DESKTOP STUDY OF THE EFFECTS OF DEPOSITORS FUNDS ON THE PERFORMANCE AND GROWTH OF FINANCIAL INSTITUTIONS

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ABSTRACT

The purpose of the study was to establish the effects of depositors' funds on performance and growth of the financial institutions. A background of continuously rising trend in the bank's deposits and profits has been a major cause for concern as questions have been raised as to whether or not the two variables have a relationship. This objective was achieved by consulting and reviewing literature from numerous authorities to access in-depth knowledge of the research subject. The research used only secondary sources for collecting data. The findings indicated that there is a positive significant relationship between deposits and performance of the bank. The findings also showed that there are variables that affect the deposits and in turn profitability, it showed that a positive change in deposits interest rate affects the level of deposits received and later on the profitability of the bank. Based on this, the study recommends the bank to develop strategies towards marketing and mobilisation of more deposits as they are indispensable tools towards the profitability of the bank.

Keywords: Depositor, Funds, Performance, Growth, Financial Institutions.

INTRODUCTION

Literature review according to Agenda & Machi, (2009), finds new ways of making the research that was previously conducted clear and understandable and this gives the way forward to further researches. The main purpose of literature review in other words is to examine facts or views presented by the recognized scholars on their researches.

THEORETICAL REVIEW

There are those factors that motivate commercial banks to secure their deposits, possible effects of such decisions on performance and growth of banks can be explained by various theory. This research made use of two theories namely, financial intermediation theory and economies of scale theory to clearly shed more light on the theoretical aspect of this research.

Financial Intermediation Theory

Werner, (2015), stresses out that currently financial intermediation theory present the fact that banks and non-banks financial institutions are similar since they are all simply financial intermediaries. The banks lend out deposits they have gathered (Werner, 2015). In the words of the latest authors, Dewatripont et al. (2010) states that commercial banks make profits by borrowing short and lending long. The theory was established by various great economists. The economists include (Gertler & Kiyotaki, 2011; Casu & Girrardone, 2006).

The theory describes the process which banks go through to make their profits. The process involves commercial banks borrowing funds from depositors that have maturities that are short and on the other hand lending funds to borrowers at longer maturities. Matthew & Thompson (2005) mentioned that bank's role is that of financial intermediary, they gather deposits to make them available for lending. The banks so firstly need to make sure that they have enough deposits for them to be able to lend out funds to their borrowers. This theory is helpful in this study as it focuses on how the banks makes their funds, they collect deposits and use them to lend to their clients. This theory shows how important deposits are and how profits are made by the banks.

ECONOMIES OF SCALE

The theory suggests that the banks which are big makes more profits than those small banks. The theory was introduced first in 1970's by the authors Vernon (1971) and Emery (1971), they were the ones to link the size of the bank to profitability (Haron & Azmi, 2004). Large banks have an advantage of producing their financial services at lower cost per unit. Their lower cost of production ensures high profits. The large banks enjoy economies of scale, they are able to produce cheaply and effectively their services. Economies of scale are different advantages that the bank enjoys. The advantages are as a result of large-scale operation. This then mean that the large banks will incur low cost of operation. So, the theory presents the fact that large banks make more profits than the small banks thus the banks should aim in improving their performance and grow. The theory is important for this research as it relates the size of the bank and profitability. This would be very useful in this research (Agyemang & Yensu, 2018).

VARIABLES THAT AFFECT DEPOSITORS' FUNDS

Monetary Variables

The study carried out by Teshome (2017), stated that variables such as deposits, number of branches, interest rates, loan to deposit ratio, annual inflation rate, population and GDP had a significant relationship with deposits of commercial banks. Monetary variables have effect on deposits. Haron & Azmi (2004) carried a research on such variables affecting the deposits in Malaysia.

