

BANK OF UGANDA



BANK SUPERVISION FUNCTION

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1.0.0 GOVERNOR'S REVIEW

The financial sector continued to be strong and resilient. Public confidence in the banking sector has increased as indicated in the rising level of total deposits. Total deposits at banks grew by Shs.158bn from Shs.1,325bn in December 2000 to Shs.1,483bn by December 2001. At the same time, banks total assets increased by 10.5% from Shs.1,845bn to Shs.2,038bn, while the ratio of non-performing assets (NPA) to total advances declined from 9.8% to 6.5%. The total assets (less administered loans) of credit institutions increased by 26.3% from Shs.47.5bn to Shs.60.0bn. Deposits amounted to Shs.44.6bn (including agency deposits at Shs.16.5bn), up from Shs 33.5bn (including Shs 13.4bn on account of Agency funds. The level of NPA to total loans in non-banking financial institutions increased from 11.0% in 2000 to 15.8% in the year 2001 due to tightening of the standards for classification of assets in line with the Basel standards to 90-180 days, 180-365 days and 365 days and above for substandard, doubtful and loss categories respectively.

Financial innovation is also evident in the financial sector. Banks have been able 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 creation of corporate divisions or special service centers to serve corporate customers. These developments are indicators of the increasing sophistication of the financial sector and the readiness of financial service providers to meet customers' needs.

While Bank of Uganda welcomes 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. Bank of Uganda shall endeavour to develop the requisite supervisory and regulatory skills while we expect to have well-capitalized and well-managed financial institutions to face up to the challenges presented by increasing globalisation.

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 the private and the public sectors to use market-hedging tools. Risks will always exist and the challenge for financial institutions is not only to take advantage of such tools but also to enhance their risk management 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 system and to the real sector of the economy is minimized. 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. Bank of Uganda is therefore determined to insulate the economy from external shocks by adopting prudent monetary policies, a credible exchange rate regime and a well-capitalized, efficient and transparent financial system. To this end the Bank of Uganda has continued with the structural reforms in the banking sector.

During 2001, Bank of Uganda took additional steps to resolve its statutory intervention in Uganda Commercial Bank Ltd. A working Committee was tasked to oversee the resolution process. Bank of Uganda strategy for resolving UCBL was to test the market by approaching international buyers whom Bank of Uganda had pre-qualified, to prepare detailed financial and operational information on UCBL for investors and facilitate extensive onsite due diligence, to design a bid process and finally to manage the bid process to ensure the best market outcome.

Two bids were received. BOU evaluated the bids and Standard Chartered Investment Banking Corporation Ltd offer for 80% of UCBL's equity was considered superior and it was duly accepted. The sale agreement was signed on 20th November 2001 by the Bank of Uganda, Standard Bank Investment Corporation Ltd and the Government of the Republic of Uganda.

With the final resolution of UCBL, Bank of Uganda expects in the medium term, increased credit to the private sector and competition in the banking system. Already, there are signs that the prime lending rates have started declining partly as a result of the increased competition in 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, Bank of Uganda is still very concerned about the wide intermediation margins. Bank of Uganda urges banks to become more efficient and to reduce the lending rates even further. High lending rates are a constraint on the real sector economy.

Although the monetisation of the economy is increasing, the levels are still low, and reflect the fact that financial deepening, broadening and development continue to face serious challenges. There is also need to widen the outreach banking services into the rural areas. Therefore, Bank of Uganda shall continue to encourage the growth of Microfinance institutions (MFIs) to improve access to financial markets. The Microdeposit taking Institutions Bill 2001 is a step in the right direction.

Besides outreach, the financial sector faces the challenge of ensuring good corporate governance. Good corporate governance builds confidence in the market and encourages stable and sustainable savings, from which investment is financed.

Bank of Uganda has instituted measures to strengthen corporate governance in licensed financial institutions by vetting all members on the Boards of Directors and executive officers under the fit and proper test prior to assuming offices. In addition, if a board member or executive officer breaches any fiduciary responsibilities, BOU reserves the right to take corrective actions.

On the international scene, increased integration of the world's financial system and the removal of barriers to the free movement of capital have raised the specter of money laundering. Uganda being one of Africa's growing financial centers shall have

to guard against these negative developments. A clearly defined regulatory framework combined with an effective enforcement structure for money laundering is required. Therefore through the Ministry of Finance, Planning and Economic Development, the draft money laundering policy has been presented to the authorities for consideration. After the appropriate consultation, a draft anti money laundering bill will be forwarded to parliament for consideration and approval.

In conclusion, I would like to congratulate the Boards of Directors and Chief Executives of financial institutions upon the satisfactory performance exhibited during the year 2001. With increased cooperation between supervised financial institutions and Bank of Uganda, we shall consolidate our achievements and strengthen the performance of the financial sector even further.

E. Tumusiime Mutebile

2.0.0 ACCOMPLISHMENTS FOR THE YEAR 2001

2.1.0 COMMERCIAL BANKING DEPARTMENT

2.1.1 Over view.

The Commercial Banking Department's mission is to foster a sound and stable financial sector that is efficient and competitive. To this end, the Department is responsible for supervising all commercial banks in Uganda. This mission is achieved through three divisions namely; on-site, off-site and financial markets intelligence regulation and resolution. In general, the on-site division conducts on-site inspections of commercial banks, while off-site division carries out surveillance of commercial banks' financial conditions and compliance with statutory requirements. The Financial markets intelligence and regulation division carries out follow-up examinations of commercial banks, enforcement of prompt corrective measures in banks, reviews, develops and drafts banking regulations and prudential guidelines and also resolves distressed commercial banks.

2.1.2 Developments

A number of new developments took place during the year 2001 in line with best international practices on Bank Supervision. This included the introduction of risk – based supervision approach and adoption of improved classification of non-performing assets.

a) Risk Based Supervision

Intensive training was conducted in the year 2001 to prepare for the risk based supervision approach. The traditional method of CAMEL based on-site inspections is based on examination of key areas of banking operations involving extensive transaction testing. In a dynamic banking market, however, transactions testing itself is not sufficient for ensuring the continued safe and sound operation of a banking institution. Evolving new financial instruments have enabled banking institutions to rapidly reposition their portfolio risk exposures. Therefore periodic assessments of the condition of a financial institution based on transactions testing alone cannot keep pace with changes occurring in financial risk profiles. Under a risk focused

examination approach the degree of transaction testing should be reduced when internal risk management processes are determined to be adequate or where risks are deemed to be minimal. However, where additional transaction testing is appropriate, testing should be sufficient to assess the degree of risk exposure in a particular function or activity. If an examiner believes that banking institution management has provided false or misleading information or has omitted material information then substantial onsite transaction testing should be performed. Risk based supervision, which will be implemented next year involves a risk focused approach which calls for emphasis on a bank's primary risk areas.

b) Revision of Period For Classifying Non-performing Debts

As of 1st September 2001, a more stringent classification of non-performing assets was adopted in line with Basle standards. The classification period was amended as follows:

Classification	Old period after due date of payment of both interest and principal	Revised period after due date of payment of both interest and principal
Substandard	180 days past due	90 days but less than 180 days
Doubtful	360 days past due	180 days but less than 365 days
Loss	2 years past due	365 days or more

After the introduction of the above stringent classification, there have been aggressive efforts on the part of the banks' management to collect non-performing assets. Consequently, the ratio of NPA to total advances in banks has declined from 9.8% in 2000 to 6.5% in 2001.

2.1.3 Capacity Building

In order to improve the quality and coverage of onsite examinations, four project teams have been constituted, namely;

- Team A - Legal Regulatory Framework
- Team B - On-Site Examination
- Team C - Off-site Surveillance
- Team D - Resolutions of Problem Banks

The major tasks of Team A comprised the review of the Financial Institutions Bill (FIB) 2001 and the drafting regulations, which are meant to implement the FIB once it is enacted into law. The Team has prepared an Implementation Matrix for the FIB and is currently drafting regulations on licensing, capital adequacy and lending limits based on the much-reinforced provisions of the FIB. There is also ongoing work on the Risk Management Guidelines, a comprehensive document which shall provide financial institutions with sound principles, standards and best practices in managing the most common risks namely; credit, liquidity, interest rate, foreign exchange and operational risks.

Team B's main task is to orient the Function towards a risk-based approach to supervision and to implement consolidated supervision for financial institutions belonging to a group or conglomerate. An in-house technical discussion on risk-based methodology was conducted in November to introduce this novel approach to supervision to all staff. Improvements in planning and scheduling examinations and more detailed examination techniques and procedures for specific areas of Bank operations are being developed. The use of such tools as Scope Memorandum and Risk Matrix shall soon be made mandatory.

Team C's focus is on improving the quality of offsite financial analysis and compliance reviews. The team has noted that the current analysis is too oriented towards CAMEL rating and that there is no trend analysis being done for each financial institution. A database for quarterly data from March 1999 to June 2001 has been compiled and each member of the team is preparing financial analysis for Banks.

New sets of ratios, especially on profitability, are being proposed to reinforce the current measures of financial performance. In addition, new benchmarks for the

CAMEL Rating System are also being looked at and the “S” (sensitivity to market risks) factor shall soon be integrated in the rating. The team recognizes the need to strengthen the link between on-site and off-site divisions in order to build a comprehensive institutional overview for each supervised entity and to prepare accurate risk profiles for them.

Team D’s tasks are geared towards early identification of problem banks and smooth handling of banks identified as such. The team places strong reliance on the Function’s experience during the 1998/99 banking crisis. Among the team’s ongoing work are documenting detailed closure procedures; reviewing the Bank of Uganda’s intervention policy in the light of the new provisions in the FIB, particularly the mandatory prompt corrective measures; outlining the receivership and liquidation procedures; and defining criteria for classifying a problem bank.

Staff in the Commercial Banking Department has participated in various training programmes as indicated below:

- Three officers attended risk based supervision courses organised by MEFMI in Maseru, Lesotho.
- Two officers attended the forex management course at the Reserve Bank of India, Mumbai.
- Two officers attended the East and Southern Africa (ESAF) Supervision course in Pretoria, South Africa.
- Two officers attended the Inspecting Officers Programme at the Reserve Bank of India, Chennai.
- One Assistant Director attended a specialized course in Bank Supervision, Federal Reserve Bank, Washington DC.

2.2.0 NON-BANKING FINANCIAL INSTITUTIONS DEPARTMENT

2.2.1 Overview

Currently, the Non Banking Financial Institutions Department (NBFI) is responsible for the supervision of six credit institutions. The department shall also supervise micro deposit- taking institutions (MDI) when the Micro Deposit-Taking Institutions Bill 2001, is passed into law by parliament. The proposed Financial Institutions Bill (FIB), 2001 has also catered for a number of non-banking financial institutions i.e. Discount Houses, Finance Houses and Acceptance Houses. The Non-Banking Financial Institutions department will supervise these institutions.

2.2.2 On-site Inspection

- During the period under review, full scope examination of all the six credit institutions was carried out. The reports indicate that the financial condition of the credit institutions ranged from fair to satisfactory. Recommendations were made for improvement in areas where deficiencies were noted. A Memorandum of Understanding was signed with one credit institution during the year.
- A review of the operations of PostBank (Uganda) Ltd was carried out in view of their application for a credit institutions' business license. Recommendations were made for a restricted license for only six branches. Additionally, the institution will not engage in lending business for sometime until capacity to manage the business i.e. human resources and financial standing have reached a satisfactory level.
- A review of a Non Governmental Organization (NGO) operations was made in response to reports that the institution was lending savings deposits illegally. After examination findings, it was recommended that the NGO must stop intermediating savings deposits. The NGO submitted a written commitment not to lend savings deposits.

2.2.3 Off-site Analysis

The off-site analysis section receives and analyses data, which is submitted weekly, monthly and quarterly by all credit institutions. The information is used to rate the performance of credit institutions based on the key financial ratios on Capital Adequacy, Asset Quality, Profitability and Liquidity. The information is also used to identify problem/potential problem areas that should be reviewed during on-site inspection. The overall performance of the six credit institutions during the year under review was fair.

2.2.4 Developments in Non Banking Financial Institutions Department.

- One credit institution, Interstate Finance Company Limited ceased accepting deposits in 1998 and was seized by Bank of Uganda on 7th August 2001 under section 31, 32 and 33 of the Financial Institutions Statute, 1993.
- Progress in the development of the regulations on MDI operations is ongoing and it is expected to be finalised by the time of passing the Bill into law.

2.2.5 Capacity Building

Staff in the NBFID department have participated in various workshops, seminars, attachments and courses as follows:

- GTZ organised missions to Indonesia, India and Bolivia aimed at enabling staff share experiences in the area of regulation and supervision of MDI.
- GTZ sponsored 3 officers for the annual basic Microfinance training programme in Boulder, Colorado USA
- 3 officers attended the Intermediary course for bank supervisors at the Kenya School of Monetary Studies.

- 2 officers attended the Integrated Risk Management programme in India.
- One officer attended the International Banking Development programme in Pune, India.
- One officer attended a workshop on the role of National Networks in Performance Monitoring of Microfinance Institutions, Zimbabwe.
- The Director of the Non- Bank Financial Institutions Department made a one week study tour in Ghana (Bank of Ghana) to study the operations of Discount Houses.

The training has enhanced staff capacity, and equipped them with basic knowledge required to supervise the new class of financial institutions such as MDI. In addition, they have also been introduced to the risk-based supervisory approach.

3.0.0 A REVIEW OF PERFORMANCE OF SUPERVISED FINANCIAL INSTITUTIONS

3.1.0 COMMERCIAL BANKS

3.1.1 Overview

During the year under review, the overall financial condition of the banking sector continued to register a satisfactory composite rating under the CAMEL rating system. The key performance parameters of capital adequacy, asset quality, earnings and liquidity improved during the year. Two banks were upgraded from fair rating in 2000 to satisfactory rating in the year under review. On the other hand, the overall performance of two banks was downgraded from satisfactory composite rating recorded in 2000 to fair composite rating during 2001 while another two moved from marginal to unsatisfactory. This was mainly due to a decline in the asset quality in the two banks, which required additional provisions. Despite this development, the overall safety and soundness of the banking sector remained satisfactory during the year. Table 3.0 below shows the performance ratings in all the commercial banks in Uganda for the years 2000 and 2001.

TABLE: 3.0 Performance Rating of Commercial Banks as at year-end

Performance Category	2000					2001				
	Capital Adequacy	Asset Quality	Earnings	Liquidity	Overall	Capital Adequacy	Asset Quality	Earnings	Liquidity	Overall
	No. of Banks	No. of Banks	No. of Banks	No. of Banks	No. of Banks	No. of Banks	No. of Banks	No. of Banks	No. of Banks	No. of Banks
Strong	0	0	0	0	0	0	0	0	0	0
Satisfactory	14	12	8	16	10	14	10	6	16	8
Fair	1	1	0	1	5	1	4	4	1	7
Marginal	0	0	2	0	2	0	1	3	0	0
Unsatisfactory	2	4	7	0	0	2	2	4	0	2
Total	17	17	17	17	17	17	17	17	17	17

Table 3.1: Composite ratings of Commercial Banks' Deposits and Assets.

