Application of Credit Risk Control Practices on Eazzy Loan of the Equity Bank in Kenya

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Abstract – Mobile banking has immensely contributed to growth in the banking sector in Kenya and world over. One of the key aspects of mobile banking is mobile loaning that has rapidly penetrated the Kenyan financial sector already spread across the financial institutions in Kenya. Over the few years of mobile loaning, banks and telecommunication institutions in Kenya have developed mobile phone loaning platforms/ applications such as the Ezzay Loan of Equity Banks, KCB Mobi Loan for KCB Bank and the M-Shwari by Safaricom. The risks associated with mobile phone loaning are high. This study therefore sought to assess the application of credit risk control practices that Equity Banks had implemented to mitigate against risk in its Eazzy Loan mobile phone loaning platform. The study was carried out in Equity Bank Limited, North and Central Rift Regions among the 27 bank branches. It adopted the descriptive research design. The target population constituted 27 credit officers and 54 credit managers in charge of Eazzy Loan. A census was done therefore all the 81 staff were included in the study. Questionnaires were used to collect primary data. Upon data collection, analysis was done descriptive statistics and chi square was used to check selected credit risk control practices were significant in controlling risk associated with mobile loaning. The study found out that all the selected credit risk control practices; namely Quantification of credit risks, Individual risk control, Portfolio risk control, Credit limits, Risk policies and procedures, Oversight Committee on performance of Eazzy Loan, Internal controls, Periodic reviews and Internal audits were fully applied on Eazzy Loan mobile phone loaning platform of Equity Bank. Although there was an Oversight Committee that reviewed the performance of Eazzy Loan to inform its future performance, a high number of the respondents were not aware of its presence. In overall, the study established that all studied indicators of credit risk control practices were significant practices that all banks with mobile banking services should embrace.

Keywords: mobile banking, mobile phone loaning,credit risk control and risk mitigation

1.0 Introduction

Risk controlling is part of the overall risk management process and follows the quantification and planning of risks, aiming to reduce the risks to a level which — according to the stipulations from the risk strategy is manageable for the institution; it is handled by portfolio management. Risk controlling is carried out at the level of the individual borrower and at the portfolio level (Oesterreichische National Bank, 2004). There are numerous instruments that can be used in risk controlling. Depending on the situation, every institution has to determine what instruments can be used economically and may help reach the state intended by the bank. The definition of limits is necessary to curb the risks associated with banks activities. It is intended to ensure that the risks can always be absorbed by the predefined coverage capital. When the limits are exceeded, risks must be reduced by taking such steps as reducing exposures or using financial instruments such as derivatives or securitization.

Internal controls include the policies and procedures that financial institutions establish to reduce risks and ensure they meet operating, reporting, and compliance objectives (Bessis, 2002). The Board of Directors is responsible for ensuring internal control programs operate effectively. Their oversight responsibilities cannot be delegated to others within the institution or to outside parties. The Board may delegate operational activities to others; however, the board must ensure effective internal control programs are established and periodically modified in response to changes in laws, regulations, asset size, organizational complexity, etc. Internal control programs should be designed to ensure organizations operate effectively, safeguard assets, produce reliable financial records, and comply with applicable laws and regulations. Internal control programs should address five key components. This overview of internal control is described further in a report by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) titled Internal Control-Integrated Framework. Institutions are encouraged to evaluate their internal control program against this COSO framework (COSO, 2012).

Bessis (2002) argue that risk control activities include the policies and procedures institutions establish to manage risks and ensure pre-defined control objectives are met. Preventative controls are designed to deter the occurrence of an undesirable event. Detective controls are designed to identify operational weaknesses and help effect corrective actions. Control activities should cover all key areas of an organization and address items such as organizational structures, committee compositions and authority levels, officer approval levels, access controls (physical and electronic), audit programs, monitoring procedures, remedial actions, and reporting mechanisms.
The paper sought to study the application of credit risk control practices on Eazzy Loan using the following indicators:

i. Quantification of credit risks
ii. Individual risk control
iii. Portfolio risk control
iv. Credit limits
v. Risk policies and procedures
vi. Oversight Committee on performance of Eazzy Loan,
vii. Internal controls
viii. Periodic reviews
ix. Internal audits

2.0 Operational Definition of Terms

Eazzy Loan Product - Under this paper, Eazzy Loan meant is a mobile loaning product of the Equity Bank in Kenya. Through this product, customers apply for loan through mobile phone devices.

