BUSITEMA UNIVERSITY
Pursuing Excellence

P.O. Box 236, Tororo, Uganda
Gen: +256 - 45 444 8838
Fax: +256 - 45 4436517
Email: info@adm.busitema.ac.ug

www.busitema.ac.ug

THE IMPACT OF CREDIT RISK MANAGEMENT ON THE FINANCIAL PERFOMANCE OF COMMERCIAL BANKS IN UGANDA

A CASE STUDY OF DFCU BANK PALLISA BRANCH

BY

BY NANDERA ANNA

BU/UP/2018/3806

SUPERVISED BY MR. WADAMBISHA BRIAN

RESEARCH REPORT SUBMITTED TO BUSITEMA UNIVERSITY

FACULTY OF MANAGEMENT SCIENCES IN PARTIAL

FULFILLMENT OF THE REQUIREMENT FOR

THE AWARD OF A BACHELOR OF

BUSINESS ADMINISTRATION

APRIL, 2022

DECLARATION

I hereby declare that this research report is my original work and it has never before been presented elsewhere for any academic award. The pieces of work from other sources have been dully recognized.

NANDERA ANNA

SIGNATURE…………………………………………..

REG NO. BU/UP/2018/3806

APPROVAL

I confirm that this research report was done under my supervision and has been submitted for approval with my authorization.

Signature ……………………………….Date: ……………………………………

Mr. Wadambisha Brian

Supervisor

DEDICATION

This research report is dedicated to my dearly beloved parents Mr. Wabwire Amos and Mrs. Wabwire Sherin, Mr. Wadambisha Brian, my husband Mr. Opule Andrew who has been there for me and supporting me. Thanks for giving me hope in despair, joy in sorrow and ease in pain. May God bless you.

ACKNOWLEDGEMENT

First of all I would like to thank God the almighty for giving me wisdom and keeping me healthy. I would like to express my sincere thanks to the various people who have assisted me in any way to reach the completion of this research report. My most sincere appreciation goes to Mr. Wadambisha Brian for his effective supervision, commitment, guidance and constructive advice whenever I needed him. I thank him very much for availing me time and energy to ensure that this research report meets the University standard. I would like to acknowledge and thank my family members, relatives for all the great support financially, socially and spiritually. I extend my sincere gratitude to the management and staff of DFCU bank who availed me with the necessary data towards the accomplishment of this study. I do also appreciate the effort of friends and the entire discussion group for invaluable contribution extended to me in times of need and success towards my study. Finally I thank all those persons whom I have not mentioned specifically in the acknowledgement. I will always remember you for your kindness, constant support and encouragement.

MAY GOD BLESS YOU!

LIST OF FIGURES

LIST OF TABLES

LIST OF ACRONYMS AND ABBREVIATIONS

DFCU	**:**	Development Finance Company of Uganda.
BOU	**:**	Bank of Uganda
NPLs	**:**	Nonperforming loans
CBs	**:**	Commercial banks
ROA	**:**	Return on Assets
ROE	**:**	Return on Equity
ROI	**:**	Return on investments.
SPSS	:	Statistical package for social sciences

TABLE OF CONTENTS

ABSTRACT

This study was carried out with the purpose of analyzing the effect of credit risk management on the financial performance of commercial banks in Uganda with DFCU bank as the case study. Specifically, the study sought to establish whether there is a relationship between credit risk control, NPLs, and capital adequacy ratio and financial performance. In achieving the objectives assigned by the study, a descriptive cross sectional research design was used and that was facilitated by the use of both primary and secondary data which was obtained from the field and the published audited financial statements and the BOU annual supervision reports. The study used the census sampling technique where all members of the staff of DFCU bank participated in the study. The data was collected using questionnaires and analyzed using correlations and regression analysis. The findings revealed that there was a positive and significant relationship between credit risk control, NPLs, capital adequacy ratio and financial performance of DFCU bank. In conclusion, the findings showed that the above dimensions of credit risk management influence financial performance of commercial banks and therefore, the study recommended that DFCU bank should be well capitalized according to the size of its loan portfolio and regulatory requirement in order to advocate for improvement in its financial performance.

CHAPTER ONE

1.0 Introduction

This study was carried out with the purpose of determining the effect of credit risk management on the financial performance of commercial banks in Uganda. This chapter basically looked at the background of the study, statement of the problem, purpose of the study, research questions, and scope of the study, significance of the study, the conceptual framework and definitions of key terms.

1.1 Background of the study

The health of the financial sector is a major concern of policy especially in developing economies where failure in financial intermediation can disturb the economic growth and retards the development processes (Osborne, 2020). However, it has been proved that, major economic upheavals are the result of the banking crisis (Ameur, 2016). The economic development and financial growth of a country is critically dependent on the financial performance and strength of its banking sector (Rey, 2019)

Since the core activities of commercial banks is credit creation, this renders credit risk inevitable. As a result, credit risk is among the core risks related to the banks' main income generating activity and therefore bank failure is a problem in different countries (Hamza, 2017)

Available literature suggests that there is a global downward trend in financial performance of commercial banks. CBRC, 2015, Munyambonera, 2013; BOU, 2017). According to the china banking regulatory commission report (Feb 2015), poor financial performance has been observed to continue to increase for Chinese banks with non-performing loans of the country’s commercial bank increasing from 1.13 Yuan in 2014 to 1.15 Yuan in 2015, return on assets ratio also reduced from 1.40% to 1.30% in 2015. However, the regulator still assured the public that the bank’s asset quality was still under control.

