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COLLEGE OF BUSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING & FINANCE

**THE IMPACTS OF LOAN POLICY ON FINANCIAL PERFORMANCE OF
PRIVATE COMMERCIAL BANKS IN ETHIOPIA**

**THESIS SUBMITTED TO ADDIS ABABA UNIVERSITY COLLEGE OF
BUSINESS AND ECONOMICS DEPARTMENT OF ACCOUNTING AND
FINANCE IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR
DEGREE MASTERS OF SCIENCE IN ACCOUNTING AND FINANCE**

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FEBRUARY, 2022

ADDIS ABABA, ETHIOPIA

Statement of Declaration

I, Gezahegn Deribew, declare that this research, titled "the impact of loan policy on the financial performance of private commercial banks in Ethiopia: I produced it independently except for the guidance and suggestions of my research advisor," was done entirely by me. This study still hasn't been submitted for any scholarly award at this or any other university, I assure you.

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Approval

The thesis, titled “The impact of loan policy on the financial performance of private commercial banks in Ethiopia,” was original and had not been submitted for examination at any other university, and it was submitted for partial fulfillment for the award of a MSc. Degree in Accounting and Finance.

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Abstract

The main objectives of the study was to assess the impact loan policy on financial performance private commercial bank in Ethiopia and the specific objectives of the study would be to assess the loan term and condition policy, loan lending policies, loan monitoring policies, loan collection policies, and loan default management policies and their effects on the financial performance. The scope of the study would be limited to six selected experienced private commercial banks in Ethiopia. The research design used both descriptive and explanatory research design. The target respondents were the general loan directorate manager and loan officer which total respondents were 118. To obtain a representative sample, the study used a purposive sampling method to sample loan directorate managers of selected private commercial banks of Ethiopia and a simple random sampling technique to select loan officers. Descriptive and inferential statistics would be analyzed by using the Statistical Package for the Social Sciences (SPSS). Data collected through primary and secondary sources. There were a moderate correlation between loan policies and financial performance. Loan term and condition policy, loan lending policies, loan monitoring policies, loan collection policies, and loan default management policies were positive and significant effect on the financial performance of the selected commercial bank in Ethiopia. The researcher recommended that private commercial banks to revise their loan policies in order to make loan funds available to their retail and corporate customers, to control loan diversion, providing training to manager and loan officers, carry out adequate financial analysis and reduce interest rates as a way of reducing loan defaults, commercial banks develop their own website and system related credit management. The study suggests that further study should be to investigate the effect of various loan policies in influencing the borrower's decision and major factors to prepare loan policies.

Key word, loan policy, monitoring, collection, default & financial performance

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List of Abbreviation

ANOVA	Analysis of Variance
ATM	Automated Teller Machines
CBE	Commercial Bank of Ethiopia
DBE	Development Bank of Ethiopia
KI	key informants
MSME	Micro and small medium enterprise
NBE	National Banks of Ethiopia
NIM	Net Interest Margin
ROE	Return on Equity
ROA	Return on Asset
POS	Point of Sale
SACCO S	Savings and Credit Co-operative
SPSS	Statistical Packages for Social Science

CHAPTER ONE

INTRODUCTION

The chapter includes the background of the study, impacts of loan policy on financial performance of Commercial bank, the statement of the problem related to loan policy and its effect on financial performance commercial banks, research question, objective of the study, scope, significant of the study and organization of the paper

1.1. Background of Study

Financial institutions play a critical role in the growth of a country's economy. The financial industry plays a crucial role in economic growth and progress; Banks are often chartered to provide a sufficient supply of loans to the public at a market set interest rate (Sonali, 2001). Any financial realities deriving from a bank's indirectly or directly advancement or commitment to advance funds to an individual that are based on the person's obligation to repay the funds on a fixed date or on demands, usually with interest, are referred to as a loan (Adriaan et al, 2002).

According to Tesfaye (2014), Banks are a type of financial institution that functions as a financial intermediary in the economy. It is critical to the success of economic development in determining the direction of financial system. This is particularly important in developing nations where capital shortages obstruct capital investment. Banks play a significant role in economic development by acting as a mediator between investors and businesses. This means that these firms accept savings from the economy and lend to entities with lack of capital, which has an effect on economic growth (Zawadi, 2013). The core function of a bank is to transfer deposits from excess to shortage units in the form of loans and advances to a variety of industries including agricultural, manufacturing, personal loans, and state. However, due to non-performing assets, banks have become more careful about making loans in recent years (Sontakke, 2013, &Tiwari, 2013).

Commercial banks are one of the banking industries that provide the majority of finance for business and other projects across the country. They serve a crucial role in the financial by transferring deposits from surplus to deficit units through loans and advances. They are critical in emerging economies since the majority of borrowers lack access to the capital market. As a

result, they are regarded as a middleman between savers and borrowers (Daniel and Wandera, 2013)

Commercial banks get their name from the fact that they only lend to businesses and industries. Shareholders or bank holding corporations own commercial banks in this case; the bank may be forced to provide higher-than-average deposit rates in order to attract additional capital. Eventually, the bank's lending rate will represent these higher rates. Higher lending rates could harm future lending efficiency by compelling the bank to lend to high-risk clients (Encyclopedia Deluxe, 2004).

According to Rawlin et al (2012) the primary goal of any firm is to make money. As a result, any asset generated throughout the course of business should generate revenue for the company. Because this issue is crucial to the banking sector, banks should pay special attention to loan management, as lending is the primary objective of commercial banks, and loans are typically their major assets and a key source of income.

Commercial banks' decisions to give out funds are always impacted and led by a variety of factors, including interest rates, economic changes, and the ability of borrowers to repay the debt or advances, among other things (Bessis, 2005). The bank's liquidity ratio, the degree of regional and abroad investment in the economy as well as in the bank, and the number of deposits for a certain period is among the other elements that influence bank lending capability. When a commercial bank offers loans or advances in excess of its cashing capabilities, the ability of the bank to lend out its funds is directly determined by customer savings (Zeller, 2001).

According to Kantor and Maital (2009), a financial institution loan policy is a declaration of its theory, criteria, and guidelines that should be followed by its staff when approving or denying a debt request. These policies, which should be based on the country's relevant legal guidelines and regulations, determine which areas of industry or sector can be lent to and which should be avoided. Banks are the most important external financial source for both businesses and individuals.

According to Rose (2002), the loan policy offers proper guidelines to the control in making man or woman loan decisions in shaping the institution's ordinary loan portfolio. This ensures that regulatory requirements are met and promotes company profitability. A written policy

declaration is useful because it communicates to personnel within the loan branch which procedures they must follow and what their responsibilities are. As a result, it enables the company to transition to a loan portfolio while controlling risk and meeting regulatory requirements. Loan policies, such as interest rates and payback periods, are critical pillars in any successful credit management strategy. They also optimize processes to ensure that all financial procedures are consistent and up to date (Thornburg, 2000).

Stafford (2001) defines a policy as a planned plan of action for guiding decisions and achieving sensible outcomes. The lending policy of a bank is a statement of ideology, principles, and criteria that its personnel must follow when approving or rejecting a loan request. Before releasing any facility, the minimum information requirements, as well as the verification process, must be met. There are indeed policies in place once a loan has been made, such as monitoring and managing existing services and processes for collecting on defaulted loans. When it comes to loan policies, every financial firm must focus on loan lending conditions, loan collection, and risk coverage policies, among other things (Pandey, 2012)

The target consumer is determined by a commercial bank's lending policy. In terms of earnings, the commercial sector is critical to banks. Despite the significant risks of commercial lending, banks are compensated through fees, interest margins, and deposit balances (Churchill et al. 1985). According to Deakins et al. (1993) Commercial banks' profits will undoubtedly suffer as a result of lending practices that are adverse to business customers. Security can be utilized as a substitute for more relevant information about a proposition's risk in the decision-making procedure. In strategies to attract and maintain profitable clients, lending policies must be designed in a customer-friendly manner. The broader the debtor's client base, the higher the loan book, and hence the more interest income, charges, and commissions associated to loan earned.

Financial firms' collection policies can make the difference between a good and great performance for the bank by taking advantage of opportunities to make collection operations more strategic, operationally efficient, and consumer (Benveniste, 2003). A loan recovery policy is described as a valid and essential business activity in which lenders and collectors can take necessary measures to acquire payment from its customers who are legally required to pay or repay the money they owe (Kitua, 2002). The research looked at how loan lending terms, defaulted loan recovery, and insurance policies impact on profitability. As a result, it is the

monitoring or lending committee's responsibility to guarantee that loan policies are strictly followed Kirangu (2014).The collection policy aims to reduce bad debt losses by speeding up collections from slow and non-paying customers. In addition, the policies encourage quick payment and lower default rates.

According to Augusto (2003), well defined lending policies should be well designed in order to improve efficient monitoring by directors and senior officers in order to meet the financial organizations goals. Loan issuance, business plan examination, performance monitoring, and debt recovery are all tasks that loan officers are responsible for. However, they are said to act like autocratic debt collectors when dealing with delinquent borrowers. They employ unusual and aggressive tactics, such as chastising or verbally assaulting members, demeaning them in front of others, and even forcing them to sell their actual goods to repay the loans (Ali et al, 2017).

Lending policy have a considerable impact on commercial banks' profitability levels; if adequate procedures and regulations are implemented for debt repayment and recovery processes, loans are the banks' most profitable source of income when compared to customers saving (Zeller, 2001).Evaluating the financial outcomes of a financial institution's policies and operations is referred to as financial performance. This was accomplished by calculating the firm's ROI and (ROA). This falls under the category of performance measures based on the ability of a bank's assets to generate income (Gatuhu, 2013). According to Nancy (2011), a loan, whether long-term or short-term, is a significant asset and revenue generator for banks, influencing the financial performance of all types of banks. The return on assets (ROA) invested in a financial institution determines its financial performance. As a result, when analyzing the financial performance of these banks, the researcher is interested in the relationships between loan policies and the financial performance of private commercial banks.

The history of Ethiopia's formal financial system dates back to the foundation of the Bank of Abyssinia a century ago. The first bank, Bank of Abyssinia, was founded in 1905 as a result of an agreement between the Ethiopian government and the British-owned National Bank of Egypt. Big financial institutions in the financial sector that aid in the proper usage of a country's financial resources. According to Uyen (2011), the commercial bank sector is expanding rapidly and has seen a large inflow of capital. Banks are part of a continually evolving business that

requires them to develop more specialized financial services in order to better meet their clients' changing requirements.

Financial institution lending in Ethiopia has long been routed through special stages. During the pre-reform period, credit scores were heavily regulated in order to conform to the government's plan and monetary requirements. Special and successive liberalization coverage and credit score coverage reforms emerged in the post-liberalization period, as a result of the discontinuation of discriminatory interest price and preferential zone lending modalities, as well as the reduction of credit score controls (Tsigab, 2014).

Currently in Ethiopia's financial industry structure consists of 18 banks (2 public banks and 16 private banks), 16 private insurance companies, 1 public insurance company, and 35 microfinance institutions in both rural and urban areas Ethiopia's financial sector (NBE, 2015/2016).

The National Bank of Ethiopia (NBE) reintroduced new financing regulation goals for both the Development Bank of Ethiopia (DBE) and the Commercial Bank of Ethiopia (CBE). primarily lent for recurrent expenditures, while the Development Bank of Ethiopia (DBE) lent for large project loans (Teklewold, 2018).

The study was motivated by the ongoing expansion of finance in the banking industry, as well as the development of the financial institution's lending functionality. The financial institution may have changed their loan lending policy to greatly assist in loan requests made by bank debtors. Lending rules of business banks change surprisingly slowly, Standards and practices that have proven successful in making loans to finance the assignment. According to a World Bank report (2015), small businesses face more difficult conditions in obtaining formal financing than large businesses; they are far more likely to be rejected for loans and far less likely to have external financing due to a loss of collateral and credit rating history.

Ethiopia has one of the world's fastest growing economies. As a result, large sums of money may be required to finance many microfinance projects, new emerging small and microbusinesses, and large capital extensive investments to borrow from the bank. Despite the importance of MSMEs to the country's economy and growing government, many of them continue to be unable to meet their full potential due to limited access to finance. The bank's loan policy will not

improve in the face of high loan demand, adversely affecting the bank's financial performance (U.S. Department of State, 2014).

1.2. Statement of the problem

Loan policies and procedures are designed to guide lending while ensuring prudent lending operations. Commercial banks are increasingly concerned about loan issuance. Small and growing businesses frequently operate in new and unexplored business locations that are prone to higher risk, making it difficult for businesses and individuals to meet the bank's loan requirements (Bruns, 2004).

All banks should be licensed by the country's NBE. Banking is a rapidly expanding industry in Ethiopia. Ethiopia currently has 17 commercial banks, one of which is state-owned and the other sixteen are privately owned. Other banks in the process of being established include Gada Bank, Amhara Bank, Goho Bank, Akufada Bank, and Hijra Bank (BBP No. 592/2008).

Loans are the most important asset held by banks, and lending accounts for the majority of bank revenue. Bank loans, as profitable as they are, are also risky. Bank loans fluctuate and are affected by general economic changes. As a result, it is critical for banks to develop loan policies that minimize risk. Sound credit management is required for a financial institution's stability and long-term profitability, and declining credit quality is the most common cause of poor financial performance and condition. As credit standards are relaxed, the likelihood of bad debts rises. Firms must therefore ensure that receivables management is efficient and effective (Gitman, 1997).

According to Ainemigisha (2015), a study that examined commercial banks' lending policies used by commercial banks in Ibanda town council, the study concludes that interest rate, property valuation, repayment period, type of loan required, and minimum and maximum amount of loan are the powerfully used policies to decide credit lending. The study examined the relationship among commercial banks' lending policies and the financial performance of small businesses in Ibanda, and it was discovered that the amount of money given, The poor relationship with financial firms, the high level of security needed, the short repayment period, and the high interest rates as a result of banking institutions' lending policies all have an impact on the financial performance of small businesses.

Kinyua (2001) for making investment and lending decisions, a bank must create Credit Policies, which represents the bank's credit risk tolerance. Before to agreeing to a credit facility the bank should examined the risk profile of its clients, including the risk level of their business, which must be accomplished through the loan policy.

Banking institutions' average profits are dropping, but their liabilities are rising. Credit policies that are unfavorable to businesses, poor administration methods, poor cash management, and a lack of resources are all factors to consider. Customer dissatisfaction and a lack of security are two issues that affect a company's financial performance (Bank of Uganda, 2012).

According to Binks et al (1992) it is in addition that commercial banks have difficulties in giving loans to clients because of asymmetric information, that's in a better level than for large companies which can be public. It's far tough for monetary establishments to collect valuable information approximately small companies, because of much less and uncertain information. According to studied by Olweny & Shipho (2011) some commercial banks in Kenya use strict loan policy for that reason losing customers to other commercial banks with soft credit policy; this has led to decline in performance of such bank.

Laile (2015) discovered that borrower habit, loan size, and borrowers' perception of repayment period, source of income, availability of training, business experience, business type, family size, and purpose of saving were all influential in determining loan repayment to microfinance institutions in Zimbabwe. These findings were consistent with the findings of Angaine and Waari's (2014) study, which found that education level, number of dependents, and interests were personal qualities influencing loan repayment in Kenyan Microfinance.

Imeokparia (2013) discovered that bank management in Nigeria failed to establish sound lending policies and adequate credit administration procedures as custodians of depositors' funds, and thus saw the need to exercise due care and prudence in their lending operations. The study also found no association between effective loan management and bank profitability.

An evaluation of lending practice: in the case of the commercial bank of Ethiopia, the financial institution lending exercise in imposing and administering loan appropriateness is low, and it was concluded that the bank operation is below medium in terms of enterprise development and loan analysis (Birtukan.et,al, 204).

According to Bereket (2017) the study indicates the need for private commercial banks to consider macroeconomic factors when developing techniques to effectively control their loans and advances, as we discovered a significant relationship between macroeconomic elements and total loans and advances.

According to Tekeste (2016), the assessment of credit management performance in emerging private commercial banks in Ethiopia, the key findings of the study show that the length of loan processing, amount of loan processed and approved, loan duration, and flexible limits affecting the overall performance of credit management are impeding loan growth and growing mortgage customers grievance on the commercial bank.

Genet (2018) the study on the trend of loan recovery performance Oromia international bank inadequate loan assessment and lack of follow-up, according to the study, are the leading causes of NPL accumulation. Diversion of funds, exaggerated property valuations or valuations that are both over and undervalued, and economic instability in some areas, Sector diversification, business decline, and business deterioration are additional factors. This suggests it had a direct negative impact on loan repayment performance.

Gadise (2014) examine the determinants of nonperforming loans (NPLs) of commercial banks in Ethiopia; the discovery of the lending rate is also unexpected. It revealed that the loan rate has a negative and significant effect on the level of NPLs. This means that, due to other variables, an increase in the lending rate reduces the levels of nonperforming loans (NPLs) for commercial banks in Ethiopia.

Local studies primarily focus on credit risk management on commercial banks in Ethiopia, where it was discovered that, despite the fact that commercial banks have implemented strict credit risk management measures, nonperforming loan, loan recovery remains a problem for many commercial banks. In Ethiopia, however, mixed research was conducted on the effect of credit policy on financial performance Tekeste (2016), Credit Management Performance Assessment in Emerging Private Commercial Banks in Ethiopia, Bereket (2017) monetary policy and loan portfolio of Ethiopian commercial banks , Birtukan.et, al an evaluation of the credit practice is carried out: the case of the Ethiopian commercial bank, Genet (2018) the study on the trend of loan recovery performance Oromia international bank and Gadise (2014) examine the determinants of nonperforming loans (NPLs) of commercial banks in Ethiopia.

The above study showed a mixed finding or mixed study on the effect of loan policy on the financial performance of commercial banks. The loan was the first source of income for the bank, and the lending policy greatly affected the financial performance of the bank. The bank has limited asymmetric information about their borrower, which affects the financial performance of the bank. The findings in various companies revealed that the results of the commercial bank's credit policy and financial performance are mixed and contradictory. Some studies are limited or subjective, while others limit the study to credit management, monetary policy, and financial performance, while still others ignore the impact of loan policies on bank financial performance. Increased interest fees, penalties, and commissions on loans have a negative impact on customers, and studies have revealed an increase in non-performing loans, which has a negative impact on the bank's financial performance. Effective loan policies lead to improved bank performance. The bank's loan policy does not reduce interest rates and is unwilling to lend, as well as the borrower's willingness to borrow funds, and the banks improve this loan policy to improve the bank's financial performance. For this reason, this study seeks to fill this gap in knowledge by studying the impact loan policy on the financial performance of the private commercial bank in Ethiopia.

1.3. Research Questions

Based on the problems stated above, a research question would be developed to answer the following question: What was the impact of loan policy on the financial performance of private commercial banks in Ethiopia?

- What is the effect of the loan term and condition policy on the financial performance of private commercial banks in Ethiopia?
- What is the effect of the lending policies on the financial performance of private commercial banks in Ethiopia?
- What is the influence of the loan monitoring policies on the financial performance of private commercial banks in Ethiopia?
- What is the effect of the loan collection policies on the financial performance of private commercial banks in Ethiopia?
- What is the effect of loan default management policy on the financial performance private commercial banks in Ethiopia?

1.4. Objective of the study

1.4.1. General objective of the study

The main objective of the study was to assess the impact of loan policy on financial performance of private commercial banks in Ethiopia.

1.4.2. Specific Objectives of the Study

The studies were guided by the following specific objectives:

- To assess the effect of loan terms and conditions policies on the financial performance of private commercial banks in Ethiopia.
- To determine the influence of lending policies on the financial performance of private commercial banks in Ethiopia
- To determine the influence of loan monitoring policy on the financial performance of private commercial banks in Ethiopia
- To assess the effect of loan collection policies on the financial performance of selected private commercial banks in Ethiopia.
- To assess the effect of a loan default management policy on the financial performance of private commercial banks in Ethiopia.

1.5. Significance of the study

The study's findings could be very important to regulators and policymakers in the government and banking sectors. The study investigates various challenges and weaknesses in commercial banks' loan policies and financial performance, and it may assist stakeholders in putting in place measures to address specific challenges in commercial banks. The study's findings may be very important to the management of various commercial banks in Ethiopia, which may revise their loan policy weaknesses in view of the study's findings. The study's findings will assist commercial bank managers in developing strategies to improve the financial performance of their commercial banks. The study has the potential to make a significant contribution to the body of knowledge in the field of loan policy and its impact on the financial performance of Ethiopian private commercial banks. It may reconcile theory and reality, and its findings may be used in future field studies. This could be of great interest to credit and finance scholars and researchers.

1.6. Scope of the study

The study's scope was limited to six experienced private commercial banks in Ethiopia that have been in operation for more than fifty years. The study assessed impact loan policy on the financial performance of Ethiopian private commercial banks. The general loan directorate managers and loan officers of each selected private commercial bank would be the study's target groups. Loan monitoring policies, loan lending policies, loan default management policies, loan collection policies, loan terms and conditions policies, and their impact on financial performance were the variables of studied. Six selected private commercial banks' head offices would be considered for the study and gather data through financial statement analysis for consecutive five years of operation (2016–2020), survey and interview would be used regarding the impact of loan policy on the financial performance of private commercial banks in Ethiopia.

