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CREDIT MANAGEMENT EFFECTS AND PERFORMANCE OF DEPOSIT MONEY BANKS IN NIGERIA

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Abstract: **The study investigated credit management effects and the performance of the Deposit Money Banks in Nigeria. The study used secondary data which was sourced from the Zenith Bank from 2009 to 2020. The chosen data was subjected to descriptive analysis, regression analysis, and granger causality. The findings reported that non-performing loan insignificantly positive to influence profit after tax, loan loss provision was significantly negative to influence PAT, loan to deposit ratio revealed a positive significant impact on PAT, and capital adequacy ratio exhibited a positive insignificant impact on PAT. The study concluded that no causal relationship between non-performing loan (NPL) and profit after tax (PAT), loan loss provision and profit after tax has no causal relationship, loan to deposit ratio (LDR) and profit after tax (PAT) revealed no uni or bi-directional relationship, and capital adequacy ratio (CAR) move free without any direction.**

Keywords**: Credit Management, DMBs, Loan loss Provision, and Non-performing loan.**

1. INTRODUCTION

The financial system does more than just a collection of institutions that encourage loans and expand credit. It includes all roles that channel actual resources to their intended users. It is a market economy's central nervous system, and it consists of a variety of distinct yet interdependent components that are all essential for the economy's productive and efficient operation. Banking sector have grown greatly in decades across the universe with the core roles of receiving consumer deposits and issuing funds in the form of loans, thereby playing a middle-man position between surplus unit and deficit unit as financial intermediary (Kegninkeu, 2018). The importance of banks to the nation lies largely in their ability to empower credit to different economic actors. Credit activities are the major banking functions and the most valuable commodity for credit institutions. In situations where credit is not adequately harnessed, managed, and handled, it has a crippling impact on banks, decreasing their efficiency, profitability and thus further contributing to banking crises and loss (Berger and Christa 2009). The possibility that a creditor will default on loan by failing to meet his own obligations is known as credit risk. When a creditor defaults, it is the consequence of replacing cash flow. From its inception, analyzing the financial soundness of creditors has been a central banking practice. The most critical feature of the banking industry, according to Cai and Anjan (2008), is credit management. It is the riskiest and most complex task undertaken by banks, as well as the most lucrative. The capacity of a bank to balance credit risk has always been crucial to its financial importance. Without an appropriate risk management, monitoring, and follow-up plan, this would not be possible. The hazard grows when credit principles are breached. Good banking policies enable bank management to set criteria for examining and accepting individual credit applications to ensure that loans given are repaid.

Credit risk is the most significant of the many challenges posed by banks, and the performance of banks is significantly impaired by the fact that a larger part of the bank 's profits is attributed to the provision of credit facilities from which interest is created. Meanwhile, Ekinci and Poyraz (2019) opined that credit management is an endogenous factor of performance in the banking industry. Ayunku and Uzochukwu (2020) viewed that credit management is written instructions, setting out the criteria, the consumer qualification requirements, the collection procedures, and the action to be followed in the event of a misbehavior of the customer. Credit management was a prominent player in the financial crisis, and it has gotten a lot of attention from the public and policymakers. This has prompted stakeholders and authorities in the Nigerian financial sector to review not just profits gained during business, but also the procedures used to regulate risks connected with credit facility in the sector, to protect shareholders' interests. The banking reforms took place against the backdrop of a financial crisis caused by DMBs' undercapitalization, poor management practices, and poor corporate governance standards (Uchendu, 2005). The restructuring and recapitalization were designed to halt anticipated or prospective banking sector crises, so avoiding future failures. Nevertheless, the impact of credit management cannot be belittled especially in the banking industry. Though it has hotly been discussed in the literature and still attracting to be discussed due to the inconsistencies in the outcome of the previous researchers.

2. LITERATURE REVIEW

In the banking industry, credit management has always been an important aspect of the loan process. Credit risk is the most critical of the many risks that banks encounter when conducting their financial intermediation functions, and banks' performance is determined by how well they manage this risk in comparison to other types of risks such as operating risk, political risk, and liquidity risk (Gieseche, 2004). The importance of the banking sector to economic growth through its intermediation responsibilities between the surplus and deficit sectors cannot be overstated; as a result, it is frequently referred to as a growth driver, especially in emerging markets with poorly performing capital markets. The success of the banking industry in terms of issuing credits to productive sectors with the intention of stimulating the economy's long-term growth and development is one of the indices for assessing the financial stability of any economy (Kolapo, Ayeni, & Oke, 2012). Of the many challenges that banks face, the most critical and difficult to control is credit risk, which is related not only to the issue of collateral and defaults, but also to the macroeconomic factors that have a direct effect on bank financial efficiency. Furthermore, the ability of banks to handle credit risk effectively is critical to their existence.

