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Nexus between Credit Management and Financial Performance in the Financial Institutions in Nigeria

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Abstract: *Achieving success in any business firm requires a formidable credit management with critical customer appraisal. This study, therefore, aims at establishing the relationship between the credit management and financial performance in financial institutions in Nigeria. To achieve this objective, the study adopted descriptive survey research design method and data were collected from the staff and customers of two selected prominent financial institutions in Nigeria. Correlation and Regression analyses were used to estimate the causal relationships between credit management and financial performance and other related variables. The results of the analyses revealed that when a company implements effective credit management systems, the firm's efficiency is enhanced. This has an impact on the level of financial performance in terms of debtors' turnover, financial growth, management and ultimately profitability. It was recommended that financial institutions should take proper cognizance of effective credit management that would enhance organisational profitability.*
Keywords: *Credit Management, profitability, Financial Performance, descriptive survey, Nigeria, correlation and regression analyses*

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I. Introduction

Credit has been defined as the situation whereby goods and services are possessed without instant payment but with a contractual agreement that the payment would be made later in future date. However, it is expedient to identify potentialcreditdefaultin timeashighdefaultrates lead to decreased cash flows, lower liquidity levels and financial distress, hence, Ifurueze (2013) opines that one of the business strategies operated by business organizations in their attempts to make profit isallowingcredittocustomers. In the same vein, Akinselure andAkinola (2019) assert that default by borrowers in repayment of loan (credit risk) adversely affect the financial performance of financial institutions.No wonder that Scheufler(2002)affirms that the current business environment, risk management and improvement of cash flows are verydifficult to manage. He (Scheufler) therefore suggested that for creditprofessionals to imbibe in proven best practices, they must avoid five pitfalls which are: failure to recognize potential frauds, underestimation of the contribution of current customers to bad debts, getting caught off guard by bankruptcies, failure to take full advantageof effectiveandefficientcreditpolicy,andspendingtoomuchtimeandresourcesoncredit or client evaluations that are not related to reduction of creditdefaults. It is therefore advisable that credit appraisal should be carried out by the experts in the field of credit management who are experienced and competent in order to avoid or reduce vulnerable credit risk at the earliest possible opportunity (Eno, Ukpe, &Essien, 2018).

The role of credit management cannot be overemphasized in any firm that engages itself in credit. It involves guidelines and strategies adopted by a firm to ascertain that they maintain an optimal level of credit and achieve its effective management (Myers and Brealey, 2003). Credit Management, according to Nelson(2002) is the method by which an entity manages its credit sales. It serves as a requirement for any organisation dealing with credit transactions. It can also be described as an aspect of financial management that involves formulating of credit policy, credit analysis, client capacity, credit rating,creditriskmanagement,creditclassificationandcreditreporting.One of the intricacies of credit management is that it usually poses higher finance costs to maintain higher amount of accounts receivables and their age. Suffice to say thatif these receivables are not collectible ontime and urgent cash needs arise, a firm may result to borrowing and the consequence of this is the interest expense paid.It is therefore expedient for the financial institutions to develop rigorous and robust credit policies that will enable them to effectively assess the creditworthiness of their customers as recommended by Kajola,Olabisi ,Adedeji andBabatolu (2018).

According to Nzotta (2004) credit management usually influences the success or failure of commercial banks and other financial institutions. He concluded thatcredit decisions to grant credit, degree of credit policy and thus the quality of the risky assets determine thefailureofdepositbanks. Therefore, credit management

always serves as a leading indicator of the quality of deposit bank's creditportfolio. Hence, Nwanna and Oguezue (2017) conclude in their study that sound credit management heightens profitability and holds the financial strength of the Deposit Money Banks. In fact, credit management commences with the sale and does not end until the full and final payment has been made. It significantly ends thesale.Of course,asaleistechnicallynotasaleuntilitsproceedshasbeen realised.

An effective credit management requires remarkable efforts to managecustomercreditlines in order to reduce bad debt exposure, over reserving and bankruptcies. It is important that business firms mustnot be oblivious of customer financialstrength(clientappraisal),creditscorehistoryandchangingpaymentpatterns through effective credit policy.