1.7. Limitation of study

The limitation of the study was that the banks were not interested in providing their whole loan policy manual for my study because the document is very confidential due to higher competitors within the banking area. The study faces challenges in collecting data due to the COVID-19 pandemic disease. The respondent fears providing information or filling in questionnaires on hard copy paper, and this would be increased the duration of data collection.

1.8. Organization of the paper

There were five chapters in the paper. The first chapter provides background information. It includes problem statements, objectives of the study, research questions, hypotheses, and the scope of the study, as well as the significance of the study, limitations, and paper organization. The second chapter addressed the key concepts used in the paper to situate the problem within a broader context of literature. The third chapter discusses methodology, while the fourth chapter discusses and analyzes empirical data. The final chapter was chapter five, which drew conclusions from the findings and made recommendations for the future.

CHAPTER TWO

2. LITERATURE REVIEW

2.1. Introduction

This chapter reviews various theories which revolve around the effect of loan policy on the performance of a commercial bank. It reviews scholarly work which has been wiped out in the sector of loan policy and financial performance in financial institutions by covering both the empirical and theoretical reviews of already existing literature. Theoretical review would enlighten the researcher on the research topic, while the empirical review would help in understanding the findings and suggestions of earlier researchers. The reviews were used in developing a research gap, conceptual framework and deep understanding of the variables that were studied.

2.2. Theoretical Review

According to Ajzen (1991), the theoretical framework of a research project refers to the philosophical foundation on which the research is conducted and serves as a link between the theoretical and practical components of the research. A theoretical framework for research aids in determining which variables to measure and which statistical relationships to seek in relation to the problems reflected. As a result, the theoretical literature assists the researcher in clearly identifying the study variables. It serves as a general framework for data analysis and aids in the selection of the appropriate research design. The study would be guided by three theories, namely the transaction cost theory, the asymmetric information theory, and the default risk models.

2.2.1. Transactions Cost Theory

Schwartz established the Transactions Cost Theory in 1974. This theory postulates that financial institutions may have an advantage over traditional creditors in determining their clients' actual financial situation or creditworthiness. Financial institutions, on the other hand, have a greater ability to display and force credit score compensation. These types of benefits may also provide with a cost advantage over financial institutions.

According to Rajan and Petersen (2007), three fee benefit resources have been cataloged, with the useful resource of benefit in data acquisition, client control, and charge salvaging from current assets.

According to Gazendam and Jorna (2002), transaction expenses with the employer within the employer may also include coordination and organizational expenses. Contracting expenses and settlement fulfillment expenses between organizations are included outside of the employer. More rents are obtained through the use of the useful resource of optimizing the predicted income on expenses. The correct assumption here is that organizations may try to optimize rents but are unsure of their success.

The model concludes that in a two-part credit with a high interest rate, buyers who do not choose to take advantage of the discount are high risks because they may be experiencing financial difficulties. Simple net terms can produce a similar sign Smith by varying the penalties for late payers (1987). Emery (1987) conducted another study related to transaction cost theory and hypothesizes that there is a positive relationship between demand variability and credit offered.

Two intriguing perspectives on this cost structure the former contends that the more long-lasting the goods, the better the assets they provide and the greater the credit offered to vendors. The latter emphasizes the importance of the extent to which customers transform the product. The less transformed they are, the easier it will be for the provider to repossess and sell the asset through the same channel (Petersen and Rajan conducted, 1997)

2.2.2. Asymmetric Information Theory

The theory, according to Ekumah and Essel (2003), describes a situation in which both parties involved in a transaction lack access to relevant information. Sellers frequently do not know their buyers' true creditworthiness, and buyers frequently do not know the quality of goods. Smith (1997) describes a framework in which vendors offer two-part credit period because they can detect potential defaults more quickly than intermediaries, Smith also suggested that when sellers have asymmetric information about product quality, they provide buyers with trade credit so that they can verify product quality before paying. Vendors are motivated to extend credit because they have a vested interest in the success of a customer because they anticipate the client purchasing more goods and services from them in the future.

While the buyer's success is important, the quality of the product sold is also important and may influence new purchases, according to Deloof and Jegers (1996). According to (Epp, 2005), all parties involved in a given transaction are unaware of the pertinent information.

According to Edwards and Turnbull (1994), information asymmetry in the capital market occurs when the lender lacks sufficient information about the borrower in comparison to the borrower who has complete information about the returns and risks associated with projects invested. The lender, on the other hand, lacks sufficient information about the borrower. According to the theory, financial institutions face two problems as a result of information asymmetry. Monitoring the entrepreneurial behavior and adverse selection that results in lending decisions that are incorrect due to moral hazard.

According to Denis (2010), low default rates and higher aggregate lending can be achieved by reducing information asymmetry between borrowers and lenders, credit registries, and allowing the extension of loans to customers previously priced out of the market. Furthermore, the exchange of client credit worthiness aids in determining the quality of credit applicants.

According to Lee and Stowe (1993), small firms tend to offer more trade credit than large firms because small firms must still establish their reputation for product quality. Firms with longer production cycles extend their collection period because they produce high-quality goods. Firms that sell goods for whom the quality is difficult to evaluate stretch long credit terms because buyers must have enough time to assess quality. Vendors of low-quality goods may try to pass them off as high-quality goods. In this case, as the cost of extending trade credit rises, these companies will have less incentive to falsify quality information.

2.2.3. Default Risk Models

According to a Moody's study (2003), collateral values and recovery rates on company loan default can be instable, and they tend to fall when the number of defaults rises during economic downturns. Credit risk models have traditionally rejected the link between recovery rates and default rates, as most of them focused on default risk and used static loss assumptions, treating the recovery rate as either a constant parameter or a stochastic variable independent of the default risk.

2.3. Overview of banking in Ethiopia

According to NBE(2019) reports, Ethiopia's commercial banking sector now consists of 17 banks (16 private, 1 public), a significant increase from the sole state-owned bank that operated in 1990 and only seven banks that worked as recently as 2000. Going to count on multiple branch expansions, an increasing number of banks have jointly broadened their geographic reach over the last decade, working to improve key access to finance indicators.. Counting on large-scale branch expansions, the rising number of banks has collectively broadened their geographic reach over the past decade, thus improving key access to finance indicators. Public and private banks increased their branch network from 571 ten years ago and a couple of,208 five years ago to 4,757 branches as of June 2018—significantly improving the population-to-branch ratio over the years, from a situation where each branch served 126,000 people in 2008 to the current status where each branch serves only 20,000 people on average. In parallel, depositors have increased from 4 million in 2010 to 10 million five years ago to over 33 million today—equivalent to roughly half of the adult population in 2018. Outside of the capital city, accessibility has improved significantly, with 65 percent of branches now located outside of Addis Ababa, up from 38 percent a decade years ago.

Legislative standards: Banking in Ethiopia is ruled by an overall banking law, the Finance Industry Proclamation Federal Negarit Gazeta Proclamation (592/2008), which has been in effect since August 2008 and grants the NBE the full range of powers of a banking regulator. This Banking Business Declaration addresses mandatory requirements for new bank licensing, share registry and shareholders, director and senior management qualifications, banks' financial obligations and limitations, financial record-keeping and audits, disclosure and inspection, and other miscellaneous areas. The Proclamation also states that detailed Directives in all of the above areas will be issued on a regular basis and revised as needed by the central bank (NBE).

Banking Guidelines: In accordance with the Banking Business Proclamation, the NBE has released numerous of Banking Directives and Circulars over the years that specify rules and regulations in all crucial sectors of banking activities. The following are some of the remarkable requirements that have an effect on bank operations. Least start-up capital: The formal paid-up capital requirement Directive No. (SBB/78/2021) is Birr 5 billion, though banks are recommended to reach Birr 2,000mn (\$70mn) by 2020. Capital adequacy: On a risk-weighted

basis, a capital adequacy requirement of 8% is required. Liquidity requirement: A 20% liquidity requirement is required. Minimum interest rate: A savings rate of 7% is required (since October 2017), All deposits must have a 5% reserve requirement. Loan limit for a single borrower: Credit limits that limit a single borrower's exposure to 25% of capital Purchase of NBE Bills: Private Banks must purchase NBE Bills equal to 27 percent of gross loans disbursed (with the Bills having a 5-year maturity and 5 percent interest rate). Limitations on equity investment: While banks may make equity investments in businesses. Such investments cannot exceed 10% of a bank's net worth and no more than 20% of the investee's capital, and a bank's aggregate equity investments cannot exceed 50% of its net worth.

According to Cepheus(2019), loans provided by Ethiopian banking institutions have typically included one of the following: term lending (those who have fixed repayment periods), goods loans (involving loans given against a stock of pledged products sold as collateral by the borrower); pre-shipment loans (for exporters who require advances to process agricultural exports, including coffee and sesame), and overdrafts (essentially a line of credit that companies can draw on up to a pre-agreed limit and for which they pay interest only on outstanding amounts). By industry, the focus of most bank lending has been on 2 groups and domestic trade and services—that used to account for half or more of most banks' loan books many years ago, but larger allocations are now going to exporters and manufacturers, with the latter two budgeting for 27 percent of commercial bank loans. Contrary to popular opinion, banks are free to offer loans without any collateral (there are no central bank restrictions preventing this), though most banks require collateral for most loan products due to tradition, sheer inertia, and general risk aversion.

According to Cepheus (2019), making loans innovations have been more constrained, but have included some things in recent years. One new innovation is 'Islamic' or interest-free lending products. Consumer loans, which contribute for less than 5-10% of total debt, are also being provided by an increasing number of banks, including mortgages, car loans, as well as other personal loans. Diaspora-focused customers and investment loans are also becoming more common, with banks using them to motivate foreign exchange. These loans are currently offered by United, Awash, CBO, BOA, and others.

Despite these minor discoveries, the large percentage of loan products provided by most banks are traditional: term loans, pre-shipment loans, and goods loans. Over the last ten years, commercial banks' overall debt to the government and private sectors has risen roughly 12-fold, from Birr 67 billion to Birr 740 billion. The latter figures are based on a broad definition of credit, which includes bank financing in the form of loans, bonds, or bills.

Interest income: Interest earned (expressed on a net basis, i.e. interest income less interest expense) has nearly fivefold risen from Birr 3.2 billion to Birr 15.5 billion since last year. The dramatic increase in (net) interest earned reflects banks' increasing loan balances, which have increased from Birr 44 billion to 178 billion in the last 5 years. The growth in loan capacity has more than mitigated the moderate decline in effective lending spreads on loans, which have declined from around 12% to 7.4% at private banks. The decrease in disperses reflects the decrease in effective bank lending rates which in turn indicates the increasing share of NBE bills in overall interest-earning assets (NBE Bills now make up 20 percent of total overall assets at private banks and are earning an interest rate of only 5 percent).

2.4. Relationships between Loan policies and bank financial performance

These variables have an impact on a bank's profitability. These variables are operated by the bank, and they vary from one bank to other. The following factors are:

2.4.1. Loan terms and conditions policy

According to Miller (2008) cites four reasons why an organization must have a written loan policy: first, it reduces default and enhances cash flow. Second, having a policy in place improves reliability across departments. This is due to the fact that by marking down what is expected, the firm's arms will achieve that they share a common goals, reducing redundant work and departmental tension. Third, it encourages customer uniformity by making decision making a logical function based on predefined parameters. This easier decision-making and enables a sense of fair play, both of which will benefit customer interactions. Finally, it can provide some acknowledgement of the credit department as a separate entity worthy of providing input into the firm's overarching plan.

Credit contracts usually include promises, the amount of the securities involved, insures, interest terms, and the time frame over which the loan must be reimbursed. To avoid misunderstandings or potential legal action, default terms must be clearly detailed. In the case of default, the terms of the bad debt collection should clearly specify the expenses involved in collecting the debt. This also applies to groups who use promissory notes. According to Cheron, Boidin, and Daghfous (2009), numerous people or organizations fight to meet the required prerequisites in terms of interest rates, fees, and repayment terms, among other things. This makes it impossible for them to obtain commercial borrowed funds. A loan contract's main objective is to define what the parties are consenting to, what duties each party has, and how long the contract will last. A loan agreement should be in accordance with state and federal regulations in order to protect both the lender and the borrower in the event that either party fails to honor the agreement. Depending based on the repayment type, the terms of the loan agreement and which state or federal laws govern the outcome requirements imposed on both groups will differ.

According to Bagachwa (2009) in his look at fittings, having agreed to the terms of credit rating with a repayment length that is clear to all stressed; the leaser has an obligation in his individual good interests to ensure that the customer follows through on his promises. The speculator is aware that his test of past due cost has been established as satisfactory with the assistance of the lender as a point of reference. As a result, the lender can no longer impose constraints on the unique credit terms because he has adopted unused expressions. The alternative is for the leaser and the bank to sit down and restart the transactions. This is an all-too-common occurrence, and a knowledgeable credit manager should never allow it to happen.

Each component of a company's credit policy is used as a tool for monitoring account receivables, which are the result of credit sales; it covers everything from the type of customers to whom credit may be extended to when actual collections would be made, there is no universal credit policy that should be adopted by every organization; rather, each organization should develop its own credit policies based on cash-flow circumstances, industry standards, current economic conditions, and the level of risk involved (Ojeka, 2010).

According to Kariuki (2010), the issue will frequently be displayed at a few point of the fundamental arrange of advance utility and thus turns into more basic all through the credit endorsement, checking, and controlling stages, in particular when arrangements, methods, and

methodologies related to credit score handling as stipulated inside the credit score rate control (CRM) recommendations are not followed, are helpless, fragmented, or are not watched. Credit statements typically include contracts, the cost of collateral included, guarantees intrigued charge expressions, and the time period over which it must be reimbursed. To avoid disarray or potential criminal courtroom development, default expressions must be earnestly verifiable. In the event of a default, the terms of collection of the obligation must be clearly stated, as well as the charges emphasized in amassing the obligation. This also applies when promissory notes are used.

According to Elyasiani and Goldber (2004), the absence of a department in any region will result in the following taking a toll of advances in terms of making visits to clients and following up on obstructed credits. This will result in approximately higher leisure activity expenses being exacted on advances from now on. The gathering of insights for the capability of having to get to budgetary offerings, particularly credits, necessitates contact between the borrower and the moneylender, which should be encouraged by implies geographic proximity. It follows that geographically close banks would result in lower costs in gathering the necessary data, and borrowers would most likely obtain better credit terms if they were close to a bank. The advance cites a boom as the gap between the lender and borrower widens as a result of the esteem. According to Atieno (2004), many organizations struggle to meet the necessary requirements, such as interest rates and repayment terms. This prevents them from obtaining commercial bank loans.

2.4.2. Lending Policy

Stafford (2001) defines policy as "a purposeful action plan to direct decisions and achieve logical outcomes" (s). The loaning policy of a bank is a statement of philosophy, standards, and regulations that its employees must obey when giving or rejecting a lending application. The minimum information requirements, as well as the confirmation, are described and must be guided before releasing any facility. There are also post-lending policies that include control and monitoring existing facilities as well as operations for collecting on non - performing loan.

According to Morsman (1993), lending policies are the rules and policies put in place by commercial banks to ensure financial firms give credit to retail and corporate parties. Credit rating guidelines are based on a variety of credit score parameters. Customer affordability is one

of these criteria, which is also known as the debt provider proportion. The primary objective of the ratio is to compare the customer's profits to his or her current and potential liabilities in order to assess the customer's ability to service any new debt that she or he incurs. This ratio is measured by the main financial institution of a given use and is usually the same across banks.

According to (Ozdemir, 2004) Lending terms of financial institutions presented a moderate positive correlation between borrower's loan size and repayment period in Turkey. In his study, he revealed that the amount of loan advanced is influenced by the borrower's level of income. He argued that the starting point of any sound lending terms must begin with establishing legitimate financial needs of the potential borrower but not the financial performance of the microfinance firm. Therefore the lending institution must ensure that loan terms are constantly updated because they will affect the growth, stability and economic wellbeing of the financial institution. However, there was no mention on how these lending terms affect financial performance in his study.

According to Kantor and Maital (2009), a financial institution's loan policy is an announcement of the institution's philosophy, standards, and recommendations that its employees must consider when granting or refusing a loan request. These policies determine which areas of the business or enterprise are eligible for loans and how to avoid them, and they must be based on the application of a's relevant laws and policies. Banks are the most important sources of outside finance for businesses and individuals.

Lending always carries some risk because of the circumstances that arise as a result of loan obligations not being paid when they become due. According to the study, depending on how it approaches credit, a company's credit policy can be either lenient or stringent. According to the study, lenient credit policy refers to a situation in which financial institutions tend to grant credit facilities to customers very liberally, i.e. credit is granted even to customers whose credit worthiness is unknown or doubtful. A strict credit policy, on the other hand, is one in which financial institutions only lend to customers who have proven their creditworthiness (Ibrahim, 2004).

Individuals and businesses rely on short-term debt, particularly bank overdrafts, according to (Bums et al, 1992). Deficiencies in banks' appraisal processes for loan guarantee scheme applications were highlighted in the Robson report (2004), according to the Rhodes report (2004). Bosanko, Dranove, and Stanley conducted a study (2006) Loans are relatively illiquid, accounting for a large portion of most banks' assets.

According to Rose (2002), the loan policy provides specific guidelines to management to improve individual loan decisions that shape the company's as a whole loan portfolio. This ensures that compliance standards are met and that the organization is cost effective. A written policy document is useful because it interacts to loan staff members which procedures they should follow and what their responsibilities are. As a consequence, it assists the organization in shifting to a loan portfolio, controlling risk exposure, and meeting regulatory standards. Any exceptions to the policy should be fully documented, as well as the reasons for them.

The Loans department considers all such changes and periodically reviews all loans until they reach maturity. Loan review is crucial as it helps management to identify problematic loans more quickly and acts as a continuing check on whether loans policy is adhered to by the loans officer. Some commercial banks review loans more efficiently such that they are able to top up loans. Written policy guides the banks towards reducing their risks and thus maintaining their profitability thus high performance. It also guides the loan officer in evaluating the kind of client they give loan to. It also helps the bank in lending to those customers who are credit worth thus maintaining the bank performance high.

According to clergymen & Minow (2004) Control processes are the rules and procedures that govern how an organization is run. According to a study by Ministers & Minow (2004), an organization with excellent corporate processes implies that it has a very good corporate company, which is defined as the connection between shareholders, the organization, board of chairmen, professionals, customers, suppliers, and various captivated groups in selecting the heading and execution of groups.

According to Hart & Milstein (2003), company management is a combination of law, direction, and relevant intentional non-public division homes that enable a business to attract financial and human capital, perform competently, and then maintain itself by producing semi-permanent value for its shareholders, all while considering the interface of partners and society as a whole.

According to Perro and Ruoff (1997) Poor lending practices had a substantial impact on Korean commercial banks and merchant banking firms and financial institution profitability had deteriorated. As a result, the significance of revising existing lending policies as a precondition for effective financial liberalization is being emphasized increasingly.

2.4.3. Loan monitoring policy

According to Mwisho (2001) Monitoring of borrowers is critical because existing and potential exposures vary with the passage of time and shifts in the underlying variables. The study goes on to say that having regular contact with consumers and fostering an environment where the bank may be perceived as a problem solver and trusted counsel are two ways that financial firms can check their credit. According to the research, the bank can build a culture of support for customers who are experiencing difficulties and are working on fixing them. Keep track of the movement of a borrower's enterprise through the bank's account; a regular assessment of the debtor's records, as well as an on-site inspection is required; updating borrowers' credit files and evaluating the credit rating provided to them at the time the loan was granted on a regular basis.

The loan recovery rate determines favorable performance, with a high recovery rate indicating a high level of financial security and a low recovery rate indicating the reverse, which can be improved by close credit monitoring (Mutua, 2016). SACCO's credit policy should be followed when recovering loans. Loan recovery delays imply poor performance, which has a negative influence on SACCO liquidity; revolving funds are retained by a limited number of persons and hence do not create extra profit (World Bank, 1995).

According to Doran and Hoyle (1986) to achieve capital adequacy standards and for long-term survival, banks must carefully evaluate the risk-return profile of their loaning portfolio, the bank's goal is to maximize profits and, as a result, shareholder wealth. If the major goal of all banks' loaning arrangements is to build trouble-free enterprises, a credit candidate's monetary

capacity and previous borrowing experience, as well as their assurance to repay their responsibilities, are critical.

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According to Ngare (2008), it was discovered that credit inspecting in banks utilize subjective credit assessment techniques to form credit awarding decisions, whereas cash flow runs on the borrowers' credit concentration and adverse exchanging by the borrowers were the most significant sources of credit risk among Kenyan banks. Furthermore, most banks were discovered to use advance widening; banks guarantee.

According to Juanjuann (2009), commercial banks administration routinely receives precise and appropriate credit reports as part of their internal credit monitoring strategy, which has a positive impact on the bank's loaning operation.

