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Study on credit analysis for commercial banks in Libya: a case of Sahara bank

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ABSTRACT

Despite significant advances in many countries which measured by the extent of the progress and development of commercial banks. This study and evaluation of its credit activities became important so as to ensure its efficiency and effectiveness. Where, the credit activity is one of the most important activities, which ensure the significant reason for the importance of evaluation. The research aims to study and analyze credit banking which be applied at one of the commercial banks that operating in Libya (Sahara Bank). The main results of the study followed: a) the lower on the risk index of non-payment for loans and burdens and the lower of the safety margins to meet the risk of the loans. b) Despite the importance of measuring the cost of each activity separately to make sure of its efficiency and to keep track of any problems that may encounter this activity and affect its profit, but the accounting system that used does not provide data and information on the costs of each revenue activity. The most important recommendations that the Sahara Bank is measuring risk lending to provide periodic information useful and adoption of an accounting system properly with the need to provide qualified human cadres scientifically and practically.

Key words: *credit, commercial Bank, risk index, costs.*

Introduction

There has been increasing interest on the liberalization of international trade in financial services, the trend toward full information technology. The banking sector, particularly the commercial banks play an important role in the economic development and supporting the national economy, which represents as the most important financial institutions in the banking system, and offers many services and activities, both in developed and developing countries and the volume of such services and activities in the economies that goes under modernization and rapid growth. It should be noted that the emergence of commercial banks was linked to the emergence of money, developed by many factors have become so as they are today (Al-dessouki, 1994). The trend toward market economy and the policy of economic openness and liberalization produced by Libya at the present time and the accompanying to remove the restrictions to investment and ratifies private banks work, committed local banks need to keep abreast of developments, and to prepare itself at all levels, to work always training human cadres, modern management systems and developing accounting systems, in particular, technological infrastructure and research on possible means to reduce the costs of banking services and achieving high returns of the Bank, and this leads to the need to focus on the function of the bank credit as the financial center of any bank is affected by many variables and elements, but the loan portfolio in particular occupies an important position within the Center financial items, the safety of the loan portfolio to achieve high returns of the bank at the least possible levels of risks associated with resolutions of granting credit (Mounir, 1996).

Commercial banks simply do not go out from being a financial mediation function, which works through the allocation of financial resources to meet various needs in order to make a profit. Thus, investments in the form of credit types and different deadlines and guarantees to (achieve the highest return to cover the various cost elements of the academic cost of obtaining funds through cost management and use of these funds and secured to a safe cost recovery again or incomplete or non-existent if the risk in whole or in part. It is a necessity, not an option for commercial banks as long as wills and growth (even the credit activity of commercial bank in particular is one of the most important sources of revenue that was not Most important, despite the increased attention by the so-called bank services revenue in particular and comprehensive banking services (Khalil, 1997).

The granting of credit shape a crucial use for the funds of commercial bank and it is also the first source of its profitability, and for this reason the importance of evaluating all aspects of banking credit to ensure the continued growth and success of the bank and the financial ratios financial analysis tools used in the assessment of different types of activities, and can identify strengths and weaknesses in how to perform these activities.

In this context the purpose of this study is to accomplish through the evaluation of some aspects of credit banking, credit interest rates which determined by the Central Bank of Libya to lend the sources of funding, the cost of these sources, the liquidity and risk of credit, and the profitability (Central Bank of Libya, 1996).

The paper will also suggest that the Sahara Bank may follow the measuring risk lending to provide periodic information useful in measuring the risk of late payment and get the bank clear picture of what has of bad loans to the possibility of censorship and take decisions on them. In addition to preparing periodic reports to evaluate the guarantees of credits granted and internationally to give accurate information to measure the cost of administration and risk all credit activities and investment besides to see how efficiently these activities and accountable those responsible for these activities in accordance with the efficiency of the activities that they have done.

