BANK SUPERVISION DIVISION

BANKING SECTOR REPORT

FOR

QUARTER ENDED 30 SEPTEMBER 2018

1. EXECUTIVE SUMMARY

1.1. The banking sector remained generally stable and results of stress tests conducted by the Reserve Bank show that the sector is largely resilient to various shocks.

1.2. All financial soundness indicators depict satisfactory condition and performance of the banking sector characterized by an expanding asset base, adequate capitalization, improved profitability and satisfactory asset quality.

1.3. Banking sector total assets maintained an upward growth trajectory during the period under review from $12.35 billion as at 30 June 2018 to $13.55 billion as at 30 September 2018.

1.4. The banking sector aggregate core capital increased by 7.24%, from $1.38 billion as at 30 June 2018 to $1.48 billion as at 30 September 2018 buoyed by increased earnings recorded by the sector.

1.5. All operating banking institutions, were in compliance with the prescribed minimum capital requirements, with the exception of one institution. Tier 1 and capital adequacy ratios of 22.70% and 26.32%, were above the regulatory minima of 8% and 12%, respectively.

1.6. There was an improvement in the banking sector loan portfolio as reflected by a decline in NPL ratio from 8.63% as at 30 September 2017 to 6.69% as at 30 September 2018.

1.7. Total banking sector deposits amounted to $9.57 billion, as at 30 September 2018, while total loans and advances were $4.01 billion, translating to a loans to deposit ratio of 41.88%.

1.8. The banking sector recorded improved earnings during the period under review with an aggregate net profit of $283.98 million for the nine (9) months ended 30 September 2018 compared to a net profit of $160.73 million for the corresponding period in 2017.

1.9. The average prudential liquidity ratio for the banking sector was 70.66% as at 30

September 2018 up from 68.45% recorded as at 30 June 2018, against the minimum regulatory threshold of 30%. However, the loans to deposits ratio declined from 43.53% to 41.8% over the quarter under review.

2. ARCHITECTURE OF THE BANKING SECTOR

2.1. As at 30 September 2018, the sector had nineteen operating banking institutions as shown in the table below.

Table 1: Architecture of the Banking Sector

Type of Institution	**Number**
Commercial Banks	13
Building Societies	5
Savings Bank	1
Total Banking Institutions	**19**

2.2. In addition, other Institutions under the supervision of the Reserve Bank were as follows.

Other financial institutions	**Number**
Development Financial Institutions	2
Deposit taking MFIs	6
Credit-only-MFIs	195
Total (including development financial institutions)	222

3. CONDITION AND PERFORMANCE OF THE BANKING SECTOR

3.1. The sector recorded satisfactory performance during the period under review as reflected by adequate capitalization and improved earnings performance.

3.2. The financial soundness indicators for the review period indicate satisfactory performance as shown in Table 2 below.

