



## Research Article

### ASSESSING THE EFFECTIVENESS OF CREDIT MANAGEMENT IN SELECTED SAVINGS AND CREDIT CO-OPERATIVES IN RWANDA

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The purpose of this study was to find out the effectiveness of credit management in selected SACCOs of Intarutwa and Umurenge in Rwanda. Descriptive design was used in this study and Slovene's formula was also used to determine a sample size of 132 respondents from 198 study population and the sampling was done by the use of simple random and purposive sampling techniques. Self-administered questionnaires and interview guides were used as research instruments for data collection. Both qualitative and quantitative data analyses were employed. Frequencies and percentages were used to determine the effectiveness credit management. Study findings reveal that credit management in the selected SACCOs was effective (mean of 2.60); The study recommended improvements should be made in the areas of cost effectiveness in collecting credits from clients; framework for the entire credit management exercise; disbursement and portfolio management up to loan repayment; establishing positive strategies instead of negative strategies that can encourage clients of the SACCO repay their loans on the agreed period of time; recruitment and training of special people in the assessment of client, their classification; and ensuring transparency in credit management.

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## INTRODUCTION

The history of savings and credit cooperatives in Rwanda dates back to the 1960s when they were established, although their existence was short-lived, as most of them became dormant because much focus was on farmers' cooperatives (Yin, 2003). However, in developing countries like Rwanda, there are low levels of saving culture owing to poor underdeveloped stock markets, dominance of urban based commercial banks, Micro Deposit Taking Institutions (MDIs) and non regulated Micro finance institutions in the financial markets as vehicles for savings (Yin, 2003). Hence Savings and Credit Cooperatives (SACCOs) are intended to offer an alternative to improve the above undesirable situation in low income countries. Savings and Credit Co-operatives (SACCOs) are community membership-based financial institutions that are formed and owned by their members in promotion of their economic interests (Annual reports of SACCOs Head Office, 2008).

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These institutions mobilize and intermediate savings exclusively with in their membership under the co-operative statute 1991. They are being promoted and developed by the government of Rwanda in an effort to alleviate poverty within the framework of Poverty Eradication Action Plan (EDPRS), through donor funded projects like Umwarimu SACCO, Rwanda Cooperative Agency, the government of Rwanda is also fully supportive of SACCOs' establishment, development under its financial services strategy (Annual reports of SACCOs Head Office, 2008). Therefore, Savings and Credit Co-Operatives (SACCOs), one of the several types of cooperatives are unique, legal, member-based Micro-Finance Institutions (MFIs) and unlike many other Micro-Finance Institutions, SACCO owners are also the users of the service that the SACCOs offer. Being socio-economic institutions, if well managed and organized, the financial performance of SACCOs can contribute favorably to bringing about Human Integrated Development (HID) (Uyemura and Deventer, 2003). Credit Unions and SACCOs are nothing new to Rwanda where diverse small SACCOs and Banque Populaire du Rwanda (BPR), the most important credit union, have operated for many years.

However despite a long history behind, SACCO's coverage remain very limited; with only 3% of the population saving with all MFIs in general, SACCOs included (Wyman, 2009). He noted that the principle products of SACCOs are savings and credit, however some offer money transfers, payment services and insurance. SACCOs sometimes join together to create second tier associations for the purposes of building capacity, liquidity management and refinancing; these second-tier associations can play a useful role in monitoring. Such associations can play a useful role in SACCOs reach out to low savings and income individuals by offer products geared towards their unique needs within a secure and accessible structure (Tummala and Burchett, 2009). The level of credit management among SACCOs is still ineffective if not poor (Babigambah, 2003). It is because of this that SACCOs are susceptible to offences that result in compliance gaps and loss of revenue. The author attributed poor financial performance of SACCOs in Rwanda to non-compliance, internal controls and poor record keeping. The financial performance of SMEs including SACCOs has also been poor because of limited resources and the capacity to attend to the complex tax rules and procedures for them to comply.