	2000			2001		
Total Deposits (Shs m)	1,324,526			1,483,285		
Total Adjusted Assets (Shs m) 1/	1,777,972			1,979,011.3		
Composite Rating	No. of Banks	% of Total Deposits	% of Total Assets	No. of Banks	% of Total Deposits	% of Total Assets
Strong	0	0	0	0	0	0
Satisfactory	10	61.48	61.82	8	63.01	64.50
Fair	5	37.17	36.58	7	35.88	34.53
Marginal	2	1.35	1.60	0	0	0
Unsatisfactory	0	0	0	2	1.11	0.97
Total	17	100.00	100.00	17	100.00	100.00

Note:

1. Total adjusted assets are total assets net of provisions.

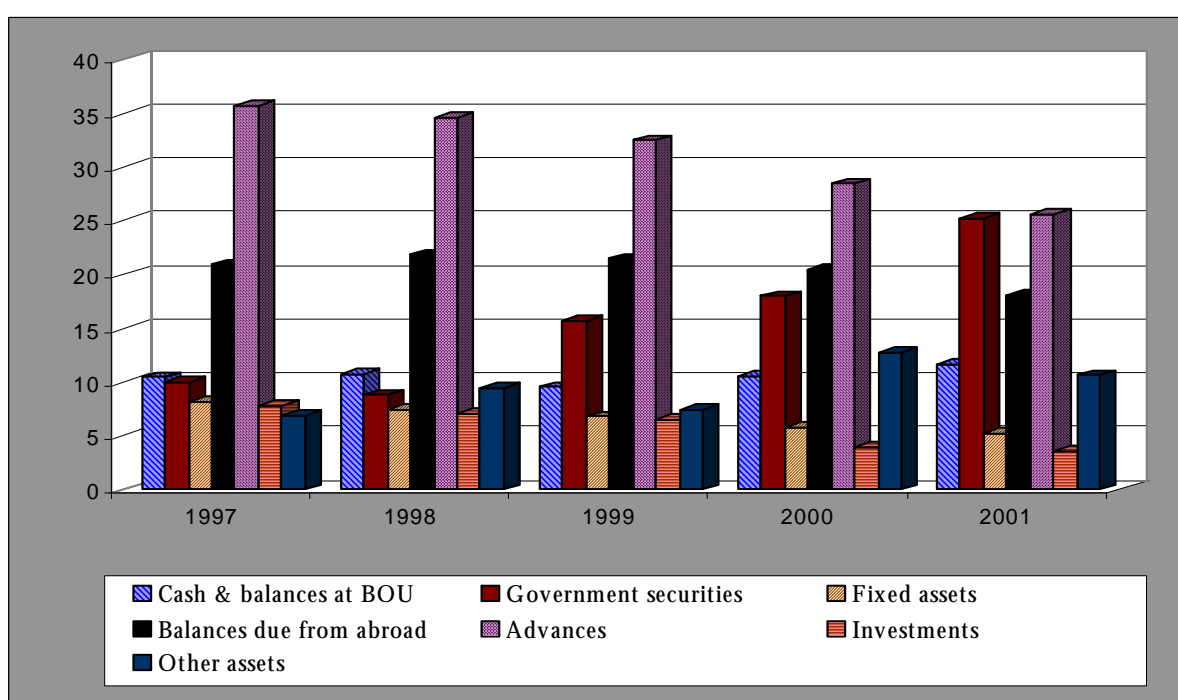
From table 3.1 above, it can be seen that during the year 2001, eight banks had satisfactory composite ratings and held 63.01% of the total deposit holdings and 64.50% of the total adjusted assets. Seven banks with a fair rating held 35.88% of total deposits and 34.53% of total adjusted assets. This shows an improvement over the year 2000, where ten banks with satisfactory composite ratings held 61.48% of deposits and 61.82% of assets. Similarly, the percentage of deposits and adjusted assets held in weak banks (those ranked marginal and unsatisfactory) fell from 1.35% and 1.60% in 2000 to 1.11% and 0.97% in 2001 respectively.

3.1.2 Assets

The banking sector's total assets recorded a growth of Shs.193bn or 10.5% from Shs.1,845bn as at the end of the year 2000 to Shs.2,038bn as at the end of the year 2001. Loans, overdrafts and discounts amounted to Shs.521bn or 25.6% of total assets but this was a drop from the respective figures of Shs.525bn or 28.5% recorded at the end of the year 2000 (Figure 3.1). Investments in treasury bills increased by Shs.182bn or 54.8% from Shs.332bn recorded at the end of 2000 to Shs.514bn and constituted 25.2% of total assets at the end of the year 2001. Balances due from banks outside Uganda totaled Shs.368bn or 18% of total assets as at the end of the period under review.

The asset structure of the banking sector shows a shift to more investments in treasury bills than private credit during the year 2001. The shift in investment strategies and particularly from lending towards less risky assets is an indication that financial institutions have become more risk averse. The increase by Shs.42bn or 21.4% in cash and balances with BOU from Shs.196bn in 2000 to Shs.238bn in the year 2001 was partly on account of an increase in cash reserve requirements by Bank of Uganda.

Fig 3.1 Structure of Commercial Banks' Assets (In percent)

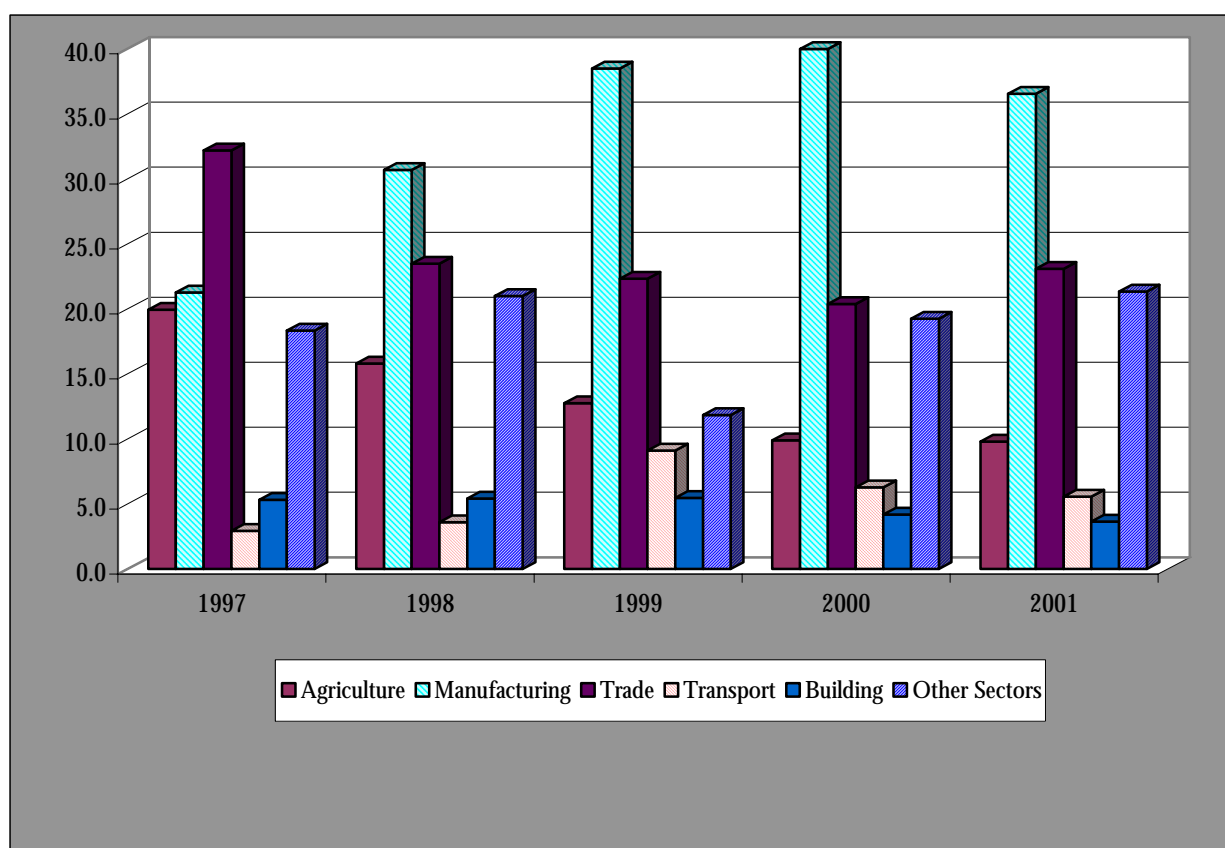


3.1.3 The sectoral distribution of loans and advances.

The banking sector recorded a marginal contraction in total credit amounting to Shs.4billion from Shs.525bn as at the end of December 2000, to Shs.521bn as at the end of the year under review. Figure 3.2 depicts the stock of credit outstanding by sector, as a percentage of total credit portfolio. During the year under review, 36% of the outstanding total credit i.e. Shs.190bn was accounted for by the manufacturing sector. Trade and commerce ranked second in credit extensions taking a share of Shs.120bn or 23% of total credit portfolio. The share of credit to agriculture and

transport sectors to total credit portfolio remained at 10% and 6% respectively during the two successive years 2000 and 2001. Although the category “Others advances” was significant, it comprised of credit outstanding to various sectors including mining, government, real estate and personal loans.

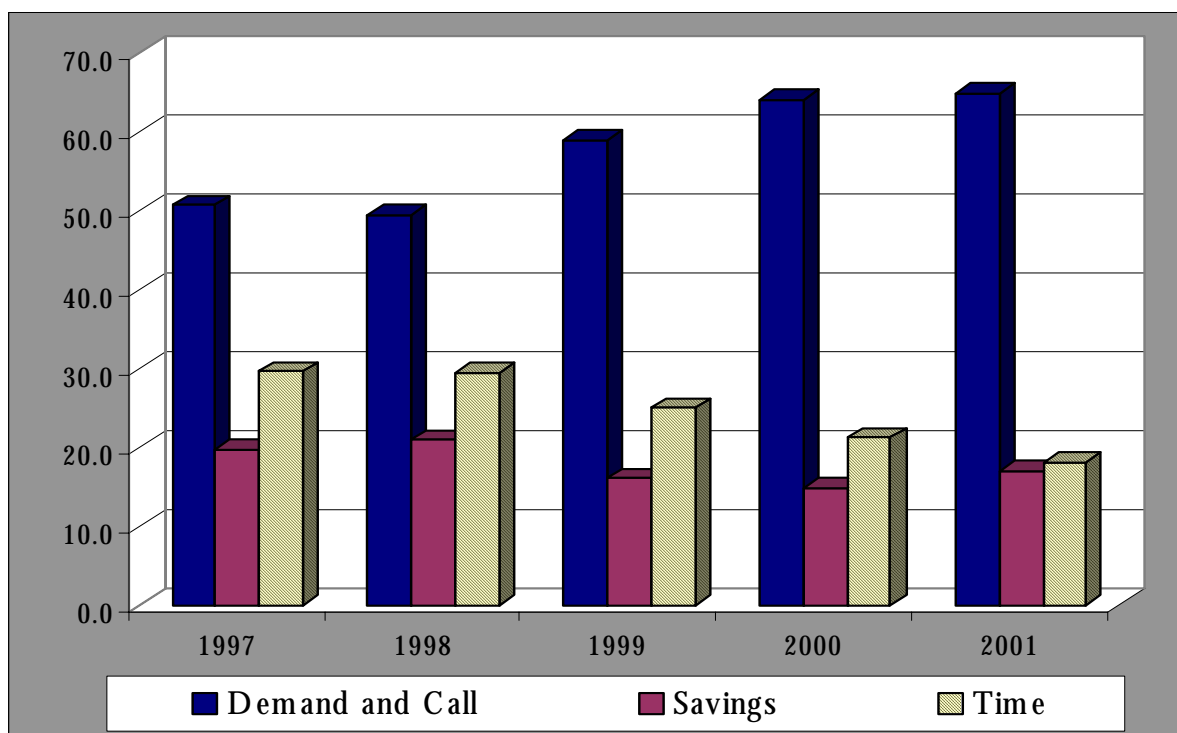
**Figure 3.2: Sectoral distribution of Commercial Banks’ Credit
(In percent of total)**



3.1.4 Deposits

The banking sector’s total deposit base grew by Shs.158bn or 11.9% from Shs.1,325bn as at 31.12.2000 to Shs.1,483bn as at 31.12.2001. As at end-December 2001, demand and call deposits represented 65% of the total deposits while time and savings deposits accounted for 17% and 18% of total deposits respectively. The growth in deposits was mainly reflected in demand deposits, which increased by Shs.113bn or 13.3% from Shs.847bn in 2000 to Shs.960bn as at the end of the period under review. Figure 3.3 shows the structure of deposits.

Figure 3.3: Structure of Commercial Banks' Deposits (in % of the total)



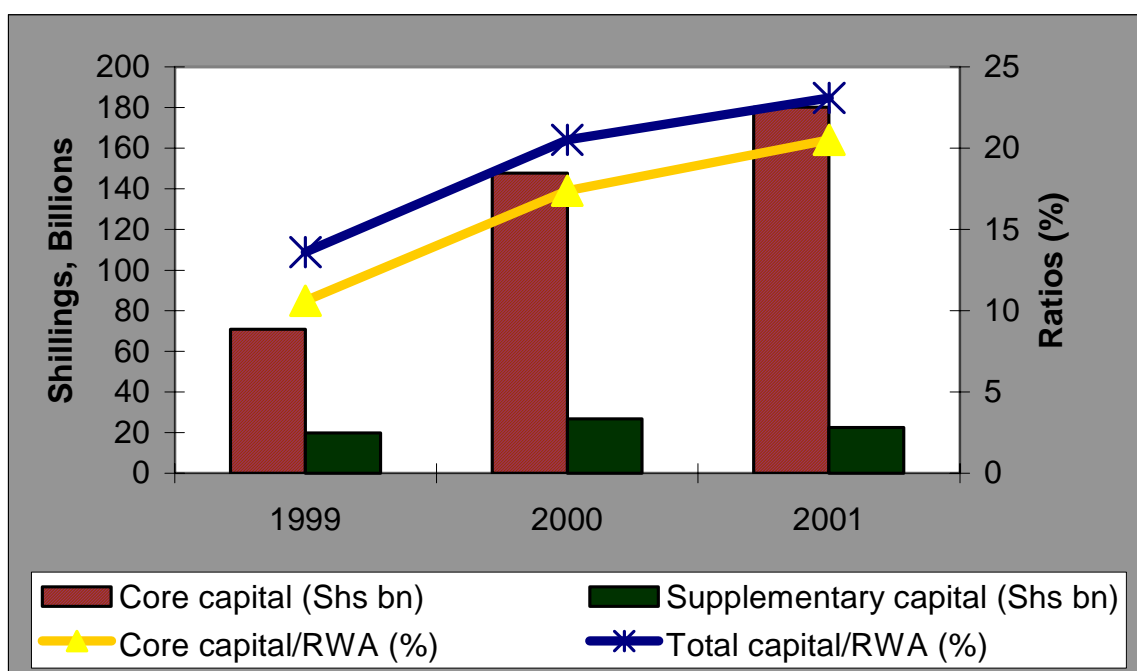
3.1.5 Capital Adequacy

Capital in banks represents a buffer against losses that may arise in the event of imprudent risk management practices. It is also a permanent source of funding that provides a base for future growth. It is, therefore, imperative that banks remain adequately capitalized in order to ensure public confidence in the sector. The strength and stability of earnings and the quality of loans and advances are important indicators for improving the capital base of banks.

As at the end of December 2001, the total capital held by the banking sector amounted to Shs.203bn, reflecting an increase of Shs.37bn or 22% from Shs.166bn as at end of December 2000. Total core capital amounted to Shs.180.3bn while supplementary capital stood at Shs.22.4bn. The sector's paid up capital was Shs.83.5bn. The improvement is mainly attributed to additional capitalization of some banks and an increase in retained earnings during the year under review.

Capital adequacy in a banking institution is measured in relation to the relative risk of assets held, both on and off the balance sheet. All the 17 commercial banks were solvent and fifteen (15) banks complied with all the regulatory and statutory capital requirements. The Average Core Capital to Risk Weighted Assets (RWA) ratio improved from 17.4% as at 31 December 2000, to 20.5% as at 31 December 2001. Figure 3.4 shows the total capital ratios, core capital and supplementary capital trends in the years 1999, 2000 and 2001. Supplementary capital, which includes revaluation reserves, unencumbered general provisions and subordinated debt recorded a very modest change of Shs.3.83bn or 20.6% from Shs.18.56bn as at 31 December 2000 to Shs.22.39bn as at 31 December 2001.

Figure 3.4: Capital Adequacy Indicators

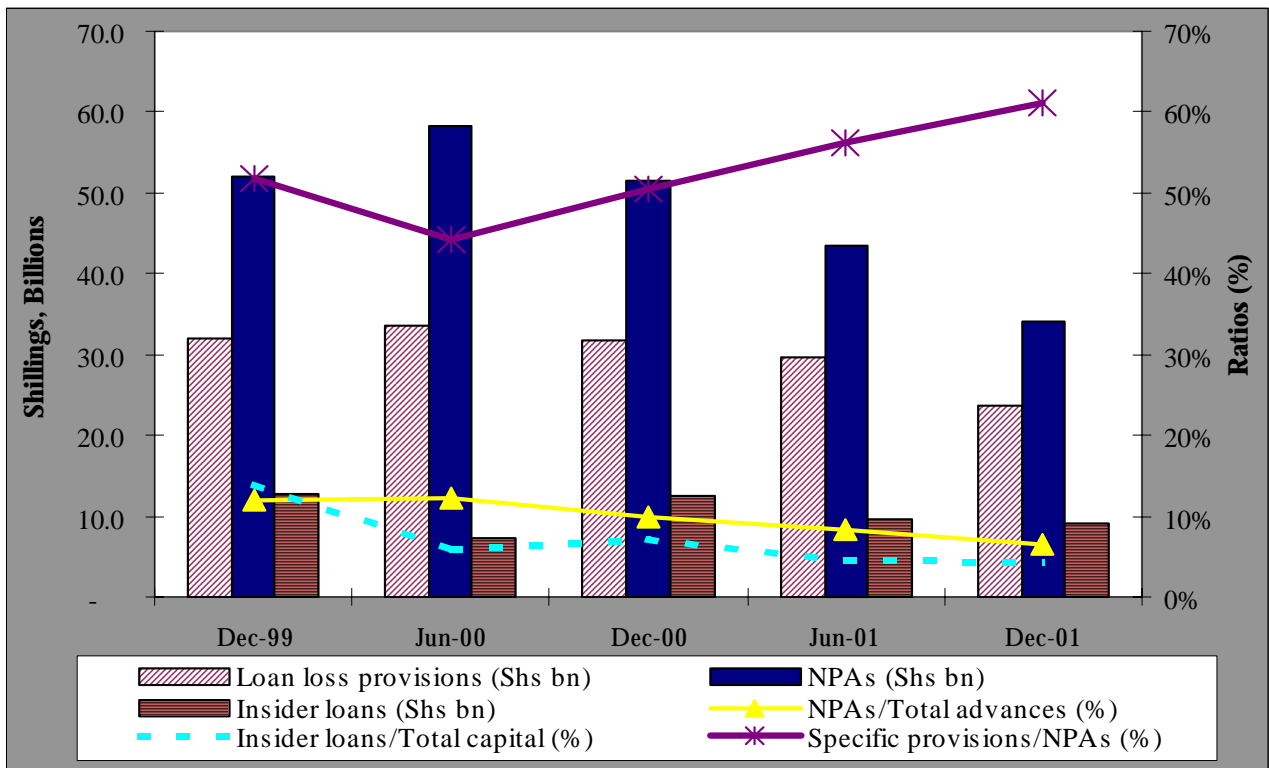


In order to further enhance the safety and soundness of the banking sector, the minimum unimpaired paid up capital requirement of Shs.2bn shall be enhanced to Shs.4bn by 1st January 2003 as per Statutory Instruments 1999 number 48. The ongoing capital adequacy ratios currently stand at 8% and 12% for core and total capital to RWA respectively.