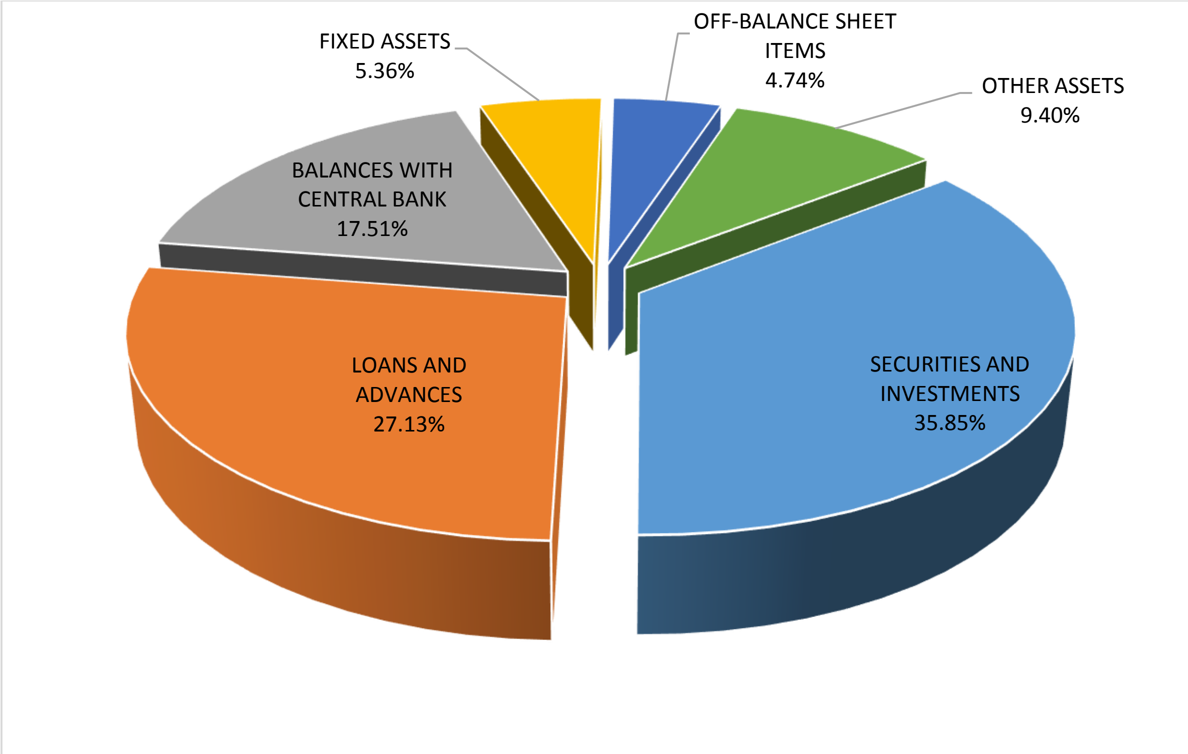
Table 2: Financial Soundness Indicators

Key Indicators	Benchmark	Sep-17	Jun-18	Sep-18
Total Assets	-	$10.26bn	$12.35bn	$13.55bn
Total Loans	-	$3.73bn	$4.08bn	$4.01bn
Net Capital Base	-	$1.43bn	$1.61bn	$1.72bn
Core Capital	-	$1.25bn	$1.38bn	$1.48bn
Total Deposits	-	$7.62bn	$9.53bn	$9.57bn
Net Profit	-	$160.73m	$176.09m	$283.98m
Return on Assets	-	1.89%	1.75%	2.56%
Return on Equity	-	11.15%	11.16%	16.64%
Capital Adequacy Ratio	12%	26.98%	26.32%	27.79%
Loans to Deposits	70%	49.01%	43.53%	41.88%
Non-Performing Loans Ratio	5%	8.63%	6.22%	6.69%
Provisions to ACL	-	83.37%	139.69%	165.86%
Liquidity Ratio	30%	62.49%	68.45%	70.66%
Cost to Income Ratio		77.02%	67.59%	66.85%

Total Banking Assets…

3.3. Total banking assets grew by 9.72% from $12.35 billion as at 30 June 2018 to $13.55 billion as at 30 September 2018.

3.4. The asset mix as at 30 September 2018 was largely composed of loans and advances (27.13%) and securities & investments (35.84%) as shown below.

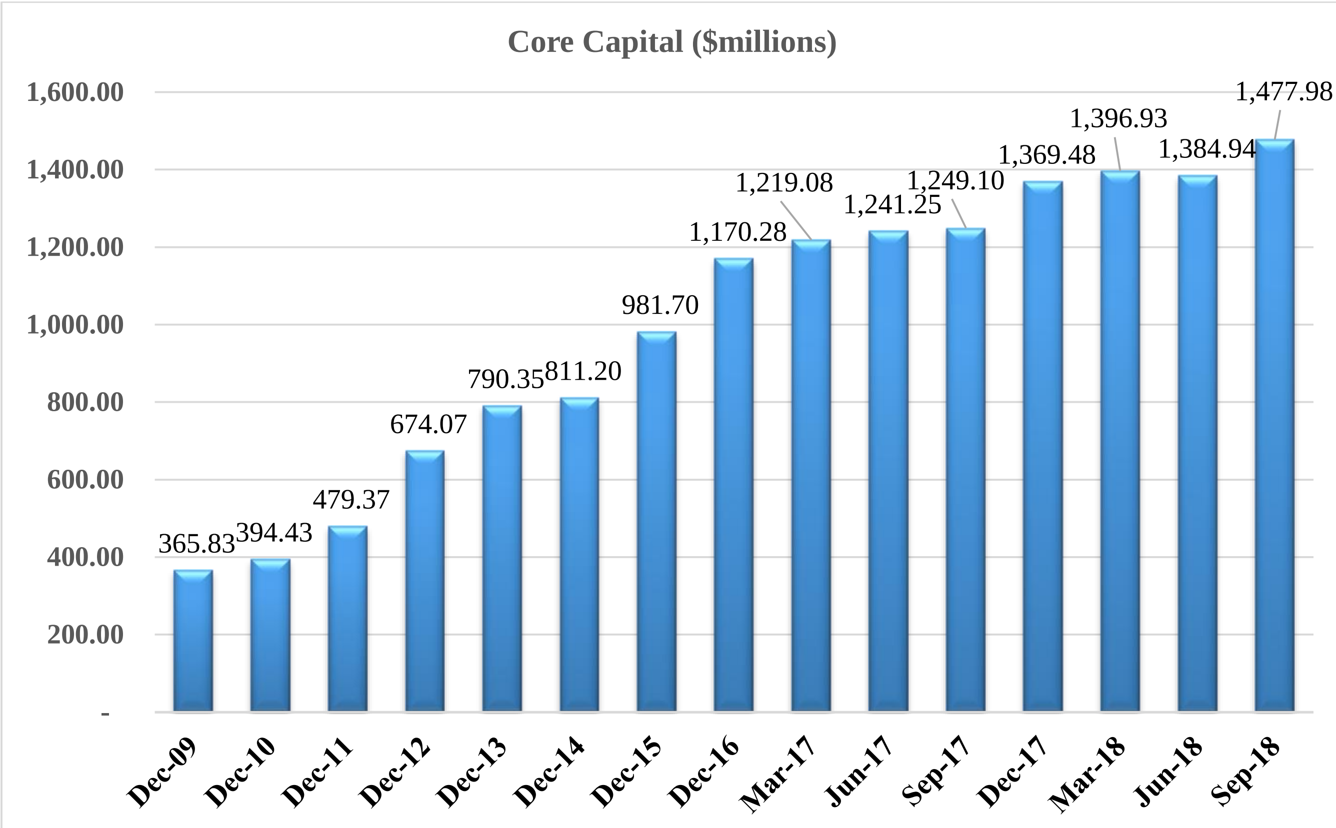


Capitalisation…

3.5. The sector is adequately capitalised with aggregate core capital of $1.48 billion as at 30 September 2018, up from $1.38 billion as at 30 June 2018.

