



**BUSITEMA
UNIVERSITY**
Pursuing Excellence

**FINANCIAL REGULATION, FINANCIAL INNOVATION,
PORTFOLIO DIVERSIFICATION AND PROFITABILITY
OF FINANCIAL INSTITUTIONS IN KAMPALA
CAPITAL CITY AUTHORITY**

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DECLARATION

This research dissertation is my original work and has never been presented to this university or to any other institution for partial fulfillment for any award.

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DEDICATION

To my family members including; Ms. Achai Elizabeth, Ms. Isoto Stella and dear children for their love and ceaseless prayers.

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ABBREVIATIONS AND ACRONYMS

AMFIU	Association of Micro-Finance Institutions of Uganda
ATMs	Automated Teller Machines
BCBS	Basel Committee on Bank Supervision
BoU	Bank of Uganda
CAR	Capital Adequacy Ratio
COSASE	Committee on Commissions, Statutory Authorities and State Enterprises
CVI	Content Validity Index
FIs	Financial Innovations.
FRs	Financial Regulations
FSB	Financial Stability Board
HHI	Hirschman-Herfindahl Index
IADI	International Association of Deposit Insurers
ICT	Information Communication Technology
IMF	International Monetary Fund
MDIs	Micro-Deposit Taking Institutions
NIM	Net Interest Margin
NPLs	Non-Performing Loans
POS	Point of Service
PwC	PricewaterhouseCoopers Private Limited
ROA	Return on Asset
ROE	Return on Equity
RTGS	Real Time Gross Settlement
SACCOs	Savings and Credit Cooperative Associations
USA	United States of America
VSLAs	Village Savings and Loans Associations.

ABSTRACT

This study investigated the mediation role of financial regulation in the relationship between financial innovation and portfolio diversification with profitability of financial institutions in Kampala Capital City Authority. The study applied a cross-sectional research design and quantitative approach to study the relationship between variables as outlined in the study objective. The population comprised 33 formal and regulated financial institutions (24 commercial banks, 4 credit institutions and 5 MDIs). From each financial institution, four respondents were purposively selected to participate in the study and these formed the unit of inquiry. These included supervisors, credit officers, business development officers and managers. Questionnaires were used to collect relevant data for the study. Data were analyzed using *SPSS version. 22.0*. Pearson Product Rank correlation coefficient was used to test the association between the dependent variable and independent variables, and the regression test was used to find out how profitability varied with financial innovation, portfolio diversification and regulation. *Med-graph* application for testing mediation effect was also used. The findings established that financial innovations, portfolio diversification and financial regulation are positively associated with profitability. A significant positive relationship between financial innovation, portfolio diversification and financial regulation was established. The study also revealed that financial regulation does not mediate the relationship between financial innovation, portfolio diversification and profitability. The study also confirmed that financial innovation, portfolio diversification and financial regulation are essential in improving profitability. The study recommended that financial institutions should embrace appropriate ICT-based applications so as to reduce operational costs, improve decision making processes, facilitate on-line transactions, enhance efficiency and customer satisfaction to achieve improved profitability and sustainable growth.

Keywords: *Financial Regulation; Financial Innovation; Portfolio Diversification; Firm Profitability*