CAUSES OF NON-PERFORMING LOANS OF CREDIT UNIONS IN GHANA

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ABSTRACT

The business of a credit union is to advance credit to members which is the main source of income. The inability to pay the loans as per the agreed repayment schedule contributes to the increasing amounts of non-performing assets. The sharp increase in non-performing loans is a matter of concern and this research considers the causes of non-performing loans on credit unions in the Greater Accra Region of Ghana. The reasons that have been attributed to borrowers' default on loan repayments are largely discussed and applicable recommendations that are likely to reduce the degeneration of these loans. Qualitative approach was used for the study where semi-structured interviews were administered to 30 of the 84 active credit unions in the region. The interview was conducted with credit union senior credit officers and borrowers to solicit their perspective. Borrowers and staff were also observed in their line of business to corroborate some of the factors identified during the interviews. Inclusive causes of loan defaults included adverse selection, inflation in the country, repayment period, and inadequate financial counselling. Notable among the recommendations included adequate training of members of staff, initiating incentive packages for borrowers who pay on schedule, and reduction of interest rate where possible to lengthen the repayment period and lessen the amount into manageable figures.

Keywords*: credit unions, non-performing loans*

1. INTRODUCTION

The primary activity of a credit union is to accept deposits and lend funds to individuals in the form of loans or advances. Hence, their main source of income is purely dependent on the loan activity which involves the risk that the borrower will not pay back the loan as promised.

The inability to pay the loans as per the agreed repayment schedule whether corporate organizations or individuals has contributed largely to the ongoing global financial crisis. Currently the biggest problem facing credit unions is the increasing amounts of nonperforming assets which have to be provided for in the credit union income statement or written off thereby affecting the performances of the credit union. A robust financial sector should be able to withstand negative economic shocks and contribute to the general stability of the financial sector and the wider economy.

If there is lack of liquidity and a considerable number of individuals find it problematic to honor their loan obligations, it will generate into default loans (Azeem *et al.,* 2017). Both internal and external factors have affected the amounts of loans that have been issued in the non-banking industry. This in return has fueled an increase in the non-performing loans.

Credit risk management is complex and unpredictable in an environment which is peculiar to the credit union industry. Yet the industry grants loans and advances to individuals, and business organizations in order to enable them undertake investments and other development activities as a means of contributing toward the economic growth in general and aiding economic development in particular. In the process, loan defaults are generated resulting from low quality of assets, high non-performing loans (NPLs) that result in loan losses and reduction in financial institution profitability. These NPLs hamper economic growth and reduce the economic efficiency.