



ADDIS ABABA UNIVERSITY
COLLEGE OF BUSINESS AND ECONOMICS
SCHOOL OF COMMERCE

**Opportunities for and Determinants of Private
Commercial Banks in Ethiopia: the case of Zemen Bank
S.C.**

By: Bontu Kelbessa Kera

**A Project Work Submitted to Addis Ababa University, School of
Commerce in Partial Fulfilment of the Requirements for the Degree of
Masters of Business Leadership (MBL)**

Advisor – Solomon Markos (PHD)

June, 2022

Addis Ababa, Ethiopia

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Declaration

I hereby declare that the project work entitled “Opportunities for and Determinants of private commercial Banks: Case of Zemen Bank S.C.” is my original work, prepared under the guidance of Dr. Solomon Markos at Addis Ababa University School of Commerce, hereby submitted by me, is of my own effort and study and has not been presented to any other Institution. It is presented in partial fulfilment of the requirements of the degree of Masters in Business Leadership. And all references materials contained therein have been duly acknowledged.

Name: Bontu Kelbessa Kera

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This is to certify that Bontu Kelbessa, has carried out this research Project work on the topic entitled: “Opportunities for and Determinants of Private Commercial Banks: The Case of Zemen Banks S.C.” under my supervision.

This work is submitted in partial fulfilment of the requirements for Masters of Business Leadership complies with the regulations of the University and meets the accepted standards with respect to originality and quality.

Approved by:

Advisor: Dr. Solomon Markos **Signature** _____ **Date** _____

Internal examiner: _____ **Signature** _____ **Date** _____

External examiner: _____ **Signature** _____ **Date** _____

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Acronyms

ATM -	Automated Teller Machine
GDP –	Gross Domestic Product
ICT –	Information Communication Technology
IT –	Information Technology
NBE –	National Bank of Ethiopia
NPL –	Non Performing Loans
POS –	Point of Sale
SPPS -	Statistical Package for Social Science

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Abstract

The study attempted to assess the opportunities for and determinants of private commercial banks. The study is a case study focusing on Zemen Bank S.C. It assessed the opportunities that exist and the determinants that affect the performance of private commercial banks, by focusing on two sets of factors. The first one is bank specific or internal factors (Capital Adequacy, Asset Quality, Earning Ability, Management Efficiency, Liquidity, and Bank Size), which are basically influenced by internal decisions of management and the board. The second one is macroeconomic or external factors (GDP, NBE Regulation, Exchange Rate, Inflation, Interest Rate, and ICT Infrastructure). The external factors are sector-wide or country-wide influences which are beyond the control of the banks. Primary data for the study was collected through questionnaires from employees of the bank and both quantitative and qualitative methods of data analysis are used. Descriptive research design method was employed. The findings of the study indicate that liquidity, weak management efficiency, and poor earning ability are the major internal factor determinants. Whereas, even though all the external factors highly influence performance of private commercial banks, NBE regulations, ICT infrastructure, and Inflation are the main determinants. Private commercial banks have bright prospects in the technological innovations & advancements and the economic growth of the country.

Keywords: Banking sector, Opportunities, Determinants, Internal & External factors.

CHAPTER ONE

1. Introduction

1.1. Background of the Study

Banks play an important function in the economy of any country. They are the main intermediaries between those with excess money (depositors) and those individuals and businesses with viable projects but requiring money for their investment (creditors). Banks have at least the following functions: lending money, depositing others' money, transferring money locally or globally and working as paying agent.

One of the major reasons for the existence of banks is that they are an efficient response to the fact that information is costly. They specialize in assessing the credit worthiness of borrowers and providing an on-going monitoring function to ensure borrowers meet their obligations. They are rewarded for these services by the spread between the rates they offer to the accumulated pool of savers, and the rates they offer to potential borrowers. This process is known as 'maturity transformation' and is at the heart of modern banking (King, 2003).

Banks (commercial banks), like any other businesses, aim to maximize profits, that is, they are profit-making institutions, which provide services to business and individuals through a network of branches. These banks are in business to make a profit for their shareholders and they are usually public limited companies (Moniruzzaman & Rahman, 1998).

But in the process of profit-making, we cannot ignore, the impact they have on the society and on the economy of a country. The proliferation of more businesses urging more investments, more developments, the availability, immediacy and easy access to credit, amenities brought to people who are in need of money, innumerable loan options, in fact, it sets an economy on a complete different level and allows it to thrive and compete and even become a trustworthy financial centre which will bring more investors, inevitably giving a boost to the economic activities as well as levelling the standard of living.

Private commercial banks are a recent phenomenon in Ethiopia. They came into existence after the downfall of the Derge regime. Before the Derge, in the Imperial regime, private commercial banks used to operate in the economy. But after Dergue came to power, private commercial banks were nationalized and amalgamated with the state owned banks. After the downfall of

the Derge regime, the country went through a process of financial liberalization in which private commercial banks were allowed to enter in to the banking sector (Gedey,1990).

Though private commercial banks are becoming major players in the Ethiopian economy, many factors determine their performances and have opportunities. Some are related with the internal organization of the banks themselves and others are external related with the wider macro-economic environment. Like any other business organization banks, specifically private commercial banks require a suitable business environment and global economy to operate in.

1.1.1. Background of ZEMEN BANK S.C

Zemen Bank S.C is a privately owned share company licensed by NBE in June 2008 and it started operation in October 2008 with an initial paid-up capital of Birr 95 million and the current paid up - capital of Birr 2.75 billion. The total number of branches and kiosk banking canters has reached sixty three outlets as of June 2021. To expand its service coverage, the Bank keeps on opening additional branches both in Addis Ababa and regional towns.

Zemen Bank is governed by the Board of Directors consisting of a Chairperson, a Vice Chairperson and seven Non-executive Directors. The overall management is entrusted to the management team which comprises the President/Chief Executive Officer, who is appointed by the Board of Directors, four vice presidents and sixteen various department directors. Its organizational structure has divided in to sixteen departments. As of June 30, 2021, the total number of employees of the Bank stood 1,151. (Source: Zemen Bank S.C Annual Report 2021).

The bank has its own vision and mission statement, main objectives and major services. ‘Ethiopia’s five star bank’ is its vision, while ‘deliver clients the most distinctive banking experience in Ethiopia through a mix of local know-how and world class standards, ensure staffs an engaging, rewarding and attractive work environment alongside a best in industry compensation scheme, provide shareholders satisfactory returns on a sustainable basis’ its mission statement.

The main objectives of the bank include: Maximizing profitability through increased efficiency, enhance growing market share, expanding the bank’s capital base, ensuring excellence in customer services, provide differentiated, varied and value added banking services.

The major services that the bank provides include: Accepting different types of deposits, granting varieties of loan facilities, offering full-fledged international banking services,

rendering local and international money transfer services and payment of Card services through ATM and POS network.

1.2. Statement of the Problem

Even though, the Ethiopian financial institutions have a far reaching history, the use of money and coins in Ethiopia has a long history, and the introduction of modern banking is nearly a century old. Despite the long history, which precedes the advent of modern banking throughout most of Africa, the Ethiopian financial system has not progressed that much as one expects and the problems that private commercial banks face in Ethiopia are many.

The Ethiopian economy has yet untapped large potential for commercial banking and private Banks in Ethiopia are in their infant stage. The country of 109mn people is served by just 18 commercial banks. With over 70% of the population being unbanked, the market represents a huge opportunity for new entrants (Tellimer Research, 2022). Even though they are less in number and scope; they are playing a vital role in the Ethiopian economy at the same time challenges exist in their operations.

Since Ethiopia is a country which has no capital or stock markets more than 90 percent financial saving is done by banks. The National Bank of Ethiopia has also raised the saving interest rate from 5 percent to 7 percent and yet this is less than the rate of inflation, and these problems call for extensive research that aims at assessing the impacts of low level of saving rate which is lower than the rate of inflation on in banking sector.

The private banking sector of Ethiopia passed-through different ups and downs starting from (Emperor to Derg Regime) period until the present. There are challenges and opportunities within the sector that have impeded and facilitated further performance of the sector. There are different responsible factors. While some of them are endogenous to the sector itself, others are macroeconomic factors in nature, in a sense that it is external to the banks.

To assess the prospects that exist and the different determinants that influence private commercial banks performance, the study focused on the following two sets of factors. The first one is bank specific or internal factors, which are basically influenced by internal decisions of management and the board. The second one is macroeconomic or external factors. The external factors are sector-wide or country-wide influences which are beyond the control of the banks.

1.3. Research Questions

- What are the opportunities of private commercial banks?
- What determines private commercial banks performance related to internal/bank specific factors?
- What determines private commercial banks performance related to external environment factors?

1.4. Objective of the Study

The general objective of the study is to assess the opportunities awaiting the private commercial banks in the coming years in Ethiopia and to identify the main determinants that influence private commercial banks performance in the case of Zemen bank. While the specific objectives are:-

- To investigate the opportunities of private commercial banks.
- To examine the internal factor determinants like: large liquidity and capital reserve requirement by the banks, information technology, branch expansion, human resources development and management efficiency.
- To examine the external environment determinants like: interest rate, exchange rate, inflation in the country, regulation changes, GDP, and technology infrastructures.
- To investigate the various determinants that influences the performance of private commercial banks as a whole.

1.5. Significance of the Study

The proposed outcome of this study is to provide the reader with a better understanding of the current opportunities awaiting private commercial banks in the coming years in Ethiopia and the main determinants of private commercial banks performance. Furthermore, this study can also be used by researchers or students as a reference or a guideline to do a research regarding this particular topic in the future. And this becomes even more important when one see's even though their exist a number of studies that work on this topic on the world arena, when you view the topic in the context of Ethiopia or even developing countries, it become an addition to a very limited number of studies done.

1.6. Scope of the study

The scope of the study is delimited conceptually, geographically and methodologically. The scope of this study tries to cover areas related with the opportunities and determinants of private commercial banks by being limited to Zemen Bank S.C. It does not cover the challenges on the remaining 18 commercial banks in Ethiopia. So as to understand the issue of the study and address the objective some internal and external factors that affect their performances are considered.

Methodologically, to conduct the study, descriptive research design was employed by the researcher based on the objectives of the study. Data is collected by using structured questionnaire. The study is focused on selected branches found in Addis Ababa City of Zemen Bank S.C. To collect relevant information from respondents, the researcher targeted employees working on managerial and non-managerial position in the two and seven selected departments and branches respectively.

1.7. Limitation of the study

The main limitation of the study is difficulty in access to relevant data to conduct the study and reluctance of some respondents to fill questionnaire required for data collection. Furthermore the quality of the output of this study depends on the genuine responses from the respondent and the large sample size due to the available cost and time the study conducted on the selected branches of the bank. In addition, shortage of time and lack of sufficient fund have also their own impact on the qualities of the study output.

CHAPTER TWO

2. Literature Review

2.1. Theoretical Literature

2.1.1. Banks

Banks accept deposits be it in any amount or form, they keep a percentage of it as reserve and loan out the remaining. They play a key role in channelling funds to borrowers, investors. Different loan schemes are granted to people in need, better services, safeguarding of savers money, ATMs, all types of accounts so as to provide savers with a reward as interest. Despite being the most conventional, it is also, the most diversified financial intermediary. There is a considerable theoretical and empirical study that establishes a link between banking sector's development and economic growth. This is because banks perform various roles in an economy (Levine, 2008).

Banks are often described as intermediaries between savers and users of capital. Banks are special intermediaries because of their unique capacity to finance production by lending their own debt to agents willing to accept it and to use it as money. They also allow risk-averse savers to hold bank deposits rather than pure (but unproductive) assets. Of particular importance is that banks can economize on liquid reserve holdings that do not contribute to capital accumulation (Ibid).

Also by eliminating self-financed capital investment, banks prevent the unnecessary liquidation of such investment by entrepreneurs who think that they need liquidity. In addition, banks play a role in providing payment and settlement services and fund transfers which are necessary for households, business and other financial institutions to settle day-to-day transactions. Some of the other services banks provide are; foreign exchange transactions, payroll services, financial advices, and safe-deposit boxes (Ibid).

Generally, as all economic activities nowadays revolve around the banking sector; better banks would imply lower costs, improved information dissemination, more resourceful capital allocation allowing for more productivity growth and contributing to economic development. Alexander Hamilton (1781), one of the founding fathers of the United States, once said that "banks were the happiest engines that ever were invented "for spurring economic growth. As such the efficiency of the banking system is a key determinant of sustainable growth. Thus,

banks are essential for any modern economy, not only in terms of turnover, but also as the primary financier of the national economy.

2.1.2. Emergence of Banks

At the core of the existence of banks are market frictions, which banks help to alleviate, such as asymmetric information between contractual partners resulting in agency problems and risks of illiquidity and default. Building on the insights by Stiglitz and Weiss (1983) on the importance of agency problems, several articles have shown how banks can economize on screening and monitoring costs of many individual lenders and, by diversifying risk across many different projects, improve on a world without them.

By pooling savings across a large number of savers with differently timed liquidity needs, banks can help overcome liquidity risks and ultimately provide savers with better returns. Thus the emergence of banks can be explained by the gains for economic agents, a theoretical argument that is consistent with the historical observance that banks have arisen at a stage of human history when exchange of goods and services across larger geographical distances and within larger societies or between societies had become more prominent (Ibid).

The endogenous emergence of banks does not in itself imply a positive impact on economic growth. A large theoretical literature, however, has explored several channels through which financial systems can contribute to the economic growth of a country, both through improved capital accumulation and through higher productivity growth.

2.1.3. The Role of Banks

Banks play a very important role in an economy of a country. Banks help private citizens save money, guard against uncertainty, and build credit; while enabling businesses to start up, expand, increase their efficiency, and compete in local and international markets. As such they are seen as playing a critical role in facilitating economic growth directly through broadening access to finance and indirectly through growth, contributing to poverty reduction. The importance of banks can be summarized in the following five channels.

Influential work during the late-1970s and early-1980s showed a strong positive correlation between growth of the banking sector and economic growth. It highlighted the positive role banks play in driving economic growth, particularly through their role in mobilizing savings,

allocating resources to the most productive investments, reducing information, transaction and monitoring costs, diversifying risks and facilitating the exchange of goods and services. This results in a more efficient allocation of resources, a more rapid accumulation of physical and human capital, and faster technological progress (Mishkin, 1998).

