

## **The Impact Of Minimum Capital Requirements On Performance Of Commercial Banks In Zimbabwe**

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**Abstract:** *The study was carried out to establish the impact of minimum capital requirements on the performance of commercial banks in Zimbabwe and to analyse the relationship between minimum capital requirements and bank performance. The study used the triangulation of a quantitative and qualitative research design where both primary and secondary data were used. The population under study was drawn from the entire commercial banking sector in Zimbabwe. Questionnaires and documentary analysis were used. The sample size of nine out of the fifteen commercial banks in Zimbabwe was used. Minimum capital requirement enable banks to make profits since meeting the minimum capital reduces the chances of bank distress as banks will not be pressured by short-term borrowing which is usually at high cost*

**Keywords:** *Minimum Required Capital, Bank Capital, Bank Performance, Capital Adequacy.*

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### **I. Introduction**

Capital acts as that cushion that will protect banks, its customers, and shareholders against possible losses from risks that banks are exposed to. The importance of capital requirements therefore is to limit risk taking by banks. Capital requirements play an important role in the supervision and regulation of commercial banks. Recent economies have revealed the importance of bank regulations to hedge against the high risk attributed to imbalances in banks' balance sheets. On the other hand, excessive regulations may increase the cost of intermediation and reduce profitability of the banking industry.

In Zimbabwe during the period, ranging from last quarter of 2003 and the first quarter of 2004 faced serious operational challenges and by the end of 2004, ten banks had been placed under curatorship whilst two were under liquidation. (RBZ Supplement, Jan 2006:2). In July 2008, the Reserve Bank of Zimbabwe (RBZ) prescribed minimum capital requirement of USD 12.5 million for commercial banks which were to be effective in August of the same year. These capital levels were to be in line with the standardised approaches of allocating capital for credit risk, market risk and operational risk in accordance with pillar 2 of the Basel II Framework. (RBZ MPS Jan 2009). Basel II framework is guided by three main pillars which are Pillar 1-Minimum capital requirements, Pillar 2 –Supervisory Review Process and Pillar 3 –Market Discipline.

The RBZ urged all commercial banks to ensure that their capital levels were adequate since those banks that would not be compliant by the effective date would be either forced to liquidate or merge with no option of curatorship. As a follow up to this, RBZ issued a "Minimum Equity Capital Implementation Plan" circular No.04-2009/ BSD to banking institutions. According to the circular, "Every banking Institution shall comply with 50 % of the prescribed minimum equity capital requirement for its class of banking business by 30 September 2009 and every banking institution shall comply with 100% of the prescribed minimum capital requirements for its banking business by 31 March 2010. Standard Minimum capital adequacy ratios prescribed in part 1 of the Third Schedule of the banking Regulations, S.I 2005 of 2000 shall apply on an ongoing basis and every banking institution whose paid-up capital does not comply with the respective prescribed level is required to submit a detailed recapitalization plan to the RBZ by 15 June 2009, for its consideration and approval indicating the amounts to be raised and time frames. Banking institutions without realistic potential to maintain adequate capital levels commensurate with their risk profiles on an on-going basis should seriously consider mergers and consolidations."

As at 30 June 2010, fifteen out of the fifteen registered commercial banks in Zimbabwe were in compliance with the minimum capital requirements. According to the July 2011 monetary policy, the number of Commercial banks had risen to seventeen and out of these three banks, namely ZABG, Kingdom, and Royal Bank were undercapitalised. Although these three banks were undercapitalised, they had presented their capital raising initiatives to the RBZ and were thus allowed to remain operational. This position remained the same by January 2012 and in July 2012 the number of Commercial banks had risen to eighteen all of which were adequately capitalised as per the expectation of the RBZ. However, the RBZ further increased the minimum capital levels of Commercial Banks from USD 12.5 million to USD 100 million in July 2012. (RBZ MPS, July 2012).

In stipulating the new capital level, the RBZ proposed a phased plan for enforcement of the minimum capital levels. The plan was for all banks to comply with 25 % of prescribed minimum equity capital by

31 December 2012, 50% by 30 January 2013, 75 % by 31 December 2013 and to have 100% of the prescribed minimum equity capital by June 2014. According to the Central Bank, the change in the capital levels had been necessitated by the dynamic nature of the financial landscape, regulatory requirements, increase in competition and economic uncertainties, which had placed an unprecedented pressure on banks to be adequately capitalized at all times ensuring that the banks' resilience to real and perceived exogenous and indigenous shocks.

