CENTRAL BANK OF KENYA

CREDIT OFFICER SURVEY

JANUARY-DECEMBER 2013

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1.0 FOREWORD

1.1 KENYAN BANKING SECTOR PERFORMANCE

For the year 2013, the Kenyan Banking Sector recorded continued growth. Some of the sector's performance indicators are as follows:

- The aggregate balance sheet increased by 16.17 percent from Kshs 2.35 trillion in December 2012 to Kshs 2.73 trillion in December 2013.
- Gross loans expanded by 17.65 percent from Kshs 1.36 trillion in December 2012 to Kshs 1.60 trillion in December 2013.
- Deposits grew by 12.50 percent from Kshs 1.76 trillion in December 2012 to Kshs 1.98 trillion in December 2013.
- Total shareholders' funds increased by 18.91 percent from Kshs 362.86 billion in December 2012 to Kshs 431.49 billion in December 2013.
- Total income increased by 1.53 percent from Kshs 352.52 billion in December 2012 to Kshs 357.90 billion in December 2013 while total expenses decreased by 4.71 percent from Kshs 244.84 billion in December 2012 to Kshs 233.32 billion in December 2013.
- Interest income on loans fell by 3.57% in 2013 to Kshs 211.19 billion down from Kshs 219.01 billion in 2012. This is a reflection of declining lending rates in 2013.
- Interest expenses on deposits fell by 27.38 % to Kshs 72.13 billion in 2013 down from Kshs 99.32 billion in 2012. This is attributable to a decline in the cost of deposits in 2013.
- Unaudited pre-tax profits stood at Kshs 107.68 billion for 31st December 2012 compared to Kshs 124.57 billion for 31st December 2013 recording an increase of 16.89 per cent.

The growth in banking sector was accompanied by an upsurge in credit risk with the gross non-performing loans increasing by 30.91 percent from Kshs 61.56 billion in December 2012 to Kshs 80.59 billion in December 2013.

1.2 CREDIT OFFICER SURVEY

Credit risk is the single largest factor affecting the soundness of financial institutions and the financial system as a whole and lending is the principal business for most banks. The ratio for total loans to total assets for the year ended 31st December 2013 was 58.20%. In order to identify the potential causes and enhance understanding of credit risk, the Central Bank of Kenya introduced a quarterly Credit Officer Survey in 2012.

For the quarter ended 31st December 2013, CBK received Credit Officer Survey responses from 42 operational banks and 1 mortgage finance company. The list of the responding banks is attached to this report as **Annex I**.

CENTRAL BANK OF KENYA
JANUARY 2014

2.0 EXECUTIVE SUMMARY

2.1 SURVEY METHODOLOGY

The credit officer survey for the year 2013 predominantly included four questions that focused on:-

- Demand for credit.
- Credit standards.
- Non-Performing loans.
- Credit recovery efforts.

Two other questions that were included in the quarters ended March 2013 and September 2013 focused on Credit Information Sharing and suggestions for improvement on the credit officer survey questionnaire to make it more useful to the banking industry.

The survey targets senior credit officers of all 42 operational banks and 1 mortgage finance company. Charterhouse Bank Ltd which is under statutory management was excluded from all the quarterly surveys for the year 2013. All forty three institutions responded to the survey throughout the year. The list of the respondents is attached to this report as **Annex I**.

2.2 KEY FINDINGS

The key findings from the survey are detailed below.

2.2.1 Demand for credit

In year 2013, demand for credit generally increased in all the eleven economic sectors. The surveys established that peaceful political transition in 2013 and a stable macro-environment were the greatest factors that led to an increased demand for credit in the year.

2.2.2 Credit Standards

In 2013, credit standards generally remained unchanged in all the eleven economic sectors. This indicates that banks adopted relatively conservative credit policies in 2013 as they did in 2012.

2.2.3 Non-Performing Loans

For the first quarter of 2014, most banks expect the levels of non-performing loans to generally remain unchanged in 10 out of 11 sectors. Non-performing loans in personal and household sector are expected to rise due to cyclical reduction of customers' disposable income as a result of increased expenditures by customers during the December/January festivities.

