QUARTERLY BANKING SECTOR REPORT

31 MARCH 2017

BANK SUPERVISION DIVISION

1. EXECUTIVE SUMMARY

1.1. The banking sector remained generally stable and performed satisfactorily for the quarter ended 31 March 2017.

1.2. As at 31 March 2017, all operating banking institutions were in compliance with the prescribed minimum capital requirements and had an aggregate core capital of $1.22 billion. The aggregate core capital represents a 6.09% increase from $1.15 billion recorded as at 31 December 2016, largely attributable to satisfactory earnings performance. Banking institutions made progress towards compliance with 2020 minimum capital requirements.

1.3. Sixteen out of 19 operating banking institutions recorded profits during the quarter ended 31 March 2017. The banking sector aggregate net profit was **$50.34 million** for the quarter ended 31 March 2017, representing an increase of 30.58%, from $38.55 million reported in corresponding quarter in 2016. The increase in profitability was largely driven by cost containment measures and increases in non-funded income due to the increased use of plastic money on the back of general cash shortages on the market.

1.4. As at 31 March 2017, aggregate banking sector deposits amounted to $**6.55 billion,** representing a 0.61% increase from $6.51 billion reported as at 31 December 2016. Total banking sector loans and advances amounted to $3.59 billion, translating into a loans to deposit ratio of 54.82%.

1.5. Credit risk in the banking sector marginally deteriorated from 7.87% as at 31 December 2016 to **8.39%** as at 31 March 2017 as a result of a decline in the total loans while NPLs remained stable. The improvement in the credit infrastructure through the establishment of the Credit Registry is expected to result in a further reduction in the levels of banking sector non-performing loans.

1.6. The sector's prudential liquidity ratio was high at **60.20%** as at 31 March 2017, against a regulatory minimum of 30%, largely as a result of a cautious approach to lending adopted by banking institutions.

1.7. The various policy measures put in place by the Reserve Bank to promote the usage of electronic payments have assisted in reducing the demand for cash. Further, banking institutions continue increasing their focus on serving previously unserved and underserved segments in line with the financial inclusion drive.

2. ARCHITECTURE OF THE BANKING SECTOR

2.1. As at 31 March 2017, the banking sector was comprised as shown in the table below.

Architecture of the Banking Sector

Type of Institution	**Number**
Commercial Banks	13
Building Societies	5
Savings Bank	1
Total Banking Institutions	**19**
Other institutions supervised by the Reserve Bank	
Credit-only-MFIs	179
Deposit-taking MFIs	4
Development Institutions - SMEDCO and IDBZ	2

3. CONDITION AND PERFORMANCE OF THE BANKING SECTOR

3.1. The financial condition of the banking sector was considered satisfactory as at 31 March 2017 on account of adequate capitalization, satisfactory earnings performance, satisfactory asset quality and high liquidity ratio.

