

THE FACTORS INFLUENCING TO RECOVER THE BANK LOANS IN THE ISLAMIC FINANCIAL INSTITUTION: SPECIAL REFERENCE TO AMANA BANK PLC

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ABSTRACT: The objective of this research is identify the influencing factors in default repayment by the customers in bank loans. Factors such as credit policy, installment, climate, and political factors are perceived on loan repayment occurrence; each of these factors significantly affects loan recovery performance in Islamic financial institutions in Sri Lanka. This study was used primary data. The study target population comprises the loan customers of the Amana Bank PLC in Akkaraipattu. Quantitative survey design was used to carry out census of Akkaraipattu branch of Amana bank. The data was collected through a structured questionnaire and administered to the loan customers for response. A total of 100 questionnaires were administered of which 67 were adequately respondent to and considered for analysis, this formed 67% response rate. Correlation of coefficient and regression analysis were used as methods of analysis in the SPSS software. The findings of this study indicated that all the four factors were tested. Four factors which credit policy, installment, climate and political factors positively impact on loan recovery. There is significant relationship between credit policy, installment, climate and political factors on loan recovery, if the hypotheses accepted that means there is relationship between dependent and independent variables, all factors are contributing to recovery the bank loan in Islamic financial institutions.

Keywords: Loan Recovery, Financial Institution, and Amana bank PLC.

1. INTRODUCTION

Financial institutions are playing a major role in a country's economy, because they provide number of services which lead to country's economic development. There is an increasingly intense competition in the Sri Lanka banking industry. This is because; the industry is much more attractive in terms of long-term returns on investors' fund and profit attractiveness.

Amana Bank PLC is one and only private fullpledged Islamic bank in Sri Lanka, offering a wide range of banking and related financial services. The bank has 24 branches offering Amana bank customers a multitude of services of the highest quality in the customer-focused manner. It has an innovative credit, collection of saving and recovery of loan installment whether who need is personal, corporate or agricultural can obtain from the Amana Bank can help with any type customers' need.

In Islamic banks and financial institutions, most of the Islamic banking products are released to their banking customers such as Mudharaba, Musharakah, Ijara, Murabaha, Qard al Hassan, Diminishing Musharakka, As salam, Isthisna etc.. Although, The facilities given such as Diminishing musharakah, murabaha, Ijara, As salam, Isthisna, Credit sale and Qard Hassan to the customers have got like loans. Because the payments for the products and services are paid as delayed payments and installment. Therefore, the researchers wish to identify the reasons to the delayed or not payments on the time limit. So the word loan is used for the delayed installment amount to be paid to the bank by the customers.

Credit management is a banking practice therefore bank lending through the products and services to customers and banks must recover the principal amount given loans due to ensure safety of depositors fund and also avoiding capital errors and loss. So, bank lending has to consider income, cost of funds, statutory requirement, depositors need and risk becomes with loan granted. For these reasons banks have credit policies and procedures which are stipulate the lending the lending process. Credit policy includes the credit standards, credit

terms, and collection procedures. While the loan recovery process are the collateral security guarantors, saving deposits money and current accounts.

Loan recovery is the process which involves the procedures that the bank uses to collect its money from the debtors. After granting the advances and loans bank has to monitor and control the customers those who given the loans by ensure the depositors money and also the bank must have the successful collection methods and collection periods. Sometimes the customers couldn't repay the loans, at that time the bank wanted to extends the period and have to think the alternative ways to collect even the capital. If not, it will be the chance of increasing the bad debts and losses.

Remarkably, financial institutions are continuing to face similar challenges of loan default like any other financial institutions in Sri Lanka. The money went out to customers are often paid late or not paid at all leaving the bank exposed to default risk. It's important to note that despite that rigorous screening under taken in the credit assessment process which includes among others; proof that customer does not have other obligations, analysis of their account performance sustainability of their income level, security and ability to pay. Most of the borrowers are unable to stick to their repayment programmed causing much hardship to the lending institution. (MilnesHolden, 1986)

Despite of the credit management policies of the bank like Installment amount, payment periods, credit worthiness of customers, collateral security to obtain the loan, assessment of the ability to monitor the credit, the rate of credit return in Amana Bank has not been recovered 100% hence this means that something must be done to evaluate why some customers do not respond in returning the credit that was extended to them.

2. PROBLEM STATEMENT

The recovery of outstanding loans generally advanced banks to individual borrowers or corporate entities was big issue, financial institutions and banks hesitating to advancing loan as the recovery of the loans were the biggest challenge they faced.