### **1.1 Objectives of the study**

- To establish whether bank competitiveness is related to the level of capitalisation.
- To establish the impact of minimum capital requirements on the ability of banks to extend credit and contribute to economic growth
- To establish whether the minimum capital requirements really act as buffers for banks in times of financial distress and whether there is a link between the bank's capital and its profits

## **II. Literature Review**

### **2.1 Capital Requirement Concept**

N. Firzili (2012) defines capital requirements as the amount of capital a bank or other financial institutions have to hold as required by its financial regulator. This is in the context of fractional reserve banking and is usually expressed as a capital adequacy ratio of liquid assets that must be held compared to the amount of money that is lent out. M. E Tahyar (2010) comes up with two broad categories of capital which are regulatory and economic capital.

### **2.2 Basel Framework**

In 1988, members of the G-10 countries adopted the International Convergence of Capital Measurement and Standards which were established by the Basel Committee on Banking Supervision which became known as Basel I. Basel I mainly focused on providing capital for credit risk as lending was considered to be the main function of bank. With Basel I capital ratios are calculated through applying predetermined risk weights to a bank's credit exposure. The Bank's capital is therefore expected to be at least 8 % of risk adjusted assets with at least 4% constituting Tier 1 Capital. With the emergence of new financial instruments, sufficient methods of risk management and mitigation techniques were not readily available and this led to the exposure of banks to operational, market sovereign risk and other risks. To address the weaknesses of Basel 1, the Basel Committee published the final version of the International Convergence of Capital Measurements and Capital Standards which is now known as Basel II which focuses on three pillars.

#### **Pillar I-Minimum Capital Requirements**

This pillar enables banks to establish capital levels that are commensurate with its risks. Its main aim is to match regulatory capital set up by the regulator to economic capital as per the bank's internal business processes.

#### **Pillar II-Supervisory Framework**

The supervisory Review process defines the supervisory review of an institution's capital to support all the risks of the business and to encourage the development and use of better risk management techniques in monitoring and managing the risks

#### **Pillar III-Market Discipline**

Pillar III details the minimum levels of disclosures by banks when publishing accounts to promote transparency and accountability from bank management.

### **2.2.1 Constituents of Capital**

According to the Basel Committee working paper on Capital requirements and Bank performance (1991), the generic definitions of Capital tiers are as follows:

**Tier I Capital:** Commonly referred to as "core capital" or "basic equity"

Tier I capital is considered as the most stable and reliable source of funding for the operations of a bank and usually it constitutes 50 % of a bank's capital and there is no limit as to what it should constitute. Tier I capital includes Equity Capital, disclosed Reserves.

**Tier II Capital:** Also called “supplementary capital.”

It constitutes undisclosed reserves, revaluation reserves, hybrid capital instruments such as perpetual preference shares and subordinated term debt. Tier II capital cannot exceed Tier I capital but is limited to 100% of Tier I capital.

**Tier III Capital:**

Tier III capital is mainly to cover the market risks and may be used only at discretion of the national authorities and it includes only short term subordinated debt that is unsecured, subordinated and fully paid. The debt should also have a maturity of at least 2 years and should be subject to a lock-in clause that stipulates that the debt should not be paid if it makes the bank go below its minimum capital requirement. Tier III capital can only be used in respect of market risk and is limited to 250% of a bank's Tier I Capital. (Basel Committee, 1999)

### **2.3 Measures of performance of a commercial Bank**

Oyetan (1997) argues that indicators or measures of a bank's financial condition and performance can be based on the CAMELS rating system. It was originally adopted by the regulators of North American Commercial Banks. CAMELS rating system CAMELS is an abbreviation for components of bank safety and soundness namely: Capital Adequacy, Asset quality, Management quality, Earnings ability and Liquidity and System and sensibility.

#### **2.3.1 Capital Adequacy**

This refers to the minimum expected balance of capital in relation to the risk exposure of the bank. Akintoye and Somoye (2008) state that capital adequacy is necessary to inspire and sustain confidence in the banks, keep it open and operating so that time and earnings can absorb losses without being forced into costly liquidation and enable banking industry to take full advantage of its profitable growth. Karlyn (1984) explains capital adequacy in terms of the analysis of the bank's capital-deposit ratio since the primary risk is depository risk which is can be caused by a run on deposits.

