RISK MANAGEMENT AND PROFITABILITY OF COMMERCIAL BANKS: A CASE STUDY OF SALAM BANK IN MOGADISHU, SOMALIA

BY

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DECLARATION

I Hafsa Abdirahman Ali declare that tis thesis is my original work and has not been presented for a degree or any other academic ward in any university or institution of learning.

Student: Hafsa Abdirahman Ali

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Signature

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Date

APPROVAL

This thesis was carried out by the candidate under my supervision and is ready for examination.

Signed ______________________

Date __________________________

DEDICATION

This book is dedicated to my beloved parents and my dear husband Mohamed Mukhtar.

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First and foremost I thank Allah for the gift of life and strength that has helped me to complete this report and the entire course at large.

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LIST OF DEFINITIONS

SPSS: Statistical Package for Social Sciences

CVI: Content Validity Index

CTP: Compensation Theory of Profit

CBs: Commercial Banks

ERM: Enterprise Risk Management

IRM: Integrated Risk Management

EU: European Union

USA: United States of America

ABSTRACT

The study sought to assess the effect of risk management on profitability of commercial banks in Mogadishu-Somalia. It was guided by three specific objectives, that included i) determining the effect of risk identification on profitability of commercial banks in Mogadishu Somalia; ii) examining the effect of risk assessment on profitability of commercial banks in Mogadishu Somalia and (iii) to establish the effect of risk monitoring and control on profitability of commercial banks in Mogadishu Somalia. This research employed a descriptive research design to describe the variables, the questionnaire and interview guide were used as the research instruments. Descriptive statistics were used in this study included frequencies, means and regression analysis on variables. The findings revealed the following: The findings indicated that risk identification significantly affects the profitability of commercial banks in Mogadishu Somalia (sig=0.000 and F-value= 84.756), the findings revealed that there is a significant effect risk assessment has on profitability of commercial banks in Mogadishu Somalia (sig=0.000 and F-value= 71.395), findings of this study proved a positive significant effect risk monitoring and control has on profitability of commercial banks in Mogadishu Somalia (sig=0.000 and F-value=93.669). Still the researcher concluded that; risk identification has a considerably high influence on the profitability of the commercial banks, hence there is need for improving the risk identification s to enhance profitability, risk assessment has a significant effect on profitability of commercial banks in Mogadishu Somalia and this indicates that risk assessment has a high bearing on profitability of the commercial banks, and finally risk monitoring and control has a positive significant effect on profitability of commercial banks in Mogadishu Somalia and hence indicating that risk monitoring and control has a bearing on the profitability hence there is need for enhancing monitoring given the state of the profits though other factors complemented in the study. The researcher recommended that: there is need to enhance risk identification through improving the mechanism for categorizing risks as the strategy for enhancing profitability. The process of risk identification in commercial banks should be very comprehensive covering all departments and sections as this will enable management to effectively implement risk identification strategies. Commercial banks in Mogadishu should look at other factors that directly affect profitability. These include availability of qualified personnel to implement risk management, the level of technology applied and the effect of changes in demand. The study contributed to new knowledge through the following; one of the most prominent findings from this study is the fact that it has provided evidence to support the fact that risk management can improve the state of profitability of the commercial in Mogadishu Somalia.

CHAPTER ONE

INTRODUCTION

1.0 Introduction

This chapter contains the background, problem statement, scope, hypothesis, general objective, specific objective, research questions, significance of the research and the operational terms.

1.1 Background of the study

The background of the study consists of the historical background, theoretical background, conceptual background and contextual background.

1.1.1 Historical Perspective

The history of risk management dates back to the 20th century where risk reporting was designed to meet the information needs of the property managed institutions like banks. With the introduction of revolutionary industrialization, complex companies became sophisticated and risk management practices were eminent. Model emphasized stewardship, decision making, and performance evaluation was emerged. This information was designed to support managerial decision making and risk management in companies (Deconan, 2013).

Marcus (2015) argued that back in 1980s there was no risk management department in financial institution and only the bank head trader had the experience an authority to rule on poor trades and have them unwound. In the 1990s financial institutions began to release the importance of risk management by setting up risk management department which was charged with measuring risk and not risk management with all the authority of decision among with the head if trader, these made the risk management powerless.

Financial risk management become a booming industry starting ’90 as a result of the increasing volatility of financial hackers, financial innovations (financial derivatives) the growing role played by the financial products in the process of financial intermediation, and important financial losses suffered by the companies without risk management systems for example, Enron and WorldCom (Barney, 2011).

Shrank (2011) opined that an incentive and accountability structure that is compatible with reduced risk taking on part of the employees is also an import element to reduce overall risk. A prerequisite of these incentive-based contracts is accruing reporting of the bank's exposures and internal control system. An efficient incentive compatible structure would limit individual positions to acceptable levels and encourage decision makers to manage risks in a manner that is consistent with the banks goals and objectives.

There are two approaches of the risk management process, the traditional one the enterprise risk management (ERM). In the traditional approach, a segmented and compartalized one consists in the following different risks are delegated to different specialized persons who use different instruments to tackle these risks. For example, the property and liability risks are the responsibility of the risk manager. At the same time, the treasurer is responsible to manage financial risks such as exchange rate, interest rate, and credit risk using different types of derivatives contracts such as options, forwards, futures, and swaps (Marcus, 2015).

In the second approach, called integrated risk management (IRM) or Enterprise risk management (ERM), all the risks are assembled in a strategic and coordinated framework. Enterprise risk management requires an entry to take a portfolio view of the risk. Corporate risk management is subsequently motivated by market imperfections, such as asymmetric information, transactions costs, non-neutral taxes and limited access to external financing. Risk management is nowadays considered as a key activity for all companies including all financial institutions. Many of the disastrous losses of the 1990s, such as those at orange county in 1994 and Barings bank in 1995, would have been avoided if good risk management practices have been in place (Hull, 2009).

The world has experienced remarkable numbers of banking and financial crises during the last thirty years and 112 systemic banking crises were identified in 93 countries since the late 1970s (Caprio and Klingebiel, 1997). Another study identified

30 major banking crises that are encountered from early 1980s and onwards (Demirguc-Kunt and Detragiache, 1998). Though most of those were experienced in the developing countries, the authors have noted that three Nordic countries-Nordic countries –Norway, Finland and Sweden have also gone through similar crises in the late 1980s and early 1990s. Interestingly, the majority of the crisis coincided with the deregulatory measures that led to excessively rapid credit extension. In the long run, continuous increase in asset prices created a bubble. At some point, the bubble burst and the asset markets experienced a dramatic fall in asset prices coupled with disruption. Finally, widespread bankruptcies accompanied by non-performing loans, credit losses and acute banking crises were observed.

In Africa specifically Ghana profit efficiency is not related to distant size, and cost and profit ratios (Zangina & Bokpin, 2011). From this study it can further be noted that distance is positively and significantly related to cost efficiency. Cost efficiency is however not influenced by size or cost and profit ratios. The financial crises were rooted in the misinterpretation and mismanagement of strategic risk, with too much focus on capital requirements for credit, market and operational risks described under the first pillar of Basel II, most financial institutions have neglected strategic risk, whereas it can be the most serious causes of value destruction as experienced nowadays by several major financial institutions. Compared to the European union (EU, risk management in the United States of America (USA) has evolved from a compliance based directive into a business competence in the new economic reality. While most European union (EU) organizations continue to identify emerging risks and create plans to mitigate risk, business leaders find that they must understand the whole spectrum of risks (World saving Banks institute, 2010).

In Somalia, particularly Salam bank, how risk management relates to profitability in commercial banks is not well known. This has prompted the researcher to investigate how risk management impacts on profitability. Somalian banking industry was not hugely affected by the global credit crisis and it is about time financial institutions take this as a lesson to embrace risk management at all functional levels. In Somalia, prudential reporting on the financial sector indicates that the banks' total exposure in the form of Nostro Balances to the troubled correspondent banks abroad remained modest with minimal risk to safety soundness of the banking sector as a whole. Somalia banking sector remains sound stable and continues to grow and exhibit resilience in the face of the on-going global turbulence. The banks' capital adequacy ratios are well above the regulatory requirement. In Somalia the crisis of the interest rate saga between commercial banks and the business sector geared by Mogadishu city traders association (MCITA) in early 2012 can be injurious to the profitability of commercial banks through the exposure of banks to risk like interest rate risk, credit risk and reputational risk (Zangina & Bokpin, 2011).

