Why banks fail? The case of the Gambia commercial and development bank

Bank failures are not uncommon, nor limited to developed or developing economies or a particular geographical region. The cost of bank failure can be high, and if this causes instability in the financial system, the effects can be adverse on the country’s growth rate and considerable bailout cost to governments and central banks. Bank failures can be attributable to both internal and external pressures. In this paper, quantitative Multivariate Discriminant Analysis Z-Score and qualitative A-Score were adopted to examine bank failure and in particular, to evaluate why The Gambia Commercial and Development Bank (GCDB) failed. The findings show that GCDB failed due to poor financial performance and weak management systems. The external factors of judicial ineffectiveness, political hijacking and severe macro-economic conditions played a considerable part in GCDB’s failure.

Key words: Bank, Finance, Failure, Gambia

JEL Classification: J016, G2, O016, D53

INTRODUCTION

Several studies on corporate bank failures focused on the developed economies with limited coverage on the developing countries, in particular, the banking industry of Sub-Saharan African countries. Much interest in the study of corporate collapse was stimulated by the high rate of corporate failure during the great depression of the 1930s in the United States of America (USA). There had been a fair number of previous studies in this field of research by other researchers including Fitzpatrick (1932), Smith (1930), Ramser and Forster (1931) and Merwin The more notable published research were from Beaver (1996, 1998a, 1998b), Altman (1996, 1984, 1998), Altman and Lorris (1994), Altman and Migough (1997), Altman et al. (1992), Deakin (1997), Blum (1996), Edwards (1985), Dun and Bradstreet (1970), Gao (2013), Argenti (1997; 1998) and Lev (1997).

The causes of the collapse of GCDB may be classified into weaknesses of management, poor financial performance and external factors. As a result of these chronic problems due mainly to its inability to recover credits and advances, environmental pressures, operational weaknesses, non-compliance with the statutory requirements and the consequent loss of public confidence, GCDB found it extremely difficult to survive despite its noble role in the economy.

However, the collapse of a commercial and development banking institutions is not uncommon in developing countries where specially created development financial institutions had to take responsibilities for development banking, and where operations, because of the demands of the situation, have increased manifold without concomitant growth in managerial systems and skills, operational or information technology infrastructure requirements. This is true of Senegal where in February 1991, six institutions including the Banque Nationale de Development du Senegal (BNDS) in the parastatal banking sector failed and a National Recovery Company (NRC) established to recover the frozen credits given out by the banks. The Commercial Bank and Capital Bank of Zambia and the Development Bank for Trade and Industries in Sierra Leone are yet other...
severe problems, some naturally inflicted, some externally and yet some internally, on the trend of the country’s economic growth. The spill-over effects of the great oil shocks of the 1970s and the erratic weather conditions, and the drought of the early 1980s explained the poor economic performance that the country experienced culminating into severe spillover effects on the financial sector. (USAID, 1992)

Objectives of the Study

Primarily, the study is aimed at investigating the factors that led to the collapse of GCDB. The collapse of GCDB remains a great concern for the vital role it played in financing key economic sectors of the economy including agriculture, tourism, building and construction, manufacturing industry, and distributive trade, among others.

The study is divided into six sections, each addressing a specific aspect. Section 1 introduces the study followed by section 2 providing a background of GCDB. Section 3 detailed the theoretical considerations by reviewing existing literature and outlining the strategic management model as our conceptual framework. This is followed by section 4 describing the methodology adopted in this study using both primary and secondary data sources. Section 5 presents the data analysis based on the quantitative and qualitative approaches. The paper concludes with summary of findings and implications of the study.

Background of GCDB

It was during the early days of the post-independence era in The Gambia that an urgent need arose for the establishment of a national development bank to take up the responsibilities of facilitating economic growth and development. Consequently, The Gambia Commercial and Development Bank (GCDB) was established by an Act of Parliament, No. 13 of 1972 as a corporate body. It had three shareholders, The Gambia Co-operative Union (GCU) with 23 percent, The Gambia Produce Marketing Board (GPMB) with 26 percent and The Gambia Government which owned a majority share of 51 percent.

GCDB mission was “to assist the economic development of The Gambia, in particular by promoting trade, industry, agriculture, fisheries, mining, public works, communication, public utilities and tourism in the country and to operate all the usual banking business concerning commercial and development banks and in accordance with the by-laws of the bank”.

Given the pivotal role of GCDB in the banking sector, its mandate in terms of small enterprise promotion, financing of public enterprises and provision of agricultural credit both directly and indirectly through The Gambia Co-operative Union (GCU) placed it in an operational environment distinct from other commercial banks in the country. However, this is not to say that the development mission is a license for financial irresponsibility and/or managerial inefficiency. It provided indispensable banking services to the majority of Gambians that do not have access to the foreign-owned banks in the country.