3.6. The trend in the banking sector core capital levels for the period December 2009 to September 2018 is shown in the graph below:

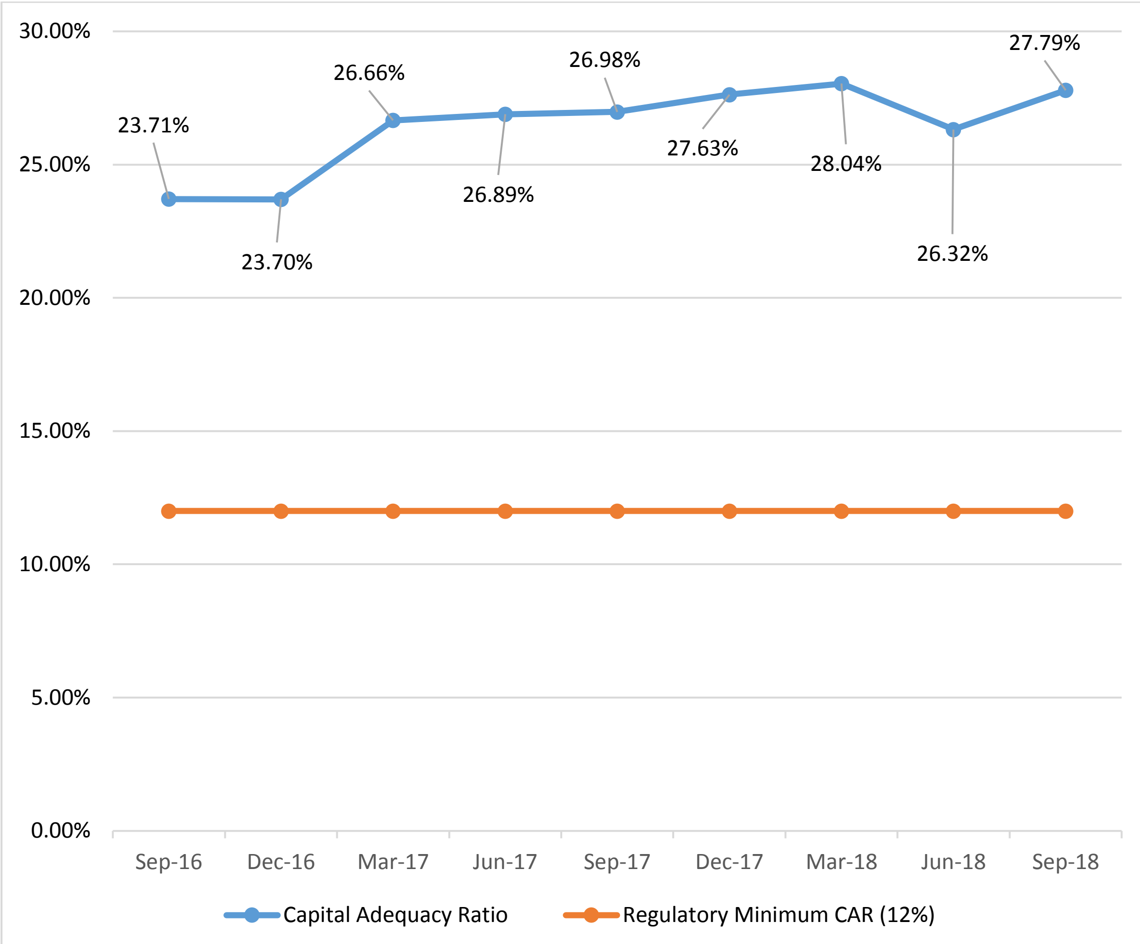
Figure 1: Core Capital Trends 2009 to September 2018



3.7. As at 30 September 2018, all operating banking institutions, with the exception of one institution, were in compliance with the minimum prescribed capital requirements.

3.8. The capital adequacy ratio (CAR), a measure of solvency, indicates that the industry is well capitalised as shown below:

Figure 2: Capital Adequacy Ratios Trend



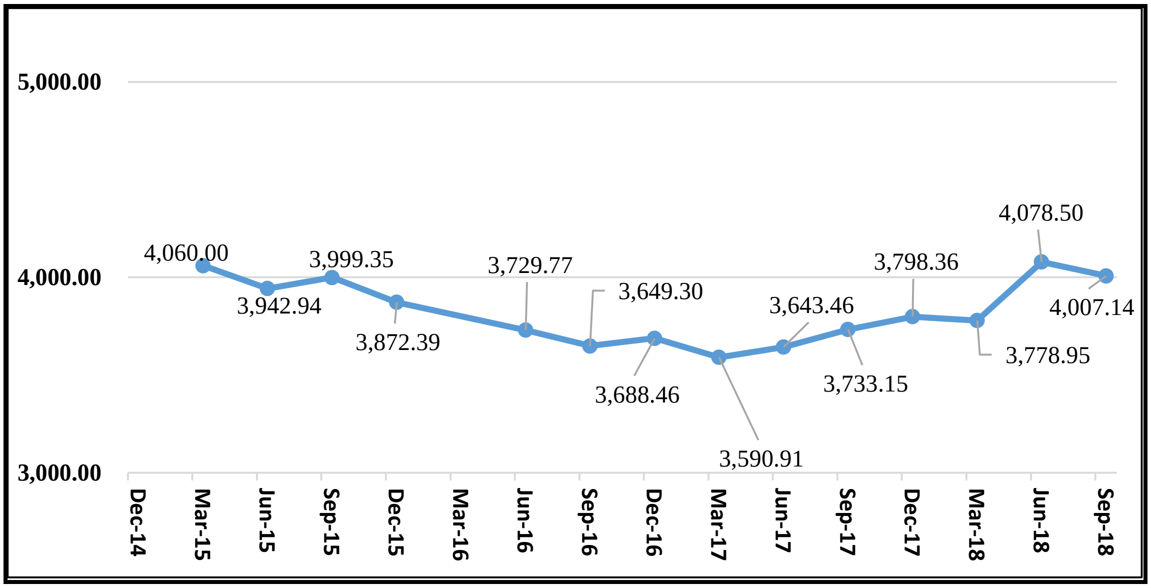
3.9. Banking institutions are on course in meeting the 2020 minimum capital requirements and as at 30 September 2018, five (5) banking institutions were already compliant with the 2020 minimum capital requirements of $100 million for tier 1 strategic group.