Recovering loans from the customers within the time period is the major challenge to the bank as a financial intermediary. Unless the bank recovers the loan, it has to be accountable for the depositors. The hypothesis of this research is why the debtors make mistakes while they are settle the loan. The financial Institutional managers are always facing to receive the loan amount using the installments or single time.

3. RESEARCH QUESTION

The study has answered the following research question

1. "What are the factors mostly influence to recover the bank loans and advances?"-especially to Amana Bank PLC.
2. What strategies are designed to improve recovering the bank loans and advances?

4. RESEARCH OBJECTIVES

The study has formulated the following Research Objectives are:-

Primary Objective:-

1. To identify the influencing factors in repayment by the customers in of bank loans in Amana bank PLC.

Secondary Objective:-

2. To identify the relationships between factors which credit policies, political factors, installment, climate and loan recovery in Amana bank PLC.

5. LITERATURE REVIEW

According to Fidrmucet *al.*,(2007) who sought to find out whether a lender extends credit to customers it recognizes the possibility that customers will be unable to pay or unwilling to pay. This

study adopted a survey research design targeting all types of lenders. He found out that lenders must establish policies for determining who will receive credit for how long and how much. He also found out that lender should built their credit policy around five of credit that character, capacity, capital, collateral and conditions for them to be successful. He concluded that borrowers may sometimes fail to pay back loans due to lack of financial ability and other related factors other than not being willing to pay for credit given.

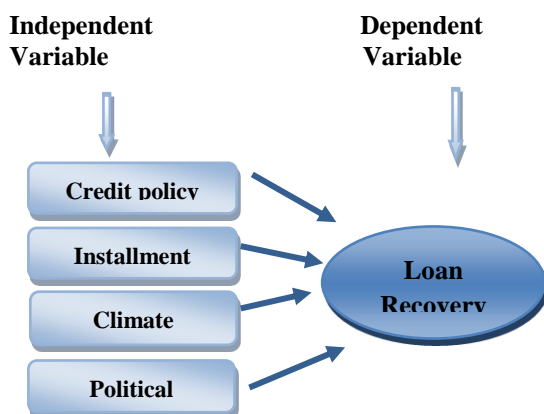
Njeru (2011), sought to find out about public debt being the structure and servicing of Kenya`s public debt. She utilized descriptive survey targeting Kenya as a country as her research methodology in studying the structure and servicing of Kenya`s public debt. Her study findings were: the Government was not happy with the level of stock of domestic debt and the government was not supporting the private sector has it should. She concludes that for government needs to put in place measures to reduce its public debt.

Saloner (2007) researched on the effect of Institutional Characteristics on default rate in developing world. The results showed that a focus on women as borrowers, on institutional incorporation into the community, and on client-led programming all lead to lower default rates and thus greater success.

Pollio (2010) examined microfinance default rates in Ghana. He found that repayment it affected mainly by the number of dependents in the household, years in business, use of proceeds, loan status, and frequency of loan monitoring.

Ainebyona Fortunata (2011), The study was focused on credit management policy and loan recovery with post bank Uganda with the main objective of finding out the relationship between the two variables of credit policy and loan recovery, examining the credit policy management of post bank and examining the loan recovery levels of post bank. The Study found out that effective credit policy leads to effective loan recovery bank has got well established loan recovery procedures among which include; telephone calls to debtors, sending reminding letters to the clients, and taking legal action on clients who fail to pay back the loan. The findings also revealed that there is a moderate relationship between credit policy management and loan recovery, it indicates that effective credit policies result into effective loan recovery.

6. CONCEPTUAL FRAME WORK



6.1 Statement of Hypothesis

Based on conceptual framework follows some variables to collect their loan installment from borrowers. Possible hypothesis are formulated based on literature as follows,

H₀:- The Credit Policy, Installment, Climate and Political factors have no impact on loanrecovery.

H₁:- The Credit Policy, Installment, Climate and Political factors have impact on loan recovery.

7. METHODOLOGY

7.1 Population and Sample

The target population for this study is customers who received the loan facility which can be debt facilities from the Amana bank Akkaraipattu branch are considered for this study. Sample for this study 100 loan customers were chosen simple randomly from the target population. 100 questionnaires were distributed directly among them. Simple Random sample is used for distribute questionnaires for researcher’s convenient. Out of 100 Questionnaires 67 were received (67%).

