BANK OF GHANA

Banking Sector Report

NOVEMBER 2018

CONTENTS

1. PREFACE 1
2. SUMMARY 2
3. BANKING SECTOR DEVELOPMENTS 3
   - 3.1 Bank's Balance Sheet 3
     - *3.1.1 Asset and Liability Structure* *5*
     - *3.1.2 Share of Banks' Investments* *6*
   - 3.2 Credit Risk 6
     - *3.2.1 Credit Portfolio Analysis* *6*
     - *3.2.2 Off-Balance Sheet Activities* *7*
     - *3.2.3 Asset Quality* *7*
   - 3.3 Financial Soundness Indicators 10
     - *3.3.1 Liquidity Indicators* *10*
     - *3.3.2 Capital Adequacy Ratio (CAR)* *10*
     - *3.3.3 Profitability* *10*
     - *3.3.4 Operational Efficiency* *12*
   - 3.4 Banks' Counterparty Relationships 13
4. Credit Conditions Survey 13
5. Conclusion and Outlook 15

ANNEXES 16

1. PREFACE

The Bank of Ghana's Banking Sector Report is published after the 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.

Brief Note on Monetary Policy Formulation in Ghana

Objective of Monetary Policy

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 intermediation since risks associated with financial markets are taken into account in monetary policy formulation.

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), in which the central bank uses 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 the Ghanaian banking sector as at October 2018 compared with the same period last year. The sector comprised thirty (30) banks in October 2018, thirteen (13) of which were domestically-controlled and the remaining seventeen (17) foreign-controlled.

The industry's balance sheet restructuring continued in October 2018 with an increase in the share of banks' investments in bills and securities relative to gross advances. Growth in the industry's assets moderated following the transfer of all the loans and advances of the five defunct banks to the receiver for recoveries, leaving the Consolidated Bank Ghana (CBG) with only the good assets. The industry also posted a stronger profit-after-tax performance in October 2018 compared with October 2017 due to slower growth of banks' operating expenses (both staff cost and other operating expenses) and total provisions. In addition, net income performance improved on account of a pick-up in growth of banks' non-interest income (fees and commissions and other income) which offset the contraction in net interest income (due to the slowdown in credit growth and decline in money market rates).

Key financial soundness indicators (FSIs) broadly improved in October 2018 compared with October 2017, reflecting gains from on-going reforms in the sector. The banking industry's solvency, measured by the Capital Adequacy Ratio, (CAR), increased to 20.0 percent in October 2018, from 18.0 percent in October 2017, reflecting some general improvement in the industry's ability to absorb losses. The increased CAR also indicates recapitalization efforts by banks as the December 31, 2018 deadline approaches. Asset quality also recorded marginal decline from 21.6 percent in October 2017 to 20.1 percent in October 2018 partly due to implementation of the loan write-off policy by some banks following the Bank of Ghana's directive issued in June 2018. While core liquidity indicators recorded some moderation, broad liquidity indicators improved in October 2018 compared with October 2017, indicating that the industry remains liquid. Similarly, the industry recorded some gains in efficiency during the period under review.

Overall, the latest FSIs showed some improvements in the banking industry. The FSIs are expected to improve further on completion of the bank recapitalization process and together with on-going reforms; including supervisory vigilance and strict enforcement of prudential regulations, confidence and trust will be restored in the financial sector.

3. BANKING SECTOR DEVELOPMENTS

3.1 Banks' Balance Sheet

Total assets in the banking sector grew by 19.6 percent to GH¢106.34 billion in October 2018, compared with GH¢88.91 billion in October 2017 (20.5percent year-on-year growth). In particular, the growth in banks' domestic assets moderated slightly by 19.1 percent in October 2018 from 19.7 percent in October 2017, while growth in foreign assets slowed to 24.1 percent from 28.9 percent during the same period. The foreign assets component of banks' total assets increased marginally to 9.7 percent in October 2018 from 9.3 percent a year earlier, leading to a marginal decline in the share of domestic assets from 90.7 percent to 90.3 percent during the period under review.

With the exception of investments, all the major components of banks' total assets recorded slower growth, reflecting the impact of the collapse of seven banks. In detail, banks' investment in shares and securities increased to GH¢42.84 billion (62.9 percent year-on-year growth) from GH¢26.29 billion in October 2017 (31.9percent year-on-year growth), constituting the largest component of total assets. The pickup in the growth of banks' investments was largely on account of the 229.0 percent growth in long-term securities, following the issuance of a GH¢5.76 billion bond by Government towards the Purchase and Assumption Agreement under which the CBG acquired all the deposits as well as other specific liabilities and good assets of the five defunct banks. Short-term bills, on the other hand, contracted by 15.3 percent in October 2018 compared with 10.2 percent growth in the same period of last year.

The industry's gross advances stood at GH¢35.48 billion[1] in October 2018, from GH¢38.36 billion, representing a year-on-year contraction by 7.5 percent compared with the 12.0 percent growth recorded a year ago. The industry's net advances (gross advances net of provisions and interest in suspense) also contracted by 4.0 percent in October 2018 (GH¢30.55 billion) compared with a growth of 7.2 percent in the same period last year (GH¢31.82 billion). The foreign currency component of banks' net advances recorded a slower growth of 3.5 percent in October 2018 (GH¢9.26 billion) compared with 7.6 percent in October 2017 (GH¢8.94 billion), as well as a decline in share from 10.1 percent to 8.7 percent of total advances during the same comparative period, partly reflecting the exclusion of the loans of the five defunct banks. The shares of both gross advances and net advances in banks' total assets also declined during the period under review, reflecting balance sheet adjustment towards less risky assets. Growth in the two other major components of banks' total assets, namely,

[1] Figure excludes all the loans and advances of the five defunct banks taken over by the CBG that are with the receiver for recoveries.

fixed assets and other assets also declined sharply during the period under review, reflecting the impact of the on-going reforms on the assets of the banking industry.