1.1.2 Theoretical Perspective

Compensation Theory of Profit

The study was guided by the Compensation Theory of Profit which was developed by Alfred Marshall (1924), the theory states that the profit is the supply price of entrepreneurship or business power where business power is the supply of capital plus supply of the ability to maintain business plus supply of organisational ability for production. This theory treats profit as a cost element and that profit is the price for the 'function' of capital, hence it is a functional theory of profit. Under these conditions economic profits would not accrue to the firms. Frictional theory of profit explains that shocks or disturbances occasionally occur in an economy as a result of unanticipated changes in product demand or cost conditions which cause disequilibrium conditions. It is these disequilibrium conditions that bring into existence positive or negative economic profits for some firms. On the other hand, when firms are making losses (i.e. negative profits), some firms will leave the industry. This will cause price of the product to rise so that losses are eliminated and the remaining firms make only normal profits. When economic profits are made in the short run, more firms will enter the industry in the long run until all economic profits are driven down to zero (that is, firms will be making only normal return or profits on their capital investment).

According to this theory there exists a normal rate of profit which is a return on capital that must be paid to the owners of capital as a reward for saving and investment of their funds rather than to consume all their income or hoard them. In a static economy where no unanticipated changes in demand or cost conditions occur, in long-run equilibrium the firms would be earning only normal rate of profit on their capital and entrepreneurial talent (Kulter, 2011).

1.1.3 Conceptual Perspective

This section presented the standard definitions of the variables (risk management and profitability) as indicated below;

Vosselman (2015) defined risk management as the process of identification, analysis and either acceptance or mitigation of uncertainty in investment decision-making. Essentially, risk management occurs anytime an investor or fund manager analyzes and attempts to quantify the potential for losses in an investment and then takes the appropriate action (or inaction) given their investment objectives and risk tolerance. Inadequate risk management can result in severe consequences for companies as well as individuals. In this study risk management was conceptualized as risk identification, risk assessment and risk monitoring and control in the organizations.

Dwivedi (2015) defined profitability as an income accruing to the equity holders in the same sense as wages accrue to labour, rent to the owners of rentable assets and interest to the money lenders.

Kakuru (2015) also defined profitability as the difference between the revenue generated by corporate firm and expenses incurred during the operation of the business. He further classified that various costs incurred by these firms some of which are fixed costs like rent while other are variable costs which can easily change for example electricity expenses and the corporate firms can easily achieve increased sales.

Brinker (2012) defined profitability as the difference between the revenue generated and the costs incurred to produce the same revenue during a given accounting period so to him corporate firms should aim at increasing sales revenue and reduce costs incurred so that they achieve the desired levels of profitability.

1.1.4 Contextual Perspective

The Commercial Banks Report (2016) indicated high incidence of risks reflected in the rising levels of non-performing loans by commercial banks of Mogadishu in the last 10 years. This is a situation that has adversely impacted on their profitability. Despite rigorous risk assessment process the, Commercial Banks in Mogadishu Somalia use that includes among others proof that banks do not have other risk obligation, analysis of their account profitability, sustainability of their income levels, security and ability to pay (Commercial Banks Manual, 2016), the Salam bank branches in Mogadishu, Somalia are faced with poor management of their loan portfolio, this leads to poor quality loan portfolios which had to be provided for fully. The financial records show that the commercial Banks' provisions and bad debts written off increased from 1.9billion in 2010 to 6.8billion dollars in 2015. This trend not only threatens the viability and sustainability of the commercial bank but also hinders the achievement of the goals for which it is intended which are to provide services to the population and bridge the financing gap in the mainstream financial sector (Hemedi, 2016).

1.2 Problem Statement

The prevailing state of low profitability of Salam bank in Mogadishu Somalia presents largely negative consequences such as poor service provision to customers due to low profits which may lead to unemployment (Commercial Banks Manual, 2016). A number of Salam bank branches have failed and closed after incurring a lot of losses and these failed bank branches include that of Haegeisa Salam bank branch and Baredwin Salam bank branch. As a result of these failed Salam bank branches, it has resulted into different negative consequences such as loss of employment among the workers. Low levels of profitability could be a result of a number of factors including poor risk management, limited funds as evidenced by the existing bank branches in Mogadishu, Somalia (Central bank of Somalia, 2017). Though a number of factors are responsible for the low levels of profitability of Salam bank, it is important to find out how risk management affects the bank profitability. Therefore this study was set to establish the effect of risk management on profitability of the commercial banks in Mogadishu Somalia.

1.3 Purpose of the study

The purpose of the study was to establish the effect of risk management on profitability of Salam bank in Mogadishu Somalia.

1.4 Specific Objectives of the study

i. To determine the effect of risk identification on profitability of Salam bankin Mogadishu Somalia.
ii. To examine the effect of risk assessment on profitability of Salam bankin Mogadishu Somalia.
iii. To establish the effect of risk monitoring and control and control on profitability of Salam bankin Mogadishu Somalia.

1.5 Research Questions

i. What is the effect of risk identification on profitability of Salam bankin Mogadishu Somalia?
ii. What is the effect of risk assessment on profitability of Salam bankin Mogadishu Somalia?
iii. What is the effect of risk monitoring and control and control on profitability of Salam bankin Mogadishu Somalia?

1.6 Hypothesis

Hi_1: There is no a significant effect of risk identification on profitability of Salam bankin Mogadishu Somalia

Hi_2: There is no a significant effect of risk assessment on profitability of Salam bankin Mogadishu Somalia

Hi_3: There is no a significant effect of risk monitoring and control on profitability of Salam bank in Mogadishu Somalia

1.7.0 Scope of the study

1.7.1 Geographical Scope

The study was conducted from Salam bank branches in Mogadishu and these branches included Grade A Branch, Grade B Branch and Grade C Branch all located in Mogadishu.

1.7.2 Content Scope

The study focused on risk management in relation to risk identification, risk assessments and risk monitoring and control, whereas profitability (dependent variable) was measured in relation to gross profit margin, returns on equity and returns on invested capital.

1.7.3 Time Scope

The study was conducted for a period of Eleven (11) months. This study was conducted from October 2017 to September 2018, whereby proposal writing took place from October 2017 to January 2018, data collection and analysis was done between February-May 2018, and then the final report was written between June-August 2018 and submitted in September 2018. This was chosen because it enabled the researcher to collect sufficient data from the respondents. The time was chosen given that it facilitated the attainment of sufficient data.

1.8 Significance of the study

The study will benefit the managers and owners of Salam bank who are experiencing nowadays risk management problem and improving their understanding towards the effect of risk management on profitability.

The findings and conclusions resulting from the study also will contribute to the body of knowledge on the effect of risk management on profitability of commercial banks. Future researchers and academicians may use the study findings to further their research.

Other bank managers can use the findings of the study to identify different risks and measures to reduce them and what they can do to improve the level of profitability.

To the **future researchers,** this research study will widen their knowledge and scope concerning risk management and profitability. As they conduct their own studies, the information in this research study can be of significance to these researchers and students because they will be able to identify the areas that need more research as they read what was researched in this research study.

The findings and conclusions resulting from the study will also fill and close the gaps in literature on risk management and profitability of commercial banks.

1.9 Operational definition of Key terms

Risk management; refers to the practice of identifying potential risks in advance, analyzing them and taking precautionary steps to reduce/curb the risk.

Risk identification; is the determining what risks or hazards exist or are anticipated, their characteristics, remoteness in time, duration period, and possible outcomes.

Risk assessment; refers to the determination of quantitative or qualitative value of risk related to a concrete situation and a recognized threat (also called hazard).

Risk monitoring and control; is the process of minimizing risks that could potentially prevent the program, enterprise, or investment from achieving its objectives.

Profitability; refers to the difference between the revenue generated and expenses incurred during the business activity.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter reviewed relevant sources of literature that deliberate on risk management and profitability of organization. It comprises four main sections which are theoretical review, conceptual framework, related studies and research gaps.

2.1 Theoretical Review

Clark's Dynamic Theory of Profit (1991)

Clark's Dynamic Theory of Profit (1991) suggest that profit is a residue, the difference between price and costs, due to the reductions in the cost effected by changes in the economy such as population increase (this reduces wages), increased capital supply (this reduces the interest rate charged and hence the cost of capital comes down), innovatins (reduces costs), higher inventory (windfall profits occur when the cost of production remains the same but the price shoots up perhaps due to inflation or higher demand), forms of organisation (reduces costs), technological improvements (reduces the costs). This theory is also known as windfall theory of profits. This theory treats profits as a residue in price after deducting costs, hence it is a residual theory of profits. The static economy is one in which the things do not change significantly or remains unchanged. Such as, the population and capital remain stationary, goods continue to be homogeneous, production process remains unchanged, and the factors of production enjoy freedom but does not move because the marginal product in each industry remains the same. Also, there is no uncertainty and risk. On the contrary, the dynamic economy is characterized by the generic changes such as an increase in population, improvement in production techniques, change and increase in the consumer demands, changes in the organizational forms, increase in capital. The major function of an entrepreneur is to work in a dynamic economy to take the advantage of these changes and promote his business, reduce costs, and expand sales (Horngren, 2015).