#### **2.3.2 Asset Quality**

The quality of assets is mainly assessed on the basis of its ability to recover the outstanding loan advances made in due, as well as the diversification and quality of the loan investment policies, procedures and practices. Frost (2004) highlights that the nonperforming loans can be used to highlight the asset quality and the bank's provision to losses reserve. Hence the adequacy of the allowance for loans and proportion of categorized loans to the total loan book can be used to determine the quality of a bank's assets.

#### **2.3.3 Management Quality**

Management quality considers such issues as the establishment of management positions, technical skills, managerial, independence, flexibility and efficiency in making decisions. It also involves the capability of the board to identify measure and control the risks associated with the operations of the organization in line with its regulatory expectations (Dang 2011). Grier (2007) suggests that management should be considered as the most important CAMELS element since issues such as the timeliness and accuracy of management information systems (MIS), succession planning, reasonableness of compensation and self dealing policies of management are also considered.

#### **2.3.4 Earnings ability**

This is usually assessed using quantity and trend in earnings using various accounting ratios. Apart from the ratios, other external factors that are likely to affect the growth and sustainability of the earnings are considered. Grier (2007) suggests that a consistent trend in earnings builds public confidence, absorbs losses and provides an impressive return for shareholders. The quality and source of earning is also considered.

#### **2.3.5 Liquidity**

Dang (2011) citing Rudolf (2009) emphasizes that liquidity refers to the ability of a bank to meet its short term obligations. Banks should therefore ensure that there are adequate sources of current and future liquidity needs through holding assets that can be easily liquidated without incurring losses. The Uniform Financial Rating System (1997) also suggests that “the fund management practices should ensure an institution maintains a liquidity level sufficient to meet its financial obligations in a timely manner and be capable promptly liquidate assets with minimal losses”.

### **2.3.6 Sensitivity to market risk**

This considers the sensitivity of earnings or economic value to undesirable changes in foreign exchange rates, interest rates, commodity prices and equity prices. It also assesses the ability of the management of a company to identify, measure, and control exposure to market risk in relation to the size and risk aversion and or risk profile of the company.

Dey and Kabir (2012) argue that CAMELS rating has become one of the major tools used worldwide tool used in respect to examining the strength and performance of financial institutions. As evidence to its usefulness, in the 2008 financial crisis, the CAMELS rating was being used by the American government to respond to the crisis through the identification of banks that needed the special help which was other than capitalization as authorized by the Emergency Economic Stabilization Act of 2008. On the contrary however, Gaytna and Johnson (2002) argue that this model is only parallel with the performance of the bank at the time when the examination was conducted whilst in reality, bank variables are highly volatile to market forces and this is not clearly shown by CAMELS.

### **2.4 Capital Adequacy and Bank Performance**

Whitehead (1997) argues that adequately capitalised banking institutions are able to undertake greater business expansion and allocate resources in order to develop capacity to compete more effectively in a more liberalised environment among internationally active banks thereby prompting them to be improving technologically as well as come up with innovative financial products ideas to remain competitive.

Aderinokun (2004) maintains that an increase in the capital base of banks improve performance as it enables them to expand the scope of their activities within the industry, reduce risk, ensure quality asset management as well as puts banks in a strong liquidity position. Whitehead (2005) also argues that if adequately capitalised, banks will be more competitive as they will have more products on offer both local and offshore thereby having a wider network cover, price products competitively, ability to finance a large number of diverse transactions across sectors. Adequately capitalised banks will also be able to offer longer loan repayment periods and have more efficient systems as compared to other banks resulting from upgraded information technology systems

According to a research on Financial Markets and Policy by the Kenya Centre for Research, capital adequacy can be used as a tool to limit excessive risk taking by shareholders who have limited liability thereby promoting sharing of risk between the owners and the depositors thereby reducing risks of bank collapse. It can also act as a buffer against financial costs of financial distress thereby reducing the probability of bank insolvency. It is also argued that banks with higher capital levels have the capacity to provide services to corporates and households in times of financial distress thereby having the capacity to perform their lending functions effectively.

