BANK SUPERVISION DIVISION

BANKING SECTOR REPORT

FOR

QUARTER ENDED 31 DECEMBER 2019

1. EXECUTIVE SUMMARY

1.1. The banking sector exhibited resilience during the quarter ended 31 December 2019, as reflected by adequate capitalisation, sustained earnings performance, as well as satisfactory asset quality and liquidity.

1.2. Overall banking sector profitability was largely buoyed by revaluation gains on investment properties and foreign currency denominated assets during the year ended 31 December 2019.

1.3. The banking sector remained adequately capitalized, with aggregate core capital of $7.47 billion as at 31 December 2019, representing a 107.90% increase from $3.59 billion as at 30 September 2019. The growth in capital was mainly attributed to capitalisation of retained earnings.

1.4. Banking sector assets increased by 47.94%, from $40.99 billion as at 30 September 2019 to $60.64 billion as at 31 December 2019. The growth in banking sector assets was mainly attributable to revaluation of properties and translation of foreign currency denominated loans.

1.5. Total banking sector loans and advances increased by 51.26%, from $8.35 billion as at 30 September 2019 to $12.63 billion as at 31 December 2019 driven by the effect of translation of foreign currency denominated loans. Total banking sector deposits amounted to $34.50 billion, an increase of 60.39% from $21.51 billion during the period under review, mainly attributable to the revaluation of foreign currency denominated deposits.

1.6. The level of the banking sector financial intermediation has, however, remained subdued as reflected by the loans to deposits ratio of 36.60%.

1.7. The deposit base for the banking sector is dominated by demand and FCA deposits, which accounted for 59.15% and 31.82% of the total non-bank deposits.

1.8. The quality of the banking sector loan portfolio continued to improve, reflected by the decline in the non-performing loans (NPLs) to total loans, from 3.95% as at 30 June 2019 to 1.75% as at 31 December 2019.

1.9. The improvement in the NPLs ratio was mainly driven by an increase in total banking sector loans and advances as well as a decrease in the level of non-performing loans, during the period under review.

1.10. During the period under review, all banking institutions were profitable, with aggregate profit of $6.41 billion for year ended 31 December 2019, up from $389.85 million for the period ended 31 December 2018. The growth in net income was largely attributed to revaluation of foreign currency denominated assets and investment properties.

1.11. The average prudential liquidity ratio as at 31 December 2019 was 72.42% compared to 76.54% as at 30 September 2019. One (1) banking institution was non-compliant with the minimum prudential liquidity ratio of 30%.

2. ARCHITECTURE OF THE BANKING SECTOR

2.1. As at 31 December 2019, there were 19 banking institutions and 227 other institutions under the supervision of the Reserve Bank, 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**

Type of Institution	**Number**
Other Institutions Under the Supervision of Reserve Bank	
Credit-only-MFIs	218
Deposit-taking MFIs	7
Development Financial Institutions	2
Total Other Institutions	**227**

3. CONDITION AND PERFORMANCE OF THE BANKING SECTOR

3.1. The performance of the banking sector was considered satisfactory for the period ended 31 December 2019, on the back of adequate capitalisation, as well as satisfactory asset quality, earnings performance and liquidity management.

3.2. The trends in key financial soundness indicators since December 2018 are shown in Table 2 below.

Table 2: Financial Soundness Indicators

Key Indicators	Benchmark	Dec-18	June-19	Sep-19	Dec-19
Total Assets	-	$13.98bn	$23.54bn	$40.99bn	$60.63bn
Total Loans & Advances		$4.09bn	$6.17bn	$8.35bn	$12.63bn
Securities & Investments	-	$1.83bn	$5.20bn	$6.82bn	$6.90bn
Net Capital Base	-	$10.32bn	$3.31bn	$5.35bn	$9.75bn
Total Deposits	-	$425.26m	$16.92bn	$21.51bn	$34.50bn
Net Profit	-	4.56%	$929.95m	$2.09bn	$6.41bn
Return on Assets	-	20.61%	5.11%	7.91%	8.99%
Return on Equity	-	30.23%	20.95%	26.85%	31.98%

