
**CREDIT RISK MANAGEMENT AND PROFITABILITY OF FINANCIAL
INSTITUTIONS IN UGANDA**

A CASE OF DFCU BANK IN PALLISA DISTRICT

BY

MUMPEREZE RINET

BU/UP/2020/1285

**A RESEARCH REPORT SUBMITTED TO THE FACULTY OF MANAGEMENT
SCIENCES, DEPARTMENT OF ECONOMICS AND MANAGEMENT**

IN PARTIAL FULFILLMENT FOR THE REQUIREMENT

OF AWARD OF A BACHELORS DEGREE IN

BUSINESS ADMINISTRATION OF


BUSITEMA UNIVERSITY

SEPTEMBER-2023

DECLARATION

DECLARATION

I MUMPEREZE RINET; REGN NO BU/UP/2020/1285, hereby declare that the contents of this research work were purely my original work and that no other study has been conducted on the topic. To the best of my knowledge, this work was never been submitted before; in any other university or higher institution of learning for any award of either a degree or any other related qualification. In all cases where other people's ideas were quoted, they have been duly acknowledged by complete references.

Signature: 

Date: 16th 01 - 2021


MUMPEREZE RINET;

(REG NO: BU/UP/2020/1285)

APPROVAL

APPROVAL

This is to certify that this Research report was done by MUMPEREZE RINET; REGN NO BU/UP/2020/1285 on the topic "credit risk management and profitability of financial institution in Uganda; a case of dfcu Bank Pallisa branch" was been under my supervision and was now submitted for examination with my approval as the University supervisor.

Signature: 

Date: 16/01/23

Mr. KALEMBE DOREEN

(UNIVERSITY SUPERVISOR)

Department of Economics and Management

Busitema University

DEDICATION

I dedicate this research work to my beloved Mother Mrs. Kirabo Mackline who provided me with both financial and non-financial assistance that enabled me accomplish this course and above all the almighty GOD.

ACKNOWLEDGEMENT

I am grateful to the almighty God that he has given me the gift of life, the gift of my beloved parents and friends, who gave me the opportunity to be in school and guided me throughout this study and writing of this report. My thanks go to all Busitema University lecturers without forgetting my special supervisor Mr. Kalembe Doreen who guided me in the right direction from the beginning till the end of this work and he greatly contributed in making a difference in my performance.

Profound thanks to all the people who have been resourceful throughout this study. It was due to your support and ideas that I have been able to produce this work.

Utmost thanks to the Head of Department, Busitema University, my sincere thanks go to my uncles, sisters, brothers, friends, course mates and lectures especially for their dedicated support throughout this research and the entire three years of the course.

TABLE OF CONTENTS

Table of Contents

DECLARATION	i
APPROVAL.....	ii
DEDICATION.....	iii
ACKNOWLEDGEMENT.....	iv
TABLE OF CONTENTS	v
LIST OF FIGURES.....	vii
LIST OF ABBREVIATIONS AND ACRONYMS.....	ix
INTRODUCTION.....	1
1.0 Introduction	1
1.1 Background of study	1
1.2 Statement of the Problem	4
1.3 Purpose of the study.....	5
1.4 Research objectives	5
1.5 Research questions.....	5
1.6.0 Scope of the Study	5
1.6.1 Content Scope.....	5
1.6.2 Geographical Scope	5
1.6.3 Time Scope.....	6
1.7 Significance of the Study.....	6
1.8 Conceptual Framework.....	7
1.8.1Explanation of the conceptual frame work.....	7
1.9 Definition of key terms	8
CHAPTER TWO:	9
LITERATURE REVIEW	9
2.0 Introduction	9
2.1 Theoretical review	9
2.1.1 Value at Risk Theory (VAR).....	9

2.1.2 DuPont Model.....	10
2.2 Empirical Review of Literature	10
2.2.1 Non performing loan ratio and profitability of financial institution	10
2.2.2 Loan loss provision ratio and profitability of financial institution	11
2.4 Capital adequacy ratio and profitability of financial institution	12
2.5. Summary of the literature reviewed	13
CHAPTER THREE:	14
RESEARCH METHODOLOGY	14
3.0 Introduction:	14
3.1 Research Design.....	14
3.2 Study Population.....	15
3.3 Sample Size	15
Source: Krejcie and Morgan’s table (1970)	15
3.4 Sampling method.....	16
3.5 Type of data	16
3.5.1 Primary data	16
3.5.2 Secondary data	16
3.6 Data Collection methods.....	16
3.7 Data Analysis plan.....	17
3.9 Reliability and Validity.....	17
3.10 Ethical Considerations.....	18
<i>REFERENCES</i>	19
Appendix II: – Questionnaire	35
Appendix III: Work Plan	40
Appendix IV: Research Budget.....	41

