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Determinants of Commercial Bank Profitability from Prior- to Post-Hyperinflation: Evidence from Zimbabwe

Alphonce Tavona Shiri[1], Silvanos Chirume[2] and Ziska Fields[3]

[1,3]University of KwaZulu-Natal School of Management, M Block Westville Campus, Durban 4001 South Africa
[2]Zimbabwe Open University, Department of Mathematics, 89th Street, Gweru, Zimbabwe
E-mail: [1]<alphshiri@gmail.com>, [2]<skchirume@gmail.com>, [3]<Fields@ukzn.ac.za

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ABSTRACT The main objective of this study was to find out the relationship between liquid assets and profitability of commercial banks in Zimbabwe. Specific objectives were to ascertain how the level of risk associated with liquid assets relates to commercial bank profitability, to determine the impact of working capital on profitability and to find out the extent to which bank capitalisation influences commercial bank profits. A quantitative correlation approach was adopted for the study in which testable hypotheses were formulated based on literature review findings. Eight years historical financial statements data relating to two periods; 2005 to 2008 and 2009 to 2012 was collected from selected commercial banks in Zimbabwe. The study found that working capital was weakly related to profitability, while capitalisation strongly influenced commercial bank profitability. An inverse relationship was found between the ratio of loans to deposits and commercial bank profitability. It was therefore concluded that the composition of current assets strongly influences commercial bank profitability. This study recommends that RBZ should monitor the capitalisation levels of commercial banks and create policies to ensure growth and commercial banks should monitor the structure or composition of current assets in order to ensure profitability.

INTRODUCTION

Liquidity management is critical for the success of a commercial bank. Bordeleau and Graham (2010) maintain that liquidity was one of the main causes for the world financial crisis experienced in 2008. Ibe (2013) agrees that liquidity is the mainstay of success in any commercial bank and there is need for an enterprise to create a liquidity position that is balanced by trimming excess cash and maintaining enough cash to meet short term obligations. (Kramarenko 2010) suggests that while adoption of a multicurrency system in Zimbabwe helped to stabilise the economy, the liquidity crunch that followed hyperinflation period of 2008 negatively influenced commercial banks' ability to make significant returns due to a slowdown in credit facilities and deposits. This implies that, although dollarization helped to maintain the stability of prices and facilitated financial activities, banks in Zimbabwe were faced with an impending liquidity risk situation. According to Madera (2011) liquidity risk entails; the risk a financial institution encounters when meeting the obligations of its financial liabilities, this often arises from the fact that assets and liabilities have different maturity periods. To this point, as withdrawals were due, some of the commercial banks failed to pay clients as a result of cash shortages or liquidity crunch.

The banking system vulnerability was also partly due to the large level of exposure to the financially distressed Reserve Bank of Zimbabwe (RBZ).The Reserve Bank of Zimbabwe held about 40% of banks' equity capital, or "frozen reserves", which other banks could not access (IMF report 2010).

The objective of this paper is to determine the extent to which working capital, ratio of loans to deposits, percentage of loans in current assets and bank capitalisation determine the profitability of commercial bank operations. Insights were drawn from the relationship between risks, associated with liquid assets and how the relationship affects bank profitability.

Background

In relation to the banking industry, Guru, Staunton and Shanmugam (1999) maintain that internal determinants of commercial bank profitability reflect on the differences in bank management policies and decisions regarding the sources and the use of funds. Guru et al. (1999) further assert that, management of induced ef-

fects on profitability can be analysed by examining the balance sheets and the statements of comprehensive income (profit and loss account).Trujillo-Ponce (2012) argues that profitability can be divided into bank specific factors and industry related factors. Bank specific factors such as; revenue diversification, capitalisation, and asset structure, and the other being banking industry related factors such as; industry concentration, economic growth, inflation and interest rates Trujillo-Ponce (2012: 23)states that "a bank holding a low portion of liquid assets (with greater liquidity risk) is more likely to earn high profits. There is a direct relationship between relative percentage of loans in bank assets and profitability, while there is an inverse relationship between liquidity and profitability". The statement above therefore raises a question concerning the character and composition of bank liquidity. While Bhunia et al. (2012) found that excess liquidity impacted positively on company profits, Trujillo-Ponce (2012) suggests that, it is the level of risk associated with liquid assets that has an impact on the profitability of a bank.

