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INFLUENCE OF BANK STABILITY ON THE FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN SOUTH SUDAN

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Abstract

Purpose: The purpose of the study was to examine the influence of bank stability on the financial performance of commercial banks in South Sudan

Methodology: The study was guided by the CAMEL model metrics in measuring stability and its influence on the financial performance of commercial banks measured by ROA and ROE. The study was primarily grounded on the CAMEL model. The study further adopted the positivism philosophy which guided the research. The research employed a descriptive research design. The population for the study was 24 commercial banks in south Sudan from which the research targeted one senior manager. The research relied on a mixed methodology which encompassed both quantitative and qualitative data. Secondary data was collected for the period 2012-2017 from audited annual financial reports of individual banks and from the Central Bank of South Sudan reports while primary data was collected by use of a semi-structured questionnaire. The collected data into SPSS 23 for subsequent descriptive and inferential statistical analysis.

Results: The correlation tests indicated a strong positive effect of asset quality on the financial performance of commercial banks (r=0 .784); a strong positive effect of management efficiency (r= 0.758) and liquidity (r=0 .620).

Unique contribution to theory, practice and policy: The study recommends that at the bare minimum the management of commercial banks should benchmark with industry experts on how to enhance their services and product offering to better their asset quality scores. Further the study recommends that banking institutions that have shied away from lending activities should reconsider the potential benefits that may accrue from undertaking lending activities. The study therefore recommends that banks should be encouraged to look beyond local market and strategically expand their operations to other geographical markets and sectors of the economy. Location of bank branches is strategically paramount if banks must maximize return on investment.

Keywords: *bank stability, financial performance*

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1.0 INTRODUCTION

1.1 Background of the Study

The financial system is a nerve center of economic development. It provides the important service of financial inter-mediation that largely entails enabling surplus spending units to save and deficit spending units to raise fund for investment and consumption (Athanasoglou, Brissimis, & Delis, 2008). The commercial banking sector plays a key intermediation role in the financial sector of any country. Over the last two decades the commercial banking sector in the world has undergone tremendous structural changes in terms of operations, structures and the general performance of the industry (Ongore & Kusa, 2013).

The main aim of commercial banks is to register better performance through sustained profitability and growth (Pearce & Robinson, 2011). However, attempts to realize such successes, are often affected by multiple operating market conditions such as the level of competition, stakeholders management, political landscape, business legal regime, the cost of doing business, new innovative products, internal organizational structure, emerging technologies, and effects of globalization (Kotler & Armstrong, 2013).

According to Hilscher and Raviv (2014) bank stability fosters market discipline within the economy of a country which is key in enhancing the foreign investor confidence level which is essential in enhancing investments and spur economic growth. In another review of transition economies, (Fang, Hasan, & Marton, 2014); indicate that the stability of banks has spurred institutional development which are integral to economic growth. Lamers, Mergaerts, Meuleman, and Vander Vennet (2016) examined the tradeoff between monetary policy and bank stability and indicated that bank stability helps reduce systemic risk within banks which helps in operationalization of accommodative monetary policies.

Bank stability can be measured by use of standalone indicators or by use of composite indicators. One measure of bank soundness according to the BASELS Accord is by using the CAMEL framework (Beck *et al*., 2009). Another measure of bank stability is the use of a banking stability index as developed by Ghosh (2010) which was based on several important aspects of banking operations and thereafter examining which sets of factors are influential in impacting the index.

Financial performance in banking industry has been of interest to academic research and to stakeholders in the banking industry. This is due to the fact that financial performance has a critical implication for economic growth in any country and its generally considered to be the reflector of financial and economic conditions of a country other than its intermediation role in an economy (Gatuhi, 2015; Ongore & Kusa, 2013). Financial performance is also important due to competitiveness in the world economy not only to stakeholders of a firm but also to firms within the same industry (Yalcin, Bayrakdaroglu & Kahraman, 2012). The study measured financial performance using ROA and ROE.

