CENTRAL BANK OF KENYA

CREDIT OFFICER SURVEY

JANUARY-MARCH 2015

Table of Contents

Contents **Page**

1.0 FOREWORD

1.1 KENYAN BANKING SECTOR PERFORMANCE

The Kenyan Banking Sector recorded growth in the quarter ended 31st March 2015, compared to the quarter ended 31st December 2014. Some of the sector's performance indicators are as follows:

- The aggregate balance sheet increased by 19.5% from Kshs 2.82 trillion in December 2014 to Kshs 3.37 trillion in March 2015.
- Gross loans increased by 3.5% from Kshs 1.97 trillion in December 2014 to Kshs 2.03 trillion in March 2015.
- Banking sector deposits grew by 3.4% from Kshs 2.33 trillion in December 2014 to Kshs 2.41 trillion in March 2015.
- Total shareholders' funds increased marginally by 0.72% from Kshs 530.09 billion in December 2014 to Kshs 533.9 billion in March 2015.
- Cumulative unaudited pre-tax profits for 31st March 2015 stood at Kshs 37.3 billion compared to Kshs 33.4 billion for 31st March 2014 recording an increase of 11.6%.

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. Lending is also the principal business for banks. The ratio for total loans to total assets for the quarter ended 31st March 2015 was 59.75% a slight increase from 59.48% reported in December 2014. 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 March 2015, 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
APRIL 2015

2.0 EXECUTIVE SUMMARY

2.1 SURVEY METHODOLOGY

The credit officer survey for the quarter ended 31st March 2015 predominantly included four questions that focused on:-

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

The survey, conducted in April 2015, targeted senior credit officers of all 42 operational commercial banks and 1 mortgage finance company. Charterhouse Bank Ltd, which remains under statutory management, was excluded from the survey. All the forty three institutions responded.

2.2 KEY FINDINGS

The key findings from the survey are detailed below:

2.2.1 Demand for credit

The demand for credit generally remained constant in six economic sectors and increased in five economic sectors in the quarter ended March 2015. The survey established that available investment opportunities, cost of borrowing, issuance of debt securities and equity, the Kenya Bankers Reference Rate (KBRR) and retention of CBR at 8.5% were the main factors that led to increased demand for credit.

2.2.2 Credit Standards

Credit standards largely remained unchanged across all eleven economic sectors in Q1 of 2015. However, the credit standards were tightened for the Tourism, Real Estate and Building and Construction sectors while those for the Trade and Personal/Household sectors were eased. Increased insecurity, bank's capital position, Balance Sheet constraints, Political Risk and cost of funds were cited as the main driving factors for banks tightening their credit standards.

2.2.3 Non-Performing Loans

For the second quarter of 2015, most banks expect the levels of non-performing loans to generally remain constant across all eleven economic sectors. However, banks foresee increasing NPLs in four sectors: Tourism, Personal/Household, Transport and Communication and Real Estate sectors.

2.2.4 Credit Recovery Efforts

In Q2 of 2015, most banks intend to intensify their loan recovery efforts in all the eleven economic sectors with Personal/Household, Tourism, Transport, Trade, Building and Construction sectors expected to witness higher recovery efforts than other economic sectors.

3.0 SURVEY FINDINGS

3.1 Demand for Credit

3.1.1 Observations

- In Q1 of 2015, Kenyan banks indicated that demand for credit increased in five sectors compared to the six sectors in Q4 of 2014. This was led by Trade, Building and Construction, Personal/Household, Transport and Agriculture sectors with 60%, 56%, 54%, 49% and 56% of the respondents reporting increased demand for credit.
- Six economic sectors led by Mining, Energy, Financial Services, Tourism, Manufacturing and Real Estate were reported to have recorded unchanged demand for credit.
- The number of banks that reported an increased demand of credit from the Agricultural and Building and construction sectors went up by 7% and 5% whereas demand for credit in the Tourism sector decreased by 17% of the respondents when compared to Q4 of 2014. Decreased demand for credit may be attributed to travel advisories, recent spate of insecurity in the country whereas increased demand in the Agriculture sector was triggered by the expected onset of rains as farmers begun to prepare for the planting season.

Chart 1 and **Table 1** below present the trend in the demand for credit in the quarter ended March 2015 as compared to December 2014.

