Finance in Africa: Addressing challenges in the 21st century

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I would like to dedicate this publication to the late Max Watson, founder and first Director of the Political Economy of Financial Markets programme."

Charles Enoch, Director, Political Economy of Financial Markets


CHAPTER 1

Introduction

Charles Enoch

In April and May 2018 the Political Economy of Financial Markets (PEFM) programme at St Antony’s College, Oxford hosted a two-stage conference on finance in Africa, the first at St Antony’s College and the second, co-hosted with the Global Strategy Forum and chaired by Lord Lothian, in the National Liberal Club in London.

Having studied the impact of the global financial crisis (GFC) on developed country economies, it was a natural step for PEFM to look at the impact on other regions. The impact on Africa has been significant, through several channels, resulting on the banking side in disintermediation from the global banking system as weakened banks from developed countries, including the United Kingdom, retrenched towards their homelands; also, low interest rates have driven investors to “search for yield” and enabled more borrowing by governments and companies in the continent, with results good and bad: infrastructure investment on the one hand, but also the accumulation of debt on the other. Development in Africa faces particular challenges: issues of the health of the population, of education, and being at the forefront in experiencing the effects of climate change. Demographic trends too cannot be ignored.

At a seminar at PEFM in late-2017 the latest forecast of the IMF’s World Economic Outlook was presented. A special study attached to the report looked at population projections, and estimated that the population of Africa would grow by over 1 billion people over the next thirty years. This is both a challenge and an opportunity not just for the continent but for the world as a whole, potentially providing markets and skills to complement those elsewhere. As Charles Goodhart remarked in his recent book, which provides a fairly gloomy assessment of prospects for the European economies, given declining birth rates and ageing populations, perhaps it will be India and Africa that come to the rescue.

The Oxford conference brought together UK academics, officials from Africa and the international financial institutions, and market practitioners. It began with a keynote address by Governor Njoroge of the Central Bank of Kenya, and was followed by three panels. These panels reflected the three elements identified in the sub-title of the conference. Governor Njoroge’s keynote address was so wide-ranging that a summary could cover this entire article (it is available in full on the PEFM website). He noted the challenges that African economies still have. 58% of the population do not have electricity; more than two thirds depend on agriculture; and 60% of the population are less than 25 years old. Half of all girls do not complete primary school. On the other side, Governor Njoroge provided examples of the considerable economic progress a number of African countries have achieved over the past decade. There have been big improvements in policies. Rwanda, which 10 years ago was ranked 137th in the world on the “doing business” indicator, is in 2018 ranked 4th. Kenya has increased access to financial services up to 75% of its population. Governor Njoroge quoted Nelson Mandela: something always appears impossible until it is done. Nevertheless, the efficacy of the financial system in helping Africa develop is questionable. Infrastructure needs, for instance, are immense, and returns would be high, but it is hard to get finance into those sectors. More generally, spreads do not reflect real risks; investors do not differentiate across countries that are miles apart and have a quite different economic base. There is also little differentiation within a country: it is hard for instance to get finance to small and medium sized enterprises: the massive

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increase in data that are now available should enable very detailed assessments of creditworthiness, but so far this is not happening. It is a big challenge, in Africa as well as worldwide, to balance the potential inherent in having large volumes of data with the challenges to privacy as such data are shared.

The first panel looked at banking issues. The panel was chaired by Rupert Thorne, Deputy Secretary General of the Financial Stability Board, the body tasked with making the world financial system safe. It recalled that one of the results of the GFC was that European and North American banks were weakened and retrenched towards their homelands. This left a vacuum which has resulted in the rapid growth of cross-border banking by African banks. The most extensive network that of Ecobank of Togo, extends to over 30 countries. Three Moroccan banks dominate the banking sectors of much of West Africa. South African, Nigerian and Kenyan banks too have expanded across the continent. This is bringing substantial benefits—innovation and management expertise, as well lending capacity and regional integration that can stimulate growth—but also challenges for supervisors, who may have limited information on banks’ activities beyond their borders and limited experience in cross-border supervisory collaboration, thus risking financial stability both locally and, in an increasingly interconnected continent and world, much more widely.

Dr Florence Dafe from the LSE examined the cross-border trends and highlighted some of the achievements and the risks. She focused in particular on Nigeria, and noted that the expansion of cross-border banking by Nigerian banks began as a result of the 20 fold increase in minimum capital imposed by the Nigerian central bank in 2005. Professor Emily Jones of Oxford reported on her DFID-sponsored project that provides case studies of countries’ compliance with emerging international standards and codes, particularly Basel capital standards, questioning whether these should have the highest priority in all cases, and examining where the pressure for compliance is coming from. Ethiopia, a rapidly-growing economy but with a different model from the mainstream, shows less interest in aiming to comply with international standards.

Ibrahim Yusuf of Dahabshiil, gave a practitioner’s perspective on the importance of financial flows in facilitating remittances, even into the most financially remote parts of the continent such as Somaliland. With de-risking causing traditional banks to withdraw, there is an increasing need for cash-based, and mobile-based, transfers, but also increasing challenges for the sector to demonstrate that it is compliant in particular with security-based requirements. Finally, for this panel, Barend Jansen of the World Bank, summarized the FSB’s recently promulgated Key Attributes of bank resolution—an important element for managing a banking system—and explained its applicability in Africa.

The panel on debt had the sub-title “this time is different?”—a largely rhetorical question, since the history of finance and financial crisis suggests that each time is different until it is not. The panel was chaired by Professor Christopher Adam of the University of Oxford, who observed that for several years there was widespread enthusiasm for Africa’s increasing access to finance, especially given its obvious infrastructure needs, but now the focus is on indebtedness and over borrowing. Does this mean that the borrowing upsurge has failed? Maxwell Opoku-Afari, Deputy Governor of the Bank of Ghana, chronicled Ghana’s entry into the international bond markets in 2007, and its subsequent borrowings, and how this related to strong and improving economic performance. In 2017 Ghana’s economy grew by 8.5%. Anne-Marie Gulde of the IMF noted that easy money had enabled improvements in infrastructure, but also led some African countries to rapidly build up debt to fill the gap provided by the debt write-downs early in the century. In some countries debt levels are already beyond critical levels that are considered sustainable. Differences across countries may be attributable to different levels of governance. In the Republic of Congo, for instance, public debt is now estimated at 117% of GDP, up from 70%, as a result of the uncovering of hidden debt. Five countries have debt in excess of 100% of GDP.
Stuart Culverhouse of Exotix described his firm’s investments into Africa, explaining what was attractive and why finance is moving into the continent. Search for yield, coupled with the financial freedom generated by debt-write downs and policy improvements in many countries, has generated the supply; evident needs have provided the demand. There was still appetite for investment into the continent, with increasing recognition of the need for differentiation across countries.

The last panel went beyond the narrowly financial elements, to examine some of the broader structural factors that will determine how successful African financial development is likely to be. It was chaired by Dr Simukai Chigudu of the University of Oxford, who quoted Zimbabwe’s handling of a cholera outbreak as an example of the interrelationship between health provision, politics and development. Dr David Johnson of the University of Oxford reported on his work in Sudan, relating state-by-state differences in educational achievement to differences in education strategies. Cyrus Rustomjee, now of the Centre for International Governance Innovation and formerly chief economist at the Commonwealth Secretariat, covered a number of innovative avenues for African development, including perhaps most interestingly the blue economy—i.e. the products in the seas, pointing out that 38 of Africa’s countries are coastal. Finally, Seth Terkper, former finance minister of Ghana, who had been directly involved in Ghana’s initial bond offering, stressed the rapid growth over the past decade of successful African countries, with the result that a number of these would no longer be eligible for concessional lending. Thus, financial markets become central to their future, and adaptation is necessary to ensure that they do not fall into the middle-income trap, whereby a country emerges up to a certain level but then is unable to complete the transition to developed economy.

All panels produced a lively debate in the subsequent question and answer sessions. The podcast of the Oxford conference is available on the PEFM website.

The session at the National Liberal Club began with a summarization of the Oxford conference by Charles Enoch, and then officials from the international agencies took the discussion forward. Antoinette Sayeh, formerly Minister of Finance in Liberia and Director of the African Department at the IMF addressed the issue of financial inclusion in Africa. She noted that access to traditional finance is low in Sub-Saharan Africa (SSA) compared to other regions, particularly in rural areas. In the face of this, the mobile banking is growing remarkably. Adult mobile banking account holders nearly doubled between 2014 and 2017 to reach 21% of the population, a far higher share than any other region. Six countries had more than 20% of the population with mobile accounts in 2014; by 2017 15 countries had reached this level, with growth expanding from its original East African base to all parts of the continent. Growth in microfinance too is remarkable, and like mobile banking has particularly benefitted women. Challenges remain, requiring appropriate regulation and supervision. Finally, Ms Sayeh turned to the emerging financial exclusion of Africa, deriving from “de-risking” by developed country banks responding to their home country authorities’ AML policies. Trade finance and other payments are under pressure as corresponding banking relations are cut, and African countries’ links to the global financial networks are under threat. Macro effects so far have been limited, but the inadvertent consequences of well-intentioned international regulations could have a significant long run negative impact on financial inclusion, and are an issue of major concern. Ms Sayeh concluded that the trilemma of the competing objectives of financial inclusion, financial stability and financial security pose difficult trade-offs that will be central to the engagement of Africa in the global financial system.

Samuel Maimbo, Head of Finance for Development at the World Bank, set out recent moves by the World Bank to enhance its efforts in Africa. He noted that access to long run financing was critical for human development, sustainability, inclusivity, and achieving the Sustainable Development Goals (SDGs) in Africa. He presented a range of data regarding trends in finance in

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2 As of February 2020 Deputy Managing Director of the IMF.
Africa, and surveyed a number of factors that explained why financing has proved challenging. He noted that solving the financing gap requires multiple actions and sustained efforts across the short term, medium term, and long term.

Finally, Sir Stephen O’Brien, former UN Under-Secretary for Humanitarian Affairs and Emergency Relief, outlined the work of the UN in providing assistance. He argued that one should not talk about “Africa”, since there are 55 countries, some very different from each other. They are experiencing a wide range of challenges: climate change, demographics, urbanization, lack of fair value for extractions, and narrowly concentrated wealth that in a number of cases stymies the growth of a wide, value-adding, ambitious, stabilizing middle class. The more successful African states are those that have stability and safety for the people, which in turn is frequently related to absence of conflict and good governance. He ended by observing that “we need to think very hard how to make an Agenda for Humanity and an agenda for people become an agenda for stability, for markets, for hope and for a future”.

