2014 Annual Banking Industry Report

FINANCIAL INSTITUTIONS COMMISSION
of the
REPUBLIC OF PALAU

This report is provided pursuant to Section 12 of the Financial Institutions Act (RPPL 6-3, Amended by 7-41).

G. Semdiu Decherong
Executive Commissioner

May 4, 2015
Date

2014 Annual Palau Banking Sector Report

Summary Industry Assessment

The overall condition of the Palau banking sector remains satisfactory and there continues to be growth and stability. Assets have grown 24% during the year as a result of expansion in deposits. Aggregate capital for the two remaining locally chartered banks grew 8% in 2014 because of strong and consistent earnings generated by one bank in particular. Capital has exhibited an increasing trend and uninsured banks demonstrate the desire to maintain capital growth.

Asset quality indicators remain satisfactory. Overall, the ratio of Non Performing Loans (NPLs) to Total Loans has fallen from 3.43% to 3.19% during the year. Loans have slightly risen by 3% or approximately $982M and Provisions for Bad Loans remain adequate to mitigate against potential losses, covering 241% of the sector's Non Performing Loans.

Return on Assets remains stable at 1.44% despite decline in Net Interest Income to Average Assets. ROA stability is primarily due to the decline in Non-Interest Expense to Average Assets suggesting that local banks have managed to keep costs down notwithstanding significant asset growth.

Liquidity remains adequate and all banks demonstrate the ability to continue to meet depositors demand. Funds management practices are adequate for the scope of local banking operations, as supported by onsite exam findings, and continue to demonstrate satisfactory results. U.S. branches continue to generate strong earnings from excess funds invested abroad, and maintain reliable access to adequate sources of funds to meet anticipated local liquidity needs.

*[Note: for the purposes of this report, numbers accompanied by the roman numeral "**M**" represent figures in thousands, and "**MM**" represents figures in millions]*

New Developments

The FIC Board officially welcomed Mr. Melwert Kikuo in November 2014. Mr. Kikuo was made a board member by Senate Resolution 9-138 adopted on October 21, 2014, making him the fifth voting member on the agency's Governing Board of Commissioners and replacing Mr. Kenneth T. Uyehara.

Mr. Uyehara, whose term and Vice Chairmanship ended August 19, 2014, was given recognition by the FIC as the longest serving member of the Governing Board of Commissioners during a farewell gathering in November 2014. He began his tenure with the FIC in August 2005 and served a remarkable nine year term on the FIC Governing Board of Commissioners. The remaining members of the board are Chairman Okada Techitong, Vice Chairman Tutii Chilton, Ms. Uroi Salii, and Mrs. Jennifer Koskelin-Gibbons.

Ms. Sandra Mincer vacated her post as President of the National Development Bank of Palau. The FIC Board has been without an Ex-Officio member of the Board since November 2014 and no formal appointment or hiring has been announced by the development bank's board as of the date of this report.

There were several legislations and regulations introduced during 2014.

- Title 17 of the Palau National Code was amended and signed into law on April 24, 2014, which expanded the criminal code and enhanced areas of the law related to the Anti-Money Laundering & Proceeds of Crime Act (AMLPCA). Because of the amendments to the AMLPCA, Palau improved on its rankings with the APG and is no longer on "enhanced monitoring".
- The National Development Bank of Palau will now fall under the supervisory authority of the FIC, as legislation allowing the entity to take deposits was signed into law on December 5th, 2014.
- New legislation was drafted regarding Credit Unions. The FIC met with representatives from active local credit unions who were looking to advance the current credit union legislation. Working with PFTAC and Legal Counsel for the Senate, the FIC completed drafting the credit union bill. The new law would establish the framework for the regulation of credit unions and update the current system of licensing, registering and monitoring. Survey work of all credit unions in the country was also conducted during the year to compile relevant financial information and to assess the size and scope of the credit union sector. ***as of the date of submission of this report to the OEK, the Credit Union Act failed to pass First Reading by the 9th OEK***
- The FIC continues work with the ADB on the Corporate Registry project, entailing the draft and introduction of amendments to the corporations act. The aim of the project is to improve corporate annual filing processes in order to promote private sector growth.
- Insurance legislation was introduced in the Senate during April 2014 and the Executive Commissioner had submitted comments as requested.
- The revised Capital Adequacy regulation PR-01 was put into effect in April 2014. This revision followed that amendment to the Financial Institutions Act which lowered the minimum required capital of uninsured foreign bank branches from five million down to two million to be held locally.
- The regulation on Voluntary Liquidation AR-04 was put into effect in September 2014.

During the 2014 calendar year, there were a few individuals/entities that expressed interest in establishing banking institutions in Palau, however, the Commission did not receive any complete application packets for new banking licenses, and thus, none have been reviewed. The Governing Board of the FIC had lifted the moratorium on issuance of new banking licenses by that resolution unanimously adopted on and dated July 29, 2010. The moratorium on the establishment of new banks in Palau became effective on February 19, 2003 by FIC Resolution No. 02-2003-03 dated the same in order to allow the Commission time to adopt and fully implement its prudential and administrative regulations as promulgated under the Financial Institutions Act.