Credit management has been defined differently by various authors. According to Sewagudde (2000), Credit management involves the collection, compilation, storage, analysis and retrieval of information regarding trading on credit. In this regard, effective credit management requires that clear guidelines and procedures are laid down for granting credit to individuals and collecting individuals' accounts. Pandey (2006) defines credit management as the process or act of lending out sums of money to people whereby the whole process is controlled, planned, organized, acquired and coordinated. Pandey's definition is similar to that of Huberman and Miles (2008) as they viewed bank credit as anything or money borrowed in order to obtain something worth having which would be out of financial business and performance as a broad study of commerce and its operation, these include area. The Credit and Savings Cooperative of Intarutwa and Umurenge were created in 1990 and 1983 respectively with a few numbers of members because of the problems of people who didn't have the culture of savings and credit (Annual reports on Umurenge and Intarutwa, 2009, 2010). According to these reports, the two SACCOs currently have around 3313 members each. At first, SACCOs were controlled by orientation bureau of "Credit and Savings Cooperative", but later this was replaced by Union of Credit and Savings Cooperatives of Rwanda (Annual reports on SACCO, 2009).

SACCOs in Rwanda therefore try to undertake two two important missions and there are to receive deposits from their members and distribute loans to those who are in need. However, from 2007, SACCO started the assignment and process of operating as commercial banks and this is in order to increase the services provided to their clients and to expand its activities. Among these services include: foreign currency exchange, usage of smart card, increasing the amount of credit to be lent to their clients and selling and buying shares (Annual reports on SACCO, 2010). However, Pandey (2006) indicated in their research that ineffective and inappropriate credit management activities greatly affect the financial performance of financial and non-financial institutions as SACCOs fail to provide methodical classification and evaluation of the information provided by the income statement and balance

sheet so as to afford full diagnosis of the profitability and financial soundness of the business. It was therefore within this framework that this study attempted to analyze the effectiveness of credit management of selected SACCO as SMEs.

### Related Literature

Credit management involves the collection, compilation, storage, analysis and retrieval of information regarding trading on credit (Derban *et al.*, 2005). Effective credit management requires that clear guidelines and procedures are laid down for granting credit to individuals and collecting individuals' accounts (Pandey, 2006). Gitman (2002) also noted that credit standards influence the quality of the firms' customers in terms of time taken to repay credit obligation and the default rate in terms of bad debts and losses. To estimate the probability of default, the credit officer should consider the various characteristics of the clients, these may include; character, conditions, capital and collateral (Babigambah, 2003). Abel (2000) noted that whether a banker lends by over draft or credit, the result is the same. This increases the total volume of the purchase power, bankers and credit institutions can also create deposits by purchasing government stock, which is simply a method by which banks can also create deposits by purchasing government stock which is simply a method by which banks can lend themselves, however, this credit management make effective and efficient rate of business turnover in the production operation.

Porter, (1992) argued that the firm ought to be cautious with its collection procedures, as a tight collection procedure may offend and send away customers while a lenient one would increase receivables, bad debts and reduces profits. Mc Laney, (1991), goes on to say that at some stage it often becomes more costly to pursue reluctant payers than their debt worth, the firm should therefore decide what its procedures on write offs and bad debts should be, and ones established should be followed except in the un-usual circumstances. Santomero (2007) carried out their studies on the impact of credit management on the performance of financial institutions in China and their study found out that credit management is most of the financial institutions acts as the support, control systems and recovery practices to manage the outstanding risky assets, normal payment and to monitor business risk, properly. It therefore involves identifying the credit terms, correction procedures, credit period, and credit appraisal. For a sound credit management, it's necessary to formulate appropriate credit procedures which provide a frame work for the entire credit management exercise by providing parameters, defining responsibilities and establishing a system of checks and this ensured better performance of those financial institutions.

Menkhoff *et al.* (2006) also urged that there is need to develop cost effective measures for identifying credit customers, monitoring the status of customers' accounts and revenue collection procedures for customers with overdue bills as means of ensuring high financial performance. In similar way, as a way of ensuring high financial performance of Microfinance institutions in India, Gitman (2002) identified three important aspects of sound accounts receivable management. These are credit standards or analysis, credit terms and collection procedures.

According to him, if these three aspects of credit management are effectively put in place, microfinance institutions are likely to grow and develop as regards to their return and asset. Shanmugan and Bourke (2000) established that tremendous increase in consumer credit has taken place in recent years, consumers borrow from small finance companies such as Saving And Credit Cooperatives (SACCOs), credit unions, small loan departments of commercial banks, most finance companies do not obtain their loan able funds from the public, instead they borrow at a rate lower than those at which their clients can borrow. Credit unions are set up on cooperative basis for a particular group, such as civil servants employees, workers in large companies or women's groups in rural areas. Members in these groups can put their savings into credit unions, savings and credit cooperative society (SACCOs) and receive shares for the contributor; members can borrow at comparatively low rates of interest.

