

# Macroeconomic Policies, Currency Risks and Banks' Competitiveness

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## ABSTRACT

This paper assesses the relationship between macroeconomic policies, Currency risks, and Banks' Competitiveness. Specifically, the study analyzed: (1) the relationship between monetary, fiscal policies and banks' competitiveness; (2) the relationship between exchange rate volatility, value at risk, credit worthiness, deteriorating loan portfolio and banks' competitiveness. To operationalise these objectives, a cross-sectional and descriptive research design was used to report on the study phenomenon. A researchers' made questionnaire was then used to collect data from a population of 200 respondents which were sampled to 185 respondents using the Krejcie and Morgan (1972) sampling method. Purposive, stratified and simple random sampling techniques were devised to collect data depending on the category of respondent targeted. Data was analyzed using the Statistical Package for Social Scientist (SPSS) computer programme. Specifically, the Pearson (r) correlation coefficient was used and indicated a significant and positive relationship between macroeconomic policies, currency risks and Banks' competitiveness (r value = .491\*\*, p<.01; r value = .301\*\*, p<.01) respective. On the other hand, the regression analysis predicted a moderated influence of (R value = 27.7%, and sig. 0.001) between macroeconomic policies, currency risks and Banks' Competitiveness. The researchers therefore concluded that, macroeconomic policies and currency risks positively relate with Banks competitiveness. Whenever macroeconomic policies and/ or currency risks are favorable, banks will be competitive and reverse is true. In this regard, managers ought to be proactive in forecasting and monitoring government policies, be it fiscal or monetary, and ensure that costs charged on loan facilities are reasonable to attract clients thus enhancing Banks competitiveness.

**Keywords:** *Macroeconomic Policies, Currency Risk, Banks Competitiveness*

## 1. INTRODUCTION

Macroeconomic policies are government policies aimed at the aggregate economy, usually to promote the macro goals of full employment, stability, and growth (Bouman, 2011). Macroeconomics is the field of economics that studies the behavior of the aggregate economy wide phenomena such as changes in unemployment, national income, rate of growth, gross domestic product, inflation and price levels (Brian & Vane, 2005). The four major objectives macroeconomic policies are; full employment, price stability, a high but sustainable rate of economic growth, and keeping the Balance of Payments in equilibrium (Gärtner, 2006). Macroeconomic policies influence and contribute to the attainment of rapid, sustainable economic growth aimed at poverty reduction in a variety of ways (Agenor, 2000). By pursuing sound economic policies, policymakers send clear signals to the private sector. Macroeconomic policies are usually implemented through two sets of tools; fiscal and monetary policy attributes (Blanchard, 2000).

Currency Risks, is sometimes referred to as exchange rate risks and credit risk is the possibility that currency depreciation will negatively affect the value of one's assets, exchange rates, investments and their related interest and dividend payment streams especially those securities denominated in foreign currency (Silvia, 2011).

Currency risk is a form of risk that arises from the change in price of one currency against another. This

decline in value negatively affects an economy by creating instabilities in exchange rates, meaning that one unit of the currency no longer buys as much as it used to in another. Whenever investors or companies have assets or business operations across national borders, they face currency risk if their positions are not hedged (Straka, 2000) and (Wheaton et al., 2001). Credit risk is the risk of loss due to the inability or unwillingness of a counter-party to meet its contractual obligations (BOU Report, 2007). In this study, currency risks attributes considered, include the following; nonperforming loans (NPLs), credit worthiness parameters, exchange rate volatility, deteriorating loan portfolio and value at risk based.

Competitiveness is the productivity with which a nation utilizes its human, capital and natural resources as defined by Ketels, (2006). Competitiveness pertains to the ability and performance of a firm, sub-sector or country to sell and supply goods and services in a given market, in relation to the ability and performance of other firms, sub-sectors or countries in the same market (Easterly & Levine, 2002). The Global Competitiveness Report 2001/2002 of the World Economic Forum defines competitiveness as "the set of institutions, policies, and factors that determine the level of productivity of a country". To understand competitiveness, the starting point must be a nation's underlying sources of prosperity. Experts say national competitiveness is regarded as a byproduct of national competitiveness at the firm level, at the industrial level and at the international level (Nyanzi, 2012).

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True competitiveness, then, is measured by productivity. Organizational competitiveness is the degree to which an organization can, under free and fair market conditions, produce goods and services that meet the test of international market while simultaneously maintaining or expanding the real incomes of its employees and owners (Ivancevich & Konopaske, 2006). Bank's competitiveness refers to the ability and performance of that institution to provide services to its customers in a given market operation while maintaining soundness and expanding incomes of its employees and owners (Vukovic, et al., 2012). Banks' competitiveness attributes are; deposits Vs loan size, profitability Vs growth, access to finances and soundness based on Easterly and Levine model (2002).

