



COLLEGE OF BUSINESS AND ECONOMICS

DEPARTEMENTES OF MANAGEMENT

**ASSESSING THE PRACTICE OF RISK MANAGEMENT IN CASE
OF COMMERCIAL BANK OF ETHIOPIA WOLKITE BRANCH**

**A RESEARCH PAPER SUMMETED TO DEPARTMENT OF
MANAGEMENT FOR THE PARTIAL FULIFILLMENT OF (BA)
DEGREE IN MANAGEMENT**

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Contents

Acknowledgment.....	i
List of Tables	iv
Acronym.....	v
Abstract.....	vi
CHAPTER ONE:	1
1. INTRODUCTION.....	1
1.1. Background of the Study.....	1
1.2. Statement of the Problem.....	2
1.3. Research Question	2
1.4. Research Hypothesis.....	3
1.5. Objective of the Study	3
1.5.1. General Objective of the Study.....	3
1.5.2. Specific Objective.....	3
1.6. Significance of The study.....	4
1.7. Limitation of the Study.....	4
1.9. Organization of the paper	5
2. LITRATURE REVIEW	6
2.1. Definition of Risk	6
2.2. Classifications of Risk.....	6
2.2.1. Pure and Speculative Risk.....	7
2.2.2. Fundamental and Particular Risks	7
2.2.3. Static and Dynamic risks.....	7
2.3. Types of Financial Risks.....	7
2.3.1. Liquidity Risk.....	8
2.3.2. Credit Risk.....	9
2.3.3. Interest Rate Risk	11
2.3.4. Foreign Exchange Risk.....	11
2.4. Risk Management	14
2.4.1. Definition	14
2.4.2. Objectives of Risk Management.....	15
2.4.3. Risk Management.....	15
2.4.4. Risk Identification:	16
2.4.5. Risk Evaluation:.....	16
2.5. Risk Management Techniques.....	17
2.5.1. Risk Avoidance.....	17
2.5.2. Risk financing Techniques	17
2.5.3. Risk Retention	18
2.5.4. Risk Transfer /Insurance/	18
2.5.5. Self-Insurance.....	19
2.6. EMPERICAL EVIDENCE	19
CHAPTER THRE.....	21
3. RESEARCH METHODOLOGY	21
3.1. Area of the study	21
3.2. The research design	21
3.3. Population and Sampling	21

3.4. Data Types and sources	21
3.5. Method of data collection	22
3.6. Data analysis and presentation	22
CHAPTER FOUR	23
DATA ANALYSIS, PRESENTATION AND INTERPRETATION	23
CHAPTER FIVE	33
5. CONCLUSION AND RECOMMENDATIONS	33
5.1 CONCLUSIONS	33
5.2 Recommendations	33
Reference	36
APPENDIX	37

WAKULISDI

List of Tables

Table 4.1 General information respondents	23
Table 4.2; General risk management system	25
Table 4.3 the techniques of risk management	26
Table 4.4 Credit risk management system	27
Table 4.5; Liquidity Risk Management Systems	30
Table 4.6; Interest Rate Risk Management System	31

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Acronym

CBE; commercial bank of Ethiopia

NBE; National Bank of Ethiopia

Ibid; the same source

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Abstract

The senior essay on the risk management practice was conducted on commercial bank of Ethiopia at Wolkite branch.

The researcher stated the statement of the problem both general and specific objectives and significance of the study. The researcher used descriptive data analysis method. To conduct the research, the researcher employed use primary data was collected through questioner on risk management practice. The data collected was analyzed using percentage and presented in tabular form base on identifiable problems. By increasing the independent variables researcher try to reduce error and the result were likely to be more accurate and precise. The financial performance would be measured by use of return on asset. The study also focused on financial risk as independent variable and more result the relationship between risk management and financial performance in commercial bank of Ethiopia. The researcher recommended that it was a high time for the bank to adopt a contemporary, proactive and decentralization risk management system if it tends to survive the thunders of local composition, the flood of globalization and the tremble of our dynamic market and economic condition.

Key word: - commercial bank of Ethiopia, risk management, descriptive data analysis

CHAPTER ONE:

1. INTRODUCTION

1.1. Background of the Study

Risk management is a logical development and implementation of plan to deal with potential losses. The purpose of risk management program is to manage an organizations exposure to loss and protection of its asset. Risk management benefits all types of organization facing potential losses including business, nonprofit organizations, individuals and families. Having clear understanding of all risks allow an organization to measure and prioritize them and take the appropriate action to reduce the loss. The existence of financial institution especially commercial bank is meaningless without managing risk of their various activities. Risk management processes are required to handle the risk that will occur in commercial bank. It is important to protect the reputation and public image of the commercial bank, to use up to date employees, technologies and machineries for its productivity and effective performance. For the development and effective risk handling, purchasing insurance and giving training to the employees of the corporation plays the greatest role of the activities of the bank in order to achieve the organization goals through the minimum use of man power. Technologies and machines, purchasing insurance and training to the workers are absolutely essential for any organization in order to enhance the operational performance management efficiency to satisfy their employees, local community, shareholders, customers & other stock holders. Operational risk management typically to cover broad range of the risk that are internal to an organization (Corrigan 1999).

While it will be impossible to list all risk confronting an individual in business we briefly line the nature of various risk that create financial in security such as personnel risk, property risk and liability risk. (Tekle George Aseffa 2004).

Therefore the researcher will be identified the major risk exposures, determine the best possible techniques to prevent risks and responsible agent in determining the bank risk.

1.2. Statement of the Problem

The risk managing practices are the most important activities for the organization reach its goals objectives as well as to maintain its competitive advantages. The risk management can add value to all most any situation where the possibility exists for services or catastrophic outcomes. The steps used to manage risk can be used at different levels of detailed and with varying degrees of formality. Depending on the key to using the process is computing each step in the most practical way provide the information. The information about possibility for one or more unrelated out comes separate risk based decision from traditional decision making. However, risk management practices are affected by so many factors. Such as lack of skilled manpower, budget deficits, lack of infrastructure like electronic, material structured and conductive policies concerned risk (Green 2003).

A problem related to the process of the bank in Wolkite branch which hinders or affects risk management practice are lack of employees training, inefficiency administrative staff, inadequate knowledge, lack of modern information system, poor communication network & lack of effective risk controlling policy.

