Non Performing loans in Commercial Banks: A case of CBZ Bank Limited In Zimbabwe

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Abstract
The purpose of the study was to find out the causes of non-performing loans in Zimbabwe. Loans form a greater portion of the total assets in banks. These assets generate huge interest income for banks which to a large extent determines the financial performance of banks. However, some of these loans usually fall into non-performing status and adversely affect the performance of banks. In view of the critical role banks play in an economy, it is essential to identify problems that affect the performance of these institutions. This is because non-performing loans can affect the ability of banks to play their role in the development of the economy. A case study research design of CBZ Bank Limited was employed. Interviews and questionnaires were used to collect data for the study. The paper revealed that external factors are more prevalent in causing non performing loans in CBZ Bank Limited. The major factors causing non performing loans were natural disasters, government policy and the integrity of the borrower.

Key words: Non Performing Loans, CBZ Bank limited, External factors, Internal factors

1.0 Introduction
A financial intermediary is an institution that acts as an intermediary by matching supply and demand of funds (Beck, 2001). Heffernan (1996) defines banks as intermediaries between depositors and borrowers in an economy which are distinguished from other types of financial firms by offering deposit and loan products. Bossone (2001) agrees arguing that banks are special intermediaries because of their unique capacity to finance production by lending their own debt to agents willing to accept it and to use it as money.
Commercial banks are the dominant financial institutions in most economies (Rose, 1997). Greuning and Bratanovic (2003), argue that commercial banks play a critical role to emerging economies where most borrowers have no access to capital markets. Well functioning commercial banks accelerate economic growth, while poorly functioning commercial banks are an impediment to economic progress and aggravate poverty (Barth et al., 2001; Khan and Senhadji, 2001) in Richard (2011).

The traditional role of a bank is lending and loans make up the bulk of their assets (Njanike, 2009). According to the research by Havrilesky and Boorman (1994), interest on loans contributes significantly to interest income of commercial banks. Reed and Gill (1989) pointed out that traditionally 85 percent of commercial banks’ income is contributed by interest on loans. Loans therefore represent the majority of a bank’s assets (Saunders and Cornett, 2005). Lending is not an easy task for banks because it creates a big problem which is called non performing loans (Chhimpa J, 2002) as cited in (Upal, 2009). Due to the nature of their business, commercial banks expose themselves to the risks of default from borrowers (Waweru and Kalami, 2009).

According to Alton and Hazen (2001) non performing loans are those loans which are ninety days or more past due or no longer accruing interest. Hennie (2003) agrees arguing that non performing loans are those loans which are not generating income. This is further supported by Caprio and Klingebiel (1996), cited in Fofack (2005), who define non performing loans as those loans which for a relatively long period of time do not generate income that is, the principal and or interest on these loans have been left unpaid for at least ninety days. Non-performing loans are also commonly described as loans in arrears for at least ninety days (Guy, 2011). Therefore in this study, non performing loans are loans that are ninety or more days delinquent in payments of interest and/or principal (Bexley and Nenninger, 2012).

The term “bad loans” as described by Basu (1998) in Fofack (2005) is used interchangeably with non-performing and impaired loans. Berger and De Young, (1997) also consider these types of loans as “problem loans”. In effect, these would be considered bad or toxic assets on the bank’s books (Bexley and Nenninger, 2012). These descriptions were used interchangeably during the study. According to Berger and De Young (1997), non performing loans could be injurious to the financial performance of banking institutions.

According to Kroszner (2002) in Waweru and Kalami (2009), non-performing loans are closely associated with banking crises. Greenidge and Grosvenor (2010), argue that the magnitude of non-performing loans is a key element in the initiation and progression of financial and banking crises. Guy (2011) agrees arguing that non performing loans have been widely used as a measure of asset quality among lending institutions and are often associated with failures and financial crises in both the developed and developing world. Reinhart and Rogoff (2010) as cited in Louzis et al (2011) point out that non-performing loans can be used to mark the onset of a banking crisis. Despite ongoing efforts to control bank lending activities, non performing loans are still a major concern for both international and local regulators (Boudriga et al, 2009)
1.1 Background of study

Over the years, there have been an increased number of significant bank problems in both, matured as well as emerging economies (Brownbridge and Harvey, 1998; Basel, 1999, 2004) cited in Richard (2011). Bank problems, mostly failures and financial distress have afflicted numerous banks, many of which have been closed down by regulatory authorities (Brownbridge, 1998). This in turn led to contraction of activities, decline in output, and imposition of substantial costs on the economy (Chijoriga, 1997; Brownbridge and Harvey, 1998) cited in Richard (2011). Borio and Lowe (2002) observed that the cost of banking crises in terms of output loss has been high; typically double digit percentage of GDP.