According to Central Bank of South Sudan (2016) there are 29 registered commercial banks operating in the country, 11 national banks 11 joint ventures, and 7 foreign-owned banks. The central bank also regulates 8 micro finance institutions and 84 forex bureaus. Statistics from the Bank of South Sudan on the financial soundness indicators for the Banking sector in the country as contained in the IMF (2017) reports indicates that Asset quality measure in terms of non-performing loans against total loans increased from 18.7% in March 2014 to a high of 54.9% in September 2016. Liquidity expressed in terms of liquid assets to total assets decreased from 78.7%

in March 2014 to a low of 46.7% in September 2016. Overall the statistics portray a negative image of the banking sector performance in South Sudan.

1.2 Statement of the Problem

Despite emerging evidence that stable banking institutions are essential to promoting institutional performance and economic growth; the IMF (2017) report indicates that commercial banks in South Sudan are faced by a myriad of internal challenges as well as macroeconomic constraints that have limited the development within the sector and as a results the report concluded that banks are failing as indicated by the financial soundness indicators utilized by the Central Bank of South Sudan. According to Bank of South Sudan, (2013) report on the South Sudan Financial sector the shift from Islamic to Conventional Banking after the independence of South Sudan in 2011 led to imbalances in the structuring of a new financial system. Garang (2014) also indicates that there has been limited growth in the South Sudan banking sector; further he stated lack of financial inclusivity and institutional structuring to be the cause of limited development and performance of the sector.

Available literature, Ongore & Kusa, 2013; Chechet & Olayiwola, 2014; Naceur & Omran,(2010); have indicated that there are both firm-specific and marekt specific factors that influence the performance of commercial banks. Despite all these efforts exerted to determine factors that influence banks performance, no study captured the influence of bank stability on commercial banks financial performance utilizing CAMEL model and moderating ownership especially in the context of South Sudan. Furthermore there is need to evaluate the effectiveness of the CAMEL model with the growing adoption of other metrics such as ROA, ROE or EAGLES model within the banking sector.

1.3 Objectives of the Study

i. To examine the influence of asset quality on the financial performance of commercial banks in South Sudan.
ii. To establish the influence of management efficiency on the financial performance of commercial banks in South Sudan
iii. To establish the influence of liquidity on the financial performance of commercial banks in South Sudan.

2.0 LITERATURE REVIEW

2.1 CAMEL Model

The CAMEL model was developed by US Federal regulators to help structure the bank examination process in the year 1979. CAMEL is, basically, a ratio based model commonly used for the evaluation of performance and ranking. In the 1980s, the US supervisory authorities, through the use of the CAMEL rating system, were the first to introduce ratings for on-site examinations of banking institutions (Hansda, 1995). The concept introduced a uniform system of rating a banking institution in the United States. CAMEL is an acronym for the five components of bank safety and soundness such as capital adequacy, asset quality, management efficiency, earning quality, and liquidity.

Even though there are many aspects of performance measurements' of commercial banks that can be analyzed, CAMEL framework is the most widely used model to evaluate performances of commercial banks due to its widely acceptance in the world and other advantages it possess. The model is advantageous due to its ability in early signaling of potential danger, further the CAMEL has the ability to improve their overall performance of banks by creating a sense of competition among each other (Bodla & Verma, 2008).

2.2 Empirical review

Kadioglu, Telceken and Ocal (2017) undertook a study on the effect of the Asset Quality on the Bank Profitability. The study sought to examine whether nonperforming loans affected the profitability of commercial banks in Turkey. The study applied panel regression method to the quarterly data of 55 Banks in Turkey from the 1st quarter of 2005 to 3rd quarter of 2016. The findings of the study indicated that there is a significant negative relationship between nonperforming loans and the profitability of Turkish banks as measured by the return on assets and return on equity. The higher the level of nonperforming loans the lower the asset quality of the commercial banks in Turkey.

Ghosh (2017) conducted a study to examine the effect of corporate governance reforms and bank performance: Evidence from the Middle East and North Africa. The study utilized bank level data for the period 2000-2012 to examine the bank performance. The study adopted fixed effects regression within a difference-in-differences specification for the analysis. The findings of the study indicated that not all governance aspects are integral in enhancing the effectiveness of the commercial banks. The results indicated that managerial components; operational efficiency and the access to capital were the main factors that influenced bank performance.