Creditmanagementcan be regarded as a catalystforincreasingfinancialperformance.Hence, Collins, M-epbari, Sira, and Miebaka, (2018) concluded in their study that credit management has a significant impact on bank performance in Nigeria. Financialperformanceentailsmeasuringtheresultsofafirm's policiesandoperationsinmonetaryterms whicharereflectedinthefirm'sreturn on investment, return on assets and value added. According to Stoner (2003) as cited in Turyahebya (2013), financial performance is the efforts exalted to operate efficiently, profitably, survive, grow and react to the environmental opportunities and threats. Also in line withthis,SollenbergandAnderson(1995)assertthat,performanceismeasuredbyhow efficienttheenterpriseisin making the optimal useofresourcesinachievingitsobjectives.Hitt,Hoskisson, andJohnson(1996)believethatmanyfirms record low financial performancebecauseof the poor performance of their assets such as debtors and baddebt.

It is against the backdrop of the above analysis that this study is set to investigate the nexus between the credit management and financial performance of financial institutions in Nigeria.

The study is grouped into five sections. Following the introduction is the literature review in section2 where the relevant literature to the study are discussed. Section three explains the methodology of the study while the findings of the analyses are discussed in section four. The concluding part of the study is explained in section five with recommendations from the findings of this study.

II. Literature review

Creditmanagementconnotes theabilitytointelligently andefficientlymanagecustomercreditlines. It is the means by which an entity manages its credit sales. Pandey (2004) opines that credit should possess three characteristics viz:

I. It should involve an element of risk that should be carefullyanalyzed.

II. It should be based on economic value. To the buyer, the economic value in goods or services possessimmediatelyatthetimeofsale,whilethesellerexpects anequivalentvalueto be received lateron.

III. It should be futuristic. Thebuyerwillmakethecashpaymentforgoodsorservicesreceived by him in the nearest future.

In their study on credit management Raymond, Adigwe, and John, (2015) revealed that timely identification of potential credit default is important as high default rates lead to decreased cash flows, lower liquidity levels and financial distress. Also, Alice and Jaya (2016) observe that credit management as a concept is of most important activities in any company and should not be treated with levity by any economic enterprise engaged in credit irrespective of its business nature. It is based on the expectation that customers will pay for the products delivered or the services rendered. By granting credit, a business firm is creating trade debts in business which can lead to good debts, doubtful and bad debts.

Credit management is also very important in the management of working capital because poor management of trade debt can result to the provision of large sum of funds for bad anddoubtfuldebts. Baddebtlossesoccurwhenthefirmis unable to collect its accounts receivable.

Financial performance isanaspectoffinancialmanagementthatevaluatesfirm's efficiency with regard to its resources. It can be measured on the basis of financial ratio analysis. Financial ratios serve as powerful tools used in measuring organizational financial performance. The ratios give the necessary and required information to the interested parties inside and outside the company. These information and data, if properly analyzed, would aid decision making and measurement of company's performance and efficiency over time (Kasali and Salako, 2016). Financial performance measures how a business firm can make the optimal use of its assets.It can also be used asageneralmeasureofafirm'soverallfinancialhealthoveragivenperiod of time which can be used as comparison among similar firms across the same industry or to compare industries or sectors inaggregation.

Several studies have been conducted to establish the relationship between credit management and financial performance of business organisations particularly inthebankingindustry. Gizaw, Kebede and Selvaraj, (2015) examined the impact of credit risk management on profitability of commercial banks in Ethiopia. Data collectedfrom8samplecommercialbanksfrom annual reports of respective banks and National Bank of Ethiopia were analyzed using a descriptive statistics and panel data regressionmodel.

Theresultshowedthatcreditriskmeasures,non-performingloan, loan loss provisions and capital adequacy have a significant impact on the profitability of commercial banks in Ethiopia. Ntiamoah, Diana and Kwamega (2014) carried out a study on assessment of the relationship between credit management practices and loan performance using some selected microfinance institutions in the Greater Accraregion of Ghana as case study. Results of the study revealed that there was high positive correlation between the credit terms and policy, lending, credit analysis and appraisal, and credit risk control and loan performance. Ayodele, Thomas, Raphael &Ajayi (2014) carried out a study on impact of credit policy on the performance of Nigerian Commercial Banks using Zenith Bank Plc as case study. Primary data were collected throughquestionnairesservedonsixty(60)respondentsofthebank.Thefindingsfrom the study showed that having a good credit policy in place goes a long way in minimizing the incidence of baddebts.