### 1.1 Problem Statement

Following the financial crisis and the Libor scandal in 2008, the banking sector globally was seen as out of control and losing competitiveness (Browne, 2013). In countries like: USA, Britain; banks were bailed-out with taxpayers' money and their global reputation and integrity took a hit (Ackerman, 2008). The Ugandan banking sector has been competitive in the East African region (Berkmen et al., 2012). In the financial year 2011/2012, the banking sector made a killing; posting impressive profit figures and contributing gross taxes of over Ushs160bn up from Ushs120bn in 2010/2011 to the economy in unresponsive macro environment characterized by high inflation and lending rates, exchange rates volatility (BOU Report, 2012). One questions if these banking institutions will remain competitive; with local banks losing out ownership to foreign banks, offering micro financial services offered by microfinance institutions and unsatisfied customers, increasingly accusing banks of ripping them off while trying to keep businesses afloat in distress economy (Kabahinda, 2013). Banks charging high interest rates on loans, assets presented as collateral being sold off as noted under the CEO Magazine (2012) and public sentiments towards banks, for paying off their top managers bonuses for turning a terrible scenario very profitable (Kabahinda, 2013). According to the UBOS (2013) April report showed a reduction in inflation at 5 percent, exchange rate stabilizing and CBR at 10 percent in the country. Banks have not come up to reflect changes in their operations, that is to say; their profitability, growth rate, loan portfolio has remained low (BOU Report, 2012), which prompted the researchers to examine why with stabilized macroeconomic policies and currency risks, banks have not gained competitiveness and efficiency in their operations.

### 1.2 Purpose of the Study

The study aimed at assessing the relationship between macroeconomic policies, currency risks and banks' competitiveness. Macroeconomic policy was dimensioned in terms of: monetary, fiscal policies; while currency risks constituted attributes like: exchange rate volatility, value at risk, credit worthiness and deteriorating loan portfolio. All

of these dimensions were analyzed independently as indicated in section six (6) of this paper.

### 1.3 Research Hypothesis

From the objective or purpose above, the study hypothesized as follows: (1) there is no significant relationship between macroeconomic policies and Bank Competitiveness, and lastly, (2) there is no significant relationship between currency risks and Banks competitiveness

## 2. LITERATURE REVIEW

### 2.1 Macroeconomic Policies

While in recent years, the financial sector debate across the African continent has been dominated by policies to increase access to financial services; maximizing competitiveness currently tops the agenda (Miles & Darroch, 2010). Financial systems across Africa have seen a deepening and broadening over the past years, partly benefiting from the Great Moderation and global liquidity glut, but also from improvements in macroeconomic policies and progress in institutional reforms (Beck et al., 2009). Macroeconomic policies variable is measured through attributes monetary and fiscal policies; and their effects on interest rates, inflation, unemployment levels, economic growth and exchange rates:

### 2.2 Monetary Policies

Monetary policy is the process by which the government, central bank, or monetary authority of a country controls; the supply of money, availability of money, and cost of money or rate of interest to attain a set of objectives oriented towards the growth and stability of the economy (Forder, 2004). Monetary theory provides insight into how to craft optimal monetary policy. It is referred to as either being expansionary or contractionary, where an expansionary policy increases the total supply of money in the economy more rapidly than usual, and contractionary policy expands the money supply more slowly than usual or even shrinks it influencing the lending policy of financial institutions. Expansionary policy is traditionally used to try to combat unemployment in a recession by lowering interest rates in the hope that easy credit will entice businesses into expanding. Contractionary policy is intended to slow inflation in hopes of avoiding the resulting distortions and deterioration of asset values according to Friedman (2001).

### 2.3 Fiscal Policy

Fiscal policy (Keynesian economics theory) involves the use of government spending, taxation and borrowing to affect the level and growth of aggregate demand, output and jobs (Riley & College, 2006). This influence, in turn, curbs inflation (generally considered to be healthy when at a level between 2-3%), increases employment and maintains a healthy value of money (John,

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2009). Fiscal policy is also used to change the pattern of spending on goods and services. It is also a means by which a redistribution of income and wealth can be achieved. It is an instrument of intervention to correct for free-market failures. Changes in fiscal policy affect aggregate demand (AD) and aggregate supply (AS). Governments spend money on a wide variety of things, from the military and police to services like education and healthcare, as well as transfer payments, such as welfare benefits (Vukovic, et al., 2012). These expenditures can be funded in a number of different ways; (taxation, seignior age, borrowing, consumption of fiscal reserves and sale of fixed assets). One of the biggest obstacles facing policymakers is deciding how much involvement the government should have in the economy. Indeed, there have been various degrees of interference by the government over the years. But for the most part, it is accepted that a degree of government involvement is necessary to sustain a vibrant economy, on which the economic wellbeing of the population depends.

In 2011, government of Uganda spent trillions of Ugandan shillings to purchase fighter jets draining the nation's reserves, leaving the nation prone to external exchange rates volatilities. Inflation the rate at which the general level of prices for goods and services is rising, and subsequently, purchasing power is falling. Central banks attempt to stop severe inflation, along with severe deflation, in an attempt to keep the excessive growth of prices to a minimum. Inflation rate was at 18 per cent in 2011, up from 12 per cent in 2010 (UBOS, 2012). Tight monetary policy by Bank of Uganda (BOU) that aimed at curbing the runaway inflation and the growth in commercial bank credit to the private sector have partly been blamed as the cause of the current inflation in Uganda. Bank of Uganda responded by revising the Central Bank Rate (CBR) to 14 per cent for the month of August up from 13 per cent in June 2011 to the third quarter of 2012, as it presses ahead with a tight monetary policy aimed at curbing the current runaway inflation. BoU intended to prevent the high food inflation from feeding through to non-food items." A decision was revised, by reducing CBR to 11 per cent August 2012.