Ndoka, Islami and Shima (2017) examined the impact of liquidity risk management on the performance of Albanian Commercial Banks during the period 2005-2015. The study employed panel data regression to analyse the impact of liquidty risk management on a sample of 16 Albanian banks for the period 2005-2015. The findings of the research indicated that positive liquidity performance was positively related to higher performance of commercial banks in Albania. Muriithi and Waweru (2017) conducted a study on Liquidity Risk and Financial Performance of Commercial Banks in Kenya. The study sampled all the 43 banks and collected panel data for the period 2005-2014. The study measure liquidity risk using liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) while the financial performance of commercial banks was assessed using ROE. The study utilized random effects estimation and generalized method of moments (GMM) to analyze the panel data. The overall effects of the analysis indicated that liquidity risk has a negative effect on financial performance. The research recommended that bank's management need to pay the required attention to the liquidity management.

3.0 RESEARCH METHODOLOGY

The study was guided by the CAMEL model metrics in measuring stability and its influence on the financial performance of commercial banks measured by ROA and ROE. The study was primarily grounded on the CAMEL model. The study further adopted the positivism philosophy which guided the research. The research employed a descriptive research design. The population for the study was 24 commercial banks in south Sudan from which the research targeted one senior manager. The research relied on a mixed methodology which encompassed both quantitative and qualitative data. Secondary data was collected for the period 2012-2017 from audited annual financial reports of individual banks and from the Central Bank of South Sudan reports while primary data was collected by use of a semi-structured questionnaire. The collected data into SPSS 23 for subsequent descriptive and inferential statistical analysis.

4.0 RESULTS AND DISCUSSION

4.1 Response Rate

The current research sought to collect data from 24 commercial banks representatives within South Sudan. The results of the study shown on Figure 4.1 below indicate that the study was able to obtain a response rate of 95% (n=23) while only 5% of the respondents did not take part in the study. Kaplowitz, Hadlock, and Levine, (2004) indicated that a response rate of above 60% is reliable for statistical analysis; hence the research response was deemed appropriate for analysis.

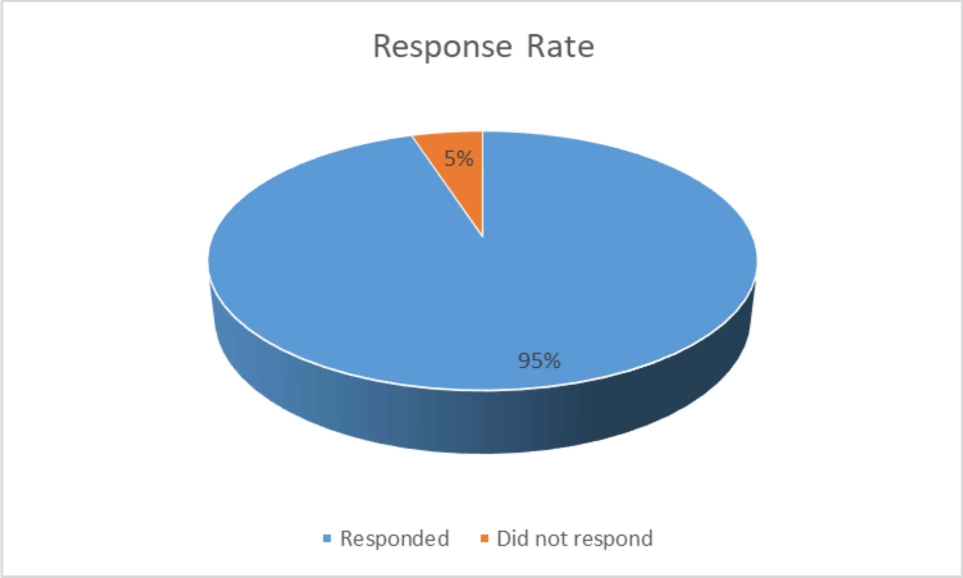

Figure 1 Response Rate

4.2 Education level of Respondents

Table 1: Education Level of Respondents

	Frequency	Percent
Doctorate	1	4.3
Masters	7	30.4
Degree	15	65.2
Total	23	100.0

The results of the study shown on table 4.1 above indicate that the majority of the respondents 65% (n=15) had attained degree level education, 30% (n=7) had attained at least a masters level education. The above findings indicate that there is growing professional competency within the personnel of South Sudan commercial banks which raises the employee technical capabilities.