Studies in other countries show that most of bank failures have been caused by non performing loans (Brownbridge, 1998). Ahmad (2002), in analyzing the Malaysian financial system, reported a significant relationship between credit risk and financial crises and concluded that credit risk had already started to build up before the onset of the 1997 Asian financial crisis, and became more serious as non performing loans increased. Li (2003) and Fofack (2005) also found this relationship to be significant. There is evidence that the level of non-performing loans in the US started to increase substantially in early 2006 in all sectors before the collapse of the sub-prime mortgage market in August 2007 (Greenidge and Grosvenor, 2010).

Nishimura et al (2001) studied the situation in Japan and concluded that some of the loans made to companies during the bubble era became non-performing when the bubble burst. The findings of Caprio and Klingebiel (2002) cited in Fofack (2005), show that in Indonesia, non-performing loans represented about 75% of total loan assets which led to the collapse of over sixty banks in 1997. While some countries such as Sweden, Norway, Finland, Australia and Spain do not seem to be exposed to non performing loans (less than 1 percent) other countries such as Egypt, Nigeria, Philippines, Morocco, Algeria and Tunisia (more than 15 percent) suffer severely from bad loans (Boudriga et al, 2009).

The problem of non-performing loans is common in Zimbabwe where some banks have been liquidated in 2004 and 2005 (Monetary Policy Statement, 2006). Commercial banks that were closed during this period include Barbican Bank Limited, CFX Bank Limited, Royal Bank Limited, Time Bank of Zimbabwe Limited and Trust Bank Limited. The Monetary Policy Statement indicated that the demise of these institutions was significantly attributed to non-performing loans (Monetary Policy Statement (MPS), 2006).

In January 2012, the Governor of the Reserve Bank of Zimbabwe, Dr Gideon Gono noted with concern the gradual deterioration in asset quality as reflected by the level of non-performing loans (MPS, 2012). He highlighted that asset quality challenges can potentially heighten liquidity risks given the current operating environment where credit is largely financed by volatile short term deposits. In this regard, he urged banking institutions to enhance their credit risk management systems with special emphasis on credit assessment, origination, administration, monitoring and control standards. Fofack (2005) argues that when left unsolved, nonperforming loans can compound into financial crisis, the moment these loans exceed bank capital in a relatively large number of banks.
Recently, Interfin Bank Limited was placed under recuperative curatorship on 11 June 2012 (Mid-Term MPS, 2012). The Governor of RBZ issued a press statement advising of the closure of Royal Bank Limited after the directors of the bank resolved to surrender their license on 27 July 2012 (RBZ Press Statement, 2012). Non-performing loans were cited as the major common problem that was faced by Interfin Bank Limited. This is the second time within a period of eight years that Royal Bank Limited has failed (Mid-Term MPS, 2012 and RBZ Press Statement, 2012). Apparently in both cases the issue of non-performing loans was mentioned. Demirguc-Kunt et al (1989), cited in Berger and De Young (1997), indicate that failing banks have huge proportions of bad loans prior to failure and that asset quality is a statistically significant predictor of insolvency.

According to the International Monetary Fund (IMF, 2012), the following are recent bank failures in Zimbabwe:

1. **Renaissance Merchant Bank**
   In June 2011, Renaissance Merchant Bank was placed under 6-month curatorship after the RBZ’s audit revealed an inappropriate shareholding structure, chronic undercapitalization and liquidity challenges, high level of nonperforming insider and related party exposures, persistent losses, and corporate governance and internal control deficiencies. The curatorship was lifted in March 2012, following a cash injection by the National Social Security Authority, which acquired 84 percent share in the holding company and installed new management.

2. **Interfin Bank Limited**
   Interfin Bank Limited was placed under recuperative curatorship on June 11, 2012, after a RBZ audit determined that it was operating in an unsound and unsafe manner involving: inadequate capitalization; concentrated shareholding; abuse of corporate structures; high level of nonperforming insider and related party loan exposures; chronic liquidity; income generating challenges; weak governance and management oversight, and violation of banking laws and regulations.

3. **Genesis Investment Bank**
   Genesis Investment Bank voluntarily surrendered its banking license to the RBZ in June 2012, after failing to realize adequate financing from partners that the bank had been courting since 2009. The RBZ has commenced the modalities on liquidating the bank.

4. **Royal Bank Zimbabwe Limited**
   On July 27, 2012, Royal Bank Zimbabwe Limited surrendered its banking license to the RBZ. Onsite inspection by the RBZ determined that the bank was critically undercapitalized, faced chronic liquidity challenges and liabilities to the RTGS system, had high non-performing insider loans, and had been misrepresenting information to the RBZ.

In Zimbabwe, the loan-to-deposit ratio, calculated on the basis of total bank deposits increased from 84.6 percent in May 2012 to 86.2 percent in June 2012 (RBZ, 2012). According to the Mid-Year Fiscal Policy Statement presented...
on the 18th of July, non-performing loans were 9.9 percent as at 30 June 2012 as shown in Figure 1 below. IMF (2012) also indicates that non performing loans in Zimbabwe increased from 6 percent on average at end-December 2011 to 10 percent at end-June 2012. This is higher than the prudential threshold of 5 percent stipulated in Basel II (Basel, 2004; ADF, 2012). Non-performing loans could rise further with the ongoing deceleration in economic activity (IMF, 2012).

