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# Drivers of Deposit Mobilization in Private Commercial Banks of Ethiopia

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**Abstract:** Deposit mobilization is a deep-seated part of banking activity. Banks have a decisive implication in enlightening economic efficiency by creating channel between lender and borrower via transferring funds from resource surplus unit to deficit resource unit that have better productive investment opportunities. Therefore, it is indispensable to examine the drivers of Commercial banks deposit mobilization in Ethiopia. To conduct the study, the panel data type from 2010-2019 has been used. Also, for this study the fixed effect model with the application of some diagnostic tests like langragian test, hausman test, unit root test heteroskedasticity test and autocorrelation tests have been used. The data has been analyzed by the descriptive and econometrics analysis. The descriptive analysis of the study shown that the average rate of commercial banks deposit mobilization in Ethiopia in the last nine subsequent years was growing by 9.7 percent and the rate of growth of branch expansion growing by 1.413 percent. In general, inflation rate rate of risk, the rate of return to asset, and Liquidity ratio altered by 137, 0.39, 0.31&0.003 percent, respectively. The result of fixed effect model indicates that, among seven explanatory variables four variables such as government expenditure, interest rate, and return on asset positively and significantly affect at 5% and 10% deposit mobilization but inflation rate is statistically and negatively affected deposit mobilization at 5% level of significance. Given the result of the study, the following recommendations have been forwarded: the responsible agent shall be increase government expenditure of infrastructure, increase interest rate and decrease inflation rate to raise deposit mobilization in Ethiopia.

**Keywords:** Commercial Banks, Deposit Mobilization, Fixed Effect Model

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## 1. Introduction

A vigorous banking system is the backbone of the development and stability of any economy of the world. This has made controllers to all globe economy in order to firms undertaking financial decision makings in its institutions. Savings and investment have an imperative implication in enhancing and promoting economic growth of any country. Adopting saving habit of individuals considered as the center of investment resources of the country, and it is indispensable to recording steady economic development and growth. Amplify of the savings will escort to the capital accumulation which will at last lead to the economic growth [1].

Depending upon the nature of deposit, funds deposited with in banks also bring in benefits as returns of asset. The higher interest rate set by the bank for savers could be motivated the customers are to deposit more resource in the

bank. Banks in turn, accept money from the customers and lend it to the borrowers [2].

In the entire economy, the financial systems where consisted the Bank-based system which stipulated and monitoring of investments fund in the banks and investors through which directly encounter ownership of securities. Banks play aliaison role of mobilizing funds from savers and afterward lend them to investors- individual/corporations.

Banks have a critical implication in enlightening economic efficiency by creating channel between lender and borrower through transform funds from resource surplus unit to those who have better productive investment opportunities. Besides, lending is the most important purpose of commercial banks- evidenced by the amount of loans that comprise banks' assets and the yearly substantial increase of loan which is granted to borrowers both to private and public sectors of the economy [3].

Deposit mobilization is an imperative factor to grooming the basis of the bank's profitability and it is considered as one integral constituent to serve the banks sustainable growth effectively. Moreover, it has an important role in providing adequate service to different sectors of the economy in order to achieve their esteemed goals. The victories of the banking institutions are greatly dependent on the deposit mobilization. As far as the Performances of the bank depend on deposits and it is as the whole considered as a cost effective source of working fund. The endurance of banking industry highly depended on the deposits acceleration. Deposits for commercial banks are extremely crucial for their expanded continued existence [4].