Credit Risk Control Practices - Under this paper, credit risk control meant practices established and implemented by Equity Bank, Kenya to manage risks and ensure pre-set credit control objectives are observed and met. The selected practices for this study were Quantification of credit risks, Individual risk control, Portfolio risk control, Credit limits, Risk policies and procedures, Oversight Committee on performance of Eazzy Loan, Internal controls, Periodic reviews and Internal audits

3.0 Methodology

The study adopted the descriptive research design where selected staff of equity Bank provided information on behalf of their institutions on the status of credit risk management in mobile loaning in relation to performance. The study was descriptive because it sought to document the current practices without modification of parameters.

The study was carried out in Equity Bank Limited, North and Central Rift Regions. Equity bank has been proactive in transforming the Kenyan Banking Industry through financial innovations. The bank runs the Ezzay Loan product that is provided and managed through the mobile platform. This makes Equity bank a suitable institution for conducting the study. The bank has presence in all major towns in East Africa.

The target population comprised credit officers in charge of Eazzy Loans and the Credit Managers in each Bank Branch. Equity Bank has 26 Bank Branches in North and Central Rift regions and each bank Branch has two credit officers either fully or partially dedicated to the Eazzy Loan Customers. Further, each bank had one credit manager responsible for the entire loan portfolio including mobile loans. This implies that each bank branch had three staff with full understanding on the mobile credit operations and credit risks management. In total, these staff were 78 in the North and Central Rift Regions. Therefore the target population for the study was 78 Eazzy Loan staff of Equity Bank. The study conducted a census of all Eazzy Loan officers and credit managers.

Table 1: Population Distribution

Region	Credit Managers	Credit Officers	Total
North Rift	12	24	36
Central Rift	14	28	42
Total	**26**	**52**	**78**

The study used questionnaire as the main tool for collection of primary data. One set of questionnaire was designed and administered to both credit officers and credit managers. The questionnaire was based on credit control practices on Eazzy Loans in the various bank branches. A five point likert scale to establish the extent of application of credit control practices on Eazzy Loans was used.

Data collected was coded and analyzed with the aid of computer programmes Statistical Package for Social Sciences (SPSS). Quantitative data was analyzed using descriptive statistics which include frequencies and percentages. Chi square analysis was then done to establish the extent of application of credit control practices on Eazzy Loans.

4.0 Results

4.1 Response Rate

The sample size for the study was 78, thus a total of 78 questionnaires were issued, 26 for credit managers and 52 for credit officers. The questionnaires returned were 23 for credit managers and 50 for credit officers as shown on Table 2. This implies that overall return rate for the study was 93.6%. Return rate for credit officers was slightly higher at 96.2% compared to that of credit managers.

Table 2: Return Rate

	Issued Questionnaires	Returned Questionnaires	Return Rate
Credit Managers	26	23	88.5
Credit officers	52	50	96.2
Total	**78**	**73**	**93.6**

4.2 General Information of Respondents

The study sought some general information about the respondents which included: their age, gender, position they held in the organization and their experience in credit management. The findings on these parameters is discussed in this section.

The age of respondents was measured on a continuous scale in years as shown on Table 3.

Table 3: Age of Respondents

	Current Position	N	Mean	Std. Deviation	Std. Error Mean
Age	Credit Officer	50	29.9	1.86	.26
	Credit manager	23	34.7	3.92	.82

The findings on Table 3 show that the mean age of credit officers was 29.9 years whereas that of credit managers was 34.7 years.
The second parameter of interest was the gender of respondents which was determined categorically as male or female; the findings were shown on Table 4.

Table 4: Cross Tabulation of Gender and Current Position

			Current Position		
			Credit Officer	Credit manager	Total
Gender	Male	Count	28	8	36
		% within Current Position	56.0%	34.8%	49.3%
	Female	Count	22	15	37
		% within Current Position	44.0%	65.2%	50.7%
Total		Count	50	23	73
		% within Current Position	100.0%	100.0%	100.0%

As shown on Table 4, the number of female staff in the credit departments was slightly higher than that of male staff at 50.7% and 49.3% respectively. Majority of the credit managers (65.2%) were male while 34.8% were male. The gender distribution of credit officers was different where 56.0% were male while 44.0% were female. This shows gender balance in employment at the Equity Bank, Credit Division with leadership roles skewed to the female gender.
The other demographic parameter of interest to the study was the experience of respondents in credit departments. This was measured in years on a continuous scale and the findings presented on Table 5.

