

**INFLUENCE OF CREDIT MANAGEMENT PRACTICES ON LOAN
PERFORMANCE OF ISLAMIC BANKS IN MOGADISHU, SOMALIA**

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DECLARATION AND APPROVAL

Declaration by the student

This project is my original work and has not been presented for a degree in any other university.

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Declaration by the Supervisor

I confirm that the work reported in this project was conducted by the candidate under my supervision

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DEDICATION

This research project is dedicated to my parents Mr. Nor Osman Abikar and Mrs Anab Sabrie Addow They provided a solid foundation for me that continues to keep me resilient and determined.



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ABSTRACT

In light of the substantial losses faced by financial institutions in Somali, effective credit management is imperative to ensure the success of Islamic banks in loan advancements. This research analysed the influence of credit management practices on the loan performance of Islamic banks in Mogadishu, Somalia. The study evaluated the effects of credit policy, credit appraisal, and collection policy on the loan performance of three prominent Islamic commercial banks: Amal Bank, Salam Bank, and Dahabshil Bank. The theoretical framework that guided this research includes the moral hazard theory, the theory of self-efficacy, and the information sharing theory. A descriptive research design was adopted, with a census study involving 72 employees from the credit departments of the three chosen Islamic banks. Data for the study were collected through questionnaires and analyzed using descriptive statistics. Multiple regression analysis was applied, and the findings were presented through graphs and tables. The study findings revealed significant and positive associations between credit policy and loan performance, credit appraisal and loan performance, as well as collection policy and loan performance of Islamic banks in Mogadishu, Somalia. The research concludes that a well-defined credit policy is foundational for shaping the performance of Islamic banks. Ensuring accessibility to the credit policy by all staff members is crucial, contributing to optimal bank performance. Additionally, obtaining borrowers' credit history from other financial institutions is a pivotal strategy for assessing creditworthiness before loan extensions. The capacity of borrowers to repay from their own sources is identified as a key factor enhancing the extension of loans by Islamic banks. Islamic banks prioritize borrowers' ability to repay from their own sources, aligning with Islamic finance principles. This approach reduces loan default and non-performance, ensuring financial sustainability. Collateral demand in loan appraisals is a risk mitigation strategy, minimizing financial risk and fostering responsible borrowing behavior. Islamic banks' rigorous debt collection approach ensures timely repayment, while penalties on loan defaults deter delinquency and promote a healthier credit environment. Auctioning customers' properties in case of default demonstrates a structured debt recovery process. Legal recourse is used to recover debts, enhancing credibility and deterring potential defaulters. To enhance credit management practices, Islamic banks are encouraged to prioritize transparency and accessibility in their credit policies. Regular reviews of the credit policy, aligning it with emerging market trends, regulatory shifts, and evolving economic conditions, are paramount. Moreover, incorporating ethical and Sharia-compliant components into the credit policy is recommended to strengthen the overall performance of Islamic banks in Mogadishu, Somalia. Islamic banks should also consider incorporating ethical and Sharia-compliant components into the credit policy. This includes a comprehensive assessment of a borrower's financial net worth, adherence to Islamic principles, and the economic viability of proposed ventures. This alignment with Sharia principles not only enhances the bank's reputation but also ensures a consistent commitment to ethical banking practices. Islamic banks should explore avenues to enhance customer education and communication regarding the credit policy.

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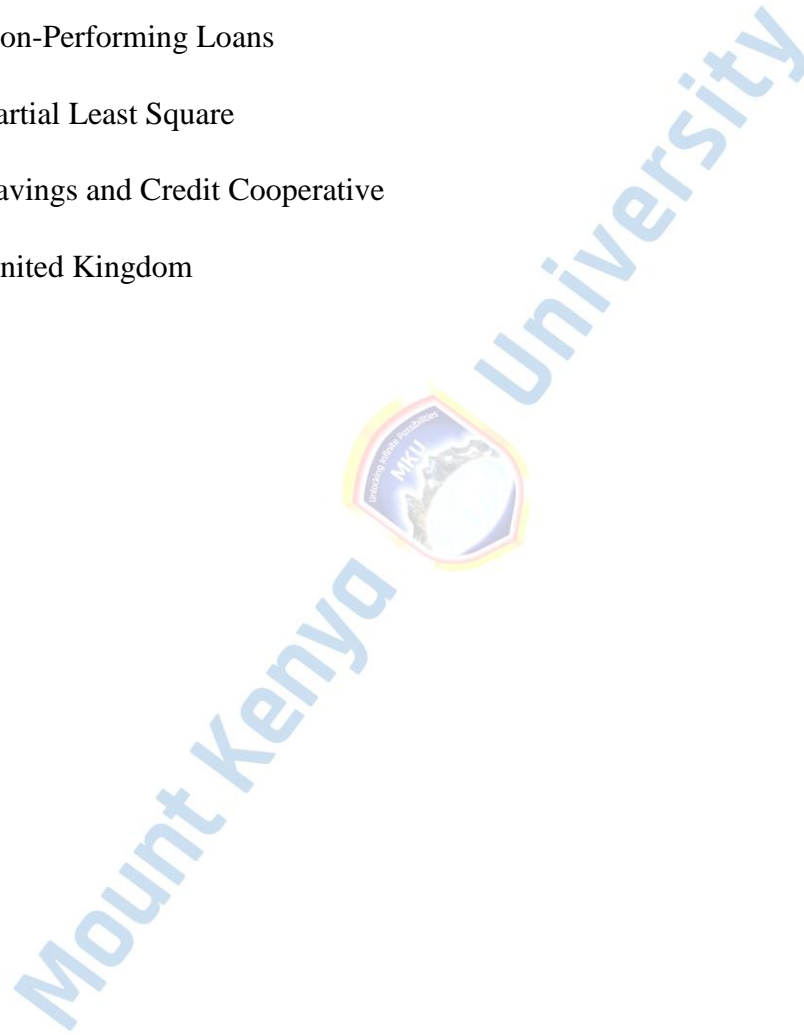
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LIST OF ABBREVIATIONS AND ACRONYMS

ANOVA	Analysis of variance
ECM	Error Correction Model
IMF	International Monetary Fund
NACOSTI	National Commission for Science, Technology & Innovation
NPL	Non-Performing Loans
PLS	Partial Least Square
SACCO	Savings and Credit Cooperative
UK	United Kingdom



CHAPTER ONE

INTRODUCTION

1.1 Background to the Study

Effective credit management not only plays crucial role in the performance of a bank's loan book but also has a major effect on the bank's overall success. Loan portfolios are a bank's most valuable asset and main source of income, as well as one of the most important factors in ensuring its stability and performance (Pradyut, 2019). Credit management is one of the blueprints for assuring the stability of any industry through credit monitoring and effectiveness. A client's character, capacity, collateral, capital and condition determine how much of the loan will be repaid based on personal, cultural, societal and economic considerations (Nsengiyumva & Harelimana, 2020). The effectiveness of the loan is affected by credit management practices. Moreover, credit regulations including collection policy, credit terms, credit standards and loan reviews can have an impact on how well loans perform (Pradyut, 2019).

The first modern Islamic banking experiment was conducted in Egypt. In 1963, the pioneering endeavor under the direction of Ahmad El Najjar took the shape of a savings bank with a profit-sharing model. By the time the trial ended in 1967, there were nine such banks operating in the nation. These banks didn't charge or pay interest. The banks invested in businesses, through a model of share of business profits (Abdullah et al. 2020). As a result, rather than acting as commercial banks, they served as institutions for savings and investments. Modern Islamic finance has evolved dramatically in both volume and breadth since its birth in the 1970s, garnering major attention on a global scale. The Islamic financial sector has evolved through time into a thriving and competitive type of international financial intermediation (Abdullah et al., 2020).

Despite attempts by financial institutions, non-performing loans have increased globally, in both emerging and industrialized nations. Globally, bank poor credit management affects loan default. According to Do et al. (2020), the loan default problem in Vietnam's banks reached 19%, and in the UK, bank loan arrears increased from 1% to 6% (Mubeen & Bashir, 2017). This is the same case in Brazil (Liu et al., 2020), India (Shylendra, 2018), Pakistan (Islam, 2020), Bosnia and Herzegovina, and Pakistan's Islamic bank sector which had high loan default rates (Zuni et al., 2021). Wan (2018) evaluated the issues small and medium-sized businesses were facing and found that credit management was a major problem. The failure of certain of their trade creditors to make timely debt payments has a substantial negative influence on small enterprises' operating capital.

The management of banks' credit and their financial outcomes are positively correlated and significant (Guna, 2022). Also, the financial success of Nepal's commercial banks is positively and significantly correlated with the management quality ratio (Guna, 2022). Nepalese commercial banks must engage in scientific credit management practices that enhance credit analyses and help manage the loans with efficacy (Guna,2022). The increase in NPLS, according to Cincinelli and Piatti (2021), is the consequence of variety of factors, including the banks' lending monitoring procedures and their limited ability to settle defaulted loans, as well as the hard and protracted recession in Italy.

Sub-Saharan African nations have a significantly greater number of NPLs. Financial institutions lose more amounts of money due to bad credit management. Brako (2018) noted substantial and positive link between Ghana's performance of loans and structures of management of credit procedures. According to Nsengiyumva and Harelimana (2020), the majority of banks operate without effective credit management methods, putting customers in danger of financial trouble. According to Ndyagyenda (2020), banks' management should

regularly evaluate their credit management procedures to see whether they remain effective in light of the operational environment's constant change.

Mburu et al. (2020) reported that Kenyan commercial banks recorded higher levels of loan non-performance than the global average. This is true even though Kenya claims to have East and Central Africa's most sophisticated and reliable financial system. The average percentage of commercial banks' NPLs over a 5-year period i.e. 2015 up to 2018 was 11%, exceeding the recommended level of 1%. Kenyan commercial banks continue to have more non-performing loans than is ideal, which may be due to poor credit management practices. Lending and Debt collection methods have a big influence on how well loans function in Kenyan commercial banks.

Wachira (2017) acknowledges that banks encounter a variety of hazards and the gravest danger is the risk of credit. The risk of loss to lender from non-performing loans is managed through credit. Both financial theory and practice provide a systematic method of regulating credit in financial institutions. Loan default is still a concern for lenders. Credit management has an impact on loan performance (Wachira, 2017). Managers must therefore evaluate customer's capability in paying back debts promptly because better credit appraisal results in higher performance from commercial banks.

Despite adopting credit management methods, microfinance banks in Kenya continue to experience an increase in non-performing loans (Mutai & Opuodho, 2021). Internal credit management procedures, credit giving procedures, credit surveillance procedures, and The effectiveness of credit management processes has been significantly improved by with which Kenya's microfinance institutions make and distribute loans. Use of a credit management system by Financial institutions will assist them in boosting and enhancing their earnings. In order to attract more creditors and increase interest income, microfinance institutions should set appropriate rate of interest.

Commercial banks in Mogadishu Somalia meet the needs for efficient risk management by allowing their customers to wisely and effectively manage their loan limits. More knowledge on the financial stability, credit score history, and shifting payment habits of customers is necessary for firms to lower their risk of bad debt, over reserving, and insolvencies. (Barre, 2023). This study examines how Islamic banks' credit management policies and procedures affect their lending outcomes. This research tries to answer the question: In Mogadishu, Somalia, how do Islamic banks' credit management procedures affect their loan performance?

1.2 Statement of the Problem

Credit management is essential because of the massive losses in the banking sector. Ineffective internal credit management procedures may cause Islamic banks to perform poorly when advancing loans. Effective credit management procedures can boost an organization's performance, profitability and liquidity. To ensure stability, performance, and profitability, management must maintain a balance between the amounts of the various financial resources. Deterioration in loan repayments not only jeopardizes the profitability of Islamic banks but also prevents them from realizing their goals. Since loans make up a large amount of credit, the decline in loan repayment among Islamic banks' customers may be the primary issue with their credit management. This points out to challenges facing the bank's loan recovery that needs investigation. Amal, Salam and Dahabshil Banks are the 3 largest banks in Mogadishu Somalia. Data from the International Monetary Fund (IMF) Country Report of 2021 indicates that non-performing loan ratios for the three banks were 3.9%, 4.1% and 3.4% respectively (IMF, 2021). These ratios are higher than the country ratio of 3% (IMF, 2021). Despite the banks' credit administration processes, the outcome is poor. This necessitates researching how credit management techniques affect the quality of loans. There is a dearth of academic knowledge on Credit management methods' impact on loan performance of Islamic banks. Mburu et al. (2020) investigated the loan performance and credit management procedures used by

Kenyan commercial banks. The study discovered that lending and debt collection policies had a considerable useful influence on the loan the banks' effectiveness. Wachira (2017) investigated how commercial banks in Nyeri County's loan performance were influenced by their credit management policies. The study's conclusion was that every bank had a proper-drafted credit policy that was adhered to rigidly and consistently. The study presents a contextual gap as it was conducted among commercial banks in Nyeri county, Kenya. Mutai and Opuodho (2021) examined how different credit management strategies affect financial institutions. Researchers found that prudent credit management improved financial institution profitability. The study presents a conceptual gap as the dependent variable was profitability. Kajirwa and Katherine (2019) assessed the financial performance and credit risk of Somali banks listed on the Somalia Stock Exchange. These studies focused on conventional banks, hence creating conceptual and contextual gaps that this research sought to fill. Hence, Research examines how credit management techniques affect the success of Islamic banks' loans in Mogadishu, Somalia.

General Objective of the Study

The general objective of the research is to analyze the influence of credit management practices on loan performance of Islamic banks in Mogadishu Somalia.

1.3 Objectives of the Study

Specific objectives of this study are:

- i. To evaluate the influence of credit policy on loan performance of Islamic banks in Mogadishu Somalia.
- ii. To examine the influence of credit appraisal on loan performance of Islamic banks in Mogadishu Somalia.

- iii. To assess the influence of collection policy loan performance of Islamic banks in Mogadishu Somalia.