Credit management applies to the whole loaning process, starting with inquiring about potential borrowers and ending with the repayment of the amount borrowed including the interest. In the finance market, credit facility management is vital, with critical activities such as approving credit demands, credit assessment, acceptance, supervision, and, of course, rehabilitation of non-performing loans if they go wrong (Shekhar, 1985). Credit management is a dynamic concern on both a small and large scale. When a facility is established inadequately, it continues to boost loan costs, dissolves funds, and reduces financial institutions' flexibility to transferring assets into elective exercises. Furthermore, the higher the facility, the greater the risk. Advance default, which occurs because of inadequate credit management, reduces the financial institution's loaning ability. Similarly, as the financial institution's earnings management becomes shaky and vulnerable, the facility's acceptance of new applicants is limited. It can, however, disrupt the normal inflow and surge of assets.

Credit risk is a significant threat to bank profitability that, if left unaddressed, might result in bank collapse. For banks with insufficient risk management and control practices, liquidity exposure may be a trap. Given recent advances in the banking business, these two risks must not be disregarded, since they have a substantial influence on bank performance and sustainability. (Coyle, 2000). Successful credit and liquidity management strategies must be developed and completely enforced in banks to reduce the cumulative impact of these factors on the total default rate of banks.

Firm Performance is characterized as the execution of a duty in such a way that the participant is released from all obligations under the contract. Cheng, Wang, Lee, and Teng (2012) described firm performance as the amount of effort a company puts in to achieving their goals and argued that performance goals should be synonyms. Efficiency and effectiveness should be weighed when assessing a company's performance. Performance means doing the right thing, as indicated by the output-to-input ratio. Effectiveness is described as doing the right thing, a somewhat vague, non-quantitative term predominantly associated with achieving goals. The role of firm performance assessment is to make a reasonable way to analyze long-term strategic capacity and business value, not only to inform managers. Firm performance may also relate to an indicator of how effectively an organization can use resources from its main mode of operation to earn income.

Empirical Studies

The work of Oke and Wale-Awe (2018) discussed on the connection between credit risk and DMBs performance in Nigeria. They used ROE, loans and advances, loan loss provision and total asset as the variables. Regression analysis was employed and reported that credit risk has no significant influence on return on equity (ROE). At the same time, Kajola, Olabisi, Adedeji, and Babtolu (2018) carried out a survey on credit management effect on financial performance among deposit money banks in Nigeria from 2005 to 2016. The study used GLS method and revealed that credit risk variables exhibited a significant correlation with ROE and ROA respectively. Continuously, Olabamiji and Michael (2018) wrote on the connection between credit management and the performance of banks in Nigeria. Primary source of data was used where descriptive and regression analyses were conducted. They reported that positive relationship exists between credit management and performance of the banks. Serwadda (2018) examined credit risk impact on the performance of the Ugandan commercial bank between 2006 and 2015. The study employed regression analysis, correlation test and descriptive analysis and the techniques revealed that credit risk exhibited a significant impact on the banks of Uganda. Ekinci and Poyraz (2019) conducted a study on credit risk and financial performance among Turkish banks between 2005 and 2017. The study used ROA, ROE, NPLs, Size, GDPg TL/TA, TC/TA, and INF as indicators while descriptive analysis and regression analysis were employed as the estimation techniques. The results reported that NPLs showed a negative relationship to ROA and ROE. Innocent, Ademola, and Teryima (2019) combined credit risk, capital adequacy and operating efficiency on bank performance in Nigeria between 2008 and 2017. They employed panel random analysis and found that credit risk and operating efficiency exhibit negative effect on the performance of banks.