Background & General Overview

The Financial Institutions Commission (the Commission or FIC) is responsible for the licensing, supervision, and regulation of all banks and financial institutions in the Republic of Palau. The Commission was established as an independent and autonomous agency by Republic of Palau Public Law No. 6-3, commonly known as the Financial Institutions Act of 2001 (FIA or the Act); the Act was further amended and improved during the 7th Olbiil Era Kelulau under Republic of Palau Public Law 7-41. The FIA was codified into the Penal Code under 26 PNCA Chapter 10.

Structure of the Commission

The Commission is governed by a **Board of Commissioners** (**Governing Board**). The Governing Board functions as a policymaking body to promulgate the rules and regulations by which the Commission operates. The Governing Board also oversees the enforcement of policies, rules, and regulations as they apply to all licensed banks. The Governing Board is composed of five voting members and an Ex-Officio member. The five voting members are appointed by the President of the Republic of Palau, subject to the confirmation of the Senate and serve staggered two and three year terms; the sixth Ex-Officio member is the President of the National Development Bank of Palau (NDBP), as mandated by law.

The **Executive Commissioner** manages and oversees administrative tasks and operational matters of the Commission. The Executive Commissioner is responsible for the implementation of Governing Board policies and ensures bank compliance with FIC Regulations and executes Governing Board approved enforcement actions. Policy initiatives, in particular those that pertain to the monitoring and regulation of the Republic of Palau banking sector, are recommended by the Executive Commissioner to the Governing Board. The Executive Commissioner is appointed by and answers directly to the Governing Board and serves as the "Examiner in Charge", which involves the tasks of conducting and managing on-site examinations and is responsible for determining the scope and type of exams for banks in noncompliance with laws and regulations. All bank examinations conducted by the Commission are subject to final approval by the Examiner in Charge.

The **Bank Examiner** answers directly to the Executive Commissioner and is primarily responsible for conducting off-site analysis and on-site bank examinations. These include but are not limited to quarterly and annual analyses of individual bank and sector-wide financial returns, as required by FIC Regulations, and any available financial sector statistics. Off-site examinations involve the review, analysis, and detection of trends and/or singular events that may impact banks' financial condition. This off-site monitoring of financial institutions is conducted quarterly or as needed to the Executive Commissioner for determination of proper supervisory actions.

On-site examinations involve visits to bank/branch offices by the Executive Commissioner and Bank Examiner for an in-depth and detailed review of bank documents, records, as well as general observations of bank operations, for the purpose of assessing six bank rating components (i.e. Capital adequacy, Assets quality, Management, Earnings, Liquidity, and Sensitivity to market risks). Such exams are mandated in the Act, and are conducted in order to regularly monitor the performance of banks to ensure the soundness and stability of the overall sector. On-site bank examinations allow for the Commission to assign an overall rating for individual banks, which allows for the appropriate levels of supervisory actions and regulatory oversight to ensure the safety and soundness of individual banks.

The **Office Manager (Administrative Officer III)** manages the administrative operations of the FIC office with oversight by the Executive Commissioner and is responsible for the maintenance of records, documentation processing, and fulfills all clerical and related operational and administrative functions. The Office Manager is responsible for preparation of annual budgets and assists in the monthly reporting to the Governing Board of fiscal performance of the agency. The Office Manager ensures proper procedures are followed in the procurement of goods and services and monitors operational expenses to ensure adherence to the Governing Board approved budget and works directly with the Executive Commissioner to ensure that internal fiscal policies or guidelines are adhered to and agency expenses are kept at a minimum. In addition to administrative tasks, the Office Manager is also the Registrar of the Secured Transactions Registry.

Anti-Money Laundering

In addition to regular bank supervision, the Commission is given authority in the Financial Institutions Act to examine all financial institutions' Anti-Money Laundering and Counter Financing of Terrorism (AMLCFT)

procedures and reporting standards. Such examinations may, at the sole discretion of the FIC, be conducted as an on-site or off-site examination, or both. The FIC includes onsite AML/CFT examinations during regularly scheduled onsite bank examinations.

Financial Intelligence Unit

The Financial Intelligence Unit (FIU), established by RPPL 6-4, is located within the FIC and operates as an independent body with an operating budget that is provided by the FIC. The FIU is overseen by the Governing Board of the FIC and the Attorney General. Although the Attorney General serves as the Head of the FIU by law, the FIU Director manages the daily administration and operations of the agency.

Mr. Nelson Werner, an American Attorney formerly with the Office of Independent Counsel and the Palau Attorney General's Office was hired to the FIU Director post effective August 1, 2014.