In attempting to distinguish the number of channels through which banks role in an economy of a country be seen, five (5) main channels could be listed out on how they would be able to do it:

(i). Mobilizing Savings: The costly task of the agglomeration of capital from individual savers for investment is carried out by banks. This coordination of savings and investments between households and firms allows for many production processes that would have been otherwise restricted to economically inefficient scales (Sirri and Tufano, 1995). Banks therefore induce pooling savings of the mass households, aggregating those small savings into a fund available for investment lending. More deposits will be attracted from savers which will make more funds available for investments as financial system expands. This involves (a) overcoming the transaction costs associated with collecting savings from dispersed savers and (b) overcoming the informational asymmetries associated with making savers feel comfortable about relinquishing control of their savings (Levine, 1997).

Because banks provide financial products and services such as credit cards, cheque books, internet banking, and many more, they offer the opportunity for households to hold diversified portfolios, thus enabling investors to diversify their investments and increase the asset liquidity of the overall economy. This further facilitates the bank's activities, and hence deepens the financial system of a country.

(ii). Risk Management: With the savings of individual savers agglomerated into big funds, banks are in better position to diversify the allocation of those investments across a range of economic activities. Since theory dictates that portfolio diversification is the best means to minimize risk, it thereby minimizes risk to return.

There are two types of risks, Liquidity risk which arises due to the uncertainties associated with converting assets into a medium of exchange. Informational asymmetries and transaction costs may inhibit liquidity and intensify liquidity risk, in turn limiting the ease and speed by which agents can convert assets into purchasing power at agreed prices. The second is the

idiosyncratic risk which is embedded in individual projects, sectors, industries, and countries (Levine, 1997).

Banks by helping to reduce such liquidity risk can thus enable long-term investment, as shown by Diamond and Dybvig (1983). By pooling savings of patient and impatient agents, banks can transform short-term liabilities into long-term assets, enabling long-term investment and ultimately economic growth. They can also ease liquidity needs of enterprises, enabling long-term investment and research and development activities.

(iii). Allocating resources: Since banks already engage in evaluating investment projects, they extend better credit facilities to businesses with greater prospects. This will eventually create an efficient allocation of funds towards projects with expansionary effect on the economy (Tobin and Brainard, 1963). Similarly, by identifying entrepreneurs with the most promising innovations, banks can also boost the rate of technological innovation and ultimately growth.

(iv). Monitoring performance and corporate control: As banks engage more with firms in providing services, the cost associated with the accumulation and dissemination of information falls substantially. It will be costly for an outsider investor to collect information related to prospects. And when project returns are insufficient, lenders will bear the costs for monitoring to verify the firm's performance. These verification costs may impede efficient investment (Bernanke and Gertler, 1989).

With the accumulation of extensive information on firms, banks take a more efficient monitoring position, subsequently encouraging managers to perform well. Thus, banks induce better governance and achievement of the objectives of the enterprise. Mobilizing savings can be impeded by the absence of financial agreements that enhance corporate control. It will then hinder the pooling of capital from flowing to profitable investments (Stiglitz and Weiss, 1981). As such it's with the existence of banks that monitoring costs will be reduced through proper financial arrangements.

(v). Facilitating transactions: Banks offer credit facilities and guarantees for payments which in effect is a facilitation of business transactions. They can profit by exploiting economies of scale from transforming primary securities into indirect securities in the process of lending and borrowing (Gurley and Shaw 1960).

Greenwood and Smith (1996) have modelled the connections between exchange, specialization, and innovation. Their findings indicate that more specialization requires more

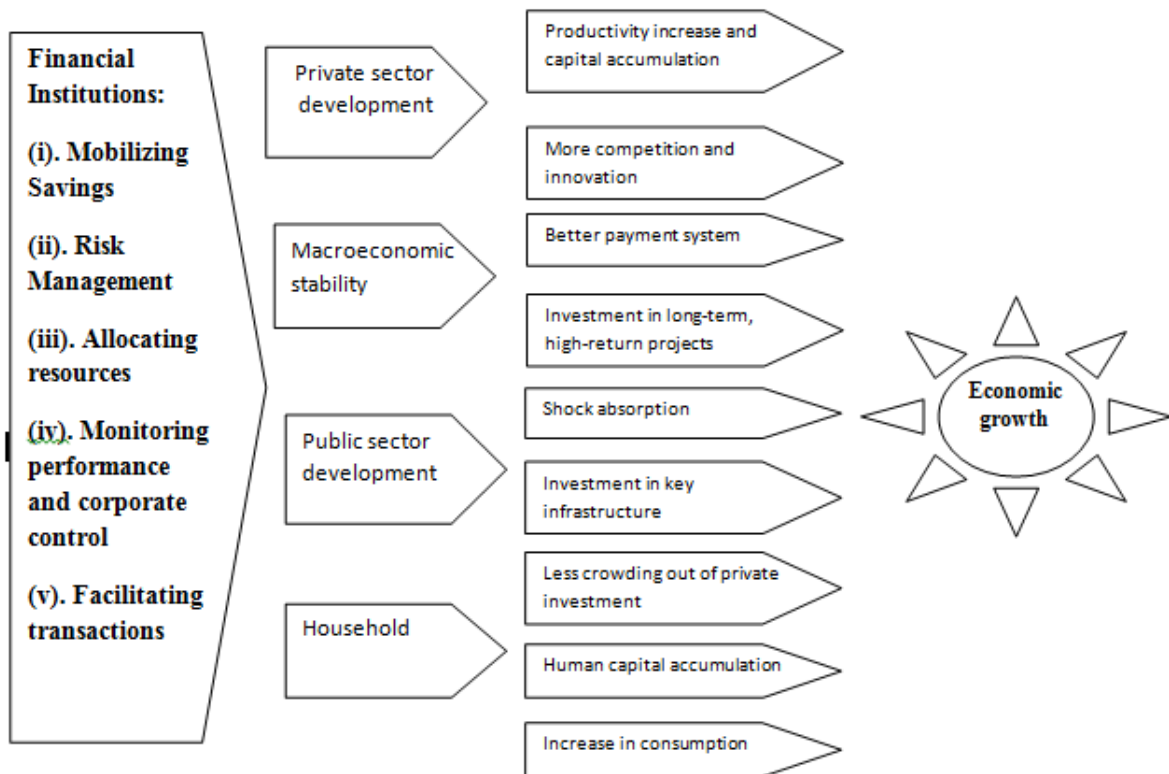
transactions. Incurring transaction costs on separate basis will be costly, financial arrangements that lower transaction costs will facilitate greater specialization and by promoting exchange, it also encourages productivity gains.

Then it's through these channels, banks exercise their impact on economic growth. Their impact also extends beyond private sector, towards public sectors and households. Public sector is impacted positively by facilitating a wider and healthier borrowing capacity to governments, allowing it to invest in key infrastructure such as roads, power plants, harbours, airports, water supply and sanitation, and telecommunications.

These key infrastructure facilities form part of the enabling environment for the private sector to grow. Moreover, active bond markets can discipline the government, thereby reducing the risks of financial crises, and prevent crowding out of private investments. These avenues provide an additional link to growth (Claessens and Feijen 2006).

Households also benefit from banks by increasing returns on and reducing risks of their invested savings. Savings enable households to smoothen their consumption. Households also borrow for a variety of reasons. By increasing consumption, the demand for goods and services increases, thus stimulating more agricultural and industrial production, leading to more jobs and higher economic growth. Households may also borrow for human capital development such as education, thus increasing employability potential and productivity that in turn impacts growth.

Figure 2.1. The Role of Banks



Source: own compilation from various literature reviewed, (2022)

Beyond theoretical models, economists have explained the take-off of the Industrial Revolution in some countries earlier than others to the availability of finance. Hicks (1969) argued that the Industrial Revolution in the United Kingdom was possible due to the development of British financial system. Although many inventions were made before the Industrial Revolution, banks enabled investment into long-term projects that could use these inventions. Similarly, the Netherlands and the United States experienced financial deepening before their economic and political rise in the seventeenth and twentieth centuries, respectively.

2.1.4. Determinants of Private Commercial Banks

To assess the determinants of private commercial banks performance, the study focused on the following two sets of factors. The first one is bank specific or internal factors, which are basically influenced by internal decisions of management and the board. The second one is macroeconomic or external factors. The external factors are sector-wide or country-wide influences which are beyond the control of the banks (Al-Tamimi & Hassan, 2010).

2.1.4.1. Bank Specific / Internal Factors

As explained above, the internal factors are bank specific factors that influence the performance and profitability of a specific bank. These factors are within the scope of the bank to manipulate and they differ from bank to bank. These include Capital Adequacy, Asset Quality, Earning Ability, Liquidity, Bank size and Management Efficiency (Dang & Uyen, 2011). Each of these indicators is further discussed below.

Capital Adequacy

Capital is one of the bank specific factors that influence the level of bank performance and profitability. It is the amount of own fund available to support the bank's business and acts as a buffer in case of adverse situation (Athanasoglou, Sophocles, & Matthaios, 2005). A banks capital creates liquidity for the bank due to the fact that deposits are most fragile and prone to bank runs. Moreover, greater bank capital reduces the chance of distress (Dang & Uyen, 2011).

Capital adequacy is the level of capital required by the banks to enable them withstand risks such as credit, market and operational risks they are exposed to, in order to absorb the potential loses and protect the bank's debtors. According to (Dang & Uyen, 2011), the adequacy of capital is judged on the basis of capital adequacy ratio (CAR). Capital adequacy ratio shows the internal strength of the bank to withstand losses during crisis. Capital adequacy ratio is directly proportional to the resilience of the bank in crisis situations. It has also a direct effect on the performance and profitability of banks by determining its expansion to risky but profitable ventures or areas (Sangmi & Tabassum, 2010).

Capital adequacy is a reflection of the internal strength of a bank, which would stand it in good stead during the times of crisis. Capital adequacy has a bearing on the overall performance of a bank, like opening of new branches, fresh lending in risky but profitable areas, manpower recruitment and diversification of business through subsidiaries or through specially designated branches, (Shankar, 1997). The NBE has set specific measure of the capital adequacy position of banks operating Ethiopia, which is the ratio of Capital adequacy (NBE Directives No.SBB/9/95). The directive clearly set out the computation mechanism and the conversion factors for both on and off-balance sheet items and strictly set for all banks not to maintain their capital level below 8% of their risk weighted assets.

Capital adequacy is measured by the ratio of equity capital to total risk weighted assets. Bank equity capital can be seen in two dimensions as stated by (Brooks, 2008), that is the amount contributed by the owners of a bank (paid-up share capital) and the amount of owners funds available to support a bank's business which includes reserves, and is also termed as total shareholders' funds. Banks capital is widely used as one of the determinants of bank performance since it indicates the financial strength of the bank (Athanasoglou, Sophocles, & Matthaios, 2005). Capital adequacy requirements generally aim to increase the stability of a national banking system by decreasing the likelihood of a bank failure and a number of negative externalities exist in banking that cause risk to systematically under price.

Asset Quality

A bank's asset is another bank specific variable that affects the performance and profitability of a bank. A bank's asset includes among others current asset, credit portfolio, fixed asset, and other investments. Often a growing asset size is related to the age of the bank (Athanasoglou et. al, 2005).

Asset quality is a measure of ability to manage credit risk for a bank or financial institution. It reflects the composition and productivity of the assets. Thus, asset quality has a direct impact on the performance of a bank. As per Yuqi , 2006, in terms of risk, poor asset quality is the major cause for banks poor performance. It is evaluated by understanding the performance of assets category wise and estimating future performance factoring in the likely distribution of the assets in future. The bank's experience of loan loss, provisions/ write off, loan recovery rate, ability to reduce nonperforming assets and extent of weak assets are to be analysed in this regard.

Loan is the major asset of commercial banks from which they generate income. The quality of loan portfolio determines the performance of banks. The loan portfolio quality has a direct bearing on bank performance and profitability. The highest risk facing a bank is the losses derived from delinquent loans (Dang & Uyen, 2011).

Thus, nonperforming loan (NPL) ratios are the best proxies for asset quality. It is the major concern of all commercial banks to keep the amount of nonperforming loans to low level. This is so because high nonperforming loan affects the performance and profitability of the bank.

Thus, low nonperforming loans to total loans shows the good health of the asset portfolio a bank. The lower the ratio, the better the bank is performing (Sangmi & Tabassum, 2010).

Non -performing loans can be defined as defaulted loans, which banks are unable to profit from. Usually loans fall due, if no interest has been paid in 90 days, but this may vary between different countries and actors. Defaulted loans force banks to take certain measures in order to recover and securitize them in the best way. Loans become nonperforming when it cannot be recovered within certain stipulated time that is governed by respective laws. Non- performing loans are defined from an institutional point of view. (Ayalew, 2009)

The definition of non-performing loan varies across economies. For Australia and New Zealand, they use the ratio of non-performing assets to total assets in the banking sector. According to NBEs directive number SBB / 48 / 2010, 'non -performing loans' means whose credit quality has deteriorated such that full collection of principal and / or interest in accordance with the contractual repayment terms of the loan or advance is in question. The definitions of non – performing loans by the NBE is that loans that are not repaid in more than three months will be considered as non – performing loans.

Non-performing loans are also sensitive to external macroeconomic factors. The existing literature provides evidence that suggests a strong association between NPLs and several macroeconomic factors such as annual growth in GDP, credit growth, real interest rates, annual inflation rate, real effective exchange rate, annual unemployment rate, broad money supply and GDP per capital (Khemraj, 2004).

Earning Ability

The quality of earnings is a very important criterion which represents the quality of a bank's performance and its capability to maintain quality and earn consistently. It primarily determines the performance and profitability of bank and explains its sustainability and growth of future earnings (Khrawish, 2011).

The quality and trend of earnings of a bank depend largely on how well the management manages the assets and liabilities of the bank. A bank must earn reasonable profit to support asset growth, build up adequate reserves and enhance shareholders value. Good earnings performance would inspire the confidence of depositors, investors, creditors, and the public at large.

The quality of earnings of a bank determines the ability of the entity to meet debt obligations, the rate of growth of assets, reserves and ultimately the shareholders' value. The quality of earning coupled with the cost impacts profitability. The quality of earning is also affected by the extent of asset liability mismatch and the resultant volatility in earnings due to changes in the interest rate (Bikker & Hu, 2002). Generally a bank that depends more on leverage will experience more volatile earnings and this also affects the credit creation and liquidity function of the bank (Tobias & Themba , 2011).

Liquidity Management

Liquidity is another factor that determines the level of bank performance. Liquidity refers to the ability of the bank to fulfil its obligations, mainly to depositors. According to Dang & Uyen, 2011, adequate level of liquidity is positively related with bank performance. The most common financial ratios that reflect the liquidity position of a bank according to the above author are customer deposit to total asset and total loan to customer deposits. Other scholars use different financial ratio to measure liquidity. For instance Ilhomovich, 2009, used cash to deposit ratio to measure the liquidity level of banks in Malaysia.

