

Municipal Owned Community Bank: Capital Raising Dilemma

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MANUSCRIPT DETAILS

TITLE: Municipal Owned Community Bank: Capital Raising Dilemma

ABSTRACT:

This case discuss the establishment of a community bank by four municipal councils following a directive from the President. The case covers field of financial services provision, bank management and bank capital raising strategies. It covers various strategies used by a community bank to raise capital and to serve its clientele at the same time upscale to a commercial bank. It also explains the bank's struggle to meet both economic and regulatory capital and being competitive in the market.

The case is suitable for Third year students in Bachelor of Commerce/Economics specializing in banking/financial services. It also suits postgraduate/master's students seeking a Postgraduate Diploma or Master of Business Administration in financial institutions/ banking course.

The case provides details of how the Capital Community Bank (CCB) raised its capital through strategic financial engineering which enabled it to raise the minimum regulatory capital required to be licensed as a financial institution unit, to a regional financial institution, to a fully-fledged commercial bank. The bank started with a paid up capital of TZS 472.3 mil in 2002, involving four Local Government Authorities and individual investors. Capital raised to TZS 31.3 bn in 2014 and down to TZS 20.6 bn at the end of 2016. The minimum regulatory capital required is TZS 15 bn, while paid up capital was 16.9 bn. With the change of the management team in 2017, the bank is looking for avenues to raise further capital to meet the regulatory limits and continue to survive as a commercial bank, given dramatic changes in the banking sector in Tanzania.

The case introduces student to basic understanding of banking sector in Tanzania as well as the strategies and struggle to raise capital through shareholdersâ€™ funds. Application of Banking theory and Pecking order theory is evidenced from the case. The case outlines why the bank struggled to raise capital and what triggers the capital raising strategies. It also give students an opportunity to think about applicable theories of capital structure and bank capital, and strategies the bank could use to rescue its capital crunch in the future.

CUST_SUPPLEMENTARY_MATERIALS :No data available.

CUST_SOCIAL_IMPLICATIONS :No data available.

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Municipal Owned Community Bank: Capital Raising Dilemma

The Beginning

In May 1999 the Association of Local Government Authorities (ALGA) held their annual general meeting in the main commercial city of Tanzania. The Chairman of the meeting was a City Mayor Mr. Mwinyi Madenge. The secretariat of the meeting was Capital City Council (CCC) headed by its Director Mr. Chacha Kyaro. The meeting resolved that there was a need to establish a commercial bank to serve the needs of local government financing and financial transactions. Local government authorities (LGAs), are by law independent from the central government, and among other functions are to serve the local communities. The central government provides a grant to LGAs to cater for operational and administrative budgetary needs. Tanzania mainland has a total of 172 LGAs, in 25 regions, 42 of which are urban authorities, and members of ALGA. Local governments were required to set aside 10 per cent of their own source revenues each year, to provide loans to the youth and women entrepreneurs, but could not rely on banks like the National Bank of Commerce Limited which were serving the central government banking needs. Thus, establishing a bank to handle all the transactions was the main motive of the proposed commercial bank. Another motive was to leverage the use of an already established Local Government Capital Fund, which was used to provide loans to LGAs to undertake infrastructure development projects which generates income. The establishment of the bank however, was required to get central government clearance through various ministries, and hence a concept note was to be prepared by a team of committee members including Mr. Chacha.

In September 1999, Mr. Chacha was hosting the number one Guest of the nation, Hon. Benjamin W. Mkapa, the third President of Tanzania. In the awake of local government elections and part of his duties, the President was visiting several areas of the City which included market places for food products. In his visit, the President talked to street vendors known as “Machingas”, a name derived from “Wamachinga”, a tribe from Southern of Tanzania where it is believed that they initiated the street vending sole proprietorship and owner managed businesses in Tanzania. The Machingas do street vending businesses by hawking convenient goods for sale, moving from one area to another, displaying the goods on the streets and sale on bargaining basis. The Machingas told the President that they have no other capital than their own strengths which was translated into a famous Swahili saying *“Mtaji wa masikini ni nguvu zake mwenyewe”* meaning *“the capital of the poor is based on their physical strength.”* A clear message was send during the President’s visit; there was lack of support from the government and the private sector to

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finance their businesses. In response to their inquiries, the President called upon the four LGAs in the City to find ways to finance the micro and small businesses. Mr. Chacha, leading the apex organization of the city, was in charge of the process. The city had a population size of 2.5 mil people in 2002. By that time Mr. Chacha recalls that out of TZS 340 mil which was loaned to entrepreneurs by the Capital City Council, 73% were non-performing loans.

Mr. Chacha convened several meetings to brainstorm on the establishment of the bank and they reached a decision to establish a community bank. In May 2000, Mr. Chacha and his team agreed to establish a Capital Community Bank (CCB). The bank was to be owned by the Capital residents and its four LGAs. One thing was clear, that to obtain a license a feasibility study needed to be undertaken. The team approached a foreign development partner which, during the time supported restructuring of one of the state owned banks. The development partner agreed to offer technical assistance in formulating strategies towards the establishment of the community bank by providing a Consultant. In July 2000, Mr. Chacha quit the public office and joined politics to contest for a parliamentary seat in the Lake zone which he won in October 2000.

Establishment

The Consultant and the rest of the team employed a project manager who had experience in microfinance, Mr. Edward Marenge to undertake the preparatory work to establish the bank working with the Consultant. By then, the Bank of Tanzania which is the regulator of the banking business in the country had issued a guideline for the minimum capital requirement to establish a regional financial unit which was TZS 750 mil. Community Banks were required to have the paid-up capital raised to the tune of TZS 1,000 mil.

Based on the feasibility study, the viable financing option for the bank was for the four LGAs to raise equity to finance the required capital in equal amounts. The rest was to be financed by Capital residents. However, the amount expected from the four LGAs was not enough to meet the required minimum capital to establish a bank. The option for raising shares through Over the Counter (OTC) market was not favoured by Capital residents, as it was also quite new as a financing strategy. The establishment team had to seek alternative fund-raising strategies to involve members of parliament, and other investors outside of the Capital city. By that time, the country had not established a stock exchange, and development finance was not available. Also, the community bank concept was new, although legally allowed, none of the banking firms was offered a community bank license. Appetite to invest in a community bank venture by

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institutional investors mostly government owned pension funds and insurance firms was low. The government was also liberalizing other financial institutions, including the restructuring of long standing government banks namely the National Bank of Commerce and the Cooperative and Rural Development Bank currently CRDB Bank PLC. In the event of disposing some of the government institutions, raising funds from the private sector for another government owned banking institution was not ideal to many. Nevertheless Hon. President Mkapa and Mr. Chacha were also among the first shareholders of the conceptualized community bank. President Mkapa was re-elected for a second term in 2000 and Mr. Chacha came back as a member of the parliament and was named a Minister. With the expanded network, they were able to persuade several other politically affiliated individuals to subscribe to the shares of the bank through OTC market.

CCB was established in September 2001 and granted a license to operate as a regional financial unit by the Bank of Tanzania (BOT) in October 2001, following subscription of capital from the LGAs. It further issued its shares to the public on a closed window in July 2002, raising about TZS 672.3 mil of the intended TZS 750 mil. Mr. Edward was appointed the first Managing Director of the bank. It opened its doors to the public for business in April 2002 with a capital of TZS 1,123 mil. The bank was granted a license to operate as a regional financial unit (a community bank concentrated in one region only) in June 2003 after meeting the minimum capital requirement of TZS 1,000 mil. The bank owners who were by majority the four LGAs, aimed to use the bank as their sole bank for public related transactions and channelled the legally required 10% of the annual own source revenues to provide loans to empower youth and women entrepreneurs from the city.

Operations and Capitalization

The operations of the bank continued well and the demand for loanable funds by the customers was high. The market segment which the bank aimed for and as instructed by the President, was still lucrative though with several challenges. Amongst the challenges was the lack of banking support infrastructure such as national identity cards, credit rating institutions and street names. There was also weak governance of the bank, an aspect which was overlooked. The Board of Directors members were among elected Councillors from the Municipal Councils who had no background in management and business of banking.

