DEPOSITS AND PROFITABILITY IN KENYA COMMERCIAL BANK, RWANDA

A Thesis
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Kampala International University
Kampala, Uganda

In Partial fulfillment of the requirements for the Degree
Master of Business Administration

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SEPTEMBER, 2012
DECLARATION A

"This thesis report is my original work and has not been presented for a degree or any other academic award in any University or Institution of learning"

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Date
DECLARATION B

"I confirm that this thesis was carried out by the candidate under my supervision"

MABONGA

Name and Signature of Supervision

____________________
Date
This thesis entitled "Deposits and loan profitability", Prepared and submitted by Musafiri B. Vedaste in the partial fulfillment of the requirements for the award of a master of Business Administration, has been examined and approved by the panel on oral examination with a grade of..................................................................................................

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Date of Comprehensive Examination: _______________________

Grade: ___________________________  

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Name and Sig of
Director, CHDR

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Name and Sig of DVC, CHDR
DEDICATION

This piece of work is dedicated to my beloved parents Safari Bahizi Charles, Muhorakeye Dative who takes care of me since my first day of life up to now, may God Almighty bless you. I cannot forget my classmates Nkunda Gasore Prince, Mukamurenzi Delphine. My brothers and sister: Karimba Yannick, Ushizimpumu Remy and Iriza Providence.
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Finally I would like to acknowledge the authors who are listed in the reference section of this work, whose works have served as important input to this study.
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ABSTRACT

The study was set out to establish the relationship between Deposits and Loan profitability in Kenya Commercial Bank of Rwanda. The objectives of this study are; to determine the profile of the correspondent in terms of age, gender, rank, and highest education qualification, to determine the impact of deposits on bank loan profitability, determine the relationship between deposits and loan profitability in Kenya commercial bank of Rwanda. The descriptive research design method was used in this study. It involves using questionnaire in collecting data from the respondents and both qualitative and quantitative research designs were used for data analysis. The SPSS was to analyze all data. The study population comprised 148 employees of Bank from which sample size of 108 respondents were chosen, using stratified random sampling method. The findings of the study revealed that there's non significant relationship between deposits and loan profitability in Kenya Commercial Bank of Rwanda. Conclusion there is no relationship between deposits and loan profitability in Kenya Commercial Bank of Rwanda. Recommendation Kenya commercial of Rwanda should put in place competitive strategies to raise more deposits and give out many secured loans for short, medium and long term. This will enhance customer royalty and deposits will be increased, the bank should encourage customers saving for future investment.
bank can’t give out loans and loans are the most important source of external finance disruptions to the loan supply might cause great changes in economic activity. Banks play a special role in providing external funds to the economy.

Statement of the problem

Banks are making little profit, others are making loss due to the insufficient of deposits and some micro finances are being closed for lack of sustainability capacity, as the main role of the bank is to collect deposits from customers who have surplus of money and lend to customers who have deficit of money, these days deposits are limited and bank have to grant loans according to regulation of National bank of Rwanda, all banks should have reserves in National bank of Rwanda, and loan to be granted can’t go above seventy percent of mandatory reserves, the profitability of banks depends on performing loans given out, performing loans are key factor of determinant of profitability of the bank.

Kenya commercial bank of Rwanda has collapsed two years consecutively due to the low of volume of loans given out, the third year the volume of loans has been increased, Kenya commercial bank of Rwanda has made profit and staff have got bonus. The volume of loan depends on the volume of the deposits, when the bank is liquid many loans can be given out and the profitability can be high.

Many banks are making loss and others are making little profit, micro finances are being closed, interest rate on savings is getting high. Therefore there is need to carry out an analytical study how deposits affect loan profitability. Loan is pillar of economic development.

It’s very important to know how the deposits affect the loan to be granted in banking industry, bank loans are the most important source of external finance. Disruption to the loan supply might cause great changes in economic activity. The bank loan has relationship with deposits which are playing a big role in the transmission process of the bank loan.
The bank loan is the most popular way that many people follow and develop as the way to clear their financial problem and it has extremely important role since it is followed by some people who usually trap and cannot solve their financial problems. In Rwanda banking industry there is challenge for banks to get deposits, it’s important to know how deposits are determinant factor of the volume of loan.

**Purpose of the study**

The main purpose of this research was to establish the extent to which deposit affects loan profitability of banking industry, to test the hypothesis of no significant relationship between the study variables, the researcher further attempts to identify the weakness and strength embedded in the deposits and to validate the theory to which the study was underpinned.

**Objectives of the Study**

**General:** The aim of this study was to establish the relationship between deposits and loan profitability.

**Specific objective**

This study achieved the following objectives

1. To determine the profile of the respondent in terms of age, gender, rank, educational qualification.
2. Determine the level of deposits on loan profitability in Kenya Commercial Bank of Rwanda
3. Determine the level of loans profitability in Kenya Commercial Bank of Rwanda
4. To determine the significant relationship between deposits and loans in Kenya commercial bank of Rwanda

**Research Questions**

In order to achieve these objectives, the following guiding questions were set:

1. What is the profile of the respondent in terms of age, gender, rank, educational qualification?
2. What is the level of deposits in Kenya Commercial Bank of Rwanda

3. What is the level of loans profitability in Kenya Commercial Bank of Rwanda

4. What is the significant relationship between deposits and loan profitability in Kenya commercial bank of Rwanda?

**Null hypothesis**
There is no significant relationship between deposits and loan profitability in banking industry in Rwanda.

**Scope of the study**

**Geographical Scope**
The study covered the Kenya commercial bank of Rwanda (KCBR) headquarter and its 9 branches.

**Theoretical scope,**

The study was guided by the Bucket theory of deposit acceptance, which provides a systematic way to set and reach financial goals and it helps in building sound loan profitability (Henderson, 1990), as well as the decision theory (Hanson, 1994), which describes a body of knowledge and related analytical techniques of formality designed to help a decision maker choose among a set of alternatives in light of their possible consequences.

**Content Scope**
The study intended to determine the relationship between deposit (independent variable) and loan profitability of selected financial institution (Dependent variable), the banks can't give out loans without having deposits. The banks should have loan monitoring system and proper assessment of loan to be granted.
Time scope
The study considered how Kenya commercial bank of Rwanda has evolved from 2009 -2012 when the world had started experiencing the effects of the global financial crisis.

Significance of the study
The findings of the study are beneficial to many different categories of people and in many different ways:

To the Government this study is of great priority to the government as a whole given to evaluate the deposits on financial institutions performance as they come up with policies regulating banks and their performance. The study findings will therefore be beneficial to policy makers as it will act as a tool in formulating the right policies that will enhance deposits acceptance in financial institutions especially Kenya commercial bank of Rwanda.

To local people, the study findings will help the different bankers to come up with informed decisions concerning the modes of accumulating more deposits and lend more with the purpose to make more profit. To the local people the study will act as a yardstick in measuring the effectiveness of the government policies among commercial banks.

To future researchers, the study will contribute to the available knowledge as well as act as basis for further research on the same subject. This study will benefit the researcher by helping him acquire practical research skills and will also serve as a partial requirement for the award of a degree of master in Finance and banking from Kampala International University.

To Kenya Commercial Bank of Rwanda, this research study will contribute in guiding the bank to set competitive strategies of mobilizing deposits and the proper assessment of the loan to be granted.

Operational Definitions of key Terms

For the purpose of this study, the following terms are operationally defined:
**Definition of Current deposit:** current deposit is the funds held in an account from which it can be withdrawn at any time without any advance notice to the depository institution.

**Saving deposit:** saving deposit means a deposit for individuals who wish to deposit certain amounts out of their current income with the aim of safeguarding their future and also earning interest during savings period.

**Fixed deposit,** the term fixed deposit means deposit repayable after the expiry of a specified period. Since it is repayable only after a fixed period of time, which is to be determined at the time of opening of the account, it is also known as time deposit. Fixed deposits are most useful for commercial banks.

**Loan,** loan is a type of debt, like all debt instruments, a loan entails the redistribution of financial assets over time, between the lender and the borrower. In a loan, the borrower initially receives or borrows an amount of money, called the principal, from the lender, and is obligated to pay back or repay an equal amount of money to the lender at a later time. Typically, the money is paid back in regular installments or partial repayments; in an annuity, each installment is the same amount.
CHAPTER TWO

REVIEW OF RELATED LITERATURE

Concepts, Opinions, Ideas from Authors/Experts Deposit

Deposits placed into a banking institution for safekeeping. Bank deposits are made to deposit accounts at a banking institution, such as savings accounts, checking accounts and money market accounts. The account holder has the right to withdraw any deposited funds, as set forth in the terms and conditions of the account. The "deposit" itself is a liability owed by the bank to the depositor (the person or entity that made the deposit), and refers to this liability rather than to the actual funds that are deposited.

