DEVELOPMENTS IN THE KENYAN BANKING SECTOR FOR THE QUARTER ENDED 31ST MARCH 2013

A. OVERVIEW OF THE BANKING SECTOR PERFORMANCE

For the quarter ended March 31st, 2013, the sector comprised 43 commercial banks, 1 mortgage finance company, 8 deposit taking microfinance institutions, 7 representative offices of foreign banks, 108 foreign exchange bureaus and 2 credit reference bureaus.

The Kenyan Banking Sector registered improved performance with the size of assets standing at Ksh. 2.4. trillion, loans & advances amounting to Ksh. 1.4 trillion, while the deposit base stood at Ksh. 1.8 trillion and profit before tax of Ksh. 28.2 billion as at 31st March 2013. During the same period, the number of bank customer deposit and loan accounts stood at 17.3 million and 2.3 million respectively.

Structure of the Balance Sheet

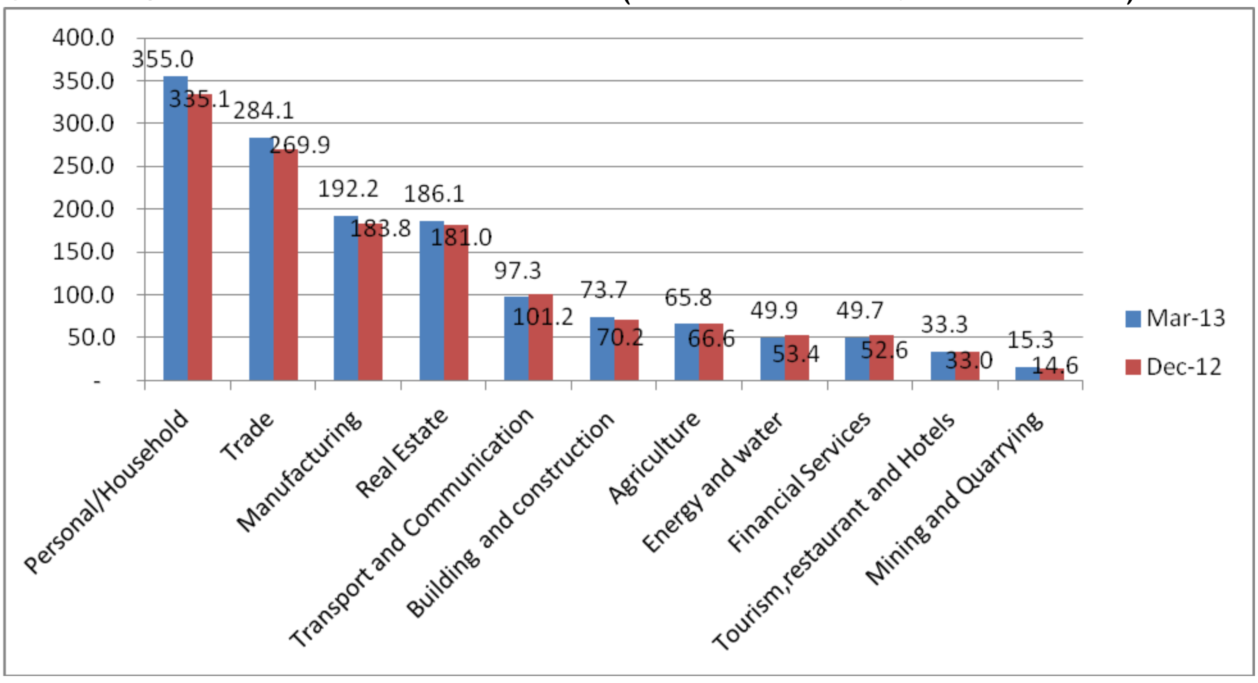
i) Assets

The banking sector's aggregate balance sheet expanded by 2.7 percent from Ksh. 2.35 trillion in December 2012 to Ksh. 2.42 trillion in March 2013. The major components of the balance sheet were loans and advances, government securities and placements, which accounted for 55.8 percent, 21.1 percent and 5.5 percent of total assets respectively.

ii) Loans and Advances

The sector's gross loans and advances increased from Ksh. 1.36 trillion in December 2012 to Ksh. 1.40 trillion in March 2013, which translated to a growth of 3.0 percent. The growth, which stood at Ksh. 40.0 billion, was in 7 sectors as shown in Chart 1 with 4 sectors registering a marginal decline occasioned by faster loan repayment rate compared with the rate at which new loans were being made in those sectors during the period.

