

THE EFFECT OF EXCHANGE RATE FLUCTUATIONS ON BANK PROFITABILITY IN ZIMBABWE

Table 1: Regression results

Variable	Coefficient	Std. Error	t-statistic	P-value
Bank size	-0.080072	0.037576	-2.130961	0.0370
Deposit to total assets	-0.264201	0.057680	-4.580455	0.0000
Economic growth	0.009599	0.005746	1.670621	0.0998
Exchange rate	-0.004373	0.001969	-2.221230	0.0299
Inflation	-0.000867	0.000344	-2.520655	0.0143
Loan to deposit	0.034001	0.010836	3.137866	0.0026
Constant	0.149839	0.041298	3.628263	0.0006

R-squared 0.507646

Source: secondary data

Adjusted R-squared 0.460755

F-statistic 10.82610

P Value (F-statistic) 0.000000

The above results lead to the specification of the regression model as:

$$ROA = 0.149839 - 0.080072BZ - 0.264201DTA + 0.009599EG - 0.004373EXC - 0.000867INF + 0.034001LTD$$

4.3.2 Interpretation of results

The above specified equation explains the profitability of banks using banks specific variables, macro-economic and exchange rates were of paramount importance in this research. Regression model stipulates that holding exchange rates, bank specific factors and macro-economic factors to zero return on assets or profitability of the bank will be 0.149839. The model R-squared was 0.507646 which concludes that the model explains 50.76% of the dependant variable bank profitability. According to Wooldridge (2012) F statistic value is a tool to test the hypothesis that all coefficient parameters are equal to zero. This means that F statistic value is the universal indicator of the model significance. Gujarati (2004) affirms the same postulating that regression coefficients are simultaneously zero. The economic principle about F statistic is that it must be greater than 5 for the whole model to be considered significant in explaining the regressand. The research F statistic value is 10.83 which portray the significance of the model in explaining banks profitability and the hypothesis that coefficients are all equal to zero is rejected.

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Exchange rates

The results established that there is a significant negative relationship between exchange rates and banks profitability. Exchange rates are statistically significant in explaining ROA (profitability), this is proved by the p-value (0.0299) which is less than 0.05 and t-statistic value of (-2.221230) which according to Gujarati (2003) depicts a statistically significant variable because the modulus of -2.221230 is greater than 2.000 the econometrically acceptable t-statistic to conclude the significance of the variable. Exchange rates have a negative statistically significant effect to banks 'profitability meaning that a single percentage change in exchange rates will lead to - 0.004373 fall in banks return on asset. The results concur with Combey and Togbenou (2017) findings that exchange rates have a negative relationship and significantly affects banks profitability which concludes the rejection of null hypothesis that exchange rates do not affect banks profitability. However, Kiganda (2014) exchange rates effect on banks profitability was one his research objective but he differs postulating that exchange rates insignificantly affects banks profitability but agreed on the existence of a negative relationship between the two.

Banks specific factors

The second objective of the research was to determine whether banks specific factors such as bank size and liquidity affects banks profitability. Two liquidity ratios deposit to total assets ratio, the loan to total deposits ratio and bank size in relation to overall market capitalization was used as banks specific variables. The results showed that there is a statistically significant strong inverse relationship between banks profitability and bank size. The notion is evidenced by the p-value which is less than 0.05 and t-statistic which also is above econometrically acceptable. According to the model, a single increase in bank size will lead to -0.080072 decline, ceteris paribus. This is in accord with Madhi (2017) that the bigger the banks exhibits low profits because they are protected by the government and hence there will be moral hazards knowing that any sign of bank run will be financed by the mother bank. Gumbo et al (2020) concluded that the bigger the bank is, the more it suffers liquidity challenges and that shows the decline in profits as the bank will not be able to issue new loans or settle obligations without incurring undesirable costs which reduces the profitability of the bank. However, Moussa (2022) postulated that there is a positive relationship between bank size and profitability but was in corroboration on the significances of banks size explaining banks ROA.

