CENTRAL BANK OF KENYA

CREDIT OFFICER SURVEY

QUARTER ENDED MARCH 2013

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1.0 FOREWORD

1.1 KENYAN BANKING SECTOR PERFORMANCE

For the quarter ended 31st March 2013, the Kenyan Banking Sector demonstrated a continued growth though at a declining rate. Some of the sector's performance indicators for the quarter were as follows:

- The aggregate balance sheet increased by 2.55 percent from Kshs 2.35 trillion in December 2012 to Kshs 2.41 trillion in March 2013.
- Gross loans and advances expanded by 2.9 percent from Kshs 1.36 trillion in December 2012 to Kshs 1.40 trillion in March 2013.
- Deposits grew by 1.1 percent from to Kshs 1.76 trillion in December 2012 to Kshs 1.78 trillion in March 2013.
- Total shareholders' funds increased by 3.5 percent from Kshs 362.87 billion in December 2012 to Kshs 375.59 billion in March 2013.
- Unaudited pre-tax profits stood at Kshs 28.22 billion for the quarter ending 31st March 2013 compared to Kshs 24.66 billion for the quarter ending 31st March 2012, a 14.44% increase.

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 activity for most banks. The total percentage of loans to total assets for the period ended 31st March 2013 was 57%. In order to identify potential risks and enhance an understanding of credit risk, the Central Bank of Kenya introduced a quarterly Credit Officer Survey effective March 2012.

Out of the forty three questionnaires sent out, CBK received responses from all the institutions. The list of the respondents is attached to this report as **Annex I**.

Comparison of findings obtained in the quarter ended March 2013 and the quarter ended December 2012 reveals that:-

- Political risk had the most significant impact in reducing demand for credit, followed by issuance of debt securities by banks and internal financing using retained earnings.
- Credit standards were tightened for the tourism, restaurant and hotels, financial services and personal/household sectors.
- Banks expect NPLs in trade, tourism, restaurant & hotel and transport & communication sectors to fall for the quarter ending June 2013.
- Banks expect credit recovery efforts in agriculture, energy & water and financial services to be intensified for the quarter ending June 2013.

CENTRAL BANK OF KENYA
APRIL 2013

2.0 EXECUTIVE SUMMARY

2.1 SURVEY METHODOLOGY

The credit officer survey for the quarter ended March 2013 comprised four key questions that focused on the following aspects:-

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

The survey conducted in April 2013 targeted senior credit officers of all 42 operational commercial banks and 1 mortgage finance company. Charterhouse Bank Ltd, which is currently 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 decreased in all economic sectors in the quarter ended March 2013. Most institutions attributed the decrease to the political risk during the run up to the concluded elections in March 2013.

2.2.2 Credit Standards

In the quarter ended March 2013, there was generally no major change in credit standards in all the economic sectors. This could be informed by the already tightened credit standards adopted by most institutions in 2012 when high interest rates were witnessed.

2.2.3 Non-Performing Loans

For the quarter ending June 2013, most of the banks forecast an increase in NPLs in the building and construction sector (15 percent of the respondents), transport & communication sector (15 percent of the respondents) and real estate (12 percent of the respondents) sector. However, the institutions forecast a decrease in NPLs in the tourism, restaurant & hotels sector (58 per cent of the respondents) and trade sector (54% of the respondents).

2.2.4 Credit Recovery Efforts

Credit recovery efforts will be intensified in manufacturing, building and construction, transport and communication, real estate and personal/household sectors in the period April to June 2013. However, the credit recovery efforts on agriculture, mining and quarrying, energy and water and financial service sectors are expected to remain constant.

3.0 DETAILED SURVEY FINDINGS

3.1 Demand for Credit

3.1.1 Observations

It has been observed from the January to March 2013 credit survey that the demand for credit decreased in all sectors as depicted in **Chart 1** and **Table 1** below. Most institutions attributed this decrease to the political risk emanating from the just concluded elections which had created uncertainty in the business environment. However, the institutions have forecasted an increase in the demand for credit going forward, following the peaceful elections which have restored business confidence.