Amongst the conclusions from the conferences: First, the African economy is important, well beyond Africa. If it were ever the case that it could be ignored, this is not so today. Finance has a critical role in fostering African development: there is plenty of room on the upside, but also downside risks and risks of contagion—through financial stress and indeed migration flows—if there is mismanagement and crisis. Secondly, Africa is changing too, integrating regionally partly as a response to global financial disintegration: the growth of cross-border banking by African banks and the ambitious free trade agreement of the African Union are but two of the signs. Thirdly, African economies can gain from the so-called “benefits of the late start”—i.e. there is no need to repeat the mistakes of those that have gone before. There is an understanding now for instance of the importance of consolidated and cross-border supervision, and of having powers and commitment to resolve failing institutions. Fourthly, African financial systems are innovative, and in some regards world-leading. The use of mobile banking in East Africa for instance is advanced, and has lessons for enhancing financial inclusiveness that are likely to be widely applicable. And the speed and efficiency of international transfers into Africa look impressive against the practices of more conventional banks. Fifthly, development does not occur through finance alone, but through a whole range of ancillary factors and policies: demography, health, education, and the impact of climate change will all be important. And sixthly, Africa is far from homogeneous. Governance factors will be critical in seeing which countries develop successfully and which do not. Some countries seem to be heading back into crisis, unless they change policies quickly; but others have been growing rapidly over a sustained period.

Finally, a short set of issues that emerged from the conference that warrant further study: First, is the financial system helping or failing Africa? Secondly, are the international financial standards appropriate for African financial systems, or could countries do better by prioritizing differently from advanced economies? Does it matter that African countries are barely represented on most of the standard-setting bodies? Thirdly, as Africa continues in the vanguard of moving into the digital age, how does one address the need to balance between data accessibility and data privacy, and strike a balance between financial inclusiveness and financial safety? Fourthly, how can one increase transparency between governments and their financiers, to avoid recurrence of hidden debt, and more generally use the financial system to improve governance where needed? And finally, as the more successful economies emerge from dependence on traditional aid flows and concessional borrowing, how does the increasing presence of new players—both public and private, including from China and India—complicate or facilitate their further development?
CHAPTER 2

Finance in Africa: Addressing challenges in the 21st century
Governor Patrick Njoroge’s keynote address

“Hello participants, colleagues and friends.

Good afternoon to you all.

It’s my pleasure to be here, and I want to express my profound gratitude to the organisers and Charles, in particular for inviting me to speak at this conference.

What Charles might not have known when he invited me is the special connection between myself, my countrymen and Oxford.

Oxford happens to be the home of [Sir] Roger [Bannister] and we all know him.

The first person to run the four-minute marathon. I was last in Oxford in June of 2016 for another conference, and the high point of that visit was my tea with Roger and his wife. So I enjoyed that very much.

So it wasn’t... ...it was a no-brainer really for me to say yes.

But as you know, he passed away last March and so this visit brings to me many memories of that occasion and indeed of his life.

So I want to thank the organisers as well for choosing a very relevant topic for our discussion today.

In my remarks, I’ll set out the highlights for some of the challenges that face all of us in the pursuit of leap forward in prosperity of our continent, Africa.

At the onset, I need to apologise that I’ll shorten my address a bit... ...remarks really, because I’m also fighting a cold which I picked up in Washington D.C.

It’s amazing how many things, how many flus come out of Washington D.C. Last time there was a bird flu, it was called the Global financial crisis. So this will only.....maybe it will go as far as Oxford and nowhere else.

And I want to start by outlining a few things, which are called the opportunities that we see in Africa.

In Africa, 58% of the population do not have electricity. Nearly two thirds of Africa’s population depend on agriculture. 60% of the population in sub-Saharan Africa and 37% of its workforce are youth under 25.

23% of the population in sub-Saharan Africa live on two to five dollars per day and in yet another statistic, 47% of Africa’s girls either do not complete high school or never attend at all. This by any means are dire numbers. And it may therefore appear surprising that I label them opportunities. But I want to emphasize that I see them as opportunities and I’ll explain why.

I want to underscore that actually, against these bleak statistics we’ve seen real change in particular areas. For instance, the macro-economic environment has strengthened by some magnitude. So against this sort of bleak background and numbers, we have seen some positive progress in particular areas.
First, the macro-economic environment has strengthened. For instance, inflation has declined across the continent. Current account deficits have contracted. Growth has strengthened largely due to stronger policy frameworks, improving price of primary commodities such as oil and also a very favourable external environment. That, I think has been clear over the last ten years. Actually, there has been remarkable progress. Another element would appear positively in this light is that in 2007, Rwanda was ranked 137 in the World Bank’s ease of doing business that is with respect to the ease of registering properties. And in 2018, it was ranked fourth in the world, so that’s a dramatic shift. A third element that is also positive, a pointer as it were in Kenya, access to formal financial services increased from 26% in 2007 to 75% in 2016. Again, a remarkable leap forward. So you can see that there are three in this specific areas, maybe ten years ago if we looked at the starting point, we would have said it is a hopeless case, it’s a lost cause. Ten years later, we have significant improvement in each one of these. It calls to mind the famous statement by among others Mandela, who said “It always appears impossible until it is done”. And I think we can go back to the three, to what I called the opportunities a moment ago and we could look at them in that same light and see that while these really are challenges, they are opportunities for us. And they will appear impossible until we get them done.

So now I want to go back to these opportunities. These numbers to me and to you. I want to convince you that they reveal huge gaps of what has to be in my view, the greatest mispricing of all. The worst misallocation of resources, and I will explain. We just mentioned that about half of African girls don’t go to high school. So, we could think of this as there’s a huge need for education for girls. And actually, the numbers for boys are a bit better but not that much better. Girls obviously are worse in this regard. Or you could think about electricity, we just talked about that. It means that there’s a huge need for it, so huge demand for it. So somehow, the private and social returns from investment in these areas – shouldn’t they be huge as well? And if you think like everything else – if you have a shortage of particular output or particular item, you’d expect that the marginal return on that is much higher and then eventually you’ll have diminishing returns and all those other things. So the question then is, why doesn’t the financial sector price and allocate resources appropriately to these areas that I mentioned? That is really the core of my question. This question allows me now to discuss the issue that is foremost in my mind in discussing opportunities and challenges in Africa, which is the failure of the financial markets in their use of information. That is key. That is what I see as the core of the problem that is before us. I will touch on this and other examples and expand on them, clarifying which I’m sure will be clarified later and expanded by others in the rest of the conference.

The first issue, if you may, is what I would call the problem that relates to the size of the risk premium or risk premia if you consider different projects. It can be argued that for instance, you think educating girls, or for that matter in the electricity sector putting up plants to generate electricity that is needed in a particular country and so forth. It could be argued that the risk premia for these projects are very large, that they overwhelm the positive returns for such investments. But this, I’m not sure. Let’s explore a little. The question here is whether we have a good yardstick for risk premia. So when you think about the risk premia that you assign to a particular investment, in education in Africa or for that matter electric generating plant in Africa, how do you assign the risk premia? And is it some sort of just let’s say a random number that you have assigned because of your sentiments in this way?

I just came back from Washington and last week we had the IMF/World Bank Spring Meetings and one of the questions that came up was the impact on the emerging markets and how the developing economies of the forthcoming normalization of monetary policy in advanced economies that we expect will happen is happening. So the question was, what is
the impact? And my answer when I was asked this question was that I actually started by recognizing that our markets or rather our investments that are in Eurobonds for instance, there’s a very large risk premium that is assigned to our Eurobond. So if you look at the yields, they are very large and most of that is actually risk. Somehow, they’ve beefed up, they’ve padded our yield with risk. Of course you cannot as I said, it’s difficult to explain how you’ve come up with that sort of number – you know the risk number, but it’s there. And that in my view is the question that we need to look at. If we cannot as practitioners come to grips with or explain to anybody why is it that we have such a risk premia for a particular investment, could be Eurobonds, we cannot explain to anybody how we have a particular risk premia on other projects...the ones that I mentioned a moment ago.

By the way, yesterday US Treasury yields broke 3% and for the first time in four years and in Kenya our benchmark, actually it’s a ten year bond, is trading at 6.8% and actually this is from a peak from 7.2% in February. We have another ten year bond that mature in 2024 which when it was issued, was at 6.7% in June of 2014. The yield went up to 9.1% at end 2015 and it’s trading currently at 6%. So you can see swings of as much as 3% from already substantial starting points of 6.7%. My point is, this is something that we need to understand better and I’m sure that those that will come after me can discuss this and explain why we have such large risk premia and what is it we need to do for the markets to correctly price risk. The concern could be risk, but could also be the thin markets that we’re trading in. So all these things need to be dealt with and isn’t just the project that is a problem. So, that is one thing that I wanted to bring on the table. But there’s a related item which I think you should also be concerned about. Again, discussing risk. A few years ago when interest rates went low in the market, they came down dramatically and there was a sort of excitement in Africa, that we could borrow Eurobonds. We could even issue Eurobonds. One of the reasons behind this some people explained, is that actually it will be good for African countries to issue Eurobonds. Why? Because the pricing of these Eurobonds will serve as a disciplining effect on the African countries. So in as much as your bonds are being priced appropriately by the market, it will punish you. And you’re getting correct information. The financial markets are getting correct information data and they’re using this to in effect punish the underperformers and reward the ones that are doing well. So we’ve come forward a few years, maybe five or six years since then but the point though is that is that it didn’t work that way. Judging by the panic that was there in Washington last week, relating to a rapid build-up of debt in Africa and other countries, somehow we can say that, that mechanism never worked. It could very well be that there were no data that were provided to the markets, but they should have asked for more data. So there’s something wrong with the mechanism and there’s something wrong with the way the financial system is working, consequently we do have a real problem with the way the markets are pricing risk and in particular for those crucial investments I mentioned a moment ago. There’s a prerogative to this and I will mention it and then move on. This is the issue of differentiating country risks and prospects. What appears to me is that at times we are all countries in Africa or a bunch of countries in Africa, could be the West African countries, could be the East African countries, could be the Southern African countries or the Central African countries we are lumped into the same pool and consequently investors put money in our investments and from their perspective, they don’t distinguish Kenya from Uganda or from Tanzania. As a matter of fact, they probably don’t distinguish Kenya from Ghana because both of them are English speaking countries and there’s only one problem, they’re several thousands of miles apart and they’ve completely different economic structures. One exports gold and cocoa the other has nothing to export except coffee and tea. So, the point about differentiating countries and doing the homework to make sure that we’re not pooling several geographies together, but rather we
are pricing the risk of each particular country is something that I think we need to think a bit more often and also maybe discuss later in the conference.

I want to move onto other things, another big area that I would want to discuss and this relates to a set of issues that relate to one of the bright spots in Africa, which is Fintech and technology more generally that have opened doors that were never before imagined. As was mentioned before by Charles a moment ago, Mpesa is now a complete ecosystem with P-to-P and P-to-B transfers and it has really transformed many lives. We can discuss some of the specifics as to how that has transformed lives, but there are many stories, there’s a lot of work that is going on to understand better how to even expand this phenomenon in Africa and the rest of the world. But before we get into the specifics, I have a pet peeve that I have to deal with. And this is I don’t understand why the Fintech gurus call themselves “disruptor”. I don’t understand that. I think of disruption as sort of impeding forward progress, impeding forward motion or progress towards an objective, and as far as I know, when Mpesa and other digital financial services came into being, they did challenge the brick and motor model of banking that was present then. But I didn’t see them as disrupting banks in terms of the banks’ objectives and indeed the customers’ objectives. Unless of course the disruptors would have us believe that the banks’ objective was inherently anti-technology. So, they’re sort of luddites. And therefore from their perspective they’re disrupting the luddites. So, in a sense, in terms of the substance, there has been progress made. A lot of progress as I mentioned which has allowed banking services to do two things:

First, to break the location and timing of transactions with the brick and mortar model. That’s really what has happened. So you can actually make a transfer from the comfort of your own kitchen or from the comfort of your own office. I mean right here I can make a transfer to my mother from my bank to MPesa or in a different setting I can actually buy Treasury Bills of our Government today, from my phone. So it has opened a whole new vehicle but separating the location and timing of the transaction with the very rigid location and timing that is imposed by the brick and mortar model that we know in commercial banks. The other thing it has done is to reduce the minimum size of transfers. So you can actually now transfer very little amount without going to the bank. I wouldn’t go to the bank to make a transfer for twenty shillings or twenty dollars, but I can do that on the mobile digital financial platform. For as little as USD30 you can buy government securities. In the past, the minimum amount was USD1000. So you can see the minimum number of the threshold has come down dramatically.