Internal and External Cooperation

In the interest of maintaining the reputation of the Republic of Palau in the international financial community, the Commission is authorized by the Act to cooperate and exchange information with agencies of foreign governments and international organizations. To this extent, Section 8 of the Act stipulates that a grant of a banking license by the Commission constitutes consent of the financial institution to release to and exchange information with any law enforcement, regulatory, or supervisory authorities of any foreign government in which the financial institution operates or conducts business. As such, the Commission has worked with the U.S. Federal Deposit Insurance Corporation (FDIC), Australian Prudential Regulatory Authority (APRA), Bank Negara (Malaysia), Banco Central (Philippines), ROC Taiwan Financial Services Commission, Hawaii State Division of Financial Institutions, FSM Banking Commission, RMI Bank Commission, and other foreign regulatory authorities on a myriad of issues concerning both foreign regulators and the Commission. The Commission cooperates with competent authorities outside Palau and with international organizations in terms of its collection of statistics and related financial sector information for the purposes of comparative analysis and compliance with international regulatory and reporting standards. It is further mandated in the Act that the Commission cooperate with local public authorities in pursuing its objectives.

Training and Technical Assistance

The Commission receives extensive technical training and support from international organizations and supervisory agencies such as the International Monetary Fund (IMF), the Pacific Financial Technical Assistance Centre (PFTAC), and recently, the U.S. FDIC. The Executive Commissioner and Bank Examiner have successfully completed the first three phases of the FDIC's series of examination schools and completion of the final part of FDIC examination training will be scheduled when funding is available. Other prior training received by the Executive Commissioner includes areas such as designing effective legal frameworks for problem bank supervision, Anti-Money Laundering and Counter-Terrorist Financing, FDIC Receivership methods, and others. In addition, the Bank Examiner has received training on liquidity frameworks and analysis as well as loan and financial statement analysis from PFTAC in conjunction with APRA and the Bank of International Settlements' Financial Stability Institute.

Sector Overview

The Financial Institutions Commission monitored and regulated five banks during the 2014 calendar year—three U.S. bank branches and two locally chartered banks. The three foreign bank branches are U.S. chartered and insured by the U.S. Federal Deposit Insurance Corporation (FDIC) whereas the locally chartered banks do not maintain depositor insurance. The National Development Bank of Palau, formerly exempt from regulation and oversight, automatically fell under the supervisory authority of the FIC when RPPL 9-41 was signed into law on December 5, 2014.

For the purposes of this report, the banking sector has been divided into two banking groups, namely the insured banks and uninsured banks, due to the broad differences in size and business scope that are unique to the banks that have been categorized within these groupings. In this report, "insured banks" means those banks/branches whose deposits are insured by the U.S. FDIC; and "uninsured banks" are those banks that do not maintain depositor insurance under a government sponsored insurance program. The U.S. bank branches

hold approximately 94% of the banking sector's aggregate Net Loans and over 99% of the sector's aggregate Total Deposits. [1]

The Commission's primary objective is to ensure the liquidity and solvency of banks in the Republic of Palau pursuant to the requirements of the Financial Institutions Act and regulations promulgated therein. The agency fulfills its objective by conducting offsite monitoring of all licensed banks and through onsite examinations.

Off-Site Monitoring and Bank Examinations

The Commission schedules onsite bank examinations based on each bank's assigned rating determined at the most recent onsite examination in accordance to a Regulatory Response Policy. The Executive Commissioner reviews quarterly an individual bank's financial information reported on the FIC Prudential Returns as well as analysis reports produced by the Bank Examiner. Quarterly returns consist of three forms and several related schedules providing current information on an institution's balance sheet and income and expense statements.[2] Quarterly prudential returns and analysis reports are the main component of the FIC's off-site monitoring program and the Commission utilizes quarterly assessment reports as an integral part of on-site bank examination planning and scheduling.

Data submitted by all licensed banks on quarterly prudential returns are entered into a computer database and used in the calculation of pertinent ratios and indicators which help to monitor the performance of each bank. These ratios and indicators are compiled into a report aptly named the Uniform Bank Performance Reports which are disseminated as appropriate to all licensed banks. The UBPRs contribute to the FIC's off-site monitoring program and provide comparative analysis and performance tracking for each bank, banking group, and industry wide. Valuable data is provided to management of each licensed institution through dissemination of UBPRs and the publication of quarterly and annual reports on the FIC's official website.

The FIC continues to regularly and consistently produce analysis reports for each licensed bank and branches, as well as an overall banking industry report every quarter. These reports are produced by the Bank Examiner and submitted to the Executive Commissioner for review and final draft. The industry report is generated as a general overview of the condition of the banking sector and is submitted to the Governing Board of the FIC. An annual report is also produced for submission to the Olbiil Era Kelulau (OEK) as required under the banking law using figures from those statements of condition published annually by each licensed bank in Palau as well as aggregate figures derived from the FIC's quarterly prudential returns. The fifth Annual Banking Sector Report to the OEK was submitted on April 15th, 2014, for the calendar year ending December 31st, 2013.