Money is given in advance to show intention to complete the purchase of a property.

Money transferred into a customer's account at a financial institution.
Funds placed into an account at a depository institution to increase the credit balance of the account.
Down payment is given in advance to support the intention to complete a commercial transaction.

Time deposits

Time deposits are savings products in which a client makes one or more deposits that cannot be withdrawn for a specified period without penalty. At the end of the term, the client can withdraw the entire amount plus the interest accrued. The financial institutions offers a range of possible terms and usually pays a higher interest rate of the longer the term, although at some point rates tend to decline as the risk of interest rate changes increases. Because time deposits tend to be larger than other types of deposits, have contracted withdrawal times, and involve fewer transactions, time deposits can provide a significant source of relatively low-cost funds that facilitate asset liability management.
**Certificate of deposit**

Certificate of deposit is a debit instrument issued by a bank that locks in interest for a specific period (six months, one year, and five years, for example). Such instruments usually carry penalties for early withdraw. A number of transformed institutions have issued certificates of deposit successfully. Most have been issued locally and tend to be bought by local institutional investors. In some cases, however, microfinance institutions have issued certificate of deposit international as a way to tap into the foreign capital markets. The first well-known example of this strategy was Bancosol in Bolivia, which issued six-month certificates of deposit on the United State market in 1995. Today, more than 50 percent of BancoSol liabilities are in certificate of deposit.

**Programmed savings**

Programmed (or contractual) savings plans require clients to deposit a fixed amount on a regular schedule. They usually pay interest, and can be a popular product for families trying to save for a large purchase, a home, school fees, or a special occasion such as a marriage.

**Primary Deposits:** Primary deposits arise or formed when cash or cheque is deposited by customers. When a person deposits money or cheque, the bank will credit his account. The customer is free to withdraw the amount whenever he wants by cheques. These deposits are called "primary deposits" or "cash deposits." It is out of these primary deposits that the bank makes loans and advances to its customers. The initiative is taken by the customers themselves. In this case, the role of the bank is passive. So these deposits are also called "passive deposits." These deposits merely convert currency money into deposit money. They do not create money. They do not make any net addition to the stock of money. In other words, there is no increase in the supply of money.

**Profitability:** is expressed in terms of several popular numbers that measure one of two generic types of performance: "how much they make with what they've got" and "how much they make from what they take in".
Extent of profit the degree to which an individual, company, or single transaction achieves financial gain.

Generation of profit is the ability to achieve financial gain from a sale or other commercial transaction.

Profits are the financial returns or rewards that business owners aim to achieve to reflect the risk that they take and given that most entrepreneurs invest in order to make a return, the profit earned by a business can be used to measure the success of that investment. Profitability, rather than profit, is the key measure of a business's performance (Hawkins, 1997).

Profit is also an important signal to other providers of finance to a business for instance banks, suppliers and other lenders are more likely to provide finance to a business that can demonstrate that it makes a profit (or is very likely to do so in the near future) and that it can pay debts as they fall due. Further profit is also an important source of finance for a business as the profits earned which are kept in the business (Lending not distributed to the owners via dividends or other payments) are known as retained profits.

**Theoretical Perspectives**

The study was guided by the Bucket theory of deposit acceptance, which provides a systematic way to set and reach financial goals and it helps in building sound loan profitability (Hederson, 1990), as well as the decision theory (Hanson, 1994), which describes a body of knowledge and related analytical techniques of formality designed to help a decision maker choose among a set of alternatives in light of their possible consequences.

This study also was based on the deposits and loan profitability, the role of the deposit to an economic system is vital; deposits represent customer’s savings or their financial assets. By depositing money in a bank, the customers expects the bank to safeguard the savings, to utilize them into productive investments, the
deposits contribute 75% of a bank’s total fund (Rose 1997).

In this study, the researcher opted to view the influence of deposits on loan profitability, the performance of financial institution depends on the level of deposits, the more the financial institutions are liquid, the bank can give out performing loans and the profitability will be high.

Related studies

According to Saunders (2000) the most important activity of commercial banks is to mobilize deposits from the public. People who have surplus income and savings find it convenient to deposit the amounts with banks. Depending upon the nature of deposits, funds deposited with bank also earn interest is higher, public are motivated to more funds with bank. There is also safety of funds deposited with the bank.

In this study, deposits are conceptualized to be referring to current deposit, saving, fixed deposit.

Current deposit also called demand deposit; current deposit can be withdrawn by the depositor at any time. Currents accounts do not carry any interest as the amount deposit in these accounts is repayable on demand without any restriction.

Savings deposit means for individuals who wish to deposit amounts out of their current income. It helps in safe guarding their future also earns interest.

The term fixed deposit means deposit repayable after the expiry of a specified period. Since it is repayable only after a fixed period of time which is to be determined at the time of opening the account, it is also known as time deposit. Fixed deposits are most useful for a commercial bank.

Recurring deposit are gaining wide popularity these days. Under this type of deposit, the depositor is required to deposit a fixed amount of money every month for a specific period of time.

A commercial bank by definition is a profit hunting institution. The bank has to earn profit to earn income to pay salaries to the staff, interest to the depositors, dividend
to the shareholders and to meet the day-to-day expenditure. Since cash is the least profitable asset to the bank, there is no point in keeping all the assets in the form of cash on hand. The bank has got to earn income. Hence, some of the items on the assets side are profit yielding assets. They include money at call and short notice, bills discounted, investments, loans and advances, etc. Loans and advances, though the least liquid asset, constitute the most profitable asset to the bank. Much of the income of the bank accrues by way of interest charged on loans and advances. But, the bank has to be highly discreet while advancing loans.

A financial institution that provides services, such as accepting deposits, giving business loans and auto loans, mortgage lending, and basic investment products like savings accounts and certificates of deposit. The traditional commercial bank is a brick and mortar institution with tellers, safe deposit boxes, vaults and ATMs. However, some commercial banks do not have any physical branches and require consumers to complete all transactions by phone or Internet. In exchange, they generally pay higher interest rates on investments and deposits, and charge lower fees.

**Customer Satisfaction**

Customer satisfaction is a measure of how products and services supplied by a company meet or surpass customer expectation. Customer satisfaction is defined as the number of customers, or percentage of total customers, whose reported experience with a firm, its products, or its services (ratings) exceeds specified satisfaction goals or the extent to which consumers are happy with the products or services provided by a business.

Consumer satisfaction is an important concept in business, because happy customers are those most likely to place repeat orders and explore the full range of service offered and as such consumer satisfaction has increasingly become a key element of business strategy (Lantos P.H., 2010).
Depositing management

Hirsch (2010) in a study of time management and venture success in Eritrean fishing empirically showed that time management contributes to success in Eritrean fishing industry.

Kaye (2005) studied customer satisfaction and business success of MTN and established that customer satisfaction is one of the major factors that contribute to success of MTN in Uganda.


Nankya (2006) in the study of improved product functions and success of Toyota Uganda empirically showed that improved product functions contribute to success of Toyota Uganda.

The portion (expressed as a percent) of depositors' balances banks must have on hand as cash. This is a requirement determined by the country's central bank, which in the U.S. is the Federal Reserve. The reserve ratio affects the money supply in a country. This is also referred to as the "cash reserve ratio" (CRR).

For example, if the reserve ratio in the U.S. is determined by the Fed to be 11%, this means all banks must have 11% of their depositors' money on reserve in the bank. So, if a bank has deposits of $1 billion, it is required to have $110 million on reserve. In national Bank of Rwanda the reserve ratio is 5%.

Reserve requirement

The reserve requirement (or cash reserve ratio) is an amount held by central bank to be used. It is normally in the form of cash stored physically in a bank vault (vault cash) or deposits made with a central bank basing on total deposit held by commercial bank. Reserve requirement is regulated by central bank. (http://en.wikipedia.org, 16th August 2012).
The required reserve ratio is sometimes used as a tool in monetary policy, influencing the country's borrowing and interest rates by changing the amount of funds available for banks to make loans with. Western central banks rarely alter the reserve requirements because it would cause immediate liquidity problems for banks with low excess reserves; they generally prefer to use open market operations (buying and selling government-issued bonds) to implement their monetary policy. The People's Bank of China uses changes in reserve requirements as an inflation-fighting tool, and raised the reserve requirement ten times in 2007 and eleven times since the beginning of 2010. As of 2006 the required reserve ratio in the United States was 10% on transaction deposits.