Owizy (2013) evaluated the impact of credit management on financial performance of Nigerian banks, with particular reference to UBA Plc. Financial ratios as measures of bank performance and credit indicators were the data collected from secondarysourcesmainlytheannualreportsandaccountsofsampledbanksfrom2004-2008. Descriptive, correlation and regression techniques were used in the analysis. The findings revealed that credit management has a significant impact on the profitability of Nigerian banks. Byusa and Nkusi (2012) investigated effects of credit policy on bank performance in selected Rwandan Commercial banks. The aim of their study was to investigate the effects of credit policy on bank performance using data on selected Commercial Banks. The results obtained indicated that the Rwanda's commercialbanksincreasedtheiraccounts,increasedcustomerbaseandimprovedtheir financial indices, thereby maximizing their profits. However, inadequate competition in the banking system led to high spreads. Banks have unusually high and increasing average interest rate spreads and interest rate margins showing both highly poor competitionandinefficiency.Djankov,McLieshandShleifer(2007)studiedtheeffects of credit management on loan repayment in private credit in 129 countries in Eastern Europe, financial managers of the finance institutions were interviewed and dataanalysis was conducted using descriptive methods. The findings of the study concluded that credit management practices facilitated payment of loan. In his study, Simiyu (2008) investigatedonthetechniquesusedbymicrofinanceinstitutionsinthemanagementof credit risk in Kenya, and to examine the main challenges facing the micro finance institutionsoperatinginKenyainthemanagementofcreditrisk.Tosatisfytheresearch objectives,thestudyusedadescriptiveresearchdesigncomprisingasampleofthirty (30)microfinanceinstitutions.ThesamplingframeincludedtheCentralbankofKenya Directory of micro finance institutions. Purposive sampling was used to select one credit officer and one loan officer from each of the sampled institutions. Primary data were collected using semi-structured questionnaires. Thetargetrespondentswere the institutions' loans and credit officers. Once the pertinent data were collected the researchercarriedoutanalysisofthesameusingmeanscores,percentagesandstandard deviations.Thestudyestablishedthatmostmicrofinanceinstitutionsuse6Ctechniques ofcreditriskmanagement,thestudyalsorevealedthatunderstandingtheorganizations exposure to the customers is treated as critical by the micro finance institutions. The study established that majority of the institutions used credit matrix to measure the creditmigrationanddefaultrisk.Theresultsconcluded thatthemicrofinanceinstitutionsare faced with the challenge of strict operational regulations from the Central Bank of Kenya.

Adegbie and Otitolaiye (2020) investigated the effect of credit risk on financial performance of money deposit banks in Nigeria.The study covered 169 firm-year observations for the period of 2006-2018 in Money Deposit Banks in Nigeria. The result of their analysis revealed that credit management had a positive significant effect on financial performance of the Deposit Money Banks in Nigeria.

The summary of empirical review shows thatcreditriskmeasures,non-performingloans,loanlossprovisionsandadequacyhave a significant impact on the profitability of financial institutions. More so, another study by Ntiamoah, Egyiri, Fiaklou and Kwamega(2014) finds out that there is positive correlation between the constructs of credit management practices and loan performance. Furthermore, a study by Ayodele et al (2014) shows that a good credit policy in place goes a long way in minimizing the incidence of bad debts. From the foregoing it can be inferred that studies on credit management, financial performance and profitability, particularly in Nigeria is quitescanty.

III. Methodology

This study adopted descriptive survey design method. The data were collected through self-administered questionnaires distributed personally to the respondents. Fifty-nine (59) respondents were selected with the use of stratified sampling technique in which the strata consist of staff and customers of two selected prominent financial institutions in Nigeria. Ordinal scale was employed to measure the relationship between variables in the study.Variables measured in the study include: credit management, credit policy, creditrisk,clientappraisal,financialperformanceandorganizationalprofitability. The study adopted Correlation and

Regression analysis to estimate the causal relationships between credit management variable and credit policy, client appraisal, creditrisk,organizationalprofitability andfinancial performance.SPSSsoftwarewas used for Correlation and Regression analysis. The collected data were analyzed using multiple regression and correlation analysis and the significance of independent variablewastestedataconfidencelevelof95%.

The test statistic of the analysis adopted is:

$$r = \frac{n\sum xy - \sum x \sum y}{\sqrt{n\sum x^2 - (\sum x)^2}\ \sqrt{n\sum y^2 - (\sum y)^2}}$$

Where r = correlation coefficient y = OP, OP and PD.
x = CM, CP, CA and CR.
n = Sample Size
The decision rule is to reject H0 if sig value ≤ 0.01.