Following the increase in demand from the customers, in 2007 the bank initiated a capital raising strategy through a rights issue which was favoured by 78% of the shareholders during the annual general meeting

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(AGM). In May 2008 the bank further split its shares. For every one (1) share, four (4) shares were given out. This however did not change the capital structure of the bank. By then, the Capital Stock Exchange (CSE) was in operation and had listed two companies. The bank decided to list its shares, from the over the counter market by initiating initial public offering (IPO). Results of the IPO were very favourable to the public and other strategic investors. IPO issue results of 2008 indicated that the bank was able to raise TZS 3.7 bn. out of the targeted TZS 1.5 bn., creating an over subscription of 147%. The bank was listed in the Main Investment Market Segment (MIMS) of the CSE in September 2008, being the first bank to be listed in the CSE. The bank share ownership structure from its inception and after the IPO is as presented in Figure 1. As noted from Figure 1 there is a good response from strategic investors namely the Government Trust Fund. For other investors there was almost a two-fold percentage inrease, taking advantage of existing shares.

INSERT FIGURE 1

The raised capital after the IPO enabled the bank to operate smoothly for few years. At the end of March 2011, the bank attained a core capital of TZS 14.7 bn (paid up capital was only TZS 9.6 bn) that prompted the Board of Directors to put in an application to change its license from "community bank" to "commercial bank". The Central bank required that for bank to have a Commercial Bank licence, it must have at least TZS 15 bn of paid up capital. The commercial bank status would help the bank to open a window to corporate customers and thus increase deposits and banking business, develop new products and services, increase the number of branches in the City and across the country and add value to the shareholder's wealth through increased dividends and capital gain of its share prices. It also allows the bank to undertake international transactions and create a relationship with other banks nationally and internationally. As of 1st October 2012, the bank shares traded at TZS 640/= per share. As the normal wisdom goes, *"You can only repair the roof of the house when it is day time and with no storms"*. Everything was good for the bank and in the same month of October 2012, the bank decided to undertake rights issue to further expand its business potential. As part of the strategy to raise capital, the bank decided that the 2012 dividend be converted into shares in form of bonus shares. Therefore for every five shares one bonus share was given out.

Another consideration was on the rights issue where for every one ordinary share, one share to be qualifying for a new share at a 40% discount, where one rights issue was priced at TZS 380. It was resolved that if a member fails to fully take up their rights, such members will be diluted. Shares not taken up by

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shareholders after renouncing their entitlement shall be offered to other members only. Keeping the costs of transaction down, the shareholders were requested to bank their share purchases with CCB branches and other special accounts which were opened by two banks with wide network countrywide. Members were also able to deposit their payments through transfers by the use of mobile money platforms, for the first time in share subscriptions in the country. Sale of rights issued shares started in October 2012 and concluded in March 2013. The results of the rights issue was as presented in the Table 1.

INSERT TABLE 1

The rights issues were highly favored and 76% of shares were exercised which enabled the bank to raise its paid up capital to TZS 16.96 bn from TZS 9.6 bn, above the minimum required paid up capital of TZS 15.0 bn limit set by the Bank of Tanzania to be licensed as a commercial bank. The bank thus qualified to operate as a commercial bank. Total economic capital for the bank at the end of 2013 was TZS 31 bn from TZS 24 bn at the end of 2012, given a good profit realised in the year. The bank changed its name to CCB Commercial Bank PLC in February 2012. The change of the name created changes in branding, strategy and increased operational costs to meet the commercial bank status. All these developments and strategies were led by Mr. Edward.

Recent Performance of the Bank

CCB has recorded a tremendous financial performance since its establishment. The bank was able to make profit after three years of operation and since then it has been making profit. Table 2 shows the performance of the bank based on the key performance indicators for the years 2012-2016.

INSERT TABLE 2

As of December 2016, CCB had 10 bank branch offices of which 8 were located in the Capital City. The bank enjoyed a network of about 193 agent bank branches or business centres located in various parts of Tanzania, recorded a 40% increase based on 2015 bank agents. The market segment served by the bank for almost 10 years, was without stiff competition. Currently, several banking and non-banking competitors including microfinance institutions have shifted focus to the micro and small businesses. The bank joined other small banks in the market to establish common technological solutions and now about

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30 banks share same infrastructure for Automated teller machines (ATMs). The bank also issued various products geared towards the use of technology such as mobile banking and agency banking which is extended by digital point of sale devices.

Capital Raising Challenge Ahead

Analysis of the capital trend of the CCB indicates that the bank core capital which resulted from good performance from 2012 reached TZS 31.3 bn in 2014 and went down to TZS 20.5 bn in 2016. Further details are as presented in Figure 2. Based on various asset quality indicators, Table 2 indicates that CCB has substantially recorded huge impact in the provision of loans with an increase of 40% of loan provisioning from 2012 to 2016. This however has caused the non-performing loans to increase by 150% from 4.0% in 2012 to 10.1% in 2016. However, the whole sector was affected by non-performing loans (NPLs) whereby industrial average as of end of December 2016 was 10.27% (see Table 3).

INSERT FIGURE 2

Mr. Godwin Haruni became the new CEO who assumed office in November 2017 where by the capital of the bank dropped to TZS 16.9 bn in December 2018, just TZS 1.9 bn above the minimum required capital by the Central Bank. After one year in the office Mr. Godwin has already set up a new management team. The management team is with high expectations given the technological developments and solutions available. One thing is clear, the sinking capital might cause a total closure of the bank. The CCB is now prompted to raise capital, this time following a capital sink. The bank is aiming to raise TZS 8.9 bn of paid up capital by offering a 22% discount on its new shares comparing with the current market price TZS 340. The capital increase will not reach the highest level attained by the bank in 2012. The call for capital is likely to be affected following new developments in the industry:

1. The Government increasing the municipal councils from 3 to 5 and maintaining the Capital City Council. This creates inquiry on the ownership of the Bank.
2. The government has implemented a Treasury Single account in 2016 where by all government institutions including LGAs are now required to bank with the Central bank and not with commercial banks. This has affected the liquidity of the banks to a great extent, including CCB.
3. The current trend in the banking industry which suggests that banks are making losses. The asset quality analysis of the banking sector indicated that some banks have non-performing loans of up

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to 80%. The industrial average was 12.5% against the 5% target by the central banks. Banks like CCB were concentrating on consumer loans to government employees. In 2015 and 2017 the government cleaned its employees' database through physical verification whereby it was found that about 15,000 employees were "ghost" employees who accessed loans from banking institutions most probably including CCB.

4. Recently the government has put in complete closure and receivership five banks, of which 3 are community banks and started after the successful performance of CCB.
5. The planned implementation of International Financial Reporting Standard (IFRS) 9. IFRS 9 introduces a forward-looking view of credit quality, with banks expected to recognise credit impairment before a loss event. This is to be implemented in the financial year 2019 for Tanzanian banking firms and it is expected that smallest banks like CCB may be affected. To mitigate the impact, banks need to have a very clean loan portfolio book.
6. Recent move to merge state owned banks – Recently through Treasury Registrar Office, the government has merged three banks into one. Given CCB is owned by majority government institutions, any capital impairment, which could not be resolved from the private sector could mean triggering a merge with another government owned bank.
7. The Government has engaged in a National Identification programme whereby national identity cards can be verified online. Related to this is naming and mapping of the streets through post codes. Recently also the government has made it mandatory for the registration of the SIM cards for every mobile phone holder.
8. The Central Bank has licensed two Credit Reference Bureau and financial institutions must subscribe by providing information to the credit bureau and may access the information on credit history of various borrowers at a fee.

Mr. Chacha who is currently a retiree thinks that further investing in the bank is not an option for him. He still believes that the bank, if focussed on its original vision of serving the city residents, could have gained a lot of momentum. "The capital risks faced by the bank is accelerated by the bank's ambition to expand quickly" he noted.

The Banking Industry

The banking sector in Tanzania is very competitive. The sector had 59 banking and non-bank financial institutions, whereby 38 are commercial banks, 12 are community banks, 3 financial institutions, 2

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development financial institutions and 4 deposit taking microfinance institutions as of December 2016. Out of these institutions, 7 banks were state owned, 52 privately owned and 30 foreign owned.