In the work of Gabriel, Victor and Innocent (2019), they investigated non-performing loan effect on the performance of the Nigerian commercial banks between 1985 and 2016. The study used regression analysis and cointegration test on these variables: cash reserve ratio, non-performing loan, inflation, and ROA. They reported that the control variables revealed a negative effect on the return on asset (dependent variable). More so, Okpala, Osanebi and Irinyemi (2019) used descriptive and regression analyses to conduct credit management impact on the profitability and liquidity in Nigeria. The study found that credit management revealed a positive impact on liquidity. Philip and Abisola (2019) carried out credit risk on the profitability of DMBs in Nigeria using regression analysis. They reported that credit risk exhibited a significant impact on profitability of the DMBs. Furthermore, Ajao and Oseyomon (2019) studied the connection between credit risk and DMBs performance in Nigeria between 2006 and 2016. Descriptive analysis, correlation test, pooled OLS and granger causality test were used as the estimation techniques. The study revealed that credit risk has a positive connection with performance of the DMBs. Al-Eitan and Bani-Khalid (2019) studied the relationship between credit risk and commercial bank performance in Jordan using panel data analysis. They reported that credit risk showed a negative impact on the performance of the commercial banks in Jordan. Ayunku and Uzochukwu (2020) wrote on the connection between credit management and bad debts among deposit money banks in Nigeria between 2014 and 2019. The study employed correlation and OLS analyses and found that credit management impact significantly on Return on Asset and Tobin-Q. Folajimi (2020) discussed the connection between credit risk and DMBs performance in Nigeria from 2006 to 2018. The study employed descriptive analysis and regression method and revealed that credit risk exhibited a positive impact on performance of the DMBs.

3. METHODOLOGY

Secondary form of external data was used and sourced from one of the DMBs in Nigeria. Meanwhile, the study purposely used Zenith bank plc because it was ranked number one among the top deposit money banks in Nigeria by Tier-one capital in 2021 with share capital worth of $2.79b and asset worth $15.7b. The data span from 2009 to 2020. The justification for the date was that 2009 marks the end period of financial crisis while 2020 was the period of pandemic.

The study employed descriptive analysis, regression analysis, and granger causality on a functional model to realize the general goal of establishing a link between credit management and DMBs performance in Nigeria. The model is shown below in its functional, mathematical, and econometric forms.

Functionality

$PAT = f(NPLR, LLPR, LDR)$ ----------eq1

Where:

PAT = Profit After Tax

NPLR = Non-performing loan ratio

LLPR = Loan Loss Provision Ratio

LDR = Loan to Deposit Ratio

Mathematical Form

$PAT = \tau_0 + \tau_1 NPLR + \tau_2 LLPR + \tau_3 LDR$ ----------eq2

Where:

τ_0 = Constant

τ_1 - τ_3 = intercept

Econometric Form

$PAT = \tau_0 + \tau_1 NPLR + \tau_2 LLPR + \tau_3 LDR + \varepsilon$ ----------eq3

Econometric Time Series Form

$PAT_t = \tau_0 + \tau_1 NPLR_t + \tau_2 LLPR_t + \tau_3 LDR_t + \varepsilon_t$ ----------eq4

Where:

ε_t = Error term

t = time series

4. RESULT DISCUSSION

Unit Root Report @ Level

Table 1: ADF and Critical Values

	ADF-test statistic	T-critical values @5%	P-value
PAT	-2.118244	-3.119910	0.2411
CAR	-1.472334	-3.119910	0.5151
LDR	-3.898358	-3.119910	0.0132
LLP	-4.401126	-3.119910	0.0056
NPL	-4.774611	-3.175352	0.0042

Source: Researcher's compilation

The unit root report presented in Table 4.1 shows the ADF t-stat values and the critical values with the p-values of all the variables. The PAT (profit after tax) has the ADF t-stat value of -2.118244 with critical value of -3.119910 and p-value of 0.2411, implying that PAT was not stationary at level. CAR (Capital adequacy ratio) has the ADF value of -1.472334, critical value of -3.119910 with p-value of 0.5151, meaning that CAR was not stationary at level. LDR (Loan to deposit ratio) has the ADF value of -3.898358, critical value of -3.119910 and the p-value of 0.0132, connoting that LDR was stationary at level. LLP (loan loss provision) has the ADF value of -4.401126, critical value of -3.119910 with p-value of 0.0056, implying that LLP was stationary at level. The NPL (Non-performing loan) has the ADF value of -4.774611, critical value of -3.175352 with p-value of 0.0042, indicating that NPL was stationary at level.