3.1.6 Asset quality

Credit risk is an inherent part of banking business. It arises when a borrower defaults on the loan repayment agreement. A financial institution whose borrowers default on their repayments may face cash flow problems, which eventually affect its liquidity position. Very often, this results into loss of revenue and value of assets. Despite innovations in the financial services sector, credit risk is still the major cause of bank failures.

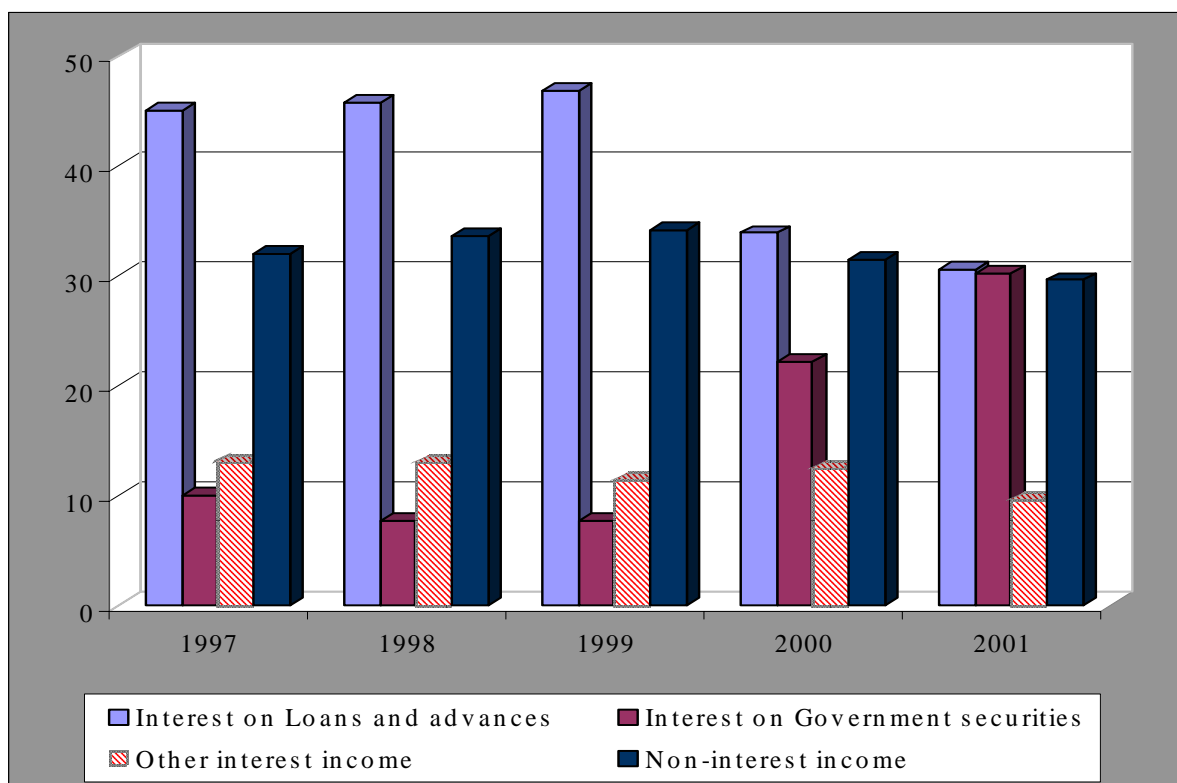
Figure 3.5: Asset Quality Indicators



During the year under review, banks registered an improvement in the asset quality. The average ratio of non-performing advances to total advances declined considerably from 9.8% in the year 2000 at the end of the period under review to 6.5% (Figure 3.5). In addition to enhancing recovery efforts of the delinquent facilities, banks made considerable progress in improving credit risk management during the year. The rise in the ratio of specific provisions to non-performing advances from 50.5% to 61.2% was due to the fact that banks were more compliant

with the new prudential regulation on Asset Quality. The ratio of insider loans to core capital remained within the prudent benchmark of 25% of core capital as per provisions of the Financial Institutions Statute 1993.

Figure 3.6: Commercial Banks' sources of income (In % of the total)



3.1.7 Earnings

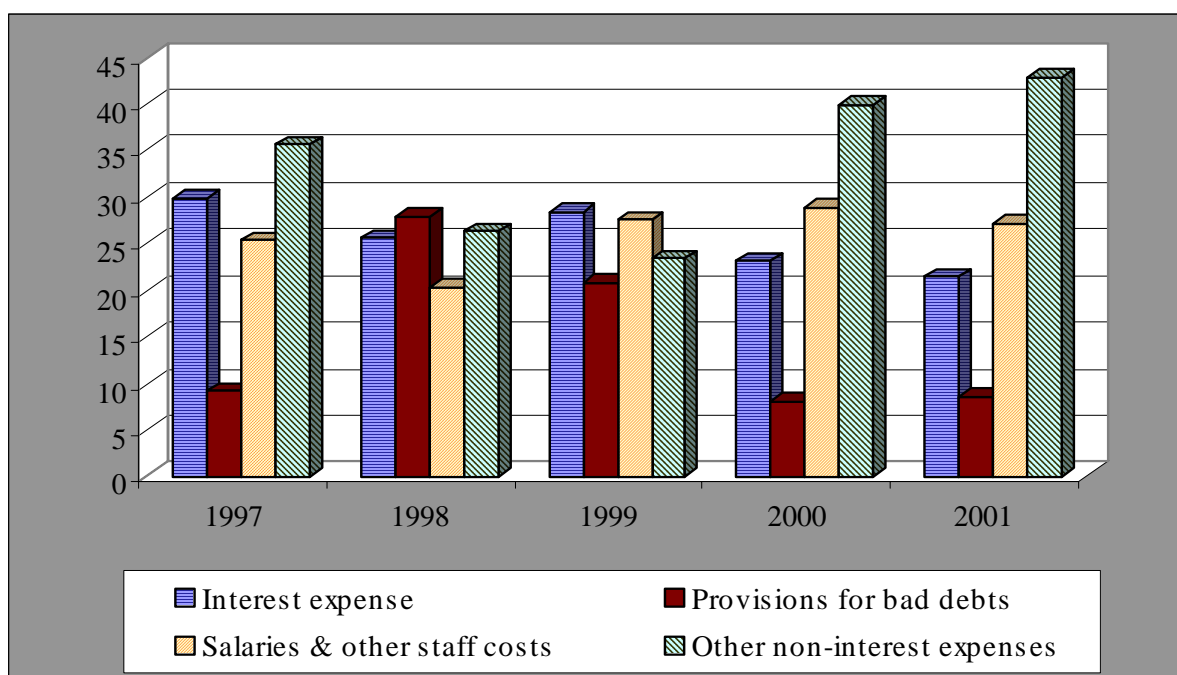
The continued viability of a bank depends on its ability to earn an adequate return on its assets and capital. Good earnings performance enables a bank to fund its expansion, remain competitive in the market and replenish and/or increase its capital base.

As at the end of the period under review, the banking sector recorded a return on assets of 4.13% compared to 4.21% registered as at the end of the previous year. The major source of earnings for the sector was interest income. Total interest income increased by Shs.35bn from Shs.170bn in 2000 to Shs.205bn as at the end of the period under review, and it accounted for the largest share of total income of

the sector at 70%. Non-interest income on the other hand rose by Shs. 8bn over the period, and represented 30% of total income, from 34% and 31% in 1999 and 2000 respectively.

During 2001, there were shifts in the sources of income. The share of earnings from Government securities rose to 30.2%, up from 22.2%, while that for interest on Advances declined to 30.6%, from 33.9% in 2000. Other interest income declined from 12.5% to 9.6% of total income.

Figure 3.7: Commercial Banks' categories of expenditure (In % of total)



The notable rise in interest income from investments in government securities from Shs.55bn in 2000 to Shs.88bn in 2001 was largely attributed to favourable rates on treasury bills during the period under review. Secondly, banks seem to have become more risk averse, shying away from lending and preferring to invest in Government securities which are risk free. This follows the rising level of Non-performing assets in the 1980s and early 1990s. Figure 3.6 depicts income earned from the various sources in relation to total income.

The sector's total interest expense recorded an increase of Shs.5bn or 12.5% from Shs.40bn in 2000 to shs45bn in 2001. Total non-interest expense (including tax and provisions for bad debts) rose by Shs.32bn or 24% from Shs.133bn to Shs.165bn during the same period. The major expenditure items were salaries, staff costs and other non-interest expenses, which increased by Shs.28bn or 24% from Shs.119bn as at end December 2000, to Shs.147bn as at December 2001. Interest expenses on time deposits remained high at Shs.24bn representing a modest increase of Shs.1bn or 4.3% from Shs.23bn spent during the year 2000. Figure 3.7 shows the relative shares of the various expenditure items to total expenses, while figure 3.8 gives the trend of the return on assets and profits during the year under review.

3.1.8 Liquidity

As at the end of 2001, the banking sector recorded an overall satisfactory liquidity position. Liquid assets (see table 1 (v) in the appendix) increased by Shs.186bn or 16.8% from Shs.1,106bn as at end of 2000 to Shs.1,292bn during the year under review. The ratio of liquid assets to deposits increased from 84.15% in 2000 to 87.59% as at the end of the period under review. The lending ratio declined marginally by nearly four percentage points from 38.98% as at 2000 to 35.33% at the end of the year under review. All banks maintained adequate credit-clearing balances with BOU. Cash reserve requirements on foreign currency deposits came into effect at the end of September 2000 and this has resulted into more reserves being held by banks. Figure 3.9 reveals that liquid assets recorded a steady increase over the period.

Figure 3.8: Return on Assets and Earnings

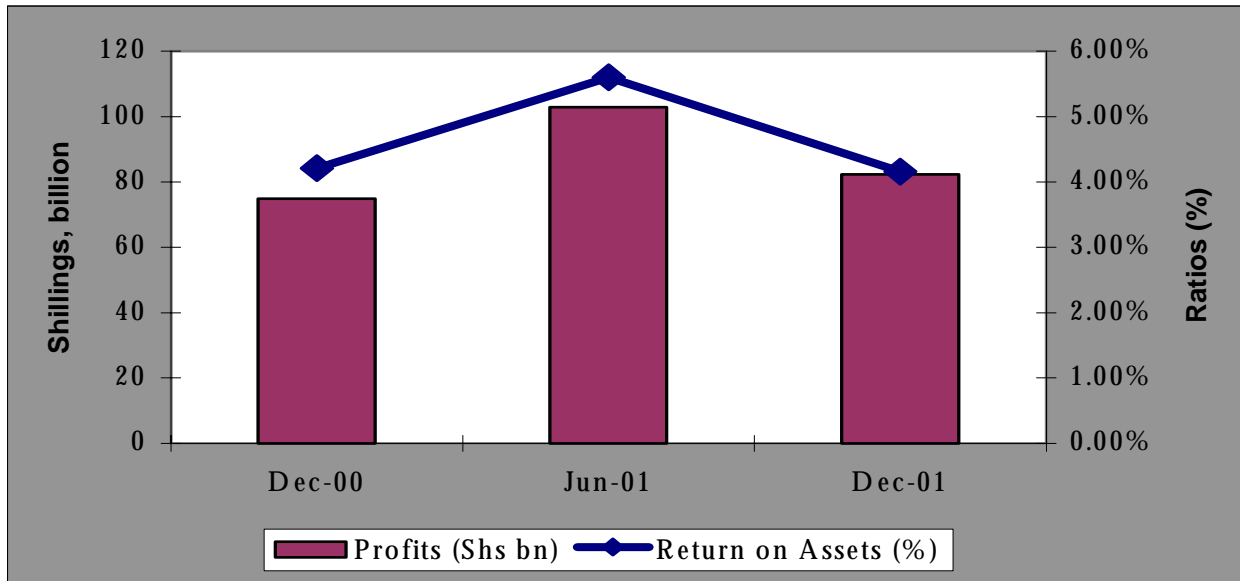
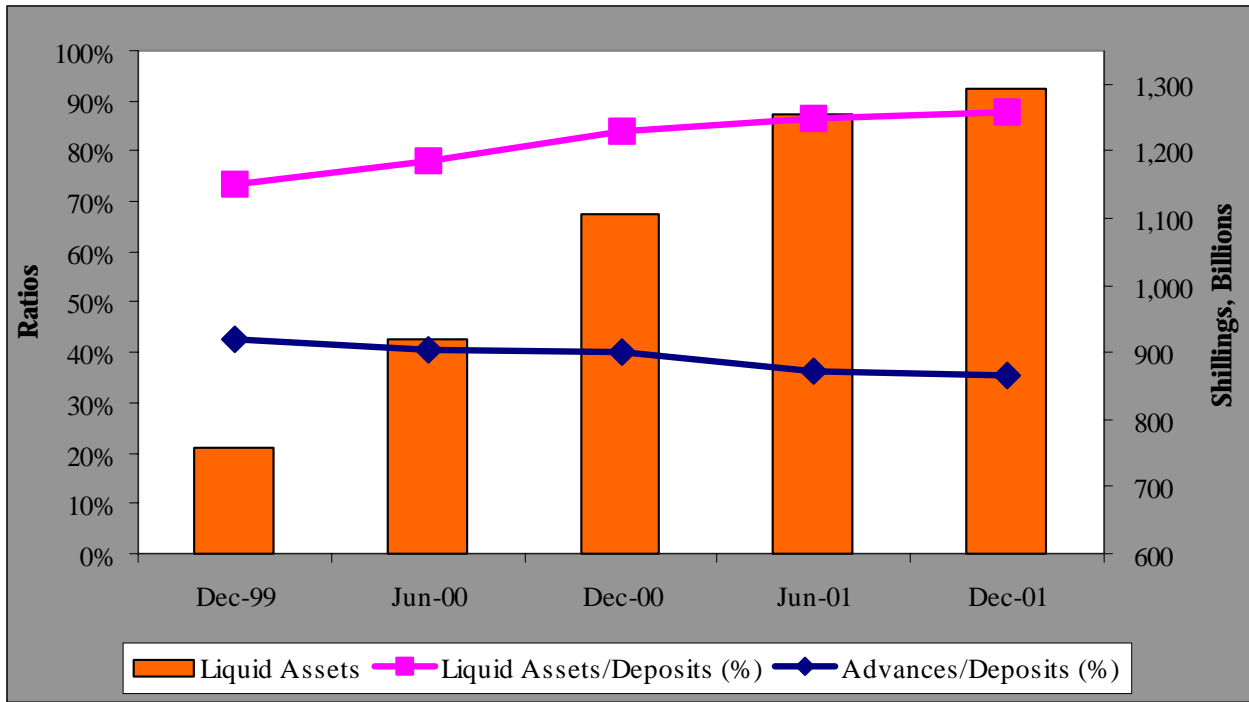


Figure 3.9 Liquidity Indicators



3.2.0 CREDIT INSTITUTIONS

3.2.1 Overview

Total assets (net of administered loans) of the six operating credit institutions increased by 26% from Shs.47.5bn in 2000 to shs.60.0bn at the end of the period under review. The financial condition of the credit institutions, based on the consolidated statements of assets and liabilities as at 31st December 2001 remained Fair. A fair rating means that overall the credit institutions exhibit some weaknesses ranging from moderate to unsatisfactory. Such institutions are less resilient to the onset of adverse business conditions and could deteriorate if the course of action taken is not effective in correcting the area of weakness. However, two credit institutions were sound in almost every aspect, and therefore, had satisfactory rating, while the other four institutions had fair rating. Furthermore, five Credit institutions remained profitable, but one made an operating loss of Shs801.86m in the financial year ended December 2001. This was mainly attributed to the high preliminary and overhead costs. During the year or review, Bank of Uganda finally seized Interstate Finance Company a non-operating credit institution. An audit firm was appointed to prepare a report on the statement of affairs of the institution.