According to the BOT Report on Banking Supervision of 2016, the banking institutions in Tanzania had 810 branches countrywide, 273 (33.70%) of which were located in the Capital city. There has been an increase in banking operations in the country for the past five years. The sector has witnessed a growth of total assets from TZS 16.98 trillion in 2012 to TZS 27.2 trillion in 2016, an increase of more than 87.6%. Related to this, there has been an increase in the interest income and number of employees in the sector. The details of the performance of commercial banks in Tanzania are presented in Table 3.

INSERT TABLE 3

The total funding to the banking sector grew at 0.92% between 2015 (TZS 23,416.25 bn) and 2016 (TZS 23,632 bn), compared to the growth of 20.14% between 2014 (TZS 22,505.55 bn). The main source of the funding is customer deposits and other liabilities; accounting for 85.25%. Shareholders' funds account for 14.75% of total funding of the banking sector in Tanzania for the year 2016.

Case Questions

1. Why Bank Capital is important and what is the current development in capital regulations?
2. Comment on the CCB financial performance taking into consideration three recent years by focusing on the performance indicators presented in Table 2 and Table 3
3. Discuss the roles played by the key persons in the case and how they were successful/unsuccessful to the performance of CCB to date.
4. Why was CCB very successful in raising its capital?
5. Why was it necessary for the bank to list the company in Capital Stock Exchange? Why were the Four Municipal Institutions not keen in increasing their shareholding structure after the bank was listed the stock market?
6. Comment on CCB Capital analysis trends as presented in Table 2 and Figure 2. What should be done to rescue the company from capital risk? Would you consider to be shareholder of CCB should it consider boosting further its capital?

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7. What are key management lessons to learn from the case?

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Municipal Owned Community Bank: Capital Raising Dilemma

Teaching Note

Introduction

This case discusses the establishment of a community bank by municipal councils to meet the demands for capital by micro, and small enterprises in, Tanzania. The establishment of the bank was made possible following a request by the President of the United Republic of Tanzania by then Hon. Benjamin William Mkapa. Hon. Mkapa served the office from 1995-2005 and he was well known for his efforts to revive the Tanzania's economy.

Capital City is the largest and commercial city of Tanzania with a population of 4,364,541 as per the official 2012 census, with a total of 406,602 businesses according to the National Micro, Small and Medium Enterprises (MSMEs) Survey 2012. The establishment of the Capital Community Bank (CCB) is one of the first initiative in Tanzania where by municipal councils joined hands and owned a majority stake to form a private bank in collaboration with few shareholders by then. The main reason for the bank's establishment are the increased cries by the micro and small entrepreneurs to seek capital from the banking sector, whereby during its establishment, no bank was focusing on offering loans to the MSMEs. They have been denied to access capital from the existing banks due to excessive conditions to secure a loan.

Methodology Adopted

The case is based on a real bank. The names have been changed to create unanimous of the key players and the bank due following several information which may be interpreted differently by various stakeholders of the bank. The characters are real but the names are note real. The bank financial affairs and performance is real. The case utilized quantitative and qualitative information. Key informants of the case were two founding Municipal Directors, one Municipal Treasurer, Three managers served the bank for more than 5 years and one former Board member. The case was also informed by a bank expert who served three top most commercial bank in Tanzania with banking experience of more than 25 years.

About the Case

Students reading the case are expected to learn about several challenges, strategies in the establishing, operating and managing a bank from capital raising perspective. Also they will understand the banking sector infrastructure in Tanzania, competition and innovations within the banking sector. The case also discusses in detail how the bank was established, raised its capital through strategic financial engineering which enabled it to raise the required minimum capital from a regional financial institution to a fully-fledged commercial bank, and the motive behind the advancement. The bank started with a paid up capital of TZS 472.3 mil in 2002 and currently is at TZS 16.9 bn., while a minimum required capital is TZS 15.0 bn.

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The case introduces a student to basic understanding of banking operations in Tanzania as well as the strategies and struggle to raise capital through shareholders' funds. It also introduces students to the basics analysis of the bank financial statements.

Target Audience

The case is applicable to students studying the following courses;

1. Banking related courses – e.g. Bank Financial Management, Bank Capital, Financial Institutions and Markets.
2. International/Emerging Market studies on Banking especially on community banking.

Learning Objectives

1. To illustrate various strategies used by banks to meet the minimum regulatory and economical capital needs.

2. To illustrate the performance and development of a community bank to commercial bank in emerging markets with financing from the local government authorities.

3. To account for complexities and struggle to build sound and competitive banking business in emerging economies based on the internally generated capital, supported by local government authorities as strategic investors.

Suggested Readings

In order to further understand circumstances of the case and its development, it is important that students are introduced to the following basic readings prior to the case:

1. Bank of Tanzania, (2017). Directorate of Banking Supervision's Annual Report. Dar es Salaam: Bank of Tanzania. Available from https://www.bot.go.tz/BankingSupervision/Reports/DBS%20ANNUAL%20REPORT%202017.pdf
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4. Calomiris, C. W. and Wilson, B. (2004). Bank Capital and Portfolio Management: The 1930s "Capital Crunch" and the Scramble to Shed Risk. *The Journal of Business* 77**,** 421-455.
5. Commonwealth Local Government Forum (2017), Local Government Systems in Tanzania. Available from http://www.clgf.org.uk/default/assets/File/Country_profiles/Tanzania.pdf
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7. Harris, M. and Raviv, A. (1991). The Theory of Capital Structure. *The Journal of Finance*, 46, 297-355.
8. International Monetary Fund (2018), United Republic of Tanzania Financial System Stability Assessment. IMF Country Report No. 18/346, November Available from https://www.imf.org/~/media/Files/Publications/CR/2018/cr18346.ashx
9. Saita, F (2007). Value at Risk and Bank Capital Management – Chapter 1 and 2. Elsevier Inc., p.170 Figure 7-1.
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11. Zeller, T. and Stanko, B. (1994) Financial Ratios for the Commercial Banking Industry: Do They Measure What You Think? *Journal of Business and Economic Perspectives* XX(1). Available from https://ecommons.luc.edu/cgi/viewcontent.cgi?article=1039&context=business_facpubs

Teaching Plan

Prior Reading and Teaching

This case requires 2 weeks and 2 hours of effective class discussions, one hour each week. Students may require about 6 hours of independent studies apart from the 2 actual hours of joint discussions in the class. The case is expected to be administered after prior teachings and readings on various aspects in bank financial management course or any other related course. Students may be grouped in 4 to 5 students per group, depending on the size of the class. This case was tested to a class size of between 6 to 90 students since 2013. Recently in the year 2018/19 a class size of 80 undergraduate students in a course named FN304: Bank Financial Management, students were divided into 3 seminar classes of not more than 24 students and 4 to 5 groups were formed in each of the seminar class. The case was also tested to 7 students undertaking Masters of Business Administration (MBA) course named FN602: Financial Institutions and Markets in the academic year 2017/18. There were no seminar groups for the MBA class and 4 groups of 2 to 3 students were formed.

Prior teaching and readings may be based on the following topics as per the reading list provided:

1. An overview of the Tanzania financial system, banking business and banking environment.
2. Theory of banking and role of banking in business environment.
3. Bank balance sheet and income statements analysis and interpretation.
4. Bank products and innovation.
5. Assets and liability management.
6. Bank capital – regulatory and economical bank capital, capital adequacy, capital planning, determinants of capital structure of banking institution.
7. Risk management in banking.

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Students were given the case in week 7 of the semester of 15 weeks and prior readings were done regarding bank financial management. Students were told to summarize the case and come up with some insights on the case, in week 10 of teaching. Case questions were distributed to the already formed groups as per the table below and they were told to discuss and prepare presentation during the seminars.

