BANK OF GHANA

Banking Sector Report

MARCH 2019

CONTENTS

1. PREFACE

The Bank of Ghana's Banking Sector Report is published after each Monetary Policy Committee (MPC) meetings. The report highlights developments in the banking sector which were deliberated on during the policy making process. The aim of publishing the report is to provide the public with information on performance of the banking sector which served as inputs for the MPC meetings. Through the publication of these documents, Bank of Ghana aims to promote accountability of its decision making and build understanding of the monetary policy formulation process among stakeholders.

Monetary Policy Formulation in Ghana

Objective

The primary objective of the Bank of Ghana is to pursue sound monetary policies aimed at price stability and creating an enabling environment for sustainable economic growth. Price stability in this context is defined as a medium-term inflation target of 8 percent with a symmetric band of 2 percent. This implies that annual changes in the Consumer Price Index (CPI) should range between 6 and 10 percent over the medium term for the economy to grow at its full potential without excessive inflation pressures. Other tasks for the Bank of Ghana include promoting and maintaining a sound financial sector and payment systems through effective regulation and supervision. This is important for financial intermediation and to ensure that risks associated with financial markets are not escalated and transmitted to the rest of the economy.

Monetary Policy Strategy

To achieve the objective of price stability, Bank of Ghana was granted operational independence to employ whichever policy tools were deemed appropriate to stabilise inflation around the target band. The Bank of Ghana's framework for conducting monetary policy is Inflation Targeting (IT) which allows the central bank to use the Monetary Policy Rate (MPR) as the primary policy tool to set the monetary policy stance and anchor inflation expectations in the economy.

The Monetary Policy Process

The MPC is a statutorily constituted body by the Bank of Ghana Act to formulate monetary policy. The MPC consists of seven members – five from the Bank of Ghana, including the Governor who acts as the Chairman, and two external members appointed by the Board of Bank of Ghana. The MPC meets once in every two months to assess economic conditions and risks to the inflation outlook, after which a policy decision is made on positioning the MPR. Each MPR decision provides a signal of tightening (increase), loosening (decrease) or maintaining (no change) the monetary policy stance. The MPC meeting dates are determined well in advance at the beginning of each year. The policy decision is arrived at by consensus with each member stating reasons underlying a preferred rate decision. An MPC policy statement is published via a press release, and a press conference is held after each MPC meeting to communicate and explain the decision of the Committee to the financial markets and the general public.

2. SUMMARY

This report covers developments in Ghana's banking sector during the first two months of 2019 compared with the same period last year. Following the completion of the recent reforms and recapitalization exercise, the industry currently comprises twenty three (23) banks, fourteen (14) of which are foreign-controlled with the remaining nine (9) being domestically-controlled. The branch network of banks across the sixteen (16) regions of the country stood at 1,225 branches as at end-February 2019, from 1,546 as at end-February 2018, also reflecting bank consolidations and the resulting branch rationalisation within the industry.

The performance of the recapitalized industry was stronger during the first two months, pointing to a profitable, liquid and solvent sector with strong growth prospects. Growth in the industry's total assets was robust, with year-on-year growth of 14.5 percent as at end-February 2019, funded largely by increased deposits and equity injection from the recapitalization exercise. The growth in the total assets reflected a rebound in gross advances after contracting a year ago, while the rate of increase in investments remained virtually unchanged from that of the previous year. The industry also posted stronger profit-after-tax during the first two months of 2019 compared with the corresponding period in 2018. The improved profitability performance was on the back of higher growth in net interest income and lower growth in operational expenses and provisions.

The key Financial Soundness Indicators (FSIs) broadly strengthened in February 2019 in line with the industry's improved financial performance. The two main profitability indicators, namely, Return on Equity (ROE) and Return on Assets (ROA) recorded significant improvements during the period under review. The industry's Capital Adequacy Ratio (CAR) went up from 19.2 percent in February 2018 to 21.7 percent in February 2019 reflecting the capital injection by the banks. This is well above the prudential requirement of 10.0 percent. The quality of banks' capital also improved, indicated by a sharp increase in the industry's Tier 1 CAR from 15.9 percent to 20.6 percent over the same period. The improved solvency enhances the industry's capacity to deepen financial intermediation as well as withstand shocks going forward. Asset quality improved with the decline in the Non-Performing Loans (NPL) ratio from 21.6 percent in February 2018 to 18.2 percent in February 2019. The industry also remained adequately liquid evidenced by improvements in broad liquidity indicators. Efficiency measures also broadly improved with the potential of translating into lower costs of banking services and charges.

The outlook for the banking sector is positive with strong growth prospects in credit, deposit mobilisation, and product innovation. However, the key risk the sector faces remains the high stock of non-performing loans which has contributed to high risk premiums, partly accounting for the stickiness in lending rates. The Bank expects that enforcement of the loan write-off policy and strengthening of risk management practices by banks will further impact positively on the industry's asset quality going forward.

3. BANKING SECTOR DEVELOPMENTS

3.1 Banks' Balance Sheet

Total assets of the banking sector grew by 14.5 percent year-on-year to GH¢108.90 billion at end-February 2019, higher than the 13.7 percent growth in a corresponding period in 2018. The higher growth in the industry's total assets reflected increases in both domestic and foreign assets. While growth in domestic assets increased from 14.9 percent in February 2018 to 15.2 percent in February 2019, growth in foreign assets increased from 3.5 percent to 6.9 percent during the same period. The share of domestic assets in total assets also increased marginally in February 2019 to 91.5 percent from 90.9 percent a year earlier, resulting in a marginal decline in the share of foreign assets from 9.1 percent to 8.5 percent during the period under review.

Banks' investment in bills and securities increased from GH¢32.59 billion at end-February 2018 to GH¢43.45 billion at end-February 2019, representing a year-on-year growth of 33.3 percent, similar to the 33.6 percent growth for same period in 2018. It is worth noting that growth in investments partly reflected the issuance of bonds by Government to finance the gap between the liabilities and good assets of the defunct banks absorbed by the Consolidated Bank Ghana (CBG). There is however a continuous shift in the investment portfolio mix of banks in favour of longer-dated instruments. Banks' investments in short term bills accordingly showed a further decline of 18.6 percent to GH¢14.22 billion at end-February 2019, much higher than the 6.1 percent contraction recorded in February 2018. Investments in long term securities on the other hand almost doubled from GH¢14.69 billion to GH¢28.82 billion during the period, albeit lower than the 174.8 percent growth recorded a year ago.

