



Reserve Bank of Malawi

Bank Supervision Department Annual Report 2010



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List of Abbreviation and Acronyms

AML/CFT	-	Anti Money Laundering and Combating Financing of Terrorism
BIS	-	Bank for International Settlement
CAMEL	-	Capital, Asset Quality, Management, Earnings, and Liquidity and Funds Management
CCBG	-	Committee of Central Bank Governors
CDD	-	Customer Due Diligence
CDH	-	Continental Discount House
East AFRITAC	-	IMF East Africa Regional Technical Assistance Centre
ECOBANK	-	ECOBANK Malawi Limited
ESAAMLG	-	East and Southern Africa Anti-Money Laundering Group
FDH BANK	-	FDH Bank Limited
FDH	-	First Discount House Limited
FIU	-	Financial Intelligence Unit
FMB	-	First Merchant Bank
FSI	-	Financial Stability Institute
FSVC	-	Financial Services Volunteer Corps
GOVT	-	Malawi Government
ICAAP	-	Internal Capital Adequacy Assessment Process
ICB	-	International Commercial Bank
IMF	-	International Monetary Fund
INDEBANK	-	Indebank Limited
ICT	-	Information Communications Technology
LFC	-	Leasing and Finance Company Limited
LRS	-	Local Registered Stock
MSB	-	Malawi Savings Bank
NBM	-	National Bank of Malawi
NBS	-	NBS Bank
NEDBANK	-	NEDBANK Malawi Limited
NPL	-	Non-performing loans
OD	-	Overdraft
OIBM	-	Opportunity International Bank of Malawi
RBM	-	Reserve Bank of Malawi
RBS	-	Risk Based Supervision
RMP	-	Risk Management Programmes
ROA	-	Return on Asset
ROE	-	Return on Equity
SADC	-	Southern Africa Development Community
SSBS	-	SADC Sub-committee of Banking Supervisors
STANDARD BANK	-	Standard Bank Malawi Limited
QIS	-	Quantitative Impact Survey
USAID	-	United States Agency for International Development

Mission Statement

As Bank Supervision Department of the Reserve Bank of Malawi, we aim at ensuring the existence of a sound and stable banking industry in Malawi in line with international supervisory standards.

This will be achieved through entry and exit control, off-site surveillance, on-site examinations, and timely submission of reports of findings to Executive Management of the Reserve Bank of Malawi, commercial banks and registered financial institutions.

In pursuance of our goal, we will endeavour to perform our work with professionalism, integrity, impartiality, and in a friendly and cooperative manner but with no compromise to our authority.

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Message from the Registrar of Financial Institutions



In pursuance of Section 18 of the Financial Services Act 2010, I am pleased to present the 2010 Bank Supervision Annual Report. Not only does the report highlight the developments in the Malawi banking sector during the year ended 31st December 2010, it further seeks to open up to investors both existing and potential, researchers, academicians and the general public, on the key activities that were undertaken by Bank Supervision Department in its continued effort to serve the best interests of the general public and the economy at large.

The report attests to the various steps taken by Government in the area of macroeconomic management and regulation that have created a platform and

impetus for the banking sector to remain vibrant. The year 2010 has seen the sector continue its growth path, inter-alia in terms of funding, assets, profitability, capitalisation and product innovation. We reaffirm our commitment to support this direction.

During the year, the Department undertook several activities in its quest to ensure a safe and stable banking system. Notably, significant strides were made with regard to preparatory work for the implementation of Basel II; consolidated supervision; financial inclusion, anti money laundering drive, deposit insurance scheme and review of banking sector laws and regulations. The Financial Services Act, Banking Act and Credit Reference Bureau Act were enacted in 2010 thereby making our regulatory framework more effective and robust.

I wish to thank all the banking institutions operating in Malawi for their cooperation and support as we carry out our supervisory function of ensuring a stable, safe and sound banking system. I also commend the Board of Directors of our banks for steering innovation in the banking sector whilst paying strong attention to risk management. Finally, I thank members of staff in Bank Supervision Department for their continued vigilance, dedication and hard work as they continue to instil market discipline and conduct in the banking system for the general good of the country.

Dr Perks M. Ligoya
REGISTRAR OF FINANCIAL INSTITUTIONS

Foreword from Director Bank Supervision



Welcome to this edition of the 2010 Annual Report for Bank Supervision Department. The report chronicles the performance and major issues that affected the banking sector during the year ended 31st December 2010. The report is part of our continued effort to engage with stakeholders by way of updating them on the performance of the banking sector and the progress made with regard to creating an enabling regulatory framework that supports the best interests of the sector and the economy. We believe that the report will strengthen public understanding of issues pertaining to the supervision of banking institutions and of the RBM's role as the Regulator. We also hope that the report will bolster public

confidence in the soundness of the banking system and contribute to the accountability of the RBM to the public.

In keeping with our mission of ensuring a stable and safe banking system in line with international standards, we continue to enhance the report to ensure that it provides sufficient information to enable users make informed decisions. We however, do not lose focus of our commitment to safeguard individual bank specific data.

The report is organised as follows: Chapter 1 presents an overview of some of the macroeconomic indicators that were key to the performance of the banking sector in 2010, while Chapter 2 provides a general overview of the Malawi banking sector in terms of composition, ownership, balance sheet structure and market share. Chapter 3 discusses the sector's performance focusing on the following key indicators: capital adequacy, asset quality, earnings analysis and liquidity analysis. Overall, all banks remained well capitalised and profitable throughout the year under review. Aggregate total and core capital increased by 23.7 percent and 27.0 percent (i.e. from K25.4 billion and K32.3 billion in December, 2009 to K31.5 billion and K41.1 billion in December, 2010), respectively. The banking sector also registered growth in earnings from K14.9 billion in December 2009 to K16.9 billion in December 2010. The quality of the bank's assets as measured by level of non-performing loans remained satisfactory despite a slight increase in non-performing loans as a percentage of total loans from 3.1 percent in December 2009 to 3.9 percent in December 2010. In terms of liquidity, all banks were considered liquid with an aggregate liquidity ratio of 40.7 percent from 48.1 percent in December 2009. The decrease notwithstanding, the ratio remained above the regulatory benchmark of 30.0 percent.



Chapter 4 outlines the key activities that the Department carried out as part of its supervisory and regulatory mandate. These are broadly categorised into Off Site Surveillance, On-site Examinations, Licensing and Compliance Review, Consumer Complaints Handling, Review of Banking Regulations and Capacity Building. Chapter 5 outlines the current issues in bank supervision and finally Chapter 6, highlights the major activities on regional and international cooperation.

On behalf of Bank Supervision Department I wish to thank the Governor and Executive Management of Reserve Bank of Malawi for the support given to the Department in terms of resources, guidance and direction. I would also like to take the singular honour to thank all banking institutions' Board of Directors and Senior Management for the efforts they have taken in ensuring that their institutions adhere to prudential requirements. In a special way, let me also recognise and thank our cooperating partners for the technical assistance that they rendered to the Department in various areas pertaining to supervision of banks.

Finally, I wish to reaffirm our commitment of ensuring the existence of a sound and stable banking system that serves the best interests of our country's growth and development agenda. As a Department, we remain receptive and encourage feedback from all stakeholders on how best we can make the regulatory framework more effective and supportive of the development needs of the country.

Noel L Mkulichi
DIRECTOR, BANK SUPERVISION



Chapter One

Macroeconomic Conditions in 2010

1.0 Introduction

This Chapter highlights key macroeconomic indicators that had significant bearing on the Malawi banking industry in 2010, namely GDP growth, trends in inflation, exchange rate, interest rates and the balance of payment position.

1.1 Gross Domestic Product

The year under review saw real GDP growth rate at 6.7 percent. This largely stemmed from growth in mining and quarrying activities at the back of increased capacity and utilisation at Kayerekera uranium mine; the expansion in the information and communications services as a result of ongoing development in mobile phone services; as well as growth in the construction and financial sectors. Albeit not comparing favourably with the 7.6 percent registered in the preceding year, the rate still remained above the 6.0 percent annual target set in the Malawi Growth and Development Strategy (MGDS).

1.2 Inflation

From the 8.4 percent registered in 2009, annual average inflation rate went down by 1.0 percentage points to reach 7.4 percent in 2010. The rate remained in single digit range largely on account of reduced inflationary pressures on food prices both in the rural and urban markets resulting from abundant maize supply from the 2009/10 growing season that emanated from Government's fertiliser subsidy programme and favourable weather patterns.

In 2010, annual average food inflation stood at 5.0 percent, compared to 7.3 percent recorded in 2009. On the other hand, non food inflation averaged 9.9 percent in 2010, from 9.6 percent in 2009. The marginal increase was primarily on account of rising transportation costs emanating from a fuel pump price hike in February 2010; the increase in excise duty on imported cigarettes and alcoholic beverages in a bid to promote local industries; and increase in housing costs.

Money supply (M2) expanded by K12.6 billion (6.6 percent) to K203.9 billion at the end of the fourth quarter of 2010 compared to an expansion of K16.0 billion (9.1 percent) to K191.3 billion in the third quarter. The development was explained by a K13.2 billion increase in net foreign assets as net domestic assets declined by K669.3 million. On annual basis, M2 growth accelerated to 17.8 percent as at end of fourth quarter of 2010 from 9.6 percent as at end of third quarter of the same year.

1.3 Exchange Rates

The foreign exchange market was characterized by lower supply against a background of higher demand, thereby exerting pressure on the local currency. The increased demand for foreign currency largely emanated from the robust economic growth the country has registered over the past six years.

This notwithstanding, the Malawi kwacha remained relatively stable against the US dollar throughout 2010, at K150.8009 per US dollar. However, the local currency exhibited mixed performance against all other currencies of the country's major trading partners, reflecting developments in exchange rate markets on both the local and international arena. Notably, the kwacha gained 3.9 percent and 4.4 percent against the pound and the euro, respectively, trading at K232.6405 against the Pound and K200.4144 against the Euro as at the close of the review period. The appreciation of the Malawi kwacha against the pound and the euro partly resulted from weakening of these currencies against the US dollar. In addition, the loss of German investor confidence and the Euro Zone's debt crisis in early 2010 further compounded pressure on the British Pound and the Euro during the review period. On the other hand, the Malawi kwacha depreciated against the Japanese yen by 10.4 percent to settle at K1.8497 per yen in 2010. The depreciation was partly on the back of the strengthening of the Japanese yen (against other major currencies) bolstered by Japan's improved economic performance towards the end of 2010.

On the regional front, the Malawi kwacha performed variably as it depreciated against the South African rand whilst it gained ground against the Zambian kwacha. The local currency weakened significantly by 15.5

percent against the South African rand to trade at K22.7182 to the rand. On the other hand, the local currency registered a 3.7 percent appreciation against the Zambian kwacha, to reach K0.0316 per Zambian kwacha as at the end of the review period.

1.4 Interest Rates

In view of declining inflation and developments in other macroeconomic indicators, the year under review saw the Reserve Bank of Malawi reducing the bank rate (discount rate) from 15.0 percent to 13.0 percent. In turn, commercial bank's base lending rates were reduced, averaging 17.5 percent, from 19.6 percent recorded at the close of 2009. On the other hand, commercial banks' average savings rate closed the year at 4.1 percent.

On the money market, subscriptions at the primary market for Treasury Bills totalled K31.4 billion at the end of the fourth quarter of 2010. This was 38.8 percent less than the subscriptions received in the preceding quarter. Comparing with the corresponding quarter of 2009, the subscriptions received were lower by 61.9 percent. There was a general decrease in Treasury Bills yields. Yields in the 91, 182 and 273 day tenors dropped by 95, 263 and 308 basis points to 6.2 percent, 7.1 percent and 7.4 percent respectively. Consequently, the all-type yield dropped by 222 basis points from 9.1 percent in the third quarter of 2010 to 6.9 percent in the fourth quarter of 2010.

1.5 Balance of payments

The country's overall balance of payments position as measured by the change in net foreign assets of the banking system recorded a surplus of K22.4 billion from a deficit of K21.7 billion in 2009. This development was due to an increase in donor capital inflows received in 2010. The Capital Account balance stood at K102.4 billion from K97.1 billion in the preceding year. Both the long term and the short term capital balance improved in 2010 when compared to the preceding year. The net long term capital balance stood at K102.3 billion, up from K97.1 billion in 2009.

The Current Account recorded a larger deficit of K148.0 billion compared to a deficit of K84.2 billion recorded in 2009. To a large part, this was attributed to the poor performance of the merchandise trade account, which recorded a trade deficit of K106.2 billion in 2010 from a deficit of K54.3 billion in the preceding year. Imports in 2010 increased slightly to K283.1 billion from K221.8 billion in 2009. The increase reflects the growing demand for imported goods in support of the economic growth that the economy has been enjoying over the past five years. The net non-factor services recorded a deficit of K48.4 billion from K38.8 billion registered in the preceding year. Similarly, net factor services registered a deficit of K8.6 billion in 2010. In contrast, the private transfers account was in surplus at K15.2 billion from K14.2 billion in 2009.



Chapter Two

Overview of the Banking Sector in Malawi

2.0 Introduction

This Chapter gives an overview of the Malawi banking sector in terms of its composition and ownership, assets and funding structures and market share.

2.1 Composition and Ownership of the Banking Sector

As at 31st December 2010, the banking sector comprised eleven commercial banks, namely: National Bank of Malawi, Standard Bank, First Merchant Bank, NBS Bank, Malawi Savings Bank, Indebank Limited, NEDBANK Malawi Limited, Opportunity International Bank of Malawi, ECOBANK Malawi Limited, FDH Bank and International Commercial Bank; one leasing company (Leasing and Finance Company) and two discount houses (Continental Discount House and First Discount House). No new bank was licensed during the year.