3.2. The following table summarises the financial soundness indicators of the banking sector as at 31 March 2017:

Financial Soundness Indicators

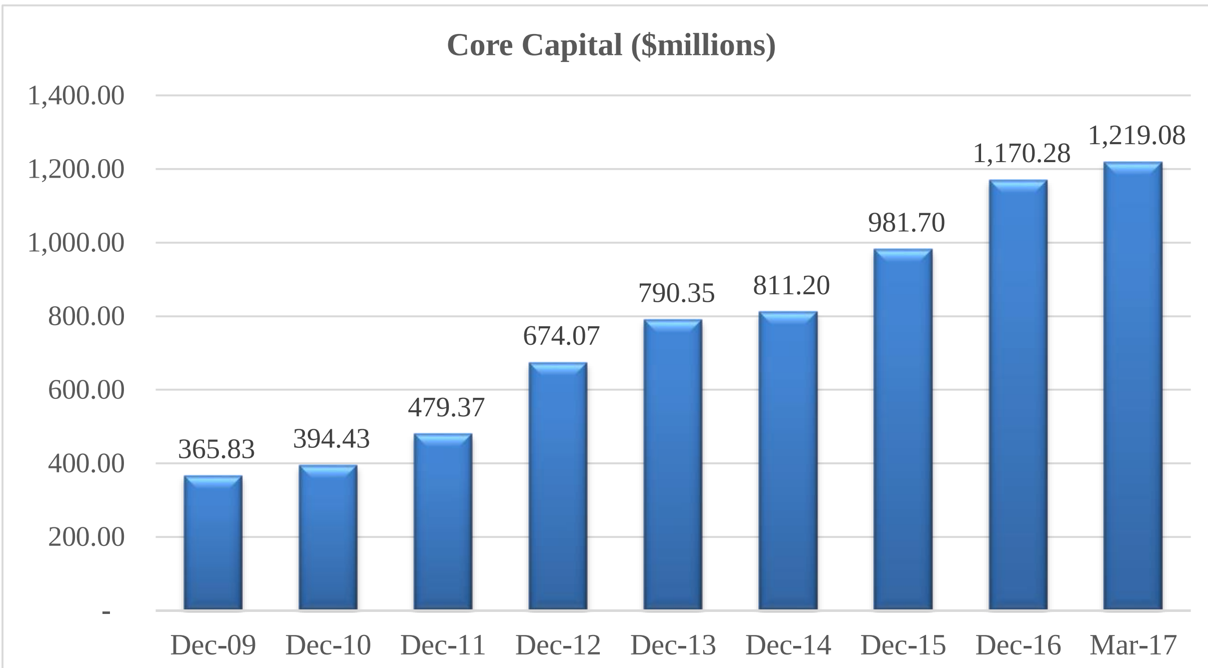
Key Indicators	Benchmark	Mar-2016	Jun-16	Sep-16	Dec-16	Mar-17
Total Assets	-	$7.79bn	$8.01bn	$8.25bn	$8.73bn	$8.88bn
Total Loans	-	$3.81bn	$3.73bn	$3.65bn	$3.69bn	$3.59bn
Net Capital Base	-	$1.16bn	$1.22bn	$1.24bn	$1.34bn	$1.37bn
Core Capital		$0.98bn	$1.04bn	$1.07bn	$1.17bn	$1.22bn
Total Deposits	-	$5.67bn	$5.91bn	$6.14bn	$6.51bn	$6.55bn
Net Profit	-	$38.55m	$67.97m	$111.78m	$181.06m	$50.34m
Return on Assets	-	0.50%	0.98%	1.57%	2.26%	0.69%
Return on Equity	-	3.29%	3.53%	8.94%	12.64%	3.65%
Capital Adequacy Ratio	12%	22.34%	23.45%	23.71%	23.70%	26.66%
Loans to Deposits	70%	67.17%	63.08%	59.45%	56.64%	54.82%
Non-Performing Loans Ratio	5%	10.81%	10.05%	10.74%	7.87%	8.39%
Provisions to Adversely Classified Loans	-	77.36%	69.87%	68.05%	68.51%	65.86%
Net Interest Margin	-	2.03%	3.52%	5.53%	6.99%	1.80%
Liquidity Ratio	30%	49.63%	52.47%	54.15%	61.91%	60.20%
Cost to Income Ratio		84.67%	84.23%	82.75%	79.20%	76.58%

Capital Adequacy…

3.3. As at 31 March 2017, all operating banking institutions were in compliance with the prescribed minimum capital requirements.

3.4. The banking sector's aggregate core capital increased by 6.09%, from $1.17 billion to $**1.22 billion** during the quarter ended 31 March 2017, while the net capital base also increased from $1.34 billion to **$1.37 billion** during the quarter under review.