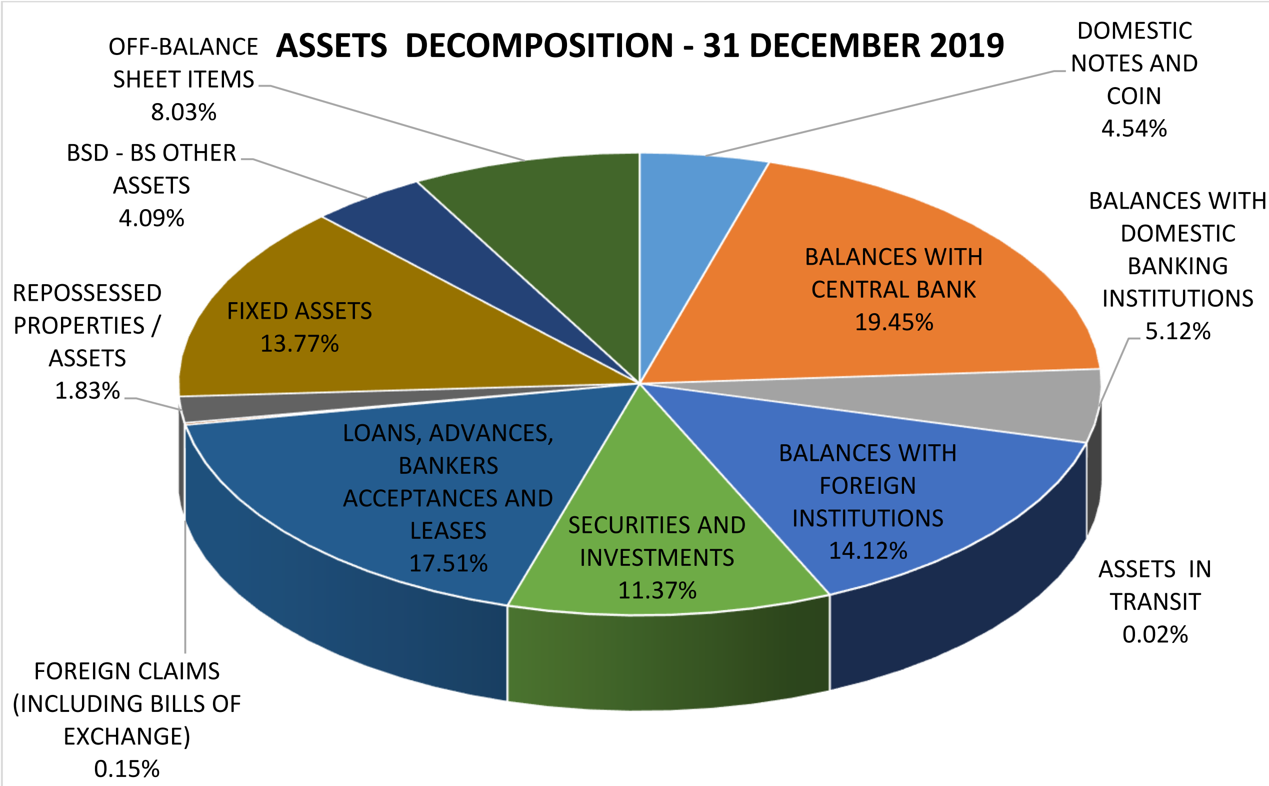
Key Indicators	Benchmark	Dec-18	June-19	Sep-19	Dec-19
Capital Adequacy Ratio	12%	39.62%	32.64%	41.24%	38.09%
Tier 1 Ratio	8%	6.92%	27.24%	27.92%	26.69%
Loans to Deposits	70%	23.84%	36.49%	38.82%	36.60 %
Non-Performing Loans Ratio	5%	67.82%	3.95%	3.23%	1.75 %
Liquidity Ratio	30%	$13.98bn	64.77%	75.59%	72.42%

Composition of Banking Sector Assets…

3.3. Total banking sector assets increased by 47.91%, from $40.99 billion as at 30 September 2019, to $60.63 billion as at 31 December 2019. The growth in banking sector assets was mainly attributable to revaluation of properties and translation of foreign currency denominated loans over the quarter. The ratio of fixed assets, including investment properties, to total assets grew from 8.43% to 13.77% during the period under review

3.4. As at 31 December 2019, total banking sector assets largely comprised balances with the Central Bank (19.45%), loans and advances (17.51%) as well as balances with foreign institutions (14.12%). The structure of banking sector assets, shifted towards balances with the Central Bank, foreign institutions and loans & advances, partly due to the revaluation and translation gains, owing to exchange rate movements. The figure below shows the asset composition as at 31 December 2019:

Figure 1: Asset Mix as at 31 December 2019



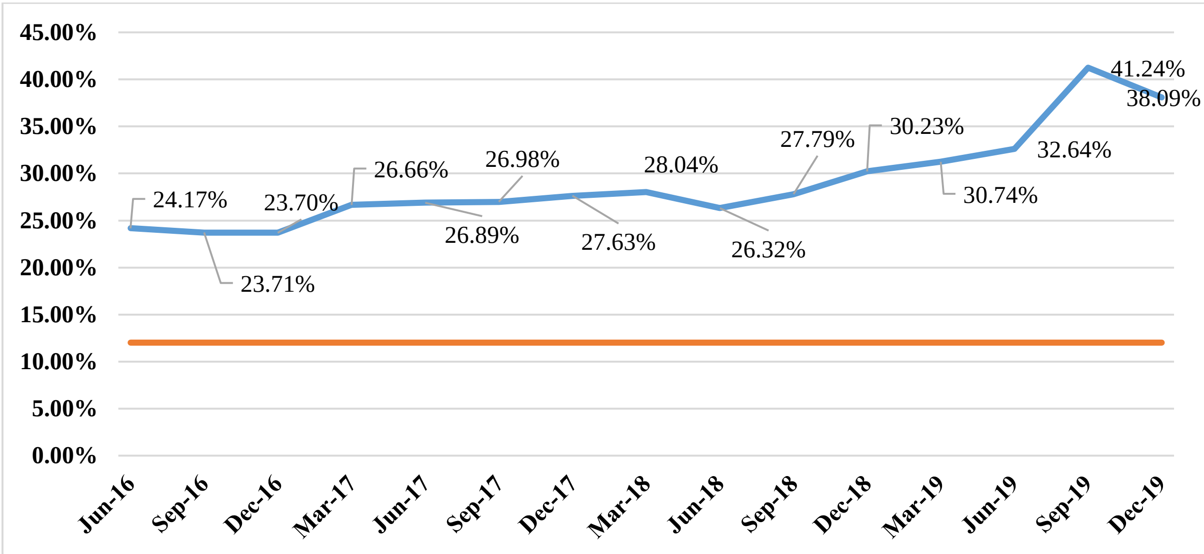
Capitalisation…

3.5. As at 31 December 2019, the banking sector was adequately capitalised, with average capital adequacy and tier 1 ratios of 38.09% and 26.69%, respectively, which complied with the regulatory minima of 12% and 8%.

3.6. All banking institutions complied with the minimum regulatory capital adequacy and tier 1 ratios.

3.7. The banking industry's average capital adequacy ratios from June 2016 to December 2019 are shown in the figure below:

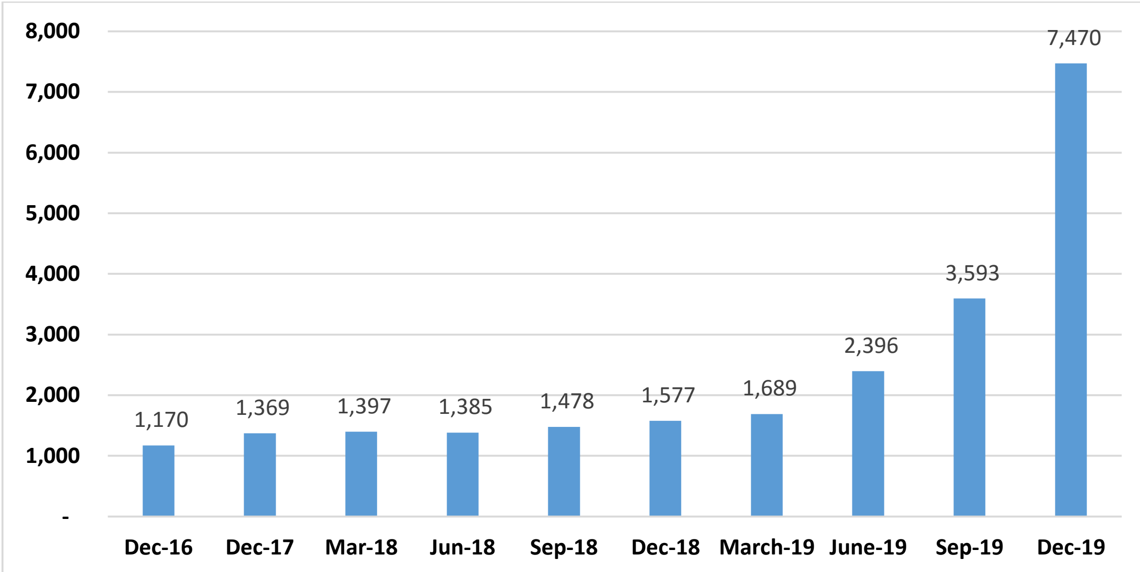
Figure 2: Capital Adequacy Ratios Trend



3.8. There has been an upward trend in the industry capital adequacy ratios, as core capital increased due to improved profitability by banking institutions over the period which largely accrued from foreign currency revaluation gains and revaluation reserves.