Literature review:

The literature has identified several problems with research in the credit analysis does not receive adequate attention so far. These problems can be grouped into two categories: i) the concept of credit bank to commercial banks and its related aspects which include the definition of credit bank and some aspects of credit bank, ii) financial ratios as tools to assess bank credit which includes performance assessment and appraisal for some aspects of credit bank. This section will review some of the evidence on the effects of these problems on the policy of economic openness and liberalization produced by Libya at the present time and the accompanying to remove the restrictions to invest and ratifies private banks work, committed local banks need to keep abreast of developments.

The concept of credit bank to commercial banks:

It is a necessity, not an option for commercial banks as long as growth (even the credit activity of commercial bank in particular is one of the most important sources of revenue that was not more important. Despite the increased attention by the so-called bank services revenue in particular and comprehensive banking services (Khalil, 1997) which declared as follows (M. Abdelaziz, 1994):

- 1-Provides funding for various sectors of economic activity.
- 2-Expand the work of financial intermediation in various fields including insurance, real estate and shipping.
- 3-Direct contribution in various types of projects and participate in governing and directing.

Credit can be defined as (the confidence Bank of clients, providing a certain amount of money to use for a specific purpose over a certain period and is repayable under certain conditions for return material agreed (Al Khudairi, 2010), or can be defined also as (exchange for current funds by promising of prospect funds, with adding up to specific and known benefit (Ahmed, 1999).

Focusing on some aspects of banking credit, and with the direct relationship with the question is the interest rate on credits granted creditor and credit financing sources (such as deposit-borrowing-property rights), and bank credit risk, liquidity and profitability, and below we review these aspects in some detail:

- a. Interest rate : in many countries the Central Bank as banks and bank supervisory authority that regulates commercial banks, the interest rate worth of loans granted by commercial banks to borrowers, and the price can be defined for that (the price paid for borrowing money, a percentage of the amount borrowed (Salloum, 1990).
- b. Sources of financing credit: according to the nature of the banking activity is a commercial bank of several sources of financing credit activity.

To have periodic evaluation of all activities of bank credit is important, especially credit (in order to detect potential hazards and avoid them before they occur, to avoid loss of funds and to ensure the circulation of these funds appropriately allows continuous liquidity for the Bank to grant more credit, achieved the objectives for which they were intended.

Financial ratios as tools to assess bank credit:

The importance of evaluating all aspects of banking credit is to ensure the continued growth and success of the banks and employ the financial ratios and financial analysis tools in the assessment of different types of activities, and it is able to identify the strengths and weaknesses in how to perform these activities as follows:

- a. Performance Assessment: Performance assessment can be defined as to ensure efficient use of available resources, and to verify implementation of planned targets (Abu-Alfutuh, 1995) and can be defined also as (a study and analysis of the strengths and weaknesses in the delivery of activities, both at the level of the individual or organization or any of its parts (Abdel Salam, 1995), there is no doubt that the Bank needs to assess its performance in various activities to ensure efficiency and success.

b. Appraisal for some aspects of credit bank: Using financial ratios to identify strengths and weaknesses in the area of banking credit, and there are several financial ratios to assess various aspects of bank credit. Financial ratios can be define as (monetary relationship between two variables, one extending and another denominator, it shows the share of units place the numerator (Abu- Alfutuh, 1994), can be define as the relationship between the two, and this relationship has no value, as compared to the other ratios, agreed, so called for the agreed reference, or industry to which it belongs (Walid, 1994).

Methodology:

In this paper, a part of the research will focus on the percentages that related to the aspects of credit, and with the sources of credit financing, liquidity sources, cost, and profitability. In order to analyze in a more systematic way, this section uses some tools to identify the factors that may significantly contribute to explaining differences in performance of the Sahara bank in Libya.