Gross advances inched up by 1.9 percent from GH¢35.76 billion to GH¢36.44 billion in February 2019, after contracting by 0.6 percent a year ago.[1] Banks' advances excluding provisions and interest in suspense (Net advances) rebounded from a -2.8 percent year-on-year growth in February 2018 to GH¢31.82 billion, representing a 4.8 percent growth in February 2019. Growth in foreign currency loans growth also recovered, largely reflecting the sharp cedi depreciation recorded over the two periods which contributed to the observed higher growth of 32.6 percent, from GH¢8.57 billion in February 2018 to GH¢11.37 billion in February 2019..

Investments remained the largest component of banks' assets constituting 39.9 percent as at February 2019 compared with 34.3 percent a year ago. The share of gross advances in total assets declined during the period under review from 37.6 percent to 33.5 percent reflecting the impact of the loans under receivership. Non-earning assets, namely, other assets and fixed assets both contracted in February 2019 compared with February 2018, suggesting greater efficiency in asset allocation. Fixed assets contracted by 2.2 percent in February 2019 from the 41.7 percent growth in February 2018, partly due to rationalisation of bank branches by GCB and CBG, following the acquisition of the defunct banks. Other assets also contracted by 5.0 percent from a growth of 13.5

[1] The marginal growth is due to the exclusion of the stock of loans and advances of the seven (7) defunct banks under receivership.

percent during the same comparative period. Accordingly, their combined share in total assets dipped from 8.8 percent to 7.3 percent over the period.

Deposits growth was more robust, increasing from an annual growth of 12.6 percent in February 2018 (GH¢59.90 billion) to 20.0 percent in February 2019 (GH¢71.86 billion), reflecting renewed confidence in the banking sector following the recent clean-up and recapitalization reforms. The growth in banks' deposits was broad-based, with both domestic currency and foreign currency deposits outperforming previous year's performance. Foreign currency deposits rebounded from a 1.1 percent contraction in February 2018 (GH¢14.92 billion) to record a 26.6 percent growth (GH¢18.89 billion) in February 2019, albeit partly due to the depreciation of the Ghana Cedi during the period. In the same vein, the deposits of non-residents increased by 33.4 percent to GH¢469.40 million in February 2019, reversing the 8.9 percent decline recorded a year ago. Domestic deposits, the largest component of total deposits, also witnessed an improved growth from GH¢59.55 billion (12.7% y/y growth) to GH¢71.39 billion (19.9% y/y growth) during the review period. Accordingly, total deposits assumed an increased share of the banking sector's pool of funds from 63.0 percent to 66.0 percent during the period under review.

With the strong growth in deposits, banks reduced their reliance on borrowings to fund their assets. Total borrowings declined by 6.3 percent from GH¢15.20 billion in February 2018 to GH¢14.24 billion in February 2019. The contraction in total borrowings stemmed from sharp declines in domestic borrowings (both short-term and long-term), which was partially offset by the growth in foreign borrowings. Short-term and long-term domestic borrowings declined by 39.9 percent and 45.9 percent respectively to GH¢5.91 billion and GH¢728.80 million at end-February 2019. On the other hand, both short-term and long-term foreign borrowings increased by 146.0 percent and 41.1 percent respectively to GH¢4.53 billion and GH¢3.08 billion over the same comparative period. It is worth noting that while foreign borrowings increased in nominal terms, it partly reflected the currency depreciation. Overall, the share of external funding for banks (comprising foreign borrowing and deposits of non-residents) increased from 4.6 percent to 7.4 percent while domestic funding (domestic borrowing and domestic deposits, excluding capital) declined from 81.1 percent to 77.9 percent over the same period.

Paid-up capital grew strongly by 78.4 percent, from GH¢5.05 billion to GH¢9.02 billion over the period as expected, following the completion of the recapitalization exercise and capital verification processes. Total shareholders' funds (paid-up capital and reserves) also grew by 18.0 percent in February 2019 to GH¢15.95 billion. The ratio of shareholders' funds in the industry's funding sources inched up marginally from 14.2 percent to 14.6 percent, with the share of paid-up capital increasing from 5.3 percent to 8.3 percent over the two comparative periods. Other liabilities recorded a slower growth of 5.4 percent in February 2019 to GH¢6.85 billion, partly due to the consolidation within the industry after the reforms. In terms of shares, other liabilities constituted 6.3 percent in February 2019 compared to 6.8 percent a year ago. In sum, the industry's balance sheet performance was stronger in February 2019 than it was a year ago with a pick-up in asset growth, funded by strong growth in deposits and paid-up capital.

Table 1: Key Developments in DMBs' Balance Sheet

	GH¢ million				Y-on-Y Growth (%)			Shares (%)		
	Feb-17	Feb-18	Dec-18	Feb-19	Feb-18	Dec-18	Feb-19	Feb-18	Dec-18	Feb-19
TOTAL ASSETS	**83,632.2**	**95,122.4**	**105,115.3**	**108,903.6**	**13.7**	**12.3**	**14.5**	**100.0**	**100.0**	**100.0**
A. Foreign Assets	8,342.4	8,631.0	8,663.2	9,227.7	3.5	9.6	6.9	9.1	8.2	8.5
B. Domestic Assets	75,289.8	86,491.3	96,452.0	99,675.9	14.9	12.5	15.2	90.9	91.8	91.5
Investments	24,389.0	32,593.5	38,164.8	43,446.2	33.6	33.6	33.3	34.3	36.3	39.9
i. Bills	18,618.9	17,478.4	12,371.3	14,220.9	(6.1)	(24.5)	-18.6	18.4	11.8	13.1
ii. Securities	5,344.9	14,690.3	25,390.7	28,820.6	174.8	115.8	96.2	15.4	24.2	26.5
Advances (Net)	31,254.5	30,371.1	31,790.4	31,815.9	(2.8)	1.0	4.8	31.9	30.2	29.2
of which Foreign Currency	9,110.7	8,571.4	9,971.2	11,367.5	(5.9)	15.5	32.6	9.0	9.5	10.4
Gross Advances	35,976.0	35,758.0	36,496.9	36,435.5	(0.6)	(3.5)	1.9	37.6	34.7	33.5
Other Assets	3,578.0	4,062.7	3,642.8	3,857.8	13.5	(26.8)	-5.0	4.3	3.5	3.5
Fixed Assets	2,997.0	4,245.7	4,068.9	4,152.4	41.7	(2.3)	-2.2	4.5	3.9	3.8
TOTAL LIABILITIES AND CAPITAL	**83,632.2**	**95,122.4**	**105,115.3**	**108,903.6**	**13.7**	**12.3**	**14.5**	**100.0**	**100.0**	**100.0**
Total Deposits	53,205.5	59,898.6	68,289.7	71,863.4	12.6	17.3	20.0	63.0	65.0	66.0
of which Foreign Currency	15,081.1	14,920.7	16,788.1	18,889.2	(1.1)	14.1	26.6	15.7	16.0	17.3
Total Borrowings	13,863.0	15,199.7	14,827.0	14,239.0	9.6	(12.4)	-6.3	16.0	14.1	13.1
Foreign Liabilities	4,361.1	4,372.2	7,555.7	8,071.1	0.3	64.6	84.6	4.6	7.2	7.4
i. Short-term borrowings	2,076.2	1,839.6	4,331.5	4,525.4	(11.4)	79.8	146.0	1.9	4.1	4.2
ii. Long-term borrowings	1,898.5	2,180.7	2,852.2	3,076.3	14.9	59.2	41.1	2.3	2.7	2.8
iii. Deposits of non-residents	386.4	351.8	372.1	469.4	(8.9)	(4.6)	33.4	0.4	0.4	0.4
Domestic Liabilities	67,685.9	77,165.1	82,754.6	84,858.6	14.0	7.8	10.0	81.1	78.7	77.9
i. Short-term borrowing	8,534.9	9,832.0	6,765.4	5,908.5	15.2	(40.7)	-39.9	10.3	6.4	5.4
ii. Long-term Borrowings	1,353.5	1,347.3	878.0	728.8	(0.5)	(33.9)	-45.9	1.4	0.8	0.7
iii. Domestic Deposits	52,819.1	59,546.7	67,917.6	71,394.0	12.7	17.5	19.9	62.6	64.6	65.6
Other Liabilities	4,999.0	6,503.4	7,291.0	6,851.9	30.1	17.4	5.4	6.8	6.9	6.3
Paid-up capital	4,135.1	5,053.1	8,639.4	9,014.8	22.2	88.7	78.4	5.3	8.2	8.3
Shareholders' Funds	11,546.2	13,516.1	14,702.5	15,949.3	17.1	19.8	18.0	14.2	14.0	14.6