3.9. Aggregate core capital increased by 110.86% from $3.59 billion reported as at 30 September to $7.57 billion as at 31 December 2019. The graph below shows the trend in the banking sector core capital levels for the period December 2014 to December 2019.

Figure 3: Core Capital Trends 2016 to December 2019 ($million)



3.10. Banking institutions are working towards meeting the minimum capital requirements effective 31 December 2020 of equivalent to USD30 million

Asset Quality...

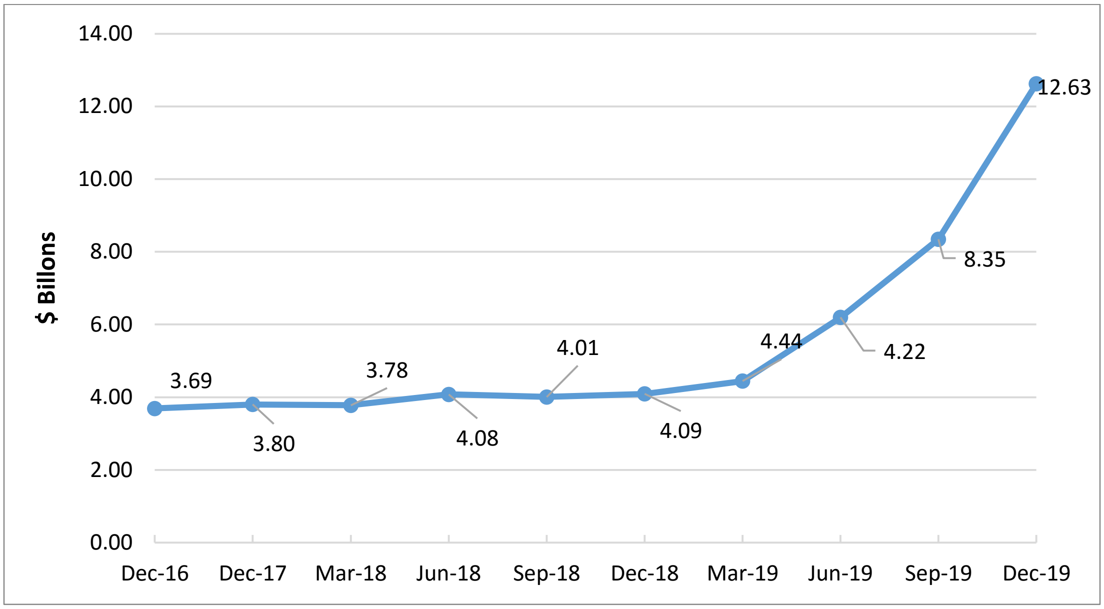
3.11. Total banking sector loans and advances increased by 47.91% from $40.99 billion as at 30 September 2019, to $60.63 billion as at 31 December 2019.

3.12. The growth in loan balances during the quarter was driven by the effect of translation of foreign currency denominated loans.

3.13. The loans to deposits ratio has remained low at 36.60% as at 31 December 2019, reflective of subdued financial intermediation due to challenges in the macroeconomic environment and foreign currency shortages.

3.14. The trend of banking sector loans and advances from 31 December 2016 to 30 December 2019 is shown in the figure below:

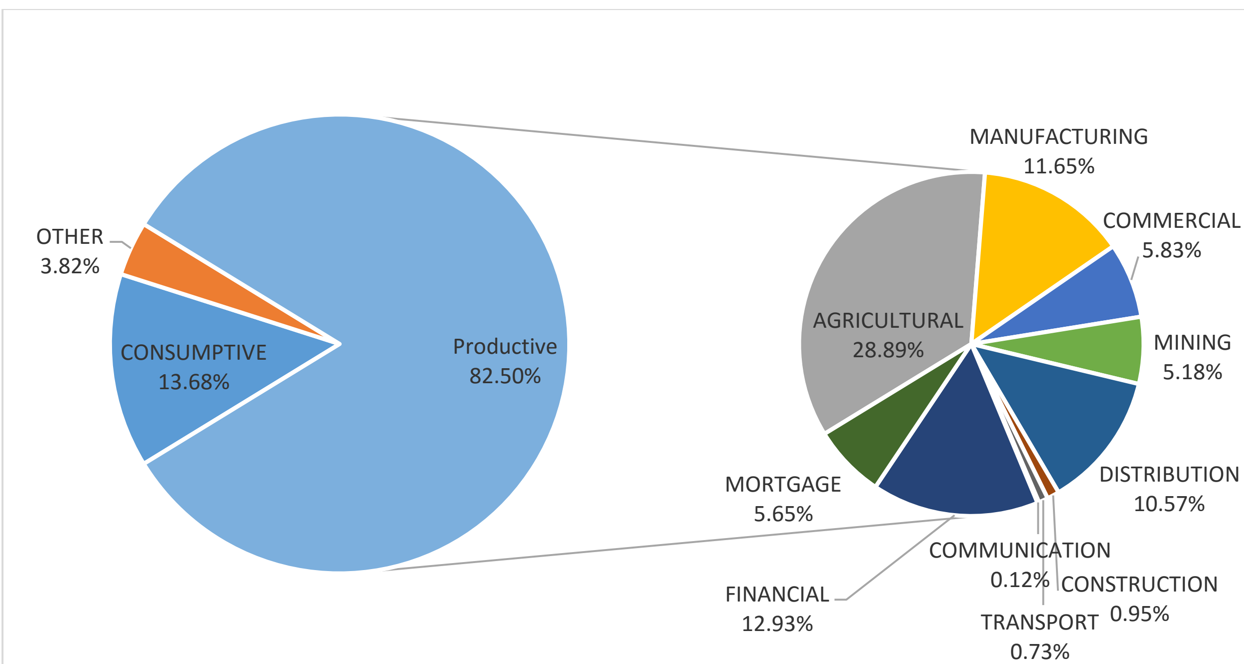
Figure 4: Banking Sector Loans & Advances ($ billions)



Distribution of Loans and Advances…

3.15. Productive sector loans accounted for 82.50% of total sector loans as at 31 December 2019 as shown in the figure below.