1.4 Research Questions

- i. What is the influence of credit policy on loan performance of Islamic banks in Mogadishu Somalia?
- ii. How does credit appraisal influence loan performance of Islamic banks in Mogadishu Somalia?
- iii. To what extent does collection policy influence loan performance of Islamic banks in Mogadishu Somalia?

1.5 Significance of the Study

This research will be undertaken on the three main commercial banks in Mogadishu. Management can use outcomes of the study to evaluate their credit management policies, to enhance credit management. The management of Islamic banks may implement the study's recommendations to improve credit management. The managers of Somali commercial banks will benefit from this study's grasp of Islamic finance as they develop products for their Muslim clients. It will assist the general public and bank customers who require Islamic products from banks that are compliant with shariah in understanding the fundamentals of Islamic banking. It will assist in understanding the operational requirements of Islamic banking and allow supervisory agencies and other stakeholders to establish guidelines for overseeing Islamic banks. Other researchers or academicians or anyone who wish to learn more may find this research to be a valuable resource. The results could also be used as supplementary information by finance students.

1.6 Scope of the Study

The study analysed the influence of credit management practices on loan performance of Islamic banks in Mogadishu Somalia. This study will be conducted on three largest commercial banks in Mogadishu, Somalia. The three major commercial banks are in Mogadishu. These are Amal Bank, Salam Bank and Dahabshil Bank, these banks are the largest Islamic commercial banks in Mogadishu. While there are other factors that may influence credit management practices on loan performance, this study will only focus on credit policy, credit appraisal and collection policy.

1.7 Study Limitations

This study was limited to the questionnaire responses. Additionally, only employees of the Islamic banks were relied on, hence a limitation in self reporting. Additionally, only a sample of 72 employees were involved in the study, hence a limitation. These limitations were overcome through inclusion of all target respondents in the study

1.8 Delimitations of the Study

This study acknowledges that several credit management practices influence loan performance of Islamic banks. However, this study will only focus on three thus, will analyse the impact of credit policy, credit appraisal and policy for collecting debt related to loan performance of Islamic banks in Mogadishu Somalia. The other credit management practices were not the focus of this study as they were not well applicable to the unit of analysis of the study. The study did not review literature on commercial banks as the focus of the study were Islamic banks. The study did not collect data through interviews as the researcher controlled the responses through questionnaire likert scale.

1.9 Assumptions of the Study

This research presumes that participants will be familiar with the concept of performance in mathematics. Consequently, they will be able to give relevant and reliable data required for the study. The study assumes that performance in mathematics is affected by pupils' attitudes, teaching and learning resources, teaching methods and teacher training. The study assumes that respondents will be honest in their responses.

1.10 Operational Definition of Key Terms

Collection Policy	method a company employs to achieve and surpass its goals for accounts receivable.
Credit Appraisal	institution uses this approach to evaluate a borrower's value in terms of their economic viability by looking at their capacity, capital, collateral, and other factors.
Credit Management Practices	involves extending credit, determining the criteria under which it is extended, paying back of credit as agreed, and maintaining compliance with the company's credit policy.
Credit Policy	method used by institutions to evaluate credit needs and the factors that influence whether or not applications are approved.
Loan	money lent to a third party in exchange for repayments into the future, at a fee.
Performance	measure of a bank's effectiveness, performance, and environmental responsibility using predetermined

metrics including cycle time, productivity, and regulatory compliance.



CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The study will examine the influence of credit policy, credit appraisal and collection policy on performance of loans of Islamic banks in Mogadishu Somalia. This chapter explains theoretical model that is relevant to the present research as well as reveal conceptual framework illustrating association between study variables. Finally, the chapter presents a recap of the reviewed literature.

2.2 Empirical Literature

Over the last three decades, Islamic banking has become a viable alternative to the traditional financial system as well as a rival (Cincinelli & Piatti, 2021). Also, it is acceptable for distinct Islamic banks to function in addition to traditional interest-based banks. Whereas conventional banks' primary product is loans, Islamic banks' primary business is funding. However, because default risk is inherent to every loan or financing, there is always a chance that the bank will experience client default and delay during the repayment time. As a result, it's possible to develop non-performing loans (NPL). A bank must increase its bad debt losses and assign more resources to the collection of NPLs if its asset base is insufficient (Kamchira, 2020). Insight is required for NPL management to protect the financial system and the health of financial institutions. The financing facility, which contributes significantly to the banks' liabilities, must be managed effectively and systematically if Islamic banks are to remain stable. If that occurs, it may result in a decline in NPLs, which will impact the liquidity of the banks (Mrindoko, Macha & Gwahula, 2020).

Islamic banking advocates an economic perspective that is important to the potential of a social order to offer both social justice and economic success. The goals of Shariah, sometimes referred to as maqasid al-Sharia, are strongly reflected in this vision (Piatti & Cincinelli, 2019). Therefore, it is important and cannot be overlooked to make efforts towards the fundamental advancement of Islamic economics that incorporate parts of maqasid al-Shariah. In this context, the Shariah's definition of maqasid refers to the defence of one's faith, life, possessions, brains, and human ancestry. The safeguarding of wealth is more evident and important in Islamic banking and finance, nevertheless. According to Sharifi, Haldar, and Rao (2019), Islam placed a high value on wealth and property. Preservation of wealth and assets is central to the goals of Shariah in matters of wealth.

The most effective methods for reducing financial risks are discovered by both Islamic and conventional institutions. The managers must disclose the procedure the bank will use to resolve these risks (Muhammad, Alwi & Muhammad, 2020). Saudi Arabia adopted the reforms in its new 2030 vision for all sectors, including banking, to improve an environment of transparency and greater disclosure with outstanding performance, all of which contributed to the creation of a competitive environment to achieve leadership and excellence in the delivery of competitive services. In order to determine whether Islamic banks or conventional banks have better risk management, Akram and Rahman (2018) examined the performance of Saudi Arabia's banking sector by examining the impact of credit risk in their operations. Data for the research was taken from the annual statements of four conventional and Islamic banks. Panel data of the chosen banks over a 10-year period, from 2009 to 2018, were utilized to indicate the connection between credit risk and performance.

According to Muhammad, Alwi, and Muhammad (2020), the percentage of NPLs in commercial banks in Malaysia is under control and does not rise over time. These possibilities are the result of the commercial banks' strict credit management policies, which, if not

adhered to, could have an effect on the profitability and liquidity of the banks. Yet, there are criticisms from the general public about how Islamic banks typically penalize their clients who are actual businessmen without a specific monthly revenue when they are just a little bit late in making their regular payments for the banks' facility or financing. The goal of an Islamic bank is to accomplish maqasid al-Shariah, hence it is expected to assist the customer. The credit management processes at one fully-fledged Islamic bank and one conventional bank that additionally offers an Islamic banking window were compared by Muhammad, Alwi, and Muhammad (2020). The report also noted how the two banks' credit management practices contributed to the accomplishment of maqasid al-Shariah. According to the study's findings, each bank has its own credit management techniques and practises. Their credit management strategies were designed to assist clients in preserving themselves from bankruptcy and insolvency while also assisting them in securing their loans, finances, and assets basically adhering to maqasid al-Shariah. It was advised that commercial banks implement a rigorous loan and financing approval process and a rigorous credit monitoring system to prevent non-performing loans.

Akram and Rahman (2018) looked at Pakistan's Islamic banks' loan management practices. Out of the entire banking sector, Five Islamic banks were chosen to serve as the study's sample. Secondary information gleaned from the thirteen-year annual financial reports of the banks. To evaluate data, multiple regression, correlation, and descriptive analysis were performed. Findings demonstrate that loan quality significantly and favorably affects credit management. Credit management is negatively impacted by asset quality. Regression model utilizing a dummy variable for financial crises was used to examine the effects of 16 ratios evaluating loan and asset quality on credit management. Performance was strong, and the model was substantial. The study presents a conceptual gap as the variables were loan quality, asset quality and credit management.

Baldina and Hendratmi (2020) looked into how supply chain management affected the relationships between the performance of Islamic banks in Indonesia and ties between credit quality, strong ties, and bridge ties. Smart-PLS and the questionnaire approach were utilized to collect the data. Findings indicated a strong relationship between this bank's management and the quality of its credit. Outcomes additionally shown that supply chain management acted as a constructive mediator between the ties between credit quality, strong ties, bridge ties, and Islamic banks' operations. These results gave adequate justification for future research into this topic, as well as for those who create regulations relating to supply chain and company performance.

2.2.1 Credit Policy on Loan Performance of Islamic Banks

The 5Cs of credit are used by financial firms in their lending operations. They are: capacity, capacity, capital, condition, and collateral. Character is essentially a tool that allocates weighting values to certain applicant traits for credit, and the applicant's total weighted score is employed to investigate applicant's credit worthiness (Ntiamoah et al.,2018). This is the first direct contact the client has with the prospective lender. Individual, cultural, social, and economic issues can all have an impact on a client (Hamid & Islam, 2019). Financial institutions observe and learn about the person to take this into account. A credit application is often not considered until after a second effort has been made. The manner a person lives falls under the category of social variables. This include the changes in how people communicate, what they buy, and what they do for fun. A person's values, beliefs, and point of view may often be inferred from their way of living. In most circumstances, reference organizations have an indirect impact on a person's trustworthiness (Islam et al.,2020).

Financial organizations work to pinpoint the target's reference groups because they can affect a client's reputation. Older families with grown children, for instance, are less likely to fail than unsettled young couples since it is simpler to attach security to their property because

they are settled (Kamchira, 2020). Financial institutions will consider the enterprise's flow of money, loan's successful repayment, and the date of the repayment. As the funds a borrower has available to settle his loan. Financial institutions use cash flow to assess a borrower's capacity to pay back the debt. Cash flow analysis can be a very complex process. It could involve more than just comparing earnings and outgoings. Financial organizations look at past cash flow figures and make logical future assumptions to determine cash flow (Pradyut, 2019). One of the items on the checklist that lenders use to examine the borrower's business plan and financial reports. These ratios serve as recommendations to help lenders decide if a borrower will be able to pay both the higher cost of a new loan and their present debt obligations.

Any asset that customers must offer as security for a loan is collateral (Sharifi, Haldar & Rao, 2019). Assets that the business commits as a possible source of loan repayment are represented by collateral. Hard assets like real estate and office or manufacturing equipment are mostly considered as collateral. Alternatively, goods and accounts receivable might be pledged as security. Short-term loan lenders seek collateral with a length that nearly matches the loan's own (Siriba, 2020). Capital is determined by an analysis of the borrower's financial ratios, with a focus towards the tangible net worth of the borrowers' firm. Capital is the money that a borrower personally invests in the firm and represents the amount that the borrower is willing to risk should the company collapse. Condition describes how sensitive the borrower is to external aspects like interest rates, inflation rates, economic cycles, and pressure from the competition. Conditions emphasize how vulnerable the borrower is (Sharifi, Haldar & Rao, 2019).

Capacity to efficiently make sound credit choices and establish good credit lines is essential for expanding into new markets and gaining new clients. Credit control begins at the time of sale and continues until full and complete payment has been received (Muhammad, Alwi &

Muhammad, 2020). That is just a key element of the agreement as finishing the sale. A sale is not finalized in the eyes of the law until the money has been collected. The best mix of credit policy factors might be challenging to come across, making it challenging to design an ideal credit policy. A company will experiment with one or two variables at once and track the results. It's important to note that the company's lending strategy is heavily influenced by economic situations (Akram & Rahman, 2018). The company's credit policy may alter as the economy changes.

Cincinelli and Piatti (2021) investigated the physiological credit risk that results from ineffective screening and management processes. Three hundred and The analysis sample consisted of thirty-eight banks. To determine the efficient border, the authors employed the greatest likelihood technique. Results indicated a connection between rising number of NPLs and both the severity and duration of the recession. This greatly decreased the ability of the borrowers to pay back their debt. The authors suggested a novel method for examining the effectiveness of the credit process. Physiological credit risk is distinguished from the credit risk brought on by ineffective screening and monitoring process management using the stochastic frontier. The authors also examined the factors that contributed to the excess of NPLs. The proposed study aims to fill the gap where the previous study's comparison of banks' credit management strategies and performance fell short.

The primary function of banks is to serve as a bridge between fund excess units and deficit units. The goals include profitability, asset growth, and customer base expansion (Abimbola, 2020). Banks offers loans and advances to people, enterprises, and governments to fulfil these goals. Loan default may be widespread as a result of poor asset quality and high non-performing risk assets, which could lead to significant loan losses and lower bank profitability. Abimbola (2020) evaluated how Nigerian money deposit banks fared in relation to non-performing loans. Data was gathered from secondary sources, and hypotheses were

formed. In its investigations, research used validated ECM model. The findings showed that performance of banks is impacted by non-performing loans. The report suggests adopting an efficient credit policy that includes variable tenure, renegotiating lending conditions, and conversion. This strategy might slow the rate of NPLs, which might lower the risk of default as return on equity increase. Their study failed to consider other variables that is credit appraisal and credit collection, hence a knowledge gap.

Despite possessing a large number of sophisticated and safe financial systems throughout East and Central Africa, commercial banks in Kenya recorded higher loan non-performance (Mburu, Mwangi & Muathe, 2020). The average percentage of commercial banks' NPLs over a 5-year period (2015 to 2018) was 11%, exceeding the recommended level of 1%. Kenyan commercial banks continue to have more non-performing loans than is ideal, which may be the result of poor credit management procedures. Mburu, Mwangi and Muathe (2020) investigated the influence of credit management practises on loan performance. The purpose of this research was to investigate how lending, client evaluation, and debt collection policies affected Kenyan commercial banks' ability to repay loans. The 5Cs model for credit served as the study's guiding theoretical framework. The study followed a positivist research methodology and employed a research design that provides explanations. A census approach was employed with 44 Kenyan commercial banks are the intended target group. Secondary data was gathered by reviewing current loan statements from banks in association to Advanced amount of loan and NPLs, while primary data was gathered using designed questionnaires tied to credit management strategies. It was decided to employ descriptive and inferential statistics to evaluate gathered data. Research discovered that lending and debt collection policies had a considerable favourable effect on the loan performance of this banks. Client evaluation, however, had no discernible impact on Kenyan commercial banks' ability to make loans. The study concluded that the effectiveness of the credit management procedures

used at the institutions could be mainly responsible for this banks' loan performance. It was recommended that this banks constantly review and improve policies related to client evaluation, debt collection policy, and lending policy in order to make sure that Credit risks are identified and documented at every level, from the department to the company. This is crucial to banking industry technological advancements like mobile lending that could hinder banks' capacity to assess and regulate loans utilizing conventional ways. Research focused on commercial banks, presenting a conceptual gap, to be filled with the current study.