In most credit institutions, the technology that they use lays down the requirements for much of the human interactions in organizations (Kraft, 2000). The scholar noted that the arrangement of a product set up or loan determines who will borrow what in what quantity as per loan schedule sheet. This indirectly determines what individuals in smaller and in larger groups will borrow and think about a particular loan. Champlain (2003) reported that any financial firm in banking should act as a major source of information to its customers and the surrounding society as a whole. In some cases they invite inquires for those wishing to extend their foreign aid and are able through their correspondents to furnish the name of goods and services and also to advice on the appointment of suitable agents to act on.

## MATERIALS AND METHODS

The study used descriptive design in assessing the credit management in the SACCOs selected for this study, the population of the study in this research comprised of 198 employees and managers from the two selected SACCOs and these came from different branches of the SACCOs. These included employees from the two selected SACCOs that is, Intarutwa and Umurenge SACCO branches in Rwanda especially those from the departments of accounts, management, loan clerks, monitoring and evaluation among others.

The two SACCOs have been purposively selected since they are the first two and biggest in the country from the total population, the study sample 132 respondents. The study employed simple random and purposive sampling techniques. Simple random sampling was used to select employees of the SACCOs while purposive sampling was used to select the managers of the SACCOs. In using simple random sampling technique, the researcher collected the names of employees from two SACCOs and arranged them in their departments. Thereafter, the names were all numbered from number 1 up to 178. Then the researcher picked those whose names landed on even numbers (for example, 2, 4, 6 etc). Since those whose names landed on even numbers were less than the target established or required, the researcher decided to select more employees to reach the required sample size and consideration to pick respondents from different departments was also taken in to consideration until the total number of respondents is reached at 112.

Then for the managers, all of them were considered purposively such that evidence-based information regarding credit management and financial performance could be established. The methods of data collection that were used in the field included the questionnaire and interview guide. The data was obtained through questionnaires. And the data on the effectiveness of credit management was analysed using the frequency counts and mean ranges with the help of SPSS package.

## RESULTS AND DISCUSSION

The objective was to assess the effectiveness of credit management in selected SACCOs of Intarutwa and Umurenge and this was established by the mean values as shown below. Mean ranges from 1.00-1.75 portrayed that majority of the respondents strongly disagreed with the statement thus, the credit management of the selected SACCOs in Rwanda was very ineffective; mean ranges from 1.76-2.50 showed that majority of the respondents disagreed with the statement thus, the credit management of the selected SACCOs was ineffective; mean ranges from 2.51-3.25 indicated majority of the respondents agreed with the item investigated thus, the credit management of the selected SACCOs was effective; and lastly; mean ranges from 3.26-4.00 portrayed that majority of the respondents strongly agreed with the item under investigation thus, credit management in the selected SACCOs was very effective.

Table 1 shows that respondents rated some items under credit management effective and others were ineffectively rated. The most effective credit management is shown in collection procedures (mean of 2.71); this is followed by the credit appraisal (mean of 2.66); then, credit terms (2.54); and the most ineffective credit management is manifested in credit period (mean of 2.50). Among the items rated effective, the most highly rated item was on tools like covenants, collateral, credit rationing, loan securitization and loan syndication being effectively used at the SACCO (mean of 2.89); this was followed by the SACCOs using telephone, writing, and collection agencies to recover loans (mean of 2.88); then, policies and strategies for loan recovery being well established at SACCOs (mean of 2.87); next was on the borrowers being first assessed both quantitatively and qualitatively in SACCO (mean of 2.80); followed by the responsibilities for credit management at the SACCO being well established and this helping in establishment of checks (mean of 2.79); then, documentation of credit facilities being effectively done at SACCO (mean of 2.74); followed by the analysis of information about the institutions' credit being well done (mean of 2.69); next was on the information regarding the institution's credits being well stored; and that normal payments being effectively done and business risks being clearly monitored (mean of 2.67); then, clear guidelines and procedure on the institutions credit being effectively laid down (mean of 2.64); then followed by there being control systems and recovery practices to manage the outstanding risks at SACCO (mean of 2.61); and finally that lending markets and credit initiation at this SACCOs being well done (mean of 2.53). However respondents disagreed with some of the items on credit management in the selected SACCOs. They disagreed that accounts and revenue collection procedures in the SACCOs are cost effective (mean of 2.44); they also disagreed that there is

