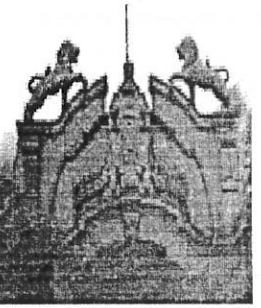
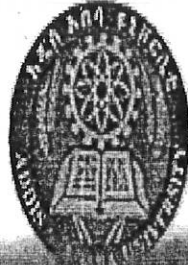


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ADDIS ABABA UNIVERSITY
SCHOOL OF BUSINESS AND PUBLIC ADMINISTRATION
DEPARTMENT OF ACCOUNTING AND FINANCE
(GRADUATE PROGRAM)

***Regulation and Supervision of National Bank of Ethiopia and its
Impact on the Activities of Ethiopian Private Banking Industry***

By:

Sofoniyas Mekonnen

April , 2012

Addis Ababa, Ethiopia

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SCHOOL OF BUSINESS AND PUBLIC ADMINISTRATION
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the Activities of Ethiopian Private Banking Industry***

***A Thesis Submitted to the School of Graduate Studies of Addis Ababa
University in Partial Fulfillment of the Requirements for the
Degree of Master of Science in Accounting and Finance***

By:

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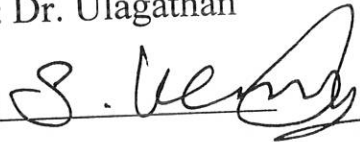
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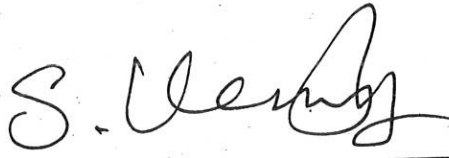
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Statement of Certification

This is to certify that **Sofoniyas Mekonnen Fekadu** has carried out his research work on the topic entitled “**Regulation and Supervision of National Bank of Ethiopia and its Impact on the Activities of Ethiopian Private Banking Industry**”. The work is original in nature and is suitable for submission for the reward of the M.Sc Degree in Accounting and Finance.

Advisor: Ulagathan. (PhD):

 22/02/2012

Abstract

This study is aimed at assessing the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banking industry. The research examined the role played by the regulatory authorities towards a healthy supervision of the operation of banks in Ethiopia and also examined the tools, scope, methods and policy framework of supervision. The study theme was guided by six specific objectives and three research questions. The research borrowed heavily from related research material which was appropriately referenced. It adopted a questionnaire based method of evaluation for the purposively selected private banks namely (Awash, Dashen, Abyssinia, Wegagen, United, Nib International Bank) and for banking supervision department employees of NBE and interview with the banking supervision department employees of NBE were conducted to meet the specific objective and to answer the research questions and comparing the survey result using descriptive statistics and analysis both results i.e. survey and interview with concurrent mixed method research approach. The results of this combined research methodology reveal that the supervisory and regulatory framework of NBE is effective. But the success of supervisory and regulatory framework of NBE endangered by NBE supervisory capacity particularly related to little experience of the banking supervision department employees and the absence of entry training for the new employees to notify about the banking operation. The effective regulation and supervision activities of NBE, results banking stability in Ethiopia. The stability of banking industry in Ethiopia measured by using three parameters namely profitability, liquidity and asset quality of the banks. Based on this their profitability, liquidity and asset quality of most of private banks in Ethiopia is currently increase time to time. As a result, banking industry in Ethiopia assure public confidence to deposit and withdraw their money at any time. Generally NBE followed preventive regulation method and on-site and off-site supervision method for banks and it has great impact on the activities of banking industry.

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List of Abbreviations

CBN	Central Bank of Nigeria
EWS	Early Warning Signals
FSI	Financial Stability Institute
MFIs	Microfinance Institutions
NBE	National Bank of Ethiopia
NDIC	Nigerian Deposit Insurance Corporation
NGO	Non Governmental Organization

Chapter One: Introduction

The financial system in any economy plays an important role in promoting economic growth and development by improving the efficiency of resource mobilization, pooling savings and allocating these savings to investment outlets. It provides liquidity and capital to firms in their production processes and facilitates a reliable payment system, thus providing a veritable platform for an effective monetary policy management. For the system to achieve the above objective, it must be developed through the collaborative efforts of the government, the monetary authorities, the operators and the general public.

The monetary authorities must therefore improve on their regulatory process and pursue policies and standards that would enhance the safety, soundness and efficiency of the financial system. Banks, as the major operators in the system, provide the institutional mechanism for financial intermediation in the system by managing the financial assets and liabilities of other economic units. They mobilize deposits, provide credits and in the process create money, offer professional advice to investors and act as agents of the government's in the implementation of various monetary and macroeconomic policies (Agu, 1984).

Given the overall importance of banks in the economy, their supervision and regulation become imperative in order to ensure a stable and healthy financial system. Supervision entails, not only the enforcement of rules and regulation, but also some judgment regarding the quality of financial institutions' assets, capital adequacy and management, while regulation involves the body of specific rules governing expected behaviors that limit or control the activities and business operations of financial institutions (Ajayi, 1995). Oftentimes, these concepts are used interchangeably because of their very close relationship. Banking regulation and supervision, as part of public infrastructure, has the major role of ensuring financial sector stability and sustainable economic growth and development. Sound economic policy management requires a robust, efficient and sound financial sector. Supervisors must therefore ensure that banks and other financial institutions are operated in a safe and sound manner that would guarantee sustainable

economic growth. Instability in the banking sector could lead to bank failures, loss of public confidence as well as adverse macroeconomic environment with negative impact on real incomes, employment and output (Keeley, 1990).

Banks' capital is only small part of their source of funds, the major source of their funding being deposits. Hence, depositors need protection, primarily because they do not have the means to determine the extent of risks taken by banks in the use of their money. The supervisory and regulatory framework must therefore ensure that banks operate within prescribed prudential limits and standards, in a safe manner and uphold high standards of professional conduct that would sustain continuing confidence in the banking system (Estrella, 1998).

Banking supervisors worldwide have consequently realized / recognized the need to harmonize laws, regulations, code and standards in order to promote economic growth and international financial stability. Thus, for the industry to be efficient, it must be regulated and supervised in view of the failure of the market system to recognize social rationality and the tendency for market participants to take undue risks which could impair the stability and solvency of their institutions.

Regulation and supervision of banks remain an integral part of the mechanism for ensuring safe and sound banking practice. At the apex of the regulatory and supervisory framework for the banking industry is the National Bank of Ethiopia (NBE).

The National Bank of Ethiopia was established in 1963 by proclamation number 206 of 1963 and began operation in January 1964. Prior to this proclamation, the Bank used to carry out dual activities, i.e. commercial banking and central banking. The proclamation raised the Bank's capital to Ethiopian birr 10.0 million and granted broad administrative autonomy and juridical personality (www.nbe.gov.et).

In the main, bank supervision entails on-site examination of the institutions and off-site analysis of periodically rendered prudential returns, a process called off-site surveillance. The two activities are mutually reinforcing and are designed to timely identify and

diagnose emerging problems in individual banks with a view to prescribing the most efficient resolution options. In line with prevailing international standards, these agencies (NBE) have continued to emphasize risk-focused bank supervision in Ethiopia. Dale (1988) had classified prudential regulation of banks into three: preventive, protective and supportive. While preventive regulation is designed to limit the risk undertaken, the protective regulation offers protection in the event of failure. The supportive regulation is in form of a lender of last resort.

This study was assessed the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banking industry. This will not only add to existing literature but also it will serve as means to improve the banking regulatory and supervisory framework that are issued by NBE.

The remaining part of the proposal is organized as follows: section1.1 deals with a statement of problem; section 1.2 research questions; section 1.3 deals with objectives of the study; section 1.4 presents the research methods to be adopted; section1.5 scope and limitation of the study deals with; Section 1.6 is about significance of the study and section1.7 deals with organization of the research report and finally section 1.8 deals definition of terms that are important to the study.

1.1.Statement of the Problem

Banks are like the heart which pumps blood to any economy of a given country (Iyade, 2006). They are among the different financial institutions in the country, which includes insurance companies and microfinance institutions. Banks play a prominent role in allocation of resources by acting as intermediaries and also help boost the economy by providing employment opportunities. They also contribute directly to the economy through their disproportional large tax payments. Based on banking sector review 2010 the banks in Ethiopia had been around birr 586 million birr and from other taxes which includes tax on dividend, salaries and tax on value added tax on purchase of fixed assets the industry is estimated to add another 500 million birr which makes the total tax paid

over birr 1 billion. This is equivalent to more than 10 percent of the birr 8.8 billion in direct income tax revenue collected by the government in previous year.

In order to increase their economic contribution of banking industry in Ethiopia, NBE should have effective banking regulation and supervision framework. Bank regulation/supervision is implemented to ensure a sound and safe financial system in the economy. The measures are mainly concerned with the quality of risk asset in banks, compliance with key ratios such as liquidity ratio, cash reserve ratio, capital adequacy ratio amongst others, the quality of management and other corporate governance issues.

However, inadequate supervisory framework and lack of an effective risk asset database and information sharing system have contributed in no small measure in disrupting the activities of banks, there by leading to the often distasteful incidents of banking distress and liquidation by the regulators.

In line with this problem, various banking legislation/acts have been promulgated as well as the introduction of different strategies all aimed at increasing the efficiency of banking regulation and supervision. Among them are on-site, off-site banking examination, routine examination, special examinations culled at the instance of the regulators as well as other methods of surveillance to be discussed in subsequent chapter. These measures are mutually reinforcing and are designed to timely identify and diagnose emerging problems in individual banks with a view to presenting most efficient resolution directed towards ensuring continued public confidence in the banking system.

Generally there is no best solution for regulating the baking business. Each regulatory consideration has to be adjusted to the exceptional situation in the country. One size fits all cannot be applied and no single model offers a universal remedy. Kassa (2010) conducted the study on the regulation and supervision of Microfinance business in Ethiopia, challenges and prospects and the major finding is that skills of Supervision staff in knowledge of efficient and effective regulatory and supervisory practices is low. As far as the knowledge of the researcher there is no research conducted on the banking supervision and regulation activities of NBE.

In sum, the above issues coupled with the gap in the literature (to be established in chapter two) call for research in the area of regulation and supervision of banking industry. To this end, the present study will provide insight into the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banking industry.

1.2. Research Questions

The supervisory and regulatory authorities play a significant role in the financial system of any economy through the promulgation of policies aimed at ensuring the prudent management of banks' assets and liabilities and thereby guarantee the safety of depositors' funds. They also promote compliance to safe and sound banking practices, encourage the institution of an efficient internal control system in individual money deposit banks in order to prevent the incidence of frauds, forgeries and other financial malpractices as well as ensure the stability and bring about public confidence in the system.

Based on the above information the researcher developed the following research questions:

1. Why is it mandatory for banks to be overtly regulated by National Bank of Ethiopia (NBE)?
2. Has the Ethiopian banking industry become safe, stable and command the confidence of the general public?
3. Have the activities of banking supervisions brought about normal banking practice, professionalism and ethical conduct in the Ethiopian banking industry system?

1.3. Objective of the Study

The general aim of this research work is to assess the impact of the regulatory and supervisory functions of the National Bank of Ethiopia (NBE) on the activities of Ethiopian private banking industry.

The specific objectives of the study were:

- To examine thoroughly how supervisory and regulatory functions of the regulator (NBE) impacts on the Ethiopian private banks
- To assess the on-site and off-site supervision activities of NBE

- Assessing the effectiveness of the regulation and supervision activities in the Ethiopian banking industry
- To examine regulatory and supervisory activities of the NBE have boosted depositors' confidence in the Banking System.
- To evaluate the minimum capital requirement for establishing new Banks
- To assess the investment activities restriction of private banking industry in Ethiopia

1.4. Research Method Adopted

To answer research questions, and to achieve the broad research objective presented in section 1.3 the study adopted a concurrent mixed method. Specifically, the research employed both survey and in-depth interview. For the head office employees of the selected banks namely Awash, Dashen, Abyssinia, Wegagen, United, Nib International Bank and for banking supervision department employees of NBE the researcher were used survey method. The researcher was conducted face-to-face in- depth interview with randomly selected from banking supervision department employees of NBE. For the survey, 125 structured self-administered questionnaires were distributed purposively selected banks head office employees and banking supervision department of NBE. Out of 125 questionnaires 96 questionnaires were distributed to the head office employees of the banks and the remaining 29 questionnaires were distributed to the NBE banking supervision department employees. With regard to the interviews, the researcher were conducted the interview with 8 randomly selected banking supervision department employees of NBE, from the total employees of 29. Further, the study were reviewed the regulatory documents including proclamation and declaration of NBE. The study tried to analyze the result obtained from the above mentioned data sources using descriptive statistics, and also tried to answer the research questions, and to achieve the broad objective.

1.5. Scope and Limitation of the Study

The scope of the study was limited to assessing the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banking industry through the

views of study participants. To this end the paper were look into general environment in which this industry operates and banking regulations and supervision in particular. In order to address this issue the study were conducted at Addis Ababa in purposively selected private banks head office specifically Awash, Dashen, Abyssinia, Wegagen, United, Nib International Bank and banking supervision department of NBE.

In conducting the study, there were some constraints. In view of the technicalities involved, it would be unrealistic to assume that all necessary facts have been gathered in the process of the study. Another potential limitation that hinder the smooth running of the research work are Shortage of finance and time, and the results of this study were not be generalized to other sectors other than banking sector.

1.6. Significance of the Study

The research findings have multi dimensional significances. Most importantly:

- It provides a platform for the regulatory authorities to appreciate the impact of their activities on the banking industry, and underscores areas for improvement.
- It is imperative to state that a study of this nature provides an independent platform via which the regulators can appraise fundamental tools of supervision in a bid to make reasonable adjustments where necessary.
- This study will be of immense benefit not only to the Ethiopian banking industry and its related institutions, but also to those interested in understanding the inter-relationship between the actions of the regulators on one hand and the banking institutions on the other as well as providing a platform for promoting an efficient and effective banking practice.
- Adds to the existing literature by examining the regulation and supervision activities of National Bank of Ethiopia
- The study will also be helpful for researcher who want to conduct their research on the area banking regulation and supervision

1.7.Organization of the Research Report

The research report is organized in to five chapters. Chapter one presents introduction where background of the study, statement of the problem, research questions, and objectives of the study, scope and limitation, and significance of the study is presented. Chapter two brings review of literature in which theories, empirical evidence and knowledge gap is identified. Chapter three presents Methodology and it contains research design, Sample population and participants, data collection instruments and data analysis procedures. Chapter four presents results and discussion, based on the collected information from the respondent. Finally, Chapter five brings to an end the research with conclusion and possible recommendation.

1.8.Definition of Terms

- **Financial Intermediation:** Financial Intermediation is the mobilization of funds from the surplus spending units at a cost or lending of such funds to the deficit spending units at a price both within and outside the shore of a country.
- **Bank regulation:** a body of specific rules or agreed behavior either imposed by some government or other external agency, or self-imposed by explicit or implicit agreement within the industry that limits the activities and business operations of financial institutions e.g. NBE
- **Bank supervision:** Is the process of monitoring banks to ensure that they are carrying out their activities in accordance with laws, rules and regulations, and in a safe and sound manner.
- **Stable banking system:** A stable banking system means that banks have the ability and capacity to meet maturing obligations as they fall due, and are making adequate profits from authorized banking business to justify their investment while at the same time keeping banking failures at a minimum within the country.
- **Prudential guidelines:** Is a body of specific rules imposed by government through the Central bank aimed at ensuring prudent management and administration of banks' funds so that reports of financial institutions are correct and reflective of their true portfolio (Iyade, 2006).

Chapter Two: Literature Review

This chapter tries to discuss the basic issues in regulation and supervision of banking institutions. An attempt is made to capture and present what is available in the literature from recent books and theoretical papers written by well known authors in the subject. Effort is also made to discuss about recent countries experience in regulating and supervising of banking industry and take lessons by adapting to the Ethiopian context.

This chapter covers three broad topics that relate to regulation and supervision of banking industry. Section 2.1 describes about the theoretical review in which a number of theories that have been developed on regulation and supervision of banks. This is followed by a review of the relevant empirical studies on the impacts of banking supervision and regulation on the banking activities and it is presented chronologically in section 2.2. Finally, conclusions on the literature review and knowledge gaps are presented in section 2.3.

2.1. Theoretical review

This section of the chapter discusses the theory on regulation and supervision of banks.

2.1.1. Introduction to Banking Supervision and Regulation

Regulation of banks has been defined by Llwellyn (1988) as a body of specific rules or agreed behavior either imposed by government or other external, agency or self imposed by explicit or implicit agreement within the industry that limits the activities and business operations of banks. In a nutshell, it is the codification of public policy towards banks to achieve a defined objective and/or act prudently. Banking regulation has two major components:

1. The rules or agreed behaviors; and
2. The monitoring and scrutiny to determine safety and soundness and ensure compliance.

Supervision on the other hand, is the process of monitoring banks to ensure that they are carrying out their activities in a safe and sound manner and in accordance with laws, rules and regulations. It is a means of determining the financial condition and of ensuring

compliance with laid down rules and regulations at any given time. Bench (1993) asserts that effective supervision of banks leads to a healthy banking industry.

Dimitri, Vitas (1990) also believes that good regulation and supervision will minimize the negative impact of moral hazard and price shocks on the banking system, thereby leading to a reduction in bank failures and banking system distress.

Traditionally, the role of banks whether in a developed or developing economy, consists of financial intermediation, provision of an efficient payments system and serving as a conduit for the implementation of monetary policies. It has been postulated that if these functions are efficiently carried out, the economy would be able to mobilize meaningful level of savings and channel these funds in an efficient and effective manner to ensure that no viable project is frustrated due to lack of funds.

In view of the importance of the banking sector in economic development and the imperfection of the market mechanism to mobilize and allocate financial resources to socially desirable economic activities of any nation, governments the world over, de regulate them more than any other sector in an economy.

This underscores the need for banking sector regulation. However, in addition, the nature of banking business (being highly geared and conducted with greater secrecy when compared with other real sector businesses) provides added reason for strict supervision. This is to constantly beam a search-light on the sector's activities with a view to ensuring that operators play by the rules of the game and imbibe sound and safe banking practices. Furthermore, such an oversight is intended to assist supervisory authorities in timely identification of deterioration in banks' financial conditions before it degenerates to threaten the stability of the banking system or even the economy.