3.5. The graph below shows banking sector core capital trends from 2009 to March 2017:



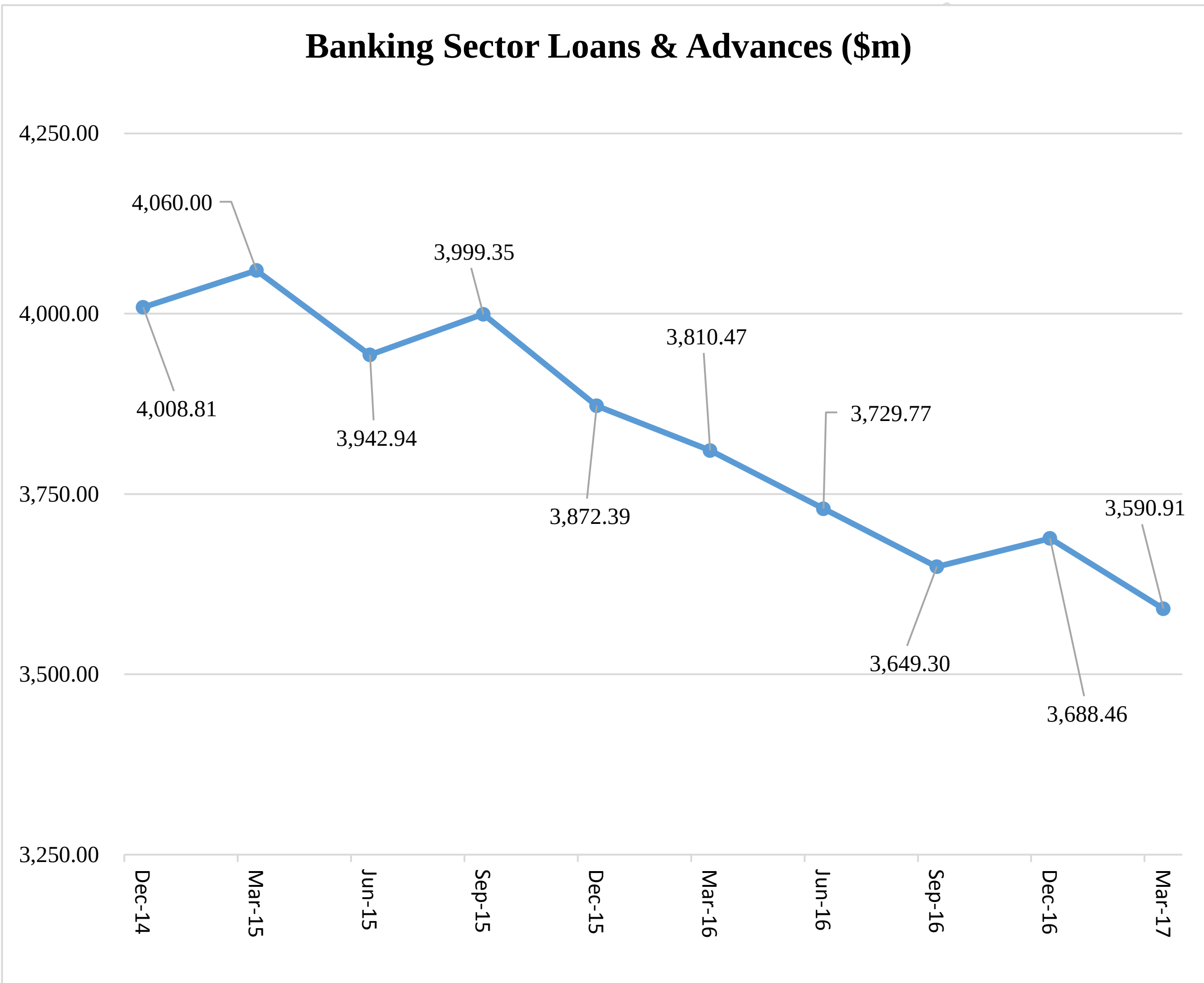
3.6. The banking sector average capital adequacy ratio was 26.66% as at 31 March 2017, which is well above the regulatory threshold of 12%. All banks complied with the minimum required capital adequacy and tier 1 ratios of 12% and 8%, respectively.

3.7. Tier 1 capital constituted 89.07% of the banking sector's net capital base of $1.37 billion as at 31 March 2017, reflecting high quality capital held by the sector.

3.8. The Reserve Bank is monitoring implementation of the banking institutions' capital plans and progress towards compliance with the 2020 minimum capital requirements, on an on-going basis.

Asset Quality…

3.9. Total banking sector loans and advances marginally decreased from **$3.69 billion** reported as at 31 December 2016, to **$3.59 billion** as at 31 March 2017. The graph below shows the trend of banking sector loans and advances from 31 December 2014 to 31 March 2017.



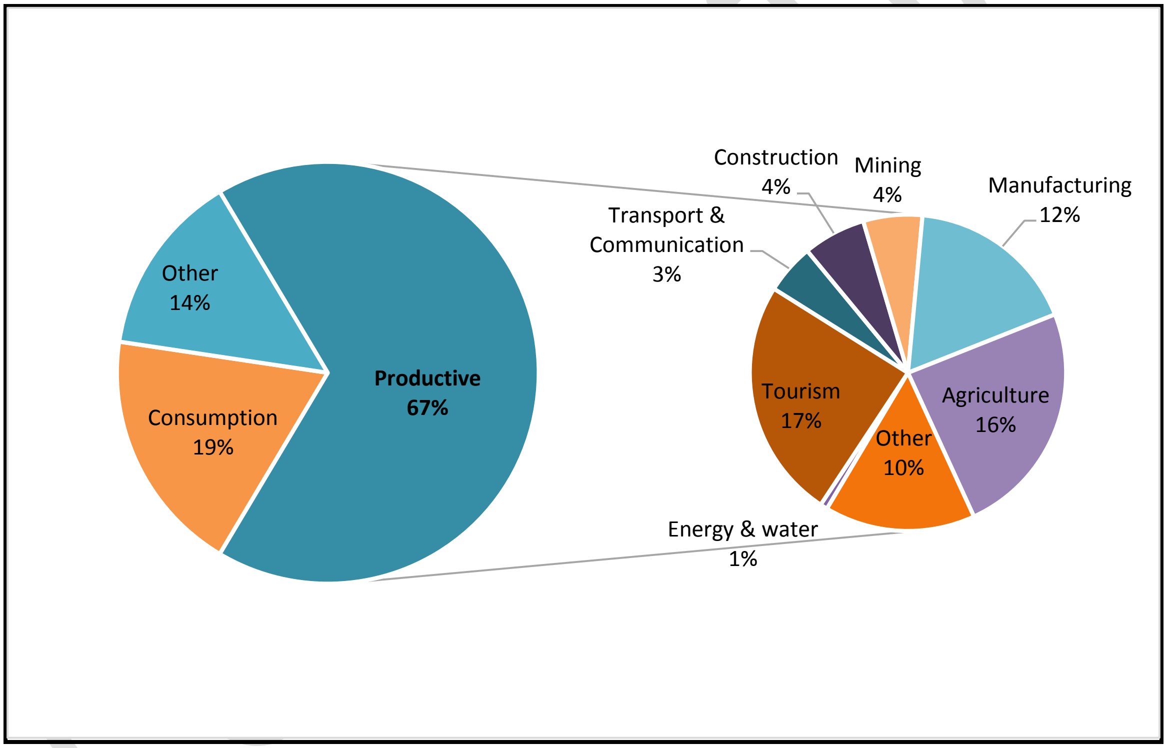
3.10. The banking sector loans have generally been on a downward trend since September 2015, largely as a result of reduction in lending by most banking institutions due to perceived high credit risk. However, a number of measures currently underway, including reduction in lending rates, facilities for cross border traders, increase in the gold support facility and facilities to support financial inclusion, among others, are envisaged to spur banking sector lending.