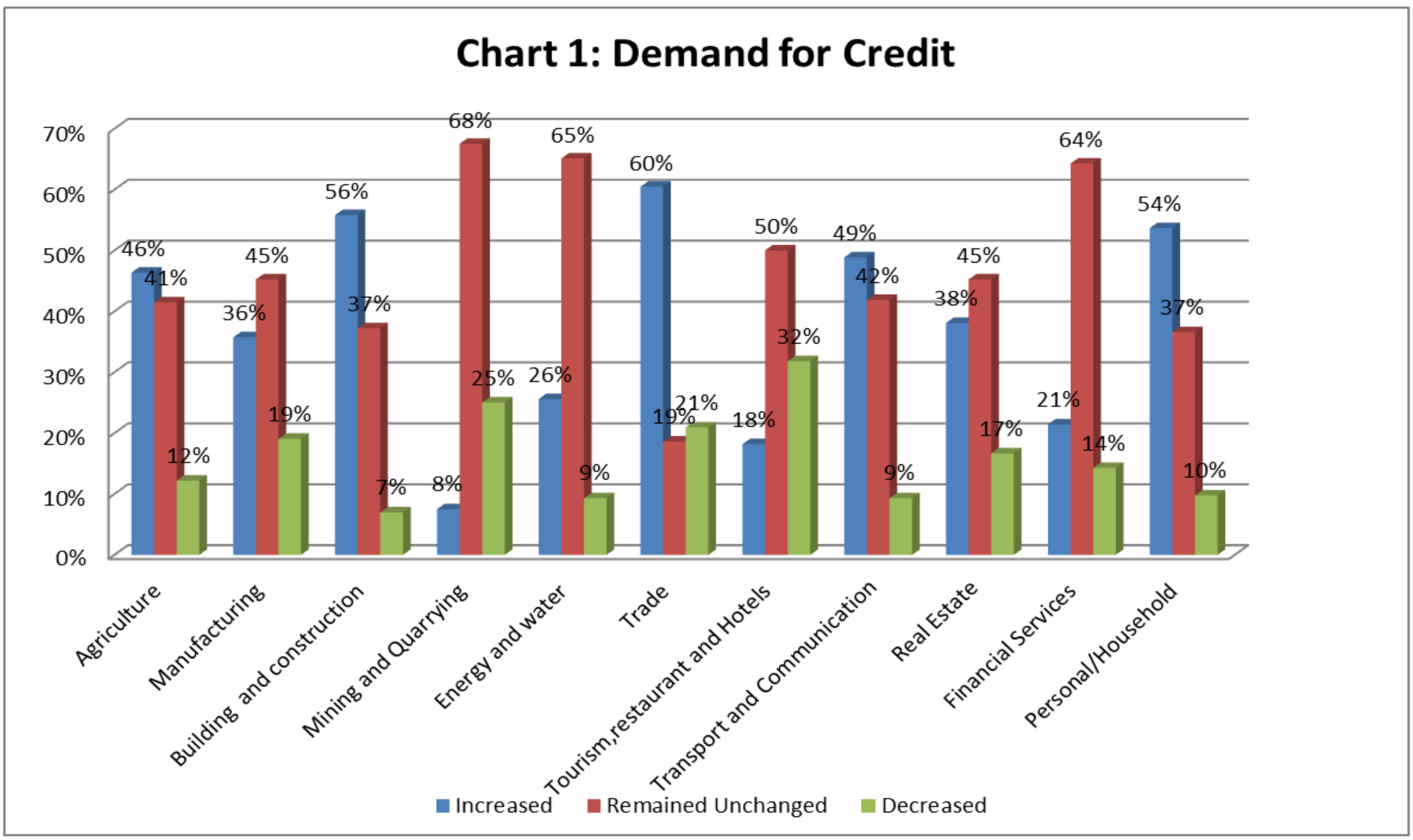

Table 1: Change in Demand for Credit

	March 2015			December 2014		
	Increased	**Remained Unchanged**	**Decreased**	**Increased**	**Remained Unchanged**	**Decreased**
Agriculture	46%	41%	12%	39%	46%	15%
Manufacturing	36%	45%	19%	45%	29%	26%
Building & Construction	56%	37%	7%	51%	40%	9%
Mining and Quarrying	8%	68%	25%	7%	80%	12%
Energy and Water	26%	65%	9%	23%	60%	16%
Trade	60%	19%	21%	72%	21%	7%
Tourism, Restaurant and Hotels	18%	50%	32%	35%	42%	23%
Transport and Communication	49%	42%	9%	54%	46%	0%
Real Estate	38%	45%	17%	55%	33%	12%
Financial Services	21%	64%	14%	17%	66%	17%
Personal/Household	54%	37%	10%	65%	30%	5%

3.2 Factors affecting demand for credit

3.2.1 Observations

- Issuance of equity, Issuance of debt securities, Loans from non-banks, Internal Financing, retention of CBR at 8.5% and Loans from other banks were cited by 88%, 83%, 71%, 69%, 67% and 65% of the respondents respectively, as having had the least influence on the demand for credit during the quarter under review.
- Reduction of KBRR, cost of borrowing, available investment opportunities and retention of CBR at 8.5% were cited as the main factors that led to increased demand for credit. 44%, 40%, 35% and 28% of the respondents respectively cited these factors as having led to increased demand in credit.