1.3. Research Question

This study would try to answer or solve the following research questions

1. What is risk exposure in commercial bank of Ethiopia at Wolkite branch?
2. What kind of prevention techniques and controlling procedures used for risk management?
3. Who is most responsible agent in determining the bank risk?

1.4. Research Hypothesis

H0: There is no risk exposure in commercial bank of Ethiopia at Wolkite branch.

H1: There is risk exposure in commercial bank of Ethiopia at Wolkite branch.

H0: There are no prevention techniques and controlling procedures used for risk management.

H1: There are prevention techniques and controlling procedures used for risk management.

H0: There is no responsible agent in determining the bank risk.

H1: There is a responsible agent in determining the bank risk.

1.5. Objective of the Study

In line with the problem statement, this study has the following general and specific objectives.

1.5.1. General Objective of the Study

The overall objective of this study is assessing the practice of risk management in commercial bank of Ethiopia Wolkite branch.

1.5.2. Specific Objective

The study would focus on the following specific objective:

1. To assess the major risk exposures of the bank.
2. To determine best possible technique in order to prevent risk in the bank.
3. To assess the most responsible agent in determining the bank risk.

1.6. Significance of The study

The study was beneficial to providing information regarding the risk exposure of CBE in Wolkite branch and it was useful insight to the risk management to apply improved techniques to handle the risk.

The study used to relate the theoretical aspect with practical activities. In addition the researcher believes that the study serve as a reference material for both academicians and practitioners, It initiates the concerned bank to reassess its existing practices and put a renewed emphasis on this main issue and it initiates other interested researchers to carry out more extensive studies in the area.

1.7. Limitation of the Study

The research study was not free from limitation. There were some issues which had hindered the attainment of the study objectives. Some limitation that the researchers face was shortage of time and cost not to assess all aspect of the company operations, unable to get the desired information or lack of adequate information and during data collection some respondent was not willing to give information. The research work was also unable to get some information were company confidential and reserved from the research presentation.

1.8. Scope of the Study

This study had been delimited in geographically and conceptually. Geographically, this research was delimited in commercial banks of Ethiopia only Wolkite branch. Conceptually, this research focuses on assessing the practice of risk management.

1.9. Organization of the paper

This paper organized by five chapters, the first chapter is introduction followed by background of the study, statement of problem, research questions, objective of the study, significance of the study, and scope of the study. The second chapter was literature review. The third chapter was methodology of the study. The fourth chapter was data analysis and presentation. The fifth chapter was conclusion and recommendation.

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CHAPTER

2. LITRATURE REVIEW

2.1. Definition of Risk

There is no single definition of risk, economics, behavioral scientist, risk theorists, tacticians, and actuaries each have their own concept of risk .The researcher will try to give different authors view and definition for the word risk.

According to Trieschman, risk can be defined as uncertainty concerning losses. The risk surrounding a potential loss creates significant economic burdens for business. Government and individuals Billions of Dollars are spent each year on strategies for financing potential losses. But when loses are not planned for in advance, they may cost even more. Business as well as individuals may try either to avoid risk as much as possible or to reduce risk, the opportunity cost activities forgone due to risk considerations, expenses of strategies to finance potential loses and the cost of a reimbursed losses. (Willies, Jr, et.al) 1998, 8th edition) (Thichmann, James and custaaoun, scndardchance of loss but no chance of gain, for instance, the owner of a car faces risk of collusion loss, if collusion occurs, he will suffer financial loss, if there is no collusion he will not be benefited. But speculative risk is a type of risk exists when there is a chance of gain as well as a chance of loss, pure risks are always distasteful but speculative risks possess some alternative features. It exists when their uncertainty about an event that could produce either a profit publishing 1998, 10th edition)

2.2. Classifications of Risk

- Pure and speculative risks
- Fundamental and particular risk
- Static and subjective risk

2.2.1. Pure and Speculative Risk

Pure risk is a type of risk exists when there is loss. In any situation involving speculative risk the society may be benefited even through the individual is hurtled. (Trencherman, Jems and Custavom, Sandra)

2.2.2. Fundamental and Particular Risks

A fundamental risk is risk that affects the entire economy or large number of persons or groups within economy. It involves on losses that are impersonal in origin and consequence and they are group risks mostly caused by economic, social and political phenomena, on the other hand particular risk is a risk that affects only individuals and not the entire community. It involves loss that arises out of individual events and is felt by a single individual rather than by the entire group.

2.2.3. Static and Dynamic risks

Static risks are those risks, which would occur even if there were no changes in the economy. These risks include losses caused by the regulation of the force of nature or human errors. On the other hand, dynamic risks are those risks resulting from changes in the economy. Changes in the price level, consumer tastes, income and out puts and technology may cause financial losses to member of the economy. These are risks related with changes in human wants. Although these dynamic risks may affect a large numbers of individuals, they are generally considered loss predictable than static risks, since they do not occur with any precise degree of regularity. (Triecheman,et.al).

2.3. Types of Financial Risks

Financial risks, which this study specifically deals with, in the comprise two types of risks. Pure risk including liquidity, credit and can result in loss for a bank if they are not properly managed. Speculative risks based on financial arbitrage, can result in a profit, if it is properly managed. Financial risks are subject to complex interdependencies that may significantly increase a bank's overall risk profile. For example bank engaged additionally to liquidity and interest rate risks if the bank

carries open positions. (Greuning, et.al).The main categories of speculative risk are interest rate and market price rate.

2.3.1. Liquidity Risk

Liquidity risk is a condition of an individual or business where in a high percentage of the assets can be quickly converted in to cash without involving any considerable loss by accepted sacrifice prices.

Liquidity implies a high degree of current and solvency in the equity sense, the ability of current assets will be able to meet current liabilities as they mature.

Liquidity risk can also be defined as uncertain future out comes that either improve or worsen the present liquidity position of the company. It may mean that holding idle cash on one hand or failure to eat financial commitments when they are due on the other holding idle cash is costly to say the least whereas failure to meet the financial commitment may imply demise the worst case scenarios.

Therefore, the purpose of liquidity risk management is to help the bank project to the worst scenarios meet its financial commitment at a minimum cost. (GreuningHennie van et.al) 2003, 2nd edition)

Fund mobilization, fund application, quality service, branch and application of new technology are the critical issues that can be emphasizes by management in minimizing liquidity risk fund raising is not limited to deposit mobilization, borrowing and equity contribution are other sources of fund raising. These are dependable sources of fundraising, which are attainable even in times of adverse circumstance to insure dependable risk weight asset ratio.