Distribution of Loans and Advances…

3.11. As at 31 March 2017, lending to the productive sectors accounted for 67% of total loans. Loans to tourism, agriculture and manufacturing sectors dominated the distribution of productive loans as at 31 March 2017.

3.12. The distribution of credit as at 31 March 2017 is indicated in the figure below.

Distribution of Credit as at 31 March 2017



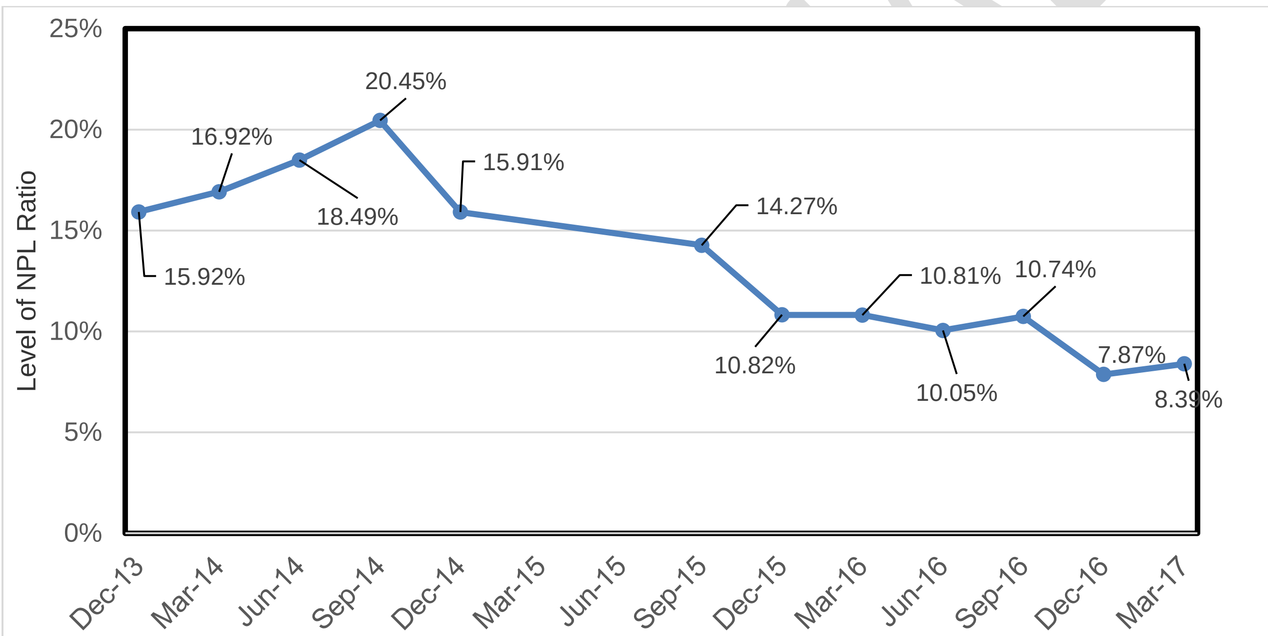
3.13. The reduction in lending rates for the productive sector, including mortgages, to 12% per annum, effective 1 April 2017 is expected to spur economic growth in the medium to long-term.

Non-Performing Loans…

3.14. There has been a general improvement in the banking sector NPL ratio over the past years, from a peak of 20.45% as at 30 September 2014 to 8.39%, as at 31 March 2017. The ratio, however, marginally deteriorated from 7.87% as at 31 December 2016. The deterioration is largely attributable to a disproportionate reduction in total loans and advances compared to increase in NPLs.

