ST. MARY'S UNIVERSITY

BUSINESS FACULTY

DEPARTEMENT OF ACCOUNTING

AN ASSESSEMENT OF NON-PERFORMING LOAN IN AWASH INTERNATIONAL BANK S.C.

BY

YOHANNESTESFAYE

MEKIN ESHETU

SISAY SEYFU

JUNE 2014

ADDIS ABABA

AN ASSESSEMENT OF NON-PERFORMING LOAN IN AWASH INTERNATIONAL BANK S.C.

A SENIOR ESSAY SUBMITTED

TO THE DEPARTEMENT OF ACCOUNTING

BUSINESS FACULTY

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FOR THE DEGREE OF BACHELOR OF ARTS IN

ACCOUNTING

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APPROVED BY THE COMMITTEE OF EXAMINERS

Department Head	Signature
Advisor	Signature
Internal Examiner	Signature
External Examiner	Signature

ACKNOLEDGEMENT

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AIB Awash International Bank

AML Anti Money Laundering

BFUB Bank Fusion Universal Banking

NPL Non-Performing Loan

TI Trade Innovation

CHAPTER ONE

1.1 BACKGROUND OF THE STUDY

Lending money is one of the important functions of a bank, this lending or advancing of money either upon or without security. Banks accept deposit from those who have surplus money and grant loans and advance to those who need them. Banks charge comparatively higher rate of interest on the amount advanced as a loan. (Kumaretal; 2002:40)

Non-performing loans as loans or advances whose credit quality has deteriorated, so that full collection of principal and/or interest in accordance with the contractual terms of the loan or advance is in question. (NBE Directive No. SBB/43/2007)

Awash International Bank S.C. (AIB) was established as the first private commercial bank (post 1991) on August, 1994 by 486 founder shareholders with a paid-up capital of Birr 24.2 million and started banking operations on February 13, 1995 with the main objective of serving as a commercial bank. Over the past nineteenth years, the amount of capital has increased to Birr 1.2 billion and plan to raise the paid-up capital of the bank to birr 1.5 billion. The bank has 115 branches and 887,000 customers. The total staff strength of the bank stood at 4,011 by the end of 2013, from 3,219 a year ago. It's the biggest private commercial bank in Ethiopia. (Annual Report of AIB; 2012/13)

The Bank aimed to replacing the existing CORE banking system (Bank master) with a new one. The implementation of the new CORE banking system would provide opportunities for installation of BFUB, TI, AML solutions. (Annual Report of AIB; 2012/13)

1.2 STATEMENT OF THE PROBLEM

Loans have a higher probability of default than any other assets because of the lack of liquidity and higher default risk, and also non-performing loan are the most challenging problem of banks in the world wide to earn the highest return on loans.

In AIB, NPL has increased by an average of Birr 143,486,028 (2.62%) for three consecutive years (2010/11 - 2012/13) even though the loan policies and procedures of AIB for NPL has been a maximum rate of 2% from the total loan. So, there is unanticipated increase of Birr 33,954,708.9(0.62%) deviation from the loan policies and procedures of AIB. (Annual report of AIB: 2010/11 - 2012/13, AIB Planning Document) Due to this data the student researchers want to assess the problem of Non-Performing Loan in Awash International Bank S.C.

Because of this problem, an attempt is made to look into the following research questions.

A What are the factors lead to NPL?
A What measures are taken to reduce NPLs?
A Are the loan policies and procedures has current and changing with the situation?
A How much NPL affects the bank's profitability with in 2010/11 - 2012/13?

1.3 OBJECTIVE OF THE STUDY

The objectives of the study are categorized as general and specific objective.

1.3.1 General Objective

The general objective of the study is to assess the current position of non-performing loans in Awash International Bank S.C.

1.3.2 The Specific Objective

The specific objective includes:

S To identifies the major factors of NPL in AIB's.
S To assess the methodology that the bank has used to reduce the amount of NPL in AIB's.

S To assess current and changing with the situation of loan policies and procedures of AIB.

S To assess the impact of NPL in bank's profitability.

1.4 SIGNIFICANCE OF THE STUDY

The main significance of this study are the following:

S To show students research theoretical knowledge in practical activities.

S To fulfill the requirements for the Bachelor's Degree in Accounting.

S To use as references material for others who have interest in the area of study.

1.5 SCOPE (DELIMITATION) OF THE STUDY

The scope of the study is delimited those loans become NPL in AIB at head office and also assess the impact of NPL in bank's profitability. The study covered the period from 2010/11 - 2012/13 G.C due to the confidentiality of information and uses data collected from AIB head office in credit department, which located in Addis Ababa specifically found behind National Theater.

1.6 LIMITATION OF THE STUDY

There are some limitations while performing this research on NPL in AIB. Those are listed below:

- Unwillingness of staff because of work load in credit department.
- Lack of information by the bank due to confidentiality.

1.7 RESEARCH DESIGN AND METHODOLOGY

1.7.1 Research Design

The study was concerned about the Non-Performing Loan of AIB. The study is descriptive because it is concerned with describing the characteristics of a particular individual, or of a group. Based on this reason the student researchers depend more on the existing data i.e. audited financial statement and related credit documents. So that

it describes the existing performance of the bank.

1.7.2 Population and Sampling Techniques

The population uses complete enumeration of all twenty credit department employees. Due to limited number of respondents, the student researchers applied census. This is presumed that in such an inquiry when all the items are covered no element of chance is left and highest accuracy is obtained.

The sampling method that has been applied in survey of data was purposive sampling method.

1.7.3 Data Sources

Both primary and secondary sources of data were used in order to achieve the real and factual result out of this study. Primary data were obtained from respondents i.e. AIB Credit management and staff members.

The secondary data were collected from audited financial statements, rules and regulation, reference books, directives and related documents which enabled the student researchers to collect relevant information directly from the Bank.

1.7.4 Data Collection Method

In order to collect the primary data through interview and questionnaires, that interview was made with vice executive manager of credit department while questionnaires were distributed for head office credit analysts, loan officers and former credit department staffs to have an overall insight about non-performing loans.

The secondary data also were collected from annual audited financial statements, journals, magazines, directives, internet, books and others documents about loan recovery performance.

1.7.5 Methods of Data Analysis

The collected data analyzed through different methods using tables, graphs, mathematical calculations such as percentages and the likes.

The study was organized into four chapters. The first chapter includes introduction part which contains background of the study, statements of the problem, significance of the study, scope of the study, research methodology and organization of the study. The second chapter concerns with presenting the review of the related literature. The third chapter deals with data analysis and interpretations. Finally, the fourth chapter presents summary, conclusions and recommendations.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

2.1 MEANING OF LOAN

Loan is an arrangement of advancing a sum of money on interest for a pre-agreed period sometimes for a particular purpose as well. As stated by Kumar and Mittal (2002:125), the main features of loan advanced by a bank are as given below:

i. The bank sanctions a sum of amount as loan for (a) per-arranged period, and (b) at an agreed rate of interest.

ii. A separate loan account is opened in the name of borrower with the amount of loan sanctioned.

iii. The loan sanctioned has to be taken in full and not partially as the full amount is transferred to the debit side of the account so opened and starts bearing interest from the date off entry in the debit side.

iv. From his loan account the customer is allowed to transfer the amount to his current account.

v. Installment repayment of loan is not permitted. But relaxation depends on the bank's discretion.

2.2 TYPES OF LOAN

As shown on National Bank of Ethiopia Directive No.SBB/32/2002, the major loan products or credit facilities practiced in Ethiopia are:

2.2.1 Short-Term Loans

A special commitment loan is a single-purpose loan with a maturity of less than one year. Its purpose is to cover cash shortages resulting from a one-time increase in current assets, such as a special inventory purchase, an unexpected increase in accounts receivable, or a need for interim financing.