7.2 Data Collection Method

The study was used primary data. Primary data was collected through structured questionnaire and formal discussion with bank’ managers. Further the secondary data is also used in this study such as relevant articles, related text books, annual reports, websites and journals are referred to get information.

7.3 Method of Data Analysis

For the statistical analysis, the researcher used SPSS 20.0 computer software packages. And also researchers analyze data by employing correlation and Regression. Correlation analysis was conducted to find out if there is an association between the Credit Policy, Installment, Climate and Political factors on loan recovery. Regression analysis was carried out to examine impact existing between the Credit Policy, Installment, Climate and Political factors on loan recovery.

8. RESULTS AND ANALYSIS

8.1 Loan Recovery and Credit Policy

In an attempt to examine the relationship between Recovery and credit policy, this study performed Correlation between credit policy and loan recovery as follows

		Loan Recovery	Credit Policy
Loan Recovery	Pearson Correlation	1	.700**
	Sig. (2-tailed)		.000
Credit Policy	Pearson Correlation	.700**	1
	Sig. (2-tailed)	.000	

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

The above Table, there is a strongly positive correlation between credit policy and loan recovery, correlation coefficient is $r = 0.700$. It means, Credit policy has the strongly positive relationship with loan recovery.

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.700 ^a	.490	.433	.07944

a. Predictors: (Constant), Credit Policy

The coefficient of determination of credit policy and loan recovery, the R^2 value is 0.490 indicated a shared variation of about 49% between loan recovery and credit policy. The results indicate that the

model explains the dependent variable which loan recovery 49% by the independent variables. Since the value is less than 50% thus the model can be normally adequate.

Coefficient					
Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	4.616	.411		11.23	.000
Credit Policy	.697	.180	-.500	-3.87	.000

Dependent Variable: Loan Recover

From the above coefficient table, B_0 is 4.616 and B_1 is 0.697. There is positive impact on Credit policy and loan recovery. Fitted simple linear regression line is:

According to the coefficient table:
 $\beta_0 = 4.616$ - (Constant)
 $\beta_1 = 0.697$ - (Credit Policy)

$$\hat{Y} = \beta_0 + \beta_1 X$$

$$LR = 4.616 + 0.697CP$$

8.2 Loan Recovery and Installment

To realize the relationship between loan recovery and Installment, this study performed Correlations between loan Recovery and Installment as follows:

		Loan Recovery	Installment
Loan Recovery	Pearson Correlation	1	.532**
	Sig. (2-tailed)		.017
Installment	Pearson Correlation	.532**	1
	Sig. (2-tailed)	.017	

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

According to the above Table, there is a significantly moderate positive correlation between Loan recovery and Installment, correlation coefficient is $r = 0.532$. This means, loan recovery has the moderate positive relationship with Installment.

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.532 ^a	.283	.258	.08923

a. Predictors: (Constant), Installment)

The coefficient of determination of Installment and loan recovery, the R^2 , value is 0.283 indicated a shared variation of about 28.3% between loan recovery and Installment. The results indicate that the model explains the dependent variable which loan recovery 28.3% by the independent variables. Since the value is less than 50% thus the model cannot be adequate.

Coefficient					
Model	Unstandardized Coefficients		Standardized Coefficient	t	Sig.
	B	Std.			

		Error	Beta		
(Constant)	1.915	.695		2.75	.008
Installment	.407	.254	.232	1.59	.117

Dependent Variable: Loan Recovery

From the above coefficient table, B_0 is 1.915 and B_1 is 0.407. There is positive impact on Installment and loan recovery. Fitted simple linear regression line is:

According to the coefficient table:

$\beta_0 = 1.915$ - (Constant)

$\beta_1 = 0.407$ - (Installment)

$$\hat{Y} = \beta_0 + \beta_1 X$$

$$LR = 1.915 + 0.407I$$

8.3 Loan Recovery and Climate

To realize the relationship between loan recovery and Climate, this study performed correlation between Loan Recovery and Climate

		Loan Recovery	Climate
Loan Recovery	Pearson Correlation	1	.615**
	Sig. (2-tailed)		.000
Climate	Pearson Correlation	.615**	1
	Sig. (2-tailed)	.000	

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

According to the above Table, there is a significantly moderate positive correlation between Loan Recovery and Climate, correlation coefficient is $r = .615$, this means, Loan Recovery has the moderate relationship with climate.