3.15. The figure below shows the trend in NPLs from 31 December 2013 to 31 March 2017.

Non-Performing Loans Trend



3.16. The level of NPLs is, however, expected to return to the downward trend in response to a number of holistic NPL resolution policy measures by the Reserve Bank, including operationalization of the credit reference system. The sustainable reduction in NPLs is expected to strengthen banks' balance sheets and position them to meaningfully contribute to the revival of the economy.

3.17. The Reserve Bank continues to monitor the NPL trends and the effectiveness of banks' credit risk management practices.

Earnings Performance...

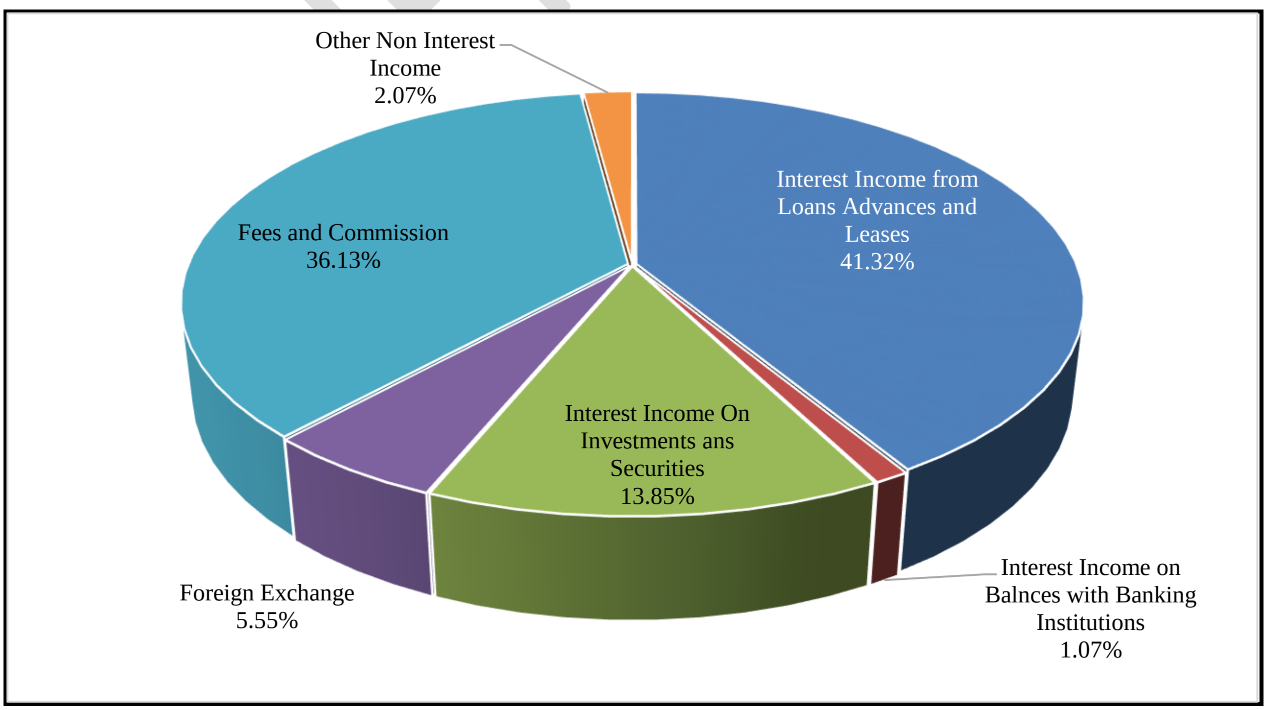
3.18. The banking sector earning performance was satisfactory during the quarter ended 31 March 2017. The sector reported an aggregate net profit of **$50.34 million,** representing an increase of 30.58% from $38.55 million in corresponding quarter in 2016.

3.19. Sixteen out of 19 operating banking institutions recorded profits during the quarter ended 31 March 2017. The loss making institutions are employing various turnaround strategies to return to profitability including cost cutting measures and increasing business volumes among others.

3.20. The average return on assets and return on equity improved from 0.50% and 3.29% as at 31 March 2016 to 0.69% and 3.69% as at 31 March 2017, respectively.