However, in contrast, some scholars have argued that capital requirements are actually cost to banks. Kenya Centre for Research on Financial Markets citing Argoraki et al, 2011 and Tieman, 2004) suggest that imposing higher capital requirement constrain banks' competitive pressure due to competition on loans, deposits as well as sources of debt and equity investment. Other researchers also argue that banks might therefore lend less, pay little on deposits in an effort to maintain the required high capital base thereby constraining the operations of the banks. Moreover in highly concentrated markets, financial institutions with adequate capital may believe they are "too-big-to-fail" and this might lead to riskier investments (Berger et al, 2008) which might in turn lead to bank failures.

### **2.5 The effect of capital requirement on economic output and extension of credit.**

Banks stand as the main player of the financial system as they play multi roles towards economic development. Basel II Framework (1999) concurs that banks play multiple roles, which are highly important and beneficial for the economy as a whole and therefore need to be regulated. Critical among their roles are the following functions: they provide payment services, they intermediate capital by providing a range of savings instruments, enable the transfer of savings from surplus units in the form of deposits to deficit units in various forms of credit to borrowers and they also handle and transform risks.

Adequately capitalised banks are in a position to meet their respective country's funding requirements thereby contributing towards the country's economic growth. Whitehead (1997) views the reason why banks should be adequately capitalised in the context of the economy as that minimum capital requirements are put in place to ensure banking institutions have sufficient capacity to undertake the intermediation function necessary for the development of the economy. Moody (2012) also agrees to the aforesaid but points out that capital requirements will progressively and significantly increase and the cost of capital should be closely monitored.

According to Chikoko and Le Roux (2013), the minimum capital can have implications on the lending capacity of banks. Firstly, it may result in reduced lending in certain sectors of the economy and secondly, it might affect the cyclical behavior of bank lending thereby resulting in overall impact on the availability of credit

in the economy which might in turn result in credit crunch. This is mainly due to the fact that if a bank's capital adequacy is reduced it might raise more capital, cut back on its lending and or shift its asset portfolio towards low-risk assets which might be through reduced lending thereby resulting in low liquidity levels in the economy.

Soludo (2004) discovered that low capitalisation of the banks has made them less able to finance the economy and more prone to unethical and unprofessional practices. Aminu and Kola (2004) maintained that increasing the capital base of banks in Nigeria would strengthen them and, in the process, deepen activities within the industry. "Growing the Nigerian economy is about the number of banks that have the capacity to operate in all the states of the federation, fund agriculture and manufacturing concerns, and in the process generate employment for Nigerians." (Ologbondiya and Aminu, 2005).

## **2.6 Capital requirements and new entrants**

The main aim of the Basel accord was to create an even playing field for all banks that participate actively in the financial Markets. The increase in the minimum capital requirements will pose some challenges to both the economy as well as the banking system as concluded by Balogun (2005) in Nigeria. D. Diamon and P. Dybring (1986) stated that regulatory policy motivated only by macro-economic goals may destroy banks by preventing them from providing the services that are major to banks.

## **2.8 Bank Capitalisation and profitability**

The basic desire of a bank's management is to make profit, as the essential requirement for conducting any business. (Babakova, 2003). Berger (1995) carried out a study on the relationship between the return on equity and the capital asset ratio for a number of banks in the United States for the period from 1983 to 1992 and his study showed that return on equity and capital asset ratio tend to be positively related. Abreu and Mendes (2002) also carried out an investigation on the determinants of bank interest margin and profitability for some countries in Europe. The results of their study indicated that adequately capitalized banks had lower funding costs and probability of bankruptcy which then translated into them having higher profit levels. Nacuer (2003) explains that a higher equity-to-asset ratio results in a lower need for external funding which in turn increases bank profits.

Insufficient capital requirements might result in investors and depositors being cautious by refraining from dealing with the banks which will therefore have an adverse effect on the overall profitability of the bank. Most researches by various scholars point to the notion that an increase in bank capital results in an increase in banks overall returns. This positive correlation between capital and profitability has also been concurred to by Furlong and Keeley (1989), Keeley and Furlong (1990), Berger (1994) and Kwan and Eisenbeis (2005) who all assert that increase in minimum capital requirements reduce the risk of bank distress which will then result in increased profitability.