The rising percentage of non-performing loans is one of the biggest issues that banks face globally. Several strategies have been developed by the government and banks themselves to decrease non-performing loans while boosting credit market uptake (Macharia & Mungai, 2021). The situation is actually the contrary; as credit demand rises, non-performing loans also rise. In order to address this issue, the Kenyan government established Credit Reference Bureaus in 2009. Nonetheless, the issues still plague the banks, making it unclear whether or not the exchange of credit information is effective. Macharia & Mungai (2021) explored the impact of sharing credit information policies on loan outcomes for Kenyan banks. Design for this research mixed primary and secondary methods. 42 commercial banks of Kenya were the intended market, and 210 credit personnel were employed. Information was gathered through questionnaires that were given to bank credit personnel by a drop-and-pick method. The banks' credit histories were obtained through document analysis. The results demonstrated that even after the credit information sharing policy was put into place, the number of non-performing loans climbed dramatically. Although if there was a noticeable increase in profits following the installation of the credit reference bureaus, a detailed examination of the pattern reveals that the policy was not the cause of any substantial changes. Although the policy of the credit reference bureaus was well-intentioned, responses from the accounting officers also demonstrated that objectives had not been realized, partly because the standards for listing

and delisting defaulters were not clearly defined. Commercial banks and credit reference agencies must to make their regulations on adding and removing defaulters from lists transparent and simple to follow. The study's focus on commercial banks revealed a conceptual hole that the current study will remedy.

Njeru, Mohammed, and Wachira (2017) investigated the relationship between Kenyan industrial banks' credit control system efficacy and their loan performance. Research design was descriptive. The sample size was 86 respondents. Given the limited size of the target population, a census study was conducted. Self-administered questionnaire was employed to gather data using the drop-and-pick technique. Survey had open and closed-ended questionnaires. Piloting was employed to evaluate the reliability of the study instruments., test-retest methodology was used to guarantee reliability. Using frequencies, percentages, and means, data was evaluated. Correlation was used to determine how strongly the variables were related. Chi square analysis was utilized to examine the theory. The data was then shown using a table and pie charts. Research have shown that financial terms affect productivity, much as credit appraisal was reported to have a substantial impact on commercial banks' performance. Similar findings showed that a strict policy had a much bigger impact on performance than a lax policy. It was advised that a significant amount of weight be given to the borrower's character, existing capacity, and collateral attachments in the appraisal. Credit officers and customers should be included in the creation of credit conditions, as loan interest rates have an impact on loan repayment and, consequently, the banks' performance.

2.2.2 Credit Appraisal on Loan Performance of Islamic Banks

Banking sector contributes significantly to economic growth and development (Baldina & Hendratmi, 2020), through credit extension. Commercial banks must extend loans to its customers in order to thrive and promote economic progress (Moti et al.,2018). Successful

implementation of lending guidelines affects financial performance and profitability, and hence may boost this income (Kenya Bankers Association, 2018). As a result, commercial banks create lending guidelines to help them when giving loans to their clients. Commercial banks' bottom lines benefit from lenders' adoption of innovative lending tactics that boost efficiency and streamline asset investment processes (Mburu, Mwangi & Muathe, 2020). The industrial revolution accelerated the pace of commercial and production activity, necessitating hefty capital outlays for projects, which is when lending methods as we know them today first emerged. At this time, many business leaders turned to the banks for help since they were unable to meet the rapid increase in financial demands (Cincinelli & Piatti, 2021). The procedures for making decisions that result in granting credit to a borrower still revolve around credit appraisal. (Nsengiyumva & Harelimana, 2020). Acceptance or rejection of a credit proposal is the primary goal of any credit evaluation. The process involves analysing the loan application to determine the applicant's repayment capacity (Sola, 2021).

For developing nations like Nigeria to accelerate and maintain their economic progress, a thriving microfinance sector is essential. To lower the risk of loan default, appropriate measures are needed for lending activities in this subsector. Sola (2021) investigated the relationship between performance of loans and credit control techniques. Effectiveness of the identified credit management measures was evaluated using primary data. The information came from the bank credit officers who were sampled responding to a research questionnaire. The associations between the variables were assessed using the ordinal logistic regression method. Customer assessment has a positive and substantial influence, whereas credit length and collection policy have favorable but non-substantial influence on performance of loan. Nigerian microfinance banks use client appraisal as a key component of their credit management approach to influence loan performance. It was advised that strict client appraisal procedures be followed by microfinance institutions in Nigeria while approving

loans. To help the banks conduct extensive client assessments, government need to establish an efficient Credit Information Reporting system about microfinance banking industry. This study was carried out in Nigeria, which has a jurisdiction difference with Somalia, hence a contextual gap to be filled.

Muhangi (2017) explored influence of loan evaluation process management on credit performance of Ugandan banks. Researcher utilized quantitative and qualitative techniques by administering questionnaires to a sample of 44 loan officers and credit managers. Banks largely depend on client appraisal for credit management. It proved that employing client appraisal as a means of reducing credit risk is a sound tactic. Research also discovered a significant correlation between client evaluation and bank credit performance. To improve their credit performance, financial institutions were advised to strengthen their client appraisal processes. Hence, there was conceptual gap to be closed because the proposed study focuses on loan performance while the previous study's dependent variable was credit performance.

Commercial banks are crucial to a country's economic development because they transfer funds from savers to lenders. Ndero, Wepukhulu, and Bogonko (2019) evaluated the connection between commercial banks' loan performance and their credit appraisal policies. The moral hazard hypothesis served as the study's foundation. The study's sample included all credit officers. For this investigation, a sample size of 128 people was selected. According to research findings, 78.1% of banks utilized the 5Cs credit assessment method, the credit-scoring model, and credit reference bureaus to conduct credit appraisals. Research also discovered a positive association between commercial banks' loan performance and credit ratings. Commercial banks should consider utilising the financial accounts of mobile phone companies to evaluate the cash flow of each borrower before approving a specific loan. The proposed study would be conducted in Mogadishu, Somalia, while the previous study

concentrated on commercial banks in a county in Kenya. Contextual and conceptual deficiencies are therefore displayed.

Abdirashid and Jagongo (2019) investigated the link between group lending and loan performance. The study had four main objectives: to determine whether or not credit policies regarding groups of loans affect loan outcomes; to analyze how group members' credit evaluation techniques affect their loans' profitability; to analyze how different group credit risk management methods affect loan performance. The work was anchored on group lending, the asymmetric information, and the portfolio theories. Descriptive research was used for this study. Sixty participants from Nairobi County made up the target population. The monitoring group consisted of credit managers and loan officers. Due to low population, a census was conducted in which every person in the study was included; as a result, all 60 respondents made up the study's sample size. Primary data were gathered for the study using a questionnaire. By pilot testing, the proposed questionnaire's reliability and validity were evaluated. Tables of frequency distributions, means, standard deviations, and measures of relative frequencies were all included in the descriptive statistics. Regression analysis, which will determine the association between variables, is a component of inferential statistics.

Abdirashid and Jagongo (2019) found a substantial association between the performance of loans at the microfinance and group internal rules, the credit evaluation process, credit policy, and credit risk control methods. In order to guarantee that members of sponsored organisations paid back loans on time, the research revealed that these organisations had put in place safeguards. Credit appraisal processes were used to inform lending to groups regarding the amount of credit for which the group qualified, its capacity to repay, and the type of security that would be required. Charges of this group loans determined whether or not the members effectively repaid loans, and the time frame given to the group to repay the loans determined the loan's terms. Microfinance institutions are urged to establish a credit risk

management team whose responsibility would be to ensure good governance within the organization and maintain stable interest rates charged by these institutions, as suggested by the research. Before agreeing to join a group loan, organizations should check to see whether its administration and managers are committed to sound governance practices. There is a contextual gap between Abdirashid and Jagongo (2019) focus on microfinance institutions and the proposed study's focus on Islamic banks.

Katula and Kiriinya (2018) examined SACCO loan repayment and financial performance. The precise goals were loan evaluation, loan interest rates, loan repayment methods, and impact of client characteristics on SACCO performance. Research used a descriptive research design and had 250 respondents as its target group. Secondary and primary data were employed in the investigation. Using surveys and the drop and pick later technique, primary data was collected. Reviewing already published resources, such as financial accounts and related empirical investigations, provided secondary data. Cronbach Alpha technique was utilized to examine study's reliability; all four of the variables' values exceeded the cutoff limit of 0.7, indicating that the study was reliable. At a 95% confidence level, multiple regression was performed. Tables and graphs were employed to show study's findings. Data analysis revealed a statistically significant relationship between the independent and dependent variables. This study concludes that achieving financial performance will be difficult until financial institutions adopt models of reducing financial risks including loan appraisal, loan interest rates, loan repayment processes, and client features models. According to the survey, financial institutions should investigate and modify their loan practises to promote timely payback. Conceptual gaps are presented via the study variables.

Understanding interest rates, one of the most important components of the financial environment, is essential for financing and investment decision-making in the changing financial environment of market participants.

Interest rates change based on whether you choose to lend money or borrow it. Banks charge interest on deposits in addition to the interest rates they lend at. Spread is the term used to describe their disparity. In the local and international money and capital markets, there is a similar disparity between the buying and selling rates.

Every industry needs sound credit management to remain stable and profitable, and reducing credit quality is a major common reason for poor financial performance and condition. Inadequate financial management of risks is the primary cause of many business failures. One of the main causes of bank failures is the credit risk management system's inability to adequately control the quality of loans. Omar, Muturi, and Samantar (2018) examined how credit management affects the financial performance. Research's primary objective was to assess how credit management procedures influenced profitability of telecommunications firms in Garowe. This research discovered that customer satisfaction and credit risk management play a substantial role in a firm's ability to remain profitable. It also discovered that the formulation and application of collection policies by companies has a favorable association with the success of the telecommunications firms in Garowe. To secure future customer loyalty, businesses should relax their stringent regulations for client assessments and credit collection. Line government officials should also monitor and develop policies on credit management practises.

2.2.3 Collection Policy on Loan Performance of Islamic Banks

Performance in regards to loan payback is crucial notion for all lending firms. It is a gauge of whether or not loans are completely repaid according to the loan arrangement. More loan repayment efficiency improves the bank's likelihood of gathering interest payments and lowers loan losses (Njeru, Mohhamed & Wachira, 2017). Lack of proper loan repayments, have an adverse effect on a firm's capital, earnings, and the potential to achieve its goals, and they can even cause a financial institution to fail. For instance, poor management of loan

repayment performance leads to losses and expensive management expenses for delinquencies (Muhangi, 2017). The increased costs are due to tighter oversight, more often portfolio reviews, and legal costs associated with pursuing substantially delinquent loans. Such expenses have a negative impact on the revenue earned and the lending institution's overall operations, making it financially unviable and thus unsustainable. Good credit standards and the removal of excess risk are achievable provided collection methods are carefully created, overseen from the top, and clearly known at all levels of the firm. A collection procedure is one of many that an organisation should implement to guarantee that credit management is carried out efficiently, as not all consumers pay their invoices to businesses on time (Omar, Muturi & Samantar, 2018).

Danstun and Harun (2019) investigated how Tanzanian microfinance institutions' portfolio at risk was affected by their credit collection policy. In Dar es Salaam, Morogoro, and Dodoma microfinance institutions were surveyed cross-sectionally. Sample of 219 participants from each of the three regions was collected via random sampling. To determine how these firms' at-risk portfolio is affected by their credit collection policies, multiple linear regression analysis was utilized. Findings indicate a correlation between microfinance institutions' portfolio at risk and the interest rates they charge. To improve the sustainability of their loan portfolios, this study advises these institutions to reevaluate interest rates they offer to their consumers. Also, grace periods for clients need to be improved by microfinance organizations. Establish effective loan product sizes that meet the requirements of various clients. This would promote and expand client repayments, improve financial results, and lower the portfolio risk of microfinance organizations.

Financial institutions in Kenya handle a large volume of non-performing loans. This propensity puts the institutions' viability and profitability at danger, which makes it more difficult for them to achieve their goals. Moti et al. (2018) examined how well credit

management practices affected the performance of lending in financial institutions. Aim of the research was to determine how loan performance was affected by credit conditions, client assessment, credit risk regulation methods, and credit collection policies. Participants were Meru town MFIs' credit officers. Repayment rates of loans were shown to be more affected by collection procedures.

Nsengiyumva and Harelimana (2020) examined how the financial performance of Rwanda's Umurenge SACCO were impacted by poor loan management. The research used a descriptive survey utilizing qualitative and quantitative techniques, with sample of 78 customers who had obtained more than double the loan amount. This was accomplished by using simple random sampling with a purpose. Data from primary and secondary sources were gathered and examined. According to the study, loan management factors such client evaluation, membership enrolment, credit risk management, and collection policies have an impact on financial performance. SACCO's financial success over the course of five years is significantly influenced by loan management procedures.

