DEVELOPMENTS IN THE KENYAN BANKING SECTOR FOR THE QUARTER ENDED 30TH SEPTEMBER 2010

A. OVERVIEW OF THE BANKING SECTOR PERFORMANCE

During the quarter ended September 30, 2010, the sector comprised 43 commercial banks, 1 mortgage finance company, 2 deposit taking microfinance institutions, 2 representative offices of foreign banks and 126 foreign exchange bureaus.

The Kenyan Banking sector registered improved performance as indicated by the size of assets which stood at Ksh. 1.6 trillion, loans & advances worth Ksh. 879 billion, deposits of Ksh 1.3 trillion and profit before tax of Ksh. 53.2 billion as at 30th September 2010. Similarly, the number of bank customer deposit accounts stood at 11.14 million with a branch network of 1,030.

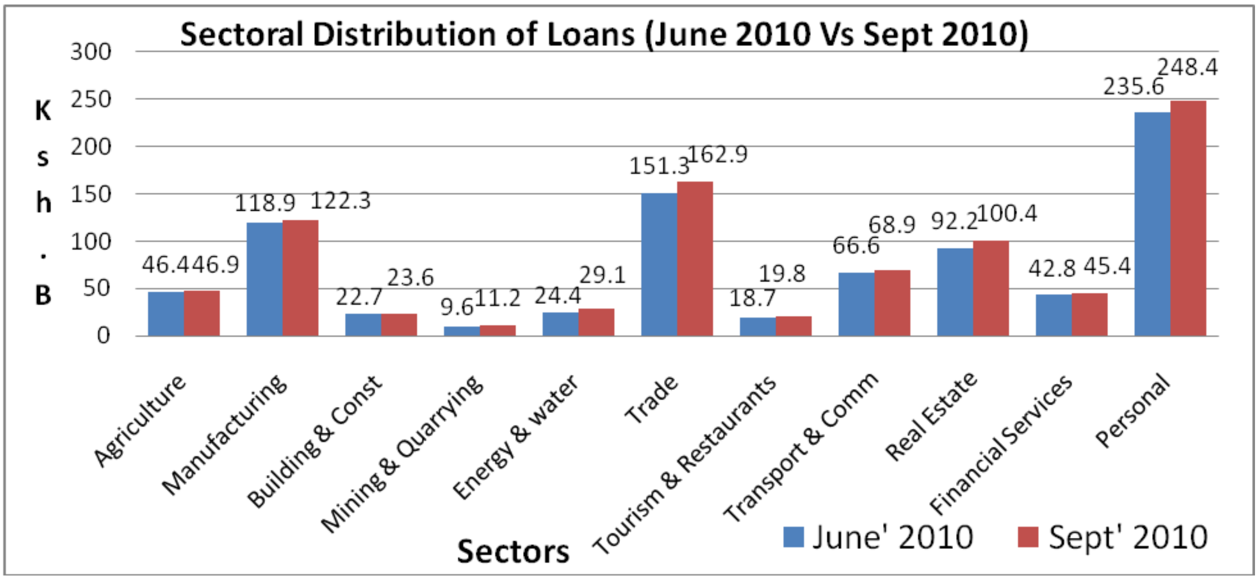
Structure of the Balance Sheet

i) Assets

The banking sector's aggregate balance sheet expanded by 5.5 percent from Ksh 1,548 billion in June 2010 to Ksh 1,638 billion in September 2010. The major components of the balance sheet were loans and advances, government securities and placements, which accounted for 50 percent, 27 percent and 6 percent of total assets respectively.

ii) Loans and Advances

The banking sector gross loans and advances increased from Ksh 828.9 billion in June 2010 to Ksh 878.8 billion in September 2010, translating to a growth of Ksh. 49.9 billion or 6.0 percent. The growth was mainly registered in households (Ksh 12.8 billion), trade (Ksh 11.6 billion) and real estate (Ksh 8.2 billion) sectors.



iii) Deposit Liabilities

Deposits from customers were the main source of funding for the banking sector, accounting for 78 percent of total funding liabilities. The deposit base increased by 4.2 percent from Ksh 1,219.5 billion in June 2010 to Ksh 1,270.6 billion in September 2010 mainly due to branch expansion, remittances and receipts from exports.