A study carried out in India indicated that banks with higher capital requirements have the ability to absorb unexpected losses easily and have reduced cost of capital which means their profit levels are usually high. Evidence from studies carried out on United States Banks state that apart from regulatory pressures, a bank's capital level may depend on their business plan. A bank that intends to take over another bank might be adequately capitalized to impress regulator without necessarily being profitable (Berge et al.).

## **2.9 Buffer capital adequacy**

Buffer Capital refers to the ratio of excess capital over risk weighted assets. A bank's buffer capital can also be described as the bank's non-regulatory internal capital that fluctuates over time as a reflection of the bank's reaction to market pressures in line with risk assessment in the assets including loans and securities portfolio. The buffer theory of Calem and Rob (1986) state that a bank whose capital close to the regulatory minimum capital ratio may have an incentive to boost capital and reduce risk in order to evade regulatory costs triggered by breach of capital requirements. Some scholars also argue that a bank's excess capital acts as insurance against costs that may occur due to losses on loans or due to random shocks and the insurance premium is usually equal to the return on equity or interest rate on subordinated debt that the bank pays in order to attract new capital.

# **III. Research Methodology**

## **3.1 Research Design**

In this study the descriptive research design was used as it allowed the use of both qualitative and quantitative information. This type of design was used since a relatively large sample size could be handled at one time and this somewhat made it easy to conclude the views of the whole population. The standardized format made it easy for the researcher to administer and record questions and answers. It was effective and convenient to administer from remote locations using mail, email and telephone.

### **3.2 Population**

Data is collected from the elements of the target population. The target population of the study was comprised of nine out of the fifteen commercial banks in Zimbabwe.

### **3.3 Sample**

The sample used for this research was nine out of the fifteen commercial banks in Zimbabwe.

### **3.4 Sampling procedure**

The researcher used stratified random sampling method in the formation of a representative sample for this research. With this method, the banks were divided into three main strata in accordance with their capital levels. The banks were ranked in relation to the amount of capital they hold from the one with least to the one with the largest amount of capital. These ranked banks were then divided into three groups coming up with the three strata namely high, low and medium. From these three strata, a sample of three banks per strata was picked randomly. The researcher used the random stratified sampling procedure as this saves time and money. It is also easy to apply and considering the nature of the research this method of sampling provided an effective sample that would clearly bring out a fair representation of the entire population. The sample size of nine out of fifteen translates to sixty percent (60%) of the entire population which is deemed representative.

### **3.5 Research Instruments**

For purposes of this research the researcher used the triangulation method. The researcher used questionnaires as well as documents and public researches as methods of collecting data. Different sources of data provide verification and validity of the data whilst complimenting the same data. The different sources will give different insights into the topic which will enable cross verification of the same data and it provides more comprehensive data which presents reliable and more valid findings. The research instruments used in the data collection were questionnaires and documentary analysis.

#### **3.5.1 Questionnaires**

Questionnaires were used by the researcher to collect data from subjects for the research analysis. The researcher used self administered questionnaires to collect data from employees of the banks which were part of the sample. Standardized questions and response format of the questionnaires ensured that every response was identical thereby facilitating easy data presentation, analysis and discussion of findings. The questionnaires were made up of both open ended and close ended questions to enable the maximum extraction of all the necessary data from the respondents. The researcher used questionnaires since they are cheap and enables standardisation of responses.

#### **3.6.2 Documentary analysis**

In conducting the research, the researcher used documental analysis because it enables access to information which would be difficult to get in other way for example ratios on the performance of banks over time. Such information will not be readily available if other instruments are used. Documents provide useful information that can be used to track change over time and relatively low costs as the documents are readily available. There is elimination of the researcher effect which might be present if the researcher is to interact with the respondents

## **IV. Data Presentation, Analysis And Interpretation**

### **4.1 Response rate**

In carrying out this research, 10 questionnaires were administered to each of the nine banks making a total of 90 questionnaires. Of these, 80 were received at the date of consolidation implying a response rate of 89% which is deemed sufficient and representative of the total population. The majority of non respondents were executives who mainly gave procrastination as the main reason and unavailability of time due to their busy schedules.

### **4.2 Gender and Age distribution of respondents**

50 % of the respondents were aged between 26-35 years, 35% between 36-45years, 10% constituted those whose age is 55 and above whilst 5% lied between 46 -55years.

