DEVELOPMENTS IN THE KENYAN BANKING SECTOR FOR THE PERIOD ENDED 30TH JUNE 2011

A. OVERVIEW OF THE BANKING SECTOR PERFORMANCE

During the period ended June 30th, 2011, the sector comprised of 43 commercial banks, 1 mortgage finance company, 6 deposit taking microfinance institutions, 2 credit reference bureaus, 3 representative offices and 124 foreign exchange bureaus.

The Banking Sector recorded improved performance as indicated by the size of assets which stood at Ksh. 1.9 trillion, loans and advances of Ksh. 1.1 trillion, deposits of Ksh.1.4 trillion and profit before tax of Ksh. 40.8 billion as at 30th June 2011. Equally, the number of bank customer deposit accounts stood at 12.8 million with a branch network of 1,102, while the bank loan accounts were 2.1 million.

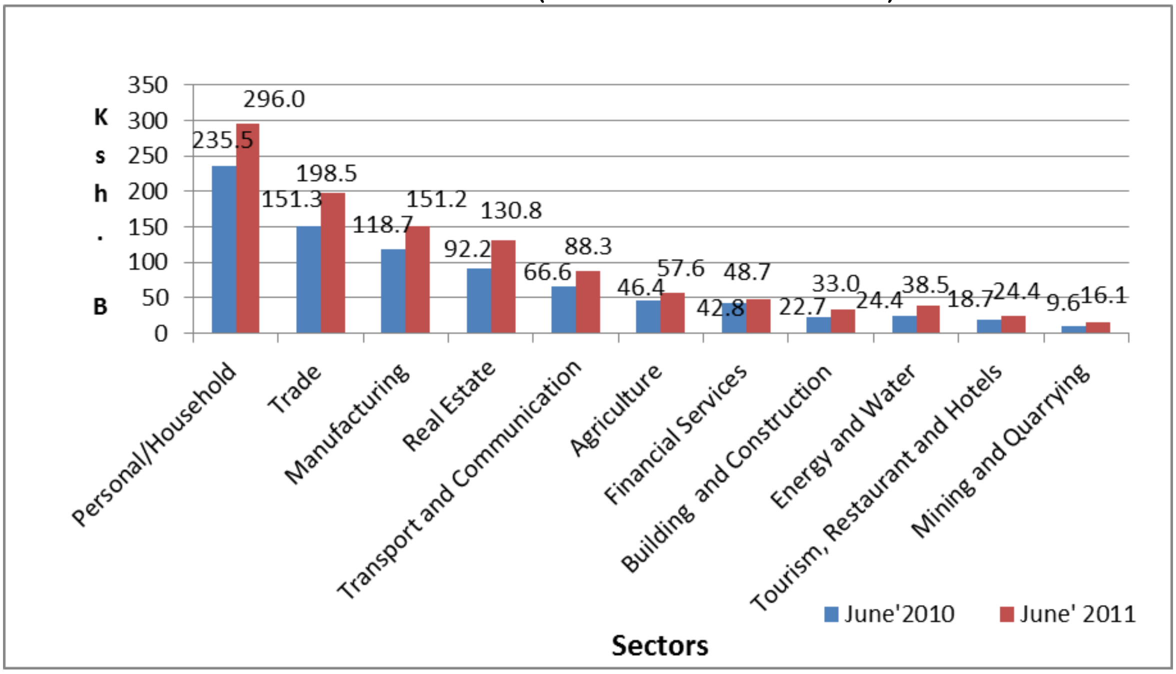
i) Structure of the Balance Sheet

The banking sector aggregate balance sheet grew by 26.7 percent from Ksh 1.5 trillion in June 2010 to Ksh 1.9 trillion in June 2011. The major components of the balance sheet were loans and advances, government securities and placements, which accounted for 55.0 percent, 22.0 percent and 6.0 percent of total assets respectively.

ii) Loans and Advances

The banking sector gross loans and advances grew from Ksh 828.9 billion in June 2010 to Ksh 1.1 trillion in June 2011, translating to a growth of 32.7 percent. The growth which was registered in all the 11 sectors was significant in personal/households, trade and manufacturing sectors. The sectoral distribution of loans is indicated in Chart 1 below:

Chart 1: Sectoral Distribution of Loans (June 2010 Vs June 2011)



iii) Deposit Liabilities

Deposits from customers were the main source of funding for the banking sector, accounting for 75.0 percent of total capital and funding liabilities. The deposit base increased by 16.7 percent from Ksh 1.2 trillion in June 2010 to Ksh 1.4 trillion in June 2011 mainly due to branch expansion, adaption of the agency banking model, remittances and receipts from exports.