The responses on factors affecting demand for credit in Q1 of 2015 are presented in **Chart 2** and **Table 2** below.

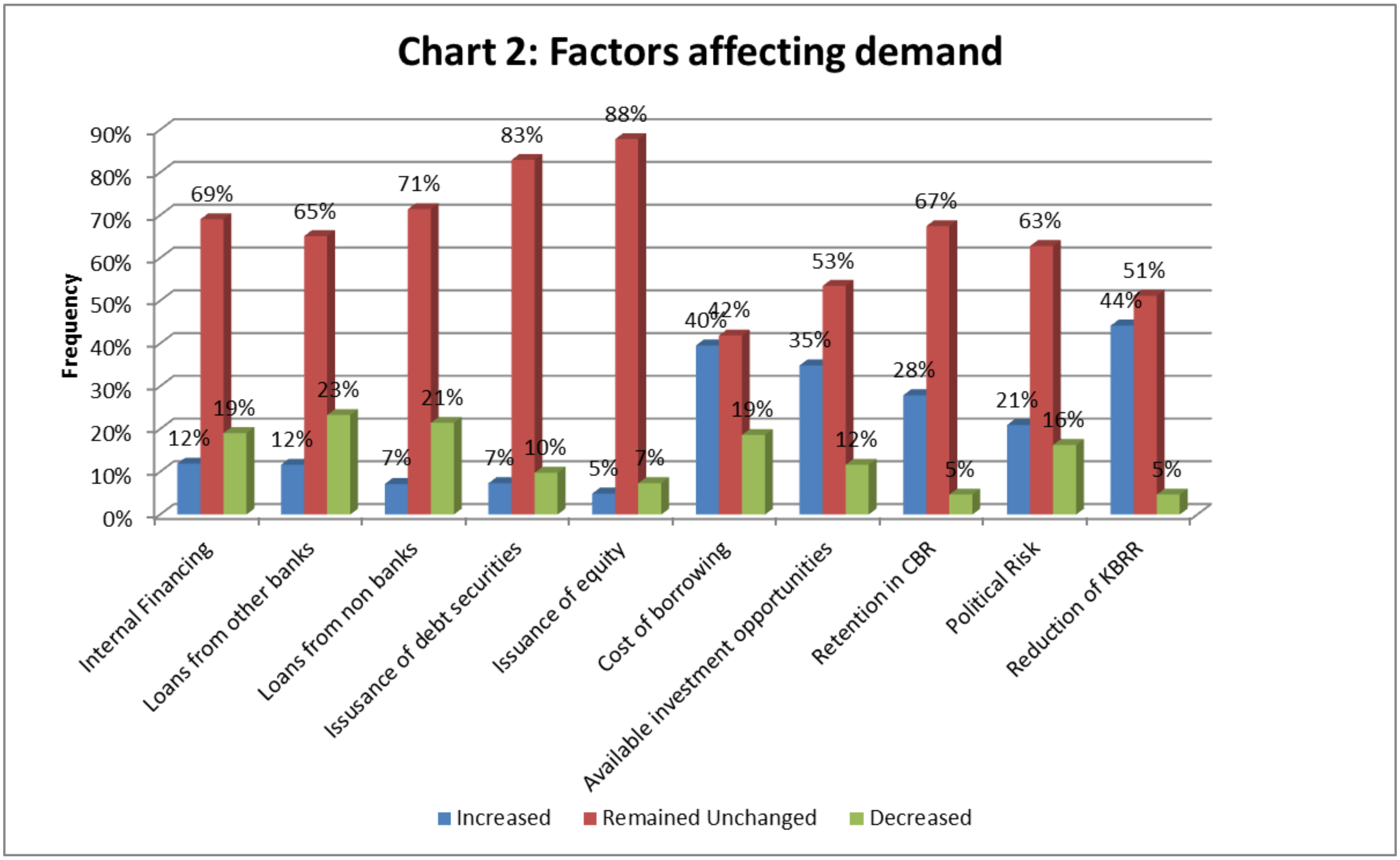

Table 2: Factors affecting Demand for credit

	March 2015			December 2014		
	Increased	**Remained Unchanged**	**Decreased**	**Increased**	**Remained Unchanged**	**Decreased**
Internal Financing	12%	69%	19%	18%	62%	21%
Loans from other banks	12%	65%	23%	29%	12%	59%
Loans from non-banks	7%	71%	21%	3%	67%	31%
Issuance of debt securities	7%	83%	10%	3%	85%	13%
Issuance of equity	5%	88%	7%	0%	95%	5%
Cost of borrowing	40%	42%	19%	32%	46%	22%
Available investment opportunities	35%	53%	12%	45%	45%	10%
Retention in CBR	28%	67%	5%	26%	71%	2%
Political Risk	21%	63%	16%	15%	66%	20%
Reduction of KBRR	44%	51%	5%	0%	59%	5%