The FIC conducted onsite examinations of two out of the five licensed banks in Palau during the 2014 calendar year as well as an onsite review of the National Development Bank's lending policies and practices by request of the development bank's management.

Onsite examinations are scheduled based on composite ratings issued using the CAMELS rating system adopted from the bank examination procedures employed by U.S. regulators. Both the Executive Commissioner and the Bank Examiner have completed several bank examination trainings by the U.S. FDIC and PFTAC.

The FIC has established amiable and productive working relationships with designated reporting officials for the three U.S. branch institutions and the Boards and Management of all other banking institutions in Palau. The Commission continues its efforts to improve the quality of information reported by fostering better communication between the agency, bank/branch managers, and related officials that play a pivotal role in ensuring adequacy and accuracy in financial reporting and compliance with regulatory requirements.

[1] Based on figures reported for 2014 published by all banks. Historical data indicates that U.S. branch institutions continue to lead the sector in assets and deposits and are reporting fairly consistent growth and stable to growing market share. As a cautionary note, published figures and those reported to the FIC may differ due to variations in reporting requirements from bank accounting procedures. Aggregate figures used here are derived from those published by all licensed banks.

[2] Previous regulatory financial forms were submitted on a voluntary basis by banking institutions until September 1, 2008 when FIC Prudential Regulations were made effective and required regular quarterly reporting from all licensed banks. The FIC prudential forms were revised in January 2009 and again in July 2012 to include more detailed breakdowns of financial statement items. The required forms were initially implemented beginning December 2009 and all banks in the sector are required to submit all relevant forms and schedules, certified by bank officials, in electronic form within 30 days following each quarter-end.

Agency Interaction and Cooperation with Regulated Banks

All licensed banks have cooperated with the FIC in compliance with Prudential Regulations and have lent their cooperation and support to this agency's efforts in statistical data collections, prudential reporting, onsite bank examinations, and other issues. The FIC intends to continue to foster the existing good working relationship with all licensed banks to ensure cooperation, assistance, and input on Regulations, the banking law, compliance issues, and other matters pertinent to the industry.

The FIC maintains open and transparent communications with all regulated banks and ensures that these industry partners are informed on matters affecting their operations, i.e. bank examinations, off-site reviews, revisions of laws and or regulations, policy initiatives, and fee assessments.

Financial Institutions Not Regulated by the FIC

Insurance providers/agencies, micro-lending facilities (a.k.a. finance companies), pension funds, and credit unions with assets less than $500,000 are exempt from regulatory oversight and supervision. However, the FIC has received expert advice and opinions from the Asian Development Bank, the IMF, and PFTAC regarding bringing these non-banks under its supervisory authority.

Below is an analysis of the current condition of the banking industry. On September 1st, 2008, Prudential Regulation PR-03 became effective and established requirements for all banks and branches of foreign banks (banks) to prepare and submit quarterly reports to the FIC within 30 (thirty) days following each quarter ending on March 31st, June 30th, September 30th, and December 31st of every year. Figures are required to be reported on a calendar year-to-date basis in accordance with written instructions prepared and issued by the FIC. Aggregate figures used in this report are derived from these quarterly prudential forms submitted to the Commission.

BANKING SECTOR INDICATORS: Capital, Assets, Earnings, & Liquidity

CAPITAL ADEQUACY (Uninsured banks):

- **Aggregate capital for uninsured banking institutions continues its upward trend and increased by 8%, or $208M, during the year.** The strong earnings performance of one locally chartered bank has resulted in aggregate capital accretion for the uninsured banks, which individually are required to maintain at least one million U.S. dollars in capital.
- The FIC monitors Uninsured banks to ensure capital levels are maintained above statutory minimum requirements and has verified each bank's capital position during onsite examinations conducted during the 2013 and 2014 calendar years. The two remaining uninsured banks in the sector remain in compliance with regulatory minimum capital ratios pursuant to statute and FIC prudential regulation PR-01 as well as the required minimum level of capital.

ASSET QUALITY:

- Quality of assets remains satisfactory for the banking sector.

  The quality of the sector's loan portfolio continues to be satisfactory with a Non Performing Loans to Total Loans ratio of 3.19%, slightly down from 3.43% last year. The sector's Non Performing Loans (NPLs) fell 4% or by $44M during 2014, a nominal decrease relative to the approximately $1MM in total NPLs and the $32.1MM in Total Loans.
- Total loans grew by $982M or 3% during the year. Unsecured consumer loans, which comprise 88% of the sector's portfolio, grew by 5.9%, or approximately $1.6MM. On the other hand, Business loans (i.e. loans to Non-financial corporations) declined by $460M or 15%.
  - *Insured banks* still hold 97%, or approximately $188MM, of the banking sector's total assets; 90% or approximately $29MM of the sector's total loans, and 56%, or approximately $569M of the sector's Non Performing Loans as of year-end.[3]
  - The ratio of Loans past due 360 days or more to Total Loans is minimal at 1.23%, down from 1.54% at prior year-end. Loans past due 360 days or more[4] fell 17.5%, or by approximately $84M, from last year bringing down the total to $396M for all commercial banks.
- **Provisions for Bad Loans remain adequate for all commercial banks**. Aggregate Provisions for Bad Loans covers 241% of the sector's Non Performing Loans indicating that there is sufficient cushioning that well exceeds the potential for loan losses.
- Due From Home Office balances of U.S. Branches comprise 80% of the banking sector's Total Assets. Approximately $155MM of the industry's $158MM in total cash and Due from Depository Institutions balances are demand deposits due from the Home Offices of U.S. FDIC-insured banks. Onsite exam findings show that all but one of the **Insured bank branches generated yields higher than the average effective Federal Funds Rate** during fourth quarter.