Halake, Rintari and Mutea (2021) investigated how Islamic auto financing arrangements affected financial performance. The research used a descriptive research strategy. Participants worked as loan officers and customer service representatives for the eleven commercial banks in Isiolo County. They were chosen by means of a census. Data collection methods included closed-ended questionnaires and secondary data. With the use of descriptive statistics, data was examined. In order to assess the study's hypothesis, multiple regression was performed. Research's final results were presented utilizing tables, graphs, and thorough explanations. Financial performance and options revealed a statistically significant association. The respondents concurred that a variety of clientele have been drawn in by the lending terms of Islamic auto financing. In contrast to other claims, participants did not agree that having a sharia committee oversee the disbursement of car loans had given customers confidence in the

loans. According to this, 74.3% of financial performance was contributed by Islamic car financing products. Financial performance was significantly impacted by Islamic auto financing arrangements. The respondents also disagreed that using a sharia committee to disburse car loans had given customers more confidence in those loans. Research demonstrated that customers' confidence in vehicle finance was linked to dependability as well as the nature and administration of the financing. Research was conducted in Kenya, presenting a contextual gap.

Muturi (2018) evaluated the impact of credit management strategies on loan repayment. The study used descriptive design. The research study specifically focused on deposit-taking financial institution workers. The workers were divided into three levels: upper level, medium level, and bottom level. Secondary data was collected from the library, Central Bank of Kenya records, and financial reports of microfinance institutions. Standard deviation and mean were among the statistical measures used to evaluate the original data. Multiple models of linear regression were used for further inferential statistics. To investigate how credit risk management strategies', affect loan repayment, models were used. A firm's performance is influenced by its credit criteria, credit policies, credit terms, and collection practices, among other factors. The study's findings indicate that credit management is a crucial function for every business. Stability and ongoing profitability of a financial institution depend on effective credit management. Financial institutions need to make sure that they embrace credit standards, credit policies, credit terms, and collection practises to a very great level.

2.3 Theoretical Frameworks

Moral hazard theory, theory of self-efficacy and information sharing theory were used in the study.

2.3.1 Moral Hazard Theory

This theory and how it relates to lending practises and information exchange among commercial banks serve as the foundation for this study. The Market for Lemons, a 1970 work by Akerlof that established the idea of quality ambiguity in financial studies, is where the theory of moral hazard first appeared (Wangari, 2017). Akerlof defines moral hazard as a risk factor that only becomes important after two parties have agreed upon and executed a financial contract. Ex post, one party to a contract may evaluate the result but not the means by which the other party arrived at that result. Furthermore, a contracting party is not permitted to determine whether the outcome is connected to what his contractual counterpart did, or if it's just the result of outside factors that are out of their control. The moral hazard argument contends that if there are no repercussions for this current credit application, a borrower will be motivated to default on the loan (Cincinelli & Piatti, 2017). When making loans, Islamic banks must deal with moral hazard problems. This happens when lender fails to recognize borrower actions that automatically affect probability that a loan will be repaid. Under this arrangement, borrowers pay back their loans since they are aware that defaulters will be blacklisted from receiving external financing in the future by credit reference agencies. Sharing credit information helps reduce moral hazard among borrowers and increases borrowers' motivation to repay their debts (Wangari,2017).

2.3.2 Theory of Self-Efficacy

The self-efficacy theory put out by Bandura (1995) serves as the intellectual underpinning for this investigation. Beliefs in one's capacity to plan and carry out the strategies needed to handle potential events. People's motives, efforts, and drive to overcome problems in life are influenced by their sense of self-efficacy. Those who have high self-efficacy are more likely to engage in endeavours they feel they can achieve in. It supports the idea that people have the

power to ameliorate and better their circumstances. The theory also recognises elements such as collective or group activities that have an impact on an individual's success or failure. To make sure that credit management is performed properly, a firm ought to employ a different measure. Since no customer ever pays their bill on time, the firms must have a collection procedure in place. Some clients take their time paying and others do not pay at all. Hence, collection effort should focus on speeding payments from reluctant borrowers and minimising bad debt losses (Bandura ,1995).

2.3.3 Information Sharing Theory

This theory was proposed by Brown, Jappelli and Pagano (2007). Disclosing information can cause either moral hazard or adverse selection in a market with asymmetric information. When moral hazard exists, sharing information may increase borrowers' incentives to perform since they no longer fear being held back by the lender-monopolist since the knowledge is now available to rival institutions. Debtors avoid defaulting since it would be bad for their reputation (Zaheer & Trkman, 2017). The disciplinary impact hazard or adverse selection occurs when borrowers' default information is made public, resulting in higher interest rates and less availability of financing from their present bank and other banks in the market. Because information is made public to rival banks in moral hazard scenarios, borrowers may have greater incentives to perform well because they are no longer concerned about being held back by the lender-monopolist. Borrowers may face higher interest rates and less access to credit from their present bank and other institutions in the market if default information is shared (Zaheer & Trkman, 2017).

Lenders would extend more credit to businesses and individuals if they could more accurately forecast whether or not their prospective clients would be able to pay it back. Therefore, the deeper the credit markets would be, the more banks would be aware of the credit histories of

potential borrowers. For the credit markets to become more complex, public or private credit registries that gather and provide financial institutions with extensive information on the repayment history of potential consumers are essential (Al-Husseini, 2021)). Financial institutions rely on lenders' voluntary information sharing, which frequently entails a tradeoff. Lenders profit from information sharing since it enables them to distinguish between qualified and unqualified loan applicants. Additionally, information exchange might reduce borrowers' moral hazard by encouraging them to put more effort into projects and repay loans (Zaheer& Trkman, 2017). On the other side, information sharing could expose lenders to more competition because it would mean disclosing sensitive client data. Therefore, in highly competitive lending markets, banks might be apprehensive of disclosing information. They might be especially wary of disclosing information to close rivals (Al-Husseini, 2021)). The concept is relevant to this research as it explains the critical role that customer's information sharing plays in the extension and subsequent repayment of loans.

2.4 Conceptual Framework

This is a set of interrelated hypotheses or assumptions regarding the nature of phenomena or the relationships among its component parts (Perry & Towers, 2018). The suggested connections may be better visualized with the help of a diagrammatic schematic description (Perry & Towers, 2018). It gives the foundation for understanding the observed links and their possible causes. This framework is presented in Figure 2.1

INDEPENDENT VARIABLE

DEPENDENT VARIABLE

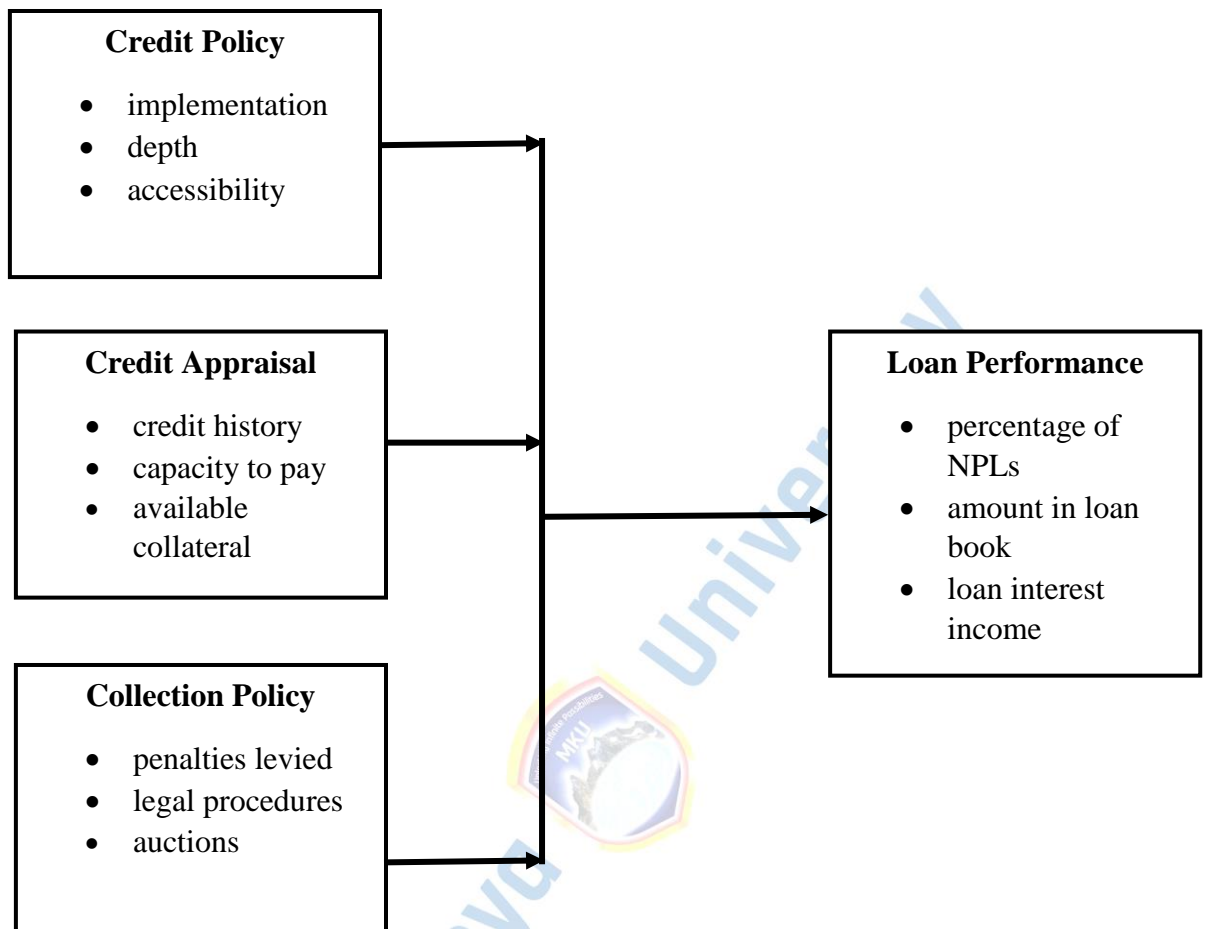


Figure 2.1: Conceptual Framework

Source: Researcher (2024)

Credit policy indicators include depth, accessibility and implementation of the policies. Indicators for credit appraisal include availability of collateral, capacity to pay and credit history. Collection policy indicators include auctions, legal procedures and penalties levied. Loan performance, the dependent variable is measured by percentage of NPLs loan book amount and loan interest income.

2.5 Recap of Literature Review

Prior researches present knowledge gaps, which the present research tries to fill. Akram and Rahman (2018) evaluated Pakistani Islamic banks' credit management issue. Credit

management was positively and significantly impacted by loan quality. Credit management was negatively impacted by asset quality. The study presents a conceptual gap as the variables were loan quality, asset quality and credit management.

Baldina and Hendratmi (2020) looked into how supply chain management affected the relationships between performance of Islamic banks in Indonesia and ties between credit quality, strong ties, and bridge ties. These findings provide policymakers who create regulations relating to the supply chain and company performance appropriate justification for future research into this topic. Cincinelli and Piatti (2021) looked into the physiological credit risk that results from ineffective screening and management processes. Results indicated a connection between rise in NPLs and severe and protracted recession.

Abimbola (2020) looked into how Nigerian money deposit banks fared in relation to NPLs. Findings showed that performance of this banks is impacted by non-performing loans. There is a knowledge vacuum because Other aspects, such credit evaluation and credit collection, were not taken into consideration in their research. Study's focus on commercial banks revealed a conceptual hole that the current study will remedy. Macharia and Mungai (2021) assessed impact of Kenyan commercial banks' loan performance on their policy for sharing credit information. Results showed that NPLs increased substantially even after execution of the credit information sharing policy. This study focused on commercial banks, presenting a conceptual gap, to be filled with the current study.

Sola (2021) investigated the relationship between loan performance and credit management techniques. Nigeria and Somalia have different legal systems. Muhangi (2017) examined the impact of managing the loan appraisal process. It proved that using client appraisal as a means of reducing credit risk is a sound tactic. Research also indicated a substantial link between bank credit performance and client evaluation. Research's dependent variable was credit

performance while the proposed research focuses on performance of loans, hence a conceptual gap to be filled.

Ndero, Wepukhulu, and Bogonko (2019) evaluated the association between commercial banks' loan performance and their credit appraisal policies. The proposed study would be conducted in Mogadishu, Somalia, while the previous study concentrated on commercial banks in a county in Kenya. Contextual and conceptual deficiencies are therefore presented. There is a contextual gap between Abdirashid and Jagongo (2019) focus on microfinance institutions and the proposed study's focus on Islamic banks. Halake, Rintari, and Mutea (2021) investigated how Islamic auto financing arrangements affected financial performance. Financial performance and options revealed a statistically significant association. The respondents concurred that a variety of clientele have been drawn in by the Islamic auto financing's lending terms. The study was carried out in Kenya, presenting a contextual gap.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This section provides a thorough explanation of the methodology used in the study. This section describes the research methods used for this study. This research explains the research design that was used for the investigation. Details on how a sample was chosen from the target population to take part in the study are also highlighted, along with information about the target population. Along with the methods utilized to conduct this study, the tools that were used for data collecting are also outlined. The methods used to examine the data are covered in the chapter's later sections. The ethical issues that persisted throughout the procedure are addressed in the chapter's conclusion.

3.2 Research Design

It entails methodical approach a researcher uses when performing scientific investigations (Abutabenjeh & Jaradat, 2018). The questionnaire was closed-ended; therefore, liker scales may be used to obtain quantitative data. Increasing the quality and utility of research necessitates familiarity with complementary research approaches in today's complex, rapidly evolving research environment.

3.3 Target Population

The study was carried out in Mogadishu, Somalia in the 3 largest commercial banks. Thus, study's populations were the three Islamic commercial banks of Amal Bank, Salam Bank and Dahabshil Bank. The total number of employees in the credit departments of the three banks was 72. The distribution is as illustrated in Table 1: -

Table 3.1: Target Population

Bank	Population
Amal Bank	23
Salam Bank	21
Dahabshil Bank	28
Total	72

Source : Amal bank (2024), Salam bank (2024) and Dahabshil bank(2024)

3.4 Sampling procedures and techniques

Although it would be difficult to poll a very big population individually, Kendra (2018) pointed out that sample is a selection of data from a larger population meant to be indicative of that population as a whole. The determining factor of the unit of analysis is the size of the research population. If population is small ($N < 100$), unit of analysis ought to include every member of the study population. This study did a census survey, wherein the entire target populations were the respondents. This is because the study's target group was manageable, small, and easily accessible. The census study was chosen because, by removing both sample bias and error, it improves the generalization of results to the study population.