### 3. CURRENCY RISKS

In recent years, the banking industry has undergone massive changes in scope and nature (Mnyande, 2012). The impact of regulation and supervision in the banking sector, the credit crisis conditions facing many end borrowers remain challenging. Credit risks shocks in the past years was the top of discussion for financial institutions to try reducing the effect from defaulting customers (Darroch, 1999). Banks having realized a reduction in credit risks, today exchange volatility risks is a concern for banks to militate against the risk as it erodes their the value of one's assets, exchange rates, investments and their related interest and dividend payment streams especially those securities denominated in foreign currency (Silvia, 2011). The banks have tightened credit standards, making lending very

difficult. Although credit demand by domestic households and companies is currently high, the stricter lending criteria could pose future risk and affect competitiveness if household and private-sector credit demand increases. Currency risks attributes are discussed below:

#### 3.1 Exchange Rate Volatility

Traditionally, it is the average of conditional or unanticipated exchange rate changes. Would say it refers to the rate at which a country's currency in terms of others adjusts to changes in market conditions or policies as given by the government or a central monetary authority (Hericourt & Poncet, 2013). The exchange currency risks of losing the value of one currency in terms of another country's currency affects the rate of inflation in ways of prices of imported and exported commodities in a number of direct and indirect ways: Bank of Uganda research suggests that a 10% depreciation in the exchange rate can add up to 3% to the level of consumer prices three years after the initial change in the exchange rate. Inflation depends also on the response of economic policies to exchange rate movements. For example if a rising value of a shilling causes inflation to drop below target, the Monetary Policy by Bank of Uganda might opt to reduce short term interest rates in order to stabilize demand and prevent the risk of price deflation (Rilley & Colledge, 2006).

To the extent of risk movements in the exchange rate affect the growth of demand, output and investment in those sectors of the economy exposed to international trade, the rate of unemployment can also be influenced by currency fluctuations. A reduction in demand and output may cause job losses as businesses seek to control costs. This leads to low savings, deposits and borrowings, increasing the risk of default. Some industries are more exposed than others to currency fluctuations e.g. sectors where a high percentage of total output is exported and where demand is highly price sensitive (price elastic) as noted by Levi (2005).

#### 3.2 Value at Risk

A statistical technique used to measure and quantify the level of financial risk within a firm or investment portfolio over a specific time frame. For example, a financial firm may determine that it has a 5% one month value at risk of \$100 million. This means that there is a 5% chance that the firm could lose more than \$100 million in any given month. Therefore, a \$100 million loss should be expected to occur once every 20 months. VaR has four main uses in finance; risk management, financial control, financial reporting and computing regulatory capital. VaR is sometimes used in non-financial applications as well (Jin & Jorion, 2006).

There are inevitable **risks** in shifting funds across international markets. What might happen to the currency if you leave shs200, 000 worth of cash in a Uganda bank

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account? What happens to the value of your investment if a shilling depreciates against the US dollar? What are the risks in exchanging a similar value of US dollars and putting it into the Uganda stock market or into government bonds? Investors often consider the **risk-adjusted relative rate of return** from different financial investments. Thus if Uganda's interest rates are persistently above those in other countries, and the risks are pretty similar, then we would expect to see a rising demand for shilling and an appreciation of the currency. Interest rates are not the only factor that drives the external value of a currency in the foreign exchange markets but they undoubtedly do have some effect on a country's currency (<http://www.mongabay.com>, accessed on 30<sup>th</sup>-November-2012).

### 3.3 Credit Worthiness Parameters

The lenders (Banks/ Venture Capitalists, etc.) carefully assess your credit worthiness and assign ratings by analyzing your business information with respect to various parameters. The criteria document identifies and briefly addresses some of the specific factors considered by Brickwork Ratings in analyzing a Credit Rating.



**Figure 1: Brickwork Ratings Criteria**

Lenders must evaluate the risks of lending money to others before engaging such transactions as a way of credit risk mitigation (Mail contractar, 2013). In commercial lending, creditors generally follow the same principles to evaluate a borrower's creditworthiness. A creditor usually looks at three factors known as the 'Three Cs' (Capacity, Capital, and Character). In days of old, the 'Three Cs' may have been all that were needed to get the nod on a loan, but in today's information age, much more is required, such as a credit report and credit score (The Educated Investor, 2014). Credit rating agencies such as Moody's Investors Service do not issue ratings on a company. Instead, they rate specific debt or preferred stock

issued by the company (ICAP Group, 2013). In order to issue a rating on any debt instrument, ratings analysts take into account the company's capital structure (debt seniority in payment preference), company financial ratios in relative terms e.g. in comparison to companies in similar industries and/or geography. Non-financial information is also checked, e.g. does the company have a working phone number, office address, etc? These can constitute significant off-balance sheet sources of risk (Kesselman, 2014).