Group No.	Case Question Allocation Week II
1	1, 6
2	2, 7
3	3, 2
4	4, 2
5	5, 7
6	6, 3

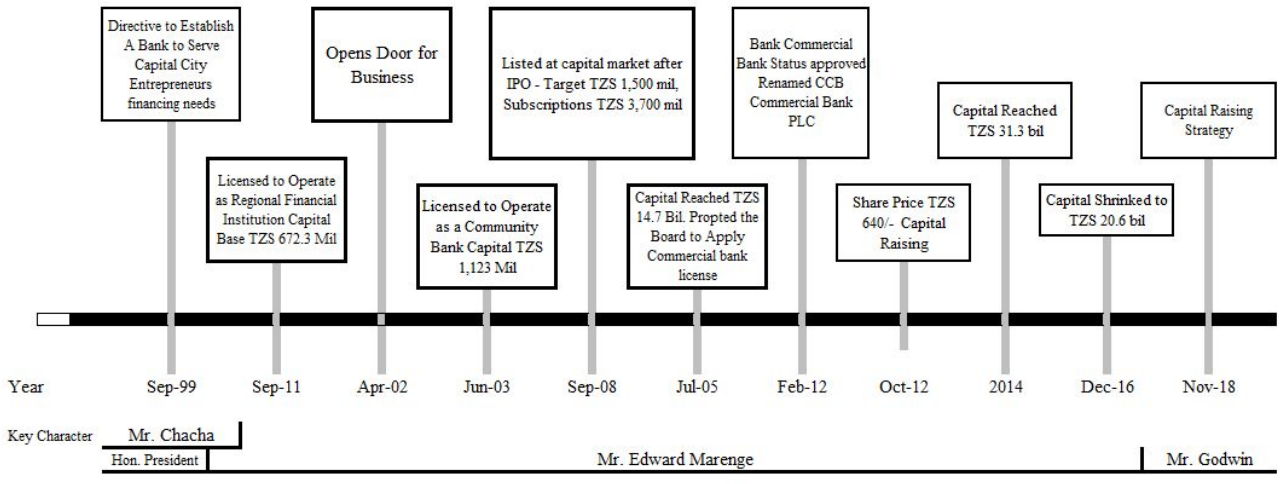
In bigger classes, same questions may be allocated to two groups and during the presentation – one group may make presentation and the other group may add missing points, or presenting an alternative answer as indicated in the suggested answers.

First Week

First 15 minutes:

Seminars normally take one hour. For the first week the instructor is expected to give a summary of the case and give a detailed discussion on the banking environment and evolving case issues, as well as the industry analysis. The instructor may also update students on the current trends on the development of banking sector including status of players, competitions and other regulatory developments.

Stages of the case and its development can be viewed as shown in the figure below.



Next 40 minutes

For some reasons students may not have time to read the case outside class room sessions, students will use the next 40 minutes to read the questions on their groups, and ask the instructor any question concerning the case. The instructor may visit the student groups and contribute to student discussions.

Remaining 5 Minutes

The remaining 5 minutes is for distribution of the case discussion questions. The case discussion questions are distributed to the students for the purpose of presentation and the instructor can choose how the presentation will be done.

Second Week

First 45 minutes:

Five groups will make presentation on the case based on their thought based on take home assignment. It is expected that for each question at least 5 minutes of presentation will be undertaken involving discussions among the students. To ensure strict time management instructor may appoint a time keeper for the presentations and sessions. Students may be required to review their answers based on the current development and submission for marking – as part of their continuous assessment. For question No. 2 students can be asked to present only two ratios as the question requires detailed analysis but, they may be assigned to look at all the possible analysis. As they present the instructor may assign marks for groups say 1 to 5 based on how good they have argued for their case and based on the guidance provided in this teaching note.

Remaining 15 minutes

The instructor is expected to give feedback to the students regarding their case submissions based on this teaching note as well as other development in the banking industry. Students may be required to review their answers based on the current development.

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Case Questions

1. Why Bank Capital is important and what is the current development in capital regulations?
2. Comment on the CCB financial performance taking into consideration three recent years by considering performance indicators presented in Table 2 and Table 3
3. Discuss the roles played by the key persons in the case and how they were successful/unsuccessful to the performance of CCB to date.
4. Why was CCB very successful in raising its capital?
5. Why was it necessary for the bank to list the company in Capital Stock Exchange? Why the Four Municipal Institutions were not keen in increasing their shareholding structure after the bank was listed the stock market?
6. Comment on CCB Capital analysis trends as presented in Table 2 and Figure 2. What should be done to rescue the company from capital risk? Would you consider to be shareholder of CCB should it consider boosting further its capital?
7. What are key management lessons to learn from the case?

Case Questions Suggested Answers

Question 1. Why Bank Capital Is Important and what is the current development in capital regulations?

Suggested Answers/Directions for Discussion:

Students can produce evidence why bank capital is important by examining some information which was presented in the case including;

1) Regulatory purposes – the bank needed to upscale to be a commercial bank from a community bank and thus need for capital
2) To cope with competition – reference to relevant sections in the
3) To invest in banking operations to cover such investments in new products, innovation and technology
4) To finance bank growth aspiration – branch expansion, investment in technology - agency banking and mobile banking

Other discussion may be cited from the already readings in the classrooms including importance of capital as a cushion to absorb losses.

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On the future of capital regulations – the students are expected to review development of capital requirement especially examining the provision of Basel II and III regulations. Students in the banking business class should be aware of Basel II and Basel III.

Basel II pillars

Pillar I: Maintenance of regulatory capital

- This is measured by credit risk, operational risk, and market risk

Pillar II: Supervisory Oversight

- Requires supervisors to review a bank's capital adequacy assessment process, which may indicate a higher capital requirement than Pillar I minimums

Pillar III: Market discipline and public disclosure

- Securities Commissions to disclosure requirements for publicly traded banks
- Bank regulators require quarterly filing and publishing of reports for all banks

Basel III

Basel III will require banks to hold 4.5% of common equity (up from 2% in Basel II) and 6% of Tier I capital (up from 4% in Basel II) of risk-weighted assets (RWA).

Basel III also introduces additional capital buffers,

(i) a mandatory capital conservation buffer of 2.5% and

(ii) a discretionary countercyclical buffer, which allows national regulators to require up to another 2.5% of capital during periods of high credit growth.

In addition, Basel III introduces a minimum 3% leverage ratio.

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Question 2. Comment on the CCB financial performance taking into consideration three recent years by considering performance indicators presented in Table 2 and Table 3

Suggested Answers/Directions for Discussion:

Students are expected to comment on the trend of the performance of the bank as indicated in Table 2. These results need to be compared with the industrial performance in Table 3. Candidates may discuss extensively on the performance of the bank and various scenarios and discussion points may emerge.

One of the options for the analysis is as indicated in Table below which combined variables of similarities between table 2 and 3 of the case study:

Performance Indicator (In Percentage Unless stated)	**2014**	**2015**	**2016**	**Average**	**2014**	**2015**	**2016**	**Average**
Return on Equity (ROE)	11	9	-10	3.33	12.64	12.16	9.26	11.35
Return on Assets (ROA)	2	2	-2	0.67	2.51	2.49	2.09	2.36
Interest Margin on Earnings Assets	23	22	20	21.67	8.37	8.19	9.18	8.58
Non-Interest Income to Gross Income	12	14	14	13.33	25.17	25.9	23.66	24.91
Gross Loans to Customer Deposits	75	70	82	75.67	74.33	78.76	86.07	79.72
Non-Performing Loans to Gross Loans	5	7.8	10.1	7.63	6.83	7.88	10.27	8.33
Earnings Assets to Total Assets	80	79	78	79.00	79.32	78.83	79.22	79.12
Growth on Total Assets	9	8	-6	3.67	14.81	20.14	0.92	11.96
Growth on Loans and Advances to Customers	9	5	5	6.33	19.89	25.07	3.81	16.26
Growth on Deposits	10	12	-10	4.00	14.01	17.33	-1.98	9.79
Overall Treasury bn Rate Annual average					13.6	12.9	16.2	14.23
12 Months Average deposit rate					10.8	10.8	11.5	11.03

Discussions on the Ratios

Return on Equity (ROE)

ROE is the measure of bank profitability for any business firm including banking firms. It measurers the company use of the shareholders' funds. It provides a clue on how good a company returns to operation which gave shareholders a good and joyful return on their invested funds. It can be noted that on average the company return to the shareholders' investment was 3.33% worst case happened in 2016 where the return was -10%. The industry in average of 3 years was 11.5%.

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This is to say that compared to the industry, the bank is not performing well in terms of rewarding its shareholders, based on the ROE measure. This may be attributed to various reasons as indicated in the case – the bank was mostly affected with Treasury single account decision in 2016 and cleaning of the 'ghost' employees from the government payroll.

