification Practice**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
To what extent you credit risk are identified properly by the Bank?	To very great extent	-	-
	To great extent	18	47
	To some extent	21	53
	To lower extent	-	-
	To very lower extent	-	-
	<b>Total</b>	<b>39</b>	<b>100</b>

As can be observed in table 6 above, Majority of the respondents i.e. 21(53%) replied that, to some extent credit risk identified properly with in the bank under study. While the rest, 18(47%) of them said to great extent credit risk is identified properly. From this, on can easily understand that the bank have possibility of minimizing credit risk since they are properly identified.

**Table 7. Credit Risk Management System of the Bank**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
To what extent you know about the credits risk management system adopted by Dashen Bank?	To very great extent	-	-
	To great extent	12	30
	To some extent	27	70
	To lower extent	-	-
	To very lower extent	-	-
	<b>Total</b>	<b>62</b>	<b>100</b>

As shown in table 7, Majority of the respondents i.e. 27(70%) replied that, To some extent they are aware of credit risk management system of the bank, where as the remaining, 12(30%) of them said they rate their awareness to great extent. This implies that, it is difficult to say respondents have in understanding credit risk and its management.

**Table 8: Qualification of Credit Officers**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
To what extent credit employees are qualified to handle their job effectively?	To very great extent	-	-
	To great extent	31	80
	To some extent	-	-
	To lower extent	8	20
	To very lower extent	-	-
	<b>Total</b>	<b>39</b>	<b>100</b>

Table 8 above indicated that, majority of the respondents i.e. 31(80%) replied that to great extent the credit officers of the bank are qualified to handle their job. The rest 8(20%) of them said credit officers are to lower extent qualified to handle their job. This indicates that the bank have no doubt with regard to competence of it credit officer.



**Table 9 Assessment of Borrower's Profile by the Bank**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
How often does the bank assess borrower's profile?	Very often	-	-
	Often	-	-
	Neutral /do not know	14	36
	Sometimes	25	64
	Not at all	-	-
	<b>Total</b>	<b>39</b>	<b>100</b>
To what extent the Bank's loan fall under NPL?	To very great extent	-	-
	To great extent	-	-
	To some extent	20	51
	To lower extent	11	28
	To very lower extent	8	21
	<b>Total</b>	<b>39</b>	<b>100</b>

As can be seen table 9 above, majority of respondents i.e. 25(64%), replied that, sometimes the bank assess borrowers profile. Where as the remaining, 14(36%) of the respondents replied that, they are neutral/ do not know about the question asked. This implies that, there is poor practice with in relation to borrower's assessment which exposes them to credit risk.

Item 2 of the same table above, Majority of the respondents i.e. 20 (51%) rate, to some extent the bank's loan fall under NPL. While the rest 11 (28%) and 8 (21%) of the respondents agreed to lower and very lower extent the banks loan fall under NPL. From this one can confirm that, the level of loans disbursed to customers have great possibility exposed to credit risk.

Moreover, according to the data obtained from the management indicted that, the bank take an assessment of its borrower always before lending the loan, but the level of its tightness may not be insurable.

**Table 10 Follow up Mechanism of the Bank**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%</b>
Is there any follow up mechanism of your customers after granting a loan?	Yes	39	100
	No	-	-
	<b>Total</b>	<b>39</b>	<b>100</b>
If your answer in the above questions is yes how often?	Monthly	-	-
	Quarterly	39	100
	Semi annual	-	-
	Annually	-	-
	<b>Total</b>	<b>39</b>	<b>100</b>

As it is depicted in table 10 item 1 above, all of the respondent's i.e. 39(100%) replied that the bank has its own follow up mechanism to its customers after granting the loan. While none of them complain the presence of follow up mechanism.

Item 2 of the same table indicted that, all of the respondents i.e. 39(100%) relied follow up of customers undertake in quarterly base. From this on can infer, the frequency of conducting follow up of its customer is taken in quarterly base. In addition to the response obtain from respondents, the management of the bank testify the availability of following up mechanism and it is conducted in every three months of the year.