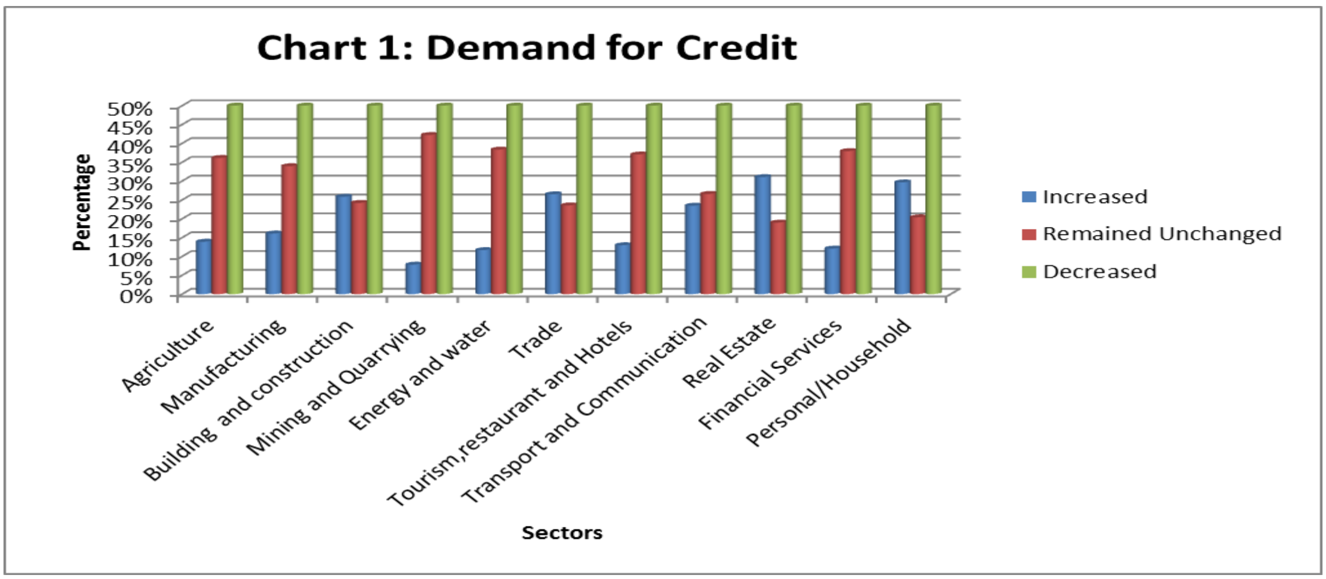

Table 1: Demand for Credit						
	March 2013			December 2012		
	Increased	Remained Unchanged	Decreased	Increased	Remained Unchanged	Decreased
Agriculture	14%	36%	50%	25%	58%	18%
Manufacturing	16%	34%	50%	51%	34%	15%
Building & construction	26%	24%	50%	55%	38%	8%
Mining and Quarrying	8%	42%	50%	12%	76%	12%
Energy and water	12%	38%	50%	34%	51%	15%

Table 1: Demand for Credit						
	March 2013			December 2012		
	Increased	Remained Unchanged	Decreased	Increased	Remained Unchanged	Decreased
Trade	26%	24%	50%	54%	37%	10%
Tourism, restaurant and Hotels	13%	37%	50%	26%	51%	23%
Transport and Communication	23%	27%	50%	46%	41%	12%
Real Estate	31%	19%	50%	51%	32%	17%
Financial Services	12%	38%	50%	36%	51%	13%
Personal/Household	30%	20%	50%	50%	28%	23%

The general decline of demand for credit in the quarter ending March 2013 was a reversal of the status in the quarter ending December 2012 which reported a general increase in the demand of credit in nine out of the eleven economic sectors. The increase in demand for credit in the last quarter of 2012 was mainly attributable to general optimism in the economy due to the fall in interest rates.

3.2 Factors affecting demand for credit

3.2.1 Observations

Comparing the last quarter of 2012 and quarter ending March 2013 indicates that political risk had the most significant impact in reducing demand for credit; followed by issuance of debt securities, loans from non-banks and internal financing. This is as shown in **Chart 2** and **Table 2** below. It is also notable that retention of the Central Bank Rate (CBR) at 9.5% in the quarter decreased volatility of funding costs, which translated to improved investor confidence. However, the then prevailing political risk associated with the March 2013 elections dampened demand for credit as investors delayed investment decisions until the political environment stabilized.

