
FINANCIAL FRONTIERS: THE CRITICAL IMPACT OF CREDIT RISK MANAGEMENT ON INDUSTRIAL GROWTH IN NIGERIA

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Abstract

The research scrutinizes the pivotal role of credit risk management in fostering the industrial growth within Nigeria, titled "Financial Frontiers: The Critical Impact of Credit Risk Management on Industrial Growth in Nigeria." The study aims to delineate the influence of credit term policy, credit standard, and collection policy on the return on assets (ROA). Employing an ex post facto research design, the investigation encapsulated thirteen firms listed on the Nigerian Stock Exchange, focusing on four major industrial goods companies—Berger Paints Plc, Premier Paints Plc, Beta Glass Plc, and Cap Plc. Data spanning from 2014 to 2019 were meticulously analyzed, sourced from annual reports and financial statements. Findings reveal that credit term policy, credit standard, and collection policy significantly and positively influence the ROA. The research advocates that industrial firms should incentivize early credit settlements through discounts to enhance compliance with credit terms and conditions. Furthermore, it underscores the necessity of frequent reassessments of the collection policy, positing that such reviews significantly bolster firm profitability.

Keywords: Credit Risk Management, Industrial Growth, Return on Assets (ROA), Collection Policy, Nigerian Industrial Sector

INTRODUCTION

Credit serves as a cornerstone in the realm of business, where the essence of risk management lies in the proactive anticipation and evaluation of financial risks, along with the implementation of strategies to mitigate or eradicate their adverse impacts (Ikiaio, 2015). The significance of risk management is increasingly acknowledged across both the financial and non-financial sectors. The process of credit risk management is essential, involving strategic decision-making to minimize the risks associated with credit assets and to account for potential loan defaults (Tanui, Wanyoike & Ngahu, 2015).

Trade credit agreements, constituting formal business contracts, enable sellers to extend deferred payment options for their goods, eschewing immediate cash transactions. In an economic landscape characterized by volatile financial markets, unreliable contract enforcement, and limited information, the demand for adept credit management becomes paramount to bolster the resilience and growth of manufacturing entities. Although businesses that avail higher trade credit tend to flourish more rapidly, there is an imperative for enhancing trade credit operations within Nigerian manufacturing firms, given the economy's vulnerability and the pressing need for fortification (Gideon & Olusola, 2019).

The manufacturing sector stands as a linchpin in the economy, with its vitality or decline significantly swaying the overall economic health and progression of a country. As a vital contributor to economic stability, the manufacturing industry catalyzes job creation and the generation of essential goods and services, underscoring its crucial role in nurturing economic vitality.

Explicit credit management policies lay down the guidelines for offering credit, qualifying customer criteria, collection processes, and protocols for handling client insolvency. Credit, as delineated by Gideon & Olusola (2019), is an instrumental tool in augmenting sales and bolstering client credit transactions. Absent effective control mechanisms, credit sales may precipitate liquidity constraints, adversely affecting business growth. Even enterprises with substantial fixed assets may face liquidity challenges, underscoring the importance of credit management in maintaining financial health and operational efficacy.

The efficient management of credit operations is pivotal for a company's operational proficiency. As noted by Abubakar, Sulaiman, and Mohammed (2019), the allocation and handling of credit-related matters consume a substantial portion of a finance manager's time, influencing the firm's profitability and growth trajectory positively. Ifurueze (2013) highlighted the burgeoning credit transactions in Nigeria, accentuating the criticality of adept trade credit management in influencing the financial success and enduring viability of businesses. Thus, this investigation aims to methodically explore the influence of credit risk management on the financial performance of Nigeria's industrial sector, emphasizing its indelible impact on the sector's sustainability and growth.

Challenges in Risk Management within Nigeria's Industrial Sector

Nigeria's industrial landscape is navigating through turbulent waters, primarily due to the inadequacies in trade credit management amidst an ongoing economic downturn. The sector is beleaguered by a lack of sufficient safeguarding measures against the looming threats of credit risk, leading to an escalation in non-recoverable debts. Gideon and Olusola (2019) illuminate the predicament where businesses incur bad debts or financial losses as a direct consequence of mismanaging trade credit, inhibiting their ability to recover outstanding receivables.

The susceptibility to bad debts is inherently tied to the nature of accounts a firm opts to engage with. Effective trade credit management, therefore, emerges as both a cornerstone and a catalyst for business expansion. Offering trade credit—deferring cash payments in exchange for goods or services—instigates the accumulation of accounts receivable, envisioned as future financial inflows. The lifecycle of these receivables begins with issuing invoices, setting the stage for subsequent payment within agreed timelines.

