Executive Summary

The Half Year 2014 Banking Sector Financial results are indicative of the turbulences facing the economy. Margins have come under pressure as total cost structures of most banks are misaligned with income generation capacity in the sector. Asset quality remains a common ledge in the sector with banks failing to continuous cleaning-up their loan books. Subsequently, Non-Performing Loans to Gross Total loans in the sector have reached some worrying levels estimated at 18.5% as at 30 June 2014 from 15.9% as at end – December 2013, reflecting the overarching liquidity challenges in the economy. However, at large the banking sector has remained vibrant as the report coverage shows that a total of 11 Banking Institutions posted profits opposed to 4 recording losses. Total deposits nexus have remained largely static at around $4.279 billion with concentration skewed towards 3 major banks, accounting for approximately 50% of deposits market share while the remaining balance was shared amongst the remaining 11 banks. To mitigate credit risk, banks have reduced their lending appetite with the banking sector aggregate loans and advances over the retrospective period abating to around $3.159 billion.

Economic Overview

The economy has remained in recession with key economic fundamentals persisting on the decline. The economic progression is anticipated to remain subdued with official gross prospects estimated at 3.1% in 2014, a downgrade from earlier estimates of 6.4%. The liquidity constrains have remained the major challenging variable to the recovery of the economy. The strong structural imbalance of Zimbabwe's exports and imports makes the country vulnerable to exogenous shocks and represents a significant risk to macroeconomic stability.

The general industrial capacity utilisation of around 40% continues to affect the revenue collections by the government. While the expenditure mix by the government is skewed towards recurrent expenditure, capital formation necessary for investment continues to ebb at around 3% of Total expenditure. On the other hand, funding constrained Central Bank have not been able to provide the lender of last resort function subsequently the cost of funding generally has remained high. The perceived high country risk compounded by policy inconsistencies continues to frustrate the much needed cash inflows in the form of foreign direct investments (FDIs) and external lines of credit.

Selected Banking Sector Developments

- Capital Bank voluntarily surrendered banking license with the subsequent cancellation of the same by the Registrar of Banking Institutions.
- The Reserve Bank of Zimbabwe established a National Special Purpose Vehicle known as Zimbabwe Asset Management Corporation (Private) Limited to acquire collateralized NPLs from local Banks.
- The RBZ proposes the establishment of the credit reference bureau to alleviate the existing information asymmetry in the credit environment.
- The RBZ Governor reviewed the deadline for the capital requirement compliance to 31 December 2020 with new minimum capital requirements settings into three tier segments; **Tier I** with minimum threshold of $100m, **Tier II** and **Tier III** at $25m and $7.5m respectively.
- The interbank market facility guaranteed by Afreximbank is earmarked to be operational by mid-September 2014.
- Authorized Dealers (Banks) will now be required to maintain a maximum of 5% of the Foreign Currency Account (FCA) balances in their Nostro Accounts from the previous 30% to improve liquidity in the economy.

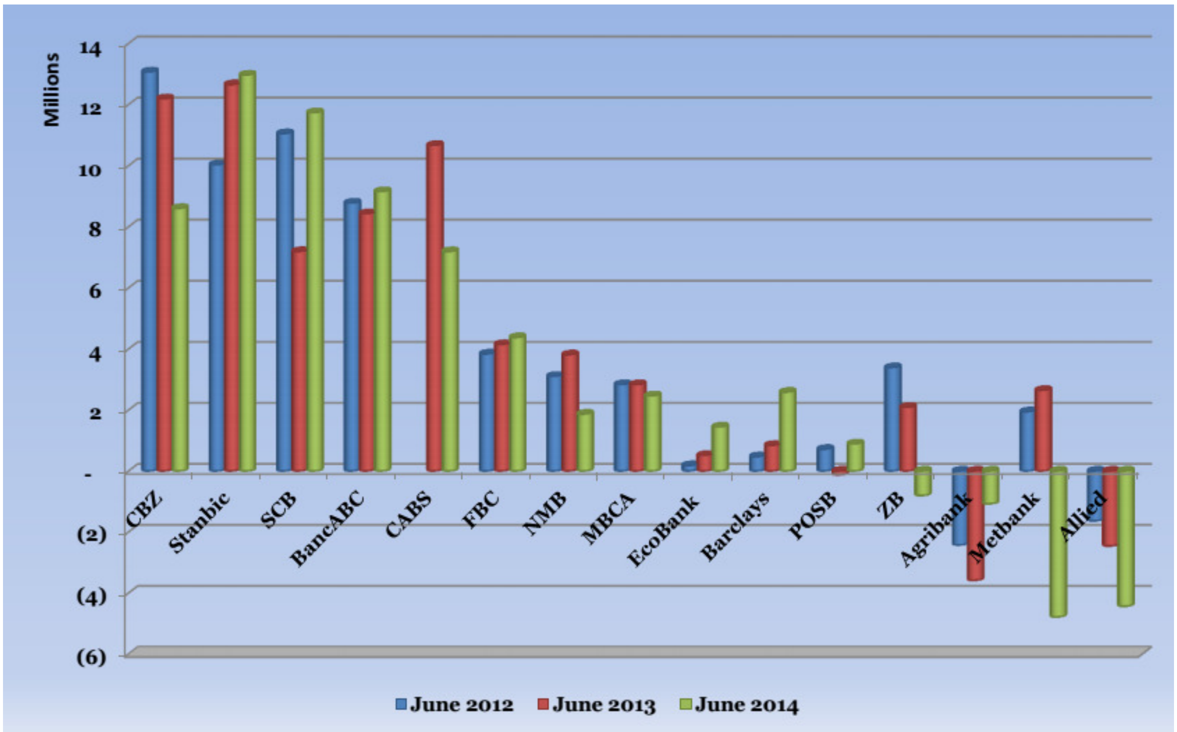
Money Supply

- Tight liquidity constraints have continued to dog the economy and to be the most immediate challenge at the detriment of the business environment.
- Cognisance of the scarcity of the liquidity conditions in the economy, money supply totals have remained largely short-term in nature.
- The lines of credit have continued to be elusive attributable to the perceived high country risk. In case the where regional and international financiers have been willing to extend the credit facilities; the pricing structures have been very prohibitive.
- The annual growth in broad money edged up 12.6 percent to $4,323.6 million as at end-June 2104 from $3,838.2 million as at end-June 2013.
- As a result of the worrying liquidity challenges, low deposit base and the risk averse behaviour due to a spiral increase in NPLs in the banking sector, banks have reduced their propensity on lending. Lending to the private sector dropped marginally by 0.01percent at US$2,955.85 million in June 2014 on prior month.

Profitability

The banking institutions analysed in this report are those that published their half year results and excludes Steward Bank and Afrisia that have their financial year-ends in February and June respectively.