In Ethiopia, commercial banks are the main actors of the financial system by performing financial intermediation through ought the structural change of sartorial economy. The contribution of commercial banks in Ethiopia is going to be very huge and they direct the largest share of investment funds from domestic deposits. Also, each of the domestic investments was held based on the banks finance offered to the investor. That is why the conventional banking business of supplying funds to the economy is immobile of significance. For instance, the majority business organizations particularly in Ethiopia are tremendously reliant on bank loans as a source of capital but the capability of banks providing loan depend much on the commercial banks ability to deposit and their strategies and activities undertaken to achieve the optimum level of deposit. Even though, mobilizing deposit is the chief activity of all commercial banks, managing and identifying the determining factors of deposit is a compulsory task for banks. Mobilizing deposits is not possible without knowing and controlling the deterministic factors [5]. Therefore, now a day in Ethiopia, the pace of the banking system to mobilize adequate resources would not be enough, given the large fund requirement of the economy that would unquestionably result in liquidity gap. The major causes for liquidity gap are money may be reserved in accustomed way and preponderance of population is unbanked. This directs that the deposit mobilization carry out among commercial banks in Ethiopia is not well developed. So this type of traditional banking practices should be barren and replaced by the new and relevant deposit mobilization strategy. Knowing such latest strategy is fundamental to scale up the current deposit mobilization pains and it enforces this study to be undertaken. Having this fact, the manuscript has been achieved the following objectives: to Examine effects of internal factors on Bank profitability on deposit mobilization of Commercial banks in Ethiopia and to Examine effects of external factors that affect the deposit mobilization of Commercial banks in Ethiopia.

## 2. Literature

The intensity of Commercial Banks deposit is reliant on savers' money as a basis of funds. As per the Keynesian theory of demand for money, three motives are there that

reflect why people hold money such as transactions, precautionary and investment motives. In order to accommodate these intentions, commercial banks proffer three classes of deposit amenities such as demand, savings and time deposits. The first deposit facility is most frequently pass on to as current account and is intended for those who require money for transaction motives. This motive demanded from the perspective of consumers who desire income to meet their household expenditure. It may hold by businessmen while they want to grooming and expanding their business activities. Therefore, the rationales of deposit apparatus are for expediency or for assembly daily dedications. Bank deposits stand for the most noteworthy apparatus of the money supply used by the public, and adjust in money growth are extremely allied with alteration in the prices of goods and services in the economy [6].

Bank deposits are all set to deposit accounts at a banking institution, such as savings accounts, checking accounts, time deposit accounts and money market accounts. The account owner has the right to take out any deposited funds, as set forth in the conditions and circumstances of the account. The "deposit" itself is liability allocated by the bank to the saver and refers to this liability rather than to the real funds that are deposited [7].

There is a direct affiliation between income and deposit. That means when the income of the society raise, the level of commercial banks deposits also raise. Gorgeous services in the bank optimistically manipulate the intensity of banks deposits and thereby uplift the rate of growth of bank deposits via boosting rate of saving. This affiliation exists among the two variables enable to direct the degree to what the extent economic growth escalating as rate of saving is increased significantly. To what extent the deposit growth rate is increased, the public would have more valuable direct over the allotment of financial resources for well-designed motives. In this regard, transaction overheads also significantly determine the level of banks deposits in which the lower transaction cost is an important pointer of management's effectiveness in a bank [8].

Banks as any extra business organizations can amass resources in the form of debt and equity. In the language of banking, increasing equity is more costly than attracting deposits. Also, when the lending channel well constructed growth of deposit enables to augmenting the supply of loans as a result of looking additional source of financing for banks. When a commercial bank produces a deposit by lending to a business man, it is evidently executing a function for which it is permitted to a return in the form of interest payments [9].

Banking sector financial reliability has a fundamental role in the insurance warehouse consumers and as well as to the company stockholders since this will permit to defend the policyholders against any possible fail to pay and determine the volume of policies an insurance company writes. Considering that there is a inflexible market competitor in insurance maneuvers and release financial regulations, several Non-life insurance companies devote cash income to

refuge underwriting loss from investment profit resulting from cash-flow underwriting. This policy is successful specially when the investments steady [10].

Financial institutions play key role in the development process by relocating funds from superfluous units to discrepancy units within the economy. The outlay of their procedures is very significant to the effectiveness of the financial intermediation process. Financial markets are allocated resourcefully when they channel surplus resources to the most industrious and lucrative uses. They further distinguished that if the intermediation outlays of allocating resources from investors to users are low then, the markets are depicted as operationally proficient. Financial intermediation costs indicates to the widen between the gross expenses of borrowing and the net returns on lending [11].

