BANK SUPERVISION DIVISION

BANKING SECTOR REPORT

FOR

QUARTER ENDED 31 MARCH 2019

1. EXECUTIVE SUMMARY

1.1. During the quarter ended 31 March 2019, the banking sector remained generally stable and continued to exhibit resilience, buoyed by adequate capitalisation, sustained earnings performance, satisfactory asset quality and improved liquidity position. There was, however heightened exposure to foreign currency risk, which negatively affected a few institutions' earnings during the quarter under review.

1.2. Stress tests conducted by the Reserve Bank on banks' exposure to credit, interest rate and foreign exchange risks reflect resilience to various shocks of differing magnitudes.

1.3. Banking sector total assets continued on an upward trend increasing by 10.17% from $13.98 billion as at 31 December 2018 to $15.40 billion as at 31 March 2019.

1.4. During the period under review, the banking sector was adequately capitalised with average tier 1 and capital adequacy ratios of 27.67% and 30.74%, respectively. Further, 18 out of 19 operating banking institutions were compliant with prescribed minimum capital requirements.

1.5. The banking sector aggregate core capital increased by 6.92% from $1.58 billion as at 31 December 2018 to $1.69 billion as at 31 March 2019.

1.6. During the quarter under review, total banking sector loans and advances increased by 8.56%, from $4.04 billion as at 31 December 2018 to $4.44 billion as at 31 March 2019. Total banking sector deposits increased marginally during the review period, from $10.38 billion as at 31 December 2018 to $11 billion as at 31 March 2019. This translated to an average loans to deposit ratio of 40.42% as at 31 March 2019, compared to a ratio of 39.62%

as at 31 December 2018.

1.7. Asset quality marginally improved as reflected by a decline in the ratio of non-performing loans (NPLs) to total loans from 6.92% as at 31 December 2018 to 5.58% as at 31 March 2019. The continued improvement in asset quality is largely due to measures instituted by banking institutions, including enhanced credit underwriting standards and risk management practices.

1.8. Although the banking sector remained profitable, aggregate net profit decreased by 8.80% from $85.58 million recorded during the period ended 31 March 2018, to $78.05 million for the period ended 31 March 2019. The decrease was largely attributable to foreign exchange revaluation losses reported by a few banking institutions during the quarter. Out of 19 operating banking institutions, 15 banks reported profits, while four (4) banks recorded losses.

1.9. The average prudential liquidity ratio for the banking sector was 66.85% as at 31 March 2019.

2. ARCHITECTURE OF THE BANKING SECTOR

2.1. As at 31 March 2019, the financial sector comprised 19 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. Other institutions under the Reserve Bank's purview were as follows:

Table 2: Architecture of Other Financial Institutions

Other financial institutions	Number
Development Financial Institutions	2
Deposit-taking Microfinance Institutions	6
Credit-only-Microfinance Institutions	204
Total	**212**

3. CONDITION AND PERFORMANCE OF THE BANKING SECTOR

3.1. The performance of the banking sector was considered satisfactory over the quarter ended 31 March 2019, on the back of adequate capitalisation, improved asset quality and satisfactory liquidity management. Aggregate profitability for the sector marginally declined compared to the same period in 2018, largely as a result of the effects of foreign exchange revaluation losses at some banking institutions.

3.2. The financial soundness indicators for the review period are provided in Table 3 below.

Table 3: Financial Soundness Indicators

Key Indicators	Benchmark	Mar-18	Sept-18	Dec-18	Mar-19
Total Assets	-	$10.95bn	$13.31bn	$13.98bn	$15.40bn
Total Loans & Advances	-	$3.85bn	$4.00bn	$4.09bn	$4.44bn
Net Capital Base	-	$1.61bn	$1.72bn	$1.83bn	$2.09bn
Total Deposits	-	$8.24bn	$9.57bn	$10.32bn	$11.00bn
Net Profit	-	$85.58m	$283.98m	$425.26m	$78.05m