### 3.4 Nonperforming Loans

A non-performing loan is a loan that is in default or close to being in default (World Bank Report, 2014). Many loans become non-performing after being in default for 90 days, but this can depend on the contract terms (World Bank Report, 2014). 'A loan is nonperforming when payments of interest and principal are past due by 90 days or more, or at least 90 days of interest payments have been capitalized, refinanced or delayed by agreement, or payments are less than 90 days overdue, but there are other good reasons to doubt that payments will be made in full' (International Monetary Fund Report, 2005). Worldwide, the most common and successful approach towards NPL management is the establishment of Asset Management Companies (AMC).

These companies use public or bank funds to remove NPAs from the bank books. For example, the Korea Asset Management Corporation purchased as much as 80% of bad loans at market rate following the Asian crises. Coming back to Uganda, one of the most ever drastic dropdown in non-performance loans was 4.7 per cent in March 2013 to 3.9 per cent in June 2013 (Bank of Uganda Report, 2013). The improvement in asset quality has been particularly pronounced in the building and construction sector whose NPLs ratio reduced by 1.5 per cent in the year to June 2013. The ratio of foreign currency NPLs to foreign currency loans was only 0.8 per cent as of June 2013. The trade and commerce, and mining and quarrying sectors contributed the highest percentage to the foreign currency NPLs (Bank of Uganda Report, 2013). The risks remain and a real depreciation of the exchange rate may increase the debt burden of borrowers in foreign currency and increase bad loans (Njihia, 2013).

### 3.5 Deteriorating Loan Portfolio

Loan portfolio is the total of all loans held by a bank or finance company on any given day. Loan portfolios are the major asset of banks, thrifts, and other lending institutions. The value of a loan portfolio depends not only on the interest rates earned on the loans, but also on their quality, that is, the likelihood that interest and principal will be paid. Stress tests assess the impact of credit risk using two shocks. The first evaluates a deteriorating loan portfolio that would result in an increase in provisions by 50% and 100%, while the second assesses the impact of migrating 25% and 50% of performing loans to the substandard



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category (Friedman, 2001). The results indicate that on the whole, banks appear resilient to the shocks measured. However, the most significant impact would be felt if a riskier client base resulted in a 100% increase in provisions. These results could be seen as providing a justification for increasing minimum capital requirements.

## **4. BANKS' COMPETITIVENESS**

### **4.1 Profitability**

Despite stringent macroeconomic policies imposed by Bank of Uganda, banking industry once again demonstrated ability to post record profits, coming to the fore once more in a generally very difficult 2011/2012 financial year. The bankers openly acknowledge the tough environment last financial year but considered this as an opportunity to increase their revenues and become profitable. "Our operational costs went up because of the high inflation in the economy, however as a bank is to turn this into an opportunity to grow our portfolio," said, Kasi the Managing Director, Centenary Bank as cited in the Centenary Bank Annual Report (2012)

### **4.2 Growth**

The profitability of the banks is a representation of the continuing growth of the sector. The banking sector has remained resilient taking advantage of an economy that is in distress to post good growth figures," said, Phillip the Managing Director, Stanbic Bank as cited under the CEO Magazine (2012). We also have customers whose businesses performed well last year. Stanbic Bank is riding high on the performances of some of these clients. With another two new foreign banks set to open shop here soon, we can now conclude that the question about what these financial institutions see in Uganda has been fully answered and competitiveness evidenced. Already Bank of Uganda has licensed two new banks including Bank of India and NIC Bank of Kenya, which is a sign that investment in this sector has returns. "Some of the sections of our society do not want to accept that banks are business shops like any other commodity shop around them with a main motive to make profits. Bankers are merchants like those shopkeepers on any street or any other trader or dealers in the market." "Bankers are blatantly misunderstood", Said Tumusiime the Executive Director, Uganda Bankers' Association, as cited under the CEO Magazine (2012)

### **4.3 Access to Finance**

The financial sector in Uganda has experienced considerable growth and regulatory reforms in recent years (GIZ Development Workers, 2011). Despite these successes, access to finance in rural areas is limited with 62 percent of Ugandans (about 18.1 million people) have no access whatsoever to financial service (Fin scope Survey Report, 2007). The divide between urban and rural areas is significant, with 52 percent of the urban population and 65 percent of the rural population unnerved (Rural Speed

Report, 2007). Agricultural finance is still limited and does not reach the majority of the population (World Bank Report, 2009). Some of the larger farmers get some funding, but even they do not get long-term funding. Subsistence farmers, who are the majority, get very little short-term funding, mainly through microfinance institutions (MFIs). They either do not own property that can be used as collateral, or they find the credit options too limited for their needs (Odongo, 2012).