The total deposits of the banking industry stood at GH¢67.38 billion as at October 2018 from GH¢55.83 billion in October 2017, representing a year-on-year growth of 20.7 percent compared with 18.2 percent a year ago. The foreign currency component of total deposits also increased from GH¢14.94 billion in October 2017 (17.3percent y/y growth) to GH¢16.99 billion in October 2018 (13.7percent y/y growth), accounting for 17.7 percent of the recorded increase in total deposits over the period. Deposits of non-residents declined by 1.5 percent to GH¢342.10 million in October 2018, from GH¢347.20 million a year earlier, while domestic deposits increased by 20.8 percent to GH¢67.04 billion from GH¢55.49 billion in October 2017. The share of banks' assets used to fund deposits increased from 62.8 percent to 63.4 percent during the review period, following the increase in the industry's total deposits. The share of total borrowings, the second largest source of funds for the banks, remained unchanged at 17.0 percent, though in year-on-year terms, growth slowed from 24.2 percent to 19.9 percent. Following the increase in the share of total deposits in banks' pool of funds, the share of other liabilities declined from 7.2 percent in October 2017 to 6.6 percent in October 2018, representing a sharp decline in year-on-year growth by 9.1 percent from 49.4 percent a year ago.

Growth in the industry's total borrowing however declined from 24.2 percent (GH¢15.08 billion) in October 2017 to 19.9 percent (GH¢18.08 billion) in October 2018, reflecting a 10.0 percent contraction in domestic borrowing which moderated the 108.2 percent growth in foreign borrowing. Banks' short-term foreign borrowing grew from GH¢1.87 billion in October 2017 to GH¢5.05 billion in October 2018 while long-term foreign borrowing increased from GH¢1.95 billion to GH¢2.89 billion during the period under review. Similarly, long-term domestic borrowing recorded a sharp growth by 82.2 percent compared to 13.9 percent in October 2017, but the short-term component of domestic borrowing contracted by 22.8 percent against 35.5 percent growth in the same comparative periods. Banks continued to reveal a preference for foreign borrowing relative to domestic borrowing in funding of assets, despite the industry's increased exposure to cross-border risks.

With the deadline for the banks' recapitalisation unchanged at end-year 2018, the industry's paid-up capital recorded increases, largely reflecting intensified recapitalisation efforts. The industry's paid-up capital increased to GH¢6.69 billion in October 2018 from GH¢4.45 billion in October 2017, representing a year-on-year growth of 50.2 percent compared with the 30.1 percent growth recorded in the same period last year. Banks' shareholders' funds, comprising paid-up capital and reserves, also grew by 19.8 percent from GH¢11.60 billion to GH¢13.90 billion during the period under review. Growth in banks' paid-up capital in October 2018 outpaced growth in shareholders' funds due to a slower growth in banks' reserves by 0.8 percent against 6.4 percent in

October 2017. The share of banks' shareholders' funds in total liabilities and capital remained unchanged at 13.1 percent during the period under review.

Table 1: Key Developments in DMBs' Balance Sheet

	GH¢million				Y-on-Y Growth (%)			Shares (%)		
	Oct-16	Oct-17	Aug-18	Oct-18	Oct-17	Aug-18	Oct-18	Oct-17	Aug-18	Oct-18
TOTAL ASSETS	**73,788.7**	**88,914.4**	**104,623.2**	**106,339.5**	**20.5**	**21.5**	***19.6***	**100.0**	***100.0***	***100.0***
A. Foreign Assets	6,431.4	8,292.3	10,955.7	10,288.0	28.9	43.2	*24.1*	9.3	*7.9*	*9.7*
B. Domestic Assets	67,357.2	80,622.2	93,667.4	96,051.6	19.7	19.4	*19.1*	90.7	*92.1*	*90.3*
Investments	19,932.1	26,292.8	67,741.5	42,839.9	31.9	175.7	*62.9*	29.6	*29.3*	*40.3*
i. Bills	15,874.1	17,487.2	15,887.8	14,812.3	10.2	(3.7)	*(15.3)*	19.7	*20.4*	*13.9*
ii. Securities	3,640.6	8,389.8	24,238.0	27,601.6	130.4	216.4	*229.0*	9.4	*8.4*	*26.0*
Advances (Net)	29,682.0	31,823.5	28,840.9	30,551.1	7.2	(7.5)	*(4.0)*	35.8	*36.4*	*28.7*
of which Foreign Currency	8,311.7	8,944.6	9,274.3	9,259.6	7.6	6.6	*3.5*	10.1	*10.3*	*8.7*
Gross Advances	34,268.8	38,364.5	33,777.9	35,480.0	12.0	(9.4)	*(7.5)*	43.1	*43.3*	*33.4*
Other Assets	3,372.9	4,931.8	4,439.5	3,793.7	46.2	(3.7)	*(23.1)*	5.5	*5.2*	*3.6*
Fixed Assets	2,654.1	3,426.1	3,941.0	3,857.0	29.1	18.6	*12.6*	3.9	*3.7*	*3.6*
TOTAL LIABILITIES AND CAPITAL	**73,788.7**	**88,914.4**	**104,623.2**	**106,339.5**	**20.5**	**21.5**	***19.6***	**100.0**	***100.0***	***100.0***
Total Deposits	47,223.2	55,831.7	67,741.5	67,382.3	18.2	26.2	*20.7*	62.8	*62.8*	*63.4*
of which Foreign Currency	12,738.5	14,942.3	17,501.4	16,984.9	17.3	18.6	*13.7*	16.8	*16.9*	*16.0*
Total Borrowings	12,145.0	15,084.7	16,774.0	18,082.7	24.2	9.8	*19.9*	17.0	*18.1*	*17.0*
Foreign Liabilities	4,026.2	4,164.0	8,241.0	8,288.1	3.4	68.8	*99.0*	4.7	*6.0*	*7.8*
i. Short-term borrowings	1,910.1	1,871.6	4,894.4	5,058.9	(2.0)	98.0	*170.3*	2.1	*3.3*	*4.8*
ii. Long-term borrowings	1,725.8	1,945.3	2,833.2	2,887.1	12.7	41.6	*48.4*	2.2	*2.3*	*2.7*
iii. Deposits of non-residents	390.3	347.2	513.3	342.1	(11.1)	25.1	*(1.5)*	0.4	*0.4*	*0.3*
Domestic Liabilities	59,579.6	73,119.1	82,652.1	83,983.0	22.7	18.2	*14.9*	82.2	*81.2*	*79.0*
i. Short-term borrowing	7,307.3	9,898.7	7,647.4	7,642.1	35.5	(19.6)	*(22.8)*	11.1	*10.9*	*7.2*
ii. Long-term Borrowings	1,201.7	1,369.1	1,398.9	2,494.5	13.9	8.6	*82.2*	1.5	*1.6*	*2.3*
iii. Domestic Deposits	46,832.9	55,484.5	67,228.1	67,040.2	18.5	26.2	*20.8*	62.4	*62.4*	*63.0*
Other Liabilities	4,277.4	6,388.6	6,484.5	6,969.7	49.4	10.1	*9.1*	7.2	*6.3*	*6.6*
Paid-up capital	3,421.9	4,452.8	6,636.0	6,687.7	30.1	52.4	*50.2*	5.0	*4.9*	*6.3*
Shareholders' Funds	10,143.2	11,604.8	13,618.2	13,899.8	14.4	21.3	*19.8*	13.1	*12.8*	*13.1*

