QUARTERLY BANKING SECTOR REPORT

31 MARCH 2016

BANK SUPERVISION DIVISION

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1. EXECUTIVE SUMMARY

1.1. The banking sector remained generally sound and performed satisfactorily for the quarter ended 31 March 2016.

1.2. All operating banking institutions were in compliance with the prescribed minimum capital requirements and institutions have made progress towards compliance with 2020 minimum capital requirements. As at 31 March 2016, the sector's aggregate net capital amounted to $1.16 billion, while aggregate tier 1 capital was $976.10 million.

1.3. Aggregate net profit increased to $38.44 million for the quarter ended 31 March 2016 from $4.02 million reported for the same period in 2015. The growth in net aggregate profit was mainly driven by lower loan loss provisions in line with improving asset quality at some institutions and realignment of cost structures.

1.4. As at 31 March 2016, total banking sector deposits and loans amounted to $5.67 billion and $3.81 billion, respectively, translating to a loans to deposits ratio of 67.19%.

1.5. Credit risk in the banking sector continues on an improving trend as reflected by a non-performing loans ratio of 10.81% as at 31 March 2016. The disposal of non-performing loans to ZAMCO and the concomitant adoption of enhanced credit risk management standards contributed significantly to the stabilisation of credit risk in the sector.

1.6. The banking sector's average prudential liquidity ratio of 49.63% as at 31 March 2016 was compliant with the minimum prudential liquidity ratio of 30%. Some banks, however, experienced cash constraints during the quarter largely driven by the macro-liquidity challenges in the economy.

2. ARCHITECTURE OF THE BANKING SECTOR

2.1. As at 31 March 2016, the composition of the banking sector was as shown in the table below.

Architecture of the Banking Sector

Type of Institution	Number
Commercial Banks	13
Building Societies	4
Savings Bank	1
Total Banking Institutions	**18**
Other institutions supervised by the Reserve Bank	
Credit-only-MFIs	160
Deposit-taking MFIs	2
Development Institutions - SMEDCO and IDBZ	2

2.2. Following the licensing of National Building Society Limited (NBS) in 2015, the Reserve Bank conducted a pre-opening inspection of the society to assess its preparedness to commence building society business. The pre-opening inspection established that NBS had largely complied with the minimum requirements and the society was granted authority to commence operations on 27 April 2016.

2.3. Collarhedge Finance (Private) Limited, which was granted a deposit taking microfinance licence by the Reserve Bank in 2015 is still finalising administrative and infrastructural facilities for proposed deposit-taking operations.

3. CONDITION AND PERFORMANCE OF THE BANKING SECTOR

3.1. The overall financial condition of the banking sector was considered satisfactory as at 31 March 2016. The following table summarises the financial soundness indicators of the banking sector as at 31 March 2016.