**Effects on money supply**

The reserve requirement can be used as an instrument of monetary policy, because the higher the reserve requirement is set, the less funds banks will have to loan out, leading to lower money creation and perhaps ultimately to higher purchasing power of the money previously in use. The effect is multiplied, because money obtained as loan proceeds can be re-deposited; a portion of those deposits may again be loaned out.

**Risks Associated with Lending**

According to the OCC’s supervision by risk philosophy (Comptroller’s Handbook, 1998), risk is the potential that events, expected or unexpected, may have an adverse impact on the bank’s earnings or capital. The OCC has defined nine categories of risk for bank supervision purposes. These risks, which are defined in other Comptroller’s Handbook sections, are credit, interest rate, liquidity, price, foreign exchange, transaction, compliance, strategic, and reputation. Banks with international operations are also subject to country risk and transfer risk.
These risks are not mutually exclusive; any product or service may expose the bank to multiple risks. For analysis and discussion, however, the OCC identifies and assesses the risks separately.

A key challenge in managing risk understands the interrelationships of the nine risk factors. Often, risks will be either positively or negatively correlated to one another. Actions or events will affect correlated risks similarly. For example, reducing the level of problem assets should reduce not only credit risk but also liquidity and reputation risk. When two risks are negatively correlated, reducing one type of risk may increase the other. For example, a bank may reduce overall credit risk by expanding its holdings of one- to four-family residential mortgages instead of commercial loans, only to see its interest rate risk soar because of the interest rate sensitivity and optionality of the mortgages.

**Lending can exposes a bank’s to the risks.**

Therefore, it is important that the examiner understands all the risks embedded in the loan portfolio and their potential impact on the institution. How each of these categories relates to a bank’s lending function is detailed in the following sections

**Credit Risk**

For most banks, loans are the largest and most obvious source of credit risk. However, there are other pockets of credit risk both on and off the balance sheet, such as the investment portfolio, overdrafts, and letters of credit. Many products, activities, and services, such as derivatives, foreign exchange, and cash management services, also expose a bank to credit risk.

The risk of repayment, i.e., the possibility that an obligor will fail to perform as agreed, is either lessened or increased by a bank’s credit risk management practices. A bank’s first defense against excessive credit risk is the initial credit-granting process sound underwriting standards, an efficient, balanced approval process, and a competent lending staff. Because a bank cannot easily overcome
borrowers with questionable capacity or character, these factors exert a strong influence on credit quality. Borrowers whose financial performance is poor or marginal, or whose repayment ability is dependent upon unproven projections can quickly become impaired by personal or external economic stress. Management of credit risk, however, must continue after a loan has been made, for sound initial credit decisions can be undermined by improper loan structuring or inadequate monitoring. Traditionally, banks have focused on oversight of individual loans in managing their overall credit risk. While this focus is important, banks should also view credit risk management in terms of portfolio segments and the entire portfolio. The focus on managing individual credit risk did not avert the credit crises. However, had the portfolio approach to risk management augmented these traditional risk management practices, banks might have at least reduced their losses. Effective management of the loan portfolio’s credit risk requires that the board and management understand and control the bank’s risk profile and its credit culture. To accomplish this, they must have a thorough knowledge of the portfolio’s composition and its inherent risks. They must understand the portfolio’s product mix, industry and geographic concentrations, average risk ratings, and other aggregate characteristics. They must be sure that the policies, processes, and practices implemented to control the risks of individual loans and portfolio segments are sound and that lending personnel adhere to them.

Banks engaged in international lending face country risks that domestic lenders do not. Country risk encompasses all of the uncertainties arising from a nation’s economic, social, and political conditions that may affect the payment of foreigners’ debt and equity investments. Country risk includes the possibility of political and social upheaval, nationalization and expropriation of assets, governmental repudiation of external indebtedness, exchange controls, and currency devaluation or depreciation. Unless a nation repudiates its external debt, these developments might not make a loan uncollectible. However, even a delay in collection could weaken the lending bank.
Transfer risk, which is a narrower form of country risk, is the possibility that an obligor will not be able to pay because the currency of payment is unavailable. This unavailability may be a matter of government policy. For example, although an individual borrower may be very successful and have sufficient local currency cash flow to pay its foreign (e.g., U.S. dollar) debt, the borrower’s country may not have sufficient U.S. dollars available to permit repayment of the foreign indebtedness. The transfer risk associated with banks’ exposures in foreign countries is evaluated by the Interagency Country Exposure Review Committee (ICERC). For examination purposes, the transfer risk rating assigned to a country by the ICERC applies to all bank assets in that country. However, examiners may classify individual loans and other assets more severely for credit risk reasons.

Interest Rate Risk

The level of interest rate risk attributed to the bank’s lending activities depends on the composition of its loan portfolio and the degree to which the terms of its loans (e.g., maturity, rate structure, and embedded options) expose the bank’s revenue stream to changes in rates.

Pricing and portfolio maturity decisions should be made with an eye to funding costs and maturities. When significant individual credits or portfolio segments are especially sensitive to interest rate risk, they should be periodically stress-tested. If the asset/liability management committee (ALCO), which typically is responsible for managing the bank’s interest rate risk, is to manage all of the bank’s positions, it must have sufficient reports on loan portfolio and pipeline composition and trends. These reports might include a maturing loans report, pipeline report, and rate and repricing report.

Banks frequently shift interest rate risk to their borrowers by structuring loans with variable interest rates. Borrowers with marginal repayment capacity may experience financial difficulty if the interest rates on these loans increase. As part of the risk management process, banks should identify borrowers whose loans have heightened sensitivity to interest rate changes and develop strategies to mitigate the
risk. One method is to require vulnerable borrowers to purchase interest rate protection or otherwise hedge the risk.

**Liquidity Risk**

Because of the size of the loan portfolio, effective management of liquidity risk requires that there be close ties to, and good information flow from, the lending function. Obviously, loans are a primary use of funds. And while controlling loan growth has always been a large part of liquidity management, historically the loan portfolio has not been viewed as a significant source of funds for liquidity management. Practices are changing, however. Banks can use the loan portfolio as a source of funds by reducing the total dollar volume of loans through sales, securitization, and portfolio run-off.

In fact, banks are taking a more active role in managing their loan portfolios. While these activities are often initiated to manage credit risk, they have also improved liquidity. Banks increasingly are originating loans "for sale" or securitization. Consumer loans (mortgages, installment loans, and credit cards) are routinely originated for immediate securitization. Many larger banks have been expanding their underwriting for the syndicated loan market. Additionally, banks are also expanding the packaging and sale of distressed credits and otherwise undesirable loans.

As part of liquidity planning, a bank's overall liquidity strategy should include the identification of those loans or loan portfolio segments that may be easily converted to cash. A loan's liquidity hinges on such characteristics as its quality, pricing, scheduled maturities, and conformity to market standards for underwriting. Loans are also a source of liquidity when used as collateral for borrowings. The ease with which a bank can participate or sell loans to other lenders or investors (and the terms on which the bank can do so) will vary with market conditions, the type of loan, and the quality of loan. Information provided for liquidity analysis should include an assessment of these variables under various scenarios.
Liquidity is also affected by the amount of the bank's commitments to lend and the actual amount that borrowers draw against those commitments. A bank should have systems to track commitments and borrower usage.

Knowledge of the types of commitments, deals in the pipeline, normal usage levels, and historically high usage levels are important in assessing whether available liquidity will be adequate for normal, seasonal, or emergency needs. Management information systems should distinguish between commitments that the bank is legally obligated to fund and those (guidance or advisory lines) that it is not. Any analysis of a bank's ability to reduce or cut existing commitments must consider more than its legal obligation to lend. It should also consider reputation risk and the potential for lender-liability actions. The withdrawal or reduction of commitments can have significant ramifications for a bank.

From a strategic perspective, any tightening of commitments may adversely affect a bank's ability to maintain or grow a customer base if it is perceived as an unreliable lender in tight credit markets. A bank's reputation may also suffer if it is perceived as unwilling to support community credit needs. Given these ancillary risks, bank management must carefully assess the implications of curtailing lending lines.