3.3 Credit Standards

3.3.1 Observations

- The survey established that credit standards generally remained unchanged for all economic sectors over the three months to 31st March 2015 continuing the trend observed in Q4 of 2014.
- However, credit standards in Q1 of 2015 were tightened for the Tourism, Real Estate, Energy and Water, and Financial Services, Trade, Mining and Manufacturing sectors when compared to Q4 of 2014.
- In the quarter ended March 2015 banks eased the credit standards in Trade, Personal/Household and Manufacturing sectors with 19%, 14% and 12% of the respondents reporting so.

These responses are presented in **Chart 3** and **Table 3** below:

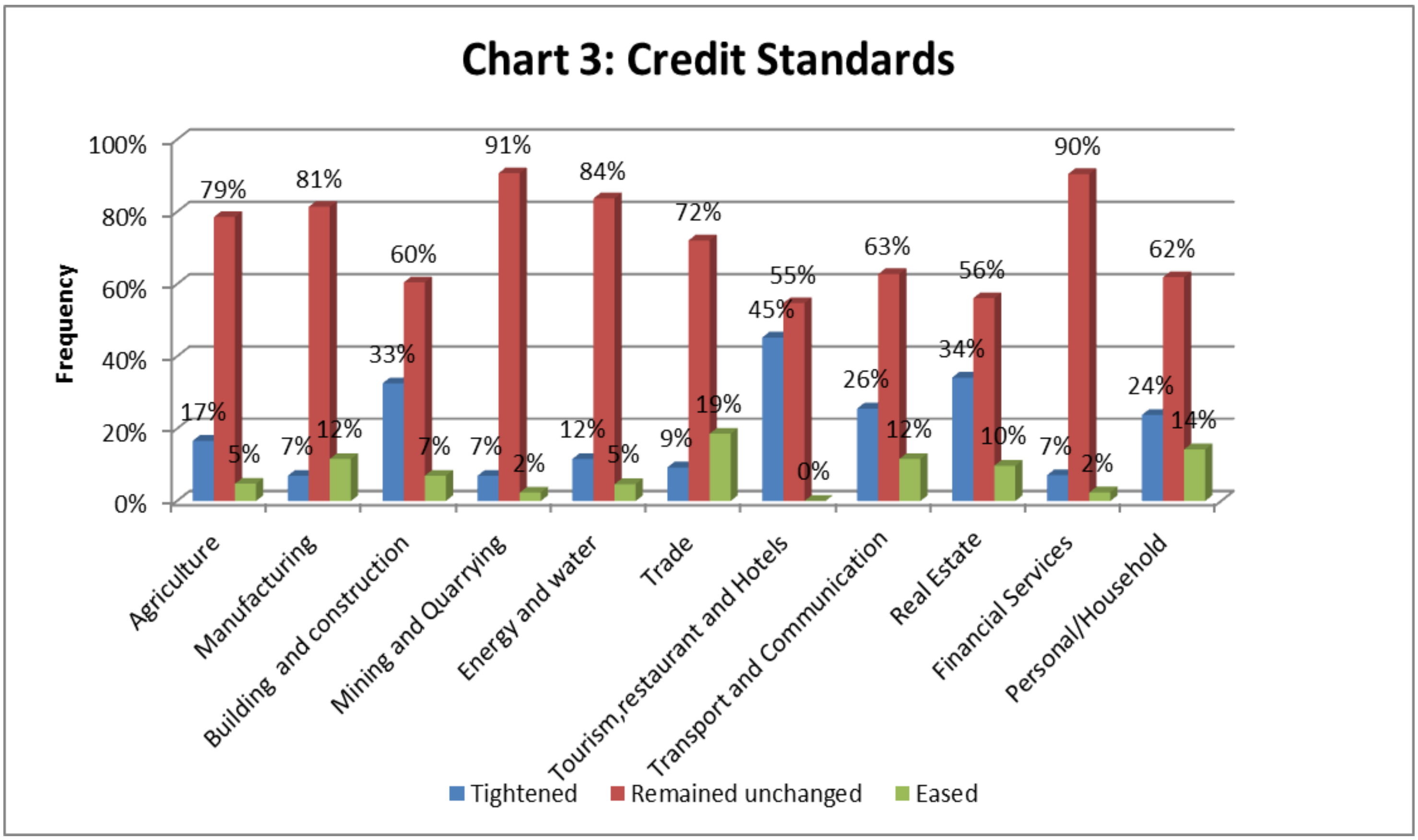

Table 3: Credit Standards

	March 2015			December 2014		
	Tightened	Remained Unchanged	Eased	Tightened	Remained Unchanged	Eased
Agriculture	17%	79%	5%	10%	83%	7%
Manufacturing	7%	81%	12%	5%	88%	7%
Building & Construction	33%	60%	7%	38%	52%	10%
Mining and Quarrying	7%	91%	2%	5%	90%	5%
Energy and Water	12%	84%	5%	5%	90%	5%
Trade	9%	72%	19%	7%	74%	19%
Tourism, Restaurant and Hotels	45%	55%	0%	40%	52%	7%
Transport and Communication	26%	63%	12%	31%	62%	7%
Real Estate	34%	56%	10%	27%	68%	5%
Financial Services	7%	90%	2%	2%	95%	2%
Personal/Household	24%	62%	14%	24%	64%	12%

3.4 Factors affecting credit standards

3.5.1 Observations

- In the quarter ended 31st March 2015, most of the factors that influence changes on credit standards had little impact. This supports the finding that credit standards to all economic sectors generally remained unchanged in the quarter.
- In Q1 of 2015, 36% of the banks tightened their credit standards due to Balance Sheet constraints, 27% due to Bank's capital position, 17% due to Political Risk and 7% due to competition from other banks.
- However, when compared to the quarter ended December 2014, more banks cited Political Risk (by 10%), Constraints relating to Bank's capital position and KBBR (by 3%) and Competition from other banks (by 2%) as factors that contributed to tightening of credit standards. Retention of CBR rate, KBRR, Competion from other credit providers and Political Risk did not have a significant impact on credit standards with 93%, 83%, 71% and 78% of the respondents respectively indicating so.

A comparison of the trend in the factors affecting the banks' credit standards are shown in **Chart 4** and **Table 4** below.