Term loans finance the purchase of furniture, fixtures, vehicles, and plant and office equipment. Maturity generally runs more than one year but less than five. Consumer loans for automobiles, boats, and home repairs and remodeling are also of intermediate term.

2.2.3 Long-Term Loans

Long term loan is a formal agreement to provide funds for more than five years: most loans are for an improvement that will benefit the company and increase earning. Such loans would be used purchasing a new building that will increase capacity or a machine to make manufacturing more efficient. And it is granted for construction sectors, agriculture and mining.

2.3 SOURCES OF LOAN

According to Kandasami, Natarajan and Paraneswaran (2003:45), the banker solicits deposits from heterogeneous remaining types of people in different walks of life having different forms of financial status, thus introduced different kinds of accounts. They are:

Demand Deposits. Are popularly known as current accounts and are technically referred to as floating deposits. A customer can operate on his current account any number of times during a working day. Thus, it has unrestricted operation. No interest is allowed on current accounts by bankers in Ethiopia. A minimum balance is to be kept by the customer. This enables the banker to earn something on the minimum balance agreed to be kept. Current accounts are generally opened by large scale businessmen, joint stock companies, institutions, etc.

Saving Deposits. While current accounts are usually meant for business people, savings deposits are popular with fixed income receivers, particularly in the middle class. Today

commercial banks have found it to be profitable to accept savings deposits. To a commercial bank one great advantage in saving deposits is that it can maintain little cash reserve to meet withdrawals on these accounts.

Fixed Deposit. In addition to accepting money on current and savings deposits, bankers receive money on deposit accounts undertaking to repay the amounts on the expiry of affixed period, or subject to a notice. Fixed deposits are also known as Time Deposits, being repayable only after expiry of a particular time or period. It is defined as a deposit of a definite sum for a fixed period at a fixed rate of interest. It carries relatively higher rates of interest because fixed deposits enable the banker to employ the funds profitably for relatively longer period since they are not refundable as and when customer likes. The banker need not keep liquid cash resources on such deposits unlike on current accounts.

2.4 CREDIT INFORMATION

According to Kumar and Mittal (2002:197), before sanctioning loans and advances, the banker is required to assess the credit worthiness of the borrowers; a banker has to collect necessary information about the borrower. In advanced countries, there are specialized institutions engaged in the collection of credit information. Apart from this there are other sources from which credit information may be collected they are:

1. Information from the borrower himself.
2. Exchange of information among banks.
3. Market reports.
4. Tax returns.
5. Profit and loss account and balance sheet and
6. Records of the Registrar of Companies.

2.5 LEVEL OF ADVANCES

According to Kumar and Mittal (2002:197), the capacity to lend money is limited the level or size of advances sanctioned by a banker depends upon the following factors:

1. The size and maturity pattern of deposits.
2. Credit control policy.
3. Seasonal variations in bank credit.
4. The demand for credit.
5. Government's policy, and
6. General business conditions.

2.6 RECOVERABILITY

According to Clemens (1963:15), when a private investor lends his own funds, he will have in mind the following considerations:

a. Earlier than the expected duration of the loan should his own position require it;
b. Otherwise at the time or by the stated installments agreed with the borrower;
c. Should the borrower's position deteriorate (as may be evidenced by his inability to meet the periodical interest payments as they fall due) and early recovery becomes necessary to protect the lender's interests.
d. By realization of the security (direct or indirect) should the borrower fail to repay when repayment is due, by reason of bankruptcy or otherwise.

All these requirements are broadly satisfied by a well secured private mortgage in the usual form; that is, a loan secured by a readily saleable property.

2.7 CREDIT ANALYSIS WHAT MAKE A GOOD LOAN?

According to Rose and Hudgins (2008:521), the division or department responsible for analyzing and making recommendations on the fate of most loan applications is the credit department. Experience has show that this department must satisfactorily answer three major questions regarding each loan application.

A. Is the borrower creditworthy? How do you know?

B. Can the loan agreement be properly structured and documented so the lending institution and those who supply it with funds are adequately protected and borrower has a high probability of being able to service the loan without excessive strain?

C. Can the lender perfect its claim against the assets or earnings of the customer so that, in the event of default, the lender's funds can be recovered rapidly at low cost and with low risk?

According to Rose and Hudgins (2008:521), let's look at each of these three key issues in the "yes" or "no" decision a lending institution must make on every loan request.

A. Is the Borrower Creditworthy?

The question that must be dealt with before any other is whether or not the customer can service the loan-that is, pay out the credit when due, with a comfortable margin for error. The usually involves a detailed study of six aspects of a loan application: character, capacity, cash, collateral, conditions, and control. All must be satisfactory for the loan to be a good one from the lender's point of view.

Character. The loan officer must be convinced the customer has a well-defined purpose for requesting credit and a serious intention to repay. If the officer is not sure why the customer is requesting a loan, this purpose must be clarified to the lender's satisfaction. Even with a good purpose, however, the loan officer must determine that the borrower has a responsible attitude toward using borrowed funds, is truthful in answering questions, and will make every effort to repay what is owed.

Capacity. The loan officer must be sure that the customer has the authority to request a loan and the legal standing sign a binding loan agreement. This customer characteristic is known as the capacity to borrow money.

Cash. This feature of any loan application centers on the question: does the borrower have the ability to generate enough cash-in the form of cash flow to repay the loan? Lenders have a strong preference for cash flow as the principal source of loan repayment because asset sales can weaken a borrowing customer and make the lender's position as creditor less secure.

Collateral. In assessing the collateral aspect of a loan request, the loan officer must ask, does the borrower possess adequate net worth or own enough quality assets to provide adequate support for the loan? The loan officer is particularly sensitive to such features as the age, condition, and degree of specialization of the borrower's assets.

Conditions. The loan officer and credit analyst must be aware of recent trends in the borrower's line of work or industry and how changing economic conditions might affect the loan. A loan can look very good on paper, only to have its value eroded by declining sales or income in a recession or by high interest rates occasioned by inflation.

Control. The last factor in assessing a borrower's creditworthy status is control. This factor centers on such questions as whether changes in law and regulation could adversely affect the borrower and whether the loan request meets the lender's and the regulatory authorities' standards for loan quality.

B. Can the Loan Agreement Be Properly Structured and Documented?

The six Cs of credit aid the loan officer and the credit analyst in answering the broad question: is the borrower creditworthy? Once that question is answered, however, a second issue must be faced: can the proposed loan agreement be structured and documented to satisfy the needs of both borrower and lender?

The loan officer is responsible not only to the borrowing customer but also to the depositors or other creditors as well as the stockholders and must seek to satisfy the demands of all. This requires, first, the drafting of a loan agreement that meets the borrower's need for funds with a comfortable repayment schedule.

A properly structured loan agreement must also protect the lender and those the lender represents principally depositors, other creditors, and stockholders by imposing certain restrictions (covenants) on the borrower's activities when these activities could threaten recovery of the lender's funds. The process of recovering the lender's funds when and where the lender can take action to get its funds returned also must be carefully spelled out in any loan agreement.

C. Can the Lender Perfect Its Claim against the Borrower's Earning and any Asset the May be Pledged as Collateral?

Reasons for taking collateral. While large corporations and other borrowers with impeccable credit rating often borrow unsecured (with no specific collateral pledged behind their loans except their reputation and ability to generate earnings) most borrowers at one time or another will be asked to pledge some of their assets of to personally guarantee the repayment of their loans. Getting a pledge of certain borrower assets as collateral behind a loan really serves two purpose for a lender. If the borrower cannot pay, the pledge of collateral gives the lender the right to seize and sell those assets designated as loan collateral, using the proceeds of the sale to cover what the borrower did not pay back. Secondly, collateralization gives the lender a psychological advantage over the borrower.