According to Kargi (2011), the levels of credits and advances, non-performing advances, and stores have a negative impact on bank productivity, exposing them to a high risk of illiquidity and trouble. According to Epure and Lafuente (2012), the reflect indicated that there was continuous evaluation of the unused and existing credit borrowers throughout the life cycle of the credit, which resulted in loaning operational enhancements with a positive effect on the net intrigued margin.

According to Ahmed et al. (2011), in their study, banks use monitoring of debtors' financial activities after credit is issued to ensure that the advance is put to appropriate use, allowing the borrower to reimburse the central and interest thus collected. This action was discovered to decrease credit misfortune arrangement and has a significant positive impact on non-performing credits. As a result, a decrease in credit misfortune arrangement implies less credit chance and softening.

2.4.4. Loan Collection Policy

According to Kariuki (2010), a collection policy is required to ensure frequent and timely collection, as well as to speed up collection from sluggish payers and decrease bad debt losses. A few customers are complete non-payers, while others do not even recognize the time factor; thus, the collection policy needs to accommodate all of these. He found that timely collection is required for quick turnover of working capital, maintaining collection costs and bad debts within limits, and efficient collection maintenance.

According to Pandey (1995), repayment policy should set clear collection methods. Inefficient loan collection reflects governance ineffectiveness. Deficit in loan distribution to clients is thus a policy established by cost per loan asset, which is identified as an average cost per loan advanced to clients in financial terms calculated by total cost and total amount of loans ratio.

According to Deakins and Hussein (2005), the information helps lenders determine the risk of lending money to potential borrowers. There are a variety of scoring systems available, but they all use the debtor's loan history to predict repayment based on the past behavior of borrowers with similar profiles. Loan information and the length of the lender's relationship with the bank are two of the most important factors in a lender's decision to reject or approve an applicant, and they also influence the rate and terms provided.

According to Rajan (1992), Peterseny (1994), and others, lending relationships reduce the severity of asymmetric information experienced by banks by offering information on the borrower's loan history and account movements.

According to Altman (2008), the theory of asymmetric information contends that differentiating higher risk debtors from lower risk borrowers may be impossible, resulting in moral hazard and adverse selection hazards. Adverse selection and moral hazard hampered the accumulation of a large number of non-performing accounts in banks.

According to Stiglitz and Weiss (1981) adverse selection occurs in a loan market because of knowledge asymmetry, because the borrower possesses information that the lender does not, it is difficult for the lender to discriminate between good and bad risk investments. Financial institutions prefer to lend to high-risk borrowers while rejecting applicants who are less risky.

This happens because high-risk borrowers are more prosperous than low-risk ones. Moral hazard arises from asymmetric information in that a party shielded from danger may behave differently than if he were completely exposed to the risks. Moral hazard can occur when a borrower invests or spends borrowed funds carelessly, which may not be prudent in the eyes of the creditor.

According to Berlin and Loeys (2008), in order to meet capital adequacy guidelines and ensure long-term survival, banks must carefully monitor the risk-return profile of their lending portfolio. The bank's goal is to maximize profits and, as a result, shareholder wealth. If the main objective of all bank lending is to make trouble-free advances, a borrowing applicant's financial ability and prior borrowing experience, as well as their willingness to pay off their debts, are crucial.

According to Atieno (2004), a business's economic performance may provide valuable information to banks in two main ways: first, it reveals the level of rivalry in aggressive markets, and second, it implies constructive diversification against domestic shocks, lowering the likelihood of default for such businesses.

2.4.5. Loan Default management policy

Loan Default management is the process of obtaining an outstanding loan and learning how to repay it by persuading the borrower to repay the outstanding loan. Debt payment is difficult because most clients do not have access to lenders (banks). Most financial institutions have loan recovery departments that track loans and try to repay them before they become delinquent (Garber, 1997)

According to Waweru and Kalani (2009), some of the causes of non-performing loans in Kenyan banks include the national economic downturn, reduced consumer purchasing power, and legal issues. Bichanga and Aseya (2013) identified a number of factors as making contributions to loan default: Banks' insufficient of micro and small businesses, delays in loan processing and payment, diversion of funds, and over-concentration of making decisions, with some banks requiring all loans to be approved by Area/Head Offices..

According to Asantey and Tengey (2014), the primary factors of bad loans among SMEs are a loanee's level of education, years of business experience, company size, availability of other income sources, kinds of products/services, loan size, and number of dependents. Other factors

include credit analysis, the suitability of the interest rate, and the duration the loan is disbursed. However, the study discovered that political stability has little effect on bad loans. According to Arishaba (2011), in a study on lending methodologies and loan losses and default in a microfinance deposit-taking institution in Uganda, the following factors were identified as relevant factors boosting loan default: Insufficient financial analysis, as well as inadequate loan assistance, is another cause of loan default. The study also revealed that illiteracy and inadequate skills, disappearance of loan clients, poor business practices, and competitive factors exist, whereby, due to the existence of many banks involved in the lending business, they ignore asking for adequate collateral and only have debtors

According to Balogun and Alimi (1998), the main causes of loan delinquency include loan inadequacies, detention at the time of loan delivery, small estate size, high interest rate, age of agriculturists, poor supervision, non-profitability of estate businesses, and excessive government intervention with the processes of government patronized credit programs. According to Olomola (1999), loan payment detainment and rising interest rates can significantly increase the cost of adopting a deal while also negatively impacting prepayment performance.

According to Okorie (1986), the nature, duration of disbursement, supervision, and profitability of enterprises that used smallholder loan programs in Ondo State contributed to the giving abilities and thus high failure rates. Other key factors associated with loan delinquencies include type of loan, term loan, loan rate of interest, poor credit history, debtors' income, and loan deal cost. What financial institutions do in practice to assist borrowers in selecting appropriate income generating conditioning to meet the giving plan should be investigated (United Nations Economic Commission for Africa, 1990).

Kohansal and Mansoori claim (2009). The majority of the defaults resulted from ineffective management techniques, advance preoccupation, and lack of willingness to reimburse loans, and as a result, moneylenders plan different regulatory elements aimed at reducing the possibility of advance default (i.e. guaranteeing of collateral, third-party credit ensure, utilize of credit rating, collection organizations, etc.). According to Aballey (2005), poor credit can be limited by ensuring that debts are made to debtors who are likely to be able to repay and are unlikely to become insolvent.

According to Montana (2012), the following are some of the suggested bank debt collection techniques that are likely to help significantly raise their debt collection success: flexible repayment plans for customers debtors experiencing financial distress, well-formulated hardship programs for debtors who are late on their reimbursement, stretch or lower payments, interest rates, or reduced fees when you anticipate customer payment problems, and create communication lines where customers can openly unsatisfied. You can avoid larger problems by reaching out to customers ahead of time. Bank debt recovery is taking on an alarming trend, with growth that appears to be unstoppable. This rise can be attributed primarily to a weak economy, which impacts both customers and markets globally. Financial institutions are developing new techniques and strategies to improve loan collection/recovery.

Debt reinstatement represents an alteration in the terms of an outstanding loan. When a financial firm determines that rescheduling a debt is in the best interests of the government and that recovery of all or a part of the loans is reasonably assured, it should consider adjusting the debt (Maphartia, 2004).

The goal of repossession of security is to recover unpaid debts, not to take property away from the borrower. The security repossession recovery process will include repossession, security valuation, and security realization through proper methods. Everything would be done fairly and openly. Only after the above-mentioned notice has been issued will repossession take place. The legal procedures will be followed when repossessing the assets. In the normal course of business, the bank will take all rational precautions to make sure the property's security and safety after taking custody (Umoh, 2007).

Credit scoring systems can be used by banks as part of their credit recovery strategy. A credit score is a number that represents a borrower's ability to repay and is based on a data analysis of the borrower's credit report. A credit rating is generally determined by information contained in a credit history. Credit ratings are used by lenders, such as banks, to evaluate the risk of lending to customers and to mitigate losses due to bad debt. Credit ratings are used by financial firms to decide who is most qualified for a loan, at what interest rate, and up to what credit limit (Capon, 2002).

2.5. Financial Performance of Commercial Banks

Various groups of individuals are particularly interested in evaluating bank performance. First and foremost, bank shareholders are directly affected by bank performance. Investors take advantage of bank information to develop expectations concerning future performance that can be used to help price common shares (in addition to capital notes and debentures that may be issued by the bank). Second, bank management traditionally is evaluated on the basis of how well the bank performs relative to previous years and compared with similar (or peer group) banks. Hence, employees' salaries and promotions are frequently tied to the performance of the bank. Bankers also need to be informed about the condition of other banks with which they have business dealings. Third, regulators, concerned about the safety and soundness of the banking system and the preservation of public confidence, monitor banks using onsite examinations and computer based "early warning systems" to keep track of bank performance. Fourth, depositors may also be interested in evaluating the performance of the bank, as the nominal values of their deposits are not guaranteed. Fifth, and last the business community and general public should be concerned about their banks' performance to the extent that their access to credit and other financial services is linked to the success or failure of their bank (Benton and James 2005)

Good financial performance of banks is important not only to their shareholders but to the whole economy as it helps the banks to continue their role of financial intermediation effectively and help economic growth of a country, especially in countries where financial markets are not well developed. Financial performance is a broad term that describes a company's overall fiscal health. When you hear that a business has strong financial performance that often means it has growing revenues, manageable debt, and a healthy amount of free cash flow (European Central Bank, 2010).

In financial perspective, performance has been defined as the final outcome of a firm's policies and operations. Lending is dangerous for most banks even though debt repayment is rarely totally protected. As a result, a bank's financial performance is the result of a number of activities carried out by management in accordance with the loan policies that have been established. This is reflected in operating income, return on assets, and earnings before interest and taxes, which are calculated by comparing various items in the financial position statement and the statement of comprehensive income (Nancy, 2011).

Financial performance is the process of calculating the financial outcomes of a financial institution's policies and operations. This was accomplished by computing the firm's return on investment and return on assets (ROA). This falls under the category of performance measures based on the ability to generate income from commercial bank assets. Financial institutions' financial performance is determined by the return on assets (ROA) invested in the business. Analysts compare and assess a company's annual asset performance using metrics such as cash conversion cycle, return on assets ratio, and fixed asset turnover ratio. An improvement in asset performance means that the company can either earn a higher return with the same amount of assets or is efficient enough to create the same amount of return with fewer assets (Adams and Buckle, 2003). Profitability will be measured using $ROA = \text{Net income} / \text{Total asset}$

2.6. Empirical Studies

According to Ainemigisha (2015), a study that examined commercial banks' lending policies used by commercial banks in Ibanda town council, the study concludes that interest rate, property valuation, repayment period, type of loan required, and minimum and maximum amount of loan are the powerfully used policies to decide credit lending. The study examined the relationship among commercial banks' lending policies and the financial performance of small businesses in Ibanda, and it was discovered that the amount of money given, The poor relationship with financial firms, the high level of security needed, the short repayment period, and the high interest rates as a result of banking institutions' lending policies all have an impact on the financial performance of small businesses.

According to Dorcas (2016), an evaluation loan policy and its effect on financial performance of commercial banks in Eldoret town in Kenya, the study concluded that, there exist systems in place and procedures that banks have in place so as to secure payment from their consumers once payment becomes due, this systems leads to enhanced organizational profitability, it leads to improved image of the organization, reduces loan defaulters, leads to improved Earnings per share

According to Linda's (2014) study on the relationship between loan policy and commercial bank financial performance in Kenya, financial performance for commercial banks significantly improved. As a result, commercial banks' loan policies boosted their financial performance

significantly. To summarize, provisions for bad and doubtful debts are the most important loan policy, followed by loan default rate and collateral.

The study also discovered a link between in a study on the requirements for effective debt repayment performed by Paxton (1996), in terms of avoiding reimbursement delays, the 100 percent rule was applied, which meant that no new credit was offered until the former was repaid in full. Later, this rule was relaxed, and loans were awarded as long as the payment rate reached 90percent of the outstanding loan balance. In order to achieve credit, every borrower had to have savings equal to 20percent of the loan amount. To be eligible for credit, each member had to buy a certain number of shares. For credit in excess of certain limits, guarantor ship was also required.

According to Jackline (2016), the study investigated the effects of credit policy on the financial performance of microfinance institutions in Nairobi County. According to his findings, credit standards, credit terms and conditions, and collection efforts all have an impact on the financial performance of microfinance institutions. As a result, management should exercise caution when developing credit policies that will not have a negative impact on the operations of microfinance institutions in order to maximize profits. Inappropriate credit risk management that is not correctly set up decrease MFI profits affects asset quality and increases loan losses and non-performing loans, potentially leading to financial distress.

Susan (2015) conducted a study on the effect of credit policy on the financial performance of regulated SACCOs in Nairobi County. The study concluded that regulated SACCOs had adopted credit standards as a credit policy, credit term policy loan ratio in determining how much a customer would borrow, applied collection policy, considered non-performing loans and total loans, loan-loss provision coverage ratio, and credit policy application, which significantly increased Return on Assets for the regulated SACCOs.

According to Chikamai M. et al. (2018), the study revealed that credit policy has a strong positive impact on the financial performance of SACCOs in Kakamega County, as indicated by Pearson Correlation results. This implied that better credit policies would result in a significant improvement in financial performance. According to the regression analysis, variability in financial performance account for a significant portion of the variation in credit policies.

Furthermore, a unit increase in credit terms would lead to a significant impact on the financial performance of Microfinance in Kakamega County in the same direction. As a result, credit policies are a relatively insignificant predictor of financial performance. As a result, SACCOs with better collection policies and a strong credit period policy would be improved profitability.

Koopahi B et al (2002) used regression techniques to distinguish defaulters from non-defaulters of agricultural bank beneficiaries in Iran. The results revealed that the use of machinery, the length of the repayment period, and bank supervision of loan use all had a direct and positive influence on agricultural credit loan repayment. But in the other hand, the time required to obtain a loan had a major effect on its repayment.

According to a study by Yaron B et al (1997), one of the obstacles that SACCOs in India encounter is that during national elections and even at other times, there is significant publicity from political platforms for the delay of loan repayment or pressure on lending institutions to grant extensions to prevent or delay loan repayment. A second issue raised was the risk of a cooperative society devolving into a pyramid scheme if the regulatory structure fails; resulting in questionable management that does not abide to conventional financial management practices. This does not abide to standard financial management. This is a common occurrence in the country, leaving numerous investors devastation caused by the loss of their money.

According to Njiru (2006), a research was conducted on a list of loan defaults that included all relevant information that should be evaluated on a case-by-case basis to determine if the situation is reversible. What steps can be taken to enhance ability to repay, as well as whether or not worked out or collection plans have been implemented. To establish the SACCO's ability to withstand loan defaults, the provision level should be considered. According to Mwaura (2005), the key factors contributing to poor performance in loan lending by SACCO societies in Kenya are a lack of credit analysis, credit follow-ups, and hostile lending.

According to Mwangi's (2010) investigation, there is a relationship among finance performance (in terms of profitability) and credit risk management in profitability (nonperforming loans and Capital adequacy ratio). According to Ronald (2011), financial performance measures are driven by three critical issues: profitability, business size, and business growth. In their study on loan performance and profitability of microfinance institutions,

Kato (2013) also used profitability as a measurement for financial performance. The research also revealed a negative correlation between loan performance and profitability of the banks. In their study of the effect of loan management on commercial bank financial performance, Nduwayo (2015) used profitability as a measure of financial performance. The study discovered that a well-managed loan returns the organization's equity and assets, which can generate financial performance.

According to Birtukan et al. (204), an evaluation of lending practice: the case of commercial bank of Ethiopia, the bank lending practice in implementing and managing loan suitability are low, and the bank procedure is below medium in terms of business advancement and loan analysis.

According to Bereket (2017), the study on Monetary Policy and Loan Portfolio of Ethiopian Commercial Banks suggests that private banking institutions should consider macroeconomic variables when developing strategies to efficiently control their loans and advances, as we showed a significant relationship between macroeconomic variables and cumulative loans and advances.

According to Tekeste(2016) the Evaluation of Credit Management Performance in Emerging Private Commercial Banks in Ethiopia, the main study results of the study revealed that impeding loan growth and higher loan client complaints on the bank are regarding the length of loan processing, amount of loan processed and authorized, loan period, and discretionary restrictions influencing credit performance management.

According to Elshaday K et al (2017), a research was conducted on the factors of the financial performance of private commercial banks in Ethiopia. It can be finalized of banks is the determining factor that increases financial performance because it allows them to achieve economies of scale. Loan loss provision and nonperforming loans are two main factors that have a negative impact on the performance of Ethiopia's private commercial banks. It can also be concluded that the greater the bank's debt position, the greater its capacity to lend and operate. It is also possible to conclude that well-capitalized banking institutions can make more loans and advances to their clients and generate more income than badly capitalized banks. The revelation

also allows us to conclude that ineffective operational costs decrease return on assets, and thus banks are estimated to work on reducing their avoidable costs.

According to Rahel M,et al(2015), the study on Factors of the Financial Performance of a Private Commercial Bank in Ethiopia, it can be concluded that capital adequacy, income diversification, export, loan output, and deposit mobilization have a significant impact on ROA with a positive relationship; this means that any increase/decrease in the value of these variables will lead to an increase/decrease in the financial performance of commercial banks. Liquidity and operating efficiency were found to have no significant impact on ROA, implying that any increase or decrease in the value of these factors will have no significant effect on commercial banks profitability.

2.7. Knowledge Gap

There has been limited research or scholarly studies about loan policy since most critics believe loan recovery consumes much of the company's time by going to look for clients and auction assists so as to recover the loans. The literature review shows that research in the area of effect of loan policy on financial performance of commercial banks has been done but it was mixed study or inadequate. The literature reviewed reported that previous researchers concentrated on determinants of the Financial Performance, assessment of credit management Performance, monetary policy and loan portfolio, the effect of nonperforming loans on financial performance. Most of the studies reviewed on different commercial banks sectors do not focus on the effect of loan policies on the financial performance of the commercial banks.

Based on the studies presented above, it is clear that little research has been conducted on the relationship between loan policies and financial performance. Many financial institutions' loan collection policies and other basic financial services are still lacking, and a credit management policy is just one of the loan management policies. According to the studies, the majority of the defaults resulted from ineffective management strategies. As a result, money lenders devise various regulatory mechanisms and loan policies to reduce the probability of advance default.

From the survey of relevant literature above, the loan policies employed are mixed. Their efficiency was determined by the removal of debt repayment defaults. The study demonstrated the need of commercial banks developing good lending policies and practices in order to achieve their desired objectives in the bank sector, which include improving loan recovery, abiding to loan terms, maintaining a strict return on assets, and hedging credit risk. The commercial banking sector in Ethiopia was growing. However, it still has loan management issues, and based on a review of the literature and studies conducted showed that mixed finding the effects of loan policy on the financial performance of Ethiopian commercial banks. As a result, the research is important. The study's objective is to fill up these important gaps in the literature by revealing the effect of loan policies on financial performance commercial banks' in Ethiopia.

2.8. Conceptual framework

In figure 2.1 is conceived as a functional relationship between the five predictor variables, which were includes, loan terms and condition policy, loan lending policy, loan monitoring policy, loan collection policy, loan defaulted management policy and financial performance as the dependent variable. It shows how specific loan policies applied by commercial private banks affect the financial performance of this private commercial bank. The financial performance would be measured by net income to total assets.