Figure 5: Sectoral Distribution of Loans as at 31 December 2019



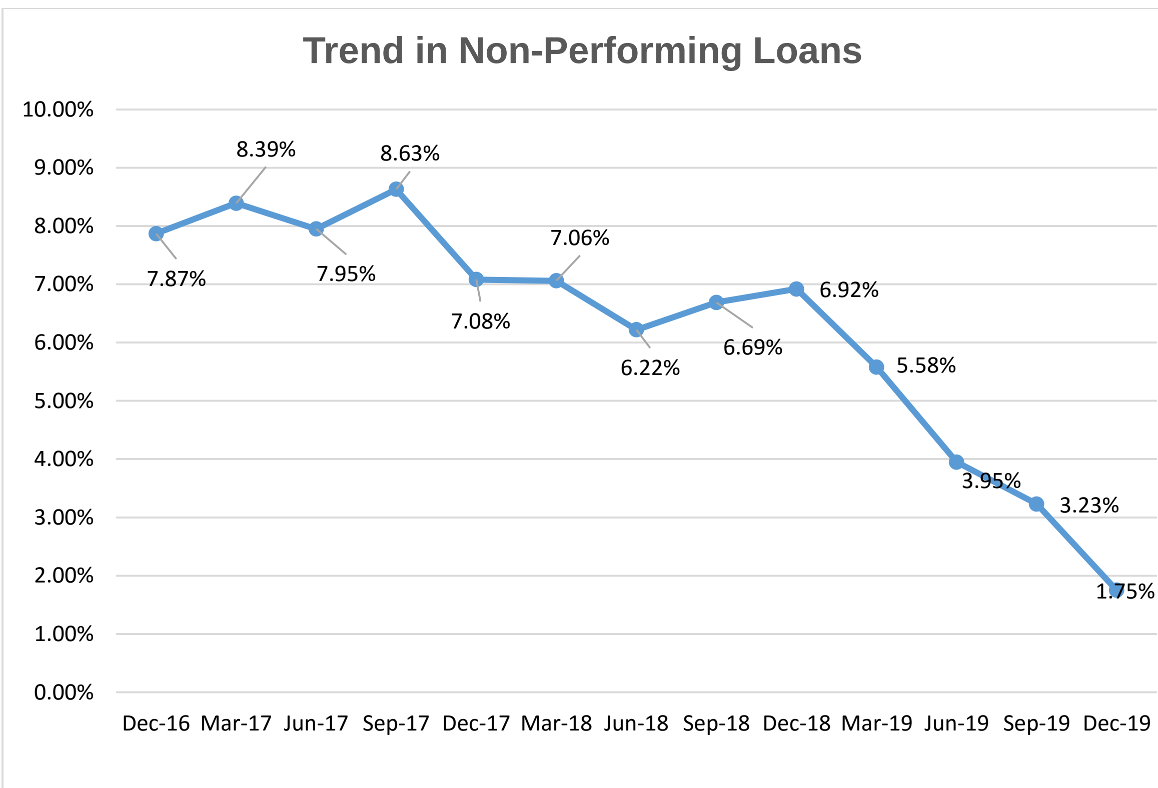
Non-Performing Loans

3.16. The ratio of non-performing loans (NPLs) to total loans improved from 3.23% as at 30 September 2019 to 1.75% as at 31 December 2019 reflecting an improvement in the quality of the banking sector loan portfolio.

3.17. The improvement in the NPLs ratio during the quarter under review was largely a result of a combination of 66.11% increase in total loans and advances and a decrease in the level of non-performing loans which declined from $269.59 million to $221.62 million.

3.18. The trend in the level of non-performing loans to total loans ratio from December 2016 to December 2019 is shown in the figure below.

Figure 6: Trend in Non-Performing Loans Dec 2016 – Dec 2019



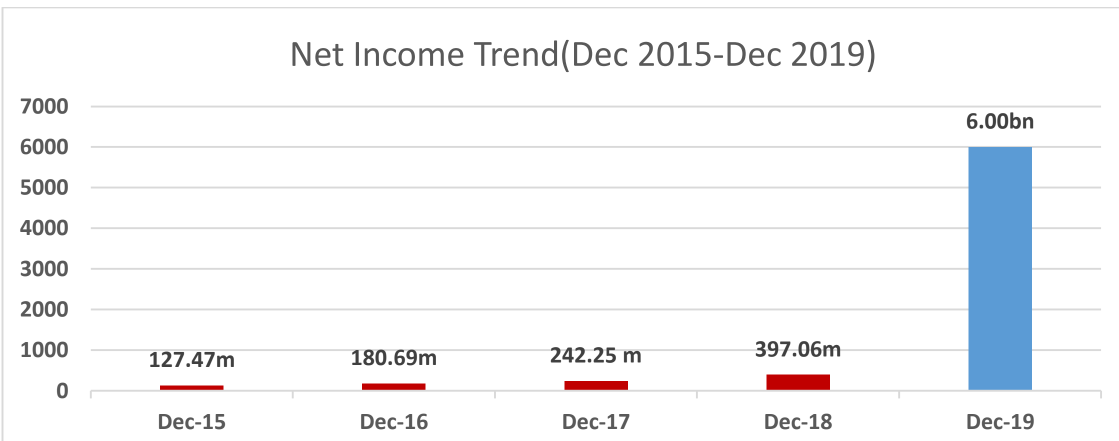
Earnings Performance…

3.19. All banking institutions were profitable during the period under review.

3.20. Aggregate banking sector net income for the year ended 31 December 2019 amounted to $6.41 billion, representing 187.08% increase from $2.09 billion reported for the corresponding period in 2018. Net income growth was mainly driven by translation gains on foreign currency denominated assets and investment properties.

3.21. The figure below shows the trend in net income from December 2016 to December 2019.

Figure 7: Net Income Trend ($ millions)