3.5 Sample Population

The study was a census for all the 72 employees working in the credit departments of Amal Bank, Salam Bank and Dahabshil Bank in Mogadishu, Somalia.

3.6 Construction of Research Instruments

Data for the study we recollected via questionnaire administration to the study respondents. Questionnaire serves as the primary source of information. There are drawbacks using a

questionnaire, such as the time commitment (Stefan, 2019). Planning ahead and outlining the study's objectives to participants can help alleviate this issue. Researcher offered guidelines on how to fill the questionnaires to the participants. In order to maintain their anonymity, participants will not be asked to write their names anywhere on the surveys. The questionnaires had five parts, containing liker ratings and demographic information for every research variable. To promote candor, the researcher reassured participants that there is no risk associated with their participation in the study. The questionnaires collected quantitative information on credit policy, credit appraisal and collection policy on performance of loans in Islamic banks in Mogadishu Somalia.

3.7 Testing for Validity and Reliability

Daryeel Bank Limited served as the site of this study's pilot test. A sample of 7 participants were involved in pilot test. 10% of the sample anticipated for the parent study should comprise the pilot sample.

3.7.1 Validity

Instrument validity describes how well an instrument for collecting data yields predictable results (Sürücü & Maslakçi, 2020). Construct, content, and criterion validity were used to assess the reliability of the data collecting methods. Construct validity was used to check whether the instruments really measure the ideas they claim to. The ways in which Islamic banks create their credit policies, credit appraisals, and collection policies regarding loan performance in Mogadishu Somalia were constructed, and the indicators and measurements of the variables tested throughout the pilot project, to verify construct validity. Only relevant questions that examined the indicators of study variables were involved in the questionnaire. Content validity focused on testing how well the instruments reflect the target populations for the research questions. The instruments were modified by removing superfluous questions

from the pilot research and replacing them with more pertinent ones. Last but not least, criteria validity assessed the reliability of several instruments during pilot testing. Correlation analysis recorded how well different instruments in the pilot research correlate with one another. The instruments were given to the supervisor for additional inspection for any potential gaps. These were then filled by the researcher.

3.7.2 Reliability

Mohajan (2017) reliability of instruments is expressed as the degree to which they consistently measure the target variables. In other words, the instrument should be able to consistently provide the same findings, or very close to them, when used to conduct the same test. The reliability of the instruments was determined using test-retest and internal consistency metrics during pilot testing. The reliability between administrations were measured using test-retest, and within-instrument reliability were measured using internal consistency. A reliability value of 0.872 was achieved. An efficient Cronbach's Alpha is defined as a value of 0.7 or above (Segal and Coolidge ,2018).

3.8 Data Collection Methods and Procedures

Once the instruments had been successfully validated, the researcher started collecting data. The administration of the questionnaire was in person. The researcher made a pre-visit to the three commercial banks to seek authority and audience with the managers. During the meeting, the objectives of the study were explained and dates for actual questionnaire distribution was agreed. On the agreed dates, the researcher visited each of the commercial banks. Research's goals were conveyed to respondents. Those who joined the research were given questionnaires to fill out and given their undivided attention. Researcher helped participants who had difficulties completing questionnaire. Questionnaires were thereafter collected and their accuracy ascertained.

3.9 Proposed Data Analysis Techniques and Procedures

Editing, coding, and tabulating data was necessary for data cleaning. This was done to search for any anomalies in the responses and assign a numerical number to each in preparation for further examination. The analyses used statistical package for social sciences. Data was evaluated utilizing descriptive statistics, like frequencies and percentages. Multiple and simple linear regression analysis we reemployed to examine quantitative data that will be gathered and coded. This were applied to determine how the variables are related. The association between the variables were determined using regression analysis at a 0.05 significant level. The below multiple regression model was adopted:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \varepsilon$$

Where:

Y is performance of loan performance

β_0 is a constant

$(\beta_i; i=1, 2, 3, 4)$ are the Beta coefficients of independent variables

X_1 is credit policy

X_2 is credit appraisal

X_3 is collection policy

ε is the error term

Study results will be revealed in graphs and tables.

3.10 Ethical Consideration

Researcher sought permission from University and NACOSTI. Permission to gather data from participants was obtained from the management of the three commercial banks. Consent from the respondents to take part in the study was requested. No respondent was exposed to harm, allowed to disclose their personal information or coerced to participate in the study. The participants were assured of no risk of participation.



CHAPTER FOUR

RESEARCH FINDINGS AND DISCUSSIONS

4.1 Introduction

The study analyzed the influence of credit management practices on loan performance of Islamic banks in Mogadishu Somalia. This chapter presents demographics, descriptive statistics, inferential statistics, thematic analysis, interpretations and discussions. Consequently, the chapter analyses data collected as per the objectives; that is, to: credit policy, credit appraisal and collection policy on loan performance of Islamic banks in Mogadishu Somalia. Frequency, inferential statistics, such as ANOVA was employed to assess the significance of the variables. Multiple regression and correlation coefficients were used to identify association between variables, as per the research objectives. SPSS software was used for quantitative data analysis.

4.2 Response rate

The study issued 72 questionnaires to employees in the credit department in three Islamic commercial banks of Amal Bank, Salam Bank and Dahabshil Bank, out of which 70 were completed and returned; hence was a response rate of 97%. Wu, Zhao and Aime (2022), pointed out that survey researchers often grapple with low response rates, seldom exceeding 50%. The authors suggest that a response rate of 50% and above is satisfactory and provides a solid foundation for data analysis. Sammut, Griscti and Norman (2021) advise that a 50% response rate is sufficient, 60% is good and an exceedance of 70% is very good. López (2023) maintains that a response rate of 70% is excellent. Furthermore, Shiyab, Ferguson, Rolls and Halcomb (2023) affirm that response rates of 50% and above are acceptable for analysis. Consequently, the study's response rate of 97% was ideal, satisfactory and reliable. The response rate is as per Table 4.1 :-

Table 4.1 : Response rate

Bank	Sample	Responses	Response rate
Amal Bank	23	22	96%
Salam Bank	21	20	95%
Dahabshil Bank	28	28	100%
Total	72	70	97%

Source: Research Data

4.3 Reliability results

The study conducted a pilot test to ascertain the reliability of the research instruments. The pilot respondents were given questionnaires to complete, and the researcher explained the objectives to them. The reliability results from the pilot research are indicated in Table 4.2.

Table 4.2 : Reliability results

Variable	Item	Alpha Value	Recommendations
Credit policy	5	0.887	Reliable
Credit appraisal	5	0.893	Reliable
Collection policy	5	0.882	Reliable
Loan performance	5	0.826	Reliable

Source: Research Data

The Cronbach Alpha Coefficient was calculated for each variable. Coefficient for loan performance was 0.826, credit policy was 0.887, credit appraisal was 0.893 and credit policy was 0.882. All the variables had reliability values higher than 0.7, which was adequate.

4.4 Validity tests

Validity testing for the questionnaire were carried out by the study. By requesting the expert guidance of the university supervisor, the research's instrument validity was attained. After receiving sufficient guidance from the supervisors, the questionnaire was reviewed, updated,

and approved. Data from the questionnaire accurately addressed the research topics of the study.

4.5 Demographic data

The study assessed demographic data of the respondents. These included gender, age, education, rank and experience.

4.5.1 Gender

Results indicated the distribution of gender in that 42 (60%) were male while 28 (40%) were female. Hence most of the respondents were male. This is illustrated in table 4.3: -

Table 4.3: Gender

Gender	Frequency	Percent
Male	42	60
Female	28	40
Total	70	100

Source: Research Data

4.5.2 Age

Findings indicated that 15 (21%) of the respondents were aged 18-25, 36,(51%) were aged 26-35, 18 (26%) were aged 36-45 and 1 (1%) was aged between 46-55. The majority were between the age bracket of 26-35. It was a fair distribution as showed in Figure 4.1: -

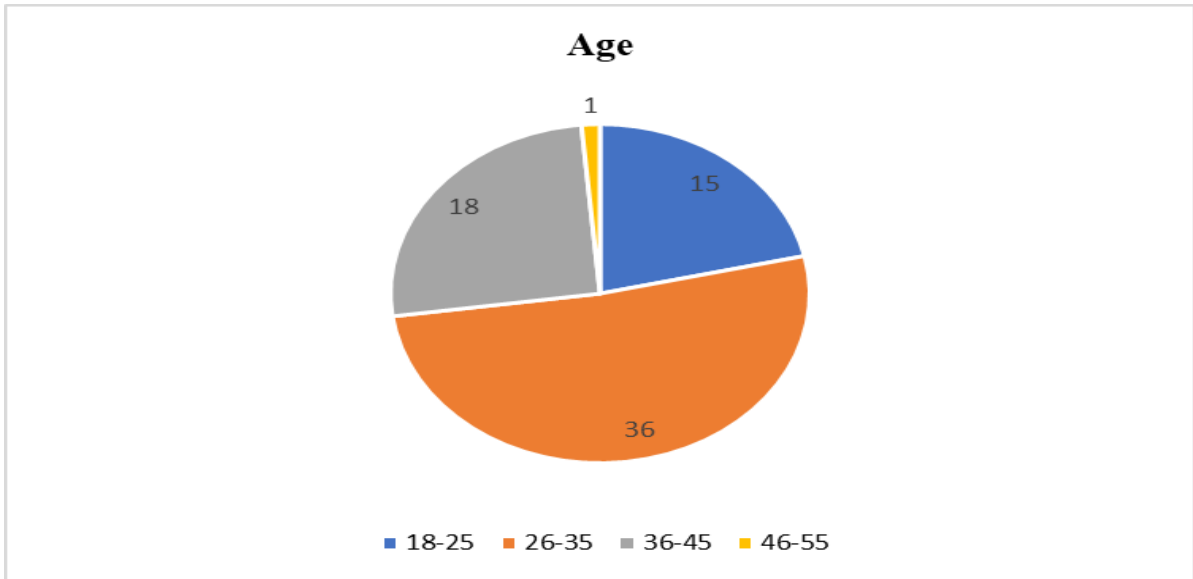


Figure 4.1 : Age of the respondents

4.5.3 Education

The study indicated education level such that diploma was 3(4%), bachelors was 57(81%) and masters was 10(14%). Most of the respondents had bachelor's degree, hence their responses could be relied for analysis. This is illustrated in table 4.5: -

Table 4.5 Education

Education	Frequency	Percent
Diploma	3	4
Bachelors	57	81
Masters	10	14
Total	70	100

Source: Research Data

4.5.4 Rank

The study showed credit officers were 55(79%), supervisors were 13(19%) and managers were 2(3%). Most of the staff was credit officers. This is indicated in table 4.6: -

Table 4.6 Rank

Rank	Frequency	Percent
Credit officer	55	79
Supervisor	13	19
Manager	2	3
Total	70	100

Source: Research Data

4.5.5 Work experience

The findings indicated that 59(84%) had 1-4 years of experience, 8(11%) had 5-9 and 3(4%) had 10-14 years of experience. Most of the employees had 1-4 years' experience. This is showed in Figure 4.2: -

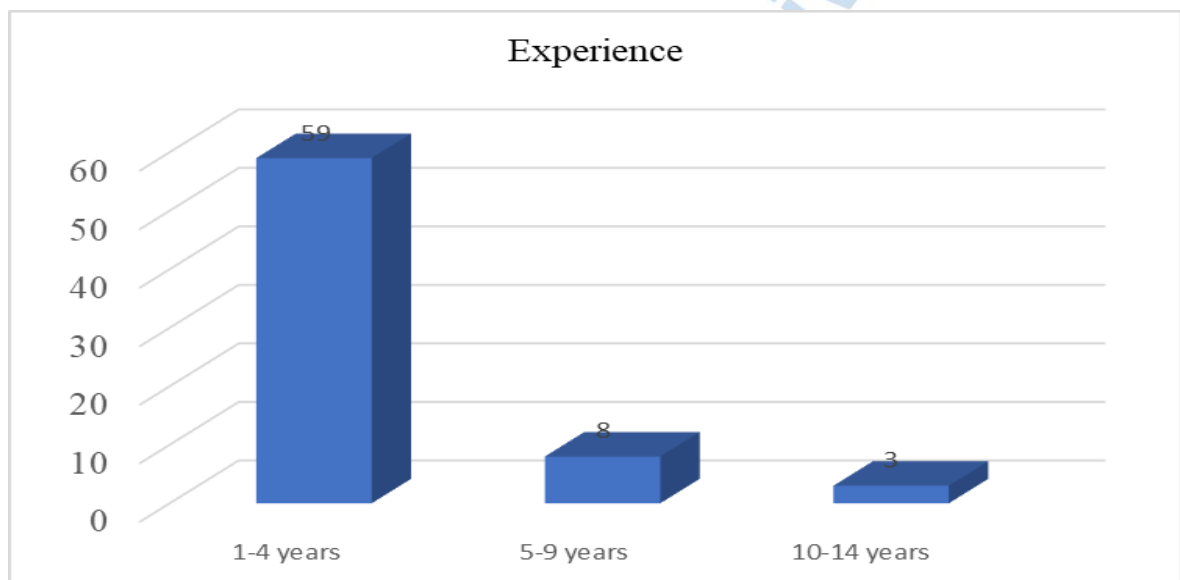


Figure 4.2 : Work experience of the respondents

4.6 Descriptive analysis

This section presents descriptive statistics used by the researcher to establish the main findings drawn from the research and draw conclusions. The analyses are related to the investigation of how credit management techniques affect Islamic banks' loan performance in Mogadishu, Somalia. The analysis is presented as per the research objectives that is: to credit policy, credit appraisal and collection policy on loan performance of Islamic banks in Mogadishu Somalia.