Prior to 1972, the only lending institutions in the Gambia were the British-owned Standard Chartered Bank (SCBG) and the French-owned Banque Internationale pour le Commerce et l’Industrie (BICI). These banks concentrated their lending to multinational corporations and to well-established, basically foreign-owned businesses with very few indigenous enterprises having access to financial services particularly, credit.

To fill this gap, GCDB quickly became the main source of institutional credit for local enterprises in the country. In addition to its role as a development-oriented entity, by the mid-1980s GCDB had become the Gambia’s largest commercial bank, accounting for almost half of the total deposits, about 88 percent of total loans, and more than half of the total commercial bank assets, CBG 1994). Although its principal activity was commercial banking, it attracted a largest share of the market for both customers’ deposits and loans portfolio as shown Table 1.

GCDB showing 49 percent of the total deposits compared to 35 percent for SCBG and 16 percent for BICI. For the loans and advances, GCDB recorded 88 percent with only 9 percent and 3 percent for SCBG and BICI, respectively showing total dominance of the industry at the time. It certainly became a significant force in the local banking community; however, this rapid growth was not without problems. At end-December 1990, the financial statements were overburdened by poor lending decisions and the weak recovery of bank’s toxic assets from the courts. In the 1980s, the bank experienced substandard performance due mainly to huge non-performing loans, huge accumulated losses and the overall poor implementation of optimal measures, (CBG reports 1992) These seriously affected the bank’s noble mission resulting in total erosion of its capital, illiquidity and non-compliance with statutory and contractual obligations.

The monopoly position of GCDB being the only government-owned bank led to political and social pressures to finance projects that had little or no commercial justification. This factor, plus inept management and/or inappropriate credit risk management, led to a very significant overhang of non-performing loans. These toxic assets impaired the financial condition of the bank, thus constraining its ability to finance creditworthy borrowers, to the detriment of national economic development, CBG, 1992).

To ensure continuity of GCDB’s meaningful role in the country, the Government took a number of measures in ensuring a turnaround of GCDB’s adverse financial condition. These measures included:

- The conversion of an outstanding International Development Agency credit of D6.4 million into
Government equity in GCDB and further D9.6 million capital injection in order to restore its financial health.

- The conversion of D35 million of loans and advances from the public sector into a long-term facility.
- GCDB loans of D72 million guaranteed by government were placed into a Managed Fund Account, most of which were non-performing, were removed from the books of the bank to restore the bank's health.
- Restructuring the management of GCDB by replacing the Managing Director and some senior management officials with expatriate Managing Director and professionally qualified personnel, USAID 1992).

Despite these financial and management restructuring, the bank's financial situation continued to worsen. In July 1990, as part of the financial restructuring plan, GCDB was converted into a public Limited Liability Company under the provisions of the Companies Act of 1995. The assets and liabilities of the bank were transferred and vested in the company as part of the divestiture and rationalisation program of the government.

The government desired further in its drive to revive public confidence in the already threatened banking sector, to liquidate GCDB in June 1992. The good assets and performing liabilities of GCDB were sold to Meridien BIAO Bank (Gambia) Limited. The residual assets and liabilities were taken over by the Asset Management Recovery Corporation (AMRC), a corporation established by parliament in December 1992 to effectively and expeditiously manage and recover the toxic assets (frozen credits) of GCDB, AMRC Act 1992).

### Definition of Terms

Bank failure is defined to include "bankruptcy, insolvency, or liquidation for the benefit of creditors" (Deakin, 1997). The primary source of statistics on bank failure, used the term "failure" to mean "the inability to meet its maturing obligations and when its total liabilities are in excess of the realisable value of its assets" (Dun and Bradstreet, 1970; Altman, 1996).

In addition, bank failure is said to have occurred when it has a greater expected value "dead" than "alive", in other words, where much of the company's assets are non-performing and its inability to meet current obligations of paying off creditors and long-term requirements. For the purpose of this study, bank failure is defined as "the inability to meet maturing obligations, excessive lending, persistent high gearing and capital erosion, and non-performing loan conditions, high accumulated losses, excessive debts and where its total liabilities are in excess of the realisable value of its assets" (Jaabi, 1995)

### Causes of Corporate Failure

Banks do provide significant benefits to the domestic economies but they also present considerable risks, with many having suffered financial distress and bank failure as a result of host of problems. The causes of corporate failure are many and they vary depending on the type of business. The causes could however be classified into weaknesses of management, poor financial performance and macro-economic pressures (Brownbridge, 1998; Jaabi, 1995). The bank failure associated with poor financial performance include, inabilities to recover credits and advances, insufficient securities in the form of collateral to meet outstanding claims, persistent high gearing condition (debt capital in excess of equity capital), inadequate working capital, fraud (insider abuse) and a significant deterioration.