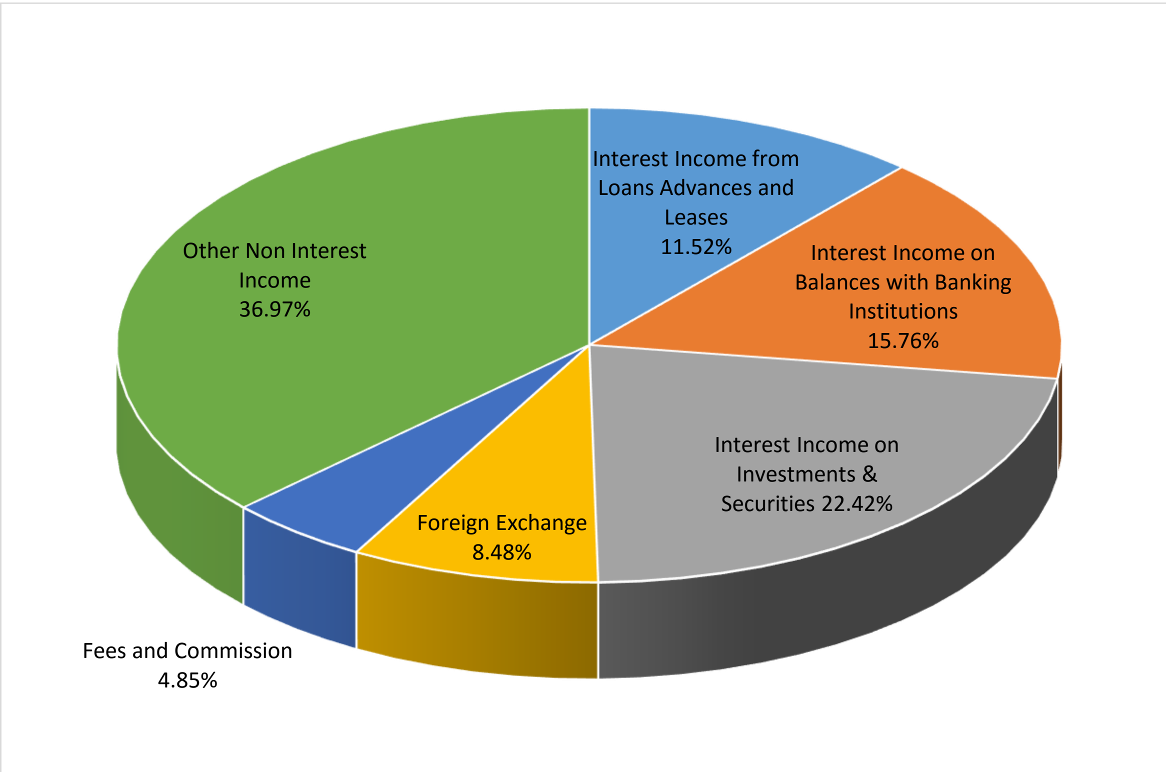


3.22. The income mix in the banking sector continue to be skewed towards non-funded income as supported by high non-interest income recorded in the year ended 31 December 2019. Non-interest income was largely attributed to increased digital transactional volumes, as most banks upheld strategies of realigning their business models in recognition of the migration by customers to digital platforms. Further, a significant portion of the income was also attributed to gains from revaluation of other assets.

3.23. There has been a declining trend in interest income from loans and advances which accounted for 27% of total income in December 2019, compared to 50.34% in December 2018.

3.24. The banking sector income mix is shown in the pie chart below.

Figure 8: Banking Sector Income Mix as at 31 December 2019



3.25. Banking sector earnings performance, as measured by the average return on assets declined from 20.61% to 8.99% and average return on equity ratios improved from 30.23% to 31.98% as at 31 December 2019.

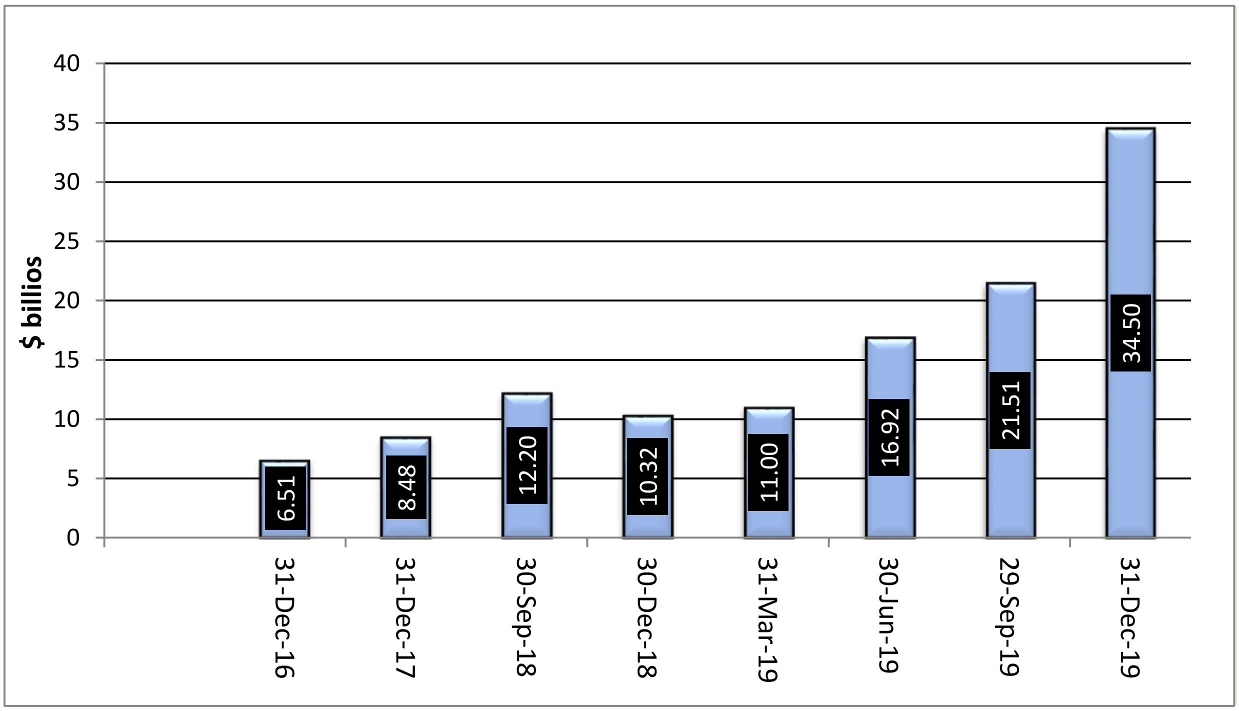
Liquidity and Funds Management...