Interest Rates

Tun et al. (2020) describes interest as a variable that is very important in encouraging customers to make deposits at the banks. Ceteris paribus a rise in interest margin leads to a rise in commercial bank deposits, (Sharma, 2009). The correlation that the interest rate margin and deposits have is negative. According to Dewatripont et al. (2010) the inefficiencies of a financial system are generally affected by great spreads or great spreads are thought to reflect cost of financial intermediation. Potential savers that have low returns tend to be discouraged when the spread is too high. In this regard, according to Nathanael and Eriemo (2014) it can be argued if the interest on deposits are high that means that deposits will be higher too (ceteris paribus). In developing countries, the banking system is characterized by a high degree of concentration of deposits in some major banks (Mohan, 2012). Aslam (2018), discovered how the interest rate affect the savings and recommended the policy makers to come up with friendly interest rates in order to enhance the savings in Sri Lanks. Mohammand & Mhadi, (2010) also made a conclusion that interest rate is very crucial in banks as it one of the effective factors that push people to put their deposits in a bank. The similar research was conducted in 2009 by Herald and Heiko and yielded similar results.

Inflation

Inflation is one of the main reasons that people hesitate to put all their money in the bank, over time, inflation can erode the value of those savings, and this was stated on financial education, (2020) website. According to Sharma, (2009) and Khizer et al. (2011) if there is an increase in inflation the deposits will head dive. A study carried out by Athukorala & Tsai (2003) also agree to that, if the inflation increase this will result in declining of deposits. The author went on to review that with the interest rate however, its different, the correlation is positive. Siaw & Lawer (2015) concluded that inflation and deposit interest rate in the long run have strong influence on the bank's deposits but in the long run the growth in money supply affects the deposits positively. However, the growth in money supply and the inflation in the short run, they both have the effect on deposits which is negative.

GDP

Sharma (2009) carried out a study and noted out increase in GDP per capital resulted in increase in commercial banks deposits. Therefore, we can note the existence of a strong correlation between level of economic activities and deposits. Bank deposits are well thought out as the key element of a country's savings, also have a huge effect on the economic performance of any country (Mushtaq et al., 2017).

Deposit Rates

Siyanbola (2012) study had similar results with Rehmat et al. (2010) and the results were consistent with that, if the deposits rate go up the bank's deposits will as well go up. A study was carried out in Zimbabwe covering the period 2000- 2006 by Mashamba et al. (2014), the study was in support that if the deposits rate goes up also the deposits of the bank goes up. That research went on to suggest that banks should focus also on the unbanked population by expanding branches, raising their deposit interest rates for them to gain more deposits and lastly offering low cost accounts. According to Tun et al. (2020) if the deposit rate rises it leads to an increase in deposits of commercial banks. Werner, (2015) is of opinion that if banks would want to obtain more deposits, they will have to raise their deposit rates.

Quality of Services

When the customers decide on the bank to bank with, they consider also services they offer. A service to be called of quality it must be able to meet the expectations of customers (Sylvester, 2010). Goiteom (2011), highlighted conditions that most people consider in their decisions to choose a bank, the author mentions the convenience of the bank, the image of the bank, the influence that the employees have on the bank and also the ability to provide the services. In the processes of bank of formulating strategies to increase their deposits they should take note of these factors that the customers consider. Nevertheless, parallel studies have been undertaken by Hooman et al. (2016), and the study focused on the quality of the bank's services and the factors affecting thereof. The study showed how the quality of the bank's services is ensured. They mentioned the factors such as reliability of the banking system, employee's competence and skills and also the best banking system. The study also carried out by Maharana et al. (2015) which is similar to that of Iswary (2015), reviewed that innovative banking services affects deposit mobilization.

Technology

According to Nkiru (2018) innovations in the banking industry like automatic payment, electronic money transfers terminals, internet banking etc. have caused reduction in bank's cost, banks to be efficient and faster in offering their services and as a result the performance is improved. Kariyawasam & Jayasiri (2016), pointed out various benefits that come from using internet banking, it is convenient, fast and reliable. The study clarifies the problems that result from not using the internet banking. It also evaluates the constraints for banks of adopting internet banking, this includes security threat, failures of system as well as the unawareness of the remote areas in terms of e banking services.it is important to note that all these innovations that aim at having competitive edge are related to the profitability of banks (Akombo, 2011). According to Andrew (2014), the productivity of employees can be increased by IT driven banking services increase. If the operations of the bank are improved and if the productivity goes up the usually more customers will be satisfied and due to that inevitably deposits increase.