3.2.2 Capital Adequacy

The Paid-in capital of the Credit institutions increased by 4.7% from shs7,102.38m in 2000, to Shs.7,435m as at the end of the period under review. All the credit Institutions maintained core capital to risk weighted assets ratios above the minimum requirement of 8%. The core capital to risk weighted assets ratio (RWA) however, declined from 27.89% in 2000 to 19.9% in 2001. These developments are depicted in figure 3.10.

3.2.3 Asset Quality

The performance of credit portfolio remained fair. The credit institutions total credit portfolio (excluding administered loans) increased by 31.8% from Shs.24,254.32m in 2000, to Shs.31,978.9m as at end year under review. Housing Finance Company of Uganda Ltd manages an administered loan portfolio for mortgage businesses i.e.

purchase of residential houses, and construction or completion of existing structures. The administered loans decreased marginally by 3.29%, from Shs.28,876.8m to Shs.27,927.41m between 2000 and 2001. As at the end of the period under review, Mortgage loans represented 73% of total loans compared to 75% in 2000. The ratio of non-performing advances to total advances (NPA) in the credit institutions' sub-sector increased from 11.0% in 2000 to 15.8% in 2001. The increase was due to the coming into force of the new BOU guidelines on classifications of non-performing assets, by 30th September 2001. The specific provisions as a percentage of NPA decreased from 28.51% in 2000 to 25.9% as at end of the period under review. These ratios are depicted in figure 3.11.

Figure 3.10: Ratio of core capital to Risk Weighted Assets (%)

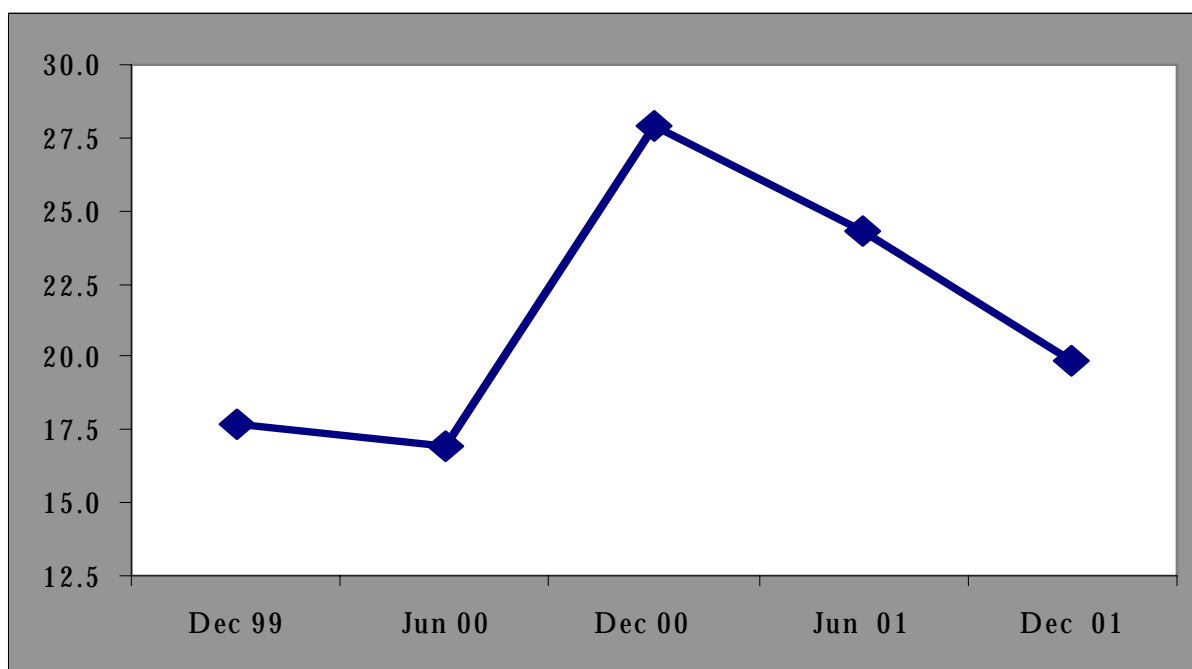
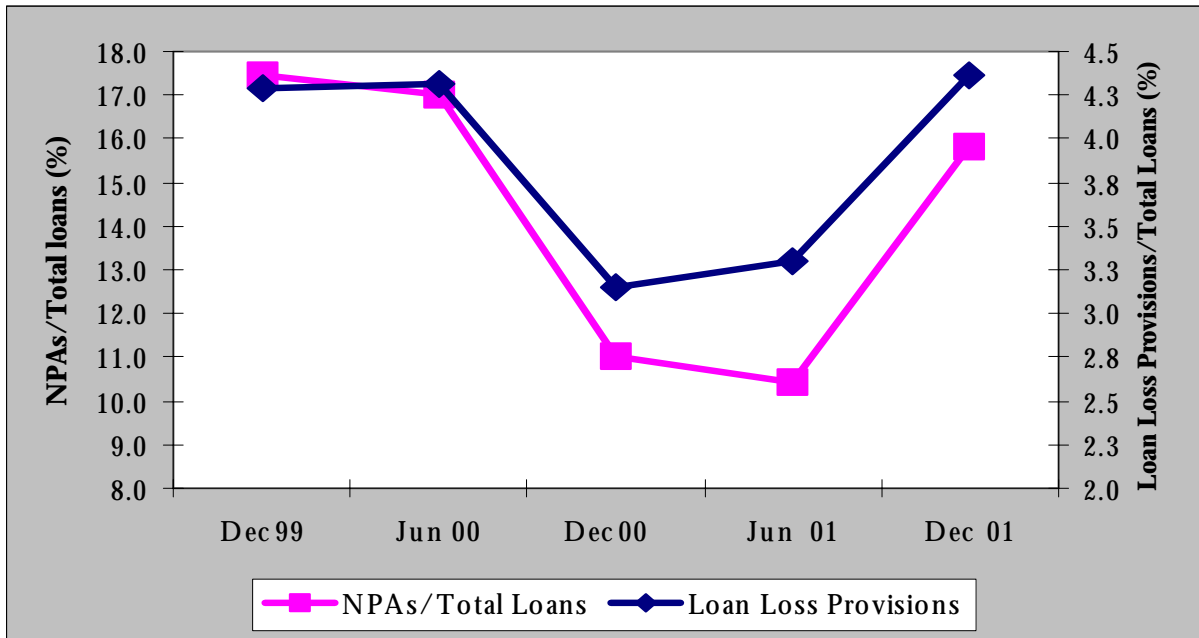


Figure 3.11: Asset Quality Indicators



3.2.3 Earnings

The overall credit institutions' profitability significantly reduced by 68.2%, from Shs.1,612.44m to Shs.511.45m, in 2000 and 2001 respectively. This was basically attributed to losses registered by two newly licensed credit institutions. Interest income from the intermediation function constituted the main source of earnings for the credit institutions. Interest income increased by 42.9% from shs 5,506.3m in 2000 to shs7,873.03m in the year 2001. Interest expenses increased by 25.2% from Shs1,295.8m in 2000 to Shs1,622.89m by the end of under review. Return on assets ratio decreased from 3.4% to 0.85% between year 2000 and 2001, while Return on Equity was 14.68% and 4.78% for year 2000 and 2001 respectively. The decline in the ratio is attributed to the losses made by the two credit institutions already alluded to. Trends in these 2 ratios are shown in figure 3.12.

3.2.4 Liquidity

All the credit institutions complied with the statutory liquidity requirements during the period under review. However, the overall liquid assets to deposits ratio declined marginally by 0.01% from 44.67% in 2000 to 44.66% at the end of 2001. Furthermore, as figure 3.13 shows, the lending ratio declined from 72.4% to 71.7% over the same period.

Figure 3.12: Return on Assets (roa) and Return on Equity (roe)

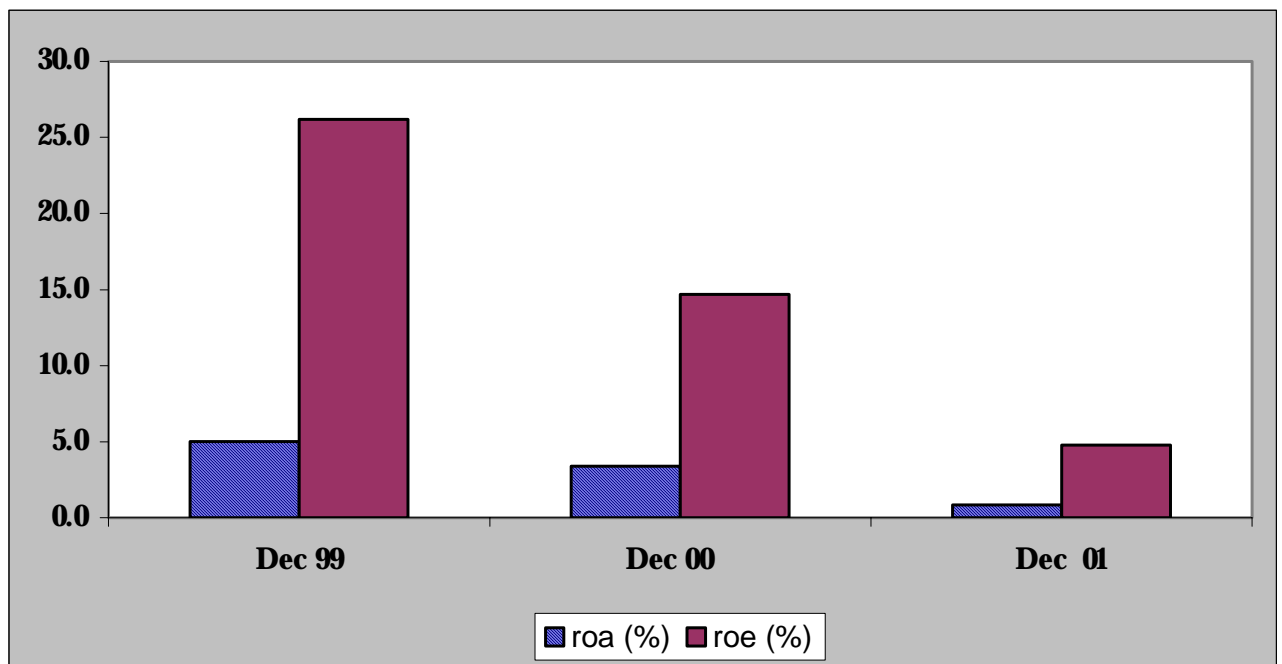
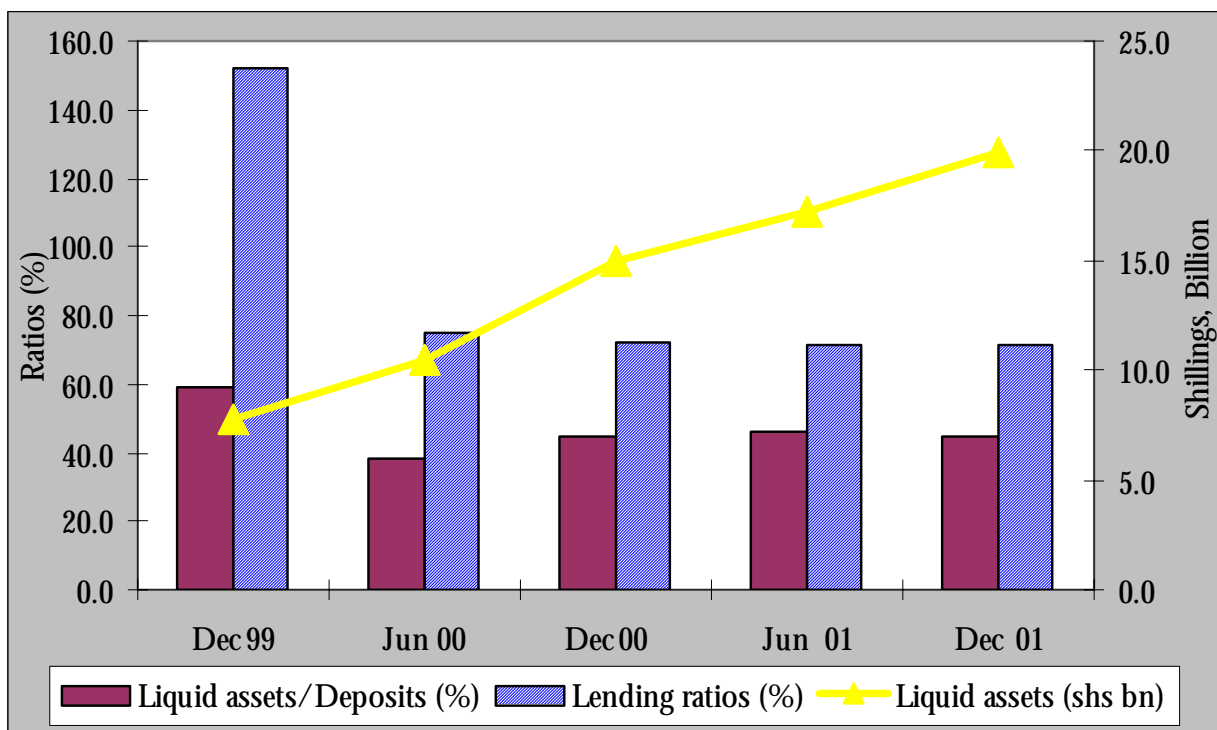


Figure 3.13: Liquidity Indicators



4.0.0 DEVELOPMENTS IN THE FINANCIAL SECTOR IN UGANDA

4.1.0 CLOSED BANKS UPDATE

International Credit Bank Ltd (ICB in Liquidation)

As at 30 December 2001, a total of Shs.5.0 billion worth of the bank's assets (loan recoveries, sale of assets and vault cash) had been realized. ICB's financial position still depicts a total deficiency of about Shs.31 billion mainly arising from contingent liabilities that have now crystallised. However, the major outstanding issue is the conclusion of judgment against insiders and unsecured borrowers who form a large percentage of the balance of the outstanding loan portfolio.

Greenland Bank Ltd. (GBL) (in liquidation)

At the time of its closure, the outstanding loans and overdrafts in the GBL was at Shs.42 billion of which advances amounting to Shs.12.8 billion have since been resolved. Total assets realized amounted to Shs.16.3bn.

Cooperative Bank Ltd. (Co-op) (in liquidation)

The Liquidation process has so far realized assets worth Shs.26.1 billion. Loans, overdrafts and other assets worth Shs.69 billion are yet to be realized. Liquidation costs incurred by the end of the year 2001 amounted to Shs.2.3 billion. The progress on the liquidation process shall depend mainly on the speed of realization of collaterals located in various places in the country.

Interstate Finance Company Ltd. (IFC)

During the year 2001, Bank of Uganda closed IFC and engaged external auditors to prepare a report on the statement of affairs of the institution. IFC was one of the credit institutions operating in Uganda with a deposit base of Shs.279 million and total outstanding loans amounting to Shs.223.4 million.

In the three closed banks under liquidation, a total of Shs.108.5 billion has been paid to the depositors. Out of this amount, Shs.91.2 billion was obtained from government, Shs.8 billion was obtained from the assets realized, while Shs.6 billion was from the Deposit Insurance Fund and shs 3.2 billion being additional depositor payments after 30th June 2000.

4.2.0 UCBL RESOLUTION

Uganda Commercial Bank Limited (UCBL) was established as Uganda Commercial Bank by an Act of Parliament in 1965 to provide banking services and promote economic development in Uganda. The bank changed its name to UCBL on its incorporation in October 1997 in preparation for privatization . UCBL, with its extensive branch network (68 branches), provides an essential banking service for many small business and personal customers. The institution was recapitalised in 1996 to cover substantial losses, incurred on its loan portfolio in the preceding years.

UCBL was partially privatized in April 1998, when the Government of Uganda (GOU) sold 49% of its equity to Westmont Land (Asia) Bhd, a Malaysian company. Westmont took control of the management of UCBL under a 3-year management contract. The bank was severely mismanaged by Westmont, which also quickly lent huge sums of money to Greenland Bank Ltd.

In November 1998, Bank of Uganda (BOU) intervened in UCBL and placed a resident supervisor in the bank. Following BOU's intervention, KPMG was tasked to conduct an audit, which revealed that UCBL was insolvent to the tune of US\$16.3 billion. In April 1999, BOU placed UCBL under statutory management, and appointed the resident supervisor as Acting Managing Director. A new board of directors was also appointed.

In May 1999, GOU instituted civil proceedings against Westmont, which were ultimately settled by an award of the International Court of Arbitration. In November 2000, GOU recovered the shares, which had been sold to Westmont, thus regaining 100% control of UCBL and paving the way for re-privatization of the bank.