Radical reforms to the system of prudential regulation and supervision have been implemented since the late 1980s. These reforms are essential because the prudential system has proved ineffective in ensuring sound bank management, as the scale of financial distress among the state government and local banks indicates.

In most African countries at the time of independence, there was no central bank and banking was dominated by foreign-owned commercial banks. After independence, new governments embarked on financial sector reform. This took a variety of forms, but the fundamental objective was increased lending to Africans and African-owned businesses, to correct the perceived bias of bank lending in the colonial period (Harvey, 1991).

In Ethiopia, there was a major change of economic strategy in 1975, after the fall of the imperial government, which was in some ways analogous to the changes in economic policy after independence in former colonies. Nevertheless, government policy on banking in Ethiopia does not really fit this generalization. Most notably, Ethiopia was not a colony; there was already a central bank in 1975; and at that time, most of the rest of the financial sector was already government-owned. The new Ethiopian government aimed to create a socialist, centrally controlled economy on the Soviet model. The main financial sector reform, therefore, was to direct the government banks to finance a greatly increased public sector.

The consequences of the post-1975 reforms in Ethiopia were also distinctive. Government ownership, and government direction of lending, might have been expected to undermine the banks, as happened elsewhere in Africa. Unusually, the damage was limited. Most notably, the single commercial bank remained sound. It did not require lengthy and costly rehabilitation, therefore, in order to be able to respond to the opportunities created by economic liberalization in the 1990s. This was not sufficient, however, for financial sector reform to achieve its objectives. Government-owned development banks expanded into commercial banking, but increased competition, and the increased productivity and improved services which should result from competition, appeared unlikely to result. A small amount of competition was possible from the licensing of new private sector commercial banks, but their success was endangered by inadequate banking legislation and central bank supervisory capacity. Moreover, expertise in both the large and small banks appeared to be inadequate for the rapid increase in sound lending to the private sector that was occurring. These factors exposed the banking system to some degree of risk (Harvey, 1991).

2.1.2. Role of Banks

The banking system in any economy plays the important role of promoting economic growth and development through the process of financial intermediation. Development economists argue that the existence and evolution of financial institutions and markets constitute an important element in the process of economic growth. The banking system, in promoting economic growth, plays the following roles among many others:-

- Improving the efficiency of resource mobilization by pooling individual savings;
- Increasing the proportion of societal resources devoted to interest-yielding assets and long-term investments, which in turn facilitate economic growth. This relates to the savings function of banks and the pivotal role of savings is demonstrated by the fact that when it is in short supply in any nation, investment and the standard of living decline.
- Providing a more efficient allocation of savings into investment than the individual savers can accomplish on their own. This flow of savings into investment ensures that more goods and services can be produced, thus increasing productivity and the nation's standard of living.
- Reducing the risks faced by firms in their production processes by providing liquidity and capital;
- Enables investors to improve their portfolio diversification by providing insurance and
- Project monitoring: apart from providing insurance services as part of the practice of universal banking, banks have developed a number of products linked to specific insurance policies which are designed to offer protection against life, health, property and income risks. In addition to these, the banks have been used by businesses and private consumers to "self- insure" against risk; that is holdings of cash and other similar products are built up as protection against future losses.
- Provides a veritable platform for an effective monetary policy implementation thereby enhancing the effective management of the economy. The banking system has been one of the channels through which government carries out its policy of stabilizing the economy and controlling inflation. Through the manipulation of

certain key variables such as interest rates and the quantum of credit, government is able to influence borrowing and spending within the economy. These in turn affect employment, production and prices.

- Facilitates a reliable payments system which provides support for the economy. In this regard, certain financial assets such as current accounts, deposit / savings accounts, domiciliary accounts etc, which serve as media of exchange for payments readily, come to mind. Checks, credit cards and electronic transfers are the principal means of payment today.
- Provides credit. The banking system provides credit to finance investment and consumption. This is a major function of the banking system (Iyade, 2006).

2.1.3. The Objectives for Banking Supervision

Banks worldwide are more regulated than other institutions because of their roles as financial intermediaries. As financial intermediaries, banks mobilize funds from the surplus spending units at a cost for on lending of such funds to the deficit spending units at a price both within and outside the shores of a country. In discharging their financial intermediating role, it is the responsibility of banks to ensure that the funds mobilized could be accessed by the depositors as when needed. While in their care, the mobilized funds are advanced as loans and advances at a price to be repaid along with the principal loan. The spread between the cost of funds and the price of the loans granted in this manner is the singular most important source of income for banks.

Banks also provide an efficient payment mechanism in the economy. They provide smooth and efficient system for making payment to settle both business and personal transactions, and international financial obligations on behalf of their customers. Thus, savings are stimulated for investment in the economy by banks. The weight of evidence is that banks in the process of intermediation contribute significantly to real economic development. According to Schumpeter (1934), banks are necessary condition for economic development. This proposition has been supported by several later scholars including Goldsmith (1999) and Cameron et al (1972). Empirical evidence also suggests that there is a positive correlation between real growth of output, investment, bank assets and money supply. Growth in the banking sector when well transmitted would result in

the growth of the real sector. The opposite is also possible if the banking sector is repressed and inefficient. It is in recognition of this that John B. Heimann, founding Chairman of Financial Stability Institute (FSI) in June 2001 asserted that “the prosperity and strength of any economy relies heavily upon the proper and prudent functioning of the country’s system of financial intermediation. If the financial system is strong, the economy has the ability to grow and the strength to absorb shocks. But if the financial system is weak, it acts as a magnifier of problems, rather than a shock absorber.

In performing their various functions, banks are expected to ensure prudent management of assets and guarantee the safety of depositors’ funds. They are expected to adhere strictly to safe and sound banking practices, maintain adequate internal control measures to prevent incidences of fraud, forgery and other financial malpractices, to ensure stability and engender public confidence in the system. The proper management of banks is therefore a pre-requisite for economic prosperity in any country as the vehicle for the implementation of monetary policy. Indeed, the contributions of banks to the development of the economy depend on the quantity and quality of their services and the efficiency with which these services are provided. Here lies the concern of the Regulatory Authorities and hence the reason for intensive banking regulation and supervision.

The objectives of banking regulation and supervision were advanced by Giddy (1984) as for monetary policy, i.e. the ability of banks to create money through the extension of credit; credit allocation function of banks; the need to ensure competition and innovation by the prevention of cartels; and because banks are depositories of public savings and managers of payments mechanism, they are very vulnerable to collapse.

The protection of depositors has come to be generally accepted as the most basic reason for banking regulation and supervision. This objective is hinged on the fact that bank depositors have difficulty protecting their interests when compared to other bank creditors and investors. On his part, Sheng (1990) stated the objectives of supervision as: promotion and development of sound and wide range of financial services to meet the needs of the economy; ensuring efficiency, security and responsiveness of banks to the needs and complaints of customers; ensuring compliance with laid-down rules and regulations which are germane to ensuring high standards of banking; and to achieve

important developmental and social goals through their compliance with monetary and credit allocation policies. Sinkey J. R. (1989) states the goals of regulation as:

- The protection of depositors;
- The protection of the economy from the vagaries of the banking system; and
- The protection of banks' customers from the monopolistic power of banks.

Dale (1988) had classified prudential regulation of banks into three: preventive, protective and supportive. While preventive regulation is designed to limit the risk undertaken, the protective regulation offers protection in the event of failure. The supportive regulation is in form of a lender of last resort.

In both developed and developing economies, the banking industry determines the financial services available to the economies. Hence, regulation is necessary to break this monopolistic power and prevent abuse. Moreover, in developing economies, banks play their traditional intermediation roles as well as being used as a vehicle for achieving developmental and social goals. Banks in third world countries have to develop indigenous entrepreneurs by channeling credits for their use. As a result of this, the World Bank (1989) noted that banks in these economies have to be regulated to ensure that they play their proper role in economic development.

In a nutshell, the rationale for bank regulation and supervision can be summarized as follows:

- Efficiency,
- Diversity of choice,
- Competition,
- Stability of banking system,
- Macro economic stability, and
- Developmental and social objectives.

2.1.4. Approaches to Banking Regulation and Supervision

The four approaches to banking regulation are standard and are applicable in all jurisdictions although with some variations here and there. A highlight of each of them is given below.

The first approach relates to information disclosure which is of two types. The disclosure to the general public through the announcement of operating results and full disclosure to bank supervisors where public disclosure may not be necessary in order to protect the clients' secrecy. Information disclosure by banks is basically designed to ensure that supervisors, depositors, investors and the general public are adequately informed of bank's performance/condition. The enforcement of adequate disclosure is paramount. The level of disclosure and timing of information to the various stakeholders should be articulated for banks to comply as a routine. This is an issue in Pillar III (Market Discipline) of the New Capital Accord.

The second approach is self regulation through the use of internal audit and controls, external audit and board audit committee. Self regulation involves the various independent checks and reviews put in place by the bank itself to ensure that its sound procedures do not deteriorate. Self regulation and self discipline are supposed to be more effective than regulation by a government agency because it is based on the conviction of self. It is also developed from industry norms; hence the stigma of non-compliance with peers and competitors are enough to encourage compliance. Basically in all banks, the primary responsibilities for safety and soundness, and prevention and detection of frauds and errors rest with the bank management.

Self regulation which is yet to be imbibed in emerging markets works in developed countries where market leaders impose market discipline. Self regulation normally fails due to competition or when market leaders themselves are weak. At such periods, self regulation becomes ineffective; indecision and self interest become a determinant.

The third approach is through banking supervision which is in two forms. The on-site examination is to ascertain the financial condition of a bank. It also aims at verifying the accuracy of the periodic reports of the banks sent to the Regulatory Authorities, analyzing those aspects of a bank that cannot be adequately monitored through off-site surveillance and confirming and ensuring compliance with laid down laws, rules and regulations. On-site examiners assess the quality of assets, management, earnings, capital and funds management as well as accounting and internal control systems.

The second form is off-site surveillance. The returns of banks to the Regulatory Authorities are analyzed by off-site supervisors for completeness, accuracy and consistency as well as compliance with prudential ratios and regulations. Regulatory Authorities, mainly in emerging markets, which do not have adequate resources rely more on off-site supervision to monitor the financial condition and performance of banks and to identify those banks that may need closer scrutiny. It is an irony of fate that where on-site examination should be emphasized due to low integrity of information from banks; resource constraints make such Regulatory Authorities to rely on off-site supervision. It is useful to add that on-site examination has been found to be more effective than off-site supervision in many jurisdictions due mainly to unreliable information that many banks do send to the Regulatory Authorities.

Finally, deposit insurance scheme is a financial guarantee scheme which seeks to protect depositors' fund against losses associated with bank failures. The scheme promotes a safe, sound and stable banking system. As a means to curtail moral hazard that deposit insurance could engender, the insured limit is always set at a low amount to ensure adequate protection of small savers for which the scheme is primarily designed. It is therefore, necessary for Regulatory Authorities to set up effective monitoring systems and increase punitive measures against the abuses in the system (Iyade, 2006)

2.1.5. Who Supervises Banks?

Banking crises, rapid structural change, and the continuing globalization of banking have led national and multilateral policy makers to focus increased attention on the crucial role of banking supervision. This focus is reinforced by the fact that "...one of the important (international) trends has been, and continues to be, a move away from regulation and towards supervision (Crockett, 2001). Policy discussions specifically focus on several issues that must be addressed in establishing and maintaining effective supervision, including who should supervise banks, i.e., the "structure" of bank supervision. Three issues for policy makers to address with respect to the structure of bank supervision are whether there should be a single bank supervisory authority, or multiple bank supervisors; whether the central bank should play a role in bank supervision; and whether the supervisor responsible for the banking industry should also have responsibility for

other financial services, in particular the securities and insurance industries. How these issues are addressed is important because policies that fail to provide for an appropriate bank supervisory framework may undermine bank performance and even lead to full-scale banking crises (Barth J., 2004).

2.1.5.1. Bank Supervisory Role of the Central Bank

Countries must also decide whether to assign responsibility for bank supervision to the central bank. As with the issue of single or multiple bank supervisors, the conceptual literature is split on the relative advantages and disadvantages of the central bank being a bank supervisor. Perhaps the most strongly emphasized argument in favor of assigning supervisory responsibility to the central bank is that as a bank supervisor, the central bank will have first-hand knowledge of the condition and performance of banks. This in turn can help it identify and respond to the emergence of a systemic problem in a timely manner.

Those pointing to the disadvantages of assigning bank supervision to the central bank stress the inherent conflict of interest between supervisory responsibilities and responsibility for monetary policy. The conflict could become particularly acute during an economic downturn, in that the central bank may be tempted to pursue a too-loose monetary policy to avoid adverse effects on bank earnings and credit quality, and/or encourage banks to extend credit more liberally than warranted based on credit quality conditions to complement an expansionary monetary policy.

As with the single-multiple bank supervisor debate, a useful first step in addressing the debate over the bank supervisory role of the central bank is to ascertain basic facts (Barth J, 2004).

2.1.6. Ways and Methods by which Regulatory Authorities Carryout Supervisory Functions in Banks

Supervisory authorities carry out their functions through bank examinations. Bank examination may be defined as the examination of the books and records of a bank for the purpose of ascertaining that the affairs of the bank are being conducted in a safe and sound manner with respect to: adequacy of capital, asset quality, board and management,

earnings, liquidity, adequacy of internal controls, adequacy of accounting system and record keeping as well as compliance with both the individual banks' internal policies and prudential regulations. To accomplish the task of examining banks, bank examiners use both off-site and on-site supervision to carry out their supervisory functions.

1. On-Site Supervision

On-site supervision of banks entails physical presence of regulators (NBE) in the financial institutions to evaluate their internal controls, compliance with the laws and regulations governing their operations with a view to determining their overall risk exposure. Emphasis is placed on their capital, asset quality of management, the strength of earnings and the adequacy of liquidity. On-site supervision is carried out by the Bank Examination Department of the regulatory bodies.

2. Off-Site Supervision

The off-site supervision of banks is carried out by the Banking Supervision Department and involves essentially the appraisal of banks returns. Essentially, it serves as an early warning device to detect a bank's emerging financial problem. This is accompanied by analyzing key bank financial ratios and other financial data that are generated from periodic bank financial reports that are submitted to the supervisor.

An off-site surveillance system can also contribute to a more efficient use of examiners' resources by giving priority to the examination of banks that are experiencing problems or which appear to be significantly increasing their risk exposure. The availability of off-site surveillance reports and analyses can help examiners to prepare for on-site bank examination by focusing attention on specific banks' operational areas that may require close supervision / attention. At the aggregate level, off-site surveillance system can be employed by bank supervision to monitor the financial condition and performance of the entire banking system. Off-site surveillance system typically focuses on a variety of key bank financial ratios covering such areas as earnings, asset quality, capital and reserves and liquidity.

3. Maiden Examination

This is usually carried out after six months of operations by a new bank to determine if the conditions and premises for granting of banking license by the regulator and the business objective of a bank are being pursued.

4. Routine Examination

This is the normal examination, currently carried out on a yearly basis to review the prudential operations, information-processing systems, foreign exchange operations and the anti-money laundering control of banks to determine the continued conduct of banking business in a safe and sound manner.

5. Target/Special Examination

This is usually carried out when serious issues of regulatory concern arise in bank, e.g. persistent illiquidity, lingering boardroom squabbles, deteriorating assets quality etc. In such a situation, the examination effort is concentrated primarily on the identified areas of regulatory concern.

6. Investigation/Spot Checks

These arise from the discovery of abnormal banking practices, complaints and petitions by the banking public and other stakeholders of issues bordering on unprofessional and unethical conduct by a bank (Iyade, 2006)

2.1.7. Conditions for Effective Banking Supervision

I. Sound and Sustainable Macro Economic Policy

Sound and sustainable macro-economic policy has been identified as a critical success factor in the application of the core principles for effective banking supervision, which set out the best practices in supervision worldwide.

II. Effective Market Discipline

Effective market discipline as a precondition requires that there exist a culture of financial transparency and the presence of good corporate governance. It is thus expected that bank lending decisions are carried out in strict commercial sense and without political pressure from the government. Banks are expected to operate credit risk thresholds that are driven strictly by the long term growth outlook and the safety and soundness of their institutions as the focus (Iyade, 2006).

III. Procedure for the Efficient Resolution of Problems in Banks

The core principles note the need for supervisory authorities to be vested with the power and authority required for effective distress resolution. Such distress resolution thresholds are expected to be flexible and robust in order to prevent contagion. That would require framework for early warning signals (EWS) and a holistic engagement of their thrusts. H. Onno Ruding, (2002) was of the view that strictness requires the setting of high standard of prudential guidelines to reduce the risks of individual banks or the entire banking system in a country from becoming illiquid or insolvent.

2.1.8. The roles of Regulatory Authorities in Bank Supervision

A. Macro-economic Policy and Data Transparency

The code on monetary and financial policies identifies desirable transparency practices for central bank in its conduct of monetary policy, and other financial agencies in their conduct of financial policies. It has been argued that monetary and financial policies can be made more effective if the public knows the goals and instrument of policies and if authorities make a credible commitment to meeting them (Iyade, 2006).

B. Institutional and Market Infrastructure

The enthronement of good corporate governance in financial systems, the need to improve the payment system, particularly in emerging market economies, and implementation of necessary anti-money laundering measures, are essential for the orderly conduct of any financial system.

Good corporate governance is essential for the development of a competitive private sector that in the long-term is able to attract and retain the domestic and international capital needed for investment. The Central Bank is strongly in favor of efforts to harmonize accounting practice internationally. Emphasis is also on the accuracy, reliability and timelessness of accounting information because these are considered fundamental for economic efficiency and financial stability.

The payment systems are essential mechanism supporting the effectiveness of financial markets. Disruption to a systematically important payment system could threaten the stability of markets both domestically and internationally. Thus, the core principles for a

systematically important payment system aim to enhance safety and efficiency in such a payment system (Iyade, 2006).

C. Financial Regulation and Supervision

As witnessed by recent financial crisis, weaknesses in the banking system of a country can threaten financial stability both within that country and internationally. In order to strengthen the banking system, the Basle Committee, developed a set of 25 core principles for banking supervision. Compliance with the principles is considered essential for any supervisory system to be effective. The core principles methodology sets out detailed guidelines for the assessment of compliance with the core principles by the central bank.