LIST OF FIGURES

Figure 1: The conceptual framework of credit risk management and profitability of financial institutions.	7
--	---

LIST OF TABLES

Table 3.1: showing a sampling frame.....	15
--	----

LIST OF ABBREVIATIONS AND ACRONYMS

BOU	Bank of Uganda
CAR	Capital Adequacy Ratio
SPSS	Social package for social sciences
CB	Centenary Bank
CRM	Credit risk management
FSR	Financial Stability Report
GDP	Gross domestic product
LCR	Liquidity coverage ratio
LLPR	Loan Loss Provision Ratio
MD	Managing Director
NIM	Net interest margin
NPLR	Non-performing Loan Ratio
PCL	Provision for Credit Loss
ROA	Return on Asset
ROE	Return on Equity

CHAPTER ONE: INTRODUCTION

1.0 Introduction

This chapter presents the introduction, background of the study, problem statement, purpose of the study, objectives, research questions, scope of the study, conceptual framework, significance of the study, and definitions of key terms.

1.1 Background of study

Internationally, it was approved that the stability and reliability of the financial institution was key to economic growth of any economy (Bhatti et al., 2020). Apart from facilitating savings, commercial banks extend credit to individuals who can be used to ease production, acquire capital assets and facilitate trade (Bagale, 2023). All financial institutions get profit through extending credit services to both institutions and individuals (Driga, 2012). Despite of that, the profitability of financial institutions still continues to decline. For instance, insight to European Central Bank (ECB) annual report (Court, 2019), the growth rate of bank loans to firms decreased from 7.1% to 4.3% in 2020 and 2021 respectively with the depreciation of euro by 3.6% affecting the bank's return on equity (ROE). ROE was well been low bank cost of equity (COE) in 2020. This was important because commercial banks with ROE persistently below their COE are deemed to have an insufficient level of profitability (KPMG, 2021). Also, according to annual report of Industrial and commercial bank of China ltd (UNICEF/WHO, 2019), Profit before provision was RMB627.5 billion, representing a decrease of 5.5% from the previous year. Net profit reduced to RMB350.2 billion, representing also a decrease of 10.2% from the previous year. Return on total average assets and return on weighted average equity remained constant ton the previous year. Capital adequacy ratio stood at 18.02%. NPL ratio was 1.42%, down 0.16% points from the end of the previous year. (Lalon & Morshada, 2020)revealed that the Banking industry of Bangladeshi Bank suffered a considerable amount of classified loan consisting over 8% of nonperforming loan so that the profitability measured with ROA of banking sector was decreased from 1.3% to 0.8% as the bankers were reluctant to lend fresh loans due to heavy burden of non-performing loan prevailing between 2019 to 2018.In sub-Saharan Africa,

REFERENCES

- Ajayi, O. V. (2017). Distinguish Between Primary Sources of Data and Secondary Sources of Data. *Benue State University, 1*(1), 1–5.
- Alhadab, M., & Alshawneh, S. (2016). Loan Loss Provision and the Profitability of Commercial Banks: Evidence from Jordan. *International Journal of Business and Management, 11*(12), 242. <https://doi.org/10.5539/ijbm.v11n12p242>
- Asikhia, O. (2013). CAPITAL ADEQUACY AND BANKS' PROFITABILITY: AN EMPIRICAL EVIDENCE FROM NIGERIA MARKET-FOCUSED STRATEGIC FLEXIBILITY AND SALES GROWTH: EMPIRICAL EVIDENCE FROM NIGERIA View project. *Emerging Markets Finance and Trade, 3*(November), 1417–1428. www.aijcrnet.com
- Bagale, S. (2023). Credit Risk Management and Profitability of Commercial Banks in Nepal. *Journal of Business and Social Development, 5*(1), 60–67.
- Bank of Uganda. (2022). *Annual Report Going Further Together*. 61–113. www.bou.or.ug
- Bank, Y. A., & Annual, S. (2021). *CENTRAL BANK OF KENYA*.
- Barus, J. J., Muturi, P. W., Kibati, D. P., & Koima, D. J. (2017). Effect of Liquidity on Financial Performance of Savings and Credit Societies in Kenya. *International Journal of Finance, 2*(7), 34–47. <https://doi.org/10.47941/ijf.188>
- Basheer, M. F., Ahmad, A. A., & Hassan, S. G. (2019). Impact of economic and financial factors on tax revenue: Evidence from the middle east countries. *Accounting, 5*(2), 53–60. <https://doi.org/10.5267/j.ac.2018.8.001>
- Bhatti, S., Tariq, N., Rizwan, M., Ajmal, M., Aslam, A. R., & Javed, K. (2020). Impact of Risk Management on Profitability of Banks. *Malaysian E Commerce Journal, 3*(3), 22–26. <https://doi.org/10.26480/mecj.03.2019.22.26>
- Budiarto, A. (2021). The Impact of Non-Performing Loans Towards Financial Performance of BPR in Central Java, the Role of Empathy Credit Risk. *Proceedings of the 4th International Conference on Sustainable Innovation 2020-Accounting and Management (ICoSIAMS 2020), 176*(ICoSIAMS 2020), 251–258. <https://doi.org/10.2991/aer.k.210121.035>