When investigating the determinants of bank profitability, Demirgue-Kunt and Huizingha (1999) cited in Husain and Abdullah (2008) found that less profitable banks were those with relatively high non-interest earning assets and banks that relied largely on deposits for their funding. Atemnkenf and Josep (2006), cited in Husain and Abdullah (2008) examined the relationship between the accounting measures of a bank's performance and its profitability. The latter then as a result found a positive effect pertaining to the loan to deposit ratio on bank profitability. These results are therefore contradicting. Some researchers detect a positive and others a negative relation concerning the loan to deposit ratio and a bank's profitability.

Literature Review

The Relationship Between Liquidity and Bank Profitability

Relevant literature was consulted in order to explore the existing interdependence between the liquidity position of a bank and its profitability. Pira (2010) argues that the interaction between liquid assets and liabilities has an impact on the profitability of banks. Pira (2010: 1) states that, "on mid-term and long-term the relationship between liquidity and profitability could be positive, meaning that a low liquidity would lead to lower profitability, due to a greater need for loans and a low profitability would not generate sufficient cash flow to finance the expansion of its needs for working capital, purchase new fixed assets, outstanding loans, etc. And it ends up compromising liquidity, thus forming a vicious circle".

Owolabi and Obida (2012:10) argue that "liquidity requirement of a firm depends on the peculiar nature of the firm and there is no specific rule on determining the optimal level of liquidity that a firm can maintain in order to ensure a positive impact on its profitability" This implies that, commercial bank liquidity can be determined by the nature of a bank's operations. In general banking business and financial intermediation involves the enlistment of funds and the mobilisation of these funds from excess components of the economy and lending out to shortfall units in the form of advances, overdrafts and loans. These functions render banks vulnerable to risks, such as liquidity risk. Amengor (2010), cited in Lartey et al. (2013: 48), states that "liquid risk results from the bank's inability to meet its obligations towards cash to fund its contractual needs as they fall payable. The obligations may include lending and investment commitments and meeting credit drawings in the normal progression of business". This therefore implies that the liquidity position of a commercial bank is largely driven by the nature of its business and is further characterised as the ability to meet all its clients' cash or liquid needs.

A correlation exists between a bank's ability to produce a profit and its ability to generate surplus, that is, generating revenue over and above its costs, relating to the bank's capital base. A well capitalised bank is able to endure negative shocks of an unstable macro-economic environment (Athanasoglou et al. 2005). The researchers on bank profitabilitysuch as Thornton (1992), Demirguc-Kunt and Huizinga (2000) and Goddard et al. (2004), employed linear prototypes to approximate the impact of the various influences that may be vital in order to successfully interpret profits (Lartey et al. 2013).

Velnampy and Nimalathasan (2010) investigated the relationship between the size of a firm and the viability of all the divisions of The Commercial Bank of Ceylon Ltd as well as The Bank

of Ceylon over a 10 year period, reaching from 1997 to 2006. Findings reveal that, an affirmative association exists between the organization's size and the profitability of the Commercial Bank of Ceylon Ltd.

Agarwal (2012) cited in in Bhunia et al. (2012), investigated the relation between liquidity and profitability using the current ratios as well as quick ratios, and then concluded that excess liquidity impacts positively on the profitability of a company. Niresh (2012: 35) upholds that "liquidity refers to the ability of a firm to meet its short term obligations. Liquidity plays a crucial role in the successful functioning of a business firm".

A sufficient understanding of liquidity is consequential to both the interior as well as exterior financial analysis due to the important role played by liquid assets in the day to day running of a business (Bhunia et al. 2012). A fragile liquidity position poses a threat to the credit worthiness and profitability of a company. Low liquid assets positions have an impact on sustainability of business operations and in commercial banks this may threaten survival of the entity. Naresh (2012) argues that liquidity position of a business as evidenced by the level of its working capital is necessary for the business's short term survival but profitability is the mainstay for long term survival.

Teruel and Salano (2007), cited in Bhunia et al. (2012), found that managers in small to medium sized Spanish firms could create value by reducing inventory levels, as well as the number of days that their accounts remained outstanding. However, when looking at commercial banks one would be interested in finding out which elements of bank operations or bank trading, would constitute "inventory". This is due to the fact that banks do not sell final products that are kept in warehouses, but trade in hard cash and cash equivalents. This paper will therefore study the components of a commercial bank's liquid assets.. Current and liquidity ratios will be computed and analysed to find out the impact of the level of liquid assets on profitability.