### 3. Methodology

To conduct this study basically the explanatory research design with panel data type have been employed from 2010-2019. The study focused on the whole private commercial banks of Ethiopia. The data were retrieved from the national bank of Ethiopia data source, Annual Reports and Accounts, and national statistics agency. To select the targeted population of the study, the simple random sampling method would be applied. In this study the panel data model specifically the fixed effect model has been used through Applying the hausman specification model to identify whether the fixed or random effect model is more efficient model. As a result, the fixed effect model of the regression model can be specified as follows

$$Y_{it} = \alpha_i + \beta_{xit} + e_{it}$$

Where,  $y_{it}$  is the dependent variable which represents bank mobilization,  $\alpha_i$ , individual heterogeneity, vector of

explanatory variable and  $\beta$ , vector of parameters and  $e_{it}$  error term at time  $t$ .

In this equation the following points are taken as informative assumption, whereis individual difference or unobserved effect. The data has been analyzed by decretive analysis tools such as mean, maximum and minimum and inferential statistics correlation and regression analysis technique.

## 4. Result and Discussion

### 4.1. Descriptive Analysis of the Study

In this segment of the study, the researcher strives to analyze and discuss findings of the study by using summary statistics. As stated earlier the data were retrieved from the National bank of Ethiopia database. Furthermore, in this study results confirm a detail description of factors that impaired examine the drivers of commercial banks deposit mobilization in Ethiopia. As long as different banks in Ethiopia inclined by various factors, the commercial banks deposit mobilization was dissimilar in the last subsequent nine years. However, the detail of this exploration can be elaborated in the following bar chart stated below.

Table 1. Summery statistics of dependent and explanatory variables.

Variable	Obs	Mean	Std. Dev.	Min	Max
LnDEPM	99	9.274	1.554	5.472	13.7
LnBEP	97	1.413	.781	-3.014	1.922
lnGOVEXG	99	12.088	.707	10.393	12.931
LnCRISK	99	-.395	1.122	-2.865	4.286
INF	99	.137	.093	.011	.38
ROA	99	.031	.04	-.021	.41
LIO	99	81463.485	810543.93	.383	8064811
INT	89	.003	.007	0	.02

Source; computed from stata 15 package result.

Table 2. The robust fixed Effect Model regression result.

lnDEPM	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]	Sig
lnBEP	-.04	.075	-0.54	.6	-.209	.128	
lnGOVEXG	.904	.192	4.71	.001	.47	1.338	***
lnCRISK	-.008	.055	-0.14	.893	-.133	.118	
ROA	3.065	1.311	2.34	.044	.1	6.03	**
INF	-1.758	.785	-2.24	.052	-3.533	.017	*
LIO	0	0	-1.65	.134	0	0	
INT	22.392	7.278	3.08	.013	5.927	38.856	**
Constant	-2.779	2.151	-1.29	.229	-7.645	2.087	
Mean dependent		9.245	SD dependent var			1.533	
R-squared		0.665	Number of obs			97.000	
F-test		.	Prob > F			.	
Akaike crit. (AIC)		178.813	Bayesian crit. (BIC)			194.261	

\*\*\* p<.01, \*\* p<.05, \* p<.1

Source; computed from stata 15 package result

Note; \*\*\* p<.01, \*\* p<.05, \* p<.1 represents the level of significance of explanatory variables on dependent variable at 1%, 5% and 10% level of significance.

The average rate of commercial banks deposit mobilization (lnDEPM) in Ethiopia in the last nine subsequent years was growing by 9.7 percent with the maximum value of 13.7 and minimum value of 5.427 percent, respectively. This shows that, the average growth of the deposit mobilization in the

commercial banks of Ethiopia was spectacular. The departure of the mean from the actual growth of deposit mobilization in the last years was only 1.554 percent. The other important variable that admitted under this thesis is the commercial banks branch expansion (lnBEP).

In Ethiopia, in the last consecutive years the rate of growth of branch expansion growing by 1.413 percent, which was not as such dramatic. The rate of government expenditure growth in Ethiopia which was layout for capital investments in the last subsequent years were increasing by 12 percents. This show that, the level of capital which is invested for facilitating public utilities in Ethiopia was increasing at alarming rate.

The variable is inflation rate (INF) which shows 0.137 percent increment of inflation in Ethiopia in the last nine years. But the rate of risk in Ethiopia which rises in commercial banking decrease by 0.39 percent. This indicates that, the degree of risk related to credit repayment in commercial banks of Ethiopia was reduced by 0.39%percent. In the last nine subsequent years, the rate of return to asset (ROA), interest rate (INT) and Bank Liquidity ratio (LIO) were increase by 0.31 percent, 0.003 percent and 81463 birr, respectively.