In the Ethiopian context there seems clear measure of the liquidity of a bank: the liquid asset to deposit ratio, which the National Bank of Ethiopia, has set the minimum liquid asset of a bank not to be less than 15% of the Bank's net current liability. Out of this the, directive obliged banks to hold 5% of them in primary reserve assets (NBE Directives No.SBB/9/95).

Bank Size

Bank size which can be measured by total deposits (Dietrich & Wanzenried, 2009) or assets (Smirlock, 1985) is one of the important variables that determine the financial performance of the commercial banks (Kosmidou K., 2008). If the relative size of a firm expands, its market power and profits increases. This is the Market-Power (MP) hypothesis which is also referred to as the Structure Conduct-Performance (SCP) hypothesis (Athanasoglou, Sophocles, & Matthaïos, 2005).

One of the most important questions underlying bank policy is which size optimizes bank performance, because there is no clear cut point which indicates the relation of appropriate bank size and its performance. The effect of a growing size on performance has proved positive to a certain extent. Larger banks are better placed to than smaller banks in harnessing

economies of scale in transactions to the plain effect that they will tend to enjoy higher levels of profit. However, for banks that become extremely large, the effect of size could be negative due to bureaucratic and other reasons (Athanasoglou, Sophocles, & Matthaios, 2005).

Management Efficiency

Management efficiency has to do with a bank's ability to use its resources efficiently, increasing revenue, and lowering operating costs. It also assesses the bank's efficiency in terms of maximizing profits per employee. It will depend on the vision, capability, agility, professionalism, integrity, and competence of the financial institutions management. A sound management is crucial for the success of any institution. The performance of a bank is largely dependent on the vision, competence, and integrity and risk appetite of the management, and also financial management and analysis of Projects. Efficiency is one of the key internal factors that determine the bank performance.

Moreover, operational efficiency in managing the operating expenses is another dimension for management quality. The performance of management is often expressed qualitatively through subjective evaluation of management systems, organizational discipline, control systems, quality of staff, and others. Yet, some financial ratios of the financial statements act as a proxy for management efficiency. The capability of the management to deploy its resources efficiently, income maximization, reducing operating costs can be measured by financial ratios.

2.1.4.2. External Factors

Those factors which are beyond the managements control are referred to as external or macroeconomic factors and are related to the industry and macroeconomic environment. The external determinants are variables that are not related to bank management but reflect the economic and legal environment that affects the operation and performance of financial institutions. Several of these macroeconomic factors are discussed below.

Regulation

Regulation at its most basic level is synonymous with law. According to Orbach (2012) regulation is state intervention in the private domain. Regulations also refers to a process in which there is a monitoring of financial institutions by a body that is directed by a government

in an effort to achieve macroeconomic goals through monetary as well as other measures permissible by law (Vittas, 1992).

Banks are one of the most heavily regulated industries, with rules and requirements surrounding every bank activity. When it works well, bank regulation helps ensure the safety and soundness of the overall banking system. Without any regulation, politicians assume that value-maximizing banks take on more risks than which is optimal and acceptable for depositors. When it doesn't, the natural cycle of banks facilitating credit, job growth and economic expansion is constricted. Finding the right balance is the key to economic prosperity.

Bank regulations cover every aspect of banking including safety and soundness and consumer protection. Regulatory responsibilities for banks include reporting suspicious activity to the government to prevent money laundering and other criminal activities. There are many aspects that together form the regulatory environment in which banks operate, such as the level and complexity of the laws and regulations and how those laws are interpreted and enforced.

Furthermore, according to Saunders and Cornett (2008) the net regulatory burden could also negatively influence bank performance. The net regulatory burden equals the cost minus the benefits of regulation. Costs of regulation are; compliance costs, referring to the costs of preparing reports and statements to regulators; or costs of being restricted from an optimal portfolio or capital structure (Nkegbe & Yazidu, 2015).

With this in mind, the regulatory body of the financial sector in Ethiopia, National Bank of Ethiopia (NBE) issues a number of regulations, directives, supervision, and rules that govern the operations of banks that operates in the country. These range from the most popular one with directive No. MFA/NBE Bills/001/2011 that required all private commercial banks to invest 27% of their every new loan disbursements on NBE bills purchase for five years at a very low interest rate; to directive FXD/54/2017 that calls for a surrender of thirty percent (30%) of all foreign currency inflows to the NBE on a monthly basis; and the most recent directive FXD/79/2021 governing the retention and utilization of foreign currency earnings from export and inward remittance. The implementation of National Bank of Ethiopia's regulations and directives has been a major challenge to the performance of private commercial banks (Eden 2014, Addisu 2017).

GDP

GDP is the sum of the value added in the economy during a given period or the sum of incomes in the economy during a given period adjusted for the effect of increasing prices (Daferighe & Aje, 2009). A study by Ugbede, Otache and Umar (2012) on the impact of Commercial Banks Credit on Nigeria's GDP discovered that Commercial banks credit has a high positive impact on the nation's GDP, meaning the higher the volume of Commercial banks credit made available, the higher the corresponding GDP.

Favourable economic conditions will affect positively on the demand and supply of commercial banks services, especially on intermediary businesses. Hence, the possibility of positive turnover on the commercial banks operation is highly expected when there is conducive macroeconomic environment, and vice versa.

Inflation

Inflation is another important macro-economic variable that affects bank performance (Perry, 1992). In particular, inflation affects companies' pricing behaviour. For instance, if companies expect general inflation to be higher in the future, they may believe that they can increase their prices without suffering a drop in demand for their output (Driver and Windram, 2009).

If inflation is anticipated, the interest rates are adjusted accordingly, which results increase in revenues faster than costs and will have positive effect on the performance of banks. On the contrary, in unanticipated case, banks may be weak in adjusting their rates of interest resulting in a faster increase cost of banks than revenues and accordingly, having negative effects on performance.

Infrastructure

The application of E-banking methods like ATM's, debit cards, credit cards, tele-banking, internet banking, mobile banking and others through the use of modern technologies presents a good prospect for the growth and development of the businesses of commercial banks. E-banking refers to the use of modern technology that allows customers to access banking services electronically whether it is to withdraw cash, transfer funds, to pay bills, or obtain commercial information and advices.

The main challenge for commercial banks in Ethiopia to seize the opportunities presented by ICT applications is the poorly developed telecommunication infrastructure in the country that results in low level of internet penetration, which is worse in rural areas and also the high cost of telecommunication devices and internet (Worku, 2010).

Interest Rate

Manchara (2016) proclaim that interest rate risk arises from movements in interest rates. A bank is exposed to interest rate risk when it experiences a situation of imbalance in terms of size or maturity dates between assets and liabilities sensitive to interest rates, leading to potential losses for the bank when interest rate increases or declines and this influences the net asset value in the budget, which some call risk gap (Claudiu and Daniela, 2009). In the scenario of rising interest rate, when liabilities re-price faster than assets, interest spread would fall and hence performance of the bank would be adversely affected.

Accepting this risk is a normal part of banking business and can be an important source of profitability. However, excessive interest rate risk can pose a significant threat to banks' earnings and capital base. Changes in interest rates affect banks' earnings by changing their net interest income and the level of other interest sensitive income and operating expenses.

Companies face interest-rate risks from the interest-rate sensitivity of their debts and/or their investments. However, for non-financial service companies, the risks from interest-rate sensitivity of their debts would usually outweigh the risks from their investments. The impact of interest rates on the business will depend on the choice of funding: the mix between capital and debt; the mix between fixed and floating rate debt; and the mix between short-term and long-term debt. There are a number of factors that need to be considered when deciding whether to use fixed-rate or floating-rate instruments: The expectation of future interest-rate movements. If interest rates were expected to fall, a floating rate would be more attractive to a borrower. Interest-rate changes would be easier to predict in the short-term than in the long-term. A mix of fixed and floating-rate instruments ensures diversification of interest rate exposure and acts as a natural hedge (Collier 2009).

According to Dawit (2017), the goal of interest rate risk management is to maintain a bank's interest rate risk exposure within self-imposed parameters over a range of possible changes in interest rates. As expressed in Basel Committee on Banking Supervision (2003), a system of interest rate risk limits and risk taking guidelines provides the means for achieving that goal. Such a system should set boundaries for the level of interest rate risk for the bank and where appropriate, should also provide the capability to allocate limits to individual portfolios, activities or business units. Limit systems should also ensure that positions that exceed certain predetermined levels receive prompt management attention. An appropriate limit system

should enable management to control interest rate risk exposures, initiate discussion about opportunities and risks and monitor actual risk taking against predetermined risk tolerances. Limits should be consistent with overall approach to measuring interest rate risk. Aggregate interest rate risk limits clearly articulating the amount of interest rate risk acceptable to the bank should be approved by the board of directors and re-evaluated periodically. Such limits should be appropriate to the size, complexity and capital adequacy of the bank as well as its ability to measure and manage risk (Amdemikael, 2012).

Foreign Exchange rate

According to Demburg and McDougall (1980), exchange rate is defined as the domestic price of foreign currency which can be determined either administratively or by the market forces of demand and supply of currencies. The importance of this definition is that it focuses on the concept of price as a nature of exchange rate. Official exchange rate refers to the exchange rate determined by national authorities or to the rate determined in the legally sanctioned exchange market. It is calculated as an annual average based on monthly averages (local currency units relative to the U.S. dollar).

The basis for exchange rate determination has been on the premise of purchasing power parity (PPP) concept as enunciated by Cassel (1918). Purchasing power parity concept defines exchange rate as the amount of the currency of one country, which endows the holder with the same amount of purchasing power. Expressed differently, purchasing power parity theory states that the same collection of goods purchased with different currencies should have same cost as measured in any of the currencies (Cooper and Fraser, 1990). The implication of the PPP in the short run is that a nation's currency will tend to depreciate in the foreign exchange market when its rate of inflation exceeds that of other nations and appreciates when its inflation rate is the relatively lower (Cookey,1997).

Foreign Exchange risk arises when a bank holds assets or liabilities in foreign currencies and impacts the earnings and capital of bank due to the fluctuations in the exchange rates. No one can predict what the exchange rate will be in the next period, it can move in either upward or downward direction regardless of what the estimates and predictions were. This uncertain movement poses a threat to the earnings and capital of bank, if such a movement is in undesired and unanticipated direction (Evans, 2014). Thus this variable has significant and positive impact on banks performance.

2.1.5. Prospects of Private Commercial Banks

Obviously, as the Ethiopian economy grows it creates a lot of potential for private commercial banks. Their customer base expands and Ethiopia is also a country with a large population and this is one of the indicators that the untapped potential in the sector is immense. Not only that, since foreign investors are not allowed in the sector, investment in the banking sector is attractive to domestic investors than other sectors.

And that the bank's share price is presumed to rise and the high yields to continue and thrive, selling shares to easily raise more equity capital from the market. However, there is no absolute price of shares, as the value of a share is what people who invest their monies in public shares are prepared to pay for it. (Access capital, 2010).

While different kinds of businesses are floating shares to raise capital to undertake various economic activities in sectors such as brewery, cement, agro-industry, trade, transportation, oil, eco-energy, and health; bank shares seemed more attractive, they seem unable to raise the required capital to start their businesses from the share market within the specified share floating period. The growing economy is sparking more investment in the banking business, expanding the industry in which more and more private banks are floating shares to raise capital in the public market.

Given the good health of the economy, and attractive profits declared in the private banking industry, investors are attracted to invest to this sector with the hope that their future value of their shares and yield. As a result, so far, many banks have floated shares to raise the required capital to start a banking business (Simeneh, 2012).

Technologies in Banking Sector

Nowadays, banks can use advanced technologies and internet, networks, payment cards, Automated Teller Machine (ATMs) and so on. This is one of the prospects that enables banks to increase the efficiency and productivity.

The banking business has continued realizing the advantages of the cutting-edge information and communication technology. It has become essential to effectively implement the appropriate technology to have faster decision support and effective data integration in the

financial intermediary process and also to look for other avenues to augment income (Simeneh, 2012).

In this regard, Ethiopian banking system is one of the most underdeveloped compared to the rest of the world. In Ethiopia cash is still the most dominant medium of exchange and electronic-banking is not well known, let alone used for transacting banking business. Most banks in Ethiopia are too late to move with technological advancement and they should clearly chart out the time schedule for their integration and technological advancement (Ibid).

Many banks have changed their system from the previous computer systems which does not have a centralized database to different kinds of soft wares which can enable them centralized database processing as well as distributed one. They have a network among their branches in different parts of the country so that any branch can access the database from those branches.

This means all the branch banks will have their own database of users, which as well be propagated to the central server of the bank. This helps the recovery of data easier than that of the previous system. If the servers at the branches crash the data can be reclaimed from the central database since the data from the branches is synchronized with the central server. The changes have not only affected the software part, but also the hardware that the previous system used to use. This includes the change in computers and network facilities and high speed computers with high memory and hard disk capacity have been introduced.

2.1.6. Indicators of Banking Development

Before proceeding to the indicators of banking sector development, it is important to internalize the concept of banking sector development. The concept of the development of the banking sector is a multi-dimensional concept and is not easy to find a single definition of this process as it is an interrelated process that includes improvements in the quantity and quality of financial services. Some of these dimensions are related to the mobilization of savings, credit granting and risk management. And thus the degree of the development of the banking system in any country is measured by its ability to deliver these functions efficiently (Touny,2014).

2.1.6.1. Banking Access

The underlying developments in the banking sector can be captured in terms of access to the basic banking services for the public at large. Some of the proxies used include:

- Broad Access: Branch and ATM density, Average loan and deposit size, and loan and deposit; and accounts per capita.
- Household Access: percentage of people with bank accounts.
- Firm Access: Collateral needed for loan, and percentage of firms with financial constraints.

Indicators for access

As per Financial Sector Operations and Policy department of the World Bank, new indicators are introduced to distinguish between access and the use of financial services. Access to financial service includes geographic and demographic access.

- Geographic: Number of bank branches per 1,000 sq. km., number of bank ATMs per 1,000 sq. km.
- Demographic: Number of bank branches per 100,000 people, Number of bank ATMs per 100,000 people.

Indicators for usage

The use of financial services can be gauged through the following indicators:

- **Number:** Number of loans per 1,000 people, number of deposits per 1,000 people
- **Size:** Average size of loans to GDP per capita, average size of deposits to GDP per capita

2.1.6.2. Banking Efficiency

Efficiency refers to the optimum output that can be obtained from any given level of input used. According to Chen (2001) cited by Das and Drine (2011), the efficiency of the banking sector can be decomposed into:

- Scale efficiency,
- Scope efficiency,
- Pure technical efficiency, and
- Allocative efficiency.