### Literature Review

Bank failure is most times interpreted in the strict legal sense of bankruptcy or liquidation where operations are ceased voluntarily or involuntarily. It may be broadly interpreted as a severe financial and/or operational difficulties reflected in bankruptcy. The problems associated with bank failure may have received little attention compared to those of bank profitability, growth and expansion. Nevertheless, it is a fact that businesses do contract in size and do fail. A study of why these events occur might offer a useful insight into the strategies to control bank failure and limits its adverse effects on national economies, regions and globally as a whole.

### Table 1. Deposits and Loans & Advances of Commercial Banks as at 31st December 1985

<table>
<thead>
<tr>
<th></th>
<th>Deposits (Millions)</th>
<th>Percentage (%)</th>
<th>Loans (Millions)</th>
<th>Percentage (%)</th>
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<tbody>
<tr>
<td>GCDB</td>
<td>82</td>
<td>49</td>
<td>218</td>
<td>88</td>
</tr>
<tr>
<td>SCBG</td>
<td>59</td>
<td>35</td>
<td>23</td>
<td>9</td>
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<tr>
<td>BICIs</td>
<td>28</td>
<td>16</td>
<td>8</td>
<td>3</td>
</tr>
<tr>
<td>Total</td>
<td>169</td>
<td>100</td>
<td>249</td>
<td>100</td>
</tr>
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</table>

in profitability, liquidity, capital, activity and leverage ratios (Okeahalam, 1998; Altman, 1996; Brownbridge, 1998; Jaabi, 1995; Obeng-Odoom, 2013; Gao, 2013). One important indicator of a bank’s health is its relative level of regulatory minimum capital, which cushions banks against losses from non-payment of loans and other losses on assets. Regulators require banks to maintain certain minimum capital requirements to help ensure the safety and soundness of the banking system and generally expect banks to hold capital above these minimums at levels commensurate with their risks (Gao, 2013). The failure of banks has considerable financial, economic and political implications to any country and region through its contagious effect.

The Southeast Asian financial crisis of 1997/98 and the global financial crisis of 2008 resulted in the failure of many banks due mainly to foreign exchange speculation, excessive loan exposure, poor risk management systems, increase risk appetite, weak regulation and capital controls, insider abuses, cronyism, among others (Corsetti et al., 1999; King, 2001; Rao, 1998; Lall et al., 2008; Krugman, 1990).

While some financial ratios are useful to show warning signs of insolvency and other financial troubles, other ratios may appear reassuring in the same entity. It may then be difficult to interpret the true state of the financial entity in such circumstances. For this reason, it is useful to turn to other non-financial causes in finding out the aggregate causes of bank failure. Most banks fail mainly due to managerial problems, including poor leadership, poor corporate governance, low morale of employees, weak internal controls, low professionally qualified and experienced personnel, poor information technology platform, fraud, non-compliance with regulatory requirements and an ineffective Board of Directors, among others.

There are, however, external forces that contributed to the collapse of banks, most notably, macro-economic instability, excess risk appetite, the social, religious, cultural, political interventions and government regulations, do affect the management decisions of banks to a very large extent. The pressures to extend credit for social and political purposes that have little or no commercial justification is a viable example. The cancellation of farmers loans also remain an important political force that has over the years put at high risk the total banking sector loan portfolios.

Sharplin (1985) championed the basic strategic management process model in his research. He concluded that financial institutions fail due to poor planning and implementation, pressures from economic, social, political and technological factors and environmental constraints as shown in Figure 1. The situation analysis is basically a blend of PEST Analysis (Political, Economic, Social and Technological Analysis) and SWOT Analysis (Strengths,
Weaknesses, Opportunities and Threats Analysis). Internal analysis is an important component of situation analysis, which studies the condition within the company (World Bank, 2015). Figure 1 illustrates that strategic management model is designed to effectively relate the organisation to its environment. First environmental scanning is employed to identify external and internal elements that will determine the future of the organisation. The simplest way to conduct environmental scanning is through SWOT and PEST analysis. Environmental scanning is the monitoring, evaluation and dissemination of information from the external and internal environments to key people within the organisation. Internal environment consists of variables (strengths and weaknesses) that are within the organisation including the organisational structure, culture and resources. External environment consists of variables (opportunities and threats) that are outside the organisation.

With the different facets which are both internal and external forces, as shown in the strategic management model, banks must adopt measures to operate optimally in the face of the challenging facets to survive.