Branch network expansion is another critical issue that contributes to the broadening of customer base because it helps to attain the desired level of growth and to avoid the excessive dependence on particular sources.

Thus, monitoring both funding mix and the concentration of depositors help to control and mitigate unnecessary exposure to liquidity arises and avoid the vulnerability associated with such satiation.

The current problem in commercial bank is excess liquidity due to the prevailing poor credit appetite and the very limited investment opportunity in the economy. Periodic and continuous assessment of liquidity position of the bank can be a solution for these problems.

In general the crucial strategic issues within which liquidity risk management is un imaginable are fund mobilization, credit allocation (fund application) ,expansion of branch networks and the prevision of quality services through application of new and appropriate technology. (Ibid)

2.3.2. Credit Risk

Credit risk is defined as the chance that debtor will not be able to pay interest or repay the principal according to the terms specified in a credit agreement, credit risk means that payment may be delayed or ultimately not paid at all which can intern cause cash flow problems and affect banks liquidity. It exists in both banks on balance sheet accounts. GreuningHennie vanet.al.,(2003), 2nd edition.

2.3.2.1 Causes of credit risk

A bank is successful when the risks are reasonable, controlled within its financial resources and credit competence. The vital issues for preservation of the quality of loans are existence of a well-developed policies and procedures, strong portfolio of management, effective credit controls and the most critical element of all well trained staff that is qualified to implement the system. Conversely, absence of adequate guidelines to monitor administration of the lending function pave the way for the occurrence of substantial amount of problem on loans. Therefore, there are many causes for the occurrence of credit risk. Some of these are:

Excessive Concern for income Growth: the loan portfolio is usually the most important sources of income. Hence growth of the loan portfolio becomes a local point

to boost the revenue, however, too much concern for revenue maximization must not permit extension of weak loans that carry undue risks, generally, weak loans cost for more than they contribute income for the bank.

Incomplete information: character and capacity may be determined using different means. However, complete credit information is the best acceptable, reasonable, and accurate method for determining a borrower's financial standing. Lack of supporting credit information is an important cause of credit risk. Therefore, adequate and comparable financial statements and other pertinent statistical data should be available in order to minimize the associated with loans.

Competition: competition among banks for market and to influence community may result in the compromise of credit principles and the acquisition of unsound loans in which its ultimate cost exceeds its temporary gains in growth.

Technical Incompetence: the ability to analyze financial statement and to obtain and evaluate other credit information thereby protecting in the placement and supervision of loans in processed by all qualified and experienced bankers. Hence, the management should seriously be concerned with the hiring of such employees. In general, controlling the above listed factors and several others, which impede growth of the bank? Therefore, financial officers and management at all levels should be seriously concerned in order to minimize the occurrence of such risk. (Ibid)

2.3.2.2 Types of Credit Risk

Credit risk, which that is the risk that the borrowed will default, can occur in different forms are:

Direct lending risk, the risk that actual customer's obligations will not be repaid on time, which exists for the entire life of the transaction.

Contingent lending risk: the risk that a potential customer's obligation will become actual obligation and will not be paid on time. It occurs in products ranging from letter of credit and guarantees, which exists still for the entire life of the transaction.

Documentation risk: the risk that documentary evidence which depend on to enforce our rights under conducts, may not be complete, correct or inferable for loan to be repaid.

2.3.3. Interest Rate Risk

According to Edward PIM Gardener, interest rate risk refers to the exposure of an economic unit to movements in the market rates of interest. It is an important part of banking balance sheet management system, which is concerned with making the corporate trade-off, sticking the correct balance between profitability, Liquidity and capital adequacy or solvency (GreuningHennie van and Brantnovic, sonidRajovic WB 2003, 2nd edition)

All financial institutions face interest rate risk, when interest rates fluctuate, a banks earning and expenses, as well as the economic value of its asset's liabilities and off balance sheet positional so change. This risk is by its nature a speculative type of risk since its consequences may result in profit or loss.

2.3.4. Foreign Exchange Risk

The term foreign exchange refers to the simultaneous purchase of one currency and selling of on there as currencies are traded in pairs. Foreign exchange risk results from change in exchange rates between a bank's domestic currency and other currencies. It is risk of volatility due to mismatch and many cause a bank to experience losses as result of adverse exchange rate movements. (Greuning, et.al).

2.3.4.1. Different type of Quotation

Quotation can be made by telephone but the most common forms can make quotations now a day is on line quotations made by using computer system. Quotations may be taken in the form of spot, fore ward, hedging and options.

Spot transaction: spot transaction refers to the type of straightforward (out ward) exchange of one currency with the other. The spot rate is the current market price or bench mark price, settlement of spot transactions conventionally must be settled two business days after the deal date. (GreuningHennie van, et.al) 2003, 2nd edition.

Fore ward transaction: refers to the type of transaction where settlement will be done on après-agree date, which will fall three or more business days after the deal date. Such quotation takes spot rate as a base and adjustment will be made taking in to account exchange and interest rate fluctuations.

Hedging Transaction: refers to a quotation for getting a fixed rate to day to cover future commitments so that settlement will be done neither at again nor at a loss in the future vis-à-vis the local currency. Such quotation takes spot rates as adjustment will be made taking in to account exchange and interest rate inflations.

2.3.4.2. Factors Affecting Foreign Exchange Market

There are a number of factors that affect a foreign exchange markets influencing the value of currencies, some of these are

- Change in interest rates of a currency affects the value of currencies in that they arises interest rates of a currency by raising exchange rate.
- The rate of inflation that is the higher the rate of inflation, in the economy of a country they lower will be the demand for the currency to result in decrease of the value.
- The country's economic and political stability have also impact with the demand and supply of currency, the local currency will be strong
- National bank intervention's either in interest rate or exchange rates have an impact on value of currencies depending on the position taken by such bank.
- The larger the market orders for comedies, services or currencies which prevail in a given country, the more volatile will be foreign exchange rates depending on the level of supply.

2.3.4.3. Risks in Foreign Exchange Operation

Risk for different kind and magnitude are expected in any institution, which engages it international trade as settlements of such transactions involve at least two different currencies and contracting parties, foreign exchange risk arises from exchanges in

exchange rates in relation to is attached value of assets and liabilities denominated in different currencies and their impact on local currencies.

Foreign exchange by itself and all other activities that require exchange of currencies are risky by their nature as they necessary rates the activities of measuring ,pricing accepting when appropriate and managing.