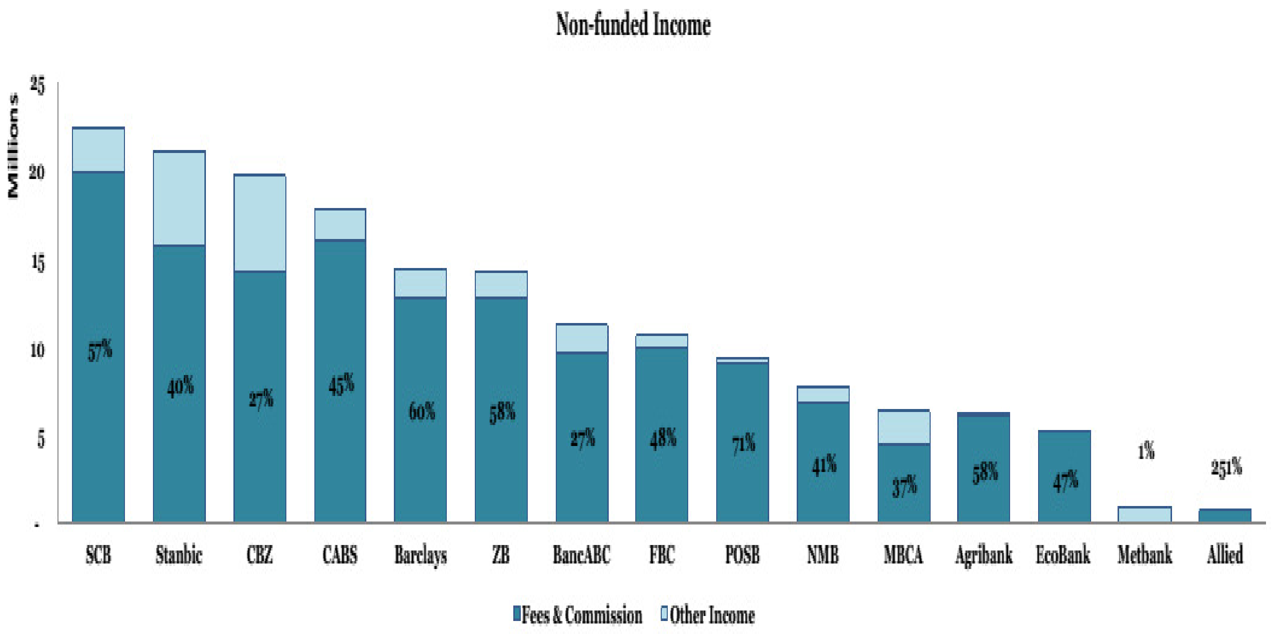
Banks Profit before Taxation (PBT) (US$'m)



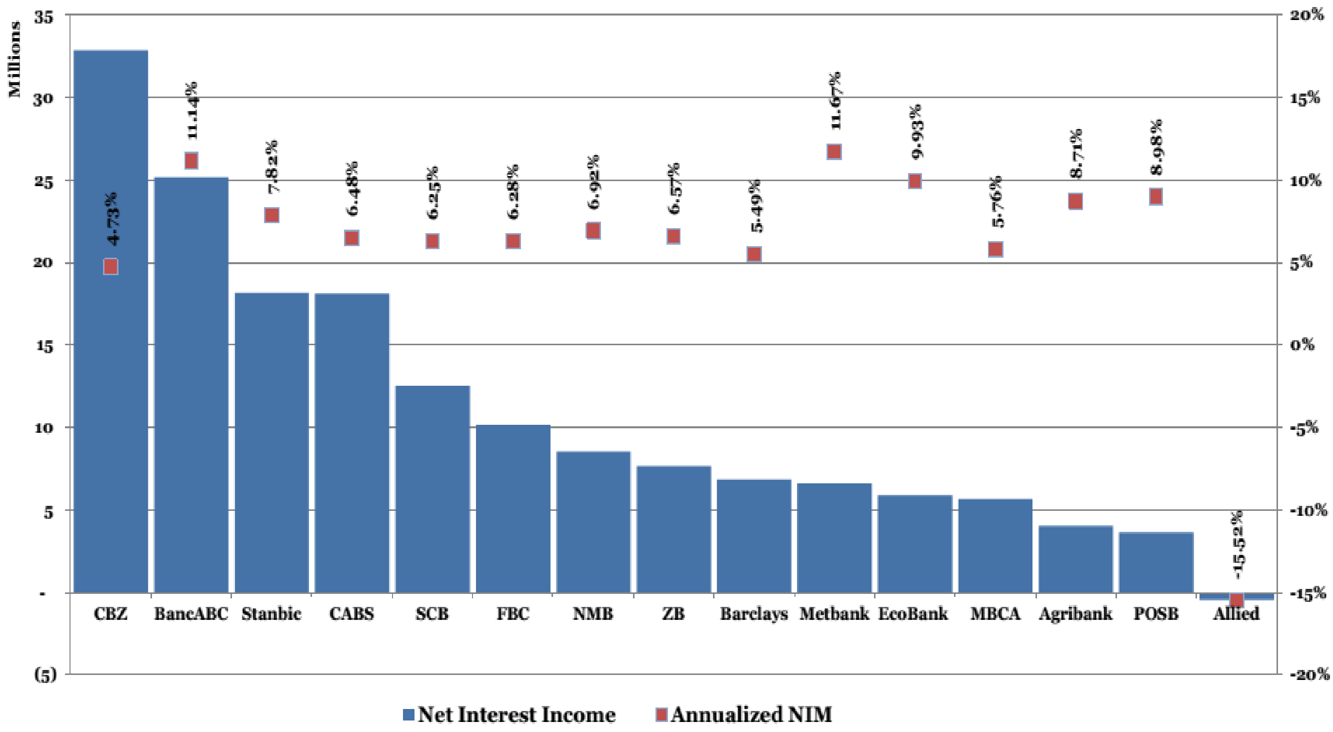
- The below expected half year results performance in terms of profitability is indicative of the tough environment that banks operate in;
- The business conditions have remained tough challenging aggravated by perennial liquidity constraints in the economy.
- The levels of non-performing loans (NPLs) have been on the rise and the multiplier effect has been limited to facilitate transactions by banks.