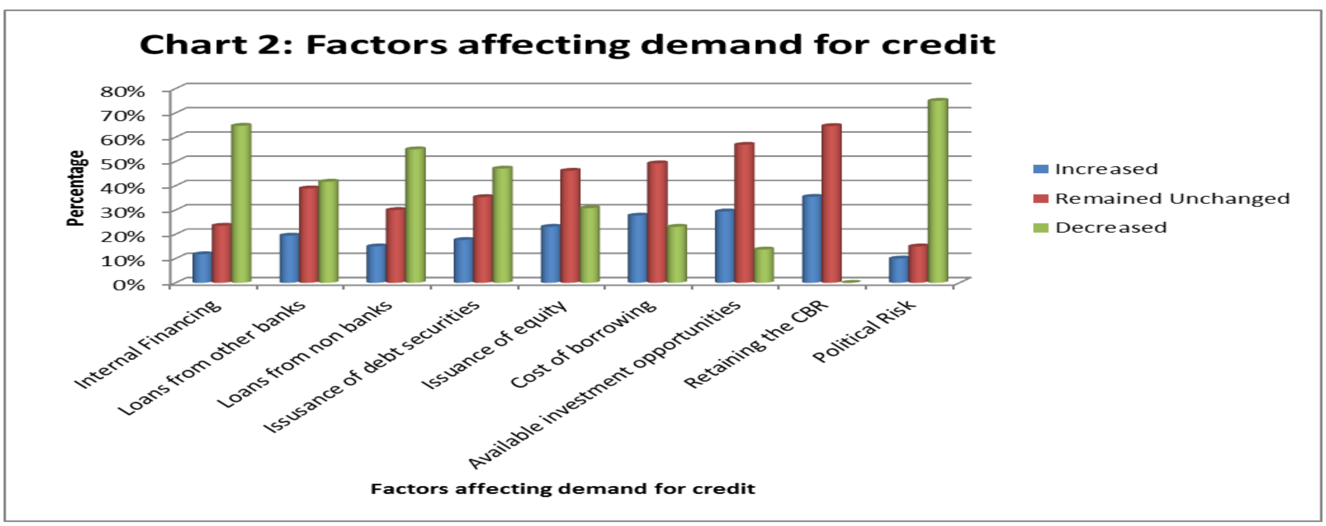

Table 2: Factors affecting Demand for credit

	March 2013			December 2012		
	Increased	Remained Unchanged	Decreased	Increased	Remained Unchanged	Decreased
Internal Financing	12%	24%	65%	13%	45%	43%
Loans from other banks	19%	39%	42%	17%	41%	41%
Loans from non-banks	15%	30%	55%	13%	65%	23%
Issuance of debt securities	18%	35%	47%	18%	66%	16%
Issuance of equity	23%	46%	31%	13%	71%	16%
Cost of borrowing	28%	49%	23%	54%	13%	33%
Available investment opportunities	29%	57%	14%	44%	44%	12%
Drop in CBR	35%	65%	-	74%	21%	5%
Political Risk	10%	15%	75%	12%	29%	59%

3.3 Credit Standards

3.3.1 Observations

In the quarter ended March 2013, there was generally no major change in credit standards in all the sectors. This could have been informed by the already tightened credit standards adopted by most institutions in 2012 during the high interest rates environment.

In comparison to December 2012, most institutions generally retained their credit standards to most of the sectors in both quarters though there was slight tightening of credit standards for energy and water, transport and communication, financial services, tourism, restaurant & hotels and personal/household sectors. **Chart 3** and **Table 3** below details the responses on credit standards in the quarter ended March 2013.