Compared with other alternative investment vehicles, the bank is earning far from the annual Treasury bn return of 14.23% and a negotiated deposit rate of 11.03% on average for the three years. This is to imply that the shareholders could have earned better returns if they could have invested in this alternative investments.

Given the nature of the investors – Majority Local Government Authorities and government institutions, the motive to establish the bank and given its history, it is unlikely that the majority of investors are looking for the ROE measures rather, meeting objectives of the establishment of the bank. However, the shareholders might have earned substantial income resulting from capital gain; as the company is listed in the stock market.

Return on Assets (ROA)

Return on Assets is a measure of the return attained on every currency unit of resources provided by the bank. Assets are used among others to acquire deposits at reasonable cost and invest the same on earning assets. The higher the earning assets the higher the ratio as well. Hence, the higher the ROA the better.

Considering CCB Average ROA is 0.67% for the last three years, highest being 2% and lowest -2% in 2016. This is to say for every TZS 100 invested, the bank earns only TZS 0.67 cents while the industry is earning TZS 2.36 on average on the past three years. This indicates that the bank is not competitive enough to transform its assets into earning assets. This also may imply that the bank is not using advantage of technology to mobilize deposits – as it is indicated from the case, there is no digital products developed and thus, the bank is investing in branch expansion which is expensive and does not bring the return needed. Although the bank has engaged into Agency banking (substantial investment is borne by the agent and not the bank), the number of agent bank outlets are not enough to derive the business. Situation would have been worse if the bank didn't join Umoja Switch network as the return could be quite low, as it could have been required to develop its own Automated Teller Machines. The results also suggest that bank is not strategically locating the branches to where they can get more return on their investments.

Interest Margin on Earning Assets

Interest margin on earning assets measures bank profitability on lending. Interest margin is difference between interest charged on loans to interest paid to depositors. Lending is core business of banking firm. When the ratio is high means it can also cover the provisions for loan losses and protect the bank from capital crisis. As indicated from the results, the bank earning almost three times as high as that of the industry, 21.67% compared with 8.58% for the average of three years. Students may recall that strategic investors especially the government institution may have contributed to this because of the fact that government institutions may put a lot of funds

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to the bank as deposits which doesn't earn interest rate (current deposits0, in a long term which can be used as core deposit to the bank. Since majority of the bank is owned by the LGAs based in the Capital city and with high budgets and expenditure, they are likely to give advantage to cheap deposits. As a rule of thumb, the higher the interest bearing deposits the lower the net interest margin.

Non-Interest Income to Gross Income

Non-interest income is income realised from non-core business of the bank. This could be income resulting from trading of the foreign exchange, commissions on services provides by the bank. This is a relative measure and it is expected that banks should earn more from its core business of loan provision. Based on the results of the analysis for the three years, it can be indicated that CCB is earning on average 13.33% as compared to 24.91% of the earnings in the industry on non-interest income. This can be contributed by various factors including the fact that the bank is small, with few branch network, shares services such as ATMs as indicated in the case, lower customer base and focusing mostly on the non-corporate clients. Corporate business clients undertake various transactional services including money transfers and imports and export business which earns non-interest income to the bank through various charges. Also the transactional handled through government transaction is not that big as most of its branches are in the Capital city affecting only four LGAs – currently six LGAs as indicated in the case out of more than 172 LGAs country wide as indicate din paragraph 1 of the case, which could earn non- interest income to the bank.

Earning Assets to Total Assets

This is a measure of the ability of the bank to possess enough assets to carry outs its core business of lending activities. From the calculations based on table above, it can be noted that the bank average of earning assets is almost the same as the industry i.e. 79%. This is to say that the bank has equal opportunity to use the earning assets. What makes one bank better in the use of the potential earning assets is the strategies, pricing, asset quality and management. To evaluate the bank potential in turning the earnings assets into profits, analysis based on the Interest Margin on Earning Assets may confirm this. Recalling from the analysis above on this ratio, the bank earning almost three times as high as that of the industry, 21.67% compared with 8.58% for the average of three years. This implies that the bank effectively used the earning assets to earn interest. The question also remains, how good is the bank in managing its assets? This can be measured based on the non-performing loans which measure assets quality.

Non-Performing Loans to Gross Loans

Non-performing loans (NPL) measures the quality of the loans provided. It also measures the ability of the bank systems and management ability to attract quality clients who honor their contractual obligation to pay both principal and interest to the bank. If borrowers do not pay, in the long run it affects the depositors, shareholders, and even the economy. The bank can be liquidated following sustained large NPL. On average, the bank possesses 7.63% for the past three years as compared to the industry average of 10.27%. Higher NPL happened in 2016 across the industry. The industrial target set by regulators is 5% based on the 95% confidence interval in

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offering loans. Based on the case, there are various developments which affected the banks including the clean of the government employees book in 2016. There was also an increase in the NPL from 2014 to 2015. This means that the banks and the general public did witness this increase and possibly respond or any other circumstances might have affected the trend adversely. This can be discussed by looking at the growth measures.

Growth measures

a) *Growth on Total Assets*
   The bank experience a negative growth of total assets from 2014 to 2016. In 2016 the growth of assets was -6% while the growth in the industry was 0.92%. This might be caused by NPL trigger. Also it can be noted that there was a change in the political regime in 2015 (it is noted in the para 2 of the case that elections were done in October 2000 and every after 5 years new election is undertaken – meaning also change in policies), where by a new president was elected which among others new policies might have been in place. Among others it the measures related to public finance – treasury single account which reduce deposits as well as ability of the banks to offer loans. Cleaning of the government employer book also affected the way banks offer loans and thus reduction of its assets.
b) *Growth of Deposits*
   This might be affected by the treasury single account policy as well as the public discipline – following the increased NPL. In 2016 the bank experienced 10% decrease of its deposits as compared to the industry -1.98%. Based on the three years' average, the banks average was 4% while the industry was 9.79%. Structure of the deposits might have explained the scenario better. But, we can find a little evidence based on the analysis of ROE and industrial deposit rate in comparison with the treasury bnls (TBs) rate. Based on ROE it was concluded that the bank was not attractive enough to rational investors. If investor quite in investing in a bank it is likely he/she will trust to deposit with the bank. In all three years the TBs rate was higher than annual deposit rate. A rational investor will thus opt to invest in TBs. Students may recall that investment in TBs has many benefits including tax advantages and the fact that it is risk free meaning, the government will always honour its obligation. The students also may recall function and operations of the depository insurance board whereby there is no guarantee of your deposits should the bank fail. Symptoms of bank failures is increasing non-performing loans, which may lead to negative earnings which affects the bank capital. Also the case has indicated various measures undertaken by the Central bank based on ill-capitalized banks.

On another comment, student may analyse the performance of the sector based on the information provided in the case.

- *The banking sector has 56 commercial banks of which 4 commands more about 50% of the banking assets as mentioned in the case. It is also indicated that 10 top banks account for 70% of the total assets and 72% of the total loans. It is also indicated in the case; it seems there a lot of players in the market but they have little contribution to the financial system. From the analysis it means that 46 banks*

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contribute less than 30% of the bank assets. On the local/foreign concentration, it seems that local banks have about 53% share of the bank assets. It is evident that either we have too many banks in the economy being and some foreign more than what the economy can provide or there is need for inclusive financial services provision.

Question 3. Roles played by the key persons in the case and how they were successful/unsuccessful to the performance of CCB to date.

The President: The decision to establish the bank was important. Since this was coming from the President there was no room to let it pass, rather to implement. The President also become a shareholder of the bank from very initial stage. This created public confidence to the bank and hence its successful story of its establishment and possibly the performance.

Mr. Chacha: This was an instrumental person leading the Apex of the Local government institutions to oversee the services across the city. He was a bit ahead of the President's initiative as he was given much high task by the Association of Local Governments to establish a bank which will suit for all the local Government institutions in the country. He successfully participated in the decision making process of establishing the bank by seeking support for the feasibility study as well as participating as a shareholder of the bank. He however not in favour of rapid expansion of the bank outside Capital city boundaries, as he was optimistic that the bank will be for the Capital City and its residents only, not to expand to a commercial bank.

