DETERMINANTS OF COMMERCIAL BANKS' CREDIT TO THE PRIVATE SECTOR IN UGANDA (1997-2013)

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DECLARATION

I, Ssebatta James declare that this dissertation is my original work and has never been presented to any university or any institution of learning for any academic award.

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Dr. MARGARET BANGA

DEDICATION

To my dear wife, parents, brothers, sisters, course mates and friends. Thank you so much for all you have done and sacrificed for me.

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Abstract

This study investigated the determinants of commercial banks' credit to the private sector, highlighting its continued subdued growth and the impact of the monetary policy framework reform in July 2011. Private sector credit was used as the dependent variable, while real economic growth, credit to government, foreign liabilities and domestic deposits were identified as the major explanatory variables. Using the Engle and Granger (1987) two-step estimator technique and data covering the third quarter of 1997 to the last quarter of 2013, a robust long run relationship was found to exist between private sector credit and the exogenous variables.

The empirical results show that before the reform of the monetary policy framework, unit percentage increases in domestic deposits, foreign liabilities and real GDP contributed 0.15%, 0.89% and 0.19% significant growths in private sector credit in the long run. Credit to government posted a 0.39% significant decline in private sector credit. In the short run, credit to government posted a significant decline, while past and present stock of foreign liabilities and the past growth in real GDP posted significant positive effects on private sector credit. The results also indicate that a one percent increase in domestic deposits led to a 0.46% growth in private sector credit in the long run after the reform. In the short run, domestic and foreign financing coupled with stronger past growths in the economy led to higher private sector credit growth. A strong economic condition coupled with improved financial health and liquidity of banks play an important role in private sector credit growth, while the crowding out effect of credit to government is detrimental to bank credit growth in Uganda.

In conclusion, policies aimed at mobilizing savings through financial inclusion, attracting foreign inflows and limiting the level of government borrowing are recommended so as to achieve a viable level of private sector credit in Uganda.

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Abbreviations

ADF	Augmented Dickey Fuller
AIC	Akaike Information Criterion
BOU	Bank of Uganda
ECM	Error Correction Model
FDI	Foreign Direct Investment
GDP	Gross Domestic product
IMF	International Monetary Fund
MoFPED	Ministry of Finance, Planning and Economic Development
OLS	Ordinary Least Squares
PSI	Policy Support Instrument
RESET	Regression Equation Specification Error Test