Credit Risk and Bank Profitability

The banking sector is naturally laden with many risks that have to be jointly managed. This presents a challenge as the activities seem to present opposing needs, such as providing cash on demand to depositors, while simultaneously extending credit and liquidity to borrowers (Cebenoyan and Straham 2004:2 0). Cornett et al. (2010) support this view and maintain that balancing the needs of depositors and borrowers may leave banks exposed and vulnerable to systemic increases in demand of liquidity from borrowers and at the same time result in runs by depositors.

Cebenoyan and Strahan (2004) maintain that, since banks should fill the immiscible role of providing both credit as well as liquidity, the issue of solvency and liquidity is of crucial importance to the industry. Saidenberg and Strahan (1999) argue that, banks hold liquid assets, such as cash and securities, as a way of guarding against unexpected withdrawals by depositors or draw downs by borrowers. This therefore nurtures the need for strategic risk management as banks attempt to balance their role of both providing liquidity, and the need to maximise shareholders' value through reasonable profits.

Salas and Saurina (2003: 208) state that "a bank interested in market share growth is likely to reduce its borrowers' quality levels". Issuing out a large proportion of loans to high risk borrowers may inflate the number of non-performing loans which ultimately affects the bottomline performance of the bank (Salas and Saurina 2003). Athanasoglou et al. (2008) advise that banks should employ a capital buffer technique to address loan issuing and liquidity risk exposure. Demsetz and Strana (1997), cited in Cebe Noyan and Strahan (2004: 23), found that "large banks were able to engage in more lending and holding less capital due to their access to large internal capital markets, whereas small banks' lending activities were affected by changes in cash flow due to shifts in deposit supply". This indicates that larger banks are less risky than smaller banks due to the fact that larger banks have access to more capital, which can act as a buffer against non-performing loans. This statement is supported by Athanasoglou et al. (2008: 123) who suggested that, "bank size was closely related to the capital adequacy of a bank since relatively large banks tend to raise less expensive capital and hence appear more profitable". This implies that capital adequacy plays an important role in mitigating the effects of risky loans and influencing the aggressive lending attitude which ultimately either breeds higher or lower profits, depending on the risk tolerance of a

particular bank. Bikker and Hu (2002), Goddard (2004) concur that a link exists between the bank size and profitability. Dietrich and Wanzenried (2011: 309) also agree that a bank's size influences its profitability. and by putting forward the argument that "larger banks are likely to have a higher degree of product and loan diversification than smaller banks and … benefit from economies of scale".

Trujillo-Ponce (2012) suggests that capital acts as a safety net for commercial bank in case of adverse developments. The latter maintains that capitalisation assists the bank in financing its assets at more favourable interest rates, increasing expected profitability and offsetting the cost of equity, which is considered to be the most costly bank liability in terms of expected return. Athanasoglou et al. (2008:123) argue that "poor asset quality and low levels of liquidity are the two major causes of bank failures". The latter maintain that banks can reduce their risk through portfolio diversification and by raising liquidity holding. While Athanasoglou et al. (2008) continue the portfolio diversification argument, Herrero et al. (2009) state that a larger share of loans to assets should imply an increased interest revenue because of the heightened risk involved. Herrero et al. (2009: 2081) however agree that "poor asset quality should reduce profitability in as far as it limits the bank's pool of loanable resources". Molyneux and Thorton (1992) found a significantly negative relation between liquidity levels and profitability, while Miller and Noulas (1997) came across a positive correlation. These conflicting findings therefore raise the question as to whether capital can be used as a risk buffering strategy.