A bank is said to have scale efficiency, when it operates in the range of constant returns to scale and have scope efficiency, when it operates in different diversified locations. Maximizing

output from a given level of input is called technical efficiency and when a bank chooses the revenue maximizing mix of output, the allocative efficiency occurs. Cited by Das & Drine, according to Farrell (1957), the efficiency of a firm consists of two components, the 'technical efficiency' and the 'allocative efficiency'. The combination of these is the measure of total economic efficiency'.

Measurement of efficiency of banking institutions serves two important purposes. It helps to benchmark the relative efficiency of an individual bank against best practices in the sector and secondly, it helps to evaluate the impact of various policy measures on the efficiency and performance of these institutions. As the banking system provides transaction services and payment system, an efficient banking system has significant positive externalities, which increases the efficiency of economic transactions in general (Das, Nag & Ray, 2004).

2.1.6.3. Banking Stability

The stability of the banking system is one of the features that can manifest in whether the banking sector is exposed to larger shocks and risks or its development in managing such risks systematically. John & Kick (2010) asserted that regular financial stability assessment and the identification of early warning indicators signalling coming risks to the banking system are major tasks of central banks and supervisory authorities. A safe and sound banking system ensures the optimal allocation of capital resources, and regulators therefore aim to prevent costly banking system crises and their associated adverse feedback effects on the real economy.

Banking sector stability and soundness may also be impacted by the strategic measures and reforms that are taken by the government to develop it. From among, slashing government borrowing and creating a stable macroeconomic environment did much to ease lending rates and reduce spreads. Increasing banks capital requirements, introducing a limited deposit insurance scheme, and provisioning aggressively against non-performing loans also contributed to greater banking sector stability (Beck et.al, 2010).

2.1.7. Features of Banking in Sub-Saharan Africa

Banks pre-dominate the financial sector in sub-Saharan Africa (SSA). With a few exceptions (for example, Botswana, Namibia, South Africa and Swaziland), the banking sector accounts for more than 75 percent of total financial system assets; and in fact in a number of African countries, the share is above 90 percent (Fuchs, Muller & Witte, 2013).

Banking systems in most of SSA remain underdeveloped as compared with other developing regions, but gradual financial deepening is underway in most countries. Impediments to development include the small size of national markets, low income levels, and weak creditor rights and judicial enforcement mechanisms (Mlachila, Park & Yabara, 2013). However, the banking systems accounted for the majority of financial sector assets and activities. The depth and coverage of financial systems measured by the ratios of broad money (M2) and private sector credit to GDP—have been gradually increasing over the past two decades, albeit from a low base. But the scale of financial intermediation in the region remains significantly lower than in other developing regions of the world and access to financial services is also relatively low.

These stylized features of SSA banking systems reflect a combination of factors, including the small size of banks and banking systems; low income levels, large informal sectors, low levels of financial literacy; weak contractual frameworks for banking activities, including weak creditor rights and judicial enforcement mechanisms; and political risk. The following features of banking sector in Africa are also worth mentioning.

- In many countries, banking systems are characterized by significant excess liquidity. In such circumstances, monetary policy is relatively ineffective as a tool for influencing lending conditions and the broader monetary aggregates.
- Banks have moved to strengthen their capital bases and improve risk management. As a result, the incidence of systemic banking crises has declined markedly, with only one major crisis recorded since 1995.
- African banking systems rely on the domestic economy for their funding base.
- The economic importance of banking systems in SSA economies varies significantly across countries reflecting differences in economic size, population density, legal code, resource dependence, and history.

Sub-Saharan African financial activity can be characterized by the oligopolistic behaviour of few commercial banks (in several cases, government-owned). The absence of adequate competition is reflected in the large gap between deposit rates for savers, which tend to be very low, and interest rates for borrowers, which tend to be very high. In most African countries, there is still not enough access to credit. Research by Kim & Captein (2012) shows that although too much credit hampers economic growth. This is the case only when the ratio between credit

and GDP exceeds 100 percent. All Sub-Saharan African countries except for South Africa and Mauritius are far below this threshold. Kenya's ratio is highest at 37 per cent and many countries are below 20 percent.

2.1.7.1. Banking Sector in East Africa

The status of commercial banking business in the region where Ethiopia is located – Intergovernmental Authority on Development (IGAD) sub-region shows that the financial system constitutes various institutions among which commercial banks are dominant. Modern commercial banking in some parts of the region started in the early 1990s, but banking activity has remained passive and rudimentary since then. Some possible factors in the low development of the financial sector are: the weak economies of member countries and limitations on the forward and backward linkages between the real and financial sectors and lack of basic infrastructures. Frequent conflicts (which seem to be a peculiar feature of the eastern part of Africa) and resource limitations explain the underdevelopment of commercial banking business (Abdi & Aragie, 2012).

The development and sophistication level of the banking sectors varies significantly across the region, with Kenya having one of the most dynamic and largest banking sectors in sub-Saharan Africa, and a significant presence in the other East African Community (EAC) countries. The banking sectors of the other countries are concentrated on their local markets. The sophistication of capital markets in East Africa differs across the region, but in general, they remain underdeveloped. There are important cross-country differences, with some markets at an early stage of development, while Kenya's market is reasonably well-developed in sub-Saharan African context (Zajc, 2013).

2.1.8. Banking in Ethiopia

One can trace the history of using modern money in Ethiopia to more than 2000 years (Pankhrust in Gedey, 1990). This had flourished in what is called the Axumite era which stretched from 1000BC to around 975 AD. Leaving that long history aside, history of banking in Ethiopia can be classified in to three main periods, from the start of modern banking in Ethiopia with the establishment of Abyssinian Bank in 1905, until now.

1. The Imperial period (pre-1974)

The establishment of the Abyssinian bank was based on a fifty year agreement with the Anglo-Egyptian National Bank. When the Bank started operation Mr. D. Mack Glivime was appointed as the first governor of the Bank. At that time, the uses and services of a bank were not widely known by the public, and many of its customers were foreigners and only few Ethiopians who knew the uses of a bank were customers. The public rather than putting its money in a bank for a small amount of interest, preferred to buy land. Because the public didn't know about the services of a bank, the bank had to face many problems. The uses of a check were not known at all, and only few foreigners used it.

After the Ethio–Djibouti rail started operation in 1894 the business of the bank started to expand. To widen its reach in the country the Bank had expanded its branches to Dire Dewa, Gore and Dessie. It also had an agency and a transit office in Gambella and at the port of Djibouti respectively (Gedey, 1990).

In 1908 a new development bank called Societe Nationale d' Ethiopie Pour le Development de l'Agriculture et du Commerce and two other foreign banks (Banque de l'Indochine and the Compagnie de l'Afrique Orientale) were also established (Gedey, 1990). These banks were criticized for being wholly foreign owned. In 1931, the Bank of Abyssinia was replaced by the Bank of Ethiopia which was wholly owned by the government and members of the Ethiopian aristocracy, becoming the first fully African-owned bank on the continent. It was also authorized to issue notes and coins and to act as the government's bank (Befekadu, 1995).

The Bank of Ethiopia operated until 1935 and ceased to function because of the Italian invasion. During the five years of the Italian occupation (1936-41), there was an expansion of banking activity. Many branches of the Italian Banks such as Banco di Italiy, Banco di Roma, and Banco di Napoli were operational in the main towns of Ethiopia. Table 2.1 shows banks that were in operation during this period.

Table 2.1: Banks in operation during the brief period of Italian occupation (1936-41)

Year of establishment	Bank name	Number of branches
1934	Banco di Italy	9
1934	Banco di Roma	18
1939	Banco di Napoli	4
1939	Banco Nazionale (De'sVoro)	4
1939	Casa de Creito	1
1939	Society Nazionale di Ethiopia	1
Total		37

Source: Gedey, B. (1990) Money, Banking and Insurance in Ethiopia, Addis Ababa: Berhanena Selam Printing Press (in Amharic).

After independence from Italy's brief occupation, where the role of Britain was paramount owing to its strategic planning during the Second World War, Barclay's Bank was established and it remained in business in Ethiopia between 1941 and 1943. Following this, in 1943, the Ethiopian government established the State Bank of Ethiopia with a capital of one million Birr. The establishment of this bank by Ethiopia was a painful process because Britain was against it. It became operational with 43 employees and two branches, and acted as the country's central bank, with a Canadian first governor, as well as the country's main commercial bank. The country's first development bank was founded in 1951: the World Bank provided USD 2 million towards the founding of the Development Bank of Ethiopia, and invested a further USD 2 million in 1960.

In 1963, a new banking law split the functions of the State Bank of Ethiopia into central and commercial banking as the National Bank of Ethiopia and the Commercial Bank of Ethiopia respectively. Both were government-owned. This banking law also allowed for other commercial banks to operate in the country. This included foreign banks provided they were 51% owned by Ethiopians. The biggest of these was the Addis Ababa Bank. It was 40% owned by Grindlays Bank (British owned) and had 26 branches by 1975. There were also two foreign commercial banks: the Banco di Roma and the Banco di Napoli, which had eight branches and one branch respectively in 1975 (Gedey,1990).

In addition to the commercial banks, the government established two development banks, both of which were 100% state owned. The Agricultural and Industrial Development Bank (AIDB)

was set up in 1969, taking over two earlier development banks: the Development Bank of Ethiopia and the Ethiopian Investment Corporation which had been established in 1963 as the Investment Bank of Ethiopia. AIDB was 100% government- owned, and provided short, medium and long term loans to the agricultural and industrial sectors. The Housing and Savings Bank was created in 1975 out of a merger between two earlier housing finance institutions created in 1962 and 1965, one of them with a grant from the United States government.

Table 2.2: Banks in Operation before 1974 in Ethiopia

Year of establishment	Bank name	Number of branches before 1974	Capital before 1974 (in millions Birr)
1939	Banco di Napoli	1	2
1963	Imperial Saving and Home Ownership Public Association	1	0.6
1963	National Bank of Ethiopia, NBE	4	10
1963	Commercial Bank of Ethiopia, CBE	65	35
1963	Addis Bank Share Co.	25	5
1964	Ethiopian Investment Corporation S.C.	1	20
1966	Banco di Roma (Ethiopia) S.C.	8	4
1969	Agricultural and Industrial Development Bank	5	100
Total		110	176.6

Source: Gedey, B. (1990) *Money, Banking and Insurance in Ethiopia*, Addis Ababa: BerhanenaSelam Printing Press (in Amharic).

2. The Derg period (1974-1991)

The pre-reform period here refers to the Derg period from 1974 to 1991. This was a regime characterized by absolute government control of major economic activities in the country. During this period all privately owned financial institutions including three commercial banks, thirteen insurance companies and two non-bank financial intermediaries were nationalized on 1 January 1975 and converted into institutions organized along socialist principles.

The nationalized banks were reorganized into one commercial bank (the Commercial Bank of Ethiopia), a National Bank (recreated in 1976), two specialized banks (the Agricultural and Industrial Bank (AIDB) – renamed today as the Development Bank of Ethiopia; and the

Housing and Saving Bank (HSB) – renamed also as the Construction and Business Bank) as well as one insurance company – Ethiopian Insurance Company. The National Bank of Ethiopia (NBE) was at the apex of the banking structure and was engaged in all the functions of a central bank (Alemayehu 1999).

The CBE, followed by the AIDB, were the most important banks in the country during that time. During the immediate years before the fall of the Derg, on average the CBE alone accounted for more than 90% of total deposit mobilized in the country, (while AIDB's share was 1.3%), and its share was the highest for demand deposits (100%) followed by saving (96%) and time (45%) deposits.

Of the total loans advanced, looking at the immediate years before the fall of the Derg (meaning 1981/82 – 1990/91), CBE and AIDB accounted for 63% and 32% of it respectively. When these loans advanced are examined based on clients, public enterprises took the lion's share followed by the private sector. On the other hand, when they are examined from a sectoral perspective, the agricultural sector came on top with 25%.

As the case of Ethiopia shows, the creation of a sound financial system together with an appropriate regulatory framework is not a straightforward task. During the era of state socialism (1974 to 1991), Ethiopia's financial institutions were charged with executing the national economic plan; state enterprises received bank finance in accordance with the plan's priorities. This system, based on the template of the Soviet Union, saw little need to develop the tools and techniques of financial regulation and supervision found in market-based financial systems. (Geda, 2001)

3. The post Derg period (post 1991)

Following the regime change in 1991 and the subsequent measures taken to liberalize and reorient the economy towards a system of economy based on commercial considerations, the financial market was deregulated and the former financial institutions were reorganized to work in a market-oriented-policy framework. CBE, EIC and NBE have retained their names and functions, whereas AIDB was renamed as Development Bank of Ethiopia (DBE), and HSB was renamed as Construction and Business Bank (CBB).

After proclamation number 84/94 was issued out to effect the deregulation and liberalization of the financial sector, a number of private banks and insurance companies were established.

Directives issued in subsequent years further led to gradual liberalizations of the interest rate, foreign exchange determination, and money market operation (Alemayehu and Seife, 2001).

At present, the Ethiopian financial sector consists of 2 public banks; Development Bank of Ethiopia and Commercial Bank of Ethiopia (there were 3 public banks until Dec. 2015 when Construction and Business Bank merged with Commercial Bank of Ethiopia (capital Ethiopia, 2015)), 17 private banks and over ten new banks under formation., 1 public insurance company, 17 private insurance companies, 39 microfinance institutions and over 8200 Saving and Credit Cooperatives (SACCOs) in both rural and urban areas. The ownership structure of microfinance institution is mixed, with the big microfinance institutions partially owned by regional states, some by NGO's and some by private owners (NBE, 2020/2021).

Currently, Ethiopian private commercial banks offer four major services in all of their branches namely saving schemes, credit facility, international banking and fund transfer. Some of the credit lines banks offer includes; overdraft facilities, term loans, letter of credit facilities, merchandise loans and personal loans. The other service the banks render is deposit services including demand deposit (that can be operated with cheques), savings deposit, time/fixed deposit and other specialized savings accounts.

The banks also render international banking services providing services like; opening letters of credit for importers, handling of incoming LCs for exporters, purchasing and selling of foreign currency denominated notes, receiving and transferring foreign currency payment by swift and handling incoming and outgoing international letters of guarantee. Moreover, some of the banks are also providing customers with card payment systems that can be used internationally (Yimam, 2015).