**Table 11 Credit Risk Handling Orientation of the Bank**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%</b>
What kind of credit risk handling orientation used by the bank ?	risk prevention	32	81
	risk reduction	7	19
	risk avoidance	-	-
	other	-	-
	<b>Total</b>	<b>39</b>	<b>100</b>

As can be seen table 11, majority of respondents i.e. 32(81%), replied that, the bank use risk prevention orientation. Where as the remaining, 7(19%) of the respondents replied that, the bank use risk reduction handling orientation. This implies that, the bank remedial action ahead of time in order to prevent the occurrence of credit risk over the bank as well as the customer.

Finally data obtained from open ended questions indicated that, the bank has some how good credit, risk management system However, most of them remain on paper and /or they are not converted in to practical actions. This may weaken the effectiveness of its credit risk management system.

### 3.3 Analysis of Data Obtained from Customer

**Table 12 Duration of stay at the Bank**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
For how long have you been customer of the bank?	Less than one year	-	-
	1-2 year	12	79
	3-4 year	-	-
	Greater than 4 year	3	21
	<b>Total</b>	<b>15</b>	<b>100</b>

As can be seen table 12 above, majority of respondents i.e. 12(79%), replied that, they are customer of the bank for the last two years. Where as the remaining, 3(21%) of the respondents replied that, they are customer of the bank grater than four years. This implies that, customers of the bank are well informed about the credit risk management practise of the bank.

**Table 13 Credit Facility of the Bank**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
Credit facility of the bank is very efficient?	Strongly agree	-	-
	Agree	4	23
	Neutral	-	-
	Disagree	11	77
	Strongly disagree	-	-
	<b>Total</b>	<b>15</b>	<b>100</b>

As can be observed in table 13, majority of respondents i.e. 11(77%), replied that, they are disagreed by the efficient facility of the bank credit facility. Where as the remaining, 4(23%) of the respondents replied that, they are agreed with the efficient credit facility of the bank. This indicated that, the credit facility of the bank needs some sort of amendment by the management.

**Table 14 Loan Approval Requirement of the Bank**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
How do you rate loan approval requirement of the Bank?	Very good	-	-
	Good	2	13
	Medium	5	33
	Poor	8	54
	Very poor	-	-
	<b>Total</b>	<b>15</b>	<b>100</b>

As can be see from table 14 above, majority of the respondents i.e. 8(54%) of them replied that the loan approval requirement of the bank is poor. While the rest 2(13%) and 5(33%) of them said good and medium respectively. This implies that the task left by the management of the bank in making amendment on it.

**Table 15 Credit risk faced by the customer**

<b>Item</b>	<b>Response</b>	<b>Frequency</b>	<b>%age</b>
Have you ever been faced with credit risk?	Yes	13	88
	No	2	12
	<b>Total</b>	<b>15</b>	<b>100</b>

As can be observed in table 15, majority of respondents i.e. 13(88%), replied that, yes the face credit risk during the relation they have. Where as the remaining, 2(12%) of the respondents replied that, no they are not faced credit risk ever before. This indicated that, customer of the bank faced credit risk this may affect the credit worthiness of the bank.

Finally, according to the data obtained from open ended question indicated, some of the customer is not satisfied by the service obtained form the bank, due to this reason they may shift to other banks those provided better credit facility.

## **CHAPTER FOUR**

### **SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS**

After all the detailed analysis is done in the previous chapter, all the data gathered were presented, analyzed and interpreted. Based on the analysis major findings are summarized, conclusions are drawn and possible recommendations are forwarded to the management of the Bank.

#### **4.1 SUMMARY OF FINDINGS**

- According to the study majority of the respondents are male those degree holders and working more than five year with in the bank.
- The study reveals that, the risk management practice of the Bank is not organized in the manner to assist the day to day operation.
- Majority (64%) of the respondents testify, polices and practices of credit risk management is inline with the overall strategy as indicated by the study.
- The study shown that, majority (91%) of the respondents has the chance to participate only in the area of credit risk management activities.
- The study revealed that, the management of the bank have some inconsistency in regard to quality of credit risk assessment.
- The study revealed that, the bank have possibility of minimizing credit risk since they are properly identified.
- As indicated by the study, it is difficult to say respondents have better understanding about the credit risk and its management.
- The study revealed that, the bank assesses borrowers profile not at satisfactory level.
- The study indicated that, the bank has its own customer follow up mechanisms which were used in every quarterly base.
- According to the study the bank uses credit risk prevention orientation as a credit risk handing mechanism.