2.2.4 Credit Recovery Efforts

In year 2013, credit recovery efforts generally increased in all the eleven economic sectors.

3.0 SURVEY FINDINGS

3.1 Demand for Credit

3.1.1 Observations

The demand for credit generally increased in the eleven economic sectors in 2013. This is supported by the expansion in gross loans from Kshs 1.36 trillion in December 2012 to Kshs 1.60 trillion in December 2013. Comparison of the eleven economic sectors shows that the highest growth in demand for credit was witnessed from Transport and Communication, Trade, Manufacturing and Agriculture sectors. At the beginning of the year the demand of credit was generally low due to the then prevailing political uncertainty, which generally had a negative impact on the business environment. However with the peaceful conclusion of the March 2013 general elections the industry experienced an upward growth in demand for credit. The fairly stable macro-economic environment was also cited as having had a positive impact on the demand for credit.

Table 1 below details the reported trend in demand for credit over the four quarters of 2013.

Table 1: Demand for Credit

	Dec-13			Sep-13			Jun-13			Mar-13		
	Increased	Remained Unchanged	Decreased	Increased	Remained Unchanged	Decreased	Increased	Remained Unchanged	Decreased	Increased	Remained Unchanged	Decreased
Agriculture	44%	44%	12%	48%	35%	18%	41%	44%	15%	14%	36%	50%
Manufacturing	48%	33%	19%	44%	41%	15%	39%	49%	12%	16%	34%	50%
Building & construction	39%	39%	22%	49%	29%	22%	40%	40%	19%	26%	24%	50%
Mining and Quarrying	14%	64%	21%	13%	60%	28%	7%	62%	31%	8%	42%	50%
Energy and water	30%	51%	19%	32%	49%	20%	29%	52%	19%	12%	38%	50%
Trade	60%	23%	16%	63%	23%	15%	67%	14%	19%	26%	24%	50%
Tourism, restaurant and Hotels	39%	46%	15%	28%	48%	25%	28%	48%	25%	13%	37%	50%
Transport and Communication	53%	28%	19%	51%	29%	20%	51%	29%	20%	23%	27%	50%
Real Estate	51%	37%	12%	61%	24%	15%	50%	29%	21%	31%	19%	50%
Financial Services	30%	58%	13%	35%	43%	23%	39%	41%	20%	12%	38%	50%
Personal/Household	59%	15%	27%	70%	20%	10%	63%	15%	22%	30%	20%	50%

3.2 Factors affecting demand for credit

3.2.1 Observations

In the last three quarters of 2013, the main factors that caused the demand for credit to increase were the drop in cost of borrowing and increased available investment opportunities as a result of a stable macroeconomic environment. However, in the first quarter, the high cost of borrowing and lack of investment opportunities were observed to have caused demand for credit to stagnate.

Internal financing, loans from other banks and non-banks as well as issuance of debt securities by banks were cited as factors that decreased the demand of credit in the quarter ended March 2013. However, the aforementioned factors did not have any impact in demand for credit in the last three quarters of 2013.

Table 2 details the factors affecting demand for credit over the four quarters of 2013.

Table 2: Factors affecting Demand for Credit

	Dec-13			Sep-13			Jun-13			Mar-13		
	Increased	Remained Unchanged	Decreased	Increased	Remained Unchanged	Decreased	Increased	Remained Unchanged	Decreased	Increased	Remained Unchanged	Decreased
Internal Financing	10%	68%	23%	13%	65%	23%	12%	68%	20%	12%	24%	65%
Loans from other banks	17%	62%	21%	14%	62%	24%	14%	49%	37%	19%	39%	42%
Loans from non-banks	7%	59%	34%	5%	65%	30%	12%	52%	36%	15%	30%	55%
Issuance of debt securities	7%	78%	15%	0%	85%	15%	3%	79%	18%	18%	35%	47%
Issuance of equity	10%	80%	10%	5%	79%	15%	0%	80%	20%	23%	46%	31%
Cost of borrowing	37%	37%	26%	43%	26%	31%	40%	28%	33%	28%	49%	23%
Available investment opportunities	49%	37%	14%	43%	43%	14%	48%	45%	7%	29%	57%	14%
Retention of CBR	37%	56%	7%	37%	59%	5%	-	-	-	-	-	-
Drop in CBR	-	-	-	-	-	-	54%	41%	5%	35%	65%	-
Political Risk	30%	53%	16%	26%	57%	17%	63%	30%	7%	10%	15%	75%