3.1.1 Asset and Liability Structure

The reallocation of banks' assets in favour of investments (bills and securities) observed in 2018 continued into the first two months of 2019 with the share of investments increasing to 39.9 percent from 34.3 percent in the corresponding period in 2018, while the share of net advances declined to 29.2 percent from 31.9 percent during the same comparative period. The share of Cash and Due from Banks also declined from 24.9 percent in February 2018 to 23.5 percent in February 2019 [See Annexes Table 1]. Similarly, the shares of fixed assets and other assets also moderated from respective levels of 4.5 percent and 4.3 percent to 3.8 percent and 3.5 percent during the period under review. On account of the enhanced solvency position and strong deposit growth, the share of net advances in total assets is expected to pick up going forward.

The share of total deposits in banks' liabilities increased during the period under review, from 63.0 percent in February 2018 to 66.0 percent in February 2019 reflecting renewed confidence in the well-capitalised sector. Banks' reliance on debt financing moderated with a decline in the share of total borrowings from 16.6 percent to 13.1 percent during the review period. Shareholders' funds constituted an increased share of 14.6 percent of the industry's liabilities and capital in February 2019 compared with 13.8 percent in the comparative period last year, while other liabilities accounted for 6.3 percent from 6.0 percent during the same review period [See Annexes Table 1].

3.1.2 Share of Banks' Investments

Banks reallocated their investments in favour of longer term securities which constituted an increased share of 66.3 percent in February 2019 from 45.1 percent in February 2018. The increase in the share of long term securities in banks' investments was also contributed in part by the issuance of the Government of Ghana bonds to offset the gap between the assets and liabilities of banks absorbed by CBG following their resolution. The share of short term bills in banks' investment portfolio accordingly declined from 53.6 percent to 32.7 percent, while the proportion of the industry's investments in shares and other equities also dipped from 1.3 percent to 0.9 percent.

3.2 Credit Risk

The risk associated with the industry's loans tapered in February 2019 compared with the same period last year on the back of the implementation of Bank of Ghana's loan write-off policy. As banks continue to align their credit risk frameworks with the Capital Risk Directive issued by the Bank of Ghana in 2018, the credit risk exposure is expected to decline even further with implications for improved profitability and credit growth.

3.2.1 Credit Portfolio Analysis

Gross loans and advances (excluding loans under receivership) was GH¢36.44 billion in February 2019, representing a modest nominal growth of 1.9 percent from the 0.6 percent contraction in February 2018.[2] In real terms, the contraction in gross loans and advances slowed from 10.1 percent in February 2018 to 6.7 percent in February 2019. The stock of credit to the private sector (comprising private enterprises and households) grew moderately in nominal terms by 0.2 percent to GH¢33.23 billion in February 2019 from GH¢33.15 billion (-0.2% nominal y/y growth) in February 2018. In real terms, private sector credit contracted by 8.2 percent in February 2019 compared with 9.8 percent a year ago. Credit to households recorded a slower growth of 1.3 percent in February 2019 to GH¢ 7.01 billion from GH¢6.92 billion (32.4% nominal y/y growth) in the same period last year. Real growth in credit to households, therefore contracted by 7.2 percent in February 2019, compared with the 19.7 percent growth in February 2018 [See Annexes Table 2].

The share of total credit to the private sector increased from 88.7 percent in February 2018 to 90.7 percent in February 2019. Private enterprises received 67.7 percent of the total credit in February 2019 compared with 68.0 percent a year ago. The share of credit to foreign private enterprises increased from 8.0 percent to 10.9 percent, while that of indigenous private enterprises declined from 60.0 percent to 56.7 percent during the period under review. Households received an increased proportion of 20.6 percent of the industry's credit in February 2019 compared with 18.7 percent a year ago, while the share of credit to 'other' private entities increased from 2.0 percent to 2.5 percent during the same comparative period.

The increase in the share of the banking industry credit to the private sector in February 2019 was associated with a decline in the share to the public sector comprising Government, public institutions and public enterprises, pointing to crowding in of the private sector. The share of credit

[2] Gross loans and advances grew in nominal terms by 21.8 percent if all the loans and advances under receivership are included.

to the public sector declined from 11.3 percent in February 2018 to 9.3 percent in February 2019, largely from the decline in the share of industry's credit to public institutions and public enterprises. The portion of the banking industry's credit to Public Institutions dipped from 2.2 percent to 1.2 percent, while the share to Public Enterprises declined from 6.7 percent to 4.5 percent during the review period. Credit to Government however recorded an increased share during the period under review from 2.4 percent to 3.6 percent [See Annexes Table 4].