The Relationship between the Depositor's Funds and the Performance and Growth in Banks

According to Agyemang (2020), bank performance reflects the way resources of a bank are used in such a way that their objectives are achieved. A study by Bakare (2011), showed that generally, there are types of individual deposits, and if a bank manages to have more of them this will result in improved performance. According to Iswary (2015), formulation of bank policies that are very aggressive in order to attract deposits of individuals will cause the profits to go up. Gul et al. (2011), the investigation was based on the effects of deposits, equity, loans, assets, economic growth and indicators of profitability such as ROE, ROA and ROCE. The study was conducted from the year 2005 to the year 2009 using the top 15 list of commercial banks in Pakistan. The findings from the study were that deposits have a correlation that is positive with ROA but this is not the same for all the indicators of profitability. ROCE as a profitability indicator have negative correlation with the depositor's funds. The research had a conflicting opinion, they believe that if the commercial banks rely entirely on deposits as the source of fund, they are likely to be less profitable.

Kigaru (2010) conducted a research with the aim of examining if there exist a relationship between the deposits of a bank and the capital in Kenya. The research successfully managed to illustrate that there is a relation that is positive between the variables. Nevertheless, they again noticed that although there seem to be a relation between the deposits and capital of the bank, the correlation is much stronger in banks that are small than those larger banks. The research however, could not address the main part that the depositors' funds play on bank's performance. Dietrich & Wanzeried (2009) carried a research to examine the factors affecting the profits of the banks in Swirterland. They managed to discover that the rise in deposits did not strongly affect the profits. The research could not pick up evidence that the commercial banks could transform deposit liabilities in assets that can earn income. Olweny & Sipho (2010) empirically analysed the impact specific bank factors on the commercial bank's profits. The specific factors were, liquidity, asset quality, differences of incomes. The results indicated that there was a positive correlation between the factors in examination and profits. They could not connect deposits directly to the profits.

Mwathi (2009) examined the relationship between the financial performance of a bank and its ownership structure. Their research showed that the commercial banks that were listed seemed to perform better than those that were not listed. This they thought it was because listed banks are expected to have good governance. They had evidence that the banks with large private ownership outperformed many banks with significant holding. The study also could not connect depositors' funds to the performance of the bank. The results established from the research by Tarawneh (2006) showed if the bank possess great capital, deposits, and massive total assets among others it does not guarantee great profits. The results evidenced that the efficiency in operating banks, the size of the bank, and management of assets, have a correlation that is positive with the profits of bank. Grigorian & Manole (2002) study clearly shows that when a bank has a strong capital base, that is if it is well capitalized it has more chance to gather more deposits than those commercial banks that have low capital. They however, could not find evidence to support that the foreign banks have the potential to collect more deposits by spending so low on rates. According to Hassan et al. net interest margins could be higher if the bank can be able to collect more deposits, and the rise in that net interest margin cause rise in profitability of the bank (Agyemang et al., 2019).

The Relationship between Statutory Instruments and Depositors' Funds

According to Udeh (2015), the monetary policy refers to any procedures carried out by the government to affect financial markets and credit conditions, with the ultimate goal of influencing the entire behaviour of the economy. Hassan et al. (2016) is of the opinion that the bank performance is affected directly by the monetary policies. The deposits are invested in both the long term or short-term investments. If more loans and advances are given to the creditors that means more profits available to the bank (Solomon, 2012). When the RBZ (… undertake policies that are contractionary, this reduces the resources that are available to the bank and this has an effect of reducing the profitability also. In contrast, monetary policies that are expansionary would have an opposite effect. Udeh (2015), conducted a research trying to come up with the relationship that exist between the monetary policies and the profitability of the commercial banks. The study concluded that the impact of the policies on the profits of the bank was insignificant and recommended that banks to increase profits they should look beyond monetary policy statements.