Table 5: Experience in Credit Department

	Current Position	N	Mean	Std. Deviation	Std. Error Mean
Experience in Credit Department	Credit Officer	50	3.48	1.18	0.17
	Credit manager	23	3.17	0.78	0.16

The average experience of the credit staff at equity bank varied across the two categories of respondents. However of concern was that the age of credit officers was slightly higher than that of credit managers at 3.48 years and 3.17 years respectively. However, the difference in the years of experience was not statistically significant $t(71) = 1.132$, $p > 0.05$. This implies that promotion of credit officers to management position was not based on the years of experience but on other factors such as performance and education level. The average experience of above three years for the two categories of staff imply that the respondents were in a position to understand the mobile loaning platform offered by the bank, thus their responses were reliable.

4.3 Application of Credit Risk Control on Eazzy Loan

The study sought to appraise the application of credit risk control practices on Eazzy Loan of Equity bank, Kenya. The indicators used to measure the application of credit risk control practices were:

i. Quantification of credit risks
ii. Individual risk control
iii. Portfolio risk control
iv. Credit limits
v. Risk policies and procedures

vi. Oversight Committee on performance of Eazzy Loan
vii. Internal controls
viii. Periodic reviews
ix. Internal audits

Table 6 presents results of application of credit risk control practices on Eazzy Loan of Equity bank, Kenya

Table 4. 1: Credit Risk Control Practices on *Eazzy Loan*

	Strongly Agree	Agree	Undecided	Disagree	Strongly Disagree	χ2	ϱ
The bank has internal mechanisms for quantification risk presented by *Eazzy Loans*	16 (21.9%)	33 (45.2%)	19 (26.0%)	5 (6.8%)	0 (0.0%)	99.6	0.02
There are well laid plans to address emerging credit risks	14 (19.2%)	29 (39.7%)	16 (21.9%)	14 (19.2%)	0 (0.0%)	95.4	0.01
There are risk control mechanisms for individual *Eazzy Loan* borrowers	15 (20.5%)	27 (37.0%)	21 (28.8%)	10 (13.7%)	0 (0.0%)	80.9	0.03
The entire *Eazzy Loan* portfolio is regularly assessed and risk control measures put in place	23 (31.5%)	26 (35.6%)	9 (12.3%)	15 (20.5%)	0 (0.0%)	71.9	0.02
There well defined limits on the credit provisions for *Eazzy Loan*	25 (34.2%)	39 (53.4%)	8 (11.0%)	1 (1.45)	0 (0.0%)	55.6	0.04
The company has well defined policies and procedures for treating risks emanating *Eazzy Loan*	25 (34.2%)	23 (31.5%)	5 (6.8%)	7 (9.6%)	13 (17.8%)	93.5	0.02
There is an oversight committee that reviews the performance of *Eazzy Loan* to inform future paths	12 (16.4%)	24 (32.9%)	21 (28.8%)	9 (12.3%)	7 (9.6%)	93.8	0.03
The Oversight Committee ensures effective internal control programs	20 (27.4%)	30 (41.1%)	23 (31.5%)	0 (0.0%)	0 (0.0%)	53.4	0.04
There were periodic reviews in response to changes in laws, regulations, asset size and organizational complexity	25 (34.2%)	33 (45.2%)	15 (20.5%)	0 (0.0%)	0 (0.0%)	31.9	0.05
There are access controls for *Eazzy Loan* information and databases	22 (30.1%)	27 (37.0%)	12 (16.4%)	12 (16.4%)	0 (0.0%)	93.9	0.02
The bank conducts internal audits to assess performance of *Eazzy Loans* in line with set principles of lending	24 (32.9%)	31 (42.5%)	15 (20.5%)	3 (4.1%)	0 (0.0%)	56.7	0.04

The study revealed that the bank had internal mechanisms for quantification of risks presented by Eazzy Loans with a majority of the respondents (67.1%) agreeing with it. A small proportion of 6.8% of the respondent disagreed while 26.0% were not decided. Further analysis using the chi-square test revealed ($\chi 2 = 99.6$, $\varrho = 0.02$) which implied that application of internal mechanisms for quantification risk as credit risk practice was a significantly working.

There were also well laid plans to address emerging credit risks from the mobile loaning platform. This was evident as 58.9% of the respondents agreed with the fact that the bank had well laid down plans to address emerging credit risk. Having well laid plans for addressing emerging credit risks was said to be a good credit risk control practice ($\chi 2 = 95.4$, $\varrho = 0.01$).

The study also sought to check whether there were risk control mechanisms for individual Eazzy Loan borrowers. Accordingly, 57.5% of the respondents agreed the bank applied risk control mechanisms for individual Eazzy Loan borrowers as a risk control practice. The risk control mechanisms was a significant credit control practice for Eazzy Loan ($\chi 2 = 80.9$, $\varrho = 0.03$).