In terms of credit allocation to economic sectors in February 2019, commerce and finance continued to hold the largest share accounting for 23.2 percent compared with 24.4 percent in the same period last year, while the services sector followed with 22.3 percent compared with 21.7 percent a year ago. The manufacturing sector was the third largest recipient of the industry's credit in February 2019, with a share of 11.9 percent, higher than the 8.2 percent in the same period last year. The lowest share of the industry's credit went to the mining and quarrying sector with 3.5 percent share, although inched up from the 3.0 percent in February 2018. Agriculture, forestry and fishing sector also received 4.8 percent of the industry loans from 4.5 percent during the same period in the previous year. While the three highest sectoral recipients (commerce and finance, services and manufacturing) accounted for 57.3 percent of the industry's outstanding credit balances, the lowest three recipients (mining and quarrying, agriculture, forestry and fishing, and construction) accounted for 16.3 percent of the industry's credit [See Figure 1].

3.2.2 Off-Balance Sheet Activities

The off-balance sheet activities of banks, largely comprising trade finance and guarantees, slowed in February 2019 compared with the same period a year ago. The industry's contingent liabilities amounted to GH¢9.73 billion as at February 2019 from GH¢8.88 billion in February 2018, translating into a lower year-on-year growth rate of 8.1 percent, from the 31.3 percent growth achieved during the same comparative period. The ratio of banks' contingent liabilities to total liabilities also declined to 10.5 percent in February 2019 from 10.9 percent a year earlier [See Annexes Table 3].

3.2.3 Asset Quality

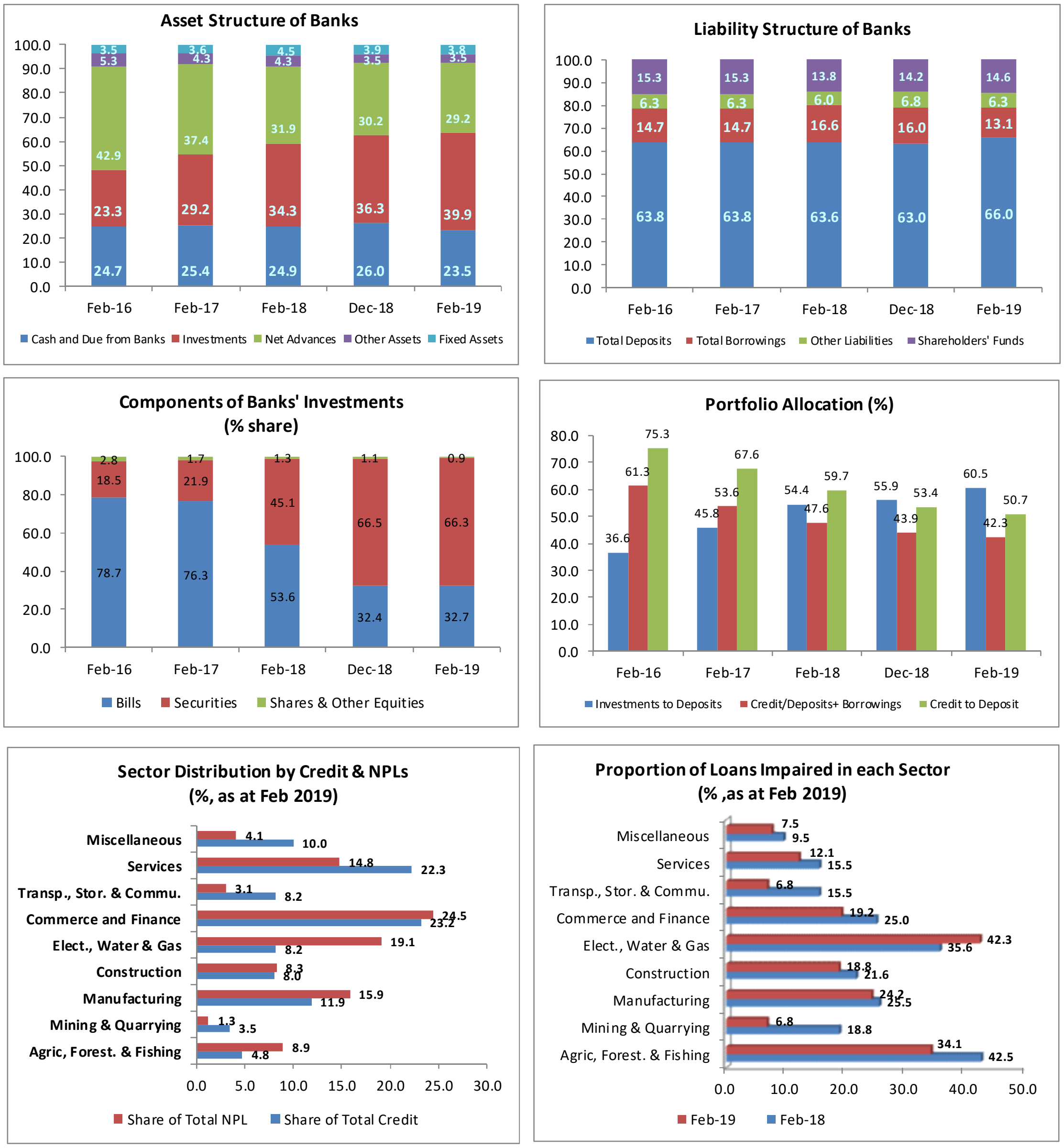
The industry's asset quality improved significantly during the period under review. The stock of the industry's Non-Performing Loans (NPLs) declined from GH¢7.74 billion in February 2018 to GH¢6.63 billion in February 2019, representing a slower growth of 14.4 percent compared with the 21.1 percent growth recorded a year earlier. The decline in the stock of NPLs coupled with the marginal pick-up in credit growth translated into a lower NPL ratio of 18.2 percent in February 2019 from 21.6 percent a year ago. When adjusted for the fully-provisioned loan loss category, the NPL ratio declines to 9.4 percent from 10.9 percent, signalling a slowdown in deterioration of loan quality.

The private sector accounted for 96.9 percent of the industry's NPLs in February 2019, up from the 92.7 percent recorded in February 2018, while the public sector's contribution declined to 3.1 percent from 7.3 percent over the same comparative period. Indigenous private enterprises accounted for a lower 75.4 percent of total NPLs in February 2019 compared with 77.0 percent in the corresponding period in 2018, while the contribution of foreign enterprises increased to 10.2 percent from 8.5 percent. The contribution of households to the banking industry NPLs rose with the increase in their share of the industry credit, accounting for 9.6 percent of total NPLs in February 2019, compared with a share of 6.6 percent a year ago [See Annexes Table 4].