There are so many factors that affect foreign exchange there by forcing participants to identify, measure, and manage risk exposures. Risk exposures may result from market risk, transaction risk, economic risk, transaction risk and settlement risk. (GreuningHennie van et.al) 2003, 2nd edition.

Market risk: refers to exposure to adverse price changes for a dealer, which includes two major components of exchange and interest rate risk. Exchange rate risk arises from change in value of currencies at closing moment of trading which will be influenced by the demand and supply of each currency during a trading session.

Transaction Risk: refers to the price based impact of exchange rate exchange on foreign receivable and foreign payables, the difference in price, at which they are collected or paid and the price at which they are recognized in local currency in financial statements.

Economic Risk: refers to the impact on exchange rate exchanges on a country's long term or company competitive position as it may cause decline in imports and larger exports.

Transaction Risk: refers to the impact of exchange rate changes on revolution of foreign currency position at the time of financial reporting or periodic consolidation of financial statements.

2.4. Risk Management

2.4.1. Definition

Risk management has been defined by different authors based on their area of emphasis and their attitudes to words their exposure, accordingly the researcher has tried to indicate different authors view in the following manner.

According to Triechaman risk management is a managerial process that involves the executive function of planning, organizing, leading and controlling those activities in a firm that deal with specified types of risks in order to maximize the value of an organization. The risk manager is charged with minimizing the value of an organization. The risk manager is charged with minimizing the adverse impact of losses on the achievement of the company's goal. (Greuning , Hennic van et.al) 2003).

Risk management is the specific approach to the problem faced by business that deals with the techniques of forecasting future so as plan, organize direct and control, efforts to minimize the adverse effect of those potential losses. It is the reduction and prevention the unfavorable effects of risk at a minimum cost through its indecision measurement and control.

According to William Jr, risk management is a general management function that seeks to identify, assess & address the causes and effects of uncertainty and risk in an organization in order to attain the goals and objectives that organization in the most direct, efficient and effective path it is a systematic way of protecting business resources and in come against losses so that the organization's aim are reached without interruption, crediting stability and canter butting to profit. (Sandra .G et.al, 1998).

Risk managements is a scientific approach to dealing with pure risks by anticipating possible accidental losses and designing & implementing procedure that minimize the occurrence of losses or the financial impact of losses that do occur. It is a systematic process for the identification and evaluation of pure loss implementation of the most appropriate techniques for treating such exposure. It focuses on a part of the total

bundle of risks, those that are classified as “pure risk” as a general rule, the risk manager is concerned with the management of pure risk ,not speculative risk and all pure risks are considered ,including those that are uninsurable . Hence, risk management is the identification, measurement and treatment of property, liability and personnel pure risk exposures.(Bratanovic et.al).

2.4.2. Objectives of Risk Management

Risk management has several important objectives that can be classified as pre loss and post loss objectives, pre loss risk management objectives are objectives prior to the occurrence of losses such as reduction in anxiety, analysis of safety program expenses and meeting external obligations were as post objectives are important risk management objectives that can be meet after the occurrence of loss such as survival of the firm ,continuity of perdition ,stability of earning per share and continued growth by developing new products \$ market or by acquisition and mergers. The first step in the risk management process is the determination of the objectives of the risk management program. In other words, the risk manager and other related departments should participate in deciding the expectation of the organization and its risk management program if it is less effective then it could be. In the absence of where at objective, there is a tendency to the view the risk management process as a serious of individuals isolated problems, and there are no guidelines to provide for a logical consistency in dealing with the risks that the organization faces. Therefore, management objectives serve as a prime source of guidance for those charged with responsibility for the program and also serve as a means of evaluating performance (Williams, Jr, 1998, 8th).

2.4.3. Risk Management

In order to have effective risk management program, the risk managements or manager must take certain general steps that can be systematically analyze and deal with the risk. These are:

- Identifying potential losses
- Evaluating potential losses

- Implement and review decision
- Evaluating and controlling the result

2.4.4. Risk Identification:

Risk identification is the process by which a business systematically and continuously identifies property and personnel exposures as soon as or before they emerge.

Unless the sources of possible losses are recognized, it is impossible to consciously choose appropriate and efficient methods for dealing with those losses should they occur. Risk identification is very difficult process because the risk manager has to look in to all operations of the company. So as to identify where exactly risk emanate from It is a continuous of job for the risk manager since risk environment is dynamic.

Approach used by many risk managers involve ,losses exposure checklists ,financial statement analysis, flow charts, contract analysis, on site in section and statically analysis of past losses, loss exposure checklist a risk identification tool that can be used by business and individual ,which specifies name row potential sources of losses from the destruction of assets and from legal liabilities risks. Financial statements analysis is another approach that can be used by business to identify, risks. Using this method all items on a firm's balance sheet and income statement are analyzed with regard to that may be present. By including budgets, long range, for casts and written strategic plans in the analysis, thus methods can also be help full in identifying possible future risks that may not currently exist. Flow charts are specially help full to business in identifying sources of risk in their production process. (Williams, JR, L. Smith)

2.4.5. Risk Evaluation:

After risks are identified, they should evaluate regarding their expected frequency of occurrence, the probable severity of associated losses, the maximum probable and possible losses. In this case the risk manager obtains information that is helpful in determining the relative importance of identified risks and in selecting particular techniques for managing those risks. As part of the overall risk evaluation, it may be

possible to measure the degree of risk in a meaningful way in some situation. (Reichman, James and Gustafson, Sandra)

2.5. Risk Management Techniques

The selection of appropriate risk management techniques is a dynamic problem. A best method for handling a particular exposure today may not be the best method to use next year because so many relevant factors change. The cost and availability of different risk management tools cannot be assumed to remain constant.

Thus the risk management plan that seems to be both effective and efficient in one year may not make as much sense in the next.

All of these factors make it clear that the risk management techniques should be, an ongoing one rather than an exercise that is performed once and then forgotten, within this framework there are four basic methods available for handling risk, these are, risk avoidance, loss control, risk retention, and risk transfer.

2.5.1. Risk Avoidance

Risk avoidance is a conscious decision not to expose one's firm to a particular risk of loss. It can be said to decrease one's chance of losses to zero. Risk avoidance is common particularly among those with a strong aversion to risk. However, avoidance is not always feasible and may not be desirable even if it is possible. Therefore the risk manager must always weigh the relative costs and benefits associated with activities that give rise to risks. When risks are avoided the potential benefits as well as costs are given up. If business is to operate at all certain risks are nearly impossible to avoid. (Gustafson, et.al, 1998).