Mr. Edward: This was the project manager and the first Chief Executive Officer. He managed to serve the institution for 17 years as a project manager, Managing Director of a regional unit bank, community bank and a commercial bank. He has served several diversified boards with political touch and professionals. He led a successful team which ended up accumulating capital of the bank. He also led the bank to various innovations and technological advancement which was beyond the normal thinking of the structure of the bank in the inception stage. It can also be seen that Mr. Edward and his team possibly overstayed in the managing the bank to the extent that the downfall of the bank capital was observed. In 4 years from the capital was shredded almost by 50%. This is a lot of money given, the focus of the bank. However, the bank still survives despite the challenges, as more than 8 banks were closed or restructured due to among others lack of minimum required capital.

Mr. Godwin: This is a new Chief Executive Officer of the bank. He inherited the operations of the bank where there is a lot of opportunities and challenges as well. Opportunities being increase in technological advancement in the financial services industry, Capital City population has doubled, CCB now a commercial bank and it can tap resources countrywide. Challenges include the changes in policies, unfavourable trend in the performance of the banking institutions and need to raise and boost the paid up capital and manage the non-performing loans. His role is to take the bank forward in the mist of all the challenges.

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Question 4. How easy or difficult for CCB to raise the required capital to serve its purpose? Why CCB was very successful in raising its capital?

Suggested Answers/Directions for Discussion:

Students could discuss two major theories, which may be given during the lecture sessions on capital.

1. Pecking order theory developed by Myers in 1984 (Myers and Majluf, 1984, Myers, 1984) The theory argues that financing of the business firm's operations depends on the order of costs of funds. Firms use retained earnings first to finance investments to fill a gap that is created due to an asymmetry of information. The assumption here is that firms have a distinct preference of using internal funds to finance investments. Firms may or may not acquire external financing, and if they do, they will choose among different external finance sources in such a way as to minimize additional costs of asymmetric information. The theory predicts that managers will follow a pecking order, using up internal funds first, then using up risky debt, and finally, resorting to equity. Studying the how the bank raised its capital it can be argued that the bank management and board thought around this theory. This can be proved following share splits and bonus shares (normally resulted from profit of the bank), as well as the spotted opportunity to list the bank in the stock market. Also it can be noted that the fund raising was aimed to cover the regulatory capital and hence the shareholders were aware that contribution of their capital was to meet regulatory capital needs to upscale the bank from community bank to commercial bank.
2. Bank capital theory as explained by Harris and Raviv (1991) and Diamond and Rajan (2000). The theory argues that banking firm assets and functions are not the same like industrial firms and thus, they do not suffer from asymmetric information costs. On the other hand, recent evidence shows that bank capital structure is completely determined by regulatory capital requirements and not related to standard determinants of capital structure (Slovik and Cournède, 2011)[1]. In this case, the amount of bank capital and thus, the capital structure is determined by the bank capital requirements set by the regulatory authority. This is quite true as the bank was prompted to convert to commercial bank following indication that they have reached the minimum regulatory capital required to convert from community bank to commercial bank.

Further, CCB was successful in raising its capital due to various reasons as may be cited from the case.

1. President's intervention on the need to finance petty traders – mostly micro businesses. The President himself was the first person to subscribe to the CCB shares and thus created a huge political influence.

[1] Slovik, P. & Cournède, B. 2011. Macroeconomic Impact of Basel III. *OECD Economics Department Working Papers* [Online]. Available: http://dx.doi.org/10.1787/5kghwnhkkjs8-en.

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2. Government institutions as strategic investors in funding the bank. We have noted that government institutions such as the four local government institutions were strategic investors of the bank. Also Government Trust Fund which is a government established institution played a key role in the IPO in 2008 owning substantial percentage of the shares.
3. The fact that CCB was the first bank to be listed in the stock market. Banking business seem to be profitable and since the establishment of the Capital Stock Exchange, there was no single bank which was listed. CCB took such a bold stem which has resulted to raise substantial amount of money, increasing its shares to general public to 58.3%. This also resulted to the pay-off of the shares through capital gain from TZS 250 to TZS 640, which also triggered the bank to increase its shares in 2012 as indicated in the case.
4. Its nature of business – CCB positioned itself to be focus to micro and small business, for them to access loans and other financial services. CCB was one of the very first community banks established in the country which set example and its performance caused establishment of several other community banks in the country, despite their current massive failures as indicated in the recent development.
5. Location – the bank was located in the commercial city of the country. The municipals involved in the establishment of the bank contribute substantially to the economic development of the country, the municipals have huge and well educated population and necessary infrastructure to support banking business.

Question 5. Why was it necessary for the bank to list the company in Capital Stock Exchange? Why the Four Municipal Institutions were not keen in increasing their shareholding structure after the bank was listed the stock market?

Suggested Answers/Directions for Discussion:

The students may discuss various points regarding to the question.

Why it was necessary for the bank to list to Capital Stock Exchange (CSE)

1. Opportunity – following the establishment of the Capital Stock Exchange, there was a room to raise capital from public sources. The idea for public funding was conceptualized before the establishment of the Capital Stock Exchange. As noted in the case, the establishment of the community bank involved over the counter shares and thus listing was ideal.
2. The fact that there was an increased demand for the services provided by the bank and thus need for expansion, which requires capital. This may be indicated given various options which were taken by the bank to increase their bank capital to meet the economical capital needed to meet the demand for the services.
3. Opportunity to involve other strategic partners and individuals who were customers of the bank. This was successful given that the same owners would have become customers of the bank and thus creating a double advantage to the bank. Already the bank had created a level of confidence to attract any strategic partner. This was also contributed by the fact that the bank was seems to have huge government influence.

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4. Opportunity to use the CSE to publicize the bank– The share prices and quarterly filling, also daily trading results are free publicity the bank and any listed firm can access from being listed.

Why Municipals did not increase their shareholding structure.

1. The need to finance street vendors and other small businesses was resolved to some extent by other private players/ banks and thus there was no such acute need and government intervention following private sector involvement.
2. In late 1990s and early 2000s the government adopted privatization and various reforms in the economy which allowed private sector participation. Some of the government operations were taken by the private sector and thus continuation in the investment in the banking business would have been contrary to this move as stated in the case, during initial capital raising challenges.
3. Investment in the banking business was not in favour of the long term mission and vision of any municipal council which is to provide social services.
4. Public response and confidence on the performance of the bank was impressive after the listing and thus, there was no need for the municipals to be engaged. The bank was listed to become a commercial bank deviating from a community bank which was the initial plan and support by the municipals.
5. Confidence the municipals had on the governance and management of the bank probably has contributed to the success of the bank and municipals to be convinced that the bank can operate successfully.
6. Government policies and regulation regarding procurement and pubic financial management has led the municipals diversify their financial resources and allocations. The development of treasury single account in 2016 was likely to have started long time ago.

Question 6. Comment on CCB Capital analysis trends as presented in Table 2 and Figure 2. What should be done to rescue the company from capital risk? Would you consider to be shareholder of CCB should it consider boosting further its capital?

Suggested Answers/Directions for Discussion:

As it can be indicated from figure 2, the bank's core capital is decreasing. For the 3 years the bank core capital decreased from TZS 31.3 bn to TZS 20.6 bn. This is a decrease of about 1/3rd of the capital in 3 years' period. This creates a capital risk to the bank. Contributing factor to this as indicated is the increase in allowance for credit losses and increase in the non-performing loans which reached 10.1% in 2016. As it can be observed from table 1, this is above the industrial average for the year which was 7.88%.