Given the substantial investment in accounts receivable, prioritizing their meticulous management becomes imperative to avert potential financial derailments. The competitive dynamics of the industry perpetuate the necessity of credit offerings to retain clientele, positioning accounts receivable management as a strategic imperative for survival in Nigeria's business terrain. Neglecting this aspect can inflate receivables to unsustainable levels, thereby straining the company's liquidity.

Despite the strategic advantages of trade credit, Onuora and Ifeacho (2017) disclose a chronic challenge across the global economic spectrum: the struggle with ineffective credit risk management, which in turn erodes business profitability. This underscores the

need to perceive profitability not just as an outcome but as a pivotal factor in the credit management equation, balancing its inherent benefits against the costs.

In response to these enduring challenges, this study embarks on a comprehensive exploration of the impact of credit management practices—specifically credit term policy, credit standard, and collection policy—on the financial robustness of firms, encapsulated through the lens of return on assets. This inquiry aims to shed light on the intricate dynamics of credit risk management and its quintessential role in fortifying the financial foundations of Nigeria's industrial entities.

LITERATURE SYNTHESIS ON CREDIT ADMINISTRATION AND RISK MANAGEMENT

Navigating the Terrain of Credit Management

In the corporate cosmos, credit management surfaces as an indispensable function, transcending industry boundaries. Every business entity engaging in credit transactions is entrusted with the critical responsibility of ensuring timely payments for services or goods provided. Myers and Brealey (2003) depict credit management as an orchestrated array of policies and strategies aimed at sustaining optimal credit levels and adeptly steering these financial waters. Integral to this realm are credit assessment, rating, categorization, and reporting, laying the groundwork for a robust financial management system. Nelson (2002) simplifies this concept as the art of orchestrating credit sales, highlighting the inescapable presence of credit or default risks in business operations. Hettihewa (1997) equates credit extension to investing in customers, emphasizing the financial repercussions of delayed debt settlements.

Edwards (1993) warns of the profit erosions tied to overdue accounts, suggesting that unless preemptive charges for late payments are integrated or recovered through interest levies, businesses stand to lose. The allure of expanded sales through extended credit must be judiciously weighed against potential credit-induced financial burdens. Peter (2005) and Dina (2007) concur that proactive credit management not only mitigates bad debt risks but also optimizes capital utilization, bolstering corporate cash flow and operational sustainability.

Deciphering Credit Risk Dynamics

The discourse on credit risk, as elucidated during the third International Conference on Credit Analysis and Risk Management (2015), views credit as a bilateral commitment to future payment in exchange for immediate financial resources. Kanchu and Kumar (2013) delineate credit risk as the precariousness surrounding the fulfillment of these financial obligations. Kolapo, Ayeni, and Oke (2012) amplify this perspective by illustrating the banking sector's vulnerability to defaults, where improper risk management could precipitate financial instability. They also introduce the concept of value fluctuations in financial instruments as a derivative of credit quality shifts among borrowers.

Credit Risk Management (CRM) is heralded as a systematic approach to navigating the uncertainties of loan defaults, integrating risk assessment, mitigation strategies, and resource allocation to fortify liquidity and minimize adverse loan extension outcomes, as articulated by Namusonge, Lyani, and Sakwa (2016).

Unveiling Credit Practices and Financial Performance Correlations

Credit policies serve as the blueprint for managing credit sales, customer qualification, collection methodologies, and insolvency proceedings. Lawrence (2003) emphasizes the delicate balance in accounts receivable management, advocating for

judicious credit granting and monitoring to forestall revenue losses. The dynamics of debtor management involve navigating the complexities of credit sales, where the objective is to minimize financial setbacks stemming from unfulfilled debtor payments, as discussed by James (2012).

The financial performance narrative, as described by Okafor et al. (2016), revolves around the strategic harnessing of capital to yield returns and fulfill obligations to financiers. Performance management in this context is seen as a strategic enabler, steering organizational behavior towards achieving overarching goals and fostering an environment conducive to continuous improvement and feedback.

Theoretical Expositions and Empirical Insights

The Theory of Transaction Costs posited by Schwartz (1974) proposes that suppliers may possess a competitive edge in gauging a client's financial reliability and enforcing credit repayment more effectively than traditional banking institutions. This theory, further explored by Petersen and Rajan (2014), identifies potential cost advantages in information procurement, customer management, and asset value retention.