**Figure 1 Non-Performing Loans: 2009–2012**

![Non-Performing Loans: 2009–2012](image)

**Source:** Mid-Year Fiscal Policy Statement (2012)

The diagram above shows an upward trend in non-performing loans in Zimbabwe from March 2009 to June 2012. Moreover, the RBZ has uncovered misrepresentation in some banks’ reporting, giving rise to concerns that non performing loans may be underestimated (IMF, 2012).

In Africa, Brownbridge, (1998) in Richard (2011) concludes that many of the bad debts in banks were attributable to moral hazards; the adverse incentives on bank owners to adopt imprudent lending strategies, in particular insider lending at high interest rates to borrowers in the most risky segments of the credit market. To the borrowers’ side, they also tend to divert the funds to risky investments once they are granted the loans.

Palubinskas and Stough (1999) note that the failure of a bank is mainly seen as a result of mismanagement because of bad lending decisions made with respect to wrong appraisal of credit status, or the repayment of non-performing credits and excessive focus on giving loans to certain customers. Goodhart et al (1998) also state that poor credit control, which results in undue credit risk, causes bank failure. Chimerine (1998) adds that a bad lending tradition leads to a large portfolio of unpaid loans. This results in insolvency of banks and reduces funds available for fresh advances, which eventually causes a financial crisis. Goodhart et al. (1998) add connected lending to the causes of bank failure. Palubinskas and Stough (1999) note that lack of dependable financial information on borrowers to help in assessing creditworthiness causes a bank failure.
National economic downturn, insider lending, political connection of bank owners, customer failure to disclose vital information during the loan application process, lack of proper skills amongst loan officials were among major factors identified in other countries to cause non performing loans (Santomero, 1997; Brownbridge and Harvey, 1998; Basel, 1999; Waweru and Kalani, 2009). Controlling non performing loans is very important for both the performance of an individual bank and the economy’s financial environment (McNulty et.al, 2001). It is thus the essence of this study to establish factors behind non performing loans in Zimbabwe and strategies at place to cater for the same.

1.2 Problem Statement
According to the Mid-Year Fiscal Policy Statement (2012) the upward trend in non-performing loans and recent bank failures in Zimbabwe is a cause for concern. Despite lessons obtained from the 2004 financial crisis in Zimbabwe, banks are still suffering from non performing loans.

1.3 Objectives of Study
The general/overall objective of the study was to find out the causes of non-performing loans in Zimbabwean commercial banks. The specific objectives of the study were: to find out the trend of non-performing loans in commercial banks since the adoption of the multicurrency regime, to identify the causes of non-performing loans, to determine the business sector that records higher non performing loans, and to determine key areas of the bank’s performance that has been affected by non-performing loans.

1.4 Scope of the Study
The study focused on the case of CBZ Bank Limited; one of Zimbabwe’s largest and oldest banks. This is premised on the fact that the Bank has been operating long enough to give the kind of academic insight the study seeks to offer. Besides, the bank lends to almost all the major sectors of the economy. Again, the nation-wide operation of the bank presents an opportunity for a national outlook of the issues under the study.

2.0 Literature Review
The theory of asymmetric information tells us that it may be difficult to distinguish good from bad borrowers (Auronen, 2003) in Richard (2011), which may result into adverse selection and moral hazards problems. The theory explains that in the market, the party that possesses more information on a specific item to be transacted (in this case the borrower) is in a position to negotiate optimal terms for the transaction than the other party (in this case, the lender) (Auronen, 2003) in Richard (2011). The party that knows less about the same specific item to be transacted is therefore in a position of making either right or wrong decision concerning the transaction. Adverse selection and moral hazards have led to significant accumulation of non performing loans in banks (Bester, 1994; Bofondi and Gobbi, 2003).

In scholar studies, problem loans are often used as an exogenous variable to explain other banking outcomes such as bank performance, failures, and bank crises (Boudriga et al., 2009). However, some studies investigate problem loans as an endogenous variable (Sinkey and Greenwalt, 1991; Kwan and Eisenbeis, 1997; Salas and Saurina, 2002) in (Boudriga et al., 2009). GDP growth, inflation and interest rates are common macro-economic factors, while size and lending policy are micro-economic variables (Greenidge and Grosvenor, 2010). These variables are by no means exhaustive, but they provide a useful framework for monitoring the development of non-performing loans.
More recent researches started studying this problem but with particular reference to both developing countries and emergent economies (Haunerand and Peiris, 2005; Matthewes et al., 2007), as cited by (Maggi and Guida, 2009).

