RECAPITALISATION STRATEGIES EMPLOYED BY COMMERCIAL BANKS IN ZIMBABWE

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ABSTRACT

Recapitalization has been a world phenomenon, with the major aim being to strengthen the banking system for effective monetary management. Banking sector’s asset and liability discrepancy as well as general instability of the banking sector resulted in the Reserve Bank of Zimbabwe (RBZ) increasing capital requirements from USD 12.5 to USD 100 million. It is against this background that the research seeks to ascertain the reasons behind an increase in capital requirements by Central Bank, the recapitalization strategies being pursued by the commercial banking sector in Zimbabwe and their effectiveness. The issue of recapitalization happens to be a hot issue at Board and top management level and it is hoped that this research may provide a good insight into the possible solutions enabling commercial banks to meet capital requirements. Literature review explores the reasons behind an increase in capital requirements, the challenges facing commercial banks and the recapitalization strategies being implemented. Literature was premised on the work of Yin (1994), where effective implementations of recapitalisation strategies is seen as a variable dependent on the independent variables of choice of rights issue, new shares issue, mergers, acquisitions, retained earnings, capital subsidy and loan stock and convertible loan stock as recapitalization strategies. In an attempt to involve an examination of perceptions in order to gain an understanding of social and human activities the interpretive research philosophy was adopted. In addition and for the purposes of collecting original data to describe a population and enable measurement of attitudes and orientations in a large population, a descriptive survey design was deemed relevant for this research. The population covered the 16 major players in the commercial banking sector who are represented in the capital city Harare. Stratified random sampling and purposive sampling methods were used in the selection of top management, board members of banks and Reserve Bank personnel as respondents in this study. A sample of 25 respondents was chosen from a target population of 36. Interviews and a structured questionnaire were the principal research instruments for primary data. The study made use of industry journals, monetary policy statements, strategic reports of commercial banks to gather secondary data. It was revealed in the research that the major reasons behind recapitalization were; to reduce possibility of bank failures, beef up inadequate capital base, curb mismanagement of funds, control, unfair competition, protection of depositors’ funds and ultimately improve the efficiency of banks. The research established that banks were recapitalizing through strategies of; new shares issue, convertible stock, retained earnings, merger, acquisitions and rights issue. These the existing recapitalization strategies were seen as effective because majority of banks have been able to comply. Further recommendations are that banks should consider further strategies in the form of mergers, acquisitions, external capital, and diversification.

Keywords: Capital requirements, Recapitalization Strategies, Monetary management, Bank failures

Introduction

The objectives of banking system world over are to ensure price stability and facilitate rapid economic development as observed by Imala (2009). Regrettably, these objectives to a large extend have remained unattained in Zimbabwe mainly a result of deficiencies in the banking system which among other things include low capital base. This was further worsened by the decline of the global economic conditions coupled with constraints in the domestic economy and liquidity shortages and imposed constraints on the growth of the commercial
banking sector of Zimbabwe. Consequently this necessitated financial reforms in the banking sector. The banking system faces enormous challenges that if not addressed urgently, could snowball into a financial crisis (RBZ Mid Term Monetary policy; 2012).

Reserve Bank of Zimbabwe noted that low capitalization of the banks made them less able to finance the economy, and more prone to unethical and unprofessional practices. Increasing the capital base of banks in Zimbabwe would strengthen them and, in the process, deepen activities within the industry (Nyamhondera, 2013). Commercial banking sector has to be constituted by the number of banks that have the capacity to operate in all the towns in the country, funding agriculture and manufacturing, and in the process generating employment for Zimbabweans. Recapitalization has been a world phenomenon, with the major aim being to strengthen the banking system for effective monetary management. Examples of countries, notable for recapitalization programmes include the likes of Nigeria, Malawi, South Africa and Egypt. Their programmes made tremendous contribution towards economic growth, through stable and competitive interests’ rates, improved lending capacity and general security of the sector as commented by the World Bank Economic Review (2013).

In light of the above mentioned trends, the Reserve Bank of Zimbabwe Governor announced that commercial and merchants banks were now required to have minimum capital requirements of US$100 million from US$12.5 million and US$10 million respectively. Minimum capital requirements for building societies were also raised from US$10 million to US$80 million, finance and discount houses from US$7.5 million to US$50 million for micro finance houses. Banks are supposed to be fully compliant end of year 2020 (RBZ Mid Term Monetary policy; 2012). Given the current economic conditions banking players have seen the amount required as too high hence the outcry on the feasibility of meeting the 100 million thresholds by 2014. Nyamhondera, (2013) concedes that capital thresholds of US$100 million is so huge an amount, nearly 2.5 times than required in South Africa where their economy is 40 times larger than that of Zimbabwe. Zimbabwean situation is quite different as the country is faced with macro-economic instability, political instability, international trade restrictions and limited access to capital, which makes an enquiry of recapitalization strategies being used by commercial banks of interest.

Statement of the Problem

There is an asset and liability discrepancy as well as general instability in the banking sector which has necessitated the Central Bank to invoke increase in capital requirements.

Research Objectives

I. Ascertain reasons behind an increase in capital requirements by Central Bank
II. Identify recapitalization strategies being employed by commercial banks.
III. Evaluate effectiveness of the current recapitalization strategies meant to meet minimum capital requirements

Research Questions

I. What are the reasons behind the increase in capital requirements by the Central Bank?
II. What are the recapitalization strategies used by commercial banks?
III. How effective are the existing recapitalization strategies in meeting capital requirements?