The central bank plays a prominent role in the development and implementation of the various key standards largely because of complementarities of the objectives of these standards and those of the central bank (Iyade, 2006).

2.1.9. The Debates and Current Evidence

2.1.9.1.Regulations on Bank Activities and Banking-commerce Links

There are five main theoretical reasons for restricting the degree to which banks can engage in securities, insurance, and real estate activities, or own nonfinancial firms. Indeed, it is these types of regulations that help define what observers mean by the term “bank.” First, conflicts of interest may arise when banks engage in such diverse activities as securities underwriting, insurance underwriting, and real estate investment. Banks, for example, may attempt to “dump” securities on or shift risk to ill-informed investors so as to assist firms with outstanding loans (John, John, and Saunders, 1994). Second, to the extent that moral hazard encourages riskier behavior by banks, they will have more opportunities to increase risk if allowed to engage in a broader range of activities [Boyd, Chang, and Smith (1998)]. Third, broad financial activities and the mixing of banking and commerce may lead to the formation of extremely large and complex entities that are extraordinarily difficult to monitor. Indeed, the former head of the International Monetary Fund, Michel Camdessus (1997), remarked that we are witnessing “... the development of new types of financial instruments, and the organization of banks into financial conglomerates, whose scope is often hard to grasp and whose operations may be

impossible for outside observers - even bank supervisors - to monitor.” Fourth, large institutions may become so politically and economically powerful that they become “too big too discipline.” Finally, large financial conglomerates may reduce competition and hence efficiency in the financial sector. According to these arguments, the government can ease market failures and thereby enhance bank performance and stability by restricting activities.

There are alternative theoretical reasons for permitting banks to engage in a broad range of activities, however. First, fewer regulatory restrictions on the activities of banks permit the exploitation of economies of scale and scope in gathering and processing information about firms, managing different types of risks for customers, advertising and distributing financial services, enforcing contracts, and building reputation capital with clients (Claessens and Klingebiel 2000). Second, fewer regulatory restrictions may increase the franchise value of banks and thereby augment incentives for banks to behave prudently. Third, broader activities may diversify income streams and thereby create more stable banks. Finally, the Shleifer and Vishny (1993) approach to regulation suggests that governments do not restrict bank activities to ease market failures. Instead, according to this view, regulatory restrictions promote government power, create a bigger role for corruption through the granting of exceptions to the rules, and thereby hinder bank performance and stability

2.1.9.2.Regulations on Domestic and Foreign Bank entry

Economic theory provides conflicting views on the need for and the effect of regulations on entry into the banking sector. Since banks play such an important role in an economy, widespread failures would reverberate throughout an economy with devastating effects. By effectively screening bank entry, governments can promote bank stability. Also, some researchers stress the naturally monopolistic role of banks. Petersen and Rajan (1994), in particular, demonstrate that banks with monopolistic power have stronger incentives to incur the necessary costs associated with overcoming informational barriers, which then facilitates the flow of credit to more worthy enterprises. Furthermore, banks with monopolistic power may possess considerable franchise value, which enhances prudent

risk-taking behavior (Keeley, 1990). Thus, there may be a 'helping-hand' role for the government in limiting destabilizing competition.

The Shleifer and Vishny (1993) approach to regulations provides a quite different perspective on regulating entry. While there may exist valid economic reasons for regulating entry, this view stresses the impact of such limits on facilitating corruption and impeding economic efficiency.

Politicians and regulators use entry restrictions to reward friendly constituents, extract campaign support, and collect bribes (Lopez-de-Silanes, and Shleifer, 2001). Furthermore, an open, competitive banking sector may be less likely to produce powerful institutions that unduly influence policymakers in ways that adversely affect bank performance and stability.

2.1.9.3.Regulations on Capital Adequacy

Traditional approaches to bank regulation emphasize the positive features of capital adequacy requirements (Dewatripont and Tirole 1994). Capital, or net worth, serves as a buffer against losses and hence failure. Furthermore, with limited liability, the proclivity for bank owners to shift toward higher risk activities decreases with the amount of capital at risk relative to assets (Lamoreaux 1994). With deposit insurance (implicit or explicit), official capital adequacy regulations play a crucial role in aligning the incentives of bank owners with depositors and other creditors (Furlong and Keeley 1989).

Researchers, however, disagree over whether the imposition of capital requirements actually reduces risk-taking incentives. Moreover, it is extraordinarily difficult if not impossible for regulators and supervisors to set capital standards that mimic those that would be demanded by well informed, undistorted private-market participants. For instance, Alexander and Baptista (2001), notes that actual capital requirements may increase risk-taking behavior. In amore guarded assessment, Thakor (1996) demonstrates the conditions under which risk-based capital requirements increase credit rationing, with negative implications for economic growth. Also, Thakor and Wilson (1995) argue that higher capital requirements may encourage borrowers to shift to capital markets and in the process impair capital allocation, while Gorton and Winton (1999) show that raising capital requirements can increase the cost of capital. Thus, theory provides conflicting

predictions on whether capital requirements curtail or promote bank performance and stability.

2.1.9.4. Supervision

Some theoretical models stress the advantages of powerful official regulators and supervisors. The line of reasoning essentially is as follows. First, banks are costly and difficult to monitor. Private agents may not have the ability or incentive to supervise banks and will attempt to free-ride. Thus, there will be too little monitoring of banks, which implies sub-optimal performance and stability. Official supervisors can ameliorate this market failure. Second, because of informational asymmetries, some argue that banks are prone to contagious and socially costly bank runs. According to the 'helping-hand' view, government supervision in such a situation can serve a socially efficient role. Third, since many countries choose to adopt a deposit insurance scheme, this situation: (1) creates incentives for excessive risk-taking behavior by banks, and (2) reduces the incentives for depositors to monitor banks. Thus, strong, official supervision will help prevent banks from engaging in excessive risk-taking behavior and thus improve bank performance and stability.

Alternatively, powerful government regulators and supervisors may exert a negative influence. Governments with powerful supervisory agencies may use this power to benefit favored constituents, attract campaign donations, and extract bribes. Powerful regulators/supervisors, according to this view, will be less focused on overcoming market failures and more concerned with currying political support and implementing their own narrow objectives. According to this so-called 'grabbing-hand' view, powerful supervision and regulation will be positively related to corruption and will not improve either bank performance or stability. In practice, policymakers and international institutions debate and make recommendations on a wide variety of bank regulatory and supervisory practices. In the area of supervisory resources and powers, countries assign very different priorities to bank supervision. (Levine R. 2002).

2.1.9.5. Regulations on Easing Private Sector Monitoring of Banks

Many supervisory agencies encourage private monitoring of banks. For instance, supervisory agencies may require banks to obtain certified audits and/or ratings from

international-rating agencies. Some countries make bank directors legally liable if information is erroneous or misleading. Some supervisory agencies compel banks to produce accurate, comprehensive and consolidated information on the full range of bank activities and risk-management procedures.

Furthermore, some countries credibly impose a “no deposit insurance” policy to stimulate private monitoring of banks. Over the years, some economists have advocated greater reliance on the private sector and expressed misgivings with official supervision of banks. For instance, Shleifer and Vishny’s (1993) “grabbing-hand” view of government regulations holds that banks will pressure politicians who, in turn, can unduly influence supervisors and regulators. Furthermore, in some countries, supervisors are not well compensated and hence quickly move into banking, resulting in a situation in which supervisors may face mixed incentives when it comes to strict adherence to the rules. Also, since supervisors do not have their own wealth invested in banks, they have different incentives than private creditors when it comes to monitoring and disciplining banks. Others, however, question placing excessive trust in private-sector monitoring, especially in countries with poorly-developed capital markets, accounting standards, and legal systems. Countries with weak institutional environments will benefit more from official supervisors and regulators containing excessive risk-taking behavior of banks and thereby instilling more confidence in depositors than would exist with private-sector monitoring.

2.1.9.6. Government Ownership of Banks

Economists hold sharply different views about the impact of government ownership of banks on financial and economic development (Shleifer, 2001). The statist or socialist view argues that government ownership of banks facilitates the mobilization of savings and the allocation of those savings toward strategic projects with long-term beneficial effects on an economy. According to this view, governments have adequate information and sufficient incentives to ensure socially desirable investments. Consequently, government ownership of banks helps economies overcome private capital-market failures, exploit externalities, and invest in strategic sectors. Lewis (1950), Myrdal (1968)

specifically advocates government ownership of banks to promote economic and financial development, especially in underdeveloped countries.

Shleifer and Vishny (1993), in contrast, argue that governments do not have sufficient incentives to ensure socially desirable investments. Government ownership tends to politicize resource allocation, soften budget constraints, and otherwise hinder economic efficiency. Thus, government ownership of banks facilitates the financing of politically attractive projects, but not necessarily economically efficient projects.

In an influential study, Shleifer (2001) piece together data on government ownership of banks from an assortment of sources. They find that countries with higher initial levels of government ownership of banks tend to have both slower subsequent rates of financial-system development and slower economic growth

2.2.Review of Empirical Studies

In contrast to the long theoretical recognition of regulation and supervision of banking industry, there had been very limited empirical evidence available until relatively recent times. Barth J., Caprio G., and Levine R. (2002) examined bank regulation and supervision: what works best? The paper uses a new database on bank regulation and supervision in 107 countries to assess the relationship between specific regulatory and supervisory practices and banking-sector development and fragility. Specifically, they examine (i) regulatory restrictions on bank activities and the mixing of banking and commerce; (ii) regulations on domestic and foreign bank entry; (ii) regulations on capital adequacy; (iii) deposit insurance system design features; (iv) supervisory power, independence, resources, loan classification stringency, provisioning standards, diversification guidelines, and prompt corrective action powers; (iv) regulations on information disclosure that foster private-sector monitoring of banks; and (v) government ownership of banks.

The results raise a cautionary flag regarding policies that rely excessively on direct government supervision of and regulatory restrictions on banks. The findings suggest that regulatory and supervisory practices that (1) force accurate information disclosure to

empower private-sector monitoring of banks and (2) create incentives for private agents to monitor banks work best to promote bank performance and stability.

Barth J, Caprio G, and Levine R (2003), study about Bank Regulation and Supervision: Lessons from a New Database based on the new database, they find that bank regulatory and supervisory practices that (1) require and enforce accurate information disclosure (2) empower private-sector corporate control of banks, and (3) foster incentives for private agents to exert corporate control work best to promote efficient bank intermediation and stability. Emerging evidence finds that, absent key supporting conditions, powerful bank supervisory agencies frequently exert a negative influence on bank performance. Existing research raises a cautionary flag regarding reform strategies that place excessive reliance on countries adhering to an extensive checklist of regulatory and supervisory practices that involve direct government oversight of and restrictions on banks.

Barth J., Gan J., Nolle D. (2004), examined Global Banking Regulation & Supervision: What Are the Issues and What Are the Practices? The past two decades have witnessed both tremendous change and tremendous growth in the financial sector in countries across the globe. At the same time, however, many countries in the world have experienced banking crises, sometimes leading to costly bank failures and overall disruption in economic activity. The changes in the banking landscape and banking crises have focused policy makers' and industry participants' attention on the appropriate role and structure of banking supervision and regulation. As countries make different choices in these regards, it is useful to inquire if there are fundamental principles countries can follow to insure financial system stability and growth. The paper does not presume to outline such principles, but it does take two necessary steps in that direction: first, it identifies basic issues in banking regulation and supervision; and second, it presents information on how countries around the globe have addressed these issues in their bank regulatory and supervisory schemes.

The study draws on recent research and detailed cross-country data, including data from a new World Bank survey of bank regulation and supervision worldwide, to focus on some of the underlying reasons for and implications of developments in a variety of areas.

These include the following: the nature and changing role of banks in promoting economic growth, development and stability; restrictions on the scope of banking activities and allowable ownership arrangements in which to conduct them; the structure and scope of bank regulatory and supervisory schemes; supervisory practices to promote safe and sound banks; market discipline and corporate governance in banking; international cooperation in regulation and supervision; offshore banking; potential disputes in banking arising from World Trade Organization membership, and deposit insurance schemes.

Iyade, (2006) examined the impact of regulation and supervision on the activities of banks in Nigeria (an assessment of the role of the CBN and NDIC). The study is an empirical analysis of the impact of regulation and supervision on the activities of Nigerian banks with emphasis on the role of the Central Bank of Nigeria and The Nigerian Deposit Insurance Corporation. It evaluates the roles and contributions of CBN and NDIC to the Nigerian banking sector. Extensive field survey with the sample of 500 respondents and library research was carried out and data collected were subjected to thorough analysis.

The analysis shows that the supervisory and regulatory framework of the Central Bank of Nigeria and the Nigerian Deposit Insurance Corporation are not sufficient to guarantee effective banking practices in Nigeria. Other findings from the study include the need to increase the maximum insurance coverage due to the effect of inflation and the persistent fall in the value of the Naira, the need to disclose transactions continuously to ensure financial prudence through regular supervision and monitoring of the financial health of local banks with the aid of the 'CAMEL' ratings and other supervisory framework.

There is need to also increase the awareness of banking activities within the general populace through a deliberate integration process aimed at demystifying certain inherent perceptions of the public with respect to distress and the role of the Nigerian deposit Insurance Corporation (NDIC). Moreover, the public, investors and depositors were not fully aware of the activities of NDIC and CBN in liquidating and revocation of banks' licenses due to the ineffectiveness of the enlightenment programs used in carrying out the awareness. The study focuses also on the consolidation agenda of the Central Bank of

Nigeria and the processes, prospect and the challenges of consolidation. A questionnaire and telephone based research was adopted for the study and the data collated was tested using the chi-square analysis and supported by fundamental evidence from the database of the regulatory authorities. Finally, the study offered suggestions as to how the problems so identified could be ameliorated

As far as the knowledge of the researcher there is no study conducted on the impact of regulatory and supervisory functions of NBE on the banking activities in Ethiopia. But, there is related study that conducted by Kassa (2010) on the Regulation & Supervision of Microfinance Business in Ethiopia. Until 1996, the provision of microfinance services in Ethiopia has been carried out mostly by donor funded programs through NGOs and government institutions. Most of the time a poverty lending approach was followed with subsidized interest rates. This practice has undermined loan collection performance leading to huge default and hence weakened the development of self sustaining MFIs. After 1996, however, a regulatory framework for Licensing and Supervision of MFIs was introduced, and as a result, most of the donor funded micro credit programs that were carried out by NGOs were transformed to be regulated institutions. The proclamation 40/1996 was issued in 1996 based on the limited microfinance experience which was prevailing at the time. In order to address various problems related with regulation and go with the development of the sector, the Government and National Bank of Ethiopia have been making effort to gradually improve the regulatory framework. The findings of this research paper suggest that the regulation and supervision of MFIs in Ethiopia brought many benefits. These are the following: The regulatory framework in Ethiopia has created an enabling environment for establishment of specialized formal financial institutions that provide financial service to those who were considered as un bankable, enabled MFIs to offer a wide range of products (for example credit, savings and money transfer etc.) and promoted standardization and transparency in the sector. In general, the regulatory and supervisory framework, in addition to other factors, has benefited the microfinance institutions in Ethiopia to show impressive performance in terms providing wide range of financial services including: extending credit, saving mobilization, money transfer and providing other related services to lower income section of the population.

Oladejo and Oladehinde .M (2011), study about Capital Regulation and the Performance of the Nigerian banks: Need for Review. The banking sector in any economy serves as a catalyst for growth and development and is therefore so sensitive and sacrosanct to the economy in term of stability and growth that must not be let loose by the Government. It is not surprising in the light of this fact, that governments the world over attempt to evolve an efficient banking system, not only for the promotion of efficient intermediation, but also for the protection of depositors, encouragement of efficient competition, maintenance of public confidence in the system, stability of the system and protection against systemic risk and collapse. Economists differ on the level of government intervention in the economy, particularly on regulation imposed on the financial intermediaries. While some believe that many regulations are necessary in order to protect the depositor's funds, other believes that the banks are over regulated. Therefore this paper seeks to explore various implications of capital regulation on the performance of the Nigeria banks with a view to proffer solutions to problems. The study adopts largely an exploratory methodology and submitted that though reforms of banks becomes necessary, there is a limit to which banks should be regulated on the issue of capital adequacy. The paper argued that consolidation arising from the recapitalization of banks brought about lots of problems that may mar the aim of the reform if not properly approached.

Ongena S., Popov A., and Udell G., (2011) study about Bank Lending Standards Abroad: Does Home-Country Regulation and Supervision Matter? The paper provides the first empirical evidence that bank regulation and supervision is associated with cross-border spillover effects through the lending activities of large multinational banks. You analyze business lending by 155 banks to 9,655 firms in 1,976 different localities across 16 countries. The finding of the paper is that more competition-friendly regulation, tighter restrictions on bank activities, and higher minimum capital requirements in domestic markets are associated with higher business lending to informational opaque firms abroad. The effects are stronger when banks are less efficiently supervised at home, and are observed to exist independently from the impact of host-country regulation.

2.3. Conclusions and knowledge Gap

The review of the literature reveals the existence of many gaps of knowledge in respect of regulation and supervision of banking industry and their relationship to regulation and supervision to the activities banking industry.

Radical reforms to the system of prudential regulation and supervision have been implemented since the late 1980s. These reforms are essential because the prudential system has proved ineffective in ensuring sound bank management, as the scale of financial distress among the state government and local banks indicates.

The banking system in any economy plays the important role of promoting economic growth and development through the process of financial intermediation. Development economists argue that the existence and evolution of financial institutions and markets constitute an important element in the process of economic growth. Banks worldwide are more regulated than other institutions because of their roles as financial intermediaries

The objectives of banking regulation and supervision were advanced by Giddy (1984) as for monetary policy, i.e. the ability of banks to create money through the extension of credit; credit allocation function of banks; the need to ensure competition and innovation by the prevention of cartels; and because banks are depositories of public savings and managers of payments mechanism, they are very vulnerable to collapse.