2.1.9. Outlook of the Banking Sector in Ethiopia

The last three decades have seen some improvement in the works of various participants of the banking sector in Ethiopia. The government and the National Bank of Ethiopia have followed a step-by-step approach in transforming the sector, not a big bang one. For instance the entry of foreign players is still prohibited. But the introduction of new technological solutions such as the CORE-Banking system has improved customer service.

Some gaps however remain such as lack of an inter-bank interest rate benchmark, absence of an active secondary market for debt and equity instruments and money market. Besides, the

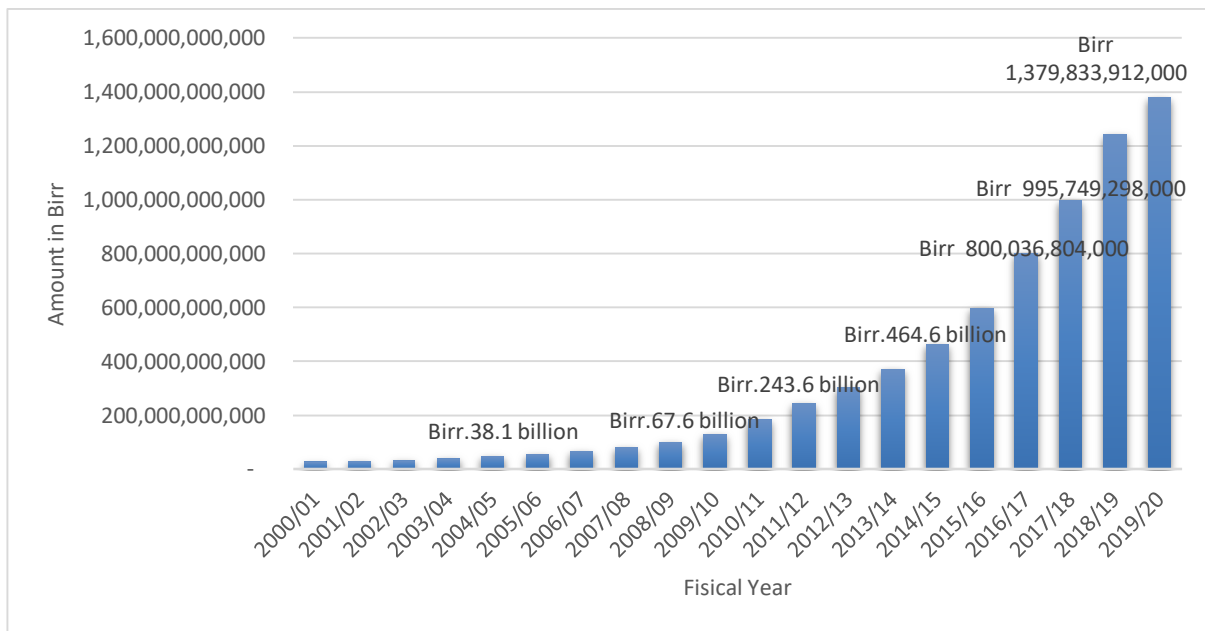
exchange rate regime is also still a managed float system. On the whole, the cumulative effect of the developments since the deregulation in 1991 can be considered a good move particularly with respect to the emergence of new banks and the automation of banks in providing real time banking products and services and enormous change in the outreach of bank branches.

Compared to most countries, Ethiopia has taken a cautious approach toward the liberalization of its banking industry. For all intents and purposes, its industry is closed and generally less developed than its regional peers. The industry comprises one state-owned development bank and 18 commercial banks, including the dominant Commercial Bank of Ethiopia (CBE), with assets approximately 70 percent of the industry's total holdings. The underdevelopment of the banking industry can be seen in the small proportion of the population that has a deposit account, further restricting the country's economic growth (Keatinge, 2014).

The structure of the banking sector is unique on account of the dominance of a state-owned bank, which control almost two-thirds of the local banking sector and which the government uses to set the desired levels of lending (such as investment in specific sectors and government projects to boost economic growth). This is contrary to the trend elsewhere in Africa, where private sector banks dominate the banking sector and drive economic growth via credit to the private sector.

Total asset of the banking system has registered remarkable growth over the past decade and a half. It has increased from Birr 26.628 billion in 2000/01 to Birr 1.38 trillion in 2019/20, an increase of 5082%. It has shown on average a 23% increase year to year. Of the total asset of the banking system, the public banks accounted for the largest share with the Commercial Bank of Ethiopia (CBE) by itself accounting for about 56% of the total asset as of June 2020. Of the private banks, the bank with the largest asset size was Awash Bank (AIB) with Birr 89.3 billion, followed by Dashen Bank (DB) with Birr 68.3 billion and Bank of Abyssinia (BOA) with Birr 56.9 billion as of June 2020. It should be noted that the banking system is the largest among the financial sector accounting for over 80% of the total assets of the financial sector.

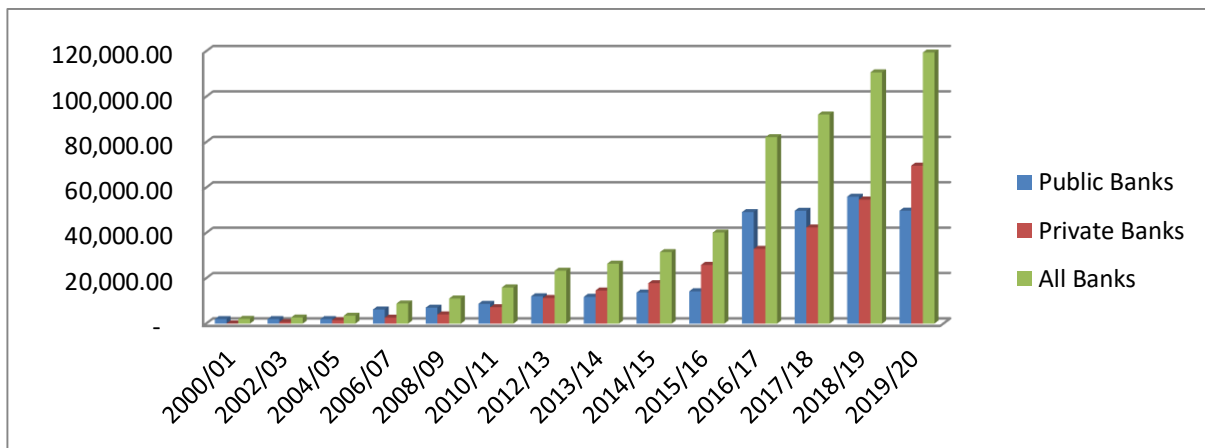
Figure 2.2: Total Asset of the Ethiopian Banking sector (2000/01 – 2019/20)



Sources: NBE, Annual reports, various issues (2000/01 – 2019/20)

The total capital of the banking sector excluding the central bank reached Birr 119.5 billion at the end of June 2020 which was an almost 50 fold increase compared to 2000/01's total capital of Birr 2.506 billion. It showed on average a 41% increase year to year in that time period. Of the total capital, about Birr 49.8 billion (42%) was held by Commercial Bank of Ethiopia. The total capital of the private banks stood at Birr 69.6 billion (58%).

Figure 2.3 Total Capital of the Ethiopian Banking system (2000/01 - 2019/20), (in millions of Birr)



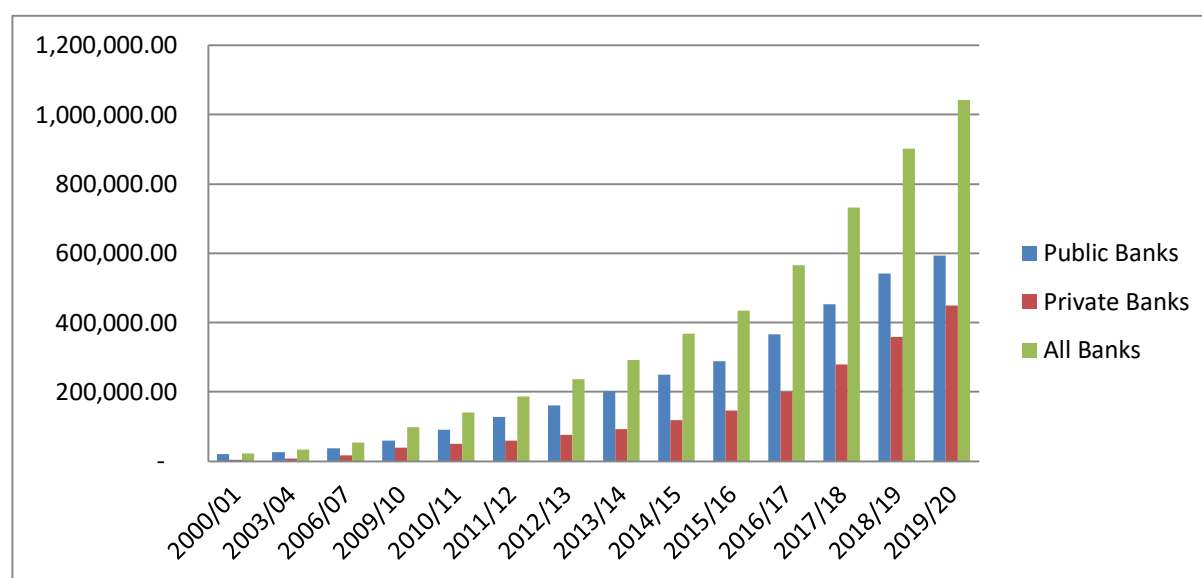
Sources: NBE, Annual reports, various issues, (2000/01 – 2019/20)

It is worth to note the increasing contribution of the private banks to the total capital of the banking sector over the last couple of years. Their share in the total capital of banks increased from around 4% in 2000/01 to 30% in 2006/07 to 56.5% in 2014/15 over taking the public sector as the largest contributor and currently as of 2019/20 fiscal year stands at 58%. Over the last 10 years, the capital of private banks has increased on the average by 40% on annual basis, while the capital of public banks increased on the average by 34% on annual basis, over the same period. Of the private banks, as of June 2020, the bank with largest capital was Awash International Bank (AIB) with Birr 9.02 billion, followed by Dashen Bank (DB) with Birr 8.3 billion and Bank of Abyssinia (BOA) with Birr 5.7 billion.

Though registering this remarkable growth, its size is still quite limited compared to the financing need of the economy. According to Tsegabirhan (2017), the Ethiopian banking industry is underfinanced itself with a total capital of Birr 83.3 billion. This constrains the size of credit available to the Ethiopian economy. Given this limited capital base relative to the credit demand of the economy, the Ethiopian banking sector at its current size cannot be expected to finance major physical infrastructure like hydroelectric power generation projects. The financing need of the economy is increasing every year mainly due to the huge infrastructural projects of the government and the expanding basic services. So, for an expanding economy registering successive double digit growth, there is a need for a diversified and highly capitalized financial sector that is capable of availing the required financing.

Due to the observed branch expansion especially in recent years, the total deposit (saving, demand and time) mobilization of the banking sector has increased significantly from Birr 23.5 billion by the end of June 2001 to Birr 367.4 billion by the end of June 2015 and to 1,041.7 billion by the end of June 2020. The average annual growth rate in deposit was 22% during that time. The public banks mobilized about 87% of total deposits mobilized by all banks by the end of June 2001. It showed only a modest decline reaching 68% by the end of June 2012, and stands at 57% as of June 2020. Among the private banks, the bank that mobilized the largest deposit as of June 2020 was Awash Bank (AIB) with Birr 70.6 billion, followed by Dashen Bank (DB) with Birr 53.5 billion and Bank of Abyssinia (BOA) with Birr 47.6 billion.

Figure 2.4: Deposit Mobilization of the Banking System (in millions of birr)



Sources: NBE, Annual reports, various issues, (2000/01 – 2019/20)

2.2. Empirical Literature

Applegarth (2004) in his study conducted on capital market and financial market development in Sub-Saharan Africa marked that Sub-Saharan Africa countries do not mobilize their domestic capital effectively. The lack of long-term local currency savings instruments is a barrier to local investment of local capital and estimated that the unbanked population Africa-wide is between 80 percent and 90 percent.

On the other hand, Mlachila, Park & Yabara, (2013) noted that recent developments, such as the expansion of mobile phone-based banking, regional financial integration, portfolio flows to new markets and the spread of pan-African banking groups, have the potential to

significantly change the landscape for banking in much of SSA, but also introduce new challenges for financial regulators.

Beck & Cull (2013) in their study comparing a sample of 307 banks from low and lower-middle income countries in Africa with 720 banks from non-African developing countries found out that there existed a significantly higher liquidity ratios for African banks. African banks are better capitalized but provide only limited lending to the real economy

Study conducted by KPMG (2013) found that various indicators in relation to financial system access, depth, efficiency and stability for Sub-Saharan Africa countries performed weakest on average. However, more than anything else, Africa represents massive financial sector growth potential due to the fact that the market is still largely unsaturated. Increased real GDP per capita in many African countries having, a rapid expansion in retail banking is foreseen in coming years bringing the sector's contribution to the continent's collective GDP to 19% from an estimated 11% in 2009.

In their study using an econometric model and descriptive quantitative and qualitative analysis on the Competition of the Banking Industry in Ethiopia, Eshete, Teshome & Abebe (2013) found that Competition in terms of price is relatively less significant competitive parameter in the Ethiopian banking industry. Bank service charges are more or less homogeneous in the industry, whereas interest rates on time and saving deposits are partially controlled by monetary authorities, rather than demand and supply forces. However, after satisfying the minimum statutory levels, banks have been engaging in price competition, as can be explained by differentiated rates on deposits, especially on time deposit, the commencement of interest payment on demand deposit, as well as differentiated interest rates on loans. Banks in the Ethiopian case are competing in terms of service quality and efficiency (including use of technological advances), branch network expansions, advertising and prices, put in the order of their significance.

Another study is one that focused on the investigation of macro factors that affect the development of the banking sector in Ethiopia by Abrha Gezae (2015). The study found out that the banking sector is rudimentary, due to problems such heavy dependence of investors in borrowed fund, excessive government borrowing, absence of secondary markets, less attractive deposit rate, limited outreach of banking services, underdeveloped saving culture, poor cross-selling activity of inflow of foreign remittance, and deficit in the trade balance of the country. The study went on to recommend strengthening of the trade balance & openness, cutting

budgetary deficit, increasing the real interest rate, cross-selling of inflow of remittance by banks and also that the NBE shall take measures that enhance financial inclusion and improve the platform of required infrastructure in collaboration with the designated organs of the government to enhance development and competitiveness of the banking sector.