The share of the banking industry NPLs across the various economic sectors in February 2019 largely reflected the industry's sectoral credit allocation, with commerce and finance, the largest recipient, accounting for 24.5 percent. The lowest recipient of banking industry credit, mining and quarrying, also had the least share of the industry's NPLs of 1.3 percent in February 2019. The proportion of industry's loans to the agriculture, forestry and fishing sector classified as impaired deteriorated marginally from 8.8 percent in February 2018 to 8.9 percent in February 2019. The increased share of the industry's loans to the manufacturing sector was also associated with a higher deterioration in the impaired component from 9.6 percent to 15.9 percent during the period under review. The proportion of the industry's NPLs to the services sector, the second largest recipient of the industry's credit, however improved from 15.6 percent to 14.8 percent. Overall, the top three largest contributors to the industry's NPLs (commerce & finance; electricity, water & gas, and; manufacturing) accounted for 59.4 percent in February 2019; whereas the three lowest contributors (mining & quarrying; transport, storage & communication; and construction) accounted for 8.9 percent during the review period [See Figure 1].

An analysis of the proportions of loans impaired in each sector showed that with the exception of the electricity, water and gas sector, all other sectors recorded improvements in February 2019 compared with February 2018.The share of loans to the electricity, water and gas sector that were classified as impaired increased to 42.3 percent in February 2019 from 35.6 percent a year ago. On the other hand, the NPL ratio for the agriculture, forestry and fishing sector declined to 34.1 percent in February 2019 from 42.5 percent in February 2018, while that of the manufacturing sector declined to 24.2 percent from 25.5 percent during the same comparative period. The NPL ratio of the commerce and finance sector also improved from 25.0 percent to 19.2 percent, with similar declines in the construction and services sectors from 21.6 percent to 18.8 percent and 15.5 percent to 12.1 percent respectively. The two sectors with the lowest NPL ratios of 6.8 percent respectively were the transport, storage & communication, and the mining & quarrying sectors [See Figure 1].

Figure 1: Developments in Banks' Balance Sheet & Asset Quality



3.3 Financial Soundness Indicators

The key financial soundness indicators broadly strengthened as at end-February 2019 compared with the position a year ago.

3.3.1 Liquidity Indicators

The banking sector remains liquid with only some marginal declines in core liquidity measures during the review period. The ratio of core liquid assets (cash and due from banks and short term bills) to total deposits declined to 35.6 percent in February 2019 from 39.6 percent in February 2018. The decline in this ratio can be explained by the fact that total deposits increased while at the same time, banks' investments in short term bills contracted as they shifted their investment mix towards long term securities [see Table 1]. Similarly, the ratio of core liquid assets to total assets declined marginally to 23.5 percent from 24.9 percent over the same period. Reflecting the significant increase in the share of longer-term investments, the increase in the industry's broad liquid assets (comprising core liquid assets, longer-term investments and shares) translated into higher broad liquidity indicators. The ratio of broad liquid assets to total deposits increased from 93.3 percent in February 2018 to 95.5 percent in February 2019 while broad liquid assets to total assets rose from 58.7 percent to 63.0 percent over the same period [See Annexes Table 5].

3.3.2 Capital Adequacy Ratio (CAR)

The banking industry's ability to absorb losses using its capital was enhanced in February 2019. The industry's solvency, measured by the Capital Adequacy Ratio (CAR) increased to 21.7 percent in February 2019 from 19.2 percent in February 2018 reflecting the impact of the recapitalization exercise. The quality of banks' capital also improved with the recapitalization, indicated by the sharp increase in the Tier 1 CAR to 20.6 percent from 15.9 percent during the period under review. Banks' risk weighted assets (RWA) to total assets declined from 62.8 percent in February 2018 to 56.1 percent in February 2019 due to the marginal pick-up in loans and the decline in the loss component [See Figure 2]. With the adoption and implementation of the Basel II framework, the capital risk measure has been enhanced to ensure banks align their risks with their capital to improve their solvency. Furthermore, banks' adherence to the Capital Risk Directive issued by the Bank of Ghana would enhance the safety of their capital against deterioration.

3.3.3 Profitability

The profitability of the banking industry improved during the first two months in 2019 compared with the same period last year. The industry recorded an after-tax profit of GH¢549.70 million, representing a year-on-year growth of 31.5 percent, higher than the 14.0 percent growth recorded for the same period last year. The higher growth in net profit was underpinned by an increase in the growth of net interest income coupled with a slowdown in the growth of operating expenses and total provisions. Net interest income grew by 17.9 percent on account of higher interest income from investments and lower borrowing cost from reduced borrowings resulting from the strong deposits mobilization. Fees and commissions however inched up by only 0.4 percent compared to the 16.8 percent growth witnessed during same period last year. This was largely due to the slowdown in the volume of off- balance sheet activities which dipped during the first two months as noted earlier. Growth in operation was somehow contained at 7.7 percent, lower than the previous year's growth of 8.6 percent, due largely to efficiency gains from bank consolidations and the rationalization of bank branches. This also contributed to lower growth in provisions for fixed assets. Total provisions (on loans and fixed assets depreciation) grew by only 2.2 percent, significantly lower than the 11.9 percent recorded for the same period a year earlier on account of reduction in fixed assets and lower NPLs. In summary, the sector's profit profitability performance was enhanced by strong net interest income and cost control [See Annexes Table 7].

(a) Return on Assets and Return on Equity

The improved profitability levels during the period under review positively reflected in the main indicators, namely, after-tax Return on Equity (ROE) and before-tax Return on Assets (ROA). The industry's after-tax ROE measured as the ratio of after-tax income to average shareholders' funds increased to 20.1 percent in February 2019 from 19.0 percent in February 2018. Similarly, the before-tax ROA measured as the ratio of income before-tax to average total assets increased to 4.2 percent from 4.0 percent during the same comparative period, pointing to improved profitability within the banking industry [See Annexes Table 6].

(b) Interest Margin and Spread

Banks' interest spreads declined marginally by 10 basis points to 1.9 percent in February 2019 from declines in both gross yields (from 3.3% to 2.8%) and interest payable on deposits and borrowings (from 1.3% to 1.0%). The narrowing of the spreads was broadly in line with declines in money market rates during the period under review. The ratio of gross income to total assets (asset utilisation) also declined marginally to 2.5 percent in February 2019 from 2.7 percent in February 2018, pointing to some moderation in the incomes generated from banks' assets. The industry's interest margin to total assets remained broadly unchanged at 1.3 percent during the period under review, whereas interest margin to gross income increased to 53.1 percent from 47.8 percent. The industry's profitability ratio also increased to 20.3 percent in February 2019 from 16.4 percent a year earlier [See Annexes Table 6].