Price Risk

Most of the developments that improve the loan portfolio's liquidity have implications for price risk. Traditionally, the lending activities of most banks were not affected by price risk. Because loans were customarily held to maturity, accounting doctrine required book value accounting treatment.

However, as banks develop more active portfolio management practices and the market for loans expands and deepens, loan portfolios will become increasingly sensitive to price risk.
Loans originated for sale as part of a securitization or for direct placement in the secondary market carry price risk while they are in the pipeline awaiting packaging and sale. During that period, the assets should be placed in a “held-for-sale” account, where they must be re-priced at the lower of cost or market. The same accounting treatment can apply to syndicated credits and distressed loans. When a bank underwrites a larger portion of a syndicated loan than its “hold” position, the excess portion must be placed in a held-for-sale account. Once a sale strategy is adopted for distressed or otherwise undesirable credits, those credits should also be placed in a held-for-sale account. Banks engaged in international lending may be affected by price changes in the secondary market for such loans. Each month, banks that actively trade foreign debt must mark to market the loans in their trading account and assess the trend of the market.

**Foreign Exchange Risk**

Foreign exchange risk is present when a loan or portfolio of loans is denominated in a foreign currency or is funded by borrowings in another currency. In some cases, banks will enter into multi-currency credit commitments that permit borrowers to select the currency they prefer to use in each rollover period. Foreign exchange risk can be intensified by political, social, or economic developments. The consequences can be unfavorable if one of the currencies involved becomes subject to stringent exchange controls or is subject to wide exchange-rate fluctuations.

**Transaction Risk**

In the lending area, transaction risk is present primarily in the loan disbursement and credit administration processes. The level of transaction risk depends on the adequacy of information systems and controls, the quality of operating procedures, and the capability and integrity of employees. Significant
losses in loan and lease portfolios have resulted from inadequate information systems, procedures, and controls. For example, banks have incurred increased credit risk when information systems failed to provide adequate information to identify concentrations, expired facilities, or stale financial statements. At times, banks have incurred losses because they failed to perfect or renew collateral liens; to obtain proper signatures on loan documents; or to disburse loan proceeds as required by the loan documents.

Compliance Risk

Lending activities encompass a broad range of compliance responsibilities and risks. By law, a bank must observe limits on its loans to a single borrower, to insiders, and to affiliates; limits on interest rates; and the array of consumer protection and Community Reinvestment Act regulations. A bank’s lending activities may expose it to liability for the cleanup of environmental hazards. A bank may also become the subject of borrower-initiated “lender liability” lawsuits for damages attributed to its lending or collection practices. Supervisory activities should include the review of the bank’s internal compliance process to ensure that examiners identify and investigate compliance issues.

Strategic Risk

A primary objective of loan portfolio management is to control the strategic risk associated with a bank’s lending activities. Inappropriate strategic or tactical decisions about underwriting standards, loan portfolio growth, new loan products, or geographic and demographic markets can compromise a bank’s future. Examiners should be particularly attentive to new business and product ventures. These ventures require significant planning and careful oversight to ensure the risks are appropriately identified and managed. For example, many banks are extending their consumer loan activities to “subprime” borrowers. The product may be familiar, but the borrowers’ behavior may differ considerably from the banks’ typical customer. Do they understand the unique risks associated with this market, can they price for
the increased risk, and do they have the technology and MIS to service this market? Moreover, how will they compete with the nonbank companies who dominate this market? Both bankers and examiners need to decide whether the opportunities outweigh the strategic risks. If a bank is considering growing a loan product or business in a market saturated with that product or business, it should make sure that it is not overlooking other lending opportunities with more promise. During their evaluation of the loan portfolio management process, examiners should ensure that bankers are realistically assessing strategic risk.

Reputation Risk

When a bank experiences credit problems, its reputation with investors, the community, and even individual customers usually suffers. Inefficient loan delivery systems, failure to adequately meet the credit needs of the community, and lender-liability lawsuits are also examples of how a bank’s reputation can be tarnished because of problems within its lending division. Reputation risk can damage a bank’s business in many ways. The value of the bank’s stock falls, customers and community support is lost, and business opportunities evaporate. To protect their reputations, banks often feel that they must do more than is legally required. For example, some banks have repurchased loan participations when credit problems develop, even though these problems were not apparent at the time of the underwriting.

Take size, for instance, introduced in the framework to account for existing economies or diseconomies of scale in the market. Smirlock (1985) and Pasiouras and Kosmidou (2007) show that size may positively and significantly influence profitability, explained perhaps by the potentially higher degree of product and loan diversification of larger banks compared to smaller, together with benefits emanating from economies of scale. Berger et al. (1987), on the other hand, show that size may only slightly reduce costs and that very large banks may actually suffer from scale inefficiencies and Micco et al. (2007) find a positive but insignificant
relationship between size and profitability. Athanasoglou et al., 2008 find that size is not important for revenue generation.

Similarly, credit and liquidity risks are shown to inconsistently influence bank profitability. Risk management is inherently associated with bank management; poor asset quality and low liquidity levels have been shown to be among the major causes of bank failure. During periods of increased uncertainty, portfolio diversification and/or liquid holdings are commonly enhanced. Abreu and Mendes (2002) find that credit risk, measured by loans to assets ratio, positively influenced the profitability of banks in Portugal, Spain, France and Germany. On the other hand, Bourke (1989) and Molyneux and Thornton (1992), among others, find a negative and significant relationship between the two. Possibly, banks exposed to riskier loans have also accumulated higher volumes of unpaid loans, which might adversely affect profits (Dietrich and Wanzenried, 2011). Similarly, holding higher levels of liquid assets may reduce profitability (Bourke, 1989; Molyneux and Thornton, 1992).

Conflicting results are also found in the case of ownership. While some studies find state ownership to be negatively related with profitability (e.g. Micco et. al., 2007; Iannotta et al., 2007), others show that ownership—state or private—may have no relevance for bank profitability (Bourke, 1989; Molyneux and Thornton, 1992), that empirical evidence may not support the theory that privately owned banks perform better than state—owned. Contrary also to popular belief, age may not positively influence profitability; Beck et al. (2005) find that in the case of Nigeria, for instance, older banks did not perform as well as the newer ones, which were better able to pursue new profit opportunities.

Similarly, regarding market power, studies by Bourke (1989) and Molyneux and Thornton (1992) confirm the structure—conduct—performance (market power) hypothesis that increased market power yields monopoly profits; the relationship is positive and significant. However, results of some other studies (Berger, 1995; Demirguc–Kunt and Huizinga, 1999; Staikouras and Wood, 2004; Athanasoglou et al., 2008) contradict the theory; the relationship may be neither positive nor significant. With respect to equity, empirical evidence suggests that better capitalised banks are more likely to be more profitable Bourke, 1989.
However, this may not necessarily be the case in all situations; Heffernan and Fu (2010), for instance, find that in the case of Chinese banks, the relationship may be positive or negative. The level of operational efficiency, measured by the cost to income ratio (Goddard et al., 2009, Dietrich and Wanzenried, 2011) or overhead costs to total assets (Athanasoglou et al., 2008) is more likely to positively influence profitability; these studies and others (e.g. Bourke, 1989; Molyneux and Thorton, 1992) show that more efficient institutions are more likely to be more profitable.
CHAPTER THREE

METHODOLOGY

Research Design

According to Shajahan (2006), a research design is a logical and systematic plan prepared for directing a research study. It specifies the objectives of the study, and the methodology and techniques to be adopted for achieving the objectives. It constitutes the blueprint for the collection, measurement and analysis of data, this study used the descriptive correlation.

Research Population

The population of the study in this research was comprised of 148 people. These included top level managers, middle level managers, and lower level managers they are all directly affected by whatever policy is made on deposits which in turn affects the bank’s performance.

Sample Size

The minimum sample size was computed using the Sloven’s formula, which states that, for any given population, the required sample size is given by:

\[ n = \frac{N}{1 + N(e^2)} \]

Where; \( n \) = the required sample size; \( N \) = the known the calculation is in the appendix .... of this work. Population size; and \( e \) = the level of significance, which is \( = 0.05 \). Given a total population of 148 respondents in selected bank of Kenya commercial bank of Rwanda a sample was 108 respondents as illustrated in Table1.
Table 2
Respondents of the Study

<table>
<thead>
<tr>
<th>Bank</th>
<th>Total Target Population</th>
<th>Sample population</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kenya commercial bank (KCB)</td>
<td>148</td>
<td>108</td>
</tr>
<tr>
<td><strong>Grand Total</strong></td>
<td><strong>148</strong></td>
<td><strong>108</strong></td>
</tr>
</tbody>
</table>

Sampling Procedures

The researcher randomly selected the institution to participate in the study and respondents were chosen basing on simple random sampling techniques. The choice of procedure was based on knowledge, experience and exposure to the functioning of the financial institutions in the area.