In July 2000, the Minister of Finance outlined the two principal objectives for re-privatization of UCBL as:

- (a) to re-privatise UCBL by selling a controlling stake to a well-established reputable and creditable bank; and
- (b) to preserve the rural branch network of the bank, to provide savings and payments services for the public in areas of the country not well served by other banks.

The sale of UCBL was handled by BOU in its capacity as statutory manager and pursuant to its powers under section 32 of the Financial Institutions Statute 1993. Throughout the year 2001, the Supervision Function, in coordination with the financial advisor and the legal advisor became fully involved in the resolution process for UCBL. The Working Committee, which was tasked to oversee the resolution process, included the Executive Director – Supervision and the Director for Commercial Banking.

On 15th February 2001, while appearing before the Joint Parliamentary Committee on the Economy and Finance, the Governor stated a clear strategy for resolving UCBL through the following steps:

- (a) test the market by approaching international bank buyers whom BOU had pre-qualified;
- (b) prepare detailed financial and operational information on UCBL for investors and facilitate extensive on-site due diligence; and
- (c) design a bid process that would enhance the opportunity for sale of the entire branch network to ensure continuity of access to banking services throughout the country.

Subsequently, four banks (Stanbic, Standard Chartered, DFCU and Barclays) completed on-site due diligence at UCBL. Only two banks, namely, Stanbic and DFCU submitted their bids by 31st August 2001. The bids were opened on 1st October 2001 after a one-month's delay on account of objections to the sale process by members of parliament. After giving parliament the assurance that the UCBL Resolution would be subject to an independent audit by a reputable international

institution to be financed by the Department for International Development of the United Kingdom (DFID), BOU proceeded to evaluate the two bids received.

While the bids were quite different, the Working Committee regarded them as sufficiently serious to invite both bidders to negotiation. Stanbic's offer for 80% of UCBL's equity was eventually considered superior and was accepted by the Board of Directors of BOU on 15th October 2001. On the same day, the Divestiture and Reform Implementation Committee (DRIC) reviewed the evaluation of the two bids and noted the recommendation that Stanbic's offer be accepted. DRIC gave a "no objection" to the UCBL resolution process and also assured that the Ministry of Finance, Planning and Economic Development would sign the share transfer forms while BOU would sign the Sale Agreement with Stanbic.

The Sale Agreement was signed on 20th November 2001 by the Bank of Uganda, Standard Bank Investment Corporation Limited, and the Government of the Republic of Uganda, represented by the Minister of Finance, Planning and Economic Development and UCBL. Stanbic's Board of Directors ratified the purchase of UCBL on 5th December 2001.

The Agreement reached with Stanbic met all of the publicly stated objectives for UCBL resolution. Stanbic is a leading sub-saharan commercial and retail banking group incorporated in South Africa with more than 30,000 employees and an extensive presence in Africa. Stanbic has committed to maintain UCBL's rural branch network over the next two years. If Stanbic wished to close any of these branches at the end of the two-year period, the bank is required to first discuss with GOU a compensating arrangement to keep such branches open. Stanbic also undertook to cooperate with BOU to make arrangements to reasonably minimize the disruption of banking services to the communities in connection with any branch closing.

By December 2001, UCBL remained under statutory management of BOU. The closure of the agreement with Stanbic which was originally scheduled for 31st

December 2001 had to be postponed until 2002 on account of certain regulatory requirements including approval of the transaction by the Reserve Bank of South Africa and the fulfillment of other suspensive conditions.

While the UCBL resolution process diverted so much attention and resources from the normal workload of Supervision Function, the priority accorded to this single, most important failure resolution exercise was justified by fact that UCBL is the largest bank in Uganda. Moreover, the lessons learned from the first failed privatization are too painful to forget. The resolution exercise has also given the Supervision Function another valuable experience in handling bank failures with systemic implications.

4.3.0 FINANCIAL SECTOR ASSESSMENT PROGRAM

Uganda is one of the first countries in the region to undergo a Financial Sector Assessment Program (FSAP). FSAP is a joint IMF/World Bank program launched in May 1999 to assess strengths and vulnerabilities of member countries' financial systems in order to reduce the potential for crisis, thereby contributing to efforts to promote national and international financial stability and growth. The program includes:

- a) an assessment of financial system stability including macroeconomic factors that could affect the performance of the system and conditions in the system that could affect the macro economy;
- b) an assessment of the extent to which relevant financial sector standards, codes and good practices are observed;
- c) an assessment of financial sector's reform and development needs.

A joint IMF/World Bank mission made several visits to Uganda during the period under review. The mission focused on assessing:

- a) the potential vulnerabilities of financial institutions and markets to macroeconomic shocks, and the macroeconomic impact of financial vulnerabilities;
- b) the system of official oversight and regulation of the financial system, including compliance with financial sector standards and codes on banking, payments systems, insurance, and transparency of monetary and financial policies, and deviations from best practice;
- c) the country's institutional arrangements for crisis management, the framework for bank restructuring, and the financial safety net arrangements;
- d) the systemic liquidity issues and the systemic risks arising from payment and settlement systems, including risk management procedures;

- e) the developmental issues in the financial sector.

The mission held a number of meetings with the staff of institutions and agencies involved in the supervision and regulation of the Uganda financial system, as well as with representatives of private financial institutions and other market participants. These included the BOU, the Ministry of Finance, and all official supervisory agencies, as well as representatives of commercial and development banks, microfinance institutions, insurance companies, brokerage houses, insurance companies, private pension funds, donor organizations, auditors, lawyers, and accountants. The mission made a presentation of its findings and recommendations to the BOU's management. The output of the FSAP team's work and of the discussions held with the authorities will feed into the International Monetary Fund's mission for the Article IV consultation discussions with Uganda.

The FSAP Team, among other things, noted that BOU's supervision of financial institutions has improved significantly since the enactment of the Financial Institutions Statute, 1993. The FSAP report dated November 2001 stated among others, that BOU, with the benefit of technical assistance, has developed and implemented a generally sound and practical approach to supervision. The Team also found that technical competence of staff is generally good, and the examination reports appear adequate and generally appropriate for the current level of financial sector development.

With respect to compliance with the Basel Committee's 25 Core Principles for Effective Banking Supervision, the FSAP revealed that Uganda is compliant with 3, largely compliant with 6 and that substantive progress towards compliance has been made with 11 other core principles. The new Financial Institutions Bill is expected to address most of the identified gaps in compliance.

Finally, the FSAP missions identified the following 3 urgent issues that could pose a threat to the financial system as follows: high volatility of interest rates; delayed privatization of UCBL; and presence of small problem banks. The Supervision

function had successfully resolved UCBL and the small banks as at the time of writing this report. The issue of high volatile interest rates remains a concern that is addressed through BOU's role of ensuring a stable macroeconomic environment.

4.4.0 NATIONAL PAYMENT SYSTEM DEVELOPMENT

During the year 2001, a number of significant payment system developments took place. These were in the areas of standards, payment system oversight, payment technology, electronic clearing and Internet banking.

(a) Issuance of Standard Cheques

During the year, all banks issued cheques that conform to the National Cheque Standard. This was an important and critical step towards the implementation of electronic cheque clearing in the country.

(b) Electronic Clearing System

At the beginning of 2001, Bank of Uganda contracted a U.K. based company to develop software for the electronic clearing system. The software was developed, installed and tested in August 2001, and was in operation by end of the period under review. It supports both debit and credit clearing.

(c) Establishment of an Autonomous Clearing House

In order to promote efficiency and stimulate innovations in the clearing process, worldwide clearing houses are increasingly being run independent of the Central Bank, and in some cases are privately owned. Against this background, a business plan and articles and memorandum of association were drafted for the establishment of an autonomous clearing house named Uganda Bankers Automated Clearing Ltd (UBACL). The papers were reviewed by the member clearing banks and subsequently adopted. Floatation of UBACL is currently being held up by various legal interpretation of Section 5(i) the Bank of Uganda Statute 1993 which provides for the Bank of Uganda to be the sole facilitator of the Clearing House for cheques and other financial instruments of financial institutions.

(d) Payment System Oversight

A payment system oversight framework was discussed and adopted during the year under review. Working closely with Supervision Function, the National Payment

System Secretariat will be periodically collecting, collating, analysing and interpreting data on payment system developments, with a view to determine the trends and strategic direction of the national payment system.

(e) Failure to Settle Rules

In order to strengthen and streamline the management of risk in the electronic clearing system, a draft set of “Failure to Settle Rules” that conform to the requirements of the BIS Core Principles for Systemically Important Payment Systems (CPSIPS) was developed. The rules are currently being reviewed.

(f) Internet Banking

During the year, one of the banks introduced internet banking. The system facilitates a customer, equipped with a password, to access account balance and carry out other banking transactions.

(g) Automated Teller Machine (ATM) Growth

In order to promote customer convenience and flexibility in the payment system, the number of ATMs installed by banks has steadily grown. From 15 ATMs at the beginning of 2001, which had been installed by four banks, the number grew to 25 by the end of the year under review. As the number of ATMs grows, there may be need to explore the viability of establishing a switch that can, besides other functionality, enable bank customers to withdraw cash from an ATM of any bank terminal. There are plans by banks to install ATMs in more upcountry centers in the next financial year.

(h) Formation of SWIFT User Group

During the year, a SWIFT User Group was formed, with a view to representing the interests of SWIFT users to SWIFT. The number of banks connected to SWIFT increased from less than ten at the beginning of 2001 to over ten by the end of year under review.

(i) Sensitisation of the Public on Payment Issues

A number of payment system articles were published by the NPSS staff in the Ugandan Banker, a journal of the Uganda Institute of Bankers. Furthermore, adverts on the introduction of new standard cheques and the implementation of electronic clearing were placed in newspapers and announced through radio stations. Sensitisation of the public is a continuous process and will be enhanced during the year 2002.

(j) Review of the Payment System Legal Framework

The current legal and regulatory framework for the payment system is inadequate and requires review. Terms of reference (TOR) for the recruitment of a legal consultant to review the existing laws and propose amendments and new laws were developed, discussed and adopted. The recruitment process is currently underway.

4.5.0 DEPOSIT PROTECTION FUND

During 2001, the Supervision Function initiated a study on the Deposit Protection Fund in Uganda. The objective was to attempt to review its mandate, structure and operation. A committee of six (6) staff members was appointed by the Executive Director Supervision Function to prepare a report on the proposed study. The report of the Study Group on Deposit Insurance of the Financial Stability Forum (FSF) issued in September 2001 represents the internationally best practice on deposit insurance. Therefore it has been adopted as a basic framework for discussions and a basis for the approach to reforming the Deposit Protection Fund in Uganda. On going monitoring of the activities of the FSF Study Group on deposit insurance enables the committee to assess the latest international developments in this regard. During the year under review, the committee had not finalised the study. The Fund will continue to exist and function as a “pay box” and membership will continue to be compulsory and prefunded. The premium will be payable limited to an insurable deposit currently set at Shs.3,000,000= per depositor. It is anticipated that the committees’ report will be issued in the year 2002.

Overall performance of the Fund

According to the audited financial statements of the Deposit Insurance Fund as at 30th June 2001, although the total assets base of the Fund is still low, there has been some improvement from the financial year which ended on 30th June 2000. Total assets increased by Shs.3.3 billion, from Shs.6.9 billion in 2000 to Shs.10.2 billion as at the end of the period under review. Total liabilities remained at Shs.37.8bn over the same period due to the unpaid borrowing from Bank of Uganda. Therefore the net liability to the Fund was Shs.27.6 billion.

Contributions received from member banks and credit institutions increased by Shs.587.0 million from Shs.1,580.1 million as at the end of June 2000 to Shs.2,167.1 million as at 30th June 2001.

The Fund continues to hold investments in treasury bills. The investment increased by Shs.1.8 billion from Shs.6.5 billion in the year 2000 to Shs.8.3 billion as at 30th June 2001. The Fund earned interest amounting to Shs.1,232.7 million from the investment during the period under review. As at 30th June 2001, payments to depositors during the year amounted to Shs.63,457,350.

Post balance sheet date events indicate that the Ministry of Finance, Planning and Economic Development refunded Bank of Uganda in July 2001. Therefore the deficit of the Fund at Shs.27.6bn shall be covered. However, due to the small size of the Fund after the above transaction, it is still insufficient to cover all insured depositors.

4.6.0 FOREIGN EXCHANGE RISK MANAGEMENT

During the year under review, the Supervision Function with the assistance of the Advisor Bank Supervision was involved extensively in drafting foreign exchange risk management guidelines for foreign exchange dealers in licensed financial institutions under the Financial Institutions Statute 1993. Based on extensive research in international best practices, standards and principles of risk management, small teams of Supervision Function staff prepared draft guidelines to be submitted to senior management of Bank of Uganda and subsequently to be presented to the Uganda Bankers Association. The contents of the draft foreign exchange risk management guidelines are summarised below:-

- **Forex Risk Management Framework**

Like the case with the other risk categories, the foreign exchange risk management framework must encompass the following critical areas: Board and Management oversight, Policies, Procedures and Limits, Risk Measurement, Monitoring and Management Information Systems, and Internal Controls. These are all relevant to the management of this kind of risk.

- **Board and Management Role in Risk Management**

The Board of Directors and senior management of financial institutions are ultimately responsible for the institution's exposure to foreign exchange risk and the level of risk assumed. Well-articulated policies, setting forth the objectives of the financial institution's foreign exchange risk management strategy and the parameters within which this strategy is to be controlled, are the focal points of an effective and prudent foreign exchange risk management program.

The Board of Directors should review and approve the foreign exchange risk management policies and procedures based on recommendations by senior management of the institution. The foreign exchange risk management program should address the establishment and implementation of sound and prudent

foreign exchange risk management policies. Management is therefore charged with developing foreign exchange risk management policies and developing and implementing procedures to measure, manage and control foreign exchange risk within these policies. This shall ensure that the foreign exchange risk is controlled and managed within the foreign exchange management program.

- **Procedures and Limits**

Financial institutions should have a written policy governing activities in foreign currencies. The purpose of a written policy is to communicate the expectations of senior management and the board of directors to management and staff. The policy should be reviewed and approved by the board of directors. In general, it should reflect the tolerance of the board and senior management for the various risks arising from foreign currency activities.

The policy should include a formal ratification of the limits governing foreign exchange operations. Normally the management of the foreign department will have proposed these internal limits. Overnight open position limits should be established by currency, and for all currencies combined, using an acceptable aggregation method. Where appropriate, intra-day limits should also be established.

Limits should be based on estimates of loss potential. Generally, limits for more volatile and less liquid currencies should be lower than those for stable and liquid currencies. If positions are relatively small, it may be acceptable to use a single limit for a group of hard currencies combined.

The mechanisms by which counter-party credit, settlement limits and country limits are established and allocated to the foreign department should be defined in the policy. In addition to an aggregate credit limit for each counter-party, a settlement risk sub-limit should be established for the size of a transaction (or transactions) that can be settled on any given day. Country limits should be established for total exposures to all counter-parties based in each individual

country. The policy should provide that the limits are clearly defined and communicated to the foreign department and that they are periodically reviewed and updated.

The policy should specify minimum accounting standards and standards for the revaluation of foreign currency positions. It should include the frequency with which such revaluations should be performed for both management and accounting purposes. For accounting purposes, revaluations generally should be performed at the time of any required periodic reporting to the Bank of Uganda. For management information purposes, more frequent revaluations should be performed, depending on the size and relevance of the foreign currency positions. The policy should establish revaluation standards that preclude the deferral of losses on foreign exchange positions for internal reporting purposes.

Overall, senior management should ensure that written board–approved policies and guidelines clearly identify the following:

- Scope of the dealing activity;
 - Type of services offered;
 - Definition of jobs and responsibilities for dealing and operational functions;
 - Currency position limits;
 - Overnight position limits;
 - Dealing and counter-party limits;
 - Code of conduct for the foreign exchange personnel;
 - Operational controls;
 - Reporting requirements; and
 - Profitability expectations and tolerance for losses
-
- **Management Information System**

Accurate and timely information systems are critical to the management of foreign currency positions, and for ensuring compliance with relevant risk limits. Financial

institutions should devote the resources necessary for generating such information. Standardised reports should be designed to communicate the information regarding open foreign exchange positions, forward interest rate positions, liquidity positions, counter party and country exposures. Positions and exposures should be reported on a consolidated basis. Such reports should be prepared and verified by persons not responsible for transacting foreign currency business.

At the minimum, the system should be programmed to avail the following reports:

- net overnight positions by currency;
- maturity distribution by currency, assets and liabilities, and exchange contracts;
- outstanding contracts by settlement date and currency;
- outstanding contracts with other financial institutions;
- total value of outstanding contracts, spot and forward;
- profit and loss, totals and comparison on previous day's data;
- market value of off-balance sheet products;
- aggregate dealing limits;
- limit or line excesses; and
- valuation of option contracts, if any.