- The study revealed that, customers of the bank is not satisfied by the efficiency of its credit facility.
- According to the study, the bank credit facility provided to customers exposed them to credit risk.

## **4.2 CONCLUSIONS**

After all major findings are summarized in the previous section, the following conclusions are drawn.

- The credit risk assessment of the bank is not well organized; this might affect the overall efficiency obtained by the bank.
- Policies and practise of credit risk management is inline with strategies, this might result reduce problems integrity.
- The level of employee's participation in the risk of credit risk management is somehow good, which may assist its effective application.
- The quality of risk management system of the bank has problem which affect proper prevention as well as protection of risk occur in the operation.
- Employees are not good enough in understanding credit risk and its management, this might cause a maximizing the probability credit risk occurrence.
- The bank conducts follows up on its customers in quarter base, this help to reduce the customer's exposure to credit risk.
- The bank use credit risk prevention orientation, this can assist to customers as well as the bank protects them before entertaining loss.
- Customers is not satisfied by the efficiency of its credit facility, this might affect the level of the bank customer and create opportunity to see somewhere else.



### **4.3 RECOMMENDATIONS**

For effective attainment of study objective, all data were presented, analyzed and interpreted. Findings are summarized and conclusion made are drawn and based on the conclusions drawn the following recommendations are forwarded.

- ✓ In order to get full benefit from its risk management system, Dashen Bank is strongly advised to create mechanism for effective application of the system.
- ✓ The Bank is advised to farther improved its risk management polices and practice with its strategy for effective achievement its goal.
- ✓ In order to make in view its credit risk management, it is recommended that the bank enhance the level of employees, participation in the area of credit management.
- ✓ In order to reduce possible errors made in credit management, the bank is advised to facilitate ways that enhance understanding of its employees.
- ✓ The Bank is strongly recommended to further improve the frequency of customer follow up, in order to ensure customers from exposure of credit losses.
- ✓ The Bank is strongly advised to evaluate its credit risk as well as risking management practice regularly, in order to being compatible with current financial environment.
- ✓ In order to retained customers within the bank, it is advisable to improve efficiently of credit facility of the bank.
- ✓ Finally the bank is advised to review its credit risk management system, in order to make its risk handling system reliable.

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# APPENDIX

**ST. MARY'S UNIVERSITY COLLEGE**  
**BUSINESS FACULTY**  
**DEPARTMENT OF MANAGEMENT**

**Questionnaires to be filled by employees of Dashen Bank**

This questionnaire is prepared by a student researcher prospective graduate of year 2011 in the field of Management. The outcome of this questionnaire is meant to support a research report to be presented for St. Mary's University College. The response provided by the respondents only used for academic purpose. Therefore you are invited respectfully to provide genuine response.

**Thank you in advance for your cooperation.**

N.B:- No need to write your name

Put '✓' or 'X' mark on your answer for close ended questions

Respond on the space provided for open ended question

**I. PERSONAL INFORMATION**

1. Sex             Male                       Female

2. Educational Background

Diploma                       MA/MSC

1<sup>st</sup> Degree

3. Work Experience

Below 5 years                       10-15 years

5-10 years

**II QUESTIONS DIRECTLY RELATED TO THE STUDY**

4. Do you think that the bank possibly have well organized risk management practice

Yes

No

5. Do you believe that the credit risk management polices and practice in line with the overall strategy of the Bank?

Yes

No

6. At the best of your understanding can we say risk management practice of the bank is participative?

Yes

No

7. If your answer in question No. 6 is “Yes” what type of risk management activities are conducted by the Bank?

Credit risk management

Liquidity risk management

Interest rate and foreign exchange risk management

Other \_\_\_\_\_

8. Are you satisfied with the quality if credit management system adopted in Dashen Bank?

Yes

No

9. If not what do you think is the problem?

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10. To what extent credit risks are identified properly by the Bank?