Bauer and Ryser (2004:332) state that Modigliani and Miller theorem (1959) assumes a perfect world in which "capital structure and risk management decisions are useless as they have no impact on shareholder's wealth". However, Bauer and Ryser (2004: 332) argue that Modigliani and Miller theorem (1959) would hold water only, if there is no debt by saying that such propositions are "ex ante propositions: once debt is in place, ex post financial decisions can alter the equity value by expropriating debt holders in what is known as asset substitution". Therefore it can be said that capital structure is an important element that affects bank profitability. Herrero et al.(2009) maintain capital structure is important for bank profitability and well capitalised banks are able to "make loans with a beneficial return or risk profile, this should imply higher profitability"

The literature mentioned above assisted the researchers in developing the following four hypotheses:

Hypothesis concerning the level of risk associated with liquid assets and bank profitability:

Null hypothesis ($\mathbf{H_0}$): There is no relationship between the levels of risk associated with liquid assets (percentages of loans in current assets) and bank profitability (to be rejected at 5% significance level)

Alternative hypothesis ($\mathbf{H_1}$): There is a strong relationship between the levels of risk associated with liquid assets (percentage of loans in current assets) and bank profitability.

Hypothesis concerning the level of working capital and its relationship to commercial bank profitability:

Null hypothesis ($\mathbf{H_0}$): Position of working capital is weakly related to bank

Profitability (to be rejected at 5 % significance level).

Alternative hypothesis ($\mathbf{H_1}$): Position of working capital has a strong impact on Bank profitability.

Hypothesis concerning the relationship between bank capitalisation and profitability:

Null hypothesis ($\mathbf{H_0}$): The level of bank capitalisation does not have a strong relationship with bank profitability (to be rejected at 5% significance level)

Alternative hypothesis ($\mathbf{H_1}$): The level of bank capitalisation has a strong relationship with profitability.

Hypothesis concerning the ratio of loans to deposits and its impact on profitability:

Null hypothesis ($\mathbf{H_0}$): The ratio of loans to deposits does not have an impact on bank profitability (to be rejected at 5% significant level).

Alternative hypothesis ($\mathbf{H_1}$):The ratio of loans to deposits has an impact on bank profitability.

METHODOLOGY

A quantitative correlation approach was adopted for the study in which testable hypotheses were formulated based on literature review findings. Eight years historical financial statements data relating to two periods; 2005 to 2008 and 2009 to 2012 were collected from selected

commercial banks in Zimbabwe. The profit determinant elements as they are stated in the hypotheses emanate from the literature reviewed and were then analysed using SPSS, version 17.0, in order to determine which variables significantly influence bank profitability.

Data was put into SPSS, version 17.0, for further regression and ANOVA analyses and the following abbreviations were used:

Profit- representing profit before tax.

Easset- representing the equity to asset ratio.

C ratio- representing the current ratio (current assets/current liabilities).

Loan- representing the percentage of loans in current assets.

ldratio-representing the loan to deposit ratio.

FINDINGS AND DISCUSSION

The *first hypothesis* to be tested was on the level of the risk associated with liquid assets and the impact they have on bank profitability. The null hypothesis ($\mathbf{H_0}$) stated that, there is no relationship between the level of risk associated with liquid assets (percentages of loans in current assets) and bank profitability. The alternative hypothesis ($\mathbf{H_1}$) stated that, a strong relationship exists between the level of the risk associated with liquid assets (percentage of loans in current assets) and bank profitability. The results from SPSS, version 17.0, concerning the correlations between these variables are displayed in Table 1. The correlation coefficient between the level of risk associated with liquid assets and profitability was found to be 0.738. The 0.738 correlation coefficient shows a strong positive relationship, therefore H_0 was rejected in favour of (H_1), significant at the level of 0.05. This implies that the level of risk associated with liquid assets has a strong positive impact on bank profitability.

An analysis of the risk associated with current assets in Figure 1, for the duration of 2005 to 2008, represented by 1-4 on the horizontal axis, in comparison to the period between 2009 and 2012, represented by 5-8 on the horizontal axis, revealed that when the percentage of loans in current assets were high, profits realized were also high. During the first period between 2005 and 2008, the percentage of loans in current assets ranged from 8.3 percent as the lowest to 12.4 percent as the highest, and profits were hovering above 10 million, with the lowest being 13.6 million, and the highest 42 million. During the second period between 2009 and 2012, 50 percent of the time, the percentage of loans in current assets fell to below 5 percent, and profits plunged to 0.6 million in 2009 and negative 1.9 million in 2010, only to increase when the ratio began to pick up during 2011. This implies that in terms of the liquidity to profitability relationship, it is the risk associated with liquid assets that drive the profits for commercial banking. Whereas the literature that was reviewed revealed that in other industries, the movement of inventory, and the number of days for which their accounts remained outstanding created excess profits (Bhunia et al. 2012). For commercial banks, it seems to be the composition of the liquid assets that has significance.