Asset Quality...

3.10. Total banking sector loans and advances remained largely stable at $4.00 billion as at 30 September 2018.

3.11. Figure 3 below shows the trend of banking sector loans and advances from 31 December 2014 to 30 September 2018.

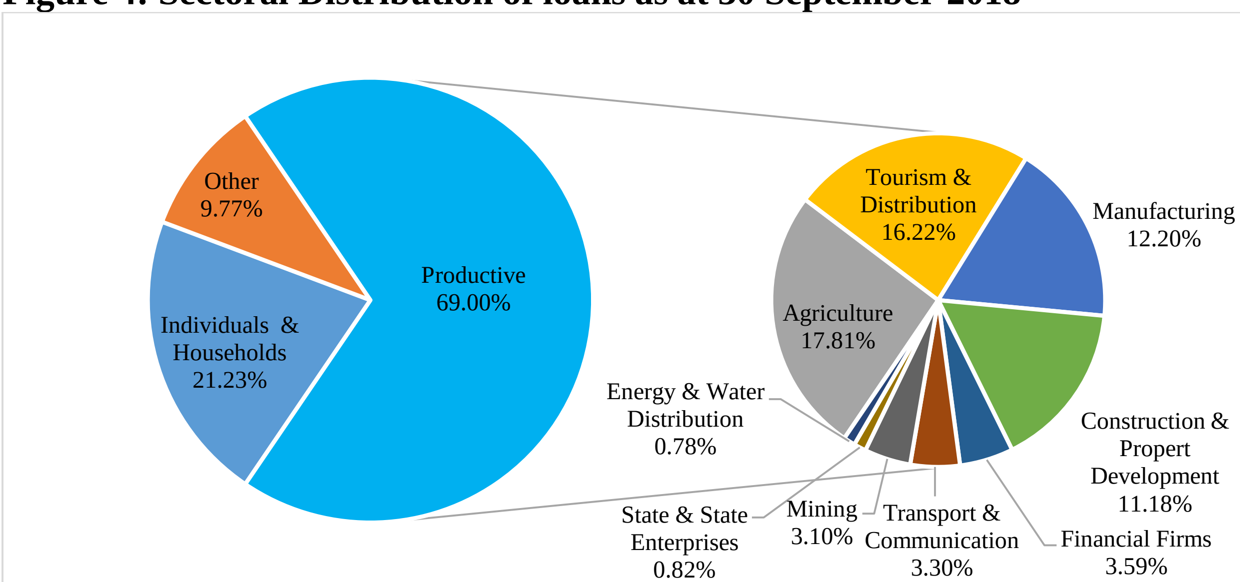
Figure 3: Banking Sector Loans & Advances ($)



Distribution of Loans and Advances…

3.12. Lending to the productive sector constituted 61.25% of total loans as at 30 September 2018 as shown in the diagram below.