Those in my mind are the two fundamental things that have happened with MPesa and the other ecosystem. But from my perspective, that is only one thing that relates to the module as we know it in banking. And I want to argue that this really has helped operational efficiency of banks. So the only thing that has happened to us in terms of the new digital financial services is to actually challenge and to push banks to be more operationally efficient. That is good but that’s not everything.

In the rest of the talk, I’ll cover some other areas where I think we’re still lagging behind and it relates to the use of information which again is my principal point in this talk. So we have not made significant breakthroughs in allocating resources to greater returns. Remember that I mentioned a moment ago that there are various projects that could be there. For instance, think of the SME’s that have huge returns, only that maybe the practitioner or the owner of the SME does not have the know-how to put together the balance sheet or financial records in a particular way and then make an argument before a bank. SME’s require the use of detailed information about the customer, about the customers’ transactions and about the customers’ relations with others. Something that we have not quite begun to address. So, for instance in my transactions on MPesa there’s a record of all the transactions I did with all my
counterparts and as an SME you can see when I’m getting paid and by whom. That is in itself very valuable information. And today, we have not had a good model that deals with that. If there’s a one thousand dollar question, that is the one thousand dollar question. I would want a Fintech that would come up and actually do justice to the information that is now available. Please don’t sell it to Cambridge Analytica. Use it for the benefit of SME’s because it gives very good data that can be used in terms of working with that institution. That, then, will allow us to provide resources to the areas where there’s the highest return. So in a sense you begin addressing the allocational efficiency that I mentioned at the beginning. So, providing the resources to the area’s investments where there’s greatest returns. So that’s one area we need to do some work in.

Then there’s another area also relating to information. We have not made strides in intermediating savings. I’m talking of transforming short-term deposits into long-term loans. Of course we have an example I gave you a moment ago, the one of M-Akiba, where you can buy government securities and therefore you can see that as a new savings vehicle. And frankly from our perspective, we believe that this will transform savings as we know it in Kenya, because it’ll open a huge new vehicle for savings. It’s available to people who are in the five dollar a day wage. So you can see if you earn five dollars a day, you can save one dollar a day every day and at the end of the month you can buy thirty dollars’ worth of Treasury Bills, which is your savings. By the way, I have to tell you that it’s not just a one-way street. It’s also important for you to have a liquid pool such that when the investor, in this case that person that earns five dollars a day, when he or she needs to liquidate his or her savings, they can do it at a moment’s notice, anytime 24/7, basically. So there’s also some work that needs to be done in the background that has also been figured out and is available. In any event, the point we’re making here is that this is just a start and there has to be more work that goes towards this intermediation efficiency. An area that also requires a lot of information and this again is something that we hope can be done for the benefit of our African countries.

There’s a third element, and again also concerning information. In a regular brick and mortar bank, you build a relationship with it through your interaction, just like the drug store or the pharmacy or the airlines. You get into a relationship with your airline and they give you bonus miles or frequent flyer miles. But if you’re dealing with an institution that is on your phone and that institution could very well be a bank or it could be backed by a bank and your relationship is via recorded voicemail, you feel from the perspective of the customer, that there’s something that is different, meaning the customer cannot distinguish whether this Fintech is a ponzi game or it’s a real deal. The recorded voice message is a human being who is representing the institution but could be in the Philippines. And the point for us is the same as for things relating to the financial sector there’s what we may call a trust threshold. So a minimum level of trust that you will need to engage with a particular institution. And you don’t get a chance to build that trust with your favourite Fintech. You get to build that trust with your brick and mortar bank when you go there and meet the customer relations person and they offer you tea and they ask you how the weather is…….I mean you’re building a relationship with them. My point in all this is that the Fintechs that we have been working with, they have been atrocious in building this relationship and actually ensuring that they meet the trust threshold that is necessary. The issue of trust comes to the fore particularly when there’s a problem, or for that matter the problem could be with the customer or could be with the institution itself. Quite often it’s with the customer and there’s no customer management system that makes sense to the customer. And so there’s a substantial loss of trust which as you can imagine, can even cause a bank run. The way banks operate nowadays, there are no lines or queues forming outside the banks and instead you have people using their phones and that’s how the runs take place. So, a bank could go from being
liquid to being completely out of money in a matter of hours just because people transacted quickly on their mobile phones. I also know that the distributed ledger technology pundits obviously claim that there is a new world order, which will replace the trust as we know it with something else. Well, we can discuss that when we have the first use case of it, so I’ll leave that for now. I should say that there’s a lot of merit in the distributed ledger technologies and we’re looking forward to seeing as a matter of fact in Kenya, we’re already looking at four specific applications, so we’re working on that. But it’s not as easy as some people claim it to be, so let’s wait and we’ll get there.

Colleagues, I’ll finish now and what I wanted to highlight and what I hope I’ve highlighted is what I consider the Achilles hill of our current financial system which is the poor use of information that is provided to ourselves or we provide about ourselves.

Honestly, the dire statistics that I mentioned before at the beginning will continue to challenge us and other practitioners until the financial system can find ways to use information in the ways I explained above, addressing those key questions that I put forward. This is a task for each of us particularly those in this conference.

And I want to end with a quote from Sir Roger “However ordinary each of us may seem, we are all in some way special and can do things that are extraordinary, perhaps until then, even thought impossible.

Thanks for your attention.”
The rise of cross-border banking and the transformation of African economies: Evidence and knowledge gaps

Florence Dafe

In recent years, the rise of cross-border banking in Africa has received significant attention by scholars and policymakers. In particular, academic and policy debates have questioned the extent to which regional banks operating cross-border, so-called pan-African banks (PABs), are contributing to the economic transformation of African countries. While PABs have undoubtedly not brought about the transformation of African economies, they have reshaped the financial landscape in Africa, raised the efficiency of financial sectors and brought about new challenges for the ability of African regulators to govern finance. There remain, however, many unanswered questions about the consequences of the rise of PABs.

This essay reviews the empirical and theoretical evidence in support of these claims, with a special consideration of the case of Nigeria, which is a home to some major PABs. The essay begins with a brief overview over the drivers of cross-border banking in Africa before turning to the theoretical costs and benefits of cross-border banking. Then it explores the consequences of PABs. In reviewing the evidence, the essay addresses three broad questions, namely: How does cross-border banking affect the mobilisation of funds for the real economy? How does cross-border banking affect regulators’ ability to maintain stable financial systems? How does cross-border banking affect regulators’ space for policies that may support economic transformation? The conclusion proposes an agenda for future research on PABs.

The rise of PABs

Cross-border banking has long been an important feature of financial sectors in Africa. The share of foreign banks has further increased in the 2000s and reached 52% in 2009 (Claessens and Horen, 2014: 302). There is, however, significant variation in the ownership of foreign banks in Africa. For instance, in 2013, the share of foreign-owned banks is 99% in Zambia and 28% in Nigeria (World Bank, 2017). A similar picture of cross-country variation in foreign ownership emerges when the focus is on the share of foreign banking sector assets, as Figure 1 shows. The only region where this share is higher is Central and Eastern Europe. An important development in the 2000s is the diversification of the foreign bank population in Africa. While before the 2000s international banks from Europe and the US dominated African banking sectors, these banks now face competition from banks from emerging countries like India and China and, importantly, from PABs.
The number of PABs has increased significantly over the past decade. As Figures 2 shows, PABs began to expand especially after 2010. Most PABs come from Kenya, Morocco, Nigeria, South Africa and, headquartering Ecobank which has by far the largest number of subsidiaries in Africa, the West African Economic and Monetary Union (WAEMU). The rise of PABs is not only significant because of the large number of subsidiaries but also because of the deposits PABs hold, as Figure 3 shows. In many countries PABs hold a share of deposits which exceeds 30 % and can therefore be considered systemically important.
What explains the expansion of African banks across the region? The existing literature highlights several reasons. One is the (perceived) declining profit opportunities in home economies, especially relative to opportunities in potential host markets (Beck et al., 2014: 50). In Kenya, for instance, the financial market has become more competitive and government borrowing from domestic banks declined in the 2000s. Thus, banks had to move away from lending to the government and prime borrowers towards the riskier business of lending to lower income households, small and medium enterprises (SMEs) and the agricultural sector. As a result, some banks considered profit opportunities in other African countries, where financial sectors tend to be less well developed, favourable.

The literature also highlights the ambition of banks to become pan-African or of regulators to create PABs as reasons for the expansion of African banks across borders (Alade, 2014). In Nigeria, for instance, the Central Bank of Nigeria (CBN) supported the expansion of Nigerian banks to create regionally competitive players, gain international recognition and mobilise international capital for development at home (Soludo, 2004). Specifically, Charles Soludo, the CBN governor argued: “(…) I can visualize the Nigerian and world economy in the year 2025 and 2050. What I see is a world economy with no more than 10-20 mega-banks all over the world. (…) Where is Nigeria (…)? (…) the Nigerian banking system remains very marginal relative to its potentials and in comparison to other countries—even in Africa. We have a duty to be proactive, and to strategically position Nigerian banks to be active players and not spectators in the emerging world.” (Soludo, 2004: 4) To encourage the regional expansion of Nigerian banks, the CBN increased the minimum capital requirements from N1 billion for existing banks (2 billion for new banks) to N25 billion in 2005. Banks had to resort to mergers and acquisitions to meet the revised minimum capital requirements. Subsequently, the search for yield, notably due to the large amount of “excess capital” available in Nigeria’s domestic banking system, drove Nigerian banks’ expansion in the regions. As Table 1 shows the strategy worked and several Nigerian banks established subsidiaries in other African countries.
Moreover, as Figure 4 shows, in several countries Nigerian banks played a systemically important role as indicated by their control of a large share of deposits.

Table 1: Presence of Nigerian banks in the region. Source: Based on data drawn from Beck et al. (2014)

<table>
<thead>
<tr>
<th>Name of the Bank</th>
<th>Number of African countries with presence</th>
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<tbody>
<tr>
<td>United Bank for Africa (UBA)</td>
<td>19</td>
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<tr>
<td>Access Bank</td>
<td>9</td>
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<td>Guarantee Trust Bank</td>
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<td>Diamond Bank</td>
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<td>Skye Bank</td>
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<td>Zenith Bank</td>
<td>4</td>
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<td>Union Bank</td>
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Figure 4: Share of deposits selected Nigerian banks held abroad in 2013 (%). Source: IMF (2017: 28)

While Pan-African ambition and perceived decline in profit opportunities in the home country compared to potential host countries highlight some of the motivations of key players, they have difficulties to explain the timing of the expansion. Three factors seem to be particularly important. First, during the 2000s the macroeconomic environment, including inflation, improved in many African countries. An improved macroeconomic environment in potential host countries made it more attractive for African banks to expand in the region and contributed to increased trade and investment among African countries, offering opportunities for banks to
follow their customers abroad. A second important factor seems to be financial liberalization in the region, which allowed African banks to enter new markets in the region and promised fewer restrictions on their activities. Finally, the global financial crisis reduced the willingness of traditional Western banks after 2008 to expand further in the region, opening up space for African banks willing to expand (Beck et al., 2014: 54).