Bercoff et al (2002) examine the fragility of the Argentinean Banking system over the 1993-1996 period; they argue that non performing loans are affected by both bank specific factors and macroeconomic factors. To separate the impact of bank specific and macroeconomic factors, the authors employ survival analysis. Using a dynamic model and a panel dataset covering the period 1985-1997 to investigate the determinants of problem loans of Spanish commercial and saving banks, Salas and Saurina (2002) reveal that real growth in GDP, rapid credit expansion, bank size, capital ratio and market power explain variation in non-performing loans.

Furthermore, Jimenez and Saurina (2005) examine the Spanish banking sector from 1984 to 2003; they provide evidence that non performing loans are determined by GDP growth, high real interest rates and lenient credit terms. This study attributes the latter to disaster myopia, herd behaviour and agency problems that may entice bank managers to lend excessively during boom periods. Meanwhile, Rajan and Dhal (2003) utilise panel regression analysis to report that favourable macroeconomic conditions and financial factors such as maturity, cost and terms of credit, banks size, and credit orientation impact significantly on the non performing loans of commercial banks in India.

Babihuga (2007), in an IMF working paper, explores the relationship between several macroeconomic variables and financial soundness indicators (capital adequacy, profitability, and asset quality) based on country aggregate data. She explained the cross-country heterogeneity by differences in interest rates, inflation, and other macroeconomic factors. However, the study does not consider the impact of industry specific drivers of problem loans.

Most empirical studies examine the influence of the macroeconomic environment on non performing loans (Louzis et al, 2011). Rinaldi and Sanchis-Arellano (2006) analyze household non performing loans for a panel of European countries and provide empirical evidence that disposable income, unemployment and monetary conditions have a strong impact on non performing loans. Berge and Boye (2007) find that problem loans are highly sensitive to the real interest rates and unemployment for the Nordic banking system over the period 1993–2005.

Lawrence (1995) examines the theoretical literature of life-cycle consumption model and introduces explicitly the probability of default. This model implies that borrowers with low incomes have higher rates of default due to increased risk of facing unemployment and being unable to settle their obligation. Additionally, in equilibrium, banks charge higher interest rates to riskier clients. Rinaldi and Sanchis-Arellano (2006) extend Lawrence’s model by assuming that agents borrow in order to invest in real or financial assets. They argue that the probability of default depends on current income and the unemployment rate, which is linked to the uncertainty regarding future income and the lending rates.
Breuer (2006), using Bankscope data, analyses the impact of legal, political, sociological, economic, and banking institutions on problem bank loans. Nevertheless, her study suffers from a representativeness bias due to the fact that Bankscope data on non performing loans are only available for a very limited number of countries and for a few numbers of banks. Other studies focusing on the macroeconomic determinants of non-performing loans include Cifter et al. (2009), Nkusu (2011) and Segoviano et al. (2006).

Carey (1998) argues that “the state of the economy is the single most important systematic factor influencing diversified debt portfolio loss rates” (Carey, 1998, p. 1382). Quagliarello (2007) finds that the business cycle affects non performing loans for a large panel of Italian banks over the period 1985–2002. Furthermore, Cifter et al. (2009) provides empirical evidence for a lagged impact of industrial production on the number of non performing loans in the Turkish financial system over the period 2001–2007. Salas and Saurina (2002) estimate a significant negative contemporaneous effect of GDP growth on non performing loans and infer the quick transmission of macroeconomic developments to the ability of economic agents to service their loans (Bangia et al., 2002; Carey, 2002). Nkusu (2011) investigating the macroeconomic determinants of loan defaults through panel regressions and panel vector autoregressive models. The author suggests that hike in interest rates result in deterioration of borrower’s repayment capacity and hence, cause of increase in non-performing loans.

There is significant empirical evidence to suggest that local economic conditions explain to some extent, the variation in non-performing loans experienced by banks (Keeton and Morris, 1987; Sinkey and Greenwalt, 1991; Salas and Saurina, 2002; Rajan and Dhal, 2003) as cited in (Greenidge and Grosvenor, 2010) Research conducted in the Caribbean includes that of Khemraj and Pasha (2009), who examined the determinants of non-performing loans in Guyana. The empirical results revealed that with the exception of the inflation rate and bank size, all other factors have a significant relationship with the non performing loan ratio (Greenidge and Grosvenor, 2010).

Causes and treatment of non-performing loans were studied in detail by Bloem and Gorter (2001). They agreed that “bad loans” may considerably rise due to abrupt changes in interest rates. They discussed various international standards and practices on recognizing, valuing and subsequent treatment of non-performing loans to address the issue from view point of controlling, management and reduction measures. A study conducted by Espinoza and Prasad (2010) focused on macroeconomic and bank specific factors influencing non-performing loans and their effects in GCC Banking System. After a comprehensive analysis, they found that higher interest rates increase non performing loans but the relationship was not statistically significant.