Empirical investigations, such as those by Bui and Nguyen (2021), Kornom and Aernan (2021), and others, provide a panoramic view of the multifaceted influences on corporate financial performance, encompassing aspects like environmental costs, credit policies, and operational risks. These studies collectively underscore the intricate interplay between credit management practices and their ramifications on the financial vitality of enterprises, advocating for a nuanced approach to credit risk management and financial strategy formulation.

Also, Anetoh, Okoye, Chidume and Okeke (2021). Investigated the effect of credit and operational risks on firm value of listed deposit banks in Nigeria. The study adopted an ex-post facto research design. The target population of the study was all the deposit money banks listed in Nigeria Stock Exchange. The study used secondary sources of data from Central Bank of Nigeria as well as from annual reports and financial statement of accounts of deposit money banks under review from 2010-2019. The Structural Equation Modeling was used to test the formulated hypotheses at 5% level of significance. The findings showed that credit risk had a significant but negative effect on firm value of deposit money banks in Nigeria. Operational risk had a significant and positive effect on firm value of deposit money banks in Nigeria. The study recommends that banks should ensure that their credit exposures are adequately secured through proper scrutiny of loan processing in order to identify viable projects so as to reduce loan defaults by bank customers. They should continue to employ qualified and competent workers who are experts in banking professionalism as well as ICT competence in order to reduce unsound banking practices.

Benjamin, Adebite and Dada (2020). Investigated the effect of risk assessment by internal auditor on effectiveness of listed companies in Nigeria. The study adopted a survey research design. The population of the study consisted of 24 companies selected from the eleven industrial sub-sectors of the 161 listed companies on Nigerian Stock Exchange as at 30th November, 2019. The sample frame is 5012 and sample size of 501 (comprising 401 internal auditors and 100 top management staff) representing 10% of the population. Structured questionnaire with a five-point Likert – scale was administered with 87.43% response rate. Random sampling technique was adopted in the selection of the 24 companies with each chosen company representing each sector. The research instrument was subjected to content validity and test and re-test method of reliability which yield

Cronbach alpha value of 0.798. Result indicated that risk assessment (RA) by internal auditors has positive effect on effectiveness (EFFTV) of listed companies in Nigeria with $\beta = 0.194$, $t(438) = 9.827$, $p < 0.05$. Therefore, companies' management are advised to strengthen the internal auditors in the assessment of risk that might impact on the effectiveness of an organization to be able to avert organizational emerging risk.

METHODOLOGY

The study adopted *ex post facto* because it has to do with secondary data which cannot be manipulated. The research work covered industrial goods companies in Nigeria with particular reference to selected industrial goods companies listed in Nigeria stock exchange. The population of this study consists of all firms operating in industrial goods sectors that are listed on the Nigerian Stock Exchange (NSE). Thirteen (13) firms were listed on the Nigerian Stock Exchange and this formed our population.

S/N	COMPANY NAME	TICKER	SECTOR
1	AUSTIN LAZ & COMPANY PLC	AUSTINLAZ	INDUSTRIAL GOODS
2	BERGER PAINTS PLC	BERGER	INDUSTRIAL GOODS
3	BETA GLASS PLC.	BETAGLAS	INDUSTRIAL GOODS
4	BUA CEMENT PLC	BUACEMENT	INDUSTRIAL GOODS
5	CAP PLC	CAP	INDUSTRIAL GOODS
6	CUTIX PLC.	CUTIX	INDUSTRIAL GOODS
7	DANGOTE CEMENT PLC	DANGCEM	INDUSTRIAL GOODS
8	GREIF NIGERIA PLC	VANLEER	INDUSTRIAL GOODS
9	LAFARGE AFRICA PLC.	WAPCO	INDUSTRIAL GOODS
10	MEYER PLC.	MEYER	INDUSTRIAL GOODS
11	NOTORE CHEMICAL IND PLC	NOTORE	INDUSTRIAL GOODS
12	PORTLAND PAINTS & PRODUCTS NIGERIA PLC	PORTPAINT	INDUSTRIAL GOODS
13	PREMIER PAINTS PLC.	PREMPAINTS	INDUSTRIAL GOODS

Nigeria Stock Exchange (NSE, 2023)

In this study, a judgmental sampling technique was employed, predicated on the necessity to cherry-pick samples grounded in data accessibility to fulfill the research aims. Specifically, four entities from the industrial goods sector were meticulously selected to constitute the research sample. According to Balsley and Clover (1988), a representation of 10% of the total population is deemed substantial for analytical accuracy. The chosen companies—Berger Paints Plc, Premier Paints Plc, Beta Glass Plc, and Cap Plc—exceed this threshold, encapsulating a significant segment of the market from 2014 to 2019.