3.1.1 Asset and Liability Structure

Banks' assets continued to reflect a shift in the structure observed earlier in 2018, with investments being the largest component, followed by net advances, and cash due from banks. The share of investments in banks' assets increased to 40.3 percent in October 2018 from 29.6 percent in October 2017, while the share of net advances declined to 28.7 percent from 35.8 percent during the same comparative period. The share of cash and due from banks in the industry's total assets also declined to 23.7 percent from 25.1 percent during the period under review, showing that banks invested more and held less cash. The share of fixed assets and other assets of banks in the industry's total assets declined. . The observed change in the structure of banks' assets revealed banks' response to the high stock of NPLs in the industry. This may well change in 2019 when banks have higher capital levels and credit growth rebounds.

The liability structure of the banking industry, on the other hand, showed a marginal share increase of total deposits in banks' funds (from 62.8percent to 63.4percent) compared with unchanged shares of 17.0 percent and 13.1 percent of borrowings and shareholders' funds respectively during the period under review. The share of banks' other liabilities also declined from 7.2 percent to 6.6 percent during the same review period [See Annexes Table 1].

3.1.2 Share of Banks' Investments

The share of long-term securities in banks' investment portfolio increased sharply to 64.4 percent in October 2018 from 31.9 percent in October 2017. The increase indicates banks' preference for long-term and less risky assets as against credit extension which is associated with increased risk due to the industry's high stock of non-performing loans. In contrast, the share of short-term securities in banks' investment portfolio declined sharply from 66.5 percent to 34.6 percent. The proportion of equities in banks' total investments also declined to 1.0 percent in October 2018 from 1.6 percent in October 2017.

3.2 Credit Risk

The industry's exposure to credit risk declined somewhat in October 2018 compared with October 2017.

3.2.1 Credit Portfolio Analysis

The banking industry's stock of gross loans and advances of GH¢35.48 billion in October 2018 translated into a 7.5 percent contraction in October 2018[2] compared with the 12.0 percent growth recorded in the same period last year due to the exclusion of loans of the banks taken over by CBG. In real terms, the October 2018 stock of gross loans and advances contracted by 15.6 percent compared with a moderate 0.3 percent growth recorded a year earlier. The industry's credit to the private sector (comprising loans to private enterprises and households) stood at GH¢33.13 billion in October 2018 compared with GH¢35.44 billion in October 2017, signalling a year-on-year contraction by 6.5 percent[3] compared with a 13.6 percent growth a year ago. Private sector credit contracted by 14.7 percent in real terms compared with the 1.8 percent growth a year earlier. Banks' credit stance to households continued to ease resulting in a 21.6 percent growth in October 2018 against 15.5 percent in October 2017. In real terms, credit to households grew by 11.1 percent in October 2018 compared with 3.4 percent growth a year earlier [See Annexes Table 2].

The share of the banking industry's credit to the private sector increased to 92.4 percent in October 2018 from 88.1 percent in October 2017. Private sector's share of the industry's total credit comprised 66.2 percent credit

[2] Gross loans and advances grew in nominal terms by 8.7 percent when all the loans and advances of the five defunct banks are included.

[3] Private sector credit including those of the five defunct banks recorded a nominal growth of 11.4 percent

to private enterprises (71.1percent in October 2017), 24.3 percent credit to households (15.3percent in October 2017) and 1.9 percent credit to "other" private entities (1.8percent in October 2017). The proportion of the industry's credit to indigenous private enterprises declined to 56.9 percent in October 2018 from 61.6 percent in October 2017, while the share of foreign private enterprises declined marginally to 9.3 percent from 9.5 percent during the same comparative period. The increase in the share of industry credit to the private sector led to a decline in the share to the public sector (credit to central government, public institutions and public enterprises) to 7.6 percent from 11.9 percent during the same review period [See Annexes Table 4].

The distribution of banks' credit to economic sectors showed that commerce and finance accounted for 24.6 percent, the highest share of the industry's outstanding credit balances as at October 2018, followed by the services and manufacturing sectors with 21.0 percent and 10.5 percent shares respectively. The mining and quarrying sector received the lowest share of 2.6 percent of total industry credit, followed by agriculture, forestry and fishing sector with a share of 4.5 percent during the period under review. Together, the mining & quarrying; agriculture, forestry & fishing, and construction sectors accounted for 15.1 percent of total credit, while commerce & finance, services and manufacturing, the three largest recipients of total credit, accounted for 56.1 percent in October 2018.