[3] The FIC has confirmed during onsite examinations of these branch institutions that internal policies and procedures, particularly those that dictate asset management, comply with prudential regulations, ensuring that asset quality remains satisfactory and resulting in minimal losses as demonstrated by historical figures reported for this group of banks.

[4] *Insured banks* do not maintain on their books any loans past due 180 or more days as pursuant to their respective internal loan policies, thus the balance of these loans that are more than a year past due is attributable to Uninsured banks.

EARNINGS PERFORMANCE:

- **Earnings performance for the sector continues to be satisfactory.** Most banks generated profits during the calendar year. Stable and growing profitability is expected overall with potential to expand lending that is stimulated by continued growth in the deposit base.
  - Return on Assets (ROA) for the overall sector remains stable at 1.44%. According to the most recent interest rate surveys conducted, deposit rates range from 0.02% to 1.5% with local demand and savings rates gradually falling. Lending rates remain stable and capped at 18% due to standing legislation. Unsecured consumer loan rates range from 11% at the lowest whereas business loans may yield as low as 7.25% depending on subjective criteria.
    - ROA for *Insured banks* has gone down slightly from 1.39% to 1.36%. However, for *Uninsured banks* ROA grew to 3.82% from 3.07% in the past year primarily due to higher net interest income as a result of loan growth combined with reduced interest and operational expenses.
  - Both Net Interest Margin (NIM)[5] and average Yield on Loans are slightly lower compared to last year, suggesting that, on average, lending rates are gradually falling. NIM fell from 3.31% to 2.99% and Yield on Loans is slightly down from 11.40% to 11.17%, both compared to prior year-end.
  - The estimated average yield on aggregate balances Due from Home Office & Other branches of the *Insured group of banks* remains stable at 0.93%, and is notably above the Effective Federal Funds Rate average of 0.10% for fourth quarter. The yield on these balances maintained abroad indicate strong earnings from the investment of excess funds in the U.S.

Condensed Income & Expense Statement

Annualized (in U.S. '000s)	CYE2013			CYE2014		
	Insured	Uninsured	All Banks	Insured	Uninsured	All Banks
Interest And Fee Income	4,029	527	4,556	4,581	557	5,138
Interest Expense	213	10	223	182	2	184
NET INTEREST INCOME	**3,816**	**517**	**4,333**	**4,399**	**555**	**4,954**
Provisions For Bad Loans Expense	**840**	**15**	**855**	**766**	**14**	**780**
NON-INTEREST INCOME	**1,067**	**8**	**1,075**	**792**	**5**	**797**
NON-INTEREST EXPENSE	**2,004**	**338**	**2,342**	**2,063**	**325**	**2,388**
NET INCOME (LOSS) BEFORE TAXES	2,039	172	2,211	2,362	221	2,583
Less: Applicable Income Taxes	83	11	94	94	13	107
Year-to-date Income (Loss)	**1,956**	**161**	**2,117**	**2,268**	**208**	**2,476**

LIQUIDITY ADEQUACY:

- **Liquidity continues to be strong for all banks in the sector.**
- The Liquidity Ratio calculated for the banking sector, at 87%, is stable and growing. This means that for every dollar in short term liabilities, the banking sector maintained 87 cents in liquid assets. Liquid assets[6] grew by approximately $37MM, or 31% during 2014, which is commensurate with the increase in short term deposits.
- Even though local liquid assets (i.e. cash balances) aggregated for *Insured branch institutions* cover just 1.05% of

[5] Net Interest Margin is equal to Net Interest Income, which is the difference between Interest Income and Interest Expense, divided by Average Earning Assets. Earning Assets comprises net loans and deposits placed with the headquarters of local branches which earn a return from investments abroad. NIM will generally be lower than the difference between average yield on loans and cost of deposits because it is a calculation of the estimated return for every dollar of earning assets.

[6] Liquid Assets (PR-10) includes (i) currency and coin, domestic and foreign, to the extent that any foreign currency is readily convertible to U.S. dollars; (ii) net balances with banks, domestic or abroad, to the extent that such balances are not encumbered or subject to withdrawal restrictions and have a remaining term to maturity of one year or less; and (iii) unrestricted, readily marketable securities which have a value that can be determined from a listing on a recognized international securities exchange.

total short term liabilities, including deposits with maturities of one year or less for this group of banks, onsite examinations of all U.S. branch institutions show that insured branches maintain sufficient funds to meet depositor demands and operational needs. All U.S. branches demonstrate a net cash export position as well as maintain adequate reporting and monitoring systems to manage risk of cash shortfall.