The year under review saw change in ownership structure for Indebank Limited after Trans-Africa Holdings Ltd disposed its shares to Malawi Government. Following this development, the total number of banking institutions with government ownership rose to two. There were five banks with foreign majority ownership. Refer to Appendix 1 for a detailed presentation of the shareholding structure of the Malawi Banking Institutions.

As at 31st December 2010, the total number of operating branches for all banks was 72, with agencies/kiosks totalling 146. Refer to Appendix 4 for a breakdown per institution.

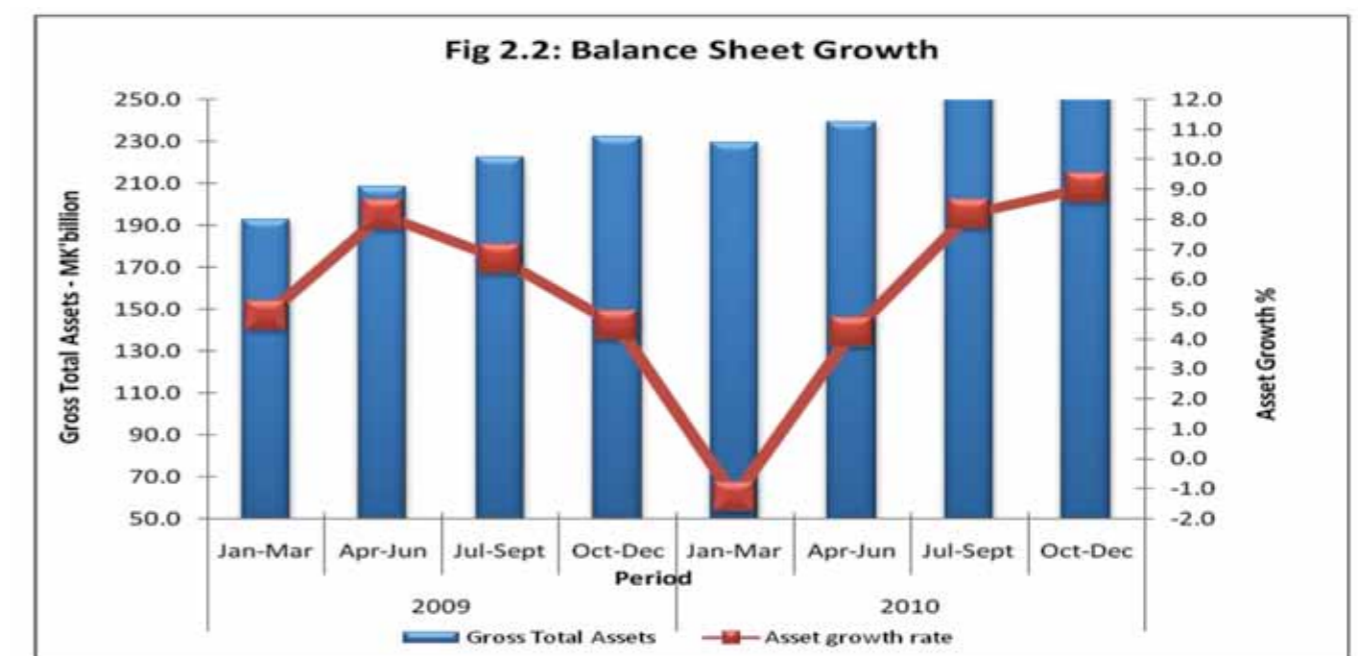
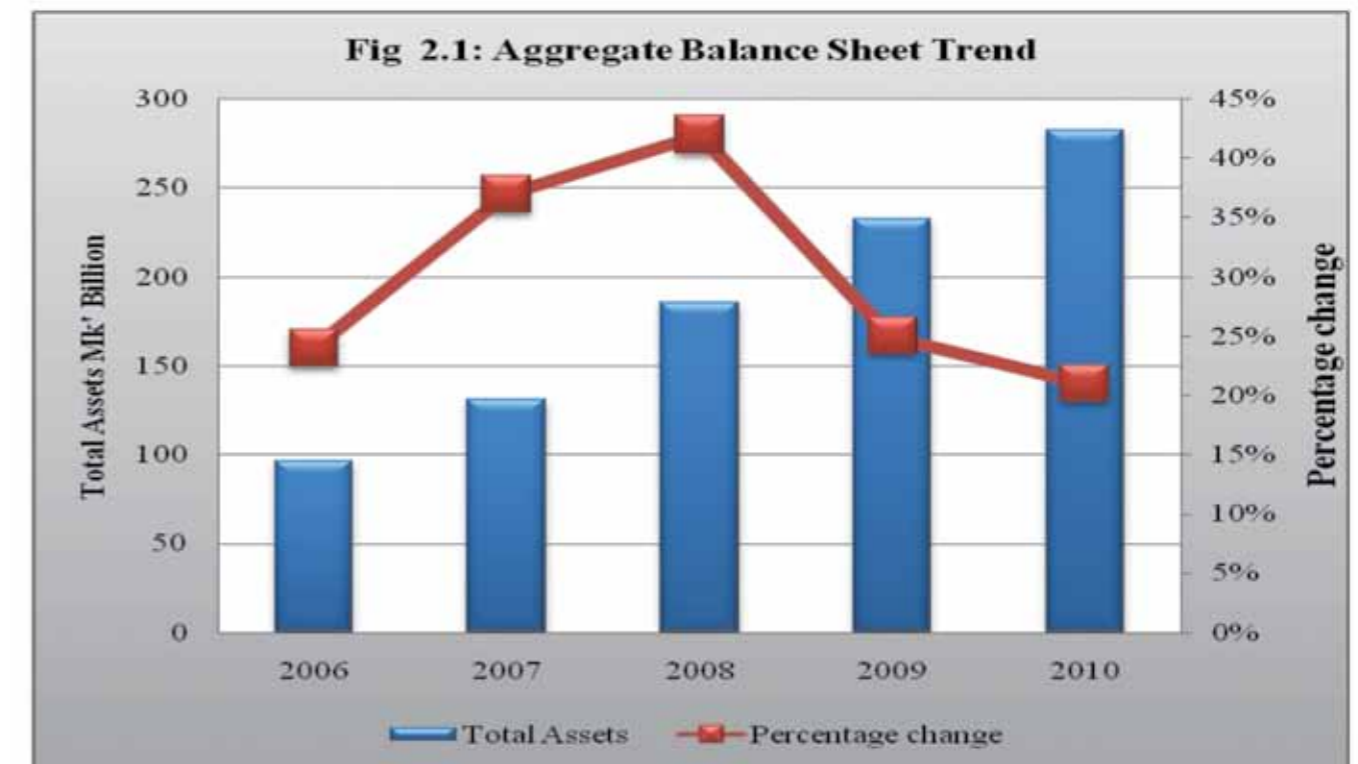
2.2 Balance Sheet Structure of the Banking Sector

During the year under review, the aggregate balance sheet of the banking sector in Malawi continued to register growth. Albeit comparing less favourably with the 24.0 percent growth rate registered during the preceding period, the period ended December 2010 posted a growth rate of 21.6 percent, with K282.4 billion in total assets as at December 2010 from K232.2 billion recorded in December 2009.

Loans and leases, cash balances and premises and equipment accounted for much of the growth in the banking sector's total asset while securities and investments generally declined over the period. Except for interest payable and other liabilities, all funding side items registered growth during the year ended December 2010. Specifically, total deposits, constituting the major component of total funds, grew by 22.4 percent to K206.4 billion in December 2010 (K168.6 billion in December 2009). Figures of aggregate balance sheet and growth rates spanning the period 2006 to 2010 have been presented in Table 2.1 below, with the trends depicted in Figures 2.1 and 2.2.

TABLE 2.1: AGGREGATE BALANCE SHEET (TOTAL ASSETS)

Period	K' Billion	Percentage Change
2006	96.1	24.0 %
2007	131.2	37.0 %
2008	184.0	42.0 %
2009	232.2	25.2 %
2010	282.3	21.6 %



2.2.1 Asset Structure

The banking sector's assets grew by 22.7 percent from K232.2 billion in 2009 to K285.4 billion in 2010. Much of this growth emanated from the following:

- i. A 13.1 percent growth in cash, balances with the Reserve Bank of Malawi and balances with other banks from K35.2 billion in December 2009 to K39.8 billion in December 2010;
- ii. A 32.5 percent increase in loans and leases, from K114.4 billion in December 2009 to K151.0 billion in December 2010;
- iii. A 37.0 percent rise in premises and equipment, from K20.6 billion in December 2009 to K28.2 billion in December 2010.

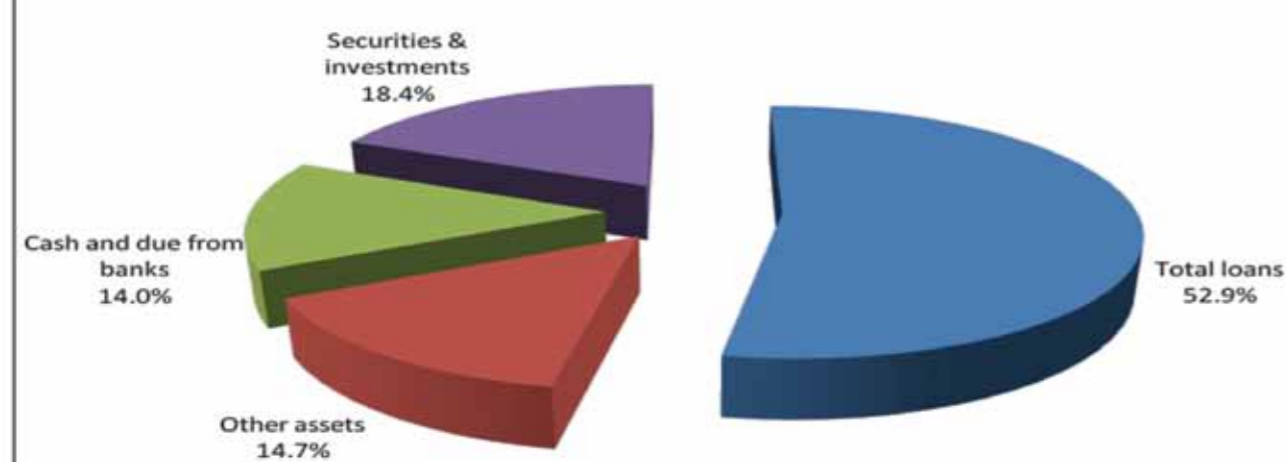
The above notwithstanding, securities and investments stood at K52.4 billion in December 2010 (K53.2 billion in December 2009), representing a decline of 1.4 percent.

In view of the above trends, cash, balances with the Reserve Bank of Malawi and balances with other banks comprised 14.0 percent of the industry's total assets as of December 2010, from 15.0 percent in December 2009. On the other hand, loans and leases remained the sector's bedrock, and constituted 52.9 percent of total assets in December 2010, from the 49.0 percent in the preceding period. Securities and investments accounted for 18.4 percent of total assets, from 22.7 percent in 2009. Premises and equipment, interest receivable and all other assets comprised 14.9 percent of total assets from 13.1 percent in December 2009. From the asset composition summary in Table 2.2, a graphical presentation is made in Figures 2.3 and 2.4 for ease of reference.

TABLE 2.2: ASSETS COMPOSITION (Figures in K billions)

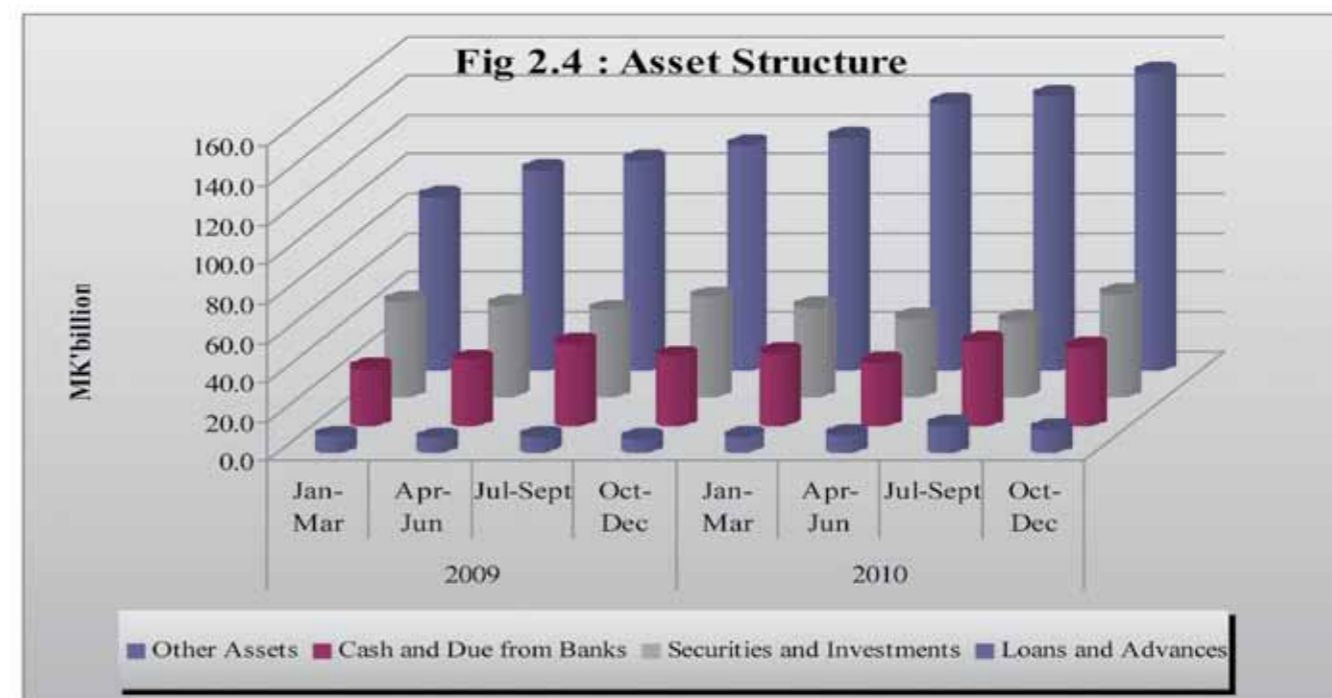
Assets	Dec-09	% Total Assets	Dec-10	% Total Assets	Growth
Cash and due from banks	35.2	15.1%	39.8	14.0%	13%
Securities and investments	53.2	22.7%	52.4	18.4%	(1.4%)
Total loans and advances	114.0	49.0%	151	52.9%	32%
Other assets	30.5	13.1%	42.0	14.7%	37.7%
Total assets	232.5	100.0%	285.4	100.0%	21.6%

Fig. 2.3 Asset Composition



2.2.2 Funding Structure

As at 31st December 2010, the banking industry's aggregate funds stood at K282.4 billion (K232.4 billion in December 2009). Total deposits, at K206.4 billion in December 2010 (from K168.6 billion in December 2009), constituted 73.1 percent of the total funds of which demand deposits and time deposits amounted K79.7 billion, and K71.6 billion respectively. On the other hand, savings deposits and foreign currency denominated accounts' deposits formed 17.3 percent and 9.4 percent of the total deposits, respectively.