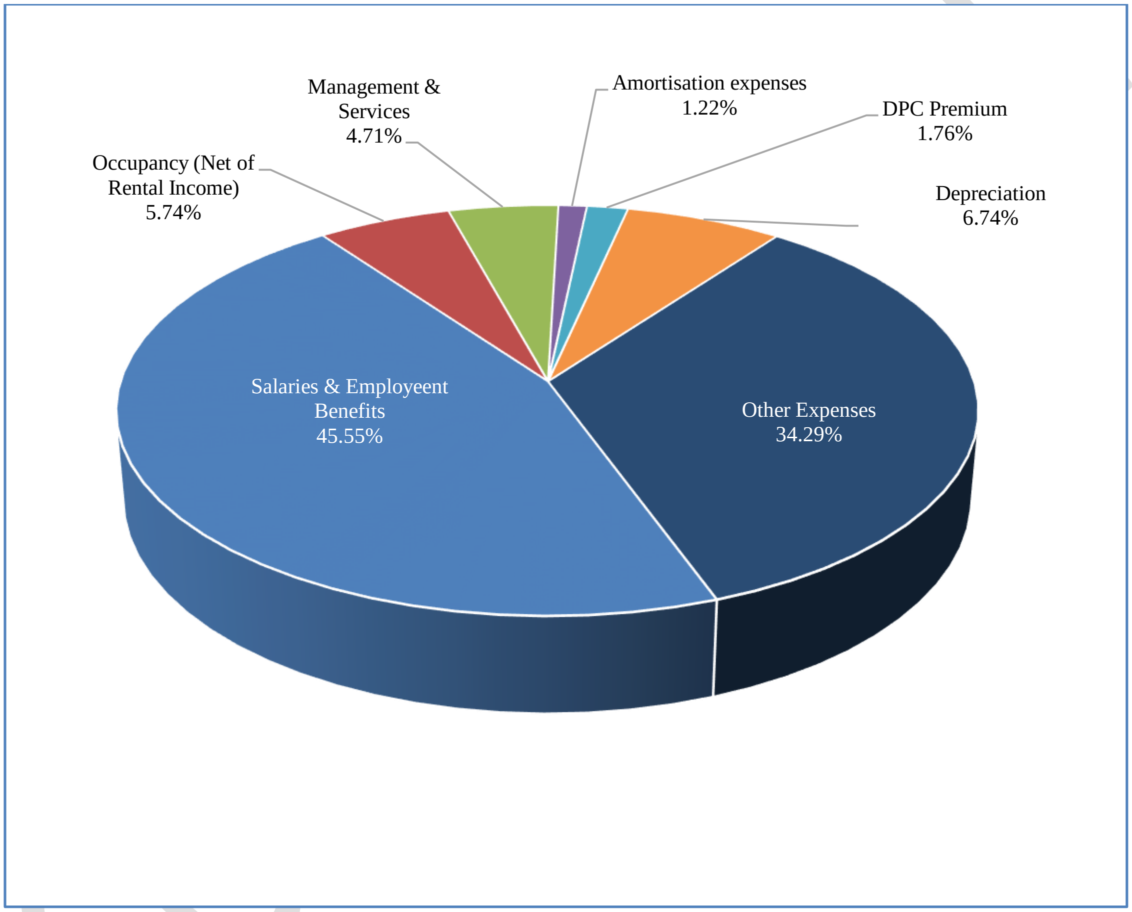
3.21. Interest income continued to be the major income driver, constituting 56.24% of total income amounting to $0.26 billion for the quarter ended 31 March 2017. The sources of income for the banking sector as at 31 March 2017 are shown in the chart below.

Banking Sector Income Mix as at 31 March 2017



3.22. As at 31 March 2017, salaries & employment benefits continued to dominate total operating costs for banking institutions as they accounted for 45.55% of total banking sector operating expenses as shown in the figure below.