Deposit to asset ratio, DTA which explains the liquidity position of the bank. Banks main function is to create loan term loans from short-term savings therefore, higher deposits entails increase in banks production which is a function of banks profitability. Research findings depicts a strong negative relationship between deposits to asset ratio to banks profitability as portrayed by p-

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value of 0.0000, t statistic of -4.580455 and coefficient of -0.264201. This expresses that on a single change of DTA ceteris paribus, banks ROA will fall by -0.2642. However, the research outcome is contrary to other research findings in the literature. According to Kana (2017) higher DTA transforms to increase in banks profitability in the case of South African banks. Combey and Toybenou (2017) after carrying out research on the performance of banking sector consorted with Kana (2017) in that increase in deposits directly increase banks profitability but they were in corroboration with research on the significance of DTA in explaining banks profitability. The results concurred with Logat (2016) research conducted in Latin America, the conclusion was that DTA is negatively related to return on assets and statistically significant. The research findings are also justified in that South African economy is different to Zimbabwe. Zimbabwean bank's deposits are mainly short-term that is why the central bank (according 2021 and 2022 Monetary policy) is constantly increasing statutory reserve and interest of demand deposits and time deposits to encourage savings and induce long term deposits or liabilities and finally long term loans. Fugacious deposits cannot be used to issue out long-term or even short-term without exposing the bank to liquidity risk therefore, the higher deposits of this type will definitely transpose to decrease on ROA of banks.

Lastly, there is loans to deposits ratio, which depicts the percentage of deposits tied up in loans. The results communicated that there is significant positive relationship between LTD and ROA because the p-value is 0.0026 which is less than the econometric principle and its t-statistic value is also greater than 2 and 0.034001 is the coefficient meaning that for a single increase in LTD it will lead to 0.034 increase in banks ROA. However, this should not be the case because according Gumbo et al (2020) the higher ratio depicts exposure of the bank to liquidity challenges. Alexiou and Sofokis (2009) corresponds arguing that the liquidity is significantly negative related to banks profitability because the higher the ratio depicts illiquid of the bank. The results may be caused by the income hungry of the banks and the real values of deposits has been eroded by weakening ZWL and hence the bank's profitability increase because the cost of funds were dampened by inflation the past years.

Macro-economic factors

The last objective of the research was to investigate the effect of other macroeconomic variables of which in this research and economic growth and inflation was used to represents macroeconomic variables. The findings proved that economic growth insignificantly affects banks profitability positively because its p value of 0.0998 which greater than 0.05 and alternatively its t-statistic value of 1.670621 which less than 2 the acceptable criterion. The results are in tandem with Sufian and Kamarudin (2012) findings on that as the economy grows economic agents rate of loan defaulting will

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be low and companies will be borrowing causing the profitability of the banks to increase and hence the positive relationship. Petria, Capraru and Ichnatov (2013) concluded the same positing that in the period of economic growth investors' confidence mount up thereby creating a favourable environment to advance loans and deposits which either way one take it, affects banks profitability positively. Shuremo (2016) differs with the research findings that economic is statistically insignificantly in explaining banks profitability after research on Ethiopia's commercial banks. In Zimbabwe, economic agents even if economy grows, they will choose to bank under mattress because of low trust in the local banks which is attributed to dynamic policies of the RBZ narrowly on exchange rates determination.

Inflation from the research was concluded to have a strong negative relationship with banks profitability. The p value of 0.0143 and -2.520655 t statistic value are images of significance of inflation on ROA with the coefficient of -0.000867. Portraying that for every single increase in inflation rate will lead to 0.000867 change on banks ROA, ceteris paribus. The results consisted with Sufian and Kamarudin (2012) findings in Bangladesh who concluded that there is an inverse relationship between inflation and ROA.

VI. RECOMMENDATION

After a thorough research on the effects of exchange rates fluctuations on banks profitability, the researcher proposes the following recommendations to the stakeholder of this study. The study recommends the need to manage the currency crisis in the country urgently as the fluctuations has a negative impact on bank profitability. Financial institutions should hedge against foreign exchange rate risk as poor management has potential of causing bank distress. The central bank should continue to devise strategies that can improve bank liquidity and exchange rates in the country. Banks are recommended to employ robust liquidity management techniques and good corporate governance because diseconomies of the scale were found to exist.

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