Figure 4: Sectoral Distribution of loans as at 30 September 2018

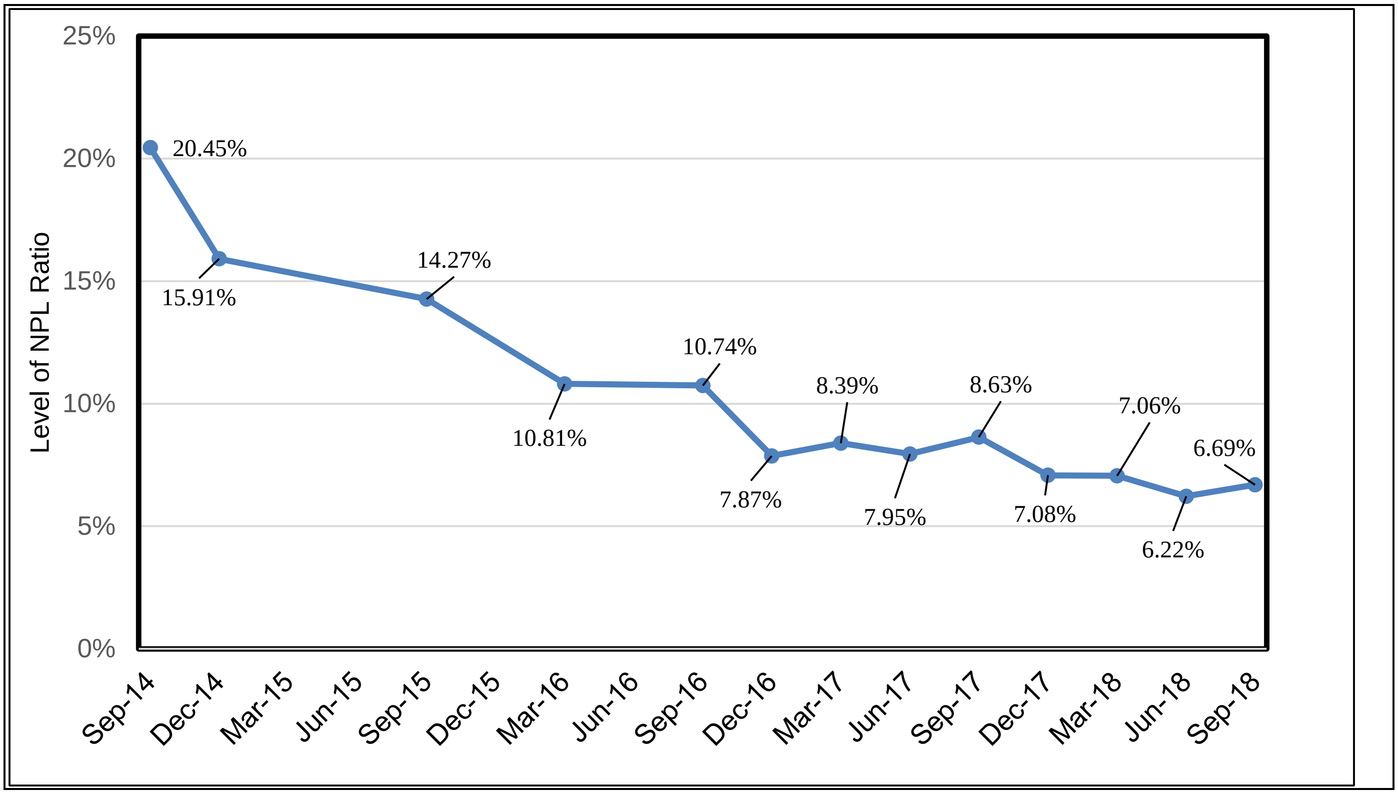


Non-Performing Loans

3.13. Credit risk remains low. The level of non-performing loans (NPLs) to total loans was 6.69% as at 30 September 2018 compared to 6.22% as at 30 June 2018.

3.14. The trend in the level of non-performing loans from 2014 to September 2018 is indicated in Figure 5 below:

Figure 5: Trend in Non-Performing Loans 2014 – September 2018



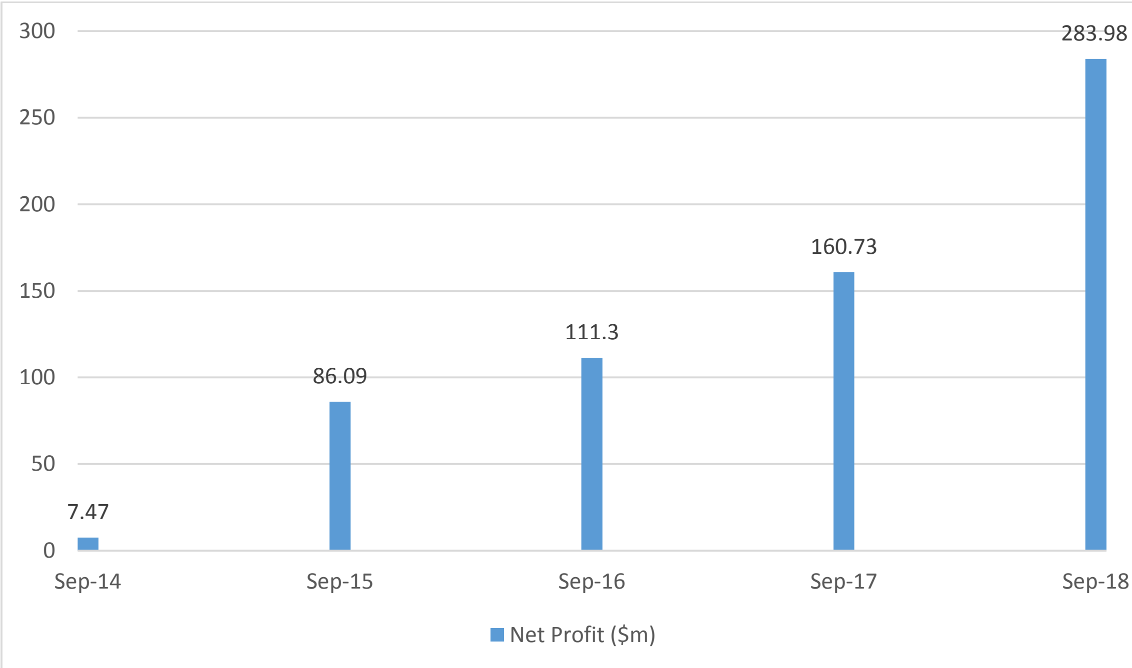
Earnings Performance...

3.15. The banking sector remained profitable posting an aggregate net profit of $283.98 million (76.68% increase) for the nine months ended 30 September 2018 compared to a net profit of $160.73 million for the corresponding period in 2017. The improved earnings performance was buoyed by non-interest income arising from a surge in digital transactional volumes as well as interest income from investments in securities, mainly treasury bills.

3.16. During the period under review, the major profitability indicators, return on assets and return on equity improved from 1.89% and 11.15%, to 2.56% and 16.64%, respectively.