#### **4.2. Econometrics Result of the Fixed Effect Model**

Based on the above, econometrics result the discussions are stated as follows;

Branch expansion (lnBEP); to achieve the same level of deposit, the largest numbers of banks are more capable to generate more of deposit than smaller banks. This can be generated from the rapid branch expansions trough economic of scale create strong network made [12]. But unlike to the result of the study conducted before, in this study the rate of branch expansion (lnBEP) is negatively affect the rate of deposit mobilization in commercial banks of Ethiopia. That means, it is statistically insignificant at all level of significance, because the P-Value of the branch expansion is greater than 0.05 ( $0.6 > 0.05$ ).

Government expenditure (lnGOVEXG) is refers to the entire layout which are made by the government to facilitate the public utilities like health, education, administration and etc. In Ethiopia, the usual government expenditure made by the government at regular time interval. These expenditures were used for expand the level of infrastructure and these in turns assist the instantaneous change in banking activities.

According to [13] study conducted in the Indian confirmed that “saving is the engine of growth. The result indicates that, Expenditure that creates jobs ensures regular income and savings, and it in turn; lead to increase deposit of commercial banks. Also, government expenditure assist to increase the level of banks deposit through generate regular income. The results of this study confirm the result of [13, 14]. The rate of government expenditure is statistically and positively significant at 1% level of significant. The p-value 0.001 is less that the 0.01 level of significant. The result interpreted as when growth rate of government expenditure increase by one percent the rate of banks deposit mobilization increase by 0.904 percent.

The fact why government expenditure directly and significantly affects saving mobilization is due to swift increase in public expenditure in order to augment and facilitate the basic infrastructure that enables to facilitate the main operations of the banks in Ethiopia. An expansion of public infrastructure at the favor of various economic sectors would have a spillover effect to increase source of income and help to the banks raise their costumer. Government

expenditure also has its own benefit to uplift the various opportunities that can increase the livelihood of the society and investment expansions in the economy. This effect automatically results to increase the income of society and their capability to save. Hence, increase expenditure indirectly increase saving mobilization.

Credit Risk (lnCRISK) it examined that, “institutional authority, possession and status of the financial institutions are the key factors for champion of deposit mobilization. Proceeding to giving intentional deposit services, Financial Institutions must assurance that they have the institutional structures that authorize them to mobilize savings publicly.

“Institutional capacities necessitate that adequate governance, management, staff and operational structures that can guarantee the financial securities. As the financial institutions are more guaranteed as regards of risk the degree of deposit mobilization can be increase at sustainable rate. In this study, rate of risk is negatively associated with banks deposit mobilization. But, it is not statistically significant at all level of significant because the p-value is at minimum greater than 10%level of significant.

Profitability (ROA); - it can be measured by return on asset (ROA) and return on equity (ROE. Profitability accounts for the end product of superior financial reliability on the bank risk bearing capacity and on their capability to execute liquidity conversion. In the aspire of this study, the proxy of profitability is return on asset that used to quantified the entire financial performance of banks. It can be determined as the ratio of net profit after tax to total Asset and it has a positive effect on deposit mobilization [15].

Results of this study confirmed the empirical result of [15] thereby the level of return to asset which is proxy of profitability is positively affiliated with deposit mobilization in commercial banks of Ethiopia. The proxy of profitability which is return to asset (ROA) statistically and positively related with deposit mobilization. It is statistically significant at 5% of level of significance. The result interoperated as, when the rate of return asset (profitability) increase by one percent, the rate of saving mobilization increase by 3.065 percent. Reasons for the positive effect of return to asset on saving mobilization is that, an increase the rate of profit in the investment of banks result to shareholders become more eager to uplift the level of deposit andthe level of loan borrowing to the investor. This investment has a positive effect on increase income level of the society and interest return of the loan. These finally support to encourage deposit mobilization.