The sector's capital, which comprised 16.0 percent of total funding, rose from K36.5 billion in December 2009 to K45.2 billion in December 2010. Growth in retained earnings, from K20.1 billion to K25.8 billion, was paramount to the upward push in total capital. Other funding sources, such as the inter-bank borrowings, discount window borrowing, and foreign lines of credit comprised the remaining 10.9 percent of total funds.

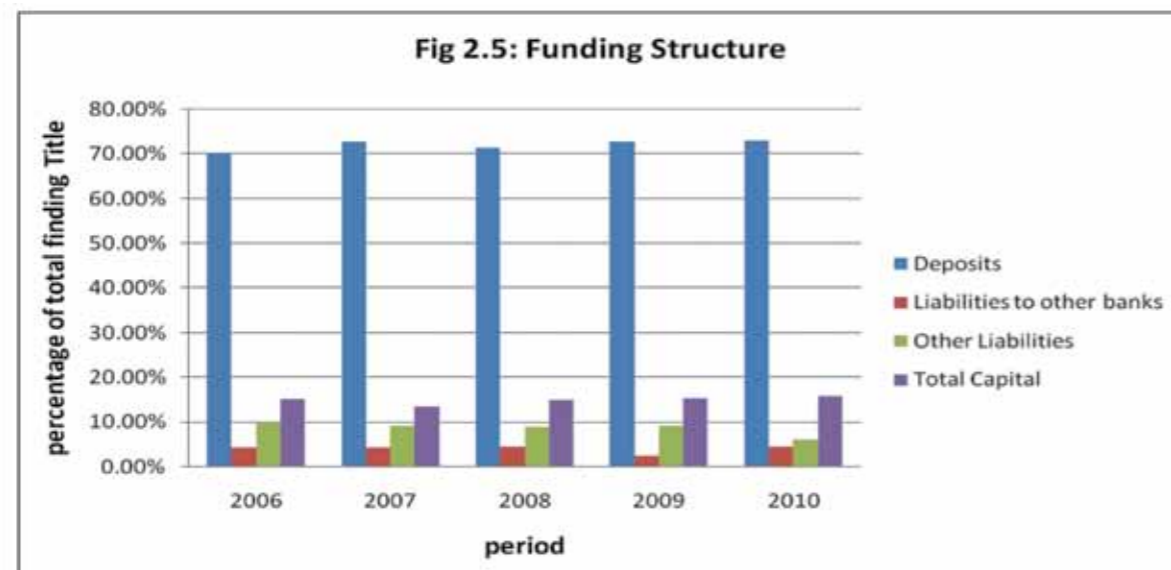
A summary of data on the funding trends and funding composition from 2006 to 2010 have been presented in Tables 2.3 and 2.4, and graphically presented in Figures 2.5 and 2.6 below:

TABLE 2.3: FUNDING TREND (Figures in K billion)

Item	Dec 06	Dec 07	Dec 08	Dec 09	Dec 10	Year on Year %Change				
						05/06	06/07	07/08	08/09	09/10
Deposits	66.9	94.4	131.5	168.6	206.4	15.7%	41.1%	39.3%	28.2%	22.4%
Liabilities to other banks	4.1	5.6	8.4	5.9	12.9	141%	36.6%	50.0%	-29.8%	118.5%
Other Liabilities	9.5	12.1	16.5	19.5	17.6	25.0%	27.4%	36.4%	18.2%	-11.9%
Total Capital	14.5	17.6	27.5	36.5	45.2	38.1%	21.4%	56.3%	31.3%	23.6%
Total Funding	95.0	129.7	183.9	232.2	282.4	23.9%	36.5%	41.8%	25.2%	21.6%

TABLE 2.4: FUNDING COMPOSITION

Item	Dec 06	Dec 07	Dec 08	Dec 09	Dec 10
Deposits	70.4%	72.8%	71.5%	73.2%	73.1%
Liabilities to other banks	4.3%	4.3%	4.5%	2.6%	4.5%
Other liabilities	10.0%	9.3%	9.0%	8.5%	6.3%
Total Capital	15.3%	13.6%	15.0%	15.7%	16.0%
Total Funding	100.0%	100.0%	100.0%	100.0%	100.0%



2.3 Market Share

During the period under review, National Bank of Malawi and Standard Bank Limited continued to command the majority of the industry's market share, as measured by their volume of total assets, deposits, gross loans and capital base. Excluding discount houses, National Bank of Malawi and Standard Bank Limited combined constituted 49.0 percent of the industry's aggregate assets, 53.0 percent of total capital, 52.0 percent of total deposits and 46.0 percent of total gross loans. Table 2.5 below depicts market share of banks in terms of total assets, loans, deposits and capital.

TABLE 2.5: MARKET SHARE SUMMARY (AS PERCENTAGE OF TOTAL)

Market share	Assets			Loans			Deposits			Capital		
	2008	2008	2010	2008	2009	2010	2008	2009	2010	2008	2009	2010
Two largest banks	55.0	53.0	49.0	52.0	52.0	46.0	56.0	54.0	52.0	55.0	56.0	53.0
Next four largest banks	33.0	34.0	37.0	37.0	38.0	41.0	33.0	33.0	36.0	33.0	28.0	32.0
Next four banks	11.0	11.0	11.0	11.0	9.0	11.0	10.0	12.0	10.0	10.0	12.0	11.0
The least two banks	1.0	2.0	3.0	0.0	1.0	2.0	0.0	1.0	2.0	2.0	4.0	4.0

Footnote: The statistics relate to 11 banks and one leasing Finance Company. (i.e. Data on discount house not available)



Chapter Three

Performance of the Banking Sector

3.0 Introduction

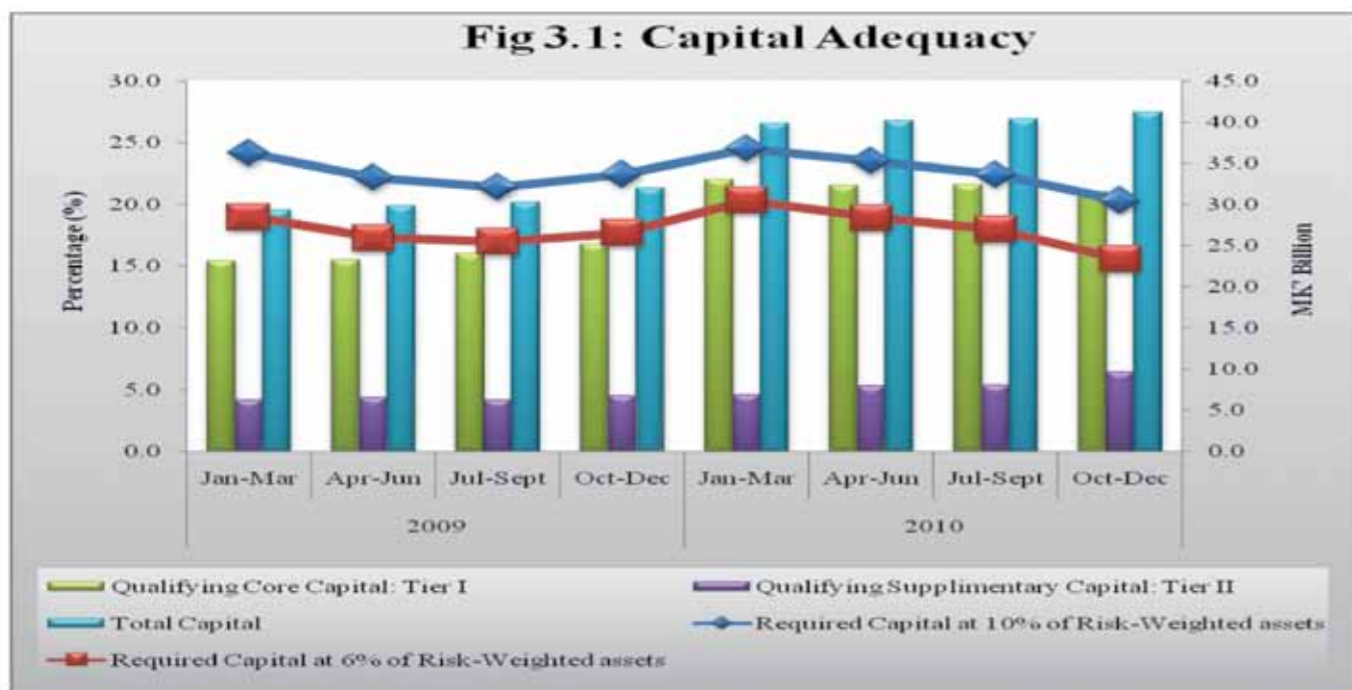
This Chapter analyses the financial performance of the banking sector during the period ended 31st December, 2010. Guided by the CAMEL rating system, the analysis covers five broad areas namely: Capital, Asset Quality, Earnings and Liquidity. The Chapter also gives a summary of selected key Financial Stability Indicators for the banking industry.

3.1 Capital Adequacy

In assessing capital, the Reserve Bank of Malawi (RBM) follows international requirements on capital which stipulates minimum capital ratios for individual banking institutions. Capital is categorized into core capital (comprising paid up capital, share premium, retained earnings and 60.0 percent of current year profits) and total capital which is sum of core capital and revaluation reserves, general provisions, hybrid debt capital and other subordinate debt.

The minimum international regulatory benchmarks for core capital and total capital to risk based assets are 4.0 percent and 8.0 percent, respectively. However, the RBM uses 6.0 percent and 10.0 percent, respectively, to ensure that banks hold more capital against their risks. Currently, the RBM assesses bank capital using the BASEL I Framework.

As at 31st December, 2010, the aggregate core capital and total capital for all banks stood at K31.5 billion and K41.1 billion respectively (December 2009: K25.4 billion and K32.3 billion) thereby representing an increase of 23.7 percent and 27.0 percent, respectively. The aggregate industry core and total capital ratios decreased from 17.8 percent and 22.6 percent in December 2009 to 15.6 percent and 20.3 percent in December 2010. This was as a result of a 46.0 percent increase in risk weighted assets from K138.7 billion in December 2009 to K202.6 billion in December 2010. On the whole, the banking industry remained well capitalized as illustrated by Figure 3.1 below.