Salas and Saurina (2002) find a negative relation between bank size and non performing loans and argue that bigger size allows for more diversification opportunities. Hu et al. (2004) and Rajan and Dhal (2003) report similar empirical evidence. Another strand of literature has focused on the degree of loan concentration in various sectors, and proposes that vulnerabilities within sectors of high loan concentration tend to exacerbate the non performing ratio (Herring and Wachter, 1999) as cited in (Guy, 2011). However, Stiroh (2004) does not find evidence of
benefits from diversification in the form of reduced risk, for the US banking system, since non-interest income growth was highly correlated with net interest income during the 1990s.

The moral hazard of too-big-to-fail banks represents another channel relating bank-specific features with non-performing loans (Louzis et al, 2011). A policy concern is that too-big-to-fail banks may resort to excessive risk taking since market discipline is not imposed by its creditors who expect government protection in case of a bank’s failure (Stern and Feldman, 2004). Consequently, large banks may increase their leverage too much and extend loans to lower quality borrowers (Louzis et al, 2011). Boyd and Gertler (1994) argue that in the 1980s the tendency of US large banks towards riskier portfolios was encouraged by the US government’s too-big-to-fail policy. On the other hand, Ennis and Malek (2005) examine US banks’ performance across size classes over the period 1983–2003 and conclude that the evidence for the too-big-to-fail distortions is in no way definite. Hu et al (2006) also show that bank size is negatively related to non-performing loans.

In a seminal study, Berle and Means (1933) in Louzis et al. (2011) argue that dispersed ownership of corporate equity may lead to a poorer performance of the firm as the incentive of shareholders to monitor the management weakens. An opposing view is that an efficient capital market imposes discipline on firm’s management and therefore dispersed ownership should not have an effect on firm’s performance (Fama, 1980) as cited in (Louzis et al., 2011). A strand in the empirical literature tests these contrasting views using loan quality as an indicator of riskiness but evidence is inconclusive (Louzis et al, 2011). Iannotta et al. (2007) find a link between higher ownership concentration and loan quality using a sample of 181 large banks over the period 1999–2004, thus lending support to the Berle and Means view.

On the other hand, Laeven and Levine (2009) employ data on 279 banks and find a positive association between greater cash flow rights of a large owner and risk taking. Furthermore, Shehzad et al. (2010) present empirical evidence, from a data set comprising 500 banks from 2005 to 2007, that ownership proxied by three levels of shareholding (10%, 20% and 50%) has a positive impact on the non performing loans ratio when the level of ownership concentration is defined at 10% but a negative impact when the level of level of ownership concentration is defined at 50%. Therefore they suggest that sharing of control may have adverse effects on the quality of loans extended up to a level, but in cases of a strong controlling owner, bank’s management becomes more efficient leading to lower non-performing loans. Azofra and Santamaria (2011) find that high levels of ownership concentration benefit both the bank’s profitability and efficiency for a sample of Spanish commercial banks.

Empirically, Novaes and Werlang (1995) report lower performance for state controlled banks in Brazil and Argentina due to high proportion of problem loans given to government. Micco et al. (2004), analyze 50,000 financial institutions with different ownership types covering 119 countries. They conclude that non-performing loans tend to be higher for banks with state ownership than for other groups. Hu et al. (2004) use a panel of Taiwanese banks and find a positive correlation between capital share owned by the state and the level of non-performing loans. Garcia-Marcos and Robles-Fernandez (2007) investigate the relationship between risk taking and
Ownership structure. They document that commercial banks (mainly private owned) are more exposed to risk than deposit banks (mainly state owned). More recently Hu et al (2006) analysed the relationship between non-performing loans and ownership structure of commercial banks in Taiwan with a panel dataset covering the period 1996-1999. The study shows that banks with higher government ownership recorded lower non-performing loans.

Using a pseudo panel-based model for several Sub-Saharan African countries, Fofack (2005) finds evidence that economic growth, real exchange rate appreciation, the real interest rate, net interest margins, and inter-bank loans are significant determinants of non-performing loans in these countries. The author attributes the strong association between the macroeconomic factors and non-performing loans to the undiversified nature of some African economies.

3.0 Research Methodology

The case study design was employed in this study. The study was based on CBZ Bank Limited which is the largest commercial bank in Zimbabwe. The sample was constructed at two levels; the first level of sampling being choice of sample bank and the second level of sampling was the choice of respondents. At the second level of sampling choice of respondents, letters were sent to 30 staff members involved in credit management intended to participate in the study and focused on employees that have been involved in corporate lending activities for at least five years. In addition, seven senior managers involved in lending activities will be interviewed.

The primary data for this research was collected using a questionnaire and interviews of senior managers involved in lending activities. Structured questionnaires were administered. An additional method of data collection was personal interviews with executives and senior management in CBZ Bank Limited. Secondary data was obtained from the company’s published audited financial statements to find out how non-performing loans have affected the bank in terms of liquidity and profitability. Data collected from questionnaires was analyzed using the Microsoft Excel and the Statistical Package for Social Sciences (SPSS).