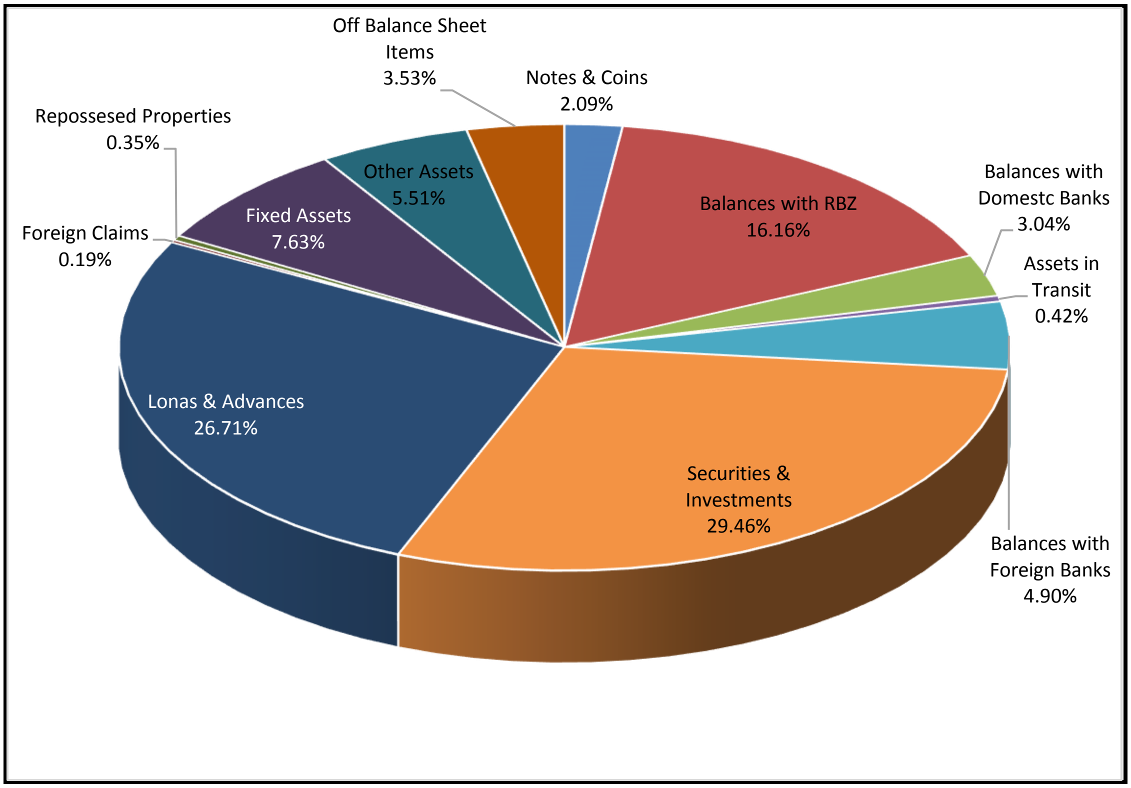
Key Indicators	Benchmark	Mar-18	Sept-18	Dec-18	Mar-19
Return on Assets	-	0.92%	2.61%	4.56%	1.37%
Return on Equity	-	5.19%	16.80%	20.61%	4.92%
Capital Adequacy Ratio	12%	27.91%	27.79%	30.23%	30.74%
Tier 1 Ratio	8%	24.16%	22.68%	23.84%	27.67%
Loans to Deposits	70%	46.69%	41.8%	39.62%	40.43%
Non-Performing Loans Ratio	5%	6.93%	6.69%	6.92%	5.58%
Liquidity Ratio	30%	62.37%	70.66%	67.82%	66.82%

Total Banking Assets…

3.3. The banking sector assets increased by 10.17%, from $13.98 billion as at 31 December 2018 to $15.40 billion as at 31 March 2019.

3.4. The banking sector assets, largely comprised investment & securities (29.46%), loans and advances (26.71%), and balances with central bank which constituted 16.16% of total assets. The proportion of securities & investments and loans & advances, however, declined from 33.50% and 27.08%, respectively as at 31 December 2018.

3.5. Asset composition as at 31 March 2019, is shown in the figure below:



3.6. Fixed assets increased from 5.75% of total assets as at 31 December 2018 to 7.63% of total assets as at 31 March 2019.

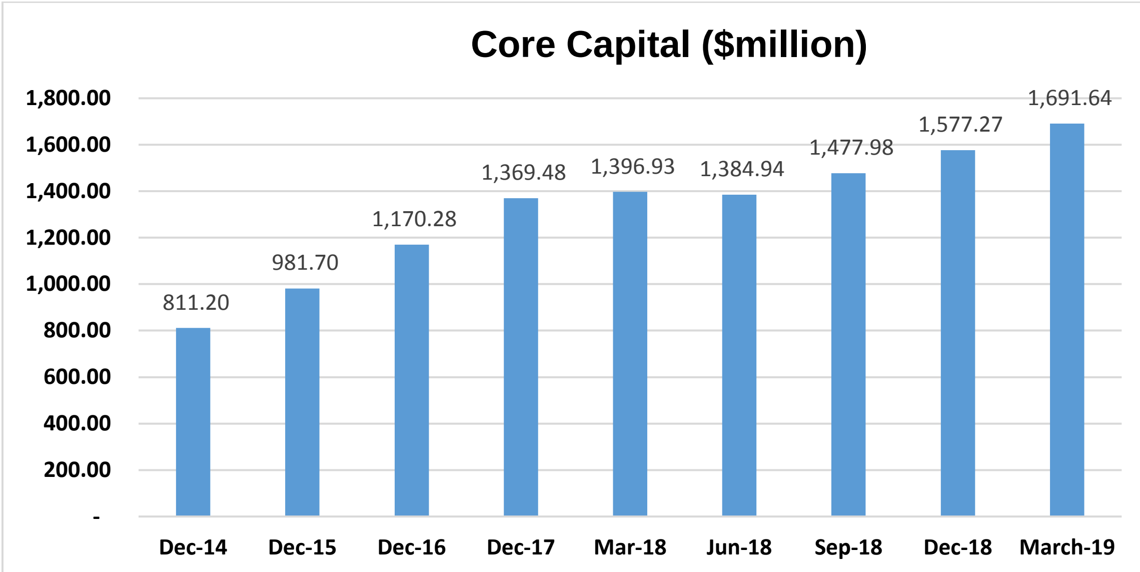
Capitalisation…

3.7. The banking sector remained adequately capitalized, with aggregate core capital of $1.69 billion as at 31 March 2019, representing a 6.92% increase from $1.58 billion as at 31 December 2018. Capitalisation of retained earnings was the major source of capital growth. The banks' capitalisation levels provide institutions with strong loss-absorption capacity.