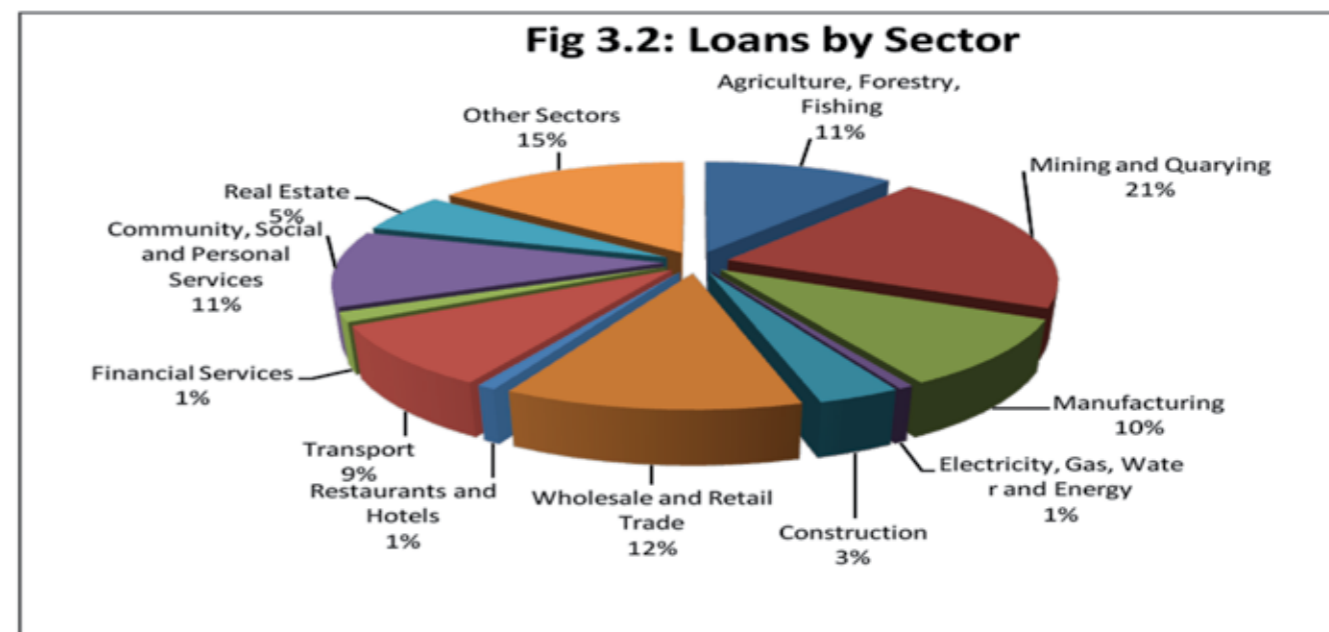


3.2 Asset Quality

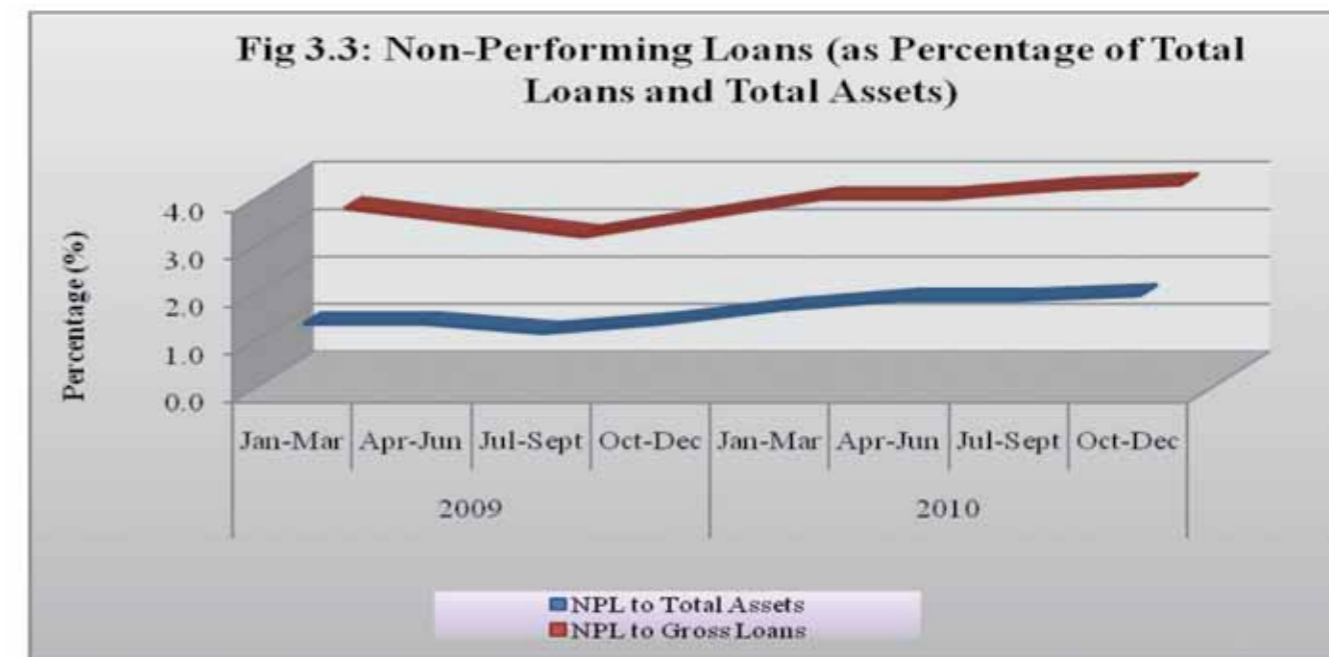
For purposes of this report, asset quality of the banking industry is measured by the level of non performing loans and adequacy of provisions. The Reserve Bank of Malawi uses the directive on asset classification, risk management guidelines, directives on large exposures and foreign currency lending ratio as tools for assessing credit risk in banks.

In the year 2010, the banks' gross loans and leases were K151.0 billion and constituted 53.4 percent of total assets. Gross loans and leases registered a growth of 32.0 percent from K114.4 billion in December 2009 to K151.0 billion in December 2010. The development is reflective of growth in the economy in general and more specifically higher returns in credit than money market securities such as TB's, RBM bills and interbank loans whose prices were low and falling.

The banking sector extended credit facilities to various sectors of the economy namely; agriculture (11.0 percent), mining and quarrying (21.0 percent), manufacturing (10.0 percent), construction (3.0 percent), wholesale and retail trade (12.0 percent), restaurants and hotels (1.0 percent), transport (9.0 percent), financial services (1.0 percent), community, social and personal services (11.0 percent), real estate (5.0 percent), and other sectors (15.0 percent), as presented in the Pie Chart in Fig 3.2 below.



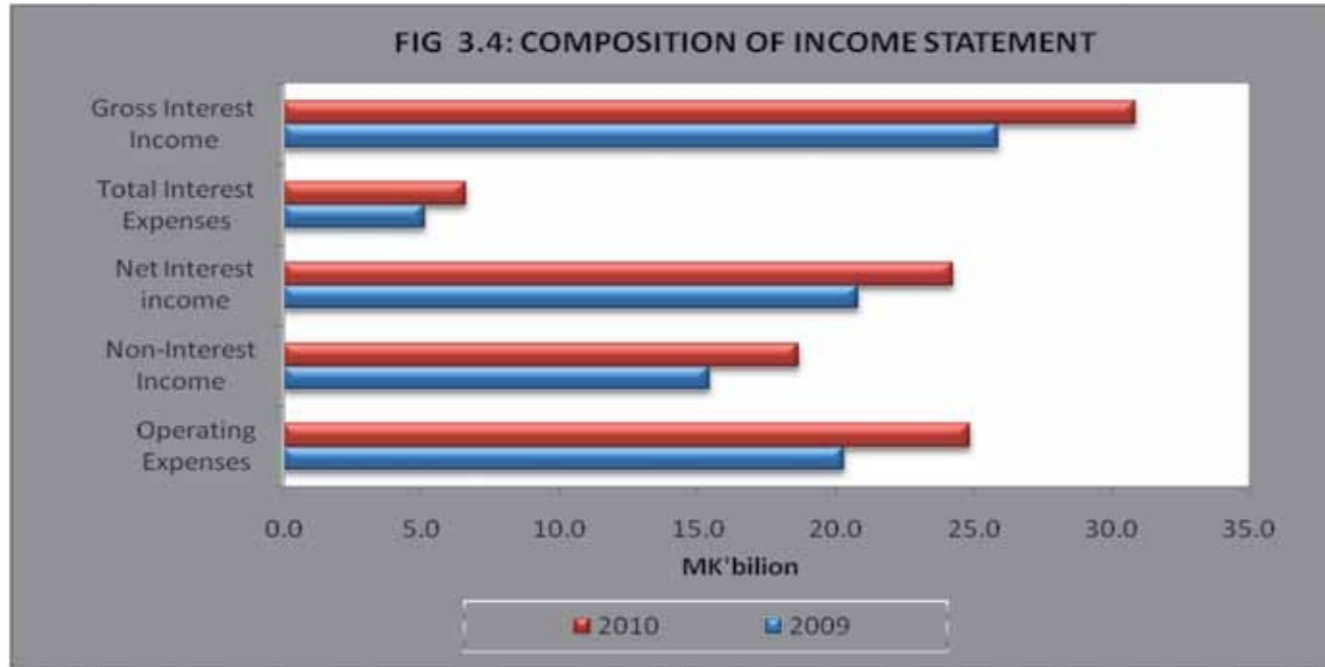
During the period under review, K5.9 billion of total loans were deemed non performing, an increase from K3.6 billion reported in 2009. As depicted in Fig 3.3 below, non performing loans as a percentage of total loans increased from 3.1 percent in December 2009 to 3.9 percent in December 2010. Specific provisions also increased from K1.5 billion in December 2009 to K1.8 billion in December 2010. However, the ratio of specific provisions to non performing loans went down from 42.4 percent in December 2009 to 31.5 percent in December 2010. Overall, the quality of the loan portfolio was considered satisfactory.



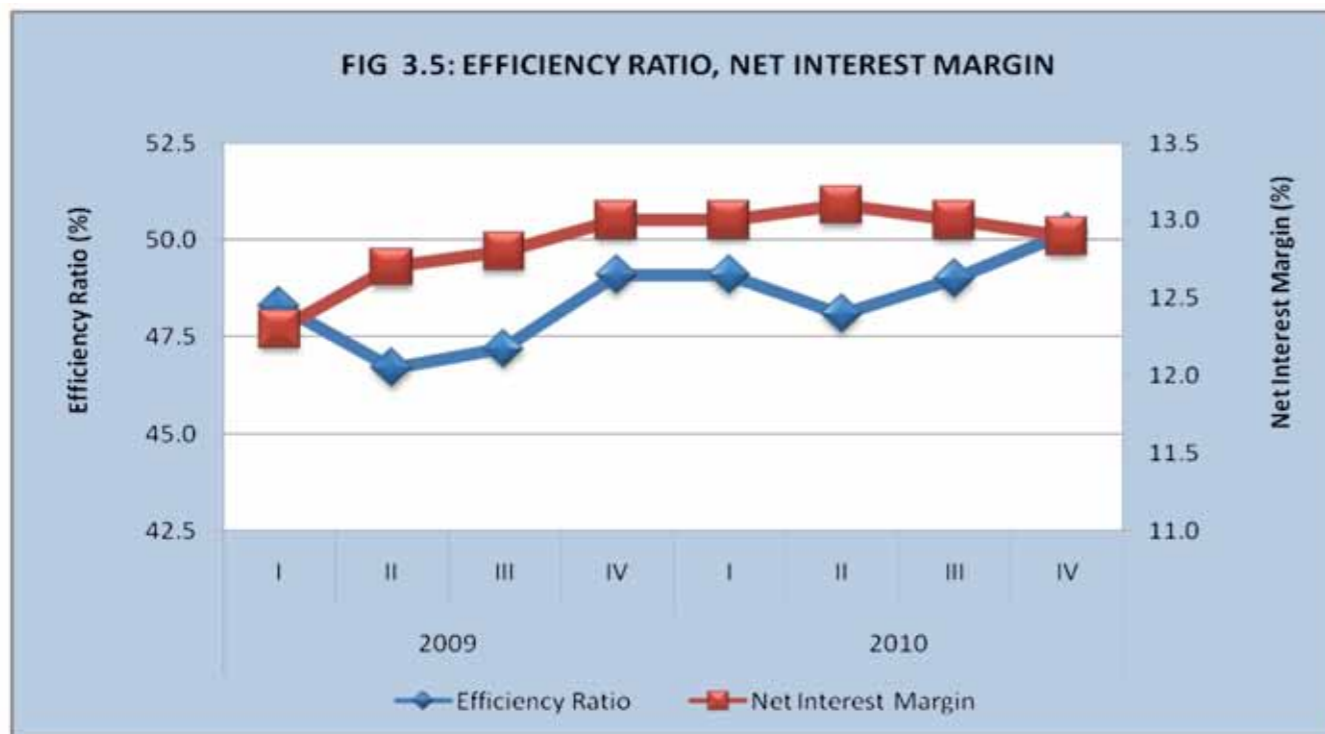
3.3 Earnings Analysis

Earnings play a vital role in cushioning for losses and in funding capital growth prospects. The banking industry recorded net income of K16.9 billion in December 2010, compared to K14.9 billion in December 2009.

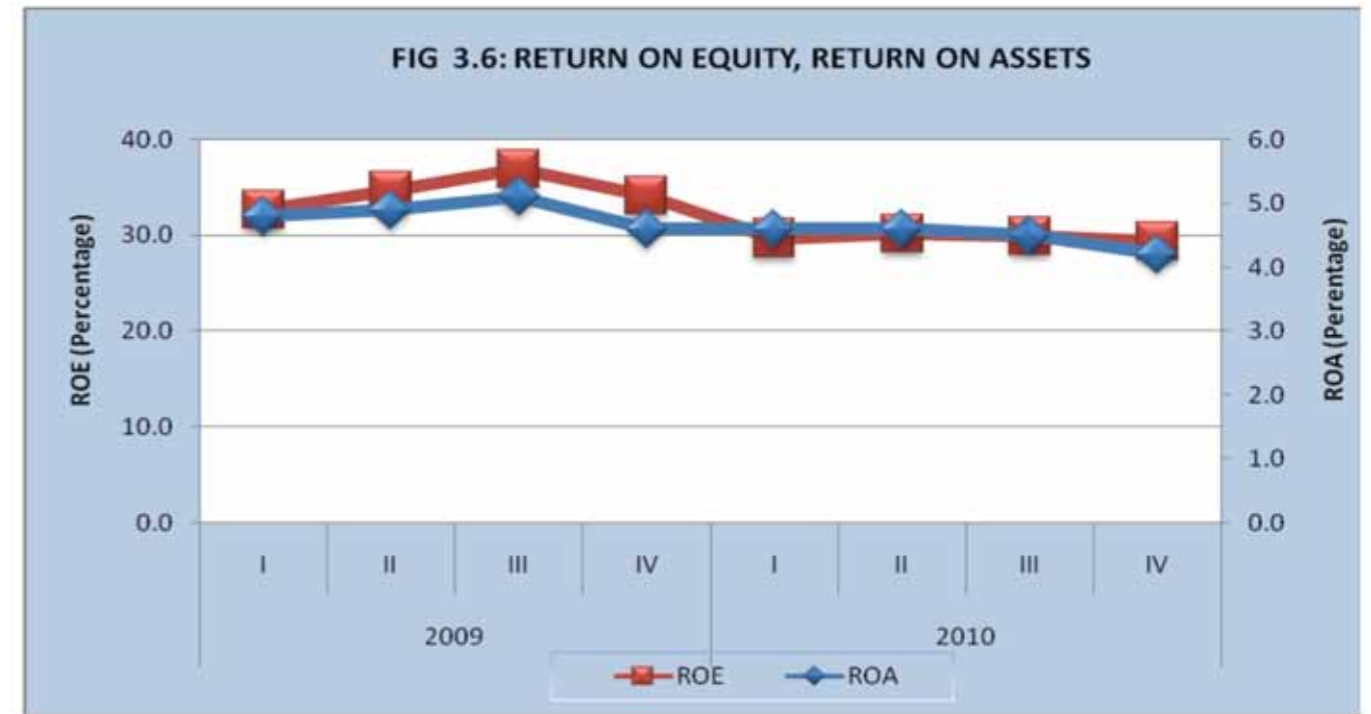
Interest income continued to account for much of the banking sector's total income, at 62.3 percent in 2010. Interest income totalled K30.9 billion in December 2010, an increase of 19.2 percent from K25.9 billion in December 2009. On the other hand, interest expenses amounted to K6.5 billion in December 2010, representing an increase of 29.4 percent from K5.1 billion in December 2009. Non-interest income also grew to K18.7 billion from K15.4 billion, representing 21.0 percent increase. The bar graph in Fig 3.4 below shows a graphical presentation of the composition of income statement for 2009 and 2010.