In sub- Sahara Africa, despite financial reforms in the financial sector during 1980s and 1990s with a view of improving credit risk management, high levels of loan default, high levels of non-performing loans and operational inefficiencies (Mutua Virginia, 2012)), the problem of poor financial performance still prevails.

In Uganda, The profitability of the banking industry reduced in the year 2017 mainly due to increased provisions for bad debts and an overall rise in operating costs. The aggregate return

REFERENCES

Emerson, S. (2017). *CREDIT RISK MANAGEMENT AND FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN RWANDA : A CASE STUDY OF BANK OF KIGALI MUGANWA PACIFIQUE MBA / 2015 / 24941 A Research Project Submitted in Partial Fulfillment for the Award of a Degree of Master of Business Admini*. *March*.

Githaiga, J. W. (2015). *EFFECTS OF CREDIT RISK MANAGEMENT ON THE FINANCIAL PERFORMANCE*. *October*.

Githinji, W. (2015). *THE EFFECT OF FINANCIAL RISK MANAGEMENT ON THE FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN BY JOEL GITHINJI WANJOHI A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILMENT OF THE REQUIREMENTS OF THE MASTER OF SCIENCE IN FINANCE DEGREE , SCHOOL OF BUSINESS , U*. *October*.

Hamza, S. M. (2017). *Impact of Credit Risk Management on Banks Performance : A Case Study in Pakistan Banks*. *9*(1), 57–64.

Henry Martines. (2013). *CREDIT RISK MANAGEMENT AND FINANCIAL PERFORMANCE IN*. *12*.

Henry Martines, J. (2017). *THE EFFECT OF CREDIT RISK MAGEMENT ON THE FINANCIAL*. *November*.

Jn, T. (2014). *Credit Risk Management : Implications on Bank Performance and Lending Growth*. 584–590. https://doi.org/10.21276/sjbms

Kaimuri, K., & Nairobi, O. (2016). *EFFECT OF CREDIT RISK MANAGEMENT PRACTICES ON FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN BY KAUNA KAIMURI EVELYN A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTER OF SCIENCE IN FINANCE , UNIVERSITY OF NAIROBI NOVEMBER 2016*. *November*.

Kennedy, Z. J. F., & Kennedy, Z. J. F. (2012). *BUSINESS SURVEY LIQUIDITY MEASURE AS A LEADING*. *3*, 280–288.

Kithinji, A. M. (2010). *CREDIT RISK MANAGEMENT AND PROFITABILITY OF COMMERCIAL BANKS IN KENYA BY SCHOOL OF BUSINESS , NAIROBI – KENYA .*

OCTOBER , 2010.

Lamberg, S., & Vincent, J. (2020). *Impact of Liquidity Management on Profitability*.

Li, Y., Feng, Y. C., Chien, S., & Chih, W. (2016). Study of optimal capital adequacy ratios. *Journal of Productivity Analysis*. https://doi.org/10.1007/s11123-016-0469-z

Maiko, B. (2019). *THE EFFECT OF AGENCY BANKING ON THE FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA BRIAN MAIKO OMBUI A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION , SCHOOL OF BU*.

Masinde, K. B. (2017). *EFFECT OF CREDIT RISK ON FINANCIAL PERFORMANCE OF*.

Mathew, K. (2019). *FINANCIAL RISK MANAGEMENT AND FINANCIAL PERFORMANCE OF*.

Mercylynne, M. W., & Omagwa, J. (2017). *Credit Risk Management And Financial Performance Of Selected Commercial Banks In Kenya*. *19*(11), 92–98. https://doi.org/10.9790/487X-1911079298

Mutua Virginia. (2012). *THE IMPACT OF RISK BASED AUDIT ON FINANCIAL PERFORMANCE IN*.

Mwangi, Y. K. (2014). *THE EFFECT OF RISK MANAGEMENT ON FINANCIAL PERFORMANCE OF*. *October*.

Osborne, A. (2020). *CREDIT RISK MANAGEMENT AND FINANCIAL PERFORMANCE OF BANKING INSTITUTIONS : A CASE STUDY OF BANK OF KIGALI HABITEGEKO EMMANUEL MBA / 2014 / 79287 A Research Project Submitted in Partial Fulfillment of the Requirements for the Degree of Master of Business A*. *June*.

Rey, K. (2019). *EFFECT OF CREDIT RISK MANAGEMENT ON FINANCIAL PERFORMANCE OF*. *7*(5), 87–103.

Reymonds, J. (2016). *THE EFFECT OF RISK MANAGEMENT ON THE FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA BY CHARLES MUTUKU A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTERS IN BUSINESS ADMINISTARION , SCHOOL OF B*.

Rodah, C. (2017). *THE EFFECT OF CREDIT RISK MANAGEMENT ON THE PROFITABILITY OF COMMERCIAL BANKS IN KENYA BY A RESEARCH PROJECT SUBMITTED IN PARTIALFULFILLMENT OF THE REQUIREMENTS FOR THEAWARD OF THE DEGREE OF MASTER OF BUSINESSADMINISTRATION , SCHOOL OF BUSINESS , UNIVERSITY OF NAIROBI NOVEMBER 2017*. *November*.

Wood, A., & Mcconney, S. (2021). *The Impact of Risk Management on the Financial Performance of the Commercial Banking Sector in Barbados*.

Yvonne, G. (2015). *THE EFFECT OF NON-PERFORMING LOANS ON THE SIZE OF THE LOAN PORTFOLIO IN COMMERCIAL BANKS IN KENYA BY KINOTI YVONNE G . A RESEARCH PROJECT PRESENTED IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTER OF SCIENCE IN FINANCE , SCHOOL OF BUSINESS , UNIVERSITY OF NAIROBI NOVEMBER 2015*. *November*.