Financial Soundness Indicators

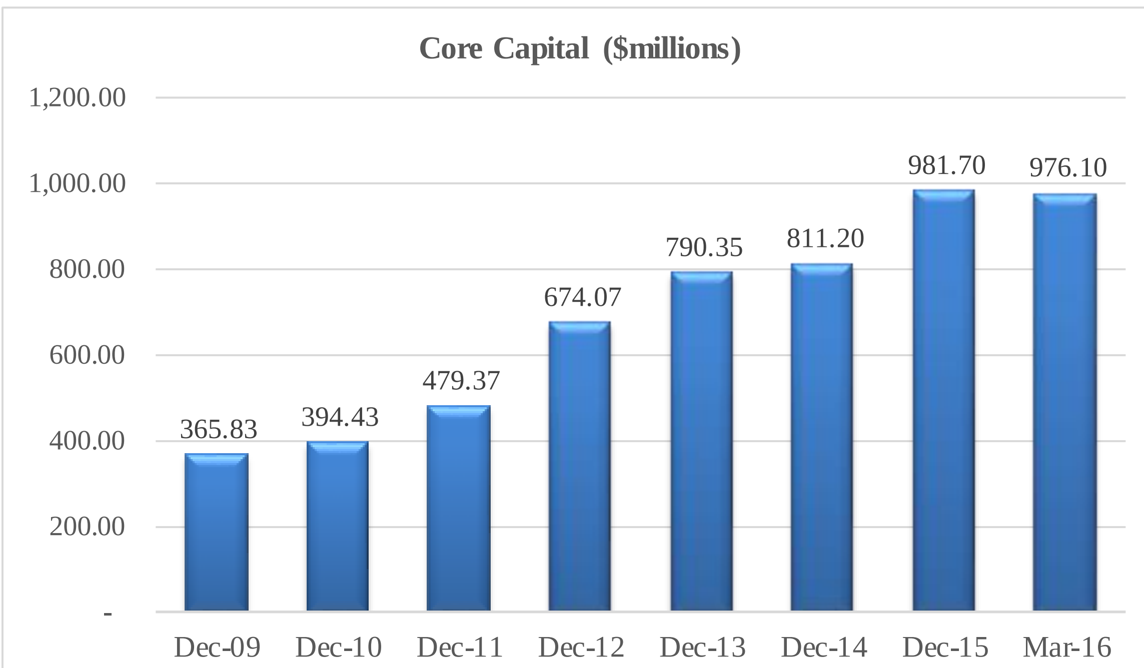
Key Indicators	Dec -09	Dec-10	Dec -11	Dec - 12	Dec – 13	Dec -14	Mar-15	Dec-15	Mar-16
Total Assets	$2.19bn	$3.69bn	$4.74bn	$6.12bn	$6.74bn	$7.12bn	$7.19bn	$7.83bn	**$7.79bn**
Total Loans	$693m	$1.56bn	$2.76bn	$3.56bn	$3.08bn	$4.01bn	$4.06bn	$3.87bn	**$3.81bn**
Net Capital Base	$382m	$458m	$512m	$644m	$706m	$926.6m	$926.3m	$1.14bn	**$1.16bn**
Total Deposits	$ 1.36bn	$ 2.31bn	$ 3.04bn	$4.41bn	$ 4.73bn	$5.08bn	$5.29bn	$5.62bn	**$5.67bn**
Net Profit	$9.50m	$37.95m	$86.00m	$69.20m	$4.46m	$50.84m	$4.02m	$127.47m	**$38.44m**
Return on Assets	0.60%	1.03%	2.43%	1.64%	0.06%	0.92%	0.08%	2.11%	**0.42%**
Return on Equity	2.47%	8.28%	15.13%	9.17%	0.51%	5.37%	0.40%	10.96%	**2.79%**
Capital Adequacy Ratio	27.26%	27.34%	13.51%	13.07%	14.01%	17.33%	17.97%	21.31%	**22.34%**
Loans to Deposits	50.99%	86.25%	90.59%	93.27%	102.36%	78.94%	76.75%	68.86%	**67.19%**
Non-Performing Loans Ratio	1.80%	10.95%	7.55%	13.46%	15.92%	15.91%	15.19%	10.82%	**10.81%**
Provisions to Adversely Classified Loans	112.81%	175.42%	57.53%	207.45%	70.88%	54.72%	61.35%	69.22%	**77.36%**
Net Interest Margin	3.29%	5.75%	8.21%	14.81%	15.26%	4.24%	0.45%	8.62%	**2.03%**
Liquidity Ratio	97.44%	70.88%	56.80%	55.70%	40.57%	39.34%	34.37%	45.35%	**49.63%**
Cost to Income Ratio	94.38%	86.93%	82.17%	86.41%	96.60%	93.72%	97.55%	84.40%	**86.30%**