- **Measuring and Limiting Exchange Rate Risk**

Measuring risk is very critical to understanding the potential loss an institution may be exposed to in event of any loss. A common approach to measuring and limiting exchange rate risk is to limit the size of the open positions in each currency as of the close of business each day. Net open positions then may be expressed as a percent of the financial institution's capital, assets or some other benchmark. Limits are established for either the nominal size of the position or the percentage. Using this approach managers attempt to control exchange rate risk where the size of net open positions is the proxy for the potential loss that such a position might produce.

This approach can be enhanced by directly estimating the potential loss that an open

position might produce. In effect, this makes explicit what is implicit in the approach described above. Management is interested in limiting the potential for losses. Management also determines the size of the loss that would be incurred should the exchange rate move against the financial institution's open position. To make this estimate management makes one or several assumptions about potential adverse exchange rate movements. It computes the loss that would be incurred by revaluing the financial institution's open position at this hypothetical exchange rate. The size of the potential loss produced in this manner is subjected to a limit that may either be expressed in terms of the nominal amount of the loss, or as a percentage of a benchmark, such as projected earnings or total capital. Normally, management's principal goal is to provide strong assurance that foreign exchange losses will not substantively diminish the total earnings of the financial institution.

Independent Review

The internal audit function of the financial institution should review and assess the foreign exchange risk management process. It should ensure that foreign exchange traders/dealers observe their instructions and the code of behaviour required of them, and that accounting procedures meet the necessary standards of accuracy, promptness and completeness.

The audit committee should, among other duties, review periodically the foreign exchange risk management process. The committee can greatly enhance the quality of reports and the reasonableness of foreign exchange risk management information supplied to the board, management and Bank of Uganda.

4.7.0 REGULATORY AND LEGAL FRAMEWORK DEVELOPMENTS

As indicated in the Annual Supervision Report 2000, one of the main objectives of the Bank Supervision Function is to ensure that the legal framework for financial institutions in Uganda remains relevant and current. The Function will fulfill this objective only if it ensures that the legal framework remains in line with the international regulatory standards and market developments. Therefore the Function has to review the financial institutions legislation on an on-going basis.

This section provides a brief overview of the proposed Financial Institution Bill, 2001 and of the recent proposed amendments. The developments in the Microfinance sector in Uganda and the Micro Deposit taking Institutions Bill 2001 are also covered.

4.7.1 Amendments to the Bank of Uganda Regulations relating to the financial Institutions

- The proposed amendments of the Financial Bill 2001, were described in some detail in the Annual Supervision 2000 report. The review of the Bill continued in the year 2001 with the objective of addressing other areas of significant supervisory concern and also implementing the core principles for effective banking. The updated Financial Institutions Bill 2002 bill be tabled in parliament in the coming year.
- During the year under review, existing regulations were reviewed and amended in line with acceptable international standards recommended by the Basel Committee on banking supervision. Unlike the guidelines, the regulations have the force of law and failure to comply therewith may lead to penalties.

A brief overview of the most important amendments to the regulations is as follows:

a) Licensing Requirements

This regulation establishes clear and objective criteria for reviewing applications for engaging in "financial institutions business" in Uganda and outlines the procedure to be followed in the licensing process. It will also enable the Central Bank to determine whether new and existing financial institutions have fit and proper shareholders, adequate financial strength and management with sufficient expertise and integrity to operate the institution in a sound and prudent manner.

b) Risk- Based Capital Requirement

Under this regulation, the objective is to ensure that each institution maintains an adequate level of capital to protect its depositors and to promote public confidence. It prescribes guidelines for computing the capital adequacy ratio according to the Basel Committee's capital adequacy framework 1988.

c) Loan Portfolio Classification

The Asset Quality regulation is intended to ensure that all loans and advances granted by financial institutions are evaluated regularly using objective and subjective criteria and that adequate allowance for loan losses or provisioning is maintained at all times. It also prescribes the proper accounting treatment for accrued but un-earned interest on non-performing assets.

d) Lending Limits

The regulation on lending limits is intended to prevent a financial institution from undertaking undue risk by accepting large exposures to a single borrower or a group of connected borrowers to any of its directors or officers or to any other related persons. It also seeks to ensure that all insider loans and advances are made on terms not more favorable than those afforded to other borrowers.

The regulations covering large extension of extension credit have been amended so that they fully comply with the core principals for effective banking supervision. Consequently, a financial institution or a controlling company may not incur an exposure to a single borrower or a group of connected borrowers or to any of its directors or officers or to any other related persons that exceeds 25 percent of the

financial institution's capital and reserve funds without the Central Bank's approval. Furthermore, the total of all large exposures exceeding 10 percent of the institutions' qualifying capital and reserve funds may not exceed 800 percent of qualifying capital and reserve funds. Any excess exposure will call for additional capital injection.

e) Liquidity and Funds Management

The purpose of this amended regulation is to ensure that a financial institution maintains adequate liquidity and manages the liquidity risk through frequent reporting and monitoring of liquidity position.

f) Foreign Currency Exposure Limits.

This regulation is aimed at determining the open foreign currency position limits of all licensed financial institutions in Uganda. It also seeks to establish adequate procedures that would ensure the determination and accurate reporting of these positions.

g) Corporate Governance

A strong and sound financial sector cannot be achieved if sound corporate governance is not in place in supervised institutions. Consequently, the Bank of Uganda has a strong interest in ensuring that there is effective corporate governance within every licenced financial institution.

The proposed new regulation seeks to ensure that a financial institution will maintain appropriate corporate governance, management, internal-control and risk-management systems. The operating controls and risk-management procedures have to be consistent with the strategy of the institution. The institution has to be capable of submitting all required statutory and prudential information in an accurate and timely manner. The management of the financial institution has to identify in a timely manner activities that may have a negative impact on the institution and the wider financial sector and must report such cases to the Central Bank.

h) Anti-Money Laundering

The Bank of Uganda has been collaborating with various stakeholders in the country to ensure that anti-money laundering legislation is introduced to guard against financial institutions being used to launder the proceeds of crime. The Uganda Anti-Money Laundering Committee (UAMLC) was established in August 2000 comprising of representatives of government departments, selected institutions, and Bank of Uganda. The Committee was given the task of drafting the appropriate anti-money laundering policy guidelines and registration. The policy is ready for discussion by Cabinet.

4.7.2 Regulatory Developments in the Microfinance Sector in Uganda

As reported in the 2000 Annual Supervision Report, the regulatory framework for micro deposit-taking institutions in Uganda became concrete in 2001, when the Micro Deposit-Taking Institutions Bill, 2001 was finalised for gazetting. During 2001, the Bank of Uganda in conjunction with the German Technical Co-operation (GTZ) participated in several forums at which various issues pertaining to the regulation and supervision of Microfinance institutions in Uganda were discussed.

In preparation for the implementation of the Micro Deposit- Taking Institutions Bill, 2001, the GTZ/FSD and the Supervision Function (NBF1 department) set up an internal project team (IPT) to focus on all the preparatory work for the regulatory and supervisory framework for micro deposit taking institutions in Uganda.

4.7.3 The BOU Proposed framework for Risk Based Supervision of the MDIs.

The Micro Deposit – Taking Institutions Bill 2001 requires Bank of Uganda to formulate performance-monitoring system and benchmarks that will facilitate the effective supervision of Micro Deposit Taking Institutions (MDIs). In accordance with the current best practices supervision of financial institutions the NBF1 department has finalized proposals for risk-based supervisory framework. The NBF1 department held a consultative workshop with the key players in the Microfinance field aimed at getting a feedback on the approach.

The major elements of this approach are as follows:

- Identify areas of greatest risk of MDIs as the starting point: These are
 - **Governance and Ownership**
 - **Management Risk**
 - **Credit Risk**
 - **Liquidity Risk**
 - **Interest Rate Risk**
 - **Operational Risk**
- Focus supervisory resources on the areas of highest risk within MDIs
- Assessment of past performance
- Quantitative and qualitative assessment
- On-site supervision and off-site surveillance
- Licensing
- Information disclosure
- Corporate policies governance, internal control and procedures manual, quality of MIS, professional staff capacity.

In order to put the above framework in perspective, the Department of Non Banking Financial Institutions conducted a survey on selected MFIs. The survey provided the Internal Project Team with an indication of the trend of performance indicators in the sub-sector. From this survey, it was possible to assess the general trends in the selected microfinance institutions. The survey results were intended to test only the quantitative aspects of the benchmarks to be proposed.

Benchmarks were proposed, based on an analysis of the performance indicators and international best practice. Quantitative indicators will be tested in the forthcoming major surveys.

5.0.0 INTERNATIONAL SUPERVISORY ISSUES

5.1.0 CORPORATE GOVERNANCE

Financial Institutions mobilize deposits from the public, which they then invest in different ventures across the economy. These different investment ventures often bear varying levels of risks. However, depositors in financial institutions have no opportunity to constantly monitor the safety of their funds that financial institutions trade with. Consequently, to assure depositors that the funds held by financial institutions are safe, there is need to have in place a dependable governance practice that is transparent and accountable. This is possible through the institution of, “Good Corporate Governance” best practices in all financial institutions. For “Good Corporate Governance “ best practices to be firmly rooted in financial institutions, the following pre-conditions must be established in the financial sector:

- Well-designed and enforceable law, which specifies the duties and obligations of shareholders, directors, management, depositors, external auditors, regulators, etc.
- High quality disclosure requirements for financial institutions based on robust accounting and auditing standards.
- Strengthen market disciplines on financial institutions as an important ingredient in promoting sound corporate governance and risk management so that prudently managed financial institutions are rewarded by the market, while mismanaged ones face market penalties.
- Effective banking supervision arrangement with particular emphasis on supervisory policies that encourage sound governance and risk management practices.

- Ensure financial institutions have adequate representation of qualified and experienced non-executive directors with no conflicts of interest.

Responsibilities of Shareholders:

Shareholders appoint the board of directors and external auditors at the annual general meetings. It is prudent that board appointments consist of a mix of proficient directors, each of whom is able to add value and promote independent judgement to bear on the decision making process. The board is accountable to the shareholders by presenting annual audited statements of accounts of the financial institution at the annual general meeting. The external auditors represent the interests of the shareholders through auditing financial statements and ensuring that they represent a true and fair picture of the financial condition and performance of the institution. Where shareholders are not satisfied with the performance of the board, appropriate action like dissolving the board and appointing a new one can be effected. In the Ugandan case, Bank of Uganda adds value to the board selection process by ensuring that the nominees are vetted under the “fit and proper” test.

Responsibilities of the Board of Directors:

The Board is charged with the following responsibilities:

- Appointing a competent management team that can run day-to-day operations of the business, monitor and evaluate the implementation of strategies, policies, performance criteria and business plan.
- Setting corporate objectives and strategic plans.
- Aligning corporate activities and behaviours with the expectation that financial institutions will operate in a safe and sound manner, and in compliance with applicable laws and regulations.

- Protecting the interests of depositors and shareholders.
- Formulating credible operational policies and procedures that can mitigate risks.

The Board further monitors the performance of management through periodic meetings at which the financial performance of the financial institution is evaluated against the annual work-plan/budget. This process imposes accountability on management as it ensures that the targets set out by the board are adhered to, short of which appropriate action can be taken against management.

Role of Bank of Uganda in strengthening Corporate Governance.

Bank of Uganda has a duty to foster a sound and stable financial sector, where depositors' funds are safe. To achieve the above objective, "Good Corporate Governance" best practices must be instituted in all financial institutions. Consequently, prior to appointment of all board members and key executive officers of commercial banks, Bank of Uganda conducts a vetting process under the "fit and proper" test to ensure that qualified and competent persons are appointed to manage depositors' funds. Besides vetting board members and key executive officers of banks prior to assuming office, if any one of them commits a breach of the fiduciary responsibilities while in office, Bank of Uganda reserves the right to remove such persons from office. Consequently, a continuous process of monitoring accountability and transparency has been established, which will go a long way in ensuring that the fiduciary responsibilities placed upon members of the Board and executive officers are carefully executed.

5.2.0. MONEY LAUNDERING

Currently, there are four (4) laws in Uganda that address albeit partially, the phenomenon of money laundering. These are the Penal Code Act (Cap. 106, Laws of Uganda (L.O.U)), the Prevention of Corruption Act (1970) (as amended), the National Drug Policy and Authority Statute (1993) and the Leadership Code (1992). These laws however, do not refer directly to money laundering. They are aimed only at various aspects thereof, e.g. drug trafficking. Apart from any conduct that may fall within the scope of these laws, no other instance of money laundering is currently punishable under the country's criminal laws.

Increased integration of the world's financial systems and the removal of barriers to the free movement of capital across international borders have enhanced the ease with which money from criminal sources can be laundered, and have complicated the tracing process. Uganda, as one of Africa's growing financial centres, has an important role to play in the combating of money laundering. Therefore, a clearly defined regulatory framework, combined with an effective enforcement structure is necessary.

The Government of Uganda is aware of the urgent need to redress the deficiencies of the existing legislation. Following the signing of the Memorandum of Understanding on 27th August 1999 by the member countries of the East and Southern Africa Anti Money Laundering Group (ESAAMLG), the Uganda Anti-Money Laundering Committee (UAMLC) was inaugurated in August 2000. The Committee convened several meetings, which resulted in drafting a policy document entitled " Uganda's Anti Money Laundering Policy". The draft policy document states the strategies to guide the fight against money laundering in Uganda. The strategies include legal, regulatory, enforcement and the assignment of responsibilities to key players in combating money laundering in Uganda. The draft policy document takes fully on board among other things the 40 recommendations and the Special Recommendations on Terrorist Financing by the Financial Action Task Force on

money laundering (FATF). This draft policy document will form the basis for the formulation of a comprehensive anti-money laundering legislation for Uganda. It is envisaged that one central reporting agency (the Financial Intelligence Authority) will be established to handle all reports of suspicious transactions that may involve money laundering. It is anticipated that once the legislation has been passed, the onus for implementation of the necessary procedures and programmes to comply with the legislation shall rest on the players in the market, and that every person has a responsibility to report suspicious transactions to a delegated person or authority.

Institutions that are often exploited in the money laundering process, such as insurance companies, banks, estate agents etc, may be expected to provide their staff with training in order to create greater awareness of the phenomenon and to facilitate the reporting and investigation of suspicious transactions.

5.3.0. CONSOLIDATED SUPERVISION

Genesis

Banks very frequently carry on activities through subsidiaries and other related companies. In most cases these subsidiaries or related companies are not supervised / regulated yet their activities affect the soundness of the banks. In theory the principle of limited liability means that banks have no legal responsibility for losses of their subsidiaries, but in practice the bankruptcy of a bank's subsidiary is certain to weaken depositors' confidence in the banks. Consolidated supervision therefore aims at capturing material or potential activities in the group as a whole.

Definition

The Financial Services Authority of the UK has defined consolidated supervision as ***“an overall evaluation both qualitative and quantitative of the strengths of a group to which a bank belongs to assess the potential impact of the Group Company on the bank”***. Consolidated supervision should however never be construed as supervising all the companies in the group to which the bank belongs but to supervise the bank as part of the group. Likewise consolidated supervision is looked at as a supplement to but not a substitute for “solo” supervision. Banking supervision on solo basis may be ineffective in circumstances where a bank belongs to a group either as parent / holding company, subsidiary¹ or an affiliate². Solo supervision in this scenario would consider only the limited activities, risks and rewards of the entire group.

Quantitative consolidated Supervision.

¹ A company is deemed a subsidiary of the reporting bank if the bank holds more than 50% in nominal value of that company's equity share in capital

² Affiliated company means a company or enterprise that controls or is under common control with a financial institution. Control means the ability to exercise dominant influence over the management or policies of the company and can be exercised through ownership ability to exercise voting rights or ability to control the election of majority board members.

Quantitative consolidated supervision seeks to take a wider account of the risks posed by group companies and business units and the extent to which they might have a material bearing on the reputation or financial soundness of the bank. It involves the preparation of returns covering the group or subgroup including the bank, as part of the risk assessment. The assessment is made in relation to a group's significant units in terms of their potential material bearing on the group. Quantitative supervision focuses on controls, organization and management. It also looks at the overall environment of the bank and the main parts of the group and takes account of these risks, which are not internally quantifiable including operational, litigation reputational risks etc.

Qualitative consolidated supervision

Qualitative consolidated supervision includes a qualitative assessment of the whole group including the activities of the group companies not incorporated in the consolidated returns, because the nature of their assets is such that their inclusion would not be meaningful. This assessment includes for example consolidation of the controls within the group etc. i.e. the additional consolidation beyond quantitative is what is known as qualitative consolidated supervision.

Rationale for consolidated supervision

1. Moral Hazard

This occurs when a bank or its controlling company, notwithstanding the absence of an actual legal liability, feels obliged or is forced to assist an associate or other entity that is in financial difficulties. Assistance may be given with the view of preventing the risk of contagion and keeping the good name of the bank or bank controlling company.

2. Double gearing

Consolidated supervision eliminates the concept of double gearing. Double gearing occurs when cross-holdings of shareholdings between institutions in a

group takes place, thereby sometimes artificially increasing the overall capital adequacy of the group. By evaluating the capital adequacy of the group as a whole, the double gearing effect is eliminated.