Table 2: Unit Root @ First Difference

	Augmented Dickey-Fuller test statistic	Test critical values @5%	P-value
PAT	-4.992829	-3.144920	0.0025
CAR	-3.606018	-3.144920	0.0234

Source: Researcher's compilation

The first differencing of the unit root reveals that PAT has the ADF value of -4.992829, critical value of -3.144920 and p-value of 0.0025, indicating that PAT was stationary only after first differencing. The capital adequacy ratio has the ADF value of -3.606018 with critical value of -3.144920 and p-value of 0.0234 connoting that CAR was stationary after first differencing.

Table 3: Integration Order

	P-value	
PAT	0.0025	Stationary
CAR	0.0234	Stationary
LDR	0.0132	Stationary
LLP	0.0056	Stationary
NPL	0.0042	Stationary

Source: Researcher's compilation

Integration order of the unit root shows that the variables ADF values in absolute terms are more than the critical statistic values and the p-values are less than 5% alpha level. However, the variables such as PAT, CAR, LDR, LLP, and NPL were stationary during the study period.

Descriptive Report

Table 4: Descriptive Analysis

	PAT	NPL	LLP	LDR	CAR
Mean	1.278030	0.328779	0.629735	1.098710	0.262850
Median	1.280087	0.045000	0.392735	0.566008	0.260000
Max.	1.715937	1.730902	2.266663	4.540828	0.357300
Min.	0.979138	0.018000	0.306110	0.442000	0.200000
Std. Dev.	0.246822	0.537182	0.599548	1.305167	0.043955
Skewness	0.462615	1.644832	2.115904	2.078112	0.467882
Kurtosis	2.163051	4.458338	5.734962	5.466027	2.594132
JB	0.907978	7.553374	14.80980	13.62403	0.606890
Probability	0.635090	0.022898	0.000608	0.001100	0.738271
Sum	17.89242	4.602905	8.816295	15.38194	3.679900
SumSq.Dev.	0.791973	3.751345	4.672951	22.14500	0.025116

Source: Researcher's compilation

The descriptive survey shows that the average value of PAT (profit after tax) is 1.278030, the median value of 1.280087, the max and min are 1.715937 and 0.979138. The Skewness value is 0.462615, Kurtosis has the value of 2.163051, and the JB statistic value with P-value are 0.907978 and 0.635090, this implies that PAT was positively skewed, and it was normally distributed. The non-performing loan (NPL) has the average value of 0.328779, the median value of 0.045000, the max and mi values are 1.730902 and 0.018000. the skewness and the Kurtosis values are 1.644832 and 4.458338 with the JB statistic and the p-value values are 7.553374 and 0.022898, this indicates that NPL was not normally distributed. The average of LLP (Loan loss provision) is 0.629735, the median value of 0.392735, the max and min values are 2.266663 and 0.306110. The skewness and the Kurtosis values are 2.115904 and 5.734962 with the JB statistic and the p-value values are 14.80980 and 0.000608, this indicates that LLP was not normally distributed. The average of LDR (Loan Deposit Ratio) is 1.098710, the median value of 0.566008, the max and min values are 4.540828 and 0.442000. The skewness and the Kurtosis values are 2.078112 and 5.466027 with the JB statistic and the p-value values are 13.62403 and 0.001100, this indicates that LDR was not normally distributed. The average of CAR (Capital Adequacy Ratio) is 0.262850, the median value of 0.260000, the max and min values are 0.357300 and 0.200000. The skewness and the Kurtosis values are 0.467882 and 2.594132 with the JB statistic and the p-value values are 0.606890 and 0.738271, this indicates that LDR was normally distributed.

Principal Component Report

Table 5: PCR

Extracting 5 of 5

Eigenvalues: (Sum = 5, Average = 1)

Number	Value	Difference	Proportion	Cumulative Value	Cumulative Proportion
1	3.106944	1.748614	0.6214	3.106944	0.6214
2	1.358330	0.923716	0.2717	4.465275	0.8931
3	0.434615	0.335245	0.0869	4.899889	0.9800
4	0.099370	0.098629	0.0199	4.999259	0.9999
5	0.000741	---	0.0001	5.000000	1.0000

Source: Researcher's compilation

The Eigenvalues principal component report shows that the value of the cumulative proportion of component 1 is 0.6214, component 2 has the value of 0.8931, component 3 has the value of 0.9800, indicating that the proportion of the variance explained of the variables are significant to explain the broad objective.