Clark believed that those entrepreneurs who successfully take the advantage of these changes in the dynamic economy make the pure profit, which is in addition to the normal profit. Pure profits are short lived because, in the long run, the competitors imitate the changes initiated by the leader. As a result, the demand for the factors of production increases, thereby increasing the factor prices and the overall cost of production. On the other hand, with an increase in the output, the price of a product declines for a given level of demand as a result of which the pure profits disappears (Kellerman, 2010).

Thus, according to Clark, the profit is an elusive amount which can be grasped, but cannot be held by an entrepreneur as it slips through the fingers and bestows itself to all the society members. Clark's dynamic theory of profit should not be misinterpreted as, the profits in the dynamic economy remain for a short period of time and then disappears forever. But, however, generic changes take place frequently, and the manager or entrepreneur through his foresight must capitalize on it and continue to make a profit in excess of the normal profit (Shrank, 2011).

Compensation Theory of Profit

Compensation Theory of Profit was developed by Alfred Marshall (1924) holds that the profit is the supply price of entrepreneurship or business power where business power is the supply of capital plus supply of the ability to maintain business plus supply of organisational ability for production. According to this theory there exists a normal rate of profit which is a return on capital that must be paid to the owners of capital as a reward for saving and investment of their funds rather than to consume all their income or hoard them. In a static economy where no unanticipated changes in demand or cost conditions occur, in long-run equilibrium the firms would be earning only normal rate of profit on their capital and entrepreneurial talent. This theory treats profit as a cost element and that profit is the price for the 'function' of capital, hence it is a functional theory of profit. Under these conditions economic profits would not accrue to the firms. Frictional theory of profit explains that shocks or disturbances occasionally occur in an economy as a result of unanticipated changes in product demand or cost conditions which cause disequilibrium conditions. It is these disequilibrium conditions that bring into existence positive or negative economic profits for some firms. On the other hand, when firms are making losses (i.e. negative profits), some firms will leave the industry. This will cause price of the product to rise so that losses are eliminated and the remaining firms make only normal profits. When economic profits are made in the short run, more firms will enter the industry in the long run until all economic profits are driven down to zero (that is, firms will be making only normal return or profits on their capital investment) (Kulter, 2011).

2.2 Conceptual framework

Figure 2. 1: Conceptual framework

Independent Variable

Risk management

- Risk identification
- Risk assessment
- Risk monitoring and control

Dependent Variable

Profitability

- Gross profit Margin
- Return on assets
- Returns on invested capital

Source: Kakuru (2015)

The study has two variables, the independent variable and the dpendent variable. The independent variable is risk management which has been conceptualized in terms of risk identification, risk assessment and risk monitoring and control. The dependent variable (profitability) was conceptualized as gross profit margin, returns on equity and returns on invested capital. The presence of positive risk management has a positive effect on the profitability of the organizations and the prevalence of negative risk management reduces to the profitability of the commercial banks. Risks can come from uncertainty in financial markets, threats from project failures (at any phase in design, development, production, or sustainment life-cycles), legal liabilities, credit risk, accidents, natural causes and disasters as well as deliberate attack from an adversary, or events of uncertain or unpredictable root-cause. Douglas also added that there are many different types of risk (Douglas, 2009).

2.3 Review of related Literature

The review of related literature was presented following the study objectives;

2.3.1 Effect of risk identification on profitability

The overall purpose of risk identification is to help managers plan and control the use of resources in systematic and logical manner to ensure that they achieve their financial objectives, that is profit satisfying(making satisfactory level of profits) and profit maximization(making the maximum profit). The Hotel after having made their assumptions about the forth coming period, the next stage is to set out their financial strategies in detail by preparing financial and non-financial budgets that cover every aspect of the firm's activities (Brinker, 2012).

Bendney and Colston (2015) argue that risk identification considers determining risks that could potentially prevent the program, enterprise, or investment from achieving its objectives. It includes documenting and communicating the concern**.** The objective of risk identification is the early and continuous identification of events that, if they occur, they have negative impacts on the project's ability to achieve performance or capability outcome goals, they may come from within the project or from external sources (Alexander, 2011).

Risks are often identified retrospectively and some risks are on the key risk list merely because they occurred recently and management wants to see them there. This is called "fighting the last battle" syndrome. In addition, these risks are often defined at too low a level of granularity, since they are descriptive of the recent specific event. Including these on the risk list, in this way, can skew the qualitative survey results. These risks are often over-weighted and participants are more sensitized to them and are not fully aware of the mitigation that has likely been put in place following the recent occurrence. Retrospectively defining risks also negatively impacts environmental scanning; it is a distraction from identifying the next risk event (Neil, 1999).

Identifying risks prospectively can help avoid these difficulties and it reduces some of the bias in the risk assessment, by not confusing recent experience with future likelihood and impact. It also focuses management away from the past, and concentrates attention on what might impact the company's ability to deliver on its strategic objectives going forward. This enables a robust, untainted examination of where the company is, where it's headed and what could get in the way. He also added that the first step in risk management is to look closely at your business and identify potential risks. Until you know the scope of all possible risks, you cannot develop a realistic, cost-effective strategy for dealing with them. The aim of this stage of risk management is to create a database of risks relevant to the particular business (Dorfman, 2011).

2.3.2 Effect of risk assessment on profitability of organizations

Joreme (2011) contend that risk assessment helps to determine the quantitative or qualitative value of risk related to a concrete situation and a recognized threat (also called hazard). Quantitative risk assessment requires calculations of two components of risk (R), the magnitude of the potential loss (L), and the probability (p) that the loss will occur. Acceptable risk is a risk that is understood and tolerated usually because the cost or difficulty of implementing an effective countermeasure for the associated vulnerability exceeds the expectation of loss (Gerry, 2013).

Kaplan and Cooper (2015) argued that Risk assessment consists of an objective evaluation of risk in which assumptions and uncertainties are clearly considered and presented. Part of the difficulty in risk management is that measurement of both of the quantities in which risk assessment is concerned where potential loss and probability of occurrence can be very difficult to measure. The chance of error in measuring these two concepts is high. Risk with a large potential loss and a low probability of occurrence, is often treated differently from one with a low potential loss and a high likelihood of occurrence. In theory, both are of near equal priority, but in practice it can be very difficult to manage when faced with the scarcity of resources, especially time, in which to conduct the risk management process. Risk assessment is simply looking closely at what in your place of work or about your work activities could cause harm to your employees and visitors to your workplace (e.g. customers, suppliers, sales representatives etc) and determining the control measures you can implement to minimise the risk

Danladi (2012) noted Once risks have been identified, they must then be assessed as to their potential severity of impact (generally a negative impact, such as damage or loss) and to the probability of occurrence. These quantities can be either simple to measure, in the case of the value of a lost building, or impossible to know for sure in the case of the probability of an unlikely event occurring. Therefore, in the assessment process it is critical to make the best educated decisions in order to properly prioritize the implementation of the risk management plan. The fundamental difficulty in risk assessment is determining the rate of occurrence since statistical information is not available on all kinds of past incidents. Furthermore, evaluating the severity of the consequences (impact) is often quite difficult for intangible assets. Asset valuation is another question that needs to be addressed. Thus, best educated opinions and available statistics are the primary sources of information. Nevertheless, risk assessment should produce such information for the management of the organization that the primary risks are easy to understand and that the risk management decisions may be prioritized.

Regina (2012) contend that the objectives of risk assessment are to explore risk response strategies for the high risk items identified in the qualitative and quantitative risk analysis. The process identifies and assigns parties to take responsibility for each risk response. It ensures that each risk requiring a response has an owner. The owner of the risk could be an agency planner, engineer, or construction manager, depending on the point in project development, or it could be a private sector contractor or partner, depending on the contracting method and risk allocation. Risk mitigation may require that agencies set policies, procedures, goals, and responsibility standards. Formalizing risk mitigation throughout a highway agency will help establish a risk culture that should result in better cost management from planning through construction and better allocation of project risks that align teams with customer-oriented performance goals. Once the agency planner, engineers, and construction managers have thoroughly analyzed the critical set of risks, they are in a better position to determine the best course of action to mitigate those risks.

According to Jensen (2010) conducted a study on risk management and Profitability in financial institutions in Sweden. The main objective was to find out if the management of the risk related to that credit affects the profitability of the financial institutions. They found that credit risk management in financial institutions has become more important not only because of the financial crisis that the world is experiencing nowadays but also the introduction of Basel II. They concluded that since granting credit is one of the main sources of income in financial institutions, the management of the risk related to that credit affects the profitability of the financial institutions (Tim, 2011).