Net interest margin for the industry went down from 13.0 percent registered in December 2009 to 12.9 percent in December 2010. During the same period, the efficiency ratio increased to 50.2 percent, from 49.1 percent in December 2009. Fig 3.5 below shows the relationship between net interest margin and efficiency ratio.



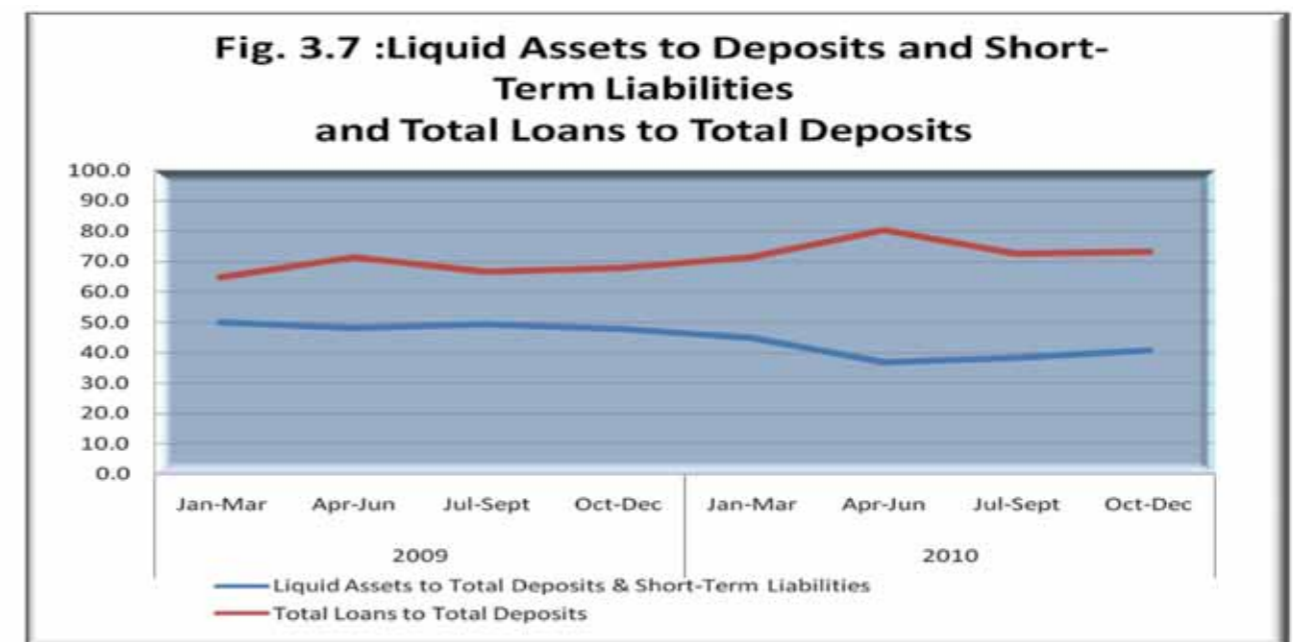
The above considered, profitability performance during the year as measured by ROA and ROE ratios declined from 4.7 percent and 34.2 percent in December 2009 to 4.2 percent and 29.4 percent respectively. Nevertheless, the banking sector recorded significant growth in profits with trends as shown in Fig 3.6 below.



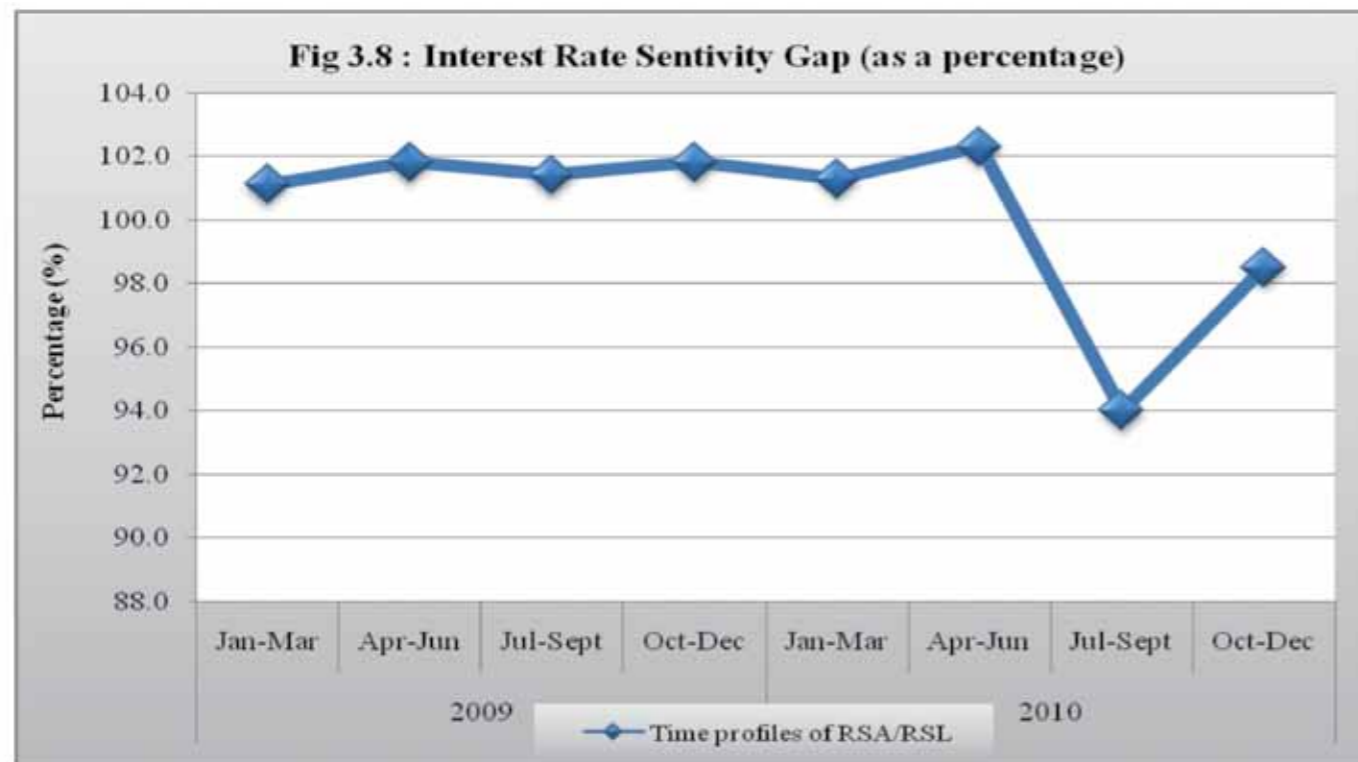
3.4 Liquidity Analysis

Liquidity and funds management is the process of ensuring that a licensed institution is able to meet all of its funding obligations. Ceteris paribus, a bank with adequate liquidity is able to fund its obligations (such as deposit withdrawals and liabilities maturing in the normal course of business) at reasonable cost. Inadequate liquidity has the potential to lead to failure by a bank to settle its maturing obligations, culminating into loss of public confidence. Similarly, profitability and capital can also be affected and may lead to insolvency. For these reasons, banks are required to maintain adequate liquidity at all times.

The liquidity position of the banking sector in Malawi in 2010 was considered fair. The liquidity ratio declined from 48.1 percent in December 2009 to 40.7 percent in December 2010. This was above the regulatory benchmark of 30.0 percent. The decline in liquidity was as a result of increased lending by the banks, (a departure from trends in the early 2000s when a significant portion of their assets were placed in form of securities and other liquid assets). Consequently, the lending ratio grew from 67.9 percent in December 2009 to 73.2 percent in December 2010. Figure 3.7 below illustrates the relationship between liquid assets to total deposits and short term liabilities and the lending ratio.



The interest rate sensitivity ratio, expressed as the percentage of interest earning assets to interest earning liabilities, stood at 98.5 percent in December 2010 (102.3 percent in December 2009). Similarly, during the period January to June 2010, the rate sensitive assets and rate sensitive liabilities were almost matched, implying that banks were well cushioned against interest rate adjustments in either direction. However, banks held more interest sensitive liabilities between June and September, 2010 resulting in the sensitivity ratio falling from 102.0 percent to 94.0 percent. The graph in Fig 3.8 below illustrates the relationship between interest rate sensitive assets and liabilities.



3.5 Financial Soundness Indicators

The table below contains three years financial soundness indicators (FSIs) for the banking system up to 31st December 2010. The indicators attest the fact that the Malawi banking sector remained stable and sound in 2010 with generally strong key stability indicators. Based on the capital and liquidity indicators, the banking institutions were generally solvent and liquid to absorb unforeseen losses and meet their contractual obligations.

Table 3.1: SUMMARY OF FINANCIAL SOUNDNESS INDICATORS

Ratios		Dec. 2008	Dec.2009	Dec. 2010
	Regulatory Total Capital to Risk			
Capital	Weighted Assets	21.5	21.2	20.3
Adequacy	Regulatory Tier 1 Capital to Risk			
	Weighted Assets	16.6	16.7	15.6
	Total Capital to Total Assets	14.8	15.6	15.8
	Total loans and advances to			
Asset	Total Assets	42.8	44.11	49.19
Composition	Foreign Loans to Total loans	19.6	19.6	9.9
and Quality	Non-performing Loans to Gross Loans			
	Loans	3.2	3.2	3.9
	Non-performing Loans Net of Provisions to Capital			
	Provisions to Capital	8.3	6.7	9.8
	Return on Assets	4.8	4.6	4.2
Earnings and Profitability	Return on Equity	43.6	34.1	29.4
	Interest Margin to Gross Income	48.2	51.0	49.0
	Non-interest Expenses to Gross Income			
	Income	49.6	47.9	50.2
	Personal Expenses to Non-interest Expenses			
	Interest Expenses	49.4	48.9	45.8
	Liquid Assets to Total Assets	53.5	48.0	40.7
Liquidity	Liquid Assets to Total Short Term Liabilities			
	Liabilities	53.5	48.0	40.7
	Total Loans to Total Deposits	62.3	67.6	72.8
	Foreign Exchange Liabilities to Total Liabilities			
	Total Liabilities	9.3	9.7	8.1



Chapter Four

Activities of the Bank Supervision Department in 2010

4.0 Introduction

Bank Supervision Department is responsible for ensuring safety and soundness of the banking system in Malawi. This is achieved through, inter-alia, controlling entry into the banking system through vigilant licensing process of banking institutions, orderly market exit, continuous review of laws and enforcing compliance with laws and directives for the industry. The Chapter highlights the major activities undertaken by the Department during the year under review using the risk based supervision model that the RBM adopted for supervision of the banking institutions.

4.1 Supervisory Activities

Bank Supervision Department currently uses the offsite surveillance and onsite examination as the major tools for carrying out its supervisory role for the banking system. Offsite surveillance is the primary tool for monitoring the financial performance of the banking industry and is used as the first test for detecting problems or areas that require further review or scrutiny. Onsite examination involves visiting the licensed institutions to examine their books of accounts to assess the adequacy of the management, internal controls as well as the risk management systems of the institution and to assess its financial performance and compliance.

4.2 Off-Site Surveillance

Off-site surveillance remains one of the key supervisory tools in assessing the financial performance and soundness of licensed financial institutions. It involves use of information obtained from prudential returns submitted by the respective licensed financial institutions to generate key quantitative prudential ratios on capital adequacy, asset quality, earnings and liquidity. Particular focus is placed on the levels, trends and comparison with benchmarks and industry ratios. In addition, off-site surveillance covers monitoring and verification of compliance with existing laws, directives, prudential regulations and guidelines as issued by the Reserve Bank of Malawi from time to time. Where non-compliance has been observed, meetings with management and board of directors of the concerned institutions are convened with the view to ironing out the anomalies and impress on the need for compliance. It also entails invoking various penalties as prescribed in the relevant laws. The financial performance of banks is fully done through analysis of off-site reports which are produced on a quarterly basis.

During the year 2010, the Department produced all offsite quarterly reports. The reviews showed that the banking industry continued to record impressive financial performance. Major supervisory concerns that were noted in some financial institutions during the period under review included declining liquidity levels, growing non-performing assets and high deposit concentration.

4.3 On Site Examination

During the year ended 31st December 2010, the Department conducted full scope on-site examinations at Leasing and Finance Company, National Bank of Malawi, Malawi Savings Bank and International Commercial Bank. The examinations embraced the risk-based supervision methodology with the view to ensuring that all risks assumed by the banking institutions were evaluated and measured.

In performing the examinations, Examiners were guided by the risk based examination procedures and risk rating indicators. Examination procedures were tailor made to the varying characteristics of each institution, in terms of size, complexity and risk profile. The procedures focused on developing appropriate documentation to adequately assess management's ability to identify, measure, monitor, and control risks. Added to that, the examiners employed core assessment and expanded procedures aimed at assessing the extent to which risks of an institution were appropriately identified and managed.