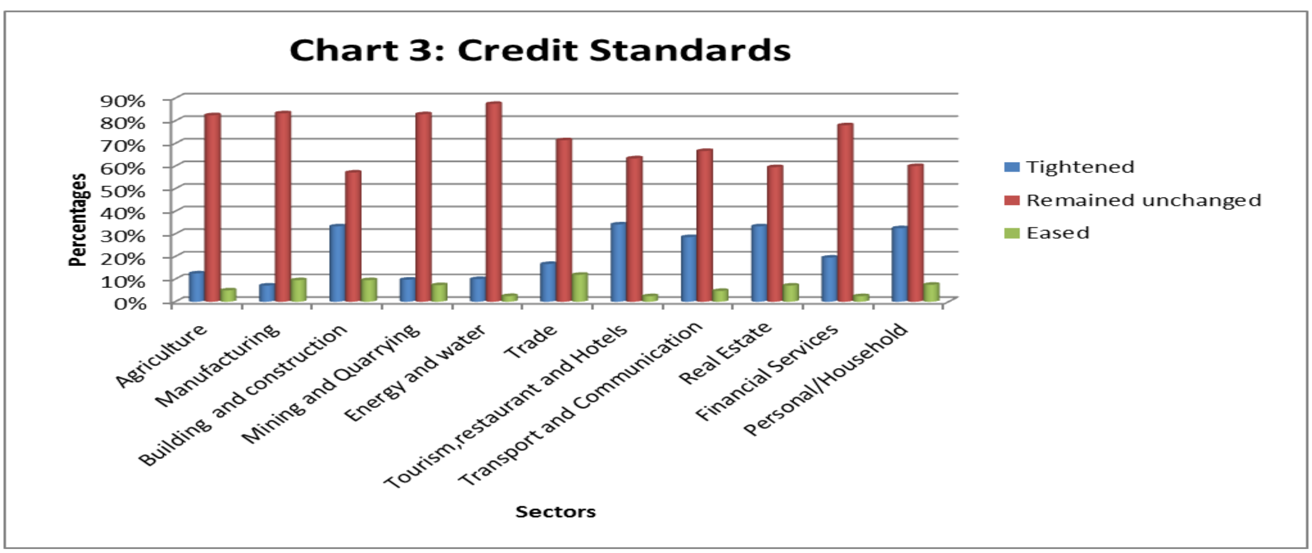

Table 3: Credit Standards

	March 2013			December 2012		
	Tightened	Remained Unchanged	Eased	Tightened	Remained Unchanged	Eased
Agriculture	13%	83%	5%	15%	70%	15%
Manufacturing	7%	83%	10%	12%	66%	22%
Building & Construction	33%	57%	10%	38%	53%	10%
Mining and Quarrying	10%	83%	7%	12%	73%	15%
Energy and water	10%	88%	3%	5%	80%	15%
Trade	17%	71%	12%	12%	61%	27%
Tourism, restaurant and Hotels	34%	63%	2%	14%	74%	12%
Transport and Communication	29%	67%	5%	22%	61%	17%
Real Estate	33%	60%	7%	34%	54%	12%
Financial Services	20%	78%	2%	5%	88%	8%
Personal/Household	33%	60%	8%	23%	64%	13%

3.4 Factors affecting credit standards

3.4.1 Observations

33 percent of the respondents reported that they eased their credit standards due to competition from other banks and expectations regarding general economic activity. Further, 54 per cent of the respondents citied political risk as the major factor that necessitated the tightening of their credit standards. Most of the banks reported that the other factors generally had no impact on their credit standards. The trend in factors affecting the banks' credit standards are indicated in **Chart 4** and **Table 4** below.