3.2. An analysis of the financial soundness indicators is detailed hereunder.

Capital Adequacy…

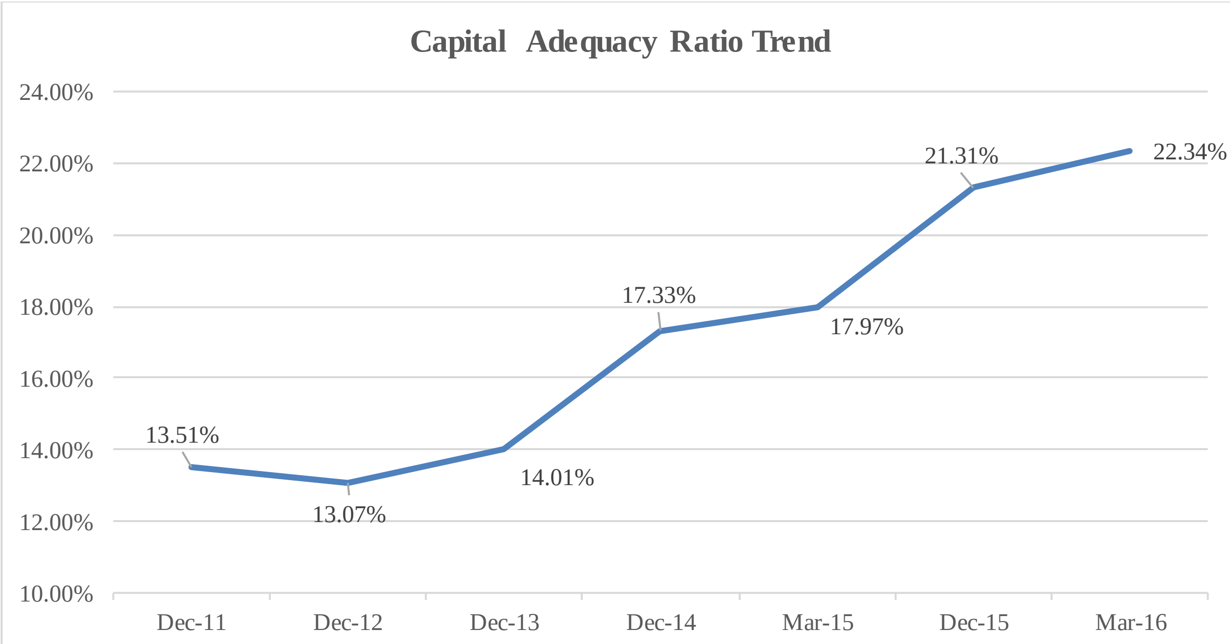
3.3. The banking sector's net capital base increased to $1.16 billion as at 31 March 2016 from $1.14 billion as at 31 December 2015. However, the sector's aggregate core capital base marginally declined by 0.57% from $981.70 million as at 31 December 2015, to $976.1 million as at 31 March 2016. The decrease in the aggregate core capital position was attributed to payment of dividends as well as post-audit adjustments at some banking institutions.

3.4. The graph below shows banking sector core capital trends from 2009 to March 2016:



3.5. The banking industry average capital adequacy ratio was 22.34% as at 31 March 2016, against minimum ratio of 12%, reflecting that the banking sector remained adequately capitalised. All banks complied with the minimum capital adequacy ratio of 12%.

3.6. The trend in the banking industry's average capital adequacy ratios (CARs) from December 2011 to March 2016 is indicated in the figure below.



3.7. Tier 1 capital constituted 84.77% of net capital base as at 31 March 2016 and all banks' tier 1 ratios were in compliance with the regulatory minimum of 8% as well as the prescribed minimum capital requirements.