Non-interest Income

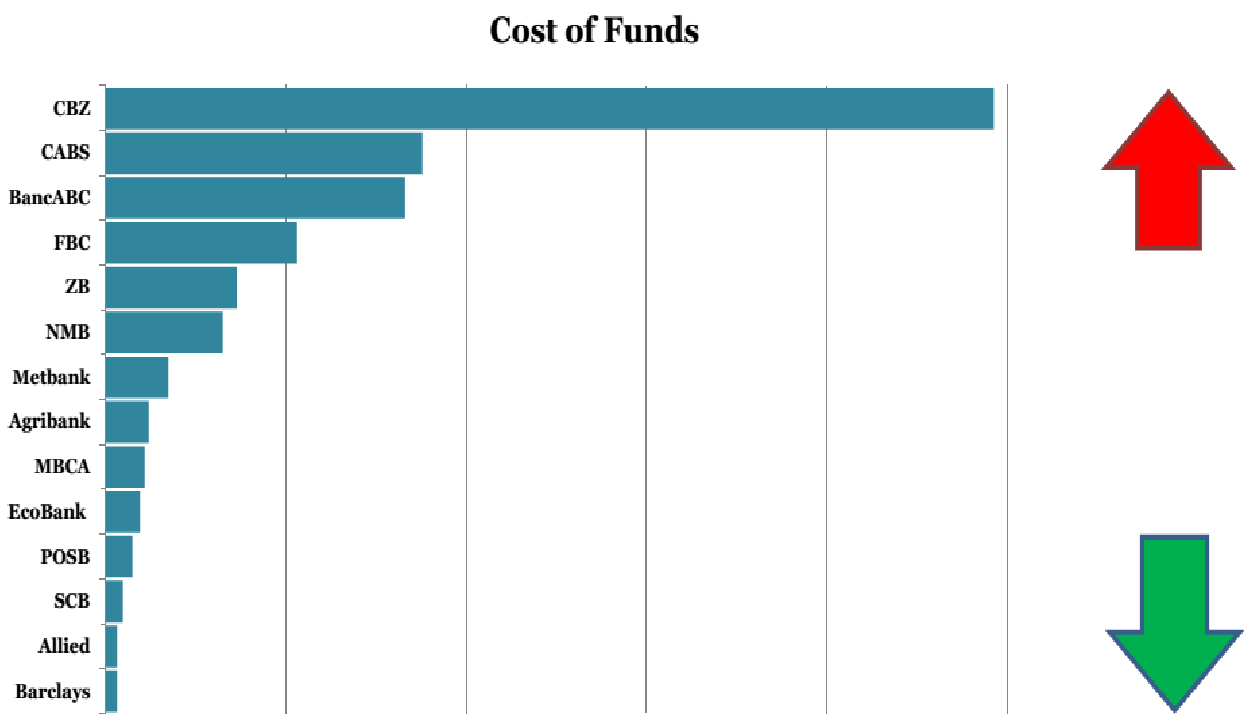
- Institutions with low loans to deposit ratios (low LDR's) non-interest income was the major driver of total income;
- Standard Chartered Bank (SCB) and Stanbic Bank have their incomes thriving non-funded income contributing $22.4 million and $21.1 million of their total income for the period under review.
- On the other hand, CBZ Bank and BancABC both have total incomes that were driven largely by funded income with fees and commission contributing 27% to the total incomes of both institutions.
- BancABC and CBZ Bank's abilities to mobilize deposits and short to medium-term lines of credit have given them the competitive edge to structure facilities that have given them good returns on investments.



Interest Income

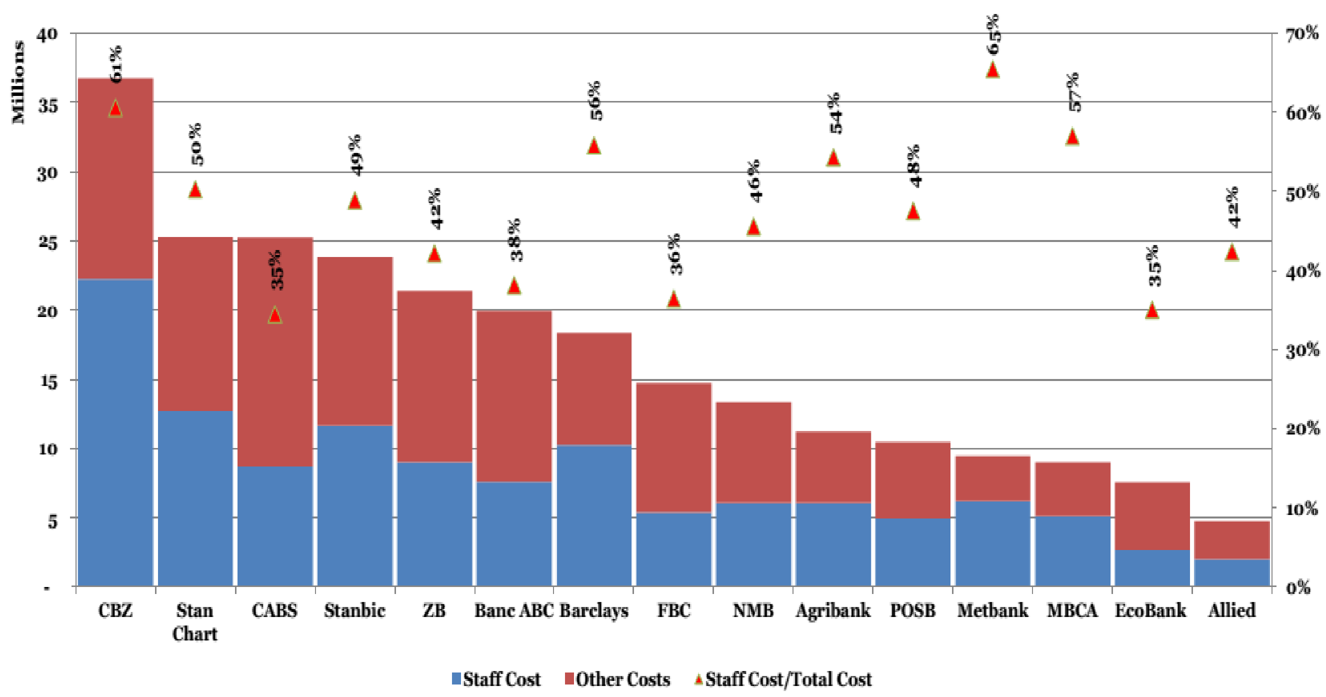


- CBZ Bank was the top earner of funded income riding on its funding base which gave it competitive advantage in the issuance of loans and advance.
- On the flipside, the cost of funding has been on the high side. CBZ Bank occupied the pole position by cost of funding resulting in its net interest margin at 4.73%.
- Internationally-owned banks recorded competitive funded incomes that were complimented by relatively low cost of funding.
- Cost of funding for foreign-owned banks has generally been low as depositors preferred them to locally-owned banks; they are considered the more stable than locally owned banks.



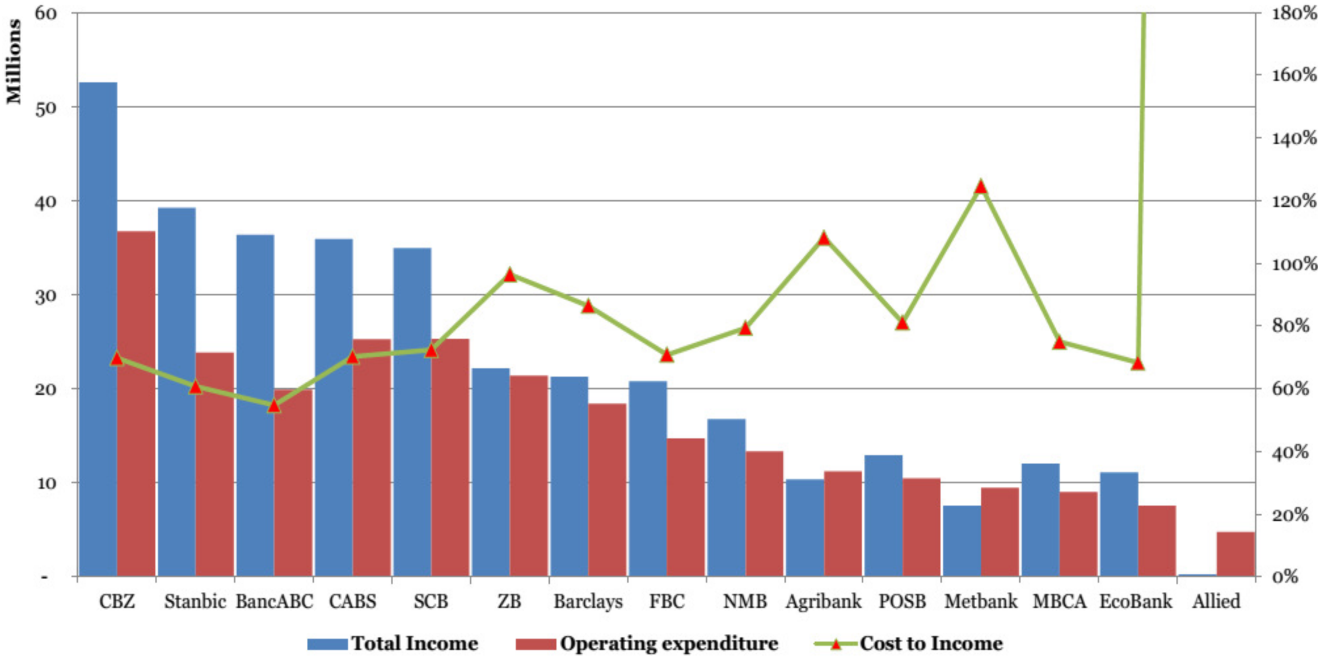
- FBC Bank occupied the 6th position market share by funded income and 5th position when cost of funding is considered.