The number of bank branches increased by 13 from 1,017 in June 2010 to 1,030 in September 2010. Similarly, the number of bank deposit accounts increased from 10,065,903 in June 2010 to 11,142,450 in September 2010 representing a growth of 1,076,547 accounts or 10.7 percent.

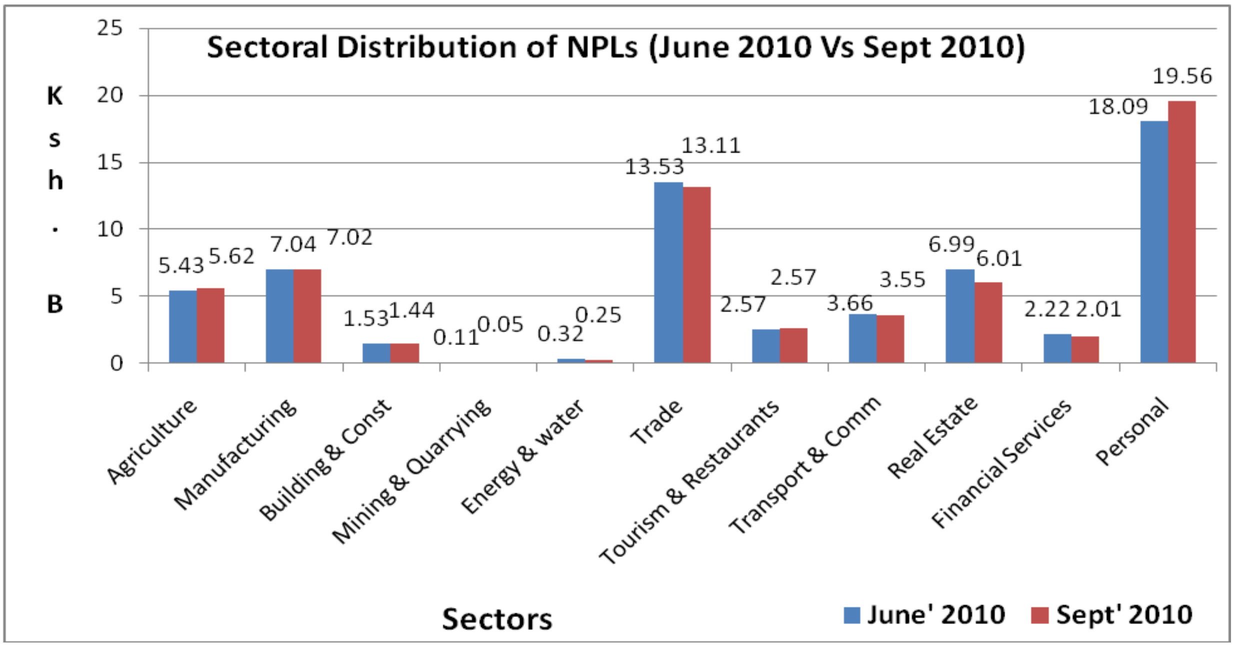
iv) Capital and Reserves

The banking sector registered strong capital levels in September 2010 with total capital growing by 9.8 percent from Ksh 191.1 billion in June 2010 to Ksh 209.9 billion in September 2010, whereas shareholders' funds increased by 11.6 percent from Ksh 222.3 billion in June 2010 to Ksh 248.1 billion. Similarly, the ratios of total and core capital to total risk-weighted assets increased from 19.6 percent and 17.5 percent to 20.6 percent and 18.6 percent respectively mainly due to a more than proportionate increase in core and total capital than the increase in total risk weighted assets. The growth in capital is attributed to profit retention and a rights issue by one bank during the quarter.