The consequences of the rise of PABs

Once scholars and policymakers recognised the rise of PABs, they began to question the extent to which PABs would contribute to the economic transformation of African countries. In theory, cross-border banking of regional banks may have both costs and benefits.

The advanced technology and managerial skills that tend to characterise banks that expand abroad may increase the efficiency of the banking sector in host countries, the availability of innovative banking products and the demand for high-skilled/educated workers, many of which are unemployed in African countries. The risk of a greater presence of banks with advanced technology and managerial skills is, however, that new products may be difficult to regulate and supervise by financial authorities in the host countries and that the associated greater competition may increase risks for financial stability when banks seek to maintain their profitability by engaging in more risky activities.

Another important concern is the effect of the entry of PABs on the availability of financing for the real economy. On the one hand, the entry of banks may reduce the interest rate spread by increasing competition. On the other hand, effects on the financing of the real economy may be negative when new banks displace a local banking industry which is particularly well placed to serve key economic sectors like agriculture. This is because domestic banks tend to rely more on soft information about borrowers as a consequence of relationship banking than foreign banks, which tend to rely on hard information, which more opaque but from a developmental perspective important borrowers like SMEs find more difficult to provide. Relatedly, there is a risk that foreign banks focus on affluent clients (“cherry-picking”). Foreign banks may be more attractive to these clients compared to smaller, domestic banks because of their international presence and advanced management and technology. In addition, foreign banks may seek out affluent clients because they are less opaque and deemed more creditworthy.

A third major consideration in assessing the consequences of the rise of PABs are the effects on financial stability. In theory, the entry of PABs may have positive effects on financial stability because foreign-owned banks may import higher regulatory standards, for instance because they tend to come from advanced economies which tend to have more stringent regulatory regimes in place. PABs may also have positive effects on financial stability because they tend to have advanced risk management skills. In addition, foreign bank entry may help to mitigate the impact of domestic shocks to the extent that foreign banks are able to mobilise capital from home countries which are unaffected by the shock. From a theoretical perspective, foreign banks may, however, also increase risks for financial stability by providing a transmission mechanism for shocks from home countries, a dynamic referred to as financial contagion.

Having established that the effects of cross-border banking are ambiguous from a theoretical perspective, the question arises what the empirical evidence for the effects is. Unfortunately, there is little empirical research on the effects of PABs on economic transformation in Africa. In addressing the question about the effects of cross-border banking the essay will therefore

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3 The effect of the financial crisis was not uniform across African banks. Some banks like Nigeria’s Access Bank and United Bank for Africa (UBA) scaled down their expansion plans in the wake of the global financial crisis (Lukonga and Chung, 2010).
present a combination of insights from the existing literature on the effects of foreign bank entry and of PABs as well as insights from Nigeria. Nigeria makes an interesting case because it sheds light on the effects of banking sector expansion in home and host-countries.

The next sections will address three issues which are of major interests for political economists interested in the expansion of cross-border banks because they relate preconditions for an economic transformation as established in the literature on industrial policy (Woo, 1991; Chang, 1998; Wade, 2003; Thurbon, 2016), namely: the effects of cross-border banking on the mobilisation of funds for the real economy, the effects of cross-border banking on financial stability and the effects of cross-border banking on policy autonomy.

Cross-border banking and the financing of the real economy

The short answer to the question how cross-border banking affects the access to finance of the productive sectors is: It depends. Existing research, which usually focuses on developed and developing countries outside Africa, has found that the effect of foreign bank entry on access to financial services varies across countries and regions, with institutional characteristics as well as with the type of bank. While some studies report that a higher share of foreign banks is associated with lower access to credit for the private sector (Detragiache et al., 2008) others fail to confirm this finding (Cull and Martinez Peria, 2010). Especially in countries where contractual and informational frameworks are weak, as is likely to be the case in many African countries and low income countries in general, the effect of foreign banks on the provision of credit seems to be lower compared to domestic banks or even negative (Claessens and Horen, 2014). In addition, there is evidence that foreign banks reduced their lending earlier and faster than domestic banks during the global financial crisis (Claessens and Horen, 2014; de Haas and van Lelyveld, 2014). Moreover, extant research provides evidence for cherry-picking by foreign banks (Beck and Martinez Peria, 2010; Beck and Brown, 2015).

There is only a dearth of research on the effect of foreign banks in the African context. Considering PABs specifically there is some evidence suggesting that these banks may have positive effects on firm access to financial services. Specifically, Leon (2016) finds that competition in the banking sectors of WEAMU countries increased in the time period during which the presence of PABs in these countries increased. While the study only explores a correlation not a causal relationship, future work building on this study and interested in the effects of PABs on access to finance for the real economy could explore whether there is a causal relationship between an increased PAB presence and competition by giving more consideration to omitted variable bias and by exploring whether competition has been associated with declining costs of finance. In addition, there is case study and anecdotal evidence that PABs have increased the branch network in host countries and introduced new products (see for instance Clarke et al., 2009). What is less clear in the extant literature, is whether the PABs have also expanded access to finance.

Beck’s study of the effect of cross-border banking on access to finance in SSA is a notable exception (Beck, 2015). He provides suggestive evidence of a positive relationship between the share of foreign banks from the region or other emerging markets and firms’ access to finance and of a negative relationship between the share of foreign banks from Europe or the USA and firm finance. While the results of Beck’s regression analysis cannot be interpreted in a causal manner, given their cross-sectional nature and potential omitted variables, they do underline the need to distinguish between different types of foreign banks in examining the effects of cross-border banking.

Overall, studies of the effect of cross-border banking remain hampered by data availability. There is a lack of evidence on whether PABs have improved access to credit for those segments which are considered a priority for an economic transformation such as SMEs, agriculture and industry
but lack adequate access. Moreover, we know little about the effects of cross-border banking on the availability of financing for the real economy in home countries.

The Nigerian case suggests that the effects of cross-border banking on the availability of financing for the real economy in home countries may be significant. As explained above, Nigerian regulators encouraged the expansion of Nigerian banks in the region by tremendously increasing the minimum capital requirement for banks. An important consequence was an increase in unproductive investment. While liquidity in the banking sectors increased, the economy was not able to absorb of the excess liquidity, which was further fueled by a high level of oil revenues. Banks provided credit but, as former CBN governor Lamido Sanusi found, “credit was going to the capital markets; it was going into commodity speculation” (FT, 2009a). Thus, higher capital resulted in significant flows to non-priority sectors and to the capital markets, mostly in the form of margin loans and proprietary trading camouflaged as loans.

Cross-border banking may also have an effect on real economy financing in home countries when it increases an export of capital. While Soludo (2004) envisaged that Nigerian banks would after the increase in minimum capital requirements become international players that are able to raise capital abroad, Nigerian parent companies contributed to the host countries’ banking systems by raising capital outside As Sarah Alade (2014: 86), a deputy governor of the CBN explains, “the expansion of Nigerian banks has so far been funded by raising capital from the Nigerian market, and the model of expansion suggests that Nigerian shareholders have funded the expansion of the banks.”

**Cross-border banking and financial stability**

“Nigerian banks are entering the market and it scares me because they are not well regulated”, was the answer of a central banker from the Bank of Uganda when I asked him in an interview whether he welcomed the entry of Nigerian banks in Uganda (Interview, Kampala, 25 November 2010). While there is little empirical evidence that Nigerian banks have posed a risk to financial stability in Uganda, the literature on cross-border banking suggests that there is no room for complacency. While the systematic analysis of the effects of PABs on financial stability constitutes a gap in the literature, there is a considerable body of work focusing on other regions than Africa suggesting that cross-border banking poses significant risks for financial stability.

A major insight from the existing literature is that cross-border banking can help mitigate the impact of local real sector shocks, but exacerbate global financial shocks. In particular, there is evidence that foreign banks are a stabilizing force in terms of credit supply during host country crises (de Haas and van Lelyveld, 2006; de Haas and van Lelyveld, 2010). For example, studies of the Tequila and Brazilian crises of the 1990s have shown that foreign banks did not pull back from host countries such as Argentina, Brazil and Mexico in the face of the crises, but rather viewed these episodes as opportunities to become more firmly rooted in these economies (Peek and Rosengren, 2000; Crystal et al., 2002). The situation is, however, different when home countries are affected by crisis. Popov and Udell (2012) for instance find that both positive and negative shocks to the balance sheets of foreign banks were transmitted from banks to firms in Central and Eastern Europe, affecting firms’ credit access. In addition, there is evidence that, historically, foreign banks have tended to cut and run in crises, repatriating capital and liquidity to their home markets and abandoning their clients in host countries (Roubini and Setser, 2004). One reason may be that banks may need to shore up capital and/or liquidity positions in their home markets to meet regulatory requirements. Accordingly, Wade (2007: 84) argues: “No country should let its banking system be taken over by foreign banks—even though in developing countries western banks are likely to be more ‘efficient’ than domestic ones—for at times of crisis banks rely heavily on their home state and are likely to sacrifice operations in developing countries in order to protect their home base.” That said, Epstein (2014b) argues, in a study of the
behaviour of foreign banks in central and eastern Europe during the global financial crisis that whether foreign banks ‘cut and run’ in a crisis depends on their business model and whether they expand operations through subsidiaries. Epstein finds that subsidiaries provided a relatively stable funding channel because foreign bank investors in the region had overwhelmingly expanded via subsidiaries rather than branches, were therefore subject to host country regulations, had long time horizons, high toleration for volatility and were pursuing a mass-marketing strategy in host economies (as opposed to just funding corporations from their home markets). In sum, foreign banks considered their Central and Eastern European host countries as a ‘second home’.

While there is little systematic analysis of the behaviour of PABs during crises in host and home countries, there are at least two reasons for concern. First, the financial sectors of home countries of some PABs are fragile. The fragility is often rooted in the vulnerability to changes in commodity prices arising from limited economic diversification. An important example is Nigeria’s banking sector, which has experienced severe financial distress between 2014 and 2018 due to an economic crisis arising from the decline in oil revenues. In fact, in 2017, four out of 22 Nigerian banks were officially undercapitalised, one of which is internationally active. A second reason for concern is that it is not clear whether PABs, which largely expanded as subsidiaries, consider their host countries indeed as a second home. Nigerian banks, for instance, are reconsidering cross-border strategies have sold subsidiaries in recent years, as shown in Table 2. This is because it turned out that subsidiaries’ activities were less profitable than envisaged and they incurred losses. Lower than expected profitability of cross-border expansion and the relatively short presence of PABs in many African countries raises doubts about the ability and willingness of PABs to provide stable funding channels in times of crises.