In order to rescue the situation, from the class reading students can consider outlining:

1. Adoption of sound lending principles by CCB

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2. Principles of Sound capital planning as issues by the Bank of International Settlements (see reading list no. 3) contains the following important fundamental components in capital planning:

(a) Internal control and governance
(b) Capital policy and risk capture
(c) Forward-looking view
(d) Management framework for preserving capital

Thus, future capital planning should take into consideration provisions set by Bank of International Settlement as well as internal or local policies. The students can recall that establishing management team over stayed and they were result of many of the decisions and changes of the banking firm. This has to be controlled in the future.
Considering being a subscriber to CCB? – *This question is critical as CCB is looking for ways to boost its capital following decapitalization and losses.*

There might be varying answers to this question

1. Yes
    a. Being backed up by government institutions and held them responsible to use their bank extensively. However, it was noted the opinion that the owners of the bank including the municipals do not consider the bank as their main transaction bank leaving the bank with limited liquidity. This is due to the Treasury Single account compliance in 2016 as noted in the case.
    b. Based on the area of focus – still street vendors and small businesses – and especially considering those in Capital city has potential for making business given the pipeline of guarantee funds from the Capital city based Municipals. Should CCB develop real solutions to micro and small businesses there is a huge potential market to this area, as the city population is constantly growing.
    c. The possibility that CCB model, and being now a commercial bank with ability to open branches countrywide, could be subscribed by other local government authorities in urban areas given its experience in servicing micro and small businesses in urban areas as well as management of Women and Youth Development Fund, as well as following its extension to other regions, out of the Capital City.
    d. Widening the scope by CCB is an added advantage to diversify its portfolio by attracting both corporate and micro and small businesses clients, and hence mitigating risks arising from serving only a small market niche.
    e. Policy improvement in the market which allows rigorous screening of the micro enterprises looking for the loans such as the National Identity card, SIM card registration and physical address registration.
    f. Good governance structure is assured as the bank is listed with various independent analysts on the performance of the bank. This is far better as only few banks and companies are listed. This gives a room to sell shares in unfavourable conditions and considering that the shares are sold on discount rate from the market price.

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2. No
    a. Performance of the bank has not been convincing enough – based on the analysis presented in question 2. Other aspects include decapitalization of the bank and increasing non-performing loans. Loan administration especially to micro and small businesses clients is one of the core functions of the bank, and with increased NPL this needs to be strengthened.
    b. Frequent changes in policies regarding operations of the local government may affect the bank and thus risky the venture
    c. The government decision on single treasury account – municipals are no longer have luxury to choose transaction banks
    d. Government institutions seem to be politically biased and hence, they lack accountability which will ruin capital and create lower returns to the shareholders.
    e. Further evidence can be drawn from the bank products and charges as compared to its competitors – political interference may drive the bank to charge less or higher than the market rates.
    f. Almost the capital raising strategies have been used by the bank and given its performance may be new investors may not find it a good decision to invest to the bank.
    g. Focusing on micro and small businesses seems not to be profitable venture. The segment is quite competitive not only to the commercial banks but microfinance institutions. Recorded failures of the community banks concentrated on the similar market segment sends bad signals to the investors in this segment.
    h. Government move to consolidate banks may be initiated to CCB and being merged with another government owned bank and hence change of strategy and focus, which may lead to lower profitability and capital gain.

Question 7. What are key management lessons to learn from the case?

1. Establishing a bank takes time and need diversified experts

This can be evidenced by the fact that since the President's directive in 1999, the bank opened its door to the public in 2002. At least more than 30 months passed since then, and it was good for the bank to chart out its strategy. The involvement of the external expert consultant was also important for the success of the bank, its early stage.

2. Banking sector is highly regulated

Banks are highly regulated. Even with the President's directives, the central bank didn't grant a licence freely to the CCB. It has to raise the required capital, by meeting the minimum required capital.

3. Focus is important to business firms including banking institutions

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It can be observed from the case that the bank was prompted to move from one license of operation to another after examining its books. The bank moved from a regional unit bank to a community bank. What drove the bank was the capital base. While the regional bank licence was TZS 750mil in 2002, it was a regional bank. Also the bank was prompted by the increase on the capital base to establish a commercial bank and open branches out of the Capital City. This move might sound good for a growth strategy but also could be lack of focus. This is because the capital base is a minimum required and not an economic capital. Being a commercial bank the bank is prepared to compete with huge established banks in the economy, but remaining a community bank could be a leader in that segment of banks.

4. Proper governance is key

Proper governance is important in the banking business. Initially, the Bank of Tanzania didn't have a vetting procedure for the personnel serving as Board members and managers of the bank. This was introduced in the implementation of Basel II capital regulatory framework. Initially the bank had elected councillors in the board with little understanding of the business of banking. Also the management by Mr. Edward overstayed for about 17 years. Edward left the office when the bank capital was shrinking at an alarming rate. At the same time the bank has extended its activities to other regions and competing with well capitalized banks. It is important for Manager to know the best time to quite. For the Author's point of view, when there is unmatched success is time to quite.

5. Take the opportunity window at right time

The decision to list the bank was quite good for the bank. The Board and Management spotted good time to raise capital through listing in 2008. Also they spotted an increase of share prices in 2012 and offer a discount and rights issue and they increased the paid up capital. Bonus created an advantage for both the shareholders and the bank. For the shareholders, bonus shares increase the number of shares which can be sold at the stock market to the prevailing price and if investor decide so to earn the transformed dividend. The investor would then remain with their initial shares and for the bank it would have raised its capital base. It is not clear whether the current call for the capital boost will succeed given the developments.

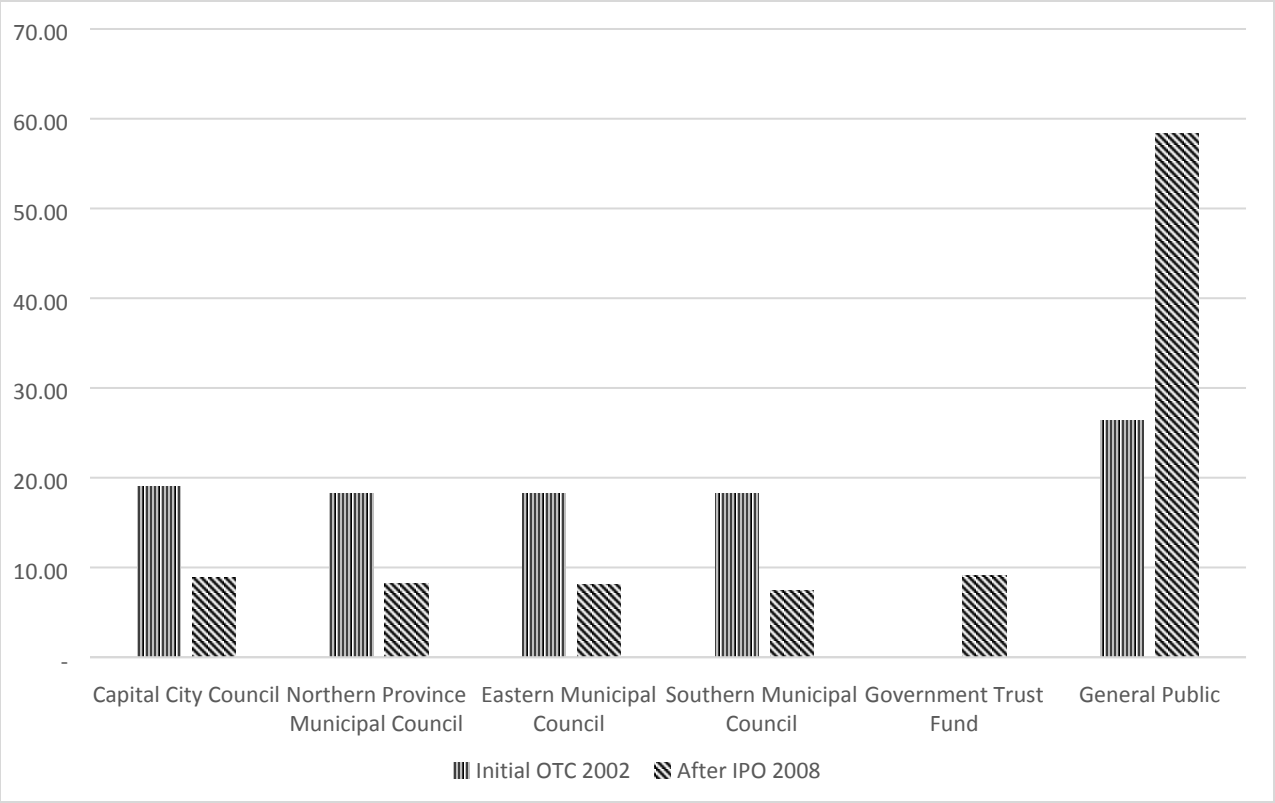
6. Technological and innovation adoption is key for success of banking business

The bank considered taking opportunity of advancement in technology through partnership with other banks for the Automated teller machines, develop the digital products accessible via the internet and mobile phone. This was important for the survival of the bank and institution which do not innovate or adopt the technological advancement they are hardly to survive. However, based on the analysis of the financial statements as presented in question 2, the bank is not utilizing its assets effectively based on ROA. Thus, the bank

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need to introduce more technological solutions. Technology was also used to sell the bonus shares in 2012 to minimize transaction costs associated to the bonus and rights issue of the shares. However, changes of the bank from Community Bank to a Commercial bank drove other costs as the bank was required to undertake rebranding and other marketing related costs.