4.3 Descriptive Statistics

4.3.1 Influence of Asset Quality on Financial Performance

The second objective of the study sought to establish the influence of asset quality on the financial performance of South Sudan bank.

Table 2: Asset Quality and Financial Performance

Statement	N	Mean	Std. Deviation
Adequate possession of asset composition of commercial banks promotes the performance of banks.	23	4.1739	1.07247
Holding high quality of assets increases bank's return	23	3.9130	.99604
Commercial banks in South Sudan use conservative provision of loan losses	23	3.9565	1.14726
Loan portfolio quality contributes to positive bank performance	23	4.2609	.61919

The second objective of the research sought to examine the influence of asset quality on the financial performance of commercial banks. The results of the study on Table 4.3 indicated that with regard to adequate possession of asset composition of commercial banks promotes the performance of banks there was strong agreement among respondents as shown by a mean of 4.1739. The study findings further showed that with regard to holding high quality of assets increases bank's return there was agreement among respondents as shown by a mean of 3.913 and a standard deviation of 0.99604 showing moderate variation in the responses. However the above results are not in line with Acharya, *et al*., (2015) study which indicated that increasing financial liabilities within emerging economies that were backed by poor asset quality in the financial industry did not result in better firm value. The researchers further did note that in Sub-Saharan Africa the lack of financial deepening in most of the countries contributed to poor performance of commercial banks which relied on lending as a revenue stream.

The results of the study also showed that with regard to commercial banks in South Sudan use conservative provision of loan losses there was agreement among respondent as indicated by a mean of 3.9565. The findings of the study also pointed out that there was strong agreement among respondents that loan portfolio quality contributes to positive bank performance as shown by a mean value of 4.2609 with minimal variation in responses obtained as shown by a standard deviation of 0.61919

4.3.2 Influence of Management Efficiency on Financial Performance

The third objective of the study sought to establish the influence of management efficiency on the financial performance of South Sudan bank.

Table 3: Management Efficiency and Financial Performance

Statement	N	Mean	Std. Deviation
Efficiency within banks' management mitigates credit risk and fosters better returns for the bank.	23	4.2609	.86431
Efficient management enhances diversification of revenue stream for commercial banks.	23	4.3043	.82212
Management efficiency leads to optimal operating expense within the firm.	23	4.5652	.58977
Efficiency in the management team promotes better investment ventures for the bank.	23	4.3478	.93462
Efficient management team ensures compliance to applicable laws and regulations	23	4.3913	.72232

The third objective of the research sought to examine the influence of management efficiency on the financial performance of commercial banks in South Sudan. The results of the study shown on Table 4.3 showed that in regard to efficiency within banks' management mitigates credit risk and fosters better returns for the bank there was strong agreement among the respondents as shown by a mean of 4.2609. The results also indicated there was strong agreement among the respondents with concern to efficient management enhances diversification of revenue stream for commercial banks as denoted by the mean value of 4.3043 and a deviation of .82212 indicating moderate dispersion in the responses. However the results of the study are not in congruence with Garang, Issa, and Ali (2017) who in their review of South Sudan tansition to stability and fiscal sustainability indicated that poor capacity and lack of social and human capital were the major challenges to fiscal growth and performance of institutions.

The findings of the research further showed that with regard to management efficiency leads to optimal operating expense within the firm there was strong agreement among respondents as shown by a mean value of 4.5652 and a standard deviation of .58977 denoting minimal variation in the responses. The study results also showed that with regard to efficiency in the management team promotes better investment ventures for the bank there was strong agreement among the respondents as shown by a mean value of 4.3478. The research findings also showed there was strong agreement among respondents with regard to efficient management team ensures compliance to applicable laws and regulations as represented by a mean value of 4.3913. SirElkhatim and Salim (2015) are in support of the above findings. In their study on prediction of bank failures in Sudan between 2006-2014 indicated that the quality of the management team of banks was key to fostering the financial growth of commercial banks.

4.3.3 Influence of Liquidity on Financial Performance

The fifth objective of the study sought to establish the influence of liquidity on the financial performance of South Sudan bank.