The goal of a lender taking collateral is to precisely define which borrower assets are subject to seizure and sale and to document for all other creditors to see that the lender has a legal claim to those assets in the event of nonperformance on a loan.

Common types of loan collateral The following are examples of the most popular assets pledged as collateral for loans.

Accounts receivable

Factoring

Inventory

Personal property

Personal guarantees

Other safety devices to protect a loan

2.8 PRINCIPLE OF LENDING

As stated by Jhingan (1998:175), broadly speaking, every bank has to keep in view certain broad principles while deciding about investment of its funds. These principles are:

Safety. It means that the granted by the bank should be fully secured by adequate securities. While making investments, the bank should keep in mine the following points:

(a) That it should not advance loans to a few industries or a group of individuals or any single individual or any particular business at a time because that would mean keeping all the eggs in one basket and the bank may find itself in a very awkward situation if it does not get its funds back in times of emergency and may even fail. That is why in some countries the maximum amount of loan money which could be given to any individual or firm or a group of firms or industries has been prescribed under law.

(b) That it should ascertain carefully about the reputation and standing and creditworthiness of the borrower.

(c) That the value of the security must be properly assessed before granting the loan.

(d) That the loans should be given only for short periods.

(e) That it should not charge a rate of interest lower than what it pays on deposits.

Liquidity. It means that the banks' investments should be as far as possible liquid; in other words, these investments should be in such a form that these are easily converted into cash whenever required. This implies that the banks should not invest their surplus funds in immovable properties and unsalable or long-term securities. The bank should invest their funds

only in such types of securities which can be easily sold out in the market. It may also advance loans against easily saleable stocks.

Productivity. It means that the banks' investments must be productive. Since the objective of the banks is to earn maximum profits, their investments must be productive, that is, they should give maximum returns to the banks. It any, however, be noted that while applying the principle of productivity, the principle of safety is not to be sacrificed and that is why it has been the policy of the banks, all over the world, not to give loans for speculative purposes.

Diversity. Another guiding principle for the banks is that they should keep their investments in different types of securities and different types of business enterprises. If the banks invest in only one type of security or in a particular business enterprise and if the value of that security falls or if that security is not easily sold out or if that business enterprise suffers a setback, then the bank is bound to suffer.

Stability. The banks should also invest their funds only in such types of stocks and securities which are fairly stable in the market. In other words, if the price of these stocks and shares fluctuate frequently and widely, then the banks' chances of suffering losses increase tremendously.

Profitability. The banks should always invest their funds in those Government securities which are exempt for Income Tax; this would increase the total profits of the bank.

2.9 CREDIT MANAGEMENT

According to Arondekar and others (2005:271), credit management is the management of the credit portfolio of bankers and financial institutions. The expression "credit" refers to short term loans and advances as well as to medium/long term loans and off balance sheet transactions.

Management includes within its preview pre-sanction, appraisal sanction, documentation and disbursal and post lending supervision and control.

Credit management is no longer "Rule of the Thumb" game. In a highly competitive and deregulated environment banks and financial institutions have to evolve better system and procedures to manage the credit needs of highly demanding customers, particularly in the corporate and retail sectors. The developments of the past decade have totally changed the prospective of management of credit. As stated by Arondekar and others (2005:272), credit management now includes:

I. Capital adequacy norms.
II. Risk management including asset liability management (ALM)
III. Exposure norms.
IV. Risk pricing policy and credit risk rating.
V. Asset classification, income recognition and provisioning norms.
VI. Appraisal, credit decision-making and loan review mechanism.

Several risks affect credit decisions. The main risks are credit risk, market risk (mainly liquidity risk/ interest rate risk) and operational risk. Credit risk is defined as the possibility of losses associated with diminution in the credit quality of borrowers or counter parties. As stated by Arondekar and others (2005:272), such risks are:

i. Principal/interest amount may not be paid
ii. Payments or series of payments due from the counter parties may not be coming in case of treasury operations.
iii. Funds /securities settlement may not be affected in securities trading.
iv. Availability and free transfer of foreign currency funds may either cease or restrictions may be imposed by the sovereign.

2.10 MANAGING CREDIT RISK

According to Saunders and Cornett (2004:9), financial institutions are special because of their ability to transform financial claims of house hold savers efficiently into claims issued to corporations, individuals and governments. A financial institution's ability to evaluate

information and control and monitors borrowers allows them to transform these claims at the lowest possible cost to all parties. The credit risk involves in lending. A credit quality problem, in the worst case, can cause financial institutions to become insolvent, or it can result in such a significant drain on earnings and net worth that it can adversely affect the financial institutions profitability and its ability to compete with other domestic and international financial institutions.

According to Hubbard (2002:326), banks profit from the spread between the interest rate they charge to borrowers and the interest rate they pay to depositors. To ensure reasonable profits, banks attempt to make loans that will be fully repaid with interest. As with lending in financial markets, the bank is concerned about credit risk that is, the risk that borrowers might default on their loans. If banks do not manage credit risk effectively, they won't be profitable for their shareholders and won't be in business very long. Bankers must cope with adverse selection and moral hazard in managing credit risks of individual loans.

Moral hazard exists in bank loan markets because borrowers have an incentive, once they have obtained a loan, to use the proceeds for purposes that are detrimental to the bank. As stated by Hubbard (2002:326), banks use screening techniques, collateral requirements, credit rationing, monitoring, and restrictive covenants and develop long-term relationships with borrowers to help reduce costs of both adverse selection and moral hazard.

Diversification. The theory of portfolio allocation predicts that investors' individuals of financial institutions can reduce exposure to the risk of price fluctuations, by diversifying their holdings. This theory applies to banks as well; if banks lend too much to one borrower, to borrowers in one region, or to borrowers in one industry, they are exposed to risks from those loans.

Credit Risk Analysis. In performing credit-risk analysis, the bank examines the borrower's likelihood of repayment and general business conditions that might influence the borrower's ability to repay the loan. Individuals and businesses apply for loans to a loan officer, who manages the bank's relationship with the borrower, gathers information about the borrower and the purpose of the loan, and assesses the credit risk. To reduce the likelihood of adverse

selection, loan officer screen applicants to eliminate potentially bad risks and to obtain a pool of creditworthy borrowers.

Collateral. To combat problems of adverse selection, banks also generally require that the borrower put up collateral, or assets pledged to the bank in the event that the borrower defaults. Collateral reduces the bank's losses in the event of default because the bank can seize the collateral.

Credit Rationing. In some circumstances, banks minimize the costs of adverse selection and moral hazard through credit rationing. In rationing credit, the bank either grants a borrower's loan application but limits the size of the loan or denies a borrower's loan application for any amount at the going interest rate.

Monitoring and Restrictive Covenants. To reduce the cost of moral hazard, banks monitor borrowers to make sure that a borrower doesn't use the funds borrowed from the bank to pursue unauthorized, risky activities.

Long-Term Relationships. One of the best ways for a bank to gather information about a borrower's prospects or to monitor a borrower's activities is for the bank to have a long-term relationship with the borrower. By observing the borrower over time-through checking account activity and loan repayments-the bank can significantly reduce problems of asymmetric information by reducing its information-gathering and monitoring costs.

2.11 DEFINATION OF NON-PERFORMING LOAN

According to en.wikipedia.org/wiki/Non-Performing Loan, there is no universally accepted definition of Non Performing Loans; loan is considered to be non-performing when that loan is in default or close to being in default. A Non Performing Loan (NPL) is any loan in which; interest

and principal payment are more than 90 days overdue; or in other words there is more than 90 days' worth of interest has been refinanced, capitalized, for delayed by agreement; or payments are less than 90 days overdue but are no longer anticipated.