### **4.4 Soundness**

Soundness is a state or condition free from damage (Edward, 2007). Soundness concern issue in Uganda is still a challenge with banks like National Chamber of Commerce and Global Trust Bank being forced to close its doors by Bank of Uganda and with new Bank of India that opened its doors late year also facing liquidity problems (BOU Report, 2012). Structural, institutional, and macroeconomic aspects of financial system stability are receiving growing attention both nationally and in international forum. The magnitude and mobility of international capital flows have made it increasingly important to strengthen the foundations of domestic financial systems as a way to build up resilience to capital flow volatility. The soundness of financial institutions is also a key part of the infrastructure for strong macroeconomic performance and effective monetary policy at the national level. Hence, central banks and governments are paying increasing attention to monitoring the health and efficiency of financial institutions and markets, and to macroeconomic and institutional developments that pose potential risks to financial stability (Sundararaja et al, 2002).

### **4.5 Deposits Growth Vs Loan Sizes**

Deposits of the commercial banks grew in 2011, which was contrary to what initially was projected as the business community tried to keep businesses a float (BOU Report, 2012). The customer deposits grew but mostly at a slower pace compared to 2010 apart from Diamond Trust Bank and Global Trust Bank. It was at the tail end of 2011 that customer deposit drives by some commercial banks increased after studying the economic dynamics. The banks were enticing customers with prizes like cars and houses so as to encourage them to save. Notably, this contributed to the customer deposits growth of which not more than 70 percent is supposed to be lent out according to BOU regulations. Not all banks have had it their way in 2011, as some like National Bank of Commerce, Imperial Bank, Mercantile Credit Bank and Tropical Bank made losses partly due to currency and credit risk.

## 5. RESEARCH METHODOLOGY

### 5.1 Research Design and Approach

The study design used was of cross sectional and descriptive in nature, which employed a quantitative approach. The study selected respondents across different departments within banks and their customers with the purpose of gathering diverse information and analyze it for comparisons as noted by Sarantakos (1997). The target population for the study was 200 respondents, which comprised 110 employees or staff from key units of inquiry. Of these 65, were from Standard Chartered Bank, 45 from Stanbic Bank Uganda Ltd and the 90 of their clientele estimated broken down in table 1.

### 5.2 Sampling Size and Techniques

The sample size was based on Krejcie and Morgan's (1972) table for determining the sample size for any population of a definite size for any population of a defined (finite) size based on this confidence level. This sampling strategy was used because of the basic law of probability and assures the researcher of an utmost representation of the total population within an accepted margin of error. A sample size of 185 participates were presented with questionnaires from an intended population of 200 comprising; employees of the selected banking institutions and their customers in the above mentioned bank branches apportioned below in the table:

**Table 1: Target Population & Sample Sizes**

Units of Inquiry	Branch	Staff	Sample size	Customers	Sample size	Total Sample
Standard Chartered Bank	Nakaseero	45	40	35	32	72
	Masaka	20	19	15	14	33
Stanbic Bank Uganda Ltd	Charm Towers	30	28	30	28	56
	Masaka	15	14	10	10	24
<b>Total</b>		<b>110</b>	<b>101</b>	<b>90</b>	<b>84</b>	<b>185</b>

Source: Primary data (2013) from Standard Chartered Bank and Stanbic Bank Uganda Limited sampled using Krejcie and Morgans (1972) sampling criteria

### 5.3 Sample Techniques

Purposive, stratified and random sampling techniques were used. The senior managerial staffs were included on the basis of purposive sampling because they are every few. The stratified random samplings design was used for other banks' employees and random sampling of customers of the above banking institutions.

### 5.4 Data Measurement and Quality Control

Both macroeconomic policies and currency risks variables were measured using the 5 point Likert Scale

ranging from 1 (Strongly Disagree) on the left to 5 (Strongly Agree), as noted Rensis (1932). On the hand, Banks' competitiveness was measured using the 5 point Likert Scale, its ranges were from 1 (very low) on the left to 5 (very high), as stipulated by Parasuaraman (1985). The Cronbach Alpha Coefficient and the Content Validity Index were then used to assess the Reliability and Validity of the research instrument respectively. The values for these coefficients are as shown in the table below.

**Table 2: Reliability and Validity of the Research Instrument**

Variable	Anchor	Cronbach Alpha Coefficient	Content Validity Index
Macroeconomic Policies	18	0.766	0.800
Currency Risks	14	0.832	0.833
Banks' Competitiveness	19	0.792	0.692

Source: Extracts from SPSS

The results in table 2 above, show that the Cronbach Alpha Coefficient (test for reliability) and the Content Validity coefficients (test for validity) were above 0.700 indicating that the research instrument were both valid and reliable, which rendered the instrument appropriate for use.

### 5.5 Data Analysis and Presentation

Data from the field was compiled, sorted, edited and coded to have the required quality, accuracy and completeness. The data was then put into computer using the statistical package for social sciences (SPSS v 10.0) for analysis. The statistical package for social scientists was used because it helps the researcher to present data by generating tables' graphics and frequency tables. At bi-variate level; SPSS helped the researcher generate standard

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deviations and percentages to show the distribution of respondents on each independent and dependent variables.

Cross tabulation was used to establish the relationship between the study variables. The regression analysis was used to establish the combined effect of study variable (Banks' Competitiveness) on the independent variables.