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.615 ^a	.378	.365	.07232

a. Predictors: (Constant), Climate

The coefficient of determination of Climate and loan recovery, the R^2 value is 0.378 indicated a shared variation of about 37.8% between loan recovery and Climate. The results indicate that the model explains the dependent variable which loan recovery 37.8% by the independent variables. Since the value is less than 50% thus the

model cannot be adequate.

Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Model Summary			
	B	Std. Error	Beta			R	R Square	Adjusted R Square	Std. Error of the Estimate
(Constant)	2.071	.183		11.334	.000				
Climate	.344	.066	.615	5.234	.000	.440 ^a	.193	.176	.08238

a. Dependent Variable: Loan Recovery

From the above coefficient table, B_0 is 2.071 and B_1 is 0.344. There is positive impact on Climate and loan recovery. Fitted simple linear regression line is:

According to the coefficient table:

$$\beta_0 = 2.071 - (\text{Constant})$$

$$\beta_1 = 0.344 - (\text{Climate})$$

		Loan Recovery	Political Factors
Loan Recovery	Pearson Correlation	1	.440**
	Sig. (2-tailed)		.002
Political Factors	Pearson Correlation	.440**	1
	Sig. (2-tailed)	.002	

$$\hat{Y} = \beta_0 + \beta_1 X$$

$$LR = 2.071 + 0.344C$$

8.4 Loan Recovery and Political Factor

To realize the relationship between Recovery and Political, this study performed correlation between loan Recovery and Political Factors

According to the above Table, there is a significantly weak correlation between Recovery and Political factors, correlation

coefficient is $r = 0.440$, this means, Loan Recovery has the weak relationship with political Factors.

a. Predictors: (Constant), Political Factors

The coefficient of determination of Political factors and loan recovery, the R^2 -value is 0.193 indicated a shared variation of about 19.3% between loan recovery and political factors. The results indicate that the model explains the dependent variable which loan recovery 19.3% by the independent variables. Since the value is less than 50% thus the model cannot be adequate.

Coefficients					
Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	1.370	.504		2.717	.009

a. *Dependent Variable: Loan Recovery*

Political Factors	.578	.176	.440	3.285	.002
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From the above coefficient table, B_0 is 1.370 and B_1 is 0.578. There is positive impact on political factors and loan recovery. Fitted simple linear regression line is:

According to the coefficient table:

$$\beta_0 = 1.370 \text{-(Constant)}$$

$$\beta_1 = 0.578 \text{-(Political factor)}$$

$$\hat{Y} = \beta_0 + \beta_1 X$$

$$LR = 1.370 + 0.578 PF$$

9. FINDINGS AND CONCLUSION

9.1 Key Findings

The objectives of this research are to identify the influencing factors in repayment of loan by the customers and also to identify the relationships between factors which credit policies, installment, climate, political factors and loan recovery in Amana bank PLC. This study has aimed to identify the evaluation of the influencing factors in repayments' period. There are some impacts on all the factors in this study which are identified as positive relationship between credit policy, installment, climate, political factors on loan recovery. In this study, the Researchers find out, all the factors contributed in repayment the loan. The most of customers between the age group of 31-45 regarding of the loan more customers have taken personal and vehicle loan for project and implementation of particular purpose of the loan but poor repayment of particular loan customers.

This study attempts to explain the selected factors influencing to loan recover in Islamic financial institutions in Sri Lanka. To find the solution to the research problem, this study examines about selected factors. Those factors are credit policy, installment, climate and political factors. It is concluded from this research, all the factors contribute to loan recovery. The findings of the study from the factors given as follow.

9.1.1 Credit Policy

The credit policy it was included that variable of instructions, repayment period, collection methods, mercy period, an installment amount and collection terms. It aimed to identifying better approaches to credit policy management and improve efficiency in loan recovery. For instance the study revealed that credit officers carried out close monitoring and loan management. The significant of the credit policy in recovering the bank loans is mostly contributed. Every bank should sustain the credit management policy.

In the finding this study the bank does not interest to give the loan to the customers who receive below Rs. 15,000 monthly income. The credit policy mostly impacts on the debtors who received the vehicle loan and housing long term. It indicates the period as 6 - 8 years and above 8 years, because of according to the questionnaires mostly the male customers who get the salary above 40,000/= are receiving like the above loan from the bank, this time some of the long term debtors have to be reminded, continuously supervising and when the customers breach their agreements with the bank the procedures which is already created also come to complete. Not only that, some of the customers is unable to finish by pay the all installment, because sometimes they die. This time the bank could not collect or recover the loan amount.