Stratified sampling was used because of the different strata in the respondents and then simple random sampling was used to select respondents from each stratum.

Research Instrument

Two sets of questionnaires were developed and included the different aspects of deposits and profitability of banking industries. Likert four scale measure were adopted to determine the degree of importance of each of the item included in the questionnaire. All questions in this section were close ended, based on four Liker Scale, ranging from one to four; where 1=Strongly Disagree, 2= Disagree,3=Agree, 4= Strongly Agree.

Validity and Reliability of the Instruments

The research instruments that the researcher used were questionnaire and observations. Questionnaires were cross examined for approval by 5 research experts, to ensure that the information they would generate is appropriate and consistent. According to Amin (2005), Validity of research instrument refers to the extent to which the instrument measures what it is supposed to measure; therefore,
content validity of the questionnaire rated at 0.9 as it is shown below and detailed in the appendix V.

\[
\text{CVI} = \frac{\text{RQ}}{\text{TQ}} = \frac{32 + 38 + 34 + 37 + 37}{40} = \frac{188}{40} = 4.7 \\
\text{CVI} = \frac{36}{40} \\
\text{CVI} = 0.9
\]

As far as reliability is concerned, the researcher employed the test-retest method of reliability. Eleven (11) respondents were administered with the instrument. A space of two weeks was allowed and the same instrument was given to the same respondents. As Amin (2005) continues, the research instrument used is reliable when the minimum reliability index recommended in survey studies is 0.7. Hence, reliability of the instrument was tested using the Cronbach Alpha’s coefficient (a) and the results obtained equal 0.82 (SPSS results) which was greater than 0.70 indicating that the instrument was highly reliable.

**Data Gathering Procedures**

The researcher collected both primary and secondary data relevant to the study using questionnaires. The data collection process was organized and conducted in three stages:

**Before the administration of the questionnaires**

1. An introduction letter was obtained from the college of higher degrees and Research at Kampala International University, for the researcher to solicit approval to conduct the study from respective officials of Kenya commercial bank of Rwanda (KCBR) and its affiliated branches.
2. When approved, the researcher secured a list of the qualified respondents. This involved seeking permission by the researcher from the senior officials of Kenya commercial bank of Rwanda to protect qualified respondents from harm or harassment and their confidentiality and superiors’ sensitive information.
3. The respondents were explained about the research study and enough questionnaires were reproduced for distribution.
4. The researcher selected assistants who would assist in the data collection; brief and orient them in order to be consistent in administering the questionnaires.

**During the administration of the questionnaires**

1. The respondents were requested to answer completely and not to leave any part of the questionnaires unanswered.
2. The researcher and assistants emphasized retrieval of the questionnaires within ten days from the date of distribution.
3. On retrieval, all returned questionnaires were checked if all are answered.

**After the administration of the questionnaires**

The data gathered was collected, encoded into the computer and statistically treated using the Statistical Package for Social Sciences (SPSS).

**Data Analysis**

The frequency and percentage distribution will be used to determine the profile of the respondents.

The means and interpretations will be applied for the levels of deposit and loan profitability.

The following mean range will be used to arrive at the mean of the individual indicators and interpretation:

<table>
<thead>
<tr>
<th>Mean Range</th>
<th>Response Mode</th>
<th>Interpretation</th>
</tr>
</thead>
<tbody>
<tr>
<td>3.26-4.00</td>
<td>strongly agree</td>
<td>Very High</td>
</tr>
<tr>
<td>2.51-3.25</td>
<td>Agree</td>
<td>High</td>
</tr>
<tr>
<td>1.76-2.50</td>
<td>Disagree</td>
<td>low</td>
</tr>
<tr>
<td>1.00-1.75</td>
<td>strongly disagree</td>
<td>very low</td>
</tr>
</tbody>
</table>
To determine whether there is a significant relationship between deposit and loan profitability, Pearson linear correlation coefficient (PLCC) will be used to compute the influence of the independent variable to dependent variable.

To interpret the responses of the respondents, the following qualification of interpretation were used:

<table>
<thead>
<tr>
<th>Mean Range</th>
<th>Description</th>
<th>Interpretation</th>
</tr>
</thead>
<tbody>
<tr>
<td>3.26-4.00</td>
<td>Strongly Agree</td>
<td>Very High</td>
</tr>
<tr>
<td>2.51-3.25</td>
<td>Agree</td>
<td>High</td>
</tr>
<tr>
<td>1.76-2.50</td>
<td>Disagree</td>
<td>Low</td>
</tr>
<tr>
<td>1.00-1.75</td>
<td>Strongly Disagree</td>
<td>Poor</td>
</tr>
</tbody>
</table>

**Ethical Considerations**

To ensure that ethics is practiced in this study as well as utmost confidentiality for the respondents and the data provided by them, the following were done:

1. Seek permission to adopt the standardized questionnaire on school effectiveness through a written communication to the author;
2. The respondents were coded instead of reflecting the names.
3. Solicit permission through a written request to the concerned officials of the Kenya Commercial Bank of Rwanda included in this study.
4. Request the respondents to sign in the *Informed Consent Form* (Appendix 3)
5. Acknowledge the authors quoted in this study and the author of the standardized instrument through citations and referencing.
6. Present the findings in a generalized manner

**Limitations of the Study**

The researcher claims an acceptable (0.05 level of significance) 5% margin of error in view of the following anticipated threats to validity with relevance to this study:

1. Testing: Differences in conditions and time when the data was obtained from respondents by different persons on different days at different hours. This was minimized by orienting and briefing the research assistants on the sampling techniques and data gathering procedures.
2. Instrumentation: The research instrument on deposits was not standardized. A validity and reliability test was done to produce a credible research tool.

3. Extraneous variables: The researcher did not have control over the extraneous variables such as honesty of the respondents, personal biases and descriptive nature of the Design. For untruthfulness where some of the respondents were expected not to say the truth, the researcher probed the respondents further to establish the truth when it was deemed necessary and personal biasness were also avoided by the researcher.

4. Attrition: The researcher experienced loss of respondents over the course of a study, such as employees retired, resigned or died but the researcher gave out more questionnaires than the required number to reduce on this.
CHAPTER FOUR
PRESENTATION, ANALYSIS AND INTERPRETATION OF RESULTS

Introduction

This chapter shows the demographic characteristics of respondents, the level of Bank deposits, level of Loan profitability and the significant relationship between Bank deposits and Loan profitability in Kenya Commercial Bank of Rwanda. The presentation is based on data as collected from the field and as analyzed by the researcher.

Respondents were asked to provide their gender, age, marital status, academic level and their banking experience their responses were summarized using frequencies and percentage distributions as indicated in table 4.1 below;
### Table 4.1
Profile of Respondents

<table>
<thead>
<tr>
<th>Category</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Gender</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Male</td>
<td>60</td>
<td>55.6</td>
</tr>
<tr>
<td>Female</td>
<td>48</td>
<td>44.4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>108</strong></td>
<td><strong>100</strong></td>
</tr>
<tr>
<td><strong>Age</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>20-29</td>
<td>35</td>
<td>32.4</td>
</tr>
<tr>
<td>30-39</td>
<td>50</td>
<td>46.3</td>
</tr>
<tr>
<td>Above 40 yrs</td>
<td>23</td>
<td>21.3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>108</strong></td>
<td><strong>100</strong></td>
</tr>
<tr>
<td><strong>Marital status</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Single</td>
<td>30</td>
<td>27.8</td>
</tr>
<tr>
<td>Married</td>
<td>40</td>
<td>37.0</td>
</tr>
<tr>
<td>Widow</td>
<td>20</td>
<td>18.5</td>
</tr>
<tr>
<td>Divorced</td>
<td>18</td>
<td>16.7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>108</strong></td>
<td><strong>100</strong></td>
</tr>
<tr>
<td><strong>Highest education Qualification</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Certificate</td>
<td>36</td>
<td>32.1</td>
</tr>
<tr>
<td>Diploma</td>
<td>25</td>
<td>23.6</td>
</tr>
<tr>
<td>Degree</td>
<td>19</td>
<td>17.9</td>
</tr>
<tr>
<td>Masters</td>
<td>18</td>
<td>17.0</td>
</tr>
<tr>
<td>PhD</td>
<td>10</td>
<td>9.4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>108</strong></td>
<td><strong>100</strong></td>
</tr>
<tr>
<td><strong>Banking Experience</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1-3 yrs</td>
<td>30</td>
<td>27.8</td>
</tr>
<tr>
<td>4-6 yrs</td>
<td>60</td>
<td>55.6</td>
</tr>
<tr>
<td>6 and above yrs</td>
<td>18</td>
<td>16.7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>108</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Results in Table 4.1 indicated that male respondents (over 55%) were higher than female respondents (over 44%), and this indicates a big gender gap among the respondents in Kenya Commercial Bank of Rwanda.