Stulz (2015) did a study on credit risks experienced by commercial banks. His objective was to find out the complexities of a number of their products, as well as their relative novelty in the contemporary financial services market, combined with the fiduciary obligations of the bank when it acts as a custodian, imply that for Banks, credit risk is very important for consideration. He found that Investment Account Holders may be considered in the absence of misconduct and negligence by the bank to bear credit and market risks of assets if their funds have been invested by the bank, the latter must be considered as being exposed to the credit risk arising from its management of those funds. He concluded that that Banks are exposed to a number of credit risks that differ from those that are faced by conventional banks (Reen, 2013).

Haron & Sudin (2004) divided the determinants of commercial banks performance into two categories, namely internal and external factors. Internal determinants of profitability, which are within the control of bank management, can be broadly classified into two categories, i.e. financial statement variables and nonfinancial statement variables. While financial statement variables relate to the decisions which directly involve items in the balance sheet and income statement; non-financial statement variables involve factors that have no direct relation to the financial statements. The examples of non-financial variables within the this category are number of branches, status of the branch (e.g. limited or full-service branch, unit branch or multiple branches), location and size of the bank (Haron & Sudin, 2004).

2.3.3 Effect of risk monitoring and control on profitability of organizations

According to Jensen and Meckling (2014), risk monitoring and control may identify a number of risks that appear to be of similar ranking or severity. When too many risks are clustered at or about the same level, a method is needed to prioritize risk responses and where to apply limited resources. Such a method should be tied to mission/business needs and maximize the use of available resources. A rational and common sense prioritization is a key component of a risk management program and becomes necessary when requirements cannot be fully satisfied.

To adequately defend risk response decisions made by senior leaders/executives (e.g, why certain risks were or were not mitigated). She also added that if a risk is highly coupled to other risks or seen as likely to lead to other risks materializing (whether the risk is the cause or materializes concurrently), such risks are given extra attention and are likely to warrant resources applied to them in hopes of preventing multiple risks from materializing at or near the same time. If a risk materializing will actually decrease the likelihood of other risks materializing, then further analysis is warranted to determine which risks become a lower priority to mitigate. To maximize the use of available resources within the organization, the cost of risk mitigation considers whether the mitigation addresses (Ruth Murray, 2011).

Willman (2015) noted that when too many risks are clustered at or about the same level, a method is needed to prioritize risk responses and where to apply limited resources. Such a method should be tied to mission/business needs and maximize the use of available resources. A rational and common sense prioritization is a key component of a risk management program and becomes necessary when requirements cannot be fully satisfied. To adequately defend risk response decisions made by senior leaders/executives (e.g., why certain risks were or were not mitigated), decision makers should know or be able to obtain the answers to the following questions (Willman, 2015).

Moore (2011) noted that there are common risks in banking that need to be taken into consideration in order to reduce/eliminate defaulting on commercial lending. It is important to the bankers to understand all risks embedded in loaning business and their potential impact on the institution for the aim of avoiding the defaulting rate. The following are the categories relate to a bank's lending function.

Malcom and Harris (2010) noted that in order to avoid risks, There are principles to be considered before lending money to customers, thus the bank should always remember that the money lent to customers does not belong to it, its depositors and shareholders money. Therefore every endeavor should be able to avoid bad debts, as this may result in few advances and loss of income to the bank. These are rules, principles and procedures to guide the bank in deciding whether to lend or not in order to reduce the defaulting cases. Garder (1992) noted that the credit Manager must adhere to the following basic rules of lending i.e, Business profitability, Source of repayment, Character and ability of the borrower, Purpose of facility, Terms of the facility and Safety.

2.4 Related Studies

Ezeamama (2010) in his study on risk management and profitability, he found a significant relationship between risk identification and profitability in the construction industry in the United States. The Wang and Gibson research summarized pre-project risk identification data collected from 62 industrial projects and 78 building projects, representing approximately $5 billion in total construction cost. Based on the information obtained, pre-project risk identification was identified as having direct impact on the profitability (cost and schedule performance).

Horngren (2005) carried out a study on risk management in commercial banks and concluded that when too many risks are clustered at or about the same level, a method is needed to prioritize risk responses and where to apply limited resources. Such a method should be tied to mission/business needs and maximize the use of available resources. A rational and common sense prioritization is a key component of a risk management program and becomes necessary when requirements cannot be fully satisfied. To adequately defend risk response decisions made by senior leaders/executives (e.g., why certain risks were or were not mitigated), decision makers should know or be able to obtain the answers to the following questions (Danladi, 2012).

Joreme (2011) in his study on risk management found out that the objectives of risk mitigation are to explore risk response strategies for the high risk items identified in the qualitative and quantitative risk analysis. The process identifies and assigns parties to take responsibility for each risk response. It ensures that each risk requiring a response has an owner. The owner of the risk could be an agency planner, engineer, or construction manager, depending on the point in project development, or it could be a private sector contractor or partner, depending on the contracting method and risk allocation. Risk mitigation may require that agencies set policies, procedures, goals, and responsibility standards. Formalizing risk mitigation throughout a highway agency will help establish a risk culture that should result in better cost management from planning through construction and better allocation of project risks that align teams with customer-oriented performance goals (Deloof, 2013).

Kotole (2011) during his study on risk assement, he noted that risk assessment consists of an objective evaluation of risk in which assumptions and uncertainties are clearly considered and presented. Part of the difficulty in risk management is that measurement of both of the quantities in which risk assessment is concerned where potential loss and probability of occurrence can be very difficult to measure. The chance of error in measuring these two concepts is high. Risk with a large potential loss and a low probability of occurrence, is often treated differently from one with a low potential loss and a high likelihood of occurrence. In theory, both are of near equal priority, but in practice it can be very difficult to manage when faced with the scarcity of resources, especially time, in which to conduct the risk management process. Risk assessment is simply looking closely at what in your place of work or about your work activities could cause harm to your employees and visitors to your workplace (e.g. customers, suppliers, sales representatives etc) and determining the control measures you can implement to minimise the risk.

Cashin (2013) found out that risk identification includes documenting and communicating the concern. The objective of risk identification is the early and continuous identification of events that, if they occur, they have negative impacts on the project's ability to achieve performance or capability outcome goals, they may come from within the project or from external sources. He added that risks are often identified retrospectively and some risks are on the key risk list merely because they occurred recently and management wants to see them there. This is called "fighting the last battle" syndrome. In addition, these risks are often defined at too low a level of granularity, since they are descriptive of the recent specific event. Including these on the risk list, in this way, can skew the qualitative survey results. These risks are often over-weighted and participants are more sensitized to them and are not fully aware of the mitigation that has likely been put in place following the recent occurrence. Retrospectively defining risks also negatively impacts environmental scanning; it is a distraction from identifying the next risk event (Ciborra, 2014).

2.5 Research Gaps

Basing on the reviews of related literature, the following gaps were identified; a number of studies reviewed were carried out in different oraginisations and countries which posses the geographical gap which this study intended to bridge. Similary, the constructs used in other countries were not exactly the same as those used in this study frexample Lazaridis and Trifonidis (2014). According to the findings of another study from a different perspective, it has been concluded that the effect of risk monitoring on profitability is stronger than the effect of current ratio on it (Eljelly, 2014). However, the literature it says nothing about the relationship between risk management and profitability and how the two are related. The current study seeks to fill this knowledge gap.

CHAPTER THREE

METHODOLOGY

3.0 Introduction

This chapter presents the research design, the research population, and the sample size, sampling procedures, research instruments, validity and reliability of instruments, data gathering procedures, data analysis, ethical considerations and limitations of the study.

3.1 Research design

This study employed a cross-sectional research design. Cross-sectional design allowed the study of the population at one specific time and the difference between the individual groups within the population compared (Mugenda & Mugenda, 2003). The study also used survey design, this was used to collect data from a large sample of respondents. This study was also descriptive whereby qualitative and quantitative research approaches were used to gain insight to variables, it was descriptive in that it described the characteristics of respondents. Qualitative approach included the use of interviews, while quantitative approaches involved use of descriptive statistics that were generated inform of frequency tables, means and standard deviations. Qualitative and quantitative approaches were adopted to enable the researcher to get and analyze information concerning respondents' opinions about the impact of risk management on profitability in commercial banks in Mogadishu Somalia.