Table 2: Decline in the number of subsidiaries of Nigerian banks. Source: The author, based on data from Beck et al. (2014) and from banks’ websites and annual reports.

<table>
<thead>
<tr>
<th>Name of the Bank</th>
<th>Number of African countries 2014</th>
<th>Number of African countries 2018</th>
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<tbody>
<tr>
<td>United Bank for Africa (UBA)</td>
<td>19</td>
<td>18</td>
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<td>Access Bank</td>
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<td>Guarantee Trust Bank</td>
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<td>First Bank of Nigeria</td>
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<td>Diamond Bank</td>
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<td>Keystone Bank Group</td>
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<td>Zenith Bank</td>
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<td>Union Bank</td>
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Existing research also highlights the role of regulatory frameworks. While it is likely that banks that are well regulated in home countries are less likely to experience financial distress at home and thus feel pressure to cut and run, stringent regulation in home countries might come at a cost in host countries. Ongena et al. (2013) find that home-country regulation which reduces banks’ profitability in their primary domestic market, such as lower barriers to entry, tighter restrictions on bank activities, and higher minimum capital requirements, leads banks to loosen their lending standards and take on more risk abroad to make up for profit lost at home.
An arguably more important consideration in the African context with respect to regulation are arrangements for cross-border cooperation in regulation. There are three main instruments in Africa and other regions to reduce the risks of cross-border banking for financial stability and the costs of potential crises. First, consolidated supervision, which entails the supervision of banking, financial or mixed groups that include at least one bank at the group level, rather than supervision of individual banks. Second, Memoranda of Understanding (MoUs), which are legally non-binding declarations of intent to cooperate on certain issues and typically established between supervisory authorities. Third, Colleges of Supervisors, multilateral working groups of relevant supervisors that are formed to enhance consolidated supervision of an internationally active banking group on an ongoing basis. Studies on cross-border banking supervision in advanced economies before the global financial crisis find that these three types of pre-crisis arrangements for cross-border cooperation did not constitute an adequate basis for crisis management because they failed address the asymmetric interests of home and host country supervisors, had limited legal value and did not address the main – legal and political – challenge that supervisors represent primarily the interests of domestic stakeholders (D’Hulster, 2011; Beck, 2016; Beck and Wagner, 2016). Thus, while consolidated supervision, MoUs and Colleges of Supervisors may be necessary, they are far from sufficient for effectively reducing risks for financial stability.

The inefficiencies in arrangements for cross-border cooperation in regulation and supervision may be compounded by at least four additional challenges in Africa. First, some PABs have complex and opaque holding structures and cover a broad range of financial activities (Lukonga and Chung, 2010), rendering cross-border regulation and supervision, which already demands a high level of human resources, even more challenging. Second, capacities of many African supervisors are already overstretched with supervising domestic banks. In Nigeria for instance, supervisors must complement off-site with on-site supervision to verify the data provided by banks, requiring significant capacity. Second, many African countries lack strong frameworks for bank resolution, rendering it difficult to establish ex-ante agreements on resolution and burden sharing on a supranational basis. Third, across African countries, there is a large variation in regulatory capacity and standards. Specifically, there is a large divergence in the employment of consolidated supervision and in reporting standards, rendering the cross-border exchange of information difficult. At the same time, the countries with PAB presence have very heterogeneous economic, political and financial systems, requiring regulators to ‘go slow’ on regulatory convergence and consider national particularities. Fourth, enforcement of domestic regulation is often weak even though domestic prudential regulation is sometimes less demanding than international standards (Enoch et al., 2015: 36). The CBN, for instance, exercised regulatory forbearance in response to banking sector distress in 2016/2017 (IMF, 2017). Regulatory forbearance is likely to reduce the effectiveness of cross-border banking supervision as well.

To sum up, existing arrangements for cross-border cooperation in regulation and supervision are at a nascent stage in Africa and require considerable strengthening to be effective in a context where home countries’ financial sectors are vulnerable and there is a risk that banks ‘cut and run’ in the face of a crisis. Much of the existing research focuses, however, on developed and emerging countries and it is questionable to what extent its findings hold in the African context where supervisory capacity and independence may be lower. Moreover, findings on the behaviour of banks in times of crisis might not travel well to the African context because PABs find it more difficult to cut and run because of restrictions on capital mobility

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4 For a detailed discussion of these mechanisms see Beck (2016).
and because there are few countries in the region which may be considered ‘safe havens’ in times of crisis.

**Cross-border banking and policy space**

The rise of cross-border banking in Africa is likely to have implications for the capacity of states to govern their financial sectors in line with their priorities, rather than the priorities of international financial institutions, thereby affecting governments’ policy space. The last section will highlight two main ways in which the rise of PABs may affect policy autonomy. First, by allowing foreign banks, which are likely to be less ‘patient’ than domestic banks, to enter jurisdictions. Second, by exerting pressure for convergence with international banking standards.

There is a significant body of literature on the political economy of finance which has examined how financial institutions may, due to their ability to relocate much needed capital to other jurisdictions, reduce the policy autonomy of governments by creating strong pressures on governments to create a policy environment that reflects the interests of financial institutions. As outlined above, there is evidence from developed and emerging countries that foreign banks ‘cut and run’ in times of crisis when they do not consider the host country a second home and do not have a long-time horizon. Conversely, extant research has shown for emerging countries that investors with limited ability to exit a market, notably domestic banks tend to be more patient, continuing for instance to lend to the government in times of crisis because of a higher debt-tolerance (Hardie, 2011). But even in less extreme situations than economic crisis, for instance when policy environments are deteriorating from the perspective of mobile investors due to dynamics such as rising inflation, budget deficits or efforts to restrict capital mobility, mobile investors, such as internationally oriented banks are able to exert pressures on governments to adopt more favourable policies by threatening to ‘exit’ (Maxfield, 1990; Mosley, 2005).

Given the importance of patient capital, that does not leave as soon as the policy environment becomes less favourable, to mobilise financing for an economic transformation, it is not surprising that in both developed and developing countries targeted political intervention to protect domestic ownership in developed countries has been common. In 2011, for instance, Mario prevented as governor of the Italian central bank the sale of UniCredit’s asset management arm to British or French interests because he feared that too much foreign ownership would dampen the market for Italian government debt (Epstein, 2014a: 778). Emerging countries like China have also protected domestic ownership in the banking sector and justified it as serving developmental purposes. While several African countries have a similar, often unofficial policy to protect domestic ownership, for instance Nigeria (FT, 2009b), there is a lack of research on the motivations of such policies and effectiveness in creating a loyal investor base.

A second way in which cross-border banking may affect policy space is by exerting pressure for convergence with international banking standards. Jones and Zeitz (2017) find in a study of Basel standard adoption in countries which are not members of the Basel Committee on Banking Supervision, so-called standard-takers, that countries are likely to pursue relatively high levels of Basel II and III implementation when large foreign and internationally active domestic banks operate in their jurisdiction. This finding is notable because experts have questioned the extent to which Basel II and III standards are appropriate for countries which have weakly developed banking sectors and noted that the adoption of these standards, especially Basel II, may increase the costs of lending to more opaque borrowers like SMEs and

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long-term lending, thus involving developmental costs (Gottschalk and Griffith-Jones, 2006; Fuchs et al., 2012; Jones, 2014).

Why might the rise of PABs encourage the adoption of global banking standards? One reason is that foreign banks operating as subsidiaries in non-member countries, which are subject to host-regulation, are likely to advocate for the implementation of Basel standards when they already comply with Basel standards at home because they can derive competitive benefits from their adoption by host regulators in jurisdictions where competitor banks will struggle to meet the costs associated with compliance (Gottschalk and Griffith-Jones, 2006; Kern et al., 2006). There is evidence that local private banks that were keen to expand into the region supported the adoption of international standards in Kenya (Upadhyaya, 2017) and Nigeria (Dafe, 2017). Another, related reason is that regulators may also implement Basel standards to help domestic banks expand abroad, as has been the case in in Kenya (Upadhyaya, 2017) and Nigeria (Dafe, 2017).

While cross-border banking exerts pressure to adopt global banking standards, the adoption of such standards makes it more difficult to use the banking sector to pursue political goals, such as providing financing to political supporters or channelling subsidised credit to development priority sectors. African regulators have not been passive in the face of this restriction of their policy space. Their response to preserve policy space has often been mock compliance, the adoption of standards on paper and relatively hidden divergence from them in practice, notably through regulatory forbearance as Engebretsen and Soares de Oliveira (2017) for Angola and Dafe (2017) for Nigeria show. Preserving policy space through mock-compliance might however come at a cost, namely increased risks to financial stability.

**Conclusion**

This paper has examined the rise of cross-border banking in Africa. The rise of PABs clearly illustrates that regulators face new dilemmas: While the rise of PABs may enhance the efficiency of banking sectors it creates new conflicts and costs for regulators. There seems to be a high value of a ‘mix and match’ strategy. Such a strategy implies having mixed banking systems, consisting of domestic and foreign, public and private banks, and a strategic use of the licensing process to welcome banks that have a track record of developing products and serving the segments that play a key role in economic transformation.

Even though PABs have become systemically important players in the region and scholars and policymakers have questioned the extent to which they have contributed to an economic transformation in Africa, the consequences of the rise of PABs are little understood. An inquiry into the consequences of the rise of PABs on the mobilisation of financing for the real economy, financial stability and policy space, has to rely significantly on anecdotal evidence and studies from other regions.

There is thus a high value added of research which examines the consequences of the rise PABs in Africa. This essay highlights at least four issues to consider in future research on the relationship between the rise of PABs and the transformation of African economies. First, if we are to understand the impact of the rise of PABs on economic transformation in Africa, we must explore whether PABs have improved access to credit for those segments which are considered a priority for an economic transformation such as SMEs, agriculture and industry but lack adequate access. In doing so, it is important to consider the effects on the availability of financing for the real economy in both host and home countries.

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For a discussion of theory and evidence on mock-compliance please see Walters (2008)
Second, to better understand the effects of the rise of PABs on financial stability, it is important to consider both the capacity and the willingness to enforce regulation and supervision. Examining regulatory frameworks on paper, including formal arrangements for cross-border supervision, is essential but will only give an incomplete picture of the effects of the rise of PABs on financial stability. There is a need for studies which explore actual compliance with regulation and the soft information that regulators exchange across borders.

Third, to better understand the effects of the rise of PABs on sustainable development it is also important to examine the extent to which PABs are patient providers of capital. To what extent do PABs consider host countries as second homes? How mobile are they, given that there are only few ‘safe havens’ in the region to which they might relocate?

Finally, to what extent do PABs restrict the policy autonomy of host and home state governments? Do PABs react similarly to a perceived deterioration in the host country environments like banks from emerging economies like China and from advanced economies? In other words, are PABs more loyal and if yes why?

For pioneers in research on cross-border banking the dynamism of Pan-African Banking opens up an exciting research agenda.