3.3 Credit Standards

3.3.1 Observations

In 2013, credit standards generally remained unchanged for all the eleven economic sectors. This seems to indicate that banks adopted conservative credit policies in 2013 as was the case in 2012. **Table 3** shows the trend in credit standards over the four quarters of 2013.

Table 3: Credit Standards												
	Dec-13			Sep-13			Jun-13			Mar-13		
	Tightened	Remained Unchanged	Eased	Tightened	Remained Unchanged	Eased	Tightened	Remained Unchanged	Eased	Tightened	Remained Unchanged	Eased
Agriculture	17%	71%	12%	13%	80%	7%	8%	70%	22%	13%	83%	5%
Manufacturing	5%	85%	10%	2%	90%	7%	3%	71%	26%	7%	83%	10%
Building & Construction	38%	57%	5%	27%	71%	2%	21%	60%	19%	33%	57%	10%
Mining and Quarrying	12%	86%	2%	2%	95%	2%	5%	83%	12%	10%	83%	7%
Energy and water	12%	86%	2%	0%	95%	5%	0%	88%	12%	10%	88%	3%
Trade	17%	62%	21%	7%	73%	20%	7%	60%	33%	17%	71%	12%
Tourism, restaurant and Hotels	10%	78%	12%	10%	88%	2%	10%	62%	28%	34%	63%	2%
Transport and Communication	34%	56%	10%	20%	76%	5%	14%	67%	19%	29%	67%	5%
Real Estate	23%	51%	26%	24%	64%	12%	19%	57%	24%	33%	60%	7%
Financial Services	7%	83%	10%	8%	88%	5%	7%	76%	17%	20%	78%	2%
Personal/Household	29%	46%	24%	27%	59%	15%	17%	51%	32%	33%	60%	8%

3.4 Factors affecting credit standards

3.4.1 Observations

The 2013 credit surveys highlighted eight factors which led to the credit standards remaining constant. These include constraints relating to the banks capital, competition from other credit providers, retention of the Central Bank Rate(CBR) and banks cost of funds. The quarterly credit survey for March 2013 demostrated that political risk prevailing during the electioneering period led banks to tighten their credit standards in the first quarter of 2013.

Its worth noting the following additional factors cited in December 2013 survey as having influenced some of the bank's credit standards:

- Delayed receipts from the Government of Kenya for completed projects/contracts affected repayment patterns of customers in the building and construction sector. As a result some banks marginally tightened their credit standards to customers in the building and construction sector in the last half of 2013 as compared to quarter two of 2013. Quarter one of 2013 generally attracted tight credit standards in all sectors due to the political risk that was surrounding the elections.
- NPLs are expected to slightly increase mainly in the personal and household sector due to reduction in disposable income after the December/January festivities. In this regard, some banks indicated their intention to marginally intensify their credit standards so as to mitigate any possible default risk.

Table 4 below shows the trend in factors influencing credit standards over the four quarters of 2013.

Table 4 : Factors influencing Credit Standards												
	Dec-13			Sep-13			Jun-13			Mar-13		
	Tightened	Remained Unchanged	Eased	Tightened	Remained Unchanged	Eased	Tightened	Remained Unchanged	Eased	Tightened	Remained Unchanged	Eased
Bank's cost of funds & Balance sheet constraints	34%	61%	5%	33%	58%	9%	40%	44%	16%	28%	63%	9%
Constraints relating to Bank's capital position	23%	74%	2%	14%	79%	7%	12%	76%	12%	12%	88%	0%
Competition from other banks	9%	56%	35%	9%	58%	33%	9%	56%	35%	7%	60%	33%
Competition from DTMs, Saccos, & other Credit Providers	2%	74%	23%	2%	79%	19%	2%	77%	21%	2%	84%	14%
Expectations regarding general economic activity	9%	63%	28%	21%	60%	19%	12%	56%	33%	40%	42%	19%
Drop in Central Bank Rate (CBR)	-	-	-	-	-	-	5%	60%	35%	19%	55%	26%
Political Risk	21%	67%	12%	19%	74%	7%	26%	63%	12%	54%	39%	7%
Retaining the CBR	7%	70%	23%	9%	72%	19%	-	-	-	-	-	-