Operating Expenditure



- The harsh operating environment has resulted in the thinning of margins for most banks and the major cost component of operating expenditure has been staff costs that averaged 48% of the total costs.
- CBZ Bank due to its presence on the market by branch network had the highest ratio of staff cost to total cost of 61%.

Total Expenditure to Total Income Ratio



- The average cost to income ratio for the market was 75%. FBC bank recorded a cost to income ratio of 71%.
- Agribank, Allied Bank and Metbank recorded operating expenditures that exceeded their total incomes thus resultantly had higher levels of cost to income ratios that were above the market average of 75%.
- The above banks including Afrisia Bank Limited are the troubled banks as per the Monetary Policy Statement issued by the Reserve Bank of Zimbabwe.

Measurement of Efficiency

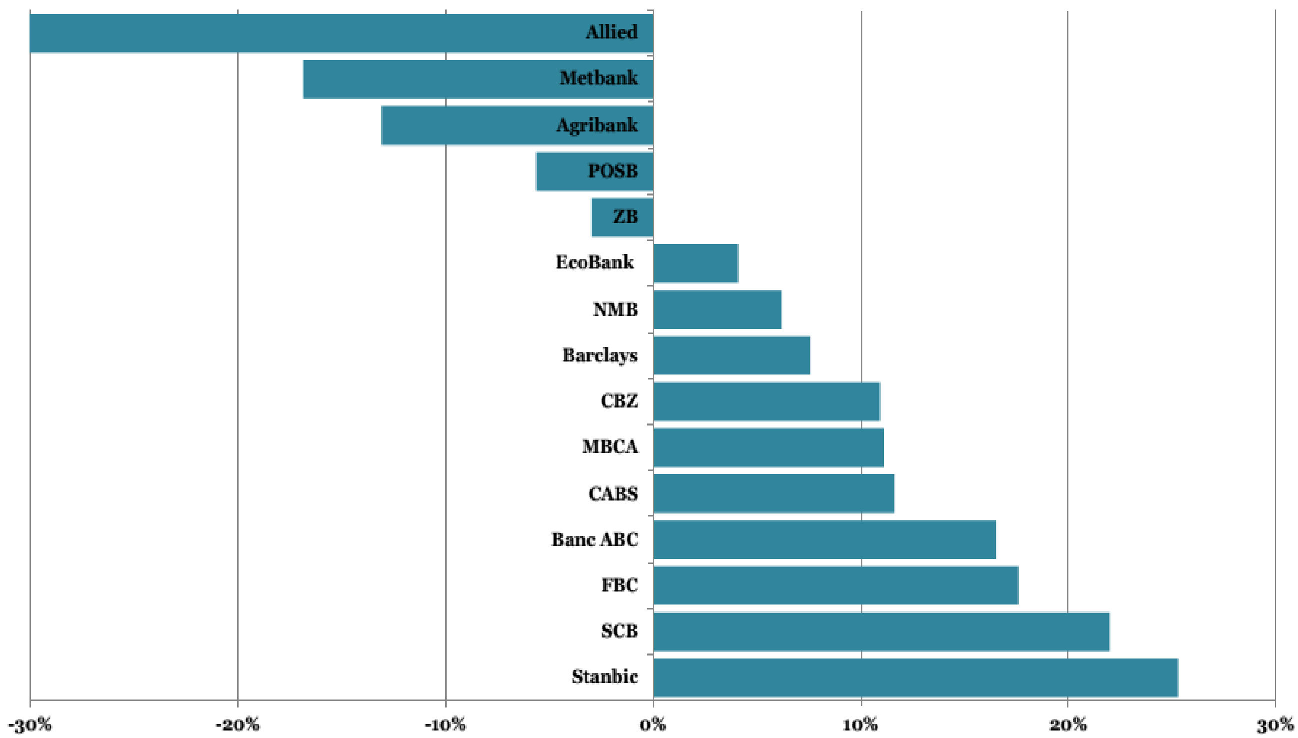
Return on Equity

- Despite the harsh operating environment, most banks managed to give shareholders return on their investments.
- However, Allied Bank, Metbank, POSB and ZB Bank recorded negative returns on shareholders' equities against a market average of 10%.
- FBC Bank recorded a return on equity of 18% and came in on the 3rd position to Stanbic and Standard Chartered Bank; CBZ Bank recorded a ratio of 11%.

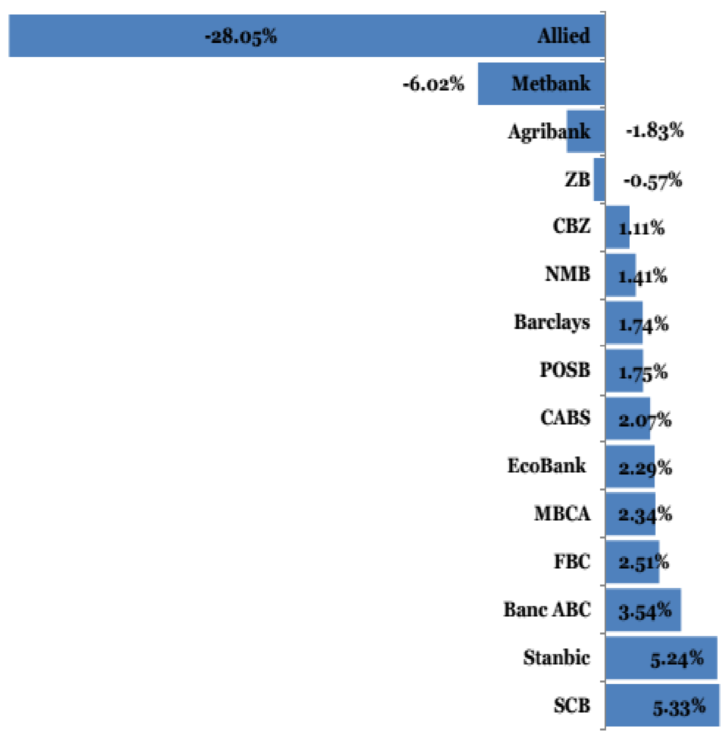
Return on Assets

- FBC Bank is amongst the top banks, on the 4th position, in terms of efficiency to sweat its resources to make profit.
- Standard Chartered Bank, Stanbic Bank and BancABC were the leaders having recorded return on asset ratios of 5.33%, 5.24% and 3.54% respectively.
- CBZ Bank recorded a return on assets of 1.11% and it occupied the 11th position.