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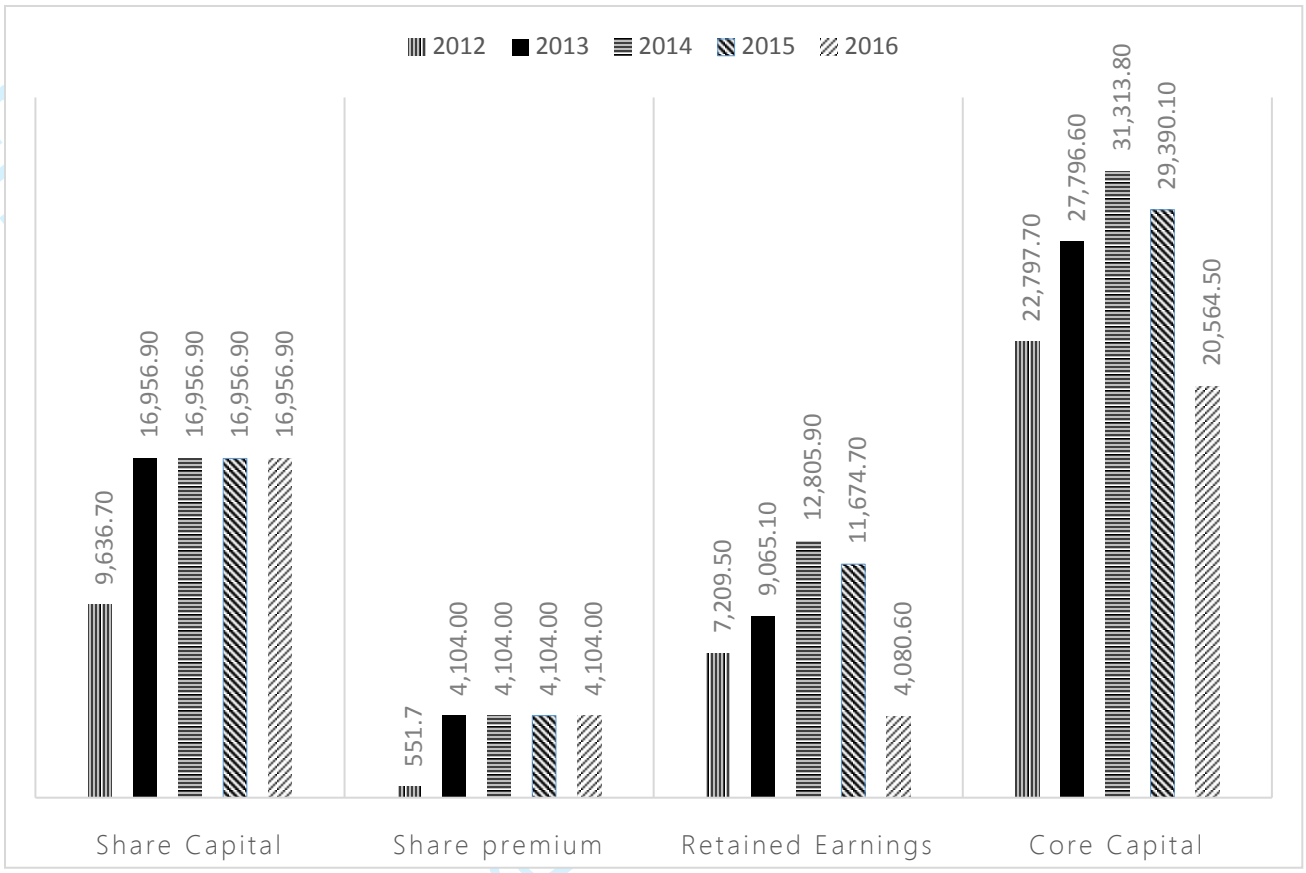
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Subscriber	Before Rights Issues		After Rights Issues	
	No of Shares each TZS 250/=	%	No of Shares each TZS 250/=	%
Municipal Housing Scheme	3,937,555	10.22	7,875,110	11.61
Capital City Council	3,416,047	8.86	6,832,094	10.07
Northern Council	3,178,713	8.25	6,357,426	9.37
Southern Municipal Council	3,125,011	8.11	6,250,022	9.21
Government Trust Fund	2,851,877	7.40	5,714,973	8.43
Eastern Municipal Council	2,863,096	7.43	5,680,431	8.37
Government Insurance Fund	2,000,000	5.19	4,000,000	5.90
Members (4,622)	17,174,492	44.55	25,117,841	37.03
Total Shares (Each @TZS 250/-)	**38,546,791**	**100.00**	**67,827,897**	**100.00**
Total Amount TZS	**9,636,697,750**		**16,956,974,250**	

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Performance Indicator (In Percentage Unless stated)	**2012**	**2013**	**2014**	**2015**	**2016**
Return on Equity (ROE)	8	12	11	9	(10)
Return on Assets (ROA)	2	3	2	2	(2)
Interest Margin on Earnings Assets	11	13	23	22	20
None-Interest Income to Gross Income	11	11	12	14	14
Earnings Per Share (Amount in TZS)	19	55	56	46	(44)
Gross Loans to Customer Deposits	74	76	75	70	82
Non-Performing Loans to Gross Loans	4	3.7	5	7.8	10.1
Earnings Assets to Total Assets	83	81	80	79	78
Growth on Total Assets	18	23	9	8	(6)
Growth on Loans and Advances to Customers	13	16	9	5	5
Growth on Deposits	12	13	10	12	(10)
Tier 1 Capital	35	30	29	26	19
Tier 1+Tier 2 Capital	35	30	30	28	20

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Ratios (All Figures in Percentage)	**2012**	**2013**	**2014**	**2015**	**2016**
Capital Adequacy					
Core capital to total deposit	12.76	13.54	13.39	14.24	16.09
Total capital to total assets	10.52	11.03	11.16	12.03	12.98
Liquidity					
Foreign exchange liabilities to total liabilities	34.36	35.03	35.73	39.73	37.5
Liquid assets to demand liabilities	38.34	36.26	35.93	37.25	35.81
Liquid assets to total assets	33.98	32.39	30.98	30.65	29.04
Liquid assets to customer deposits liabilities	44.82	43.66	41.93	42.52	42.95
Total loans to customer deposits	68.72	71.35	74.33	78.76	86.07
Asset Quality					
Gross non-performing loans to gross loans	8.01	6.43	6.83	7.88	10.27
Non-Performing Loans (NPLs) net of provisions to total capital	22.41	14.26	16.02	18.59	23.56
Net loans and advances to total assets	49.84	50.85	52.89	54.62	55.28
Performance Ratios					
Net interest income to earning assets	7.81	8.25	8.37	8.19	9.18
Non-interest expenses to net interest income	103.41	203.15	99.17	102.87	117.78
Return on Assets (ROA)	2.58	2.55	2.51	2.49	2.09
Return on Equity (ROE)	13.88	13.08	12.64	12.16	9.26
Net interest income to gross income	51.83	52.71	52.99	66.72	52.87
Non-interest expenses to gross income	67.87	67.00	67.24	68.64	62.27
Personnel expenses to non-interest expenses	42.46	43.32	44.29	43.72	44.32
Non-interest income to total income	27.21	25.90	25.17	25.9	23.66
Other measures					
Interest rate paid on deposits (1 year time deposit)	9.93	11.42	10.8	10.8	11.5
Spread (lending rates – deposits rates)	4.06	2.45	3.69	3.06	3.52
Treasury Bill Rates (Annual average)	13.6	14.2	13.6	12.9	16.2

Source: Bank of Tanzania, Directorate of Banking Supervision Annual Report, 2016

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