3.26. During the quarter under review, total banking sector deposits increased by 60.39% from $21.51 billion as at 30 September 2019 to $34.50 billion as at

31 December 2019. The increase in the deposit base is mainly attributable to the revaluation of foreign currency denominated deposits following the introduction of a floating exchange rate in February 2019.

3.27. The trend of banking sector deposits over the period 31 December 2016 to 31 December 2019 is shown in the Figure 10.

Figure 10: Trend of Banking Sector Deposits ($ billions)

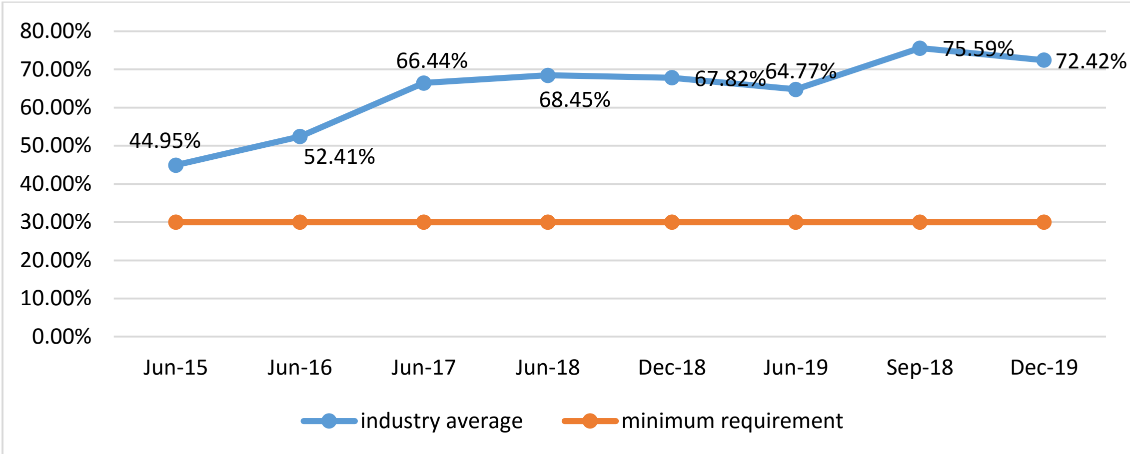


3.28. As at 31 December 2019, the average prudential liquidity ratio declined from 75.59 % as at September 2019 to 72.42% to December 2019.

3.29. One (1) banking institution was non-compliant with the minimum prudential liquidity ratio of 30%. The institution is implementing measures to address non-compliance, while the Reserve Bank continues to monitor the institution to ensure compliance with the regulatory minimum.

3.30. The trend in the banking sector average prudential liquidity ratio since June 2015 is shown in the figure 12 below.

Figure 11: Prudential Liquidity Ratio Trend (%)



3.31. The persistently high prudential liquidity ratio has been reflective of a selective approach to lending by banking institutions on the back of high inherent credit risk and preference for securities and investments.

Sensitivity to Market Risk…

3.32. As at 31 December 2019, the banking sector had an overall asset sensitive book with positive cumulative re-pricing gaps in all time bands implying that most banks will gain if market interest rates remain on an upward trajectory.

3.33. In the year ended 31 December 2019, all banking institutions were resilient to a shock of 15 percentage increase in interest rates, as their capital adequacy ratios would remain above the prescribed minimum of 12%.

3.34. As at 31 December 2019, the overall banking sector's net forex open position was a positive $137.31 million. This is due to banks reducing their foreign currency exposures given the continued depreciation of the local currency.

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