The *second hypothesis* test concerned the impact of the working capital position on commercial banks' profitability. The null hypothesis ($\mathbf{H_0}$) stated that the position of working capital

Table 1:Correlations

		Profit	*Easset*	*Cratio*	*Loan*	*Ldratio*
Pearson Correlation	Profit	1.000	.640	.131	.738[0]	-.389
Sig. (2-tailed)	Easset	.640	1.000	-.329	.162	-.431
First Period	Cratio	.131	-.329	1.000	.435	.749
(2005-2008)	Loan	.738[(*)]	.162	.435	1.000	-.240
	Ldratio	-.389	-.431	.749	-.240	1.000
Second Period	Profit	.	.044	.378	.018	.170
(2009-2012)	Easset	.044	.	.213	.351	.143
	Cratio	.378	.213	.	.141	.016
	Loan	.018	.351	.141	.	.283
	Ldratio	.170	.143	.016	.283	.

[*]Correlation is significant at the level of 0.05 (2-tailed).
Source: Research data output computed in SPSS version 17.0.

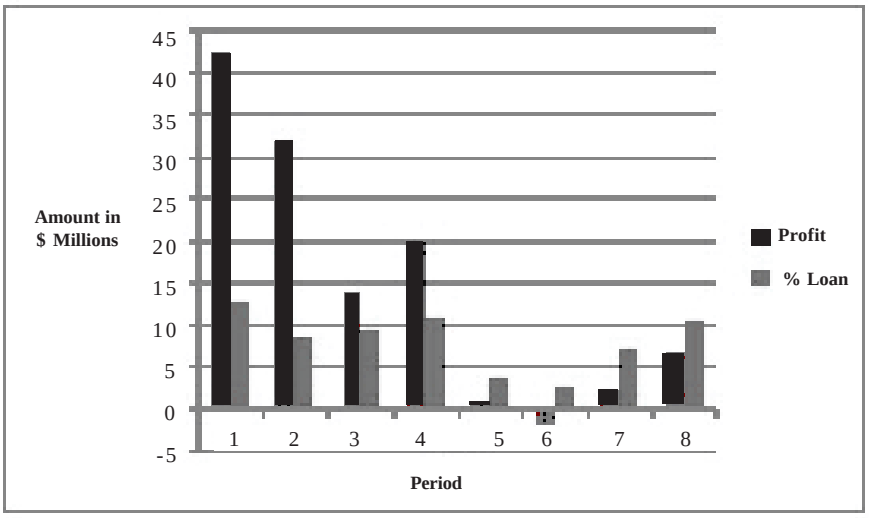

Fig.1. Percentage of loans in current assets (measuring risk associated with current assets) in comparison with profits for two periods, 2005-2008 (period 1-4), and 2009-2012 (period 5-8)
Source: Research data

is only weakly related to bank profitability. On the other hand, the alternative hypothesis ($\mathbf{H_1}$) stated that the position of working capital has a strong impact on bank profitability. According to output, as displayed in Table 1, the output from SPSS version 17.0 shows a Pearson correlation coefficient of 0.13 at the significant level of 0.05. The null hypothesis is therefore not rejected in this case. The output shows lack of sufficient evidence for a strong relationship between the level of bank working capital and profitability.

While in general the relationship between working capital and profitability was very weak with r = 0.131 during the period before the liquidity crisis (2005-2008). The relationship between working capital and profitability however, grew stronger to an r = 0.378 during the post hyper-inflation period from 2009 to 2012. Bordeleau and Graham (2010: 4) state that "liquid assets such as cash and government securities generally have a relatively low return and holding them imposes an opportunity cost on a bank". This makes sense when comparing the liquidity position of the two periods in relation to the liquid asset levels as measured by working capital in this study. The liquid assets, as depicted in Figure 2, show an almost even horizontal line. This illustrates that banks in Gweru were cautious not to hold too much liquid assets during these above mentioned periods.