For weak financial institutions, it is difficult to sustain the significant internal and external factors. Even normal business challenges become severe challenges to poorly performing banks, therefore it is important that these internal and external challenges are addressed in time for sustainability sake.

Several studies have shown that major cause of financial institutions failure stemmed from managerial inexperience and incompetence (Dun and Bradstreet, 1970, Argenti, 1996 summarised the term "bad management" in the following passage:

“*If the management of a financial institution is poor then two things will be neglected; the information and internal control systems will be deficient and the financial institution will not respond to change. Poor management will also result to at least one of the three mistakes; overtrading, increase risk appetite or allowing the financial institution’s gearing to rise so that even normal business hazards become constant threats*” (Argenti, 1996).

Dun and Bradstreet (1970) prepared the best known study of the causes of corporate failure in the United States of America. The breakdown of the apparent causes of failure included negligence, fraud, disaster and management incompetence. The managerial incompetence account for 91% of corporate failure followed by negligence, fraud and disaster by 4%, 2% and 1%, respectively while other causes form 2%(Table 2).

**METHODOLOGY**

In this study, quantitative and qualitative (primary and secondary data) approaches are adopted to address the objective of the study. In using quantitative approach of determining corporate failure, use is made of Altman’s (1996) Z-Score Multiple Discriminant Analysis (multivariate) and Argenti’s (1996, A-Score qualitative model.

**Quantitative Approach**

The technique of multiple discriminant analysis (MDA) creates a quantitative model based on ratios which best distinguishes between failed and solvent banks, and thereby produces the best correlation with financial health.

Altman (1996) like Beaver (1996) selected a sample of thirty-three failed and thirty-three non-failed financial institutions to distinguish between the classes using MDA. From the twenty-two ratios, five ratios were selected that appeared to be most effective in discriminating between the classes. The twenty-two ratios were classified into five ratio categories: liquidity, leverage, profitabity, solvency and activity.

MDA assesses financial institutions using these financial ratios to determine their solvency threshold and financial track record. In using this approach, data is collected on various economic characteristics which are deemed relevant to discriminate between failed and non-failed financial institutions. The MDA technique derives a linear combination of all these characteristics that best discriminates between the classes of failed or non-failed five years prior to failure (Barach, 1996).

The discriminant function transforms the values of the individual variables into a single discriminant score (z-score), which is then used to classify the financial institutions into failed and non-failed businesses. The following discriminant function best discriminate the bankruptcy status of corporate bodies (Marc, 1998)

\[ Z = B_1X_1 + B_2X_2 + B_3X_3 + B_4X_4 + B_5X_5 \]

Where:

\[ Z = \text{Discriminant Score} \]

\[ X_{1to5} = \text{Independent Variables (Financial Institution’s Characteristics)} \]

\[ X_1 = \text{Working Capital to Total Assets} \]

\[ X_2 = \text{Retained Earnings to Total Assets} \]

\[ X_3 = \text{Earnings Before Interests and Taxes to Total Assets} \]

\[ X_4 = \text{Market Value of Equity to Total Debts} \]

\[ X_5 = \text{Sales to Total Assets} \]

However, Altman (1996) made an implicit assumption with respect to discriminant coefficients being invariant with respect to time, accordingly, the weights (B1toB5) contributed 0.012, 0.014, 0.033, 0.006 and 0.01, respectively to the model’s operation. His multivariate discriminant analysis of data, five years to failure, for a paired sample of failed and non-failed firms, yielded the accuracy in classification. The predictive accuracy of the model produced by his study improves as the failure approaches. A Z-score of 2.675 was established as a cut-off point with financial institution classified as failed if it
scores less than 2.675 and vice versa as non-failed.

MDA has also been used successfully by credit analysts to formulate default probabilities for loan applicants and by portfolio managers in evaluating share and bond investments. For the purpose of this study, however, the use of MDA will be restricted to discriminating between the classes.

Qualitative Approaches

While quantitative approach made use of financial ratios to assess the performance of financial institutions, qualitative approach looked at the financial institutions beyond the ratios. With the limitation of financial ratios, it is necessary to look into non-financial measures, which remain useful and a valid addition to knowledge in finding out the aggregate causes of corporate failure.

Qualitative analysis made use of three characteristics in signaling failure; defects, mistakes and symptoms. However, qualitative analysis is a deliberately subjective approach contrary to the objective nature of the quantitative analysis approach, nonetheless, it is useful in complementing the secondary data analysis in aggregating causes of corporate failure.

It is a consensus among researchers that before failure, financial institutions display a number of defects, mistakes and symptoms of corporate failure. Defects include but not limited to autocratic managing director, no depth of professional managers, irresponsiveness to change, poor planning, costing and budgetary control systems, passive directors and an ineffective finance manager, among others.