3.2 Population of the study

Mugenda and Mugenda (2003) defined population as a set of people, services, elements, and events, group of things or households that are being investigated. This definition ensures that population of interest is homogeneous. This study was conducted in Salam bank branches in Mogadishu and therefore, the population of this study included the operational staffs, middle managers and administrators from the three Salam bank branches of Grade A Branch, Grade B Branch And Grade C Branch which had a population of 280 employees in the category of operational staffs, middle managers and administrators. The respective populations of the individual bank branches were presented in table 3.3 below. This population was chosen because of having adequate data concerning risk management and profitability trends in the bank (Human resource Manual for the Commercial banks for April, 2017).

3.3 Sample Size

A sample is the subset of a population that was used to represent the entire group as a whole. Based on the study population, the researcher selected respondents using Krejucie and Morgan table of 1970 (Amin, 2005).

3.3.1 Sampling Procedure

Table 1 Showing sample size and sampling techniques

Category	Population	Sample Size	Sampling technique
Grade A Branch			
Operational staff	76	44	Simple random Sampling
Middle mangers	11	06	Simple random Sampling
Administration	10	06	Simple random Sampling
Sub total	**97**	**56**	
Grade B Branch			
Operational staff	72	42	Simple random Sampling
Middle mangers	09	05	Simple random Sampling
Administration	12	07	Simple random Sampling
Sub-total	**93**	**54**	
Grade C Branch			
Operational staff	68	39	Simple random Sampling
Middle mangers	08	05	Simple random Sampling
Administration	14	08	Simple random Sampling
Sub total	**90**	**52**	
Overall total	**280**	**162**	

Source: Human resource Manual, April (2017) for the Commercial banks

3.3.2 Sample Technique

According to Sekaran (2013), sampling is the process of choosing the research units of the target Population, which are to be included in the study. The study used simple random sampling during the process of data collection from the study respondents. The study applied purposive sampling technique because it gave all the people the chances of being selected. Simple random sampling was used to select all the study respondents during data collection process in the study area.

3.4 Data sources

The researcher gathered information through the primary sources.

Primary source

This enabled the researcher to attain information from the field. Data collection in this case was done through the use of questionnaire. Data was collected from people's opinions, ideas through questioning and interviewing the study respondents.

3.5 Data collection instrument

3.5.1 Questionnaire

A questionnaire was the major instrument used for data collection. The questionnaire was preferred for this study because it enabled the researcher reach a larger number of respondents within a short time, thus made it easier to collect relevant information. The first section in the questionnaire was the face sheet, to collect data on profile of respondents. The second section in the questionnaire was risk management, the third section of the questionnaire had questions on profitability. All the questions were Likert Scaled on four points ranging from 1= strongly disagree, 2 = disagree, 3 = agree, and 4 = strongly agree. The questionnaires contained close-ended questions to collect quantifiable data relevant for precise and effective correlation of research variables. They were also preferred to save time, enabled respondents to easily fill out the questionnaires and keep them on the subject and relatively objective.

3.5.2 Interview Guide

The interview was used to collect information about the study from the selected administrators and managers of Salam bank branches. The respondents were asked questions including opinions on the subject matter.

3.6 Validity and Reliability

3.6.1 Validity

The researcher ensured the validity of the instrument by face validity analysis using research supervisors who went on checking if all the items constructed could help achieve the aim of the study. This was done by use of content validity index, and then a content validity index (CVI) was computed using the following formula:

$$CVI = \frac{No.of questions declared valid}{total No.of questions in the questionnaire}$$

$$CVI = \frac{30}{35}$$

$$CVI = \underline{\mathbf{0.85}}$$

The CVI was 0.85 above 0.70 which is the minimum value always based on to declare a research instrument valid.

3.6.2 Reliability

To ensure the reliability of the instrument, the researcher used the test-retest method. The questionnaire was given to 10 people who were part of the target population and after two weeks, the same questionnaire was given to the same people and the Cronbatch Alpha was computed using SPSS.

Table 2: showing reliability test result

Reliability Statistics

Cronbach's Alpha	N of Items
.886	30

The research instrument was declared reliable since the Cronbach's Alpha value was above 0.75 which is the minimum Cronbach's Alpha value required declaring an instrument reliable.

3.7 Data Gathering Procedures

3.7.1 Before the administration of the questionnaires

Before the administration of the questionnaires the researcher took an introductory letter from the College of Economics and Management (CEM), the researcher had to first seek authorization from the proposed respondents to conduct research and review the questions to avoid errors and ensured that only qualified respondents are approached.

3.7.2 During the administration of the questionnaires

The respondents were requested to sign and answer the questionnaires. The researcher emphasized retrieval of the questionnaires within three days from the date of distribution. And lastly, all returned questionnaires were checked if all are answered.

3.7.3 After the administration of the questionnaires

The data gathered was collected, coded into the computer and statistically treated using the Statistical Package for Social Sciences (SPSS). Interrelated statistics such as frequencies, means, regression analysis were used to determine the magnitude of variables.

3.8 Data Analysis

3.8.1 Qualitative data

After collecting data, it was processed and analyzed. The qualitative data was analyzed by sorting out major themes, concepts and ideas that relate to the variables of the study so as to make meaning and draw conclusions. All the relevant information was put in place to ensure that the necessary information is available before data analysis.

3.8.2 The quantitative data

The data collected was entered into statistical package for social scientists coded and all the errors were removed, and the results attained on mean and standard deviations. The data on mean attained a numerical scale that was designed based on highest value minus lowest and divided by highest value in the likert scale. The interpretations for the data for both the independent and dependent variables were interpreted using the following mean ranges:

Mean Range	Response Mode	Interpretation
3.26 - 4.00	strongly agree	Very satisfactory
2.51 - 3.25	agree	Satisfactory
1.76 - 2.50	Disagree	Unsatisfactory
1.00 - 1.75	strongly disagree	Very unsatisfactory

The regression analysis was used to determine the effect of risk identification, risk assessment and risk monitoring and control on profitability of commercial banks. The decision rule for the data analysis was based on simple regression to determine the effect of risk management on profitability of the commercial banks in Mogadishu and the decision rule based on 0.05 level of significance.

3.8.3 Decision rule

The hypotheses were tested based on the decision rule of 0.05 level of significance. The decision to test hypothesis was on the regression coefficients (significant values, all the values that were below 0.05 level were found to be significant and the hypothesis was rejected on all the variables since they were all found to have significant value less than 0.05.

3.9 Ethical consideration

Seeking permission from bank authorities to conduct research

Maintaining the privacy and confidentiality of the respondents that is to say keep their personal issues private and non disclosure of response from particular respondents to maintain integrity and also protect them from potential victimization.

Maintaining honesty and avoiding exceptional and deceptive behavior such as creating false impression in the minds of participants through withholding information, establishing false intimacy or telling lies as this could potentially harm research participants.

Reported what was actually found and published but not dream up data and also giving due recognition to any one whose work could have been used in this research and not try to pass it as the researchers original work.

CHAPTER FOUR

DATA PRESENTATION, ANALYSIS AND INTERPRETATION

4.0 Introduction

This chapter presented, analyzed and interpreted data collected from the field. Data analysis and interpretation was based on the research objectives. Below are the data presentations and analysis of research findings;

4.1 Demographic characteristics of the Respondents

Table 4.1 below showed the profile information of respondents as to gender, age, level of education, years spent in a bank and position held.

Table 3: Demographic characteristics of the Respondents

Gender	**Frequency**	**Percent**
Male	102	63
Female	60	37
Total	**162**	**100**
Age		
20-29	37	22
30-39	62	38.3
40-49	38	23.5
50 years and above	24	14.8
Total	**162**	**100**
Education qualification		
Certificate	18	11.1
Diploma	45	27.8
Degree	78	48.1
Masters	19	11.7
Others	2	1.2
Total	**162**	**100**
Years spent working in the bank		
Less than 1 year	16	9.9
1-3 years	34	21.0
4-6 years	87	53.7
7 years and above	25	15.4
Total	**162**	**100**
Position held		
Administrator	24	14.8
Human resource	33	20.4
Customer consultant	18	11.1
Staff	87	53.7
Total	**162**	**100**

Sources: Primary Data 2018

According to gender, results showed that 63% were male and 37% of the respondents were female. This clearly implied that majority of Salam bank branches in Mogadishu Somalia are run and dominated by men. Results in table 4.1 indicated that majority of the respondents represented in this study were between 30-39 years (38.3%), followed by respondents' age between 40-49years (23.5%), 22% were between 20-29 years and finally 14.8% were 50 years and above.