2.5.2. Risk financing Techniques

After selecting appropriate risk management techniques to be applied in order to minimize the occurrence of various risks, the risk manager should look for the risk financing techniques because by no means we cannot avoid all risks rather we can minimize to a minimum level. According to there are four best techniques of financing

risk, these are, risk retention, self-insurance on insurance transfer and insurance. (James, et.al, 1998).

2.5.3. Risk Retention

It is the techniques of risk financing, which involves assumption of risk that is if a loss occurs, an individual or firm will pay for it out of whatever funds are available at the time. Retention can be planned or unplanned and losses that occur can either be founded or unfounded in advance, planned sometimes occurred even when the existence of risk is acknowledged.

Thus, even though the exposure is recognized, the firm is engaging in unplanned retention of losses that exceed its estimate of the maximum possible losses.

Many risk retention strategies evolve the intention to pay for losses as they occur without making any funding arrangements in advance of a loss. If a loss happens, it is paid out taking any funding arrangements in advance of loss, happens, it is paid for from the firm's current revenue. Such type of retention is unfounded retention. In contrast founded retention is made by making various pre-loss arrangements to insure that many are readily available to pay for losses that occur. In many situations the risk manager should consider several techniques as financial resources, ability to predict losses and feasibility of establishing a retention program in order to make decisions regarding retention. (Triechaman et.al) 1998, 10th edition).

2.5.4. Risk Transfer /Insurance/

Risk transfer or insurance is another risk financing technique, which involves payment by the transformer to the transferee (risk bearer). The transferee agrees to assume a risk that the transformer desires to escape. It reduces risk by combining under one management a group of objects situated so that the aggregate losses to which the insured become predictable within narrow limits, sometimes the degree of risk is reduced through the transfer process because the transferee may be in a better position to use of large numbers to predict losses, in other words cases the degree of

risk remains the same and is merely shifted from the transfer or to the transferee for the price. (Ibid)

2.5.5. Self-Insurance

If the firm has a group of exposure unit large enough to reduce risk and three by predicting losses, the establishment of the fund to pay for those losses is a special form of planned retention known as self-insurance. In this case there are two necessary elements of self-insurance. The first one is the existence a group of exposure units that is sufficiently large to enable accurate loss prediction and pre-funding of expected losses through a fund specially design for that purpose.

2.6. EMPIRICAL EVIDENCE

Internationally a good number of studies in the research area have been done. Mohad & Salina (2010) investigated the relationship between risk administration practice and financial execution of Malaysia Islamic banks. The period study covered 2006-2008. In order to measure the risk administration practice; the researchers used 5 components issues in regard to bank supervision practice as per the basel committee. The 5 components used in study are the firm risk management environment, policies and procedures of firm, risk measurement procedures, risk mitigation, firm risk monitoring and firm internal control. The study focused only the 3 independent variables as the risk management measure determining financial performance.

According to Wanjohi (2013) did study on the relationship between financial risk management and financial performance of commercial bank of Kenya. The study used the regression analysis equation to determine the relation between the variables. The components of risk management used as independent variable were the risk management environment of institution, risk measurement skill, risk mitigation procedure, risk monitoring and adequate internal control of the organization all those 5 segments of the risk administration were then connected with mean of return on asset for 5 years (2008-2012). The study Wanjohi identify acknowledge gap since the study only focused on the relationship between financial risk management and financial performance of commercial bank of Kenya. The study used only some independent

variable as compared to this study which has employed more independent variables hence reducing the error term.

Research gap exists since all the study reviewed on the management risk and financial performance in insurance firm have focused only on 3 independent variables so increasing the independent variables result in the reduction of error and the result are likely to be more accurate and precise. The financial performance would be measured by use of return on asset.

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CHAPTER THREE

3. RESEARCH METHODOLOGY

3.1. Area of the study

The study would be conducted on the risk management practice on performance of commercial bank of Ethiopia at Wolkite branch.

3.2. The research design

The study would be descriptive design type of research would be going to use, because the aim of the study would be to describe the risk management practice on performance of Wolkite branch.

3.3. Population and Sampling

The target populations of the study were employees of Commercial Bank of Ethiopia in Wolkite branch. The total populations of CBE in Wolkite branch were 36 in number, from those 32 males and 4 females. In order to get an information/data about risk management practice, the researcher would use all employees as a respondent to conduct this research because they were few in number and was not difficult to distribute questionnaire and make interview with employees.

3.4. Data Types and sources

For this study the researcher would be used both qualitative and quantitative type. This study used mixed approach.

Qualitative research approach was carried out when the researcher's wished to understand meaning, look at, describe and understand experiences, ideas, beliefs and values. It was general way of thinking about conducting qualitative research. Interview was best characterized this approach. Quantitative research approach was useful to answer the questions about the relationships among the variables with the purpose of explaining, predicting and controlling phenomena. Questionnaire was the best example. The researcher also use primary source of data. For this study primary data's

would collect data's were those which were actually directly collected from the sample unit of the study. Those primary data's had been collected through distributing questioners to the sample units, interview and observation.

3.5. Method of data collection

For this study the data had been collected from primary source of data. Those primary data collection method includes questionnaires, (Questions may be unstructured or structured.) Unstructured questions ask respondents to provide a response in their own words. Whereas, structured questions ask respondents to select an answer from a given set of choices. Structured interviews were an interview that had a set of predefined questions and the questions had been asked in the same order for all respondents and direct observation.

3.6. Data analysis and presentation

The information or data that were obtained through questionnaires in support of interview would be analyzed by using table, and percentages.

The researcher would give a meaning for the figure and items that would be presented through tables, and percent. The interview responses would be analyzed qualitatively whereas, the questionnaires quantitatively.

CHAPTER FOUR

4. DATA ANALYSIS, PRESENTATION AND INTERPRETATION

In this section, data obtained by way of questionnaire was analyzed and interpreted so that conclusion could be drawn based on findings. And the research design was descriptive because of risk management practice was required describing.

The questionnaires were distributed for 36 employees. Who has direct work relationship with the risk management practices of the Bank and 32 respondents had completed and submitted the questionnaire? The data acquired from the management, which was compiled and Annexed, was narrated here below.