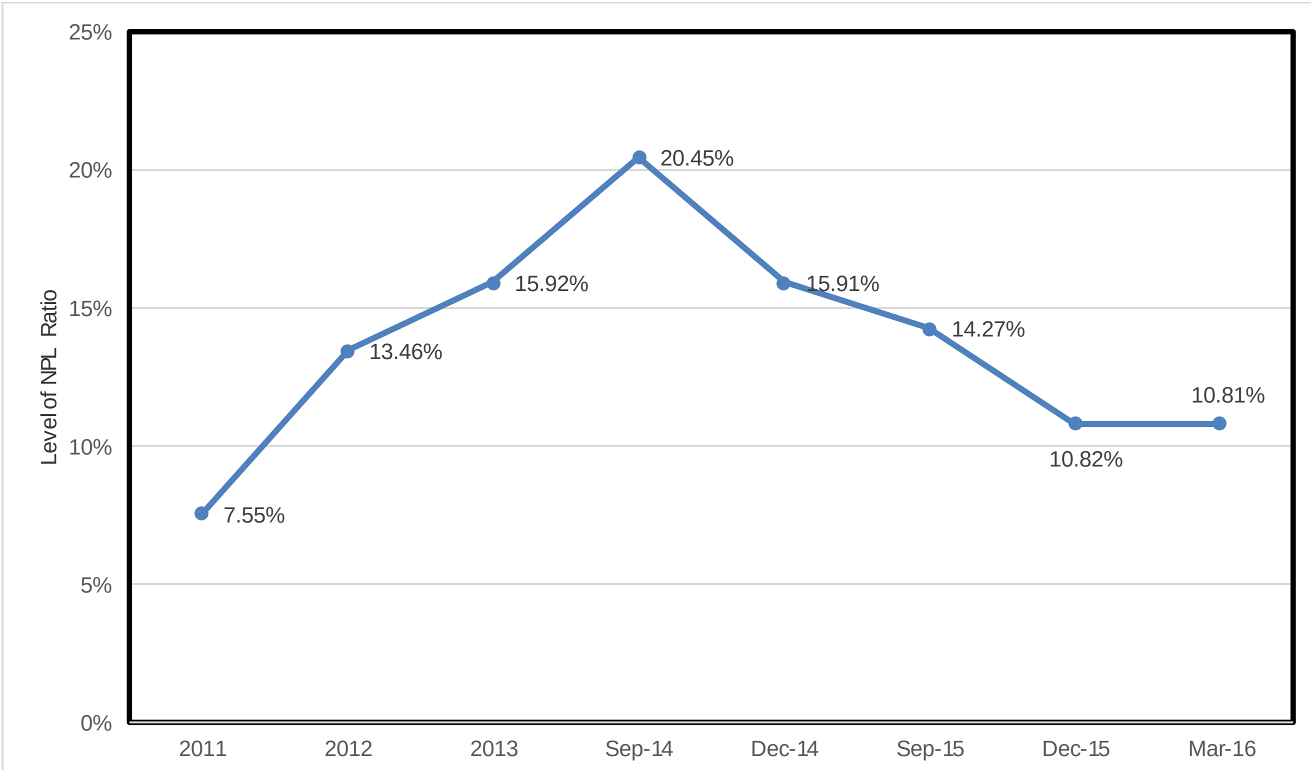
3.8. Banking institutions submitted their capitalisation plans to comply with the 2020 minimum capital requirements, which will be achieved through a combination of organic growth and fresh capital injection. The Reserve Bank is monitoring implementation of the banks' capital plans.

Asset Quality…

3.9. Total banking sector loans and advances amounted to $3.81 billion as at 31 March 2016, a marginal decline from $3.87 billion as at 31 December 2015.

3.10. Credit risk in the banking sector continues on an improving trend as reflected by a non-performing loans ratio of 10.81% as at 31 March 2016 from a peak of 20.45% in September 2014 as shown in the graph below.

Non-Performing Loans Trend



3.11. Banking institutions continued to strengthen their credit risk management strategies through, among other initiatives, stringent credit granting requirements, intensified collections and workout plans.

3.12. Further, banking institutions continued to dispose of qualifying NPLs to ZAMCO. As at 31 March 2016, banking sector had disposed NPLs valued at $418.62 million to ZAMCO, an increase from $357 million as at 31 December 2015.