3.2.2 Off-Balance Sheet Activities

The banking industry's contingent liabilities (off-balance sheet items) of GH¢9.35 billion as at October 2018 showed a slower growth of 6.1 percent compared to the 23.3 percent growth recorded a year earlier, signalling some moderation in trade finance and guarantees. The ratio of banks' contingent liabilities in the total also declined to 10.1 percent in October 2018 from 11.5 percent in October 2017. [See Annexes Table 3]

3.2.3 Asset Quality

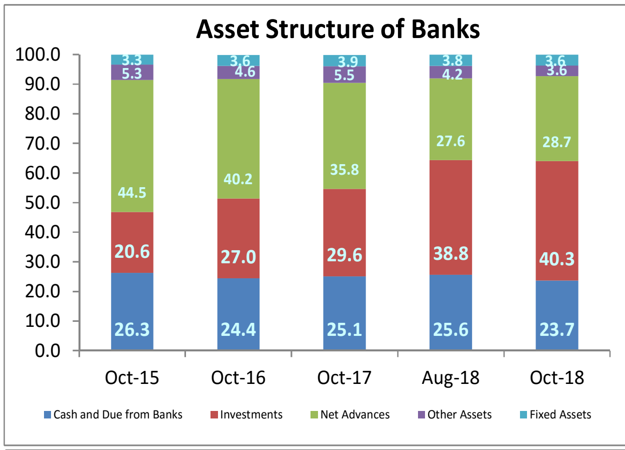
The stock of non-performing loans (NPLs) in the banking industry declined to GH¢7.14 billion in October 2018 from GH¢8.3 billion in October 2017, representing 14.0 percent contraction compared with the 27.2 percent growth a year ago. Consequently, the ratio of NPLs to gross advances declined to 20.1 percent from 21.6 percent during the same review period. However, the industry's adjusted NPL ratio (NPLs adjusted for fully-provisioned loss-loans category) increased to 11.4 percent in October 2018 from 10.5 percent in October 2017, reflecting the decline in the loss loan category as a result of the write-offs by banks that were given approval by the Bank of Ghana. To reduce the size of the loss loan component of the industry's NPLs, the Bank of Ghana in June 2018, issued a directive to all banks to submit a schedule of loss loans that were past due for more than two years to activate the write-off policy. This directive was in line with Section 75(2) and 92(2) ii of the Banks and

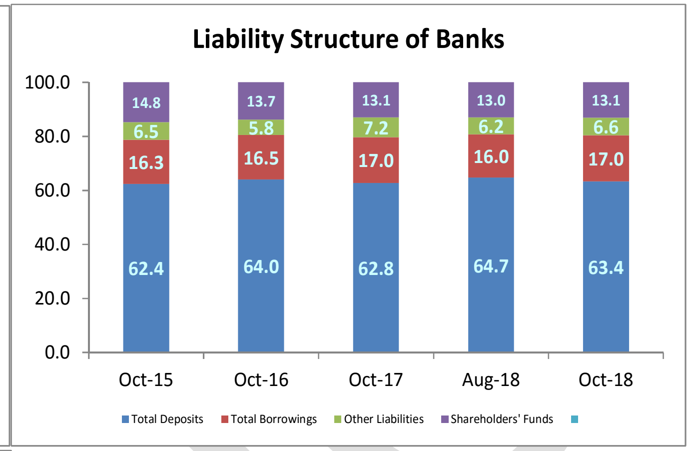
Specialized Deposits-taking Institutions Act, 2016 (Act 930). Following that, the Bank of Ghana gave approval to some banks to write-off their loss loans totalling GH¢1.2 billion in August 2018. The banks that received approvals to write-off their loss loans are required to submit quarterly reports on recoveries made on the loans that have been written off to Bank of Ghana to ensure full loan recovery.

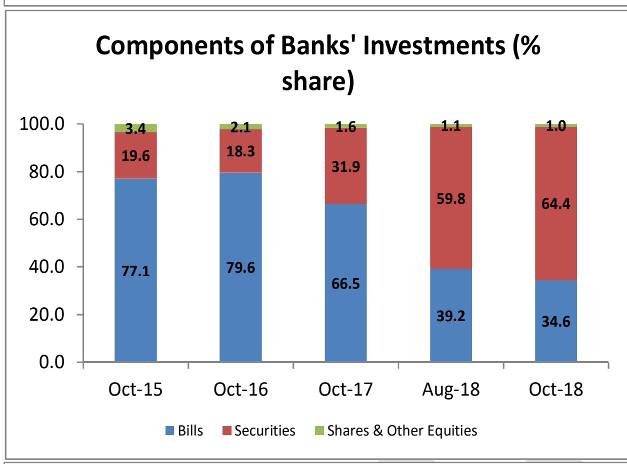
The private sector accounted for 95.5 percent of the industry's NPLs in October 2018, up from the 94.7 percent recorded in October 2017, while the public sector's contribution declined to 4.5 percent from 5.3 percent over the same comparative period. Indigenous private enterprises accounted for 73.2 percent of total NPLs in October 2018 compared with 78.2 percent in the corresponding period in 2017, while the contribution of foreign enterprises declined marginally to 10.5 percent from 10.8 percent. The contribution of households to the banking industry NPLs rose with the increase in their share of the industry credit, accounting for 11.3 percent of total NPLs in October 2018, compared with a share of 5.3 percent a year ago. [See Annexes Table 4]

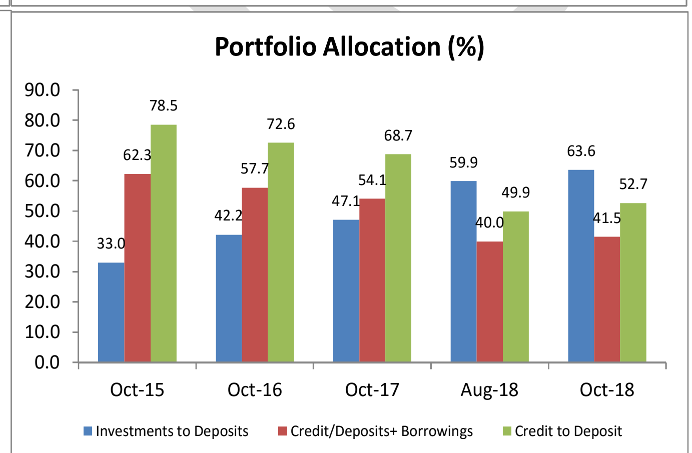
The contribution to the banking industry NPLs by the various economic sectors mirrors that of the industry's sector credit allocation, with commerce and finance, the largest recipient, accounting for 23.9 percent of the NPLs in October 2018 against 35.2 percent in October 2017. The lowest recipient of banking industry credit, mining and quarrying, also contributed the least to the industry's NPLs of 1.4 percent in October 2018 from 2.1 percent in October 2017. However, electricity, water and gas sector contributed a higher proportion of 18.3 percent compared with 12.7 percent for the manufacturing sector, though the former received a greater proportion of the banking industry credit. The top three largest contributors to the industry's NPLs (commerce & finance; electricity, water & gas, and; services) accounted for 56.9 percent in October 2018 compared with 61.3 percent a year ago; whereas the three lowest contributors (mining & quarrying; agriculture, forestry & fishing, and; transport, storage & communication) accounted for 15.1 percent against 13.6 percent during the same comparative period.