The method adopted in presentation of the data is simple percentage method of tabular presentation. The correlation test analysis was employed to test the stated hypothesis and to test the significant relationship between the actual and the observed variables;thiswasdoneviatheaidofStatisticalPackageforSocialScience(SPSS).In analyzing the data, frequency and descriptive tables were used as analytical tools. Qualitative explanations were made of quantitative data to give meaning to them as well as explain their implications. From these, appropriate conclusions and recommendations were made from the findings of theresearch.

IV. Findings and Discussions

Responses from the questionnaires were gathered from total of fifty-nine (59) selectedrespondents. Thestrengthofreliabilityandvalidityofthequestionnaireisanalysed in Table 1 usingthe Cronbach'salphareliabilityteststatistics.Theresult revealedthatthequestions are reliable because the Cronbach's is close to1.00

Table no1: *Reliability Statistics*

Cronbach's Alpha	N of Items
.587	28

Source: Authors' Survey (2017).

To achieve the objectives of the study and based on the identified variables through literature, the following hypotheses were tested and their results are discussed in the section. Pearson correlation (r) was employed to test the association between the variables stated in the hypotheses at 0.01 level of significant.
Decision Rule: Accept the Alternative Hypotheses and reject the Null Hypotheses ifthe Pearson correlation (r) is positive. The level of strength between this variable can also be determined as indicated in a table 2.

Table no2: Benchmark for Measuring Hypotheses

Coefficient Value	**Strength of Association**
0.1 < / r / < .3	Small correlation
0.3 < / r / < .5	Medium/moderate correlation
/ r / > .5	Large/strong correlation

Where r represents the absolute value of the Pearson correlation coefficient.
H1: There is a significant relationship between credit policy and organizational profitability.
α =0.01
Decision rule: If sig value $\leq$ 0.01, reject H0

Table no 3: Hypothesis one Correlations

	Credit Policy	Organizational Profitability
Pearson Correlation	1	.445**

Credit Policy	Sig. (2-tailed)		.000
	N	59	59
	Pearson Correlation	.445**	1
Organizational Profitability	Sig. (2-tailed)	.000	
	N	59	59

**. Correlation is significant at the 0.01 level (2-tailed).
Source: Authors' field study (2017)

Interpretation: From table 3, the Sig. value (0.000) is less than 0.01, we, therefore, reject H0. This implies that there is a significant relationship between credit policy and organizational profitability at 1% significant level, also the Pearson correlation coefficient (0.445) shows that there is moderate positive relationship between credit policy and organizational profitability in the selected banks.

H2: There is an effect of proper credit management on financial performance.
α =0.01
Decision rule: If sig value ≤ 0.01, reject H0

Table no 4: Hypothesis two Correlations

		Credit Management	Organizational Performance
	Pearson Correlation	1	.443**
Credit Management	Sig. (2-tailed)		.000
	N	59	59
	Pearson Correlation	.443**	1
Financial Performance	Sig. (2-tailed)	.000	
	N	59	59

**. Correlation is significant at the 0.01 level (2-tailed).
***Source:* Authors' Survey (2017)**

Interpretation: From table 4, the Sig. value (0.000) is less than 0.01, wetherefore reject H0. We conclude that there is an effect of proper credit management on financial performance at 1% significant level, also the Pearson correlation coefficient (0.443) shows that there is moderate positive relationship between credit management and financial performance in the selected banks.
H3: There is an association between successful client appraisal and payment default.
α =0.01
rule: If sig value ≤ 0.01, reject H0

Table no 5: Hypothesis three Correlations

		Client Appraisal	Payment Default
	Pearson Correlation	1	.553
Client Appraisal	Sig. (2-tailed)		.000
	N	59	59
	Pearson Correlation	.553	1
Payment Default	Sig. (2-tailed)	.000	
	N	59	59

**. Correlation is significant at the 0.01 level (2-tailed).
Source: Researcher field study (2017)

Interpretation: From table 5, the Sig. value (0.000) is less than 0.01, we, therefore, reject H0. The study concludes that there is an association between successful clientappraisalandpaymentdefaultat1%significantlevel,alsothePearsoncorrelation coefficient (0.553) shows that there is strong positive relationship between client appraisal and payment default in the selectedbanks.
H4: There is a significant relationship between credit risk and organizational profitability.
α =0.01
Decision rule: If sig value ≤ 0.01, reject H0

Table no 6: Hypothesis four Correlations

		Credit Risk	Organizational Profitability
	Pearson Correlation	1	.358**

Credit Risk	Sig. (2-tailed)		.005
	N	59	59
	Pearson Correlation	.358**	1
Organizational Profitability	Sig. (2-tailed)	.005	
	N	59	59