Table 4.1 also showed that majority of the respondents had attained bachelor's degree (48.1%), the second group of the respondents were (27.8%) had only attained diploma as far as education is concerned, the third group (11.7%) had attained masters, 11.1% were certificate holders and only 1.2% were regarded as others who could be having professional certificates. In terms of years spent working, majority of the respondents (53.7%) had worked for 4-6 years, followed by those between 1-3 years (21%), 15.4% had worked for 7 years and above, finally 9.9% had worked for less than 1 year. This indicated that majority of these respondents had enough experience in their respective bank branches, and therefore they could provide the researcher with the information required. With respect to position held; results indicated that majority were operational staffs (53.7%), 20.4% were from human resource, 14.8% were administrators and finally 11.1% were customer consultants.

4.2 Risk management

The independent variable in this study was risk management, this variable (IV) was broken into three constructs and these were; risk identification (with five items/questions), risk assessment (with four questions) and risk monitoring and control (with five questions). Each of these questions was based on a four point Likert scale whereby respondents were asked to rate the risk management by indicating the extent to which they agree or disagree with each question, as indicated in table 4.2.

Table 4: Risk management

Items on risk management	**Mean**	**Interpretation**	**Rank**
Risk identification			
You always document and communicate to your bosses about the potential risks	3.41	Very Satisfactory	1
As your first step in risk management you always look closely at your work which let you identify the potential risks	2.93	Satisfactory	2
Identifying of risks has helped you avoid the difficulties and biasness in your department	2.87	Satisfactory	3
The risks in your organization are always over weighted and participants are sensitized to them	2.41	Unsatisfactory	4
Risks in your organization are always identified prospectively and some of them are on the key risk list	2.21	Unsatisfactory	5
Average mean	2.77	Satisfactory	
Risk assessment			
You always carryout objective evaluation of risks in which assumptions and uncertainties are clearly considered and presented	3.34	Very Satisfactory	1
You always determine quantitative value of risk related to concrete situation in your bank	3.27	Very Satisfactory	2
You always determine the rate of occurrence when the statistical information is available on all kinds of past incident	2.77	Satisfactory	3
You always assess, priotise and implement the risk management plan	2.33	Unsatisfactory	4
Average mean	2.93	Satisfactory	
Risk monitoring and control			
Your objective during risk monitoring and control is always to explore risk response strategies	3.30	Very satisfactory	1
Your risk monitoring and control always identifies and assigns parties to take responsibility for each risk response	2.87	Satisfactory	2
Your always explore risk response strategies	2.54	Satisfactory	3
You organization always set policies, procedures, goals and responsibility standards during risk monitoring and control	2.35	Unsatisfactory	4
Your organization always formalize risk monitoring and control throughout a high way agency which helps in establishing a risk culture	2.12	Unsatisfactory	5
Average mean	**2.66**	**Satisfactory**	
Overall mean	**2.80**	**Satisfactory**	

Source: Primary Data, 2018

Mean range	Response range	Interpretation
3.26 - 4.00	strongly agree	Very satisfactory
2.51 - 3.25	agree	Satisfactory
1.76 - 2.50	disagree	Unsatisfactory
1.00 - 1.75	strongly disagree	Very unsatisfactory

Results in table 4.2 denoted that the extent of risk management in Salam bank is generally satisfactory and this was indicated by the overall mean of 2.80, implying that the bank managers and workers always document and communicate to their bosses about the potential risks in the bank. With respect to risk identification; results indicated that risk identification was rated satisfactory and this was indicated by the average mean (mean=2.77), the bank managers and workers always document and communicate to the bosses about the potential risks in the bank and this was the highest rated item on risk identification (mean=3.41), still under risk identification results indicated that the risks in these Salam bank branches are always not identified prospectively and some of them are not on the key risk list (mean=2.21), implying that as their first step in risk management, bank managers and workers always look closely at their job activities which helps them identify the potential risks.

Regarding risk assessment; results in table 4.2 indicated that four items were used to measure this construct and it was also rated satisfactory on average and this was indicated by the average mean of 2.93, the highest rated item on risk assessment was; You always carryout objective evaluation of risks in which assumptions and uncertainties are clearly considered and presented (mean=3.34), under risk assessment managers and workers always determine quantitative value of risk related to concrete situation in the bank (mean=3.27), still under risk assessment managers and workers always determine the rate of occurrence when the statistical information is available on all kinds of past risk incidents (mean=2.77), yet the results still indicated that bank managers and workers do not always prioritize and implement the risk management plan (mean=2.33), implying that the bank managers and workers always fail to carryout objective evaluation of risks in which assumptions and uncertainties are not clearly considered and presented.

Concerning risk monitoring and control; results in table 4.2 indicated that five items were used to measure this construct and it was also rated satisfactory (average mean=2.66), the highest rated item on risk assessment was that the managers' and workers' objective during risk monitoring and control is always to explore risk response strategies (mean=3.30), under risk monitoring and control managers and workers always identify and assign parties to take responsibility for each risk response (mean=2.87), still under risk monitoring and control managers and workers always explore risk response strategies (mean=2.54), yet the results still indicated that bank managers and workers do not always formalize risk monitoring and control throughout a high way agency which helps in establishing a risk culture (mean=2.12), implying that the managers' and workers' objective during risk monitoring and control is always not to explore risk response strategies.

4.3 Profitability

Profitability is the dependent variable in this study and was broken into two constructs and these are; profitability (with five questions) and sales growth (with five items). Each of these questions was based on a four point Likert scale and respondents were asked to rate profitability by indicating the extent to which they agree or disagree with each question, their responses were analyzed using SPSS and summarized using means and standard deviations as indicated in tables 4.3;

Table 5: Profitability

Items on profitability	Mean	Std.	Interpretation	Rank
Gross profit margin				
The profit margin is appropriate to the expectations of the owner(s)	2.90	1.053	Satisfactory	1
You always plan and meet the profit margin	2.73	1.053	Satisfactory	2
Survival of this business has been due to the profits you always earn	2.65	1.165	Satisfactory	3
You always plan to increase profit margin in the business	2.60	1.048	Satisfactory	4
Your profit margin has always exceeded the expenditure	2.41	1.037	Unsatisfactory	5
Average mean	**2.66**	**.59070**		
Return on assets				
The current assets are generative of more profits in your business	3.32	.863	Very satisfactory	1
The net operating assets sufficiently support your daily operations	2.84	1.083	Satisfactory	2
The return on assets is higher than the costs of operation in the previous period	2.52	1.079	Satisfactory	3
There has been gained profits on the capital employed by business	2.47	1.107	Unsatisfactory	4
Your business has attained expansion because of high returns on assets	2.42	1.107	Unsatisfactory	5
Average mean	**2.72**	**.67783**		
Returns on invested capital				
Your bank has reached a point at which returns on invested capital are equal to expenses	3.29	.910	Very satisfactory	1
The state of invested capital in your bank is steadily growing every day	2.79	.971	Satisfactory	2
Your net returns on invested capital are high	2.72	1.128	Satisfactory	3
Your returns on invested capital are higher than the cost of goods sold per month	2.64	.974	Satisfactory	4
Shareholders of this bank receive relatively high returns on invested capital	2.09	1.123	Unsatisfactory	5
Average mean	**2.70**	**.59182**		
Overall mean	**2.69**	**.44560**		

Sources: Primary Data 2018

Results in table 4.3 indicated that the level of profitability is high and this was indicated by the overall mean of 2.69, which implies that commercial banks in

Mogadishu Somalia have resources which can make them financially perform well. With respect to gross profit margin; this was the first construct on the dependent variable and was measured using five items/questions and it was rated satisfactory (average mean=2.66), implying that the commercial banks in Mogadishu Somalia always earn relatively high profits. Still results indicated that the profit margin is appropriate to the expectations of the owner(s) (mean=2.90), always plan and meet the profit margin (mean=2.73), survival of this business has been due to the profits you always earn (mean=2.65), always plan to increase profit margin in the business (mean=2.60), but however during business activities the profit margin has not always exceeded the expenditure (mean=2.41).

Concerning returns on assets; results in table 4.3 indicated that this construct was rated satisfactory and this was indicated by the average mean of 2.72. Still results indicated that the current assets are generative of more profits in the bank (mean=3.32), the net operating assets sufficiently support the daily operations (mean=2.84), the return on assets is higher than the costs of operation in the previous period (mean=2.52), however there has been no gained profits on the capital employed by bank blanches for the last few months (mean=2.47) and they have not attained expansion even though they have got high returns on assets (mean=2.42).

With respect to returns on invested capital; results in table 4.3 indicated that this construct was rated satisfactory and this was indicated by the average mean of 2.70. Still results indicated that Salam bank has reached a point at which returns on invested capital are equal to expenses (mean=3.29), the state of invested capital in the bank is steadily growing every day (mean=2.79), the net returns on invested capital are high (mean=2.72), the returns on invested capital are higher than the cost of goods sold per month (mean=2.64), however shareholders of this bank receive relatively high returns on invested capital (mean=2.09).