### **4.3 Banking Sector in Zimbabwe can be described as stable**

5 % of the respondents to this question strongly agreed that the sector is stable, 35 % agreed, 20 % were uncertain whilst 30% and 10% disagreed and strongly disagreed respectively. These results can be further presented as that only 40% of the respondents believe the sector is stable against 40 % who strongly disagree with the remaining 20% being uncertain of whether it is stable or not. These results can be the possible

explanation to the liquidity challenges that are experienced in the market which can also be taken to mean that the confidence in the banking sector from the participants themselves (the bankers) is still quite low.

#### **4.4 Banks and their own desired levels of capital**

With reference to whether banks should be allowed to have their own desired capital levels, the responses indicate that there is no general consensus on whether banks should stipulate their own capital requirements. The results also indicate that the least percentage of respondents strongly agree that banks should be given their own mandate to determine their own capital levels. This could be viewed in support of the Basel II Framework's Pillar II which states banks should establish its own capital levels that are commensurate with its risk profile and internal business processes.

#### **4.5 Central Banks and the imposition of Minimum capital requirements**

85 % of the respondents agreed that the central bank should impose capital requirements on banks contrary to the 10% that strongly disagrees. 5 percent neither agreed nor disagreed. These results can be attributed to the fact that banks play an important role in the economy therefore it is necessary for the Central bank to impose minimum capital requirement so as to maintain stability in the sector. Linds (2005) and Oladejo and Oladipupo (2011) states that the special nature of banks makes it important for the Central Bank to set minimum their capital levels so as to promote the development of common, integrated management policies within banks or across banks and nation which also limits systematic risk.

#### **4.6 Minimum capital requirements strengthen bank performance**

25 % of the respondents strongly agree that if a bank meets its minimum capital requirements, its performance will be enhanced. The results also show that 60% percent of the respondents also agree to this whilst the remaining 15% split amongst uncertainty, disagreeing and strongly disagreeing with the fact that minimum capital requirements strengthen bank performance. The majorities of the respondents' opinions move in tandem with the assertions of Whitehead (2004) who maintains that an adequately capitalised bank will be able to offer longer term loans and will also have efficient systems as compared to other banks which will definitely strengthen the bank performance.

#### **4.7 Relationship between Capitalisation and competitiveness**

56 out of the total 80 are in agreement with the existence of a positive relationship and this constitutes 70% of the total respondents. The remaining 30% can be taken to have disagreed with the existence of a positive relationship between capitalisation and competitiveness. Whitehead (2005) argues that proposes that capitalisation and competitiveness have a positive relationship because an adequately capitalised bank will be more competitive as it has the ability to offer more products both locally and internationally resulting in wider market coverage which means improved competitiveness. Anyanwaokarao (1996) agrees that adequate capitalisation will enable the bank execute fully its mandates thereby increase public confidence.

#### **4.8 Bank's capital level determines its profitability**

50% of the respondents denied that a bank's capital level determines its profitability and 30% agree either strongly or just agreeing. 20% were uncertain of relationship between these variables. 50% seem to confirm the arguments by Hughes and Mester (1997) that higher capital levels synchronize with high variable cost which will then reduce the profitability of the bank. However, Furlong and Keely (1989) state that adequate capitalization reduce the risk of bank distress which in turn determines the profitability of the bank, this could be the possible explanation as to why some respondents agreed that capital level determines profitability. Pringle (1971) observed that undercapitalised banks are usually characterized by high levels of short-term borrowings at excessively high costs which will in turn reduce their profits.

#### **4.9 The minimum capital levels set for Zimbabwean banks are too high and unattainable**

65 % of respondents agreed that the imposed capital levels were too high whilst 20% felt the levels were not too high. 10 % strongly agreed whilst 5% remained uncertain. These results could be taken to indicate that the respondents do not fall into a general consensus as their results are almost spread across. What this means is that the determination of "adequate and attainable" capital is a debatable issue that may not easily bring a foregone conclusion.