When we come to the Ethiopian context as stated by NBE Directive (No. SBB/43/2007), it is defined as:

Non-performing loans as loans or advances whose credit quality has deteriorated, so that full collection of principal and/or interest in accordance with the contractual terms of the loan or advance is in question.

Loans or advances with pre-established repayment programs are non-performing when principal and/or interest is due and uncollected for ninety consecutive days or more beyond the scheduled payment date or maturity.

2.12 TYPES OF NON-PERFORMING LOAN

For the purpose of proper follow-up and reviewing, Non-Performing Loans and Advances should be classified as stated by NBE Directive (No. SBB/43/2007), in to following five categories depending up on the level of arrears or overdue:

Pass. Loans or advances are categorized as pass when it has no arrears, the current financial and paying capacity of the borrower is strong and when we are confident for the repayment of the load.

Special Mention. These are loans and advances which are one or two re-payments in arrears and past due 30 (thirty) up to 89 (eighty nine) days.

Substandard. Past due repayment of loans and advances between 90 (ninety) days and 180 (One hundred eighty) days are sub standard loans.

Doubtful. Loans and advances which its repayment is past due 180 (One hundred eighty) days or more but less than 360 (three hundred sixty) days are said to be doubtful loans.

Loss. Loans and advances past due over 360 (three hundred sixty) days are considered as Loss. But this does not mean that the loans are not recoverable at a future date, or that there is no salvage value.

According to the Ethiopian context classification of all Non-Performing Loans whose repayments have been discontinued for 90-180 days as **"Substandard",** 181-365 days as **"Doubtful"** and over 365 days as **"Loan Loss".**

2.13 PROVISION

The provisioning requirements for loan loss account shall always have a credit balance. Additions to or reductions of the provisions for loan losses account shall be made only through charges to provisions in the income statement at least every calendar quarter. The minimum provision percentage differs from country to country. According to the NBE directive number SBB/32/2002 it is replaced by SBB/43/2007, the Ethiopia banks shall maintain the following minimum provision percentage.

Minimum Provision Percentages

	Classification category	**Minimum provision**
1	Pass	1%
2	Special mention	3%
3	Substandard	20%
4	Doubtful	50%
5	Loss	100%

According to NBE Directive (No.SBB/43/2007), when we assess the level of provision, the total level of provisions indicates the capacity of bank to effectively accommodate credit risk.

Adequate loan classification and provisioning practice are essential parts of a sound and effective credit risk level and provide general or specific provision. General provision is held for possible losses not yet identified where a certain percentage is provided for total loans and advances in a lump sum. On the other hand, specific provision is provided for identified losses. Depending on the magnitude of risk associated to each loan or advance.

DATA PRESENTATION, ANALYSIS AND INTERPRETATION

This chapter is concerned with the presentation and analysis of data on the basis of the questionnaire distributed and interview made based on primary data and secondary data sources gathered annual report of Awash International Bank Share Company. This secondary data received from the three consecutive years i.e. 2010/11, 2011/12 and 2012/13 G.C.

Furthermore, primary data has been collected from Awash International Bank credit department employees through distributing questionnaires and an interview made with the credit department manager. Out of the total of 20 questionnaires 18 were filled out and returned. The significance of causes and reducing methodology is ranked from one up to five; one given to low significance and five given to high significance.

3.1 CHARACTERSTICS OF THE STUDY

Table 3.1 Background of Respondents in AIB

S.No.	Item	Option	Number	Percentage
1	**Sex**	Male	13	72
		Female	5	27
		Total	18	100
2	**Age**	18-30 years	11	61
		31-40 years	7	39
		Above 40 years	-	-
		Total	18	100
3	**Education Level**	Certificate/Diploma	-	-
		1st Degree	15	83
		2nd Degree and above	3	17
		Total	18	100
4	**Experience on credit area in the bank**	Less than 1 year	2	11
		From 1-3 years	7	39
		From 3-5 years	3	17
		Above 5 years	6	33
		Total	18	100
5	**Position**	Low level manager	1	6
		Loan officer	7	39

		Credit Analyst Accountant	8 2	44 11
		Total	18	100

Source: Primary Data

Table 3.1 shows the back ground of the respondents in the credit department of AIB. As we can see in item 1 from table 3.1 there are 13(72%) male and 5(28%) female workers in the department. This shows the dominancy of male respondents in number compared to female.

According to item 2 regarding age of respondents in table 3.1 represents 11(61%) are between 18-30 years and the rest 7(39%) are between 31-40 years of age. This indicates majority of respondents are youngster and the rest are in the middle age.

As far as level of education in item 3 from table 3.1 shows 15(83%) are 1st degree holders and 3(17%) have 2nd degrees and above. This means the bank more concerned high status educational background of the employees to improve the effectiveness and efficiencies of bank services.

According to item 4 of table 3.1 regarding experience of respondents there are 2(11%) have less than 1year experience, 7(39%) have 1-3years experience, 3(17) % have3-5years experience, and 6(33%) have above 5years experience. The above shows the staff has more experienced due to there job.

As we can see in item 5 from table 3.1 there are 1(6%) manager, 7(39%) loan officers, 8(44%) credit analysts and 2(11%) accountants. This figure shows that the department is mostly composed of credit analysts and loan officers.

3.2 ANALYSIS OF FINDINGS OF THE STUDY

Table 3.2 shows the major factors of NPL at Borrower level. As shown in item 1 of table 3.2 from total respondents select strongly agree 3(16%), agree 9(50%), neutral 4(22%), strongly disagree 2(11%). This shows staff dominantly agrees that division of the borrowed fund to other purpose is the major factor of NPL at borrower level.

As we can see in item 2 of table 3.2 the respondents select strongly agree 1(5%), agree 9(50%), neutral 5(27%), disagree 3(16%). Based on this data the student researchers conclude that majority of respondents believes insufficient credit awareness may causes for NPL at borrower level.

Table 3.2 The Major Factors of NPL in AIB at Borrower Level

S.No.	Item	Options	Number	Percentage
1	Division of the borrowed fund to other purpose	Strongly agree	3	16
		Agree	9	50
		Neutral	4	22
		Disagree	-	-
		Strongly disagree	2	11
		Total	18	100
2	Insufficient credit awareness	Strongly agree	1	5
		Agree	9	50
		Neutral	5	27
		Disagree	3	16
		Strongly disagree	-	-
		Total	18	100
3	Unwilling customer to disclose the information required	Strongly agree	3	16
		Agree	8	44
		Neutral	6	33
		Disagree	-	-
		Strongly disagree	1	5
		Total	18	100
4	Contingencies at borrower level e.g. death and sickness	Strongly agree	3	16
		Agree	5	27
		Neutral	7	38
		Disagree	3	16
		Strongly disagree	-	-
		Total	18	100
5	Lack of proper business plan	Strongly agree	4	22
		Agree	7	38
		Neutral	5	27
		Disagree	1	5
		Strongly disagree	1	5
		Total	18	100

Based on item 4 of table 3.2 the respondents select strongly agree 3(16%), agree 5(27%), neutral 7(38%), disagree 3(16%). This indicates greater numbers of respondents are not support either agree or disagree in the case of Contingencies at borrower level i.e. death and sickness is the major factors of NPL at borrower level.

As shown in item 5 of table 3.2 from total respondents select strongly agree 4(22%), agree 7(38%), neutral 5(27%), disagree 1(5%), strongly disagree 1(5%). Due to this data more of staff members accept that lack of a proper business plan is another factor of NPL at borrower level.