When comparing the hyperinflation period from 2005 to 2008 as well as the post- hyperinflation period between 2009 and 2012, it would be sensible to conclude that profits were spiralling down as profit margins were reduced due to hyperinflation but liquid assets held were within a range of 5 million to 6 million, working towards an average of 5.2 million. This led to the conclusion that it is the type and the quality of liquid assets that are more significant than the quantity of liquid assets.

The *third hypothesis* was on the relationship between bank capitalisation and profitability. In this case, the null hypothesis ($\mathbf{H_0}$) stated that the level of bank capitalisation does not have a strong relation to bank profitability. The alternative hypothesis ($\mathbf{H_1}$) stated that the level of bank capitalisation does indeed have a strong correlation with profitability. The SPSS version 17.0 output shows a Pearson correlation coefficient of .64 at significant level .05. In this case, the null hypothesis ($\mathbf{H_0}$) was rejected in favour of the alternative hypothesis. This illustrates the strong relationship between bank capitalisation and profitability.

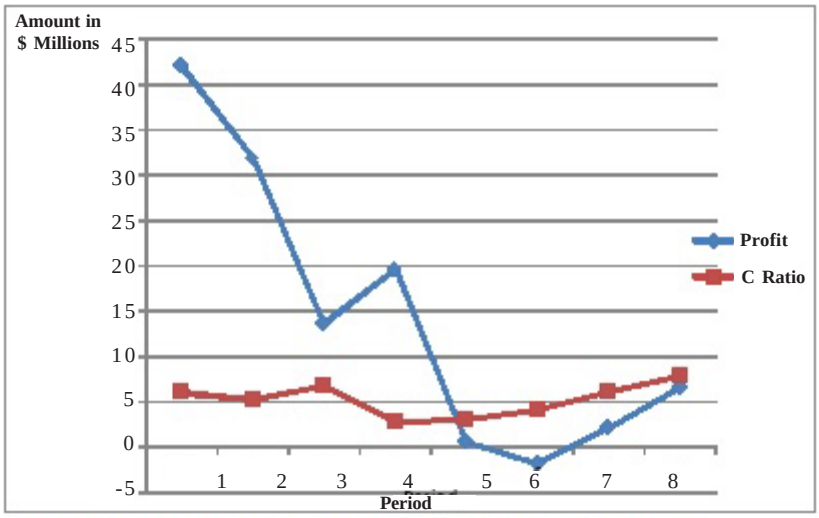

Fig. 2. Relationship between current ratio (measure of working capital) and profit
Source: Research data

Onaolapo and Olufemi (2012: 65) state that the "nexus between capitalization and profitability is particularly pronounced given the significance of business profit as a tool for risk mitigation, business survival, and a sign of successful product development". This conclusion supports the findings that show a strong relationship between capitalisation and bank profitability. Figure 3 illustrates that during the hyperinflation period (2005-2008), in average the con-

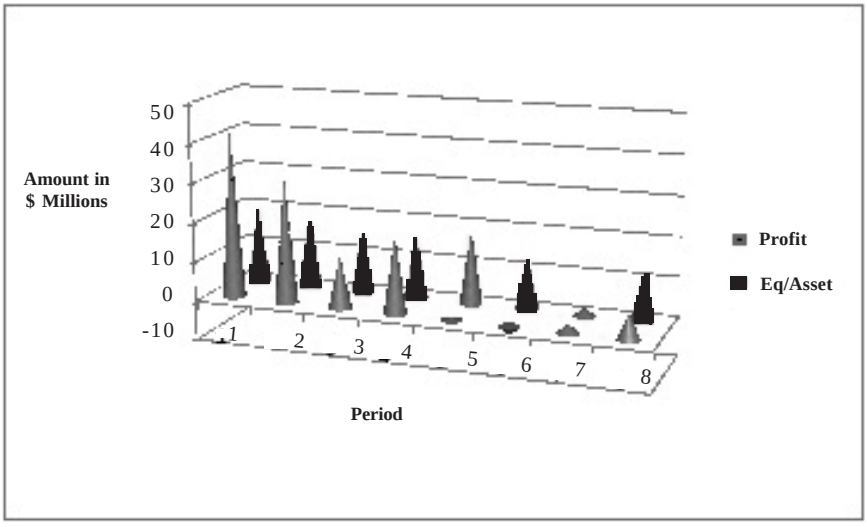

Fig. 3. The relationship between bank capitalisation and profitability, two periods, 2005-2008, (period 1-4), and 2009-2012 (period 5-8)
Source: Research data

cerned banks were highly capitalised and profits were hovering above ten million dollars. During the second period (2009-2012), the capitalisation had decreased and profitability tumbled to below 1ten million dollars, only to start picking up in the 8th period (2012), when the Reserve Bank of Zimbabwe raised the minimum capital requirements. Capitalisation is therefore an important variable driving bank profits and ensuring commercial bank profitability.