4.4 Licensing and Compliance Review

4.4.1 Licensing

The purpose of the vigilant licensing process regime that the Department has adopted is aimed at ultimately protecting the interests of depositors and the public. It is geared to help minimise future bank failures by ensuring

that only fit and proper players are allowed to conduct banking business in the country

During the year under review, the Reserve Bank of Malawi did not license any new applicants to conduct banking business, nor were there any operators that were de-licensed. During the year, the Reserve Bank reviewed an application to convert from a discount house into an investment bank. The banking sector continued to grow in terms of branch network and product range. Out of the existing 11 banks, 9 opened a total of 44 new branches (including agencies and kiosks). In terms of new product development, approvals were mainly in the areas of mobile phone and internet banking as well as customised savings accounts with death benefits or with medium to longer term incentives.

4.4.2 Compliance Review

Compliance review covers an evaluation of the operations of each licensed institution to determine level of compliance with the financial sector laws, policies, directives and regulations.

A review of the 2010 offsite and onsite reports reflects that there was general compliance with the set directives, policies, regulations and law. However, there were few instances of non compliance with the Foreign Currency Lending Ratio Directive and Foreign Currency Exposure Directive. Such non compliance, to a larger part, was attributed to little attention with regard to trading positions as well as failure by the banks to adhere to own limits. Another isolated instance is where one bank overlooked on the need to seek prior approval from the Registrar before introducing new products and before appointing its senior management officials. In this regard, the Board and Management were appropriately cautioned by the Regulator.

4.4.3 Review of Banking Regulations

The year 2010 saw the enactment by Parliament of the Financial Services Act 2010 (the FSA), the Credit Reference Bureau Act 2010 and the Banking Act 2010. The objective of the FSA is to provide a platform for regulation and supervision of financial institutions in Malawi. It ensures that all operators in the financial services industry are regulated unlike previously when only banking, capital markets and insurance entities were supervised. The FSA also consolidates the supervisory responsibility for the financial sector in a single agency; the Reserve Bank of Malawi (RBM) and appoints the Governor of the RBM as the Registrar of Financial Institutions. The FSA further incorporates more detailed requirements for licensing and supervision of financial institutions that are consistent with international standards as set by international regulatory bodies to which the RBM is affiliated. The Credit Reference Bureau Act 2010 aims at regulating and supervising credit reference bureau business in Malawi. The main objectives of the Act include the provision of a mechanism for banks to share credit information in order to enhance information symmetry, improve credit repayment culture and promote risk based pricing of loan facilities in the banking sector. Further to the Act, the Department finalised and sent for gazetting Regulations governing the licensing and operations of credit reference bureaus in Malawi.

During the year, the Department also issued Guidelines on Corporate Governance and on Mergers and Acquisitions. The Framework for Problem Bank Resolution was also drafted and incorporated comments from FSVS. It is the intention of the Department to conclude the Framework in 2011 by including procedures on handling of systematically important banking institutions. The Department also finalised and submitted for gazetting the Directive on Disclosure of Public Information by Banking Institutions and reviewed the Directive on Foreign Currency Lending Ratio.

4.5 Consumer Complaints Handling

During the year ended, the RBM received several complaints from consumers of financial services, mainly relating to alleged lack of fairness and transparency in commercial banks' execution of foreclosure of customer's collateral pledged as security. There was also a reported instance of a customer account being allegedly defrauded by a bank employee. The RBM took effort to follow up on the resolution of the disputes. The issue of customer account being defrauded by a bank employee is still being investigated.

From the complaints, it was generally noted that, while most customers lodged their complaints to the Registrar, the issues were either already being handled by the courts through their lawyers, or were already concluded in the courts. In this regard, procedures for lodging complaints need to be developed and structures put in place both at the licensed institutions and the Reserve Bank. Once developed, it will be vital that these procedures and structures

are made known to the public and bank customers through various channels. Most importantly, there is strong need to fast track the financial literacy programs that are currently being initiated.

4.6 Training and Staff Development

As at end 2010, the Department had a staff compliment of twenty-four. Given the continued growth and sophistication of the banking system, buttressed by developments in the world economy at large and the need to sustain the resilience of Malawi's banking market, the Department continued to support initiatives aimed at developing and enhancing capacity. In this regard, the year 2010 saw some members of staff attending various conferences and training workshops including Seminar on Senior Bank Supervisors from Emerging Economies organised by the World Bank Institute; Anti-Money Laundering Course organised by the SADC Training Forum; Instruments of Financial Markets offered at the Swiss National Bank Institute; Deposit Insurance Scheme; Credit Risk Analysis School and Bank Management School at the Federal Reserve Training Centre; Specialised Course in Bank Supervision at the Federal Reserve Bank of New York; as well as other courses in Basel II; Consolidated Supervision; Mobile Banking; Risk Based Supervision and Financial Institution Analysis. In addition, other members were also attached to the Bank of Namibia and Reserve Bank of Zimbabwe on Basel II, Bank of Tanzania on Risk Based Supervision and FDIC on Anti-Money Laundering Examination.

Two members of staff in the Department were awarded scholarships to undergo postgraduate studies, one by the Reserve Bank of Malawi and the other by the Australian Government through the Government of Malawi.

The Department continued to utilise the FSI Connect which is an interactive web based information resource and learning facility for Bank Supervisors hosted by the Basel Financial Stability Institute. FSI Connect tutorials provide the most up-to-date information that supervisors need to perform their jobs.



Chapter Five

Current Issues in Bank Supervision

5.0 Introduction

The Malawi banking industry, just like the global banking system, has continued to remain dynamic and growing in innovation and level of sophistication, bringing with it new opportunities and challenges. It is therefore imperative for bank supervisors not only to prudentially respond to such risks, but perhaps most importantly to have foresightedness in their oversight role. During the year under review several activities were lined up in this regard, including strides towards Basel II preparedness, development of framework and systems to effect consolidated supervision, regulation of credit reference bureaus, regulation of electronic banking services, measures to prevent the financial system from being conduit for money laundering and progress towards further automation of system for reporting and managing financial institution data through the Bank Supervision Application Solution (BSA).

5.1 BASEL II and the Way Forward for Malawi

The Department continued with its Basel II preparations in 2010. The following key activities were undertaken on Basel II:

- (i) Five days training workshop on Basel II for all sub-committee members (i.e. from the RBM and banking institutions). The objective of the training was to equip members with basic knowledge and requirements of the New Capital Accord. Emphasis was put on illustrating the standardised approaches for measuring and calculating capital charges for credit and market risks and the basic indicator approach for operational risk¹;
- (ii) Two RBM Committee members were sent for attachment to Reserve Bank of Zimbabwe on market risk and two to Bank of Namibia on Basel II in general in January and May, 2010 respectively. The visits were for duration of five days each. In addition, four members attended Basel II courses organized by different providers;
- (iii) An excel template to be used for the Quantitative Impact Survey (QIS) was developed in house based on the Basel Committee format. The template has been simplified and modified to reflect the level of sophistication (in terms of products, systems and services) applicable in the Malawi banking sector;
- (iv) Areas requiring national supervisory discretion were all identified, outlined and communicated to all banks. A few areas however, are likely to be modified as discussions with banks intensify in 2011 and as more data is submitted by banks on various areas;
- (v) A three days workshop was held for all sub-committee members to take them through the template, section by section. An Instructions Manual to guide banks on how to compile the template was also developed and circulated to all banks;
- (vi) The first QIS was conducted on all banks to assess the likely impact of the new capital rules on each bank's existing capital level. The Survey was conducted with technical support from two Consultants under an existing technical assistance arrangement with Financial Services Volunteer Corps (FSVC); and
- (vii) A full report of findings and recommendations was drafted and submitted to RBM Executive Management. In addition, two update reports on Basel II progress were compiled and submitted to Executive Management (one in August 2010 and another one in December, 2010).

Going forward, the Department has lined up a number of activities for 2011 on Basel II. Key among them are: the modification of the call report to include trading book balance sheet and income statement; conducting the second QIS; holding Basel II National Steering Committee (NSC) and sub committee meetings; implementing market risk capital charge; initiating the development of Internal Capital Adequacy Assessment Processes (ICAAPs) by banks and continued training of both RBM Committee members and market players.

5.2 Consolidated Supervision

With approval of Executive Management of the RBM, the Department undertook to implement consolidated

¹The standardised approach for measuring operational risk was also covered; but all banks in Malawi will only be allowed to adopt the basic indicator approach. The standardised approach will only be allowed upon RBM approval and satisfaction of a bank meeting specified requirements.

supervision in line with the recommendations of the 2007 Financial Sector Assessment Program (FSAP) in Malawi that was conducted under the auspices of the World Bank. Implementation of consolidated supervision has been necessitated by the various developments that have taken place with regard to the ownership structure of most financial institutions in the country, namely: the increase in the number of foreign entities acquiring licences to operate financial institutions in Malawi; financial holding companies investing in non bank financial institutions; local banks acquiring and or investing in subsidiaries abroad; conglomerates owning banks and other financial institutions with some conglomerates having in their structures entities which have no formal supervision.

Undertaking non financial business in subsidiaries, associates or affiliates can mean that activities which could affect the soundness of the financial institutions are not under the direct oversight of the supervisory authority. In the absence of consolidated supervision, the above developments can create various risks to financial institutions belonging to conglomerate groups.

The passing into law of the Financial Services Act 2010 and Banking Act, 2010 respectively provide the Registrar of Financial Institutions powers to supervise, call or information from subsidiaries, associates or affiliates of supervised institutions. Further, the two pieces of legislation also provide the Registrar with powers to share information with other monetary and financial regulatory authorities at home and abroad.

5.3 Anti Money Laundering and Combating of Financial Crime

During the year under review, several activities were conducted in the field of Anti Money Laundering and Combating Financing of Terrorism (AML/CFT). Two full scope on-site examinations were conducted, namely at National Bank of Malawi (NBM) and NBS Bank. The examinations covered the following areas; AML/CFT compliance program, internal/external audit, customer identification program and due diligence, suspicious activity reporting, correspondent banking and wire transfers.

The Department continued to enhance AML/CFT knowledge through training and participation in various meetings. During the year under review, representatives from the Department attended both the March 2010 Task Force of Senior Officials meeting in Arusha, Tanzania and the August –September 2010 Task Force and Ministerial Council Meeting in Lilongwe. The Department also participated in a Workshop organised by the World Bank (WB) in conjunction with the East and Southern Africa Anti-Money Laundering Group (ESAAMLG) in Zambia aimed at providing skills to develop Strategic Implementation Plans (SIP). Further, the Department participated in a consultative workshop organised by Financial Intelligence Unit (FIU) on the development of National AML/CFT Strategy. It was aimed at soliciting ideas from relevant sectors in order to come up with an encompassing strategy.

As per the Memorandum of Understanding between the RBM and the FIU which was signed in December 2009, the Department conducted series of meetings and shared information such as on-site examinations findings and compliance reports.

5.4 Mobile Banking and E- Commerce

While the two terms are similar and often used interchangeably, the latter is broad as it encompasses the former. It also covers internet banking, card based payments and transactions, ATMs among others. Mobile banking, on the other hand, refers to bank transactions and instructions that are executed via mobile phones.

The Department has an Electronic Banking Committee whose members are also in the RBM E-Banking Task Force. The task force draws membership from other departments within the RBM. At departmental level, the Committee is tasked to:

- Develop guidelines for regulating E-Banking products and services; and
- Evaluate risks associated with E-Banking products and services in order to afford effective oversight.

The final draft Electronic Banking Guidelines are yet to be issued but banks have already embraced the E-Banking delivery channel in one way or the other².

² Such as internet banking, Mobile phone banking, ATMs, VISA Cards, Cash Pass port, Point of Sales, Credit Cards, Debit Cards.

The RBM E-Banking Task force was engaged in drafting Mobile Payment Guidelines and assessing applications for introduction of mobile payments. Chief among the applications is the ZAP System³ by Zain (now Airtel). The applicant is now piloting the product while awaiting formal regulatory approval.

5.5 Financial Stability Report

Bank Supervision Department is a member of the Reserve Bank of Malawi Financial Stability Task-Force. The role of the Task-Force is to look at financial stability issues and produce financial stability reports biannually. Bank Supervision Department provides input into the report on the banking sector. The official launch of the first report is slated for 2011. Meanwhile, the Department is in the process of building capacity in the area of stress testing to enhance the off-site surveillance and also to feed into analyses for the financial stability reports.

5.6 Bank Supervision Application Solution

Bank Supervision Application solution (BSA) is a web based reporting tool that was adopted by a number of SADC Central Banks to replace Microsoft Excel Spreadsheet-based Database in carrying out financial analysis of banking institutions. The application contains two modules namely; the Risk Analysis Automation System (RAAS) which contains the quantitative tools for off-site surveillance and the Business Support System (BSS) that is used as a Supervisory Information System (SIS) for automating workflows as well as acting as an electronic filing system. The application is supported by the BSA Support Office (BSO) based at the Central Bank of Mozambique.

To date its usage has been limited and full adoption has been slow. As a result, the application is running on parallel to the existing database beginning with November 2009 returns. However the parallel run did not materialise into full usage as it presented problems. The Department is currently exploring the possibility of acquiring an alternative database solution.

5.7 Credit Reference Bureau

Credit Reference Bureau law was enacted in 2010. The law gives powers to the Governor of the Reserve Bank of Malawi, as Registrar of Financial Institutions, to license, supervise and regulate credit reference bureau business in the country. The main objective of licensing the business is to provide a mechanism for banks to share credit information in order to enhance information symmetry, improve credit repayment culture in the country and promote risk based pricing of loan facilities in the banking sector.

In this regard, technical assistance was received from International Monetary Fund's East AFRITAC and USAID towards the development of regulatory framework for the licensing and operations of Credit Reference Bureaus. Regulations were formulated and are awaiting gazetting by Government.

³ Is a phone based payment system involving a mobile phone company, bank and agents. The system leans on agents who make deposits with banks, which in turn maintain a trust account of the system. Upon making a deposit, the agents get electronic monetary value equal to the deposit made. It is a requirement that at any point the electronic value in circulation should be equal to the balance in the trust account. Agents then 'sell' the electronic value to ordinary subscribers for a commission for transfer of funds to any beneficiary of their choice.