Mistakes comprise of high gearing, overtrading and an undertaking of a big project of such a size that should it go wrong, the financial institutions will be crippled.

Symptoms of corporate failure comprise of deteriorating financial ratios, the practice of creative accounting, decline in product quality, fall in market share and terminal signs such as writs and resignations. These three characteristics (defects, mistakes and symptoms) of determining corporate failure using qualitative approach which are combined into a qualitative model (A-score), used in classifying financial institutions into failed or non-failed entities.

Non-Financial A-Score Model

The A-score built by Argenti (1996) requires the observer to ask a number of questions and to score answers on the three signs of failure as mentioned below. Unlike the objective nature of the financial ratios, Argenti’s study is a deliberate subjective approach. The process of corporate failure appears in three stages, the questions and scores of the three stages are as follows:

The defects - Financial institutions before failure display a number of defects such as:

- Management depth - where there is no depth of professional managers, Score 1.
- Where there is an authoritarian managing director than a more professional manager, Score 8.
- Accounting defects - where there is no cash flow planning system, costing system and budgetary control, Score 3.
- Response to change - if the financial institution is old-fashioned in some significant areas, for example out-of-date systems, services and products, Score 15.
- Chairman of the Board and the Managing Director - Ineffective Board of Directors to take weak Managing Director to task, Score 4.
- Passive Directors - if the other directors do not normally contribute to the discussion of major decision-making, Score 2.
- Unbalanced Board - if the directors of the board do not reflect a wide spectrum of knowledge, Score 2, for example of five out of seven Board members of a financial institution are bankers.
- Finance Director - Score 2, if the finance director is not a strong enough personality to make his views clearly known to the Board.

Total possible score for defects = 43
Pass mark for defects = 10

Thus, if a financial institution score 10 or more, the observer is entitled to some anxiety, for it is sufficiently defective to allow it to make one of the total mistakes.

Mistakes - mistake is composed of three characteristics:

- Gearing - where a financial institution that allows its gearing to rise to a level at which its future is placed in jeopardy by a stroke of ill-fortune, Score 15.
- Overtrading - financial institutions that expand faster than their capital funding are in danger. This is a mistake which well-managed financial institutions can make with impunity for long periods but which catch the defective financial institution unawares, Score 15.
- Big project - if the financial institution has recently launched a project of such a size that should it go wrong,
it will be crippled, Score 15.

Total possible score for defects = 45
Pass mark for defects = 10

Thus, if a financial institution score above 10 or more in this section, the observer is entitled to some anxiety, if in addition, the score in defects exceed 10, his anxiety should be acute.

Symptoms - This is made up of:

♦ Financial signs - if the financial ratios, the Z-score, income statement and the Balance Sheet show signs of deterioration, Score 4.

♦ Creative accounting - if the observer detects any accounting tricks designed to dress up the accounts (for example, low depreciation, overvalued stocks or assets, low repairs and maintenance) Score 4.

♦ Non-financial signs - if there are such signs of stringency as a decline in product quality, fall in market share, score 3.

♦ Terminal signs - if there are writs, rumours and resignations, score 1.

The total score for symptoms is 12
Pass mark is 5

If the financial institution scores more than 5, in addition recorded higher score in defects and mistakes, then failure is eminent.

Total A-score (Defects, Mistakes and Symptoms) = 100
Pass mark = 25

Therefore, any financial institution scoring more than 25 is deemed failed by Argenti's study. The higher the A-score, the closer banks are to the final collapse. Argenti (1984, 1996) carried out the study by observation and interviews on corporate institutions including banks and assigning scores to the characters in the A-score model. These scores are summed up to determine the potential collapse of banks.

With limitations in quantitative analysis, this study is unique in scope and methodology as it involves a comprehensive study of both the quantitative and qualitative approaches to determine bank failures. Argenti's study is interesting as it provides largely qualitative approach alongside the quantitative and statistical research studies, in an attempt to identify common themes in the behaviour of failing banks.

Information Sources

Financial statements and reports were obtained mainly from the Assets Management Recovery Corporation (AMRC), the legal successor of GCDB. In addition, some information were also obtained from the Office of the Registrar of Companies, the National Archives, Central Bank of The Gambia (CBG), the United States Agency for International Development (USAID) Banjul Office and the Attorney General's Chambers. Personal interviews and questionnaires were administered with the then management teams, Central Bank of The Gambia, and officials of AMRC. These provided vital additional information in the postmortem study of GCDB.