Table.4 distributed and returned questionnaires to and by the management & officers of the Bank

Questionnaires	No. of respondents	Percentage of respondents (%)
Returned	32	89%
Not returned	4	11%
Distributed	36	100%

Table 4.1 General information respondents

Questionnaire	No. of respondents	Percentage (%)
Sex	Male	29 91%
	Female	3 9%
Total	32	100%
Educational Level	Diploma	2 6.25%
	Fist Degree	27 84.37%
	Above First Degree	3 9.37%
	Total	32
Position	Division Manager	4 13%
	Branch Manager	11 34%

	Marketing Officer	17	53%
	Total	32	100%
Service Year	Below 5 years	24	75%
	5-10 Year	7	22%
	Above 10 Years	1	3%
	Total	32	100%

(Source, survey 2019)

As we observe from the above table, the sex distributions of the respondents show that the majority of the respondents 29(91%) were males and 3(9%) were females. Educational level, from 32 employees 84.37% of respondent were first degree, 9.37% of respondents were above first degree, and 6.25% of respondents were Diploma. Therefore, the researcher was concluded that the majority respondents were first degree.

The position share of the responds constitutes 13% of the division manager, 34% of branch managers and 53% of them are marketing officers. This has an advantage to the researcher in that it was mainly marketing officers and branch managers who were involved in the Risk Management Process than Division managers that mostly authorizers of the request for credit approval, and other main decisions.

Service years, from 32 employees 75% of the respondents were less than 5 year of service, 22% of respondents were 5-10years and 3% of respondents were above 10 years. This also shows that the company was filled with youngsters and this which would have a positive impact on the performance of the banks. However the employees had not enough experience. So this leads to the banks unable to minimize risk and maximize profitability of banks performance. Therefore the bank was better hiring the experienced employees.

Table 4.2; General risk management system

Categories of work?	Item	No of respondents	Percentage (%)
	Professional and high level Management Group	14	44%
	Professional and medium level Group	7	22%
	Technical and Skilled	11	34%
	Total	32	100%
Do you believe that the science of risk Management systems is well Applied in the Bank?	Perfectly applied	8	25%
	Need some Adjacent	16	50%
	Not at all	8	25%
	I am not Quite aware of it	0	0%
	Total	32	100%
How do you rate the Quantity of risk Management system Adopted in CBE?	Excellent	23	72%
	Very Good	7	22%
	Fair	2	6%
	Poor	0	0%
	I have no idea	0	0%
	Total	32	100%

(Source, survey 2019)

The category of work distribution on the above table (4.2) shows that 14 employees (44%)of the participants were categorized under professional & high level management group, 7(22%)professional and middle level management and 11 (34%) are technical and skilled. Therefore the majority of the respondents were Professional and high level management group. So the researcher concludes that Categories of work in Professional and high level management group.

From the above table (4.2), second item 8 (25%) 66% of the respondents were perfectly applied, 16 (50%) respondents were need some adjacent, 8(25%) respondents were Not at all and the remaining 0% were I am not quite aware of it. Therefore, the

majority of the respondents were need some adjacent in the organization. So the researcher concludes that the science of risk Management systems is well Applied in the Bank. Need some adjacent in the organization.

From the above table (4.2), third item out of 32 respondents 23 (72%) respondents were responded Excellent, 7 (22%) respondents were very good, 2(6%) respondents were faire and the remaining were zero percent. therefore the researcher was concluded the majority of the respondents were responded Excellent. Therefore, from the above analysis majority of the respondents responded that risk management system was applied in the bank. Hence the management of risk applied in the bank, the errors related to risk were reduced.

Table 4.3 the techniques of risk management

	Item	No. of respondents	Percentage (%)
The techniques of risk management Today will be used year after year.	Strongly agree	2	6%
	Agree	24	75%
	Neutral	0	0%
	Dis Agree	6	19%
	Strongly Disagree	0	0%
	Total	32	100%

(Source, survey 2019)

In the above table 4.3, first item out of 32 the respondents 2(6%) strongly agree, 24(75%) respondents agree, 6(19%) respondents were disagree, and the remaining neutral and strongly disagree were zero percent. therefore the researcher was concluded that agree. The majority of the respondents responded that the techniques of risk management today will be used year after year, so the bank's ability to manage risk was high.

Table 4.4 Credit risk management system

CBE Adopted good credit risk management system.	Item	No. of respondents	Percentage (%)
CBE Adopted good credit risk management system.	Strongly agree	0	0%
	Agree	26	81%
	Neutral	2	6%
	Disagree	4	13%
	Strongly disagree	0	0%
	Total	32	100%
The bank asses borrowers past financial history, credit worthiness and perform detail financial analysis before extendandng the loans.	Strongly Agree	4	13%
	Agree	24	75%
	Neutral	1	3%
	Disagree	3	9%
	Strongly disagree	0	0%
	Total	32	100%
There is any Follow Up Mechanism of your customers after Granting a loan.	Strongly Agree	1	3.125%
	Agree	27	84.375%
	Neutral	2	6.25%
	Disagree	2	6.25%
	Strongly Disagree	0	0%
	Total	32	100%
When the borrower faces a certain problem and un abler to pay the loan, you apply extension of the life of the loan mechanism in order to the loan to be collected.	Strongly Agree	2	6%
	Agree	18	56%
	Neutral	4	13%
	Disagree	8	25%
	Strongly Dis agree	0	0%
	Total	32	100%
When the borrower faces a certain problem and un abler to pay the loan, you apply injection of additional loan mechanism in order to the loan to be collected.	Strongly agree	6	18.75%
	Agree	16	50%
	Neutral	4	12.5%
	Disagree	6	18.75%
	Strongly disagree	0	0%
	Total	32	100%
	Strongly agree	9	28%

When the borrower faces a certain problem and unable to pay the loan, you apply rearrangement of loan repayment structure mechanism in order to the loan to be collected.	Agree	16	50%
	Neutral	0	0%
	Disagree	7	22%
	Strongly disagree	0	0%
	Total	32	100%
From the total loans and advances guaranteed to its customers in which sector does the bank usually emphasized?	Agricultural sector	15	47%
	Manufacturing sector	6	19%
	Domestic trade and services	6	19%
	Building and construction	5	15%
	Transport sector	-	-
	Total	32	100%

(Source, survey 2019)

In the above table 4.4, first item out of 32 the respondents 0(0%) strongly agree, 26(81%) respondents agree, 2(6%) respondents were neutral, 4 (13%) disagree, and strongly disagree were zero. Therefore, the majority of the respondents were Agree on CBE Adopted good credit risk management system. From these the researcher conclude that commercial bank of Ethiopia Adopted good credit risk management system to improve its efficiency and effectiveness.