The *fourth hypothesis* that was tested involved the ratio of loans to deposits and its impact on profitability. The null hypothesis ($\mathbf{H_0}$) stated that the ratio of loans to deposits does not have an impact on bank profitability, while the alternative hypothesis ($\mathbf{H_1}$) entailed that the ratio of loans to deposits does have an impact on bank profitability. The correlation coefficient of -0.389 indicated that a negative relationship exists between the ratio of loans to deposits, and bank profitability, significant at the level of 0.05.Thus the null hypothesis ($\mathbf{H_0}$) was rejected in favour of the alternative hypothesis ($\mathbf{H_1}$). ,The negative impact implies that an inverse relationship exists between the ratio of loans to deposits and a bank's profitability. However during the period 2009-2012 this relationship was positive but small at r=0.17.

The correlation of -0.389 between the loan to deposit ratio and bank profitability confirms the findings of Demirgue-Kent and Huizingha (1999), cited in Husainr and Abdullah (2008) that less profitable banks rely on deposits for their funding. The results obtained in this paper also reject the findings of Atemnkenf and Josep (2006), cited in Husain and Abdullah (2008), whose findings illustrated a positive correlation between the loan to deposit ratio and a bank's profitability. During the analyses of Figure 4, it was found that during the hyperinflation period (2005-2008), loan to deposit ratios were rising while profits were declining. During the post-hyperinflation period, loan to deposit ratios were steadily high in comparison to the very low profits. The loan to deposit ratio remained inversely related to profitability regardless of the economic climate.

The linear regression equation produced by the SPSS, version 17.0 was:

Y(profit) = Constant + 0.174 (loan) + 0.726 (cratio) + 0.574 (easset) – 0.644 (ldratio). The values of 0.174 (loan), and others were taken from Table 2 on coefficients, under the standardized beta-column. This means that if (loan) is increased by one unit, profit would increase by 0.174, or 17 percent, provided other variables remain constant.

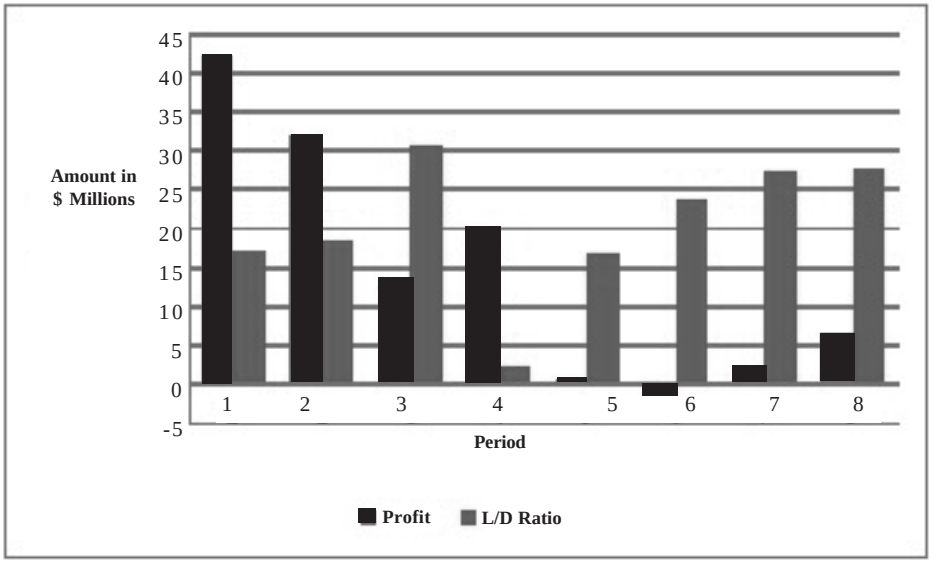

Fig. 4. The relationship between Loan to deposit ratio and bank profitability, for two periods, 2005-2008, (period 1-4), and 2009-2012 (period 5-8)
Source: Research data