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Table 4: Liquidity and Financial Performance

Statements	N	Mean	Std. Deviation
Adequate liquidity ensures bank is able to meet financial obligations in a timely manner.	23	4.0870	1.16436
Access to optimal liquidity level ensures minimal loss in liquidation of assets	23	4.3043	.82212
High liquidity levels leads to low profit levels within commercial banks.	23	3.8261	1.07247

The fifth objective of the study sought to establish the effect of liquidity on the financial performance of commercial banks. The findings of the research showed that with regard to adequate liquidity ensures bank is able to meet financial obligations in a timely manner there was strong agreement among the respondents as shown by a mean value of 4.087. The results of the study also indicated that with regard to access to optimal liquidity level ensures minimal loss in liquidation of assets there was strong agreement as shown by a mean value of 4.3043. The study results also indicated there agreement among the respondents with regard to high liquidity levels leads to low profit levels within commercial banks as shown by a mean value of 3.8261 and deviation of 1.07 showing moderate dispersion in the responses. These results are in line with Elgadi and Yu (2018) who examined profitability of commercial banks in Sudan and indicated that commercial banks that were able to wither liquidity problems posted higher financial results than the other banks.

4.4 Correlation Analysis

Table 5: Correlation Analysis

		Financial Performance
Asset Quality	Pearson Correlation	.784
	Sig. (2-tailed)	.001
	N	6
Management efficiency	Pearson Correlation	.758
	Sig. (2-tailed)	.002
	N	6
Liquidity	Pearson Correlation	.620
	Sig. (2-tailed)	.001
	N	6

The results of the research indicated that there was a strong positive association between asset quality and financial performance of commercial banks as shown by p-value = 784, Sig =.001. These findings are supported by Ganguli, (2017) who posited that lack of commercial banks to diversify their product portfolio and weak asset quality was negatively associated with financial performance of banks.

The findings of the research indicated that there was a strong positive relationship between management efficiency and the financial performance of commercial banks as shown by *p-value = 758, Sig = .002.* These results are not in agreement with Sarker, Sultana, and Prodhan (2017) who noted that improved management efficiency is positively related to the financial performance of commercial banks. The findings of the research indicated that there was a positive relationship between liquidity and financial performance of banking institutions as indicated by *p-value = 620, Sig = .001*. These results are supported by Ndoka, Islami, and Shima, (2017) who concluded that liquidity was positively related to higher bank performance.

5.0 CONCLUSIONS AND RECOMMENDATIONS

5.1 Conclusions

The research concluded that holding assets in a highly liquid form tends to increase the commercial income of the banks hence this should be encouraged. Banks with poor asset quality and thus high credit risk are less profitable; this can be avoided by adopting better screening policies that are geared towards an improvement of the service offering within the commercial banks. In addition, as much as possible, these banks should use their effort to deploy their assets to earning assets to strengthen their earnings ability. The study further notes that adoption of better asset allocation mix will result in better profitability for the institution.

The research study concluded that commercial banks should strive to tap the best talent in the market that will help in enhancing the operational efficiency of the financial institutions. The commercial banks should further undertake better employee motivation strategies such as training, career advancement programs and better remuneration that will help in expanding the management efficiency within the commercial banks.

From the review of the results the study concludes that most of the commercial banks have enhanced their liquidity position over the past. However much needs to be done in order to limit financial distress challenges that have been occasioned by the heightened insecurity and macroeconomic volatility. The study further concludes that commercial banks should increase their holding of highly liquid assets as this will limit their default risk and increase their standing among lenders and other institutions.

5.1 Recommendations

The study recommends that at the bare minimum the management of commercial banks should benchmark with industry experts on how to enhance their services and product offering to better their asset quality scores. Further the study recommends that banking institutions that have shied away from lending activities should reconsider the potential benefits that may accrue from undertaking lending activities. The study therefore recommends that banks should be encouraged to look beyond local market and strategically expand their operations to other geographical markets and sectors of the economy. Location of bank branches is strategically paramount if banks must maximize return on investment.

Liquidity in a bank is highly sensitive and most crucial issue than other enterprises. Therefore, those banks should be in a position to meet its liability holders as when demand arises. Thus the appropriate mixture of liquid and non-liquid asset should be maintained. For this an appropriate strategy of liability management and assets management should be designed by the management of these banks.

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