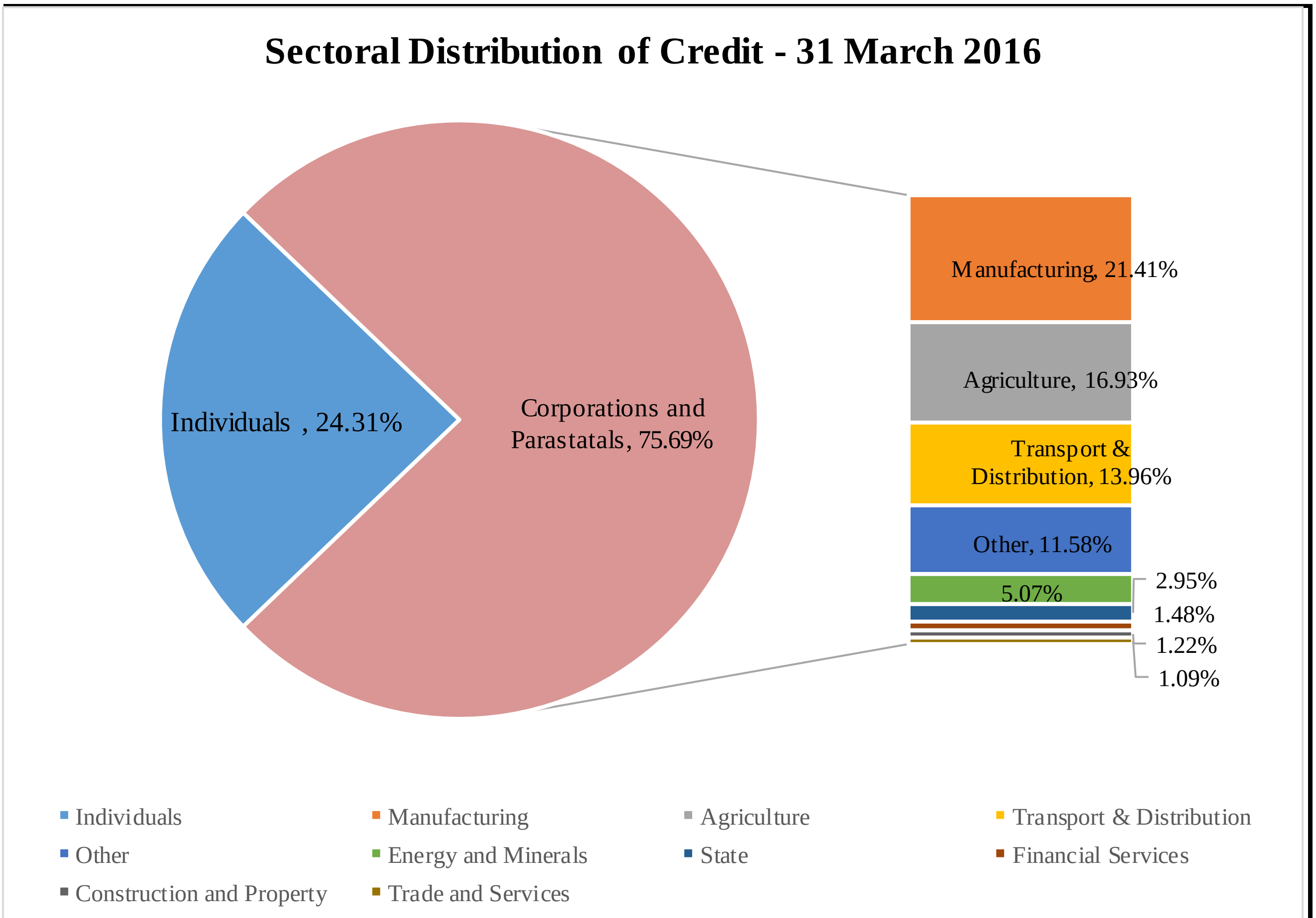
3.13. It is envisaged that the gradual decline in interest rates, review of credit risk management systems, bank balance sheet clean-ups through the ZAMCO initiative, as well as the enhancement of credit infrastructure through the establishment of a credit reference system and a collateral registry, should result in further improvement in asset quality and increased appetite for lending by banks.

3.14. As at 31 March 2016, thirteen banking institutions were already compliant with the target NPL ratio of 10% set for June 2016. The remaining banks are instituting measures to improve the quality of their credit portfolio.

3.15. As at 31 March 2016, commercial banks accounted for 77.36% of total banking sector loans and advances.

3.16. The top five banks had loans & advances amounting to **$2.48 billion**, which accounted for **63.25%** of total banking sector loans & advances as at 31 March 2016.

3.17. The distribution of banking sector lending to the various sectors as at 31 March 2016 is indicated in the figure below.



3.18. The distribution of credit remained largely unchanged from the previous quarter and remains largely dominated by lending to individuals and the manufacturing sector. The banking sector continued to be constrained in its ability to meet long-term funding requirements of capital intensive sectors such as construction and mining, due to the generally short-term nature of deposits held.