- To very great extent
- To great extent
- To some extent
- To lower extent
- To very lower extent

11. To what extent you know about the credit risk management system adopted by Dashen Bank?

- To very great extent
- To great extent
- To some extent
- To lower extent
- To very lower extent

12. To what extent credit officers are qualified to handle their job effectively?

- To very great extent
- To great extent
- To some extent
- To lower extent
- To very lower extent

13. How often does the bank assess borrower's profile?

- Very often
- Often
- Neutral/do not know
- Sometimes
- Not at all

14. Is there any follow-up mechanism of your customers after granting a loan?

- Yes
- No

15. If your answer in question No. 14 is “Yes” how often?

- Monthly
- Quarterly
- Semi Annually
- I am not quite aware of it

16. What kind of credit risk handling orientation used by are Bank?

- Risk Prevention
- Risk reduction
- Risk avoidance
- Other, please specify \_\_\_\_\_

17. What kind of trend registered in credit risk management of the Bank?

- Stable
- Fluctuated
- Continuous increase
- Continuous decrease

**ST. MARY'S UNIVERSITY COLLEGE**  
**BUSINESS FACULTY**  
**DEPARTMENT OF MANAGEMENT**

**Questionnaires to be filled by credit customer of Dashen Bank**

This questionnaire is prepared to gather information regarding credit risk management practice of Dashen bank for the partial fulfillment of bachelor of degree in St. Mary's University College. The response provided by the respondents only used for academic purpose. Therefore you are invited respectfully to provide genuine response.

**Thank you in advance for your cooperation.**

**N.B:-** No need to write your Name

Put 'X' mark on your answer for clause ended questions

Respond on the space provided for open ended question

**I. Personal Information**

1. Sex                  Male                          Female

2. Age                  18 – 23                      30-35

     24-29                      36-41

     Above 41

3. Type of business engagement

Private business

Cooperative business

Some other business

**II. Questions directly related to the study**

4. For how long have you been customer of the bank?

Less that 1 year                          3-4 year

1-2 year                                      greater than 4 year



5. Credit facility of the bank is very efficient?

- Strongly agree       disagree  
 Agree       strongly disagree  
 Neutral

6. How do you rate loan approval requirement of the bank?

- Very good       poor  
 Good       very poor  
 Medium

7. To what extent the bank loan provision practice expose customer to credit risk?

- To a very great extent       to lower extent  
 To great extent       to a very lower extent  
 To some extent

8. Have you ever been faced with credit risk?

- Yes       No

9. If you said "Yes" for the above question pleas specify the risks!

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10. The bank properly follows up borrowers after disbursing the loan to reduce risk?

- Strongly agree       disagree  
 Agree       strongly disagree  
 Neutral

11. If you said disagree/strongly disagree pleas specify your reason!?

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12. If you have any comment and/or suggestion regarding credit risk management practice of the bank please specify.

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**BUSINESS FACULTY**  
**DEPARTMENT OF MANAGEMENT**

The following interview questions were delivered to the management of Dashen Bank by the study.

1. To what extent the Bank properly apply risk management science and are?
2. To what extent employees participate in credit risk management?
3. How often the Bank assess borrower's profile?
4. Is there mechanism to follow up borrowers?
5. How often the Bank conducts follow up of its customers.

## DECLARATION

I, the undersigned, declare that this senior essay/project is my original work, prepared under the guidance of Ato Mergia Mekuria. All sources of material used of the manuscript have been duly acknowledged.

Name Nigatua Tafere  
Signature \_\_\_\_\_  
Place of submission SMUC  
Date of Submission June 2011

This paper has been submitted for examination with my approval as the University College adviser.

Name Ato Mergia Mekuria  
Signature \_\_\_\_\_  
Date of Submission \_\_\_\_\_