Analysis tools:

The next subsection explains in detail the methodology employed. In this paper the researcher can be able to introduce a percentage associated with three tips below:

i) **Employment rates:** there are several financial ratios can be judged on how the efficient to use or fund employment in the form of credit, and one of the most important ratios as follows:

Deposits in the form of loans= Loans/deposits x 100 (1)

Conventional loans resources= Loans (deposits + property rights) x 100 (2)

Resources in the form of credit=Loans (deposits + copyright + borrowing from other banks) x 100 (3)

The credit portfolio: measuring the relative importance of each of its components a percentage of the total value of the portfolio components.

ii) **Deposit ratio:** It is important to know how to configure the structure of commercial bank deposits, the deposits are the main source of financing of credit activity.

Ratio of deposits to assets= All kinds of deposits/total assets x 100 (1)

The proportion of deposits to total deposits= defined behavior and liquid deposits with the Bank (2)

iii) **Ratios assess the cost of funding sources:** Once calculating the average cost then it will be simple to calculate several ratios which including:

Cost ratio paid (weighted) = Cost paid/average value of funds x 100 (1)

Cost ratio paid to the sources= paid / (total value for money + demand deposit) x 100 (2)

The interest rate paid to the earning assets = Interest paid / average balance of assets that yield income x 100 (3)

The proportion of the total cost of funds invested = Interest paid + other costs / invested funds x 100 (4)

The average percentage of the interest paid on the loan financing sources = Total interest paid + salaries and public expenses / deposits from other bank loans + other borrowed funds x 100 (5)

Targeted weighted average cost = the total cost of the sources/total average assets x 100 (6)

i) **Liquidity ratios:** It assigns pointers on how to meet the cash requirements of the Bank, these proportions had nothing to do with the ratios of investment because of high liquidity ratios mean funds need to recruit, and one of the most important ratios as follows:

The liquidity ratio= Cash + current account stocks in the Central Bank and other banks + deposits with the Central Bank and other banks paid/all kinds of deposits + deposits cash and accounts address such as deposits + loans from other banks x 100 (1)

The average percentage of the average cash demand deposits = Average/average cash demand deposits x 100 (2)

This percentage represents how the contribution of interest rate received from loans to total income for the Bank.

Results and discussion

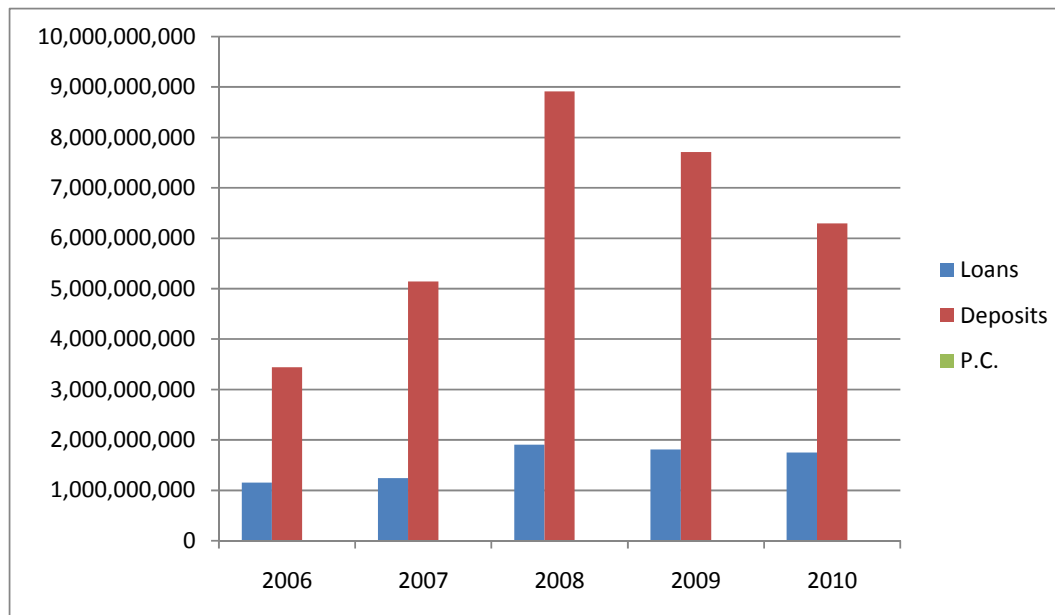
Empirical results:

Employment rates:

- i. The employment rate for deposits in the form of loans (Al-dessouki, 1994) = Loans/deposit x 100

Fig. 1: Shown the employment rate for deposits in the form of loans.