Regarding age group, respondents in this sample were dominated by those between 30-39 years (46%), suggesting that most of the respondents in Kenya Commercial Bank of Rwanda are youths. About marital status, the biggest portion of
the respondents (over 37%) were married, however, there were some divorced over (over 16%).

With respect to academic qualification, majority of the respondents (over 32%) were Certificate holders, indicating that respondents are relatively qualified, and these were followed by Diploma holders (over 23%). Concerning Banking experience, results indicate that majority of respondent have a Banking experience of 4-6 years in Kenya Commercial Bank of Rwanda.

**Extent of Bank deposits**

The independent variable in this study was Bank deposits, for which the researcher wanted to determine its level. Bank deposits was measured using 20 questions, each of these questions was based on the four Likert scales. Respondents were asked to rate the extent to which Bank deposits is high or low by indicating the extent to which they agree or disagree with each question. Their responses were analyzed using SPSS and summarized using means as indicated in table 4.2 below;
### Table 4.2
Level of Bank deposits in Kenya Commercial Bank of Rwanda

<table>
<thead>
<tr>
<th>Category</th>
<th>Mean</th>
<th>Interpretation</th>
<th>Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mission of commercial banks is finance projects with money</td>
<td>3.34</td>
<td>Very high</td>
<td>1</td>
</tr>
<tr>
<td>Depositors to boost economy</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Price of loan depends on how banks are liquid</td>
<td>3.24</td>
<td>High</td>
<td>2</td>
</tr>
<tr>
<td>Mandatory reserves are managed by central bank to manage</td>
<td>3.23</td>
<td>High</td>
<td>3</td>
</tr>
<tr>
<td>Commercial banks and Micro finances institutions</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Commercial bank is not liquid it can't sustain operations of withdrawals</td>
<td>3.11</td>
<td>High</td>
<td>4</td>
</tr>
<tr>
<td>Institution has risk unit that manages fixed deposit</td>
<td>3.11</td>
<td>High</td>
<td>5</td>
</tr>
<tr>
<td>Efficient of bank deposits lead to the failure in its daily operations</td>
<td>3.06</td>
<td>High</td>
<td>6</td>
</tr>
<tr>
<td>Efficient liquidity has an impact on bank performance</td>
<td>2.89</td>
<td>High</td>
<td>7</td>
</tr>
<tr>
<td>Mandatory reserves are low, banks give out many loans</td>
<td>2.88</td>
<td>High</td>
<td>8</td>
</tr>
<tr>
<td>Institution does analysis recurring deposit prior to accept</td>
<td>2.87</td>
<td>High</td>
<td>9</td>
</tr>
<tr>
<td>Price of loan depends on cost of funds in banking industry</td>
<td>2.85</td>
<td>High</td>
<td>10</td>
</tr>
<tr>
<td>A commercial bank of Rwanda has system of deposits</td>
<td>2.83</td>
<td>High</td>
<td>11</td>
</tr>
<tr>
<td>Illiquidity</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Institution has strict conditions on accepting recurring deposit</td>
<td>2.80</td>
<td>High</td>
<td>12</td>
</tr>
<tr>
<td>Deposits are key indicators of the volume of loan to be granted</td>
<td>2.77</td>
<td>High</td>
<td>13</td>
</tr>
<tr>
<td>Bank performance depends on deposits and ability to give out</td>
<td>2.76</td>
<td>High</td>
<td>14</td>
</tr>
<tr>
<td>Borrowing loans</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deposits create loan in banking industry</td>
<td>2.76</td>
<td>High</td>
<td>15</td>
</tr>
<tr>
<td>Without sufficient deposits can't be allowed to give out loans</td>
<td>2.75</td>
<td>High</td>
<td>16</td>
</tr>
<tr>
<td>Institution has strict conditions for accepting fixed deposit</td>
<td>2.74</td>
<td>High</td>
<td>17</td>
</tr>
<tr>
<td>Deposits in banking industry</td>
<td>2.40</td>
<td>Low</td>
<td>18</td>
</tr>
<tr>
<td>Institutional liquidity determine the conditions of lending on short</td>
<td>2.37</td>
<td>Low</td>
<td>19</td>
</tr>
<tr>
<td>Term or term</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Efficient of bank liquidity can be the source of insolvency to</td>
<td>2.24</td>
<td>Low</td>
<td>20</td>
</tr>
<tr>
<td>Different obligation</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Key for interpretation of means**

<table>
<thead>
<tr>
<th>Mean range</th>
<th>Response mode</th>
<th>Interpretation</th>
</tr>
</thead>
<tbody>
<tr>
<td>3.26-4.00</td>
<td>strongly agree</td>
<td>Very high</td>
</tr>
<tr>
<td>2.51-3.25</td>
<td>Agree</td>
<td>High</td>
</tr>
<tr>
<td>1.76-2.50</td>
<td>Disagree</td>
<td>Low</td>
</tr>
<tr>
<td>1.00-1.75</td>
<td>Strongly disagree</td>
<td>Very low</td>
</tr>
</tbody>
</table>
Results in Table 4.2 the level of Bank deposits is generally high and this is indicated by the overall average mean of 2.78, as the mission of commercial banks is to finance projects to boost economy and increase the profitability of the bank, basing on the results there is a need from KCBR to take measures and strategies of increasing deposits, it will facilitate the bank to decrease loan interest rate hence increase loan access, the costs of funds will be reduced. It was discovered that when the insufficient of bank deposits lead to the failure in its daily operations and the mandatory reserves are low, it limits the banks to give out many loans.

For sustainability of bank's mission, the new strategies of rising up deposit and innovation on different savings and fixed deposits has to be permanent. Insufficient liquidity has an impact on bank performance and the institution does analysis recurring deposit prior to accept this will lead the institution to the insolvency to honor different obligation where the results indicate the mean of 2.24 which shows that the back needs to incur more effort for better performance.

The results indicated that from items 2-17 were rated high (means from 3.24-2.74) this means that respondent agreed with the researcher. This means that the banks have to analyse in-depth strategies for their daily operations.

**Level of Loan profitability**

The dependent variable in this study was the level of Loan profitability in Kenya Commercial Bank of Rwanda. This variable was operationalized using twenty questions in the questionnaire, with each question Likert scaled between one to four, where 1=strongly disagree, 2=disagree, 3= agree and 4= strongly agree. Respondents were required to rate the extent to which the level of Loan profitability is high or low by showing the extent to which they agree or disagree with each item. Their responses were analyzed using means as summarized in table 4.3;
### Table 4.3
Level of Loan profitability in Kenya Commercial Bank of Rwanda