Literature Review

Various theorists have presented findings on the reasons behind increase in capital requirements for commercial banks. The Soyinbo and Adekanye (2002) and Adam (2003) traced the increase in capital requirements as taking its roots from bank failures. In agreement, Imala (2005) noted that bank failures have been the major driver toward recapitalisation especially with reference to countries like Greece and Nigeria. Zimbabwe banking sector experienced major bank failures in 2004. With the major reason being misappropriation of depositors’ funds (RBZ Mid Term Monetary Policy 2005). However some observers argue that bank failures occur as a result of the central bank’s failure to undertake their mandate, in making sure that banks comply with banking acts through strict supervision (Gelos and Roldos 2006)/.
Onaolapo (2008) and Soyinbo and Adekanye (2008) concluded that increasing capital requirements was a result of inadequate capital base, mismanagement of funds, overtrading, lack of regulation and control; and unfair competition from the foreign banks. This is further supported by Imala (2005) who identified four rationales behind banking system reform. These were low capital base of banks, a large number of small banks with relatively few branches, the dominance of a few banks and poor rating of a number of banks. Adeipe (2005) argued that the most fundamental reason for increase in capital requirements was due to growing distress in the industry which was identified as the real threat of imminent bank failures. In Zimbabwe some banks were put under curatorship because of their involvement in speculative and fraudulent activities.

The researcher believes that there is a general consensus that change of a fundamental nature is necessary to redirect the banking system towards its traditional role of providing effective intermediation and financing economic growth. Soludo (2004) presented that increasing capital requirements is critical in bringing depositor confidence and protecting depositor funds. In agreement, Spong (2009) presented that banks must have enough capital to provide a cushion for absorbing possible loan losses, funds for its internal needs, and expansion and added security for depositors. Sani (2008) presented that increase in capitalization of banks is also done by authorities as a result of bringing confidence and financial state of stock holders. Adedipe (2005) concurred with these theorists when he said that bank regulators view it as an important element in holding government banking risks to an acceptable level.

**Research Methodology**

Research paradigm namely interpretivism, or qualitative approach was adopted for this research. In this regard the researcher will attempt to understand phenomena through accessing the meanings participants assign to them. Crucial to the interpretivist epistemology is that the researcher has to adopt an empathetic stance. The challenge here is to enter the social world of our research subjects and understand their world from their point of view. An interpretivist perspective is highly appropriate in the case of business and management research, particularly in such cases where the issue of recapitalization is both a complex and unique business situation. As for the research design the researcher will use a descriptive survey method. In this survey method research, the participants are going to answer questions administered through interviews and questionnaires and this will provide the primary data. The survey will also enable the researcher to measure attitudes and orientations in a large population.

The population of the study will be confined to the commercial banking industry which is made up of 16 players. To get a detailed view and to balance the study, the researcher will consider top management and board members of these commercial banks and personnel in the Banking, Licensing, Supervision and Surveillance departments at the Reserve Bank of Zimbabwe (RBZ), as respondents. Stratified random sampling method will be used in the selection of respondents. Simple random sampling was used to 25 respondents out of a population of 36. As for secondary data the researcher will make use of industry journals, monetary policy statements, strategic reports etc. The data will also be collected through interviews to enable the researcher to adapt the questions as necessary, clarify doubts, and ensure that the responses are properly understood by repeating or rephrasing the question and also pick non verbal cues from the respondents.

**Conclusion**

There was an ideal response rate of 67 % with 50% of respondents having been in the same position for 10 to 15 years, while 25% of respondents have experience above 15 years. and 25 % with less than 5 years. This demonstrated that the banking industry personnel had sufficient experience to effectively understand and handle recapitalization issues. Thus, this study noted that increase in capital requirements was motivated by the need to reduce possibility of bank failures. The results further demonstrate that mismanagement of funds was one of the reasons behind increase in capital requirements as alluded to by 80% of the respondents. The results also indicate that increase in capital requirements by Reserve Bank of Zimbabwe was prompted by inadequacy of the capital base. Recapitalization, as concluded from the research, was a key strategy in protecting the depositors’ funds.

Strategic reports from RBZ revealed that the banking sector of Zimbabwe is faced with a situation
where there are little deposits as depositors are sceptic about the future currency in use (DPC; 2013). Thus, recapitalisation will cushion the risks of those few deposits being made. Hence the study noted that recapitalisation of banks will result in increased depositor confidence. Soludo (2004) presented that increasing capital requirements is critical in bringing depositor confidence and protecting depositor funds. Respondents revealed that banks were considering new shares through listing on the Zimbabwe Stock Exchange. Loan stock which is long-term debt capital raised by a company for which interest is paid, usually half yearly and at a fixed rate, was being considered by banks, but it was not materializing due to the prevailing economic situation faced by the country. The study revealed that retained earnings were an alternative in the recapitalisation of banks in Zimbabwe unfortunately this may be compromised by the recent introduction of caps on interest rates and controls on bank charges, as this is likely to adversely affect profitability.

**Recommendations**

The study recommends more mergers as a recapitalization strategy as these have proved to be a success in the past. Banks in Zimbabwe can consider an offer for sale, a prospectus issue, a placing or an introduction to enable them raise capital. The banks can also consider being acquired by established local or international institutions. This strategy proved to be successful with reference to Steward Bank. The government can also play a pivotal role by assisting in the capitalization of banks through provision of capital to distressed banks.

**References**

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