3.8. As at 31 March 2019, all banking institutions were compliant with the prescribed minimum capital requirements.

3.9. The graph below shows the trend in the banking sector core capital levels for the period December 2014 to March 2019:

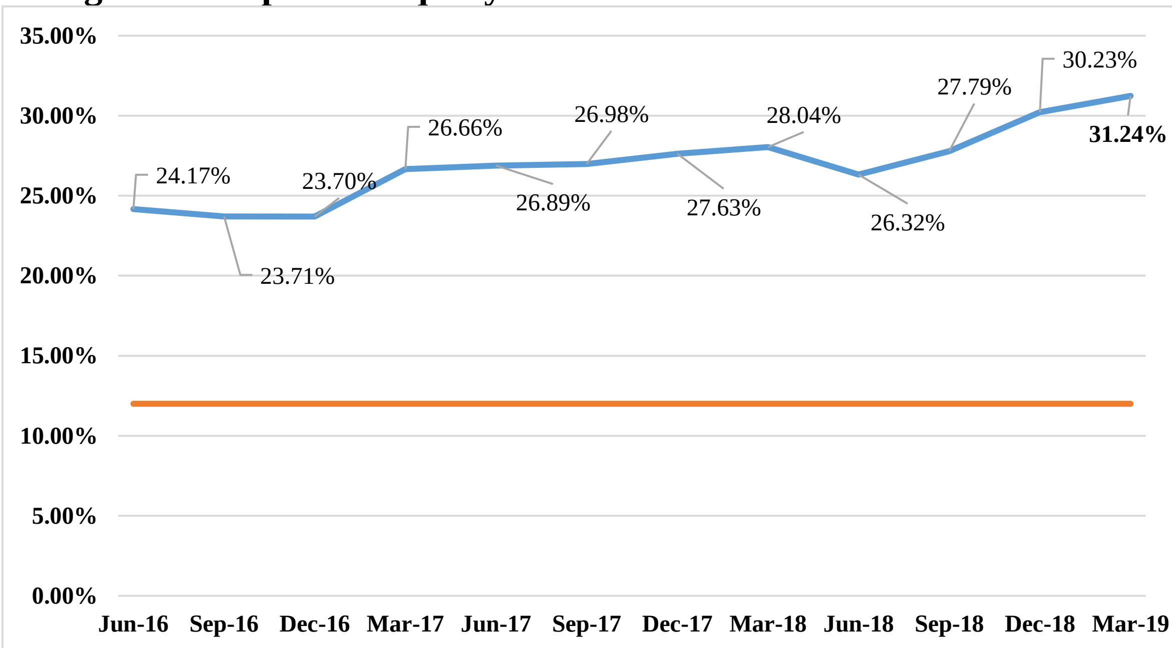
Figure 1: Core Capital Trends 2014 to March 2019



3.10. The sector remained adequately capitalized with average tier 1 and capital adequacy ratios of 27.67% and 31.24%, respectively. All banks reported tier 1 and capital adequacy ratios which were in compliance with the regulatory minima of 8% and 12%, respectively.

3.11. The banking industry's average capital adequacy ratios (CARs) from June 2016 to March 2019 are shown in the figure below.

Figure 2: Capital Adequacy Ratios Trend



3.12. While all banking institutions were compliant with minimum capital adequacy ratio, it is critical that the institutions continue implementing capital preservation strategies in light of the challenging macroeconomic environment.

Asset Quality...

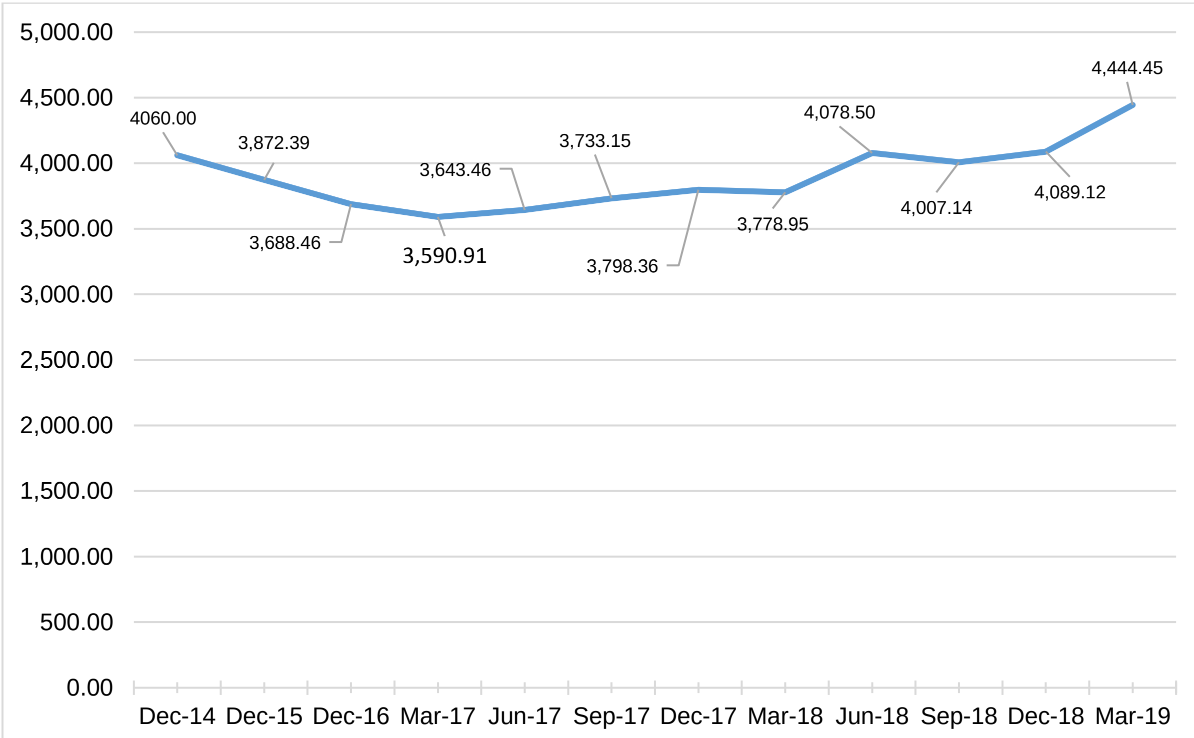
3.13. Total banking sector loans and advances increased by 8.56%, from $4.09 billion as at 31 December 2018 to $4.44 billion as at 31 March 2019.