The interviews were however targeted to managers, customers, regulators, loan Recovery and Inspectorate Units, Ministry of finance officials, AMRC staff, and others having a stake in the affairs of GCDB. The sample was conveniently selected from a population of key stakeholders of GCDB.

In making use of Argenti's diagnostic model (the A-score) in this study, questionnaire respondents were required among others, to assign a score to each characteristic of the three main causes of corporate failure: defects, mistakes and symptoms. Respondents provided answers to the questionnaire by giving scores to each characteristic and the average score is taken as the bank’s score. The cut-off score of 25 is set above which financial entity is considered to have failed.

Like the personal interviews, questionnaire guide target senior management levels and other interest groups of GCDB. Summary of respondents were collated to determine yet another measure to determine the causes of GCDB's failure. The findings on the primary data sources were collated to complement quantitative conclusions to assist in addressing the objective of the study.

RESULTS AND FINDINGS

In an attempt to minimise the tendencies of subjective judgments used in pursuance of the objective of the study, use has been made of the multiple discriminant analysis to analyse the financial performance of GCDB as one of the approaches in the diagnostic study.

Multiple Discriminant Analysis (MDA)

Use is made of Altman's MDA to classify GCDB into either of the classes - failed or non-failed. The main criterion in the investigation process is bankruptcy and the model called "the discriminant function" is found suitable in distinguishing financial institutions into classes of failed and non-failed. The following expression is used to symbolically present the discriminant function.

\[ Z = 0.012X_1 + 0.014X_2 + 0.033X_3 + 0.006X_4 + 0.01X_5 \]

where \( Z \) = Discriminant score

\( X_1 = \) Working Capital to total assets
\( X_2 = \) Retained earnings to total assets
\( X_3 = \) Earnings before interest and taxes to total assets
\( X_4 = \) Market Value of equity to total debts
\( X_5 = \) Sales to total assets

Altman made an implicit assumption with respect to discriminant coefficients being invariant to time and on the basis of this, weights are assigned after 'numerous computer runs'. However, the larger the discriminant coefficient or weights of the variable \((x_1-x_5)\), the more important is the variable in the discriminating process. Therefore, \( X_3 \) (Earnings before interest and Taxes to Total Assets) is found to be the most important variable in the
discriminant function followed by $X_2$, $X_1$ and $X_5$ with the least contributor to the equation provided by $X_4$. The cut-off point is set at 2.675, therefore, banks with a discriminant score below 2.675, are considered to have financially failed.

Having worked out all the independent variables, the computation of the Z-score shows the following results:

Figure 2 shows the graphical presentation of the Z-score in Table 3. The cut-off score of 2.675 is compared with the actual score, thus showing deteriorating trend five years prior to final failure. The results in Table 3 show negative levels throughout the five-year period with 1991 and 1992 manifesting worst positions.

From Figure 2, it is evident that GCDB failed to achieve the cut-off score of 2.675 throughout the period – 1988 to 1992. The bank was at its worst level during the last two years, when the Z-score ran into significant negative scores of 3.8127 and 2.9796. The Performance Analysis Services score which permits a bank’s relative performance to be tracked through time, shows a downward trend of the Z-score from 1988 through to 1991 with marginal improvement in 1992 though remained negative at 2.9796.

### Qualitative Data

The A-score analysis from both the questionnaire and interviews, the average score recorded 72 out of 100 with 25 as a pass mark cut-off point. This clearly showed GCDB has failed on both quantitative Z-Score and qualitative A-Score approaches. Average defects showed 30, Mistakes 35 and Symptoms 7, totaling 72 well above the maximum point of 25.

Quite apart from the quantitative Z-Score and qualitative A-Score analyses, other analysis such as the external factors were made use of that remained crucial to the diagnostic study.

### Recoveries of GCDB’s Toxic Assets

The recovery Unit encountered considerable problems in pursuing the recovery of debts especially in the court. It is evident that mortgages and title deeds lodged with the bank as collaterals were not traceable and got missing in the files totaling some D5.8 million.

As of March 31st, 1988 the loans outstanding by 12 largest debtors totaled D103.7 million. The recoveries of these debts took many years in the court before judgment could be delivered. This extremely high loan concentration represented these levels below in violation of statutory and prudential laws:

- 48 percent of the total outstanding loans
- 82 percent of the total customer’s deposits
- 377 percent of the share capital and reserves excluding accumulated losses.

The poor recovery of these toxic assets had severe effects on GCDB’s profitability, capital, liquidity and survival as a going concern entity.