4.6.1 Credit policy on loan performance

The first objective evaluated the influence of credit policy on loan performance of Islamic banks in Mogadishu Somalia. Respondents were asked five questions regarding the effect of credit policies on the loan efficiency of Islamic banks in Mogadishu Somalia. The responses were presented on a likert scale. The study participants' responses are summarized and presented in Table 4.8. Out of 70 respondents 4% of them agreed, 11% of the members were not sure, 57% disagreed and the remaining 27% strongly disagreed that the bank had an elaborate credit policy (Mean=1.93, SD =0.748). However, 4% of the participants agreed that the bank's credit policy was effectively implemented, 7% were not sure, 50% disagreed and 39% strongly disagreed (Mean=1.77; Dev=0.765). Four percent of the respondents agreed that the credit policy was accessible to all staff, 3% were not sure, 49% disagreed and 44% strongly disagreed (Mean=1.67; SD=0.737). Additionally, 3% agreed that the credit policy outlined discounts allowable to customers, 1% were not sure, 40% disagreed and the remaining 56% strongly disagreed (Mean=1.51; SD=0.676). Lastly, 1% agreed that the credit policy was reviewed periodically, 4% were not sure, 49% disagreed and 46% strongly disagreed (Mean=1.61; SD=0.644).

Table 4.8 : Credit policy on loan performance

Statement	N	Mean	Std.					SD
			Deviation	SA	A	NS	D	
The bank has an elaborate credit policy.	70	1.93	0.748	0	4	11	57	27
The bank's credit policy is effectively implemented.	70	1.77	0.765	0	4	7	50	39
The credit policy is accessible to all staff.	70	1.67	0.737	0	4	3	49	44
The credit policy outlines discounts allowable to customers.	70	1.51	0.676	0	3	1	40	56
The credit policy is reviewed periodically.	70	1.61	0.644	0	1	4	49	46

Source: Research Data

4.6.2 Credit appraisal on loan performance

The second objective evaluated the influence of credit appraisal on loan performance of Islamic banks in Mogadishu Somalia. Respondents were asked five questions regarding The effect of credit evaluation on Islamic banks' loan performance in Mogadishu, Somalia. The responses were presented on a likert scale. The study participants' responses are summarized and presented in Table 4.9. Out of 70 respondents 4% agreed that the bank obtained borrowers' credit history from other financial institutions,6% were not sure,59% disagreed and 31% strongly disagreed (Mean=1.83; SD=0.722).Borrowers' financial net worth was assessed by the bank in such that 4% agreed,6% were not sure,46% disagreed and the remaining 44% strongly disagreed (Mean=1.70; SD=0.768). Also,6% agreed that the integrity of the borrowed was assessed before loaning,4% were not sure,60% disagreed and 30% strongly disagreed (Mean=1.86; SD=0.748). Four percent of the population agreed that the ability of a borrower to repay form owned

sources was appraised ,4% were not sure,53% disagreed while the remaining 39% strongly disagreed (Mean=1.74; SD=0.736). Nevertheless, 3% agreed that the collateral was part of the appraisal process before loaning borrowers.,7% were not sure,47% disagreed and 43 % strongly disagreed (Mean=1.70; SD=0.729).

Table 4.9 : Credit appraisal on loan performance

Statement	N	Mean	Std.					SD
			Deviation	SA	A	NS	D	
The bank obtains borrowers' credit history from other financial institutions.	70	1.83	0.722	0	4	6	59	31
Borrowers' financial net worth is assessed by the bank.	70	1.70	0.768	0	4	6	46	44
The integrity of the borrow is assessed before loaning.	70	1.86	0.748	0	6	4	60	30
The ability of a borrower to repay from own sources is appraised.	70	1.74	0.736	0	4	4	53	39
Collateral is part of the appraisal process before loaning borrowers.	70	1.70	0.729	0	3	7	47	43

Source: Research Data

4.6.3 Collection policy on loan performance

The third objective evaluated the influence of collection policy on loan performance of Islamic banks in Mogadishu Somalia. Respondents were asked five questions regarding The influence of collection policies on Islamic banks' loan performance in Mogadishu,

Somalia. The responses were presented on a likert scale. The study participants' responses are summarized and presented in Table 4.10. Out of 70 respondents, 4% agreed that the bank maintained strict deadlines in collection of debt, 3% were not sure, 33% disagreed and 60% strongly disagreed (Mean=1.51; SD=0.756). One percent agreed that the borrowers are slapped with penalties on loan defaults, 6% were not sure, 54% disagreed and the remaining 39% strongly disagreed (Mean=1.70; SD=0.645). Notably, 4% agreed that the customers properties were auctioned on loan default, 43% disagreed and 53% strongly disagreed (Mean=1.56; SD=0.715). Four percent agreed that the bank employed legal means to recover debt from loanees, 7% were not sure, 54% disagreed and 35% strongly disagreed (Mean=1.81; SD=0.748). Lastly, 3% agreed, 3% were not sure, 47% disagreed and 47% strongly disagreed (Mean=1.61; SD=0.687).

Table 4.10 : Collection policy on loan performance

Statement	N	Mean	Std. Deviation	Std.				
				SA	A	NS	D	SD
The bank maintains strict deadlines in collection of debt.	70	1.51	0.756	0	4	3	33	60
Borrowers are slapped with penalties on loan defaults.	70	1.70	0.645	0	1	6	54	39
Customers properties are auctioned on loan default.	70	1.56	0.715	0	4	0	43	53
The bank employs legal means to recover debt from loanees.	70	1.81	0.748	0	4	7	54	35
Customers' loan file is continuously reviewed	70	1.61	0.687	0	3	3	47	47

and updated.

Source: Research Data

4.6.4 Loan performance

The purpose of the study is to investigate how Islamic banks in Mogadishu, Somalia, perform when they issue loans by looking at their credit management techniques. Respondents were asked five questions and responses were presented on a likert scale. The study participants' responses are summarized and presented in Table 4.11. Out of 70 respondents, 6% agreed that the non-performing loans had reduced, 6% were not sure, 66% disagreed and 22% strongly disagreed (Mean=1.94; SD=0.720). Moreover, 4% agreed that the banks' loan booked had increased, 6% were not sure, 47% disagreed and 43% strongly disagreed (Mean=1.71; SD=0.764). Six percent agreed that the active loanees had increased. 3% were not sure, 60% disagreed and 31% strongly disagreed (Mean=1.83; SD=0.742). Four percent agreed that the bank's profitability had increased, 4% were not sure, 54% disagreed and 38% strongly disagreed (Mean=1.76; SD=0.731). Lastly, 3% agreed that the loan repayments were timely. 3% were not sure, 47% disagreed and 47% strongly disagreed (Mean=1.61; SD=0.687).

Table 4.11 : Loan performance

Statement	N	Mean	Std.		SA	A	NS	D	SD
			Deviation						
Non-performing loans have reduced.	70	1.94	0.720		0	6	6	66	22
The banks' loan booked has increased.	70	1.71	0.764		0	4	6	47	43
Active loanees have increased.	70	1.83	0.742		0	6	3	60	31
The bank's profitability has increased.	70	1.76	0.731		0	4	4	54	38
Loan repayments is timely.	70	1.61	0.687		0	3	3	47	47

Source: Research Data**4.7 Inferential analysis**

Correlation analysis was done in the study. These demonstrated the relationship between the research variables.

4.7.1 Correlation analysis

Pearson correlation analysis was carried out and results illustrated in Table 4.12

Table 4.12 : Correlation analysis

		loan performance	credit policy	credit appraisal	collection policy
loan performance	Pearson Correlation	1	.882**	.824**	.747**
	Sig. (2-tailed)		0.000	0.000	0.000
	N	70	70	70	70

credit policy	Pearson	.882**	1	.846**	.700**
	Correlation				
	Sig. (2-tailed)	0.000		0.000	0.000
	N	70	70	70	70
credit appraisal	Pearson	.824**	.846**	1	.586**
	Correlation				
	Sig. (2-tailed)	0.000	0.000		0.000
	N	70	70	70	70
collection policy	Pearson	.747**	.700**	.586**	1
	Correlation				
	Sig. (2-tailed)	0.000	0.000	0.000	
	N	70	70	70	70

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

Source: Research Data

The research findings highlight correlations between variables and the performance of the banks. These relationships' relevance is established by p-values. In this context, ($p < 0.05$) is regarded substantially significant, while values above 0.05 are regarded as insignificant. The results exhibited a strong correlation ($r=0.882$, $p=0.000$), indicating a significant link between credit policy on loan performance of Islamic banks in Mogadishu Somalia. Effective credit management is a pivotal aspect of financial success, particularly when expanding into new markets and cultivating a broader client base. The ability to make sound credit decisions and establish favorable credit lines ensures a healthy cash flow and sustainable growth. Credit control, initiating at the point of sale, is a continuous process until complete payment is received (Muhammad, Alwi & Muhammad, 2020). Development of an optimal credit policy involves a balance of various factors, presenting a challenge in design. Islamic banks, serving

as intermediaries between entities with excess funds and those in need, heavily align their lending strategies with prevailing economic conditions (Akram & Rahman, 2018). The core objectives of Islamic banks include achieving profitability, fostering asset growth, and expanding their customer base (Abimbola, 2020). To fulfill these goals, Islamic banks provide advances and loans to people, companies, and governments. However, there are dangers associated with the financing environment. Poor asset quality and a high prevalence of non-performing risk assets can lead to widespread loan defaults, resulting in substantial losses and diminished Islamic banks profitability. Thus, managing credit risk is paramount in maintaining a healthy financial institution. Comprehension of economic conditions, effective credit policies and proactive risk management are imperative for Islamic banks to navigate these challenges successfully. Similarly, the study found a strong and favorable correlation between Islamic banks' loan performance and their credit evaluation in Mogadishu, Somalia. ($r=0.824$, $p=0.000$). In any industry, the importance of sound credit management cannot be overstated, as it serves as a linchpin for stability and profitability. A significant contributor to poor financial performance and condition is the erosion of credit quality, with numerous business failures attributable to insufficient handling of credit risk. The weakness in the credit risk management system of Islamic banks when it comes to monitoring loan quality is a recurrent factor in banking failures, emphasizing the critical role of effective credit management in maintaining the robustness of financial institutions. Credit appraisal stands is a crucial component for Islamic banks (Baldina & Hendratmi, 2020). The success of Islamic banks in extending loans to customers is pivotal for its thriving existence and fostering economic development (Moti et al., 2018). The implementation of effective lending guidelines is critical; influencing not only the financial performance and profitability of the Islamic banks but also contributing to the overall economic environment (Kenya Bankers Association, 2018). The adoption of innovative lending tactics plays a transformative role in

the financial success of Islamic banks. As emphasized by Mburu, Mwangi, and Muathe (2020), commercial banks benefit substantially from the implementation of these tactics, which enhance efficiency and streamline asset investment processes. The creation and adherence to lending guidelines become instrumental in ensuring that Loans are given out carefully, Reducing the possibility of defaults and consequently contributing to the bottom line of Islamic banks.

Results show a significant and favorable relationship between Islamic banks' loan performance and their collection policies. in Mogadishu Somalia ($r=0.747$, $p=0.000$), The timely repayment of loans is not just a procedural requirement for lending firms; it serves as a critical indicator of financial health and stability. Efficient loan repayment is a litmus test for adherence to agreed-upon terms and conditions, directly impacting Islamic banks' ability to collect interest payments while mitigating loan losses (Njeru, Mohhamed & Wachira, 2017). The significance of proper loan repayments extends beyond the immediate financial transaction; it profoundly influences a firm's capital, earnings and its overall ability to achieve strategic objectives. Furthermore, a failure to manage loan repayment performance can escalate into severe consequences, even leading to the failure of a financial institution. Ineffective management of loan repayment performance not only results in financial losses but also incurs substantial operational expenses associated with handling delinquencies (Muhangi, 2017). The increased costs stem from better oversight, more frequent portfolio reviews and legal expenses incurred in pursuing substantially delinquent loans. These expenses, in turn, adversely affects the revenue generated and the overall operational efficiency of Islamic banks, rendering them financially unviable and unsustainable in the long run. Establishing and adhering to good credit standards while minimizing excess risk is achievable through well-crafted collection methods. A robust collection policy, when carefully designed, overseen from the top, and clearly communicated across all levels of the

firm, plays a pivotal role in ensuring efficient credit management (Omar, Muturi & Samantar, 2018). Such policies become imperative as not all consumers adhere to timely payment of invoices, and for lending institutions to remain solvent and financially stable, a methodical approach to collections is necessary. The efficacy of loan repayment processes is a linchpin for the overall success and viability of Islamic banks.

4.7.2 Linear regression model

A regression analysis was done to examine the relationship between the independent and dependent variables. An overview of the linear regression model is shown in Table 4.13

Table 4.13 : Model summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.913 ^a	0.833	0.826	0.20454	1.868

a. Predictors: (Constant), collection policy, credit appraisal, credit policy
b. Dependent Variable: loan performance

Source: Research Data

Results reveal that r square is 0.833 that is, 83.3%. This means that performance of Islamic banks in Mogadishu Somalia would vary by 83.3% due to changes in credit policy, credit appraisal and collection policy, at 95% confidence level. Only 16.7% of the variations in performance of the banks can be ascribed to additional influencing factors. The correlation coefficient, denoted as R, evaluates the connection between different variables. The variables had a strong and positive association, according to the findings., evident by a correlation coefficient of 0.913. With a Durbin Watson statistic of 1.868, it can be inferred that no autocorrelation exists among the variables.

Table 4.14 ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	13.822	3	4.607	110.128	.000 ^b
	Residual	2.761	66	0.042		
	Total	16.583	69			

a. Dependent Variable: loan performance

b. Predictors: (Constant), collection policy, credit appraisal, credit policy

Source: Research Data

ANOVA results exhibited a level of significance at 0.000, hence a significant relationship between the dependent and independent variables. The calculated F-value was observed to be greater than the critical F-value ($110.128 > 2.736$). As a result, the model used in the research is reliable. Consequently, the results are sufficient to draw firm conclusions and make reliable recommendations.