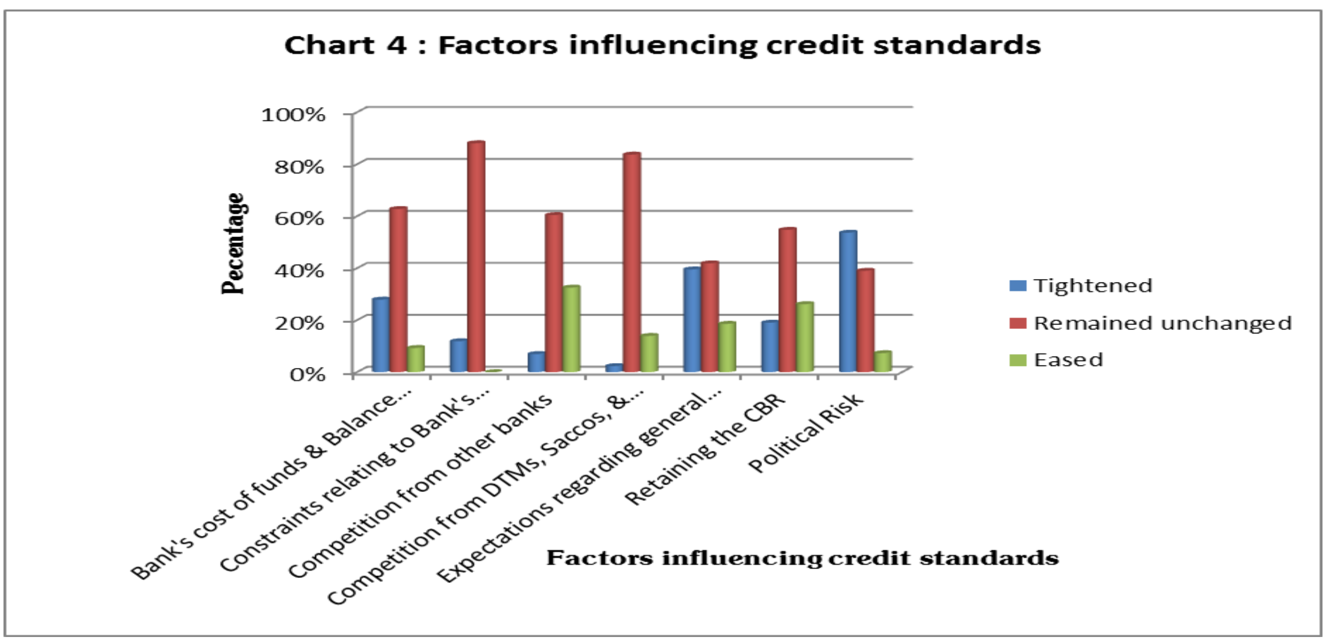

Table 4: Impact of factors affecting credit standards

	March 2013			December 2012		
	Tightened	Remained Unchanged	Eased	Tightened	Remained Unchanged	Eased
Bank's cost of funds & Balance sheet constraints	28%	63%	9%	45%	45%	10%
Constraints relating to Bank's capital position	12%	88%	0%	32%	66%	2%
Competition from other banks	7%	60%	33%	17%	66%	17%
Competition from DTMs, Saccos, & other Credit Providers	2%	84%	14%	7%	78%	15%
Expectations regarding general economic activity	40%	42%	19%	23%	62%	15%
Drop in Central Bank Rate (CBR)	19%	55%	26%	7%	51%	41%
Political Risk*	54%	39%	7%	-	-	-

* Political Risk as a factor affecting credit standards was introduced in the quarter ended March 2013 survey.

3.5 Non-Performing Loans (NPLs)

3.5.1 Observations

In the December 2012 credit survey, banks had forecasted an increase in NPLs in the trade, tourism, transport & communication, and real estate sectors in the quarter ended March 2013 due to expected increase in political risk. The March 2013 data on actual NPLs generally confirmed the banks forecast especially on the trade and real estate sectors. However, the March 2013 financial data revealed an increase of NPLs in personal/household sectors. For the quarter ending June 2013, institutions forecast that the NPLs will generally remain unchanged. However, some institutions forecast a decrease in NPLs in the tourism, restaurant & hotels sector (58 per cent of the respondents) and trade sector (54% of the respondents) following the just concluded peaceful elections.

It was noted that gross non-performing loans increased by 14.1 percent from Kshs 61.57 billion in December 2012 to Kshs 70.25 billion in March 2013.

Chart 5 and **Table 5** below indicate the banks expectations on NPL trend.