Table 3.3 The Major Factor of NPL in AIB at Bank Level

S.No.	Item	Options	Number	Percentage
1	Lack of continues follow up and proper risk assessment	Strongly agree	1	5
		Agree	5	27
		Neutral	5	27
		Disagree	5	27
		Strongly disagree	2	11
		Total	18	100
2	Lack of consultation and communication with defaulter	Strongly agree	1	5
		Agree	4	22
		Neutral	3	16
		Disagree	8	44
		Strongly disagree	2	11
		Total	18	100
3	Lack of credit information from other commercial banks	Strongly agree	-	-
		Agree	3	16
		Neutral	4	22
		Disagree	5	27
		Strongly disagree	6	33
		Total	18	100
4	Problem associated with loan eligibility criteria's	Strongly agree	1	5
		Agree	2	11
		Neutral	9	50
		Disagree	2	11
		Strongly disagree	4	22
		Total	18	100

Table 3.3 represents the major factor of NPL in AIB at bank level. Our data shows the following figures: in item 1 of table 3.3 the respondents select strongly agree 1(5%), agree 5(27%), Neutral 5(27%), disagree 5(27%), strongly disagree 2(11%). This data represents greater number of respondents are not support either agree or disagree and also accept lack of continues follow up and proper risk assessment is not major factor of NPL at bank level.

In item 2 of table 3.3 from all respondents select strongly agree 1(5%), agree 4(22%), Neutral 3(16%), disagree 8(44%), strongly disagree 2(11%). These magnify that lack of consultation and communication with defaulter is not critical cause of NPL at bank level.

When we come to item 3 of table 3.3 the respondents select agree 3(16%), neutral 4(22%), disagree 5(27%), strongly disagree 6(33%). This figures show that the staff believes lack of credit information from other commercial banks is not the major factors of NPL at the bank side.

As we can see in item 4 of table 3.3 the respondents select strongly agree 1(5%), Agree 2(11%), Neutral 9(50%), disagree 2(11%), strongly disagree 4(22%). This clarifies that the respondents may not have any clue about problem associated with loan eligibility criteria's.

Table 3.4 The Major Factor of NPL in AIB at Economic Level

S.No.	Item	Options	Number	Percentage
1	Excessive government intervention	Strongly agree	1	5
		Agree	7	38
		Neutral	5	27
		Disagree	3	16
		Strongly disagree	2	11
		Total	18	100
2	Political power of borrower	Strongly agree	-	-
		Agree	2	11
		Neutral	9	50
		Disagree	4	22
		Strongly disagree	3	16
		Total	18	100
3	Impact of change in fiscal and monetary policies	Strongly agree	3	16

		Agree	9	50
		Neutral	5	27
		Disagree	-	-
		Strongly Disagree	1	5
		Total	18	100
4	Weak economic plan and strategic implementation	Strongly agree	-	-
		Agree	4	22
		Neutral	2	11
		Disagree	9	50
		Strongly disagree	3	16
		Total	18	100

Source: Primary Data

Table 3.4 shows the major factor of NPL in AIB at economic level. In item 1 of table 3.4 from total respondents select strongly agree 1(5%), agree 7(38%), neutral 5(27%), disagree 3(16%), strongly disagree 2(11%). Due to this data more of staff members accept that excessive government intervention is another factor of NPL in economy side.

Based on item 2 of table 3.4 the respondents select agree 2(11%), neutral 8(50%), disagree 4(22%), strongly disagree 3(16%). This indicates greater numbers of respondents are not support either agree or disagree in the case of political power of borrower is the major factors of NPL at economy level.

In the case of item 3 of table 3.4 the respondents select strongly agree 3(16%), agree 9(50%), neutral 5(27%), strongly disagree 1(5%). So, we can clearly Show that the major factor of NPL in AIB at economic level is Impact of change in fiscal and monetary policies according to the data collected from the staff.

As we can see in item 4 of table 3.4 the respondents select agree 7(38%), neutral 6(33%), disagree 2(11%), strongly disagree 3(16%). The student researchers conclude that there is no any diffusion in the weak economic plan and strategic implementation for the causes of NPL in the economic side.

To the question; what are the major causes of NPL in AIB? The response by the vice executive manger of the credit department said that; the major causes on NPL in AIB divided in to two. Those are;

1. Pre-disbursement

2. Post-disbursement

Pre-Disbursement is a type of NPL problem that caused by some errors that occur before loan has been given. Fore example;

- When the credit worthiness of the borrower doesn't check properly.
- When the borrower business plan doesn't analyzed properly.
- When the capacity/cash flow of the borrower doesn't confirm.
- When the borrower right doesn't examine in appropriate way i.e. minority, legal status and other condition of the borrower must be analyzed.

Post-Disbursement is a type of NPL problem that caused by some error that occur after loan has been given. For example;

- Borrower sickness (death, insanity, illness)
- Political problem
- Economic condition
- Change of loan policies and procedure
- International market condition (e.g. deflation of coffee market in 2012/13)

Table 3.5 The Bank's Credit Policies and Procedures

Item	Options	Number	Percentage
Are the credit policies and procedures current and changing with the situation (changing environment)?	Yes	16	88.89
	Neutral	1	5.56
	No	1	5.56
	Total	18	100

Source: Primary Data

From table 3.5 which is a data was acquired for the question; are the credit policies and procedures current and changing with the situation (changing environment), 16(88.89%) answered Yes, 1(5.56%) answered No and 1(5.56%) answered Neutral. This data shows the staff in the credit department believe that policies and procedures current and

changing with the situation or changing environment. Therefore policies and procedures in AIB are continuously changing with the situation on hand.

Based on these questions: What are the weakness of loan policies and procedures regarding to AIB? And what are the obstacles to fulfill loan policies and procedures in AIB? The vice executive manger of the credit department responded that; the loan policies and procedures has been made to reduce credit risk and also prepared by the following things;

- Business condition
- NBE directives
- Commercial laws
- Bazele committee laws (found in Netherland) and others.

There is some awareness of loan policies and procedures in Awash International Bank. For example; the loan policies and procedures amended through five years. Based on this it has its own effect on it. Some of the factors are;

- Economy fluctuation
- Changes of NBE directives
- The capacity of other competitor
- Political condition
- NPL can be happened due to dynamite of business condition.

The loan policies and procedures of AIB may not fulfill in different situations. For example due to long time duration of loan policies and procedures i.e. five years may not be meet with business conditions and bank services. Furthermore lack of knowledge in the case of practicing the loan policies and procedures is another factor to maintain.

Table 3.6 The Major Methodology to Reduce NPL in AIB

S.No.	Item	Options	Number	Percentage
1	Having proper analysis of the borrower's request and documents	Strongly agree	9	50
		Agree	7	38

		Neutral	1	5
		Disagree	1	5
		Strongly disagree	-	-
		Total	18	100
2	Having proper collection of the required information from other banks	Strongly agree	7	38
		Agree	6	33
		Neutral	4	22
		Disagree	1	5
		Strongly disagree	-	-
		Total	18	100
3	Giving sufficient credit awareness for borrowers	Strongly agree	8	44
		Agree	8	44
		Neutral	2	11
		Disagree	-	-
		Strongly disagree	-	-
		Total	18	100
4	Having efficient attention in treating NPL	Strongly agree	7	38
		Agree	10	55
		Neutral	-	-
		Disagree	1	5
		Strongly disagree	-	-
		Total	18	100
5	Giving full attention in treating NPL	Strongly agree	7	38
		Agree	10	55
		Neutral	-	-
		Disagree	1	5
		Strongly disagree	-	-
		Total	18	100
6	Having efficient loan collection mechanisms that your bank uses for loan recovery	Strongly agree	6	33
		Agree	10	55
		Neutral	1	5
		Disagree	1	5
		Strongly disagree	-	-
		Total	18	100

Source: Primary Data

Table 3.6 shows the major methodology to reduce NPL in AIB. In item 1 of table 3.6 justify that from the over all respondents select strongly agree 9(50%), agree 7(38%), neutral 1(5%), disagree 1(5%). This data represents the bank strive to prepare proper analysis of the borrower's request and documents in order to reduce NPL.