9.1.2 Installment Amount

The installment is very important element in lending the money and recovering the money for banking sector, as the installment amount goes to high continually making the debtors facing hardships, the borrowers especially the small entrepreneurs and regular income earning group find it difficult to pay their bank loans. It is continued with the banking sector at all products and services given by the bank or financial institutions.

Most of the Customers who are receiving the loan from the bank they are not rich. Therefore, installment not mostly but affects generally the income which from the business because make installment by the bank is ordinary than the other banks. Installment is influencing commonly on all customers particularly but, it does not have very little impact on the loan recovery.

However, the objective of this study, the study examines the relationship between installment and loan recovery, installment has an impact on loan recovery, because the installment has already been fixed by the bank and the debtors, so the installment is also influence by the debtors.

9.1.3 Climate

According to the data collected through the questionnaire, most of the debtors who are receiving the loan from the bank are affected by the climate when they engaging their agricultures and other based on the weather condition. Some of the customers with primary and secondary level educational knowledge got their monthly income between Rs.15000-25000 also receive the personal loan from the bank.

Male and female of the debtors in particular period are mostly equal in receiving the loan. Some customers who received above 25000 monthly incomes they also receive the above mentioned loans. The debtors of the Amana Bank PLC, those who received loans they put in agriculture, farming, paddy and poultry through Assalam and Isthisna. Although, they engage in jobs without awareness of climate, with the experience and past events by the climate and the weather and earn the money. But, when the climate changes the affects come up to the debtors. Therefore, they are unable to earn more and settle the loan. But, government officers affected but not much, because they able to settle the loan amount by their salary. This is the problem for the credit department of the bank.

Bank also guides with awareness to the customers related to the type of agriculture and suitable climate for them. These guides help the clients to earn the expected profit and escape from the default their business. Clients or debtor can feel free from the stress of loan given by the bank due to the warning arise from the particular bank.

9.1.4 Political Factors

Political factors include government policies, international trade, paying tax etc., influencing mostly to male customers this is why they are receiving the loans more than the females because they are earning to their families. There are number of customers are as university degree holders, lecturers and high salary persons they do the job in government sectors or private. When they are getting salary above Rs. 62500, they have some of the responsibilities to the government by paying tax some of the deductions in their salaries and increasing the paying tax. Therefore, they sometimes they default in pay the installments.

Moreover, there is no contribution of the government in repaying the loan. It can support to the debtors who are unable to settle the loan and also it would be helpful if the affected debtors are provided with subsidizes or any contribution to repayment the amount due. And also the goods and services produced from the loan received for business or agriculture are not marketed with the appropriate circumstances and the price of them also is not fixed strongly. Here, Therefore, according to the subjects indicated above the level of loan recovery and loan repayment will be different and contribute.

9.2 Conclusion

Lending is the major activity of the financial institutions therefore every financial institution has the credit department. The money went out to customers are often paid late or not paid at all leaving the bank exposed to default risk. It's important to note that despite that rigorous screening under taken in the credit assessment process which includes among others, proof that customer does not have other obligations, analysis of their account performance sustainability of their income level, security and ability to pay. Most of the borrowers are unable to stick to their repayment programmed causing much hardship to the lending Islamic financial institution.

9.3 Recommendations

Based on the analyses the researchers have recommended the following recommendations as suggestions, the following recommendations are considered for useful adapt. By these recommendation the bank conductivity its financial planning and financial control, increase its efficiency more than entire.

- Provide preferential treatment to borrowers who implement modern technology to improve their trade and development activities.
- Bankers should be trained to motivate the borrowers to pay back soon the loan amount through giving the promotions activities to improve the customers' attitude to pay their loan.
- Whenever customers come with politician's letter of recommendations they must be politely and prudently declined on occasions other than the particular politician becomes a guarantor himself.
- The bank must consider that the reason for requesting the bank for a loan, and always keep in touch with the borrowers regularly and monitor their business well before the non- performance signal.
- Provide facilities to borrowers who promptly settle their bank loan with in time limit.
- The customers want be an interest in given the bank loans in proper repayment period.
- The bank must take a security from the debtors to avoid becoming losses from the loan according to the law of recovery of loan No 4 of 1990.
- Weather or climate pattern should be taught as awareness to the farmers and who are engaging in agricultural field by the department of agriculture. And the customers should be advised in selecting their suitable weather pattern area.

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