4.4 Objective one; effect of risk identification on profitability of commercial banks in Mogadishu Somalia

Table 6

Variables regressed	**R Squared**	**F-value**	**Sig.**	**Interpretation**	**Decision on H_o**
Risk identification VS Profitability	.352	84.756	.000	Significant effect	Rejected
Coefficients	**Beta**	**t-value**	**Sig.**		
(Constant)	1.607	13.232	.000	Significant effect	Rejected
Risk identification	.380	9.206	.000	Significant effect	Rejected

Regression analysis results in the Model Summary table revealed that risk identification accounted for 35.2% on profitability of commercial banks in Mogadishu Somalia and this was indicated by r-squared of 0.352 implying that risk identification contribute to the profitability of commercial banks in Mogadishu Somalia.

The ANOVA table indicated that risk identification significantly affects the profitability and this was indicated by the F-value=84.756 and Sig-value=.000, since the sig. value (0.000) was less than 0.05 and which is the maximum level of significance required to declare a significant effect. This implies that risk identification highly contributes to the profitability of commercial banks in Mogadishu Somalia.

The coefficients table indicated that considering the standard error, risk identification significantly influence the profitability of commercial banks in Mogadishu Somalia (β=0.380, Sig=0. 000).

Testing for hypothesis

The hypothesis was rejected since the significant value was found to be less than 0.05 (Sig=0. 000).

4.5 Objective two; the effect of risk assessment on profitability of commercial banks in Mogadishu Somalia

Table: 7

Variables regressed	R Squared	F-value	Sig.	Interpretation	Decision on H_o
Risk assessment VS Profitability	.315	71.395	.000	Significant effect	Rejected
Coefficients	**Beta**	**t-value**	**Sig.**		
(Constant)	1.646	12.991	.000	Significant effect	Rejected
Risk assessment	.373	8.450	.000	Significant effect	Rejected

Regression analysis results in the Model Summary table indicated that the risk assessment accounted for 31.5% on profitability of commercial banks in Mogadishu Somalia and this was indicated by r-squared of 0.315 implying that risk assessment significantly contributes 31.5% on profitability of commercial banks in Mogadishu Somalia.

The ANOVA table indicated that risk assessment significantly affects the profitability and this was indicated by the F-value=71.395 and Sig-value=.000, since the sig. value (0.000) was less than 0.05 and which is the maximum level of significance required to declare a significant effect. This implies that risk assessment highly affects the profitability of commercial banks in Mogadishu Somalia.

The coefficients table indicated that considering the standard error, risk assessment significantly affects profitability of Salam bank (β=0.373, Sig=0. 000).

Testing for hypothesis

The hypothesis was rejected since the significant value was found to be less than 0.05 (Sig=0. 000).

4.5 Objective three; effect of risk monitoring and control on profitability of commercial banks in Mogadishu Somalia

Table 8

Variables regressed	**R Squared**	**F-value**	**Sig.**	**Interpretation**	**Decision on H_o**
Risk monitoring VS Profitability	.377	93.669	.000	Significant effect	Rejected
Coefficients	**Beta**	**t-value**	**Sig.**		
(Constant)	1.601	13.716	.000	Significant effect	Rejected
Risk monitoring	.399	9.678	.000	Significant effect	Rejected

Regression analysis results in the model Summary table indicated that the risk monitoring and control significantly affects profitability of commercial banks in Mogadishu Somalia at a rate of 37.7% and this was indicated by r-squared of 0.377, hence implying that risk monitoring and control significantly influence the profitability of commercial banks in Mogadishu Somalia.

The ANOVA table indicated a positive significant effect risk monitoring and control has on profitability and this was indicated by the positive F-value=93.669 and Sig-value=.000, since the sig. value (0.000) was less than 0.05 and which is the maximum level of significance required to declare a significant effect. This implies that risk monitoring and control highly affects the profitability of commercial banks in Mogadishu Somalia. Still this implied that high levels of risk monitoring and control can improve the level of profitability and poor risk monitoring and control measures reduce it.

The coefficients table indicated that considering the standard error, risk monitoring and control significantly affects profitability of Salam bank (β=0.399, Sig=0. 000).

Testing for hypothesis

The hypothesis was rejected since the significant value was found to be less than 0.05 (Sig=0. 000).

CHAPTER FIVE

DISCUSSIONS, CONLUSIONS AND RECOMMENDATIONS

5.0 Introduction

This chapter focuses on the findings, conclusions, recommendations based on the conclusions of this study and suggested areas that need further research following the study objectives;

5.1 Discussions

This study examined the effect of risk management on profitability of Commercial banks in Mogadishu Somalia, three specific objectives guided this study and these were i) determining the effect of risk identification on profitability of commercial banks in Mogadishu Somalia; ii) examining the effect of risk assessment on profitability of commercial banks in Mogadishu Somalia and (iii) to establish the effect of risk monitoring and control on profitability of commercial banks in Mogadishu Somalia.

5.1.1 Objective one; the effect of risk identification on profitability

The findings indicated that risk identification significantly affects the profitability of commercial banks in Mogadishu Somalia, this effect therefore implies that risk identification contribute to the profitability of Commercial banks in Mogadishu Somalia. This finding is in line with Douglas (2009) who noted that risk management involves acts such as identification, assessment, and prioritization of risks followed by coordinated and economical application of resources to minimize, monitor, and control the probability and/or impact of unfortunate events or to maximize the realization of opportunities. Risks can come from uncertainty in financial markets, threats from project failures (at any phase in design, development, production, or sustainment life-cycles), legal liabilities, credit risk, accidents, natural causes and disasters as well as deliberate attack from an adversary, or events of uncertain or unpredictable root-cause (Douglas, 2009).

The finding is also in line with Dorfman (2011) who noted that identifying risks prospectively can help avoid these difficulties and it reduces some of the bias in the risk assessment, by not confusing recent experience with future likelihood and impact. It also focuses management away from the past, and concentrates attention on what might impact the company's ability to deliver on its strategic objectives going forward. This enables a robust, untainted examination of where the company is, where it's headed and what could get in the way. He also added that the first step in risk management is to look closely at your business and identify potential risks. Until you know the scope of all possible risks, you cannot develop a realistic, cost-effective strategy for dealing with them. The aim of this stage of risk management is to create a database of risks relevant to the particular business (Dorfman, 2011).

5.1.2 Objective two; the effect of risk assessment on profitability

The findings revealed that there is a significant effect risk assessment has on profitability of commercial banks in Mogadishu Somalia, this also implied that high risk assessment can improve on the level of profitability of Commercial banks in Mogadishu Somalia and poor risk assessment reduces it. This finding agrees with Simon (2000) who noted that risk assessment consists of an objective evaluation of risks in which assumptions and uncertainties are clearly considered and presented. Part of the difficulty in risk management is that measurement of both of the quantities in which risk assessment is concerned where potential loss and probability of occurrence can be very difficult to measure. Peter Simon also added that the chance of error in measuring these two concepts is high. Risk with a large potential loss and a low probability of occurrence, is often treated differently from one with a low potential loss and a high likelihood of occurrence. In theory, both are of near equal priority, but in practice it can be very difficult to manage when faced with the scarcity of resources, especially time, in which to conduct the risk management process. Risk assessment is simply looking closely at what in your place of work or about your work activities could cause harm to your employees and visitors to your workplace (e.g. customers, suppliers, sales representatives etc) and determining the control measures you can implement to minimise the risk (Peter Simon, 2000).

5.1.3 Objective three; the effect of risk monitoring and control on profitability

The findings of this study proved a positive significant effect risk monitoring and control have on profitability of commercial banks in Mogadishu Somalia, this therefore implies that good risk monitoring and control increases the level of profitability of Commercial banks in Mogadishu Somalia and poor risk monitoring and control reduces it. This finding is in line with Vick (2013) who noted that the objectives of risk monitoring and control are to explore risk response strategies for the high risk items identified in the qualitative and quantitative risk analysis. The owner of the risk could be an agency planner, engineer, or construction manager, depending on the point in project development, or it could be a private sector contractor or partner, depending on the contracting method and risk allocation. Risk monitoring and control may require that agencies set policies, procedures, goals, and responsibility standards. Formalizing risk monitoring and control throughout a highway agency will help establish a risk culture that should result in better cost management from planning through construction and better allocation of project risks that align teams with customer-oriented performance goals (Vick, 2013).

5.2 Conclusions

5.2.1 Objective one; the effect of risk identification on profitability

According to the findings risk identification has a positive significant effect on profitability of commercial banks in Mogadishu Somalia. Therefore risk identification has a considerably high influence on profitability of the commercial banks, hence there is need for improving the risk identification so as to enhance profitability.