According to item 2 of table 3.6 from total respondents select strongly agree 7(38%), agree 6(33%), neutral 4(22%), disagree 1(5%). Therefore, to reduce NPL in AIB the credit department believes that having proper collection of the required information from other banks should be implemented in the bank.

As shown in item 3 of table 3.6 respondents choose strongly agree 8(44%), agree 8(44%), neutral 2(11%), from the given respondents. This situation clarify that giving sufficient credit awareness for borrowers is used to minimize NPL in the banking system.

As we can see in item 4 of table 3.6 from total respondents select strongly agree 7(38%), agree 10(55%), disagree 1(5%). Based on these result the student researchers reaches efficient attention in treating NPL is one way of reducing mechanism in AIB.

In item 5 of table 3.6 shows from the overall respondents select strongly agree 7(38%), agree 10(55%), disagree 1(5%). So that, to reduce NPL in AIB, giving full attention in treating NPL is a vital methodology.

When we come to item 6 of table 3.6 the given respondents choose strongly agree 6(33%), agree 10(55%), neutral 1(5%), disagree 1(5%). Due to these data the student researcher summarizes having efficient loan collection mechanisms that your bank uses for loan recovery is useful for deducting NPL at the bank.

The vice executive manger of the credit department answered the following respectively to this question. How do you assess the performance of NPL with regards to safeguarding of loans and advances? And how do you assess the adequacy and effectiveness of the NPL reducing methodology of the bank?

Most of the time borrower makes relation with the branch office. Based on this regard the branches assess the performance of NPL with related to safeguarding of loan and advances. The branches transfer some NPL loss to Head Quarter that cannot examine through branch level. And also give necessarily information to the Head Quarter by using different mechanism like meeting, discussion and other ways.

The adequacy and effectiveness of NPL reducing methodology assessed by based on employees comment and economic and market condition. While assess those methodology contained and implemented the 6th Cs credit criteria and other things.

Table 3.7 The Effect of NPL on the Bank's Profitability

Item	Options	Number	Percentage
How much NPL affects the bank's profitability	Low	6	33.33
	Medium	5	27.77
	High	7	38.89
	Total	18	100

Source: Primary Data

From table 3.7 which is a data was acquired for the question; How much NPL affects the banks profitability, 6(33.33%) answered low, 5(27.77%) answered medium and 7(38.89) answered high. From the data acquired we can see that the staff at the credit department believes that the bank's profitability is highly affected by NPL.

As per this question; how much NPL affects the bank's profitability? The Vice Executive Manger of the credit department said that; NPL has their own problem on the bank profitability. At the end of fiscal year it covers by provision fund. This provision for NPL is considered as loan expense. Due to this result the bank assume that the incremental of provision expense is the detrimental of profitability. For instance, the provision expense of AIB increased by Birr 6,035,798 million and in 2011/12 and by Birr 44,670,202 million in 2012/13. So, directly the profit of AIB is decreased by those amounts.

NON-PERFORMING LOAN POSITION

According to secondary data collected the position of NPL in AIB can be analyzed in the following manner.

Deposits versus Outstanding Loan

Table 3.8 Ratio of Outstanding Loan and Deposits

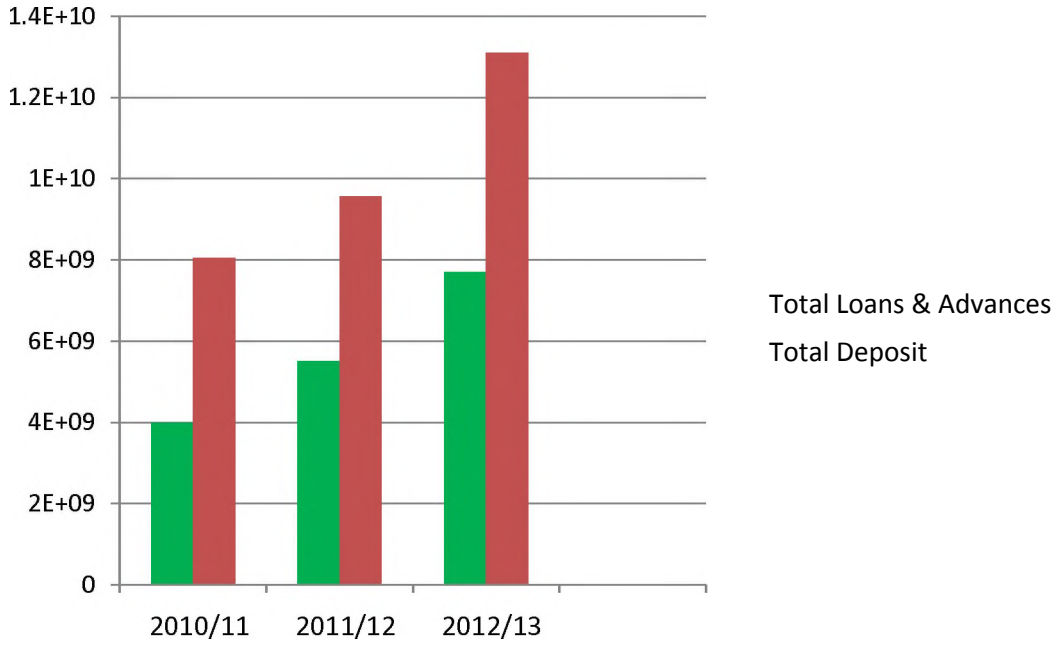
Deposit	Year		
	2010/11	2011/12	2012/13
Saving Deposit	5,647,594,700	6,565,012,100	8,505,559,900
Demand Deposit	2,014,009,000	2,158,287,900	3,289,689,100
Fixed Deposit	82,177,600	481,057,700	749,959,600
L/C Margin	300,754,200	360,182,400	559,587,900

Total Deposit	8,044,535,500	9,564,540,100	13,104,796,500
Outstanding Loan	3,986,464,776	5,504,610,376	7,709,998,250
Percentage Proportional	49.55	57.55	58.83

Source: Annual Report of 2012/13

Tables 3.8 and chart 3.1 can simply explain the growth trend and proportion of loan and deposit of AIB through three years data. Table 3.8 show the proportion that the loans and advances growth as total deposit increased. More or less the proportion has shown all increasing trend from year to year. Especially for the year ended 2012/13 it was 58.83% which has the highest amount the covered period. We can see chart 3.1 how then trend of both outstanding loan and total deposit were growing for the period starting from 2010/11 to 2012/13. This growth trends can also be seen on table 3.9.

Chart 3.1 Growth Rates of Outstanding Loan and Deposit



N.B E+09 represent Billion

Table 3.9 Growth Rate of Outstanding Loan and Deposit

Year	Outstanding Loan	Growth Rate	Total Deposit	Growth Rate
2010/11	3,986,464,776	-	8,044,535,500	-