#### **4.10 Banks that do not meet the minimum capital requirements should be closed**

20 % felt that all those banks that did not meet the required capital requirements should be closed, 12.5 % were uncertain whilst 55 % disagreed with a further 12.5 % strongly disagreeing. This is probably due to the contagion effect that closed banks might cause in the entire sector. Those disagreeing support Hazlina et al

(2011) who proposed the bank consolidation programme in Malaysia which resulted in larger banks with higher capital levels, greater technical and improved scale efficiency. This ensures that banks become more resilient to shocks and enable them to reposition their operations so as to survive in the globalized banking system. The formation of the Zimbabwe Allied Banking Group (ZABG) in 2005 can also be used to support the responses that the banks should not be closed. The ideal solution will be to put such banks under curatorship whilst they are working on their strategies to raise the required capital.

#### **4.11 Increase in capital constraints credit extension of banks**

80% agreed whilst 20% disagreed to the above sentiment. The respondents' views alluded to Chikoko and Le Roux (2013) who state that minimum capital requirements have an impact on the lending capacity of banks in response to meet the regulatory capital. Increase in capital might reduce lending by banks in certain sectors of the economy and might affect the cyclical behavior of bank lending thereby resulting in overall reduction of credit availability in the economy which might in turn result in a credit crunch.

#### **4.12 Meeting required capital eliminates bank failures**

33% agreed that meeting capital requirements would completely eliminate bank failures whilst 67% disagreed. Meeting minimum capital requirements does not guarantee elimination of the risk of bank failure as was witnessed in Zimbabwe during the 2004-2005 banking crisis. Other schools of thought also argue that there are likely to be many other factors such as liquidity challenges, nonperforming loans and fraud among others that may cause bank failure apart from capital. Meeting the adequate capital may actual cause banks to fail as a result of the "too-big-to-fail" syndrome that banks might have. An example to note is the collapse of the Lehman Brothers in 2008 which was the fourth largest bank in the United States at the time of its collapse.

### **V. Findings, Recommendations And Conclusions**

#### **5.1 Findings**

From the research findings, it can be concluded that capital requirements enable banks to make profits through cheap funding. If a bank has adequate capital this reduces the chances of distress as the bank will not be pressured by short-term borrowing which is usually cost. Capital acts as a buffer for absorbing shocks that might occur in the market due to risks such as credit risk, counterparty and default risk. If a bank has capital, the impact of these risk will be reduced and this will have minimum impact on the income of the bank. Capital ensures the reduction of the need for external funding by a bank and this will enable the bank to efficiently utilize its assets in generating more income which will eventually translate to profit. If a bank is adequately capitalized, it will attract more investors and depositors and an increase in these will eventually contribute to profit as the bank will have a source of funding.

There is a positive relationship between a bank's capital, its competitiveness as well as strength and the overall performance of the bank. The research findings indicate that a bank which is adequately capitalized will be more competitive as it has the ability to offer more products than its peers and this will result in a larger market share. As the market share increases, so does the strength of the bank as it would have convinced the market of its capabilities thereby maintain competitiveness. The capital threshold completely eliminates the probability of new entrance coming. There should be no blanket application of the minimum capital requirement but that banks should be allowed to have minimum capitals that commensurate with the risks they are associated with.

#### **5.2 Recommendations**

There is need for ensuring that the Central Bank has more interactive supervision of commercial banks than the current system where there is more of the RBZ relying on the information supplied by the banks. A more interactive approach will reduce the market risk as with the current one, banks might manipulate records and still convince the regulator that they are adequately capitalised whilst in actual fact they are not. There is need to have a centralized system where the banks will make a certain deposit with the central bank in line with meeting the capital requirements as the current system has loopholes where management can manipulate figures so as to meet the requirements yet in actual fact they are not adequately capitalised. The researcher recommends that further studies be carried out on the analysis of the effectiveness of using the CAMELS rating as a supervisory tool for central banks.

#### **5.3 Conclusion**

Available literature was explored to give the researcher an understanding on the background of the problem, root cause of the problem, effects and possible remedies of the problem identified in chapter one as 'the impact of minimum capital requirements on the performance of commercial banks. The researcher made use of primary and secondary data, qualitative and quantitative methods of data collection in order to gain an



understanding on the effects of bank failures on depositors. The findings of the research presented and analysed the major findings were the positive impact of capital requirements on the performance of commercial banks. The research established that if a bank is adequately capitalised, it will be highly competitive and faces low risk of bankruptcy.

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