4.0 Results

4.1 Questionnaire response rate and interview success rate

Out of the thirty questionnaires sent to the target population, twenty-eight usable responses were collected. This represented a response rate of 93.3 percent and implies that 6.7 percent of the questionnaires were not returned at all. Of the seven projected interviews, only four were successfully contacted, giving a success rate 57.1 percent. Three interviews were unsuccessful primarily because the targeted interviewees were time constrained. Despite this, the target population was fairly represented considering that key senior managers who are relevant to the study were interviewed. The results are shown in table 4.1 below.
Table 4.1: Questionnaire and interview success rate

<table>
<thead>
<tr>
<th>Target respondents</th>
<th>Successful</th>
<th>Success rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Questionnaires</td>
<td>30</td>
<td>28</td>
</tr>
<tr>
<td>Interviews</td>
<td>7</td>
<td>4</td>
</tr>
</tbody>
</table>

Source: Own computation from primary data

The statistics in Table 4.1 above gives a fair representation of the target population and hence the validity of data.

4.2 Profile of respondents

Table 4.2.1: Working position of questionnaire respondents

<table>
<thead>
<tr>
<th>Current Role</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit Analyst</td>
<td>10</td>
<td>35.7</td>
</tr>
<tr>
<td>Relationship Manager</td>
<td>7</td>
<td>25</td>
</tr>
<tr>
<td>Loan Officer</td>
<td>7</td>
<td>25</td>
</tr>
<tr>
<td>Recoveries Officer</td>
<td>4</td>
<td>14.3</td>
</tr>
<tr>
<td>Total</td>
<td>28</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Computation from SPSS

Most of the questionnaire respondents were credit analysts representing 35.7% of the total respondents. Relationship managers and loan officers represent 25% of the respondents each while recoveries officers represented 14.3%. Their working experience is indicated in table 4.2.2 below. All of them have been with the bank for more than 5 years. Their age range is between 40 and 50 years.

Table 4.2.2: Working experience in lending

<table>
<thead>
<tr>
<th>Number of years</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>5 – 10 years</td>
<td>13</td>
<td>46.4</td>
</tr>
<tr>
<td>11 – 15 years</td>
<td>10</td>
<td>35.7</td>
</tr>
<tr>
<td>More than 15 years</td>
<td>5</td>
<td>17.9</td>
</tr>
<tr>
<td>Total</td>
<td>28</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Own computation from primary Data

The results in table 4.2.2 above show that all respondents have worked with the bank in lending units for more than five years. This shows that all respondents possess required knowledge of the lending activities.

The following tables show a summary of frequency and statistics obtained from questionnaire responses.
Table 4.2.3 Frequency

<table>
<thead>
<tr>
<th>Questions</th>
<th>Valid Response</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Determinants of non-performing loans are obvious</td>
<td>Agree</td>
<td>28</td>
<td>100</td>
</tr>
<tr>
<td>Are non performing loans a problem</td>
<td>Yes</td>
<td>28</td>
<td>100</td>
</tr>
<tr>
<td>Do you think the bank is adequately assessing credit applications</td>
<td>Yes</td>
<td>28</td>
<td>100</td>
</tr>
<tr>
<td>Are there any policies or procedures in place to reduce non performing loans</td>
<td>Yes</td>
<td>28</td>
<td>100</td>
</tr>
<tr>
<td>Overall rating with regards to non performing loans</td>
<td>Moderate</td>
<td>27</td>
<td>96.4</td>
</tr>
</tbody>
</table>

Source: Computation from SPSS

Table 4.2.4 Statistics

<table>
<thead>
<tr>
<th></th>
<th>Determinants of non-performing loans are obvious</th>
<th>In your opinion are non performing loans a problem</th>
<th>In your opinion do you think bank is adequately assessing credit applications</th>
<th>Overall rating with regards to non performing loans</th>
</tr>
</thead>
<tbody>
<tr>
<td>N</td>
<td>Valid</td>
<td>28</td>
<td>28</td>
<td>28</td>
</tr>
<tr>
<td></td>
<td>Missing</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Mean</td>
<td>1.00</td>
<td>1.00</td>
<td>1.00</td>
<td>2.04</td>
</tr>
<tr>
<td>Mode</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>2</td>
</tr>
</tbody>
</table>

Source: Computation from SPSS

There were two possible responses namely YES (1) and NO (2) for the questions highlighted in the first three columns in Table 4.2.4. The mode of 1 show that all respondents answered YES to the highlighted questions. The results indicate that all 28 respondents agree that non performing loans are a problem in CBZ Bank Limited and that the determinants of non-performing loans are obvious. Non-performing loans in CBZ Bank Limited were rated as moderate(2) and respondents agreed that the bank is adequately assessing credit applications.