Chapter Six

Regional and International Cooperation

6.0 Introduction

This Chapter gives an overview of the Technical Assistance that Bank Supervision Department received in support of the various projects that were lined up during 2010. The Chapter ends by describing prospects and challenges that the Department is currently facing.

6.1 IMF East Africa Regional Technical Assistance Centre (East Afritac)

The IMF East Africa Regional Technical Assistance Centre (East AFRITAC) is a collaborative venture between the International Monetary Fund (IMF), the recipient countries, and bilateral and multilateral donors. It derived from the IMF's response to African leaders' call on the international community to increase technical assistance (TA) to Africa and focus on capacity building. Its strategic goal is to strengthen the institutional capacity of African countries to design and implement their Millennium Development Goals and poverty-reducing strategies, supported by sound macroeconomic and financial policies, as well as to strengthen the coordination of capacity-building. East AFRITAC was the first Center to be established in Africa in 2002, and is based in Dar es Salaam, Tanzania.

In 2010 Bank Supervision Department was assisted by East AFRITAC in the following areas:

6.1.1. Credit Reference Bureau

An East AFRITAC mission visited Malawi during the period 15 to 26 February 2010, to assist the RBM to prepare regulations to be issued under the Credit Reference Bureau Act 2010. The RBM, specifically requested for this TA in order to develop a robust and comprehensive program for oversight of credit reference bureaus (CRB) in Malawi.

The mission developed draft regulations, licensing guidelines for consideration of the RBM and stakeholders and also provided comments and recommendations for amendments to the Credit Reference Act, 2010. A workshop was conducted for RBM officials that included best practices around the World for CRB in the context of licensing operations, data security requirements, access to credit reports and obligations of the various users.

6.1.2. Stress Testing

The mission to RBM on stress testing from IMF EAST AFRITAC took place from 3 to 7 May 2010. The main purpose of this mission was to strengthen the RBM's off-site surveillance activities, with specific reference to developing the capacity to stress testing prudential data submitted by banking institutions. The mission's work concentrated on developing basic stress tests that can be applied to prudential data.

The mission conducted a half-day workshop to sensitize selected RBM staff on basic issues related to stress testing and subsequently worked with a Stress Testing Working Group (STWG), which consisted of members of staff from Bank Supervision, Research and Statistics, and Banking and Payment Systems Departments. The output of the mission was the development of initial guidelines for the stress testing of prudential data. The guidelines were developed to be consistent with the RBM's Risk Based Supervision (RBS) framework and were focused on RBM's oversight of credit, liquidity, interest rate and foreign exchange rate risk. The guidelines provide instructions on ways in which different tests can be applied to determine the impact on asset quality, liquidity, profitability and capital adequacy.

6.2 Financial Services Volunteer Corps (FSVC)

In 2010, the Department continued to benefit from the technical assistance by Financial Services Volunteer Corps (FSVC). Under a Technical Assistance Agreement, which was supposed to end by 31 January 2010 but was extended for another twelve months to 31 January 2011, FSVC provides the Department with technical assistance through in-house workshops/seminars on topical areas of supervision and by making commentaries on work originally initiated by the Department. During the year under review, FSVC provided the following technical assistance:

- (i) Basel II in country workshop for sub-committee members, (April 2010);
- (ii) Commentary on QIS template, areas of national discretion, and Instructions Manual (between July and September 2010);

- (iii) On the job guidance through Consultants during the first QIS (November 2010);
- (iv) Commentaries on Guidelines for Mergers and Acquisition and on Problem Bank Resolution Framework documents;
- (v) Study tour by the Governor to FSVC Headquarters in USA, and familiarisation to the Federal Reserve;
- (vi) Training of new examiners in financial institution analysis
- (vii) Drafting of a Policy Paper with recommendations on establishment of a Deposit Insurance Scheme (DIS) in Malawi.

FSVC has very close working relationship with USAID in Malawi. As such, the Department also benefited from USAID through commentary on the CRB Regulations by an external Consultant. Subject to FSVC identifying another funding, there is expectation that the technical assistance will continue with focus on implementation of Basel II and Deposit Insurance Scheme.

6.3 Macroeconomic and Financial Management Institute of Eastern and Southern Africa (MEFMI)

The Department continued to benefit from the courses offered by MEFMI. During the year under review, two members of staff attended a Workshop on Consolidated Supervision while one member in the Department was also accredited by MEFMI as a Trainer in specialized bank supervision courses in July 2010.

6.4 Committee of Central Bank Governors (CCBG) and Committee of Central Bank Officials (CCBO) in SADC

At regional level, the Reserve Bank of Malawi is an active member of the Committee of Central bank Governors (CCGB) which is a regional grouping of Central Bank Governors from the SADC block. The CCBG was established as part of the protocol on Finance and Investment and focuses on projects designed to contribute to the process of regional economic cooperation and integration such as development of a monetary and financial statistical database; development of an information bank on the policies and structures of SADC Central Banks; development of a national payment, clearing and settlement systems for SADC countries; co-ordination of training of central bank officials in SADC; analysis of the legal and operational frameworks of SADC central banks; co-operation in the area of information and communication technology; CCBG Macroeconomic Subcommittee; CCBG Financial Markets Subcommittee and Banking supervision.

The CCBG established a SADC Subcommittee of Banking Supervisors (SSBS) to deal with the supervision of banks within the region. The SSBS has a steering committee and the Reserve Bank of Malawi is one of the members of the steering committee as well as the SSBS. The SSBS is currently working on a project to develop a SADC Model Banking Law with the objective of harmonising regulatory and supervisory standards within the region. A working group called the Legal Taskforce on SADC Model Law was formed to spearhead this project comprising of Reserve Bank of Malawi, Bank of Zambia, Reserve Bank of Zimbabwe and South African Reserve Bank. One member of staff was nominated a member of the working group. The Reserve Bank of Malawi will host the next meeting of the CCBG in April 2011.

6.5 East and Southern Africa Anti Money Laundering Group (ESAAMLG)

The Eastern and Southern Africa Anti Money Laundering Group (ESAAMLG), a Financial Action Task Force (FATF) regional style body, was formed in 1999 in Arusha, Tanzania. It comprises of fourteen member countries⁴ in the Sub Saharan southern Africa region.

The main objective of the group is to foster anti money laundering and combating of terrorist financing efforts in the region. This is achieved through Mutual Evaluation exercises conducted in all countries and through progress reports submitted by members at the plenary meetings. In addition, the group carries out research on the trends and typologies of AML/CFT cases happening in the region.

ESAAMLG meetings are held twice in a year. Task Force of Senior Officials Meetings are normally held in March

⁴ Botswana, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe

and hosted by the Secretariat in Tanzania and the Task Force of Senior Officials and Ministerial Council Meetings are held in August hosted by any member country on a rotational basis. The Ministerial Council is the key decision making body within ESAAMLG representative from each member country. The Council elects the President and Vice President among its members.

Malawi is one of the founding members of the group and has continued to support all efforts of the grouping by attending all plenary meetings. Meetings of this group are attended by Government officials from all the relevant government arms i.e. Ministry of Finance, Ministry of Justice, Reserve Bank of Malawi (through Bank Supervision, Pensions and Insurance Supervision and Microfinance and Capital Markets Supervision and Legal Departments), Financial Intelligence Unit, Anti Corruption Bureau, Immigration Department, Director of Public Prosecutions and Malawi Police Service.

Malawi hosted the ESAAMLG 20th Task Force of Senior Officials meeting from 30th August to 3rd September 2010 and 10th Ministerial Council meeting on 8th September 2010 at Cresta Hotel in Lilongwe. The Minister of Finance for Malawi was elected the President of the ESAAMLG and the Secretary to the Treasury became the Chairperson of the Task Force of Senior Officials of the group for one year from September 2010 to August 2011. Malawi stands to gain knowledge and experience by representing ESAAMLG at various International AML/CFT meetings whilst raising its AML/CFT achievements and initiatives at such forums. Previously, the presidency was with the Republic of Lesotho. During the Lilongwe meeting, Bank Supervision Department participated in Finance and Audit working group, Mutual Evaluation Working Group and Development Strategy Implementation Working Group.

The Task Force meeting was also attended by representatives from the member countries. In addition, Cooperating and Supporting Nations, Organizations and Observers from Australian Transaction Reporting Centre (AUSTRAC), East African Community (EAC) Secretariat, International Monetary Fund (IMF), SADC Secretariat, Union of Comoros, United Nations Counter Terrorism Executive Directorate (UNCTED), United Nations Office On Drugs Crime (UNODC), UN Taliban and Al Qaida Analytical Support and Sanctions Monitoring Team, USA and World Bank attended.

During the 20th Task Force of Senior official Meetings, Private Sector consultations on the implementation of FATF Standards and promotion of Financial Inclusion in the ESAAMLG region were accorded a full day. The policy makers (Financial Action Task Force, Consultative Group to Assist the Poor, Alliance for Financial Inclusion) and the financial services providers across the globe discussed the challenges faced in balancing the implementation of FATF recommendations particularly the Customer Due Diligence (CDD) requirements and simultaneously promoting the financial inclusion agenda. Several presentations on strides made towards attainment of financial inclusion were shared by Kenya, Tanzania and Uganda.

6.6 Financial Stability Institute (FSI) and Bank for International Settlement (BIS) Programs

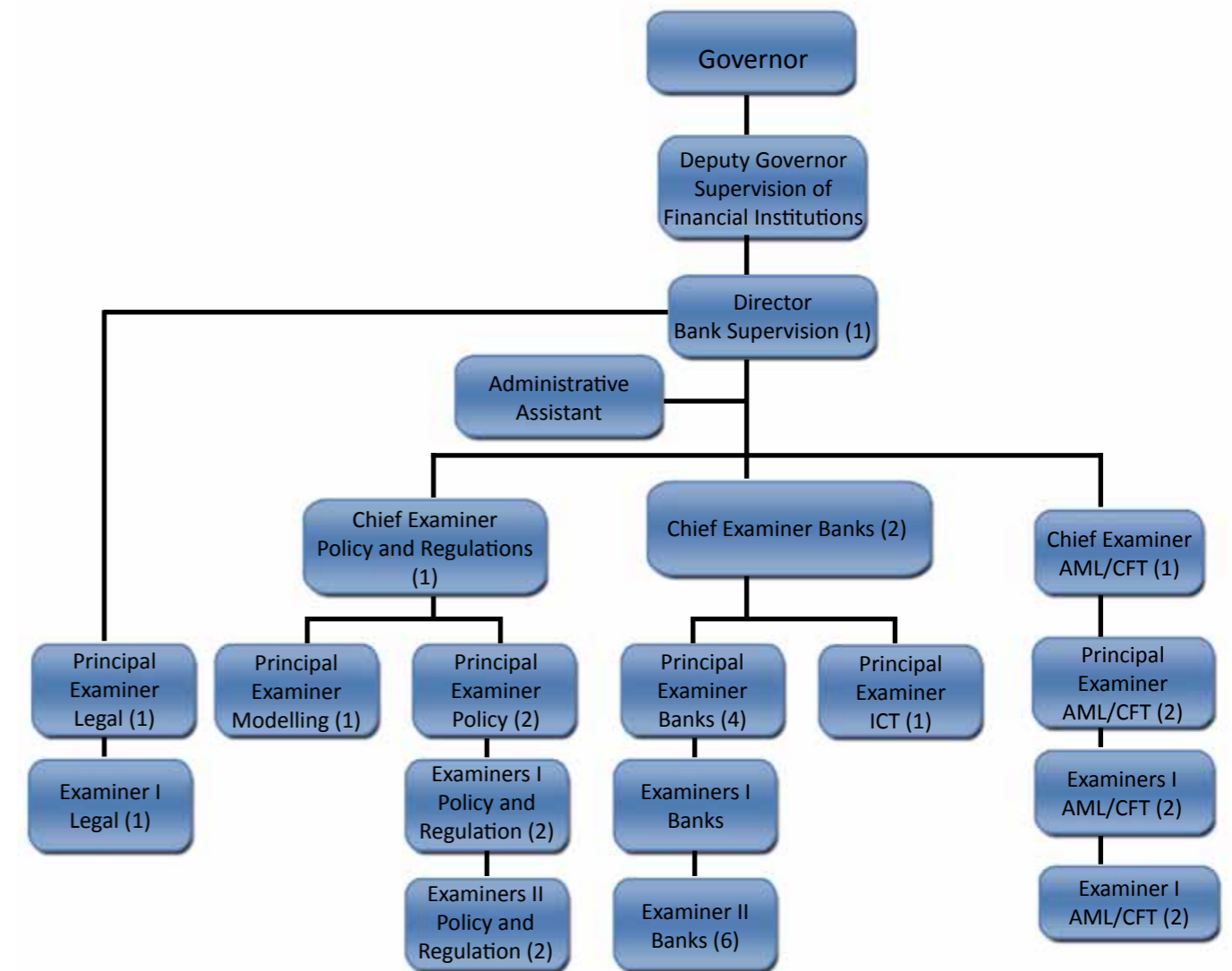
The Department continued to maximize benefits from programs offered by the FSI. During year 2010, one member attended a regional workshop on Risk Based Supervision in Mauritius jointly organised by FSI and SADC. Members also benefited from the use of the FSI Connect on line tutorials. The FSI has proved very beneficial to the Department as a provider of Basel II relevant courses. Its full utilization however, is constrained by the duration of most of its courses which are for three days or less.