Table 4.15: Coefficients

	Unstandardized Coefficients	Standardized Coefficients	t	Sig.	VIF
(Constant)	-0.111		-1.034	0.305	
credit policy	0.537	0.465	4.359	0.000	4.517
credit appraisal	0.276	0.279	2.970	0.004	3.509
collection policy	0.295	0.258	3.666	0.000	1.961

a. Dependent Variable: loan performance

Source: Research Data

Table 15 shows the model equation to be:

$$Y = -0.111 + 0.465 X_1 + 0.279 X_2 + 0.258 X_3 + \varepsilon$$

Results showed that Islamic banks' loan performance and credit policy were related is positive and significant ($\beta = 0.465$, $p < 0.05$).The results align with those of Abimbola (2020),who evaluated how Nigerian money deposit banks fared in relation to non-performing loans. Findings showed that performance of banks is impacted by non-performing loans. The report suggests adopting an efficient credit policy that includes variable tenure, renegotiating lending conditions, and conversion. This strategy might slow the rate of NPLs, which might lower the risk of default as return on equity increase. Additionally, Mburu, Mwangi and Muathe (2020) examined the effects of credit management strategies on the performance of loans. The study concluded that the banks' loan success may be mostly attributable to how well their credit management practices worked. It was suggested that these institutions continuously assess and enhance their client evaluation policies, debt collection policy, and lending policy in order to make sure that credit risks are detected and recorded from the level of the department to the firm as a whole. This is crucial to banking industry technological advancements like mobile lending that could hinder banks' capacity to assess and regulate loans utilizing conventional ways. Research focused on commercial banks, presenting a conceptual gap, to be filled with the current study. Njeru et al. (2017) explored the relationship between Kenyan commercial banks' credit management system efficacy and loan performance. Similar to how credit appraisal was found to have a significant influence on the performance of commercial banks, the study found that credit terms also have an effect on performance. It was revealed that a strict policy has a much bigger impact on performance than a lax policy. It was advised that a significant amount of weight be given to the borrower's character, existing capacity, and collateral attachments in the appraisal. Credit officers and customers should be included in the creation of credit conditions, since interest rates on loans affect loan repayment and, by extension, the performance of these banks.

The findings showed a positive and significant relationship between Islamic banks' loan performance and credit appraisal. ($\beta = 0.279$, $p < 0.05$). These results agree with those of Sola (2021), who explored the relationship between loan performance and credit management techniques. Customer assessment had a positive influence, whereas credit length and collection policy have favorable but non-substantial influence on performance of loan. Muhangi (2017) explored influence of loan evaluation process management on the credit performance of Ugandan banks and observed that using client appraisal to lower credit risk is crucial. Research also discovered a significant correlation between client evaluation and bank credit performance. To improve their credit performance, financial institutions were advised to strengthen their client appraisal processes. In the same breadth, Ndero, Wepukhulu and Bogonko (2019) evaluated the connection between commercial banks' loan performance and their credit appraisal policies. There was a positive association between commercial banks' loan performance and credit ratings. Commercial banks should consider utilising the financial accounts of mobile phone companies to evaluate the cash flow of each borrower before approving a specific loan. Likewise, Abdirashid and Jagongo (2019) found a substantial association between the performance of loans at the microfinance and group internal rules, the credit evaluation process, credit policy, and credit risk control methods.

Findings revealed that the association between collection policy and loan performance of Islamic banks is positive and significant ($\beta = 0.258$, $p < 0.05$). These findings corroborate those of Danstun and Harun (2019), who investigated how Tanzanian microfinance institutions' portfolio at risk was affected by their credit collection policy. Findings indicated a correlation between microfinance institutions' portfolio at risk and the interest rates they charge. Nsengiyumva and Harelimana (2020) examined how the financial performance of Rwanda's Umurenge SACCO were impacted by poor loan management. According to the study, loan management factors such client evaluation, membership enrolment, credit risk

management, and collection policies have an impact on financial performance. SACCOs financial success over the course of five years is significantly influenced by loan management procedures. Likewise, Halake, Rintari and Mutea (2021) investigated how Islamic auto financing arrangements affected financial performance. Financial performance and collection policy revealed a statistically significant association. Financial performance was significantly impacted by Islamic auto financing arrangements. The respondents also disagreed that using a sharia committee to disburse car loans had given customers more confidence in those loans. Additionally, Muturi (2018) assessed how credit management techniques affect loan repayment. Credit standards, credit policies, credit terms, and collection practises all had an impact on how well a firm performs.



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CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

Credit management is vital for a bank's loan book and overall performance. Loan portfolios are a significant asset and income source for banks, impacting their stability and success (Abdullah et al.,2020). Effective credit management ensures industry stability through monitoring and efficiency (Pradyut, 2019). A client's characteristics and external factors determine loan repayment. Credit management practices influence loan effectiveness (Nsengiyumva & Harelimana, 2020). Regulations like collection policy and credit terms affect loan performance. Overall, credit management is crucial for a bank's success and the stability of the industry (Pradyut, 2019). This chapter provides an overview of how credit management techniques affect Islamic banks' loan performance in Mogadishu, Somalia, is given in this chapter. In addition, the implications derived from these study results are examined. There are also suggestions for academia and practice.

5.2 Summary of the result findings

This section is presented in consistent with the objectives of the study, they aim to assess how credit policy affects Islamic banks' lending performance in Mogadishu Somalia, to investigate the impact of credit appraisal on loan performance of Islamic banks in Mogadishu Somalia, and to assess the impact of collection policy on loan performance of Islamic banks in Mogadishu Somalia.

5.2.1 Influence of credit policy on loan performance

The main objective of this research was to assess the impact of credit policy on the loan performance of Islamic banks in Mogadishu, Somalia. The findings showed a positive and

significant correlation between Islamic banks' loan performance and their credit policy. The bank had an elaborate credit policy. Bank's credit policy was effectively implemented; the credit policy was accessible to all staff, outlined discounts allowable to customers and was reviewed periodically.

5.2.2 Influence of credit appraisal on loan performance

The study's second purpose was to analyze the impact of credit appraisal on loan performance of Islamic banks in Mogadishu, Somalia. Findings revealed that the bank obtained borrowers' credit history from other financial institutions, borrowers' financial net worth was assessed by the bank, integrity of the borrowed was assessed before loaning, the ability of a borrower to repay from owned sources was appraised and collateral was part of the appraisal process before loaning borrowers.

5.2.3 Influence of collection policy on loan performance

The study's third objective was to evaluate the influence of collection policy on loan performance of Islamic banks in Mogadishu, Somalia. Findings revealed that the association between collection policy and performance of loans of Islamic banks is positive and significant. The bank maintained strict deadlines in collection of debt, the borrowers were slapped with penalties on loan defaults, customer's properties were auctioned on loan default, the bank employed legal means to recover debt from loanees and customers' loan file was continuously reviewed and updated.

5.3 Conclusions

An elaborate credit policy is a foundational element that plays an essential role in shaping the banks' operational performance, and this importance is particularly pronounced in the context of Islamic banking. A well-designed credit policy serves as a guiding framework that dictates how a bank evaluates, approves, and manages its credit operations. This policy typically

outlines the risk tolerance, credit assessment criteria, and other key parameters that contribute to effective decision-making regarding lending activities. An elaborate credit policy establishes a structured approach to credit management, enabling banks to navigate the intricate landscape of financial risk while aligning with Islamic principles. Credit policy is important in the attainment of sustainable development goals (SDGs) as it directs financial resources towards projects and businesses that support sustainable practices. This encourages investments in renewable energy, social equity and environmental protection, enhancing economic growth that is inclusive and environmentally responsible, ultimately contributing to achieving the SDGs.

The effective implementation of a bank's credit policy is paramount for achieving optimal performance. The mere existence of a comprehensive credit policy is not sufficient; it must be put into practice consistently and across all levels of the organization. When a bank successfully implements its credit policy, it ensures that every aspect of the lending process adheres to the established guidelines. This, in turn, fosters a sense of discipline and accountability within the institution, contributing to the overall effectiveness of credit management. Effective implementation translates the theoretical framework of the credit policy into tangible practices, fostering a credit culture that is aligned with the institution's strategic objectives.

Accessibility to the credit policy by all staff members is a critical factor that enhances the performance of Islamic banks. When the credit policy is readily available to all employees, it promotes a shared understanding of the institution's credit philosophy and guidelines. This accessibility ensures that every staff member involved in credit-related activities, from front-line officers to management, is well-informed and can make decisions that align with the established policies. This widespread understanding minimizes the risk of misinterpretation or

deviation from the credit policy, fostering a cohesive approach across the organization and contributing to improved overall performance.

Allowing discounts to customers, as outlined in the credit policy, is another facet that can positively impact the performance of Islamic banks. Offering discounts within the framework of the credit policy can attract and retain customers, promoting a positive relationship between the bank and its clientele. This customer-centric approach not only enhances customer satisfaction but also contributes to the bank's reputation and market competitiveness. The strategic allowance of discounts, as per the credit policy, reflects flexibility in adapting to market conditions while ensuring that such practices are well-defined and aligned with the bank's financial objectives.

Regularly reviewing the credit policy is a proactive measure that ensures its relevance and effectiveness over time. In a dynamic financial landscape, market conditions, regulatory frameworks, and economic factors can evolve, necessitating periodic reviews of the credit policy. Such reviews allow banks to adapt to changing circumstances, incorporate lessons learned from past experiences, and stay ahead of potential risks. By keeping the credit policy current and aligned with the broader financial environment, Islamic banks can enhance their ability to navigate uncertainties, contributing to sustained performance and resilience in the face of challenges.

The practice of banks obtaining borrowers' credit history from other financial institutions is a pivotal strategy that significantly contributes to tracking creditworthiness before extending loans. This approach provides banks with valuable insights into the borrower's financial behavior, payment history, and existing credit obligations. By leveraging information from external sources, banks can make more informed decisions regarding the creditworthiness of potential borrowers. This practice enhances risk management, reduces the likelihood of

default, and contributes to the overall performance of Islamic banks by ensuring that loans are extended to individuals or businesses with a proven track record of responsible financial behavior.

The assessment of a borrower's financial net worth by the bank is a fundamental component that enhances transparency in the loan extension process and subsequently improves the performance of Islamic banks. Evaluating a borrower's financial net worth involves a comprehensive analysis of their assets, liabilities, and overall financial position. This assessment provides a clear picture of the borrower's ability to meet financial obligations, making the credit extension process more transparent and aligned with the principles of Islamic finance. Transparent and ethical lending practices strengthen the trust between the bank and its clients, fostering a positive reputation and contributing to the sustained success of Islamic banks.

Ensuring the integrity of borrowers before loaning is a critical aspect of credit extension that holds significant importance in the context of Islamic banking. Evaluating the integrity of potential borrowers involves assessing their adherence to ethical and moral principles. This assessment goes beyond financial metrics and considers the individual's character, business ethics, and commitment to ethical conduct. By prioritizing the integrity of borrowers, Islamic banks not only mitigate the risk of engaging with unreliable individuals but also uphold the principles of ethical finance, reinforcing their standing as socially responsible institutions.

The capacity of borrowers to repay from their own sources is a key factor that enhances the extension of loans by Islamic banks. This assessment involves evaluating the borrower's income sources, financial stability, and the ability to generate sufficient funds to meet repayment obligations. Emphasizing a borrower's capacity to repay from their own resources aligns with Islamic finance principles, which emphasize fair and equitable financial

transactions. This approach not only ensures the financial sustainability of borrowers but also contributes to the overall success and performance of Islamic banks by decreasing the chance of loan default and non-performance. Effective credit management practices are crucial for achieving Vision 2030's economic goals. Through ensuring financial stability and promoting responsible lending, these practices support sustainable growth, reduce default risks and enhance credit accessibility. This aligns with Vision 2030's objectives of economic diversification, financial inclusion and improved living standards.

Demanding collateral as part of the appraisal process before loaning borrowers is a risk mitigation strategy that further strengthens the performance of Islamic banks. Collateral serves as a security measure, providing the bank with recourse in the event of loan default. By requiring collateral, Islamic banks minimize the financial risk associated with loan disbursement. This prudent approach not only protects the bank's interests but also fosters responsible borrowing behavior among clients. The demand for collateral, when aligned with Islamic principles, ensures that the appraisal process remains ethical and transparent, contributing to the long-term stability and success of Islamic banks.

The bank's rigorous and disciplined approach to debt collection is a testament to its commitment to ensuring the timely repayment of loans. The strict adherence to deadlines reflects a proactive stance aimed at maintaining financial discipline among borrowers. By establishing clear timelines for debt repayment, the bank not only sets expectations but also enforces a sense of responsibility among borrowers, contributing to a more organized and efficient debt management process.

Imposing penalties on loan defaults serves as a deterrent against delinquency, reinforcing the importance of meeting financial obligations. The imposition of penalties aligns with the bank's commitment to maintaining the integrity of its lending agreements and discouraging

any potential misuse of credit facilities. This approach not only protects the bank's financial interests but also encourages borrowers to prioritize timely repayments, fostering a healthier credit environment.

The auctioning of customers' properties in the event of loan default underscores the bank's determination to recover outstanding debts. This measure serves as a last resort for the bank to recoup losses, emphasizing the severity of default consequences. While auctions may seem stringent, they are indicative of a well-defined and structured debt recovery process, reinforcing the bank's commitment to sound financial practices and safeguarding its overall stability.

The use of legal means to recover debts further underscores the bank's proactive stance in protecting its financial interests. Legal recourse provides the institution with a formal and systematic approach to recovering debts, ensuring that the bank operates within the bounds of the law. This not only enhances the credibility of the bank but also serves as a strong deterrent against potential defaulters, reinforcing the seriousness with which the bank approaches debt recovery.

The continuous review and updating of customers' loan files demonstrate a commitment to maintaining a thorough monitoring process. By staying informed about the financial health of borrowers, the bank can identify early warning signs of potential financial distress and take timely corrective actions. This ongoing scrutiny ensures that the bank remains agile and responsive to changing economic conditions, thereby contributing to a robust and resilient debt management strategy.