- Notwithstanding concerns with the security of their respective liquid assets, *Uninsured banks* demonstrate ability to cover all customer deposits and short term liabilities and rely more on capital to generate earnings.

- **All banks in the sector demonstrate continued ability to meet depositor demands**.

- Total short-term Customer Deposits for the banking sector grew 25%, or by approximately $36MM, during the calendar year. The deposits of non-financial corporations in particular grew by a significant $21.5MM or 32% during the year. The deposits of State Governments and Individuals follow suit expanding by $7.6MM or 104% and $5MM or 10%, respectively, during 2014. National government deposits on the other hand fell slightly by 1% from approximately $17.6MM down to $17.4MM.

The ratio of Total Deposits to Total Loans slightly rose from 471% to 573% commensurate with deposit growth outpacing loan growth. This ratio means that on average, for every dollar in loans, the sector maintains approximately $5.73 in deposits. This ratio has several implications, including that deposits continue to be taken in faster than new loans are being issued by banks in the sector. Although bank officials have expressed during onsite exams the willingness and capacity to expand their respective loan portfolios, there are factors inhibiting any significant growth in loans. Namely, lack of legislative support for real estate secured lending and market size (i.e. limited pool of qualified borrowers). Rather than investing locally in terms of expansion in lending, U.S. banks continue to invest excess liquidity abroad with the U.S. Federal Reserve.

OTHER BANKING SECTOR STATISTICS

Remittances

- **A total of approximately $108MM came into Palau and approximately $130MM were sent abroad during the 2014 calendar year** through the banking sector. Remittances to and from the U.S., 'All Others' unspecified countries, Taiwan, and Japan – our main trading partners – top the list.

- Remittances from those above listed main trading partners together comprise 96%, or approximately $104MM, of total funds received during 2014. Of the total Outgoing remittances during 2014, approximately $115MM in funds, or 88%, were sent to those same main trading countries listed above.

- Remittances to the U.S., 'All Others' unspecified countries, Taiwan, and the Philippines have grown significantly compared to the previous year. Outbound remittances to the aforementioned countries grew $12MM or 26%, $5MM or 25%, $3.8MM or 49%, and $3.2MM or 32%, respectively, compared to the totals reported for calendar year 2013.

- The volume of Outgoing remittances originated by Individuals totaled approximately $21MM during 2014. Figures reported show that the majority of these funds were sent to the U.S., Japan, All Countries unspecified on prudential return forms, the Philippines and Taiwan—in that order.

Financial Access

The number of Depositors and number of Borrowers are aggregated from figures reported by all five banks, and as such, there will be overlap as there are customers that will have accounts at multiple banks.

- Both the number of Depositors and number of Deposit Accounts increased during the year, contributing to further expansion in the sector's deposit base and resulting in the banking sector's asset growth. The aggregate number of Depositors reported by all banks went up from 21,379 to 22,231. The average number of depositors for the banking sector is 7,410 if depositors banked with at least three of the five licensed financial institutions—up from 7,126 last year. The total number of Deposit Accounts grew from 22,968 to 23,902.

- The total number of Borrowers and the number of Loan Accounts are also higher compared to last year by 379 and 373, respectively. Total number of Borrowers is 6,220 whereas Loan Accounts total 6,232 as of the end of 2014. This implies an opening up of credit access in the sector even though the volume of loans aggregated for the sector has only gone up by a nominal $982M or 3%.

Ratios & Summary Balance Sheet

KEY RATIOS (%)	CYE2013			CYE2014		
	Insured	Uninsured	All Banks	Insured	Uninsured	All Banks
Total Capital to Total Assets	n.a.	50.71	n.a.	n.a.	53.26	n.a.
Tier 1 Leverage Capital Ratio	n.a.	47.70	n.a.	n.a.	49.50	n.a.
Tier 1 Risk Based Capital Ratio	n.a.	92.39	n.a.	n.a.	94.19	n.a.
Total Risk Based Capital Ratio	n.a.	99.95	n.a.	n.a.	103.14	n.a.
Non Performing Loans to Total Loans	1.12	25.94	3.83	1.97	14.12	3.19
Provisions for Bad Loans to NPLs	355.60	162.41	212.56	194.73	298.02	240.57
Net Income to Average Assets (ROA)	1.39	3.07	1.45	1.36	3.82	1.44
Net Interest Income to Average Earning Assets	2.81	14.30	3.11	2.72	14.44	2.99
Interest Margin to Gross Income	78.15	98.48	80.12	84.74	99.11	86.14
Non Interest Expense to Average Assets	1.42	6.44	1.60	1.24	5.97	1.39
Average Yield on Loans	11.13	15.43	11.57	10.66	15.72	11.17
Average Cost of Deposits	0.16	1.67	0.16	0.11	0.35	0.11
Liquidity Ratio (PR-10)	82.94	110.93	83.08	86.77	164.83	87.01
Cash Balances to Short Term Liabilities	2.34	18.07	2.42	0.98	21.68	1.05
Average Earning Assets to Average Assets	96.33	68.86	95.34	96.91	70.56	96.08
Net Loans to Total Assets	17.96	34.74	18.55	14.77	33.62	15.31
Customer Deposits to Total Loans	522.16	18.63	470.97	634.88	17.04	572.95