3.14. The level of the banking sector financial intermediation has remained subdued given a loans to deposits ratio of 40.42%, largely as a result of cautious lending approach adopted by some banking institutions coupled with shortages of foreign currency required by some borrowers to import raw materials.

3.15. The figure below shows the trend of banking sector loans and advances from

31 December 2014 to 31 March 2019.

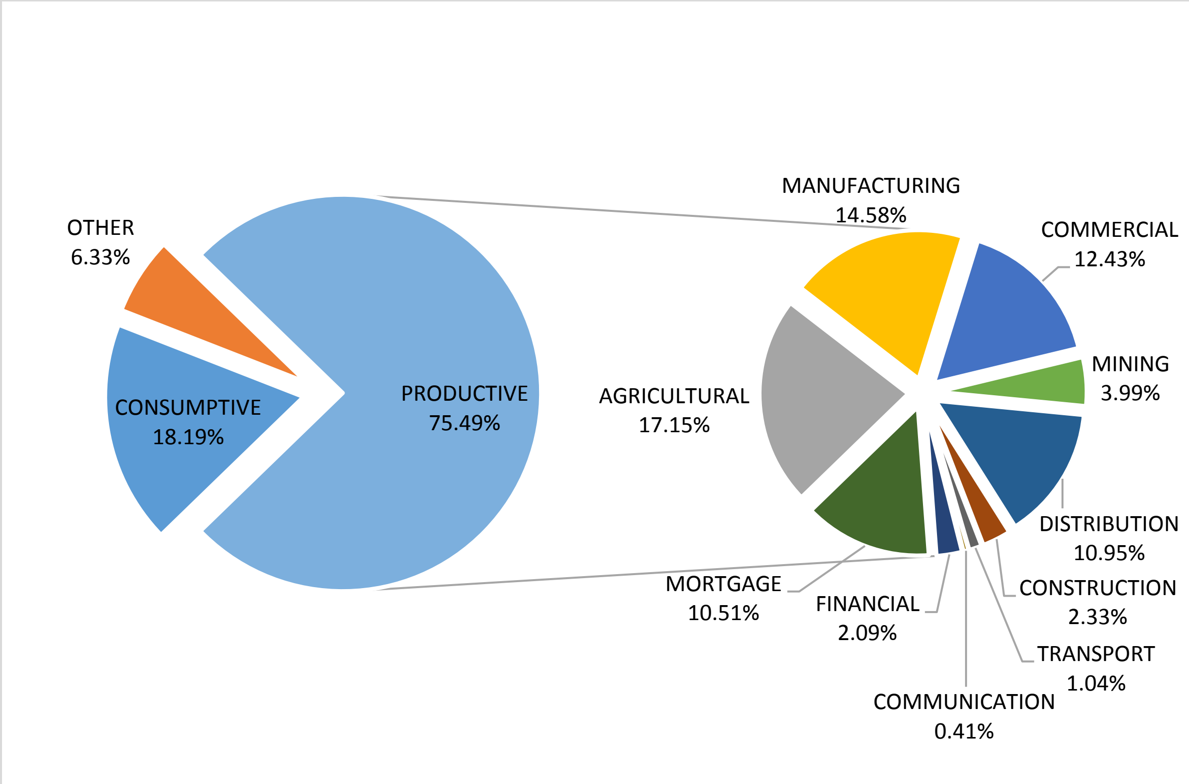
Figure 3: Banking Sector Loans & Advances ($ millions)



Distribution of Loans and Advances…

3.16. Banking sector lending remained skewed towards loans to productive sectors of the economy, constituting 75.49% of total sector loans as at 31 March 2019, as shown in the diagram below.