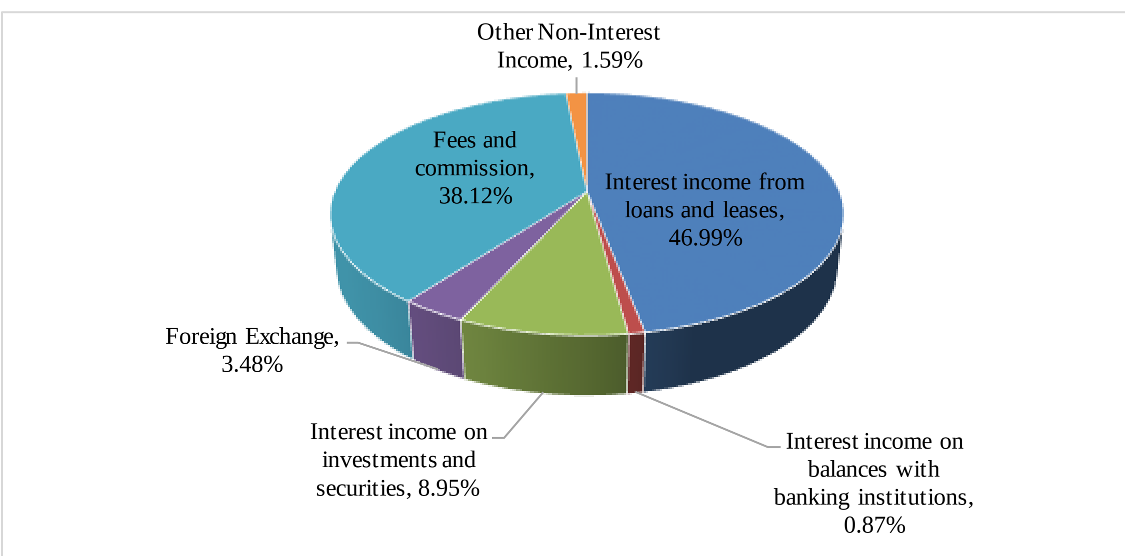
Earnings Performance…

3.19. The banking sector reported an aggregate net profit of $38.44 million for the quarter ended 31 March 2016 up from $4.02 million reported for the same period in 2015. The increase in profitability was largely driven by lower loan loss provisions in line with improving asset quality at some institutions, realignment of cost structures as well as exclusion of a loss-making banking institution which is under provisional liquidation.

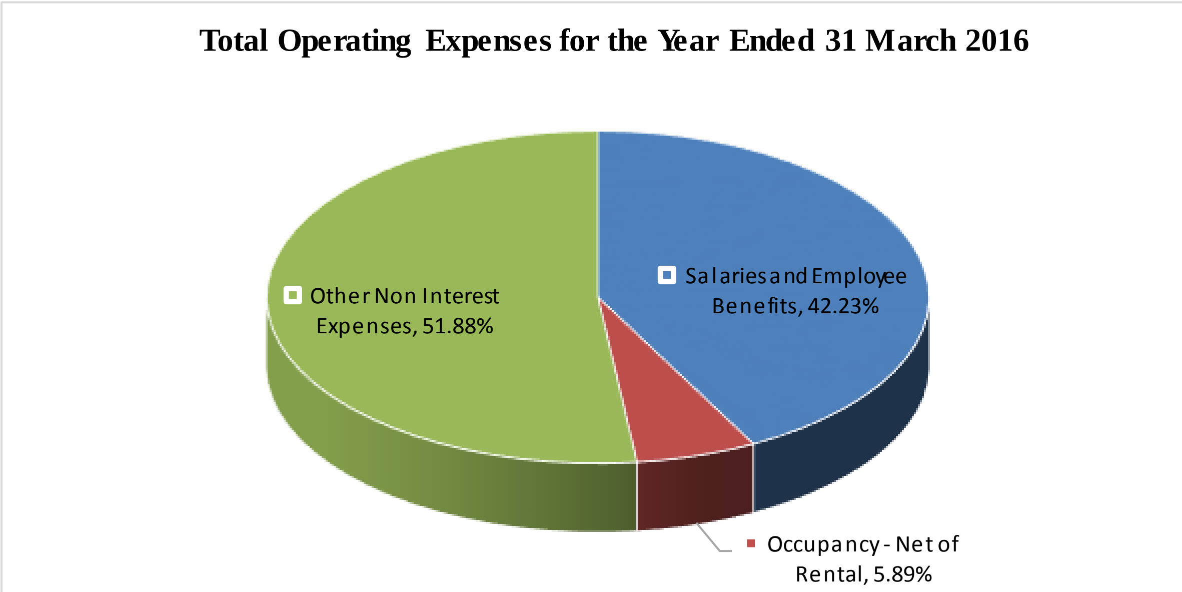
3.20. Sixteen out of 18 operating banking institutions recorded profits during the quarter ended 31 March 2016. Losses at the two (2) banking institutions were mainly a result of increased provisioning and a decline in interest income arising from reduced lending activities.

3.21. The average return on assets and return on equity improved to 0.42% and 2.79% as at 31 March 2016, from 0.08% and 0.40%, respectively, recorded as at 31 March 2015.