In the above table 4.4, second item out of 32 the respondents 4(13%) strongly agree, 24(75%) respondents agree, 1(3%) respondents were neutral, 3 (9%) respondents were disagree, and strongly disagree were zero. Therefore, the majority of the respondents were Agree. The bank assesses borrowers past financial history, credit worthiness and perform detail financial analysis before extending the loans.

In the above table 4.4, third item out of 32 the respondents 1(3.125%) strongly agree, 27(84.375%) respondents agree, 2(6.25%) respondents were neutral, 2 (6.25%) respondents were disagree, and strongly disagree were zero. Therefore, the majority of the respondents were agreeing on follow up any mechanism of your customers after granting a loan.

In the above table 4.4, fourth item out of 32 the respondents 2(6%) strongly agree, 18(56%) respondents agree, 4(13%) respondents were neutral, 8(25%) respondents were disagree, and strongly disagree were zero. Therefore, the researcher was concluded the majority of the respondents responded Agree. So the bank borrower faces a certain problem and unable to pay the loan, you apply extension of the life of the loan mechanism in order to the loan to be collected.

In the above table 4.4, fifth item out of 32 the respondents 6(18.75%) strongly agree, 16(50%) respondents agree, 4(12.5%) respondents were neutral, 6(18.75%) respondents were disagree, and strongly disagree were zero percent. Therefore the majority of the respondents were Agree. From these the researcher concludes that the borrower faces a certain problem and unable to pay the loan, you apply injection of additional loan mechanism in order to the loan to be collected.

In the above table 4.4, item six out of 32 the respondents 9(28%) strongly agree, 16(50%) respondents agree, 0(0%) respondents were neutral, 7 (22%) respondents were disagree, and strongly disagree were zero percent. Therefore the majority of the respondents were Agree. From these the researcher concludes that the borrower faces a certain problem and unable to pay the loan, you apply rearrangement of loan repayment structure mechanism in order to the loan to be collected.

In the above table 4.4, item seven out of 32 the respondents 15(47%) employees were Agricultural sector, 6(19%) respondents were manufacturing sector, 6(19%) respondents were domestic trade and services, 5(15%) respondents were building and construction, and transport sector were zero percent. Therefore the majority of the respondents were Agricultural sector. From these the researcher concludes that the total loans and advances guaranteed to its customers in which sector does the bank usually emphasized.

Table 4.5; Liquidity Risk Management Systems

There is any mechanism to fulfill the liquidity need of the bank in the case of deficit.	Item	No of respondents	Percentage
	Strongly agree	2	6%
	Agree	28	88%
	Neutral	0	0%
	Disagree	2	6%
	Strongly disagree	0	0%
	Total	32	100%
What are sources of fund raising do CBE currently relying?	Deposit mobilization	19	59%
	Borrowing	6	19%
	Equity contribution	7	22%
	Total	32	100%

(Source, survey 2019)

In the above table 4.5, in the first item out of 32 the respondents 2(6%) strongly agree, 28(88%) respondents agree, 0(0%) respondents were neutral, 2(6%) respondents were disagree, and strongly disagree were zero percent. Therefore the majority of the respondents were said agree any mechanism to fulfill the liquidity need of the bank in the case of deficit. From these the researcher understands that the organization uses mechanism to fulfill the liquidity need of the bank in the case of deficit and Liquidity degree of current and solvency in the equity of current assets will be able to meet current liabilities.

In the above table 4.5, in the second item out of 32 the respondents 19(59%) employees were deposit mobilization, 6(19%) respondents were borrowing, and 7(22%) respondents were equity contribution. So the majority of the respondents were deposit mobilization sources of fund raising do CBE currently rely. From these the researcher understands that the sources of fund raising do CBE currently rely.

Table 4.6; Interest Rate Risk Management System

Item	No of respondent	Percentage (%)	
There is any assigned department responsible for interest rate risk management.	Strongly agree	1	3%
	Agree	30	94%
	Neutral	0	0%
	Disagree	1	3%
	Strongly disagree	0	0%
	Total	32	100%
	There is any policy or procedure adopted in managing interest rate risk.	Strongly agree	4
Agree		21	65.625%
Neutral		5	15.625%
Disagree		2	6.25%
Strongly disagree		0	0%
Total		32	100%
CBE revises its interest rate structure in order to minimize the risk.	Strongly agree	2	6.25%
	Agree	20	62.5%
	Neutral	5	15.625%
	Disagree	5	15.625%
	Strongly disagree	0	0%
	Total	32	100%
The interest rate accurately works in the bank before the NBE fixes it.	Strongly agree	6	18.75%
	Agree	15	46.875%
	Neutral	7	21.875%
	Disagree	4	12.5%
	Strongly disagree	0	0%
	Total	32	100%

(Source, survey 2019)

In the above table 4.6, in the first item out of 32 the respondents 1(3%) strongly agree, 30(94%) respondents agree, 0(0%) respondents were neutral, 1(3%) respondents were disagree, and strongly disagree were zero percent. Therefore the majority of the respondents said on assigned department responsible for interest rate risk management were Agree. From this the researcher concludes that most of the time the bank was assigned department responsible for interest rate risk management.

In the above table 4.6, in the second item out of 32 the respondents 4(12.5%) strongly agree, 21(65.625%) respondents agree, 5(15.625%) respondents were neutral,

2(6.25%) respondents were disagree, and strongly disagree were zero percent. Therefore the majority of the respondents were Agree on policy or procedure adopted in managing interest rate risk. From this the researcher concludes that most of the time the bank adopted policy or procedure in managing interest rate of risk for the successes implementing and managing interest to the customer.

In the above table 4.6, in the third item out of 32 the respondents 2(6.25%) strongly agree, 20(62.5%) respondents agree, 5(15.625%) respondents were neutral, 5(15.625%) respondents were disagree, and strongly disagree were zero percent. Therefore the majority of the respondents were Agree CBE revises its interest rate structure in order to minimize the risk. From this the researcher understands that the bank revises its interest rate structure in order to minimize the risk. The risk manager was revised the interest rate to minimizing the adverse impact of losses on the achievement of the company's goal.