Chart 1: Sectoral Distribution of Loans (December 2012 Vs March 2013)



iii) Deposit Liabilities

Deposits, which form the main source of funding for the banking sector, accounted for 73.5 percent of total funding liabilities. The deposit base grew by 0.8 percent from Ksh. 1.76 trillion in December 2012 to Ksh. 1.78 trillion in March 2013 mainly due to branch expansion, remittances and receipts from exports.

The number of deposit accounts increased from 15.9 million in December 2012 to 17.3 million in March 2013 representing a growth of 1.44 million accounts or 9.1 percent.

iv) Capital and Reserves

The banking sector registered improved capital levels in March 2013 with total capital growing by 6.7 percent from Ksh. 333.5 billion in December 2012 to Ksh. 355.7 billion in March 2013. Shareholders' funds increased by 3.5 percent from Ksh. 362.9 billion in December 2012 to Ksh. 375.6 billion in March 2013. Similarly, the ratio of total capital to total risk-weighted assets increased from 21.9 percent in December 2012 to 23.2 percent in March 2013 while core capital to total risk weighted assets increased from 18.9 percent to 20.3 percent over the same period.

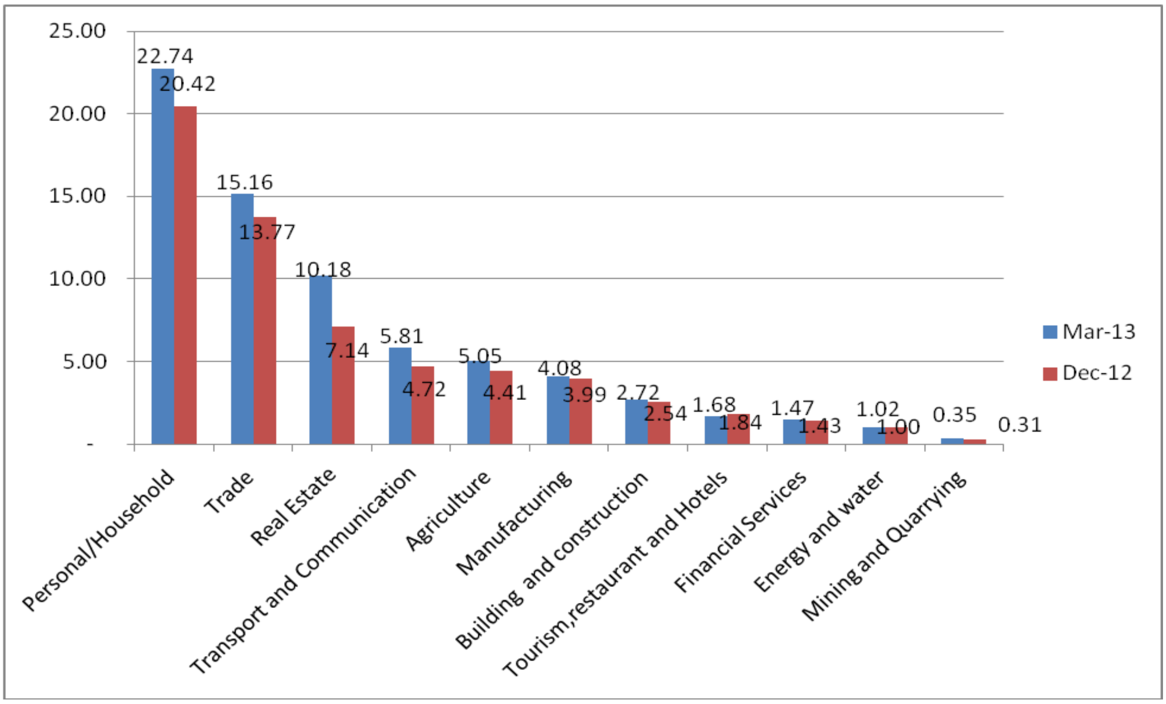
Other Banking Sector Performance Indicators

i) Assets Quality

The stock of gross non-performing loans (NPLs) increased by 14.1 percent from Ksh. 61.6 billion in December 2012 to Ksh. 70.3 billion in March 2013. The ratio of gross NPLs to gross loans increased from 4.5 percent in December 2012 to 5.0 percent in March 2013. The increase in the NPLs levels was mainly attributable to the spill-over effects of the high interest rates regime in 2011 and 2012. Similarly, the quality of assets, measured as a proportion of net non-performing loans to gross loans declined from 1.5 percent to 2.0 percent over the same period.