**. Correlation is significant at the 0.01 level (2-tailed).
Source: **Authors' Survey (2017)**

Interpretation: From table 6, the Sig. value (0.005) is less than 0.01, wetherefore reject H0.Weconclude that there is a significant relationship between credit risk and organizational profitability at 1% significant level, also the Pearson correlation coefficient (0.358) shows that there is moderate positive relationship between credit risk and organizational profitability in the selected banks.
The study was aimed at investigating the relationship between credit management and financial performance with special focus on financial institutions in Nigeria.
The empirical analyses revealed thatthereexistsamoderatesignificantrelationship between credit policy and organizational profitability on the basis of the responses providedbytherespondents.ThisresultisinaffirmationwiththeresultofByusa and Nkusi (2012), in their study titled "Effect of credit policy on bank performance in selectedRwandanCommercialbanks".Theimplicationofthisreskultontheorganization shows that when there is a viable credit policy in place, it tends to guide the flow of cash from the source (bank) to the destination (debtors) as well as flow from the destination(debtors)tothebank. It isworthyofnotehoweverthatthisprocesstendsto increase cash flow, thus having a great effect on the financial performance of organisations. A related study carried out by Ayodele, Thomas, Raphael and Ajayi (2014) portray that a good credit policy in place goes a long way in minimizing the incidence of baddebts. Also, the study confirms that there is a significant relationship between credit management and organizations' financial performance. This corroborates with the outcome of the study of Adegbie and Otitolaiye (2020) where it was confirmed thatcredit management had a positive significant effect on financial performance of the Deposit Money Banks in Nigeria.
Furthermore, the result of this study affirms that there exists a strong association between client appraisaland payment default which is in tandem with the outcome of the study of Alice and Jaya (2016) who found out that client appraisal has an effect on financial performance of commercial banks. They further asserted that client appraisal is a viable strategy for creditmanagement. Finally, this study established that there exists a moderate significant relationship between credit risk and organizational profitability within the selected banks. The result isinlinewiththefindingsofGizaw,KebedeandSelvaraj(2015).The finding from their study posits that credit risk measures, non-performing loan,loan loss provisions and capital adequacy have a significant impact on the profitability of commercial banks in Ethiopia.
Summarily, the analysis of the hypotheses in relation to the objectives of the study shows that credit policy, credit management, credit risk and successful client appraisalinfluence less paymentdefault,financialperformance,and the limit of the strength of association between these variables ismoderate.

V. Conclusion and Recommendation

It has been established that credit facilities to customers can make or mar the goals set by a business firm. Suffice to say that quick credit recovery from customers tends to be favorable for the organization but where there is bad debt on loan advancement to customers; such credit tends to decrease the profitability of the organization. A well-functioning credit managementwillbringbotheconomicbenefitintermsofprofitabilityandbring good image to the company. It will enable the company to recover its assets as atwhendue,hencecreatingalinkofrelationshipbetweenthemanagementand the customers (debtors). When a company implements effective credit management systems, the firm's efficiency is enhanced. This has an impact on the level of financial performance in terms of debtors' turnover, financial growth, management and ultimately profitability as purported by previous studies by Gizawetal(2015),Aliceetal(2016),Owizzy(2013),Ayodeleetal(2014)and Byusa et al (2012). Creditmanagementensuresthatthefirmembarks on effectiveplanningaheadoftimeto avoid shortages of fund and make sure that borrowed money are returned as at when due and at the right time. Credit management is very important since it enablesfirmstoavoidlockingtheirmoneyinbaddebtsandhelpbuildgoodand permanent relationship withcustomers.
The following are recommendations given as an aid in enhancing the efficiency and effectiveness of credit management in the financial institutions:

i. From the finding and conclusions, the financial institutions should ensure the adoption of credit

standards, credit policy, credit termsandcollectionpolicies.That is, beforegivinganyloan,client'srepayingcapacity;statusofcashflowsmust be properly assessed.

ii. Banks should develop and maintain a credit administration function that provides guidance to anyone in the credit function of the institution and to ensure safeguards are in place to manage the loanportfolio.

iii. The study recommends that management of banking firms should enhance their collection policy by adapting a more court litigation, collateral assets andenforcesaving.Thecollectionpolicyshouldensurepromptandregular repayment for fast turnover of working capital keeping collection costs and bad debts within limits and hence maintaining collectionefficiency.

iv. Finally, management should develop appropriate credit policies to ensure thatcreditadministrationisdoneeffectivelysoastoencourage quickloan repayments and reduce the rate of bad debts.

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