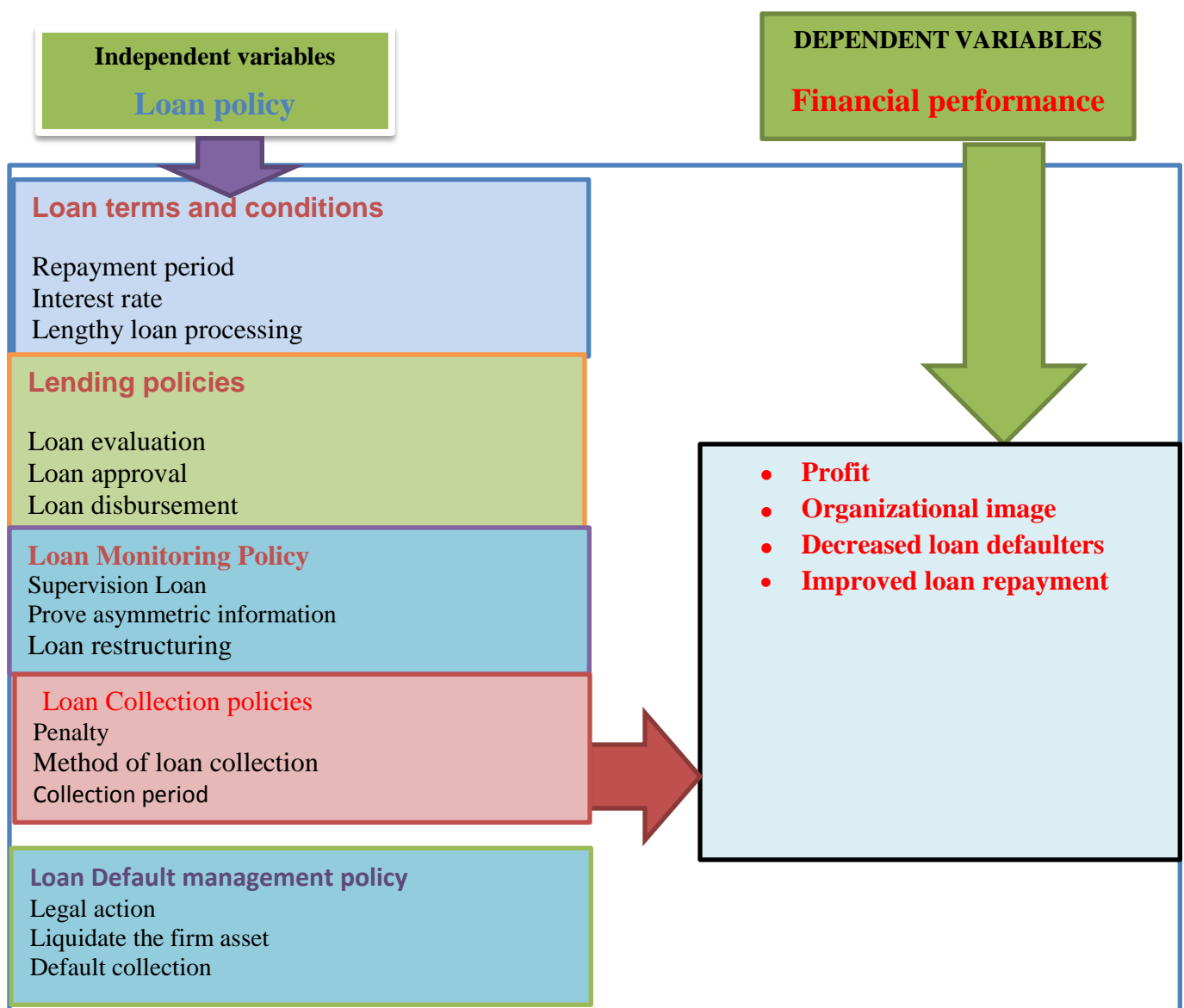


Figure 2.1 Conceptual framework

Source researcher: (2021)

2.9. Research hypothesis

In order to test the relationship of the independent variables and financial performance the following hypotheses has been tested. The studies that were guided by the null hypothesis were Loan policies had no effect on the financial performance of a selected private commercial bank in Ethiopia, and the alternative hypothesis was as follows:

HA1: There is a positive and significant relationship between loan terms and conditions policy and financial performance.

HA2: There is a positive and significant relationship between lending policies and financial performance.

HA3: There is a positive and significant relationship between loan monitoring policies and financial performance.

HA4: There is a positive and significant relationship between loan collection policies and financial performance.

HA5: There is a positive and significant relationship between default management policies and financial performance.

CHAPTER THREE

RESEARCH DESIGN AND METHODOLOGY

3.1 Introduction

This chapter described the study's research design and methodology. This chapter included methods and techniques for facilitating the research endeavor, such as assembling the target population, the research design used data collection methods, data sorting and analyzing procedures, results presentation methods, and research ethics to achieve the specified goal.

3.2. Background of the Study Area

Addis Ababa is the capital city of Ethiopia and the diplomatic capital of Africa, with a population of 5,005,524 people. It is the seat of the national government and is located at 2,380 meters above sea level on a well-watered plateau (UN World Urbanization Prospects, 2021). It would be chosen as a study area because the head office of each bank, which represents the entire branch in the country, and the country's national bank are both located in the city. The research would focus on selected private commercial banks operating in Addis Ababa.

3.3. Research paradigms

Epistemology is defined as "a method of comprehending and clarifying how we know the truth." Epistemology is also "focused on offering a philosophical foundation for determining what kinds of knowledge are possible and how we can ensure that they are both sufficient and valid. Defines ontology as "the study of being." It is concerned with "the nature of reality, the structure of reality, and what kind of universe we are conducting an investigation." (Crotty, 2003). For this study, I thought it would be best to have both qualitative and quantitative (mixed methods research) approaches. On the basis of this research strategy, I employed two paradigms: the social constructivism (interpretive) paradigm, which employs inductive logic and qualitative research approach, and the post positivism (positivist) paradigm, which employs deductive logic and quantitative research methods. The interviews used to collect data from the respondents in addressing qualitative questions embraced the social constructivist perspective of this study. By seeking answers to theory-driven questions, the questionnaire (quantitative instrument) embraced

the post positivist perspective. The study was used quantitative research approach based on the philosophy of post positivism.

3.4. Research Approach

The research approach clarifies the methods for data collection, data analysis, interpretation, communicating findings, validation, and the questions to be answered. The chosen method of investigation also influences the research techniques. In this study, the researcher employed a mixed research approach that included both qualitative and quantitative research methods. The quantitative research approach will mainly concentrate on the collection of quantitative data, which will result in a systematic report comprised of numbers constructed by researchers using measurement procedures and imposing structure (Kent, 2007). The qualitative method is defined as "a method of information inquiry in which the researcher develops a complex, holistic picture, analyzes words, reports detailed informant views, and conducts the study in a natural setting." In this approach, the researcher makes knowledge claims based on constructivist perspectives. The use of this method ensures that the collected data is effectively interpreted and analyzed through the use of descriptive statements. The mixed method approach uses both quantitative and qualitative approaches concurrently to be more effective and beneficial to the study and thus goes beyond simply collecting and analyzing quantitative and qualitative data from the study (Creswell, 2009).

3.5. Research Design

Both descriptive and explanatory research designs would be used in the study. Robinson (2002) defines descriptive research design as "observing and describing the behavior of specific objects using scientific tools without influencing it." This is due to the fact that descriptive survey research design is appropriate when the study seeks to describe the characteristics of specific groups, estimate the proportion of people who have certain characteristics, and make predictions (Cooper and Schindler, 2003). According to Kothari (2004), the design is also appropriate because it assisted in explaining the issue as it exists without the manipulation of variables that changed the goal of the have aspect. The explanatory research design aids in identifying and evaluating the causal relationships among the variables under consideration (Marczyk et al, 2005). The explanatory research design would be used to investigate the relationship between the

variables listed. Surveys are designed to gather information that will be investigated, designs derived, and comparisons made in order to categorize and to provide information on which to make decisions. Given the timespan and financial constraints, as well as the fact that academic research contains many factors that cannot be truthfully controlled, the descriptive and explanatory design would be best suited to the study of, Assessment of loan policy and its effect on financial performance of selected private commercial banks in Ethiopia.

3.6. Research strategy

According to Wisker (2009), research strategies can include case studies, surveys, ethnography, field experiments, simulations, laboratory experiments, action research, archival analysis, role playing, and other methods. The suitability of these methods is determined by the research objectives and the investigation's philosophy. This study's research strategy would be survey-based, with cross-sectional data quantitative as well as qualitative. According to De Vaus (2002), Surveys are used to collect data from a large population. A survey is more than just a data collection technique; it also includes questionnaires and in-depth interviews, content analysis, and observation, among other things. This will be appropriate for this study because some objectives will necessitate the collection of a large amount of data from a variety of professions. The surveys will be both quantitative and qualitative in nature.

3.7. Population of the study and Sample and Sampling Techniques

In statistics, the population is the entire group of people for whom data is sought. A population, according to Orodho (2003), is a well-defined or analyzed group of people, organizations, elements, events, and households. All private commercial banks operating in Ethiopia would be the study population. Six banks were selected from a group of sixteen private commercial banks depending on their years of establishment and banking experience of greater than fifteen years. Profitability does not come overnight, so the banking experience is also the most important to develop good loan policy and almost the majority of revenue stream of the banks comes from the interest income. To manage the loan required knowledge, experience and effective lending policy are important. Those banks that were selected were (Awash Bank, Dashen bank, Nib international bank, united bank, Wegagen bank and cooperative bank of oromia), but bank of Abyssinia not interested to provide information for my research so excluded from selection.

Currently there are 16 private commercial banks operating in Ethiopia. Loan officers and loan general directorate from each private commercial bank would be selected as the target respondent.

According to Trochim (2005), sampling is the process of obtaining a representative sample from a larger population. Sampling techniques are a type of statistical procedure that entails the choosing of observed values in order to gain insight into a population of interest, particularly for statistical inference. Sampling's primary goal is to eliminate statistical error. A sample size has the property of being able to identify and include any item in the sample. Purposive sampling would be used to choose six general loan managers for in-depth interviews about loan policy and its impact on financial performance, and sample size would be used to sample loan officers who worked on loan processing (, loan appraisal officer, loan analyst officer, customer relation management officer, Loan recovery officers and loan follow up officer, would be the major respondents). The targeted respondents of loan officers from the six private commercial banks were 155 but 112 loan officers were chosen from this group. The study employed Yamane's sampling method to choose loan officers, and then used a basic random sample technique as indicated below:

Sample determination

Simplified formula to calculate sample sizes used by Yamane's (1967) provides a. This formula assumed a 95% confidence level and margin of error (e) 0.05 which is as follows;

$$n = \frac{N}{1 + N(e)^2}$$

Wherein;

n refers to the sample size,

N refers to the populace size, (155)

e is the extent of precision (0.05).

$$n = \frac{155}{1 + 155(0.05)^2} \quad n = 112$$

Table 3.1 Sample size of Respondent

s.no	Names of banks	target population	sample size
1	Wegagen Bank	27	$112(27/155)=19$
2	Dashen Bank	30	$112(30/155)=22$
3	Cooperative Bank of Oromia	18	$112(18/155)=13$
4	Nib international bank	26	$112(26/155)=19$
5	Awash international bank	28	$112(28/155)=20$
6	United bank	26	$112(26/155)=19$
Total		155	112

Therefore, six general loan directorate sampling purposively and 112 loan officers selected by sample size.

3.8. Data Collection

There are instruments that were used in collection of primary data were closed ended questionnaires, open ended questionnaires and interviews. Primary data would be by administering questionnaires to the respondent to get data from loan officers of private commercial banks and interviews was used for general loan manager of private commercial banks and secondary data was collected from financial statements reports from each bank for consecutive five years from (2016-2020).

3.9. Description of Research instruments

To carry out the research, 46 closed ended questionnaires, 5 open ended questionnaires and 8 interview questions were prepared and secondary data would be collected from annual financial reports of banks for five consecutive years. The questionnaire allowed measurement for or against a particular viewpoint. A questionnaire has the ability to collect a large amount of information within a very short time. Through use of questionnaires, information would be collected from a large number of people and the questions would be easily analyzed and it allows anonymity, (Orodho, 2009).The questionnaire would be used for both open-ended questions and closed questions. The questionnaire contained the questions which would be structured of close-ended questions and also a few open -ended questions. Close-ended questions would be accompanied by a list of possible alternatives from which respondents would be required to select the answer that best describes their situations. The main advantage of closed ended questions is that they are easier to analyze since they are in an immediate usable form. They are

also easy to administer because each item is followed by an alternative answer and was also economical to use in terms of time saving. To measure the response of respondents from closed ended questionnaires to used five scale likert scale (strongly agree, agree, not sure, disagree and strongly disagree). while open-ended questions would facilitate in-depth response and opinions beyond the researchers scope of under stability. According to Yin (1989) Semi-structured interviews were conducted to enhance and supplement the results of questionnaires. Interviews would be face to face encountered with a purpose. In undertaking the research, face-to-face would be used together with information from the general loan manager of the bank and recorded the voice of the interviewer for collecting the quality of information. It is directly involved with the general loan directorate manager. Interviews would be used to get detailed information about the effect of loan policy on financial performance of selected private banks.

3.10. Description of the Data Collection Procedures

Data is anything given as a fact on which research inference would be based. It is anything actual or assuming as a basis of estimate (Mugenda and Mugenda, 2008). In this study the researcher obtained an introductory letter from Addis Ababa University and submitted it to each head quarter of a private commercial bank to get permission from the bank. The researcher would collect data using questionnaires. Questionnaires would be used, mainly with variables that cannot be directly observed such as views, opinions, perception and feeling of the respondents. Questionnaires would be distributed to the respondents then collected after the agreed period of time and interviewed general loan manager of six private commercial banks at their office and secondary data collected from National Bank of Ethiopia, six selected private commercial banks financial statements from years of(2016-2020) operation

3.11. Data Analysis

The data that would be collected using a data collection sheet are edited, coded and cleaned. The paper would be primarily based on primary data which would be collected through questionnaires; the collected data will be analyzed by using the Statistical package for the social sciences (SPSS). According to Brooks (2008) the study would use both quantitative and qualitative data. Descriptive statistics data analysis method would be applied to analyze numerical data gathered using closed-ended questions. SPSS would be considered appropriate

since it would allow the study to follow a clear set of quantitative data analysis procedures that leads to increasing data validity and reliability and demonstrates the relationship between the research variables. According to Kothari (2005) descriptive analyses provided the foundation upon which correlational studies emerge; they also provided clues regarding the issues that would be focused on leading to further studies. Descriptive statistics assist in computing measures of central tendencies and measures of variability in order to determine how independent variables would affect the dependent variable.

Inferential facts would be practiced by correlation analyses which would be used to establish with statistical significance, the character of the present seeing among the establishing variables and the unbiased variables. The researchers would be to examine further multivariate regression versions to study the determinants of loan policy within the financial performance. The research chose a regression approach because of its capability to test the nature of influence of impartial variables on establishing variables. Regression could be capable of estimating the coefficients of the linear equation, concerning one or greater impartial variables, which high-quality expected the value of the based variable, despite the fact that Multivariate analysis has the following assumptions; Linear relationship, Multivariate normality. They have a look at linear regression analysis to research the data. Regression analysis is the formulation of statistical relationship between one or more variables (Fraenkel and wallen 2011).Data was sorted using descriptive analysis such as standard deviation, multiple regression analysis, mean and correlation coefficient.

The regression model will be in the form:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \epsilon$$

Where Y=financial performance and;

X1= loan terms and condition policy

X2= lending policies

X3= Loan Monitoring Policy

X4= loan collection policy

X5= Loan Default management policy

α =constant value

ϵ = Error term

β =coefficient of independent Variables

3.12. Variables Definition

According to Creswell (2009), to make it clear to readers what groups are receiving the experimental treatment and what outcomes are being measured, the variables need to be specified in quantitative research.

3.12.1. Dependent Variable

Financial performance, it's the rate at which an organization is able to generate income through effective and efficient loan management. Profit of the bank can be dependent variable of the study. Profitability will be measured using $ROA = \text{Net income} / \text{total asset}$. Return on Assets; this is the rate of return accruing from the use of assets involved in generating an organization's income to assess its viability.

3.12.2. Independent Variable

The independent variables were loan terms and condition policy, loan lending policies, Loan Monitoring Policy, loan collection policy and loan default management policy. Definition of Independent variables were

Loan terms and conditions are the requirements that a customer must follow in order to be eligible for a bank loan. The term "loan terms" refers to the terms and conditions of borrowed funds. This can contain the loan's repaying time, length loan processing, rate of interest and charges, any penalty fees debtors may be charged, and any other particular circumstances that may be applicable.

Loan lending policies determine the applicant's capacity to repay the amount of the loan borrowed according to the loan policy's guidelines. This covers the overall loan application, appraisal, and disbursement process.

Loan Monitoring Policy, It's the process of following up on a loan from the time the funds are disbursed until the last installment is due. Loan monitoring improves the recovery process by keeping the repayment track and discouraging loan default.

Loan collection policy is a strictly regulated procedure. The creditor usually offers the loan with collateral or a guarantee to the debtor since the creditor wants to collect the amount plus interest. The debtor and the lender agree into a legal agreement to repay the loan by a specific date and time.

Loan default management policies, default management policy is the process of collecting default loans which have not been repaid and managing to recover them by convincing the debtors to make attempts to repay their outstanding loans.

3.13. Validity and Reliability of Research Instruments

3.13.1. Validity

Validity of an instrument is the success of a scale in measuring what it units out to degree so that differences in individual ratings can be taken as representing actual differences on the characteristics under observation. Content validity refers back to the subjective settlement among specialists that a scale logically seems to mirror accuracy of what it significance to degree (Kothari, 2005). The pattern of instrument changed into pre-tested to enhance its validity and relevance to the goals of the take a look at. The questionnaires could be scrutinized for errors and omissions, ambiguity, legibility and relevance. The questionnaires content, shape and sequence would be correctly amended to do away with any ambiguities and to enhance content material validity. To determine the content material validity of the questionnaire objects, studies experts would be used to have a look at them and their suggestions and comments may be used as a foundation to alter the research items.

3.13.2 Reliability

Reliability refers to the consistency that advice demonstrates while implemented repeatedly under similar situations (Kerlinger, 2003). To determine reliability of research devices, the tool can be pre-testing complete a peer evaluation with pilot observation before the actual information series to enhance reliability. The significance of pre-testing a questionnaire

according to Creswell (2003) is to help the researcher understand the means of the questions to be put to the respondents and how they arrive at their response.

Table 3.2. Reliability Test of Constructs

Variables	NO. Items	Reliability Cronbach's alpha	Comment
Loan terms and condition policy	10	.751	Accepted
Loan lending policies	10	.704	Accepted
Loan monitoring policies	10	.786	Accepted
Loan collection policies	10	.837	Accepted
Loan default management policies	10	.647	Accepted
Financial performance	6	.914	Accepted

Table 3.2 shows that the reliability test for all variables is more than 0.6 for all kinds of research variables. Nunnaly (1978) established the 0.6 alpha value criteria against which the study was measured. The presence of reliability (internal consistency) is shown by a value greater than 0.6, and thus the result reveals that the test of reliability of a research instrument is acceptable.

3.14. Research ethics

According to Saunders et al. (2013) research subjects have ethical rights. In the spirit of honesty, all thoughts, ideas, writing or drawings that were borrowed from others even if paraphrased into my own words were properly credited through acknowledgement and citation. Researchers have to conduct themselves in a responsible manner when conducting their profession and relating with respondents and must adhere to high ethical standards to ensure that both the study and the information therein are not brought into disrepute. The researcher followed ethical guidelines which included an ethical review process before engaging respondents to ensure that procedures were fair and unbiased to all who were involved. Before the administration of the questionnaire, the researcher explained the purpose of the study to the respondents and ensured utmost confidentiality about the information was maintained. Responses were kept strictly confidential and I used them only for academic purposes.

CHAPTER FOUR

4. DATA ANALYSIS, PRESENTATION AND INTERPRETATION

4.1. Introduction

This study was conducted to evaluate loan policy and its effect on the financial performance of a selected private commercial bank. Following the objectives of this research study, this chapter presents the findings obtained from various respondents, their demographic characteristics, and data analysis in the tables, correlation, regression, and their relevant interpretation.

4.2 Response rate

The study had sample size of 112 respondents, and all of the respondents participated in the study as planned, indicating that the response rate was 100 percent.

4.3 Demographic characteristics of the respondents.

4.3.1 Gender distribution of respondents.

The age of respondents was investigated to find out if there was a certain age bracket that dominated the study. The findings from the respondents were revealed on table 4.1

Table 4.1. Gender respondent

No	Item	Frequency	Percentage
1	Gender		
	Male	83	74.1
	Female	29	25.9
	Total	112	100

According to the table above, out of the 112 respondents who participated in the study, most of the respondents were males who made 83 or 74.1% of the study while 29 or 25.9% were females. Therefore according to the above table the leading respondents were males 83(74.1%) and the least number of the respondents were females 29(25.9). In this study having respondents who are males and females as shown above therefore implies that the study was gender sensitive and therefore the views of all sexes were captured and represented in this study.

4.3.2 Age distribution of respondents.

The profile of the respondents was looked into to see if there was a predominant age group in the research. Table 4.2 summarizes the results from the participants.

Table 4.2. Age of respondent

Age in Years	Frequency	percentages
20-30	44	39.3
31-40	60	53.6
41-50	7	6.3
Above 50	1	9
Total	112	100

As seen in the table above, the age bracket that dominates the study population was 31-40 years old, accounting for 53.6 percent of the total population, followed by those aged 20-30 years old at 39.6 percent, 41-50 years old at 6.3 percent, and those aged above 50 years old at 9%. This indicates that the data was reliable because it came from mature respondents who were able to complete the questionnaire with ease and was familiar with how loan policy affects the financial performance of private commercial banks because the majority of them had prior experience with loans from this case study. Having a large number of respondents between the ages of 31 - 50, indicates that the data was collected from mature respondents and so may be trusted in this study.

4.3.3 Marital status

The issue of married status was also investigated, and the following results were discovered, as given in table 4.3.

Table 4. 3. Showing marital status of respondents

Marital Status	Frequency	percentages
Single	44	39.3
Married	68	60.7
Total	100	100%

According to table 4.3, 60.7 percent of the 112 respondents were married, while 39.3 percent were single. This considered to be a significant feature of the study because they had a good understanding of the topic and thus supplied credible information. This indicates that there were a large number of married respondents (68.7%), followed by single respondents (44%). (39.3)

4.3.4 Education background

When making business judgments, a loan officer's educational qualification is an important factor to consider. Education enhances capacity building by developing skill, capability, communication, and accessibility. As a result, because education is such an essential component, it was investigated if the majority of the respondents had received education up to the level of a PhD. This allowed the researcher to determine whether they had grasped the meaning of lending policy and its impact on the financial performance of a particular private commercial bank.