In the above table 4.6, in the fourth item out of 32 the respondents 6(18.75%) strongly agree, 15(46.875%) respondents agree, 7(21.875%) respondents were neutral, 4(12.5%) respondents were disagree, and strongly disagree were zero percent. Therefore the majority of the respondents were Agree on the interest rate accurately works in the bank before the NBE fixes it. From this the researcher understands that the interest rate accurately works in the bank before the NBE fixes it.

CHAPTER FIVE

5. CONCLUSION AND RECOMMENDATIONS

5.1 CONCLUSIONS

The bank has both strong and weak sides. Detail financial analysis of past financial history of the borrowers and forecasting of the future prospective development would enable the bank to identify the capacity of the borrowers and to process loan in the safest condition this is one of the bank's strong points. The other strong points of the bank is introduction of wide area network (WAN) which makes the bank to have efficient communication system with its branches easily and all current information would reach to the management on times so that timely decision would be made without savior damage or loss. Which is basically required to have such trend among other banks in Ethiopia so that they can adopt information technologies, which would enable them to communicate easily among banks? Unfortunately, however, the weak sides outweigh their antagonists. Most of them will be cited above in the analysis of the findings. Just too high light some of them: The bank should make the employees to aware about the policies, procedures and strategies of risk management system so that every employee would be a risk manager. It should also speculate its interest rate before the government determines it. The bank should make sectarian analysis in addition to evaluating the viability of the project so that it can handle its credit customers easily without exposing the company at risk.

5.2 Recommendations

Based on the fact observed from the questionnaire and unstructured interview, the following are recommended as possible solutions, which might alleviate the shortcomings and to reduce various risk management costs:

- The Management of CBE should arrange duplication of Risk management manuals, policies and procedures, prepare publications and distributes to employees [at least to the department level] so that every employee will have a clear understanding about the risk management process, policies and

procedures of the Bank so that they can protect the company accordingly and recommend alternative ways.

- The practical evidence indicates that the staffing system of the Bank is based on long stay on the job which is called life experience rather than qualification and job experience, therefore the Bank should assign qualified, professional and experienced individuals to their proper positions and it should also design adequate professional training scheme through providing off and on the job training, so that the risk management cost would update themselves with the dynamic nature of risk and the company will be better, competitive in the market & profitability performance.
- The Bank should speculate its interest rate risk before establishment of the rate by the government in order to minimize its expected risk. For instance when the lending rate in the marketing is high and saving rate is low, profitability of the bank would increase by lending more, so that the bank would encourage the investors to borrow and it's depositors to get more deposits by making diversified advertisement. On the other hand when lending rate low, and saving rate is high, the bank would not be benefited neither from lending nor saving account in this case the Bank should discourage both alternatives in order to minimize its risk. Therefore in order to manipulate such activities the Bank should perform speculation every time.
- As per the information obtained from the questionnaire, the actual practice indicates that CBE branch of wolkite doesn't specify a particular sector and emphasize on financing but it supports any viable business venture. However, the researchers believe that viability of the project doesn't mean that it is risk free and the actual practice may differ from the theoretical viability. Therefore, the Bank should make a detail sectarian analysis of each project and should determine/select/ the project with the highest profitability and minimum risk and emphasized on it.
- The banking business mostly faces various risks. Thus, CBE branch of wolkite should implement effective risk evaluation systems and identify the overall

risks by designing cost effective and efficient techniques in order to minimize the risk management cost and increase the overall return of the Bank.

The above recommendations should not be taken as conclusive guidelines and are not the only ones. The risk management committee & senior management of the bank should have the culture of gathering various suggestions from the employees and customers and revise its policies, procedures and develop new strategies, which are flexible in nature so that they could fit to the dynamic market environment.

Finally, the researcher would like to stress that it is a high time for the bank to adopt a contemporary, proactive and decentralization risk management system if it tends to survive the thunder of local composition, the flood of globalization and the tremble of our dynamic market & economic condition.

WIKULISD

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APPENDIX
WOLKITE UNIVERSITY
College of Business and Economics
Department of management

Research Questionnaires

Dear respondents this questionnaire is prepared by management Department Student. Its purpose is to write a senior essay entitled on assessing the practice of Risk management in CBE at Wolkite brunch. Your purposeful information is very important to-do this study. To be filled by employees of Commercial Bank of Ethiopia in Wolkite brunch.

Please mark your answers (x) or (√)

General information

1. Sex: A. Male B. Female
2. Educational level:
- A. Diploma B. First degree
- C. Above first degree D. Graduated
3. Position
- A. division manager
- B. Brunch Manager
- C. Marketing officer
4. Service year
- A. below 5 years B. 5-10 years

C. above 10 years

5. What seems like the categories of work?

Professional and high level management group

Professional and medium level group

Technical and skilled

6. Do you believe that the sciences of risk management systems are well applied in the Bank?

Perfectly applied

Need some adjacent

Not at all

I am not quite aware of it.

7. How do you rate the quantity of risk management system adopted in CBE?

Excellent

poor

Very good

I have note idea

Fair

8. The techniques of risk management today will be used year after year.

a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

9. CBE adopted good credit risk management system.

a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

10. The bank assesses borrowers past financial history, credit worthiness and perform detail financial analysis before extending the loans.

a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

11. There is any follow up mechanism of your customers after granting a loan.

- a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

12. When the borrower faces a certain problem and unable to pay the loan, you apply extension of the life of the loan mechanism in order to the loan to be collected.

- a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

13. When the borrower faces a certain problem and unable to pay the loan, you apply injection of additional loan mechanism in order to the loan to be collected.

- a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

14. When the borrower faces a certain problem and unable to pay the loan, you apply rearrangement of loan repayment structure mechanism in order to the loan to be collected.

- a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

15. from the total loans and advances granted to its customers in which sector does the bank usually emphasized?

- Agricultural sector
- Manufacturing sector
- Domestic trade and services
- Building and construction
- Transport sector
- Others.....

16. There is any mechanism to fulfill the liquidity need of the bank in the case of deficit.

- a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

17. What are sources of fund raising do CBE currently relying?

- Deposit mobilization
- Borrowing
- Equity contribution

Others.....

18. There is any assigned department responsible for interest rate risk management.

a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

19. There is any policy or procedure adopted in managing interest rate risk.

a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

20. CBE revises its interest rate structure in order to minimize the risk structure.

a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

21. The interest rate accurately works in the Bank before the NBE fixes it.

a. strongly agree b. agree c. neutral d. disagree e. strongly disagree

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