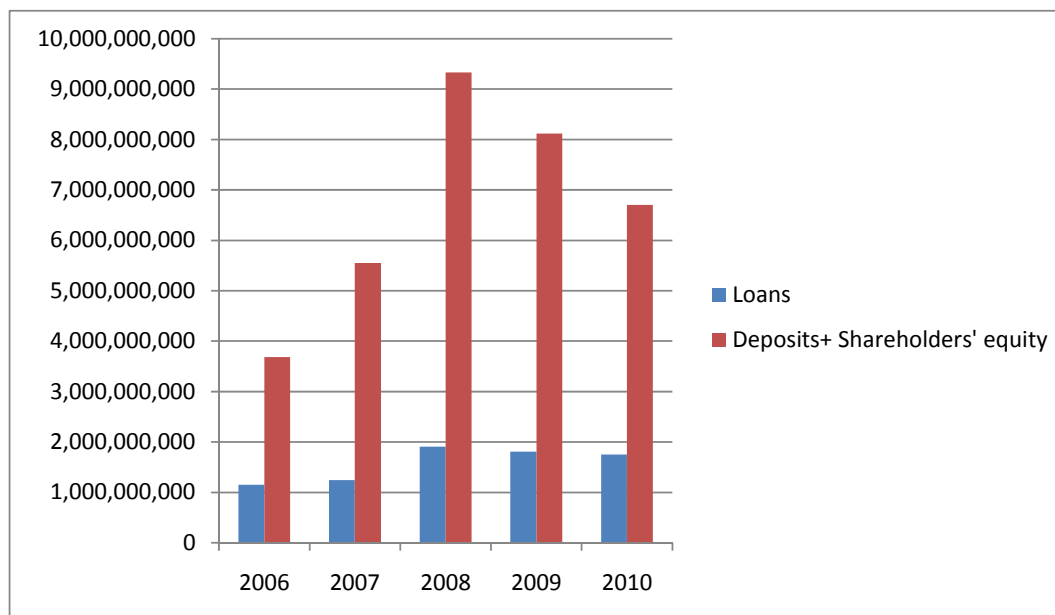
Statement	2006	2007	2008	2009	2010
Loans	1,152,120,064	1,240,082,386	1,902,654,593	1,811,909,195	1,750,596,053
Deposits	3,438,034,261	5,146,190,911	8,910,589,010	7,714,940,139	6,295,097,537
P.C	34%	24%	21%	23%	28%



- ii. The employment rate for conventional loans resources (Mounir, 1996) = $\frac{\text{Loans}}{\text{Deposits} + \text{property rights}} \times 100$

Fig. 2: The employment rate for conventional loans resources.

Statement	2006	2007	2008	2009	2010
Loans	1,152,120,064	1,240,082,386	1,902,654,593	1,811,909,195	1,750,596,053
Deposits+ Shareholders' equity	3,684,011,585	5,547,633,391	9,330,398,738	8,117,422,365	6,705,262,296
P.C	31%	22%	20%	22%	26%