Inflation (INF) the consistence increase price level represents inflation. This may resulted from either in cost related and demand related factors. As [10] explained inflation is measured alternatively by Consumer price index. The result confirms that inflation has a diverse effect on income and saving level for more of risk adverse persons. Also, [16] conclude that inflation can influence saving through its impact on real wealth. Likewise, the result of the above scholars, result of this study verified that inflation rate negatively affiliated with banks deposit mobilization. It is statistically significant at 10%level of significant because the

P-value (0.052) is less than 0.01. This interpreted as, when inflation rate increase by one percent, the rate of deposit mobilization decrease by -1.758 percent. Inflation rate is negatively affected deposit mobilization of banks. This is because of that inflation can be deterring the purchasing power of consumer and the capability of saving. These effects decrease the society's ability to save and interest to save in the bank again, this result to decrease the rate of deposit mobilization.

Bank's Liquidity ratio (LIO) Managing liquidity is a daily procedure requiring bankers to examine and scheme cash flows to ensure adequate liquidity is maintained. Maintaining a balance between short-term assets and short-term liabilities is critical. Bank liquidity can be measured with different liquidity ratio. For the purpose of this study, Total loan and advance to deposit liquidity ratio is used. But it is not statistically significant at all level of significant.

Interest rate (INT) According to [17, 5] research supposed that, a decrease in real interest rate could increase true demands for money. Therefore, the result postulated that, interest rate and deposit of the banks have positive relationship. In line with the result of the above scholars, result of this study confirmed the positive effect of interest rate on banks deposit mobilization. As real interest rate increase the households demand for holding money become decrease and the level and interest to save can be increase. The combined effects of these factors result to increase saving mobilization of banks in Ethiopia.

## 5. Conclusion

Rapid economic growth in Ethiopia resulted from expansion of financial system. This swift spreading out of financial system rendered a fundamental role to realized basic structural change in the economy through expanded commercial banks and micro finances. Flourishing Bank-based system economic strategies rally round to raise public and private investments that reshape the economy through create employment opportunity in national economy over its source of fund contributions.

Deposit account is a savings account, current account or any other categories of bank account that allows money to be saved and withdrawn by the account holder. These transactions are recorded on the bank's books, and the resulting balance is recorded as a liability for the bank and represents the amount owed by the bank to the customer. In Ethiopia almost all banks may charge a fee for this service, while others may pay the customer interest on the funds deposited. The account holder has the right to withdraw any deposited funds, as set forth in the terms and conditions of the account. Nonetheless, as result of different studies stated that, deposit mobilization affected by different factors.

Hiving this fact, this study conducted on drivers of commercial banks deposit mobilization in Ethiopia. The descriptive analysis of the study shown that the average rate of commercial banks deposit mobilization (LnDEPM) in Ethiopia in the last nine subsequent years was growing by 9.7

percent and the rate of growth of branch expansion growing by 1.413 percent. In general, inflation rate (INF), rate of risk, the rate of return to asset (ROA), and Liquidity ratio (LIO) altered by 137, 0.39, 0.31&0.003 percent, respectively. As the robust fixed effect model result shown, among seven explanatory variables admitted in the model, four explanatory variables such as government expenditure return on asset, interest rate and inflation rate are statistically significant. The first statistically significant variable is government expenditure which straightforwardly affected the rate of commercial banks deposit in Ethiopia. In this study interest rate (INT) and return to asset (ROA) directly positively and statically affiliated with rate deposit mobilization whereas inflation rate is statistically significant but it is negatively affiliated with deposit mobilization. In increase government expenditure, return on assets, interest rate has a positive effect on increment of deposit mobilization of commercial banks in Ethiopia. This because of that the, increase public infrastructure through government spending enables to increase saving interest though increase public facilities that can grooming deposit mobilization. An increase interest rate and return on asset positively affiliated with the deposit mobilization of banks. But, an increase inflation rate negatively affected the deposit mobilization through initially affects the purchasing power of the society. Given the results retrieved from econometric regression and descriptive analysis of this study, the researcher forwarding the following pieces of recommendations as follows: To increase the rate of deposit mobilization in commercial banks of Ethiopia, the managers and the share holder of the bank should increase the return of assets through increase the effective service provision, to expand the rate of deposit mobilization of banks the government should expand the public infrastructures to the extent that can accelerating the rate of saving mobilization in Ethiopia and Finally the central bank shall be set the higher interest rate that can motivate the interest of societies to saving.

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