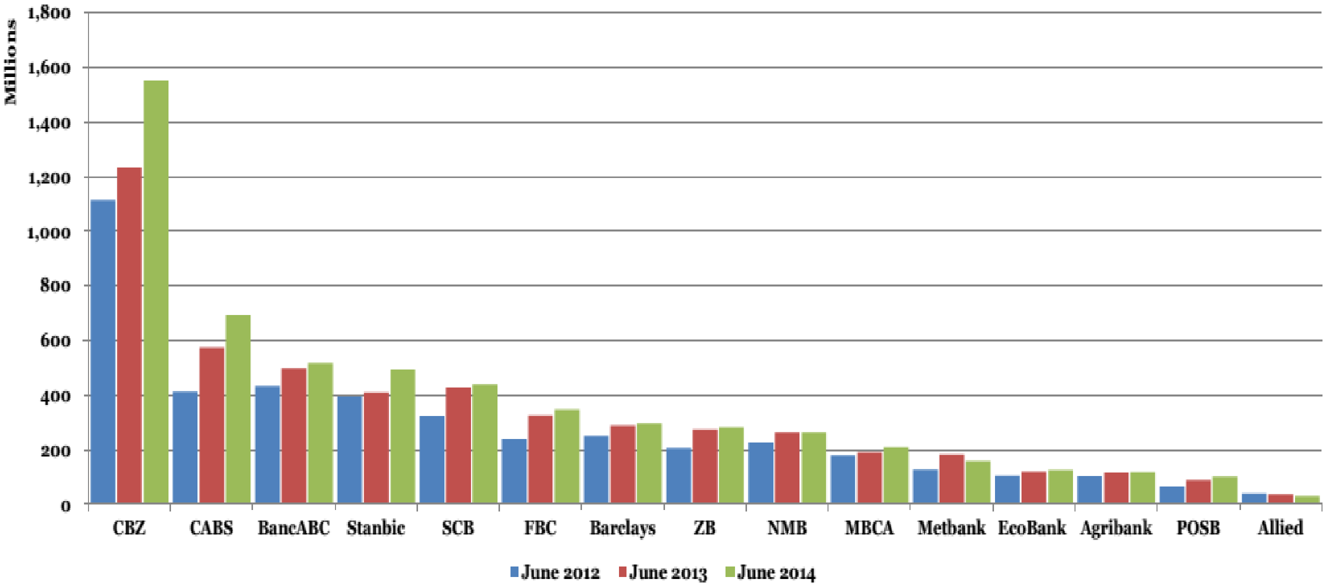
Return on Equity



Return on Assets

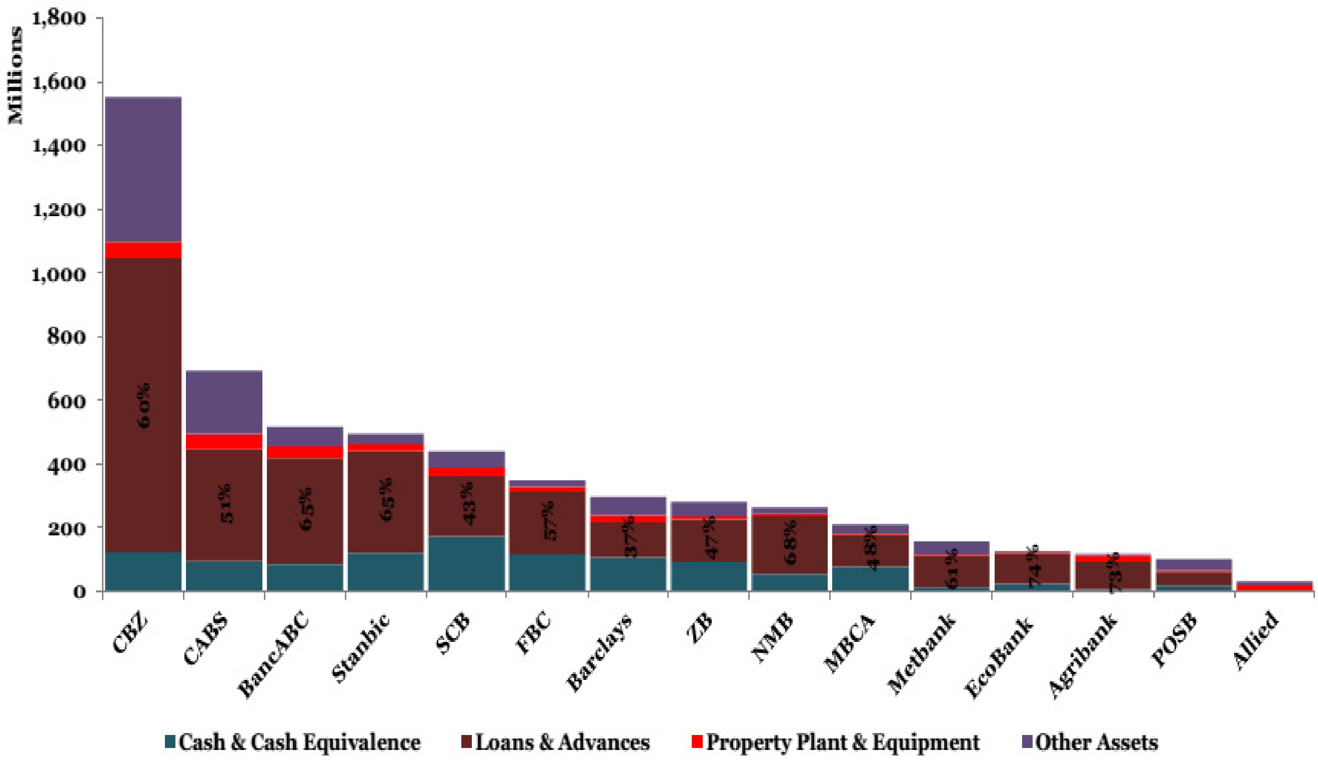


Analysis of Balance Sheet

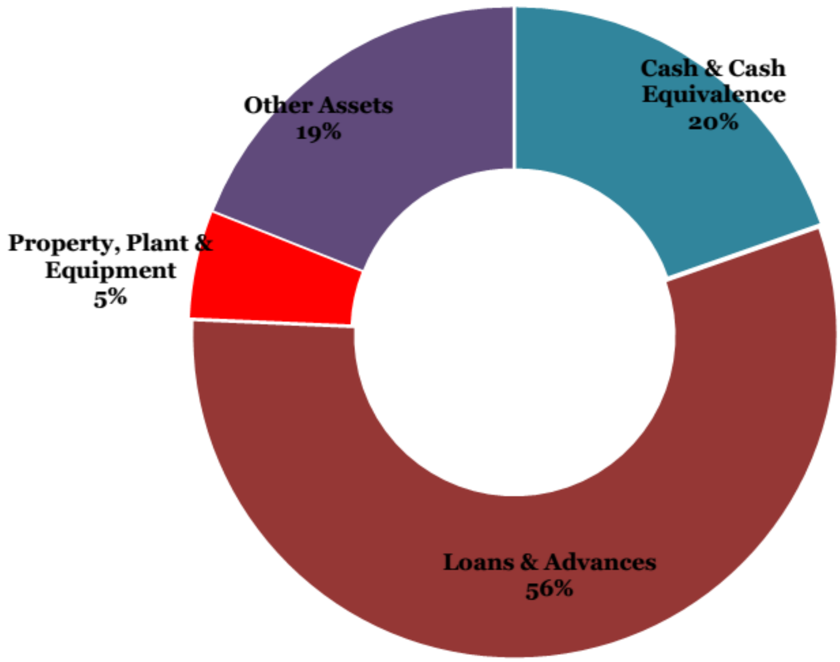


- Despite the harsh economic environment, most banks recorded growth rates on their balance sheets save for Metbank and Allied bank.
- The structures of the balance sheets are such that loans and advances comprise the major part of the total assets.
- This means banks that lead the market share by deposits are the same ones that generally lead the market share by total loans and advances.
- The fixed assets of banks take-up a very little percentage of the total assets of the banks.