Figure 4: Sectoral Distribution of loans as at 31 March 2019



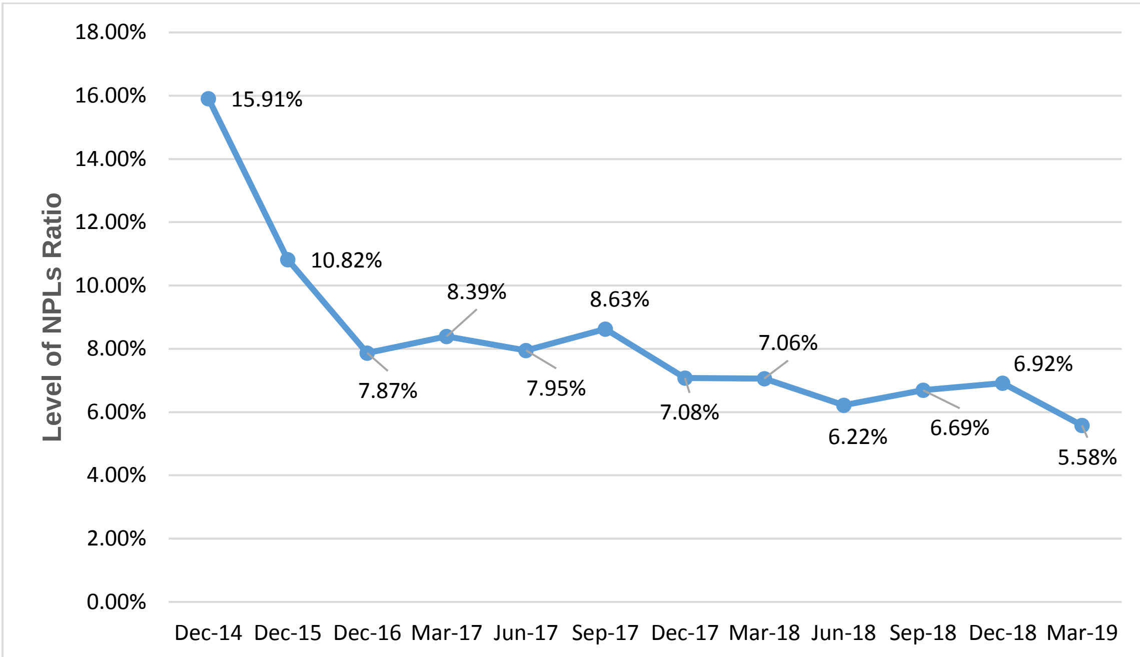
Non-Performing Loans

3.17. The quality of the banking sector loan portfolio improved marginally during the period under review, reflected by the decline in the non-performing loans (NPLs) to total loans, from 6.92% as at 31 December 2018 to 5.58% as at 31 March 2019.

3.18. The improvement in the NPLs ratio, was a result of some banking institutions enhancing their credit risk management practices, notably loan origination, monitoring, collection and recoveries.

3.19. Figure 5 below shows the trend in the level of non-performing loans from December 2014 to March 2019:

Figure 5: Trend in Non-Performing Loans Dec 2014 – March 2019



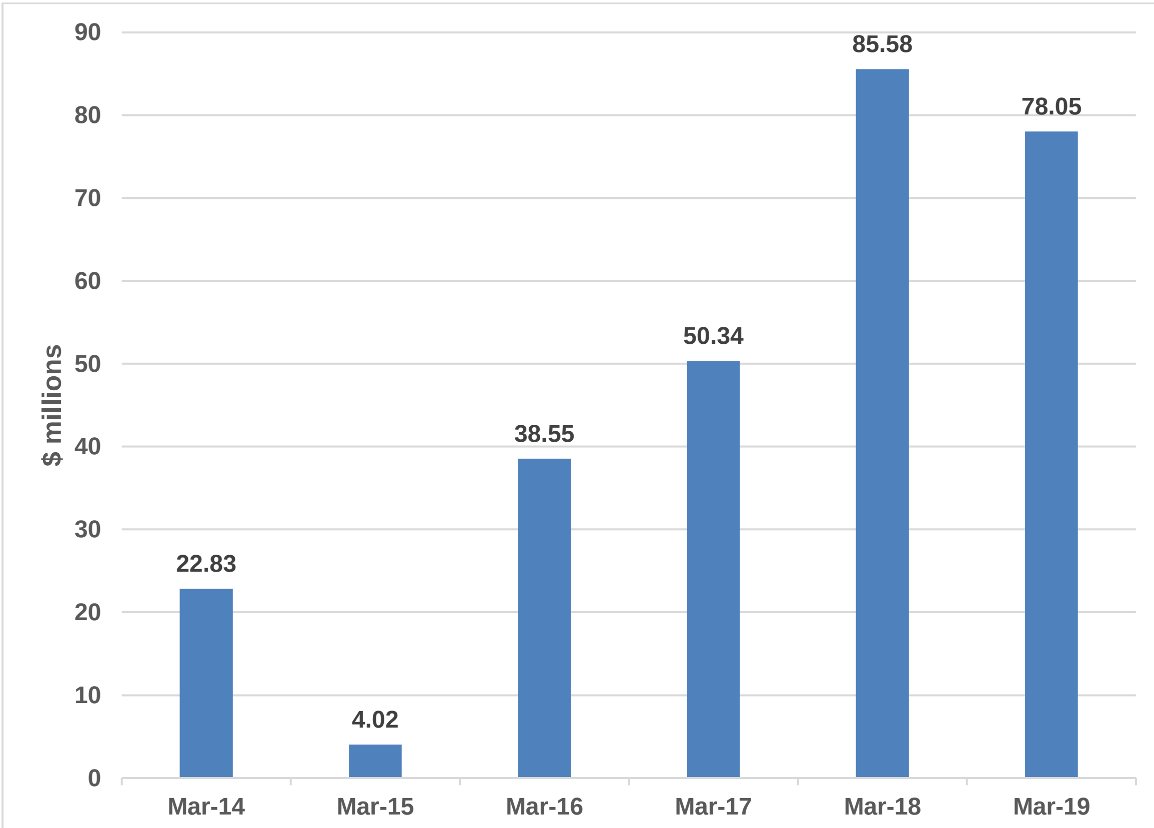
Earnings Performance...