3.17. Figure 6 shows trend in net profit from September 2014 to September 2018.

Figure 6: Trend in Net Profit from 30 September 2014 to 30 September 2018

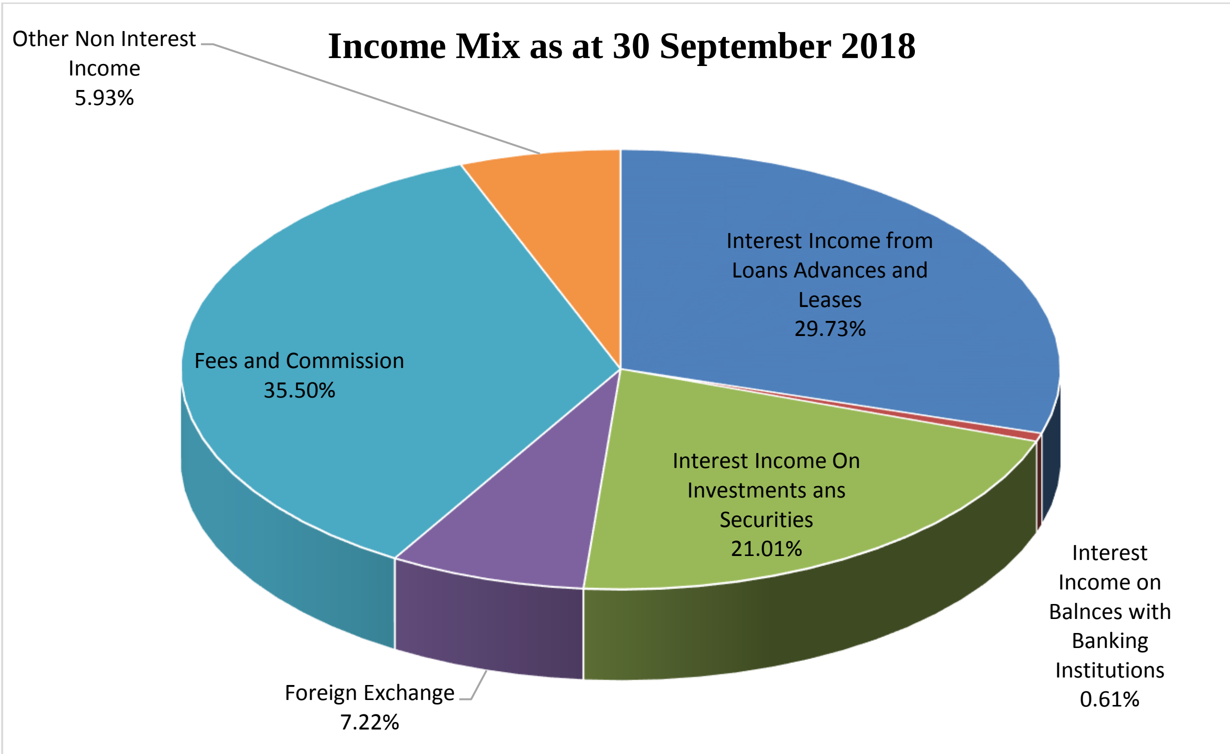


3.18. Fees and commission continues to drive growth in total income as it increased by 15.75% from $318.97 million during the nine months ended 30 September 2017 to $369.20 million during the corresponding period in 2018, and accounted for 35.50% of total income, as at 30 September 2018.

3.19. Interest income from loans and advances constituted 29.73% of total income for the nine months ended 30 September 2018, compared to 36.54% in 2017, while interest on investments and securities accounted for 21.01% (in 2018) against 15.46% (in 2017).

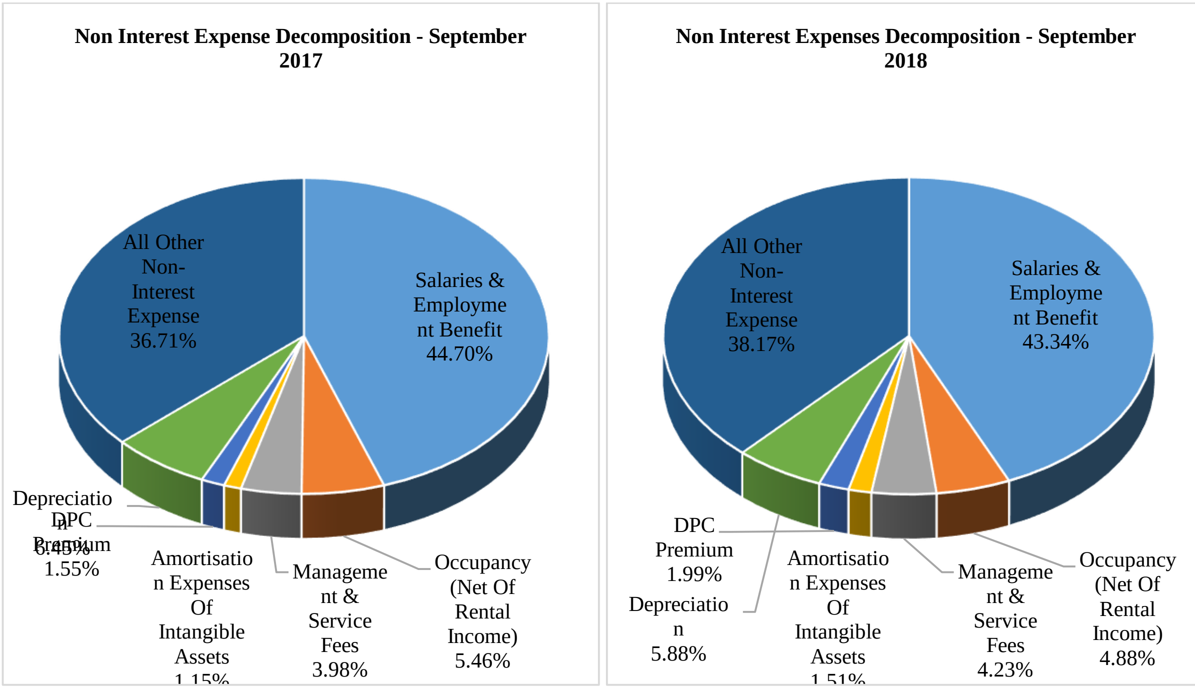
3.20. The income mix for the sector for the nine months ended 30 September 2018 is shown in Figure 7:

Figure 7: Banking Sector Income Mix as at 30 September 2018



3.21. For the nine months ended 30 September 2018, salaries & employment benefits constituted 43.34% of total banking sector costs as shown in the figure below.