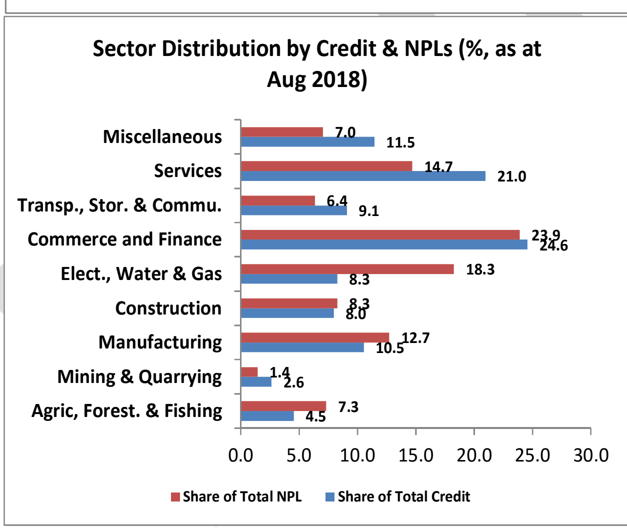
Developments in Banks' Balance Sheet & Asset Quality

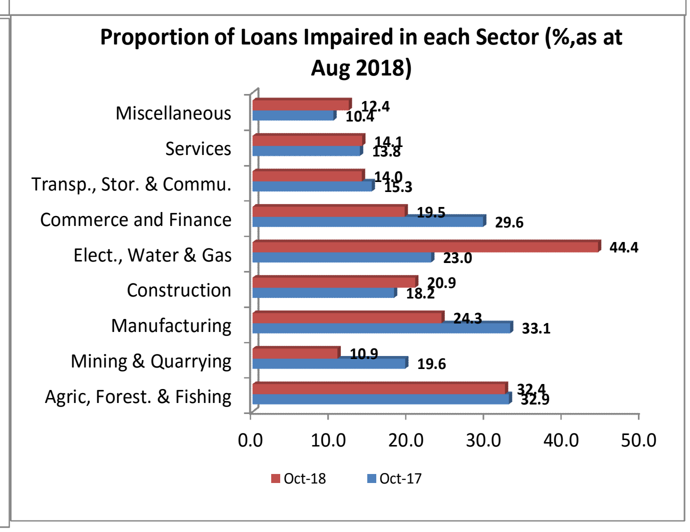












3.3 Financial Soundness Indicators

The main financial soundness indicators recorded broad improvement in October 2018 compared with the same period last year.

3.3.1 Liquidity Indicators

Operational liquidity indicators recorded mixed performance with declines in core liquidity measures while the broad liquidity measures recorded significant increases. The industry's core liquid assets (comprising cash and due from banks denominated in both domestic and foreign currency and short term bills) to total deposits declined to 37.4 percent in October 2018 from 40.0 percent in October 2017. Similarly, core liquid assets to total assets declined to 23.7 percent from 25.1 percent during the same review period. The industry's broad liquid assets (comprising core liquid assets and shares and other equities) increased following the issuance of the ESLA bond and the recent GOG bond to offset liabilities of the collapsed banks. The increase translated into higher broad liquidity indicators, namely, broad liquid assets to total deposits of 100.4 percent in October 2018 relative to 86.3 percent in October 2017 and broad liquid assets to total assets rose to 63.6 percent from 54.2 percent. The industry therefore remained adequately liquid to meet its short-term obligations, despite the declines in the core liquidity measures. [See Annexes Table 5]

3.3.2 Capital Adequacy Ratio (CAR)

The banking industry's Capital Adequacy Ratio (CAR) increased to 20.0 percent in October 2018 from 18.0 percent in October 2017, signalling the industry's improving ability to absorb losses using its capital. The increase in the industry's CAR was attributed to rising adjusted capital as banks continued to push towards meeting the new minimum capital of GH¢400 million by December 31, 2018. The slowdown in the growth of the industry's loans and advances also translated into a decline in the industry's risk-weighted assets to total assets to 56.3 percent in October 2018 from 62.7 percent a year ago, reinforcing the increase in the adjusted capital. The industry's solvency is projected to improve as banks conclude efforts at bringing in fresh capital to meet the new minimum paid-up capital.

3.3.3 Profitability

The banking industry recorded an improved income statement with after-tax profit of GH¢1.95 billion in October 2018, representing a year-on-year growth of 22.3 percent, compared with GH¢1.59 billion representing a modest 1.0 percent growth in October 2017. The sharp increase in banks' net income came from the 10.0 percent increase in net operating income to GH¢4.02 billion in October 2018 from GH¢3.66 billion (7.6percent y/y growth) a year ago. Net operating income of banks increased following the slower growth of banks' interest income compared with interest expenses. Banks' interest income declined due to the slowdown in loans and advances which constitute the bulk of interest-bearing assets of the banks, while the decline in money market rates and the Monetary Policy Rate (MPR) between October 2017 and October 2018 led to a decline in the interest expense of banks, especially the interest paid on deposits. Consequently, growth in banks' operating expenses slowed to 5.2 percent in October 2018 from 18.0 percent in October 2017, and was attributed to sharp declines in staff cost and other operating expenses during the review period. Also, the industry's gross income contracted by 3.5 percent to GH¢12.49 billion in October 2018 from GH¢12.94 billion in October 2017 due to weak operating and interest income outturns, though the other income category recorded a sharp growth by 57.4 percent against 14.6 percent during the period under review. [See Annexes Table 7]