Table 4.4. Education background of respondent

Education background	Frequency	Percentage%
Degree	58	51.8
Masters	53	47.3
PhD and Above	1	.9
Total	112	100.0

Table 4.4 demonstrates that all participants had varying degrees of education depending on their qualifications. According to the above data, many respondents who completed university degrees: 58 (51.8%) completed a bachelor's degree, 53 (47.3%) obtained a master's degree and 1 (0.9%) acquired a PhD degree.

4.3.5. Loan Related Experience

The purpose of the study was to determine the length of time that respondents had been involved in loan-related experience. This was also taken into account in order to assist the researcher in assessing the length of time the participants had spent in their respective occupations.

Table 4.5. Loan Related Experience

Loan Related Experience	Frequency	Percentage%
Loan Related Experience		
1-5	40	35.7
6-10	49	43.8
Above 10	23	20.5
Total	112	100.0

Table 4.5 illustrates respondents' job experience. Of the 112 respondents, 35.7 percent have worked for a period of 6-10 years, 43.8 percent have worked for a period of more than 10 years, and 20.5 percent have worked for more than 10 years.

The preceding table clearly reveals that 49 (43.8 percent) of the respondents had been employed for 6-10 years, followed by 40 (35.71%) who had been engaged for 1-5 years, and the least number of respondents had been employed for more than 10 years, as demonstrated by 23 (20.5).

As a result of the preceding findings, a significant proportion of respondents have had loan-related experience. The majority of responders have more than six years of experience, which was the most significant determinant in my study.

4.4. Descriptive Analysis

The descriptive statistical analyses are reported in the next section; the data was collected in connection to the study's objectives. The study used the descriptive data in this part, such as mean and standard deviation. According to Aggesti (2009), the mean (\bar{x}) is the weighted sum calculated by summing the values of each case of the research variables and dividing the sum of cases; it's used to evaluate the data's central tendency. The standard deviation is a number that illustrates how variable a set of data. It shows how close the data is to the mean. According to Aggesti (2009), a mean of 1.00 -2.49 was rated very weak, 2.50 -3.49 Weak, 3.50 -4.49 Strong, and 4.50 - 5.00 Very Strong, while a standard deviation of larger than 0.5 was considered homogeneous and less than 0.5 was considered heterogeneous.

4.4.1 Loan terms and condition policy and financial performance

Loan terms and conditions are phrase and guidelines that any borrower should follow both before and after obtaining a loan. They have the most important capabilities of any financial institution and cannot be used by any employer in the money lending sector, regardless of the nature or environment in which they operate. The terms are in place to guarantee that debtors can easily meet their commitments while incurring the least amount of cost to the institution. According to Drzik(2012), these laws include interest fees, time, and the strategies used by the lender to collect the entire amount owed from the borrower.

Table 4.6 .Loan terms and condition policy and financial performance

Statements	Mean	Std. Deviation
Bank has well developed written loan policy	4.65	.497
Does your bank frequently review its loan policy	4.33	.621
Bank set interest rates charged on loans at market rate	4.30	.641
the repayment schedules set for each loan negotiated with the client	4.02	.958
Loan terms and conditions practiced by your bank influence the volume of loans obtained from your bank	4.07	.744
Loan terms and conditions put in place by a bank affect its ability to attract loan seekers	3.96	.805
The bank adjusts the interest rates on the loan granted without referring to the customer	3.56	1.184
The bank lending offer mostly long terms loans	3.21	1.132
During your loan processing, you are strictly enforced to fulfilled the conditions and terms set by loan approval team before loan disbursement	4.45	.655
Well-developed loan terms and condition policy increase banks profitability	4.55	.567

As illustrated in the table above, the majority of respondents agreed with the effect of loan terms and condition policy on financial performance of a selected private commercial bank in Ethiopia. The majority of respondents strongly agreed with mean 4.65 and SD 0.497, the bank has a well-developed written loan policy this study was agreed with Kantor and Martal (2001), banks that conduct business without a written credit policy may lack a standard way of administering credit to customers, reducing their ability to compete with other market players. Also, according to Ibrahim (2004), a rigorous loan policy is one in which financial systems provide credit rating facilities to their customers who have validated credit worthiness. Banks and businesses with strict loan policies adhere to strict credit score standards and terms, lowering the cost, risks, and

chances of bad debt and liquidity problems. Miller (2008) cites four reasons why a company should have a credit policy in writing: It reduces bad debts and enhances cash flow in the first place. Second, a policy ensures that departments are operating in the same direction. Third, it provides clients with a consistent way in which decision-making becomes a logical feature based on pre-determined parameters. Finally, it can provide some acknowledgement of the credit department as a separate organization.

Most of the respondents agreed with the mean of 4.33 and SD of 0.621. The bank has frequently reviewed its loan policies. These findings indicate that the bank loan policies are reviewed regularly. Most of the respondents agreed that with a mean of 4.3 and SD of 0.641, banks were charged interest rates on loans at market rates, taking the economic condition into account when setting the interest rate on the loan. The majority of respondents agreed with the mean of 4.02 and SD of 0.958. The bank discussed with the borrower about repayment schedules, method of payment, due date and any terms when providing the loan to the borrowers.

The majority of respondents agreed with the mean of 4.07 and SD of 0.744 that loan terms and conditions practiced by banks influence the volume of loans obtained from banks. Most respondents agreed with the mean 3.96 and SD 0.805 loan terms and conditions policy of the bank that attracted loan seekers, so the bank has a good loan policy that could compete with other banks. The majority of respondents agreed that the bank adjusts the interest rates on the loan granted without referring to the customer, with a mean of 3.56 and SD of 1.184; this means the bank would set the interest rate by themselves without discussion with customers. When setting interest on the loan, the banks considered the risk area of the business, economic condition, general inflation, and national bank directives into account.

Most of the respondents agreed that the bank offers slightly longer-term loans, with a mean of 3.21 and SD of 1.131. This study indicated that the bank is lending both short-term and long-term loans to the borrowers. The majority of respondents strongly agreed that during loan processing, strict enforcement was used to fulfill the conditions and terms set out in the loan policy, that approved by the loan committee team before loan disbursement to the borrower with a mean of 4.45 and SD 0.655. This means that banks efficiently evaluated the borrowers to fulfill the terms and conditions on the loan policy.

With a mean of 4.55 and a SD of 0.567, the majority of respondents highly agreed with the bank's well-developed loan terms and condition policy, which increases the bank's profitability. This indicates that the bank has a strong lending terms and conditions policy that evaluates the borrower; according to Ozdemir (2004), loan terms of financial institutions in Turkey demonstrated a somewhat positive relationship between debtor loan size and repayment terms.

One of the KI. "Prior to loan lending to consumers, customer relations officers (CRM) engaged in such activities as preliminary conversations with customers, appraising the customers' activities, counseling the customers on the most efficient way for them, and the objective of the loan," If a project loan requires a bill of quantity, a business plan proposal, an environmental impact assessment of the project, a market assessment, a financial plan, and a feasibility study, the bank determines the interest rate by analyzing cost-benefit and market conditions on the product set by the bank's board of directors based on terms and tariffs. Review the loan policy on a regular basis based on market conditions." (KI General Directorate of Private Commercial Bank Loan Managers).

One of the key informants said that "loan terms and condition policies of the bank would be discussed with customers during the initial stages; the bank would negotiate with the customers about loan terms and conditions; choose the contract types; and the bank would develop (CAF) guidance for the customers to clear the terms and conditions for customers. To set interest rates, the banks would consider the following factors: credit risk, sector, nature of collateral, and duration of loan to be taken into account. Long-term loan interest is high because the risk of collectability is high." (KI general directorate of loan managers of private commercial banks).

4.4.2. Loan lending policies and financial performance

The fundamental business bank of economic activity is lending. According to Ozdemir (2004), loan lending signals from financial institutions showed a link between the size of the loan and the length of the repayment period. In his investigation, he discovered that the amount of loan

superior is influenced by the borrower's level of earnings. It is necessary to begin by organizing the legitimate economic needs of the capable borrower, rather than the banks' financial performance. As a result, the lending institution must ensure that loan terms are always current, as they may have an impact on the financial company's growth, balance, and financial well-being. Loan assessment, approval, and distribution are all aspects of lending. The process of analyzing a loan request in order to obtain information regarding the individual's ability to repay the loan according to the conditions of the lender's lending policy is known as loan inspection. More overs discovered that loan regulations were recruited to improve performance and coordination of asset investment activities, resulting in improved monetary overall performance (Mraba, 2009).

Table 4.7. Loan lending policies and financial performance

Statements	Mean	Std. Deviation
The lending policy developed by bank adequate and effective	4.18	.604
Good lending policy increase loan repayment	4.36	.628
Stringent loan policy minimize cost of collection, bad debt expense and unnecessary legal cost	4.22	.667
When considering granting loans, the bank requests the availability of guarantees in excess of the value of the loan granted	3.96	.842
The bank's board of directors delegates the management of lending responsibilities to specialized committees that carry out responsibilities for implementing the lending policy.	4.21	.776
The bank takes into account the laws and regulations in force by the monetary authorities in the country, especially with regard to lending policies.	4.49	.569
The banks approve the maximum limit for lending according to the number of funds available for lending.	4.21	.728
When making a lending decision, the bank takes into account the evaluation of loan that lending	4.35	.532
The bank, before granting the loan, studies the experience, suitability, and reputation of the borrower	4.49	.553
Lending policies adopted by banks greatly influence the performance of the bank.	4.47	.519

According to table 4.7.above, the majority of respondents agreed that the lending policies had an effect on the financial performance of private commercial banks in Ethiopia. Most respondents agreed with the mean of 4.18 and SD of 0.604. The lending policy developed by the bank was adequate and effective, so the bank has a policy that guides their loan this study was agreed with

Stafford (2001) a policy is a planned path of action that leads to a sensible result (s). The lending policy of a bank is a declaration of philosophy, principles, and procedures that personnel must consider before approving or rejecting a loan request.

Most of the respondents agreed that good lending policies increase loan repayment with a mean of 4.36 and 0.628. This indicates that the lending policy assesses the ability and capability of the borrower before disbursement loan to the debtors, this study was agreed with Hogan, Lemon, and Rust (2001), who state that the goal is to attract and retain profitable clients and also the study agrees with Abedi's (2000) 5Cs model of credit scoring to evaluate a client as an ability borrower, namely, character (trustworthiness and integrity of the business owners); potential (whether the enterprise's (or household's) cash flow can service loan repayments); collateral (the asset provided as a safety net in case the loan defaults); capital (property and liabilities of the commercial enterprise or household); and situation (marketing technique that recognizes the commercial enterprise's or household , and the legal and monetary climates).

With a mean of 4.22 and 0.667, the majority of respondents agreed on a stringent loan policy to reduce the cost of collection, bad debt expense, and unnecessary legal costs. Research found that having adequate and effective credit appraisal, monitoring, and loan recovery is necessary. This is in agreement with Pandey (2001), who stated that strict credit policies reduce collection costs, bad debts, and unnecessary legal fees. It also aligns with Ibrahim's (2004) research. Financial institutions with a strict credit policy provide credit to customers who have proved credit worthiness. Banks or organizations with stringent credit policies adhere to strict credit standards and terms, reducing costs, risks, and chances of bad debts and liquidity issues. With a mean of 3.96 and a standard deviation of 0.842, the majority of respondents agreed that when considering granting loans, the bank requests the availability of guarantees in excess of the loan's value.

The majority of respondents agreed that the bank's board of directors delegates the management of lending responsibilities to specialized committees that carry out responsibilities for implementing the lending policy with a mean of 4.21 and SD.776. Based on the amount of loan, from small to large funds, there are the level committees from the district branch of the bank up to the head office of the bank that are assigned to prove the loan request and evaluate customers' ability to repay debt. The majority of respondents strongly agreed as the bank takes into account

the laws and regulations in force by the monetary authorities in the country, especially with regard to lending policies, with the mean of 4.49 and SD of .569.

The majority of respondents agreed with the banks' approval of the maximum limit for lending according to the amount of funds available, with a mean of 4.21 and SD of 0.728. This study showed that the bank first checks the availability of resources for providing loans and also sets the maximum and minimum limits based on the types of customers. Most of the respondents agreed on when making a lending decision; the bank takes into account the evaluation of loans that are lent to customers with the mean of agreed 4.35 and SD.532. Most respondents agreed that the bank, before granting the loan, studies the experience, suitability, and reputation of the borrower, with a mean of 4.49 and SD of 0.553. The majority of respondents strongly agreed that the lending policies adopted by the bank greatly influence the performance of the bank with the mean of 4.47 and SD of 0.519. This supports the findings of Esty & Megginson (2003), who found that a bank's lending policies are expected to have a major impact on its financial performance.

One of the key informants said that "the bank did 360 days of diligence on customers, such as, where was their business location? What to do, where do you get raw materials? Who are the customers of the borrowers?" To study the feasibility of the business, they did NPV, RRR, PBP, working capital determination, management capability, management risk grading, and ratio analysis, such as inventory holding ratio, inventory conversion ratio, and loan to deposit ratio. The bank would be proved the information provided by customers, the legal documents checked and authenticated, submit audited financial statements and also send a letter to auditors for conformity that the financial statements audited by him, site visit, and what the business looks like and by sending a professional to evaluate the customer's business "(KI loan manager of private commercial bank).

One of the KI said that "the lending policies and procedures of each loan department are driven by master strategies; the bank has long-term, medium-term, and short-term strategies." Based on these master strategies, the banks decide how much credit to provide to customers per year. But the loan policies were affected by many factors, such as COVID-19, import and export

conditions, hard currency, political instability, and the market conditions. For such factors, the bank revises the loan policy and negotiates with customers. Effective lending policies are affected by internal and external factors. Large volumes of loans were provided for import and export trade, manufacturing, industry, agro-food processing, and the least loans were provided for the agriculture sector because of the high risk of the sector. Most of the Ethiopian banking industry's lending is collateral-based loans. Without collateral, it is very rare. They have been mostly providing loans for corporate types of customers and have existed with banks for a long period of time. The bank could not use peer lending or co-borrowers as collateral to provide loans to customers; this was very rare. The loan processing takes days after the last submission of required documents for a project loan, seven days, and for a working capital loan, five days” (KI loan manager of a private commercial bank).

One of the key informants said that “to lend efficiently types of lending, the bank prepared policies and procedures based on the national bank directives. Before lending funds to customers, the bank verifies the following information: the legal document or article of association (PLC), the legal license of the business, the length or duration of the loan, the tax identification number, clearance, checking customers in defaulter lists in NBE servers, customer history, asking for current audited financial statements less than three months old, and also checking the name of qualified auditors in NBE servers and during loan providing of loan appraisal, approval, disbursement and record processing was maintained” (KI loan manager of private commercial).

One of the key informants said that “to lend efficiently types of lending, lending requires loan evaluation, loan approval, and loan distribution. Loan evaluation is the appraisal of a loan application with the goal of providing information on the applicant's ability to repay the loan in accordance with the standards outlined in the bank's loan policy. Before approval, the credit manager and credit committee must ensure that the loan follows all required processes as specified in the credit policy requirements in order to avoid

early default caused by an inadequate evaluation strategy” (KI loan directorate manager of private commercial).

4.4.3. Loan monitoring policy and financial performance

Loan monitoring enhances restoration procedure because it maintains track on the reimbursement and discourages loan default. The bank should make proper loan observations-as much as enhance high returns from loan investments and decrease delinquency levels, as a consequence indicates high economic overall performance of the financial institution. Adequate and powerful monitoring rules that assist examine customers earlier than advancing loans, display payments and recover non-performing loans. Exact credit score control policies increase loan reimbursement rates properly as decrease the cost of series, bad debts and unnecessary legal charges as well as making sure timely allocation of sources. According to Mutua (2016) favorable performance is decided through the rate of loan recovery where a high recovery fee shows high level of economic low recoveries fee depicts the opposite that is superior through close credit score tracking. Delays in loan recovery consequently motive loss within the loan assets (Sobhan, 1991).

Table 4.8. Loan monitoring policy and financial performance

Statements	N	Mean	Std. Deviation
Bank has a policy to guide its loan.	112	4.63	.484
Bank has a policy to evaluate the customer asymmetric information before advancing loan to them	112	4.33	.649
Bank has a policy that help to monitor the customer repay their loan	112	4.39	.559
Management efficient in the loan recovery of funds from non-performing loan	112	4.36	.613
Does regularly assessed collateral and related to applicants financial health	112	4.21	.764
Does the bank do restructuring loan repayment of borrower after lending	112	4.33	.649
The bank periodically prepare loan grading reports for signaling loan loss in any portfolio	112	4.17	.804
Continuous monitoring of cash flows of borrower	112	3.84	.865
The bank does follow-up to ensure that funds provided for the stated function are being used properly.	112	4.09	.754
Bank loan monitoring policy increase bank profitability	112	4.45	.534

According to table 4.8 above, the majority of respondents agreed that loan monitoring policies have an effect on the financial performance of private commercial banks in Ethiopia. The majority of respondents strongly agreed that the bank has a policy to guide its loan to follow up and monitor the customers who have borrowed with the mean of 4.63 and SD of 0.484. This study agrees with Seppala (2000) credit monitoring refers to measures too; ensure that the bank understands the current financial condition of the borrower or counterparty; ensure that all loans comply with the existing agreement; track customer usage of approved credit lines; ensure that projected cash flows for large exposures meet debt servicing requirements; ensure that the collateral provides adequate coverage where applicable. Almost all respondents agreed that the bank has a policy to evaluate the customer's asymmetric information before advancing a loan to them, with a mean of 4.33 and SD of 0.649. Credit monitoring includes on-site visits, regular contact and checking compliance with covenants in credit agreements. This finding indicates that the bank evaluated the information that was provided by customers. The majority of respondents agreed that the bank has a policy that helps monitor the customer repay their loan with a mean of 4.39 and SD of 0.559. This result was agreed with by (Mwisho, 2001), which found out that monitoring of borrowers could be very important due to the fact that it could help a business enterprise forecast default in time.

Most of the respondents agreed with the bank policy that has guided the loan recovery of funds from non-performing loans, with a mean of 4.35 and SD of 0.613. This study agrees with Montana (2012) Bank debt recovery is developing an alarming trend, with its expansion appearing practically irreversible. This increase is primarily due to the global economic downturn that has impacted both consumers and markets. Financial institutions are devising new techniques and strategies to boost their collections and recovery rates.

Most of the respondents agreed that the bank has regularly assessed collateral and related to the applicant's financial health, with a mean of 4.21 and SD of 0.764. This finding indicated that the bank restructured their loan repayment for borrowers after lending with a mean of 4.33 and 0.649. This finding indicated that the bank during loan monitoring and follow-up saw the difficulties of borrowers who were unable to repay the debt, so the bank restructured the repayment schedules of the debt based on the debtor's ability to repay. This study agrees with Montana (2012) that some of the recommended actions for collecting bank debt that are likely to

help increase your success in collecting accounts receivable are; flexible repayment plans for clients in financial difficulty; well-formulated hardship programs for late borrowers; extension or reduction of payments; interest rates or lower fees.

Majority of respondents agreed that the bank periodically prepared loan grading reports for signaling loan loss in any portfolio with the mean 4.17 and 0.804, thus finding out that the bank prepared the loan grading report in each investment during follow up and monitoring the debtors. So the banks were advised the debtors the way of enduring /preventing the loss that affects the business, this study was agreed with Ibrahim (2004) showed that the way banks handle their loan portfolios has a significant impact on its profitability in Nigeria. Some respondents agreed on the bank continuously monitoring the cash flows of borrowers with the mean of 3.84 and SD .865 this study was agreed with (Tracy & Carrey 1998; Basel 1999) monitoring the flow of business of the borrower through the bank account; regular inspection of borrowers' financial reports and on-site visits by bank employees; Update of borrowers' credit files and regular review of borrower ratings at the time of borrowing.

The majority of the respondents agreed that the bank does follow-up to ensure that funds provided for the stated function are being used properly, with a mean of 4.09 and SD of 0.754. The study found that the bank would follow up the funds the borrowers used as a loan objective, some debtors' diversion of loans for other purposes, so the bank used effective monitoring and a follow-up system only used for its intended purpose. This study was agreed with (Seppala, 2000) credit monitoring refers to measures to; ensure that the bank understands the current financial condition of the borrower or counterparty; ensure that all credits are in compliance with existing agreements; follow the customer's use of approved credit lines; ensure that projected cash flows on major credits meet debt servicing requirements; ensure that where applicable, collateral provides adequate coverage relative.

The majority of respondents strongly agreed on the bank loan monitoring policy to increase bank profitability, with a mean of 4.45 and SD of 0.534. The bank has developed an effective loan monitoring policy to follow up, control, and repay debt on maturity date. This study was agreed with Makori (2015) the study concluded that credit monitoring, collection practices, and credit risk governance practices all have a positive impact on financial performance.