3.20. During the quarter under review, 15 banking institutions were profitable in their operations, while four (4) banks reported losses. The losses were largely attributed to foreign exchange revaluation losses as a result of the floating exchange rate and increased operating costs.

3.21. In comparison to the corresponding period in March 2018, the banking sector recorded an 8.80% decline in aggregate profits, from $85.58 million to $78.05 million during the quarter ended 31 March 2019.

3.22. The figure below shows the trend in net income from March 2014 to March 2019.

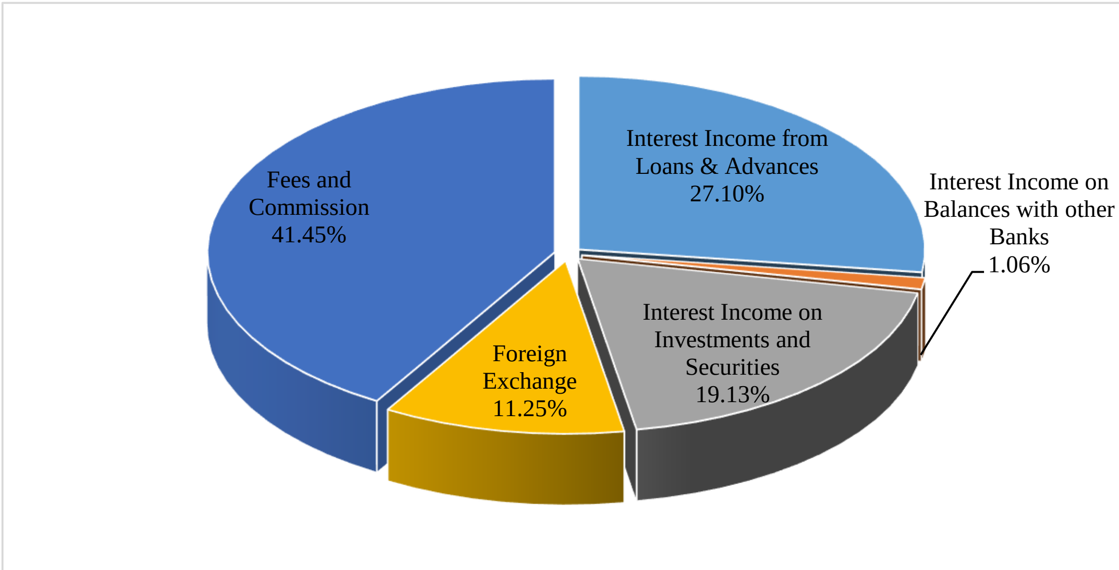
Figure 6: Net Income Trend from March 2014 to March 2019.



3.23. The income mix in the banking sector continued to be skewed towards funded income during the quarter ended 31 March 2019. Non-interest income was largely driven by increased digital transactional volumes as most banks upheld strategies of realigning their business models in response to migration by customers to digital platforms.

Figure 7 below shows the income mix for the sector for the three months ended 31 March 2019:

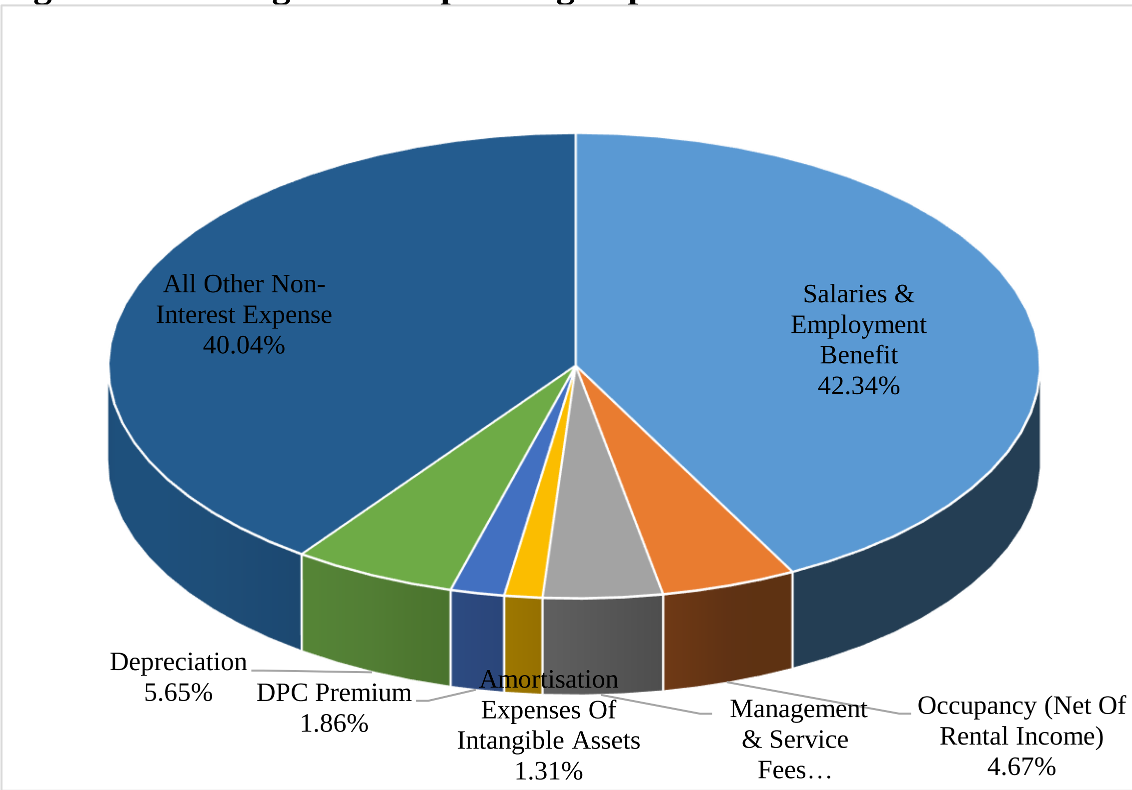
Figure 7: Banking Sector Income Mix as at 31 March 2019



