THE ACHIEVEMENTS AND CHALLENGES OF UGANDA' S FINANCIAL SECTOR

SPEECH DELIVERED ON THE OCCASION OF THE OFFICIAL OPENING OF THE NEW HEADQUARTERS OF ORIENT BANK LIMITED

BY

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Honourable Ministers,
Your Excellencies the Ambassadors, High Commissioners and other members of the Diplomatic Corps,
Honourable Ministers,
Honourable Members of Parliament,
The Managing Director, Orient Bank,
Distinguished Guests,
Ladies and Gentlemen,

We are here today to witness the opening of the new Headquarters of Orient Bank Limited and its main branch. This institution has registered remarkable growth since 1993 as a result of hard work by the Board, management and staff of the Bank, as well as the confidence of the Bank's clients.

As a result of the reforms introduced within the Government's Economic Recovery Programme, and the hard work of the players in the financial institutions, a stronger financial sector has emerged. This is reflected in various financial sector indicators. Private sector deposits for example, increased from 5.3 percent of GDP in December 1992 to 16.3 percent of GDP in December 2001. Over the same period, the total assets of the banking system rose from the equivalent of 12.2 percent of GDP to 25.9 percent of GDP. There has also been increased financial deepening as measured by the M2 to GDP ratio, from about 7 percent in 1986/87 to 12.3 percent in 2000/2001. This is impressive growth.

The conducive liberalised environment has also enabled banks to introduce new products such as cards (debit and cash), Automatic Teller Machines (ATM), and specially packaged accounts to attract savers. Other innovations include the establishment of Corporate divisions or special service centres to serve Corporate customers. Most of these innovations have been possible with the advancements in the technology available. Technological advance has also facilitated links amongst various branches of one bank, thus realising faster and better service to the banks' customers.

Improved risk assessment together with increased loan recovery efforts have led to a reduction of non-performing assets from more than 50 percent in June 1995, to 5.1 percent in March 2002. Prime lending rates have followed a general downward trend in response to our bold financial sector reforms and sound macroeconomic policies. At the end of June 2001, the prime rates ranged from 15 percent to 23 percent. The range has declined between 11 percent and 18 percent as at the 30 June 2002.

The prudential and regulatory framework which is essential to ensuring prudential behaviour of financial institutions was strengthened by repealing the Banking Act 1969, and replacing it with the Financial Institutions Statute 1993. In addition, new prudential regulations to bolster minimum capital requirements were effected in January 2001 requiring commercial banks to raise paid-up capital to shillings 2, and the credit institutions to shillings 1 billion.
Government and the Bank of Uganda have recognised the need to close loopholes and to remove the remaining weaknesses in the regulatory environment. In this regard, Government will, in the near future, table in Parliament, the Financial Institutions Bill 2002. A major provision in the bill is

a set of mandatory and prompt corrective actions by Bank of Uganda on distressed financial institutions.

In addition, a bill to govern the regulation and supervision of micro-finance business in Uganda will very soon be tabled in Parliament. The aim of the Micro Deposit-Taking Institutions Bill 2001 is to ensure that micro-finance business is conducted in a safe and sound manner conducive to the orderly growth of the financial sector.

An important challenge in the conduct of monetary policy undoubtedly remains the need to improve Commercial banks' response to Central Bank's policy signals. While we note the recent decline in the prime lending rates, we still very concerned about the wide intermediation margins. We therefore, urge banks to become more efficient, and to reduce the lending rates even further. High lending rates are a constraint on the real sector of the economy.

Although the monetisation of the economy is increasing, the levels are still low, and reflect the fact that financial deepening, broadening and development continues to face serious challenges. There is need to spread banking services further into the rural areas.

While we welcome the increased use of technology and the growth in financial innovations, there is a challenge in terms of preparing the sector for the implications of increasing globalisation, dollarisation and yet further improvements in technology in financial markets. On our part, we shall endeavour to develop the requisite supervisory and regulatory skills, while we expect to have well capitalised and managed financial institutions to face up to the challenges presented by increasing globalisation.

There is also the need to attract new players into our financial system so as to enhance dissemination of know-how, and new technology, and new types of institutions such especially merchant and investment banks.

The payments and settlement system in Uganda is being improved. This will involve the introduction of new financial products by the banks, improvement in the clearing systems, widespread automation of the banking system, and linking more rapidly the national payments system, as well as improving the outreach for both the users and promoters of financial services.

Globalisation has enhanced the transmission of external shocks to domestic economies. However, integration into the world financial system has also provided better opportunities for both private and public sector to use market-based hedging tools. Risks will always exist, and the challenge for our financial institutions is not only to take advantage of such tools but also to enhance their risk managerial skills, and to develop forward markets and instruments to hedge against risk. Crises are endemic to a capitalist system; they will never be completely eliminated. The important point is to strengthen the financial system so that it is less prone to crisis and so that whenever a crisis does occur, the resultant damage to the financial sector and to the real sector of the economy, is minimised. When banks are not prudently run, not only do they allocate resources inefficiently, they also expose themselves to losses at the lightest whiff of market turbulence. That is why the Bank of Uganda is determined to ensure that we insulate ourselves from external shocks by adopting prudent monetary policies and a credible exchange rate regime and a well capitalised, efficient and transparent financial system.

In conclusion, I would like to congratulate the management and staff of Orient Bank upon yet another milestone in the growth and development of the bank. The relocation of your main branch and headquarters in more spacious premises will no doubt go a long way in improving the services rendered to your clientele. We note with gratitude the introduction of a number of new products at Orient Bank

It is now my pleasure to open the Main branch and Head office of Orient Bank.

KAMPALA
16 July 2002