During the period under review, 10 out of 11 sectors registered increase in NPLs by Ksh. 8.7 billion with Tourism, Restaurants and Hotels being the only sector that registered a decline as shown in Chart 2 below.

Chart 2: Sectoral Distribution of NPLs (December 2012 Vs March 2013)



ii) Profitability

The banking sector profit before tax for the quarter ended March 2013 stood at Ksh. 28.2 billion representing an increase of 14.2 percent from the Ksh. 24.7 billion registered in the first quarter of 2012. Interest on loans and advances, fees and commissions and government securities, which are the major sources of income accounted for 62 percent, 17 percent and 13 percent of total income respectively. On the other hand, interest on deposits, staff costs and other expenses were the key components of expenses, accounting for 42 percent, 24 percent and 20 percent respectively.

iii) Liquidity of the Banking Sector

For the period ended March 2013, average liquid assets amounted to Ksh. 749.4 billion while total liquid liabilities stood at Ksh. 1,751.3 billion, resulting to an average liquidity ratio of 42.8 percent, against 41.9 percent registered in December 2012, and above the minimum statutory limit of 20 percent. The gross loans to deposits ratio increased from 77.3 percent in December 2012 to 79.0 percent in March 2013.

B. BANKING SECTOR POLICY DEVELOPMENTS

i) Credit Reference Bureaus

The Credit Information Sharing (CIS) mechanism, which was launched in July 2010, continues to be used by both commercial banks and individuals. The number of credit reports requested by institutions stood at 2,596,600 in March 2013 up from 2,321,766 reports in December

2012, representing an increase of 11.8 percent or 274,834 reports. Over the same period, the number of reports requested by customers increased from 28,733 to 35,172 reports.

The introduction of the credit information sharing mechanism has further strengthened credit appraisal standards. Banks have now incorporated credit reference reports in the credit risk appraisal. It is also expected that credit referencing will go a long way in inculcating credit discipline in borrowers.

ii) Agency Banking

As at 31st March 2013, there were 11 commercial banks that had contracted 18,082 active agents facilitating over 48.4 million transactions valued at Ksh. 250.1 billion. This was an increase from 10 banks that had contracted 16,333 active agents facilitating over 38.7 million transactions valued at Ksh. 195.8 billion in December 2012.

iii) Deposit Taking Microfinance Institutions

As at 31st March 2013, 8 Deposit Taking Microfinance Institutions (DTMs) were in operation and had gross loans worth Ksh. 21.2 billion compared to Ksh. 20.6 billion registered in December 2012 thus translating to a growth of 3.7 percent. Similarly, the deposits base stood at Ksh. 16.4 billion representing a growth of 6.4 percent from Ksh. 15.4 billion in December 2012. The long-term borrowings by DTMs increased from Ksh. 8.3 billion in December 2012 to Ksh. 8.8 billion in March 2013. The number of DTMs deposit accounts and loan accounts stood at 1.79 million and 0.47 million respectively in March 2013 compared to 1.76 million deposit accounts and 0.46 million loans accounts registered at end of December 2012.

iv) Revised Prudential and Risk Management Guidelines

The revised Prudential and Risk Management Guidelines issued in November 2012 came into effect in January 2013. Seven new Prudential Guidelines were issued covering various operating aspects of banks. These include Outsourcing, Representative Offices of Foreign Institutions, Voluntary Liquidation, Consolidated Supervision, Stress Testing, Prompt Corrective Action and Consumer Protection. In addition, the existing nine Risk Management Guidelines were reviewed while two new guidelines on Country and Transfer Risk and Information and Communication Technology Risk Management were introduced.

Banking Sector 2013 Outlook

The banking sector is expected to sustain its growth momentum on the backdrop of a stable macro-economic environment, and domestic and regional expansion by banks.