Other Banking Sector Performance Indicators

i) Assets Quality

The stock of gross non-performing loans (NPLs) declined by 0.5 percent from Ksh 61.5 billion in June 2010 to Ksh 61.2 billion in September 2010. The quality of assets, measured as a proportion of net non-performing loans to gross loans improved from 3.0 percent to 2.5 percent over the same period. Similarly, the ratio of gross NPLs to gross loans improved from 7.4 percent in June 2010 to 7.0 percent in September 2010.
The reduction in NPLs is attributed to enhanced appraisal standards deployed by financial institutions. Subsequently, reduction in NPLs was registered in 8 out of 11 sectors with higher decline being registered in real estate sector from Ksh 7.0 billion in June 2010 to Ksh 6.0 billion in September 2010.



ii) Profitability

The sector recorded a 2.2 percent growth in pre-tax profits, from 17.9 billion registered in the quarter ending June 2010 to Ksh 18.3 billion for the quarter ending September 2010. Total income went up by 7.3 percent from 51.8 billion in the June 2010 quarter to Ksh 55.6 billion in September 2010 quarter. Whilst total expenses increased by 10.0 percent from Ksh 33.9 billion in the June 2010 quarter to Ksh 37.3 billion in September 2010 quarter.

Interest on loans and advances, fees and commissions and government securities were the major sources of income accounting for 49 percent, 28 percent and 16 percent of total income respectively. On the other hand, staff costs, other expenses and interest on deposits were the key components of expenses, accounting for 34 percent, 29 percent and 28 percent respectively.

Consequently, the profits before tax for the nine months to September 2010 stood at Ksh 53.2 billion, which surpassed the twelve months profit before tax for the year ended December 2009 of Ksh 48.9 billion by 8.8 percent.

iii) Liquidity of the Banking Sector

As at end of September 2010, liquid assets amounted to Ksh 568.7 billion while total liquid liabilities stood at Ksh 1,219 billion, resulting to an average liquidity ratio of 46.7 percent, against 45.1 percent registered in June 2010, and above the minimum statutory limit of 20 percent. The high liquidity ratio is attributed to sustained uptake of government securities by banks which form liquid assets.

B. BANKING SECTOR POLICY DEVELOPMENTS

i) Credit Reference Bureaus

The credit sharing mechanism for institutions licensed under the Banking Act was rolled-out with effect from 31st July 2010. The roll-out followed the operationalization of the Banking (Credit Reference Bureau – CRB) Regulations, 2008 on 2nd February 2009. The CRB regulations amongst others provide for establishment, licensing and operations of banking sector credit reference bureaus. The Central Bank has so far licensed one credit reference bureau, CRBAfrica Limited, whereas three other applications are at various stages of being processed. Licensed CRBs collect and share credit information of institutions licensed under the Banking Act.

As at 30th September 2010, banks had requested for 103,332 credit reports. The uptake of credit reports by banks' is expected to increase as use of credit referencing is entrenched in banks' credit appraisal processes.

ii) Agency Banking:

Since the coming into operations of the Guidelines on Agent Banking in May 2010, six banks have applied to the CBK for Agent Network approval. Of these, two applications had been granted approval by end of September 2010, while the other four are at various stages of review. As at 30th September 2010, CBK had approved 5,892 agents of which 4,392 of these agents are telcom related with 1,500 comprising other types of enterprises. In addition, 66% of the approved agents are in the rural areas while the rest are in urban areas.

The introduction of agent banking is intended to enable institutions to provide banking services in a more cost effective way which is equally cheaper to the customers. It is further intended to enhance financial access especially for those people who are currently unbanked.

iii) Microfinance Institutions:

The gross loans and advances by the two licensed deposit taking microfinance institutions stood at Ksh. 14.9 billion translating to a growth of 5.7 percent from Ksh 14.1 billion registered in June 2010. Whilst the number of microfinance deposit accounts increased from 610,552 in June 2010 to 858,000 in September 2010 representing a growth of 247,448 accounts or 40.5 percent.

The micro-finance institutions also registered growth in deposits as at 30th September 2010 with Ksh. 7.2 billion in mobilized deposits, which represented a growth of 5.9 percent from Ksh. 6.8 billion in June 2010. The number of branches for microfinance institutions remained at 31 as at 30th September 2010.

Banking Sector 2010 Outlook:

The sector is expected to register higher performance in 2010 compared to performance registered in 2009. The performance in the fourth quarter of 2010 will largely be supported by credit referencing and agent banking among other initiatives being pursued by the Central Bank as well as the continued positive economic climate.