A similar research carried out by Ekpung et al. (2015), of the effects that the monetary policy has on the bank's performance. The deposit liabilities were representing the performance of the bank and deposit rate, exchange rates, minimum discount rate were used as the independent variables (Almazari, 2011). The results of the findings were that there is a negative relationship between the minimum discount rate, deposit rate and deposit liabilities. The search made a conclusion supporting that the monetary policy has effect on depositors' funds, thus they have control on the level of deposit liabilities of banks. The causal correlation of the imposed interest rates by the central bank in Pakistan and performance of the banking industry from the period of 2007 to 2011 was investigated by (Zaman et al., 2014). Taking the size of the firm as the control variable, the study showed that the monetary policy has a negative correlation with the banks' performance. The performed being measured by the ROE and ROA and the interest rate representing the monetary policy.

Punita et al. (2006) carried out an investigation on the impact of monetary policies on profitability of banks from 1995 - 2000. The findings were of the variables that represent monetary policy; bank rate, statutory ratio a strong inverse relationship on banks profitability, while lending rate has positive effect on this variable. When the private sector was pooled to explain the relationship between profitability of banks and monetary policy instruments the same results was obtained.

Challenges Affecting the Bank's Performance in Zimbabwe

The banking industry is facing extraordinary changes as it moves toward digitalization. Most banks are starting to embrace the technological changes however, there is still the need to overcome some challenges. If the banks fail to deal with these challenges, they are likely to struggle to maintain validity in the long term. Financial institutions are being challenged in many ways and some of these challenges are discussed below (Ahmed, 2015).

Low Quality Asset

The main assets used for the bank's investment are deposit at other banks, reserve, cash item in process of collection and most importantly loans. Most of the banks are suffering in their operations because they are using assets of very low quality. According to Casu et al. (2006), one of the activities that are so important to the bank is credit. Credit have to be managed very well by the bank managers for the bank to avoid loan loss. Usually banks fail due to bad loans and loan losses.

Increasing Pressure from Customers

Huyett & Viguerie (2005) noted that companies are facing severe competition in this era which include in as a result of technology, domestic as well as global competition and economic conditions makes the existence of the banks tougher than before. Customer in banking sector today have great expectations, they demand fast access and expects results that are better than those in the past. According to Boot & Schmeits (2005) if there is increased competition, it can have adverse impact on access to financial services thus affecting the performance of the bank. Competition can weaken the bank's incentives to invest in information acquisition and lower their lending to information-intensive borrowers.

Investor Expectations

Nkuru, (2018) state that even though most of the commercial banks today are reporting profits, they are failing to meet the return on investment expected by their shareholders. The possible reason for this is not understanding the expectations of customers, which translate into lower retention rates and lower customers.

Customer Expectations

Expectations of customers has changed due to changes in technology according to Sullivan, (2019), the experience of customers is at the forefront of the challenges that is being faced by the banking sector today. According to Mwathi (2009) traditional banks are failing to deliver the quality of services that the customers are now demanding due to technology. The confidence that the depositors put in the banks is a crucial ingredient for the liquidity health of any financial institution. Nhavira et al. (2013) and the RBZ (2016) detected general doubts in the banking industry as the foremost driver of cash hoarding by the public and this results in cash circulating outside the system of the bank and hence reducing the liquidity of the system of financial sector.

Regulatory Conditions

The continuing escalating regulatory conditions of financial services industry requires banks to spend much of their discretionary budget on compliance. Claessens et al. (2003) as well as Claessens (2006), noted that as products and financial markets become more global and complex, new competition and regulatory policy issues will rise. Banks that are able to keep up with the industry standards and regulations are in need of resources in every level.

Foreign Currency Shortages

The central bank of Zimbabwe according to Zwinoira, (2018) have been struggling to acquire adequate levels of foreign currency to support industry in importing raw materials that are critical for their production operations. The author believes that if the problem of forex shortages is addressed, this will not only sustain the industry, lead to increased production and hence, exports, but also this will address liquidity problems.