Banking Sector Operating Expense Mix as at 31 March 2017



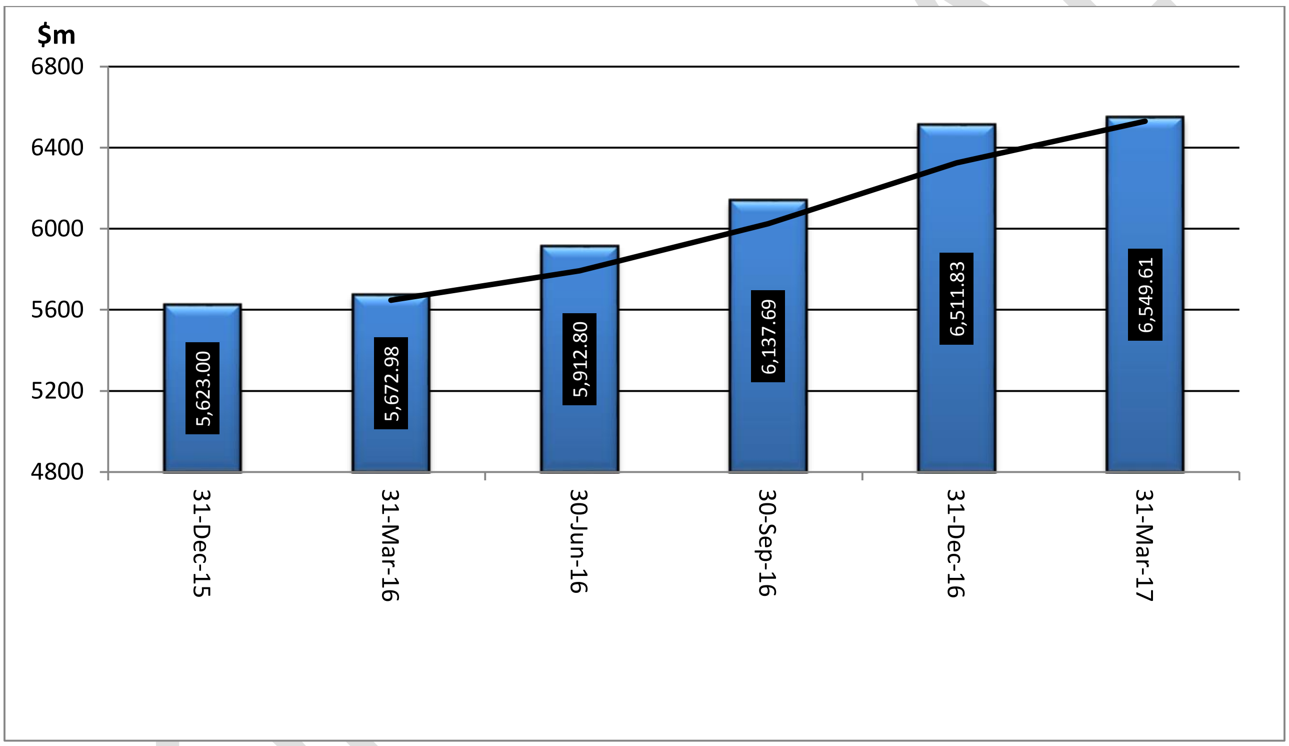
3.23. As part of measures to improve their earnings capacity and efficiency, banking institutions continue to implement a number of measures, which include adoption of electronic platforms and alternative delivery channels such as agency banking model.

Liquidity and Funds Management...

3.24. The aggregate banking sector deposits increased by 0.61%, from $6.51 billion as at 31 December 2016 to **$6.55 billion** as at 31 March 2017.

3.25. The figure below shows the trend of banking sector deposits over the period 31 December 2015 to 31 March 2017.

Trend of Banking Sector Deposits

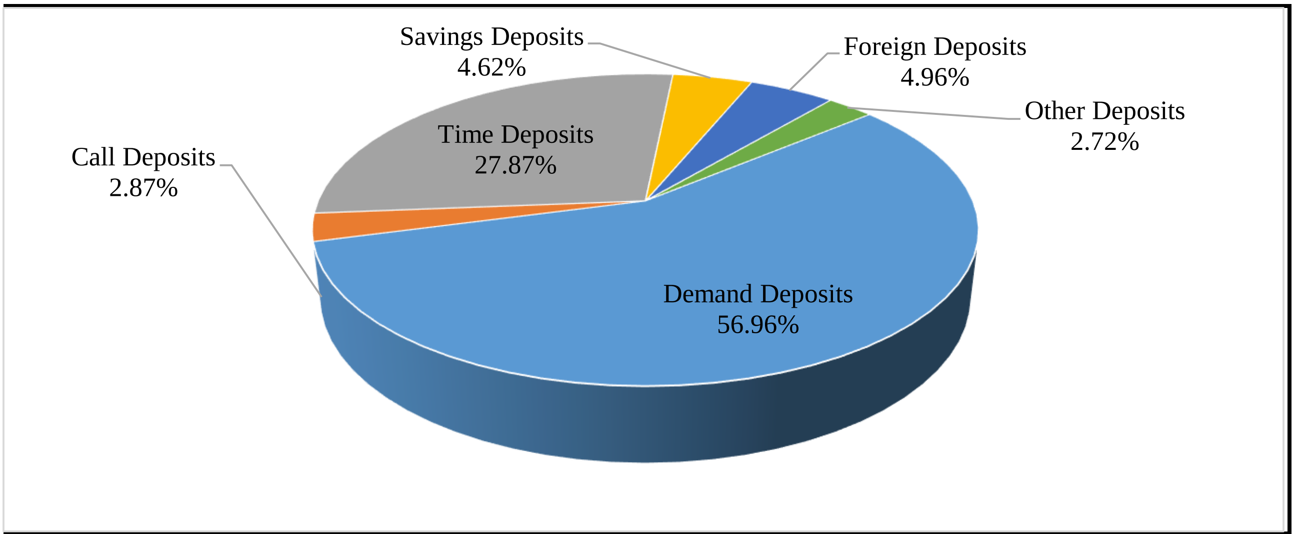


3.26. The commercial banking sub-sector accounted for 83% of total banking sector deposits and 74.16% of total banking sector loans as at 31 March 2017.