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CHAPTER 4

Challenges for resolution of banks in Africa
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Introduction

In many of the Sub-Saharan Africa countries the macro-economic conditions have deteriorated over the last two years. Often such developments create fiscal challenges for countries and profitability issues for their financial institutions which potentially gives rise to a vicious feedback loop. At the same time banking groups with a headquarter in Africa, so-called Pan-African Banks, have expanded rapidly. These banking groups often have a systemic presence in their African host countries. Against this background the question arises whether the regulatory and oversight systems of the Sub-Saharan Africa countries are well equipped to weather a financial crisis when it comes to Africa. At first, this requires strong legal and supervisory regimes, and well-equipped supervisors. But even then, banks will from time to time fail and thus there is a need for strong insolvency frameworks designed for banks, in particular for those that are systemic.

A new standard has been established in the aftermath of the recent global financial crisis for effectively resolving financial institutions as part of a package of policy measures to address the moral hazard risks posed by systemically important financial institutions (SIFIs). The Key Attributes (KA) are a non-binding set of principles that form the new international standard for strengthening the resolution regimes for banks and other financial institutions. Many of these principles not only provide good guidance for resolving global systemically important financial institutions, but also for resolving smaller financial institutions. Therefore, the KA also provide useful guidance for designing insolvency frameworks for banks in less developed countries, but the implementation of the KA must take into account the complexity of the financial sector and the systemic importance of their financial institutions; thus, not all KA might be relevant for these countries, or should only be implemented proportionally.

Economies and financial sectors in Africa have their own characteristics. So, in designing insolvency frameworks for SSA countries, one wonders what the specific challenges are for resolution of banks in Africa and how best to overcome them. In this chapter an attempt is undertaken to map these challenges guided by the principles laid down in the KA.

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1 The views expressed in this chapter are entirely those of the author. They do not necessarily represent the views of the World Bank Group, or those of the Executive Directors of the World Bank or the Governments they represent.
2 General insolvency frameworks for commercial firms have proven to be ineffective for dealing with failing banks, especially during financial crises.
3 In October 2011 the FSB adopted the Key Attributes of Effective Resolution Regimes for Financial Institutions (Key Attributes at its Plenary meeting). At the Cannes Summit of November 2011, they were endorsed by the G20 Leaders as a new international standard for resolution regimes, while they were supplemented in October 2014 with new Annexes containing among others sector-specific guidance for insurers and financial market infrastructures. See Financial Stability Board, 2011.
4 According to the KA a bank is systemically significant (or critical) if its failure could lead to a disruption of services critical for the functioning of the financial system or real economy. A distinction can be made between those financial institutions that are considered to be systemic for the global economy (G-SIFIs) and those financial institutions that are considered to be systemic for domestic economies (D-SIFIs). A sub-category of the SIFIs is the Systemically Important Banks (SIBs) category divided in G-SIBs and D-SIBs.
Context
Many SSA countries enjoyed a decade or more of uninterrupted growth since the beginning of the century, albeit from a relatively low base. Real GDP per capita doubled in the median SSA country and slightly more in the average SSA country. However, the economic circumstances have deteriorated considerably since 2016. Among others this has been due to lower commodity prices and the tightening of monetary policies in developed countries, especially higher interest rates in the US, which led to higher borrowing costs for SSA countries, and an increase of public debt in foreign currency. Public debt (foreign or domestically held) has risen considerably in countries like Mozambique, Ghana, Kenya, Senegal and Cote d’Ivoire. In addition, the risk profile of the banking sector has weakened; non-performing loans have started to increase in several countries, such as Angola, Ghana, Kenya, Nigeria, and republic of Congo. Some of these countries (e.g. Angola, Nigeria) have a large share of their bank lending in foreign currencies. In addition, in many SSA countries the exposures of the financial sector to the sovereign are increasing, directly to government or indirectly through supply chains that depend on the State. Many sovereigns are building up their arrears or financing large parts of their expenditures via issuance of government securities, thereby crowding out private sector funding (e.g. The Gambia). Surveys of the World Bank have indicated that correspondent banking relationships have also come under pressure in smaller countries in Africa. The result has been a diminished supply of US dollars, with a large share of bank lending in FX in some countries (e.g. Angola and Nigeria), and a slowdown in international trade operations in countries like Liberia, Angola and Guinea, further weakening their financial systems. The recent increase in FX-denominated government debt also increases FX risk, which could result in balance of payments difficulties for some countries and corresponding financial stability implications (e.g. in Mozambique and Angola). All by all, recent deterioration in the macroeconomic environment represents the main financial stability risks in SSA. This has already led to bank failures in some SSA countries, such as Angola, DRC, Ghana, Kenya, Mozambique, and Uganda. In other countries the impact may have been delayed (as exposures are rolled over, or temporary liquidity support is provided), but those policy choices will only magnify the potential impact, if and when, a crisis hits.

Large banking groups have emerged since the mid-2000s in many SSA countries mainly via the acquisition of existing banks, resulting in Pan-African Banks (PABs) that have subsidiaries (rarely branches) across many borders with a significant presence in many of the host countries. While there are many African banking groups, seven of them dominate the field. Three have headquarters in Morocco, two in Togo, one in Nigeria, and one in South Africa. In addition to these systemic PABs, there are some smaller African banking groups with a sub-regional presence. Major PABs have complex holding structures overseeing many different financial and real sector activities. Some of the financial holdings are unregulated. The emergence of these PABs has a number of benefits, such as improved competition, strengthened inclusion, and economies of scale, but they also pose supervisory challenges, and they may increase systemic and cross-border contagion risks.

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6 See International Monetary Fund, 2015, page 17.
8 International Monetary Fund, 2016, page 15.
9 Attijariwafa Bank, Groupe Banque Centrale Populaire, and Banque Marocaine du Commerce Extérieur (BMCE) from Morocco; Ecobank and Oragroup from Togo, Standard Bank from South Africa; and United Bank for Africa from Nigeria.
10 See International Monetary Fund, 2015 page 28.
The heterogeneity of the SSA countries is large: Some countries have relatively large banking sectors (South Africa, Nigeria and Angola are the largest), while others have micro financial systems (Lesotho, Seychelles, Swaziland, and Sao Tome are among the smallest). Most countries fall in the middle, but even then, it can be difficult to speak of the region as a whole, as there are different monetary arrangements and endogenous factors.

The SSA countries are in different stages of implementing international supervision standards; some of them have implemented Basel II standards, while others are still preparing to introduce them. There are supervisory weaknesses concerning consolidated supervision, home-host relationships, capacity, and enforcement of the laws and regulations, in many SAA countries. The quality of financial reporting varies and different accounting standards are used by countries, which further complicates supervision of the PABs. Also, many of the SSA countries have not yet introduced depositor protection schemes. Some parts of Africa have established regional institutions to cooperate on monetary, banking, and capital market issues; i.e. the West African Economic and Monetary Union (WAEMU), the East Africa Community (EAC), the Southern African Development Community (SADC), and the Association of African Central Banks (AACB).

Key attributes: Before the recent global financial crisis most countries around the globe had only a few tools at their disposal for resolving banks, often a combination of supervisory forbearance, ‘voluntary’ mergers with other financial institutions, and nationalization. Only as a very last resort, authorities were able and willing to liquidate banks. The available instruments (blanket guarantees, recapitalization, AMCs) depended in most cases also on large public support measures. As a result, authorities ended up with high public costs and were at the same time not able to resolve SIFIs.

If anything, the global financial crisis showed that the regulatory frameworks for resolving SIFIs were inadequate in most countries, very costly for the tax payers, and could easily lead to fiscal crises with serious consequences for the real economies. One part of the policy measures that the international community (G20, FSB, BCBS) initiated after the crisis were the Key Attributes, targeted at SIFIs and setting out the mandates, powers and tools that national authorities must have to deal with financial institutions whose failure could have a systemic impact. They are intended to provide national authorities the ability to efficiently resolve those institutions at least cost for the State. Although targeted at SIFIs, the KeyAttributes also provide very useful guidance for smaller financial institutions.

For resolution regimes to be most effective a number of preconditions have to be in place. In case these preconditions are not fully implemented, or only partly in place, the effectiveness of a resolution regime can be seriously hampered. In this regard the following preconditions are important:

- A well-established framework for financial stability, surveillance and policy formulation;
- An effective system of supervision, regulation and oversight of banks;
- Effective protection schemes for depositors and other protected clients or customers;
- A robust accounting, auditing and disclosure regime; and

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11 Including Emergency Liquidity Assistance provided by central banks to ailing banks, turned into unrecoverable solvency support.

12 See the FSB, 2016.
• A well-developed legal framework and judicial system.

The key attributes contain twelve essential features of an effective resolution regime. These features should be integrated in the national resolution frameworks for financial institutions and tailored to the local circumstances and legal traditions. There is not a one size fits all approach. The implementation of these essential features in Africa comes with its own challenges. Although the key Attributes are designed for all kind of SIFIs, covering banks, insurers, financial market infrastructures, and possibly other kind of SIFIs, below we will give attention to African banks only.

Scope and authority

**Key attributes:** Designed to help countries establish effective resolution frameworks for SIFIs and more particularly for SIBs. Therefore, it is important that a resolution framework clearly indicates which banks are systemically important. The Key Attributes (KA 1.1) declares that a resolution regime should extend to holding companies, non-regulated entities that are significant to the business of the group (e.g. treasury services, risk management and valuation), and branches of foreign banks.

Many of the powers, tools, and legal safeguards, are also useful for resolving smaller banks, but not all of them. For instance, the establishment of a bridge bank or the requirement to draft resolution plans are only useful for systemic banks. Thus, the determination that a bank is systemic has important implications; from a supervisory perspective (e.g. extra capital requirements, higher scrutiny), but also for its treatment in resolution.

An administrative authority should be established in charge of exercising the resolution powers and tools provided under the resolution regime for resolving banks. Such a resolution authority should aim at pursuing financial stability, ensure continuity of critical financial services, avoid unnecessary destruction of value and minimizing costs of resolution for all stakeholders, while considering the potential impact of resolution actions on financial stability in other jurisdictions.

In pursuing its objectives and functions, the resolution authority should be operationally independent. The Key Attributes lay down some safeguards in this respect by requiring a sound accountability framework with adequate checks and balances, such as on independent decision-making, proper appointment and dismissal procedures for the head of the resolution authority, members of the governing body and senior management, regulations to prevent conflicts of interest, and sound reporting requirements. The resolution authority should also have adequate human and budgetary resources to operate independently. However, the Key Attributes itself are silent with respect to the preferred institutional set-up of the resolution authority and whether it should be a stand-alone institution or be part of an existing financial authority, but the explanatory notes acknowledge that the resolution authority may be part of an institution in charge of other functions (but operationally separated), such as a supervisor or a deposit insurer.\(^{13}\)

**Challenges for Africa:** Although none of the SSA countries have a G-SIB headquartered in their jurisdiction, several of them are home to a PAB. A PAB has a systemic presence in its own jurisdiction, but also in many jurisdictions of the region via subsidiaries. Further, smaller African banking groups have a systemic presence in some SSA countries. The failure of a D-SIB always threatens the financial stability of the jurisdiction in dispute, while the failure of a smaller bank in most cases does not. Therefore, it is essential for resolution frameworks in Africa to determine which banks are systemically important for a country and which are not. A

\(^{13}\) See explanatory notes for KA 2.
resolution framework should enable the resolution authority to make such a determination ex-ante, or at the time of intervention. Thus, the resolution framework should provide the authorities enough flexibility to determine that a bank is systemic at the time of failing, even though not considered to be systemic in advance. The rise of PABs has amplified the need in Africa for establishing resolution frameworks for systemic banks that are able to efficiently resolve these institutions at least cost for the State.