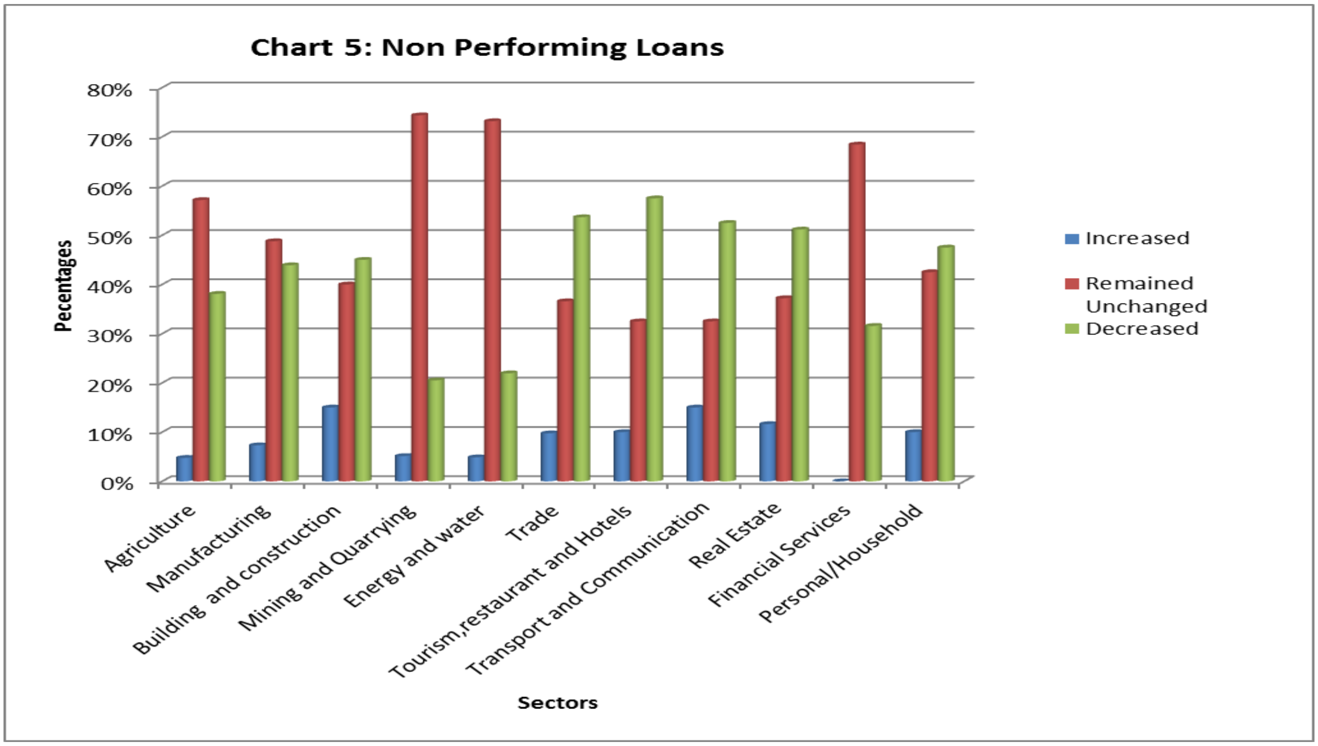

Table 5: Non Performing Loans Trend

	March 2013			December 2012		
	Rise	Remained Constant	Fall	Rise	Remained Constant	Fall
Agriculture	5%	57%	38%	13%	60%	28%
Manufacturing	7%	49%	44%	13%	55%	33%
Building & construction	15%	40%	45%	21%	49%	31%
Mining and Quarrying	5%	74%	21%	3%	74%	24%
Energy and water	5%	73%	22%	3%	69%	28%
Trade	10%	37%	54%	26%	46%	28%
Tourism, Restaurant & Hotels	10%	33%	58%	28%	48%	25%
Transport & Communication	15%	33%	53%	18%	56%	26%
Real Estate	12%	37%	51%	20%	51%	29%
Financial Services	0%	68%	32%	0%	77%	23%
Personal/Household	10%	43%	48%	38%	38%	25%

3.6 Credit Recovery Efforts

3.6.1 Observations

The banks expect to intensify their credit recovery efforts in manufacturing, building and construction, trade, transport and communication, real estate and personal/household sectors in the quarter ended June 2013. However, the credit recovery efforts towards agriculture, mining and quarrying, energy and water and financial service sectors are expected to generally remain constant. Some banks indicated that they intend to intensify credit recovery efforts so as to move towards less provisions and higher profitability. Others observed that their credit recovery efforts will remain unchanged as they continuously use credit reference bureaus when originating credit facilities, they also continuously monitor their loans books to identify early warning signs and others have also been using debt collection agents to fast track credit recovery.