Figure 8: Banking Sector Operating Expenses



Liquidity and Funds Management...

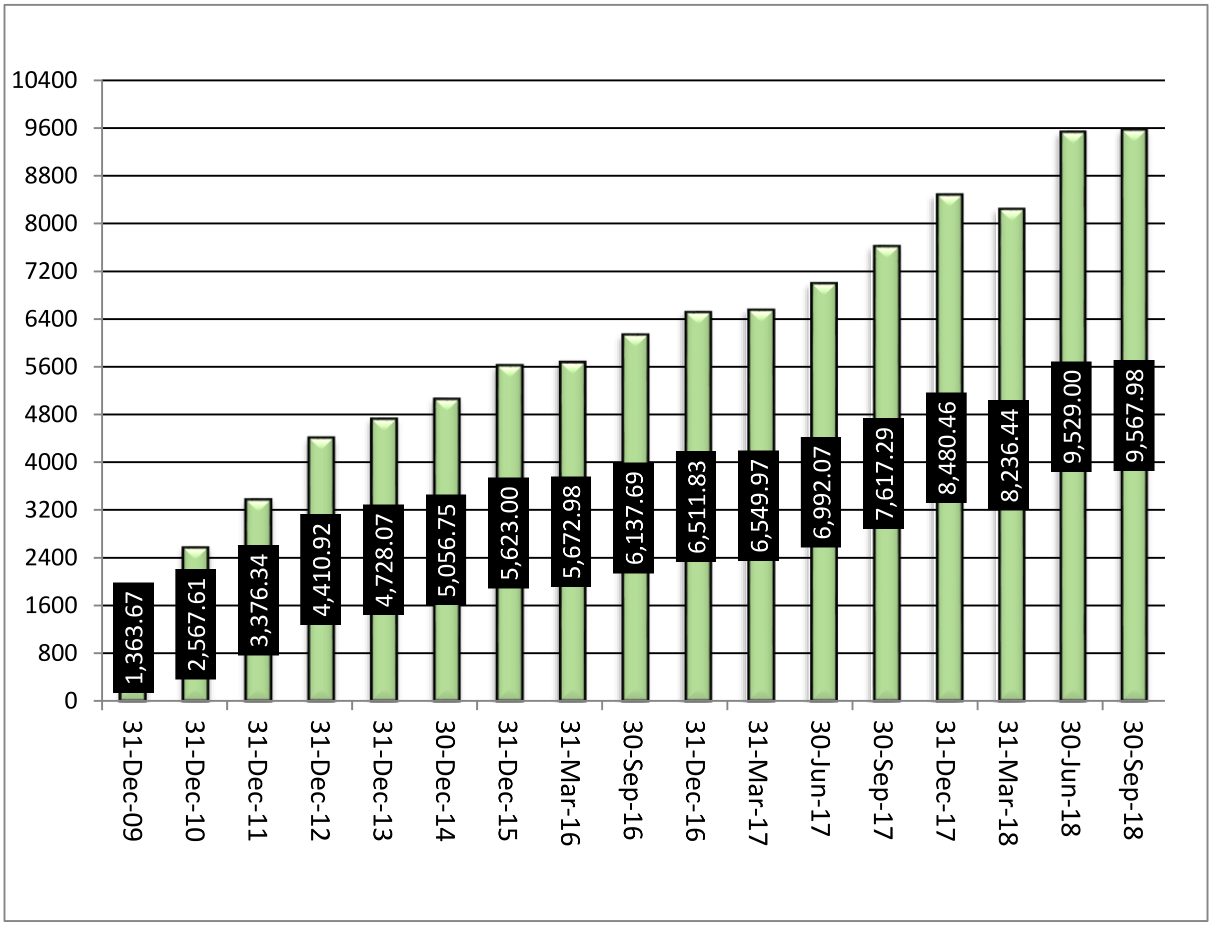
3.22. As at 30 September 2018, banking sector deposits increased by 0.76% from $9.53 billion as at 30 June 2018 to $9.57 billion as at 30 September 2018.

3.23. Total loans and advances totaled $4.01 billion, translating to a loans to deposit ratio of 41.88%.

3.24. The average prudential liquidity ratio for the banking sector was 70.66% as at 30 September 2018, up from 68.45% recorded as at 30 June 2018 against a regulatory minimum of 30% while the loans to deposits ratio was 41.8% and deposits to assets ratio was 70.6%.