5.2.2 Objective two; the effect of risk assessment on profitability

According to the findings risk assessment has a significant effect on profitability of commercial banks in Mogadishu Somalia. Hence risk assessment has a high bearing on profitability of the commercial banks, and therefore that the bank managers and workers should always document and communicate to their bosses about the potential risks.

5.2.3 Objective three; the effect of risk monitoring and control on profitability

According to the findings risk monitoring and control has a positive significant effect on profitability of commercial banks in Mogadishu Somalia. Therefore risk monitoring and control has a bearing on the profitability hence there is need for enhancing monitoring given the state of the profits though other factors complemented in the study.

5.3 Recommendation

5.3.1 Effect of risk identification on profitability of commercial banks

Risk identification was found operating though with limited capacity, there is need to enhance risk identification through improving the mechanism for categorizing risks as the strategy for enhancing profitability. The process of risk identification in commercial banks should be very comprehensive covering all departments and sections as this will enable management to effectively implement risk identification strategies. Commercial banks in Mogadishu should look at other factors that directly affect profitability. These include availability of qualified personnel to implement risk management, the level of technology applied and the effect of changes in demand.

5.3.2 Effect of risk assessment on profitability of commercial banks

Risk assessment appropriateness needs to be enhanced through enhancing the risk assessments mechanisms as practical situations to improve profitability. There is need for bank managers who are responsible for the setting risk assessment standards and should be educated on the relevance for the risks in the commercial banks. Adherence to the standard risk information should be practiced by the top management as it is a tool for the improvement of profit in the commercial banks.

5.3.3 Effect of risk monitoring and control on profitability of commercial banks

The commercial banks need to improve the status quo on risk monitoring and control in order to enhance the state of monitoring aspects that negatively affect profitability. There is need to improve the stakeholders' involvement in risk monitoring and control especially in assessing the challenges involved in determining risks.

5.4 Contribution to knowledge

The following are the risk management techniques used in maintaining the profitability of commercial banks in Mogadishu Somalia; risk identification, risk assessment and risk monitoring and control. The following are the measurements of profitability in commercial banks in Mogadishu Somalia; gross profit margin, return on assets and returns on investment. One of the most prominent findings from this study is the fact that it has provided evidence to support the fact that risk management can improve the state of profitability of the commercial banks in Mogadishu Somalia. Another important revelation that can be attributed to this study is that it is now clear that risk management is of low nature, little is done through risk management to improve profitability in commercial banks in Mogadishu Somalia. This is contrary to common belief that banks operate on profits with less control on risks this could be due to the insignificant degree of the prevalence of risk management.

5.5 Limitations of the study

Long distance from the institution to the area of the study is one of the anticipated limitations the researcher faced. However, the researcher tried as much as possible to move to the area to collect the data in phases to ease on transport charges.

Non-response to certain questions and providing of false information was another anticipated limitation to the study. This was due to the fear by some respondents that the researcher could expose their identities. However, the researcher used logical questions so that the respondents were able to release such information needed by the researcher.

5.6 Areas for further research

Prospective researchers and even students are encouraged to research on the following areas;

1) Risk assessment and profitability of commercial banks in Mogadishu Somalia
2) Risk control and profitability of commercial banks in Mogadishu Somalia
3) The challenges facing the profitability of commercial banks in Mogadishu Somalia

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Appendix i: Research Questionnaire

Section A: Demographics of respondents (Pick the appropriate response)

1. Gender
   1) Male ☐
   2) Female ☐
2. Highest level of qualification
   1) Certificate and Diploma ☐
   2) Degree ☐
   3) Masters ☐
   4) others ☐
3. Age
   a) 20 - 29 ☐
   b) 30 – 39 ☐
   c) 40 – 49 ☐
   d) 50+ ☐
4. How long have you worked in this organization
   1) Less than 1 year ☐
   2) Below 1-3 years ☐
   3) Between 3-5 years ☐
   4) 6 years and above ☐
5. Position held in the organization
   1) Administrator ☐
   2) Human resource ☐
   3) Customer consultant ☐
   4) Staff ☐

The use of Likert scale were 1= Strongly disagree, 2= Disagree, 3=Agree, 4= Strongly Agree.

Direction: please tick the column corresponding rating that best describes your response using the guide below

Score mode of response description

4 Strongly agree you agree with no doubt

3 Agree you agree with some doubt

2 Disagree you disagree with some doubt

1 Strongly disagree you disagree with no doubt

SECTION B: questionnaire to determine the level of risk management

Direction: please tick your rating on the space under each column which corresponds to your best choice.

Rate	**Response mode**	**Description**	**Interpretation**
4	Strongly agree	You agree with no doubt at all	Very satisfactory
3	Agree	You agree with some doubt	Satisfactory
2	Disagree	You disagree with some doubt	Fair
1	Strongly disagree	You disagree with no doubt	Poor

Extent of risk management		**Rating**			
No		**4**	**3**	**2**	**1**
	Risk identification				
1	Risks in your organization are always identified prospectively and some of them are on the key risk list	4	3	2	1
2	The risks in your organization are always over weighted and participants are sensitized to them	4	3	2	1
3	Identifying of risks has helped you avoid the difficulties and biasness in your organization				
4	As your first step in risk management you always look closely at your business which let you identify the potential risks				
5	You always document and communicate to your bosses about the potential risks in this project	4	3	2	1
	Risk assessment				
1	You always determine the rate of occurrence when the statistical information is available on all kinds of past incident	4	3	2	1
2	You always priotise and implement the risk management plan	4	3	2	1
3	You always carryout objective evaluation of risks in which assumptions and uncertainties are clearly considered and presented	4	3	2	1
4	You always determine quantitative value of risk related to concrete situation in your business				

	Risk monitoring and control				
1	Your always explore risk response strategies	4	3	2	1
2	Your risk monitoring and control always identifies and assigns parties to take responsibility for each risk response	4	3	2	1
3	You organization always set policies, procedures, goals and responsibility standards during risk monitoring and control	4	3	2	1
4	Your organization always formalize risk monitoring and control throughout a high way agency which helps in establishing a risk culture				
5	Your objective during risk monitoring and control is always to explore risk response strategies.				

SECTION C: Level of Profitability in commercial banks in Mogadishu Somalia

Indicate your level of agreement on the following determinants of profitability in commercial banks.

	Profitability	**1**	**2**	**3**	**4**
	Gross profit margin				
1	You always plan and meet the desired profits				
2	Survival of this bank has been due to the profits you always earn				
3	The returns on capital employed is appropriate to the expectations of the bank owner(s)				
4	You always plan to increase profitability in the bank				
5	Your bank revenue have always exceeded the expenditure				
	Return on assets				
1	Your bank has attained expansion because of high returns on assets				
2	The current assets are generative of more profits in your bank				
3	There has been gained profits on the capital employed by bank				
4	The net operating assets sufficiently support your daily operations				
5	The return on assets is higher than the costs of operation in the previous period				
	Returns on invested capital				
1	Shareholders of this bank receive relatively high returns				
2	Your net profit margins are high				
3	Your bank has reached a point at which revenues are equal to expenses				
4	Your sales are higher than the cost of goods sold per month				
5	The state of capital in your bank is steadily growing every day				

Appendix ii: Interview Guide for Administrators

1. What is the effect of risk identification on profitability of commercial banks in Mogadishu , Somalia?
2. What is the effect of risk assessment on profitability of commercial banks in Mogadishu , Somalia?
3. What is the effect of risk monitoring and control and control on profitability of commercial banks in Mogadishu , Somalia?

Appendix iii: Table for determining the sample size

Krejucie, Robert V, Morgan, Daryle W, table of 1970

N	S	N	S	N	S	N	S	N	S
10	10	100	80	**280**	**162**	800	260	2800	338
15	14	110	86	290	165	850	265	3000	341
20	19	120	92	300	169	900	269	3500	246
25	24	130	97	320	175	950	274	4000	351
30	28	140	103	340	181	1000	278	4500	351
35	32	150	108	360	186	1100	285	5000	357
40	36	160	113	380	181	1200	291	6000	361
45	40	180	118	400	196	1300	297	7000	364
50	44	190	123	420	201	1400	302	8000	367
55	48	200	127	440	205	1500	306	9000	368
60	52	210	132	460	210	1600	310	10000	373
65	56	220	136	480	214	1700	313	15000	375
70	59	230	140	500	217	1800	317	20000	377
75	63	240	144	550	225	1900	320	30000	379
80	66	250	148	600	234	2000	322	40000	380
85	70	260	152	650	242	2200	327	50000	381
90	73	270	155	700	248	2400	331	75000	382
95	76	270	159	750	256	2600	335	10000 0	384

Note: "N" is population size

"S" is sample size.