The protection of depositors has come to be generally accepted as the most basic reason for banking regulation and supervision. This objective is hinged on the fact that bank depositors have difficulty protecting their interests when compared to other bank creditors and investors. On his part, Sheng (1990) stated the objectives of supervision as: promotion and development of sound and wide range of financial services to meet the needs of the economy; ensuring efficiency, security and responsiveness of banks to the needs and complaints of customers; ensuring compliance with laid-down rules and regulations which are germane to ensuring high standards of banking; and to achieve important developmental and social goals through their compliance with monetary and credit allocation policies.

The major purpose of NBE as stated in National bank of Ethiopia establishment proclamation no.591/2008 is maintaining stable rate of price and exchange and fostering a healthy financial system. Banking supervision is one directorate that is responsible for supervising banks to ensure that the sector may not negatively affect the integrity of the Financial Sector and hence contributing to safe guarding of the whole economy. This is ensured through supervision of banks.

In Ethiopia the banking supervision consists of two components. The first one is the offsite and the second approach is on-site examination. The off-site surveillance in Ethiopia as done elsewhere in other countries relies on the continuous analysis of data reported to supervisory authority by banks themselves. Its main purpose is to provide a frequent depiction of the financial health and risk of each bank. During on-site examination, the Banking supervision staff physically visit the banks to check the accuracy of reports submitted to NBE and also assess the overall performance of the institution based on CAMEL approach. Therefore, the on-site examination helps NBE to have first hand information on compliance of prudential standards and performance of banks. The current on-site examination carried out by NBE is more of compliance checking and not risk based supervision. However, the NBE is now preparing itself to follow more of a risk based supervisory approach in examining the banks.

Generally, there is no best solution for regulating the banking business. Each regulatory consideration has to be adjusted to the exceptional situation in the country. One size fits all cannot be applied and no single model offers a universal remedy. Kassa, (2010) conducted the study on the regulation and supervision of Microfinance business in Ethiopia, challenges and prospects and the major finding that skills of Supervision staff in knowledge of efficient and effective regulatory and supervisory practices is low. As far as the knowledge of the researcher there is no research conducted on the banking supervision and regulation activities of NBE.

Chapter Three: The Overview of Financial System in Ethiopia

Major economic reforms have been taken by the Ethiopian government after the fall of the socialist government in 1991. Consequently, the Ethiopian Financial System has passed through significant reform process since 1992 as a part of transition from a planned to a market economy. Prior to this reform process, there had not been any competition within the financial sector due to the fact that all of the formal financial institutions were state owned and private financial institutions were not allowed to operate. After the implementation of the reform process starting from 1992, there have been significant measures undertaken by the government. The major reform measures taken include: Liberalizing and reforming the financial sector, relaxing foreign exchange controls, dismantling the administered interest rate regime, establishing a new regulatory framework for banks, insurance companies, microfinance institutions and cooperatives. The Ethiopian Financial system, generally speaking falls into three categories. These include: Formal, semi-formal and informal financial system. The formal financial system is a regulated sector, which is well organized and provides financial services mainly to urban areas. This formal financial system in Ethiopia is mainly composed of financial institutions such as banks, insurance companies and microfinance institutions. At the end of 2008/2009, there are 12 Commercial Banks (two government's owned), 1 government owned development bank, 12 insurance companies (one of which is government owned,) and 30 microfinance institutions (Kassa, 2010).

3.1.The Agents of Banking Supervision and Regulations

This section of the chapter discusses about the evolution, mandates and Principal role of the National Bank of Ethiopian.

3.1.1. The National Bank of Ethiopia

The principal role of a central bank in an economy is to nurture an efficient financial system through the application of appropriate instruments to influence the levels of the monetary and credit aggregates in the pursuit of low inflation, economic growth and balance of payments viability. In developing economies, central banks usually go beyond these traditional roles to engage in developmental activities in order to speed up the

economic development process and enhance the environment for the performance of their primary role.

3.1.2. Evolution of the National Bank of Ethiopia

The National Bank of Ethiopia was established in 1963 by proclamation 206 of 1963 and began operation in January 1964. Prior to this proclamation, the Bank used to carry out dual activities, i.e. commercial banking and central banking. The proclamation raised the Bank's capital to Ethiopian birr 10.0 million and granted broad administrative autonomy and juridical personality. Following the proclamation the National Bank of Ethiopia was entrusted with the following responsibilities.

- To regulate the supply, availability and cost of money and credit
- To manage and administer the country's international reserves.
- To license and supervise banks and hold commercial banks reserves and lend money to them.
- To supervise loans of commercial banks and regulate interest rates.
- To issue paper money and coins.
- To act as an agent of the Government.
- To fix and control the foreign exchange rates.

However, monetary and banking proclamation No. 99 of 1976 came into force on September 1976 to shape the Bank's role adoring to the socialist economic principle that the country adopted. Hence the Bank was allowed to participate actively in national planning, specifically financial planning, in cooperation with the concerned state organs. The Bank's supervisory area was also increased to include other financial institutions such as insurance institutions, credit cooperatives and investment-oriented banks. Moreover the proclamation introduced the new Ethiopian currency called 'birr' in place of the former Ethiopia Dollar that ceased to be legal tender thereafter.

The proclamation revised the Bank's relationship with Government. It initially raised the legal limits of outstanding government domestic borrowing to 25% of the actual ordinary

revenue of the government during the proceeding three budget years as against the proclamation 206/1963, which set it to be 15%.

This proclamation was in force till the new proclamation issued in 1994 to reorganize the Bank according to the market-based economic policy so that it could foster monetary stability, a sound financial system and such other credit and exchange conditions as are conducive to the balanced growth of the economy of the country. Accordingly the following are some of the powers and duties vested in the Bank by proclamation 83/1994.

- Regulate the supply and availability of money & credit and applicable interest and other changes.
- Set limits on gold and foreign exchange assets which banks and other financial institutions authorized to deal in foreign exchange and hold in deposits.
- Set limits on the net foreign exchange position and on the terms and amount of external indebtedness of banks and other financial institutions.
- Make short and long-term refinancing facilities available to banks and other financial institutions.

Moreover, the proclamation has also raised the paid-up capital of the Bank from Birr 30.0 million to Birr 50.0 million (www.nbe.gov.et).

3.1.3. Mandates of the National Bank of Ethiopia

National Bank of Ethiopia (NBE) has the following powers and duties:

- ✓ Coins, prints and issues the legal tender currency, and regulates the country's money supply.
- ✓ Regulates the applicable interest rate and other cost of money charges.
- ✓ Formulating implements and follows-up the country's exchange rate policy, and manages and administers the international reserves of the country.
- ✓ Licenses, supervises and regulates the operations of banks, insurance companies and other financial institutions.

- ✓ Sets limits on gold and foreign exchange assets, which banks, and other financial institutions authorized to deal in foreign exchange a hold in deposits.
- ✓ Sets limits on the net foreign exchange positions and terms, and the amount of external indebtedness of banks and other financial institutions.
- ✓ Provides short and long term refinancing facilities to banks and other financial institutions.
- ✓ Accepts deposit of any kind from foreign sources
- ✓ Promotes and encourages the dissemination of banking and insurance services throughout the country.
- ✓ Prepares periodic economic studies, together with forecasts of the balance of payments, money supply, prices and other relevant statistical indicators of the Ethiopian economy useful for analysis and for the formulation and determination by the Bank of monetary, saving and exchange policies.
- ✓ Acts as banker, fiscal agent and financial advisor to the Government.
- ✓ Represents the country in international monetary institutions and acts consistently with international monetary and banking agreements to which Ethiopia is a party.
- ✓ Exercises and performs such other powers and activities as central banks customarily perform (www.nbe.gov.et).

3.2.The Banking Regulatory Framework in Ethiopia

3.2.1. Objectives of Regulation and Supervision

As per National Bank of Ethiopia Establishment Proclamation no. 591/2008, its purpose is to maintain stable rate of price and exchange, and to foster a healthy financial system in the country. The banking institutions are a part of the formal financial system that are regulated and supervised by national bank of Ethiopia. The objectives of regulation and supervision of banks focus on the following:

1. Protecting Depositors
2. Ensuring Integrity and Stability of the banking sector in particular and Financial Sector in general
3. Promote Efficient Performance of the institutions

3.2.2. Key Principles Followed in Regulation and Supervision of Banking Institutions

Key Principles Followed in Regulation and Supervision of banking Institutions are the following:

- All supervisory decisions of the Bank shall primarily focus on the stability of the financial system and also consider safety and soundness of banks and protection of depositors.
- Prudential regulation focuses on type of transaction rather than the type of institution
- Efficiency: Negative effects of regulation should be minimized.
- Cost & benefit analysis: All regulatory & supervisory methods and practices should be cost effective.
- Degree of supervisory intervention of the Bank shall be in accordance with clear guidelines and commensurate with risk profile of banking industry and the expected benefits.
- The Bank shall increasingly use works of third parties like external auditors and actuaries for its supervisory work and endeavor to improve their performance standards.
- Key supervisory outputs of the Bank like examination reports shall pass through quality assurance and others.

The regulatory framework that governs the financial system in Ethiopia among others consists of National Bank of Ethiopia establishment proclamation no. 591/2008, licensing and supervision of Banking Business Proclamation No. 592/2008, licensing and supervision of Insurance business Proclamation No 86/1994 and licensing and supervision of Microfinance Business Proclamation No. 626/2009. National Bank of Ethiopia establishment proclamation no. 591/2008 has provided authority for NBE to set prudential standards for banking and other financial institutions. The proclamations are enacted by the parliament and secondary legislations or directives that govern the operation of financial institutions are issued by the central bank.

3.2.3. Important Feature of Proclamation No. 592/2008 and Directives issued by National Bank of Ethiopia

The Licensing and Supervision of Banking Business proclamation number 592/2008 and directives issued by NBE contain a comprehensive package of rules for licensing, registering and supervising banks. There are 28 directives issued by NBE that govern the operation of banking institutions. A detailed discussion of main components of the regulatory system in Ethiopia is as follows:

3.2.3.1. Definition of Banking Business

Licensing and supervision of banking business Proclamation No. 592/2008 defines banking business as " "bank" means a company licensed by the National Bank to undertake banking business or a bank owned by the Government; Article 2(1) of the proclamation.

3.2.3.2. Types of Activities that could be carried out by Banks

According to Article 2(2) of the aforementioned proclamation, Banks are allowed to carry out the following activities:

- a) Receiving funds from the public through means that the National Bank has declared to be an authorized manner of receiving funds;
- b) Using the funds referred to under paragraph (a) of this sub-article, in whole or in part, for the account and at the risk of the person undertaking banking business, for loans or investments in a manner acceptable by the National Bank;
- c) The buying and selling of gold and silver bullion and foreign exchange;
- d) The transfer of funds to other local and foreign persons on behalf of the banks themselves or their customers;
- e) The discounting and negotiation of promissory notes, drafts, bills of exchange and other evidence of debt;
- f) Any other activity recognized as customary banking business, which a bank engaged in the activities described from paragraph (a) to (e) of this sub-article may be authorized to undertake by the National Bank.

3.2.3.3.Entry Requirements

The regulatory framework (Proclamation No 592/2008 and directives issued by NBE) has defined entry requirements that have to be fulfilled by those who are interested to be engaged in banking business. The most important entry requirements include minimum capital requirement, institutional form, ownership restrictions, feasibility study and conditions to be fulfilled by Board of Directors.

A. Minimum Capital Requirement

According to the Directives number SBB/50/2011 the minimum capital requirement for establishing new Banks is Birr 500,000, 000 million which is approximately equivalent to US\$29,411,764 which shall be fully paid in cash and deposited in a bank in the name and to the account of the bank under establishment.

The minimum capital is often required for the purpose of registration and licensing of Companies. Globally, 103 economies still require entrepreneurs to put up a predetermined amount of capital before starting registration or licensing formalities. On the other hand 39 economies around the world have reduced or abolished their minimum capital requirement for the past seven years. Different countries require different amounts of minimum capitals. As observed by the World Bank, developed countries tend to request lower minimum capital than developing countries. In the Asia-Pacific region, Australia, New Zealand and Singapore do not require minimum capital. China, India, Indonesia, Mongolia and Uzbekistan have higher minimum capital requirement than other countries in the region (the World Bank, Doing Business 2011, p. 22). This high minimum capital requirement limits market competition because only a small group of individuals or companies can meet such requirement.

B. Institutional Form and Ownership Restrictions

The current regulatory framework requires banking institutions to be formed as share companies owned only by Ethiopian nationals. Foreign nationals are not allowed to invest in the financial sector, including in banking business. Most of the shareholders of the Banks are governments, associations, individuals.

C. Feasibility studies and other Licensing Requirements

Detailed licensing requirements are stipulated on proclamation no.592/2009 Article3 and on Directive number SBB/39/2006. Applicants are required to submit memorandum and articles of association, work plan (including major financial services to be offered, overview of economic condition of the area, cash flow and income statement and balance sheet projections) for the first year of operation and curriculum vitae and additional necessary documents of board of directors and chief executive offices. According to directive number SBB/39/2006, the chief executive officer must have a minimum of first degree or equivalent from a recognized higher institution of learning and minimum of 10 years experience in banking, of which, at a minimum, five years shall be in senior managerial position.

Members of Board of directors are required, at least seventy five percent of a bank's board members shall hold a minimum of first degree or equivalent from recognized higher learning institution; and the remaining board members should, at a minimum complete general secondary school to hold at least completion of high school education with the ability to read and grasp reports, especially financial statements. Qualification required for board of directors is lower than that of chief executive officer. In such a situation, the board can not be in a position to oversee and control the activities of the manager and hence it could negatively affect the performance of the institutions.

3.2.4. Ongoing Regulatory Requirements

3.2.4.1.Capital Adequacy

The principal objective of capital adequacy is to require institutions to have an adequate amount of capital to protect the interest of depositors, creditors and the public in general, and to ensure that institutions maintain capital standards that ensured financial solvency. Therefore, capital adequacy standards help to prevent insolvency of Banks and to ensure that the capital base can absorb unexpected losses and the risk inherent in banking business activities.

According to directive number SBB/9/95 the total capital of a bank consists of issued and fully paid in shares, legal reserves and other reserves to be approved by the National Bank of Ethiopia. The minimum capital requirement shall be applied to a bank on a

consolidated basis, including subsidiaries and affiliates engaged in banking and financial activities.

3.2.4.2.Liquidity Requirement

In Ethiopia according to directive number SBB/44/2008 any licensed bank shall maintain liquid assets of not less than 25% (twenty five percent) of its total current liabilities. For the purpose of meeting the liquidity requirement, each bank shall maintain, at least twenty percent (20%) of the current liabilities in the form of primary reserve assets; and five percent (5%) of the current liabilities in the form of secondary reserve assets. The main objective of the liquidity requirement is to ensure that banks maintain an adequate level of liquidity to meet all known and unexpected obligations and hence promotes public confidence.

3.2.4.3.Branching Requirements

According to directive number SBB/40/2006 the current regulatory framework of banks allows every licensed bank shall obtain prior authorization from the National Bank to open a branch office. A bank planning to open a branch shall submit a duly completed application attached to these directives together with a covering letter to the Bank and shall pay the fee Birr 500 (Birr five hundred) for each branch. A bank authorized to open a branch shall open the said branch and commence operation within 6(six) months from the date of the grant of authorization and shall notify the Bank the date it plans to commence operation in the new branch 15 (fifteen) days before the planned date of commencement of operation.

Before commencing operation a bank authorized to open a branch shall fulfill the following:

- Ensure that the bank's relevant policy and procedure manuals, and NBE directives are distributed to appropriate staff members of the branch to be opened;
- Ensure that the branch is adequately guarded;
- Display in a visible area of the branch working hours, copy of the bank's license and branch authorization;

- Ensure that the banking hall and staff operating area are suitable for the type of business to be undertaken in the premises housing the branch include

3.2.4.4.Frequency and Content of Reporting

According to the directive number SBB/21/96 Reports shall be submitted to the Supervision Department of the National Bank of Ethiopia within twenty days after the end of the period for which the data are reported.

3.2.4.5.Restriction on Investment

According to banking Proclamation number 84/1994, no bank shall engage in insurance business but may hold up to 20% in an insurance company and up to a total of 10% of the banks equity capital in such business. Banks are prohibited from engaging directly in non-banking businesses such as agriculture, industry, and commerce. A bank may hold shares in a non-banking business only up to 20% of the company's share capital and total holdings in such business shall not exceed 10% of the bank's net worth.

A bank's equity participation in another bank shall be subject to prior authorization by National Bank of Ethiopia and no bank shall commit more than 20% of its net worth in real estate acquisition and development other than for own business premises with out prior approval of the National Bank of Ethiopia. A bank may not invest more than 10 % (ten percent) of its net worth in other securities. The aggregate sum of all investments at any one time (excluding investment in government securities) may not exceed 50% of the bank's net worth, with out prior approval by the National Bank of Ethiopia. Dealing in securities shall be done by banks only through a limited liability subsidiary company wherein the holding of the bank shall not exceed 10% (ten percent) of its equity capital.

3.2.4.6. External Audit Report

It is stipulated in Proclamation number 592/2008 (banking business proclamation) that financial statements of the banks should be audited by an independent auditor acceptable to the central bank prior to the payment of dividend to shareholders. Independent auditor appointed line with Article 370 of the Commercial Code of Ethiopia, every licensed bank shall annually apply to the National Bank of Ethiopia for approval of the appointed independent auditor and the auditor, his partners or associates do not operate an account or have not been granted any type of facilities in the bank except in the normal course of

business and at arm's length. According to Directive no SBB/19/96/, banks are required to submit external audit report to the central bank annually at end of its financial year.

3.2.4.7. Penalty convince

According to banking proclamation no.591/2008 any bank that fails to comply with the requirements of any of the Directives of the National Bank of Ethiopia, shall be subject to a penalty of Birr10,000 (ten thousand Birr) for each violation. The National Bank of Ethiopia may, in addition to the penalty indicated above, take any other measures it considers necessary. It waives the penalty on grounds that it considers to be reasonable.

3.2.5. Supervisory Approach and its Performance in Ethiopia

The major purpose of NBE as stated in National bank of Ethiopia establishment proclamation no. 591/2008 is maintaining stable rate of price and exchange and fostering a healthy financial system. Banking supervision is one directorate that is responsible for supervising banks to ensure that the sector may not negatively affect the integrity of the Financial Sector and hence contributing to safe guarding of the whole economy. This is ensured through supervision of banks.