3.5 Non-Performing Loans (NPLs)

3.5.1 Observations

In the first quarter of 2013, most banks forecasted an increase in NPLs in the building and construction, transport & communication and real estate sectors. The institutions forecasted a decrease in NPLs in the tourism, restaurant & hotels and trade sectors. However, the actual NPLs for the quarter ended 30th June 2013 increased in personal/household, trade sector and real estate sectors whilst there were decreases in energy and water and mining and quarrying sectors.

In the second quarter of 2013, there was an expectation that NPLs would generally remain constant. However the actual NPLs for the quarter ended 30th September 2013 decreased in personal/household, transport and communication, agriculture, tourism, restaurant and hotels, financial services and mining and quarrying sectors. Actual NPLs for the third quarter increased in trade, real estate, manufacturing, building and construction and energy and water sectors.

In the third quarter, banks had forecasted an increase of NPLs in the Personal/Household sector while a decline was expected in the Trade and Tourism sectors as well as building and transport sectors. The actual NPLs in the fourth quarter showed a decrease in mining and quarrying sector and an increase in personal/household sector in the last quarter of 2013.

For the first quarter of 2014, the banking sector has forecast an increase in NPLs in the Transport & Communication and Personal and Household sectors. The expected increase is attributed to revised regulations on night travel for public service vehicles and cyclical reduction of customers' disposable income as a result of increased one off expenditures during the December/January festivities. The current instability in South Sudan was also cited as a likely cause for negative impact on the businesses especially in Energy and Water as well as in Transport and Communication sectors who export and transport directly to South Sudan.

Some banks are optimistic on reduced NPLs in the quarter ended 31st March 2014 due to:-

- Cost cutting measures being embraced by Government of Kenya to manage recurrent expenditures is expected to increase the government's ability to make prompt payments for its development expenditure/projects. Similarly, stabilizing of the interest rates and decline in inflation rate is expected to culminate to growth in the economy.
- Receipt of payments by contractors from Government of Kenya on government funded contracts commencing end of 2013.

The trend on expectations of NPLs is shown in **Table 5 below**.

Table 5: Non Performing Loans												
	Dec-13			Sep-13			Jun-13			Mar-13		
	Rise	Remained Unchanged	Fall	Rise	Remained Constant	Fall	Rise	Remained Constant	Fall	Rise	Remained Constant	Fall
Agriculture	10%	63%	27%	12%	61%	27%	2%	61%	37%	5%	57%	38%
Manufacturing	7%	68%	24%	7%	71%	22%	5%	66%	29%	7%	49%	44%
Building & construction	15%	48%	38%	18%	55%	28%	15%	43%	43%	15%	40%	45%
Mining and Quarrying	3%	83%	15%	8%	80%	13%	5%	82%	13%	5%	74%	21%
Energy and water	8%	78%	15%	3%	83%	15%	8%	65%	27%	5%	73%	22%
Trade	18%	43%	40%	20%	43%	38%	15%	34%	51%	10%	37%	54%
Tourism, Restaurant & Hotels	15%	48%	38%	23%	40%	38%	0%	55%	45%	10%	33%	58%
Transport & Communication	25%	43%	33%	20%	53%	28%	10%	48%	43%	15%	33%	53%
Real Estate	10%	58%	33%	21%	52%	26%	17%	38%	45%	12%	37%	51%
Financial Services	3%	73%	25%	5%	75%	20%	6%	81%	13%	0%	68%	32%
Personal/Household	44%	33%	23%	41%	39%	20%	34%	29%	37%	10%	43%	48%

3.6 Credit Recovery Efforts

3.6.1 Observations

In year 2013, credit recovery efforts generally increased in all the eleven economic sectors. The increase was mainly driven by banks urge to recover NPLs which had consistently built up in the year.