One of the KI said that *"The loan monitoring and follow-up were done in the following steps: first the branch followed their customers and communication with customers, second follow-up by loan departments, and third follow-up by the head office, and if there was no repayment, the last option was taken to court."* Based on the volume of loans permitted by four committees, committee A, led by the president, Committee B, vice president, committee C, loan department, and committee D, led by the district, up to 5000,0000, branches have no authority to provide loans to their customers" (KI general directorate of loan managers, private commercial bank).

One of the KI said that "types of policy and procedure to monitor and follow up loans were: visiting customers, advice during harsh times, site visiting at least once per year, continuous follow-up ,calling to customers, controlling loan diversion, and every loan officer's responsibility to follow up the borrowers." (KI general directorate of loan manager private commercial bank).

4.4.4. Loan collection policy and financial performance

Strict loan policies to be able to ensure high loan repayment address loan delinquency and minimize the fee of loan recovery of all superior loans. According to Morduch (1999) who noted that everyday repayment schedules can be characteristic as screening devices against undisciplined debtors and as an early caution to the program about capability repayment problems. Additionally, they stress borrowers to prioritize reimbursement earlier than cash is consumed or diverted.

Table 4.9. Loan collection policy and financial performance

Statements	N	Mean	Std. Deviation
The bank have formulated collection policy procedures and systems to secure repayment from customers	112	4.25	.637
Penalizing clients for late payment loan	112	4.38	.633
Strong loan collection campaign made to keep loan repayment timely	112	4.18	.674
Bank loan collection policies to improve the loan collection producers.	112	4.18	.604
Available collection policies have assisted towards effective loan collection.	112	4.18	.588
Regular reviews have been done on collection policies to improve state of loan collection	112	4.20	.551
The bank has strict and effective loan repayment policy	112	4.20	.613
Formulation of collection policies have been a challenge in loan management	112	3.87	.935
Bank collection of loan use both installment and lump sum methods	112	4.27	.553
loan collection policies to improve bank profitability	112	4.39	.491

As illustrated in table 4.9 above, the majority of respondents agreed that loan collection policies had an effect on the financial performance of selected private commercial banks in Ethiopia. The majority of respondents agreed that the bank has formulated collection policies, procedures, and systems to secure repayment debt from customers with a mean of 4.25 and SD of 0.637. This result was agreed with According to Kabiru (2002), an effective collection policy is important for managing consumer investments while also lowering the risk of loss of money and sluggish payment. The bank has developed an effective collection policy to collect principal and interest income from the customers according to the terms and conditions stated on the agreement.

The majority of respondents agreed that the banks penalized clients for late payment loans with a mean of 4.38 and SD 0.633, which passed their maturity date of payment. Most of the respondents agreed that the bank has a strong loan collection campaign made to keep loan repayment timely with the mean of 4.18 and SD of 0.674. The bank's method of collection used to collect debt from customers such as informing them about deadlines through telephone, by writing letters, by going to the premise, and through emails inform them about the last due date of debt. This result agrees with Masinde, et al (2012) who observed that companies in microfinance institutions have used arrears monitoring systems and strict policies as the most effective loan recovery tactics. This study discovered that the bank's current collection policy was effective in the repayment of loans from debtors. At most, many respondents agreed that the

bank should have regularly reviewed collection policies to improve the state of loan collection with a mean of 4.20 and SD of 0.551.

With a mean of 4.20 and SD of 0.613, the majority of respondents agreed that the bank has a strict and effective loan repayment policy. According to Moti, et al (2012), firms in the microfinance sector have adopted arrears monitoring systems and stringent loan collection policies as the most efficient loan collection methods. Some respondents agreed that the bank's formulated collection policies have been a challenge in loan management with a mean of 3.87 and SD of 0.935. This result indicated that formulation of collection policies is difficult if there are unexpected circumstances in the economic state that affect the business performance riskily. This affects loan collection. The majority of respondents agreed on bank collection policies using both installment and lump sum methods, with the mean of 4.27 and SD of 0.553. This found that the bank would be used to collect the principal and interest income from debtors using both methods.

With a mean of 4.39 and a standard deviation of 0.491, the majority of respondents agreed that loan collection policies were the most important function of the bank for improving profitability and reducing loss provisions for non-performing loans.

The data collected from key informants "the challenges of loan collection was classified into two. The first one was a project loan for this type of loan giving grace period because the business immediately generates no income. The project would be affected by hard currency, shortages of raw materials and finishing materials. In this condition, the extension of additional grace periods for the customers is necessary. The second type of loan was a working capital loan that was affected by customers' behaviors, economic slowdown, political instability, COVID-19, low market, insufficient income, and the nature of business; these affected the loan collection of the bank"

According to one of the KI "the major challenges you face in the loan collection procedure, the challenges of loan collection are categorized into two internal and external factors. Internal factors that arise from the customer's side are how they utilize funds, lack of management of funds, diversion of funds, ineffective and

inefficient uses of funds, and customer behavior. External collection challenges were out of the customer's control; these were export and import problems, political instability, environmental impacts, and a slowdown in the economy. The major reasons for the loan's non-repayment were the customer's character, poor credit analysis, the borrower's capability, being a new customer, and lack of follow-up on the loan” (KI general directorate of loan managers, private commercial bank)

4.4.5. Loan Default management policy and financial performance

Defaulting on payment is a serious offense and ought to be avoided at all cost. Most of the time defaulting on payments is temporary in nature because of client’s loss of jobs, a temporary extra expenditure that leaves no money to make the payment or prolonged illness which may additionally motivate the customer's financial distress or preserve him in the clinic for a few months. In very rare cases, humans default because of everlasting failure or the surprising dying of an individual who wasn’t insured or did not have sufficient assets left for his or her own family. Transient reasons can be controlled through close supervision and tracking and evaluating the projects financed through the mortgage. Proper schooling of loan applicant’s vital before loan disbursement. Debt recovery is the process of getting an outstanding loan and learning how to repay it by convincing the borrower to pay off the outstanding loan. Loan repayment is not an easy task because customers usually do not have access to lenders (banks). In most cases, the banking sector has debt collection departments that track loans and attempt to repay them before they become delinquent (Garber, 1997)

Table 4.10 Loan Default management policy and financial performance

Statements	N	Mean	Std. Deviation
The banks default management policy to taking legal actions against chronic defaulters of bank-loans.	112	4.29	.514
The bank default policy If the loan is unsecured the bank must request that the court liquidate the firm assets	112	4.00	.644
The default policy they enforce guarantee to provide chances for loan recovery in case of loan defaults	112	4.15	.506
The bank default policy has staff incentives that are effective in improving recovery of default loans.	112	2.26	1.063
loan Default policy examinee borrower's ability to pay loan	112	3.96	.621
The bank default policy does limits in loan amount to collateral value	112	3.91	.754
loan Default management policy hiring collection agency for loan default	112	2.31	.978
loan Default management policy write off for loan default	112	3.99	.637
Penalties upon loan default	112	4.33	.509
Bank loan default management policy increase bank profitability	112	4.33	.509

According to the above table, a majority of respondents agreed with the bank's default management policy to take legal action against chronic defaulters of bank-loans, with a mean of 4.29 and SD of 0.514. This showed that the bank, after evaluating the defaulter's non-repayment on the due date, takes legal action to collect the debt from the debtors. This study was agreed with Visaria (2009) notes that the collection agency is involved in today's task of ensuring that the loans made to bank customers are repaid in accordance with the contractual plan signed by the customer and the bank. The job of debt recovery is to compile and accumulate a list of all of unpaid loans and practically manage and organize the loans by following up on defaulting individuals. The debt collection unit interacts with lawyers to summarize warning letters to the borrowers and send the same letter to the defaulting customers.

The majority of respondents agreed with the bank default policy, requesting the court to liquidate the assets of the borrowers with a mean of 4.00 and SD of 0.644. This is the final option that the banks take to liquidate the assets of the firms that made the non-performing loans. This study, like Visaria (2009), confirms that court negotiation is beneficial in debt recovery by financial institutions and concurs with Swanson et al. (2008) ideally debt collection techniques have been used as a legitimate and necessary organizational activity where debt collectors and creditors can take reasonable steps and procedures to secure payments from companies or customers who are legally required to repay money they have paid or owed.

Most of the respondents agreed with the default policy of the bank's guarantee to provide chances for loan recovery in case of loan defaults, with a mean of 4.15 and SD.506, suggesting that the bank enforced the guarantee by having the debtors repay the debt before taking the case to court. This study was agreed with Kamau (2009) the study found that being a guarantor is a critical responsibility, and if the borrower fails to meet the bank's payment obligations under a loan agreement, the guarantor may be required to pay the debt, or the lender may be able to take possession and sell the property that the guarantor has pledged as security for the debt. A guarantor is a person who agrees to the borrower's payment terms and also agrees with Ogolla (2003) the study showed that guarantors are liable for loans guaranteed in accordance with the guarantee commitment. The percentage of debt that the guarantor must pay is the amount that the creditor does not receive from the debtor as a result of debt restructuring.

The majority of respondents did not agree with the bank's default policy as staff incentives are effective in improving the recovery of defaulted loans. With a mean of 2.26 and an SD of 1.063, the study found that the bank loan default policy did not use staff incentives as motivation for improving collection of debt. Most of the respondents agreed that the bank's default policy examined the borrower's ability to pay the loan with a mean of 3.96 and a SD of 0.621. This result indicated that banks assessed the defaulter's ability to repay debt, whether they assessed the debtor's ability to repay debt or not, and took other measures to collect the defaulted loan.

Most respondents agreed that the bank default policy does a limited loan amount to collateral value, with a mean of 3.91 and an SD of 0.754. This study agreed with Bester (2007) that when a bank has collateral as security, it aids in debt recovery and risk reduction. When a customer defaults on a loan agreement, the bank can foreclose or repossess to take possession of the stated

collateral. Collateral reduces the bank's loss and also agrees with Moti et al. (2012) that collateral attached as security and the signing of covenants perform an essential position in improving loan reimbursement.

The majority of respondents did not agree with the bank loan default management policy of hiring a collection agency for loans that defaulted, with a mean of 2.31 and SD.978. This indicated that the banks were not to hire a collection agency for defaulted loans. According to Njiru (2006) the study a bank may hire private collection companies to assist in the recovery of an outstanding obligation in early Private collection companies charge fees, which are taken from the total amount recovered. When it comes to resolving disagreements, negotiating payments, suspending or terminating collection efforts, and referring individuals to credit reference institutions, the creditor organization has the full decision.

Most respondents agreed on the bank loan default management policy write off for loans that are non-performing with a mean of 3.99 and 0.637. This found that the bank, if they know the borrowers do not have any resources or assets to cover their debt, the last option was to write off the amount of the loan that defaulted. This negatively affected the financial performance of the banks. This was agreed with Magalia (2013), who discovered that the loaners sometimes defaulted on their loans and this was attributed to the insufficient capabilities in loan portfolio management. This turned into loan defaults and negative portfolio management.

The majority of respondents agreed that the bank has penalties upon loan default, with a mean of 4.33 and SD of 0.509. Based on their terms and conditions stated in the agreement, the bank put a penalty on the loan that was defaulted on. This study agreed with the finding of Pandey (2004), who held that a credit score policy is needed due to the fact that sometimes clients do not pay the financial institution's installments on time, and consequently, guidelines should be installed to display compensation and that those policies need to be handy for the lender and the borrower. The majority of respondents agreed with the bank's loan default management policy to increase bank profitability, with a mean of 4.33 and SD of 0.509. This indicated that the bank effectively collected the non-performing loans from defaulters. This increased the profitability of the bank. This study agreed with the study that discovered that a well-managed loan returns the organization's equity and assets, which can generate financial performance (George et al, 2013) The key informants said that for defaulted loans, the bank's taking legal action was not the last

option. The bank would discuss with debtors the ways to get out of financial difficulties and give advice by giving many alternatives to starting the operation of the business and being capable of generating sufficient income to cover their operational costs and their expenses. According to the national bank directive's SBB/69/2018, NBE would classify that loan and hold provisions for each loan that shows a defaulted sign. Special mansions greater than 30 days with 5% hold provisions, substandard greater than 90 days with 20% hold provisions, doubtful greater than 180 days with 50% hold provisions and loss greater than 360 days with 100% hold provisions (NBE 2018).

The bank would then renegotiate with the debtors to reschedule the repayment terms when the borrowers were too overwhelmed to repay the loan on time. The bank also injected additional capital to encourage the business to resume normal operations, and the bank, after implementing many alternatives, discovered the last chance to liquidate the borrower's firm assets. If the bank was not satisfied with the sale of the debtors' assets, the bank had the right to ask for the uncovered loan again. The major reasons for loan defaults were character, management inefficiency, political, economic, technological, social, environmental, and legal. This study agreed with Asantey and Tengey's (2014) study that a borrowers educational background, years of experience in business, organization size, accessibility of other sources of income, kinds of goods, loan size, and household size are the primary factors of bad loans among small and medium enterprises, and the following are the pertinent elements boosting loan default: inadequate financial analysis, insufficient loan support, illiteracy and poor abilities, the absence of loan clients, improper business practices, and aggressive components were also highlighted in the study, with several institutions implicated. In the enterprise of lending, they ignore asking for adequate collateral and just have borrowers.

The procedures to follow to collect the defaulted loan were: plan A to collect as much as possible of the defaulted loan; plan B, sale of collateral; and if there is no collateral, write off the debt. The estimation of collateral value with the loan that was granted based on the types of loan, location of customers, the market condition, the types of business, the foreign currency exchange rate, and character of the borrower was considered the volume of loan that provided the collateral value of the borrower

One of the KI said that *"the loan officers of the bank, just like the security of the bank, play a vital role by studying the character of the customer and collecting reliable information on the borrower, by visiting the premise of the borrower, and by evaluating the legal documents before lending funds to the borrower."* (KI of the general directorate of loan managers).

One of the KI said that "The main reasons for loan defaults were loan diversion, owner death, political risk, transportation risk, low purchasing power of money, lack of knowledge about the business operated and lack of training and advice on how to efficiently use funds for intended function" (KI general directorate loan managers of private commercial bank).

This study was agreed with Wakuloba (2010), who investigated the factors that contribute to loan default in the African country's Trade Development Joint Loan Board (UGTDJLB) theme. The theme had high and rising default rates, which corresponded to the findings. Poor business performance, fund diversion, and domestic issues were the leading causes of default.

4.4.6. Financial performances of commercial banks

Financial performance is a measure of an organization's financial outcomes achieved via the utilization of human capital given rules and procedures and measured in measurable units. Corporations consider the results in terms of capital employed, return on property, and profitability margin. Profitability can be quantified using the return on assets (ROA) ratio. ROA is the earnings-to-total-assets ratio of a bank, and it measurements management's ability to make profits through the use of commercial enterprise assets at their disposal (Khrawish, 2011).

Table 4.11. Financial performances of commercial banks

Statements	N	Mean	Std. Deviation
Organizational loan policy leads to improved profitability	112	4.66	.476
Organizational loan policy leads improved organizational image	112	4.56	.498
Organizational loan policy leads to reduced loan defaulters	112	4.53	.502
Organizational loan policy leads to increase loan collection	112	4.54	.500
Organizational loan policy leads to improved loan monitoring and follow up enhance high returns from loan investments	112	4.56	.498
Organizational loan policy leads to improved quality loan lending capacity	112	4.55	.499

The findings in Table 4.10 show the effect of loan policy on the financial performance of selected private commercial banks in Ethiopia. Almost all the respondents strongly agreed that organizational loan policies lead to improved profitability of the banks, with a mean of 4.66 and SD of 0.76. This finding indicated that the banks have good loan policies to improve profitability. study was agrees with Mutua (2016) discovered a positive relationship between loan policy in risk mitigation and financial performance, as well as a strong positive relationship between credit monitoring and financial performance and also agreed with Mraba (2009) also found out that lending policies are employed to increase efficiency and coordination of asset investment operations thus better financial performance. Establish sound lending policies. The bank raises its earnings and Effective lending policies help the bank to improve its credit risk portfolio, and effective lending improves the bank's profitability. Good lending policies enable the bank to attract and maintain profitable clients, and good lending policies encourage the bank to attract more customers. Majority of respondents strongly agreed that organizational loan policy leads to improved organizational image, with the mean 4.56 andSD0.498.

Majority of respondents strongly agreed that organizational loan policy leads to reduced loan defaulters with mean 4.53and SD 0.502, this finding reveals that the loan policy used by the bank decreased loan defaulters and non-performing loans, this study was agreed Stella (2012) a study on loan collection policies in traders' SACCOs in Tanzania's Ilala municipality found that there was a need for effective supervision of borrowers to ensure that loan repayments were made on a

regular basis. The researcher emphasized that this would help reduce loan delinquency, which has an impact on financial performance, and that loan policies used by this sector have an impact on growth and financial performance.

The majority of respondents strongly agreed that organizational loan policies lead to increased loan collections, with a mean of 4.54 and SD of 0.500. This indicated that organizational loan policies increase debt collection from debtors and improve the profitability of the bank. The study was conducted in Ghanaian commercial banks. Dang (2011) discovered a positive relationship between loan policy and monetary performance. Majority of respondents strongly agreed that the loan policy of the banks led to improved organizational loan monitoring and follow up, with the mean 4.56 and SD 0.498. Majority of respondents were strongly agreed on loan policy of the banks were leads to improved organizational lending volume, with the mean 4.55 and SD.499

Data collected by interviews with key informants said that "the effect of loan policies was positive on the financial performance of private commercial banks. The loan policy that the bank would use was strict to decrease credit risk on the loan. The bank's majority of revenues come from interest income from landed loans. The loan policy of the bank would be evaluated by the internal auditors, external auditors, and NBE and risk department"

One of the KI said that "loans the major assets of the banks that affect the profitability of the bank." The interest income was the first source of income for the bank. Almost ninety percent of the income segment comes from the interest income for the bank. The first source of income comes from loans provided by international trade customers. The loan policies have strongly and positively driven the bank's financial performance" (General Directorate Loan Manager CBE)

4.5. Inferential Statistics

Inferential facts became carried out through correlation analysis which turned into used to set up, with statistical importance, the character of the prevailing relationship among the structured variable and the impartial variables. The have a look at additionally employed a multivariate

regression model to have a look at the determinants of loan policy and its effect on the financial performance of a private commercial bank. The established variable became the financial overall performance of the commercial banks in Ethiopia which measured the usage of loan policies such as loan term and condition policies, loan lending policies, loan monitoring policies, loan collection policies and loan default management policy.

4.5.1. Correlation between loan policy and financial performance

The correlation between loan term & condition policies, loan lending policies, loan monitoring policies, loan collection policies and loan default management policy and financial performance

Table 4.12. Correlation loan policy and financial performance

Loan policy	Financial performance	
Loan term and condition policy	Pearson Correlation	.336 ^{**}
	Sig. (2-tailed)	.000
	N	112
loan lending policy	Pearson Correlation	.431 ^{**}
	Sig. (2-tailed)	.000
	N	112
loan monitoring policy	Pearson Correlation	.401 ^{**}
	Sig. (2-tailed)	.000
	N	112
loan collection policy	Pearson Correlation	.298 ^{**}
	Sig. (2-tailed)	.001
	N	112
loan default management policy	Pearson Correlation	.337 ^{**}
	Sig. (2-tailed)	.000
	N	112
Financial performance	Pearson Correlation	1
	Sig. (2-tailed)	
	N	112

** . Correlation is significant at the 0.01 level (2-tailed).

Table 4.12 shows the relationships between loan terms and conditions policy and the financial performance of a selected private bank in Ethiopia, where the respondent N 112 had a significant level of 0.01. The results showed that the bank's loan terms and condition policy had a moderate positive correlation with the financial performance of a private commercial bank ($r = .336$ $P = .000$), which was less than the significant level of 0.05. When the p-value is less than 0.05, the null hypothesis is rejected and the alternative hypothesis is used (Saunders, 2003). This

demonstrates that there is a relationship between loan terms and conditions policy and the financial performance of Ethiopia's private commercial banks. The objective was to determine the effect of loan terms and conditions policies on financial performance. This shows that the bank's loan terms and conditions lead to the positive financial performance of private commercial banks.

Table 4.12 shows the relationships between lending policies and financial performance of selected private banks in Ethiopia with the respondent N 112 at a significant level of 0.01. The results showed that the bank's lending policies had a moderate positive correlation with the financial performance of private commercial banks at a correlation of $r = .431$ ($P = 000$), which was less than the significant level of 0.05. It is possible to conclude that variables are correlated when the p-value is less than 0.05. The null hypothesis was rejected and the alternative hypothesis was accepted. This suggests that there was a high correlation between lending policies and the financial performance of Ethiopia's private commercial banks. This means that loan lending practices used by private commercial banks in Ethiopia contribute to improved financial performance.