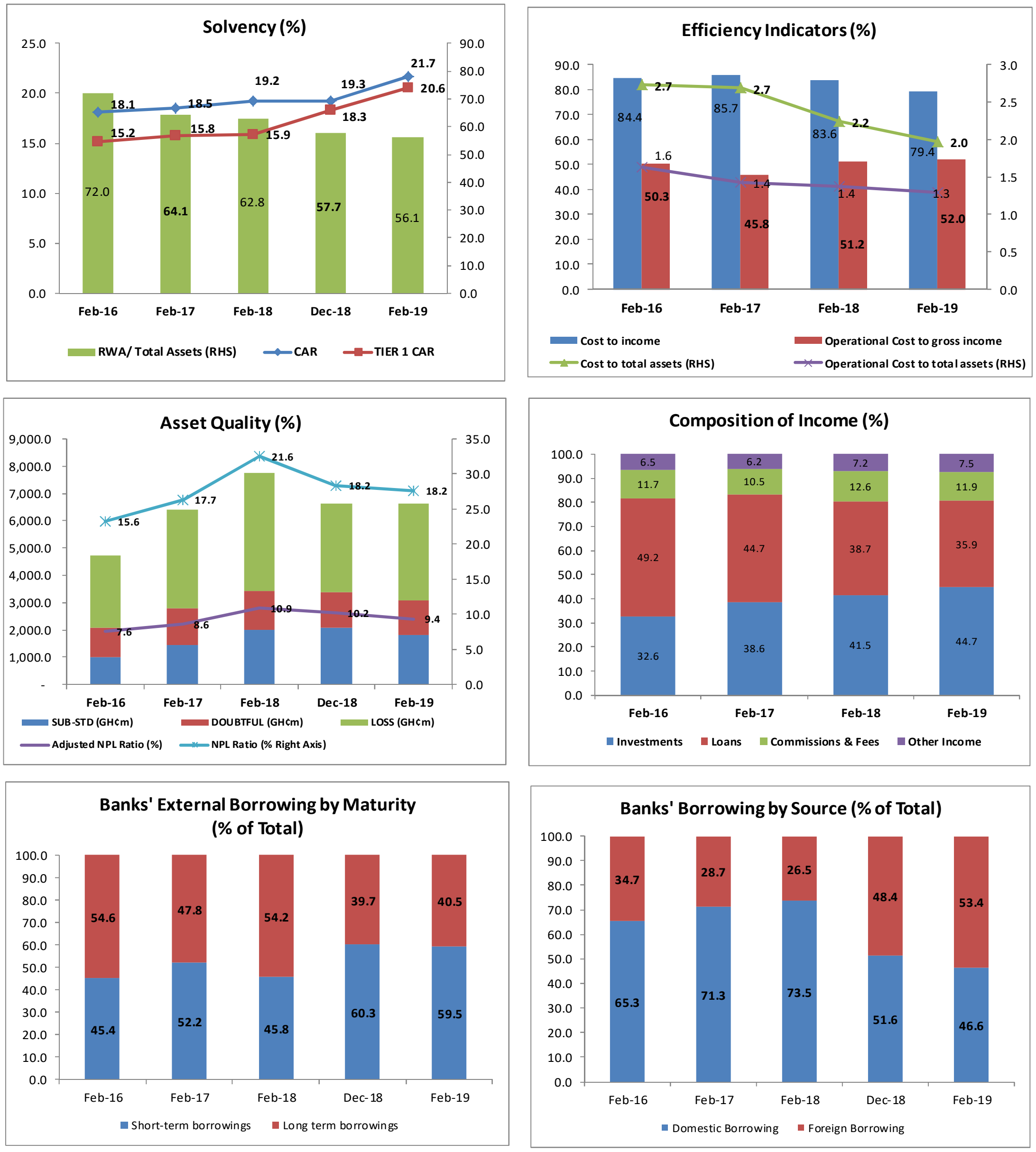
(c) Composition of Banks' Income

The composition of banks' income broadly reflected the shares of the various components of total assets. Thus, the share of investments income in banks' income rose with its share in total assets. Investments (both short and long-term) constituted the largest source of income for banks, with its share increasing to 44.7 percent in February 2019 from 41.5 percent in February 2018. The share of income from loans declined to 35.9 percent from 38.7 percent during the period under review, following the decline in the size of loans in the industry's assets. The share of banks' income from commissions and fees also declined to 11.9 percent in February 2019 from 12.6 percent a year earlier, while other income sources from non-core banking activities inched up to 7.5 percent of their total income from 7.2 percent over the same period in 2018 [See Figure 2].

3.3.4 Operational Efficiency

The banking industry's efficiency at minimizing costs relative to income and assets broadly improved during the review period. With the exception of operational cost to gross income which increased marginally to 52.0 percent in February 2019 from 51.2 percent a year earlier, all the operational efficiency indicators improved. Operational cost to total assets declined marginally to 1.3 percent from 1.4 percent during the same comparative period. The industry's cost to income ratio declined to 79.4 percent in February 2019 from 83.6 percent in February 2018, while cost to total assets declined marginally to 2.0 percent from 2.2 percent during the same period [See Figure 2]. The improvement in these cost efficiency ratios partly accounted for the improved industry profitability during the period.

Figure 2: Financial Soundness Indicators (FSIs)



3.4 Banks' Counterparty Relationships

Banks' offshore accounts posted a mixed performance in February 2019 compared with February 2018.

(a) Developments in Banks' Offshore Balances & External Borrowing

Banks' offshore balances increased to GH¢8.57 billion (7.5% y/y growth) in February 2019 from GH¢7.97 billion (2.5% y/y growth) in February 2018. The pickup in the growth of banks' offshore balances came largely from the sharp increase in the growth of other claims on non-residents or placements abroad by 67.9 percent in February 2019 compared with the contraction of 14.0 percent a year ago. However, banks' nostro balances comprising balances with foreign banks contracted by 31.2 percent from the 16.9 percent growth during the same comparative period. The ratio of banks' offshore balances to their networth however declined from 59.0 percent in February 2018 to 53.7 percent in February 2019, pointing to a moderation in the industry's exposure to cross-border risks [See Annexes Table 8].

The banking industry however borrowed more from foreign counterparties than from domestic counterparties in February 2019 relative to February 2018. The share of banks' borrowing from foreign counterparties in total borrowed funds doubled to 53.4 percent in February 2019 from 26.5 percent in February 2018 while the share of domestically borrowed funds dropped to 46.6 percent from 73.5 percent during the same review period. The proportion of banks' short-term borrowing in total external borrowing increased to 59.5 percent in February 2019 from 45.8 percent in February 2018, while the share of long-term external borrowing declined to 40.5 percent from 54.2 percent over the same comparative period [See Figure 2].