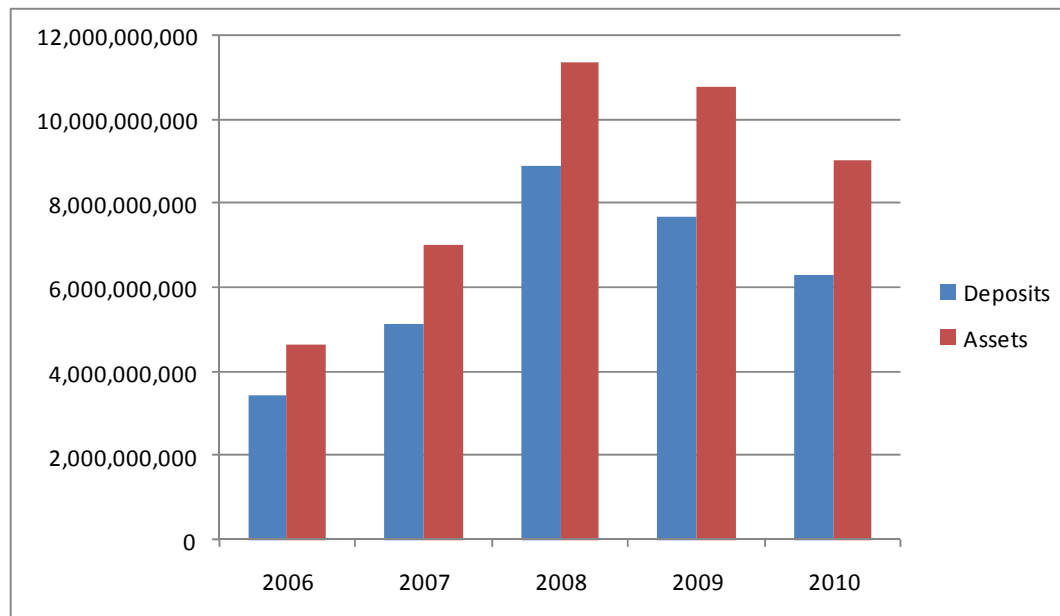


Deposit ratio:

I. Ratio of deposits to assets= All kinds of deposits/total assets x 100

Fig. 3: Ratio of deposits to assets.

Statement	2006	2007	2008	2009	2010
Deposits	3,438,034,261	5,146,190,911	8,910,589,010	7,714,940,139	6,295,097,537
Assets	4,646,388,925	7,012,387,778	11,388,091,613	10,811,227,145	9,044,968,336
P.C	74%	73%	78%	71%	70%

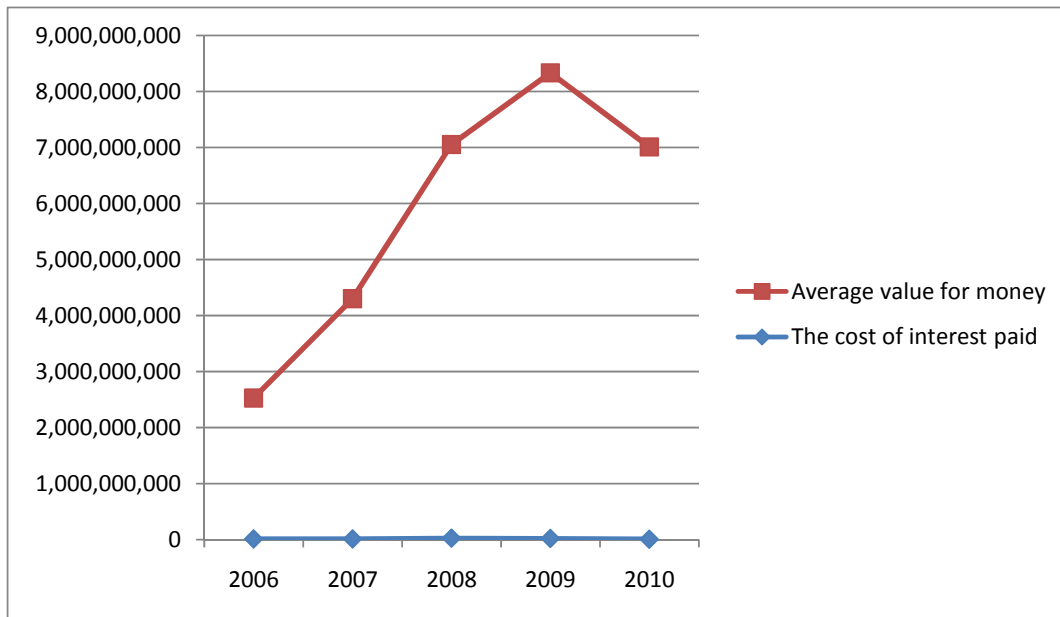


Ratios assess the cost of funding sources:

i. Cost ratio paid (weighted) = Cost paid/average value of funds x 100

Fig. 4: Proportion of costs (weighted) paid.