Structure of Banks' Assets

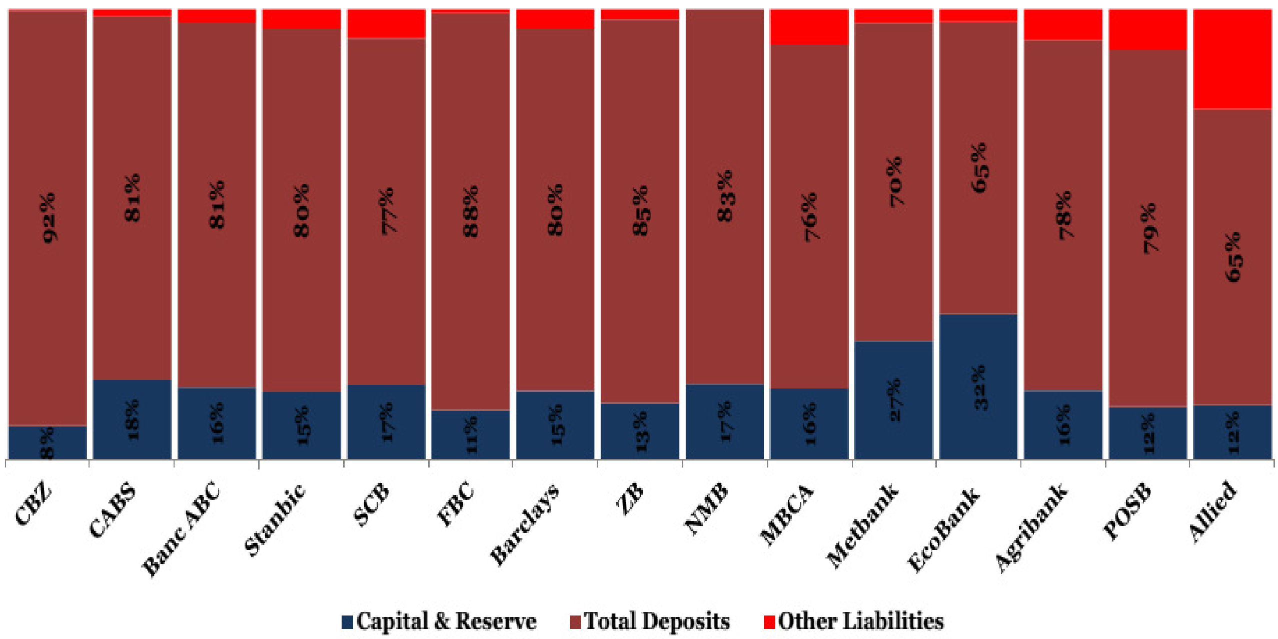


Average Structure of Banks' Assets

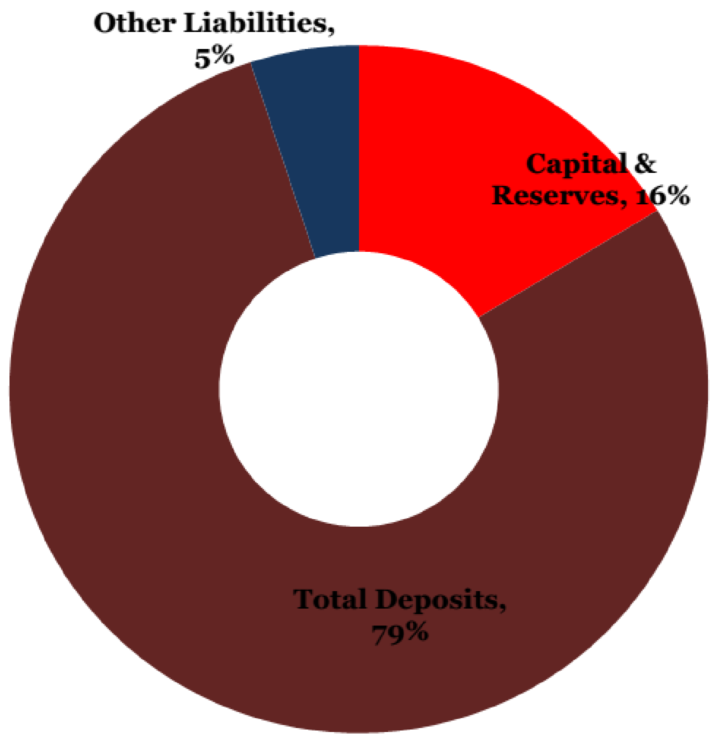


Structure of Liabilities

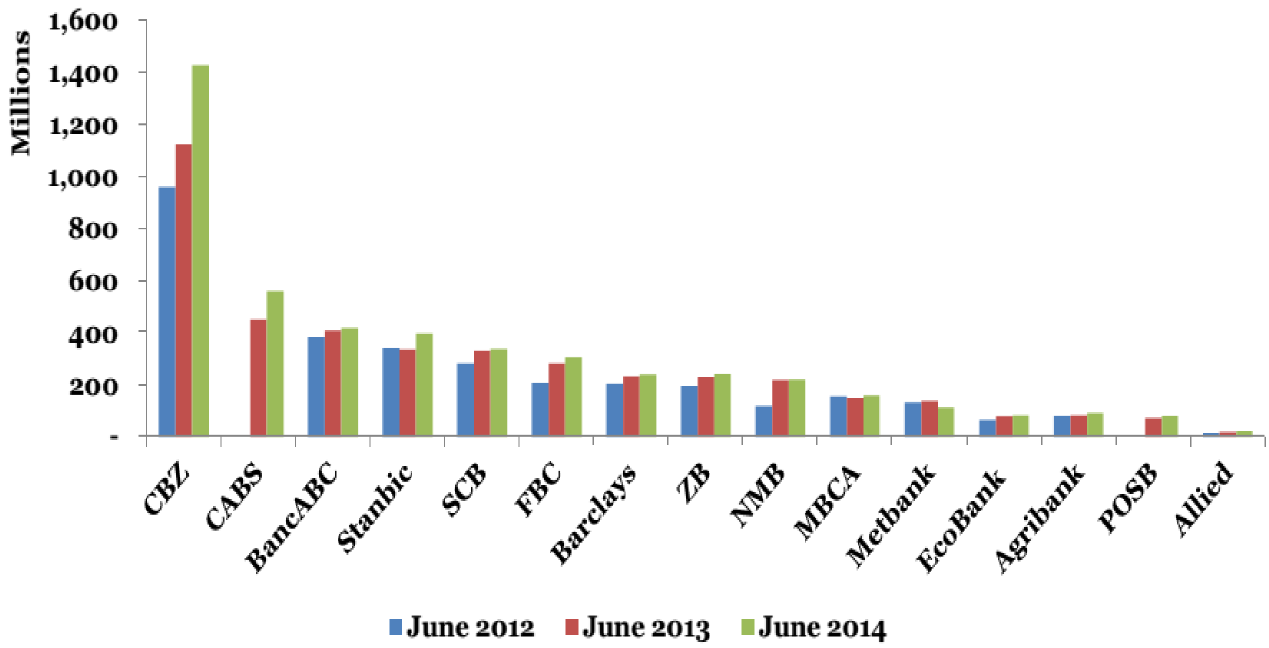
- The major portion of banks' assets were funded majorly by customer deposits constituting 79% of the banks' liabilities.
- This then means that those banks with capacities to mobilize deposits had the competitive advantage to convert them same into assets.
- Capital and reserves constituted 16% and other liabilities constituted 5% of the total liabilities.