Ways for Improving Performance and Growth under the Prevailing Situations

Introduce adequate procedures and policies to increase bank deposits

One of the most important aspects in the banking sector is mobilization of deposits, because the banks depend on deposits as their funding (Guest et al., 2003). According to Kariyawasam & Jayasiri (2016), the deposits are very crucial and they affect performance, they generate working fund at lower cost. The research is recommending that since the deposits seem to be very important in the survival of every commercial bank, then much emphasis must be exerted on the ways to increase the deposits. In order to mobilise more deposits, the banks should consider increase in deposit interest rates. Sylvester (2010) agrees to the fact for the banks to be successful they have to be able to mobilise much deposits.

New quality products and services

The study carried out by Andrew (2004), shows how banking services driven by IT increase the employee’s productivity. This productivity has impact on the mobilization of deposits, it increases customer satisfaction and hence mobilisation of deposits is automatic. Banks should generate services and products for the unbanked groups. Increasing the number of ATMs also helps in the increase of deposits, Nkiru (2018) support this, the author noticed that if the POS machines are increased increase the volume of the bank.

Increase branch networks

Banks should seek to increase the number branches this is in support Amene (2017) stating that increase branch networks of banks helps to move to the unbanked population and to the remote areas thereby creating awareness of services offered by the bank. The expansion of the banking facilities is the vital aspect for mobilisation of deposits.

Improve marketing strategies

According to Hakimuddin (2012) there is the need of customer awareness in order to improve performance. Masood et al. (2014) suggests that banks need to provide awareness to customers by doing seminars, and having excellent strategies of marketing their services. Also, when banks design the marketing strategies, they should consider some important dimensions as they should be high quality and low cost (pull marketing strategies). Seminars and advertisements should be simple and powerful. Ryan (2011), emphasized that the banks should aim to have a good brand name and position for this is alone is a good awareness strategy.

Strong regulatory policies

Good corporate governance practices and minimum capital requirements should be emphasized by the policy setting bodies. The government and other regulatory bodies have to have measures that are strong and this will help the banks in turn.

Bank should ensure security

The reason behind the saving of money in banks by so many people is that they have confidence that the banks are the best in terms of safeguarding their savings. Samarasiri (2014), is of belief that more caution should be used when handling or using the funds of the depositors as this funds are the bank's capital for the business to continue to operate. Hence Garo (2015) mentions that banks need deposit just as a person need oxygen. Therefore, for the banks to continue their operations and to keep their reputation they have to use the savings wisely and with care (Samarasiri, 2014). According to Samuel (2015), a bank can attract more deposits when the bank has high security adoptions. Lately, various banks face the risks that is related to savings, by implementing deposit insurance scheme. This can be noticed in banks in Zimbabwe. Samuel (2015), goes on to state that insurance scheme gives a signal to the depositors that their savings are protected in the event that there is a bank failure.

Gap analysis

Nafula (2003) is of the opinion that due to the opportunity cost, the customer's deposi ts have a significant and negative impact on the profitability of banks. Dancan (2012) deliver ed evidence on the fact that the banks that maintain high levels of deposits accounts are the b est performing banks. A review of selected global studies for instance, Dancan (2012) discov ered that there is a difference in opinions on the relationship between bank deposits and perfo rmance. Some studies are still insufficient because they fail to single out deposits in their rese arches of commercial bank's performances. For instance, Mwathi (2009) did a research conce rning the relationship between financial performance of banks and their ownership structure b ut failed to relate performance to the level of deposits. Also, Kigaru (2010) reviewed the relat ionship between the profitability of banks and the capital inadequacy but was unsuccessful in addressing the part played by deposits in the performance of the bank. This therefore implies that studies are yet to cover adequately the subject concerning the deposits impact on perform ance of banks.

CONCLUSION

From this study, the conclusion is that there is a strong relationship between depositors' funds and the performance and growth of the financial institutions. For banks to survive and to grow they need funds and the revenue generation and loan disbursement can only be made possible if the banks have enough deposits. Therefore, the deposits matters. One of the strategies that can be used to mobilise deposits is strong marketing strategies.

Recommendations

The research seems to suggest that banks should fight to have as much deposits as possible, they should adopt strategies to attract deposits. This is because the banks usually depend on the deposits to generate revenue and they are very important as they are the major fiancé for the bank's assets.

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