**Table 1. Mean Values Showing Effectiveness of Credit Management in Selected SACCOs in Rwanda**

	Mean	Rank	Interpretation
<b>CREDIT MANAGEMENT</b>			
<b>Credit Terms</b>			
Tools like covenants, collateral, credit rationing, loan securitization and loan syndication are effectively used at the SACCO	2.89	1	Effective
The borrowers are at first assessed both quantitatively and qualitatively in SACCO	2.80	2	Effective
At this SACCO, lending markets and credit initiation are well done	2.53	3	Effective
The financial institution distinguishes bad borrowers from good borrowers	2.30	4	Ineffective
Stakeholders can retrieve the data concerning the credits of SACCO	2.18	5	Ineffective
Mean Average for Credit Terms	2.54		Effective
<b>Collection Procedures</b>			
The SACCO uses telephone, writing, and collection agencies to recover loans	2.88	1	Effective
There is proper collection of information regarding credits in SACCO	2.82	2	Effective
Accounts and revenue collection procedures in the SACCO are cost effective	2.44	3	Ineffective
Mean Average for Collection Procedure	2.71		Effective
<b>Credit Period</b>			
Normal payments are effectively done and business risks are clearly monitored	2.67	1	Effective
There is timely control systems and recovery practices to manage the outstanding risks at SACCO	2.61	2	Effective
Disbursement and portfolio management up to loan repayment is timely and properly done at SACCO	2.37	3	Ineffective
Clients of the SACCO repay their loans on the agreed period of time	2.36	4	Ineffective
Mean Average for Credit Period	2.50		Ineffective
<b>Credit Appraisal</b>			
Policies and strategies for loan recovery are well established at SACCO	2.87	1	Effective
Responsibilities for credit management at the SACCO are well established and this helps in establishment of checks	2.79	2	Effective
Documentation of credit facilities is effectively done at SACCO	2.74	3	Effective
The analysis of information about the institutions' credit is well done	2.69	4	Effective
The information regarding the institution's credits is well stored	2.67	5	Effective
Clear guidelines and procedure on the institutions credit is effectively laid down	2.64	6	Effective
There is provision of sound framework for the entire credit management exercise in SACCO	2.42	7	Ineffective
The financial institution has sound accounts receivable management	2.42	8	Ineffective
Mean Average for Credit Appraisal	2.66		Effective
Overall Mean Average	2.60		Effective

Source: Primary Data

**Table 2. Difference in the Effectiveness in Credit Management and Level of Financial Performance between Umurenge and Intarutwa SACCO**

Variable	Category of saccos	Mean	F	Sig.	Interpretation	Decision on HO
Credit Management	Intarutwa SACCO	1.1838	1.762E	0.000	Significant difference	Rejected
	Umurenge SACCO	2.9559				
	Average Mean	2.06985				

Source: Primary Data

provision of sound framework for the entire credit management exercise in SACCO; and that the financial institutions have sound accounts receivable management were all disagreed with at the mean of (mean of 2.42); they continued to disagree that disbursement and portfolio management up to loan repayment is properly done at SACCOs (mean of 2.37); they also disagreed that clients of the SACCOs repay their loans on the agreed period of time (mean of 2.36); they further disagreed that the financial institution distinguishes bad borrowers from good borrowers (mean of 2.30); and finally, respondents disagreed that stakeholders can retrieve the data concerning the credits of SACCO (2.18).

Although some items were highly rated and others were lowly rated, the general picture drawn from the overall average mean of 2.60 is that the credit management of the two selected SACCOs is generally effective since the mean value falls under effective under the rating scale. The information obtained from the key informants through interviews was also consistent or in line with the one obtained through questionnaire. In other terms, those interviewed clearly mentioned that their SACCOs have streamlined the entire credit management framework to minimize gaps that have been involved in credit management.

One of the key informants was quoted saying, "In order to improve credit management of this SACCO, we train, appraise and evaluate our employees periodically. This has enabled our employees to get dedicated and realistic in the manner in which they administer their duties." From the two SACCOs, at least two further training programs have been organized for employees; 4 employees of Intarutwa SACCO have been supported to advance their studies and currently 3 of those from Umurenge have been financed to advance their studies at post graduate levels.