APPENDICES

Appendix 1: Malawi Banking Institutions' Shareholding Structure

Banking Institution	Shareholder	Stake
Ecobank Malawi Limited	ECOBANK Transnational Incorporated	92.93%
	Loita Capital Partners International	7.07%
FDH Bank Limited	FDH Financial Holdings Ltd	100.00%
First Merchant Bank Limited	Zambezi Investments Ltd	44.94%
	Simsbury Holdings Limited	22.47%
	Prime Bank Limited (Kenya)	11.24%
	Prime Capital and Credit Limited (Kenya)	11.24%
	General Public	10.11%
Indebank Limited	ADMARC Investments Holding Company	25.67%
	Press Trust	30.0%
	Employment Share Ownership	2.95%
	The Government of the Republic of Malawi	41.38%
International Commercial Bank	ICB Global Financial Holdings	99.99%
	Lee Ooi Kim	0.01%
Malawi Savings Bank	Malawi Government	100%
National Bank of Malawi	Press Corporation Limited	51.6%
	Old Mutual	24.6%
	General Public	22.3%
	Employee Share Ownership Scheme	1.5%
NBS Bank Limited	NICO Holdings Ltd	60.0%
	General Public	31.3%
	National Investment Trust Limited	6.6%
	NBS ESOP	2.1%
Nedbank Malawi Ltd	MN HOLDINGS	97.1%
	ESOP	2.9%
Opportunity International Bank of Malawi	Opportunity Microfinance Investments Limited (UK) (OMIL)	22.9%
	Opportunity Transformation Investments (USA) (OTI)	60.5%
	Africap Microfinance Fund Ltd	12.6%
	Trust for Transformation	4.0%
Standard Bank of Malawi Limited	Standard Bank Africa Holdings Limited	60.18%
	NICO Holdings Ltd	20.00%
	Public	19.82%
Continental Discount House	TRANSAFRICA HOLDING LIMITED:	84%
	PRESS TRUST:	15%
	ESOP	1%
First Discount House Limited	FDH Financial Holdings Ltd	100%
Leasing and Finance Company	First Merchant Bank	100%

Appendix 2: Organisational Structure of Bank Supervision



Appendix 3: List of licensed banking institutions as at 31 December 2010

Name of Banking Institution	Title & Name of Top Officer	Postal Address	Phone and Fax Numbers	Location of Head Office
National Bank of Malawi	Managing Director Mr. G Partridge	Box 945, Blantyre	01 820622 01 820321	Victoria Avenue, Blantyre
Stanbic Bank Malawi Ltd	Managing Director Mr. C Mudiwa	Box 1111, Blantyre	01 820144 01 820360	Glyn Jones Road, Blantyre
NEDBANK Malawi Ltd	Managing Director Mr. A. Kulugomba	Box 750, Blantyre	01 820477 01 820102	Victoria Avenue, Blantyre
Indebank Malawi Ltd	Chief Executive Mr. W Chatsala	Box 358, Blantyre	01 820055 01 835703	Top Mandala, Blantyre
First Merchant Bank	Managing Director Mr. K Chaturvedi	P/Bag 122, Blantyre	01 821942 01 821978	Glyn Jones Road, Blantyre
Ecobank Limited	Managing Director Mr. O. Salu	P/Bag 389, Blantyre 3	01 822681 01 822683	Victoria Avenue, Blantyre
NBS Bank Ltd	Chief Executive Officer Mr. J Bizwick	Box 32251, Blantyre 3	01 876222 01 875485	Ginnery Corner, Blantyre
Opportunity International Bank Malawi Ltd	Chief Executive Mr. A Kalanda	P/Bag A71, Lilongwe	01 758403 01 758400	Old Town, Lilongwe
Malawi Savings Bank	Acting Chief Executive Mr. K. Sadala	Box 521, Blantyre	01 825111 01 821089	Victoria Avenue, Blantyre
Leasing and Finance Company	General Manager Mr. A Chigwale	Box 1963, Blantyre	01 820233 01 820275	Glyn Jones Road Blantyre
Continental Discount House Ltd	Chief Executive Mr M. Esau	Box 1441, Blantyre	01 821 300	Victoria Avenue, Blantyre
International Commercial Bank	Mr J.Gopalan	Box 437 Blantyre	01847901	Stansfield House Blantyre
FDH Bank	Managing Director Mr J. Kayuni	Box 152 Blantyre	01820219	Umoyo House Blantyre
First Discount House Ltd	Managing Director Mr. E. Chilima	Box 512, Blantyre	01 820 219	Victoria Avenue, Blantyre

Appendix 4: Bank Staff Compliment & Branch Network Data as at 31st December 2010

Name of Institution	Branch Network	Agencies	No of ATMs	No of Employees
National Bank of Malawi Ltd	11	14	54	810
Standard Bank Malawi Ltd	8	13	46	634
NEDBANK Malawi Ltd	3	2	4	95
Indebank Malawi Ltd	5	4	9	188
First Merchant Bank Ltd	7	15	43	557
ECOBANK	6	0	7	84
NBS Bank Ltd	13	32	57	614
Opportunity International				
Bank Malawi Ltd	3	23	23	413
Malawi Savings Bank Ltd	6	40	15	450
Leasing and Finance Co Ltd	1	0	0	17
First Discount House Ltd	0	0	0	12
FDH Bank	5	3	0	150
Continental Discount House Ltd	1	0	0	55
International Commercial Bank	3	0	3	54

Appendix 5: Number of banks per CAMEL rating category as at December 2010

NUMBER OF INSTITUTIONS RATED

RATING STRENGTH	COMPOSITE RATING	CAPITAL	ASSET QUALITY	MANAGEMENT	EARNINGS	LIQUIDITY
Strong (1)	0	0	0	0	0	0
Satisfactory (2)	2	6	5	4	4	4
Fair (3)	9	5	5	7	7	4
Marginal (4)	0	0	1	0	0	3
Unsatisfactory (5)	0	0	0	0	0	0

Appendix 6: Directives in force during 2010

DO2-93/MCR	Minimum Capital Ratios for Banks
DO1-97/FX	Foreign Currency Exposure Limits
DO2-97/FXLR	Foreign Currency Lending Ratio
DO1-04/CR	Submission of Call Reports by Banks and other Financial Institutions
DO1-05CDD	Customer Due Diligence for Banks and Financial Institutions
DO1-06/FMO	Liquidity Reserve Requirement
DO1-06/SF	Supervisory Fees
DO1-06/ASCL	Asset Classification and Provisioning
DO2-06/LA FX	Large Exposures
DO3-06/DAS	Audit Committee and Annual Audits
DO4-06/TRP	Transactions with Related Persons
DO5-06/IA	New Directors and Senior Management Officials
DO1-2008/PID	Premises Inspection
DO1-2010/DR	Directive on Disclosure and Publication of Financial Statements
	Policy Statement on the Prudential Aspects of Bank Liquidity
	Corporate Governance Guidelines
	Guidelines on Mergers & Acquisitions

STATISTICAL TABLES

TABLE 1: COMPOSITION OF BALANCE SHEET: LIABILITIES

	Deposits	Due to Other Banks	Interest Payable	Other Liabilities	Capital and Reserves	Total Capital and Liabilities
K' millions						
Average End of Quarter						
2009: 01	136,144	7,722	398	16,318	30,575	191,156
2009: 02	141,705	13,878	638	18,460	32,032	206,713
2009: 03	161,163	5,226	20	20,601	33,512	220,521
2009: 04	168,597	5,935	1,079	18,465	36,087	230,163
2010: 01	165,231	5,605.6	536	17,042	39,384	229,569
2010: 02	168,585	11,260.4	769	17,147	40,491	239,152
2010: 03	191,764	9,302.1	304	15,550	41,978	258,898
2010: 04	206,382	12,965.6	269	17,613	45,158	282,388
Month-end balance for year						
Dec 2008	131,484	8,410	702	15,847	27,548	183,991
Dec 2009	168,597	5,935	1,079	18,465	36,087	230,163
Dec 2010	206,382	12,965.6	269	17,613	45,158	282,388

TABLE 2: COMPOSITION OF BALANCE SHEET: ASSETS

	Cash and Due from Other Banks	Loans and Advances	Securities and Investments	Other Assets	Total Assets
K' millions					
Average End of Quarter					
2009: 01	28,724	86,628	41,674	18,538	175,564
2009: 02	33,269	99,477	42,601	19,153	194,501
2009: 03	41,436	104,328	47,946	21,821	215,531
2009: 04	35,205	114,389	52,839	30,490	230,163
2010: 01	36,414	117,928	46,157	8,370	232,266
2010: 02	31,820	135,520	40,091	8,942	242,240
2010: 03	42,742	139,341	39,260	14,010	261,906
2010: 04	39,834	151,015	52,444	12,108	285,391
Month-end balance for year					
Dec 2008	21,266	80,173	58,978	23,574	183,991
Dec 2009	35,205	114,389	52,839	30,490	230,163
Dec 2010	39,834	151,015	52,444	12,108	285,391

TABLE 3: COMPOSITION OF BALANCE SHEET DEPOSITS

	Demand Deposits	Savings Deposits	Time Deposits	FCDAs	Total Deposits
K' million					
Average End of Quarter					
2009: 01	52,343	22,531	44,276	16,995	136,144
2009: 02	52,908	25,826	44,146	18,824	141,705
2009: 03	55,988	30,131	53,321	21,723	161,163
2009: 04	59,259	28,670	61,877	18,791	168,597
2010: 01	56,705	29,494	58,077	20,955	165,231
2010: 02	61,399	35,276	51,980	19,930	168,585
2010: 03	76,652	33,681	60,913	20,517	191,765
2010: 04	79,780	35,727	71,625	19,251	206,382
Month-end balance for year					
Dec 2008	48,815	25,921	42,226	14,521	131,484
Dec 2009	59,259	28,670	61,877	18,791	168,597
Dec 2010	79,780	35,727	71,625	19,251	206,382

TABLE 4: TRENDS IN CAPITAL ADEQUACY

	Tier 1 Capital	Total Capital	Risk Weighted Assets	Tier 1 Capital Ratio %	Total Capital Ratio
K' million					
Average End of Quarter					
2009: 01	23,138	29,362	121,528	19.0	24.2
2009: 02	23,279	29,840	134,520	17.3	22.2
2009: 03	24,016	30,285	141,566	17.0	21.4
2009: 04	25,208	31,955	142,353	17.7	22.4
2010: 01	33,011	39,890	162,630	20.3	24.5
2010: 02	32,325	40,207	170,795	18.9	23.5
2010: 03	32,377	40,374	179,876	18.0	22.4
2010: 04	31,530	41,174	202,625	15.6	20.3
Month-end balance for year					
Dec 2008	18,760	24,113	111,903	16.8	21.5
Dec 2009	25,208	31,955	142,353	17.7	22.4
Dec 2010	31,530	41,174	202,625	15.6	20.3

TABLE 5: COMPOSITION OF INCOME STATEMENT: SELECTED ITEMS

	Total Gross Income	Interest Income	Non-Interest Income	Interest Expenses	Operating Expenses
K' million					
Average End of Quarter					
2009: 01	8,986	55,609	3,426	1,070	4,341
2009: 02	19,589	11,900	7,689	2,324	9,154
2009: 03	30,434	18,614	11,820	3,664	14,367
2009: 04	41,350	25,900	15,450	5,098	20,296
2010: 01	11,089	7,174	3,916	1,463	5,444
2010: 02	23,485	14,795	8,691	3,151	11,361
2010: 03	36,290	22,633	13,658	4,932	17,788
2010: 04	49,573	30,881	18,691	6,594	24,890
Month-end balance for year					
Dec 2008	31,757	18,536	13,222	3,238	15,829
Dec 2009	41,350	25,900	15,450	5,098	20,296
Dec 2010	49,573	30,881	18,691	6,594	24,890

TABLE 6: PROFITABILITY: SELECTED RATIOS

	Interest Margin	Efficiency Ratio	ROE	ROA	
	%	%	%	%	%
Average End of Quarter					
2009: 01	12.3	48.3	32.7	4.8	36.4
2009: 02	12.7	46.7	34.7	4.9	37.3
2009: 03	12.8	47.2	36.9	5.1	41.8
2009: 04	13.0	49.1	34.1	4.6	42.4
2010: 01	13.0	49.1	29.7	4.6	37.6
2010: 02	13.1	48.4	30.2	4.6	37.0
2010: 03	13.0	49.0	29.9	4.5	35.2
2010: 04					31.5
Month-end balance for year					
Dec 2008	12.1	49.8	43.6	4.8	43.3
Dec 2009	13.0	49.1	34.1	4.6	42.4
Dec 2010	12.9	50.2	29.4	4.2	31.5

TABLE 7: ASSET QUALITY

	Gross Loans and Advances	Non-Performing Assets to Gross Loans %	Non-Performing Assets to Total Assets %	Specific Provisions to Gross Loans %	Specific Provisions to Non-Performing Assets %
K' million					
Average End of Quarter					
2009:01	88,300	3.4	1.5	1.2	36.4
2009:02	101,345	3.1	1.5	1.2	37.3
2009:03	106,314	3.8	1.3	1.2	41.8
2009:04	113,953	3.2	1.5	1.3	42.4
2010:01	117,928	3.6	1.8	1.4	37.6
2010:02	135,520	3.6	2.0	1.3	37.0
2010:03	139,341	3.8	2.0	1.3	35.2
2010:04	151,015	3.9	2.1	1.2	31.5
Month-end balance for year					
Dec-08	81,948	3.2	1.4	1.4	43.3
Dec-09	113,953	3.2	1.5	1.3	42.4
Dec-10	151,015	3.9	2.1	1.2	31.5

TABLE 8: LIQUIDITY

	Liquid Assets to Total Deposits & Short Term Liabilities %	Liquid Assets to Total Deposits %	Rate Sensitive Assets/Rate Sensitive Liabilities%
K' million			
Average End of Quarter			
2009:01	50.1	52.9	101.1
2009:02	48.2	52.9	101.8
2009:03	49.5	51.1	101.4
2009:04	48	49.6	101.8
2010:01	44.9	46.9	101.3
2010:02	36.9	39.6	102.3
2010:03	38.3	40.2	94.0
2010:04	40.7	43.2	98.5
Month-end balance for year			
Dec-08	53	56.8	162
Dec-09	48	49.6	101.8
Dec-10	40.7	43.2	98.5