3.27. Banking sector deposits were dominated by demand and time deposits, which accounted for 56.96% and 27.87% of total deposits, respectively, as at 31 March 2017.

3.28. The composition of total banking sector deposits as at 31 March 2017 is depicted in the figure below.

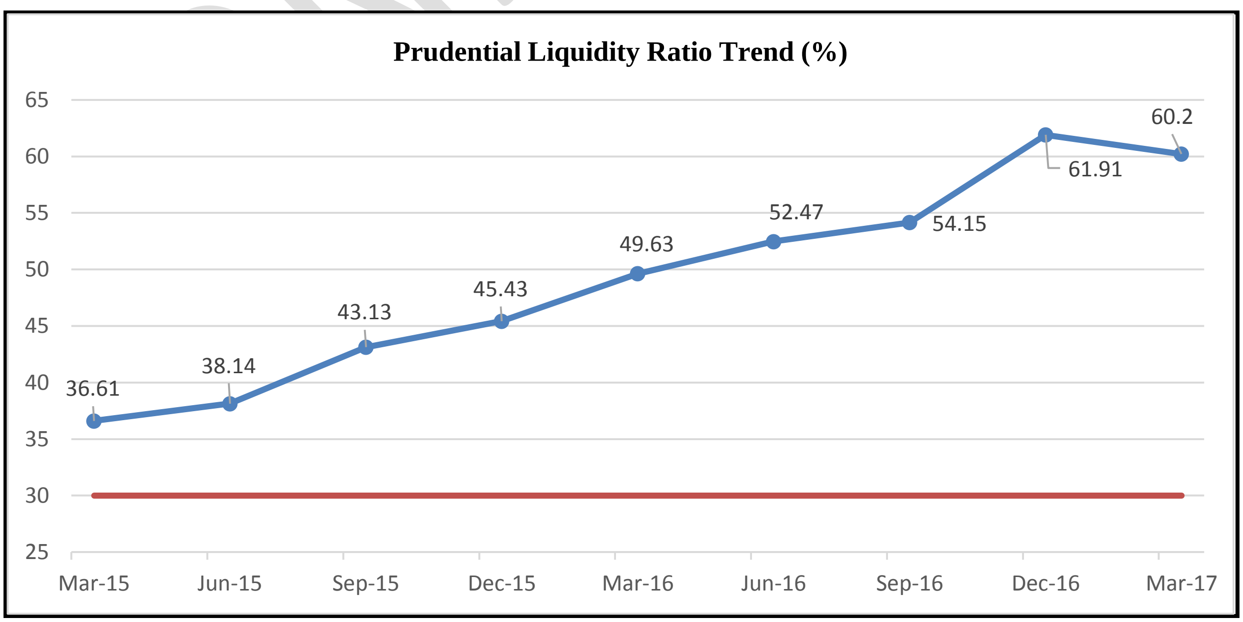
Banking Sector Deposit Mix as at 31 March 2017



3.29. The banking sector prudential liquidity ratio was high at 60.20% as at 31 March 2017, against regulatory minimum of 30%, as banking institutions adopted a cautious approach to lending during the period under review.

3.30. The trend in the banking sector average prudential liquidity ratio since 31 March 2015 is shown in the figure below.

Trend of the Prudential Liquidity Ratio (31 March 2015 – 31 March 2017)



3.31. Notwithstanding the high prudential liquidity ratios recorded across the sector, the banking industry continued to experience underlying cash challenges on the back of continued high demand for cash by the banking public.

3.32. The Reserve Bank will continue to implement measures aimed at addressing the cash challenges and these measures include encouraging the banking public to embrace alternative payment platforms, in particular the use of plastic money.

Sensitivity to Market Risk…

3.33. Generally, the sector's exposure to market risk remained low and the sector's exposure to interest rate risk was mainly in the banking book.

3.34. Aggregate stress test results reflect strong resilience to market risk shocks for the banking system as a whole.

3.35. Inherent foreign exchange rate risk remained low given banks' current balance sheet structures. Banks are not undertaking proprietary trading positions, while client transactions are mainly currency switches. The banking sector had an overall positive net foreign exchange open position of **$1.68 billion** as at 31 March 2017, an increase from $1.47 billion as at 31 December 2016.

3.36. Stress tests conducted to assess the vulnerability of banking institutions' to foreign exchange rate movements showed that only one (1) banking institution is susceptible to a major level foreign exchange rate risk shock of a 15% appreciation of the US dollar against major currencies.

31 March 2017