Gardachew (2018) conducted a research on the opportunities and challenges of E-banking in Ethiopia and found that lack of suitable legal and regulatory frame works for E-commerce and E payments, political instability in neighbouring countries, frequent power interruption, lack of trained personnel's in key organizations, high rates of illiteracy and absence of financial networks that links different banks are the major challenges. The research output showed Opportunities offered by ICT through e-learning programs and Commitment of the governments on development of ICT infrastructures is considered as drivers of using Ecommerce and E-payment systems.

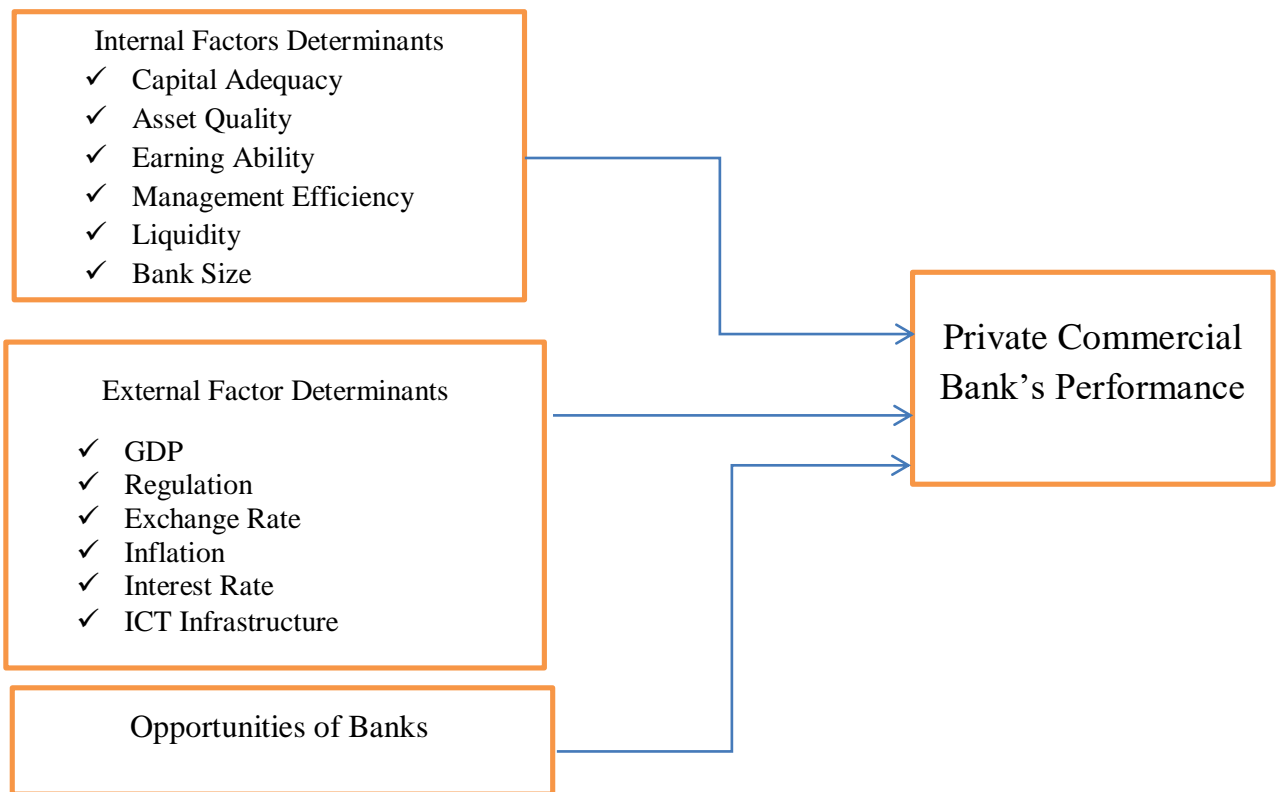
Abdissa (2016), applied balanced panel data of eight Ethiopian commercial banks for the period of 2002 - 2012. The study used ordinary least square (OLS) technique to see the impact of the factors on profitability of Ethiopian commercial banks by using ROA and NIM as a profitability measure. The study identified that except expense management, regulation and credit risk, all the considered bank specific variables had positive and significant relationship with profitability. Those three variables, expense management, regulation and credit risk, found to have negative and significant relationship with the performance of commercial banks. On the other hand, the macroeconomic variables, economic growth, interest rate spread and exchange rate, had positive and strong relationship with profitability.

The study made by Boru (2014), on the determinants of Ethiopian bank performance for the period 1990-2012 by using both descriptive and econometrics techniques found that bank specific variables by large explain the variation in profitability. On the other hand, bank size and macro-economic variables such real GDP growth rates have no significant impact on banks 20 profitability. Among the external determinant factors, inflation has found significant effect on the bank's performance. Provision to total loans, share of service charge to total income and the non-interest expense to total expense were significant and considered to be drivers of the banks' profitability in Ethiopian banking industry. The capital adequacy ratio and the loan to deposit ratio were insignificant to explain profitability. The ratio of service charge to gross income which is used to measure income from foreign operation has a positive impact on profitability. On the other hand, strong and negative relationship identified between the ratio of non-interest expense to total expense and profitability, which is a proxy measure of management efficiency.

Elshaday et al, (2018) noted that bank size, leverage ratio and credit interest income have positive and statistically significant impact on the financial performance measured by return on equity. Loan loss provision and NPL has statistically significant negative effect on return on assets. Ratio of debt to asset, a measure of leverage, negatively correlated with the profitability measured by ROA. The study was conducted on ten private commercial banks in Ethiopia for a period covering from 2007 to 2016.

2.3 Conceptual Frame Work

Based on the related literature of both theoretical and empirical studies the following conceptual work was developed:



Source: Developed by the Researcher.

CHAPTER THREE

3. Research Methodology

3.1. Research Design

According to Kothari (2004), descriptive research studies are those studies which are concerned with describing the characteristics of a particular individual or of a group. In order to achieve its objectives, this study applied a descriptive research design as it collected data with a view to describe and analyse the opportunities awaiting private commercial banks in the coming years in Ethiopia and to identify the main determinants of private commercial banks performance in the case of Zemen bank S.C.

3.2. Research Approach

There are three basic types of research approaches; namely: quantitative, qualitative, and mixed approach. Quantitative research approach relies on the philosophy of post positivism world view. It is also reductionist in that the intent is to reduce the ideas into a small, discrete set of ideas to test, such as the variables that constitute hypotheses and research questions. In addition, quantitative approach uses statistical methods in describing patterns of behaviour and generalizing findings from samples to population of interest, and employs strategies of inquiry such as experiments and surveys (Creswell 2003).

Hence, by taking the research objectives and questions into considerations, the study employed both quantitative and qualitative research approach through primary data collected by using standard questionnaire.

3.3. Target Population

Population is a group of individuals, objects or items from which samples are taken from (Kombo and Tromp, 2006). A population refers to an entire group of persons or elements that have at least one thing in common. The entire population of this study includes all the employees that work in the two departments (International Banking Department and Credit Department) and seven branches located in Addis Ababa of Zemen Bank S.C, which are selected using purposive sampling technique. The procedure used for drawing the sample from the available lists was based on their seniority i.e. long years services in providing services and based on specific factors such as time, due to limited resource. There are 181 officers including

branch managers and division managers at head office in the selected two departments and seven branches.

3.4. Sampling Design

3.4.1. Sampling Technique

In this study, the stratified and purposive sampling techniques are used in combination. The researcher preferred stratified sampling technique based on Kothari (2004) statement that, “If a population from which a sample is to be drawn does not constitute a homogeneous group, stratified sampling technique is generally applied in order to obtain a representative sample. In this technique, population is divided into several sub-populations that are individually more homogeneous than the total population (the different sub-populations are called strata).

In general, since each stratum is more homogeneous than the total population, the researcher is able to get more precise estimates of the sample for each stratum and by estimating more accurately each of the component parts and get a better estimate of the whole; in brief, stratified sampling results in more reliable and detailed information (Kothari, 2004).

Besides to the stratified sampling technique, purposive sampling technique is used to select the respondents from each stratum. This technique is needed to choose members of the population to participate in the study purposively based on researcher’s own judgments to answer research questions and/or achieve research objectives

3.4.2. Sample size determination methods

There are several approaches to determine the sample size. This includes a census for small population, imitating a sample size of similar studies, using published tables, cut off point in terms of percentage and applying formulas to calculate a sample size. To determine the required sample size from the target population for this study, Yemane’s formula (1967) was used. The researcher employed the following formula to determine the sample size:

$$n = \frac{N}{1 + (N * e^2)}$$

Where: n = Sample size

N = Target population

e = The level of precision, ±5% (0.05) or 95% confidence level

$$n = \frac{181}{1 + (181)0.05^2} = 124$$

Thus, the total number of sample size is 124 respondents.

Following the sample size determination, the researcher was allocated the sample size of each stratum through the method of proportional allocation under which the sizes of the samples from the different strata are kept proportional to the sizes of the strata. In order to do so, proportionate stratified sampling (PSS) formula ($n=Ni/N*ni$) was used.

Where: n: represents sample size taken from each stratum, Ni: total no. of population of each stratum, ni: total sample size of the study, and N: total population size.

Table 3.1: Sample size of respondents from each department and branch category

S/N	Category	Total number of staff as of April 2022.	Sample from each category
			$ni=Ni/N*181$
1	IBD	38	26.00
2	Credit Department	36	25.00
3	Main Branch	31	21.00
4	Bole Branch	22	15.00
5	CMC Branch	12	8.00
6	Arada Branch	10	7.00
7	B/Gebrel Branch	11	8.00
8	Gotera Branch	11	7.00
9	Mexico Branch	10	7.00
Total		181	124

3.5. Data Collection Methods

This study employed both secondary and primary data to answer the objectives of the study. Secondary data are collected from books, journals, reports and databases that provide relevant information on the topic. Primary data are collected through structured questionnaire given to some selected participants.

3.5.1. Data Collection Instruments

This study used a questionnaire carefully designed to include both close and open ended questions. The questions have been structured with Likert scale question types rated at 5 levels namely, 5 = Strongly Agree, 4 = Agree, 3 = Neutral, 2 = Disagree and 1 = Strongly

Disagree. The open ended questions structured to include key questions that explored additional information not captured or elaborated in the close ended questions.

3.5.2. Validity and Reliability

Validity is defined as how much any measuring instrument measures what it is intended to measure. Validity refers to the issue of whether an indicator (or set of indicators) that is devised to gauge a concept really measures that concept. On the other hand, the tendency toward consistency found in repeated measurements is referred to as reliability. This can be checked by comparing the responses for similar or consistent questions of the questionnaire.

Several ways of establishing validity are: content validity; predictive validity; construct validity; and convergent validity (Bryman and Bell,2003). This study addressed content validity through the review of literature and adapting instruments used in similar previous researches. In addition, the Cronbach's Alpha using SPSS has been calculated to measure the reliability of the collected qualitative data. According to Hair, et al., (2006), if α is greater than 0.7, it means that it has high reliability and if α is smaller than 0.3, then it implies that there is low reliability.

3.5.3. Ethical Consideration

The information which is gathered from participants are treated with highest degree of confidentiality and has been only used for the purposes of the study. This gathered information will not be revealed to anybody without the participants consent. The participants are informed on the purpose of the research. The researcher also preserve the anonymity of the informant by not writing the names of all those involved in the research.

3.6. Method of Data Analysis

Both quantitative and qualitative techniques are used to process and analyse the collected data. Creswell (2009), there is more insight to be gained from the combination of both qualitative and quantitative research than either form by itself. Their combined use provides an expanded understanding of research problems. Thus, with the intention of getting the general picture of the research under study, both quantitative and qualitative methods of data analysis are used in conducting the study. The data are coded and arranged in frequency distribution tables showing Frequency and the percentages, mean and standard deviation. Statistical tools such as Ms Excel and SPSS version 20 are used for data analysis.

CHAPTER FOUR

4. DATA ANALYSIS AND PRESENTATION

4.1 Introduction

The first chapter stated and justified the research problem, which focused on the opportunities and determinants of private commercial banks in the case Zemen bank, chapter 2 offered a survey of literature around the concepts of internal/external determinants and opportunities. The other chapter 3 provided a detailed account of the methods and techniques that were adopted for collecting and Analysing data and consequently, for answering the research problem. This chapter presents the findings in a systematic, sequential and logical manner so that recommendations and conclusions are arrived at. The data analysis for this study is quantitative data analysis.

4.2 Presentation and analysis of quantitative data

Quantitative data for this study was descriptive statistics that analyses the response of participants. A total of 124 copies of questionnaires were distributed to respondents/samples, out of which 97 of them were properly filled and returned.

4.2.1. Demographic Characteristics of the Respondents

A link to the instrument was distributed to staffs of the two departments and seven branches through questionnaire. A total of 97 staff members completed the questionnaire. The next sections comprise of items relating to demographic profiles of participants and the purpose of this section is to provide a summary of the profiles of participants.

Table 4.1: Statistics

		Sex	Position	Age	Service year	Education level
N	Valid	97	97	97	97	97
	Missing	0	0	0	0	0
Sum		97.00	97.00	97.00	97.00	970.00
Percentiles	100	100	100	100	100	100

Source: Own Survey, 2022

The above table shows that the statistics of valid and missing participant responses with regard to demographic data of the participants, as we see from the table all distributed questionnaires were valid with 100% in all demographic characteristics of the participants.

Table 4.2: Sex frequency

	Frequency	Percent	Valid Percent	Cumulative Percent
MALE	62	63.9	63.9	63.9
Valid FEMALE	35	36.1	36.1	100.0
Total	97	100.0	100.0	

Source: Own Survey, 2022

Table 4.2 above shows that 63.9% of the respondents are male, while the remaining 36.1% are females.

Table 4.3: Age frequency

	Frequency	Percent	Valid Percent	Cumulative Percent
<25	32	33	33	33
26-35	38	39.2	39.2	72.2
Valid 36-45	18	18.6	18.6	90.7
46-65	7	9.3	9.3	100.0
Total	97	100.0	100.0	

Source: Own Survey, 2022

In terms of age the above table 4.3 shows that 33% (32) of participants are <25, 39.2 % (38) of participants are aged 26-35, 18.6 % (18) of the participants aged between 36-45, and the remaining 9.3% (7) participants of this research aged between 46-65. The age distribution though uneven, it spreads across all age categories.

Table 4.4: Position frequency

	Frequency	Percent	Valid Percent	Cumulative Percent
Operation staff	51	52.6	52.6	52.6
Senior Officer	32	33.0	33.0	85.6
Valid Section Head	8	8.2	8.2	93.8
Middle level management	6	6.2	6.2	100.0
Total	97	100.0	100.0	

Source: Own Survey, 2022

Table 4.4 shows that the position of the participants for this study and 52.6% of the respondents were operation staffs, 33% senior officers, 8.2% section head and the remaining 6.2% of the participants are middle level managements.