Summary Balance Sheet Calendar Year to Date Amounts (in U.S. '000s)	CYE2013			CYE2014		
	Insured	Uninsured	All Banks	Insured	Uninsured	All Banks
Cash and Due from Other Banks	119,945	822	120,767	156,926	928	157,854
Other Assets	3,165	2,708	5,873	3,284	2,750	6,034
Net Loans	26,956	1,879	28,835	27,761	1,863	29,624
Gross Loans	*27,941*	*3,162*	*31,103*	*28,869*	*3,216*	*32,085*
Provisions for Bad Loans	*(985)*	*(1,283)*	*(2,268)*	*(1,108)*	*(1,353)*	*(2,461)*
Performing Loans	*27,664*	*2,372*	*30,036*	*28,300*	*2,762*	*31,062*
Non Performing Loans	*277*	*790*	*1,067*	*569*	*454*	*1,023*
******Loans over 360 days past due******	*NA*	*480*	*480*	*NA*	*396*	*396*
******Past Due Loans (includes NPLs)******	*1,246*	*969*	*2,215*	*1,646*	*699*	*2,345*
TOTAL ASSETS	**150,066**	**5,409**	**155,475**	**187,971**	**5,541**	**193,512**
Total Deposits	145,898	589	146,487	183,284	548	183,832
Demand/Checking	*63,963*	*0*	*63,963*	*83,029*	*0*	*83,029*
Savings	*69,224*	*569*	*69,793*	*87,934*	*513*	*88,447*
Time Deposits	*12,711*	*20*	*12,731*	*12,321*	*35*	*12,356*
Other Liabilities	2,212	2,077	4,289	2,419	2,042	4,461
TOTAL LIABILITIES	**148,110**	**2,666**	**150,776**	**185,703**	**2,590**	**188,293**
Issued and Fully Paid Up Common Stock	NA	4,005	4,005	NA	4,005	4,005
Paid-in Premium	NA	0	0	NA	0	0
Retained Profits (Losses)	1,956	(1,264)	692	2,268	(1,054)	1,214
Other Changes to Capital	0	2	2	0	0	0
TOTAL CAPITAL	**1,956**	**2,743**	**4,699**	**2,268**	**2,951**	**5,219**
TOTAL LIABILITIES & CAPITAL	**150,066**	**5,409**	**155,475**	**187,971**	**5,541**	**193,512**

APPENDIX

	As of Calendar Year-End 2014[1] (In U.S. Thousands)					As of Calendar Year-End 2014 (In U.S. Thousands)		
Statements of Condition figures published by all banks	Bank of Hawaii	Bank of Guam	BankPacific[2]	Palau Construction Bank	Asia Pacific Commercial Bank	**Insured Banks**	**Uninsured Banks**	**Aggregate All Banks**
Cash & Due From Banks	1,039	61,261	14,224	639	297	76,524	936	77,460
Net Loans	17,759	8,016	1,977	1,054	815	27,752	1,869	29,621
Other Assets[3]	82,905	89	18	618	98	83,013	716	83,729
TOTAL ASSETS	**101,703**	**69,366**	**16,219**	**2,311**	**1,210**	**187,288**	**3,521**	**190,809**
Deposits	97,834	69,350	16,260	422	126	183,443	548	183,991
Other Liabilities	27	17	46	20	2	90	22	112
TOTAL LIABILITIES	97,861	69,366	16,306	442	128	183,533	570	184,103
CAPITAL	3,842		(87)	1,869	1,082	3,755	2,951	6,706
TOTAL LIABILITIES & CAPITAL	**101,703**	**69,366**	**16,219**	**2,311**	**1,210**	**187,288**	**3,521**	**190,809**
Statements of Income (Loss) figures published by all banks	Bank of Hawaii	Bank of Guam	BankPacific[2]	Palau Construction Bank	Asia Pacific Commercial Bank	**Insured Banks**	**Uninsured Banks**	**Aggregate All Banks**
Interest Income	3,100	1,146	159	358	160	4,405	518	4,923
Interest Expense	164	131	13	1	1	309	2	311
NET INTEREST INCOME	**2,936**	**1,015**	**146**	**357**	**159**	**4,096**	**516**	**4,612**
Non Interest Income	856	148	102	39	5	1,107	44	1,151
Non Interest Expense	1,641	843	335	165	174	2,820	339	3,159
Net Income (Loss) before Tax	2,151	319	(87)	231	(10)	2,383	221	2,604
Less: Applicable Net Income Tax	84	16	0	11	2	100	13	113
NET INCOME (LOSS) after Tax	**2,067**	**303**	**(87)**	**220**	**(12)**	**2,283**	**208**	**2,491**