Regression Report

Table 6: Report of the regression

Dependent Variable: PAT

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.964310	0.402380	2.396516	0.0401
NPL	0.068356	0.271138	0.252109	0.8066
LLP	-3.600298	1.726270	-2.085593	0.0537
LDR	1.678469	0.844666	1.987140	0.0782
CAR	2.717633	1.612460	1.685395	0.1262
R-squared	0.634428			
Adjusted R-Sqr	0.471951			
F-statistic	3.904734	Durbin-Watson stat		2.313847
Prob(F-stat)	0.041629			

Source: Researcher's compilation

The report of the regression displays the variation of the independent variables against the dependent variable. The coefficient of the constant value is 0.964310, with std value of 0.402380, t-stat of 2.396516 and the p-value of 0.0401, signifying that at constant, a positive significant impact exists on the dependent variable. The NPL coefficient value is 0.068356, with the std value of 0.271138, t-stat of 0.252109 and p-value of 0.8066, implying that non-performing loan insignificantly positive to influence profit after tax. The coefficient value of loan loss provision is -3.600298, std value of 1.726270, t-stat value of -2.085593 with p-value of 0.0537, meaning that LLP was significantly negative to influence PAT. Loan to deposit ratio has the coefficient value of 1.678469, with std value of 0.844666, t-stat value of 1.987140 and p-value of 0.0782, indicating that LDR exhibited a positive significant impact on PAT. While capital adequacy ratio has the coefficient value of 2.717633, with std value of 1.612460, t-stat value of 1.685395 and p-value of 0.1262, connoting that CAR exhibited a positive insignificant impact on PAT.

Granger Causality Report

Table 7: P-Granger Causality

Causality Tests **** (means does not granger cause)		
Null Hypothesis:	F-Statistic	Prob.
NPL **** PAT	0.74183	0.5103
PAT **** NPL	2.13952	0.1883
LLP **** PAT	2.46590	0.1547
PAT **** LLP	1.51037	0.2849
LDR **** PAT	2.14088	0.1882
PAT **** LDR	2.42775	0.1582
CAR **** PAT	2.12779	0.1897
PAT **** CAR	3.82450	0.0754

Source: Researcher's compilation

The outcome of the granger causality testing reported that NPL and PAT has F-stat value of 0.74183 with p-value 0.5103 while PAT and NPL has the F-stat and p-value of 2.13952 and 0.1883, indicating that no causal relationship between non-performing loan (NPL) and profit after tax (PAT). The F-stat value of LLP and PAT was 2.46590 with p-value of 0.1547 while the causality between PAT and LLP has the value of 1.51037 with p-value of 0.2849, connoting that no causal relationship between the variables since their p-values are more than 5% alpha level. More so, the F-stat value of LDR and PAT was 2.14088 with p-value of 0.1882 while PAT and LDR has the F-stat value of 2.42775 with p-value of 0.1582, meaning that no uni or bi-directional relationship between LDR and PAT. Capital Adequacy Ratio (CAR) has the F-stat value of 2.12779 with the p-value of 0.1897 while the F-stat value between PAT and CAR was 3.82450 and p-value of 0.0754, indicating that the two variables move free without any direction.

5. CONCLUSION

The study concluded that non-performing loan insignificantly positive to influence profit after tax during the study period, loan loss provision was significantly negative to influence PAT. The loan to deposit ratio exhibited a positive significant impact on PAT and capital adequacy ratio exhibited a positive insignificant impact on PAT. Furthermore, it was concluded that no causal relationship between non-performing loan (NPL) and profit after tax (PAT), loan loss provision and profit after tax has no causal relationship, loan to deposit ratio (LDR) and profit after tax (PAT) revealed no uni or bi-directional relationship, and capital adequacy ratio (CAR) move free without any direction.

6. RECOMMENDATIONS

The executives should be mindful in setting up a credit strategy that will adversely influence productivity and they need to realize what credit strategy means for the operation of the organization to boost of benefit.

Inappropriate credit risk lessens organization's benefit, influences the nature of its resources, and expands advance misfortunes and non-performing loan which may ultimately increase financial distress.

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