The KA provide a powerful resolution framework, not only for systemic banks, but also for medium and small domestic banks in SSA jurisdictions. Implementation of the KA in Africa will strengthen the overall resolution regimes for banks by introducing new concepts in addition to the liquidation option, such as a powerful independent resolution authority, a pallet of resolution tools, legal safeguards for shareholders and creditors of banks, funding arrangements for resolution, access to data, cross-border cooperation, and recovery and resolution plans. These concepts can be used in many circumstances and for many banks, and will help to resolve banks in a more efficient manner. However, the implementation of the KA should be tailored to the local jurisdictions and be implemented taken into account the complexity and importance of the financial sector of SSA countries. In other words, they should be implemented proportionally in Africa. To find the right balance in implementing the KA in Africa is a challenge and not straightforward.

For many SSA countries it would make sense to establish the resolution authority in an existing financial authority, such as the central bank or supervisory authority. This has several advantages, such as being able, right from the start, to profit from the independence of such an institution, safeguarded in many SSA countries by laws and regulations. An efficient resolution regime must have a resolution authority that is shielded from political and industry influences. This will be a challenge in Africa (as in many other parts of the world), where in the past vested interests formed an obstacle for resolving failing banks, resulting in zombie banks at the expense of State coffers.

In an environment of scarce resources, it is also advantageous for the resolution authority to lean upon the reputation, financial resources, expertise, and IT systems of the central bank. However, to manage conflicts of interest, strong fire walls must be put in place between the supervision and resolution functions of central banks, including separate reporting lines till the highest level. At the same time, regulators should realize that the capacity of many supervisors and central banks in SSA countries is tight or inadequate. Therefore, adding a new task to an existing authority should be accompanied by extra resources. To prepare for taking on the task of resolution authority, central banks should also improve their IT systems for gathering relevant data, train their staff, and strengthen cross-border cooperation.

**Powers & tools**

**Key attributes:** Financial authorities should have a variety of powers and tools to protect the stability of the financial system and the interests of all stakeholders involved. Interventions in ailing banks should start at the stage of supervision, ranging from warnings to more intrusive measures, such as orders to end business lines and implement recovery plans, that, in worst case scenarios, cross over to interventions by the resolution authority at the resolution stage. The resolution authority should have a broad gamma of intervention powers at its disposal to achieve its objectives of preserving financial stability, protecting depositors, while minimizing value destruction and overall costs of resolution. The resolution authority should be able to use these

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14 In principle, the RA could also be vested in a deposit insurance fund, but these funds are still lacking in many SSA countries; see below on funding issues.
powers in a flexible manner, separately, or in combination with other resolution tools, and tailored to the situation at hand. Many of the resolution tools can be applied to smaller and larger institutions and in countries at all stages of economic development.

Arguably, the most fundamental principle laid down by the Key Attributes is KA 3.1, which determines that resolution should be initiated when a firm is no longer viable or likely to be no longer viable and has no reasonable prospect of becoming so. Resolution authorities’ prime task is to initiate early interventions. History has shown that in many cases authorities act too late and too slow, thereby destroying whatever value is left with the ailing firm. KA 3.1 firmly states that interventions should start before a firm is balance-sheet insolvent and before all equity has been fully wiped out, triggered by clear and transparent criteria of non-viability, which are based on quantitative and qualitative factors. Most importantly, a clear process should be in place to transfer the decision-making authority from the supervisor to the resolution authority.

KA 3.2 contains a long list of resolution powers, but it is important to realize that withdrawal of the license and liquidation of a failing bank is the preferred option for smaller and medium banks that are non-systemic (KA 3.2 xii). Only in case there are systemic reasons (broader financial stability concerns), or that resolution of a failing bank is the least cost solution, resolution actions should be undertaken; and still some parts of the failing bank will end in liquidation.

Some of the resolution powers and tools can be applied in all jurisdictions and are useful powers for resolving SIBs and for liquidating smaller, non-systemic banks, while other powers and tools are targeted only at resolving G/D-SIBs (see box).\textsuperscript{15} \textsuperscript{16}

\textsuperscript{15} World Bank, 2017.
\textsuperscript{16} There is a last resort resolution power to put a failing financial institution under temporary public ownership in case the stability of the financial system is at risk. This tool is not mentioned in KA 3 on Resolution Powers, but curiously enough in KA 6 on Funding. This power to temporary nationalize financial institutions can be applied by all jurisdictions.
In addition to the power to liquidate a bank, the following ‘common resolution powers’ can be applied to small and larger banks:

- Remove and replace the senior management and directors and recover monies from responsible persons (KA 3.2 i). This power is both a supervisory power as a resolution power;
- Appoint an administrator to take control of and manage the affected firm (KA 3.2 ii). This power is also both a supervisory power as a resolution power.
- Operate and resolve the financial firm, including powers to terminate contracts, continue or assign contracts, purchase or sell assets, write down debt and take any other action necessary to restructure or wind down the firm’s operations (KA 3.2 iii);
- Override rights of shareholders of the firm in resolution (KA 3.2 v);
- Transfer of assets and liabilities, legal rights and obligations (KA 3.2 vi and KA 3.3). This tool, also called the Purchase (of assets) and Assumption (of liabilities) tool, is one of the most efficient and (cost) effective resolution tools.

Some of the powers and tools are only targeted at G/D-SIBs:

- Ensure continuity of essential services and functions by requiring other companies in the same group to continue to provide such essential services (KA 3.2 iv);
- Establish a temporary bridge institution, owned by Government, to take over and continue operating certain critical functions and viable operations of a failed firm (KA 3.2 vii);
- Establish a separate asset management vehicle (KA 3.2 viii);
- Carry out bail-in within resolution as a means to achieve or help achieve continuity of essential functions (KA 3.2 ix, KA 3.5, and KA 3.6);
- Temporarily stay the exercise of early termination rights that may otherwise be triggered upon entry of a firm into resolution or in connection with the use of resolution powers (KA 3.2 x and KA 4);
- Impose a moratorium with suspension of payments to unsecured creditors and customers and a stay on creditor actions to attach assets or otherwise collect money or property from the firm, while protecting the enforcement of eligible netting and collateral agreements (KA 3.2 xi).

Challenges for Africa: For SSA countries that are considering introducing a resolution regime for banks it is essential that in advance a thorough assessment of the financial sector is undertaken to determine which resolution powers and tools would be appropriate for the country. Apart from deciding which banks are systemic and which are not, this should entail reviewing banks’ business plans, products, and their balance sheets, to determine their assets and liabilities’ portfolios. In addition, it is important to take stock of the integration of the financial markets; countries where banks are integrated with other financial institutions, such as insurance companies, resulting in financial groups or holding companies, require a more sophisticated resolution framework than countries without such financial groups. Lastly, countries which are home to banks with subsidiaries and branches abroad, or countries with many subsidiaries and branches from foreign banks, must put more emphasize on the cross-border aspects of resolution, including the cooperation and information exchange with foreign authorities.

Such an assessment should not be a static, but a dynamic assessment taking into account new developments in the financial markets. The financial markets in many SSA countries are undergoing rapid changes, such as the growth of PABs, but also the development of new financial banking and payment services that are competing with traditional banks, and are often blurring the boundaries between traditional financial sectors.
SSA countries are well advised to introduce all the common resolution powers. This, by itself, is not an easy exercise. The new powers should be integrated in the domestic legal framework, what might be a challenge given the intrusive character of some of the powers (i.e. the power to override shareholder rights), but they should also be woven into the existing regime for supervision of banks and the existing bank liquidation framework. A clear separation between supervision, resolution, and liquidation should be spelled out in the law. Highly recommended, most tools should not be used for different purposes; it should be or a supervision tool, or a resolution tool, clearly indicating the character of intervention by the authorities, thereby reducing legal uncertainty.

As indicated above, some of the tools are only relevant for G/D-SIBs and therefore not relevant for SSA countries which are lacking such institutions. For instance, the power to ensure of essential services and functions is only relevant in case a systemically important institution must be resolved going-concern. Also, a bridge bank should only be established in case such a temporary institution is necessary ‘to bridge time’ to find a viable solution for a failing SIB. Smaller banks should be liquidated, while their valuable assets might be transferred to other banks. An asset management vehicle is a useful tool to deal with a large amount of non-performing assets of the same class. Thus, only to be used when a SIB is failing, or in case a crisis hits the broader financial sector and same class assets of several failing smaller banks might best be brought together in the asset management vehicle. However, history has shown that asset management vehicles often have been used to store non-performing assets (at book-value), resulting in high costs for the State. Smaller SSA countries are advised to establish them only on ad-hoc basis, when needed, and not to make them part of the standard resolution toolbox.

Some other resolution powers are not suitable for SSA countries even in case they have SIBs operating in their jurisdictions, because their financial markets are less developed. The bail-in tool requires that there are sufficient liabilities on the balance sheet of a failing G/D-SIB to be bailed-in. In many SSA countries, the liability side of the balance sheet of their banks consists mainly of small depositors and/or small retailers. Bailing in those depositors would only enlarge a financial crisis by eroding the trust in the financial system. Also, the financial markets of these countries are not sufficiently developed for banks to issue bail-in-able debt securities, as banks can do in highly developed financial markets to raise enough TLAC. The power to stay the exercise of early termination rights is only appropriate in those jurisdictions where financial contracts (e.g. derivatives contracts) are commonly used, and therefore less adequate and necessary for SSA countries. In the same vein, a moratorium with a suspension of payments should better not be used in jurisdictions where trust in the financial markets is already low, as it often tends to worsen this trust, might lead to run on banks, and smaller banks can better directly be liquidated, once they are failing.

Triggers for entering the resolution stage of an ailing bank should be clearly defined. The legal frameworks of many SSA countries have very general and broad criteria to initiate early supervisory intervention or liquidation of a bank (e.g. ’the condition of the institution is unsound’), without any additional specific criteria for liquidation. Therefore, when drafting a regime for resolution of banks, the law should include very specific and mandatory triggers for initiating resolution that force resolution authorities to take early action.

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17 The Financial Stability Board (FSB) published requirements regarding TLAC (total loss absorbing capacity) on November 9, 2015, which were adopted at the G20 summit in Turkey. TLAC requires G-SIBs to develop their ability to cope with large losses without burdening taxpayers. These banks are required to have a certain amount of loss absorbing securities outstanding, which together make up the bank’s TLAC.
Most importantly, the introduction of adequate legal resolution powers is a necessary step to improve the resolution regime of banks in all SSA countries, but it will not be sufficient to overcome the lack of action many of their authorities have exhibited in the past in resolving failing banks in a timely and efficient manner. What often is missing is a willingness to act in sensitive cases, leading to unnecessary forbearance, loss of value in banks, and high public costs. The introduction of best international practices in resolution of banks should be accompanied by a change in culture and attitude of the supervision and resolution authorities. It should also be well understood that the final stone of a sound resolution building is the availability of well-educated and trained staff. Some of the new resolution powers are technical sophisticated (e.g. valuation of assets in the case of bail-in; stay and action on exercising early termination rights of financial contracts) and require that resolution authorities are able to attract and retain (costly) top-notch financial experts.