Table2: Coefficients[a]

Model		*Unstandardised Coefficients*		*Standardised coefficients*	*t*	*Sig.*
		B	*Std. error*	*Beta*		
1	(Constant)	-55.996	30.351	-1.845	.162	
	Loan	.791	3.767	.174	.210	.847
	Cratio	6.467	10.804	.726	.599	.592
	Easset	3.291	1.517	.573	2.170	.118
	Idratio	-1.124	1.923	-.644	-.584	.600

a. Dependent Variable: profit.

The relationship between the independent variables: easset, cratio, loan, ldratio, and the dependent variable, profit, is summarised by the regression output from SPSS version 17.0 as depicted in Table 2. Per the regression output, R^2 was 0.841, which illustrates that the independent variables strongly explain the dependent variable profit by about 84 percent.

What this entails is that the whole model's independent variables accounted for 84.1 percent of the variability in profit. This model was considered appropriate for the purpose of this paper (Table 3).

Table 3: Regression Model Summary[b]

Model	*R*	*R square*	*Adjusted R square*	*Std. error of the estimate*
1	.917[a]	.841	.630	9.65034

a. Predictors: (Constant), ldratio, loan, easset, cratio.
b. Dependent Variable: profit.
Source: Regression output from SPSS using research data

CONCLUSION

This paper found that when a large proportion of a commercial bank's current assets are non-interest bearing current assets, there is loss of potential profits, thus creating an opportunity cost. Excess working capital should be shaded of as a profit maximisation strategy. The results indicate that the independent variables mentioned, explained 84.1 percent of net profit before tax. These results also stress the importance of the composition of current assets as a way of optimising profitability, for example, the percentage of loans in current assets had a correlation of 0.738, which illustrates a strong positive relationship. It is therefore recommendable that banks should increase the risk associated with current assets as another way of achieving optimal profitability. Since the current ratio showed a weak relationship to profitability, it is further evident that what is of more importance is the composition of current assets rather than creating excess working capital. A further discovery highlights the importance of capitalisation as a way of leveraging profitability. The correlation of capitalisation to profitability was a strong 0.64, indicating an interdependent relationship. Banks can in conclusion optimise profitability by means of careful management of the elements that constitute liquidity as explained by capitalisation, working capital, and risk associated with current assets.

RECOMMENDATIONS

Specific Recommendations Based on Hypothesis

This paper found that the level of risk associated with liquid assets have a strong positive impact on bank profitability. This means that the level of loans issued by a commercial bank does indeed determine its profitability. It is therefore recommended that commercial banks in Zimbabwe issue out loans as a way of maximising their profitability.

It was also found that a weak relationship exists between working capital position and the profitability of commercial banks in Zimbabwe. This correlates with Bordeleau and Graham (2010) who state that maintaining high levels of liquid assets, such as cash, results in opportunity cost for commercial banks.

It is further recommend that commercial banks should be highly capitalised due to the fact that this paper found a strong relationship between bank capitalisation and profitability.

This result confirms the capitalisation argument presented by Onaolapo and Olufemi (2012), who argue that capitalisation is not only a risk mitigation tool but also a necessary requirement for commercial banks in order to grow exponentially and profitably.

Additionally it is recommended that commercial banks should not rely on deposits to fund their operations, seeing as it was found that an inverse relationship exists between the ratio of loans to deposits and profitability.

Recommendations to the Zimbabwean Banking Community and Stakeholders

Role of the Reserve Bank

The results of this study illustrate a strong existing relationship between capitalisation and bank profitability. The recommendation is therefore made that the Reserve Bank of Zimbabwe monitor the capitalisation levels of commercial banks and create policies to ensure growth, stability and protection of both depositors' and investors' interests. The RBZ has to remain vigilant when monitoring vulnerable commercial banks by enforcing minimum capital requirements and strengthening the monitoring of bank credit risk.

Role of Commercial Banks

The results produced during this study revealed that the composition of current assets significantly influences commercial bank profitability. Bank managers should therefore constantly monitor the structure or composition of current assets by shedding excess cash and investing in interest earning assets, such as issuing loans to clients.

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