3.2.5.1. Supervisory Methodology of Banks and its performance in Ethiopia

In Ethiopia the banking supervision consists of two components. The first one is the offsite and the second approach is on-site examination.

3.2.5.1.1. Off-site Surveillance

The off-site surveillance in Ethiopia as done elsewhere in other countries relies on the continuous analysis of data reported to supervisory authority by banks themselves. Its main purpose is to provide a frequent depiction of the financial health and risk of each bank.

The NBE, for off-site monitoring and surveillance of banks, requires quarterly reports that show the financial condition of banks. The off-site returns that should be submitted by banks include: income and expense statement, balance sheet, capital adequacy report, liquidity report, loan status and provisioning reports. In order to carry out the off-site surveillance, a data base is established at Banking Supervision Department. The overall

financial condition of financial institutions is determined based on analysis and evaluation of capital adequacy, asset quality, earning and Liquidity. Quarterly off-site reports with key findings in above areas are produced and are submitted to senior policy makers to inform them about on-going view of banks soundness in key financial areas (Kassa, 2010).

3.2.5.1.2. On-site Examination

During on-site examination, the Banking supervision staff physically visit the banks to check the accuracy of reports submitted to NBE and also assess the overall performance of the institution based on CAMEL approach. Therefore, the on-site examination helps NBE to have first hand information on compliance of prudential standards and performance of banks. The current on-site examination carried out by NBE is more of compliance checking and not risk based supervision. However, the NBE is now preparing itself to follow more of a risk based supervisory approach in examining the banks.

The duration period for completion of on-site examination varies with the size of the banks and type of examination (Full-scale, special or follow up examination). Since there are large numbers of banks (18)¹ when compared with the number of banking Supervision staff, the directorate has not been able to supervise the banks at least once on annual basis.

Currently, the national Bank of Ethiopia is implementing Business Process Re-engineering study to radically enhance its regulatory and supervisory practices and performance. The current supervisory practice of the bank has been relying basically on historical performance of the banks. However, the bank has now finalized all preparations to introduce risk based supervision approach which concentrates an assessment of banks capability to manage current and future risks.

NBE has conducted a stock taking analysis of risk management practices in banking institutions. In addition, NBE has issued draft risk management guideline for banks. This

¹ Obtained from the access capital review (2010), twelve of Ethiopia's private banks (Abyssinia, Awash, Berhan, Bunna, CBO, Dashen, Lion, NIB, OIB, United, Wegagen, and Zemen) and entry of six new banks (Abay, Enat, Hawassa, Debub Global, Noah, Zam-Zam).

risk management guideline tries to convey to the banking industry what framework NBE expects institutions to have in place to manage the various types of risk with which they are faced. Banks are expected to send their risk management program which will enable NBE to review what institutions propose or already have in place to manage the risk with which they are faced. Subsequent work and actions will also be carried out to effectively introduce risk based supervision (Kassa, 2010).

Chapter Four: Research Design and Methods

Research designs are plans and the procedures for research that span the decisions from broad assumptions to detailed methods of data collection and analysis. This plan involves several decisions, and they need not be taken in the order in which they make sense to me and the order of their presentation here. The overall decision involves which design should be used to study a topic. Informing this decision should be the worldview assumptions the researcher brings to the study; procedures of inquiry (called strategies); and specific methods of data collection, analysis, and interpretation. The selection of a research method is also based on the nature of the research problem or issue being addressed, the researchers' personal experiences, and the audiences for the study (Creswell, 2003). The purpose of this chapter is to present the research questions and objectives, the underlying principles of research design and the choice of the appropriate research method for the study. The chapter is arranged as follows. Section 4.1 presents the research questions and objectives of the study. This is followed by the research method to be adopted in the study in section 4.2. Finally, the summary of the research design were presented in section 4.3.

4.1. Research Questions and objectives of the study

As already shown in the first chapter, the intent of this study was to assess the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banking industry. In order to achieve this broad objective three research questions and six specific objectives have been developed.

The researcher were developed the following research questions:

1. Why is it mandatory for banks to be overtly regulated by National Bank of Ethiopia (NBE)?
2. Has the Ethiopian banking industry become safe, stable and command the confidence of the general public?
3. Have the activities of banking supervisions brought about normal banking practice, professionalism and ethical conduct in the Ethiopian banking industry system?

In addition the following specific objectives were developed:

- To examine thoroughly how supervisory and regulatory functions of the regulators (NBE) impacts on the Ethiopian private banks
- Assessing the effectiveness of the regulation and supervision in the Ethiopian banking industry
- To examine regulatory and supervisory activities of the NBE have boosted depositors' confidence in the Banking System.
- To assess the on-site and off-site supervision activities of NBE
- To evaluate the minimum capital requirement for establishing new Banks
- To assess the investment activities restriction of private banking industry in Ethiopia

4.2.Method Adopted

Research methods are specific technique or methods of data collection and analysis used to achieve the broad objective through addressing research question and specific objective.

The purpose of this study is to examine impact of regulatory and supervisory functions of National Bank of Ethiopia on the activities of Ethiopian private banking industry. A research design refers to the plan of action that links the philosophical assumption to specific methods. To address the research questions and to achieve the specific objective, both quantitative and qualitative research approaches (mixed research approach) were used. Mixed method research involves both collecting and analyzing quantitative and qualitative data. Quantitative data includes closed- ended information such as that found on attitude, behavior, or performance instruments. In contrast, qualitative data consists of open - ended information that the researcher gathers through interviews with participants. The mixing of data is a unique aspect of the mixed methods research. By mixing the datasets, the researcher provides a better understanding of the problem than if either dataset had been used alone. In addition mixed methods research approach provides strengths that offset the weaknesses of both quantitative and qualitative research.

Mixed method research approach has three general strategies that is sequential mixed method, Concurrent mixed method and transformative mixed methods. From those strategies the researcher used concurrent mixed method. The researcher converges or merges quantitative and qualitative data in order to provide a comprehensive analysis of the research problem. In this design, the investigator collects both forms of data at the same time and then integrates the information in the interpretation of the overall results.

For quantitative data the researcher were used cross sectional survey. A cross-sectional survey collects data to make inferences about a population of interest (universe) at one point in time. Cross-sectional surveys have been described as snapshots of the populations about which they gather data (Creswell, 2003). Cross-sectional surveys are useful in providing an overall estimate of prevalence and coverage in a geographic area. The researcher used Self-administered questionnaires for the banks head office employees and banking supervision department employees of NBE.

For qualitative data the researcher was conducts face-to-face interviews with participants. These interviews involve unstructured and generally open-ended questions that are few in number and intended to elicit views and opinions from the participants.

The following section, thus, discusses consecutively the quantitative and qualitative aspects of the research method and also discuss about the source of data and methods of data analysis.

4.2.1. Quantitative Aspect of the Research Method

Quantitative research method used to answer question about relationships among measured variables with the purpose of explaining, predicting and controlling phenomenon. Quantitative studies represent the mainstream approach to research and structured guidelines exist. Variables, hypotheses and methods of measurement tend to be defined before the study begins and remain the same throughout. Even if there are two strategy of inquiry i.e. survey and experimental under quantitative approach, this study were used a survey design. "Survey research involves acquiring information about one or more group of people perhaps about their characteristics, opinions, attitudes, or previous

experiences-by asking them questions and tabulating their answers. The ultimate goal is to learn about a large population by surveying a sample of that population.” (Leedy and Ormord, 2005 p183).

The purpose of survey research is to generalize from the sample to the population so that inferences can be made about some characteristic, attitude or behavior of the population (Creswell.2009). The researcher selects survey design because of budget and time constraint i.e. economy of the design. The data collection included self administered questionnaires.

4.2.1.1.Sampling Design

According to Asika (1991), the population of a research study is defined as the census of all items or objects that possess the characteristic or that have the knowledge of the phenomenon being studied.

The sampling techniques can broadly be divided as probability sampling and non-probability sampling. Probability sampling includes: Simple Random Sampling, Stratified Random Sampling, Proportional Random Sampling, Cluster Sampling, and Systematic Sampling. Non-Probability Sampling includes: Convenience or Accidental Sampling, Quota Sampling, and Purposive Sampling (Leedy and Ormrod, 2005).

The sample frame was the twelve Ethiopian private banks namely Abyssinia, Awash, Berhan, Bunna, Cooperative Bank of Oromiya (CBO), Dashen, Lion, Nib International Bank (NIB), Oromiya International Bank (OIB), United, Wegagen, and Zemen banks that are registered by NBE and under the operation on the current year and the study also include NBE under the sample frame.

From the sample frame six Ethiopian private banks specifically Awash, Dashen, Abyssinia, Wegagen, United, Nib International Bank was selected. The rational behind for the selection of those banks is that they operate more than a decade under the regulation and supervision of National Bank of Ethiopia (Banking Sector Review 2010). And from the NBE the researcher were selected purposively banking supervision

department. The rational behind for the selection is that the issue is more concern the banking supervision department.

For the study the researcher was use non probability sampling design. From the non probability sampling design the researcher particularly were used purposive sampling for the distribution of questionnaires to the head office employees of the six selected private banks and banking supervision department of NBE. Purposive sampling the researcher selects the sample on his particular purpose for instance the researcher may choose people who represent diverse perspective and knowledge on the issue (Leedy and Ormrod, 2005). According to Diamantopoulou and Schlegelmilch (2000) purposive sampling is used when sample members are chosen with specific purpose or objective in mind. The rational behind for the selection of purposive sampling because of the issue is not concern all bank employees and officials.

The sample selection form the head office employees of the six private banks based on the following process: The head office of each bank has top management and middle management. The top management is defined to include: president (CEO), corporate planning and development, senior risk management advisor, controller, vice president system and resource management, area bank coordinator, executive secretary and vice president operations management, whereas, that of middle management comprises information technology head, engineering and building administration head, fund management and accounts head, human resource and logistics head, credit department head, legal department head, international banking head and payment card head.

Selecting respondents from the two hierarchies has mainly taken nature of the business, the exposure of the domains to the business and the degree of exposure to the legal and regulatory issues is taken into consideration. The banking business in its very nature is professional, skill intensive and managerial rank sensitive. The other rationale for taking the sample was time and budget constraints.

Sample size is determined by time and budget of the researcher. Because of time and budget constraint, the sample was restricted to head offices residing in Addis Ababa.

According to NBE (2008) all head offices of banks which operate in Ethiopia found in Addis Ababa.

The sample selection from NBE, the researcher was selected purposively the banking supervision department. The rational for selection is that the issue is more concern banking supervision department. The total employees of this department are 29. Based on this the researcher was included all employees of the department under the study.

Based on the above purposively selected respondents, the sample size for self-administered questionnaires were 125 respondents which comprised of head office employees of the six selected private banks and banking supervision department staffs of the NBE delivered physically to all targeted categories. As it has been explained by Fowler J. (2002) that the larger the sample size the smaller the error will be in estimating the characteristic(s) of the whole population but the more it will cost to administer a survey and analyze the data therefore, the sample size were limited to 125 employees because of insufficient cost to administer the survey. The researcher believes that the sample size is sufficient to make sound conclusion about the population. As Fowler J. (2002) stated that the absolute size of a sample is the crucial factor rather than the relative size or the proportion of the population sampled.

The distribution of 125 questionnaires are as follows: out of 125 questionnaires 96 questionnaires were distributed on the head office employees of the six selected privet banks and the researcher were give equal chance for the six banks head office. Based on this, 96 questionnaires divided by the number of banks i.e. six private banks equals to 16 questionnaires were distributed to each six selected Ethiopian private bank head office particularly to the top and middle management of the above listed department head. As already stated in the above the banks have eight top management and eight middle management based on this out of the sixteen questionnaires eight questionnaires were distributed to top management and the remaining eight questionnaires were distributed to the middle management. Therefore, sixteen questionnaires' times by number of banks i.e. six private banks equals to 96 questionnaires were distribute to head office employees of

the six banks. The remaining 29 questionnaires were distributed to banking supervision department employees of NBE because as stated in the above the total population of banking supervision department employees of NBE are 29 and all are included under the study.

Table 4.1

The Distribution of Survey Questionnaires in Tabulated form to the six private Banks Head Office Employees

Banks	Location of Head office	Number of questionnaires distributed to top management	Number of questionnaires distributed to middle management	Total Number of questionnaires to be distributed
Awash International Bank	Addis Ababa	8	8	16
Bank of Abyssinia	Addis Ababa	8	8	16
Dashen Bank S.C	Addis Ababa	8	8	16
Nib International Bank	Addis Ababa	8	8	16
United Bank	Addis Ababa	8	8	16
Wegagen Bank S.C	Addis Ababa	8	8	16
Total		48	48	96

4.2.1.2. Survey Instrument

To address the research problem using a survey method the researcher was use self administered structured questionnaires. With respect to questionnaire design Saunders et al. (2007) indicted that the validity and the reliability of the data collected depend, to a large extent, on the design and the structure of the questionnaire. In this study, the questionnaire were adapt from Iyade, (2006) and some questions were developed by the researcher by taking some ideas that help to develop the questionnaire from regulation and supervision of banking industry research journal article and regulatory reform survey report. The questionnaire compromised structured questions which made it easy for the respondents to indicate their views. It also five-point likert scale ranging from “strongly disagree=1”, to “strongly agree=5” questions were used. This enables respondents to indicate their opinion on various issues of the regulatory and supervisory functions of NBE and its impact on the activities of Ethiopian private banking industry.

Due to its low cost requirement and not consume much time to be answered by the respondents self-administered closed ended questionnaire were use. Also it is quicker to administer by the researcher but, if questions are wording and unclear and if respondents are not literacy, its response rate is low.

This survey instrument was prepared in one language i.e. English language by taking in to account the background and the level of education of the respondents. Self administered questionnaire had two parts; the first part were comprised of demographic profile of respondents including category of bank staff, level of education, gender, and number of years of experience and the second part were comprised of questions in relation with the study area which were problem related with regulation and supervision of National Bank of Ethiopia (NBE).

The 125 self-administered questionnaires were delivered by hand to each respondent and collected later (delivery and collection of questionnaires). These questionnaires were answered by the head office employees of the six private banks specifically Awash, Dashen, Abyssinia, Wegagen, United, Nib International Bank and banking supervision

department employees of NBE. The questionnaires aimed to inquire into the participants' personal opinion about the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banking industry.

4.2.2. Qualitative Aspect of the Research Method

Qualitative approach to research is concerned with subjective assessment of attitudes, opinions and behavior. It is one in which the inquirer often makes knowledge claims based primarily on constructive perspective (i.e., the multiple meanings of individual experience meaning socially and historically constructed, with an intent of developing a theory or pattern) or advocacy/ participatory perspectives (i.e., political, issues oriented, collaborative, or change oriented) or both. It also includes strategies of inquiry such as narrative, ethnographies, grounded theory studies, or case studies (Creswell, 2003).

Kvale (1983, p.174) defines the qualitative research interview as "an interview, whose purpose is to gather descriptions of the life-world of the interviewee with respect to interpretation of the meaning of the described phenomena". Collecting these descriptions can be done in several ways, of which face-to-face interviews are the most common.

It is also an opportunity to gain insight in to how people interpret and order the world (Milena, 2008). In depth interviewing is a qualitative research technique that involves conducting intensive individual interviews with a small number of respondents to explore their respective on a particular idea, program, or situation (Boyce and Neale 2006).

The purpose of these qualitative interviews was to probe in more depth some of the issues arising from the quantitative survey and to have an insight on the study issue. As a result of the above reasons the researcher conduct an in-depth face-to-face interview method with unstructured questions.

Interviews were conducted with randomly selected from NBE banking supervision department employees on the research topic. From the total population of 29 employees of banking supervision departments of NBE the researcher was select randomly 8 employees for interview, the rational for selection of simple random because of it gives

equal chance for respondents and their responses was very helpful to the final outcome of the study.

In relation with instrument, unstructured face to face interview were used because of its flexibility, high response rate and also allowing new questions to be brought up during the interview.

4.2.3. Sources of Data

To ensure the reliability of the information resulting from the research, the researcher was used both primary and secondary sources of data.

4.2.3.1. Primary Data

Primary sources are the materials on a topic upon which subsequent interpretations or studies are based, anything from firsthand documents such as poems, diaries, court records, and interviews to research results generated by experiments, surveys, ethnographies, and so on. Primary sources are records of events as they are first described, without any interpretation or commentary. They are also sets of data, such as census statistics, which have been tabulated, but not interpreted. Primary data has the advantage of giving the researcher the opportunity to conduct an unbiased and extensive study on the research problem set out to solve (Iyade, 2006).

For the purpose of the research, the following primary data collection techniques were used:

- ✓ **Questionnaires:** A structured questionnaire is the one, which contains a series of questions and it has the advantage of presenting questions in sequence. It standardizes the research instruments and equally removes the chances of the respondent tele-guiding the researcher.
- ✓ **Face-to-face interview:** Interviews will be conducted with banking supervision department employees of national bank of Ethiopia on the research topic. The rational behind using of interview are the researcher is able to adapt questions (re frame) and clarify doubts. Also the researcher can pick up nonverbal clues such as

body language in order to observe the interviewee's personal traits and behavioral patterns.

4.2.3.2.Secondary Data

Secondary sources, on the other hand, offer an analysis or a restatement of primary sources. They often attempt to describe or explain primary sources. Some secondary sources not only analyze primary sources, but use them to argue a contention or to persuade the reader to hold a certain opinion.

Textbooks, journals, proclamation, and declaration were use for the theoretical frame work of the study.

In order to access this information, data were collected from the following information centers:

- A. The National Bank of Ethiopia website (www.nbe.gov.et)
- B. The University of Addis Ababa Library
- C. The use of the internet downloaded materials
- D. Materials from the print media

4.2.4. Method of Data Analysis

Quantitative data from the questionnaires were analyzed using descriptive statistics. This enables the researcher to make comparison between of the perception of the banking sector. The rational to use this descriptive statistics is to describe the basic feature of the data in a study and to provide summaries about the sample and statistical package for social science (SPSS) tool were used.

Further, data collected from in-depth interview was transcribe in to word document and analyzed through triangulating with data collected through questionnaire and make argument i.e. the opinion of majority of interviewees forward is used for argument by supporting the result of the questionnaire.