One of the key informants was also quoted saying, "As a way of improving credit management of our SACCO, we have resorted to employing professional. In all our branches, we have at least diploma holders and most of our employees are graduates in particular fields. This has helped us to reduce cases of negligence in credit management among employees."

The following were some of the key procedures key informants interviewed mentioned as important for their SACCOs to deal with issues related to credit and they include: considering covenants, collateral, credit rationing, loan securitization and loan syndication; assessment of borrowers both quantitatively and qualitatively; proper documentation of credit facilities;

streamlining control systems and recovery practices to manage the outstanding risks; and minimizing cost related to accounts and revenue collection procedures. From the information obtained through interview guide, it is clear that the SACCOs have made all attempts to make their credit management more effective than before.

### Difference in the Effectiveness in Credit Management between Umurenge and Intarutwa SACCO

To establish whether there is a significant difference: (a) in the effectiveness of credit management between Umurenge and Intarutwa SACCOs; Significant differences in these items were determined by the use of using both the F-test and mean differences derived from ANOVA. The summary on this is presented in Table 2. Table 2 indicates that there is a significant difference in the level of different credit management between Umurenge and Intarutwa SACCOs. This significant difference is indicated in the differences of mean values computed (1.1.838 for Intarutwa SACCO and 2.9559 for Umurenge SACCO) and at the F value of 1.762E and significant value of 0.00. Thus, the SACCO with the best credit management is Umurenge SACCO and this is justified by its higher mean value of (2.9559) against Intarutwa SACCO with mean value (1.1838). Thus, the result shows that there is no significant difference in the credit management between Umurenge and Intarutwa SACCOs. Although none of the SACCOs admitted that the author they were not well in credit management was lower than the other, the information obtained from the two SACCOs revealed that the two SACCOs had differences in credit management. This was justified by the number of clients of each SACCO, their number of branches, the qualification of the people they employed. In general, Umurenge was more effective in credit management as most of its employees were professions; the SACCO also had 4 % more customers than its counterpart; and it had 5 more branches than Intarutwa. These details reveal that there were differences in credit management between the two selected SACCOs in Rwanda and this confirms the information obtained through questionnaires.

### Conclusions

From the research findings, the following conclusions have been derived. This study concludes that the credit management at the two SACCOs in Rwanda is effectively done as tools like covenants, collateral, credit rationing, loan securitization and loan syndication are effectively used at the SACCOs; the SACCOs use telephone, writing, and collection agencies to recover loans; the policies and strategies for loan recovery are well established at SACCOs; the borrowers are first assessed both quantitatively and qualitatively in SACCOs; the responsibilities for credit management at the SACCO are well established and this helps in establishment of checks; the documentation of credit facilities are effectively done at SACCOs; the analysis of information about the institutions' credit are well done; the information regarding the institution's credits are well stored; the normal payments are effectively done and business risks are clearly monitored; the clear guidelines and procedure on the institutions credit are effectively laid down; there are control systems and recovery practices to manage the outstanding risks at SACCOs; and the lending markets and credit initiation at this SACCOs are well done.

### Recommendations

- The management of the selected SACCOs should consider revising and reestablish it procedures of collecting credits from clients so as to be cost effective. This can be done by using alternative and cheaper sources of debt collection procedures.
- The management of the selected SACCOs should also consider establishing sound framework for the entire credit management exercise. This could be done engaging in research and consulting experts in related field. Such exercise can lead to effectiveness in credit management.
- Since the disbursement and portfolio management up to loan repayment were not properly done at the selected SACCOs, the management of the banks should also address weaknesses resulting from these areas. This can be done by offering further training opportunities to the staff such that they can demonstrate their abilities in managing disbursement and portfolio.
- The management of the SACCOs should also establish in place positive strategies instead of negative strategies that can encourage clients of the SACCO repay their loans on the agreed period of time. This can be done by providing some attractive incentives such as cutting down interest for such clients, recognizing their efforts and many other ways.
- The management should also recruit and train some special people in the assessment of client, their classification. If this is to be done, the SACCOs can greatly improve in distinguishing bad borrowers from good borrowers.
- To improve on effectiveness in credit management and ensure transparency in credit management, stakeholders can retrieve the data concerning the credits of SACCO. This practice can trust and lead to increase in customer base.

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