The responses on the expected credit recovery efforts by the banks during the quarter ending June 2013 are indicated in **Chart 6** and **Table 6** below.

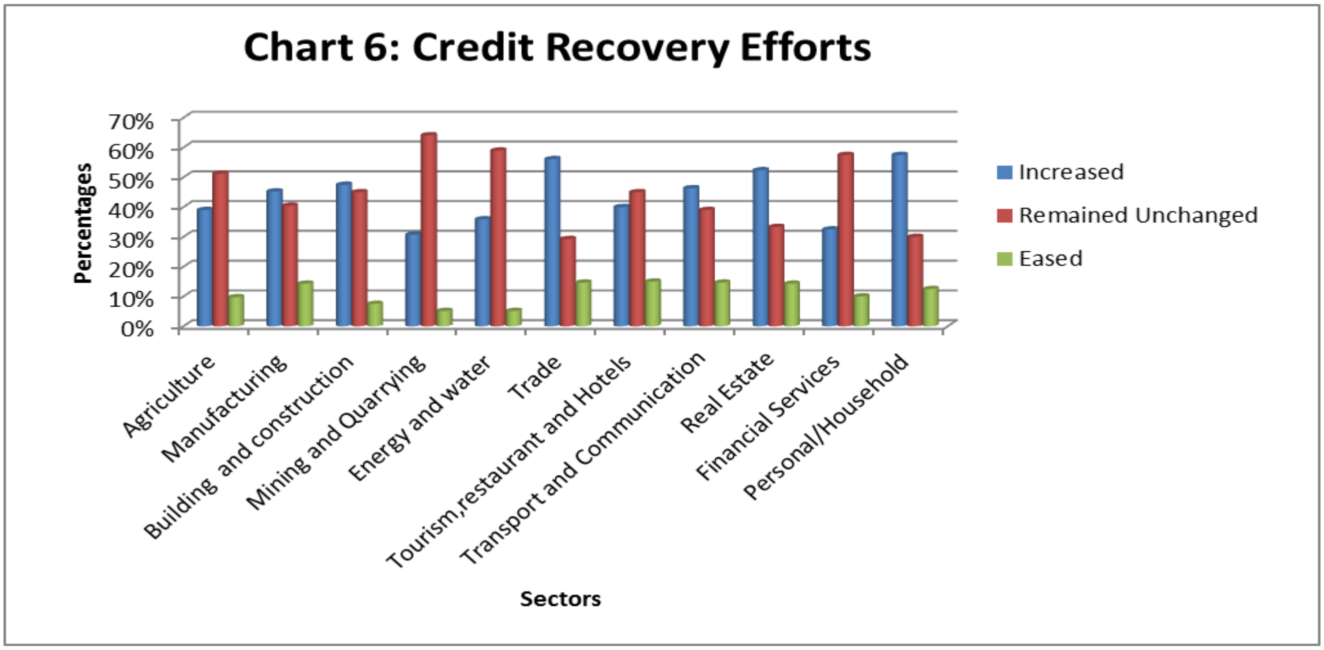

Table 6: Credit Recovery Efforts

	March 2013			December 2012		
	Intensified	Remained Unchanged	Eased	Intensified	Remained Unchanged	Eased
Agriculture	39%	51%	10%	28%	65%	8%
Manufacturing	45%	40%	14%	44%	49%	7%
Building & construction	48%	45%	8%	45%	48%	8%
Mining and Quarrying	31%	64%	5%	24%	68%	8%
Energy and water	36%	59%	5%	26%	63%	11%
Trade	56%	29%	15%	58%	35%	8%
Tourism, Restaurant & Hotels	40%	45%	15%	41%	49%	10%
Transport & Communication	46%	39%	15%	45%	48%	8%
Real Estate	52%	33%	14%	61%	37%	3%
Financial Services	33%	58%	10%	23%	69%	8%
Personal/Household	58%	30%	13%	63%	30%	8%

Annex I (List of Respondents)

LIST OF THE 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. Fina Bank 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.