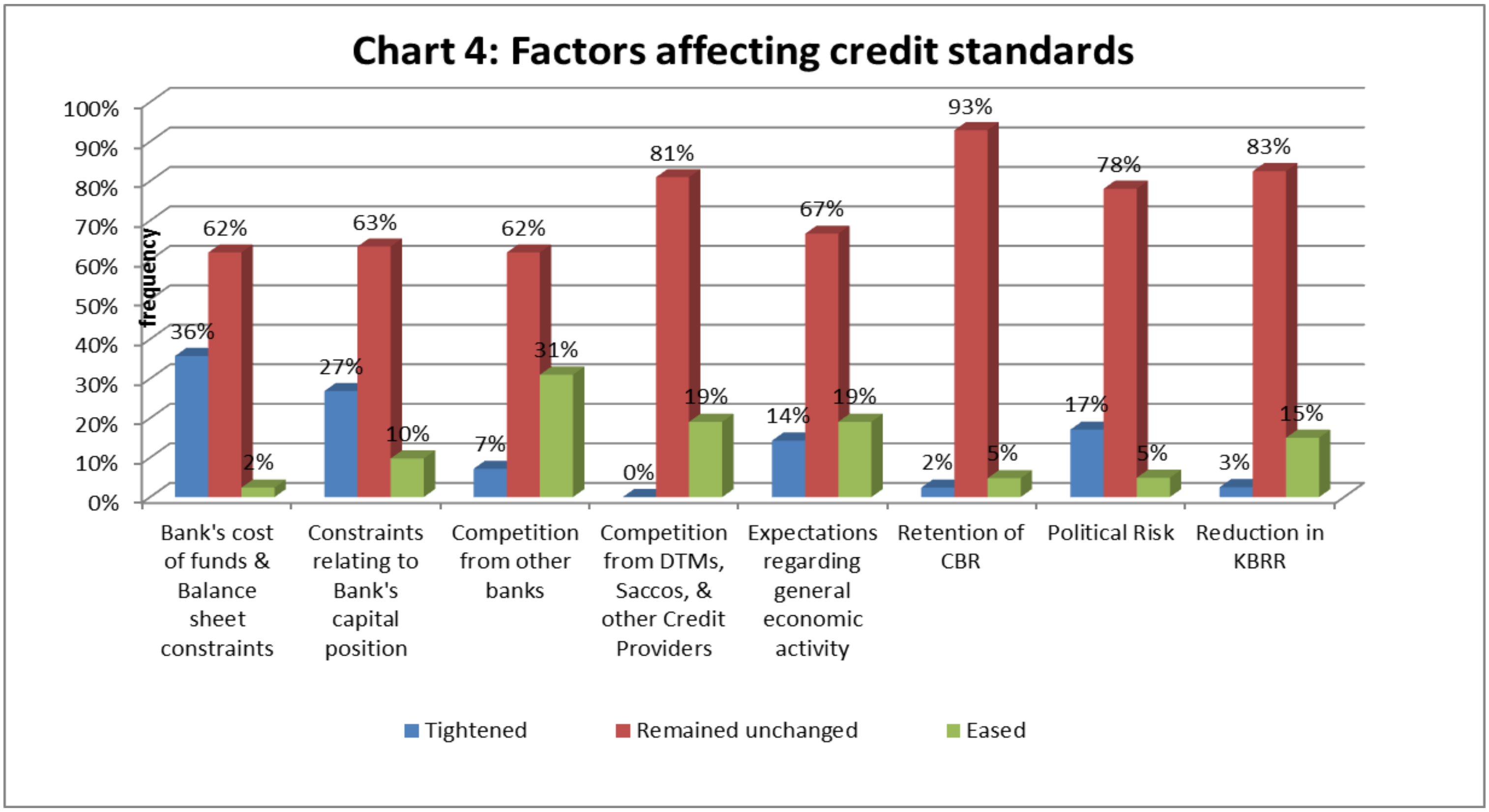

Table 4: Impact of factors affecting credit standards

	March 2015			December 2014		
	Tightened	**Remained Unchanged**	**Eased**	**Tightened**	**Remained Unchanged**	**Eased**
Bank's cost of funds & Balance sheet constraints	36%	62%	2%	38%	57%	5%
Constraints relating to Bank's capital position	27%	63%	10%	24%	71%	5%
Competition from other banks	7%	62%	31%	5%	67%	29%
Competition from DTMs, Saccos, & other Credit Providers	0%	81%	19%	0%	81%	19%
Expectations regarding general economic activity	14%	67%	19%	14%	67%	19%
Retention of Central Bank Rate (CBR)	2%	93%	5%	5%	86%	10%
Political Risk	17%	78%	5%	7%	79%	10%
KBRR	3%	83%	15%	0%	0%	0%

3.5 Non-Performing Loans (NPLs)

3.5.1 Observations

- Though most of the banks expect level of NPLs to remain unchanged in Q2 of 2015, there was a significant increase in the number of respondents that foresee higher NPLs in the Trade, Transport and Communication, Mining and Quarrying and Tourism sectors. These were 15%, 11%, 5% and 4% increase in the number of respondents respectively as compared to the quarter ended December 2014.
- The current spate of insecurity in the country, travel advisories and the heightened political activity may support the expected increase in NPLs in the Tourism sector. The expected increase in NPLs in the Mining and Quarrying sector may be attributed to the on-going reforms in the Mining sector.

Chart 5 and **Table 5** below indicate respondents' expectations on NPL trend in Q1 of 2015.