### Political Influences

GCDB being a parastatal bank, owned by government of The Gambia, it was not unusual for some politicians to consider as part of the bank’s duties to finance their requests which
Table 4. Violation of The Liquid Asset Requirement

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<td><strong>Statutory requirement</strong></td>
<td>Percent</td>
<td>Percent</td>
<td>Percent</td>
<td>Percent</td>
<td>Percent</td>
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<td>GCDB's Liquid asset holding</td>
<td>30</td>
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<td>30</td>
<td>30</td>
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<tr>
<td><strong>Percent</strong></td>
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<td>1.78</td>
<td>21</td>
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<td>3.16</td>
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Table 5. Non-Compliance with Lending Requirement To Customers

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<td><strong>Capital and Reserves</strong></td>
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<td>(76276)</td>
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<td><strong>Advances to Customers</strong></td>
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<td>189404</td>
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<td>40514</td>
</tr>
</tbody>
</table>


are often commercially and economically unviable. The lack of political will on the part of the government proves to be a major contributing factor to GCDB's huge non-performing credits. The bank was largely used to finance what was considered as disguised social welfare programs. This is particularly true with regards to the forgiveness of loans to rural agricultural borrowers (directly or indirectly through the Gambia Cooperative Union) who form an important political constituency.

This resulted in poor debtor morality as members who paid their loans soon learnt that it was a disincentive to pay off their debts when government write-off is forthcoming. This led to poor loan quality of most banks' portfolios even the private banks. GCDB was put under considerable pressure by those in positions of power and with political constituencies to continue lending regardless of the poor debt servicing of the Gambia Cooperative Union (GCU) and other debtors of agricultural credits.

**Non-Compliance with Statutory Requirements**

GCDB had consistently violated key provisions of the Financial Institutions Act and the Central Bank Act. The non-performing loans, impairment of GCDB's capital and illiquidity conditions to a large extent resulted to these violations. However, non-compliance with statutory requirements may be considered the greatest violation an entity can commit. An entity's image and reputation and therefore its credibility depend to a great extent on how it fulfils its commitments to regulatory authorities and other contractual obligations. In this regard, GCDB's track record left much to be desired. GCDB was in violation of the liquidity and capital unimpaired requirements as shown in Tables 4 and 5.

GCDB had violated this vital prudential requirement further putting pressure on its bankruptcy potentials in meeting its obligations on time.

From Table 5, the Bank's capital and reserves were completely eroded for all the years except for 1990. As far as the requirements of section 17(1), which require not more than 25% of bank's unimpaired capital, GCDB was not legally in a position to grant any credit since its capital and reserves were in deficits for most of the years and minimal in 1990. The bank was, therefore, in breach of this section of the Act.

**Judicial Systems**

GCDB needed to interact with the judicial system for both civil and criminal courts. Borrowers do default on their obligations and lending institutions all over the world find it necessary to seek civil restitution in the courts. There were overcrowded courts resulting too much time and money being wasted. In other words, there were no commercial courts to expeditiously decide on cases. As a result, cases spend years in court before being decided upon.

GCDB incurred considerable cost in its legal battles to recover credits with little or no success. Cases dragged for many years in court creating liquidity and compliance to regulatory requirement problems, hence a major contributing factor to GCDB's subsequent collapse.

The difficulties in loan recovery especially through the courts severely affected the banking sector. The judicial ineffectiveness, which in the short-term serve to frustrate implementation of GCDB creditor rights, have the potential of directly impacting on the future development of the banking and financial sectors by exposing the actual inability of creditors to recover credits under the contractual lending arrangements. Ultimately, the detrimental effect on national development has become evident as financial institutions were increasingly compelled to restrict future credit to only the shortest term and lowest risk transactions, supported by liquid collateral or by external guarantees. In such instances, banks may shy away from lending and turn to investments in government bonds.
As at the date of liquidation and takeover, 26 largest debtors whose exposure aggregated to D139 million constituted nearly half of the outstanding credit. These borrowers were in a financial and political position to take advantage of potential delaying tactics within the judicial process and exploit its inadequacies and shortcomings to their own benefit. In some cases, bank case files on loan recovery were in court for several years before judgement could be heard.

**Macro-Economic Constraints**

The vital extraneous factors are yet other contributing factors associated with the demise of GCDB. The adverse macro-economic conditions of the 1980s, undiversified agricultural sector, low value addition, low economic structure and the external trade imbalances, among others, were the external factors that adversely affected the ability of borrowers to repay loans, (USAID 1992).

As a development and government-owned bank, GCDB had to lend much of its loanable funds to agriculture, thus making it highly exposed to the vagaries of weather, rainfall and all its supply and value chain challenges. Severe droughts resulting to poor harvest of the country’s main cash crop – groundnuts impacted negatively on agricultural loans repayments which form the largest sectoral credit of GCDB. With the absence of credit insurance against agricultural lending coupled with the drought and resultant poor harvests in the 1980s to 90s increased non-performing loans of most banks, particularly GCDB.