4. CREDIT CONDITIONS SURVEY

The February 2019 survey round of the Credit Conditions revealed net tightening of overall credit stance to enterprises following a net tightened stance on short-term enterprise loans, long term enterprise loans and loans to large enterprises [See Figure 3]. However, banks' stance on loans to Small and Medium Enterprises (SMEs) eased in net terms during the current survey round compared with the December 2018 survey round. The net tight stance on loans during the first two months of 2019 continued to reflect concerns with the industry's adversely classified loans and risks associated with performance of the industry's largest borrowers. Banks however reported that they expect the stance on overall enterprise credit to ease two months from the February 2019 survey round, broadly in line with the expected increase in credit following the recapitalization. Banks however revealed that they expect the net tight stance that applied to large enterprises to continue into April 2019, while they maintain their net ease stance on loans to SMEs during the same period. Banks project a net ease in stance on both long term and short term enterprise loans for March 2019 and April 2019.

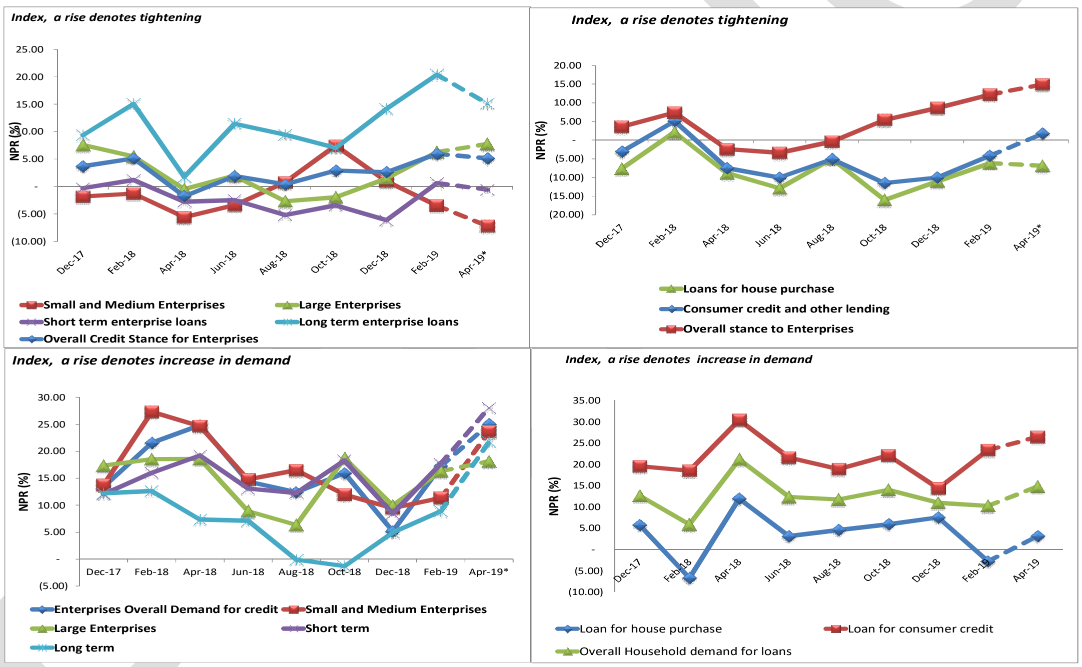
The survey findings also pointed to net tightening in banks' overall credit stance to households. The net tightened stance on loans to households reflected in both loans for house purchases and loans for consumer credit and other lending, also pointing to concerns over the industry's exposure to credit risk. Banks project further tightening in the credit stance on overall loans to households and loans for consumer credit and other lending over the next two months, moderated by a net ease in the stance on loans for mortgage.

In respect of demand for credit, the survey results showed an increase in the overall demand for enterprise credit, from increases in all the components of enterprise credit demand. Demand for credit increased in net terms for both large enterprises and SMEs between December 2018 and February 2019. Similarly, there was a net increase in enterprises demand for both long term and short term loans during this survey round. Banks project an increase in overall demand for credit by enterprise which will be reflected in the demand for both short term and long term loans. While demand for credit by large enterprises is projected to record a marginal increase, banks expect demand for credit by SMEs to increase significantly in net terms two months from now.

However, the survey reported a net decline in the overall household demand for credit from a sharp decline in the demand for mortgage loans, while demand for loans for consumer credit and other lending recorded a net increase. Over the next two months, banks project a net increase in the overall demand for credit by households from net increases in the demand for mortgage loans as well as consumer credit and other lending.

The banking sector's one-year inflation expectations index declined during the February 2019 survey round, indicating that banks expect inflation to decline one year from now. Banks attributed the inflation expectation to the decline in actual inflation as well as higher expectations on the performance of the economy. Banks' lending rates expectations however continued to be sticky downwards citing the risk associated with their adversely classified loans and performance of their largest borrowers as the main reasons. Banks' lending rates expectations are projected to decline with the resolution of the industry's high NPL problem and sustained macroeconomic stability.

Figure 3: Credit Conditions Survey Results



5. CONCLUSION AND OUTLOOK

An assessment of the banking sector's performance during the first two months of 2019 showed a well-capitalized, profitable, liquid and stable sector with strong prospects for increased financial intermediation. The key financial soundness indicators were broadly positive during the period and are projected to improve further as banks continue to adhere to the prudential and regulatory standards of the industry. The anticipated expansion of the banking sector's loan portfolio following the recent recapitalization would further enhance the growth and profitability of the industry. As banks continue to enforce the write-off policy on bad loans as well as intensify credit risk management practices in line with the Capital Risk Directive issued by the Bank of Ghana, the industry's exposure to credit risk would moderate further and safeguard stability in the sector. The outlook for the banking industry therefore remains positive.