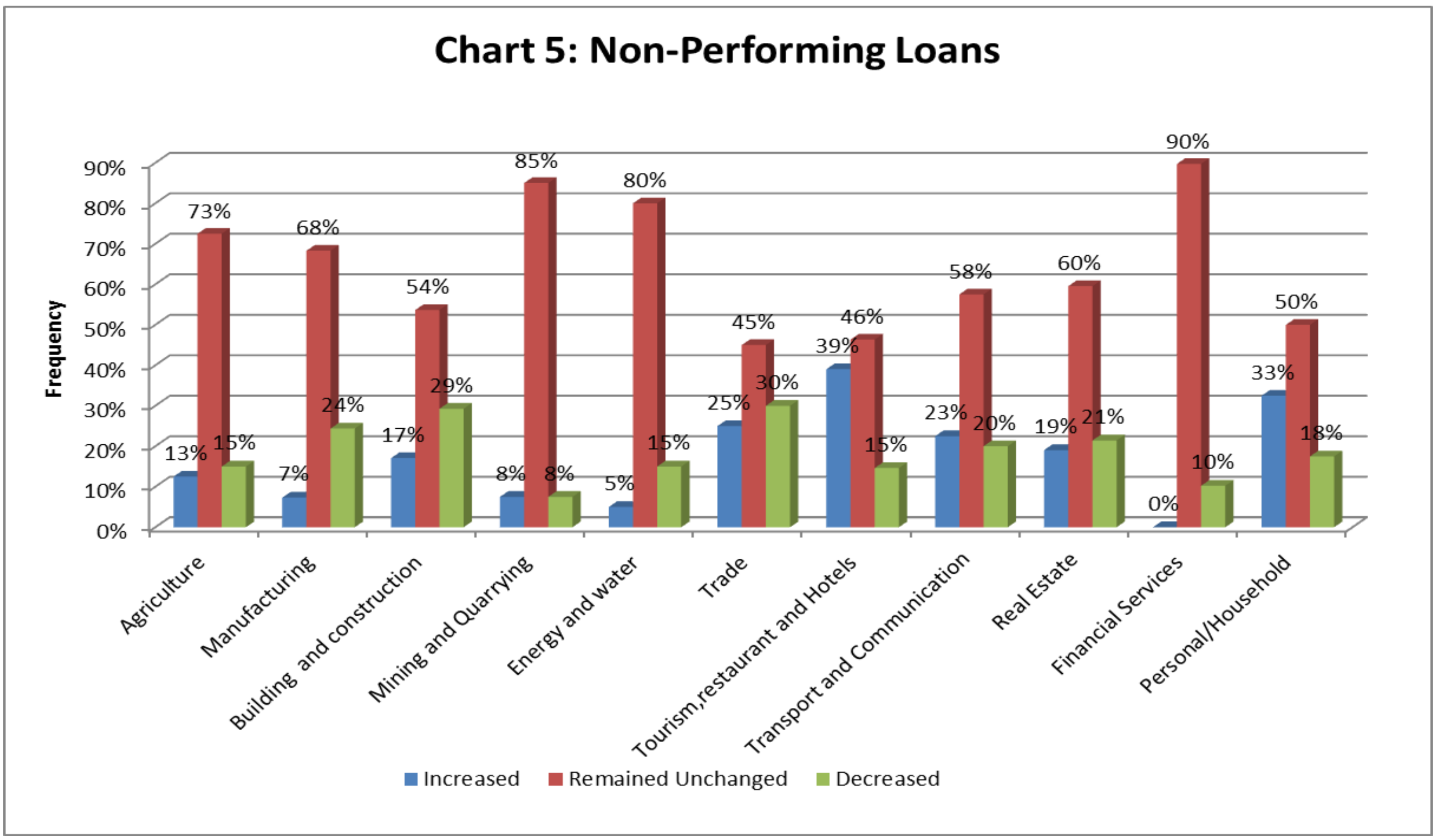

Table 5: Non Performing Loans Trend

	March 2015			December 2014		
	Rise	**Remained Constant**	**Fall**	**Rise**	**Remained Constant**	**Fall**
Agriculture	13%	73%	15%	10%	71%	20%
Manufacturing	7%	68%	24%	5%	66%	29%
Building & construction	17%	54%	29%	29%	44%	27%
Mining and Quarrying	8%	85%	8%	3%	80%	18%
Energy and water	5%	80%	15%	5%	75%	20%
Trade	25%	45%	30%	10%	63%	27%
Tourism, Restaurant & Hotels	39%	46%	15%	35%	48%	18%
Transport & Communication	23%	58%	20%	12%	63%	24%
Real Estate	19%	60%	21%	22%	59%	20%
Financial Services	0%	90%	10%	0%	85%	15%
Personal/Household	33%	50%	18%	32%	49%	20%

3.6 Credit Recovery Efforts

3.6.1 Observations

- In the quarter ending 30th June 2015, banks generally intend to increase their credit recovery efforts to improve the overall quality of their asset portfolio.
- Personal/Household, Tourism, Transport and Communication and Trade sectors are expected to witness the greatest recovery efforts in Q2 of 2015, with 68%, 66% and 61% (each for Transport and Trade sectors) of the respondents intensifying their recovery efforts. These are followed by the Real Estate, Building and Construction sectors with 52% each of the respondents increasing recovery efforts than in Q1 of 2015.
- The intensified recovery efforts in the Tourism, Building and Construction, Mining and Quarrying and Real Estate sectors are in line with the banks expectations that loan defaults in these sectors will rise during Q2 of 2015.
- Banks cite heightened political activity, the current spate of insecurity and pending Mining Bill in parliament as reasons for them to intensify credit recovery in the Tourism, Mining and Quarrying sectors. Delayed payments to contracts by the government may be attributed to intensified credit recovery efforts in the Building and Construction sector.

The responses on the expected credit recovery efforts by the banks during the quarter ending 31st March 2015 are depicted in **Chart 6** and **Table 6** below.