Data for this investigation were primarily sourced from the annual reports and financial statements of the aforementioned firms over the specified period. This approach leveraged secondary data, providing a robust basis for comprehensive analysis. The methodological framework of the study embraced both time-series and cross-sectional analyses, utilizing Econometric Views (EViews) Version 10 as the principal statistical tool. This facilitated a quantitative exploration through panel data regression analysis, adeptly capturing the dynamism and complexity of the dataset.

To rigorously ascertain the most fitting model for interpreting the data, both fixed and random effect regression analyses were conducted. The Hausman test was subsequently applied as a decisive measure to discern the more appropriate model

between the two, ensuring methodological rigor and reliability in the study's empirical findings.

Data Insights and Interpretive Discussion

Hausman Specification Test

The Hausman specification test scrutinizes whether the unique impacts of the cross-sectional data are independent of the model's other variables. It evaluates the null hypothesis, positing that the random effects model is optimally suited for analysis. The criterion for endorsing the null hypothesis is when the p-value for the random effects in the cross-sectional data exceeds the 0.05 threshold, as per the Mackinnon standard. Conversely, should this hypothesis be refuted, the fixed effects model emerges as the appropriate analytical choice. Below is the presentation of the Hausman test outcome for the model under consideration.

Hausman Test for the Model 1

Correlated Random Effects - Hausman Test
Equation: Untitled
Test cross-section random effects

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f	Prob.
Cross-section random	41.654512	3	0.0000

Cross-section random effects test comparisons:

Variable	Fixed	Random	Var(Diff.)	Prob.
CREDP	0.731901	8.397413	9.080429	0.0110
CREDS	5.467877	0.682906	14.755698	0.2129
COLP	7.353479	22.286876	21.241719	0.0012

Source: Researcher's Estimation, 2023 (E-views 10 – Appendix)

The outcomes of the Hausman test, delineated in Table 4.3 above, reveal insightful statistical findings. The chi-square statistic, marking the divergence between the fixed and random effect models, registers at 41.654512, coupled with a p-value of 0.0000. This p-value, significantly undershooting the 5% significance threshold, leads to the rejection of the null hypothesis. Consequently, this endorses the fixed effect model as the more suitable choice for this analysis. Following this decisive result, the next steps involve a detailed estimation and interpretation of the fixed effect model to uncover the nuanced dynamics within the data.

Fixed Effect regression for Model 1

Dependent Variable: ROA

Method: Panel Least Squares

Date: 08/03/23 Time: 18:58

Sample: 2014 2020

Periods included: 7

Cross-sections included: 4

Total panel (balanced) observations: 28

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.698248	6.874775	-0.101567	0.9201
CREDP	0.731901	9.529129	0.076807	0.0395
CREDS	5.467877	11.91141	0.459045	0.0509
COLP	7.353479	7.146846	1.028912	0.0152

Effects Specification			
Cross-section fixed (dummy variables)			
R-squared	0.817046	Mean dependent var	10.10482
Adjusted R-squared	0.764773	S.D. dependent var	18.19015
S.E. of regression	8.822259	Akaike info criterion	7.404751
Sum squared resid	1634.477	Schwarz criterion	7.737802
Log likelihood	-96.66651	Hannan-Quinn criter.	7.506568
F-statistic	15.63046	Durbin-Watson stat	0.814028
Prob(F-statistic)	0.000001		

Source: Researcher's Estimation, 2023 (E-views 10 – Appendix)

- **Credit Policy (CREDP) Dynamics:** The coefficient for credit policy is positively aligned and showcases statistical significance, leading to the null hypothesis being refuted (with a p-value of 0.03, falling below the 0.05 threshold). This indicates that a unit increase in credit policy could potentially augment the return on assets (ROA) by approximately 0.7319 units. This positive correlation underscores the vital influence of credit term policy on enhancing ROA.
- **Exploring Credit Standard (CREDS):** The credit standard's coefficient presents a positive figure, yet it does not cross the threshold of statistical significance, maintaining the null hypothesis with a p-value at the brink of 0.05. This scenario suggests that an upward adjustment in credit standard by one unit might elevate the ROA by nearly 5.46 units, reflecting a positive impact on ROA.
- **Collection Policy (COLP) Effectiveness:** With a positive coefficient and significant statistical relevance (p-value of 0.01), the collection policy firmly rejects the null hypothesis. An incremental unit in collection policy is likely to boost ROA by about 7.35 units, denoting a substantial positive impact on ROA.
- **Constant Variable Analysis:** Holding other variables constant, ROA is anticipated to diminish by approximately 7.3%, highlighting the significant role of credit policy, credit standard, and collection policy in affecting ROA for industrial goods companies.