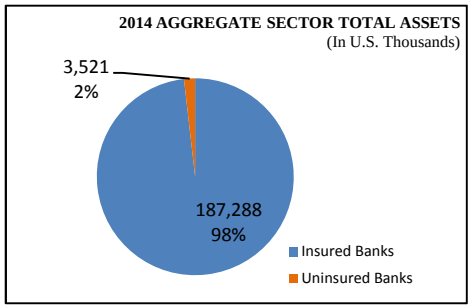
1/ All banks published Statements of Condition and Statements of Income (Loss) by March 1st 2015 with postings in bank lobbies

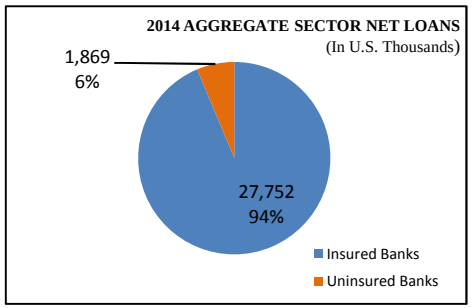
2/ BankPacific's figures are as of June 30, 2014, since the bank's fiscal year ends on June 30th.

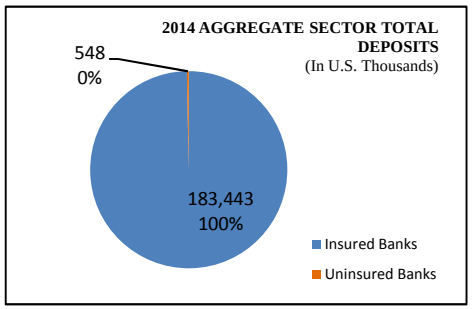
3/ includes fixed assets and accrued receivables other than loans; for Bank of Hawaii, Other Assets includes balances Due From Home Office

Key Ratios

Return on Total Assets	2.03%	0.44%	-0.54%	9.52%	-0.99%	1.22%	5.91%	1.31%
Return on Total Equity				11.77%	-1.11%		7.05%	
Capital to Average Assets				73.75%	98.41%		29.99%	
Liquid Assets to Total Deposits	1%	88%	87%	151%	236%	42%	171%	42%







from Annual Statements of Condition for all banks in Palau published and posted on March 1st by all banking institutions pursuant to FIC regulatory requirements (PR-11)

BANKING INSTITUTIONS OPERATING IN PALAU

As of January 2015

Bank Name	Home Country Charter	Date of Charter	License Status	Primary Regulator	Local Management	Address	Contact Information
Asia Pacific Commercial Bank	Palau	1/21/2000	Active	FIC	Mr. Mun Chee Woo, *President* Ms. Georgina Misajon, *Bank Manager*	Ikelau, Koror P.O. Box 10025 #2B-105 Republic of Palau 96940	Tel. 488-8388 / 488-8981 Email: asiapac@palaunet.com
Bank of Guam	Guam	Guam: 1972 Opened Palau branch: 3/13/1984	Active	U.S. FDIC	Mr. Mathew Cruz, *VP/Branch Manager*	Dngeronger, Koror P.O. Box 338 Republic of Palau 96940 http://www.bankofguam.com	Tel. 488-2696 / 488-2697 Email: bog@palaunet.com Email: matthew.c.cruz@bankofguam.com
Bank of Hawaii	Hawaii	9/18/1961	Active	U.S. Federal Reserve	Mr. Richard Ziegler, *Branch Manager*	Medalaii, Koror P.O. Box 340 Republic of Palau 96940 http://www.boh.com	Tel. 488-2602 / 488-3285 Email: Richard.Ziegler@boh.com
BankPacific, Ltd.	Guam	7/28/1995	Active	U.S. FDIC	Mr. Joseph Koshiba, *Branch Manager*	Dngeronger, Koror P.O. Box 1000 Republic of Palau 96940 http://www.bankpacific.com	Tel. 488-5635 / 488-5226 Email: joek@bankpacific.com
Palau Construction Bank	Palau	7/28/1995	Active	FIC	Ms. Lucia Tellei, *General Manager*	Meyuns, Koror P.O. Box 7077 Republic of Palau 96940	Tel. 488-1946 / 488-5888 Email: pc.bank@palaunet.com
National Development Bank of Palau	Palau	2/24/1982	*conditional*	FIC	Mr. Harley Fletcher, *Acting President* Ms. Karla West, *Operations Manager*	Ngetkib, Airai P.O. Box Republic of Palau 96940	Tel. 587-2578 Email: hfletcher@ndbp.com, or kwest@ndbp.com