ANNEXES

Table 1: Asset and Liability Structure of the Banking Sector

	Feb-16	Feb-17	Feb-18	Dec-18	Feb-19
Components of Assets (% of Total)					
Cash and Due from Banks	24.7	25.4	24.9	26.03	23.5
Investments	23.3	29.2	34.3	36.31	39.9
Net Advances	42.9	37.4	31.9	30.24	29.2
Other Assets	5.3	4.3	4.3	3.47	3.5
Fixed Assets	3.5	3.6	4.5	3.87	3.8
Components of Liabilities & Shareholders Funds(% of Total)					
Total Deposits	63.8	63.8	63.6	63.0	66.0
Total Borrowings	14.7	14.7	16.6	16.0	13.1
Other Liabilities	6.3	6.3	6.0	6.8	6.3
Shareholders' Funds	15.3	15.3	13.8	14.2	14.6

Table 2: Gross Loans and Real Credit Growth

Gross Loans and Credit Growth

	Feb-16	Feb-17	Feb-18	Dec-18*	Feb-19*
Gross Loans and Advances (GH¢m)	30,119.8	35,976.0	35,758.0	36,496.9	36,435.5
Nominal Growth (y-o-y)	19.5	19.4	(0.6)	(3.5)	1.9
Real Growth (y-o-y)	0.8	5.5	(10.1)	(11.8)	(6.7)
Private Sector Credit (GH¢m)	28,182.08	33,219.01	33,149.89	33,463.93	33,229.43
Nominal Growth (y-o-y)	23.0	17.9	-0.2	-5.4	0.2
Real Growth (y-o-y)	3.8	4.1	-9.8	-13.5	-8.2
Household Loans (GH¢m)	5,350.68	5,227.52	6,920.13	6,759.17	7,008.39
Nominal Growth (y-o-y)	30.0	(2.3)	32.4	19.1	1.3
Real Growth (y-o-y)	9.7	(13.7)	19.7	8.9	(7.2)

**** Excludes loans under Receivership***

Table 3: Contingent Liability

	Feb-16	Feb-17	Feb-18	Dec-18	Feb-19
Contingent Liabilities (GH¢)	6,748.6	7,341.8	8,883.7	10,062.0	9,733.0
Growth (y-o-y)	- 8.8	8.8	31.3	18.4	8.1
% of Total Liabilities	12.7	10.2	10.9	11.1	10.5

Table 4: Distribution of Loans and NPLs By Economic Sector (Percent)

	Feb-17		Feb-18		Dec-18		Feb-19	
	Share in Total Credit	Share in NPLs	Share in Total Credit	Share in NPLs	Share in Total Credit	Share in NPLs	Share in Total Credit	Share in NPLs
a. Public Sector	**14.0**	**2.9**	**11.3**	**7.3**	**8.6**	**2.9**	**9.3**	**3.1**
i. Government	1.5	1.1	2.4	1.0	3.0	1.0	3.6	1.0
ii. Public Institutions	5.1	0.1	2.2	0.4	1.2	0.3	1.2	0.3
iii. Public Enterprises	7.4	1.7	6.7	5.8	4.4	1.6	4.5	1.7
b. Private Sector	**86.0**	**97.1**	**88.7**	**92.7**	**91.4**	**97.1**	**90.7**	**96.9**
i. Private Enterprises	71.0	90.9	68.0	85.6	66.3	87.0	67.7	85.6
o/w Foreign	8.8	12.6	8.0	8.5	9.9	9.6	10.9	10.2
Indigeneous	62.2	78.3	60.0	77.0	56.4	77.4	56.7	75.4
ii. Households	13.7	5.6	18.7	6.6	22.9	9.4	20.6	9.6
iii. Others	1.2	0.6	2.0	0.6	2.2	0.6	2.5	1.8

Table 5: Liquidity Ratios

	Feb-16	Feb-17	Feb-18	Dec-18	Feb-19
Liquid Assets (Core) - (GH¢'million)	15,505.5	21,283.5	23,708.77	27,366.31	25,551.82
Liquid Assets (Broad) -(GH¢'million)	29,710.0	45,247.3	55,877.50	65,128.31	68,593.36
Liquid Assets to total deposits (Core)-%	38.8	40.0	39.58	40.07	35.56
Liquid Assets to total deposits (Broad)- %	74.3	85.0	93.29	95.37	95.45
Liquid assets to total assets (Core)- %	24.7	25.4	24.92	26.03	23.46
Liquid assets to total assets (Broad)- %	47.4	54.1	58.74	61.96	62.99

Table 6: Profitability Indicators (%)

	Feb-16	Feb-17	Feb-18	Feb-19
Gross Yield	4.3	3.7	3.3	2.8
Interest Payable	1.8	1.8	1.3	1.0
Spread	2.5	1.9	2.0	1.9
Asset Utilitisation	3.2	3.1	2.7	2.5
Interest Margin to Total Assets	1.5	1.4	1.3	1.3
Interest Margin to Gross income	47.6	43.4	47.8	53.1
Profitability Ratio	15.6	14.0	16.4	20.3
Return On Equity (%) after tax	20.7	19.6	19.0	20.1
Return On Assets (%) before tax	4.6	4.0	4.0	4.2

Table 7: DMBs' Income Statement Highlights

	Feb-16	Feb-17	Feb-18	Feb-19	Feb-18	Feb-19
	(GH ¢'million)				Y-on-y Growth (%)	
Interest Income	1,656.8	2,182.7	2,045.9	2,179.4	(6.3)	6.5
Interest Expenses	691.51	1045.80	826.98	741.75	(20.9)	(10.3)
Net Interest Income	**965.3**	**1,136.9**	**1,219.0**	**1,437.7**	**7.2**	**17.9**
Fees and Commissions (Net)	238.0	275.6	321.9	323.3	16.8	0.4
Other Income	131.5	161.2	184.3	203.0	14.3	10.2
Operating Income	1,334.8	1,573.7	1,725.2	1,964.0	9.6	13.8
Operating Expenses	692.68	848.29	921.03	991.65	8.6	7.7
Staff Cost (deduct)	371.22	435.91	483.54	545.69	10.9	12.9
Other operating Expenses	321.46	412.38	437.49	445.96	6.1	1.9
Net Operating Income	**642.2**	**725.4**	**804.1**	**972.4**	**10.9**	**20.9**
Total Provision (Loan losses, Depreciation & others)	170.8	184.3	206.3	210.9	11.9	2.2
Income Before Tax	**471.3**	**541.2**	**597.8**	**761.5**	**10.5**	**27.4**
Tax	154.99	174.48	179.75	211.80	3.0	17.8
Net Income	**316.3**	**366.7**	**418.1**	**549.7**	**14.0**	**31.5**
Gross Income	2,026.4	2,619.5	2,552.1	2,705.8	(2.6)	6.0

Table 8: Developments in Offshore Balances

	Feb-16	**Feb-17**	**Feb-18**	**Dec-18**	**Feb-19**
Offshore balances as % to Networth	47.2	67.4	59.0	55.5	53.7
Annual Growth in Offshore balances (%)	-7.0	72.3	2.5	10.8	7.5
Annual Growth in Nostro Balances (%)	-8.3	30.7	16.9	0.0	-31.2
Annual Growth in Placement (%)	-4.0	173.4	-14.0	21.4	67.9