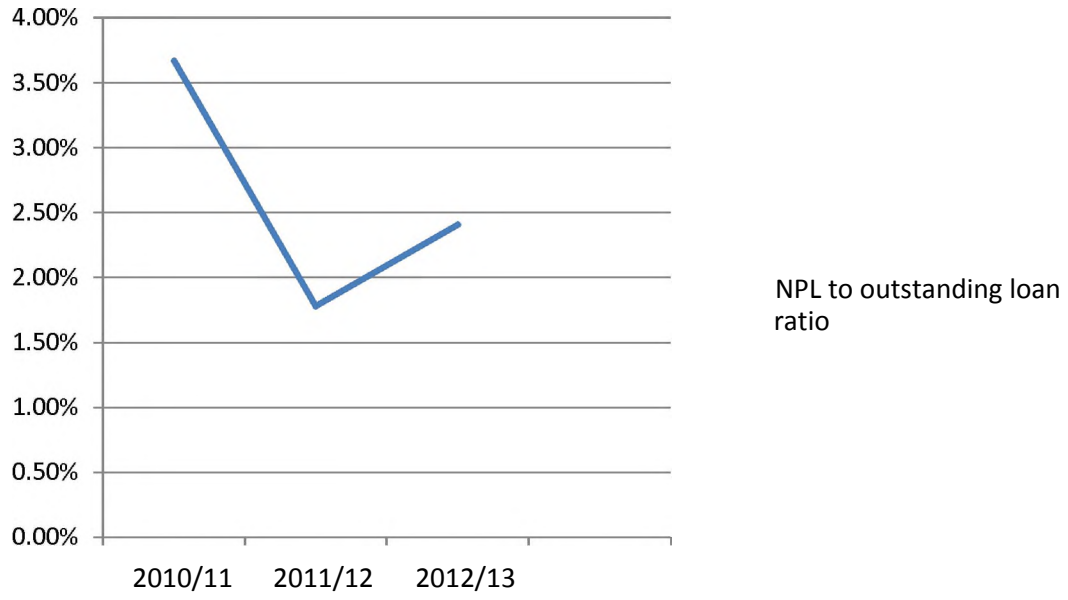
2011/12	5,504,610,376	38.08%	9,564,540,100	18.89%
2012/13	7,709,998,250	40.06%	13,104,796,500	37.01%

Source: Annual Report of 2012/13

Table 3.9 presents on what percentage that both outstanding loan and total deposit have been growing from year to year, when we compare the year 2011/12 to its consequent year 2012/13 the growth of outstanding loan and deposit were substantial i.e. 38.08% and 18.89% respectively. The outstanding loan went up from Birr 3,986,464,776 billion in year 2010/11 to Birr 7,709,998,250 billion in year 2012/13 depicting a growth of 93.4%. Similarly the total deposit increased from Birr 8,044,535,500 billion in 2010/11 to Birr 13,104,796,500 billion in 2012/13 i.e. a growth of 62.9%. Since branches are the principal interface between banks and their clients, the increase in the number of branches creates more opportunity for the bank to increase its loans disbursed and deposit. The other reason for the above mentioned improvement is the goodwill of bank that is developed through the three consecutive years.

Outstanding Loan versus NPL

Chart 3.2 NPL to outstanding Loan Ratio



Year	Outstanding loan	Total NPL	Percentage proportion
2010/11	3,986,464,776	146,232,055	3.67
2011/12	5,504,610,376	98,041,858	1.78
2012/13	7,709,998,250	186,185,115	2.41

Source: Annual report o' 2010/11-2012/13

Table 3.10 and chart *3.2* shows the total balance of NPL to outstanding loan ratio in percentage from 2010/11 to 2012/13 it decreases from 3.67% to 2.41%. This indicates that the total NPL of percentage proportion with outstanding loan is varying due to different constraints.

Composition of Income and Expense

Table 3.11 Composition of Income

Item	2010/11	2011/12	2012/13	Total income	Percentage
Interest income	394,708,700	668,692,900	890,192,100	1,953,593,700	56.49
Commission and service	257,139,100	251,323,800	322,727,200	831,190,100	24.03
Gain on foreign exchange dealings	255,682,500	166,912,000	171,464,000	594,058,500	17.17
Other income	20,019,300	23,802,100	35,317,900	79,139,300	2.28
Total				3,457,981,600	100

Source: Annual report of 2012/13

As we can see from table 3.11 interest income from loan and advance accounted for Birr 1,953,593,700 billion of the total revenue, which shows a slightly higher as compared to the other composition of the banks income. Therefore, the student researchers conclude that interest income is a major source of revenue.

Table 3.12 Composition of Expense

Year	Interest expense	salary and benefits	Administrative and general expense	Provision for Doubtful loans and advances	Total expense	Percentage
2010/11	209,473,100	121,146,800	86,647,200	5,213,000	422,480,100	22.97

2011/12	284935100	150,262,000	133,685,600	11,248,800	580,131,500	31.54
2012/13	362,656,900	248,934,600	169,172,200	55,919,000	836,682,700	45.49
Total					1,839,294,300	100

Source: Annual report of 2012/13

As the table 3.12 shows that interest expense during as of the year 2012/13 fiscal period incurred by Birr 362,656,900 million, which is reflection of the increase in the amount of interest bearing deposit. General expense and salary benefit also grow by Birr 82,525,000 and Birr 127,787,800 million respectively, mainly as a result of increase in staff salary, benefits and recruitment of new employees.

Growth Rate of Provision for NPL

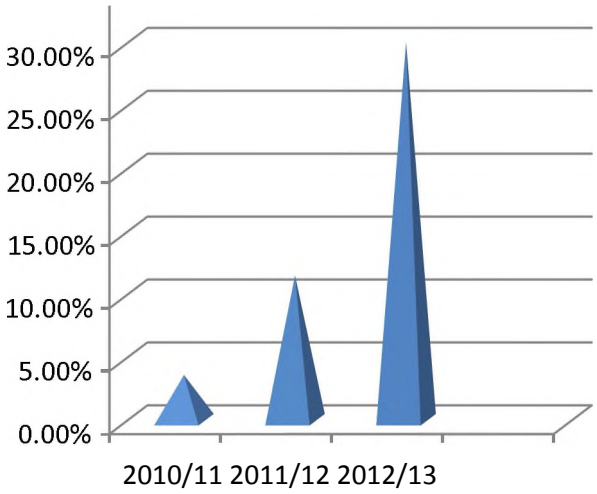
Table 3.13 Ratio of Total NPL to Provision for NPL

Year	Total NPL	Provision for NPL	Percentage Proportion
2010/11	146,232,055	5,213,000	3.56%
2011/12	98,041,858	11,248,800	11.47%
2012/13	186,185,115	55,919,000	30.03%

Source: Annual Report of 2010/11 - 2012/13

Table 3.13 and 3.14 shows that total NPL decreases in 2011/12, but increases during 2010/11 and 2012/13, provision for NPL increases from year 2010/11 up to 2012/13. Provision for NPL calculated from total NPL. According to these data the impact to increase or decrease of provision for NPL depends on the loans recovery.

Chart 3.3 Ratio of NPL to Provision for NPL



Provision for NPL/Total NPL

Table 3.14 Growth Rate for Provision for NPL

Year	Provision for NPL	Growth in Amount	Growth Rate
2010/11	5,213,000	-	-
2011/12	11,248,800	6,035,800	115.78%
2012/13	55,919,000	44,670,200	397.11%

Source: Annual Report of 2012/13

Growth Rate of Profit

Table 3.15 Growth Rate of Profit

Year	Total Profit	Growth in Amount	Growth Rate
2010/11	360,629,582	-	-
2011/12	394,423,070	33,793,488	9.37%
2012/13	438,608,637	44,185,567	11.2%

Source: Annual Report of 2010/11 - 2012/13

Table 3.14 represents the increasing of the bank profitability. Awash international bank registered an operating profit of Birr 438,608,637 million in the year 2012/13 fiscal year which is greater than that of the preceding year; it shows 11.2% increase last fiscal years profit. According to their audit report conducted by independent audit Service Corporation, the succeeding year profit increased by Birr 44,185,567 million that of the

preceding year. This magnifies the profitability of the bank increase through high collection of revenues.

Growth Rate of Profit as Compared With Growth rate of Provision for NPL

Table 3.16 Growth rate of profit as compared with growth rate of provision for NPL

Year	Growth of Provision for NPL	Growth of profit
2010/11		
2011/12	**115.78%**	**9.37%**
2012/13	**397.11%**	**11.2%**

Source: Annual Report of 2010/11 - 2012/13

Table 3.16 shows that the relationship between provision for NPL and profitability i.e. as we can see from the table in the year 2012/13 the growth rate of provision for NPL was 397.11% with that of same period the growth rate of profitability shows 11.2% that means the growth rate of profit is highly depend on the provision for NPL. Finally in the year 2010/11 up to 2012/13 the growth of profit shows minimum increasing amount in the case of growth of provision for NPL.