3. Contagion risk

Contagion risk can best be described as the risk that a problem or problems in one or more associate entities rub off onto the bank, leading to negative implications for the bank. In some cases, the implications can be so serious that the bank fails as a result of the problems. Although contagion risk is so difficult to measure and quantify, it is a risk that bank management needs to be constantly aware. Apart from the financial implications of contagion risk, a more intangible risk also exists, namely that of the reputation of the bank or bank controlling company.

4. Systemic risk

Systemic risk is an issue that is always at the forefront of the supervisor's mind. Consolidated supervision is a powerful tool in preventing the systemic risk that can arise through the contagion effect in the market. It is however important to note that contagion of banks can also take place from outside the banking group, for example where there is a general lack of confidence in certain types of or sizes of banks e.g. the so called '*small bank syndrome*'

Scope of consolidated supervision.

Consolidated supervision is done both at National and International levels. At national level consolidated supervision would involve supervision of the bank controlling company, subsidiaries and affiliates. Supervision of banks would involve looking at the operations of the group to which they belong.

Consolidated Supervision at International level

Banking business conducted outside the border of the home country should be supervised as well as banking business of foreign banks within the host country

should be supervised. The supervision of international banking group was strengthened in 1992 when the Basle committee on Banking Supervision issued a paper entitled “ *Minimum standards for the supervision of international banking groups and their cross-boarder establishments*”. The intention of these standards was to ensure that both the host country and home country authorities are fully aware of the methods of supervision carried out in their respective countries so that no international banking group escapes adequate supervision.

Minimum standards

- All international banking groups and international banks should be supervised by a home-country authority that ably performs consolidated supervision and adheres to the Basle Capital adequacy standards.
- The creation of cross boarder banking establishment should receive the prior consent of both the host and home country supervisory authorities. Home country supervisor must confirm to the host country supervisor that approval was given to the banking group to establish a subsidiary or branch in the host country.
- Supervisory authorities should possess the right to gather information from the cross-boarder banking establishments of the banks or banking groups for which they are the home –country supervisor. The home-country supervisor must confirm to the host the extent to which it may share prudential information with the host supervisor and undertakes to advise the host country supervisor of any matters that may have an impact on the bank in the host country.
- If host –country authority determines that any one of the foregoing minimum standards is not met to its satisfaction, that authority could impose such restrictive measures necessary to satisfy its prudential concerns, consistent with those minimum standards including the prohibition of the creation of the banking establishment.

Knowledge of the structures and risk of the group

Supervisors must understand the business conducted in each material entity in the group, and be able to evaluate potential moral and contagion risk. Information on the group is important because it helps the supervisor to:

- Determine solvency of shareholders
- Ensure that funds are available to support bank or bank subsidiaries in times of crisis
- Evaluate possible domination by major shareholder and determine who is in control
- Determine whether the group is adequately capitalized to sustain both the banking and non-banking entities
- Determine the exposure of all entities within the group to the bank i.e. exposure of all entities within the group to the bank must be aggregated to obtain group's exposure to the bank
- Limited knowledge and information of group structure renders consolidated supervision ineffective.

The rationale for consolidated supervision –Uganda's perspective.

Background

In Uganda, we have both foreign and locally owned banks whose parent / holding companies are foreign and/or locally domiciled.

Bank of Uganda (BoU)supervises these foreign banks as the host country. It is also true that the home supervisors do supervise these banks as well. What is lacking is that the host supervisor does not have direct channel of gathering / sharing information about the parent companies of these banks. BoU assumes the home country authority performs consolidated supervision and adheres to Basle capital adequacy standards.

In the latter category, we have two local banks that are either subsidiaries or affiliates whose parent companies are either financial or non-financial companies that are not

necessarily regulated by independent regulatory authority. The holding company of one of the banks though foreign owned is locally domiciled and is a financial institution as well but currently not supervised by any independent regulatory supervisory authority. The principal activities of the company consist of provision of banking, loan equity, lease finance and letting out property for development of business in Uganda. These activities require adequate funding. The subsidiary is thus likely to be called upon to fund the parent company activities. BoU needs to safeguard depositors' funds and ensure that such funding is done at arms length. This can be achieved if BoU is able to evaluate the strength of the group to which the bank belongs but not on a solo basis.

Whilst there are no legal liabilities by these banks to their parents, companies or affiliates, their operations are vulnerable to the mentioned risks. The past experience with the defunct Greenland Bank (in liquidation) should expedite the decision to adopt consolidated supervision. BOU supervised Greenland Bank (in liquidation) on a solo basis and in the process its dealings with the affiliated companies and the parent company evaded the BoU supervision arm. The consequences have been costly to the sector and consolidated supervision aims at minimizing such costs.

Way forward / action plan

The Uganda financial sector is ripe for consolidated supervision. The past experience of the closed banks especially Greenland Bank Ltd. (in liquidation) and the current set up / ownership of some financial institutions are strong pointers in support of our endeavors to adopt consolidated supervision. The necessary provision for consolidated supervision has been made in the proposed Financial Institutions Bill 2001.

5.4.0. REGIONAL CO-OPERATION INITIATIVES

In line with the spirit of cooperation with member states, Uganda has continued to participate in regional and international initiatives. Bank of Uganda has actively supported activities of ESAF in providing prudential guidance and standards in order to enhance safety and soundness of banks in member countries and stability of the financial system in the region. The Basel Committee on Bank supervision continues to support regional initiatives like ESAF in promoting effective supervisory standards worldwide through the release of supervisory international guidelines for banks.

- **East and Southern African Banking Supervisors Group (ESAF)**

The ESAF members signed a Memorandum of Understanding, in 1997 which includes the following objectives:

- (a) Promotion and enhancement of the quality, nature and ambit of banking supervision conducted by the members of ESAF.
- (b) Harmonization of banking supervisory philosophies and practices within the region.
- (c) International cooperation towards the development and maintenance of stable and sound banking institutions within the region.
- (d) The implementation and maintenance of internationally acceptable standard of banking supervision within the respective supervisory jurisdiction of the members.
- (e) Contribute towards ensuring a healthy and sound banking system in which depositors are given greater protection within the ESAF region.
- (f) Subscription and adherence to the minimum standards, pronouncements and directives pertaining to the supervision of banks issued by the Basel Committee.

During the year under review, implementation of regional initiatives were as follows:

- **Compliance with Core Principles for Effective Banking Supervision**

ESAF members endorsed the Core Principles for Effective Supervision and are committed to implement them through a consultative framework among the member countries. Compliance with the Core Principles For Effective Supervision remains an important objective for the ESAF members. Members carry out a periodic self - assessment of compliance along the Core Principles Methodology published by the Basel Committee on Banking Supervision. The objective is to raise awareness of the underlying principles by conducting regular training of supervisors in the region. In addition, the self- assessment constantly promotes adherence to the Core Principles and sets benchmarks for their supervisory systems.

During the period under review, Bank of Uganda responded to the self -assessment questionnaire on implementation of the Basel Core Principles. Although Bank of Uganda was generally compliant with the essential criteria, some principles are yet to be complied with.

- **Accounting standards**

ESAF has been encouraging harmonization of accounting practices and transparency in the banks within the region, through publication of audited financial statements of financial institutions. In order to enhance this process, the International Accounting Standard 30 (IAS) regarding the publication of audited financial statements of commercial banks was forwarded to each supervisory authority in the region. The publication of audited financial statements will enhance transparency of banks through more disclosure details and will provide scope for a comparative analysis of banks in the region. Accounting disclosures agreed upon by ESAF is contained in the proposed Financial Institutions Bill 2002.

In view of the above move during trilateral meetings and on site examinations, Bank of Uganda must be satisfied that financial statements are prepared in line with consistent accounting policies and practices that enable the supervisor obtain a true and fair view of the financial condition of the institution.

- **On- site surveillance**

ESAF has made studies in member countries on on-site surveillance. The information is to be used for determining minimum standards for on site supervision in the ESAF region and to harmonize on site standard best practices. Specific emphasis was made on risk-based approach of on site examination in line with the Basel Core Principles for Effective Banking Supervision.

During the year under review, Bank of Uganda adopted the risk-based examination approach geared towards improving the planning process of bank examination. This enables Supervision Function to prioritize and allocate resources to areas of high risk and incorporating current and prospective view of the institutions risk profile. This Risk- based approach therefore, enables examiners to determine the underlying problems of financial institutions and enables adequate evaluation of effectiveness of an institutions risk management practices.

- **Provisioning standards**

ESAF also made a study among member countries on their loan loss provisioning practices. Harmonization in this area is considered very critical. The information obtained will be used to recommend common standards of provisioning for identically perceived risks. During the year, Bank of Uganda revised provisioning requirements for non-performing loans effective September 2001, which are in line with International best practices.

- **ESAF training programs**

Since inception, identification of training programmes for ESAF members has been one of the groups' core priorities. Training requirements of ESAF were raised with the Basel Committee of Banking Supervision and a subcommittee was assigned the task of identifying ESAF training needs at basic, intermediate and advanced level and make recommendations to avoid duplication of courses. During the period under

review, several high level seminars were conducted by ESAF with the support of the Financial Stability Institute, the IMF and the World Bank.

With assistance from USAID, the Barents Group conducted courses on the Core Principles and new techniques of banking supervision at the Bank of Uganda for officers' of middle and senior management.

During the period under review, the Financial Stability Institute (FSI) of the Bank for International Settlements held a seminar for senior supervisors in ESAF in Namibia from 12-16 November 2001. The purpose of the seminar was to promote high-level exchanges between supervisors. Uganda was selected as the next country to host the Financial Stability Forum to cover topics on the New Capital Accord in 2002.

- **Harmonization of Licensing Standards**

A proposal on the criteria for sharing information among the ESAF membership regarding issuing of new banking license and renewing licence for operating banks and financial institutions has been distributed to the Executive Committee for further discussion. A subcommittee of ESAF was assigned with drawing up a memorandum of understanding on cross border licensing. The proposed Financial Institutions Bill 2001 incorporated aspects on cross border Licensing.

- **Harmonization of Banking Supervision Project: Business Processes and Supporting Information Systems**

The project description is to identify the shortcomings and weaknesses of the current legislation, regulations, procedures and systems in the ESAF region; to provide the necessary resources to design a generic architecture of the business; to investigate and identify a cost effective solution to support the architecture; and to ensure the implementation of quality systems.

This project was initiated in June 1997 and following subsequent workshops, business process models were developed and presented by SADC IT Forum in

November 2000. In March 2001, the ESAF Executive Committee decided to support the IT solution to be developed by SADC IT Forum.

The Central Bank of Mozambique, Banco de Moçambique, volunteered to develop and implement the system with the help of the South African Reserve Bank. In November 2001, they contracted T-Systems to develop the solution and implement it, first in Banco de Moçambique, and thereafter, in other ESAF countries, that would decide to implement it.

In December 2001, representatives from ESAF Central Banks met to update the business specifications and drew up a number of conclusions and recommendations. It was decided then that a meeting takes place in January 2002 to finalize the Project Plan and sign off the Project Definition Report. According to the plan, the definition and development of the solution are expected to commence in 2002. Implementation of the system in Banco de Moçambique is also expected to be completed in 2002 and other Central banks would follow thereafter, probably from 2003 onwards.

Money Laundering

Member countries of East and Southern African Anti Money Laundering Group (ESAAMLG) agreed in a Memorandum of Understanding signed in 1999 to adopt and implement the Forty Recommendations of the Financial Action Task Force (FATF) and also implement any other measures contained in multilateral Agreements and initiatives to which they subscribe, for the prevention and control of the laundering of the proceeds of all serious crimes. Significant among these multi lateral agreements and initiatives is the Basel statement of Principles on “Prevention of Criminal Use of the Banking System for the purpose of Money Laundering”.

The Memorandum of Understanding mandates the member states to set up National Committees comprised of a broad representation of the relevant disciplines: Legal and Judicial, Financial and Law enforcement.

COMESA

Uganda remains committed to initiatives in the COMESA region. The first meeting of Bank Supervisors was convened in Lusaka Zambia in the second quarter of the year, in compliance with the decisions of the 4th summit of COMESA Authority Heads of State and Governments. The seminar objectives were among others, to review and exchange ideas and experiences in Banks Supervision and come up with a program of action for harmonizing Banking Supervision in the COMESA region. In the meeting, it was resolved that Banking Supervision be harmonized in the COMESA region by adopting minimum standards of harmonization, common licensing and disclosure standards and minimum capital adequacy, cross border and consolidated supervision. The seminar also had a session on operations of a Deposit Insurance scheme and other pertinent issues.

In order to achieve a harmonized approach to bank supervision, a sub committee of Bank supervisors from 6 Member States was set up to make proposals on harmonization of bank supervision. The committee will do the following:

- a. Review bank supervision and regulation in COMESA.
- b. Assess compliance with the 25 Core Principles for effective Banking Supervision developed by the Basel Committee on banking supervision.
- c. Propose a harmonized approach to bank supervision for the COMESA region.

The subcommittee was assigned a task of coming up with minimum standards for harmonization of bank supervision in the region, which includes harmonized disclosure standards; harmonized accounting standards; common standards for licensing; and minimum standards for capital adequacy.

Appendix I: Tables of Commercial Banks

Table 1: COMMERCIAL BANKS' ASSETS AND LIABILITIES

(Shillings, billions)

ASSETS	1997	1998	1999	2000	2001
Cash and Balances with BOU	110	137	129	196	238
Treasury Bills	106	113	212	332	514
Fixed asset	86	95	92	106	106
Due from Banks Outside Uganda	220	279	290	377	368
Loans & advances to customers	376	443	439	525	521
Investments	82	91	89	73	74
Other assets	73	121	101	236	217
Total assets	1,053	1,279	1,352	1,845	2,038
LIABILITIES					
Due to Deposit Money Banks	191	247	9	77	65
Deposits	584	691	1,040	1,325	1,483
Capital (excl. year-to-date profits) ²	74	88	72	106	167
Provisions	58	86	53	63	58
Other liabilities	132	166	152	196	199
Year to date profit ²	14	1	26	78	66
Total Liabilities & Capital	1,053	1,279	1,352	1,845	2,038

Note:

1. As at December for each year. Figures for closed banks are excluded from the data for subsequent periods.
2. Does not take into consideration the end of reporting periods for individual banks and therefore, does not take reflect the calendar year profits owing to differences in reporting periods between Financial Institutions.

Source: Monthly returns of Commercial banks

Table 2: COMMERCIAL BANKS' COMPARATIVE INCOME STATEMENT

(Shillings, billions)

PROFIT & LOSS	1997	1998	1999	2000	2001
Income					
Interest on advances	45	60	74	84	89
Interest on government securities	10	10	12	55	88
Other interest income	13	17	18	31	28
Total interest income	68	87	104	170	205
Total non-interest income	32	44	54	78	86
Other operating income	0	0	0	0	0
Total Income	100	131	158	248	291
Expenses					
Total Interest Expense	26	34	34	40	45
Provisions for bad debts	8	37	25	14	18
Salaries & other staff costs	22	27	33	50	57
Other non-interest expense	31	35	28	69	90
Total Expenses	87	133	120	173	210
Net Income	13	(8)²	38	75	82

Note:

1. As at December for each year. Figures for closed banks are excluded from the data for subsequent periods.

2. The loss occurred as a result of large losses in Co-op Bank Ltd (Shs 10.1bn), Gold Trust Bank Ltd (Shs 2.7bn) Greenland Bank Ltd (Shs 7.9bn) and others.

Source: Commercial banks' quarterly income statements.

Table 3: SECTORAL DISTRIBUTION OF COMMERCIAL BANKS' CREDIT
(Shillings, billion)

Sector	1997	1998	1999	2000	2001
Government	2	3	2	3	2
Agriculture	75	70	56	52	51
Mining and Quarrying	0	1	2	2	4
Manufacturing	80	136	169	210	190
Trade and Commerce	121	104	98	107	120
Transport, Comm. Elec. & Water:	11	16	40	33	29
Building and Construction	20	24	24	22	19
Other Services ²	67	89	48	96	105
Total	376	443	439	525	521

Note:

1. As at December for each year. Figures for closed banks are excluded from the data for subsequent periods.
2. Includes bills of exchange, real estate, and lending to NBFIs.

Source: Monthly statements of Commercial banks.

Table 4: STRUCTURE OF DEPOSITS OF COMMERCIAL BANKS
(Shillings, billions)

Type of Deposits	1997	1998	1999	2000	2001
Demand and Call	296	342	612	847	960
Savings	115	145	167	197	253
Time	173	204	260	281	270
Total	584	691	1,039	1,325	1,483

Note:

1. As at December for each year. Figures for closed banks are excluded from the data for subsequent periods.

Source: Monthly returns of commercial banks.