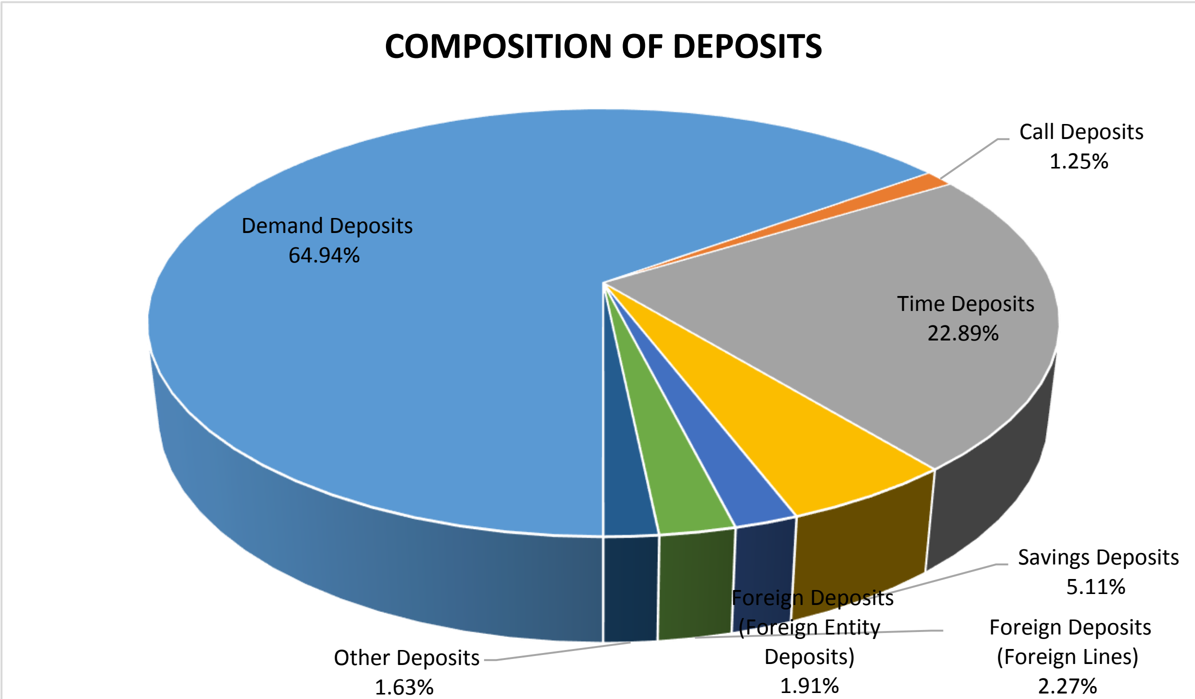
3.25. The figure below shows the trend of banking sector deposits over the period 31 December 2009 to 30 September 2018.

Figure 9: Trend of Banking Sector Deposits ($)



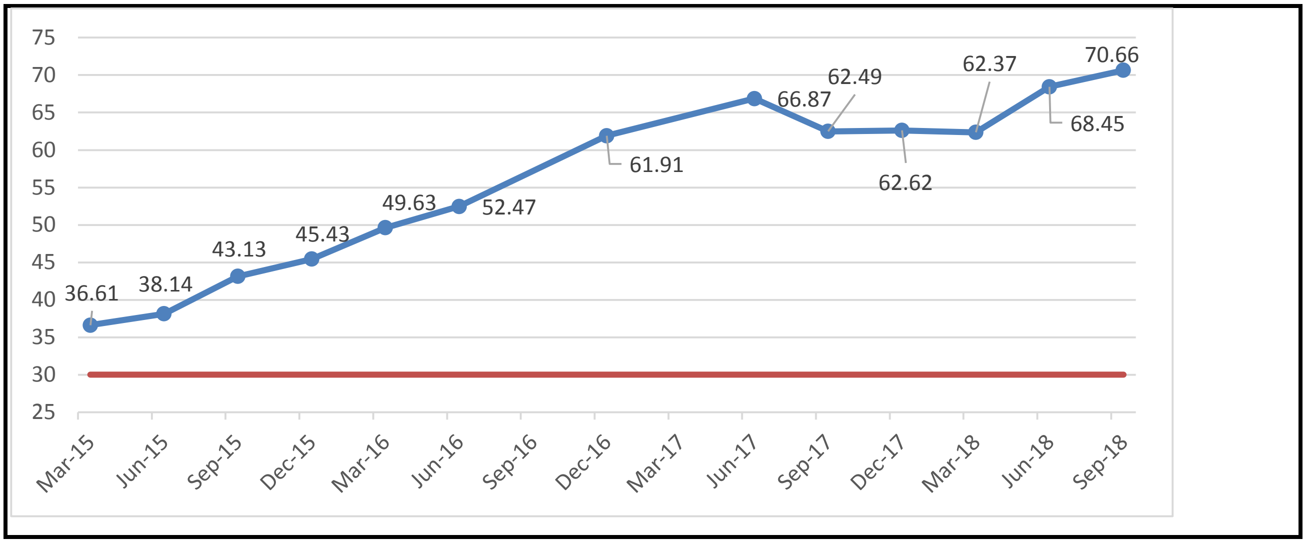
3.26. As at 30 September, the banking sector was predominantly funded by demand deposits which constituted 64.94% of total deposits as depicted in Figure 10.

Figure 10: Composition of Deposits as at 30 September 2018



3.27. The average prudential liquidity ratio for the banking sector was 70.66% as at 30 September 2018 and two institutions were non-compliant with the minimum prudential liquidity ratio of 30% as at 30 September 2018. The trend in the prudential liquidity ratio is shown in Figure 11 below:

Figure 11: Prudential Liquidity Ratio Trend (%)



3.28. The high average prudential liquidity ratio is reflective of the high stock of treasury bills (TBs) held by banking institutions, constituting 46.557% of net available liquid assets of $7.42 billion held by banking institutions.

Sensitivity to Market Risk...

3.29. The banking sector's exposure to foreign exchange rate risk remained low on account of limited trade in foreign exchange by banks as they are not taking positions on their own account.

3.30. All banking institutions were resilient to a major level interest rate risk shock of 10% increase or decrease in interest rates as their capital adequacy ratios would remain above the prescribed minimum of 12%.

3.31. As at 30 September 2018, sixteen (16) banking institutions had liability sensitive books, implying that the banks would benefit from a decrease in market interest rates.

3.32. Stress testing results indicate that the sector is resilient to a major foreign exchange risk shock of an appreciation of the USD against major currencies by 15% as the capital adequacy ratio will remain above 12% at 19.48%.