4.3.Summary of the Research Design

In general, this chapter discussed and provides explanation about the research design and signifies the research approach and specific methods used in the study. The discussion on the research design has been comprised of the three research approach namely, quantitative, qualitative and mixed approach. For those specific method used, sample design that includes sample frame, sample size, sampling procedure, data collecting instrument, source of data and data analysis method also identified.

For the study, mixed approach were adopted and the researcher incorporated two sources of data for both methods those were self administered closed ended questionnaire quantitative aspect of the method and face-to-face interview for qualitative aspect of the method.

The research sampling frame is the twelve Ethiopian private banks namely Abyssinia, Awash, Berhan, Bunna, Cooperative Bank of Oromiya (CBO), Dashen, Lion, Nib International Bank (NIB), Oromiya International Bank (OIB), United, Wegagen, and Zemen banks that are registered by NBE and the sample frame also include NBE. Out of the sample frame six private banks specifically Awash, Dashen, Abyssinia, Wegagen, United, Nib International Bank was selected. The rational for the selection is that they operate more than decade under the regulation and supervision of national bank of Ethiopia (Banking sector review 2010). From NBE banking supervision department were selected. The rational behind for the selection is that the issue is more concern the banking supervision department and all employees of the banking supervision department employees of NBE included under the study.

In the study non-probability purposive sampling for the selection of respondents from the six private bank head office and from NBE were used. The research was employed both survey and face-to -face interview. The researcher was use survey method for the bank head office employees and banking supervision department employees of NBE. 125 structured self- administered questionnaires were distributed to bank head office employees of the six private banks and banking supervision department employees of

NBE. With regard to in-depth interview the researcher were conducted interview with randomly selected 8 baking supervision department employees of NBE. The data collected from questionnaire were analyzed through descriptive analysis technique and then triangulated and supported by data to be collect through interview. Further, this in-depth interview was corroborated survey questionnaires results and address research questions and to achieve the broad objective.

Chapter Five: Data Presentation and Analysis

The major objective of this study is to assess the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banking industry. This chapter involves the presentation and analysis of data gathered from the questionnaires which were administered on the sample selected and interview result. For the analysis, tables, and percentage were used. The statistical tool adopted was opted for because it allows for effective understanding and interpretation of results. Furthermore, in order to reduce the bulkiness of data the data analyzed are those that are considered relevant to the problems, Objectives and research question of this research work.

5.1. Survey Results

The questionnaires which were designed to get the respondents' views on a number of issues relating to an assessment of the regulatory and supervisory impact of the NBE in relation to the activities of Ethiopian private banks were administered to the two units of the sample population. These are six purposively selected private bank head office staff and banking supervision department employees of NBE. A summary of the questionnaires to each category of respondent and the response rate is presented in Table 4.1 and the summary of demographic profile of the respondent is presented in Table 4.2.

Table 5.1

Percentage Distribution of Returned Questionnaires by Respondents

Category of respondents	Administered	Returned/ completed	Percentage %
Awash International Bank head office	16	11	68.75
Bank of Abyssinia head office	16	13	81.25
Dashen Bank S.C head office	16	8	50
Nib International Bank head office	16	12	75

United Bank head office	16	9	56.25
Wegagen Bank S.C head office	16	12	75
Banking supervision department employees of NBE	29	24	83
Total	125	89	71.2

Source: survey result

From the table above, it can be seen that a total of 125 questionnaires were administered but only 89 or 71.2% was completed and returned. The average response rate of 71.2% or 89 questionnaire was considered adequate for the analysis. It is considered that a response rate of anything over 30 percent in a survey is acceptable (Fowler J., 2002).

Table 5.2

Demographic Profile of the Respondent

Variable	Classification of variable	Frequency	Percentage
Level of education	A. Diploma	8	8.9
	B. Bachelor degree	77	86.5
	C. Masters	4	4.5
	D. Other (specify)	0	0
Sex	A. Male	61	68.5
	B. Female	28	31.5
Number of years of experience	A. <1year	4	4.5
	B. 1-5 year	53	59.5
	C. 5-10 year	20	22.5
	D. > 10 year	12	13.5

Source: survey result

5.1.1. Respondents' Assessment of the Impact of Regulation and Supervision on the Ethiopian Private Banks activities

In order to assess the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banking industry, the degree of respondents' opinion was

sought using a five-point likert scale statements and the degree of their answers measured on the following scale as shown below:

- Strongly disagree (1)
- Disagree (2)
- Neutral (3)
- Agree (4)
- Strongly agree (5)

A. Effectiveness of regulatory and supervisory framework of NBE

Q1: The supervisory and regulatory framework of NBE is very effective in Ethiopian banking system

N Valid	89
Missing	36
Mean	3.5169
Median	4.0000
Mode	4.00

Table 5.3

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	2	1.6	2.2	2.2
	disagree	16	12.8	18.0	20.2
	neutral	15	12.0	16.9	37.1
	agree	46	36.8	51.7	88.8
	strongly agree	10	8.0	11.2	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The summary of responses in Table 5.3 shows that 10 (11.2%) of the respondents strongly agreed that the supervisory and regulatory framework of NBE is very effective

in Ethiopian banking system, 46 (51.7%) agreed; 2 (2.2%) strongly disagree; 16 (18.0%) disagree while 15 (16.9%) of the respondent were indifferent. When this value is described in terms of mean, the mean value of the respondents' response is 3.5 it approaches to agree. The breakdown analysis shows that the supervisory and regulatory framework of NBE is very effective in Ethiopian banking system.

Q2: the stability in the banking system was as a result of effective regulation and supervision by the national bank of Ethiopia (NBE)

N	Valid	89
	Missing	36
Mean		3.5281
Median		4.0000
Mode		4.00

Table 5.4

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	3	2.4	3.4	3.4
	disagree	14	11.2	15.7	19.1
	neutral	18	14.4	20.2	39.3
	agree	41	32.8	46.1	85.4
	strongly agree	13	10.4	14.6	100.0
Total		89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The responses in Table 5.4 try to affirm whether the stability in the banking system was as a result of effective regulatory and supervisory functions of the NBE in Ethiopia banks. From the responses, 13 (14.6%) of the respondents strongly agreed, 41 (46.1%) agreed, 3 (3.45%) strongly disagree and 14 (15.7%) disagreed while those that were neutral are 18 representing (20.2%). In terms of mean, the response for question no.2 has

a mean value of 3.528 which approach to agree. The break down indicates that most respondents believe that the stability in the banking system was a result of effective regulatory and supervisory functions of the NBE.

Q3: The performance rating of NBE in controlling banks’ activities is very high.

N	Valid	89
	Missing	36
Mean		3.6404
Median		4.0000
Mode		4.00

Table 5.5

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	2	1.6	2.2	2.2
	disagree	6	4.8	6.7	9.0
	neutral	24	19.2	27.0	36.0
	agree	47	37.6	52.8	88.8
	strongly agree	10	8.0	11.2	100.0
Total		89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

Table 5.5 shows that the performance rating of NBE in controlling banks’ activities is very high. 10 respondents (11.2%) strongly agreed that the performance rating of NBE is high, 47 respondents representing (52.8%) agree, 2 respondents (2.2%) and 6 respondents (6.7%) strongly disagreed and disagreed respectively, while 24 respondents representing (27.0%) were indifferent. In terms of mean, the respondents’ response has a mean value of 3.64, which is the point are approaches to agreed. Based on this analysis, most respondents believe that NBE in the performance rating of controlling banks’ activities is very high.

Q4: The regulators/supervisors of banks have helped in protecting depositors' funds by restricting certain banking activities and minimizing bank losses through the Banks and Other Financial institution.

N Valid	89
Missing	36
Mean	4.0337
Median	4.0000
Mode	4.00

Table 5.6

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	.8	1.1	1.1
	disagree	2	1.6	2.2	3.4
	neutral	13	10.4	14.6	18.0
	agree	50	40.0	56.2	74.2
	strongly agree	23	18.4	25.8	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

Table 5.6 presents a breakdown of the analysis. From the summary table, 23 respondents representing 25.8% of the sampled population strongly agreed that the regulators/supervisors of banks have helped in protecting depositors' funds by restricting certain banking activities and minimizing bank losses through the Banks and Other Financial institution. 50 respondents representing 56.2% of the population only agreed while 1 respondent or 1.1% of the population size and 2 respondents representing 2.2% of the populations strongly disagreed and disagreed respectively. 13 respondents (14.6%) remained indifferent. When this value is described in terms of mean, the mean value of the respondents' response is 4.03. The conclusion from this breakdown is that

respondents believe that the regulators/supervisors of banks have helped in protecting depositors' funds by restricting certain banking activities and minimizing bank losses through the Banks and Other Financial institution.

Q5: Bank legislation has helped in guiding against undue influence by the bank directors, managers and officers over depositors' funds and bank activities in general through disclosure of interest in any particular advances or loans

N Valid	89
Missing	36
Mean	3.8764
Median	4.0000
Mode	4.00

Table 5.7

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	1	.8	1.1	1.1
disagree	4	3.2	4.5	5.6
neutral	15	12.0	16.9	22.5
agree	54	43.2	60.7	83.1
strongly agree	15	12.0	16.9	100.0
Total	89	71.2	100.0	
Missing System	36	28.8		
Total	125	100.0		

Source: Survey result

On analyzing the responses in Table 5.7, (Bank legislation has helped in guiding against undue influence by the bank directors, managers and officers over depositors' funds and bank activities in general through disclosure of interest in any particular advances or loans), it was discovered that a total of 15 (16.9%) and 54 (60.7%) of the respondents strongly agreed and agreed respectively that Bank legislation has helped in guiding

against undue influence by the bank directors, managers and officers over depositors' funds and bank activities in general through disclosure of interest in any particular advances or loans; it was also discovered that about 1 (1.1%) and 4 (4.5%) of the respondents strongly disagreed and disagreed respectively while those that are neutral represent only 15 (16.9%) of the respondents. In relation to mean, the respondents' response has a mean value of 3.87 which is nearest to agree. Based on this analysis, most respondents were of the view that bank legislation has helped in guiding against undue influence by the bank directors, managers and officers over depositors' funds and bank activities in general through disclosure of interest in any particular advances or loans.

Q6: Effective regulation and supervision will go a long way in minimizing the negative impact of moral hazard, thereby leading to reduction in bank failure.

N	Valid	89
	Missing	36
Mean		4.0337
Median		4.0000
Mode		4.00

Table 5.8

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	6	4.8	6.7	6.7
	neutral	11	8.8	12.4	19.1
	agree	46	36.8	51.7	70.8
	strongly agree	26	20.8	29.2	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The sampled opinion in Table 5.8 shows that about 26 (29.2%) and 46 (51.7%) of the respondents strongly agreed and agreed respectively, that effective regulation and

supervision will go a long way in minimizing the negative impact of moral hazard, thereby leading to reduction in bank failure while no respondents say strongly disagree and 6 (6.7%) disagree to the statement. 11(12.4%) were neutral. In terms of mean, the respondents' response has a mean value of 4.03. Based on this analysis, it shows that majority of the respondent are supportive of Effective regulation and supervision will go a long way in minimizing the negative impact of moral hazard, thereby leading to reduction in bank failure.

Q7: Effective banking regulations encourage quality services and promote an efficient and competitive banking system.

N Valid	89
Missing	36
Mean	4.4719
Median	5.0000
Mode	5.00

Table 5.9

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	2	1.6	2.2	2.2
	neutral	5	4.0	5.6	7.9
	agree	31	24.8	34.8	42.7
	strongly agree	51	40.8	57.3	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The summary of the responses in table 5.9 shows that 51 (57.3%) and 31 (34.8%) of the respondents strongly agreed and agreed respectively, that effective banking regulations encourage quality services and promote an efficient and competitive banking system while 2 (2.2%) disagreed and no respondents to say strongly disagree to the statement. 5

(5.6%) were neutral. In relation to mean, the respondents' response has a mean value of 4.47. Based on this; Effective banking regulations encourage quality services and promote an efficient and competitive banking system.

Q8: Effective regulation and effective supervision of banks have helped in ensuring prudent management of bank assets and guarantee the safety of depositors' funds.

N Valid	89
Missing	36
Mean	4.1910
Median	4.0000
Mode	4.00

Table 5.10

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	2	1.6	2.2	2.2
	disagree	2	1.6	2.2	4.5
	neutral	6	4.8	6.7	11.2
	agree	46	36.8	51.7	62.9
	strongly agree	33	26.4	37.1	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The sampled opinion in Table 5.10 in response to whether effective regulation and effective supervision of banks have helped in ensuring prudent management of bank assets and guarantee the safety of depositors' funds indicates that 33 (37.1%) strongly agreed and 46 (51.7%) agreed of the respondents uphold this statement. 2 (2.2%) and 2 (2.2%) respectively, strongly disagreed and disagreed to the statement while 6 (6.7%) of the respondents were indifferent. In terms of mean, the respondents' response has a mean value of 4.19. Based on this analysis, it shows that most respondents uphold the statement.

Q9: Effective regulation/supervision focuses attention on protecting customers' interest through the legal institution.

N	Valid	89
	Missing	36
Mean		3.7753
Median		4.0000
Mode		4.00

Table 5.11

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	.8	1.1	1.1
	disagree	12	9.6	13.5	14.6
	neutral	14	11.2	15.7	30.3
	agree	41	32.8	46.1	76.4
	strongly agree	21	16.8	23.6	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The summary of responses in Table 5.11 shows that 21 (23.6%) and 41 (46.1%) of the respondents respectively, strongly agreed and agreed that effective supervision of banks would ensure prudent management of banks assets and guarantee the safety of the depositors' funds. while 1(1.1%) and 12 (13.5%) of the respondents strongly disagreed and disagreed respectively to the statement. However, 14(15.7%) of the respondents were indifferent. In relation to mean, the respondents' response has a mean value of 3.77 which is close to agreed. Based on this analysis, it shows that effective supervision of banks would ensure prudent management of bank assets and guarantee the safety of depositors' funds.

B. On-site Supervision Activities of NBE

Q10: The regular on-site inspection visit to banks has helped in identifying problem areas in banks, such as quality management, bank asset, capital funds, internal control, audit, information and account system.

N Valid	89
Missing	36
Mean	4.0225
Median	4.0000
Mode	4.00

Table 5.12

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	.8	1.1	1.1
	disagree	9	7.2	10.1	11.2
	neutral	9	7.2	10.1	21.3
	agree	38	30.4	42.7	64.0
	strongly agree	32	25.6	36.0	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The summary of responses in Table 5.12 shows that 32 (36.0%) of the respondents strongly agreed that the regular on-site inspection visit to banks has helped in identifying problem areas in banks, such as quality management, bank asset, capital funds, internal control, audit, information and account system, 38 (42.7%) agreed; 1(1.1%) strongly disagreed; 9 (10.1%) disagree while 9 (10.1%) of the respondents were neutral. In terms of mean, the respondents' response has a mean value of 4.02. The breakdown analysis shows that the regular on-site inspection visit to banks has helped in identifying problem areas in banks, such as quality management, bank asset, capital funds, internal control, audit, information and account system.

Q11: Persistent illiquidity, lingering boardroom squabbles, deteriorating assets quality is determined through on-site supervision of bank.

N Valid	89
Missing	36
Mean	3.5169
Median	4.0000
Mode	4.00

Table 5.13

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	4	3.2	4.5	4.5
disagree	16	12.8	18.0	22.5
neutral	17	13.6	19.1	41.6
agree	34	27.2	38.2	79.8
strongly agree	18	14.4	20.2	100.0
Total	89	71.2	100.0	
Missing System	36	28.8		
Total	125	100.0		

Source: Survey result

From the summary of the analysis in table 5.13, 18 (20.2%) of the respondents strongly agreed that Persistent illiquidity, lingering boardroom squabbles, deteriorating assets quality, etc are determined through on-site supervision of bank , 34(38.2%) agreed, 4 (4.5%) strongly disagree , 16 (18.0%) disagreed while 17 (19.1%) were indifferent. In relation to mean, the respondents' response has a mean value of 3.51 which is approach to agree. The breakdown analysis shows that most respondents believed that Persistent illiquidity, lingering boardroom squabbles, deteriorating assets quality, etc are determined through on-site supervision of bank.

Q12: On-site supervision has helped in reducing unprofessional and unethical conduct in Ethiopian banks.

Valid	89
Missing	36
Mean	3.6742
Median	4.0000
Mode	4.00

Table 5.14

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	3	2.4	3.4	3.4
	disagree	11	8.8	12.4	15.7
	neutral	16	12.8	18.0	33.7
	agree	41	32.8	46.1	79.8
	strongly agree	18	14.4	20.2	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

From the summary of the analysis in Table 5.14, 18 respondents (20.2%) strongly agreed that On-site supervision has helped in reducing unprofessional and unethical conduct in Ethiopian banks. 41 (46.1%) agreed, 3 (3.4%) and 11 (12.4%) of the respondents strongly disagreed and disagreed respectively while 16 (18.0%) were neutral. In terms of mean, the respondents' response has a mean value of 3.67 which is approach to agree. The breakdown analysis shows that On-site supervision has helped in reducing unprofessional and unethical conduct in Ethiopian banks.

C. Off-site Supervision Activities of NBE

Q13: The off-site supervision of banks by the NBE acts has check and analysis as well as prudential returns from banks.

N Valid	89
Missing	36
Mean	3.8427
Median	4.0000
Mode	4.00

Table 5.15

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	10	8.0	11.2	11.2
	neutral	18	14.4	20.2	31.5
	agree	37	29.6	41.6	73.0
	strongly agree	24	19.2	27.0	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The response in Table 5.15 tries to affirm the off-site supervision of banks by the NBE acts has check and analysis as well as prudential returns from banks. From the opinions expressed, 24 (27.0%) strongly agreed, 10 (11.2%) disagreed, no respondents say strongly disagree and 10 (11.2%) disagree while 18 (20.2%) were indifferent. In relation to mean, the respondents' response has a mean value of 3.8 which is approach to agree. It is interesting to note that the majority of the respondents were of the view that the off-site supervision of banks by the NBE acts has check and analysis as well as prudential returns from banks.

Q14: Off-site supervision has helped in assisting the discovery of financial problems in the banks through financial ratio and periodic bank returns.