5.4 Recommendations for practice

Islamic banks must prioritize transparency and accessibility in their credit policies. Conducting regular training sessions for all staff is crucial to ensuring a comprehensive understanding of policy guidelines. This approach enhances staff knowledge and fosters consistent, standardized implementation across various departments. By promoting transparency and knowledge dissemination, Islamic banks can strengthen their internal processes, aligning operations with ethical principles and enhancing the overall effectiveness of credit policies. This commitment to clarity and education supports a cohesive organizational culture, ultimately contributing to the integrity and success of Islamic banking practices.

Regularly reviewing the credit policy is paramount, aligning it with emerging market trends, regulatory shifts, and evolving economic conditions. This proactive strategy ensures the bank's adaptability and resilience in a dynamic financial landscape. Effective communication of policy updates to all stakeholders is equally crucial, fostering a shared understanding of the bank's evolving credit practices. This transparency not only strengthens internal cohesion but also positions the bank to navigate changing financial dynamics with agility, contributing to its sustained effectiveness and relevance in the ever-evolving financial sector. Periodic market analysis and benchmarking against industry standards are important to ascertain that the offered discounts are not only appealing to customers but also sustainable for the bank. This strategic evaluation ensures that the bank remains in tune with market dynamics, optimizing its offerings to strike a balance between customer attractiveness and long-term financial sustainability.

Islamic banks should also consider incorporating ethical and Sharia-compliant components into the credit policy. This includes a comprehensive assessment of a borrower's financial net

worth, adherence to Islamic principles, and the economic viability of proposed ventures. This alignment with Sharia principles not only enhances the bank's reputation but also ensures a consistent commitment to ethical banking practices. Islamic banks should explore avenues to enhance customer education and communication regarding the credit policy. Clear and transparent communication channels, such as workshops, seminars and informational materials, can be employed to educate customers about the credit policy, discounts available, and the importance of adherence to deadlines.

5.5 Recommendations for further research

The current research's limitation to Mogadishu restricts the generalizability of findings, and therefore, researchers should explore a broader geographical scope to ensure a more comprehensive understanding of Islamic banks' credit practices in different contexts. To advance the understanding of credit management practices within Islamic banking, future research endeavors should expand beyond the confines of Mogadishu and incorporate a more diverse range of Islamic banks. This geographical diversity could encompass various regions or even multiple countries with distinct economic and cultural characteristics.

The methodological approach employed in this study focused solely on quantitative techniques for data collection and analysis. Future studies should adopt a mixed-methods approach. By integrating qualitative techniques, such as interviews, focus groups, or case studies, with quantitative methods, researchers can gain a better understanding on how credit management techniques influence the effectiveness of loans perform.

The scope of this study was examining independent factors was the exclusive focus of this investigation. ,that is, credit policy, credit appraisal and collection policy. To enhance comprehension of credit management methods and their effect on how well loans perform,

future research should consider incorporating other variables. For example, Further research could look into how credit worthiness affects loan performance or assess how credit conditions affect loan performance. Considering the interconnected nature of credit management, future studies could also explore the relationships between different variables and their combined influence on loan performance. This would provide a more comprehensive and integrated view of credit management practices, allowing for a better analysis of the impact of credit management practices on loan performance.



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APPENDICES

Appendix I: Letter of Introduction

Dear Participant,

I am a student at the Mount Kenya University pursuing a Master's of Business Administration specializing in Finance. As part of the requirements, I am undertaking a research project on, "*the influence of credit management practices on loan performance of Islamic banks in Mogadishu Somalia.*" Kindly be a respondent in the research. Results of this research will help in coming up with policies credit management practices of Islamic banks. This research's recommendations would be resourceful to policy makers in the banking industry.

Thank you.

ABDISHAKUR NOR OSMAN

MBA/2021/42047



Appendix II: Consent form

Dear Participant,

I invite you to participate in a study titled "**an analysis of the influence of credit management practices on loan performance of Islamic banks in Mogadishu Somalia**" I am a student pursuing a Master's degree in Business Administration at Mount Kenya University. The purpose of this study is to analyse the influence of credit management practices on loan performance of Islamic banks in Mogadishu Somalia.

Your involvement in this research project is voluntary. You are under no obligation to answer any questions you are uncomfortable with and you may choose to omit responses. The risks related with taking part in this research are minimal .Your responses will be handled with confidentiality. Data gathered from this study will be maintained in a secure and confidential manner and will only be presented in an aggregated format. There are no direct incentives for taking part in this study but your engagement could provide valuable insights into the topics covered, benefiting the industry and potential customers alike.

If you decide to participate, I kindly request that you provide your best possible answers to the questionnaire's inquiries. The completion of the questionnaire is estimated to take approximately 30 minutes. Should you have any inquiries concerning this research project, please do not hesitate to contact Abdishakur Nor Osman. For any concerns regarding your rights as a research respondent, please direct your queries to the Chairman of the Mount Kenya University Ethical Review Committee, reachable at P.O. Box 342-01000, Thika.

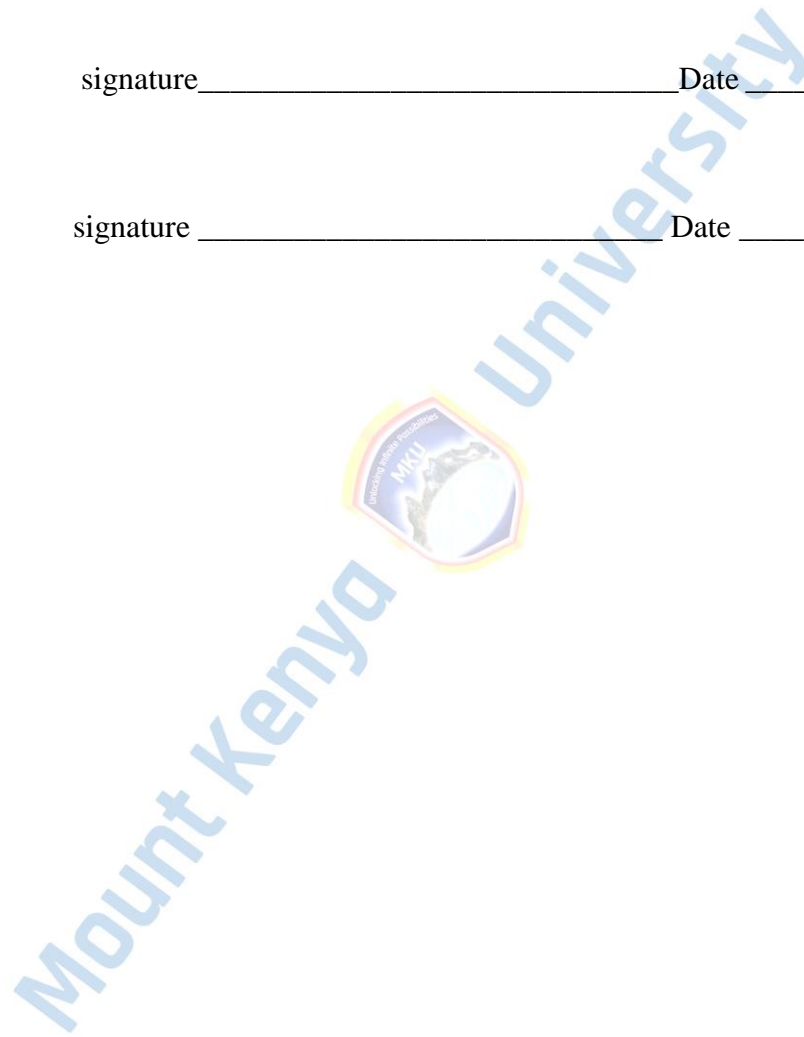
Thank you for your assistance in this important endeavor

CONSENT

I have read and understood the content presented to me. I have the chance to seek clarifications and ask questions relating to the information provided. I acknowledge that my involvement in this study is completely voluntary. I am aware that I will be provided with a copy of this consent form. I willingly give my consent to participate in this research.

Participant's signature _____ Date _____

Investigator's signature _____ Date _____



Appendix III: Questionnaire

This questionnaire seeks your responses on the influence of credit management practices on loan performance of Islamic banks in Mogadishu Somalia.

SECTION A: BACKGROUND INFORMATION

1. Indicate your gender.

- i. male ()
- ii. female ()

2. Indicate your age bracket.

- i. 18-25 years ()
- ii. 26-35 years ()
- iii. 36-45 years ()
- iv. 46-55 years ()
- v. above 55 years ()

3. Indicate your highest education level.

- i. diploma ()
- ii. bachelor's degree ()
- iii. master's degree ()
- iv. PhD ()

4. What is your rank in the bank?

- i. credit officer ()
- ii. supervisor ()
- iii. manager ()

5. How many years have you worked in credit management?

- i. 1-4 years ()
- ii. 5-9 years ()
- iii. 10-14 years ()
- iv. 15-29 years ()
- v. 30+ years ()

SECTION B: CREDIT POLICY AND LOAN PERFORMANCE OF ISLAMIC BANKS

In this part, and the following four parts, utilize below scale and tick (√) the score that you agree with most scale: *5=strongly agree, 4= agree, 3=not sure, 2=disagree and 1=strongly disagree*

Statement	5	4	3	2	1
The bank has an elaborate credit policy.					
The bank's credit policy is effectively implemented.					
The credit policy is accessible to all staff.					
The credit policy outlines discounts allowable to customers.					
The credit policy is reviewed periodically.					

SECTION C: CREDIT APPRAISAL AND LOAN PERFORMANCE OF ISLAMIC BANKS

Statement	5	4	3	2	1
The bank obtains borrowers' credit history from other financial institutions.					
Borrowers' financial net worth is assessed by the bank.					
The integrity of the borrow is assessed before loaning.					
The ability of a borrower to repay form own sources is appraised.					
Collateral is part of the appraisal process before loaning borrowers.					

SECTIOND: COLLECTION POLICY AND LOAN PERFORMANCE OF ISLAMIC BANKS

Statement	5	4	3	2	1
The bank maintains strict deadlines in collection of debt.					
Borrowers' are slapped with penalties on loan defaults.					
Customers properties are auctioned on loan default.					
The bank employs legal means to recover debt form loanees.					
Customers' loan file is continuously reviewed and updated.					

SECTION E: LOAN PERFORMANCE OF ISLAMIC BANKS

Statement	5	4	3	2	1
Non-performing loans have reduced.					
The banks' loan booked has increased.					
Active loanees have increased.					
The bank's profitability has increased.					
Loan repayments is timely.					

THANK YOU

Appendix IV: Proposal approval letter



REF: MKU/ISERC/3334
TO: ABDISHAKUR NOR OSMAN

Date: 15 November 2023

REG: MBA/2021/42047

Dear Sir/Madam,

RE: INFLUENCE OF CREDIT MANAGEMENT PRACTICES ON LOAN PERFORMANCE OF ISLAMIC BANKS IN MOGADISHU, SOMALIA

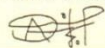
This is to inform you that **Mount Kenya University** has reviewed and approved your above research proposal. Your application approval number is **2378**. The approval period is **15/11/2023 - 14/11/2024**.

This approval is subject to compliance with the following requirements;

- i. Only approved documents including informed consents, study instruments, MTA will be used
- ii. All changes including amendments, deviations and violations are submitted for review and approval by **Mount Kenya University**
- iii. Death and life threatening problems and serious adverse events or unexpected adverse events whether related or unrelated to the study must be reported to **Mount Kenya University** within 72 hours of notification
- iv. Any changes, anticipated or otherwise that may increase the risks or affect the safety or welfare of study participants and others or affect the integrity of the research must be reported to **Mount Kenya University** within 72 hours
- v. Clearance for export of biological specimens must be obtained from relevant institutions
- vi. Submission of a request for renewal of approval at least 60 days prior to expiry of the approval period. Attach a comprehensive progress report to support the renewal
- vii. Submission of an executive summary report within 90 days upon completion of the study to **Mount Kenya University**

Prior to commencing your study, you will be expected to comply with any additional requirements from the relevant authorities in the country where this study will be conducted

Yours sincerely,



Dr. Alfred Owino, PhD
Chairman, Mount Kenya University ISERC

The Chairman
Mount Kenya University
Ethics Review Committee
P.O. Box 342 - 0100, Thika

Main Campus, General Kago Road, P.O. Box 342-01000 Thika. Tel: +254 67 2820 000,

Cell: +254 720 790 796, 0709 153 000

Email: info@mku.ac.ke, Web: www.mku.ac.ke

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Appendix V: University introduction letter



DIRECTORATE OF GRADUATE STUDIES

MBA/2021/42047

16th November, 2023

TO WHOM IT MAY CONCERN

Dear Sir/Madam,


RE: ABDISHAKUR NOR OSMAN – REGISTRATION NO. MBA/2021/42047

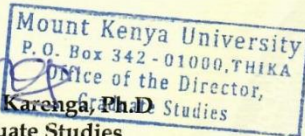
The purpose of this letter is to introduce the above named student who is pursuing **Master of Business Administration** in the department of **Accounting and Finance** in the school of **Business and Economics**

The title of the research is **“Influence of Credit Management Practices on Loan Performance of Islamic Banks in Mogadishu, Somalia.”** It has been cleared by the University’s Ethics Review Committee (Certificate attached) and now has to proceed to the field to collect data between **November, 2023 and January, 2024.**

Any assistance accorded to the student will be highly appreciated.

Thank you.


Dr. Samuel M. Karenga, Ph.D.
Director, Graduate Studies
Enc.



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Appendix VI: Map of Somalia showing Mogadishu



INFLUENCE OF CREDIT MANAGEMENT PRACTICES ON LOAN PERFORMANCE OF ISLAMIC BANKS IN MOGADISHU, SOMALIA

by Abdishakur Nor Osman

Submission date: 26-May-2024 03:03PM (UTC+0300)

Submission ID: 2386628404

File name: ABDISHAKUR_NOR_OSMAN_6.doc (1.51M)

Word count: 19957

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INFLUENCE OF CREDIT MANAGEMENT PRACTICES ON LOAN PERFORMANCE OF ISLAMIC BANKS IN MOGADISHU, SOMALIA

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Mount Kenya