The number of branches grew by 85 from 1,017 in June 2010 to 1,102 in June 2011. Over the same period, the number of bank deposit accounts increased from 10.1 million to 12.8 million representing a growth of 2.7 million accounts or 27 percent.

iv) Capital and Reserves

The banking sector registered strong capital levels in June 2011 with total capital increasing by 25.6 percent from Ksh 191.1 billion in June 2010 to Ksh 240.1 billion in June 2011, whereas shareholders' funds increased by 19.2 percent from Ksh 222.3 billion in June 2010 to Ksh 264.9 billion. However, the ratios of total and core capital to total risk-weighted assets declined from 19.6 percent and 17.5 percent to 19.0 percent and 16.9 percent respectively mainly due to higher growth in total risk weighted assets compared to growth in total and core capital.

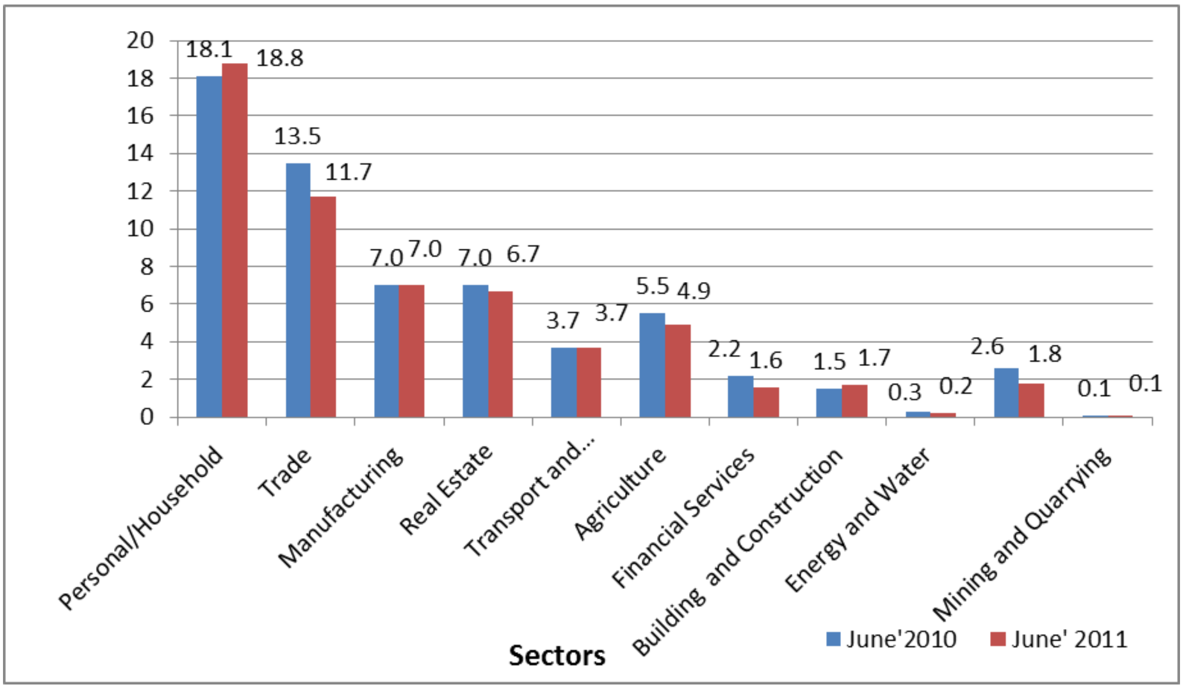
Other banking sector performance indicators

i) Assets Quality

The stock of gross non-performing loans (NPLs) reduced by 5.2 percent from Ksh 61.5 billion in June 2010 to Ksh 58.3 billion in June 2011. The quality of assets, measured as a proportion of net non-performing loans to gross loans improved from 2.3 percent to 1.3 percent over the same period. Similarly, the ratio of gross NPLs to gross loans improved from 7.4 percent in June 2010 to 5.4 percent in June 2011.