<table>
<thead>
<tr>
<th>Category</th>
<th>Mean</th>
<th>Interpretation</th>
<th>Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>The level of bank profitability depends on level of performing loans given out by the bank</td>
<td>3.54</td>
<td>Very high</td>
<td>1</td>
</tr>
<tr>
<td>The interest rate depends on the potential risk that a bank will face in the future</td>
<td>3.12</td>
<td>High</td>
<td>2</td>
</tr>
<tr>
<td>You do not make a profit during the first years of your business, then investors don't expect to be paid and you don't have the money to pay on the counter for withdrawals operations</td>
<td>3.06</td>
<td>High</td>
<td>3</td>
</tr>
<tr>
<td>Loan management has impact on bank profitability</td>
<td>3.04</td>
<td>High</td>
<td>4</td>
</tr>
<tr>
<td>Bank liquid grant loans for long term</td>
<td>3.02</td>
<td>High</td>
<td>5</td>
</tr>
<tr>
<td>Pending on who your investors are, they may offer valuable business assistance that you may not have.</td>
<td>3.01</td>
<td>High</td>
<td>6</td>
</tr>
<tr>
<td>The interest rate for long time finance is high compared to short time finance</td>
<td>2.87</td>
<td>High</td>
<td>7</td>
</tr>
<tr>
<td>Risk of loan management has negative impact on bank performance</td>
<td>2.85</td>
<td>High</td>
<td>8</td>
</tr>
<tr>
<td>Bank profit comes from loan granted and fees and commissions related</td>
<td>2.80</td>
<td>High</td>
<td>9</td>
</tr>
<tr>
<td>Bank also earns some fees on exchange operations and on foreign transfers international and national.</td>
<td>2.77</td>
<td>High</td>
<td>10</td>
</tr>
<tr>
<td>The rate of mandatory reserves is high, the banks can still lend out many loans</td>
<td>2.71</td>
<td>High</td>
<td>11</td>
</tr>
<tr>
<td>Bank reserves determine the level of loan to be granted avoid bank collapse to pay withdrawals operations</td>
<td>2.67</td>
<td>High</td>
<td>12</td>
</tr>
<tr>
<td>An monitoring increase the level of loan performance in the banking industry</td>
<td>2.64</td>
<td>High</td>
<td>13</td>
</tr>
<tr>
<td>You are able to get a loan and pay schools fees at any time from banks where you are depositing from.</td>
<td>2.61</td>
<td>High</td>
<td>14</td>
</tr>
<tr>
<td>The amount required is accessed easily even if loan is not well paid</td>
<td>2.60</td>
<td>High</td>
<td>15</td>
</tr>
<tr>
<td>Recovered loans have negative impact on the economy of the country</td>
<td>2.58</td>
<td>Low</td>
<td>16</td>
</tr>
<tr>
<td>The bank has none performing loans, investors know that they will not get their money back</td>
<td>2.46</td>
<td>Low</td>
<td>17</td>
</tr>
<tr>
<td>The volume of loans depends on liquidity in banking industry</td>
<td>2.33</td>
<td>Low</td>
<td>18</td>
</tr>
<tr>
<td>The commissions and fees received from time to time on loans is a source of bank profit.</td>
<td>2.32</td>
<td>Low</td>
<td>19</td>
</tr>
<tr>
<td>Average mean</td>
<td><strong>2.69</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
The results in Table 4.3 showed that the level of Loan profitability in Kenya Commercial Bank of Rwanda is relatively high with the overall average mean range of 2.69. For better performance of loans given out by the bank there is a requirement of strong loan analysis, monitoring and management, basing on the average mean of 3.54 proof that a great emphasis on analysis is required. The forecast budgeting and loan analysis is required to predict the decrease of interest rate which will depend on the potential risk that a bank may face in the future. Some of the items indicated in the table above from 2-16 respondents agreed that an new assessment and redesign of the system to increase profitability is required since the means range is between 3.12-2.58. still items from 17-20 were rated low (means from 2.46-2.14). The highest aspect on Loan profitability was The level of bank profitability depends on level of performing loans given out by the bank (mean=3.54), yet the lowest aspect on Loan profitability was The commissions and fees received from time to time on loans are a source of bank profit (mean=2.14).

Lack of loan management increase negative impact on bank performance, when banks will be served with sufficient liquidity this will affect positively the profitability where the loan interest rate will be decreased, client will be motivated for deposits and loan applicant’s, this will increase the earnings of additional fees on exchange of the operations and on different transfers international and national.

When there is no adequate analysis and loan management, bank’s portfolio can be affected provisions will be made for bad loans and bank’s profits will be reduced, thus the credit department should assess properly loan applications and set and implement new strategies for loan monitoring to reduce the unrecovered loans.
Significant relationship between Bank deposits and Loan profitability in Kenya Commercial Bank of Rwanda

The last objective in this study was to establish whether there is a significant relationship between Bank deposits and Loan profitability in Kenya Commercial Bank of Rwanda, for which it was hypothesized that the level of Bank deposits and Loan profitability in Kenya Commercial Bank of Rwanda are significantly correlated. To test this null hypothesis, the researcher correlated the mean indices on Bank deposits and those on Loan profitability using the Pearson’s linear correlation Coefficient (PLCC), results of which are indicated in Table 4.4

Table 4.4
Significant relationship between Bank deposits and Loan profitability in Kenya Commercial Bank of Rwanda

<table>
<thead>
<tr>
<th>Variables Correlated</th>
<th>R-value</th>
<th>Sig</th>
<th>Interpretation</th>
<th>Decision on Ho</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank Deposits</td>
<td>0.963</td>
<td>0.000</td>
<td>No significant correlation</td>
<td>Rejected</td>
</tr>
<tr>
<td>Vs Loan profitability</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The PLCC results in Table 4.4, indicated that there is no significant correlation between Bank deposits and Loan profitability in Kenya Commercial Bank of Rwanda, (r = .963, sig. = .000). Basing on the results, the null hypothesis was rejected and it is concluded that Bank deposits and Loan profitability in Kenya Commercial Bank of Rwanda are not significantly correlated since the sig value is less than 0.05 the level of significance.
### Table 4.5
Regression Analysis between Bank deposits and profitability

<table>
<thead>
<tr>
<th>Variables Regressed</th>
<th>$R^2$</th>
<th>F-value</th>
<th>Sig.</th>
<th>Interpretation</th>
<th>Decision on Ho</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank deposits</td>
<td>.927</td>
<td>229.903</td>
<td>.000</td>
<td>Significant effect</td>
<td>Rejected</td>
</tr>
<tr>
<td>Vs Profitability</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The regressed results in the Table 4.5 above showed that 92.7% ($R^2=0.927$) of the dependent variable is explained by the independent variable. This means that Bank deposits have a strong significant effect on Profitability. There is a need of incurring much effort in improving and performing bank deposit
CHAPTER FIVE
SUMMARY, CONCLUSION AND RECOMMENDATIONS

This chapter presents a summary of major findings, conclusions and recommendations plus the suggested areas that need further research.

Findings
The study intended to determine the demographic characteristics of the respondents as to: Gender, Age, rank and Qualifications. The results indicated that most respondents were male (55%), between 30-39 years of age, 37% were married couples, majority were Certificate holders (over 32%) and 55% had banking experience of 4-6 years.

In relation to determine the extent of deposits in Kenya Commercial Bank of Rwanda, the results indicated an overall average mean of 2.78. The lowest aspect of Bank deposits was insufficient of bank liquidity which can be the source of insolvency to honor different obligation (mean=2.24), whole as the highest aspect of Bank deposits is the mission of commercial banks is finance projects with money from depositors to boost economy (mean=3.34). The bank has to set out different competitive strategies to raise more deposit.

The profitability in Kenya Commercial Bank of Rwanda was rated high with an overall mean range of 2.68. Basing on the analysis, the extent of deposit has an effect on the profitability. There is a need of focusing in partnership with microfinance’s institutions to keep high the profitability. This strategy will contribute to high deposit in Kenya Commercial Bank of Rwanda.

The findings indicated a positive and significant relationship between Bank deposits and profitability in Kenya Commercial Bank of Rwanda. The null hypothesis was rejected at the r= .963 and sig. value of .000 which is less than the level of significance 0.05 the maximum level of significance required to declare a relationship significant. There is no strong significant effect of the bank deposit to profitability in Kenya Commercial Bank of Rwanda.
Conclusions

The purpose of this study was to test the hypothesis relationship of the significant relationship between deposits and loan profitability in Kenya commercial bank, testing the null hypothesis, the PLCC results indicated that there is no significant correlation between deposits and loan profitability in Kenya Commercial bank Rwanda.

The study attempts to contribute to the deposits literature by comprehending the current experience of data collection the bankers. Based on the findings of the study, the foregoing analysis indicated that there is no significant relationship between these two variables. The results indicated negative significant correlation between deposits and loan profitability in Kenya commercial bank of Rwanda, the null hypothesis was accepted and conclusion was made that deposits and loan profitability in Kenya commercial bank of Rwanda are significantly not correlated, since the significant level is less than 0.05. The result from regression indicated that deposits affect strongly loan profitability. The bank should set competitive strategies to raise more deposits, without deposits bank can’t give out loans and loans are the most important source of external finance disruptions to the loan supply might cause great changes in economic activity.

Recommendations

The researcher would recommend more research on this study of deposits and loan profitability basing on the findings and the conclusions drawn from the study, further study should be conducted in order to discover in depth and find out new and detailed information on deposits and loan profitability in Kenya commercial bank of Rwanda.