3.24. As shown in the diagram above, the sector is steadily drifting away from the traditional sources of revenue such as interest income from loans and advances diversifying toward activities that generate fee income, trading revenue, and other types of non-interest income.

3.25. As at 31 March 2019, the major component of non-interest expenses was salaries & employment benefits, which accounted for 42.34% of total banking sector costs as shown in the figure below.

Figure 8: Banking Sector Operating Expenses



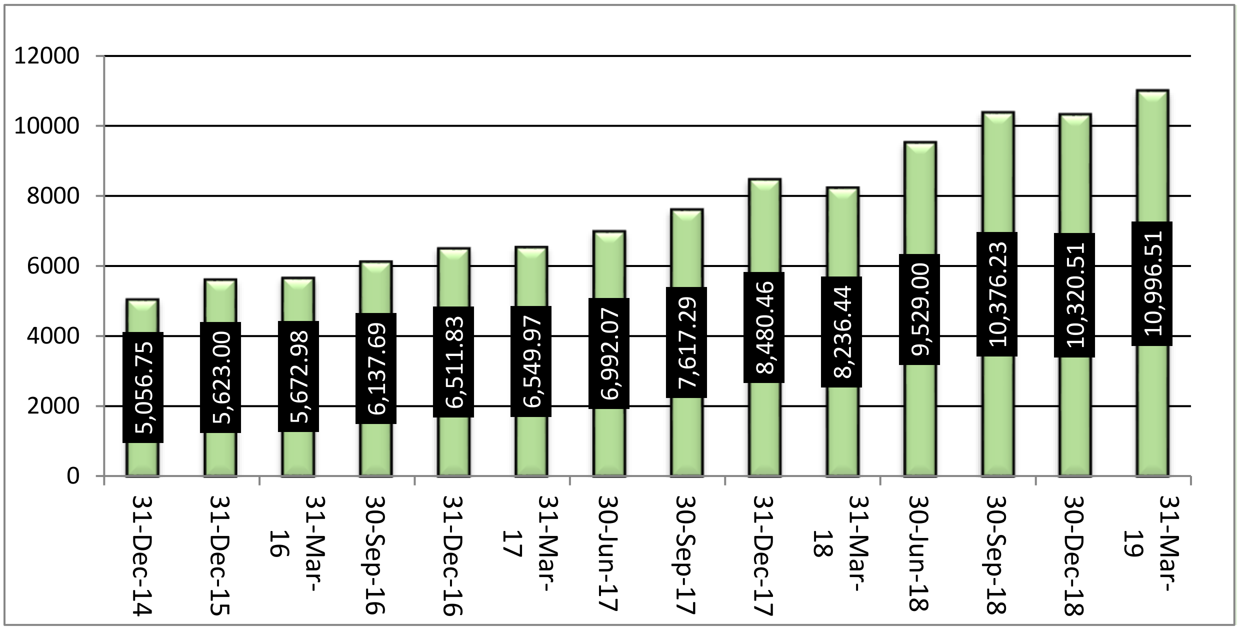
3.26. There was an improvement in the average banking sector profitability indicators during the period under review, as return on assets and return on equity improved from 0.92% and 5.19% as at 31 March 2018 to 1.37% and 4.92% as at 31 March 2019, respectively.

Liquidity and Funds Management...

3.27. Banking sector deposits increased to $11billion as at 31 March 2019 from $10.32 million as at 31 December 2018, an increase of 6.59%. In comparison to March 2018 the sector recorded an increase of 33.50% from $8.24 billion.