The reduction in NPLs is attributed to continued deployment of enhanced appraisal standards by the financial institutions. As a result, reduction in NPLs was registered in 6 out of 11 sectors with higher decline being recorded in trade sector from Ksh. 13.5 billion in In June 2010 to 11.7 billion in June 2011. The sectoral distribution of NPLs is set out in chart 2 below.

Chart 2: Sectoral Distribution of NPLs (June 2010 Vs June 2011)



ii) Profitability

In the six months to June 2011, the sector registered a 16.9 percent growth in pre-tax profits, from 34.9 billion in June 2010 to Ksh 40.8 billion as at end of June 2011. Total income went up by 8.7 percent from Ksh 101.5 billion in June 2010 to Ksh 110.3 billion in June 2011, while total expenses increased by 4.2 percent from Ksh 66.6 billion in June 2010 to Ksh 69.4 billion in June 2011.

Interest on loans and advances, fees and commissions and government securities were the major sources of income accounting for 54 percent, 23 per cent and 14 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 36 percent, 29 percent and 20 percent respectively.

iii) Liquidity

As at end of June 2011, liquid assets amounted to Ksh 522.2 billion while total liquid liabilities stood at Ksh 1.3 trillion, resulting in an average liquidity ratio of 38.9 percent, against 45.1 percent registered in June 2010, which remained above the statutory limit of 20 percent. The decline in liquidity is attributed to increased lending to the private sector.

B. BANKING SECTOR POLICY DEVELOPMENTS

i) Credit Reference Bureaus

The sharing of credit information which was launched in July 2010 is picking up gradually. As at 30th June 2011, there were 728,553 credit reports requested by institutions compared to 284,722 reports in December 2010. The uptake of credit reports by banks is expected to increase as use of credit referencing is entrenched in banks credit appraisal processes.

CBK granted Metropol Ltd a licence in April 2011 to operate as a credit reference bureau thus becoming the second bureau after CRBAfrica which was licensed in 2010.

ii) Agency Banking

The agency banking model which was rolled out in 2010 has drawn interest from the financial institutions. In February 2011, CBK granted approval to a commercial bank to roll out Agent Banking Network thus bringing the total approved banks to 6 as at 30th June 2011. Over the same period, 6,513 agents had been granted approval. The introduction of agent banking is intended to enable institutions to provide banking services more cost effectively to customers. It is expected that this initiative will enhance financial access for those people who are currently unbanked or under banked.

iii) Deposit Taking Microfinance Institutions

In June 2011, CBK granted a license to Rafiki DTM Ltd to commence nationwide deposit taking microfinance business, making it the sixth DTM to be licenced by CBK.

The gross loans and advances for the 5 DTMs that were operating at end of June 2011 stood at Ksh.15.2 billion compared to Ksh. 14.9 billion registered in December 2010 thus translating to a growth of 2.0 percent. Similarly, the deposits base stood at Ksh. 9.6 billion representing a growth of 20.0 percent from Ksh. 8.0 billion in December 2010. The number of deposit accounts stood at 1.4 million while the number of loan accounts were 0.5 million.

iv) Representative Offices

In March 2011, CBK granted approval to the Hongkong Shanghai Banking Corporation Ltd (HSBC) to open a representative office in Kenya. HSBC becomes the third bank to be granted approval for a representative office after HDFC Bank (India) and Nedbank (South Africa).

Banking Sector 2011 Outlook

The sector is expected to continue with its growth momentum into the second half of 2011. The momentum will be sustained by opportunities in regional markets and enhanced outreach through innovations in delivery channels.