## 6. RESEARCH FINDINGS

### 6.1 Factor Analysis of Macroeconomic Policies, Currency Risks & Banks' Competitiveness

#### 6.1.1 Macroeconomic Policies

This section presents results on the first independent variable (macroeconomic policies) of the study, which was dimensioned as monetary and fiscal policies, as indicated in table 3 below:

**Table 3:** Macroeconomic Policies Factor Loading Results

Macroeconomic Policies	Monetary policies	Fiscal policies
Monetary policies affect the whole country or region	.762	
Expansionary policy increases the total supply of money in an economy more rapidly than usual	.763	
Contractionary policy expands the supply of money slowly than usual influencing lending policies of financial institutions	.797	
Banks acknowledge a tough macro environment in the financial year 2011/2012	.713	
Banks used it to their advantage to post high profits last financial year	.660	
Growth in banks credit to private sector is partly blamed to have caused inflation in the financial year 2011/2012	.681	
BoU responded by revising the CBR to 16 percent in August up from 13 percent in April in 2011	.591	
Increase in CBR was intended to discourage public borrowing	.561	
Tight monetary policy aimed at mopping up runaway inflation	.621	
Despite CBR reduction to 11 percent in August 2012, banks have not reduced their interest rates to reflect the change	.597	
Fiscal policies focus on the economy as a whole		.560
Fiscal policy is used to change the pattern of spending on goods and services		.758
Changes in fiscal policy affect aggregate demand and supply		.660
Fiscal policy aims redistribution of income and wealth		.756
Government spends money on a variety of activities		.512
These expenditures can be funded in a number of different ways		.660
Economic growth received a backlash growth last financial year		.763
This negatively affected employment creation and poverty reduction		.681
Eigen Value	24.319	28.795
Variance %	52.407	44.841
Cumulative %	52.407	97.248

Source: Primary Data (2015)

From table 3 above, macroeconomic policies examined were monetary and fiscal policies. These two attributes explain a cumulative variance of 97.248% of the main variable. With the monetary policies which was the most important as observed above with their corresponding percentage scores, comprised 52.407% variance of the main variable and on the aspect of fiscal policies which explained 44.841% variance.

#### 6.1.2 Currency Risks

This Section presents results of the second independent variable (currency risks) of the study, which was dimensioned as nonperforming loans, creditworthiness parameters, exchange rate volatility, deteriorating loan portfolio, and lastly, value at risk, as indicated in table 4 below:

<http://www.ejournalofbusiness.org>**Table 4: Currency Risks Factor Analysis Results**

<b>Factor Analysis Results: Currency Risks</b>	<b>Nonperforming loans (NPLs)</b>	<b>Creditworthiness Parameters</b>	<b>Exchange rate volatility</b>	<b>Deteriorating loan portfolio</b>	<b>Value at risk (VaR)</b>
When financial institutions compete with each other for customers, loan default increases	.686				
Credit risk is proxy by the ratio of NPLs to the total loans advanced	.560				
Assesses creditworthiness and assign ratings with respect to various parameters		.506			
These parameters are used to assess defaulting on debtors' obligations		.668			
Exchange rate volatility exposes one to loss of value of one currency in terms of another			.637		
Exchange rate volatility affects the prices of imported and exported commodities either directly or indirectly			.570		
Exchange rate risk is increases the rate of default			.714		
Inevitable risks in shifting funds across international markets			.812		
My institution is affected by exchange rate volatilities			.821		
My institution undertakes foreign exchange risk mitigation			.678		
Loan portfolio is a major asset of financial institution				.536	
It value is dependent upon interest rates and quality				.667	
Statistical technique used to measure and qualify the level of financial risk over a specified time					.677
Value at risk is also used in non-financial applications					.611
Eigen Value	4.612	1.694	1.849	1.217	2.113
Variance %	12.327	11.294	30.746	8.111	9.232
Cumulative %	12.327	23.621	54.367	62.478	71.171

Source: Primary Data (2015)

The results from table 4, currency risks variable was noted to be mainly composed of; nonperforming loans, creditworthiness parameters, exchange rates volatility, deteriorating loan portfolio and value at risk. These five attributes explain cumulative variance of 71.171% of the main variable. With the exchange rates volatility which was the most important as observed above with corresponding percentage scores' of 30.746% variance of the main variable; on the aspect of nonperforming loans 12.327%,

creditworthiness parameters 11.294%, deteriorating loan portfolio 8.111% and value at risk 9.232%

## 6.2 Banks' Competitiveness

This section presents the dependent variables (Banks' Competitiveness) of the study, which was dimensioned as profitability vs. growth, deposit vs. loan size, organizational soundness and access to finance, as indicated in table 5 below:



<http://www.ejournalofbusiness.org>**Table 5: Banks' Competitiveness Factor Analysis Results**