(a) Return on Assets and Return on Equity

Following the improved after-tax profit performance in October 2018 compared with October 2017, the industry's main profitability indicators, namely, after-tax Return on Equity (ROE) and before-tax Return on Assets (ROA) also improved during the review period. The ratio of after-tax income to average shareholders' funds (after-tax ROE) increased to 17.6 percent in October 2018 from 14.4 percent in October 2017 The ratio of income before-tax to average total assets (before tax ROA) however recorded a modest increase to 3.3 percent from 3.0 percent during the same comparative period. The ratio of after-tax income to gross income (profitability ratio) also increased to 15.6 percent in October 2018 from 12.3 percent in October 2017, indicating that the banking industry continues to be profitable. [See Annexes Table 6]

(b) Interest Margin and Spread

The contraction in banks' gross income in October 2018 resulted in a decline to 11.7 percent in the ratio of gross income to total assets (asset utilisation) from 14.6 percent in October 2017, pointing to some moderation in the incomes generated from banks' assets. Banks' interest spread also narrowed to 8.1 percent from 9.5 percent during the same review period reflecting general declines in money market rates. Similarly, interest margin to total assets declined to 5.7 percent from 6.9 percent while interest margin to gross income increased from 47.3 percent in October 2017 to 48.9 percent in October 2018 over the same review period. [See Annexes Table 6]

(c) Composition of Banks' Income

The composition of banks' income in October 2018 broadly showed an increase in the shares of non-interest income sources (incomes from investment, commissions and fees and other income) relative to interest income. The share of banks' income from investments (both short and long-term) increased to 42.9 percent in October 2018 from 39.6 percent in October 2017, making investments the largest source of income for banks. The share of income from loans declined to 36.1 percent from 44.9 percent during the period under review, consistent with the slowdown in credit growth. The share of banks' income from commissions and fees also increased to

12.7 percent in October 2018 from 10.4 percent a year earlier, while the other income sources for banks constituted 8.2 percent of their total income in October 2018 from 5.0 percent a year ago.

3.3.4 Operational Efficiency

The banking industry's operational efficiency indicators broadly improved as cost to income ratio declined to 84.3 percent in October 2018 from 87.6 percent in October 2017, while cost to total assets ratio declined to 9.9 percent from 12.8 percent during the same comparative period. Similarly, operational cost to total assets declined to 6.4 percent in October 2018 from 7.3 percent in October 2017, while operational cost to gross income ratio increased to 54.1 percent from 50.4 percent in the period under review, due to a slower growth in the industry's gross income. Overall, the industry was more efficient at minimizing costs relative to assets and income in October 2018 than last year.

Financial Soundness Indicators (FSIs)

3.4 BANKS' COUNTERPARTY RELATIONSHIPS

Banks' offshore activities turned out a mixed performance in October 2018 relative to the same period last year, with a pickup in external borrowing while growth in offshore balances moderated.

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

Banks' offshore balances increased to GH¢9.70 billion (25.2percent y/y growth) in October 2018 from GH¢7.74 billion (30.0percent y/y growth) in October 2017. The slower growth of banks' offshore balances came largely from the contraction in banks' nostro balances (from 64.3percent in October 2017 to -1.2percent in October 2018), while other claims on non-residents or placements grew sharply to 59.4 percent in October 2018 from 2.7 percent in October 2017. The slowdown in banks' offshore balances points to some moderation in the industry's exposure to cross-border risks. [See Annexes Table 8]

The share of banks' borrowing from foreign counterparties in total borrowed funds increased to 43.9 percent in October 2018 from 25.3 percent in October 2017 while the share for domestically borrowed funds dropped to 56.1 percent from 74.7 percent during the same review period. The proportion of banks' short-term borrowing in total external borrowing increased to 63.7 percent in October 2018 from 49.0 percent in October 2017, while the share of long-term external borrowing declined to 36.3 percent from 51.0 percent during the same comparative period.