Table 5: KEY FINANCIAL INDICATORS

INDICATOR	1997	1998	1999	2000	2001
CAPITAL ADEQUACY					
Core Capital/RWAs (%)	5.5	7.7	10.6	17.4	20.5
Owner's funds – Equity (Shs bn)	74	88	72	166	194
EARNINGS RATIOS					
ROA (%)	1.58	-0.18	1.02	4.21	4.13
ROE (%)	27.78	-13.10	24.50	45.10	50.85
LIQUIDITY					
Liquid assets/Total deposits (%)	56.36	40.98	73.62	84.15	87.59
Total Advances/Total deposits (%)	64.4	64.01	41.46	38.98	35.33
Liquid assets (Shs bn)	329	392	783	1,106	1,292
ASSET QUALITY					
Loans and Advances (Shs bn)	376	443	439	525	521
Non Performing Advances-NPA (Shs bn)	98	251	266	52	34
Provisions for NPA (Shs bn)	44	69	56	32	24
Specific Provisions (Shs bn)	41	66	28	26	21
NPA/Total Advances (%)	26.1	56.7	60.6	9.8	6.5
Specific Provisions/NPA (%)	42.2	26.4	10.5	50.5	61.2

Note:

- ROA - Return on Assets
- ROE - Return on Equity
- NPA - Non Performing Assets (primarily loans and advances)
- RWA - Risk Weighted Assets

Source: Monthly returns of Commercial banks.

Appendix II: TABLES FOR CREDIT INSTITUTIONS

**Table 1: CREDIT INSTITUTIONS' STATEMENT OF ASSETS AND LIABILITIES
(Shillings, millions)**

	Dec-99	Dec-00	Dec-01
LIABILITIES			
Total Liabilities to Depositors	13,242.8	33,486.8	44,631.7
Balances due to Commercial Banks/Associated Cos	100.0	-	-
Administered Funds 2/	39,083.2	28,469.2	27,918.4
Other Liabilities	1,410.6	1,597.8	1,385.9
Provisions	1,629.1	1,859.6	3,341.9
Capital	4,633.6	9,369.1	9,847.9
Profit/(loss) for the current year	1,643.9	1,612.4	845.5
Total liabilities and capital	61,743.2	76,394.8	87,971.3
ASSETS			
Cash	273.2	804.0	1,454.2
Balance with Commercial banks & Associated Cos	5,281.7	9,924.5	13,535.0
Balance with Commercial Banks Outside Uganda	968.8	1,406.6	1,217.2
Investments:	1,675.7	3,069.6	4,352.3
Bank of Uganda Schemes	-	-	-
Loans and Advances	49,032.2	53,131.1	59,906.3
O/w Administered Loans	29,018.4	28,876.8	27,927.4
Premises & other fixed assets	3,440.4	4,872.5	5,438.7
Other assets	1,071.3	3,186.5	2,067.5
Total Assets	61,743.2	76,394.8	87,971.3

Note:

1. Contra entry for Administered Mortgage loans managed by Housing Finance Company of Uganda under the agreement with Government of Uganda.

Source: Monthly returns of Credit Institutions.

Table 2: SECTORAL DISTRIBUTION OF LOANS AND ADVANCES OF CREDIT INSTITUTIONS

(IN PERCENTAGE OF TOTAL)

Sector	Dec-99	Dec-00	Dec-01
Agriculture	0.2	0.0	0.1
Mining & quarrying	0.0	0.0	0.0
Manufacturing	0.9	0.9	0.6
Trade and commerce	5.8	9.1	9.9
Transport and communication	0.1	0.4	2.3
Electricity and water	0.0	0.0	0.0
Building and construction	92.4	88.5	85.8
Other services	0.6	1.1	1.3
Total	100.0	100.0	100.0

Source: Monthly returns of Credit Institutions.

Table 3: LIQUID ASSETS OF CREDIT INSTITUTIONS

(Shillings, millions)

Liquid Asset	Dec-99	Dec-00	Dec-01
Cash in vaults	273.21	804.01	1,454.25
Treasury bills holdings	1,266.74	2,823.41	3,724.79
Balances at Commercial banks in Uganda	5,281.71	9,784.88	13,535.02
Balances at Commercial banks abroad 1/	968.79	1,406.59	1,217.24
Total	7,790.45	14,818.88	19,931.29

Note:

1. Call or demand deposits.

Source: Monthly returns of Credit Institutions

Table 4: STRUCTURE OF DEPOSITS OF CREDIT INSTITUTIONS

(Shillings, millions)

Type of deposit	Dec-99	Dec-00	Dec-01
Savings Deposits	8,383.7	15,455.7	21,211.3
Time Deposits	4,769.8	4,557.1	6,808.3
Other Deposits(Agency funds) 1/	-	13,415.2	16,499.7
Accrued Interest	89.4	58.8	112.4
Total Liabilities to Depositors	13,242.8	33,486.8	44,631.7

Note:

1. "Agency funds" represent amount collected so far from the beneficiaries of the government pool house sale scheme and interest charged thereon, by the Housing Finance Company Ltd.

Source: Monthly statements from the Credit Institutions.

Table 5: KEY FINANCIAL INDICATORS.

Indicator	Dec 99	Dec 00	Dec 01
CAPITAL ADEQUACY			
Core Capital/RWAs (%)	17.68	27.89	19.87
er's funds (Equity)	6,277.5	10,981.52	10,693.36
EARNINGS RATIOS			
ROA (%)	5.03	3.4	0.85
ROE (%)	26.2	14.68	4.78
LIQUIDITY			
Liquid assets/Total deposits (%)	59.23	44.67	44.66
Total advances/Total deposits (%)	85.9	72.43	71.65
Liquid assets (Shs millions)	7,790.45	14,818.48	19,931.29
ASSET QUALITY			
Loans and Advances (Shs millions)	20,013.79	24,254.32	31,978.9
Non Performing Advances-NPA (Shs millions)	3,495.60	2,676.30	5067.44
Provisions for NPA (Shs millions)	858.00	762.89	1395.39
NPA/Total Advances (%)	17.47	11.03	15.85
Provisions/NPA (%)	24.55	28.51	27.54

Source: Quarterly returns of Credit Institutions

Appendix3: REGISTERED COMMERCIAL BANKS AS AT 31 DECEMBER 2001.

Name of Institution	Ownership	No. of Branches	No. of Agencies	Other
1 Uganda Commercial Bank*	Government		67	2
2 dfcu Bank	Foreign		4	
3 Nile Bank Ltd.	Foreign		3	
4 Allied Bank International	Foreign		3	
5 Centenary Rural Dev. Bank	Local		17	
6 National Bank of Commerce	Foreign		2	
7 Orient Bank Ltd.	Local		3	
8 Barclays Bank (U) Ltd.	Foreign		2	
9 Bank of Baroda(U) Ltd.	Foreign		7	
10 Stanbic Bank	Foreign		1	1*
11 Standard Chartered Bank	Foreign		5	
12 Tropical Bank	Foreign		3	
13 Crane Bank	Local		2	
14 Cairo Bank	Foreign		1	
15 Diamond Trust Bank	Foreign		1	
16 TransAfrica Bank	Local		4	
17 CitiBank	Foreign		1	
Total			126	2 1

Note:

1. Stanbic Bank opened a representative office at UMA show grounds.
2. The Government sold 80% of its shares in UCBL to Standard Bank Investment Corporation to Stanbic bank.

Appendix 4: REGISTERED CREDIT INSTITUTIONS AS AT 31/12/2001

	Name of Credit Institution	Ownership	Number of Branches
1	Housing Finance Company (U) Ltd.	Local	2
2	Commercial Micro Finance Ltd.	Local	6
3	Mercantile Finance Co. Ltd.	Local	0
4	Capital Finance Corporation Ltd.	Local	1
5	Stanhope Finance Co. Ltd.	Local	0
6	Imperial Investments Finance Co. Ltd.	Local	0
7	Interstate Finance Company Ltd	Local In Liquidation	1
	TOTAL		10

**Appendix 5: CIRCULARS TO FINANCIAL INSTITUTIONS ISSUED DURING
2001**

BANK OF UGANDA

**OFFICE OF
EXECUTIVE DIRECTOR
DOMESTIC OPERATIONS**



37/43 KAMPALA ROAD,
P. O. BOX 7120,
KAMPALA.

Tel: 258441
Direct Line: 230931
Fax: 258218
Cables: UGABANK

EDO.C.1

9th July, 2001

All Chief Executives of Commercial Banks

**Demonetisation of Bank of Uganda Currency Notes in the denominations of
Shs: 5/=, 10/=, 20/=, 50/=, 100/=, 200/= and 500/=**

As you are well aware, the low value currency notes in Shs: 5/=, 10/=, 20/=, 50/=, 100/=, 200/= and 500/= ceased being legal tender on 31st December 2000. The public was however, allowed to continue exchanging the notes up to 30th June 2001.

This is therefore to advise that all the low value notes exchanged by the Commercial banks be deposited with the Bank of Uganda offices located at Kampala Headquarters and Currency Centres at Jinja, Mbale, Masaka, Kabale, Fortportal, Gulu and Arua latest by 3:00p.m on 27th July 2002. this deadline is for enabling banks to deposit the notes, already exchanged, with Bank of Uganda and in no way affects the exchange of the subject currency notes which exercise stopped on 30th June 2001.

Yours faithfully

J. F. Kahenano
Executive Director Operations

N.O.O.: Governor
Deputy Governor
EDS
D/Currency

BDJK/JLM

Appendix 1:

BANK OF UGANDA

OFFICE OF
EXECUTIVE DIRECTOR
SUPERVISION



37/43 KAMPALA ROAD,
P. O. BOX 7120,
KAMPALA.

Tel: 258441
Direct Line: 230051
Fax: 258515
Cables: UGABANK

EDS.01.01.B

17th May 2001

TO: All Commercial Banks

COMMERCIAL BANK OWNED FOREX BUREAU NEW OPERATING REQUIREMENTS

Bank of Uganda has reviewed and revised the operational requirements of commercial bank owned forex bureau with a view to improving the supervision and monitoring of financial institutions and made the following decisions.

- i) Bank owned bureau which are located within banks shall merge their activities and operations with those of their respective international divisions and close the bureau corporate entity.
- ii) Banks that wish to operate independent forex bureau may do so subject to the following conditions.
 - a. The bureau business should be distinctly separate from the Bank.
 - b. The ownership of the bureau should be clearly spelt out in the Memorandum and Articles of Association.
 - c. The bureau should be located outside the bank's offices and must not use the word "Bank" as part of their name.
 - d. The management and staff of the bureau should be distinctly separate from that of the bank.
 - e. The bureau should maintain separate books of Account and submit returns and reports directly to the Trade and External Debt Department.
 - f. Existing bank-owned bureau wishing to renew their license for the year 2001/2002 will be licensed only if they conform to the above conditions.

It is anticipated that the above measures will drastically improve the Bank of Uganda's supervisory and monitoring of the bureau business and streamline the operations of the financial sector and should be implemented commencing 1 July 2001.

Yours faithfully

E Katimbo Mugwanya
Executive Director Supervision

c.c. Governor
c.c. Deputy Governor
c.c. Executive Director Research
c.c. Director Commercial Banking

Appendix 2:

BANK OF UGANDA

**OFFICE OF
EXECUTIVE DIRECTOR
SUPERVISION**

EDS.01.01.B

20 March 2001



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Tel: 258441
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Cables: UGABANK

**All Chief Executives of Commercial Banks
Dear Sirs**

**PRUDENTIAL GUIDELINES ON AUTHORISED DEALER BANKS' FOREIGN
EXCHANGE BUSINESS**

Pursuant to Section 17 of the Financial Institutions Statute 1993, Bank of Uganda recently reviewed the foreign exchange operations of the authorised dealer banks. The review was prompted after Bank of Uganda recognized that risks inherent in banks' foreign exchange business particularly in running open positions, lending in foreign currency and placing foreign currency deposits with other banks had increased in the recent past.

The review covered the adequacy of banks' foreign exchange risk management systems and the current foreign exchange policy and basis for the computation of banks' overnight exposure limits.

Please find attached to this circular a set of prudential foreign exchange guidelines which cover in brief: (a) the modalities for computing foreign exchange exposures, (b) the minimum risk management systems required of banks to identify, measure, monitor and control foreign exchange risks. (c) the prudential requirements on foreign exchange lending and placements, (d) the appropriate reporting requirements about foreign exchange transactions and (e) the penalties plus other administrative sanctions applicable in case of failure to comply with the guidelines. Additionally, Bank of Uganda is introducing three new returns to be submitted by dealer banks.

These guidelines come into force effective 2 May 2001.

Yours faithfully

**E Katimbo Mugwanya
Executive Director Supervision**

c.c. Governor
D/Governor
EDS
DCB (or)
DNB
Ag DCB

Appendix 3:

BANK OF UGANDA



EDS.01.01.B

4th June 2001

TO:ALL FINANCIAL INSTITUTIONS

**COMMERCIAL BANKS AND CREDIT INSTITUTIONS OWNED FOREX BUREAU NEW
OPERATING REQUIREMENTS**

Bank of Uganda has reviewed and revised the operational requirements of commercial banks and credit institutions owned forex bureau with a view to improving the supervision and monitoring of financial institutions and made the following decisions.

- i) Banks and credit institutions owned forex bureau which are located within banks or credit institutions premises shall merge their activities and operations with those of their respective international divisions if they are licensed forex dealers and close the bureau corporate entity.
- ii) Banks and credit institutions that wish to operate independent forex bureau may do so subject to the following conditions:-
 - a. The bureau business should be distinctly separate from that of Banks and Credit Institutions.
 - b. The ownership of the bureau should be clearly spelt out in the Memorandum and Articles of Association.
 - c. The bureau should be located outside the bank's or Credit Institution's offices and must not use the word "Bank" as part of their name.
 - d. The management and staff of the bureau should be distinctly separate from that of the banks and credit institutions.
 - e. The bureau should maintain separate books of Account and submit returns and reports directly to the Trade and External Debt Department.

- f. Existing bank's and credit institution's owned bureau wishing to renew their licence for the year 2001/2002 will be licensed only if they conform to the above conditions.

It is anticipated that the above measures will drastically improve the Bank of Uganda's supervisory and monitoring of the bureau business and streamline the operations of the financial sector and should be implemented commencing 1 July 2001.

Yours faithfully

E Katimbo Mugwanya
Executive Director Supervision

c.c. Governor
c.c. Deputy Governor
c.c. Executive Director Research
c.c. Director Commercial Banking

Appendix 4:

BANK OF UGANDA



1st June 2001

C I R C U L A R

To: All Financial Institutions

Guidelines and Regulation Asset Quality – Period of Classification Section 52(a) of FIS 1993

Bank of Uganda issued the Guideline and Regulation on asset Quality to financial institutions during the year 1994. the guideline among others explained to financial institutions how to determine the quality of their loan/advances portfolio.

Due to prevailing circumstances in Uganda, the standard classifications under the objective criteria was set at maximum periods which were far in excess of what the international best practices recommend. This has tended to result into a delay in recognizing problem assets which often leads to an overstatement of the institutions' financial position.

Given the notable improvements in the legal and regulatory environment and the inevitable effects of globalisation on the sector, it has been found necessary to adjust downward the maximum period within which loan/advances facilities should be regarded as non-performing. This issue was focused and agreed to at the last meeting held with the Uganda Bankers' Association members.

With effect from 30th September 2001, the classification of NPA based on the objective criteria must follow the following norms:

	Classification	Period after due date of payment for both interest and principal
1.	Substandard	90 days but less than 180 days
2.	Doubtful	180 days but less than 365 days
3.	Loss	365 days or more.

The subjective criteria in classifying NPA remains the same. Non-cash collateral will continue not to be considered in the classification and will not be deductible in determining the amount of required provisions.

The prudential Regulation on Asset Quality is amended accordingly.

E Katimbo Mugwanyu
Executive Director Supervision

Copy Governor
Deputy Governor
Executive Directors

Appendix 5:

BANK OF UGANDA

**OFFICE OF
EXECUTIVE DIRECTOR
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EDS.01.01.B

1st June 2001

CIRCULAR TO: ALL FINANCIAL INSTITUTIONS AND FOREX BUREAUX

ARMED ROBBERIES

Bank of Uganda has noted with serious concern the recent wave of violent and armed robberies resulting into substantial loss of cash and life at various institutions in the country.

Due to the increasing risk of loss of funds through robberies, Bank of Uganda strongly recommends that security arrangements and procedures be strengthened both at all branch offices and in transit whenever cash is being transferred from one location to another.

Additional safeguards should be taken to enhance the insurance coverage of both cash at premises and in transit.

Bank of Uganda wishes to further caution financial institutions that some of the incidents of robbery and thefts may at times be facilitated by staff from within. It would therefore be necessary to keep cash movement to and from one place to another a strict secret at all times.

E Katimbo Mugwanya

Executive Director Supervision

- c.c. Governor
- c.c. Deputy Governor
- c.c. Executive Director Research
- c.c. Director Commercial Banking