<b>Factor Analysis Results: Banks' Competitiveness</b>	<b>Profitability Vs Growth</b>	<b>Deposits Vs Loan size</b>	<b>Soundness</b>	<b>Access to Finances</b>
Banks defined the odds posting huge profits and revenue growth in a gloomy economy Profitability and revenue growth is not new to banks	.754 .762			
With new banks like NIC and Bank of India opened doors last year	.599			
Despite this impressive performance, our customers are not happy Banks questioned of their fairness to make huge profits	.745			
Banks profited high, at the expense of struggling customers Banks charge high interest rates on both old and new loans Banks justified their charging high interest rates due to high inflation in the economy Not all banks made profits; some made losses partly due to currency and credit risks	.880 .678 .845 .610 .712			
Despite a distress economy last financial year, banks' deposits grew Banks entice their customers with prizes to attract new customers' deposits and borrowings Not all banks' deposits grew last financial year Tough times ahead, a reduction in deposits forecasted in financial year 2012/2013 Banks' deposits grew at a slower pace compared to financial year 2010/2011		.609 .613 .712 .576 .598		
Banks' soundness is still a challenge in the country			.735	
Banks are proud of customers' successes, despite the high costs of doing business Banking institutions have failed to provide adequate banking services to the bulk of Ugandans With the majority of Ugandans, depend on savings from their little incomes Others rely on incomes from friends, relatives, remittances and informal money lenders				.640 .517 .561 .612
Eigen Value	4.559	1.421	1.284	1.092
Variance %	35.073	10.934	9.874	8.398
Cumulative %	35.073	46.007	55.881	64.279

Source: Primary Data

From table 5 above, results show that, Banks' Competitiveness is mainly composed of profitability vs. growth, deposits vs. loan size, soundness and access to finances, which is explained by a cumulative variance of 64.279%. Profitability vs. growth as a dimension of Banks' competitiveness presented the highest scores of corresponding percentages with a variance of 35.073%, followed by deposits vs. loan size with a variance of 10.934%, then soundness with a variance of 9.874%, and lastly, access to finances with a variance of 8.398%. The lowest cumulative variance for all the four dimension was

35.073%, which implied a moderate level of Bank competitiveness.

### 6.3 Correlation Results for Macroeconomic Policies, Currency Risks and Banks' Competitiveness

The section presents correlational results on the variables of the study (macroeconomic policies, currency risks and banks competitiveness). The Pearson (r) correlation coefficient was used and this was ranging between -1.00 and 1.00, as indicated in table 6 below:

<http://www.ejournalofbusiness.org>**Table 6: Relationship between the Study Variables**

	Macroeconomic Policies	Currency Risks	Banks' Competitiveness
Macroeconomic Policies	1.000		
Currency Risks	.491**	1.000	
Banks' Competitiveness	.491**	.308**	1.000

Source: Primary Data (2015)

### 6.3.1 Relationship between Macroeconomic Policies and Banks' Competitiveness

From table 6 above, there is a moderate positive relationships between Macroeconomic Policies and Banks' Competitiveness ( $r = .491^{**}$ ,  $p < .01$ ), which results into the rejection of the null hypothesis, which stated that, there is no significant relationship between macroeconomic policies and Bank Competitiveness.

### 6.3.2 Relationship between Currency Risks and Banks' Competitiveness

The results in table 6 further revealed a moderate and significant relationships between currency risks and

Banks competitiveness ( $r = .301^{**}$ ,  $p < .01$ ). This also resulted into the rejection of the null hypothesis, which stated that, there is no significant relationship between currency risks and Banks competitiveness

### 6.4 Regression Analysis for Macroeconomic Policies, Currency Risks and Banks' Competitiveness

The section presents the regression analysis of the study showing the degree at which macroeconomic policies and currency risks predict Banks' competitiveness.

**Table 7: Prediction of Banks' Competitiveness**

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	1.693	.369		4.588	.000
Macroeconomic Policies	.289	.097	.345	2.968	.004
Currency Risks	.100	.088	.134	1.139	.259
<b>Dependent Variable: Banks' Competitiveness</b>					
R Square	.306				
Adjusted R Square	.277				
Std. Error of the Estimate	.613				
F Statistic	10.433				
Sig.	.001				

Source: Primary Data (2015)

The results in the table 7 above showed that the predictors can account for 27.7% of the variance in Banks' Competitiveness (Adjusted R Square = .277). The results showed that Macroeconomic Policies (Beta = .345, sig. < .004), is the most influential at explaining Banks' Competitiveness. In other words, banks in Uganda should priorities the issues related to Macroeconomic Policies if Banks' Competitiveness is to be greatly improved. These issues can range from strategy mitigates, and monitoring government and business environment responses to changes in monetary and fiscal policies.

## 7. DISCUSSIONS

### 7.1 Relationship between Macroeconomic Policies and Banks' Competitiveness

Results showed that there is a moderate positive relationships between Macroeconomic Policies and Banks' Competitiveness ( $r = .491^{**}$ ,  $p < .01$ ) and this relationship is statistically significant. These results show that if banks design realistic Macroeconomic Policies strategies

mitigates, and proactively monitor them in the course of government changes in monetary and fiscal policies, banks are most likely to improve on their competitiveness and this will be noted in terms of increased customer deposits, profitability, growth, and soundness of their organizations.