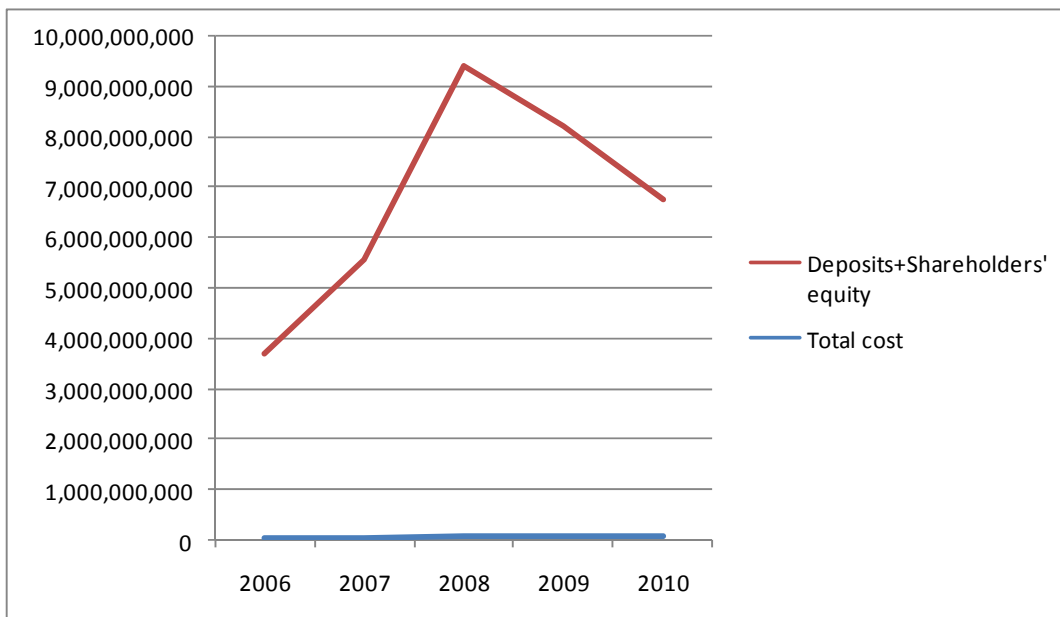
Statement	2006	2007	2008	2009	2010
The cost of interest paid	8,325,138	7,852,117	22,636,269	18,707,950	3,829,780
Average value for money	2,517,262,981	4,292,112,586	7,028,389,961	8,312,764,575	7,005,018,838
P.C	0.3%	0.2%	0.3%	0.2%	0.1%



ii. Cost ratio paid to the sources= paid / (total value for money + demand deposit) x 100

Fig. 5: Ratio of average total cost funding recourses.

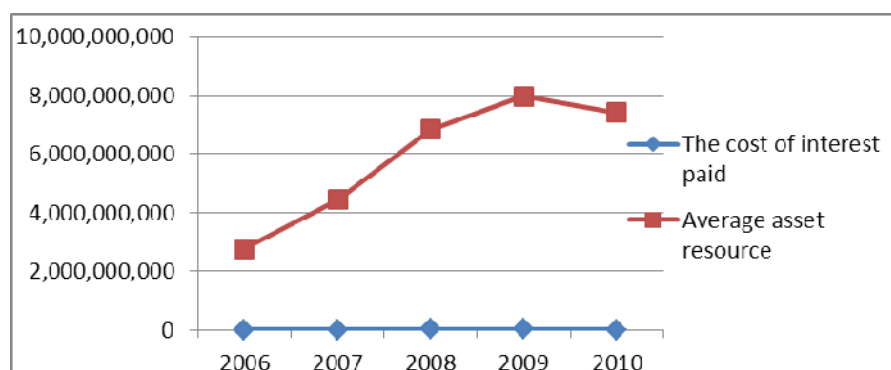
Statement	2006	2007	2008	2009	2010
Total cost	28,697,632	42,333,717	87,292,269	95,922,503	82,391,038
Deposits+Shareholders' equity	3,684,011,585	5,547,633,391	9,330,398,738	8,117,422,365	6,705,262,296
P.C	0.8%	0.8%	0.9%	1.2%	1.2%