N Valid	89
Missing	36
Mean	4.0337
Median	4.0000
Mode	4.00

Table 5.16

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	2	1.6	2.2	2.2
	neutral	13	10.4	14.6	16.9
	agree	54	43.2	60.7	77.5
	strongly agree	20	16.0	22.5	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

From Table 5.16, 20 (22.5%) and 54 (60.7%) of the respondents strongly disagreed and agreed respectively, that Off-site supervision has helped in assisting the discovery of financial problems in the banks through financial ratio and periodic bank return. No respondents say strongly disagree and 2 respondents (2.2%) disagreed. While 13(14.6%) were neutral. In terms of mean, the respondents' response has a mean value of 4.03 which is agree. The breakdown analysis shows that Off-site supervision has helped in assisting the discovery of financial problems in the banks through financial ratio and periodic bank returns.

Q15: Off-site supervision has assisted in approving board and management positions in the bank through sufficient banking experience and post-qualification experience.

N Valid	89
Missing	36
Mean	3.9551
Median	4.0000
Mode	4.00

Table 5.17

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	3	2.4	3.4	3.4
	neutral	18	14.4	20.2	23.6
	agree	48	38.4	53.9	77.5
	strongly agree	20	16.0	22.5	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

Table 5.17, 20 (22.5%) and 48 (53.9%) of the respondents strongly agreed and agreed respectively that off-site supervision has assisted in approving board and management positions in the bank through sufficient banking experience and post-qualification experience. A total of 3 (3.4%) disagreed and no respondents say strongly disagree while 18 (20.2%) were neutral. In terms of mean, the respondents’ response has a mean value of 3.95 which is very close to agree. By implication, it shows that majority of the respondents believed that Off-site supervision has assisted in approving board and management positions in the bank through sufficient banking experience and post-qualification experience.

Q16: The approval/expansion of banks’ branches has been keenly monitored through off-site supervision.

N	Valid	89
	Missing	36
Mean		3.8202
Median		4.0000
Mode		4.00

Table 5.18

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	3	2.4	3.4	3.4
	disagree	4	3.2	4.5	7.9
	neutral	23	18.4	25.8	33.7
	agree	35	28.0	39.3	73.0
	strongly agree	24	19.2	27.0	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The summary of response in Table 5.18 shows that 24 (27.0%) of the respondents strongly agreed that the approval/expansion of banks’ branches has been keenly monitored through off-site supervision, 35 (39.3%) agreed, 3(3.4%) and 4 (4.5%) strongly disagreed and disagreed respectively, while 23 (25.8%) of the respondents were indifferent. In relation to mean, the respondents’ response has a mean value of 3.8 which is close to agree. The breakdown analysis shows that the approval/expansion of banks’ branches has been keenly monitored through off-site supervision.

D. Disclosure of Information to the General Public

Q17: Disclosure of banks' annual financial statements or audit reports will give the depositors, investors and the general public adequate information about banks' performance.

N	Valid	89
	Missing	36
Mean		4.0337
Median		4.0000
Mode		5.00

Table 5.19

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	.8	1.1	1.1
	disagree	8	6.4	9.0	10.1
	neutral	14	11.2	15.7	25.8
	agree	30	24.0	33.7	59.6
	strongly agree	36	28.8	40.4	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The sampled opinion in table 5.19 in response to whether the disclosure of banks' annual financial statements or audit reports will give the depositors, investors and the general public adequate information about banks' performance, shows 36 (40.4%) and 30 (33.7%) respondents respectively, strongly agreed and agreed to this statement while 1 (1.1%) and 8 (9.0%) strongly disagreed and disagreed to the statement. 14 (15.7%) of the respondents were indifferent. In terms of mean, the respondents' response has a mean value of 4.03. The summary of this analysis shows that majority of the respondents upholds the statement that the disclosure of banks' annual financial statements or audit

reports will give the depositors, investors and the general public adequate information about banks' performance.

Q18: The introduction of prudential guidelines has promoted the nations' banking stability.

N	Valid	89
	Missing	36
Mean		3.7865
Median		4.0000
Mode		4.00

Table 5.20

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	2	1.6	2.2	2.2
	disagree	7	5.6	7.9	10.1
	neutral	15	12.0	16.9	27.0
	agree	49	39.2	55.1	82.0
	strongly agree	16	12.8	18.0	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

From the summary of the analysis in Table 5.20, 16 (18.0%) of the respondents strongly agreed that the introduction of prudential guidelines has promoted the nations' banking stability; 49 (55.1%) agreed, 2 (2.2%) and 7 (7.9%) strongly disagreed and disagreed respectively, while 15 (16.9%) were indifferent. In relation to mean, the respondents' response has a mean value of 3.78 which is close to agreed. The breakdown of the analysis shows that most respondents believe that the introduction of prudential guidelines has promoted the nations' banking stability.

Q19: Banks and other financial guideline /directives is adequate for supervision of financial institution in Ethiopia

N Valid	89
Missing	36
Mean	3.4831
Median	4.0000
Mode	4.00

Table 5.21

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	3	2.4	3.4	3.4
disagree	17	13.6	19.1	22.5
neutral	14	11.2	15.7	38.2
agree	44	35.2	49.4	87.6
strongly agree	11	8.8	12.4	100.0
Total	89	71.2	100.0	
Missing System	36	28.8		
Total	125	100.0		

Source: Survey result

From the summary of the analysis in table 5.21, 11 (12.4%) and 44 (49.4%) of the respondents respectively, strongly agreed and agreed that Banks and other financial guideline /directives is adequate for supervision of financial institution in Ethiopia while 3 (3.4%) and 17 (19.1%) of the respondents respectively, strongly disagreed and disagreed whereas 14 (15.7%) of the respondents were neutral. When this value is described in terms of mean, the mean value of the respondents' response is 3.48 it approaches to agree. The breakdown of the analysis shows that most respondents supported the statement.

Q20: Disclosure of financial statements to depositors, investors and the public will go a long way in enhancing public confidence in the banks.

N Valid	89
Missing	36
Mean	4.0225
Median	4.0000
Mode	4.00

Table 5.22

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	3	2.4	3.4	3.4
	neutral	16	12.8	18.0	21.3
	agree	46	36.8	51.7	73.0
	strongly agree	24	19.2	27.0	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The summary of response in Table 5.22, shows that 24 (27.0%) and 46 (51.7%) of the respondents respectively, strongly agreed and agreed that disclosure of financial statements to depositors, investors and the public will go a long way in enhancing public confidence in the banks; 0 (0%) and 3 (3.4%) respectively, strongly disagreed and disagreed to the statement while 16(18.0%) of the respondents were indifferent. In relation to mean, the respondents’ response has a mean value of 4.02. The summary of this analysis shows that majority of the respondent upholds the statement that disclosure of financial statements to depositors, investors and the public will go a long way in enhancing public confidence in the banks.

Q21: Disclosure of banks’ annual financial statements to depositors, investors and the general public will help in determining the soundness of the bank.

N	Valid	89
	Missing	36
Mean		4.0225
Median		4.0000
Mode		4.00

Table 5.23

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	neutral	20	16.0	22.5	22.5
	agree	47	37.6	52.8	75.3
	strongly agree	22	17.6	24.7	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

From the summary of response in table 5.23 shows that 22 (24.7%) and 47 (52.8%) of the respondents respectively, strongly agreed and agreed that disclosure of banks’ annual financial statements to depositors, investors and the general public will help in determining the soundness of the bank; no response for, strongly disagreed and disagreed while 20 (22.2%) were indifferent. When this value is described in terms of mean, the mean value of the respondents’ response is 4.02 .The breakdown analysis shows that most respondents supported the statement.

E. On going Regulatory Requirements

Q22: The minimum capital requirement 500 million birr can limits market contribution because only a small number of individuals or companies can meet the requirement.

N Valid	89
Missing	36
Mean	3.5393
Median	4.0000
Mode	5.00

Table 5.24

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	9	7.2	10.1	10.1
disagree	15	12.0	16.9	27.0
neutral	13	10.4	14.6	41.6
agree	23	18.4	25.8	67.4
strongly agree	29	23.2	32.6	100.0
Total	89	71.2	100.0	
Missing System	36	28.8		
Total	125	100.0		

Source: Survey result

The summary of response in table 5.24, shows that 29 (32.6%) and 23 (25.8%) of the respondents respectively, strongly agreed and agreed that the minimum capital requirement 500 million birr can limits market contribution because only a small number of individuals or companies can meet the requirement; while 9 (10.1%) and 15 (16.9%) of the respondents respectively, strongly disagreed and disagreed to it. However, 13 (14.6%) of the respondents were indifferent. When this value is described in terms of mean, the mean value of the respondents' response is 3.53 it approaches to agree. The breakdown analysis indicates that most respondents supported the above statement.

Q23: The liquidity requirement of banks can maintain all known and unexpected obligations and hence promotes public confidence

N	Valid	89
	Missing	36
Mean		3.6292
Median		4.0000
Mode		4.00

Table 5.25

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	10	8.0	11.2	11.2
	neutral	24	19.2	27.0	38.2
	agree	44	35.2	49.4	87.6
	strongly agree	11	8.8	12.4	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

From the summary in Table 5.25, 11 of the respondents representing 12.4% of the sample population strongly agreed, and 44 respondents representing 49.4% of the population agreed that the liquidity requirement of banks can maintain all known and unexpected obligations and hence promotes public confidence, while no response and 10 (11.2%) of the respondents strongly disagreed and disagreed respectively. When this value is described in terms of mean, the mean value of the respondents' response is 3.6 which approach to agree. However, 24 (27.0%) of the respondents were indifferent. The breakdown analysis shows that majority of the respondents uphold the statement.

Q24: High regulatory restrictions of the banks activities promote government power, create a bigger role for corruption through the granting of exceptions to the rules, and thereby hinder bank performance and stability

N	Valid	89
	Missing	36
Mean		3.1910
Median		3.0000
Mode		4.00

Table 5.26

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	9	7.2	10.1	10.1
	disagree	13	10.4	14.6	24.7
	neutral	26	20.8	29.2	53.9
	agree	34	27.2	38.2	92.1
	strongly agree	7	5.6	7.9	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

From summary of the table in 5.26, 7 respondents representing 7.9% of the population size strongly agreed; 34 respondents representing 38.2% of the respondents agreed that high regulatory restrictions of the banks activities promote government power, create a bigger role for corruption through the granting of exceptions to the rules, and thereby hinder bank performance and stability while 9 (10.1%) and 13 (14.6%) strongly disagree and disagreed respectively to it. However, 26 (29.2%) respondents were indifferent. When this value is described in terms of mean, the mean value of the respondents' response is 3.19. Based on this analysis, it shows that majority of the respondents were support the statement.

Q25: Fewer regulatory restrictions on the investment activities of bank permit the exploitation of economies of scale and scope in gathering and managing information about firms.

N	Valid	89
	Missing	36
Mean		3.6742
Median		4.0000
Mode		4.00

Table 5.27

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	5	4.0	5.6	5.6
	disagree	7	5.6	7.9	13.5
	neutral	20	16.0	22.5	36.0
	agree	37	29.6	41.6	77.5
	strongly agree	20	16.0	22.5	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Source: Survey result

The summary of responses in the table 5.27, shows that 20 (22.5%) and 37 (41.6%) of the respondents strongly agreed and agreed respectively that the fewer regulatory restrictions on the investment activities of bank permit the exploitation of economies of scale and scope in gathering and managing information about firms, 5 (5.6%); 7 (7.9%) strongly disagreed and disagreed respectively while 20 (22.5%) of the respondents were indifferent. In relation to mean, the respondents’ response has a mean value of 3.67 which is close to agree. The analysis indicates that most respondents supported the statement that the fewer regulatory restrictions on the investment activities of bank permit the exploitation of economies of scale and scope in gathering and managing information about firms.

F. Penalty Convince

Q26: Imposition of sanctions by the NBE on banks due to non-compliance to the enabling laws, rules and regulations may jeopardize the financial activities of the bank.

N	Valid	89
	Missing	36
Mean		2.8539
Median		3.0000
Mode		2.00

Table 5.28

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	12	9.6	13.5	13.5
	disagree	29	23.2	32.6	46.1
	neutral	16	12.8	18.0	64.0
	agree	24	19.2	27.0	91.0
	strongly agree	8	6.4	9.0	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

Table 5.28 shows that imposition of sanctions by the NBE on banks due to non-compliance to the enabling laws; rules and regulations may jeopardize the financial activities of the bank. 8 respondents (9.0%) strongly agreed that imposition of sanctions by the NBE on banks due to non-compliance to the enabling laws; rules and regulations may jeopardize the financial activities of the bank, 24 respondents representing (27.0%) agree, 12 respondents (13.5%) and 29 respondents (32.6%) strongly disagreed and disagreed respectively, while 16 respondents representing (18.0%) were indifferent. In terms of mean, the respondents' response has a mean value of 2.85, which is the point are approaches to neutral. Based on this analysis, most respondents are neutral imposition of

sanctions by the NBE on banks due to non-compliance to the enabling laws, rules and regulations may jeopardize the financial activities of the bank.

Q27: NBE sanctions on banks can lead to taking over of management of banks and revocation of banking license.

N	Valid	89
	Missing	36
Mean		3.7303
Median		4.0000
Mode		4.00

Table 5.29

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	.8	1.1	1.1
	disagree	8	6.4	9.0	10.1
	neutral	20	16.0	22.5	32.6
	agree	45	36.0	50.6	83.1
	strongly agree	15	12.0	16.9	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

The summary of the responses in table 5.29 shows that 15 (16.9%) and 45 (50.6%) of the respondents strongly agreed and agreed respectively, that NBE sanctions on banks can lead to taking over of management of banks and revocation of banking license while 1 (1.1%) strongly disagreed and 8 (9.0) disagree to the statement. 20 (22.5%) were neutral. In relation to mean, the respondents' response has a mean value of 3.7 which approach to agree. Based on this; NBE sanctions on banks can lead to taking over of management of banks and revocation of banking license.

Q28: Imposing sanctions on banks by NBE may lead to removal/prosecution of directors and officials of the bank.

N	Valid	89
	Missing	36
Mean		3.7191
Median		4.0000
Mode		4.00

Table 5.30

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	.8	1.1	1.1
	disagree	9	7.2	10.1	11.2
	neutral	22	17.6	24.7	36.0
	agree	39	31.2	43.8	79.8
	strongly agree	18	14.4	20.2	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

The summary of responses in Table 5.30 shows that 18 (20.2%) of the respondents strongly agreed that imposing sanctions on banks by NBE may lead to removal/prosecution of directors and officials of the bank, 39 (43.8%) agreed; 1(1.1%) strongly disagreed; 9 (10.1%) disagree while 22 (24.7%) of the respondents were neutral. In terms of mean, the respondents’ response has a mean value of 3.7 which is close to agree. The breakdown analysis shows imposing sanctions on banks by NBE may lead to removal/prosecution of directors and officials of the bank.

Q29: Imposing sanctions on banks can result to payment of monetary penalty.

N	Valid	89
	Missing	36
Mean		3.7753
Median		4.0000
Mode		4.00

Table 5.31

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	2	1.6	2.2	2.2
	disagree	3	2.4	3.4	5.6
	neutral	22	17.6	24.7	30.3
	agree	48	38.4	53.9	84.3
	strongly agree	14	11.2	15.7	100.0
	Total	89	71.2	100.0	
Missing	System	36	28.8		
Total		125	100.0		

The sampled opinion in table 5.31 in response to imposing sanctions on banks can result to payment of monetary penalty, shows 14 (15.7%) and 48 (53.9%) respondents respectively, strongly agreed and agreed to this statement while 2 (2.2%) and 3 (3.4%) strongly disagreed and disagreed to the statement. 22 (24.7%) of the respondents were indifferent. In terms of mean, the respondents' response has a mean value of 3.77. The summary of this analysis shows that majority of the respondents upholds the statement that imposing sanctions on banks can result to payment of monetary penalty.

5.2. Data Analysis

This section of the chapter discusses the analysis of both survey and interview results. The analysis is based on the theoretical framework and the data collected through the data collection instruments. The data are analyzed in light of the specific objectives stated. Hence, the analysis focus on the results of how supervisory and regulatory functions of the regulators (NBE) impacts on the Ethiopian private banks; to assess the effectiveness of the regulation and supervision in the Ethiopian banking industry; to examine regulatory and supervisory activities of the NBE have boosted depositors' confidence in the Banking System; to assess the on-site and off-site supervision activities of NBE; to evaluate the minimum capital requirement for establishing new Banks and to assess the investment activities restriction of private banking industry in Ethiopia.

Traditionally, the role of banks whether in a developed or developing economy, consists of financial intermediation, provision of an efficient payments system and serving as a conduit for the implementation of monetary policies. It has been postulated that if these functions are efficiently carried out, the economy would be able to mobilize meaningful level of savings and channel these funds in an efficient and effective manner to ensure that no viable project is frustrated due to lack of funds. The objectives of banking regulation and supervision were advanced by Giddy (1984) as for monetary policy, i.e. the ability of banks to create money through the extension of credit; credit allocation function of banks; the need to ensure competition and innovation by the prevention of cartels; and because banks are depositories of public savings and managers of payments mechanism, they are very vulnerable to collapse. In view of the importance of the banking sector in economic development and the imperfection of the market mechanism to mobilize and allocate financial resources to socially desirable economic activities of any nation, governments the world over, de regulate them more than any other sector in an economy. Furthermore, such an oversight is intended to assist supervisory authorities in timely identification of deterioration in banks' financial conditions before it degenerates to threaten the stability of the banking system or even the economy.

Dimitri, Vitas (1990) also believes that good regulation and supervision will minimize the negative impact of moral hazard and price shocks on the banking system, thereby leading to a reduction in bank failures and banking system distress. The survey result indicates that most of the respondents believe that effective regulation and supervision will go a long way in minimizing the negative impact of moral hazard, thereby leading to reduction in bank failure.

Bench (1993) asserts that effective supervision of banks leads to a healthy banking industry. Maintaining effective supervision, including who should supervise banks, i.e., the “structure” of bank supervision. Three issues for policy makers to address with respect to the structure of bank supervision are whether there should be a single bank supervisory authority, or multiple bank supervisors; whether the central bank should play a role in bank supervision; and whether the supervisor responsible for the banking industry should also have responsibility for other financial services, in particular the securities and insurance industries. When come to in Ethiopian case banking industry is supervised by the NBE (central bank of Ethiopian) because according to the interview with banking supervision department employees of NBE, the NBE (central bank) will have first-hand knowledge of the condition and performance of banks and to insure price stability and to protect the healthiness of financial institutions in order to ensure public confidence. This in turn can help it identify and respond to the emergence of a systemic problem in a timely manner. The survey results indicated that most of the respondents believe the supervisory and regulatory framework of NBE is very effective in Ethiopian banking system. But according to the interview with baking supervision department employees of NBE who is an assistant examiner state that their success of supervisory and regulatory framework of NBE endangered by NBE supervisory capacity particularly related to little experience of the banking supervision department employees and the absence of entry training for the new employees to notify about the banking operation. These factors exposed the banking system to some degree of risk.