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

This research paper topic deals with the assessment of NPL in the case study of AIB. Particularly, the study focuses on the following basic questions. To what extent NPL affects its profitability, what are the major factors of NPL, what are the methodologies' to reduce NPL and what are the loan policies and procedures in AIB.

To gather the necessary information about the research title, data were collected using questionnaires distributed to all credit department employees of the bank and interview conducted with vice executive manager of the bank who are working at credit department. Out of 20 questionnaires 18 were filled out and returned. In addition to this; descriptive analysis method like percentage, tables and figures were used to analyze and present the data.

From the analysis and interpretation made in the previous chapter the following summary, conclusions and recommendation are drawn.

4.1 SUMMARY

Based on the analysis made in the previous chapter, the following major findings are summarized.

-I- As the result of the analysis, majority of the respondents 11(61%) were found in the age of 18-30 years and the rest 7(39%) are between 31-40 years of age.

-I- With regard to qualification of the respondents, majority of the respondents 15(83%) were degree holders and 3(17%) have 2nd degrees and above.

-I- 7(39%) and 8(44%) of the respondents are in the position of loan officer and credit analyst respectively.

The study indicates that, 9(50%) of respondents say division of the borrowed fund to other purpose is the major factors of NPL at borrower level and the others select strongly agree 3(16%), neutral 4(22%).

- The respondents replied to the problem of insufficient credit awareness of NPL at borrower level as follows, agree 9(50%), neutral 5(27%), disagree 3(16%).
- In addition on interview got the causes of NPL divided in to two, those are pre-disbursement and post-disbursement.
- The loan policies and procedures of AIB are almost all current and changing with situation (environment).
- Most of the respondents believe that having proper analysis of the borrowers request and documents is preferred methodology to reduce NPL.
- Almost all respondents replied have efficient loan collection mechanisms is another methodology to reduce NPL in AIB.
- To the question; how much NPL affects the bank's profitability, the respondents answered that 6(33%) low, 5(28%) medium and 7(39) high.
- From secondary data, the bank deposits and outstanding loans are increased by average rate of 27.95% and 39.07% respectively.
- Due to AIB annual report of 2010/11-2012/13, NPL shows an average increasing rate of 2.62% for those three consecutive years.
- The finding shows that when growth of provision for NPL in highest amount, the profitability of the bank become decreased by those amount.

4.2 CONCLUSONS

By considering the summary of findings the student researcher made the following conclusions.

- The majority of the respondents are youngsters. Due to these age group employees has willingness and power to create good image building and more preferable to facilitate customer service.
- Pre disbursement (at the bank level) and post disbursement (at the borrower and economic level) are affects the loan recovery performance in the bank. In addition post disbursement factors are difficult for banking activities to control.

-I- Insufficiency credit awareness and division of borrowed funds to other purpose is the one of the major problems that AIB in countered of Non-performing Loan.

-I- The credit policies and procedures of the bank are up to date and changing with environment but it may not fulfill in different circumstances and time duration.

-I- The profitability of the banks depends on the provisions for Non-performing Loan. I.e. increasing of provision for NPL and growth of profit are inversely related.

4- AIB's performance shows that it has an increasing trend in deposits and outstanding loans; this means the bank is in a faster lane to growth and also an increasing of Non-Performing Loans indicates that the bank has less effort in the area.

4.3 RECOMMENDATIONS

According to results of finding and conclusions made, the student researchers forward the following recommendations.

1. The bank should provide loan advisory service to borrowers by assigning qualified personnel because it improves the performance of loan collection.
2. The bank should use effectively its requirements for evaluating credit worthiness. Furthermore it should increase other requirements to reduce NPL like; analysis of documentation, evaluating collateral, feasibility of business plan and others.
3. The management body should improve the profitability of the bank through diversifying the outstanding loan to different less risky working environments.
4. AIB should focus on controlling of borrowers activities like; relations with previous creditors, suppliers, customers and others to minimize fraud and risky loans.
5. Lastly, the student researchers suggest that planning unit should place more emphasis on implementation and drafting of loan policies and procedures with changing environment.

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Appendices

St. Mary's University

Faculty of Business

Department of Accounting

Questionnaire

This questionnaire is designed and prepared by the student researchers at SMU doing research paper in partial fulfillment of requirement of degree in accounting. With this questionnaire the student researchers intends to assess management of AIB: special reference to head office credit department employees.

Please answer it the questions by making (/) either Yes or No; and write your answer for open end questions briefly.

Thanking you for the cooperation. We would like to inform you that all your responses will only be used for academic purpose and be kept confidentially.

N.B. You are not expected to write your name

1. **Personal data**

Gender: Male Female

Age: 18-30 Years 31-40 Years Above 41 Years

Level of Education: Certificate/Diploma 1st Degree

2nd Degree and above

Position: Manager Loan Officer

Credit Analyst Accountant

Experience on credit area in the Bank:

Less than 1 From 1-3

From 3-5 Ye Above 5 Y

2. Information related to Non-Performing Loan

N.B. 1 =Strongly Disagree 2 =Disagree 3 = Neutral

4 = Agree 5 = Strongly Agree

1. The major factors of NPL in AIB at borrower level:

Items	1	2	3	4	5
Diversion of the borrowed fund to other purpose					
Insufficient credit awareness					
Unwilling customer to disclose the information required					
Contingencies at borrower level e.g. Death and Sickness					
Lack of proper business plan					

If you think is another significant factors please specify.

2. The major factors of NPL in AIB at Bank level:

Items	1	2	3	4	5
Lack of continues follow up and proper risk assessment					
Lack of consultation and communication with defaulter					
Lack of credit information from other commercial banks					
Problems associated with loan eligibility criteria's					

If you think is another significant factors please specify.

3. The major factors of NPL in AIB at Economic level:

Items	1	2	3	4	5
Unstable political position					
Excessive government intervention					
Political power of the borrower					
Impact of change in fiscal and monetary policies					
Weak economic plan and strategy implementation					

If you think is another significant factors please specify.

4. The major methodology to reduce NPL in AIB:

Items	1	2	3	4	5
Having proper analysis of the borrower's request and documents					
Having proper collection of the required information from other banks					
Giving sufficient credit awareness for the borrower					
Having efficient and proper follow up risk assessment					
Giving full attention in treating NPL					
Having efficient loan collection mechanisms that your bank uses for loan recovery					

5. Are the credit policies and procedures current and changing with the situation (changing environment)? _____ _____ _____

Yes |_____| Neutral |_____] No |_____|

6. How much NPL affects the bank's profitability?

Low Medium High

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Interview Questions

For credit department vice executive manager

1. What are the major causes of NPL in AIB?
2. How do you assess the performance of NPL with regards to safeguarding of loans and advances?
3. How do you assess the adequacy and effectiveness of the NPL reducing methodology of the bank?
4. What are the weakness of loan policies and procedures regarding to AIB?
5. How much NPL affects the bank's profitability?
6. What are the obstacles to fulfill loan policies and procedures in AIB?

We, the undersigned declare that this senior essay is our original work, prepared under the guidance of Ato. Meseret Kinfe. All source of material manuscript have been duly acknowledged.

Names	Signature
Yohannes Tesfaye	_____
Mekin Eshetu	_____
Sisay Seyfu	_____

Place of submission: St. Mary's University

Date of submission: June 02, 2014

This paper has been submitted for examination with my approval as the university advisor.

Name_____

Signature_____

Date