Average Structure of Banks' Liabilities

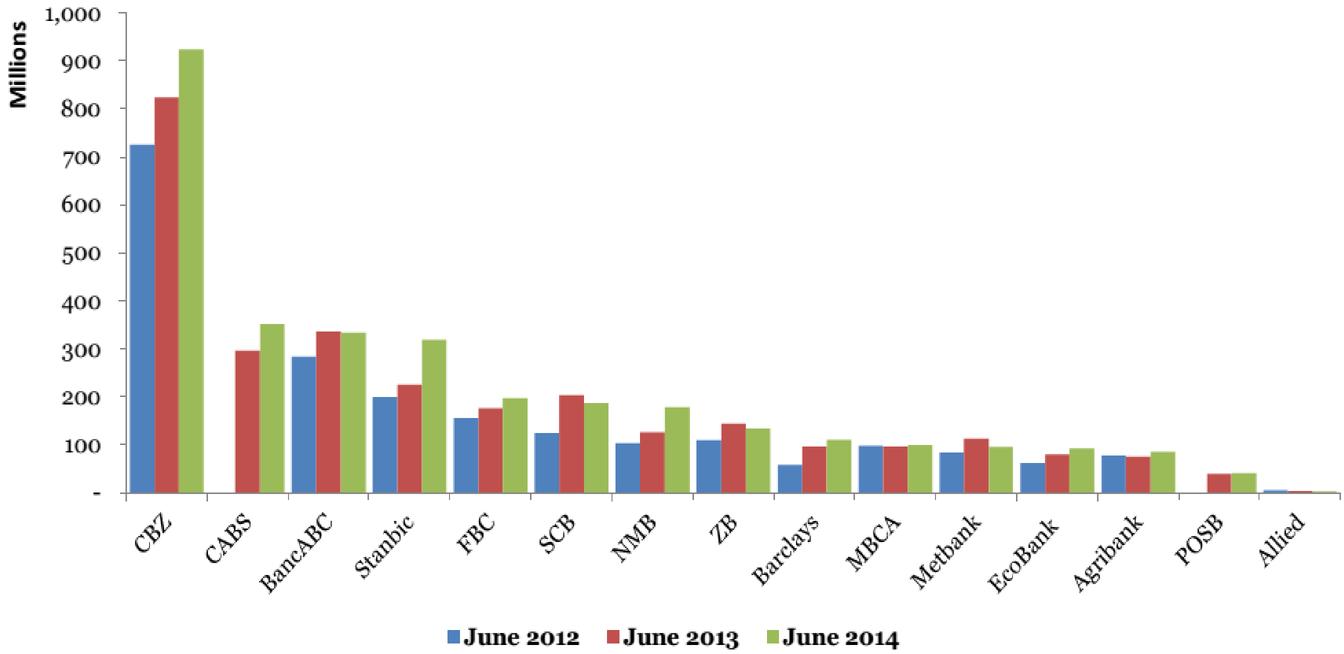


Total Deposits



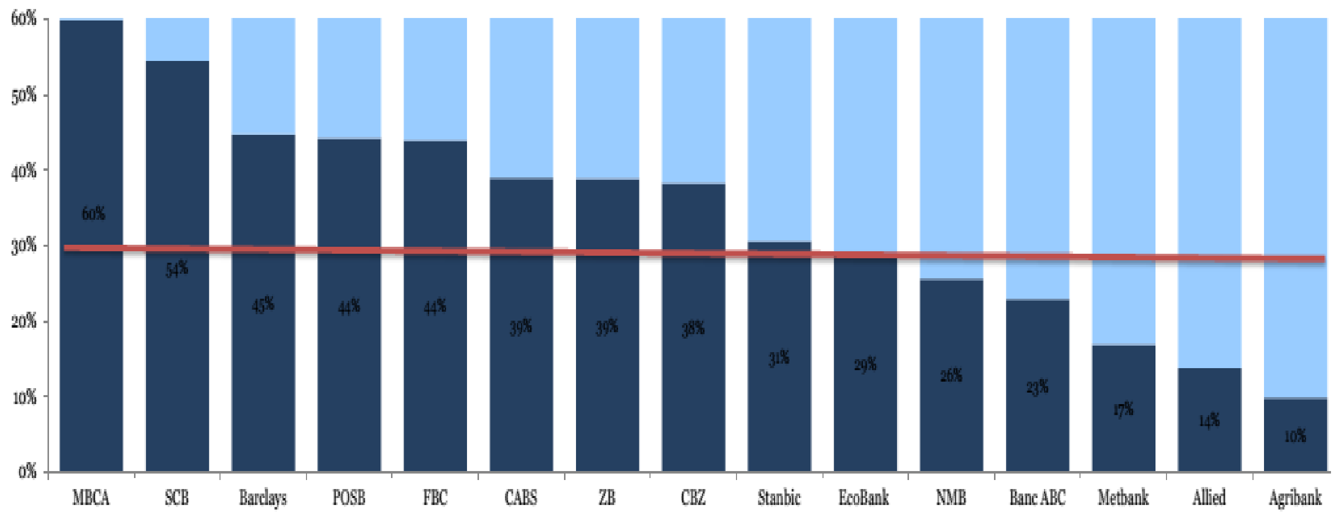
- CBZ Bank continues to the market share leader by total deposits which gave it the competitive advantage to be market share leader by balance sheet size.
- FBC Bank occupied the 6th position and worth noting is the fact that its funding base is on the increase.
- Metbank due to its existing liquidity challenges and battered reputation is witnessing a decline in its deposit base as the customers are looking for alternative banks.