4. CREDIT CONDITIONS SURVEY

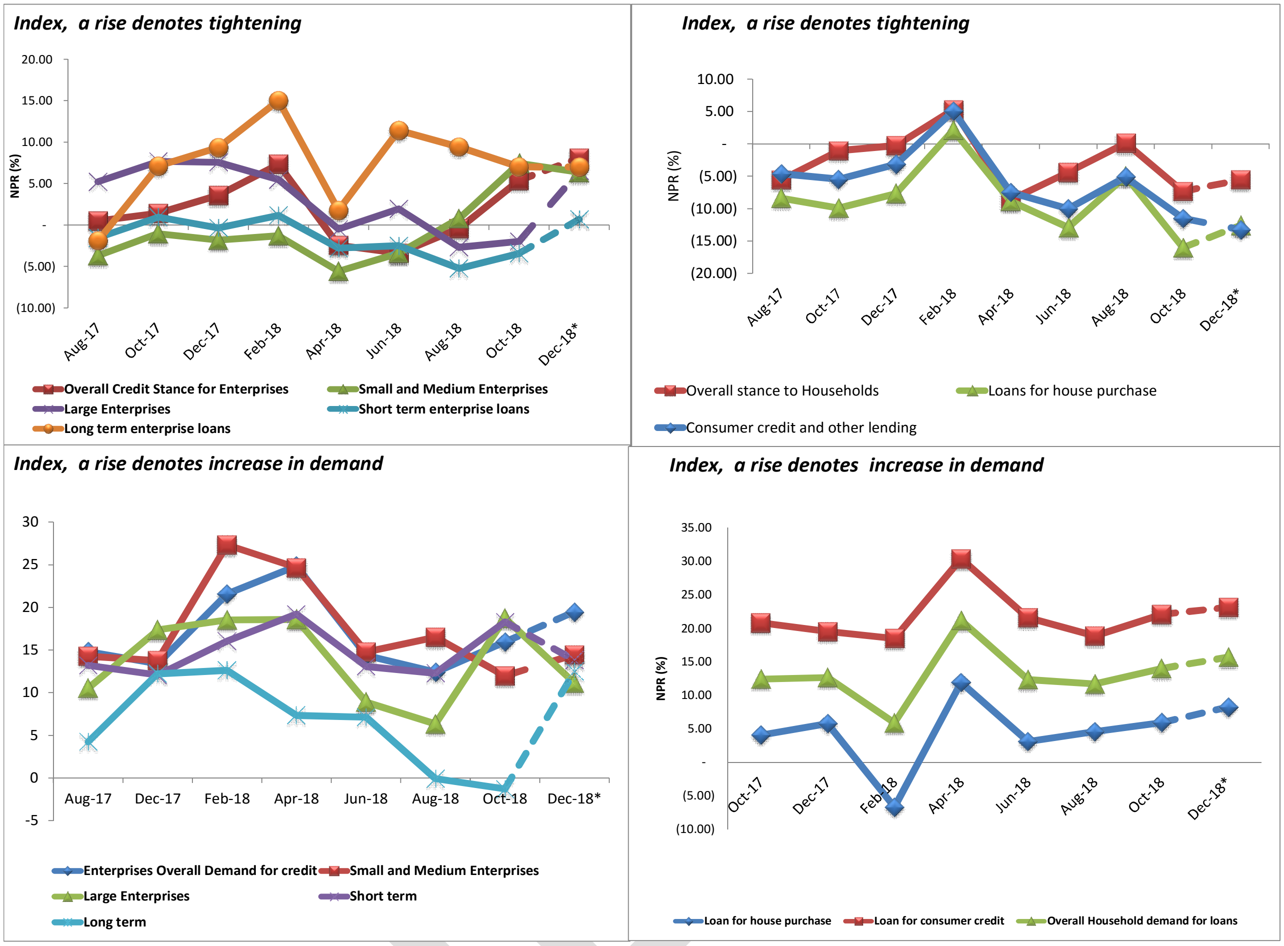
The October 2018 survey round of the Credit Conditions revealed net tightening of overall credit stance to enterprises following a net tightened stance on loans to large enterprises, Small and Medium Enterprises (SMEs) as well as short-term enterprise loans. However, banks' stance on long-term enterprise loans eased in net terms during the current survey round compared with the August 2018 survey round. Banks also reported that they expect the stance on overall enterprise credit to tighten further, two months from the October 2018 survey round. Similarly, banks expect credit stance on loans to large enterprises as well as short-term enterprise loans to tighten two months on, while the stance on loans to SMEs is projected to ease on net basis. The net stance on long-term enterprise loans was projected to remain broadly unchanged between October 2018 and the next survey round in December 2018. Banks' tight credit stance on loans to enterprises was in response to the high stock of the industry's adversely classified loans and risks associated with performance of the industry's largest borrowers. Banks' stance on credit to enterprises also reflected concerns with the current and expected capital positions as the deadline for recapitalization approaches, and cost of funds and balance sheet constraints.

The survey findings however pointed to net easing in banks' overall credit stance to households for mortgages, consumer credit and other lending. Banks however expect the credit stance on overall loans to households and loans for house purchase to tighten over the next two months, and moderated by a net ease in the stance on loans for consumer credit and other lending. The net ease in banks' stance on loans to households broadly supports the pickup in credit to households as indicated by the prudential returns.

The October 2018 survey also reported an increase in the overall demand for enterprise credit, largely from increased demand for loans by large enterprises and short term enterprise loans. Demand for loans by SMEs and long-term loans dipped during the survey period but are projected to pick up over the next two months. Banks reported that overall demand for credit by enterprises are expected to increase due to a sharp increase in demand for long-term loans, alongside a modest increase in demand for loans by SMEs. Both demand for loans by large enterprises and short-term enterprise loans are projected to decline over the next two months, moderating the expected increase in demand for long-term loans over the same period. The survey also reported a net increase in the overall household demand for credit from increases in demand for loans for house purchases and consumer credit and other lending. Banks expect the increase in the demand for loans by households to continue over the next two months, with increases in the demand for credit for house purchase and consumer credit and other lending.

The October 2018 survey round recorded a moderate increase in banks' inflation expectation for the next one year. The marginal increase in inflation expectation was on the back of volatility in the exchange rate during the third quarter. Banks' lending rates expectations however moderated compared with the August 2018 survey round. The expected decline in the bank lending rates has been gradual despite the introduction of the Ghana Reference Rate (GRR) and declining trends in money market rates, due to the high stock of NPLs.

Credit Conditions Survey



5. CONCLUSION AND OUTLOOK

Broadly, the performance of the banking industry improved in October 2018 compared with the performance in October 2017. The industry remains stable and resilient as indicated by the key financial soundness indicators. With just a few weeks to the deadline for banks' recapitalization, many banks are close to meeting the new minimum capital requirement and a few others concluding merger discussions. The industry will likely witness some consolidation, voluntary winding down or downgrade of some banks' licenses to lower-tiered financial institutions in response to efforts at meeting the new minimum capital. All these developments will contribute to creating a well-capitalized and resilient banking system capable of supporting economic growth.

ANNEXES

Table 1: Asset and Liability Structure of the Banking Sector

	Oct-15	Oct-16	Oct-17	Aug-18	Oct-18
Components of Assets (% of Total)					
Cash and Due from Banks	26.3	24.4	25.1	25.58	23.7
Investments	20.6	27.0	29.6	38.76	40.3
Net Advances	44.5	40.2	35.8	27.57	28.7
Other Assets	5.3	4.6	5.5	4.24	3.6
Fixed Assets	3.3	3.6	3.9	3.77	3.6
Components of Liabilities & Shareholders Funds(% of Total)					
Total Deposits	62.4	64.0	62.8	64.7	63.4
Total Borrowings	16.3	16.5	17.0	16.0	17.0
Other Liabilities	6.5	5.8	7.2	6.2	6.6
Shareholders' Funds	14.8	13.7	13.1	13.0	13.1