iii. The interest rate paid to the earning assets = Interest paid / average balance of assets that yield income x 100

Fig. 6: Interest rate paid for the earning assets.

Statement	2006	2007	2008	2009	2010
The cost of interest paid	8,325,138	7,852,117	22,636,269	18,707,950	3,829,780
Average asset resource	2,763,333,598	4,440,051,477	6,834,402,244	7,970,729,824	7,414,408,604
P.C	0.3%	0.2%	0.3%	0.2%	0.1%



From the analysis on the credit for Sahara Bank in Libya, it is achieving the objectives regarding the assessment of the banking credit aspects (credit sources of funding - the cost of these sources - liquidity - credit risk - profitability). Based on the earlier analyzes the paper was accomplishing the results with the details below:

It is not practical to determining how much money available for hire in the form of credit during the fiscal year following the scientific methods, but is granted credit relying entirely on the experience officials' process and without planning or prior study.

Furthermore, it is meaningless supporting Sahara Bank to borrow from other banks as a funding source, and note that clearly because the value of the employment rate for traditional resources are the same as the value of the employment rate of available resources.

It is the wrong way to put predict adequate cash reserves to be duty retention according to the size and behavior and the type of deposits held by Sahara Bank, which refers to the absence of system budgets discretionary.

Make sure the development of accurate estimates of the cost of the target for cash reserves to be maintained to meet the work requirements, liquidity and comparing actual results and tracking reasons differing and addressed to ensure control cost, liquidity and control them.

Conclusion and recommendations:

In this paper, it appears that credit issued by the bank is incidental to its major functions of making, executing, and interpreting the law. The commercial banks have undertaken this specialized function. Their business is the issue and guaranty of credits for business uses; they are dealers in credits, and are sometimes, although too narrowly, called "manufactories" of credit. The fundamentals of banking, however, are most easily grasped from the point of view of purely commercial credit operations. There is an imperative need to modify the credit and financial services delivery system to achieve greater inclusion. The implementation of the recommendations made in this Report could go a long way to modify particularly the credit delivery system of the banks and other related institutions to meet the credit requirements policy. While banks and other financial institutions can also take some efforts on their own to improve the absorptive capacity of the clients, it is equally important for Government at various levels to initiate actions to enhance the earnings capacity of the Sahara bank.

The following recommendations proposed to overcome some shortcomings in its performance and credit as follows:

Despite the importance of benefiting from past experience of the officials on the credit operations, but the planning is to facade all the variables affecting the adoption of scientific methods to determine how much money available for hire in the form of credit during the financial year.

Take advantage of the sources of funds and self is self available to the bank and by adopting the concept of banks overall with the need to manage its activities diverse efficiently, and seek with the banking system towards the development of the laws regulating the banking business in order to keep up with trends in modern banking credit (such as credit leasing and loan variable interest and credit cards).

The expansion in the granting of credit facilities (overdraft), one of the largest investment credit of the bank is not Qaeda credit, has its rules and tactics technical and usually given in the form of temporary and non-recurring and their clients financial centers are excellent and based on credit studies scientific depth carried out

by the bank itself, so that any negligence in assets and foundation grant is one of the most important reasons for credit risk.

Finally an integrated system of budgets estimated to achieve predictable good cost target for funding sources and comparing the actual cost and track reasons differ and addressed to ensure cost control and control, and also predict the appropriate cash reserves to be maintained to meet the liquidity requirements and work according to the size and behavior and type deposits located has.

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