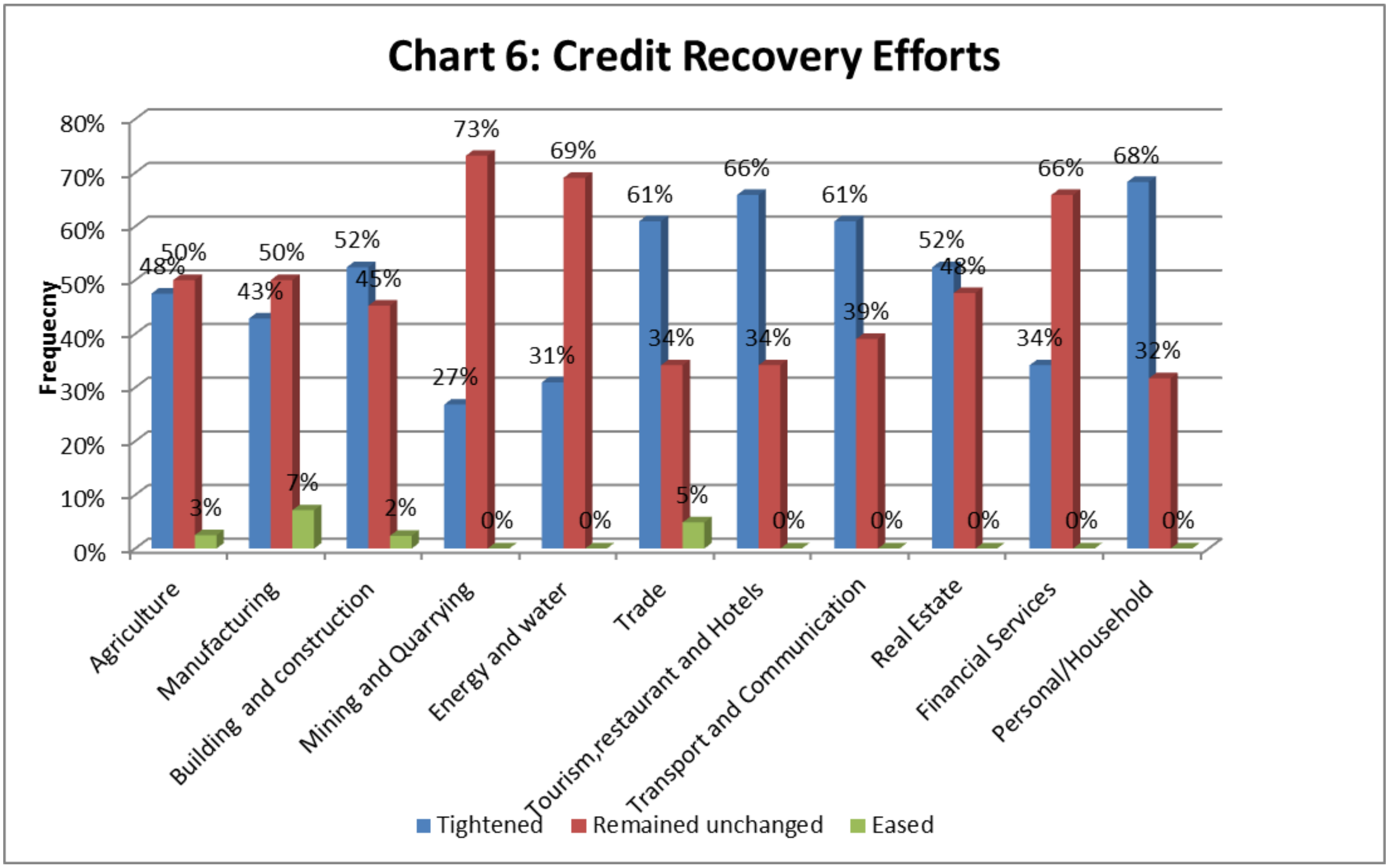

Table 6: Credit Recovery Efforts

	March 2015			December 2014		
	Intensified	**Remained Unchanged**	**Eased**	**Intensified**	**Remained Unchanged**	**Eased**
Agriculture	48%	50%	3%	49%	51%	0%
Manufacturing	43%	50%	7%	48%	50%	2%
Building & construction	52%	45%	2%	64%	33%	2%
Mining and Quarrying	27%	73%	0%	24%	76%	0%
Energy and water	31%	69%	0%	36%	60%	5%
Trade	61%	34%	5%	59%	41%	0%
Tourism, Restaurant & Hotels	66%	34%	0%	63%	37%	0%
Transport & Communication	61%	39%	0%	59%	41%	0%
Real Estate	52%	48%	0%	48%	52%	0%
Financial Services	34%	66%	0%	30%	70%	0%
Personal/Household	68%	32%	0%	73%	27%	0%

Annex I (List of Respondents)

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. Guaranty Trust Bank (Kenya) Ltd.
22. First Community Bank Limited.
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. Victoria Commercial Bank Ltd.
42. UBA Kenya Bank Ltd.
43. Housing Finance Ltd.