Table 4.5: Service year (work experience)

	Frequency	Percent	Valid Percent	Cumulative Percent
<3 YEARS	12	12.4	12.4	12.4
3-5 YEARS	22	22.7	22.7	35.1
Valid 5-8 YEARS	40	41.2	41.2	76.3
>8 YEARS	23	23.7	23.7	100.0
Total	97	100.0	100.0	

Source: Own Survey, 2022

The above table 4.5 shows the work experience of respondents. 12.4% of respondents have less than three years work experience, 22.7% of the participants have 3-5 years' work experience, 41.2% of participants have 5-8 years' work experience and the remaining 23.7% of the respondents have above eight experience. This shows that participants have sufficient working experience that qualifies them as participants for this study, and the researcher's believes that those staffs who worked above three years have more knowhow about banking industry.

Table 4.6: Education level

	Frequency	Percent	Valid Percent	Cumulative Percent
MASTERS	41	42.3	42.3	42.3
Valid BACHELOR	56	57.7	57.7	100.0
Total	97	100.0	100.0	

Source: Own Survey, 2022

Table 4.6 depicts that there are 42.3% of the participants have master's degree and the remaining 57.7% of the participants have bachelor degree. This shows that participants have attained a reasonably high level of education qualification.

In conducting this sub-section on the descriptive statistics, table 7 summarizes the demographic characteristics of the participants discussed above.

Table 4.7: summarized demographic characteristics of participants

Item	Category	Frequency	Percentage
Sex	Male	62	63.9
	Female	35	36.1
		97	100
Age	<25	32	33
	26-35	38	39.2
	36-45	18	18.6
	46-65	7	9.3
		97	100
Position	Operation Staff	51	52.6
	Senior Officer	32	33
	Section Head	8	8.2
	Middle-level Management	6	6.2
		97	100
Work experience	<3 YEARS	12	12.4
	3-5 YEARS	22	22.7
	5-8 YEARS	40	41.2
	>8 YEARS	23	23.7
		97	100
Education Level	MASTERS	41	42.3
	BACHELOR	56	57.7
		97	100

Source: Own Survey, 2022

4.2.2. Reliability (Cronbach's alpha) values

One of the most commonly used indicators of internal consistency is Cronbach's alpha coefficient. We used the cronbach's alpha to check the reliability of the questionnaire. The cronbach's alpha of all the variables was measured and resulted as follows in the table below.

Table 4.8: Cronbach's alpha result for each variable

Variable	Cronbach's alpha	Number of Items/questions
Capital Adequacy	0.755	2
Asset Quality	0.725	3
Earning Ability	0.852	2
Management Efficiency	0.604	2
Liquidity	0.828	2
Bank Size	0.763	4
GDP	0.701	5
Regulation	0.738	3
Exchange Rate	0.765	2
Inflation	0.822	3
Interest Rate	0.74	2
Infrastructure	0.747	2
Opportunities	0.741	5

Source: Own Survey, 2022

Table 4.9: Cronbach's alpha result for the major three variables

Cumulative of the major variables	Cronbach's alpha	Number of Items/questions
Internal Factor Determinants	0.827	15
External Factor Determinants	0.714	17
Opportunities	0.741	5
Overall (cumulative)	0.858	37

Source: Own Survey, 2022

The ideal result of the coefficient of the alpha is 0.7 and above where in this case all internal factor determinants of banks; Capital Adequacy, Asset Quality, Earning Ability, Liquidity, and Bank Size scored 0.755, 0.725, 0.852, 0.828, and 0.763 respectively, all external factor determinants of banks; GDP, Regulation, Exchange Rate, Inflation, Interest Rate, and Infrastructure scored 0.701, 0.738, 0.765, 0.822, 0.74, and 0.747 respectively, and Opportunities of banks scored 0.741. Which makes all these mentioned results reliable measures of scale.

Management Efficiency scored 0.604 which makes it unreliable scales of measure. However the aggregate alpha result of the major variables as shown in the second table is for Internal Factor determinants 0.827, External Factor determinants 0.714 and Opportunities of banks 0.741, which makes all the three variables reliable scales of measure. The overall result of the alpha/reliability coefficient with 37 question items calculated result is 0.858.

4.2.3. Internal Factor that Determinants the Financial Performance of Private Commercial Banks in Ethiopia

This part required the respondents to indicate whether the various internal factors influenced financial performance of private commercial banks and to what extent. The internal factors listed were; capital adequacy, asset quality, earning ability, management efficiency, liquidity and bank size/branch.

Table 4.10: Internal Factor Determinants Descriptive Statistics

		N	Minimum	Maximum	Mean	Std. Deviation
Capital Adequacy	Capital adequacy is a reflection of the internal strength of a bank	97	2.00	5.00	3.8247	.54026
	Capital adequacy requirements aim to increase the stability of banking system	97	2.00	5.00	3.7835	.58143
	Aggregate				3.8041	.56084
Asset Quality	Having up to date Credit Policy manual is helpful in credit processing	97	2.00	5.00	4.0928	.56055
	Proper system of credit monitoring and follow up minimizes NPL	97	3.00	5.00	4.0825	.65622
	Your bank practice a sectorial portfolio allocation in maintaining credit risk	97	2.00	5.00	3.6186	.60283
	Aggregate				3.9313	.60653
Earning Ability	Earning ability has a significant influence on performance of banks.	97	3.00	5.00	3.9794	.55863
	Earning ability represents bank's capability to maintain quality and earn consistently	97	3.00	5.00	4.0309	.60301
	Aggregate				4.0052	.58082
Management Efficiency	Restructuring of top management improves financial performance	97	3.00	5.00	4.0000	.45644
	Continuous training of employees improves financial performance	97	3.00	5.00	4.5258	.52227
	Aggregate				4.2629	.48935
Liquidity	Liquidity is fundamental to the well-being of banks, that It determines their growth and development	97	3.00	5.00	4.1959	.63965
	Liquidity problem has been major challenges for private commercial banks	97	3.00	5.00	4.2784	.59059
	Aggregate				4.2371	.61512
Bank Size	Deeper distribution in terms of more branches leads to higher financial performance	97	2.00	5.00	3.8969	.56797
	Partnering with other related institutions improves financial performance	97	2.00	5.00	3.6907	.68253
	The strategic positioning of bank branches directly impacts the profit	97	3.00	5.00	3.6804	.55050
	Offering of a wide range of products contributes to more profits	97	2.00	5.00	3.8660	.55206
	Aggregate				3.7835	.58827
	Overall score				3.9697	0.5776

Source: Own Survey, 2022

Table 4.11: Internal Factor Determinants Frequency Statistics

			Disagree	Neutral	Agree	SA	Total
Capital Adequacy	CA1	Frequency	3	15	75	4	97
		Percent	3.10	15.50	77.30	4.10	100.00
	CA2	Frequency	5	14	75	3	97
		Percent	5.2	14.4	77.3	3.1	100
Asset Quality	AQ1	Frequency	2	5	72	18	97
		Percent	2.10	5.20	74.20	18.60	100.00
	AQ2	Frequency	-	17	55	25	97
		Percent	-	1.5	56.7	25.8	100
	AQ3	Frequency	4	31	60	2	97
		Percent	4.1	32	61.9	2.1	100
Earning Ability	EA1	Frequency	-	16	67	14	97
		Percent	-	16.5	69.1	14.4	100
	EA2	Frequency	-	16	62	19	97
		Percent	-	16.5	63.9	19.6	100
Management Efficiency	MGMT1	Frequency	-	10	77	10	97
		Percent	-	10.3	79.4	10.3	100
	MGMT2	Frequency	-	1	44	52	97
		Percent	-	1	45.4	53.6	100
Liquidity	LQ1	Frequency	-	12	54	31	97
		Percent	-	12.4	55.7	32	100
	LQ2	Frequency	-	7	56	34	97
		Percent	-	7.2	57.7	35.1	100
Bank Size	BS1	Frequency	3	12	74	8	97
		Percent	3.1	12.4	76.3	8.2	100
	BS2	Frequency	3	33	52	9	97
		Percent	3.1	34	53.6	9.3	100
	BS3	Frequency	-	35	58	4	97
		Percent	-	36.1	59.8	4.1	100
	BS4	Frequency	1	19	69	8	97
		Percent	1	19.6	71.1	8.2	100

Source: Own Survey, 2022

Capital Adequacy

As the results of respondents indicate, where above half of the respondents agreed that capital adequacy reflects the internal strength of a bank and increases its stability. It reflects the overall financial condition of the banks and also the ability of management to meet the need of additional capital. Capital also serves as an indicator whether the bank has sufficient capital to absorb any possible shock or not. Therefore a good Capital adequacy stand a bank in good stead during the times of crisis, where it is a major indicator of the financial health of banks.

Asset Quality

As the results of respondents indicate, having credit policy with strong credit monitoring and follow up system is essential in maintaining or minimizing credit risk. The primary factor affecting overall asset quality is the quality of the loan portfolio and the credit administration program. Since loans typically comprise a majority of a bank's assets and carry the greatest amount of risk to their capital, without proper credit risk management, it becomes challenge to their performance.

Earning Ability

The respondents were asked to indicate whether earning ability has significant influence on banks' financial performance and represents bank's capability to maintain quality and earn consistently, the analysis was that; above 80% of the respondents agreed. A bank with good earnings performance inspire the confidence of depositors, shareholders, creditors, borrowers, and the public at large.

Management Efficiency

As the result of respondents show, providing continuous training and restructuring of managements improve performance of banks. Sound management is crucial for the success of a bank and efficiency is one of the key internal factors that determine the bank performance. As operational efficiency in managing through different mechanisms, efficiency of management needs also to be managed since many banks are determined with this factor.

Liquidity

According to the feedback obtained from respondents, where above 30% and 50% of respondents strongly agreed and agreed respectively, liquidity problem has been the major challenges of private commercial banks. Since Liquidity is a bank's ability to meet its cash and collateral obligations without sustaining unacceptable losses, they must ensure that sufficient funds are available at a reasonable cost to meet potential demands from both investors and borrowers.

Bank size

Increase in Size of bank in terms of asset enables to expand their operations geographically, to make huge investments in technology and other input factors which increase efficiency as well

as customer base. The respondents reply was except very few respondents disagree, most agreed that bank size individually do not have strong influence on zemen banks financial performance. It is highly related with factors like the strategic positioning of bank branches and partnerships with other institutions.

Product range and distribution networks were other key factors that most banks in Ethiopia deal with retail banking and therefore access to customers and improved service through branch networks are essential.

4.2.4. External Factors That Determines the Financial Performance of Private Commercial Banks in Ethiopia

Respondents were required to indicate whether the various external factors determine the financial performance of private commercial banks and to what extent. The external factors listed were; GDP, Regulation, Exchange rate, inflation, Interest rate, and Infrastructure.

Table 4.12: External Factor Determinants Descriptive Statistics

External Factor Determinants						
		N	Min	Max	Mean	Std. Deviation
GDP	Ethiopian Banking Industry has been on upward trend in the last 5 years	97	3.00	5.00	4.0000	.50000
	Ethiopia banking industry is highly concentrated and high competition exists.	97	2.00	5.00	3.8969	.56797
	The development of financial sector in Ethiopia has an impact on performance	97	3.00	5.00	4.0103	.56816
	The economic growth or GDP has a key role on the bank's financial performance	97	3.00	5.00	4.1546	.54658
	As the economy grows and more private commercial banks join the market, it will bring challenges to the existing banks activities	97	3.00	5.00	3.7010	.61517
	Aggregate					3.95258
Regulation	Bank ownership, whether public or private has a role to play on performance/profitability	97	3.00	5.00	4.0412	.67573
	Macro-economic policies by the government such as increasing or decreasing its expenditure affects bank's financial performance	97	3.00	5.00	4.4536	.61272
	Implementation of NBE regulations and directives has been a major challenge to the performance of private commercial banks	97	4.00	5.00	4.7010	.46018
	Aggregate					4.3986
Exchange Rate	The volatility of exchange rates affects bank's financial performance	97	2.0	5.0	3.680	.7151
	Depreciation and appreciation of the Ethiopian currencies is a key determinant of bank's financial performance	97	2.00	5.00	3.9278	.64948
	Aggregate					3.8041
Inflation	The consumer purchasing power plays a role in bank's financial performance	97	3.00	5.00	4.1134	.45360
	Stability of inflation rate plays a role in the profit the bank makes	97	3.00	5.00	4.0515	.39187
	Imbalance of trade, which is the gap between import and exports in Ethiopia affects bank's	97	3.00	5.00	4.0309	.39406
	Aggregate					4.0653
Interest Rate	The saving culture and practices of Ethiopians has an impact on bank's financial performance	97	3.00	5.00	3.9794	.53966
	Interest rate variation has effect on financial performance	97	3.00	5.00	4.1959	.57080
	Aggregate					4.0876
Infrastructure	Ethiopian banking industry comprises an unsupportive Information technology culture	97	3.00	5.00	4.0825	.39974
	There is poorly developed telecommunication infrastructure in the country	97	3.00	5.00	4.1856	.52698
	Aggregate					4.1340
Overall score					4.071	0.5405

Source: Own Survey, 2022

Table 4.13: External Factor Determinants Frequency Statistics

			Disagree	Neutral	Agree	SA	Total
GDP	GDP1	Frequency	-	12	73	12	97
		Percent	-	12.40	75.30	12.40	100.00
	GDP2	Frequency	1.00	18.00	68.00	10.00	97.00
		Percent	1.00	18.60	70.10	10.30	100.00
	GDP3	Frequency	-	15.00	66.00	16.00	97.00
		Percent	-	15.5	68	16.5	100
	GDP4	Frequency	-	8	66	23	97
		Percent	-	8.2	68	23.7	100
	GDP5	Frequency	-	37	52	8	97
		Percent	-	38.1	53.6	8.2	100
Regulation	RG1	Frequency	-	20	53	24	97
		Percent	-	20.60	54.60	24.70	100.00
	RG2	Frequency	-	6	41	50	97
		Percent	-	6.2	42.3	51.5	100
	RG3	Frequency	-	-	29	68	97
		Percent	-	-	29.9	70.1	100
Exchange Rate	ER1	Frequency	6	27	56	8	97
		Percent	6.2	27.8	57.7	8.2	100
	ER2	Frequency	4	12	68	13	97
		Percent	4.1	12.4	7.01	13.4	100
Inflation	I1	Frequency	-	5	76	16	97
		Percent	-	5.2	78.4	16.5	100
	I2	Frequency	-	5	82	10	97
		Percent	-	5.2	84.5	10.3	100
	I3	Frequency	-	6	82	9	97
		Percent	-	6.2	84.5	9.3	100
Interest Rate	IR1	Frequency	-	15	69	13	97
		Percent	-	15.5	71.1	13.4	100
	IR2	Frequency	-	8	62	27	97
		Percent	-	8.2	63.9	27.8	100
Infrastructure	ICT1	Frequency	-	4	81	12	97
		Percent	-	4.1	83.5	12.4	100
	ICT2	Frequency	-	6	67	24	97
		Percent	-	6.2	69.1	24.7	100

Source: Own Survey, 2022

GDP

Gross Domestic Product or economic growth refers to the total value of final goods and services produced in the country in a specific period of time specifically measured in terms of dollars. Higher the value of GDP means economic growth of the country and economic prosperity as well. Economic growth affects bank performance as shown in the above table, where most respondents agreed.