Kenya commercial bank of Rwanda should set competitive strategies to raise more deposits, Kenya commercial bank of Rwanda should set strategies to access deposits in rural area, instead of to concentrate in town.
In addition Kenya commercial bank should put in place different deposits scheme to attract companies and individuals to save money at Kenya commercial bank for their future investments, this scheme will help Kenya commercial bank of Rwanda to raise deposits and give out loans to be profitable and preferred bank in Rwanda.

**Areas for Further Research**

The researcher cannot guarantee that the study was completely exhausted. In any case, the scope of the study was limited in accordance with the space, and objectives. It is therefore, suggested that a national research covering the whole country be undertaken, therefore prospective researchers and students should be encouraged to carry out research on the following areas:

1. The Relationship between interest rates and Loan profitability in Kenya Commercial Bank of Rwanda.
REFERENCES


Amin, M., E. (2005) Social Science Research: Conception, Methodology, and Analysis; Kampala: Makerere University


Beltratti, A. and R. Stulz, 2009, Why did some banks perform better during the credit crisis? A cross-country study of the impact of governance and regulation, ECGI

Berger, A., D. Hanweck and D. Humphrey, 1987, Competitive viability in banking: scale,


UNEP (United Nations Environment Programme).: 2004, Sustainable Development Priorities for South Pacific [online].
APPENDIX IA
TRANSMITTAL LETTER FOR THE RESPONDENTS

Dear Sir/ Madam,
Greetings!
I am a master student of Business Administration candidate of Kampala International University. Part of the requirements for the award of a thesis. My study is entitled, **Deposit and Loan Profitability in Banking Industry.** Within this context, may I request you to participate in this study by answering the questionnaires. Kindly do not leave any option unanswered. Any data you will provide shall be for academic purposes only and no information of such kind shall be disclosed to others.

May I retrieve the questionnaire within two Weeks (07) days
Thank you very much in advance.

Yours faithfully,
Mr. Musafiri B. Vedaste
OFFICE OF THE HEAD OF DEPARTMENT, EDUCATION, OPEN AND DISTANCE LEARNING
COLLEGE OF HIGHER DEGREES AND RESEARCH (CHDR)

Date: 20th June, 2012

RE: REQUEST FOR MUSAFIRI B. VEDASTE MBA/32905/102/DF
TO CONDUCT RESEARCH IN YOUR ORGANISATION

The above mentioned is a bonafide student of Kampala International University pursuing a Masters of Arts in Business Administration (Finance and Banking)

He is currently conducting a research entitled "Deposit and Loan Profitability in Kenya Commercial Bank of Rwanda"

Your Organization has been identified as a valuable source of information pertaining to his research project. The purpose of this letter is to request you to avail him with the pertinent information he may need.

Any information shared with him from your organization shall be treated with utmost confidentiality.

Any assistance rendered to him will be highly appreciated.

Yours truly,

Dr Fred Ssemugenyi
Head of Department
Education, Open and Distance Learning (CHDR)

NOTED BY:
Dr Sofia Sol T. Gaita
Principal-CHDR

"Exploring the Heights"
APPENDIX 11

CLEARANCE FROM ETHICS COMMITTEE

Date_______________

Candidate's Data

Name________________________________________
Reg.# ________________________________
Course ______________________________________
Title of Study ______________________________________

Ethical Review Checklist

The study reviewed considered the following:

___ Physical Safety of Human Subjects
___ Psychological Safety
___ Emotional Security
___ Privacy
___ Written Request for Author of Standardized Instrument
___ Coding of Questionnaires/Anonymity/Confidentiality
___ Permission to Conduct the Study
___ Informed Consent
___ Citations/Authors Recognized

Results of Ethical Review

___ Approved
___ Conditional (to provide the Ethics Committee with corrections)
___ Disapproved/ Resubmit Proposal

Ethics Committee (Name and Signature)

Chairperson ______________________________
Members ______________________________
APPENDIX III

INFORMED CONSENT

I am giving my consent to be part of the research study of Mr. Musafiri B. Vedaste that will focus on deposit and loan profitability.

I shall be assured of privacy and confidentiality and I will be given the option to refuse participation or withdraw my participation at any time.

I have been informed that the research is voluntary and that the results that will be given to me if I request for it.

Initials: ...........................................

Date: ...............................................
APPENDIX IV

SAMPLE SIZE OF SLOVEN'S FORMULA,

\[ n = \frac{N}{1 + N(e^2)} \], Where; \( n \) = the required sample size; \( N \) = the known the calculation is in the appendix .... of this work. Population size; and \( e \) = the level of significance, which is = 0.05. Given a total population of 148 respondents in selected bank of Kenya commercial bank of Rwanda a sample was 108 respondents as illustrated in Table1.
APPENDIX V

CALCULATION OF VALIDITY AND RELIABILITY

VALIDITY

CVI = \frac{RQ}{TQ} = \frac{32 + 38 + 34 + 37 + 37}{40} / 5

CVI = \frac{36}{40}

CVI = 0.89

CVI = 0.9

RELIABILITY

<table>
<thead>
<tr>
<th>NUMBER OF ITEMS</th>
<th>Scrubach Alpha Coefficient</th>
</tr>
</thead>
<tbody>
<tr>
<td>40</td>
<td>0.82</td>
</tr>
</tbody>
</table>
APPENDIX 1VA

FACE SHEET: PROFILE OF THE RESPONDENTS

1. Gender (Please Tick):
   ______ Male
   ______ Female

2. Age:
   ______ 20-29
   ______ 30-39
   ______ Above 40

3. Marital status:
   ______ Single
   ______ Married
   ______ Widow
   ______ Divorce

4. Highest certificate awarded:
   ______ Certificate
   ______ Diploma
   ______ Degree
   ______ Masters
   ______ Phd

5. Banking experience
   ______ 1-3 years
   ______ 4-6 years
   ______ Above 40
II. QUESTIONNAIRE TO DETERMINE THE LEVELS OF DEPOSITS

**Direction:** Please write your preferred option on the space provided before each item. Kindly use the rating guide below:

<table>
<thead>
<tr>
<th>Response Mode</th>
<th>Rating</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly Agree</td>
<td>(4)</td>
<td>You agree with no doubt at all.</td>
</tr>
<tr>
<td>Agree</td>
<td>(3)</td>
<td>You agree with some doubt</td>
</tr>
<tr>
<td>Disagree</td>
<td>(2)</td>
<td>You disagree with some doubt</td>
</tr>
<tr>
<td>Strongly Disagree</td>
<td>(1)</td>
<td>You disagree with no doubt at all</td>
</tr>
</tbody>
</table>

1. Deposits are key indicators of the volume of loan to be granted
2. The price of loan depends on how banks are liquid
3. If the mandatory reserves are low, banks give out many loans
4. Kenya Commercial Bank of Rwanda has system of deposits mobilization
5. Your Institution has risk unit that manages fixed deposit
6. Your Institution has strict conditions for accepting fixed deposit
7. Your Institution does analysis recurring deposit prior to accept
8. Your Institution has strict conditions on accepting recurring deposit
9. The price of loan depends on the cost of funds in banking industry
10. Deposits create loan in banking industry
11. Loans create deposits in banking Industry
12. Bank without sufficient deposits can’t be allowed to give out loans
13. The mission of commercial banks is to finance projects with money collected from depositors to boost economy
14. The mandatory reserves are determined by central bank to manage commercial banks and Micro finances institutions
15. If the bank is not liquid it can’t sustain operations of withdrawals on the counter
16. Bank liquidity determine the conditions of lending on short term or long term
17. Insufficient liquidity has an impact on bank performance
RESEARCHER'S CURRICULUM VITAE

Names: Musafiri B. Vedaste

Gender: Male

Date of Birth: 1976

Place of Birth: RDC (Masisi)

Nationality: Rwandese

Marital status: Single

Address: Kigali

Tel.: +250788309361

Email: vmusafiri@yahoo.fr

Educational Background

2010-2012: Kampala International University (KIU); Master of Business and Administration

2000-2004: Kigali Independent University in Management

1990-1997: Groupe Scolaire de Kigombe

Work Experience

2003 – 2004 Teller at Bank of Kigali

Skills, interest and experience

Fluent English, French, Kinyarwanda and Swahili, Computer skills.

THANK YOU FOR YOUR PARTICIPATION