The relationships between loan monitoring policies and the financial performance of selected private banks in Ethiopia are shown in table 4.12, where the respondent N 112 is at a significant level of 0.01. The analysis indicated that the bank's loan monitoring policies had a significant positive correlation with the financial performance of private commercial banks at a correlation level of $r = .401$ ($P = 000$), which was less than the significant level of 0.05. When the p-value is less than 0.05, the null hypothesis was rejected and the alternative hypothesis was accepted. the variables are said to be correlated. This suggests that loan monitoring practices and the financial performance of private commercial banks in Ethiopia are correlated. This demonstrates that banks' loan monitoring policies contribute to private commercial banks' positive financial performance.

The relationships between Loan collection policies and financial performance of selected private commercial banks in Ethiopia were presented in table 4.12, with the respondent N 112 having a significant level of 0.01. The results showed that the bank's Loan collection policies had a moderate positive relationship to financial performance of private commercial banks at correlation($r=.298$ $P=000$), which was less than the significant level of 0.05. When the p-value is

less than 0.05, the null hypothesis was rejected and the alternative hypothesis was accepted. the variables are said to be correlated. This suggests that there is a relationship between loan collection policies and the financial performance of private commercial banks in Ethiopia. This suggests that bank loan collection policies contribute to the positive financial performance of commercial banks.

Table 4.12 provided the relationships between loan default management policies and financial performance of a selected private bank in Ethiopia whereby the respondent N 112 at a significant level of 0.01, the results indicated that the loan default management policies practiced by the bank had a moderate positive correlation with the financial performance of a private commercial bank in Ethiopia at a correlation ($r = .307$, $P = 000$), which was less than the significant level of 0.05. When the p-value is less than the significant level of 0.05, the null hypothesis was rejected and the alternative hypothesis was accepted. It can be concluded that variables are correlated. This indicates that there is a significant association between loan default management policies and the financial performance of private-select commercial banks in Ethiopia. This implies a positive correlation between loan default management policies and the financial performance of private-selected commercial banks.

4.5.2. Regression analysis

A multiple regression analysis model was used to investigate the variables of lending policy and their impact on the financial performance of a private commercial bank.

4.5.2.1. Test of linearity assumption

The linear regression analysis tests the relationship between the independent variables (loan policies) and dependent variables (financial performance) and if the relationships are linear in nature.

Table 4. 13. Test of linearity assumption

Correlations							
		Loan term and condition policy	loan lending policy	loan monitoring policy	loan collection policy	loan default management policy	financial performance
Loan term and condition policy	Pearson Correlation	1					
	Sig. (2-tailed)						
	N	112					
loan lending policy	Pearson Correlation	.472**	1				
	Sig. (2-tailed)	.000					
	N	112	112				
loan monitoring policy	Pearson Correlation	.538**	.608**	1			
	Sig. (2-tailed)	.000	.000				
	N	112	112	112			
loan collection policy	Pearson Correlation	.370**	.476**	.534**	1		
	Sig. (2-tailed)	.000	.000	.000			
	N	112	112	112	112		
loan default management policy	Pearson Correlation	.336**	.497**	.424**	.541**	1	
	Sig. (2-tailed)	.000	.000	.000	.000		
	N	112	112	112	112	112	
Financial performance	Pearson Correlation	.336**	.431**	.401**	.298**	.337**	1
	Sig. (2-tailed)	.000	.000	.000	.001	.000	
	N	112	112	112	112	112	112

** . Correlation is significant at the 0.01 level (2-tailed).

4.5.2.2. Test of Homoscedasticity assumption

The assumption of homoscedasticity is that the dependent variable has the same level of variation across all predictor variables. These are some of the requirements for multiple regressions are homoscedasticity. To evaluate the concept of homoscedasticity, the study used the Durbin-Watson statistic, which should be between 1.5 and 2.5. Table 4.17 shows that the Durbin-Watson statistic is 1.973, which is between 1.5 and 2.5, showing that the data is not auto correlated, as seen in Table 4.17.

Table 4.14. Test of Homoscedasticity assumption

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.486 ^a	.236	.200	.37081	1.973

a. Predictors: (Constant), loan default management policy, Loan term and condition policy, loan collection policy, loan lending policy, loan monitoring policy

b. Dependent Variable: overall financial performance

4.5.2.3 Test of Normality assumption

One of the requirements for multiple regressions is normality. Skewness and kurtosis were utilized to test data normality in this research. Kurtosis is used to explain how flat or peaked the distribution of data is, while Skewness is used to characterize how symmetrical the distribution of the data. Skewness and kurtosis should be between -1.96 and 1.98(Hair et al, 2010). All variables are listed in Table 4.15, along with their skewness and kurtosis values. The fact that the majority of the variables were between -1.96 and 1.98 showed that the distribution is normal.

Table 4. 15. Skewness and Kurtosis Scores

	N	Mean	Skewness		Kurtosis	
	Statistic	Statistic	Statistic	Std. Error	Statistic	Std. Error
Loan term and condition policy	112	4.1107	.015	.228	.166	.453
loan lending policy	112	4.2946	.194	.228	-.508	.453
loan monitoring policy	112	4.2804	.039	.228	-.405	.453
loan collection policy	112	4.2089	.550	.228	-.290	.453
Loan default management policy	112	3.7536	1.139	.228	1.519	.453
Financial performance	112	4.5685	-.278	.228	-1.601	.453
Valid N (listwise)	112					

4.5.3. Regression analysis between loan policies and financial performance

The regression analysis tests between the independent variables (loan policies) and dependent variables (financial performance) and if the relationships are linear in nature.

Table 4. 16. Regressions between loan terms & condition policies on financial performance

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.336 ^a	.113	.105	.39238

a. Predictors: (Constant), Loan term and condition policy

b. Financial performance

As shown in the regression model of this study, R^2 , the coefficient of determination, which tells us the variation in the dependent variables of the study due to changes in the independent variables, was 0.113, implying that there was a variation of 11.3 percent in the financial performance of selected private commercial banks due to changes in loan terms and condition policy practice by banks, This represented a shift of 11.3 percent in the financial performance of Ethiopia's private commercial banks. Because loan terms and conditions are the correlation coefficient that reveals the relationship between the dependent variables, the study found a moderately positive relationship between loan terms and conditions policy and the financial performance of selected private commercial banks.

Table 4.17. ANOVA of loan terms and condition on financial performance

ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2.151	1	2.151	13.969	.000 ^b
	Residual	16.936	110	.154		
	Total	19.086	111			

a. Dependent Variable: financial performance

b. Predictors: (Constant), Loan term and condition policy

Table 4.17 illustrates the Analysis of Variance (ANOVA) which assesses the overall significance of the model. According to the table $p < 0.05$, (0.000), indicating that there was sufficient evidence that the model is useful in explaining the financial performance of commercial banks in Ethiopia.

Table 4. 18.Coefficient of loan terms and condition on financial performance

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	2.807	.473		5.935	.000
1 Loan term and condition policy	.429	.115	.336	3.738	.000

a. Dependent Variable: financial performance

The equation $Y = 2.807 + .429X_1$ was derived from the table above. With a p value less than 0.05, it was discovered that loan terms and condition policies are statistically significant in influencing the financial performance of selected private commercial banks in Ethiopia. The study discovered that a unit increase in loan terms and conditions leads to a 0.429 factor increase in the financial performance of selected private commercial banks.

Table 4. 19 Model summary loan lending policies on financial performance

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.431 ^a	.186	.179	.37581

a. Predictors: (Constant), loan lending policy

This study's model conclusion according to the data in Table 4.19, the R squared coefficient of determination was 0.186, implying that there was an 18.6 percent variation in the financial performance of selected private commercial banks due to variations in loan lending policies adopted by the banks. The financial performance of Ethiopia's private commercial banks improved by 18.6 .The correlation coefficient indicates the relationship between the dependent variables and the loan lending policies, and it is used to represent the loan lending policy. As a

result, the study found a moderately positive relationship between selected private commercial banks' loan lending policies and financial performance.

Table 4.20. ANOVA of lending policies on financial performance

ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	3.551	1	3.551	25.144	.000 ^b
	Residual	15.535	110	.141		
	Total	19.086	111			

a. Dependent Variable: financial performance

b. Predictors: (Constant), loan lending policy

The Analysis of Variance (ANOVA) is shown in Table 4.20, and it is used to determine the model's overall significance. According to table p 0.05, (0.000), there is significant evidence that the model is effective in describing the financial performance of Ethiopian commercial banks.

Table 4.21. Coefficient of loan lending policies on financial performance

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.306	.453		5.096	.000
	loan lending policy	.527	.105	.431	5.014	.000

a. Dependent Variable: financial performance

From the above table, we established the equation $Y = 2.306 + .527X_2$. From the above regression equation, it was discovered that loan lending policies are statistically significant in influencing the financial performance of selected private commercial banks in Ethiopia with a p value less than 0.05. The study found that a unit increase in loan lending policies would lead to an increase in the financial performance of selected private commercial banks by **0.527** factors.

Table 4.22 Model summary loan monitoring policies on financial performance

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.401 ^a	.161	.153	.38157

a. Predictors: (Constant), loan monitoring policy

The value of R squared in the above table was 0.161, indicating that there was a 16.1% variation in the financial performance of selected private commercial banks due to changes in loan monitoring policies and practices by each bank. This indicated a 16.1% change in the financial performance of selected private commercial banks in Ethiopia. Loan monitoring policies are the correlation coefficients, which show the relationship between the dependent variables and the dependent ones. Therefore, the study indicated that there was a moderate positive relationship between loan lending policies and the financial performance of selected private commercial banks in Ethiopia.

Table 4. 23.ANOVA of loan monitoring policies on financial performance

ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	3.071	1	3.071	21.090	.000 ^b
	Residual	16.016	110	.146		
	Total	19.086	111			

a. Dependent Variable: OFP

b. Predictors: (Constant), loan monitoring policy

Table 4.23 illustrates the Analysis of Variance (ANOVA), which assesses the overall significance of the model. According to the table, p 0.05, (0.000), indicating that there was sufficient evidence that the model is useful in explaining the financial performance of commercial banks in Ethiopia,

Table 4. 24.Coefficient of loan monitoring policies on financial performance

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.772	.393		7.058	.000
	loan monitoring policy	.420	.091	.401	4.592	.000

a. Dependent Variable: financial performance

From the above table, we established the equation $Y = 2.772 + .42X$ From the above regression equation, it was discovered that loan lending policies are statistically significant in influencing the financial performance of selected private commercial banks in Ethiopia with a p value less

than 0.05. The study found that a unit increase in loan monitoring policies would lead to an increase in the financial performance of selected private commercial banks by **0.42** factors.

Table 4.25. Model summary of loan collection policies on financial performance

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.298 ^a	.089	.080	.39767

a. Predictors: (Constant), loan collection policy

Table 4.25 showed that the coefficient of determination for this study was R squared, which tells us the variation in the dependent variables of the study due to changes in the independent variables. Based on the findings in the above table, the value of R squared was 0.089, indicating that there was an 8.9% variation in financial performance of selected private commercial banks due to changes in loan collection policies practiced by banks. This suggested that selected private commercial banks in Ethiopia showed 8.9% changes in financial performance. The correlation coefficient, which indicates the relationship between the dependent variables, was used as a loan collection policy; as a result, the study indicated that there was a moderate positive relationship between loan collection policies and financial performance of selected private commercial banks in Ethiopia.

Table 4. 26. ANOVA of loan collection policies on financial performance

ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.690	1	1.690	10.689	.001 ^b
	Residual	17.396	110	.158		
	Total	19.086	111			

a. Dependent Variable: financial performance

b. Predictors: (Constant), loan collection policy

Table 4.26 illustrates the Analysis of Variance (ANOVA) which assesses the overall significance of the model. According to the table $p < 0.05$, (0.000), indicating that there was sufficient evidence that the model is useful in explaining the financial performance of commercial banks in Ethiopia

Table 4. 27. Coefficient of loan collection policies on financial performance

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	3.208	.418		7.682	.000
1 loan collection policy	.323	.099	.298	3.269	.001

a. Dependent Variable: financial performance

From the above table, we established the equation $Y = 3.208 + .323X$ From the above regression equation, it was discovered that loan collection policies are statistically significant in influencing the financial performance of selected private commercial banks in Ethiopia with a p value less than 0.05. The study found that a unit increase in loan collection policies would lead to an increase in the financial performance of selected private commercial banks by **0.323**.

Table 4.28. Model summary of loan default management policies and financial performance

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.337 ^a	.113	.105	.39224

a. Predictors: (Constant), loan default management policy

The value of R squared was 0.113 based on the findings in the preceding table, indicating that there was a variation of 11.3% in the financial performance of selected private commercial banks due to changes in loan default management policies and practices by each bank. This indicated an 11.3% change in the financial performance of selected private commercial banks in Ethiopia. Loan default management policies are the correlation coefficients that show the relationship between the dependent variables; thus, the study found a moderately positive correlation between loan default management policies and the financial performance of selected private commercial banks in Ethiopia.

Table 4.29. ANOVA of loan default management policies on financial performance

ANOVA^a

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	2.163	1	2.163	14.056	.000 ^b
Residual	16.924	110	.154		
Total	19.086	111			

a. Dependent Variable: financial performance

b. Predictors: (Constant), loan default management policy

Table 4.29 illustrates the Analysis of Variance (ANOVA) which assesses the overall significance of the model. According to the table $p < 0.05$, (0.000), indicating that there was sufficient evidence that the model is useful in explaining the financial performance of commercial banks in Ethiopia.

Table 4.30. Coefficient of loan default management policies on financial performance

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	3.039	.410		7.416	.000
loan default management policy	.408	.109	.337	3.749	.000

a. Dependent Variable: OFP

From the above table, we established the equation $Y = 3.0398 + .408X_5$. From the above regression equation it was discovered that loan default management policies is statistically significant in influencing financial performance of selected private commercial banks in Ethiopia with a p value less than 0.05, the study found that a unit increase in loan default management policies would be leads to increase the financial performance selected private commercial bank by 0.408 factors.

4.5.3.1 Overall Regression Analysis

The multivariate regression model is used to determine the effect of loan policies and financial performance of selected private banks in Ethiopia and also to measure the relationship between independent and dependent variables that are loan terms and conditions, loan lending policies, loan monitoring policies, loan collection policies, and loan default management policies.

Table 4.31. Model Summary of the loan policy and financial performance

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.486 ^a	.236	.200	.37081

Predictors are (constant), loan terms and conditions, Loan lending policies, loan monitoring policies, loan collection policies and loan default management policies

Table 4.7 illustrates this model summary in the study, R squared coefficients of determination, which tells us about the version in the dependent variable due to changes in the independent variable, from the findings in the above and condition: loan lending policies, loan monitoring policies, loan collection policies, and loan default management policies.

This shows that 23.6% of the changes in financial performance of commercial banks and selected banks in Ethiopia could be accounted for by independent variables (loan policies), while the remaining 76.4% of the financial performance is explained by factors outside the model. R squared was the correlation coefficient, which shows the relationship between the study variables. From the findings shown in the table above, it is evident that there was a moderate positive relationship between independent variables and dependent variables.

Table 4.32 ANOVA summary of the loan policy and financial performance

ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4.511	5	.902	6.561	.000 ^b
	Residual	14.575	106	.138		
	Total	19.086	111			

a. Dependent Variable: financial performance

b. Predictors: (Constant), loan default management policy, Loan term and condition policy, loan collection policy, loan lending policy, loan monitoring policy

Table 4.32 illustrates the Analysis of Variance (ANOVA) which assesses the overall significance of the model. According to the table $p < 0.05$, (0.000), indicating that the regression model was useful in explaining the financial performance of commercial banks in selected private commercial banks in Ethiopia.

Table 4. 33 Summary coefficients of the loan policy and financial performance

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	1.577	.552		2.855	.05
1 Loan term and condition policy	.132	.132	.104	1.001	.049
loan lending policy	.277	.141	.227	1.956	.050
loan monitoring policy	.161	.126	.154	1.278	.044
loan collection policy	.003	.120	.003	.027	.052
loan default management policy	.148	.129	.122	1.144	.055

From the data in the above table the established regression equation was

$$Y = 1.577 + .132x_1 + .277x_2 + .161x_3 + .003x_4 + .148x_5$$

The regression weights of all the independent variables were significant with loan terms and condition policies $p=0.049$, loan lending policies $p=0.50$, loan monitoring policies $p=0.044$, loan collection policies $p=0.052$, and loan default management policies $p=0.055$, according to the above regression equation. All variables, including loan terms and conditions, loan lending policies, loan monitoring strategies, loan collection policies, and loan default management policies, are predictors of financial performance of private Ethiopian commercial banks.

The unstandardized coefficients indicate the corresponding change in the dependent variable when a change of one unit is affected in the independent variable. One unit changes in loan term and condition policy, it leads to change in financial performance of selected private commercial bank by .132 unit, one unit changes in loan lending policies lead to 0.277 unit changes in financial performance of selected private commercial bank in Ethiopia. A unit change in loan monitoring policies, leads to 0.161 unit changes in financial performance of selected private commercial banks in Ethiopia. Also, one unit change in loan collection policies leads to .003 unit changes in financial performance of selected commercial banks and one unit change in loan default

management policies leads to .148 unit changes in financial performance of selected private commercial banks in Ethiopia.

4.6. The relationships between loan policies and return on asset

4.6.1. Loan policies and financial performance (ROA)

To support our primary data, the researcher gathered secondary data to demonstrate the relationships between loan policies and return on assets in order to improve the study's quality. Independent variables were loan terms and conditions, loan lending policies, loan monitoring, loan collection policies, and loan default management policies, and the dependent variable was the financial performance of selected private commercial banks.

4.6.2. Return on asset

The study required to establish the returns on assets of the selected private commercial bank over the five years from 2016-2020 periods by taking financial statements of six private banks which was measured by net income per total assets. The results were presented in table 4.33.

Table 4. 34. Return on asset (ROA)

Descriptive Statistics

Years	N	Minimum	Maximum	Mean	Std. Deviation
2016	5	.00	.03	.0201	.01165
2017	5	.01	.03	.0221	.00762
2018	5	.02	.03	.0260	.00554
2019	5	.02	.04	.0244	.00780
2020	5	.02	.03	.0262	.00479
Valid N (listwise)	5				

The mean value of the highest ROA was in year 2020, followed by year 2018, 2019 and 2017 and the least ROA was 2016

4.6.3. Relationships between loan policies and (ROA)

The study to found the relationships loan policies and financial performance (net income) this to indicate that the relationships between loan policies and quantities aspects of financial statements

by taking return on asset for five years periods better result to establish the correlation between the loan policies and financial performance of the bank. To revealed that good and positive correlation between the independent variable that are loan terms and condition policies; loan lending policies, loan monitoring, loan collection policies and loan default management policies and dependent variable is financial performance of selected private commercial bank by analyzed the coefficient correlation between them.

Table. 4.35 correlation coefficient between loan policy and return on asset

Loan policies	Financial performance (ROA)	
loan terms and condition policies	r1	0.624
loan lending policies	r2	.904
loan monitoring policies	r3	.461
loan collection policies	r4	.159
loan default management policies	r5	..318

In the above data, there was a strong correlation between loan policies and the financial performance of private-selected commercial banks in Ethiopia. There is a strong positive correlation between loan terms and condition policies and financial performance ($r = .0624$), whereas there is a strong positive correlation between loan lending policies and financial performance (.904). There is a moderate positive correlation between loan monitoring policies and financial performance (.461) and also, again, there are weak positive relationships between loan collection policies and financial performance (.159). There is a moderate positive correlation between loan default management policies and financial performance (.318) of selected private commercial banks in Ethiopia. This study agreed with Wei (2007), stating collection policies are a very important part of the general credit risk management method among commercial banks. A good collection of policies is essential in dominating the investments of debtors and additionally reducing the dangers of monetary loss and ill liquidity through slow payment. This study was agreed upon in line with Mwaura and Jagongo (2017), who showed that credit policy positively affects the performance of commercial banks. Similar results were obtained by Nyawera (2013), who revealed a positive and significant relationship between credit policies and deposit-taking microfinance organizations' financial profitability. The study further agreed with the findings of Pandey (2004), holding that credit policies are needed because sometimes customers do not pay the bank's installments on time and, therefore,

policies should be put in place to monitor repayment and that these policies should be convenient for both the lender and the borrower.

There were positive relationships between loan policies and the bank's return on assets after analyzing primary data on loan policies and financial performance as well as secondary data from the financial statements of selected private commercial banks. So the study revealed that loan policies practiced by the bank greatly affect the profitability of the selected private bank in Ethiopia.

Table 4.36 Summary of hypothesis testing

Hypothesis	result	effect of test
H01: There is no significant relationship between loan terms and condition policy and financial performance	P=0.000	H01=Rejected
H02: There is no significant relationship between lending policies and financial performance	P=0.000	H02=Rejected
H03: There is no significant relationship between loan monitoring policies and financial performance	P=0.000	H03=Rejected
H04: There is no significant relationship between loan collection policies and financial performance	P=0.000	H04=Rejected
H05: There is no significant relationship between default management policies and financial performance	P=0.000	H05=Rejected

CHAPTER FIVE

SUMMARY OF FINDING CONCLUSION AND RECOMMENDATION

5.1. Introduction

This chapter provides a summary of the study's findings and conclusions based on the results and analysis of research data and findings in literature reviews. Recommendations and limitations that were met, as well as additional area research, are provided. The study provides a summary of the research findings derived from an analysis of primary and secondary data on the impact of loan policies on the financial performance of selected private commercial banks in Ethiopia. A discussion of the results is completed, and recommendations are made to several stakeholders. As a result, the chapter is based on a summary of research findings' conclusions and recommendations.