The study sought to assess whether entire Eazzy Loan portfolio was regularly assessed and risk control measures put in place. Majority of respondents (67.1%) agreed that Eazzy Loan portfolio was regularly assessed and risk control measures put in place as credit risk control practice. Accordingly, 20.5% of respondents disagreed with the fact. Portfolio risk assessment and the corresponding risk mitigation measures were found to be significant credit control practice ($\chi 2 = 71.9$, $\varrho = 0.02$).

An overwhelming majority of respondents (87.6%) indicated that there well defined limits on the credit provisions for Eazzy Loan which was also found to be a significant credit control practice ($\chi 2 = 55.6$, $\varrho = 0.04$). A negligible 1.45% of the respondent disagreed that the bank had well defined limits on the credit provisions for Eazzy Loan. According to 65.7% of the respondent, the company has well defined policies and procedures for treating risks emanating Eazzy Loan. However, 27.4% disagreed which shows that to some extent the policies and procedures for treating risks emanating Eazzy Loan were not well defined. This notwithstanding, policies and procedures for treating risks emanating Eazzy Loan were a significant credit risk control practice ($\chi 2 = 93.5$, $\varrho = 0.02$).

The study established that 49.1% of respondents agreed that there was an oversight committee that reviewed the performance of Eazzy Loan to inform future performance and strategies. A percentage of 28.8 of the respondents were not aware whether such Committees existed. On the other hand, 21.9% disagreed with the fact that the bank had oversight committee that reviewed the performance of Eazzy Loan. However, presence of an active oversight committee was seen to be a significant credit risk control practice ($\chi 2 = 93.8$, $\varrho = 0.03$). Additionally, the study sought to whether the Oversight Committee ensured that there were effective internal control programs in the bank. A whopping 68.5% of respondents agreed that wherever the committee was functional, it ensured that effective internal control practices were in place. Although none disagreed with this fact, 31.5% were not sure whether the Committees were effective in instituting internal controls. Internal controls instituted by the Oversight Committees were seen to be a significant credit control practice ($\chi 2 = 53.4$, $\varrho = 0.04$).

To manage the mobile loaning risks better, the study revealed that the bank put in place periodic reviews of the service terms and conditions in response to changes in laws, regulations, asset size, and organizational complexity. This was cited by 79.5% of the respondents who agreed, the rest 20.5% were not sure whether there were periodic reviews in response to changes in laws, regulations, asset size, and organizational complexity while none of the respondents disagreed. Periodic reviews were found to have a close association with credit risk control and thus was significant risk control practice ($\chi 2 = 31.9$, $\varrho = 0.05$).

Access controls for Eazzy Loan information and databases was also present as observed by 67.1% of the respondents. This was a key risk control practice that would protect the bank against information risks. Access control to information and database was a significant control practice at ($\chi 2 = 93.9$, $\varrho = 0.02$) and thus minimized fraud.
Finally it was also established that the bank conducted internal audits as a routine credit control practice as identified by 75.4% of the respondents who agreed, 20.5% were not sure while 4.1% disagreed. Conducting internal audit to assess performance of Eazzy Loans in line with setting principles of lending was a significant credit risk control practice at ($\chi 2 = 56.7$, $\varrho = 0.04$).

5.0 Conclusion

In managing the credit risks associated with mobile loaning at the equity Bank, it was established that, the bank has internal mechanisms for quantification of risks presented by Eazzy Loans. There were well laid plans to address emerging credit risks from the mobile loaning platform as well as risk control mechanisms for individual Eazzy Loan borrowers. The entire Eazzy Loan portfolio was regularly assessed for the prevailing risks and relevant control measures in place. Limits on the credit provisions for Eazzy Loan customers with varying risk profiles was found to have a significant effect on performance of mobile loaning

The bank also had in place well defined policies and procedures for treating risks emanating Eazzy Loan. The Oversight Committees ensured that there were effective internal control programs for managing risks. There were periodic reviews of the service terms and conditions in response to changes in laws, regulations, asset size, and organizational complexity and the risks thereof. Access controls for Eazzy Loan information and databases was also present and finally the bank conducted internal audits to assess performance of Eazzy Loans in line with other elements of the loan portfolio and prudent credit management. Although there was an Oversight Committee that reviewed the performance of Eazzy Loan to inform its future performance, a high number of the respondents were not aware of its presence. In overall, the study established that all studied indicators of credit risk control practices were significant practices that all banks with mobile banking services should embrace.

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