The above findings are consistence with the work of Beck et al (2009) whose work reveals that while in recent years, the financial sector debate across the African continent has been dominated by policies to increase access to financial services; maximizing competitiveness currently tops the agenda. Financial systems across Africa have seen a deepening and broadening over the past years, partly benefiting from the Great Moderation and global liquidity glut, but also from improvements in macroeconomic policies and progress in institutional reforms. In the financial year 2011/2012, banking sector remained resilient taking advantage of stringent macroeconomic policies imposed by Bank of Uganda to post good growth figures," said, Odera the Managing Director, Stanbic Bank as cited in the CEO Magazine (2012). With another two new foreign banks; Bank of India and NIC Bank of Kenya opening

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shops, we can now conclude that the question about what these financial institutions see in Uganda has been fully answered and competitiveness evidenced (BOU Report, 2012).

### 7.1.1 Relationship between Currency Risks and Banks' Competitiveness

The results further revealed moderate positive relationships between Currency Risks, Lending Policies and Banks' Competitiveness ( $r = .366^{**}$ ,  $p < .01$  &  $r = .384^{**}$ ,  $p < .01$ ) and relationship is statistically significant. These results show that when banks efficiently monitor and follow best currency risks mitigates in terms of; credit worthiness parameters, exchange rate volatility and manage risks related to nonperforming loans (NPLs) of their customers, banks shall be in position to design and improve on their lending policies of their customers. This in turn will improve on banks' competitiveness in the country through; increased profitability, growth and soundness of the organizations.

Friedman (2001) noted that governments' operating of monetary policies like; the contractionary monetary policy to curtail inflation expands the money supply more slowly than usual or even shrinks it influencing the lending policy of financial institutions, cost of credit and investment in the country. Financial institutions need to watch more closely the changes and effects of macroeconomic policies. This was the Ugandan case, inflation at 31 percent in October 2011. The central bank increased central bank rate (CBR) 18 per cent to curtail inflation. This increased the Inter Bank Rate and thus reflected by high costs to borrow for banks and borrowing customers. The motive of the central bank was to discourage borrowing from the public (Yotopoulos and Floro, 1992).

## 8. CONCLUSION AND RECOMMENDATION

### 8.1 Conclusion

In the light of the fore stated findings and the discussion of the results; it was concluded that macroeconomic policies of fiscal and monetary policies, and their effects on the are essential for the banks to monitor and understand in order to stay competitive and improve on their operating policies in the country. Currency Risks aspects of; value at risk, non-performing loans, exchange rates volatilities if not well managed and monitored by banks, have significant effects on banks' lending policies and their competitiveness. For each of the variables indicated in the factor analysis, the most important attribute is the one with the greatest variance percentage and these are the main attributes that should be considered in case the variables are to be improved upon by banks to increase on their competitiveness. After the most dominant attributes are dealt with, then banks should work on the

second most important attributes in the order they are indicated. When this is done, ensures that there are positive relationships between the variables.

### 8.2 Recommendation

Owing to the conclusions and the findings in the previous sections, the researcher saw it fit to suggest these recommendations which should be implemented so as to ensure better banks' competitiveness.

#### 8.2.1 Relationship between Macroeconomic Policies and Banks' Competitiveness

Results showed that there is a moderate positive relationship between Macroeconomic Policies and Banks' Competitiveness ( $r = .491^{**}$ ,  $p < .01$ ) and this relationship is statistically significant.

- Banks need to proactively forecast and monitor government changes in monetary and fiscal policies and charge costs relatively to the loan facilities available to their customers. Banks should always have their customers at heart in all their dealings and not to increase interest rates on old loans in case of macroeconomic policy changes.
- Although banks are like any other business shops with a motive of making profits, they should be considerate not to rip off their customers trying to keep their businesses a float in case of future tough macroeconomic environment.
- Banks need to sensitize their customers that although there is a reduction of inflation at 5.4 percent as of May 2013 and CBR at 10%, this does not necessarily mean automatic reduction of cost of finance.
- There is need for banks to increase financing access to potential customers in rural sparsely populated areas. Although operational costs are still high in such areas, banks need to devise low cost strategies so as to increase on their competitiveness.

#### 8.2.2 Relationship between Currency Risks and Banks' Competitiveness

The results further revealed moderate positive relationships between Currency Risks, Lending Policies and Banks' Competitiveness ( $r = .366^{**}$ ,  $p < .01$  &  $r = .384^{**}$ ,  $p < .01$ ) and relationship is statistically significant.

- Although health competition for customers by banks is good, if poorly mishandled increases customers' default and affects banks' competitiveness; thus it needs attention.
- Although there has a reduction of defaulting customers, banks should maintain a well functioning risk management policy as this reduces future loss of value of assets, dividends and

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interest rates payment streams of portfolios especially dominated in foreign currency.

- Just like today's ever changing business environment, there is no business entity that is not affected by exchange rates volatilities. Banks need to proactively hedge against such risks in order to stay competitive.
- Banks' soundness threat need not to be undermined as it's still a challenge in the country with some institutions facing liquidity problems.

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