Respondents agreed on major factors affecting non performing loans in CBZ Bank Limited. The factors and their weights are shown in Table 4.2.5 below.
Table 4.2.5: Weight of significant factors causing non performing loans

<table>
<thead>
<tr>
<th>Significant factors causing non performing loans</th>
<th>Frequency</th>
<th>Weights (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank ownership</td>
<td>1</td>
<td>3.57</td>
</tr>
<tr>
<td>Government policy</td>
<td>5</td>
<td>17.86</td>
</tr>
<tr>
<td>Inadequate market information</td>
<td>2</td>
<td>7.14</td>
</tr>
<tr>
<td>Inadequate risk management</td>
<td>1</td>
<td>3.57</td>
</tr>
<tr>
<td>Insider loans</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Integrity of borrower</td>
<td>5</td>
<td>17.86</td>
</tr>
<tr>
<td>Lack of collateral security</td>
<td>1</td>
<td>3.57</td>
</tr>
<tr>
<td>Low capitalization</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Natural disasters</td>
<td>9</td>
<td>32.14</td>
</tr>
<tr>
<td>Poor credit monitoring</td>
<td>1</td>
<td>3.57</td>
</tr>
<tr>
<td>Poor credit policy</td>
<td>1</td>
<td>3.57</td>
</tr>
<tr>
<td>Cost of borrowing</td>
<td>1</td>
<td>7.14</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>28</td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

*Source: Computation from SPSS*

Respondents highlighted that the top three significant factors causing non performing loans in CBZ Bank Limited are natural disasters (32.14%), government policy and integrity of the borrower both at 17.86%. The rest of the factors have a significant weight of less than 10%. It was highlighted that the largest exposures in the bank are under the agricultural sector which has not been performing well during the past decade.

Government policy was also ranked second with interview respondents blaming the look east policy for poor performance in the country’s manufacturing sector. Most companies in the manufacturing sector have obsolete equipments which cannot be compared to sophisticated machinery being used mainly in Asia resulting in cheap imported products.

**4.3 The trend of non-performing loans**

Generally non performing loans in CBZ Bank Limited have been increasing since the adoption of multicurrency as shown in Table 4.4.1 below.

Table 4.3.1: Trend of non-performing loans

<table>
<thead>
<tr>
<th></th>
<th>December 2009</th>
<th>December 2010</th>
<th>December 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non Performing Loans ($)</td>
<td>856,680.00</td>
<td>1,744,826.00</td>
<td>47,223,532.00</td>
</tr>
<tr>
<td>Total Loans ($)</td>
<td>244,288,572.00</td>
<td>430,036,911.00</td>
<td>750,149,025.00</td>
</tr>
<tr>
<td>Ratio of non-performing loans</td>
<td>0.35</td>
<td>0.41</td>
<td>6.3</td>
</tr>
<tr>
<td>to total loans (%)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The total loan book of the bank increased from $244 million in December 2009 to $750 million in December 2011. Interview respondents mainly attributed the upward trend in non-performing loans to the growth of the bank’s loan book since 2009 as shown in Table 4.4.1 above. The significant increase in the ratio of non-performing loans to total loans from 0.41% in December 2010 to 6.3% in December 2011 was mainly attributed to the poor performance of loans in the agricultural and manufacturing sectors of the economy.

4.4 Sectorial Distribution of Loans

Secondary data and interviews with senior managers revealed that the majority of loans were granted to the Agricultural, Distribution and Manufacturing sectors of the economy.

Table 4.4.1 Industrial sector analysis

<table>
<thead>
<tr>
<th>Sector</th>
<th>Frequency</th>
<th>Percent</th>
<th>Valid Percent</th>
<th>Cumulative Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>16</td>
<td>57.1</td>
<td>57.1</td>
<td>57.1</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>5</td>
<td>17.9</td>
<td>17.9</td>
<td>75.0</td>
</tr>
<tr>
<td>Distribution</td>
<td>7</td>
<td>25.0</td>
<td>25.0</td>
<td>100.0</td>
</tr>
<tr>
<td>Total</td>
<td>28</td>
<td>100.0</td>
<td>100.0</td>
<td></td>
</tr>
</tbody>
</table>

Source: Computation from SPSS

The results summarized in Table 4.4.1 above show that 57.1% of the respondents agree that agriculture is the major sector with the largest loan exposure. This is in line with published financial statements which show that agriculture, distribution and manufacturing sectors constitute 30.1%, 23.9% and 15.3% of total loans respectively.

4.5 Key areas affected by non-performing loans

Liquidity and Profitability

Table 4.5.1 below shows non-performing loans, profitability and liquidity ratio for the period 2009 to 2011.

Table 4.5.1: Non-performing loans, Profitability and Liquidity ratios

<table>
<thead>
<tr>
<th>Year</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-performing loans ($)</td>
<td>856,680.00</td>
<td>1,744,826.00</td>
<td>47,223,532.00</td>
</tr>
<tr>
<td>Profitability ($)</td>
<td>7,896,701.00</td>
<td>20,947,197.00</td>
<td>24,698,365.00</td>
</tr>
<tr>
<td>Liquidity ratio (%)</td>
<td>37</td>
<td>26.26</td>
<td>25.99</td>
</tr>
</tbody>
</table>

In December 2011, Non-performing loans at $47 million were more than the profit of $24.6 million recorded by the bank. Also, the liquidity ratio is decreasing as non performing loans are increasing. The above statistics indicated that non-performing are negatively affecting the bank in terms of profitability and liquidity.