In addition, an attempted coup in July 1981 against the government of The Gambia created additional economic crisis with low tourist arrivals affecting the country’s main foreign exchange source dearly. Of course, the loan forgiveness program and the political and social pressures were other important constraints in the recovery process. These coupled with the political pressures, non-compliance with prudential and statutory requirements, judicial ineffectiveness in enhancing efficient loan recovery, macro-economic constraints. The effects of poor loan recovery as shown in Table 6.

From the toxic assets (total frozen credits) of GCDB, 45.6 percent represented loans and advances of D1 million and above, 3.5 percent between the ranges of D500,000 to D999,999 and 27 percent by Managed Fund Account. It follows that loans and advances were highly concentrated as D145.3 million was advanced to only 22 customers with an average of D6.6 million.

The high gearing condition of GCDB was a great concern. The equity/debt ratio showed (0.388):1 in 1988, (0.3506):1 in 1989, 0.144:1 in 1990, (1.4029):1 in 1991 and (0.8745):1 in 1992. It follows that GCDB is highly geared, that is debt capital more than equity capital. This was due to increased operational costs, high accumulated losses over the years and excessive poor asset quality. The total loans advances as of 31st January 1991 showed a total value of 227.5 million Dalasis with a provision of 73.38 percent for doubtful debts. As at the date of liquidation in June 1992, the loan portfolio totaled D318.29 million.

**Conclusions and Implications of the Study**

In the diagnostic study of GCDB, many factors were responsible for the demise of the bank. These were divided into internal and external factors. The internal factors included management weaknesses and poor financial performance as evident by the A-score and Z-score in Section 5. The financial weaknesses were revealed by the discriminant function (Z-score) and high provisions of doubtful debts. In addition, GCDB remained highly geared coupled with operational costs, high accumulated losses and excessive poor asset quality that were significantly severe to allow GCDB to survive as a development financing institution in the country.

Management weaknesses were revealed by the A-score model, reporting an average score of 72 well above the threshold of 25. This is associated with the poor quality of GCDB’s management coupled with poor and weak internal controls, poor accounting systems, overtrading, poor credit management and an ineffective loan recovery. These coupled with weak judicial effectiveness, poor recovery of loans, political interventions, non-compliance with statutory and prudential requirements and external factors putting considerable pressure on GCDB to survive despite its viable mission in the economy.

It is important to note that GCDB had experienced a

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**Table 6. Loans and Advances on Liquidation**

<table>
<thead>
<tr>
<th>Range</th>
<th>Number of Accounts</th>
<th>Amount (Dalasis)</th>
</tr>
</thead>
<tbody>
<tr>
<td>D1 million and Above</td>
<td>22</td>
<td>145,343,846.50</td>
</tr>
<tr>
<td>500,000 - 999,999</td>
<td>15</td>
<td>11,149,312.41</td>
</tr>
<tr>
<td>100,000 - 499,999</td>
<td>164</td>
<td>31,900,396.97</td>
</tr>
<tr>
<td>50,000 - 99,999</td>
<td>185</td>
<td>12,883,568.40</td>
</tr>
<tr>
<td>Less than 50,000</td>
<td>3745</td>
<td>31,016,493.59</td>
</tr>
<tr>
<td>Total</td>
<td>4128</td>
<td>232,293,617.87</td>
</tr>
<tr>
<td>Managed Fund Account</td>
<td></td>
<td>86,000,000.00</td>
</tr>
<tr>
<td>Total Frozen Credits of GCDB</td>
<td></td>
<td>318,293,617.87</td>
</tr>
</tbody>
</table>

Source: Price Waterhouse (1991)
lengthy institutional learning process at considerable cost to the government and The Gambian people. It appeared to have had two fundamental and mutually exclusive goals:

i. To be loved as a magnanimous source of government funds through the liberal granting of financing with lenient loan recovery efforts.

ii. To be respected as a professional institution that protects depositors funds by investing them wisely in the economy, where they can act as a catalyst to create additional national wealth while providing the source of repayment of depositors’ funds.

From the analysis, it is clear that GCDB had been functioning in the former role. Although it had earned the thanks of its largess, it had earned the disrespect of the public, the authorities and the international financial community. The direct cost is clearly visible in the equity injections that were required overtime, the Managed Fund and the huge accumulated losses. The indirect cost is less quantifiable, but includes impairment of the reputation of The Gambia in the International financial circles and the retardation of the domestic economic development compared with the level that could have been achieved had GCDB been playing a more professional and constructive role.

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Conflict of Interests

The author declare that there is no conflict of interests regarding the publication of the paper.

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