The stability of banking industry in Ethiopia, the survey result indicates that most of the respondents believe that the stability in the banking system was as a result of effective

Regulation and Supervision by the national bank of Ethiopia (NBE). According to the interview with banking supervision employees of NBE the stability of banking industry in Ethiopia measured by using three parameters namely profitability, liquidity and asset quality of the banks. Based on this, the respondent's states that their profitability, liquidity and asset quality of most of private banks in Ethiopia is currently increase time to time. As a result, banking industry in Ethiopian assure public confidence to deposit and withdraw their money at any time. Moreover the respondent's said that the stability of banking industry in Ethiopia is the result of restriction of foreign bank investment in the country.

The disclosure to the general public through the announcement of operating results and full disclosure to bank supervisors where public disclosure may not be necessary in order to protect the clients' secrecy. Information disclosure by banks is basically designed to ensure that supervisors, depositors, investors and the general public are adequately informed of bank's performance/condition. The enforcement of adequate disclosure is paramount. The level of disclosure and timing of information to the various stakeholders should be articulated for banks to comply as a routine. This is an issue in Pillar III (Market Discipline) of the New Capital Accord (Iyade, 2006). The survey result indicates that most of the respondents assure that disclosure of banks' annual financial statements or audit reports will give the depositors, investors and the general public adequate information about banks' performance.

Dale (1988) had classified prudential regulation of banks into three: preventive, protective and supportive. While preventive regulation is designed to limit the risk undertaken, the protective regulation offers protection in the event of failure. The supportive regulation is in form of a lender of last resort. According to the interview with the banking supervision department employee, NBE followed preventive methods of regulation which is designed to limit the risk undertaken. Some of the preventive regulation of NBE consists of capital adequacy, liquidity requirement, branching requirement, frequency and content of financial reporting, restriction of investment;

external audit report and penalty convince which were described in the literature review section.

In Ethiopia the banking supervision consists of two components. The first one is the off-site and the second approach is on-site examination. The on-site examination is done by the Banking supervision staff physically visit the banks to check the accuracy of reports submitted to NBE. It also aims at verifying the accuracy of the periodic reports of the banks sent to the regulatory authorities, analyzing those aspects of a bank that cannot be adequately monitored through off-site surveillance and confirming and ensuring compliance with laid down laws, rules and regulations. On-site examiners assess the quality of assets, management, earnings, capital and funds management as well as accounting and internal control systems. According to the survey result most of the respondents uphold all statements that are arise in relation to on-site examination activities of NBE.

The second form is off-site surveillance. The returns of banks to the regulatory authorities are analyzed by off-site supervisors for completeness, accuracy and consistency as well as compliance with prudential ratios and regulations. Regulatory Authorities, mainly in emerging markets, which do not have adequate resources rely more on off-site supervision to monitor the financial condition and performance of banks and to identify those banks that may need closer scrutiny. It is an irony of fate that where on-site examination should be emphasized due to low integrity of information from banks; resource constraints make such regulatory authorities to rely on off-site supervision. It is useful to add that on-site examination has been found to be more effective than off-site supervision in many jurisdictions due mainly to unreliable information that many banks do send to the Regulatory Authorities. According to the survey result most of the respondents supported all statements that arise in relation to off-site surveillance activities of NBE.

The minimum capital is often required for the purpose of registration and licensing of Companies. According to the Directives number SBB/50/2011 the minimum capital

requirement for establishing new Banks is Birr 500,000,000 million which is approximately equivalent to US\$29,411,764 which shall be fully paid in cash and deposited in a bank in the name and to the account of the bank under establishment. As observed by the World Bank, developed countries tend to request lower minimum capital than developing countries (the World Bank, Doing Business 2011, p. 22). According to the survey result most of the respondents support that the minimum capital requirement 500 million birr for establishing new Banks can limit market contribution because only a small number of individuals or companies can meet the requirement.

There are five main theoretical reasons for restricting the degree to which banks can engage in securities, insurance, and real estate activities, or own non-financial firms, in the contrary there are alternative theoretical reasons for permitting banks to engage in a broad range of activities that are explained in the literature review part.

According to banking Proclamation number 84/1994, no bank shall engage in insurance business but may hold up to 20% in an insurance company and up to a total of 10% of the bank's equity capital in such business. Banks are prohibited from engaging directly in non-banking businesses such as agriculture, industry, and commerce. A bank may hold shares in a non-banking business only up to 20% of the company's share capital and total holdings in such business shall not exceed 10% of the bank's net worth. According to the interview with the banking supervision department employees of NBE states that banks are restricted to invest in non financial sectors rather it invest their money in the form of loan to those sectors. But with regard to financial sectors banks may hold securities of insurance company up to 20%. Moreover the interviewee states that NBE has an impact on banks by prohibiting banks to invest in risky business sector. The survey result also support fewer regulatory restrictions on the investment activities of bank permit the exploitation of economies of scale and scope in gathering and managing information about firms. Generally to achieve the objective of banking regulation and supervision of NBE which is protecting depositors, ensuring Integrity and Stability of the banking sector in particular and Financial Sector in general and promote efficient performance of the institutions NBE should build up the capacity of banking supervision department .

Chapter Six: Conclusions and Recommendations

The preceding chapter presented the results and analysis, while this chapter deals with the conclusions and recommendations based on the findings of the study. Accordingly this chapter is organized into two sub-sections. Section 6.1 presents the conclusions and section 6.2 presents the recommendations.

6.1. Conclusions

It is clear that regulation and supervision of NBE affect the activities of banking industry. This study is aimed at assessing the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banks. The research examined the role played by the regulatory authorities towards a healthy supervision of the operation of banks in Ethiopia and also examined the tools, scope, methods and policy framework of supervision. The research theme was guided by six specific objectives that are stated in the earlier sections and three research questions. The research borrowed heavily from related research material which was appropriately referenced. It adopted a questionnaire based method of evaluation and interview with the concerned body to meet the specific objective and to answer the research questions and comparing the survey result using descriptive statistics and analysis both results i.e. survey and interview with concurrent mixed method research approach.

The purpose of the National Bank is to maintain stable rate of price and exchange, to foster a healthy financial system and to undertake such other related activities as are conducive to rapid economic development of Ethiopia. In view of the importance of the banking sector in economic development and the imperfection of the market mechanism to mobilize and allocate financial resources to socially desirable economic activities of any nation, governments the world over, de regulate them more than any other sector in an economy.

Supervisory and regulatory framework of NBE is effective in Ethiopian banking system. But the success of supervisory and regulatory framework of NBE endangered by NBE supervisory capacity particularly related to little experience of the banking supervision

department employees and the absence of entry training for the new employees to notify about the banking operation. These factors exposed the banking system to some degree of risk.

Banking industry in Ethiopia is stable. The stability in the banking system was as a result of efficient Regulation and Supervision by the national bank of Ethiopia (NBE). The stability of banking industry in Ethiopia is measured by using three parameters specifically profitability, liquidity and asset quality. Based on this in Ethiopia most of the private banks profitability, liquidity and asset quality is increase time to time. As result this brings the confidence of the public is increase to deposit and withdraw their money at any time. More over the restriction of foreign banks also there own contribution for the stability of Ethiopian banking industry.

The disclosure to the general public through the announcement of operating results and full disclosure to bank supervisors where public disclosure may not be necessary in order to protect the clients' secrecy. Information disclosure by banks is basically designed to ensure that supervisors, depositors, investors and the general public are adequately informed of bank's performance/condition.

NBE is supervised banks using two components. The first one is on-site supervision of banks entails physical presence of regulators (NBE) in the financial institutions to evaluate their internal controls, compliance with the laws and regulations governing their operations with a view to determining their overall risk exposure. Emphasis is placed on their capital, asset quality of management, the strength of earnings and the adequacy of liquidity. On-site supervision is carried out by the Bank supervision department of the regulatory bodies. The second form the off-site supervision of banks is carried out by the Banking Supervision Department of the NBE and involves essentially the appraisal of banks returns. Essentially, it serves as an early warning device to detect a bank's emerging financial problem. This is accompanied by analyzing key bank financial ratios and other financial data that are generated from periodic bank financial reports that are submitted to the supervisor.

The minimum capital is often required for the purpose of registration and licensing of banking industry in Ethiopia required 500 million birr. According to the World Bank, doing business 2011 developing countries tend to request higher minimum capital than developed countries. As a result minimum capital requirement 500 million birr can limit market contribution because only a small number of individuals or companies can meet the requirement.

In Ethiopia Banks are prohibited from engaging directly in non-banking businesses such as agriculture, industry, and commerce. A bank may hold shares in a non-banking business only up to 20% of the company's share capital and total holdings in such business shall not exceed 10% of the bank's net worth. Banks are restricted to invest in non financial sectors rather it invest their money in the form of loan to those sectors. But with regard to financial sectors banks may hold securities of insurance company up to 20%. Moreover NBE banking supervision has an impact on banks by prohibiting banks to invest in risky business sector. Generally fewer regulatory restrictions on the investment activities of bank permit the exploitation of economies of scale and scope in gathering and managing information about firms.

6.2.Recommendations

Based on the findings of this study, the banking supervisory structure currently being pursued by the regulatory authorities the researcher recommends the following points:

- Build up the capacity of NBE, strengthen skills of banking Supervision staff in knowledge of efficient and effective regulatory and supervisory practices and experience of other countries through training and exposure visits, enhance the existing logistical support to increase on-site inspection.
- Increases the ways and methods by which Regulatory Authorities Carryout Supervisory Functions in Banks in addition to on-site and off-site supervision like Maiden Examination, Target/Special Examination and Investigation/Spot Checks.

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Appendix 1: Survey Instrument

Questionnaire on Regulation and Supervision of National Bank of Ethiopia and its impact on the activities of Ethiopian private banking industry

Dear Sir/Madam

The intent of this questionnaire is to explore information regarding the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banking industry. The questionnaire will be distributed to the purposively selected six private banks head office employees namely Awash, Dashen, Abyssinia, Wegagen, United, Nib International Bank and banking supervision department employees of NBE. The information you provide in response to the items in the questionnaire will be used as part of the data needed for a study of regulation and supervision of NBE and its impact on the activities of Ethiopian private banking industry. The results of the study are anticipated to supply to the understanding of the impact of regulation and supervision of NBE on the activities of Ethiopian private banking and be used to obtain insight to regulation and supervision activities of NBE.

I would like to assure you that this is fully academic research and your responses are confidentially kept. Your involvement is regarded as a great input to the quality of the research results. Hence, I believe that you will enlarge your assistance by participating in the study.

Your honest and thoughtful response is invaluable

Thanks you for your participation

Kinds regard,

Sofoniyas Mekonnen, MSc student

Addis Ababa University

School of Business and Public Administration
Department of Accounting and Finance

Date: January, 2012

General Instruction

This questionnaire contains 6 pages and is expected to take approximately 10 to 15 minutes to complete. Please provide your responses to the questions based on the instructions under each section. If you have comments or if you want to provide further explanations, please provide further explanation, please use the spaces provide at the end of the questioner.

Section I

Instruction: Please indicate the following by ticking (✓) on the space in front of the response options

1. Background information of respondents

1.1. Category of Bank Staff

A. Top Management ☐ B. Middle Management ☐ C. NBE employee ☐

1.2. Level of education

A. Diploma ☐ B. Bachelor degree ☐ C. masters ☐ D. other (specify) _____

1.3. Sex

A. Male ☐ B. Female ☐

1.4. Number of years of experience

A. < 1 year ☐ B. 1-5 ☐ C. 5-10 ☐ D. > 10 year ☐

Section II Regulation and Supervision of NBE context

Instruction: below are the lists of statements pertaining to impact of regulation and supervision of NBE in your organization. Please indicate whether you agree or disagree with each statement by ticking (✓) on the space that specifies your choice from the options that range from 'strongly agree' to 'undecided'

Note: 1= strongly disagree (SD)
2= Disagree (DA)
3= Neutral (N)
4= Agree (A)
5= strongly agree (SA)

	SD(1)	DA(2)	N(3)	A(4)	SA(5)
A. Effectiveness of regulatory and supervisory framework of NBE					
1. The supervisory and regulatory framework of NBE is very effective in Ethiopian banking system	()	()	()	()	()
2. The stability in the banking system was as a result of sound and effective supervisory and regulatory framework of NBE.	()	()	()	()	()
3. The performance rating of NBE in controlling banks' activities is very high.	()	()	()	()	()
4. The regulators/supervisors of banks have helped in protecting depositors' funds by restricting certain banking activities and minimizing bank losses through the Banks and Other Financial Institution.	()	()	()	()	()
5. Bank legislation has helped in guiding against undue influence by the bank directors, managers and officers over depositors' funds and bank activities in general through disclosure of interest in any particular advances or loans	()	()	()	()	()
6. Effective regulation and supervision will go a long way in minimizing the negative impact of moral hazard, thereby leading to reduction in bank failure.	()	()	()	()	()
7. Effective banking regulation encourages quality services and promotes an efficient and competitive banking system.	()	()	()	()	()

8. Effective regulation and effective supervision of banks have helped in ensuring prudent management of bank assets and guarantee the safety of depositors' funds.	()	()	()	()	()
9. Effective regulation/supervision focuses attention on protecting customers' interest through the legal institution.	()	()	()	()	()
B. On-site Supervision Activities of NBE					
10. The regular on-site inspection visit to banks has helped in identifying problem areas in banks, such as quality management, bank asset, capital funds, internal control, audit, information and account system.	()	()	()	()	()
11. Persistent illiquidity, lingering boardroom squabbles, deteriorating assets quality is determined through on-site supervision of bank.	()	()	()	()	()
12. On-site supervision has helped in reducing unprofessional and unethical conduct in Ethiopian banks	()	()	()	()	()
C. Off-site Supervision Activities of NBE					
13. The off-site supervision of banks by the NBE acts has check and analysis as well as prudential returns from banks.	()	()	()	()	()
14. Off-site supervision has helped in assisting the discovery of financial problems in the banks through	()	()	()	()	()

financial ratio and periodic bank returns.					
15. Off-site supervision has assisted in approving board and management positions in the bank through sufficient banking experience and post-qualification experience.	()	()	()	()	()
16. The approval/expansion of banks' branches has been keenly monitored through off-site supervision.	()	()	()	()	()
D. Disclosure of Information to the General Public					
17. Disclosure of banks' annual financial statements or audit reports will give the depositors, investors and the general public adequate information about banks' performance.	()	()	()	()	()
18. The introduction of prudential guidelines has promoted the nations' banking stability.	()	()	()	()	()
19. Banks and other financial guideline /directives is adequate for supervision of financial institution in Ethiopia	()	()	()	()	()
20. Disclosure of financial statements to depositors, investors and the public will go a long way in enhancing public confidence in the banks.	()	()	()	()	()
21. Disclosure of banks' annual financial statements to depositors, investors and the general public will help in determining the soundness of the bank.	()	()	()	()	()

E. On going Regulatory Requirements					
22. The minimum capital requirement 500 million birr can limits market contribution because only a small number of individuals or companies can meet the requirement.	()	()	()	()	()
23. The liquidity requirement of banks can maintain all known and unexpected obligations and hence promotes public confidence	()	()	()	()	()
24. High regulatory restrictions of the banks activities promote government power, create a bigger role for corruption through the granting of exceptions to the rules, and thereby hinder bank performance and stability	()	()	()	()	()
25. Fewer regulatory restrictions on the investment activities of bank permit the exploitation of economies of scale and scope in gathering and managing information about firms	()	()	()	()	()
F. Penalty Convince					
26. Imposition of sanctions by the NBE on banks due to non-compliance to the enabling laws, rules and regulations may jeopardize the financial activities of the bank.	()	()	()	()	()
27. NBE sanctions on banks can lead to taking over of	()	()	()	()	()

management of banks and revocation of banking license.					
28. Imposing sanctions on banks by NBE may lead to removal/prosecution of directors and officials of the bank.	()	()	()	()	()
29. Imposing sanctions on banks can result to payment of monetary penalty.	()	()	()	()	()

Additional Comments

Appendix 2: Interview Questions

Dear Sir/ Madam

The intent of this interview is to explore information regarding the impact of regulatory and supervisory functions of NBE on the activities of Ethiopian private banks to have sufficient response to the research problem in addition to questioners distribute to six purposively selected private banks head office employees and banking supervision department employees of NBE. This interview will conduct with 8 randomly selected banking supervision department employees of NBE. The information obtain in response to the items in the interview will used as part of the data needed for a study of regulation and supervision of NBE and its impact on the activities of Ethiopian private banking industry.

I would like to assure you that the information you provide was accessible only to the investigator. Your involvement is regarded as a great input to the quality of research results. Hence, I believe that you will enlarge your assistance by participating in the study

Your honest and thoughtful response is invaluable

Thanks you for your participation

Kind regards,

Sofoniyas Mekonnen, MSc student

Addis Ababa University

School of Business and Public Administration

Department of Accounting and Finance

Date 1/27/2012

Part I: personal information

1.5. Level of education

B. Diploma ☐ B. Bachelor degree ☐ C. masters ☐ D. other (specify) _____

1.6. Sex

B. Male ☐ B. Female ☐

1.7. Number of years of experience

B. < 1 year ☐ B. 1-5 ☐ C. 5-10 ☐ D. > 10 year ☐

Part II- Interview questions

1. Why is it mandatory for banks to be overtly regulated by National Bank of Ethiopia (NBE)?
2. Has the Ethiopian banking industry become safe, stable and command the confidence of the general public?
3. Have the activities of banking supervisions brought about normal banking practice, professionalism and ethical conduct in the Ethiopian banking industry system?
4. Prudential regulation of banks had classified in to three: preventive, protective and supportive. According to this which method of prudential regulation followed by NBE?

Appendix -3 Organizational Structure of National Bank of Ethiopia