5.2. Summary of findings

The objectives of the study were the loan policies and its effect on the financial performance of private commercial banks in Ethiopia.

5.2.1. Loan terms and condition policies and its effect on financial performance

The study results indicate that almost all respondents agreed that the bank has a well-developed written loan policy. According to a study by Kantor and Martal (2001), banks that operate without a written credit policy may lack a standard way of administering credit to customers, which may adversely affect their ability to compete with other players in the market. All banks have frequently reviewed their loan policies. The bank would revise their loan policies every two to five years and also revise them when unexpected circumstances happen in the banking industry or in the general economic environment and force the policies that are reviewed regularly.

The study found that banks generally charged interest rates on loans at market rates and adjusted the interest rates on the loans without referring to the customer. When the bank charged interest on loans, it took into account the risk in the industry, such as economic conditions, general inflation, and national bank directives. The bank also discussed repayment schedules with customers, negotiated loan terms with clients, discussed the method of payment, the duration of the loan, and took into account any economic conditions during lending.

Study found that bank loan terms and conditions policies influence the volume of loans obtained from the bank as well as the loan seekers. During the loan processing phase, the banks strictly enforced the borrower to fulfill the terms and conditions of the loan, such as: preliminary interview of the customers, types of business engaged, assessing the activities of the customers, advising the customers, the purpose of the loan, If the project loan request bill of quantity is to request a business plan proposal, an environmental impact assessment of the project, a market assessment, a financial plan, and a feasibility study of the project, Loan terms and condition policy have a positive correlation with the financial performance of Ethiopian private commercial banks. The R^2 coefficient of determination of loan terms and condition policy was 0.113, which implying that a shift of 11.3 percent in the financial performance of CBEs. Loan terms and condition policies has a positive correlation of 0.336 with financial performance of CBEs and a significant regression coefficient of .132.

5.2.2. Loan lending policy and its effects on the financial performance

The study found that the lending policies of the banks were developed, adequate, and effective in guiding their loans. The lending policies of the banks increased loan repayment by assessing the ability, behaviors, and capability of the borrower before disbursement of the loan to the debtors. The banks' stringent loan policies minimized the cost of collection, bad debt expense, and unnecessary legal costs. This agrees with Pandey's (2001) finding that lending is a risky venture. The research found that having adequate and effective credit appraisal, monitoring, and loan recovery.

The study showed the banks' lending policies have technical, lawyer, and loan officer departments that jointly estimate the fair value of the collateral of the borrower and also evaluate the pre-feasibility study of the business of the customers. The banks' lending policies require the following information before lending: to prove the legal document or article of association (PLC), legal license of the business, length or duration of loan, tax identification number clearance, checking customers in the defaulter list on NBE servers, experience, reputation of the borrower, customer history, asking for current audited financial statements less than three months old, and also checking the qualified auditors According to Laile (2015), borrower dependency, loan size, borrowers' perception of repayment period, supply of earnings, availability of training, business experience, commercial enterprise type, own family size, and

purpose of saving have all been found to be influential in determining loan reimbursement. The study also showed that the banks' lending policies have a board of directors' delegation of the management of lending responsibilities to specialized committees for implementing the lending activity. These are three subdivision committees: credit and portfolio department, vice president committee, and president office committee to approve the loan request.

The banks developed their lending policy under the umbrella of national bank Ethiopia, this lined up with the laws and regulations of the monetary authorities in the country. The study also showed that lending policy of the bank was affected by many factors such as, pandemic disease, import and export condition, hard currency, political instability and the market condition. In such factors, the bank revised their lending policy by negotiating with customers. In addition, the lending policy of the banks where large volumes of loans were provided for import and export trade, manufacturing, industry, agro food processing and the least loan was provided for the agriculture sector because of the high risk of the area sector. Most Ethiopian banking industry collateral based loans without collateral was very rare. The study summarized that lending was the major activities of the banks and the utmost source of revenue that was collected from interest income; bank used efficient types of lending required loan evaluation, loan approval, and loan distribution. Lending policy has a positive correlation with the financial performance of private commercial banks in Ethiopia. The R^2 coefficient of determination of loan lending policy was 0.186, which implying that a shift of 18.6 percent in the financial performance of CBEs. Loan lending policies has a positive correlation of 0.431 with financial performance of CBEs and a significant regression coefficient of 0.277.

5.2.3. Loan monitoring policy and its effect on the financial performance

The study established that commercial banks have adequate and effective monitoring policies that help evaluate customers before advancing loans, monitor repayments, and recover non-performing loans. This finding also revealed that good loan monitoring policies increase loan repayment rates, as well as minimizes the cost of collection, bad debts, and unnecessary legal costs, as well as ensures timely allocation of resources. This finding also showed that the bank monitors the progress of customers, such as: activity of the business, collateral pledged, applicant's financial health, profitability, follows the customers' do not diversion of funds in other activities, at least once a year, visiting the site of the borrower, and Verifies that finances

provided for a certain objective are being used effectively. The banks have also forced the customers to repay their debt at agreed periods or on the maturity date of the debt.

The bank's monitoring policies were restructuring loan repayment terms for borrowers based on the following criteria: if the borrower was unable to generate sufficient cash due to an economic slowdown, political instability, or pandemic disease such as Covid-19, put penalties on outstanding debt balances to reactivate the debtors. In addition, the banks periodically prepared loan grading reports for signaling loan losses in any portfolio. This finding also meant the banks were to advise the debtors on ways of enduring or preventing the loss that affected the business of the debtor and continuously track the cash flows of the borrower. The finding summarized that the banks developed an effective loan monitoring policy that follows up, controls, and repays debt from customers on their due date. The R^2 coefficient of determination of loan monitoring policy was 0.161, which implying that a shift of 16.1 percent in the financial performance of CBEs Monitoring policies has a positive correlation with the financial performance of private commercial banks in Ethiopia. Loan monitoring policies has a positive correlation of 0.401 with financial performance of CBEs and a significant regression coefficient of 0.161.

5.2.4. Loan collection policies and its effect on financial performance

The finding indicated that the selected private commercial banks have well-formulated and effective collection policies to collect principal and interest income from the customers according to the repayment terms, and the finding also showed that penalizing clients for late payment of the debt is not an option. The banks used strong loan collection methods to keep loan repayments in a timely manner and informed about deadlines through the telephone, writing letters, going to the premises and through emails.

The study also found that the banks periodically review their collection policies based on the economic condition, political condition, and the performance of the business of the debtor. Furthermore, the findings revealed that the formulation of collection policies in the loan management system was difficult due to unforeseen circumstances that occurred in the economic condition that adversely affected the business performance, customers' behaviors, inflation rate, and shortage of foreign currency or hard currency, loss incurred in business operation, and so on.

The study further revealed that banks' collection policies used both installment and lump-sum methods to collect the principal and interest income from debtors.

The study furthermore established that challenges of loan collection categorized into internal and external factors. Internal factors that arise from the customer's side were lack of management of funds, new customer, poor credit analysis, capability of the borrower, diversion of loan, lack of follow up, and customer behavior. External collection challenges were export and import problems, political instability, and environmental impacts and slow down of the economy.

The study moreover showed that the strong collection policy increased profitability and decreased loss provisions for non-performing loans of banks. The study summarized that the banks' Loan collection policies has a positive correlation with financial performance of private commercial bank in Ethiopia. The R^2 coefficient of determination of loan collection policy was 0.089, which implying that a shift of 8.8 percent in the financial performance of CBEs. Loan collection policies have a positive correlation of 0.298 with financial performance of CBEs and a significant regression coefficient of 0.003.

5.2.5. Default management policy and its effect in financial performance

The study showed that the main causes of loan defaults were loan diversion, owner death, political risk, transportation risk, low purchasing power of money, lack of knowledge about the business operated, and lack of training on how to manage finance. The study also revealed that the bank's default management policies, such as taking legal action against chronic defaulters, were not the last option for liquidating the borrowers' assets; instead, the banks discussed alternative methods of debt repayment with their customers first. If the problem was finance, they could inject other funds to activate the business and also provide some advice on the way out of from financial difficulties.

The study showed that the bank after evaluating the loan default was categorized according to national bank directives: NO SBB/69/2018: pass 30 days, special mention 90 days, substandard 180 days, doubtful and loss 360 days based on the maturity date. The bank loan default policy enforces the guarantee of debtors' repaying the debt within specified dates. The study found that the bank's default management policy did not use staff incentives for effective default loan recovery.

The study also discovered that the bank did not use a collection agency for defaulted loans, so the bank itself collects defaulted loans that do not repay within the maturity date. It was found that the last option was to write off the amount of the loan that defaulted, but this is not the last option. If the borrower defaults on any property in the future, the bank has the right to ask for their asset again. In addition, the bank put a penalty on the defaulted loan. This finding further showed that bank loan default management policies improve the financial performance of the bank through effectively and efficiently managing the defaulters' ability to repay their debt within short periods.

The impact of loan policy on the financial performance of selected Ethiopian private commercial banks. The study found that the loan policies that were practiced by banks improved the profitability and financial performance of private-sector commercial banks. Organizational loan policies have increased the profitability of the banks, and organizational loan policies lead to fewer loan defaulters by using effective loan default management policies. Loan collection policies practiced by the banks increase the profitability of the banks. Organizational loan monitoring and follow-up policies increased the loan recovery from the customers on the due date, and organizational lending policies increased the financial performance of the selected private commercial bank. The study concluded that the banks' default management policies have a positive correlation with financial performance and improved profitability of private commercial banks in Ethiopia. The R^2 coefficient of determination of loan default management policy was 0.113, which implying that a shift of 11.3 percent in the financial performance of CBEs. Loan default management policies have a positive correlation of 0.337 with financial performance of CBEs and a significant regression coefficient of 0.148.

5.2.6. Financial performance of private commercial bank

According to the study's findings, loan policies improved profitability or return on assets, loan terms and conditions improved organizational image, boosted borrowers' follow-up and monitoring, improved loan repayment, and reduced loan defaulters. This means that commercial bank lending policies are a vital component of performance since they help banks reduce the risk of monetary loss and illiquidity, which leads to better results. Interest income was the first source of revenue for the bank which improves profitability of the bank so loan policies were strong positive relationships with financial performance of the bank

5.3 Conclusions

The study found that the impact loan policy on financial performance private commercial banks in Ethiopia. From the study findings it can be concluded that banks have well-developed loan terms and condition policy in which guiding their customers, negotiated with customers, revised regularly their loan policies, charge interest rate based on market conditions, discussed the repayment periods, attract loan seekers, improved banks image and improved profitability the bank's. Lending policies that used by the bank was the stringent loan policies which minimize the cost of collection, bad debt expense, and unnecessary legal costs. The findings also showed the banks' lending policies used 5C credit analysis policy to evaluated customer ability to borrowed loan. The banks' lending policy was powerfully evaluated, approved, and distributed loan to the customers. Therefore, the lending policies of the banks improved profitability of the bank.

Loan monitoring policies of the banks were follow up the customers, evaluate the customer's asymmetric information provided during borrowing, follow the customers not diversion of funds for other activities and supervise the borrower at least twice per year and restructured loan repayment terms during unforeseen circumstances and improved loan repayment. The banks were formulated loan collection policies that increased the repayment of debt on the maturity date, banks with good collection policies and strong credit period policies would improve their financial performance of the bank. However, the challenges for formulating collection policies were the slowdown in economic conditions, customer behaviors, inflation rate, shortage of foreign currency or hard currency, and loss in business operations. The banks penalized client's for late payment. The study also concluded that default management policies of the bank, which take legal actions against chronic defaulters, help with how to get out of financial distress. The study further concluded that the bank's default management policies did not use staff incentives for effective recovery of defaulted loans and also did not hire a collection agency. The study established that the loan officers of the banks served as security for the bank; the study concluded that loan default management policies decreased loan defaulters and improved the financial performance of the bank.

The study lastly summarized that the prevailing organization loan policy were increased the profitability of the bank, by decreased the defaulters, reduced the danger of financial loss, increased return on asset, increased loan recovery ratio, and improved organizational lending images. Therefore, the study concluded that the loan policies of the banks were significantly improving the financial performance of the CBEs.

5.4. Recommendation of the study

The researcher, as per the findings of this study, suggests the following recommendations for this study:

The study recommends that commercial banks develop lending policies in order to improve customer relationships and use lending policies as a tool to gain a competitive advantage in the market. Commercial banks ought to carry out adequate financial analysis and reduce interest rates as a way of reducing loan defaults.

Further, the study recommended that commercial banks develop their own website and system related to loan and credit management, which would allow easy monitoring and follow-up of each debtor's status, information about their performance and outstanding balance, and communicating with customers through the system.

Due to the increasing complexity of technology and business around the world, commercial banks focus on capacity building activities and providing training to managers and loan officers that work on loan and credit activities to cope with business environments. They also continuously monitor the cash flow the borrowers to control diversion of funds for other purposes.

Finally, the study recommends that commercial banks develop and implement loan policies to increase the level of bank books and shareholder value, create customer satisfaction, reduce loan loss defaults and increase bank profitability.

5.5. Further research study

The study suggests that further study should be done on the factors and the major inputs for commercial banks to prepare the lending policies and the effects of various loan policies in influencing the borrower's decision.

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APPENDIX 1.QUESTIONNAIRES QUESTIONNAIRE

Dear respondents: This is a questionnaire designed to collect data on the **Assessment of loan policy and its effect on financial performance of private selected commercial banks'** which will be used as an input for a thesis in a partial fulfillment of Masters of science Degree in accounting and finance. Your genuine response is solely used for academic purposes and the data will be treated with utmost confidentiality. Therefore, your kindly cooperation is appreciated in advance.

I. General Instructions

- There is no need of writing your name
- Please put a tick (✓) marks in the appropriate box of your answer
- The questionnaires contains 12 page includes cover page

Contact Address: If you have any questions please contact me and I am available as per your convenience @**Mobile: 09-34-40-16-58** or e-mail: gezahegnde21@gmail.com

Thank you in advance for sacrificing your time to fill this questionnaire!

Demographic Information

(Tick the appropriate box)

1. Gender

Male Female

2. Age

20-30 years 31 -40 years 41 -50 years above 50

3. Marital status

Single Married

4. Educational back ground

Diploma Degree Masters PhD and above

5. Current position

Branch Managerial Loan officers Above 10 years Loan manager

6. Loan related experience within the bank

1-5 years 5-10years greater than 10 years

II. RESEARCH RELATED QUESTIONS

Please respond to the following statements by indicating the extent to which you agree or disagree

Kindly rate the extent to which you agree with the following statements on the financial performance of commercial banks private commercial bank

Key - 5- Strongly Agree, 4- Agree, 3 – Not sure, 2- Disagree, 1- Strongly Disagree

A. Effect of Loan terms and condition policy on financial performance of private commercial Bank

statements	Strongly agree 5	Agree 4	Not sure 3	Disagree 2	Strongly disagree 1
1.bank have well developed written loan policy					
2.Does your bank frequently review its loan policy					
3.Bank set interest rates charged on loans at market rate					
4.the repayment schedules set for each loan negotiated with the client					
5.Loan terms and conditions practiced by your bank influence the volume of loans obtained from your bank					
6.Loan terms and conditions put in place by a bank affect its ability to attract loan seekers					
7.The bank adjusts the interest rates on the loan granted without referring to the customer					
8.The bank lending offer mostly long terms loans					
9.During your loan processing, you are strictly enforced to fulfilled the conditions and terms set by loan approval team before loan disbursement					
10. well-developed loan terms and condition increase banks profitability					

Any other specify

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B. Effect of Loan lending policies on financial performance of private commercial bank

statements	Strongly agree 5	Agree 4	Not sure 3	Disagree 2	Strongly disagree 1
1. The lending policy developed by bank adequate and effective					
2. Good lending policy increase loan repayment					
3. Stringent loan policy minimize cost of collection, bad debt expense and unnecessary legal cost					
4. When considering granting loans, the bank requests the availability of guarantees in excess of the value of the loan granted					
5. The bank's board of directors delegates the management of lending responsibilities to specialized committees that carry out responsibilities for implementing the lending policy.					
6. The bank takes into account the laws and regulations in force by the monetary authorities in the country, especially with regard to lending policies.					
7. The banks approve the maximum limit for lending according to the number of funds available for lending.					
8. When making a lending decision, the bank takes into account the evaluation of loan that lending					
9. The bank, before granting the loan, studies the experience, suitability, and reputation of the borrower					
10. Lending policies adopted by banks greatly influence the performance of the bank.					

Any other specify

.....

C. Effect of Loan monitoring policy on financial performance of private commercial bank

statements	Strongly agree 5	Agree 4	Not sure 3	Disagree 2	Strongly disagree 1
11. Bank has a policy to guide its loan					
12. Bank has a policy to evaluate the customer asymmetric information before advancing loan to them					
13. Bank has a policy that help to monitor the customer repay their loan					
14. Bank has a policy that guiding in the loan recovery of funds from non-performing loan					
15. Does collateral estimation regularly assessed & related to applicants financial health					
16. Does the bank do restructuring loan repayment of borrower after lending					
17. The bank periodically prepare loan grading reports for signaling loan loss in any portfolio					
18. Continuous monitoring of cash flows of borrower					
19. The bank undertakes follow up to check proper utilization of funds released for the intended purpose					
20. Bank loan monitoring policy increase bank profitability					

Any other specify

.....

Effect Loan collection policy on financial performance of private commercial bank

statements	Strongly agree 5	Agree 4	Not sure 3	Disagree 2	Strongly disagree 1
1. The bank have formulated collection policy procedures and systems to secure repayment from customers					
2. Penalizing clients for late payment loan					
3. Strong loan collection campaign made to keep loan repayment timely					
4. We have regular reviews on collection policies to improve the state of loan collection					
5. Available collection policies have assisted towards effective loan collection.					
6. Regular reviews have been done on collection policies to improve state of loan collection					
7. The bank has strict and effective loan repayment policy					
8. Formulation of collection policies have been a challenge in loan management					
9. Bank collection of loan use both installment and lump sum methods					
10. loan collection policies to improve bank profitability					

Any other specify

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E .Effect of Loan Default management policy on financial performance of private commercial bank

statements	Strongly agree 5	Agree 4	Not sure 3	Disagree 2	Strongly disagree 1
1.The banks default management policy to taking legal actions against chronic defaulters of bank-loans.					
2.the bank default policy If the loan is unsecured the bank must request that the court liquidate the firm assets					
3.The default policy they enforce guarantee to provide chances for loan recovery in case of loan defaults					
4.The bank default policy has staff incentives that are effective in improving recovery of default loans.					
5.loan Default policy examinee borrower's ability to pay loan					
6.The bank default policy does limits in loan amount to collateral value					
7. loan Default management policy hiring collection agency for loan default					
8.loan Default management policy write off for loan default					
9.Penalties upon loan default					
10. bank loan default management policy increase bank profitability					

Any other specify

.....

F. Financial performances of commercial banks

Kindly rate the extent to which you agree with the following statements on the financial performance of commercial banks private commercial bank

Key - 5- Strongly Agree, 4- Agree, 3 – Not sure, 2- Disagree, 1- Strongly Disagree

	Statement	5	4	3	2	1
1.	Organizational loan policy leads to improved profitability					
2.	Organizational loan policy leads improved its loan terms and condition					
3.	Organizational loan policy leads to reduced loan defaulters					
4.	Organizational loan policy leads to improved loan collection					
5	Loan policy leads to improved organizational loan monitoring and follow up					
6.	Loan policy leads to improved organizational loan lending capacity					

G. Interview questions

1. Do the banks discuss with customers about Loan terms and condition policy? If not why.
2. What is types of policy can be used to give efficient types of loan lending
3. What are the major challenges you face in loan collection procedure?
4. What are the types of policy and procedure to monitor and follow up loan?
5. what are the main reason for loan that can be defaulted
6. What are the major policies and procedures used to collect for the loan that is deflated
7. Your loan policy at what extent affects the financial performance of bank

APPENDIX TWO

Return on asset of six selected private commercial bank from year 2016-2020 years of operation (%)

S.no	Names of Bank	2016	2017	2018	2019	2020
1	Awash International Bank	0.028	0.028	0.031	0.038	0.032
2	Dashen Bank	0.0273	0.0239	0.0232	0.02	0.025
3	Cooperatives Bank of Oromia	0.001	0.01	0.02	0.02	0.03
4	Unite Bank	0.02	0.02	0.02	0.02	0.02
5	Wegagen Bank	0.0251	0.0287	0.0328	0.0217	0.025
6	Nib International Bank	0.0268	0.0241	0.0216	0.0239	0.027