Gross Loans and Credit Growth

	Oct-15	Oct-16	Oct-17	Aug-18	Oct-18
Gross Loans and Advances (GH¢m)	29,326.60	34,268.85	38,364.52	33,777.89	35,480.00
Nominal Growth (y-o-y)	22.1	16.9	12.0	(9.4)	(7.5)
Real Growth (y-o-y)	4.0	0.9	0.3	(17.5)	(15.6)
Private Sector Credit (GH¢m)	27,112.44	31,188.83	35,437.92	31,537.31	33,126.09
Nominal Growth (y-o-y)	23.5	15.0	13.6	-7.7	-6.5
Real Growth (y-o-y)	5.2	-0.6	1.8	-16.0	-14.7
Household Loans (GH¢m)	4,284.47	4,738.20	5,470.67	6,498.13	6,654.14
Nominal Growth (y-o-y)	18.3	10.6	15.5	19.6	21.6
Real Growth (y-o-y)	3.2	2.8	3.4	8.1	11.1

Table 3: Contingent Liability

	Oct-15	Oct-16	Oct-17	Aug-18	Oct-18
Contingent Liabilities (GH¢)	7,283.2	6,754.7	8,904.7	8,806.6	9,347.7
Growth (y-o-y)	10.5	(7.3)	23.3	12.4	6.1
% of Total Liabilities	14.3	10.6	11.5	9.7	10.1

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

	Oct-16		Oct-17		Aug-18		Oct-18	
	Share in Total Credit	Share in NPLs	Share in Total Credit	Share in NPLs	Share in Tota Credit	Share in NPLs	Share in Total Credit	Share in NPLs
a. Public Sector	**15.3**	**11.3**	**11.9**	**5.3**	**7.6**	**5.6**	**7.6**	**4.5**
i. Government	1.8	1.3	1.5	0.9	2.7	1.1	2.6	0.8
ii. Public Institutions	7.6	0.1	3.5	0.1	0.9	0.3	0.8	0.3
iii. Public Enterprises	5.8	9.8	6.9	4.3	4.0	4.2	4.2	3.4
b. Private Sector	**84.7**	**88.7**	**88.1**	**94.7**	**92.4**	**94.4**	**92.4**	**95.5**
i. Private Enterprises	67.8	83.3	71.1	89.0	68.5	85.0	66.2	83.7
o/w Foreign	8.8	7.7	9.5	10.8	9.5	10.3	9.3	10.5
Indigeneous	59.1	75.6	61.6	78.2	59.0	74.6	56.9	73.2
ii. Households	14.7	5.1	15.3	5.3	22.2	8.8	24.3	11.3
iii. Others	2.1	0.4	1.8	0.5	1.7	0.7	1.9	0.6

Table 5: Liquidity Ratios

	Oct-15	Oct-16	Oct-17	Aug-18	Oct-18
Liquid Assets (Core) - (GH¢'million)	15,712.8	18,022.0	22,313.83	26,764.4	25,216.2
Liquid Assets (Broad) -(GH¢'million)	27,625.8	37,536.7	48,190.81	66,890.3	67,630.1
Liquid Assets to total deposits (Core)-%	42.1	38.2	40.0	39.5	37.4
Liquid Assets to total deposits (Broad)- %	74.0	79.5	86.3	98.7	100.4
Liquid assets to total assets (Core)- %	26.3	24.4	25.1	25.6	23.7
Liquid assets to total assets (Broad)- %	46.2	50.9	54.2	63.9	63.6

Table 6: Profitability Indicators (%)

	Oct-16	Oct-17	Aug-18	Oct-18
Gross Yield	22.4	17.0	10.3	13.1
Int Payable	9.7	7.5	4.0	5.0
Spread	12.7	9.5	6.3	8.1
Asset Utilitisation	15.3	14.6	9.3	11.7
Interest Margin to Total Assets	7.3	6.9	4.5	5.7
Interest Margin to Gross income	47.8	47.3	48.6	48.9
Profitability Ratio	14.0	12.3	16.7	15.6
Return On Equity (%) after tax	20.2	14.4	16.9	17.6
Return On Assets (%) before tax	4.3	3.0	3.3	3.3

Table 7: DMBs' Income Statement Highlights

	Oct-16	Oct-17	Aug-18	Oct-18	Oct-17	Oct-18
	(GH ¢'million)				Y-on-y Growth (%)	
Interest Income	9,501.84	10,943.49	7,647.08	9,874.54	15.2	(9.8)
Interest Expenses	4,107.26	4,819.66	2,933.51	3,770.70	17.3	(21.8)
Net Interest Income	**5,394.58**	**6,123.84**	**4,713.57**	**6,103.84**	13.5	(0.3)
Fees and Commissions (Net)	1,218.79	1,346.63	1,242.71	1,590.24	10.5	18.1
Other Income	568.28	651.05	801.05	1,025.06	14.6	57.4
Operating Income	**7,181.65**	**8,121.51**	**6,757.33**	**8,719.14**	13.1	7.4
Operating Expenses	**3,784.69**	**4,465.74**	**3,632.09**	**4,697.02**	18.0	5.2
Staff Cost (deduct)	2,012.43	2,276.25	1,638.94	2,470.68	13.1	8.5
Other operating Expenses	1,772.26	2,189.49	1,993.15	2,226.33	23.5	1.7
Net Operating Income	**3,396.96**	**3,655.78**	**3,125.24**	**4,022.12**	7.6	10.0
Total Provision (Loan losses, Depreciation & others)	1,048.29	1,234.96	776.47	1,133.41	17.8	(8.2)
Income Before Tax	**2,348.96**	**2,412.82**	**2,337.48**	**2,875.43**	2.7	19.2
Tax	771.32	819.79	719.01	927.46	6.3	13.1
Net Income	**1,577.64**	**1,593.03**	**1,618.48**	**1,947.96**	1.0	22.3
Gross Income	**11,288.91**	**12,941.17**	**9,690.84**	**12,489.84**	14.6	(3.5)

Table 8: Developments in Offshore Balances

	Oct-15	Oct-16	Oct-17	Aug-18	Oct-18
Offshore balances as % to Networth	51.9	58.7	66.7	75.9	69.8
Annual Growth in Offshore balances (%)	2.8	29.7	30.0	45.4	25.2
Annual Growth in Nostro Balances (%)	21.4	-20.9	64.3	52.9	-1.2
Annual Growth in Placement (%)	-27.3	167.6	2.7	39.0	59.4