A higher GDP growth causes firms loans and deposits to increase and make bank's net interest income and loans losses to improve. Also, a higher GDP growth implies a higher disposable income and reduce defaults on consumer loans number.

Regulation

As the results of respondents indicate, where above half of the respondents strongly agreed that NBE regulations and directives has been a major determinant to the performance of private commercial banks. Currently, NBE is repeatedly revising regulations which make private commercial banks barrier in their performance. NBE-Bill purchase, legal reserve requirement, foreign currency requirement, capital requirement, and other regulations and directives has been negatively affecting banks performance.

Exchange Rate

Exchange rate is the rate at which one currency will be exchanged for another or the value of one country's currency in relation to another currency. As most respondents agreed that bank's financial performance is highly affected by foreign exchange rate and the depreciation and appreciation of the currencies is key determinant.

Foreign exchange volatility has a negative impact on the return on banks' assets. Banks are exposed to a variety of risks due to foreign exchange volatility including transaction risk, conversion risk, credit risk, interest rate risk, and inflation risk, thereby reduces their profitability.

Inflation

Inflation is defined as a sustained increase in the general level of prices for goods and services in a county, measured as an annual percentage change. Or it is general prices rise, which results in value of money or purchasing power fall. Based on respondents result, stability of inflation

affects banks' profit. High inflation rate would result in low demand for banks' products because it would discourage saving since interest rate on saving is lower and raised interest rate on loans due to inflation might also discourage demand for credit.

Interest Rate

Interest rate is the amount charged to borrower for the use of assets, expressed as annual percentage of principal. Amount of interest earning is directly determined by the amount of interest rate the banks charge on their loans and advances they provide to various individuals and organizations.

As the respondents answer indicated, the interest earning's relationship to financial performance of banks reflects whether the amount of interest rate charged on loans and advances is at an appropriate level compared to the market.

Infrastructure

ICT help banks improve the efficiency and effectiveness of services offered to customers, and enhances business processes, managerial decision making, and workgroup collaborations, which strengthens their competitive positions in rapidly changing and emerging economies. In a country where there is poorly developed telecommunication infrastructure, ICT infrastructure is a major drawback to their performance, as almost all respondents has agreed.

Major determinants/challenges of bank

Respondents were asked to identify the major determinants/challenges to their bank, and their response is summarized below.

Table 4.14: Major Bank Challenges

Determinants	Frequency	Percent
Competition from other banks	42	43%
More banks joining the market	9	9%
Lack of technology	48	49%
Expertise/Management turnover	15	15%
High inflation rate	28	29%
Capital position (Size of capital)	26	27%
NBE regulation	89	92%

Source: Own Survey, 2022

As per the above table, where respondents were asked to identify the major determinants or challenges to their performance, NBE regulation or directives are the major determinant to the performance of Zemen bank. Especially the recently amended directives on the legal reserve requirement on Birr and foreign currency deposit liabilities held by commercial banks, which was raised to 10% from 5%, effective on September 1st, 2021, minimum capital requirement raised to 5 billion birr, and the foreign surrender requirement of banks that is, banks are required to surrender 70% of the foreign currency earnings from export of goods and services, remittance, and NGO's transfers to the NBE have affected performance of Zemen bank.

In second, the poorly developed technological advancement in the country and competition from other banks in the sector are the main determinants to the performance of Zemen bank as per the respondents answer with 49% and 43% of them agreed.

4.2.5. Opportunities of Private Commercial Banks in Ethiopia

Regarding the opportunities of private commercial banks, respondents were asked whether the below stated factors are opportunities for performance of banks.

Table 4.15: Opportunities of private commercial banks Descriptive Statistics

Opportunities of private commercial banks Descriptive Statistics						
		N	Min	Max	Mean	Std. Deviation
Opportunities	The liberalization of the industry	97	3.00	5.00	4.0412	.55748
	Working collaboration with other financial institutions	97	3.00	5.00	4.0515	.54717
	Majority of the population is unbanked and fast customer service	97	3.00	5.00	4.3093	.54698
	Growing economy of the country	97	3.00	5.00	4.3196	.55050
	Technological innovation and advancements in the country	97	4.00	5.00	4.6392	.48273
	Overall score				4.2722	0.537

Source: Own Survey, 2022

Table 4.16: Opportunities of private commercial banks Frequency Statistics

			Disagree	Neutral	Agree	SA	Total
Opportunities	OP1	Frequency	-	13	67	17	97
		Percent	-	13.40	69.10	17.50	100.00
	OP2	Frequency	-	12.00	68.00	17.00	97.00
		Percent	-	12.40	70.10	17.50	100.00
	OP3	Frequency	-	4.00	59.00	34.00	97.00
		Percent	-	4.1	60.8	35.1	100
	OP4	Frequency	-	4	58	35	97
		Percent	-	4.1	59.8	36.1	100
	OP5	Frequency	-	-	35	62	97
		Percent	-	-	36.1	63.9	100

Source: Own Survey, 2022

When respondents were asked about the prospects of private commercial banks, the recent technological innovations and advancements in the country like E-Banking which improve the efficiency, quality and the speed in delivering services and the economic growth of Ethiopia are the major opportunities of Zemen bank. In addition, majority of the population in the country, about 70% still being unbanked is also major opportunity to most private commercial banks.

CHAPTER FIVE

5. Discussion, Conclusion and Recommendation

5.1. Discussion and Conclusion

The main objective of this study was to analyse the opportunities and determinants of private commercial banks in Ethiopia. This research strived to give an understanding into the major internal and external factors that determines or challenges the financial performance and prospects of private commercial banks in Ethiopia. In order to achieve this, the following research questions guided the study. What are the internal factors that influence or challenge the financial performance of private commercial banks in Ethiopia? What are the external factors that determine the financial performance and are prospect to private commercial banks in Ethiopia?

As per the feedback obtained from the respondents, it was observed that, Liquidity had an aggregate mean of 4.23 indicating that respondents of the study generally agreed that liquidity that determines the well-being, growth and development of banks has been a major determinant to private commercial banks performance.

Management efficiency and earning ability had an aggregate mean of 4.26 and 4 respectively indicating, restructuring management improves communication and decision-making and simplifying management reorders the organizational hierarchy, opens the lines of communication and removes barriers to productivity. Continuous training program helps employees improve their knowledge and skills and provides them with a clear picture of their strengths and weaknesses which in return improves performance of the bank.

The other internal factors, asset quality, capital adequacy, and bank size with aggregate mean of 3.93, 3.8, and 3.78 respectively indicated that a banks with poor credit manual, credit monitoring and follow up system that result in high loan default rate, maintaining the NBE 10% minimum capital adequacy ratio requirement that indicate the internal strength of a bank are also determinants as per respondents reply.

Among the external factors, NBE regulation had an aggregate mean of 4.398 indicating the different NBE directives highly influence the performance of private commercial banks. As different studies also indicated, mostly the recent directives on legal reserve requirement of 10%, minimum capital requirement of 5 billion birr, and foreign currency surrender

requirement of 70% are the major challenges to private banks even though they may have edge to other parties.

The other major external determinants based on respondents result were ICT infrastructure that had an aggregate mean of 4.13. ICT infrastructure in Ethiopia is too underdeveloped to implement e-Banking effectively. Network and infrastructural inferiority is major obstacle.

Interest rate and inflation had an aggregate mean of 4.087 and 4.065 respectively indicating, Interest rates and bank performance are connected, with banks benefiting from higher interest rates. When interest rates are higher, banks make more money, by taking advantage of the difference between the interest banks pay to customers and the interest the bank can earn by investing. High inflation might be attributed to the shortage of the volume of savings and the increase in consumers' spending on goods and services. It discourages people from saving, because money saved for future use will have less value.

The other GDP and exchange rate factors had an aggregate mean of 3.95 and 3.80 indicating, a higher GDP growth causes loans and deposits to increase and make bank's net interest income and loans losses to improve. A higher GDP growth implies a higher disposable income and reduce loan defaults. Whereas, Foreign exchange volatility has a negative impact on the performance of banks', because banks will be exposed to a variety of risks due to foreign exchange volatility.

Regarding opportunities of private commercial banks, all the stated factors with aggregate mean of 4.27 shows prospects to the growth of their financial performance. The high technological innovation and advancements in the country (especially, the high enhancements in internet access), economic growth of the country and still more than 70% of the country population being unbanked are the major opportunities for private commercial banks.

5.2.Recommendation

Management bodies of private commercial banks should strive to strengthen the internal factors like capital adequacy, asset quality, earning ability, management efficiency, liquidity, and bank size. Because, the competition become tough since increase in new entrant to the market, and Ethiopia has become a member of the WTO that the domestic banks are obliged to prepare themselves to the inevitable competition that will come from foreign banks.

Even though the banking industry in Ethiopia is growing rapidly, the banking industry is still in its early stages even by the standards of other low-income countries: more than 70 percent of the population is unbanked, and many other metrics such as the total number of banks, banks contribution to GDP, bank accounts per person, branches per person, and bank credit per person are lower in Ethiopia compared to other African countries. Thus, private commercial banks should focus to reach this unmet demand of finance by adjusting their strategy with the government regulation.

Develop a comprehensive regulatory and legal framework for e-commerce and payment, raise public awareness on the use of ICT, e-banking, and e-Payment, provide incentives for banks to invest rigorously on ICT and use of e-banking and e-Payment, encourage the current efforts to develop and expand ICT infrastructure. The use of e-banking and digital payment systems may place extra pressure across networks; so Ethio-telecom need to work hard on network expansion in this regard.

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Annex

Addis Ababa University School of commerce Masters of Business Leadership

Dear respondents

This questionnaire is prepared to employees of Zemen Bank S.C. The objective of the questionnaire is to collect information for a study on Opportunities for and Determinants of Private Commercial Banks in Ethiopia.

INSTRUCTION

- Do not write your name or any other personal identification information anywhere in this questionnaire.
- Tick where appropriate in the spaces provided.
- Use the scoring guide where applicable.
- The information you provide will be valuable for the successes of the research paper. Please be honest and objective while filling the questionnaire.
- The information you give is used only for academic purpose and will be kept confidential.

Thank you in advance for your cooperation.

Part one: Demographic Information

1. Gender

Female Male

2. Age

<25 26-35 36-45 46-65

3. Level of education

Diploma Degree Masters Above

4. Length of Service

<3 Years Years 5-8 Years >8 Years

5. Your position in the organization.

Senior Management

Middle level Management

Head of Section/Unit

Senior Officer

Operations staff

Part Two: Determinants of private Commercial banks

The major factors that affect private commercial banks in Ethiopia are listed below. The factors are classified as internal and external factors. After you read each of the factors and their relation as determinant, evaluate them in relation to your bank experience and then put a tick mark (√) under the choices below.

1. Firm Specific/internal factors

	Statement	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
1	Capital adequacy is a reflection of the internal strength of a bank.					
2	Capital adequacy requirements aim to increase the stability of banking system					
3	Having up to date Credit Policy manual is helpful in credit processing					
4	Proper system of credit monitoring and follow up minimizes NPL					
5	Your bank practice a sectorial portfolio allocation in maintaining credit risk,					
6	Earning ability has a significant influence on performance of banks.					
7	Earning ability represents bank's capability to maintain quality and earn consistently.					
8	Restructuring of top management improves financial performance					
9	Continuous training of employees improves financial performance					

10	Liquidity is fundamental to the well-being of banks, that It determines their growth and development.					
11	Liquidity problem has been major challenges for private commercial banks.					
12	Deeper distribution in terms of more branches leads to higher financial performance					
13	Partnering with other related institutions improves financial performance					
14	The strategic positioning of bank branches directly impacts the profit					
15	Offering of a wide range of products contributes to more profits					

2. External factors

	Statement	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
16	Ethiopian Banking Industry has been on upward trend in the last 5 years					
17	Ethiopia banking industry is highly concentrated and high competition exists.					
18	The development of financial sector in Ethiopia has an impact on performance					
19	The economic growth or GDP has a key role on the bank's financial performance					
20	As the economy grows and more private commercial banks join the market, it will bring challenges to the existing banks activities.					
21	Bank ownership, whether public or private has a role to play on performance/profitability					

22	Macro-economic policies by the government such as increasing or decreasing its expenditure affects bank's financial performance					
23	Implementation of NBE regulations and directives has been a major challenge to the performance of private commercial banks					
24	The volatility of exchange rates affects bank's financial performance					
25	Depreciation and appreciation of the Ethiopian currencies is a key determinant of bank's financial performance					
26	The consumer purchasing power plays a role in bank's financial performance					
27	Stability of inflation rate plays a role in the profit the bank makes					
28	Imbalance of trade, which is the gap between import and exports in Ethiopia affects bank's					
29	The saving culture and practices of Ethiopians has an impact on bank's financial performance					
30	Interest rate variation has effect on financial performance					
31	Ethiopian banking industry comprises an unsupportive Information technology culture.					
32	There is poorly developed telecommunication infrastructure in the country					

❖ What do you think are the main determinants/challenges to your bank? You can tick more than one.

Competition from other banks

High rate of inflation

More banks joining in the market

Capital Position (Size of capital)

Lack of technology

NBE regulation

Expertise/Management turnover

Are there other determinants contributing to performance of private commercial banks? If yes please specify.

.....

Part Three: Opportunities of private Commercial banks

	Statement	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
33	The liberalization of the industry.					
34	Working collaboration with other financial institutions.					
35	Majority of the population is unbanked and fast customer service.					
36	Growing economy of the country.					
37	Technological innovation and advancements in the country.					

Are there other opportunities contributing to performance of private commercial banks? If yes please specify.

.....

Thank you for your cooperation.