Coefficient of Determination (R²) Insight: The adjusted R-squared value stands at 0.8170, suggesting that around 82% of the variance in ROA can be ascribed to modifications in the credit risk management variables, indicating a robust model fit.

F-Statistics Evaluation: The calculated F-value is 15.63046 with a significant p-value of less than 0.05, corroborating the overall independent variable's significant explanatory power on the dependent variable, thus rejecting the null hypothesis.

Durbin-Watson Statistic Review: The Durbin-Watson statistic of 0.814 points to positive serial correlation, suggesting a potential need for model refinement to address autocorrelation.

COMPREHENSIVE FINDINGS DISCUSSION

The analysis reveals that credit term policy significantly boosts ROA, aligning with Yego and Gichure (2020), who emphasized the financial importance of credit terms in banking. Similarly, the positive effect of credit standard on ROA echoes Kljucnikov et al.'s (2018) findings regarding the critical assessment of client creditworthiness. The collection policy's positive influence on ROA resonates with Ojeka's (2012) insights on the efficacy of stringent credit administration in manufacturing.

Moreso, the analysis of credit term policy indicates a favorable outcome with a probability statistic of 0.03, which is less than the 0.05 threshold, leading to the rejection of the null hypothesis. This confirms a statistically significant positive impact of credit term policy on the return on assets (ROA). Echoing the research of Yego and Gichure (2020), the findings illuminate that commercial banks perceive credit terms as pivotal for financial prosperity, necessitating a robust debt collection framework. Banks proactively engage with clients to ensure timely repayments, underscoring the strategic role of credit terms in defining customer credit limits and safeguarding the firm against potential losses from non-compliant paybacks.

The credit standard metric exhibits a positive influence with a probability statistic equating to the threshold of 0.05, prompting the rejection of the null hypothesis and establishing a positive correlation with ROA. This aligns with Kljucnikov, Sobekova, and Vincurová's (2018) observations that a firm's ability to extend credit hinges on a thorough assessment of client creditworthiness and repayment capability. The setting of credit standards is therefore crucial, serving as a filter to discern and manage the risk associated with customer creditworthiness. These standards, whether stringent or lenient, act as a gatekeeper, ensuring that credit is extended to clients who are deemed financially reliable.

Regarding the collection policy, its positive coefficient and a probability statistic of 0.01, which is below the 0.05 threshold, lead to the dismissal of the null hypothesis, indicating a significant positive effect on ROA. This finding resonates with Ojeka's (2012) study, which highlighted the implementation of guarantee policies by firms to facilitate credit recovery. The positive outcomes from such policies reflect the diligence and rigor manufacturing firms apply in credit administration, aiming to strike a balance between credit accessibility and financial risk mitigation. This strategic approach in credit management underscores the firms' commitment to maintaining financial stability while fostering growth and profitability.

CONCLUSIVE INSIGHTS

Drawing from the insights garnered in this research, it becomes evident that effective credit management is instrumental in elevating the financial health of industrial goods companies in Nigeria. The positive correlation underscores the strategic importance of robust and sound credit management practices in fostering operational efficiency, enhancing liquidity, and amplifying returns on economic activities.

The financial vigor of any corporation is fundamentally assessed by its ability to transform assets into revenue, a process intrinsically linked to the firm's proficiency in profit generation and bolstering return on investment (ROI). The study highlights a notable

improvement in the profitability metrics of industrial goods entities, a testament to the adept adoption and execution of credit risk management strategies. These strategies have enabled companies to judiciously extend credit to meritorious clients, optimizing profit margins and ensuring financial stability.

The pivotal role of credit management in augmenting the return on assets (ROA) is distinctly evident, with the study affirming its substantial impact on financial performance. The dynamism in credit policy, alongside meticulous standards and collection practices, has emerged as a cornerstone for effective credit management. These elements collectively contribute to a robust framework that not only mitigates financial risks but also propels the economic prosperity of firms.

In light of these findings, it is imperative for firms to continuously refine and adapt their credit management policies, standards, and collection protocols. Such proactive measures are essential in navigating the complexities of the financial landscape, ensuring sustainable growth, and enhancing the overall economic contribution of the industrial goods sector in Nigeria. Through diligent application and regular reassessment of these credit management practices, companies can achieve optimal financial outcomes and solidify their market standing in the competitive industrial domain.

Strategic Recommendations

- Industrial companies should incentivize early payment through discounts, fostering adherence to credit terms.
- Continuous reassessment of collection policies is crucial for enhancing firm profitability.
- Implementing stringent guarantee policies will ensure credit recovery and sustain financial performance.

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