3.22. Interest income was the major driver of income of $199.99 million for the quarter ended 31 March 2016 as shown in the graph below.



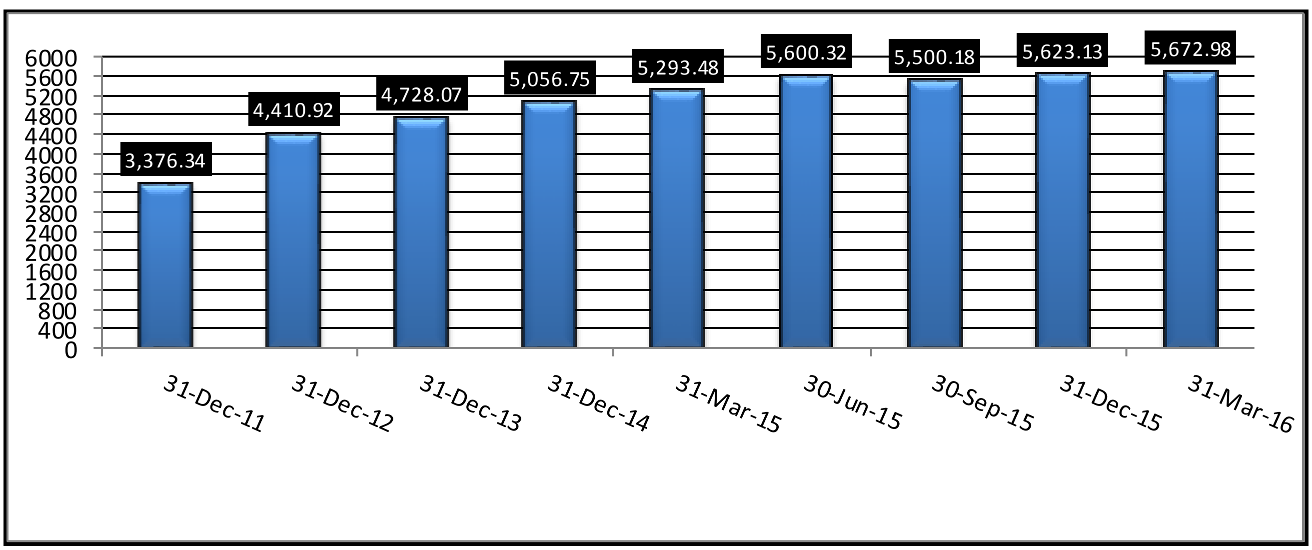
3.23. As at 31 March 2016, salaries & employment benefits and administrative costs were the major cost drivers as shown in the figure below.



Liquidity and Funds Management...

3.24. As at 31 March 2016, total banking sector deposits amounted to $5.67 billion from $5.62 billion in the previous quarter. The trend in deposits from December 2011 to 31 March 2016 is shown in the graph below.

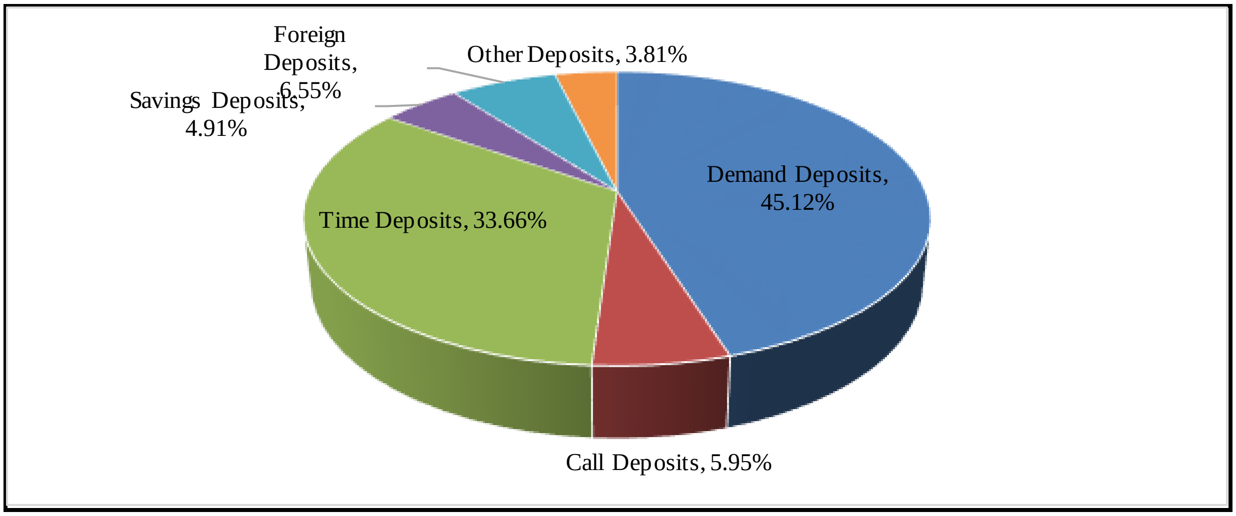
Banking Sector Deposits - December 2011 to March 2016



