THE IMPACT OF NON PERFORMING LOANS ON COMMERCIAL BANKS IN UGANDA: A CASE STUDY OF CENTENARY RURAL DEVELOPMENT BANK (CERUDEB)

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ABSTRACT

The purpose of this study was to analyze the impact of nonperforming loans on the performance of Commercial Banks in Uganda taking Centenary Bank as a case study. So the study performed a trend analysis on six key variables that included depositors, deposits, borrowers, non-performing loans and profits. In order to obtain associations between the variables, the Pearson correlation coefficient test was used.

The results obtained show that a one unit change in nonperforming loans leads to a non significant impact on profits by 0.1988 units. The same variable has an inverse relationship with deposits where by a 1 unit change in nonperforming loans leads to a reduction in deposits by 0.2343 holding other factors constant. The number of depositors is positively and significantly related to profits where a one unit change in depositors significantly leads to 0.5192 units of profits. An observation was also made that a 1 unit change in deposits will lead to a 0.3899 unit change in profits holding other factors constant. However, this relationship is not significant at the 5% level of significance (95% confidence level). Hence this study shows non significant effect of deposits on profits. This inverse relationship is statistically insignificant. on the other hand borrowers have a positive relationship with profits where by holding other factors constant, a 1 unit change in borrowers leads to profits to increase by 0.4743 units. Borrowers too has a positive correlation with deposits whereby a one unit change in borrowers impacts non significantly on deposits with a change of 0.1344 units.

Given the key findings above, if the performance of commercial banks is to be improved, then there is unequivocal need to direct efforts towards raising the number of depositors, improving customer care, customer recruitment and devising products that are attractive to customers. The study also recommends that monetary authorities should intervene by reducing on the interest rates that the central bank charges commercial banks. This will automatically be reciprocated by commercial banks charging less interest rate to their borrowers hence creating beneficial effects to increasing the number of borrowers. The use of open market operations is important in inducing savers to bring their deposits to banks.