This is in line with questionnaire respondents who pointed that non performing loans have significantly affected the liquidity of the bank as shown in Table 4.5.2 below.

**Table 4.5.2: Key areas of performance affected by non performing loans**

<table>
<thead>
<tr>
<th></th>
<th>Frequency</th>
<th>Percent</th>
<th>Valid Percent</th>
<th>Cumulative Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Liquidity</td>
<td>28</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

**Source:** Computation from SPSS

Table 4.5.2 above shows that all questionnaire respondents chose liquidity as the most key area affected by non performing loans. Interview respondents pointed out that both liquidity and profitability were negatively affected by non performing loans. Interview respondents attributed non performing loans as the main cause of liquidity challenges faced by the bank during the first quarter of 2012.

### 4.6 Management’s response to non performing loans

**Table 4.6.1 Statistics**

<table>
<thead>
<tr>
<th></th>
<th>Strict credit assessment</th>
<th>Adherence to credit policy</th>
<th>Collateral security</th>
<th>Training and development</th>
<th>Effective credit monitoring</th>
<th>Frequent contact with borrowers</th>
</tr>
</thead>
<tbody>
<tr>
<td>N</td>
<td>Valid</td>
<td>28</td>
<td>28</td>
<td>28</td>
<td>28</td>
<td>28</td>
</tr>
<tr>
<td></td>
<td>Missing</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Mean</td>
<td></td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Mode</td>
<td></td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
</tbody>
</table>

**Source:** Computation from SPSS

All respondents agreed that management has put in place effective strategies to curb the increase in non-performing loans as shown in Table 4.6.1 above. The mode shows that all the majority of respondents answered YES (1) as opposed to NO (2), to the strategies that management has put in place.

Primary data obtained from interviews revealed that the bank has a strict credit policy and has put in place structures that prevent the build up of non-performing loans. It was also noted that separation of duties on the entire activities in processing of loans is also an effective way to reduce non performing loans. The bank has centralized approval of loans through the Central Credit Committee and the Executive Credit Committee. However, all interviewees argued
that though the bank has put in place effective control and monitoring measures to reduce non performing loans, problem loans could not be avoided mainly because of external forces.

5.0 Recommendation from interview respondents

Interview respondents recommended that the bank should not issue additional loans to the agricultural and manufacturing sectors of the economy because of the prevailing harsh operating environment characterized by high cost of borrowing and increased competition from globalization.

5.1 Recommendations

It is apparent that banks need to seriously consider all the internal and external factors causing non performing loans as well as the impact of non-performing loans on the bank’s overall performance. The impact of environmental factors such as natural disasters and government policy should be considered seriously during the credit assessment process. The bank should slow down on issuing loans to companies in the agricultural and manufacturing sectors as they are currently not performing well. Loans in these sectors should only be granted if the borrower proves that they have the capacity to pay back loans given.

Management need to ensure that borrowed funds are being used for the intended purpose through enhanced credit monitoring. This can be achieved by adopting a relationship management approach which helps management to have a closer look at the business as well as the characters of the senior managers running the organization.

5.2 Conclusions

Research findings indicated that non performing loans were caused by internal and external factors. In the context of CBZ Bank Limited, internal factors such as poor credit policy, weak credit analysis, poor credit monitoring, inadequate risk management and insider loans have a limited influence towards non performing loans. The research findings highlighted that external factors namely natural disaster, government policy and the integrity of the borrower as the major factors that caused non performing loans in CBZ Bank Limited.

Findings indicated that there is an upward trend in non-performing loans since the adoption of multicurrency in 2009. The upward trend has been attributed to the growth in the loan book of the bank during the period under review mainly in the agricultural and manufacturing sectors of the economy. The agricultural sector has not been performing well owing to climate changes and expensive costs related with farming in Zimbabwe. Both sectors suffer severely from the increased competition from cheap products which are being imported from Asia and South Africa thereby threatening their viability.

Findings further indicated that non performing loans have negatively affected the performance of the bank in terms of liquidity and profitability. It was established that an increase in non-performing loans resulted in a reduction in
the company’s profitability as well as the liquidity ratio. Despite strategies put in place by management to reduce non-performing loans, problem loans continue to increase.

Internal factors can be easily controlled while external factors can be a threat to the viability of banks. Banks have to be vigilant in their lending decisions so as to avoid loan losses and the accumulation of non-performing loans. Banks need to concentrate on sectors that are performing well and avoid lending to those sectors which have already recorded a significant amount of non-performing loans. One thing to note is that these results can be generalized to the whole banking sector in Zimbabwe as almost all the banks have been affected by non-performing loans. Therefore the recommendations generated are a prescription for all banks in Zimbabwe.
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