3.25. As at 31 March 2016, the commercial banking sub-sector accounted for 81.89% of banking sector deposits.

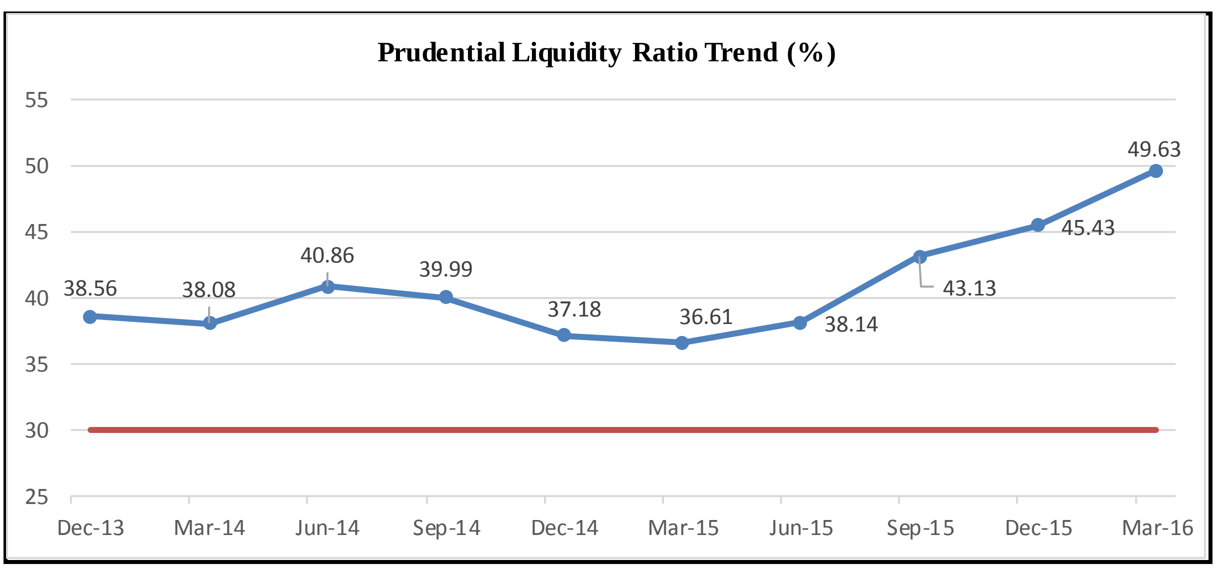
3.26. Demand and time deposits continued to dominate banking sector deposits as shown in the figure below.

Composition of Banking Sector Deposits as at 31 March 2016



3.27. The banking sector average prudential liquidity ratio of 49.63% as at 31 March 2016 was compliant with the regulatory minimum of 30%, with all banking institutions complying with the minimum requirement.

3.28. The diagram shows average prudential liquidity ratios since December 2013.



3.29. Notwithstanding high prudential liquidity ratios reported by banking institutions, the sector experienced cash constraints during the quarter largely driven by the macro-liquidity challenges in the economy.

Sensitivity to Market Risk…

3.30. Generally, the sector's exposure to market risk remained low. Under the current operating environment, the sector's exposure to interest rate risk was mainly in the banking book.

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

3.32. 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 $932.55 million as at 31 March 2016.

3.33. Stress tests conducted to assess the vulnerability of banking institutions' to foreign exchange rate movements showed that all banking institutions are resilient to a major level foreign exchange rate risk shock of a 15% appreciation of the US dollar against major currencies.

31 March 2016