- Court, E. (2019). *2019 Annual Reports on the implementation of the EU budget for the 2019 financial year and on the activities funded by the 8th, 9th, 10th and 11th European Development Funds (EDFs) for the 2019 financial year*. <https://doi.org/10.2865/150022>
- DFCU bank. (2019). *2020-dfcu-Limited-Audited-Financials.pdf*.
- Hyman, M. R., & Sierra, J. J. (2016). *Open- versus close-ended survey questions*. February.
- Ishtiaq, M. (2019). *Book Review Creswell, J. W. (2014). Research Design : Qualitative , Quantitative and Mixed Methods Approaches (4th ed .). Thousand Oaks , CA : Sage. 12(5), 40–41*. <https://doi.org/10.5539/elt.v12n5p40>
- Jing, E. (2020). Impact of high non-performing loan ratios on bank lending trends and profitability. *Int. J. Financial Stud*, 8(August), 12. www.mdpi.com/journal/ijfs
- Jonson, R. (2019). *profitability*. July, 1–23.
- KPMG. (2021). European banks ' profitability : plus ça change ? *KPMG Economic Outlook*, 1–13.
- Lalon, R. M., & Morshada, F. (2020). Impact of Credit Risk Management on Profitability of Commercial Banks in Bangladesh: An estimation of Dynamic Panel Data Model. *International Journal of Finance & Banking Studies (2147-4486)*, 9(3), 131–147. <https://doi.org/10.20525/ijfbs.v9i3.874>
- Li, F. (2014). *The Impact of Credit Risk Management on Profitability of Commercial Banks* : UMEA University.
- Mafumbo, P. W. (2020). Credit Management, Credit Policy and Financial Performance of Commercial Banks in Uganda. *International Journal of Business and Management Review*, 8(5), 68–99. <https://doi.org/10.37745/ijbmr.vol8.no5.p68-99.2020>
- Mi, J., Li, Y., Huang, H. Z., Liu, Y., & Zhang, X. L. (2013). Reliability analysis of multi-state system with common cause failure based on bayesian networks. *Eksploatacja i Niezawodnosc*, 15(2), 169–175.
- Shingjergji, A. (2013). The Impact of Bank Specific Variables on the Non-performing loan s Ratio in the Albanian Banking System. *Research Journal of Finance and Accounting*, 7,

148–152.

Silaban, P. (2018). *Analisis Hubungan Indeks Global Dengan Indeks Pasar Modal Indonesia*.
[http://repository.uhn.ac.id/handle/123456789/4765%0Ahttp://repository.uhn.ac.id/bitstream/handle/123456789/4765/PASAMAN %28GENAP 2017_2018%29.pdf?sequence=3&isAllowed=y](http://repository.uhn.ac.id/handle/123456789/4765%0Ahttp://repository.uhn.ac.id/bitstream/handle/123456789/4765/PASAMAN%28GENAP%2017_2018%29.pdf?sequence=3&isAllowed=y)

UNICEF/WHO. (2019). व ा र्ष ि क प र्त ि व े दन Annual Report Annual Report.
Fresenius.Com, December, 2–2. <https://www.pvh.com/-/media/Files/pvh/investor-relations/PVH-Annual-Report-2020.pdf>

Wang, R., & Krosnick, J. A. (2020). Middle alternatives and measurement validity: a recommendation for survey researchers. *International Journal of Social Research Methodology*, 23(2), 169–184. <https://doi.org/10.1080/13645579.2019.1645384>