3.28. The figure below shows the trend of banking sector deposits over the period 31 December 2014 to 31 March 2019.

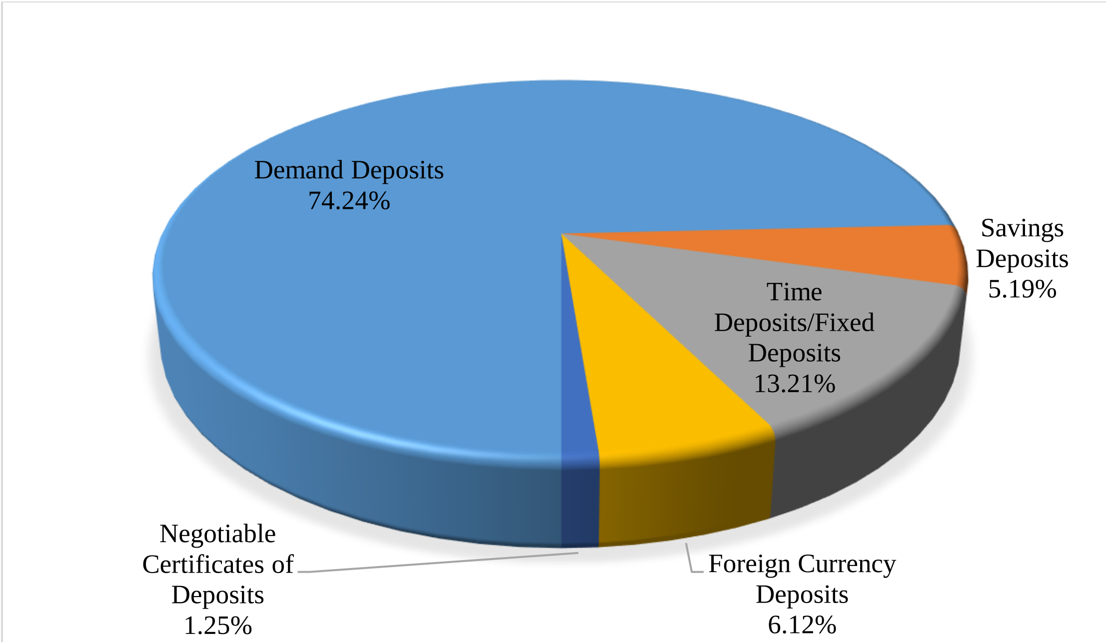
Figure 9: Trend of Banking Sector Deposits ($ millions)



3.29. The increase in the deposit base during the quarter under review is mainly attributable to the revaluation of foreign currency denominated.

3.30. The deposit base for the banking sector has continued to be dominated by demand deposits which constituted 66.75% ($7.34 billion) of the total non-bank deposits, as shown in the figure below.

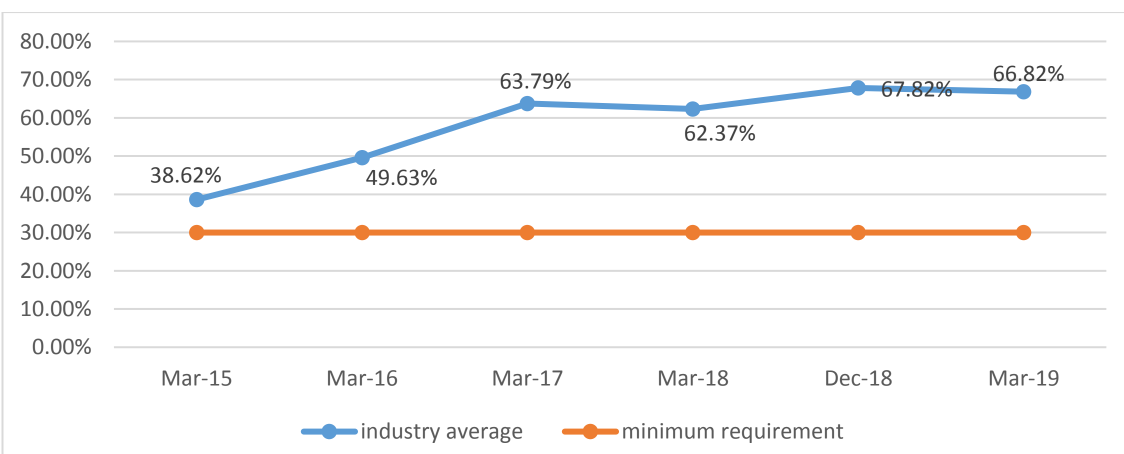
Figure 10: Composition of Deposits as at 31 March 2019



3.31. The average prudential liquidity ratio as at 31 March 2019 was 66.82%, a decrease from 67.82% as at 31 December 2018. As at 31 March 2019, two (2) banking institutions were non-compliant with the minimum prudential liquidity ratio of 30%. The non-compliant banking institutions are taking measures to ensure compliance with the minimum prudential liquidity ratio.

3.32. The figure below shows the trend in the banking sector average prudential liquidity ratio from March 2015.

Figure 12: Prudential Liquidity Ratio Trend (%)



3.33. The prudential liquidity ratio has remained high reflective of the cautious approach to lending with increased investments in securities.

Sensitivity analysis...

3.34. As at 31 March 2019, most banking institutions were resilient to a major shock of 15 percentage point increase in interest rates, as their capital adequacy ratios would remain above the prescribed minimum of 12%, except for one institution whose capital adequacy ratio would fall to 9.40%, which is below the prescribed minimum.

3.35. All banking institutions were resilient to a major foreign exchange risk shock of either an appreciation or depreciation of the USD against major currencies by 15%. The sector however continued to face foreign currency shortages on the back of structural bottlenecks in the economy. Various policy interventions to promote foreign exchange generation need to be instituted.

31 March 2019