Loans & Advances to Private Sector



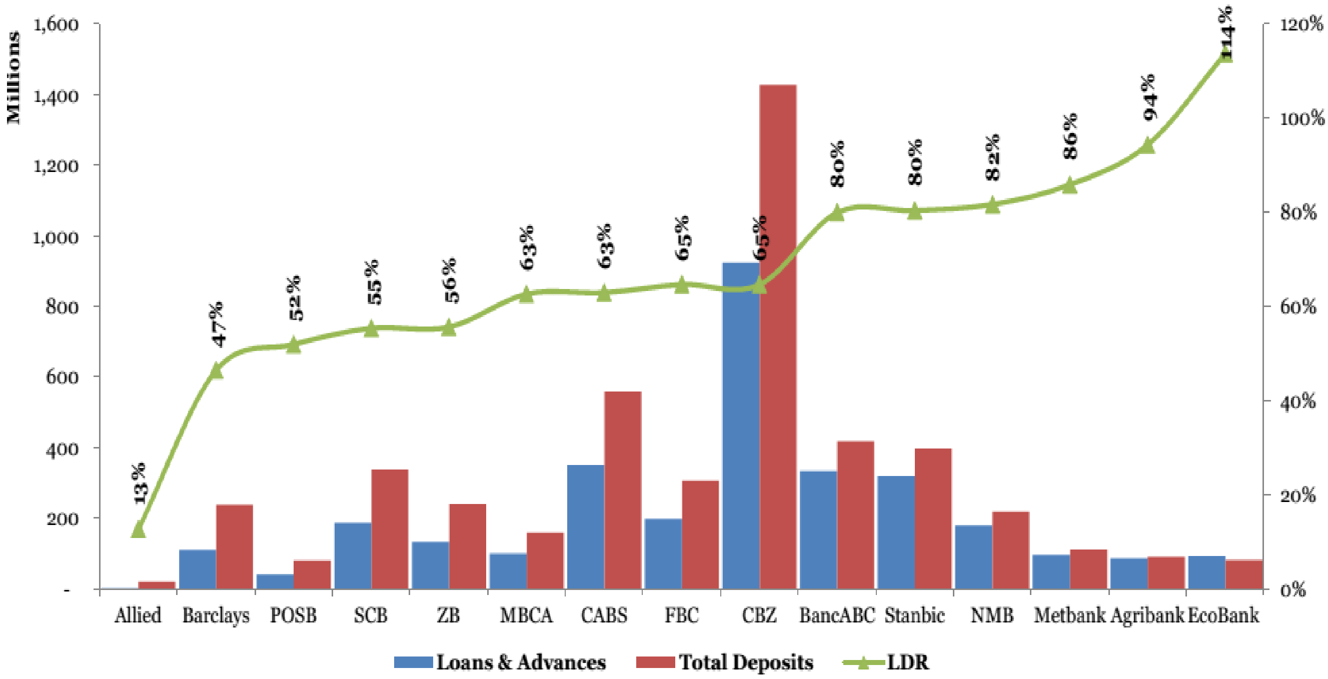
- Capacity to issue credit to the private sector hinges on the ability to mobilize deposits. Thus those institutions with high deposit bases have high levels of credit issued.
- The exception is with Standard Chartered Bank and Barclays Bank that have remained conservative where lending is concerned and have thrived on non-funded income for profitability.

Liquidity Ratios



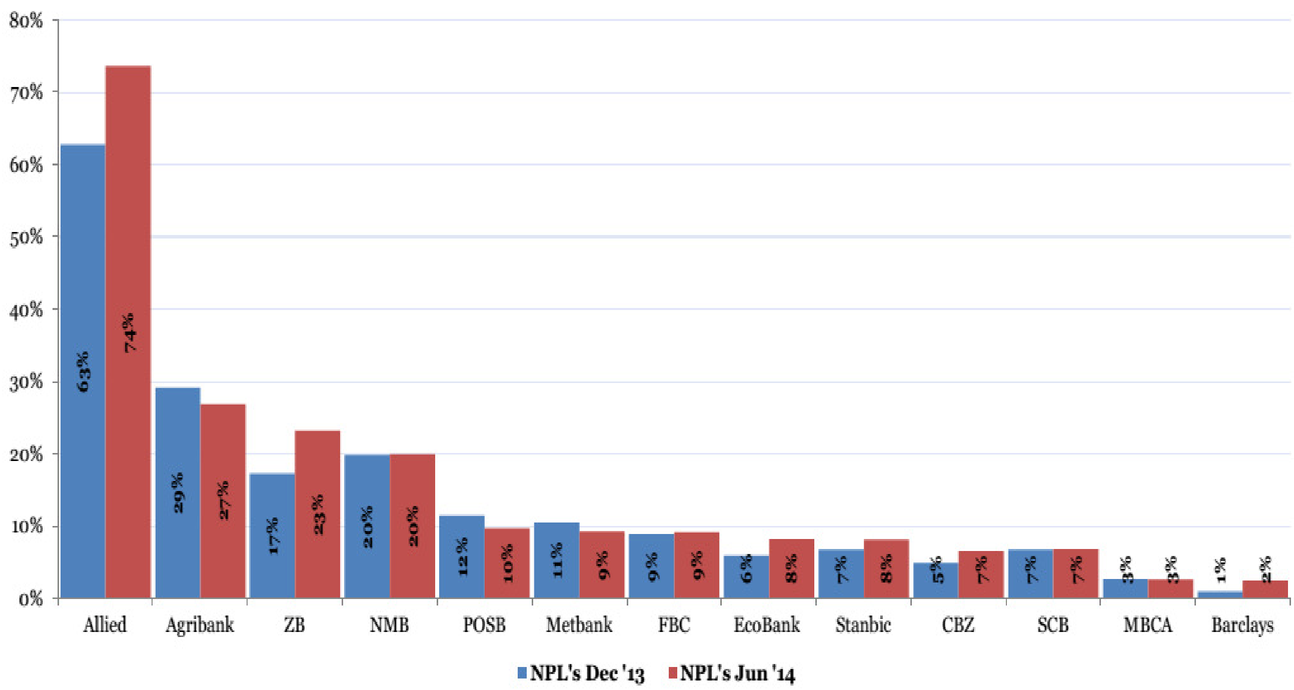
- Though the liquidity challenges have persisted in the economic environment, most banks have operated fairly liquid with 9 out of the 15 banks recording liquidity ratio above the regulatory minimum of 30%.
- Foreign-owned banks; MBCA, Standard Chartered Bank and Barclays Bank enjoy the greater share of the liquidity in the market.

Loans, Total Deposits and LDR



- The average loan to deposit ratio (LDR) for the market stood at 68% and FBC Bank's LDR stood at 65%.
- Generally, banks with high LDR ratios had the lowest liquidity ratios.

Non-performing Loans (NPLs)



- For most banks, the level of non-performing loans (NPLs) to total loans has been on the rise.
- The persistent liquidity challenges in the economy are heightening the surge in non-performing loans as most of the industrial sectors are reeling from lack of working capital to boast productive and resultant alleviate the worsening liquidity crunch.
- The initiatives by the Central Bank to purchase from banks all securitized non-performing loans will go a long way in improving liquidity positions of banks.

Top Ten (10) Ranking Map

	Profitability	Loans	Total Deposits	Balance Sheet
1	Stanbic	CBZ	CBZ	CBZ
2	SCB	CABS	CABS	CABS
3	Banc ABC	BancABC	BancABC	BancABC
4	CBZ	Stanbic	Stanbic	Stanbic
5	CABS	FBC	SCB	SCB
6	FBC	SCB	FBC	FBC
7	Barclays	NMB	ZB	Barclays
8	MBCA	ZB	Barclays	ZB
9	EcoBank	Barclays	NMB	NMB
10	NMB	MBCA	MBCA	MBCA