For the quarter ending 31st March 2014, the banks expect to:-

- Ease credit recovery efforts in the Tourism, Restaurant and Hotels sector arising from the good yield from the just concluded peak season.
- Reap good repayment results based on some banks indications of having restructured some loans so as to accommodate borrowers' repayment instalments within their disposable incomes. The borrowers envisage to consistently service their loans due to the expected growth in the economy. The growth is supported by the continuous efforts by

the government to strengthen both fiscal and monetary policies to support macroeconomic stability.

The trend on credit recovery efforts is shown in **Table 6**.

Table 6: Credit Recovery Efforts												
	Dec-13			Sep-13			Jun-13			Mar-13		
	Intensified	Remained Unchanged	Eased	Intensified	Remained Unchanged	Eased	Intensified	Remained Unchanged	Eased	Intensified	Remained Unchanged	Eased
Agriculture	51%	44%	5%	49%	46%	5%	40%	53%	8%	39%	51%	10%
Manufacturing	45%	52%	2%	43%	55%	3%	22%	67%	11%	45%	40%	14%
Building & construction	54%	44%	2%	58%	40%	3%	55%	38%	8%	48%	45%	8%
Mining and Quarrying	29%	71%	0%	30%	70%	0%	31%	67%	3%	31%	64%	5%
Energy and water	37%	61%	2%	40%	60%	0%	32%	63%	5%	36%	59%	5%
Trade	61%	37%	2%	53%	38%	10%	56%	34%	10%	56%	29%	15%
Tourism, Restaurant & Hotels	41%	54%	5%	58%	35%	8%	43%	45%	13%	40%	45%	15%
Transport & Communication	66%	29%	5%	59%	37%	5%	51%	41%	8%	46%	39%	15%
Real Estate	43%	55%	2%	53%	45%	3%	55%	33%	12%	52%	33%	14%
Financial Services	35%	60%	5%	36%	62%	3%	33%	60%	8%	33%	58%	10%
Personal/Household	68%	27%	5%	71%	29%	0%	76%	17%	7%	58%	30%	13%

Annex I (List of Respondents)

LIST OF THE RESPONDENTS[1]

1. African Banking Corporation Ltd.
2. Bank of Africa Kenya Ltd.
3. Bank of Baroda
4. Bank of India
5. Barclays Bank of Kenya Ltd.
6. CfC Stanbic Bank Ltd.
7. Chase Bank (K) Ltd.
8. Citibank N.A Kenya.
9. Commercial Bank of Africa Ltd.
10. Consolidated Bank of Kenya Ltd.
11. Co-operative Bank of Kenya Ltd.
12. Credit Bank Ltd.
13. Development Bank of Kenya Ltd.
14. Diamond Trust Bank (K) Ltd.
15. Dubai Bank Kenya Ltd.
16. Ecobank Kenya Ltd.
17. Equatorial Commercial Bank Ltd.
18. Equity Bank Ltd.
19. Family Bank Ltd.
20. Fidelity Commercial Bank Ltd.
21. First Community Bank Limited
22. Guaranty Trust Bank Ltd.
23. Giro Commercial Bank Ltd.
24. Guardian Bank Ltd.
25. Gulf African Bank Limited.
26. Habib Bank A.G Zurich.
27. Habib Bank Ltd.
28. I & M Bank Ltd.
29. Imperial Bank Ltd.
30. Jamii Bora Bank Ltd.
31. Kenya Commercial Bank Ltd.
32. K-Rep Bank Ltd.
33. Middle East Bank (K) Ltd.
34. National Bank of Kenya Ltd.
35. NIC Bank Ltd.
36. Oriental Commercial Bank Ltd.
37. Paramount Universal Bank Ltd.
38. Prime Bank Ltd.
39. Standard Chartered Bank (K) Ltd.
40. Trans-National Bank Ltd.
41. UBA Kenya Bank Ltd.
42. Housing Finance Ltd.
43. Victoria Commercial Bank Ltd.

[1]Charterhouse Bank Ltd which is under statutory management was excluded from all the quarterly surveys for the year 2013