**Funding**

**Key attributes:** The funding of resolution actions must be well regulated to protect the tax payer by minimizing public financial support (KA 6). The funding of resolving a failing bank should in first instance be borne by the bank, its unsecured and uninsured creditors and, if necessary, by other parts of the banking sector. Credible funding arrangements for resolution may consist of a privately funded resolution fund, a privately funded deposit insurance scheme, or a combination of these funds, while temporary public funding arrangements should be in place to provide liquidity or solvency support, if needed, to ascertain orderly resolution, combined with arrangements to recover any public losses from the financial industry. To minimize the risk of moral hazard, such temporary public support should only be provided if it is necessary to foster the stability of the financial system and permits a resolution option that is best able to achieve an orderly resolution of one or more failing banks, while all private resources of funding have been exhausted.

**Challenges for Africa:** The lack of funding for resolving failing banks is often a major challenge in SSA countries. The lack of resources is caused by several factors. First, while secured depositors should be reimbursed by privately funded deposit insurance schemes, the number of deposit insurance schemes in Africa is still lacking behind those in other parts of the world. The International Association of Deposit Insurers (IADI) indicates on its website that per 22 September 2017 only 25 countries (of the 55 African countries) have an explicit deposit insurance scheme. So, in less than half of the African countries there is an official funding arrangement in place for paying insured depositors out. This means that in most African countries resources must come from the State, or ex-post from the remaining banks. In addition, in many African countries with an explicit deposit insurance scheme, the deposit insurance funds

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18 Losses are allocated to shareholders and unsecured/uninsured creditors in accordance with the hierarchy of claims and they should carry the losses provided that they are no worse off than in liquidation. See the section on legal safeguards below.

19 Or private resources of funding would not achieve the statutory objectives of the resolution regime (see essential criteria ii for KA 6.2).

20 The Key Attributes recognize that there might be cases where reliance on nationalization or public ownership is the only viable option for continuing critical functions and that therefore some countries might incorporate in their resolution framework this as a last resort option (KA 6.5).

21 See [http://www.iadi.org](http://www.iadi.org). An explicit deposit insurance scheme is established by statute and typically insures deposits up to a statutory coverage limit.

22 Fortunately, as in other countries, triggered by the most recent global financial crisis, the number of explicit deposit insurance schemes is rapidly rising in Africa. According to IADI 10 African countries are currently developing a deposit insurance protection scheme.
have not reached their minimum target size. This means that already the failure of a medium sized bank will result in a funding gap. In principle, such funding gap could be financed by the deposit insurance scheme through borrowing in the domestic market\(^{23}\), or the State could temporary shoulder a full pay-out to the insured depositors.\(^{24}\) However, these financing options are not available in many SSA countries. For the above-mentioned reasons many deposit schemes in Africa are not able to contribute to the resolution of a SIB.

In many SSA countries fiscal resources are insufficient to set-up temporary public funding arrangements to provide solvency support, if needed. Therefore, even in case the resolution authority has all the statutory powers and tools, the swift resolution of a failing systemically important bank, will be held back by the lack of sufficient temporary public resources. This is a major obstacle in Africa for carrying out swift, efficient, and least-cost resolutions of D-SIBs. This lack of a sufficient fiscal back-up undermines the trust in the financial system and will hamper the resolution of a systemic bank, but when the preconditions are in place (e.g. effective supervision), SSA countries could establish a privately funded scheme combining deposit protection and resolution frameworks, ex ante to be funded by the financial industry.

The private funding of a D-SIB is in many SSA countries limited because of less developed financial markets and the lack of more sophisticated financial products and instruments. The resolution of a D-SIB should according to the KA in first instance be borne by its shareholders and its unsecured and uninsured creditors, such as bond holders. But the issuance of bonds in many SSA financial markets is very limited. Often government bonds are the only bonds that are traded at those markets. The bail-in resolution tool is for this reason not a realistic option for the funding of a D-SIB in many SSA countries.

The withdrawal by global banks of correspondent banking relationships (CBRs) with SAA countries might complicate the resolution of a PAB. International financial flows are important for the economic growth and financial stability of the SSA countries. Less CBRs have resulted in a concentration of cross-border flows, which may pose financial stability risks.\(^{25}\) More specifically, it might increase liquidity stress in foreign denominations and thereby accelerate the resolution of a failing bank and/or complicate its resolution.

**Legal safeguards**

**Key attributes:** Contain far reaching measures that infringe upon third party’s rights, such as the powers to terminate contracts, to override rights of shareholders, and to transfer or sell assets and liabilities of a failing bank (KA 3.2). The overruling of these rights is justified on grounds of public interest, i.e. to preserve the stability of the financial system and to contain costs for the society (tax payer).

However, the Key Attributes also contain a number of explicit safeguards designed to protect the governance and economic rights of creditors, counterparties and shareholders of a failed bank, or to protect an orderly and prompt resolution by the resolution authority. The Key Attributes try to establish a delicate balance between providing the resolution authority all the necessary tools to ensure prompt corrective resolution, while protecting to the extent possible the essential rights of the parties involved.

In particular, the key attributes specify that “just” compensation should be awarded to creditors for any expropriation: KA 5.2 states that creditors should have a right to compensation where

\(^{23}\) If the statutes of the deposit insurance scheme provide for this.

\(^{24}\) Temporary sources of funding must ex-post be recovered from the financial system participants, according to KA 6.2.

\(^{25}\) International Monetary Fund, 2016, page 15.
they do not receive at a minimum what they would have received in a liquidation of the firm (“no creditor worse off than in liquidation safeguard”). Another safeguard in the Key Attributes (KA 5.1) states that the resolution authority is required to exercise resolution powers in a way that respects the applicable hierarchy of creditor claims. Respecting the hierarchy of claims means, in principle, absorbing losses in the following order: equity should absorb losses first; then losses should be imposed on sub-ordinated debt, and only then on senior debt holders. A resolution authority, as a general principle, should treat creditors of the same class equal (“pari passu principle”), while providing flexibility to depart from that principle, if necessary to protect financial stability, or to maximize the value for the benefit of all creditors.\(^{26}\)

The resolution authority should have the capacity to exercise the resolution powers with the necessary speed and flexibility, subject to constitutionally protected legal remedies and due process (KA 5.4). Where prior court approval is required, the timelines required for completing court proceedings should be consistent with the Key Attributes and should be incorporated into resolution planning. The legal framework should according to KA 5.5 provide that the only remedy that can be obtained from a court or tribunal through judicial review of measures taken by the resolution authority acting within their powers and in good faith, is compensation (thus, not staying or reversing the resolution measures).

**Challenges for Africa:** The introduction of intrusive resolution powers in Africa requires a balanced protection of the rights of creditors, counterparties and shareholders of a failed bank. Authorities must navigate the existing protection of property rights in their country, often anchored in constitutional provisions. The “no creditor worse off than in liquidation safeguard” necessitates an adequate valuation at the time of resolution of these rights, as well as a counterfactual valuation of these rights in liquidation.\(^{27}\)

The SSA countries should secure a clear hierarchy of claims that will apply in the process of liquidation and resolution of banks, which hierarchy has enough flexibility to depart from the “pari passu principle” if necessary to protect financial stability, or to maximize the value for the benefit of all creditors. If SSA countries already have a hierarchy of claims, it is often for commercial firms (not specifically for banks), depositors are not ranked first, and the order in which claims are rewarded is not always straightforward. This creates uncertainty for shareholders (investors) and unsecured creditors of banks alike and is detrimental for economic growth and the stability of the financial system. A tricky legal issue in many countries is to incorporate enough flexibility in the legal system to depart from the ‘pari passu principle’ when necessary in the interest of financial stability or the benefit of all creditors. Often this requires careful drafting to stay within the legal traditions of a country.

Courts play a key role in the process of liquidation of banks in most SSA countries, which role must be more limited in case of resolution of banks. As it is essential that resolution measures are taken swiftly and that the measures taken by the resolution authority enjoy a high degree of legal certainty, courts in SSA countries must be able to use expedited procedures in case court approvals are necessary for the resolution authority to exercise resolution powers. Courts should not be able to overrule resolution measures taken in good faith by the resolution authority, but should be able to award monetary compensation, if errors were made. Such limitation of court powers runs against many legal traditions in SSA countries and, in some cases, challenges their constitutional provisions. The implementation of these resolution principles requires a clear

\(^{26}\) See essential criteria for KA 5.2.

\(^{27}\) A precondition for such complicated exercises is that the relevant data and the necessary valuation expertise are quickly available, what is most often not the case in SSA countries. However, resolution authorities could have ex-ante contracts set up with (international) accounting firms that can do this valuation on short notice. See also next section on access to information.
explanation to the judiciary and the regulators of the resolution objectives and principles, and a
careful and precise drafting to incorporate these principles in local legal frameworks. Central
banks could play an active role in engaging with the judiciary and transferring knowledge. Also,
many courts in the SSA countries have limited capacity and judges are not specialized in certain
parts of law. Courts should consider creating specialist divisions that deal with commercial and
financial matters, including the liquidation and resolution of banks.

Access to information

Key attributes: To be able to take accurate and swift resolution measures banks’ management
and resolution authorities should have access to all relevant information. This requires that
banks have accurate and up-to-date data systems in place. Resolution authorities should have
direct access to banks to gather all critical information, if needed. In normal times such non-
public information should be available for recovery and resolution planning, while in times of
crisis this information should be available to take resolution measures. It should be accessible
for all domestic authorities who play a role in safeguarding the stability of the financial system
(“safety-net players”), such as financial supervisory authorities, central banks, resolution
authorities, ministries of finance, and deposit insurance funds. The information exchange
between the domestic safety-net players should be embedded in broader cooperation
agreements to formalize the work procedures and the division of responsibilities between
them. In case a failing bank has cross-border operations, legal frameworks must also enable
the exchange of information with all relevant foreign safety-net players.

Accurate data systems are especially necessary for making proper mandatory valuations of a
failing bank’s assets and liabilities, including its off-balance sheet items. Best international
practice is that the supervisor, or the resolution authority, will instruct an independent institution
(e.g. a recognized auditor firm) to undertake such a valuation when a bank is nearing the
conditions (triggers) for entering in resolution.

Challenges for Africa: As an efficient bank resolution regime is fully dependent on the
accuracy and accessibility of relevant bank data, data systems in many SSA countries need to
be strengthened. Weak data systems are due to many factors, such as outdated reporting and
information systems, a lack of adequate internal risk control and compliance frameworks, and
weak accounting and auditing configurations. For instance, important data gaps exist for PABs
at the level of subsidiaries, limiting the analysis of the soundness of the bank, in particular the
analysis of capital and non-performing loan ratios. Therefore, the implementation of a new
resolution framework in SSA countries must go hand-in-hand with a serious investment in data
systems. In addition, the staff of banks and that of supervision and resolution authorities need
to get adequate training to be able to use the new systems.

The introduction of a sound bank resolution regime not only requires a dedicated effort by the
authorities to set it up, but also sufficient financial resources, often scarce in fiscally stressed
SSA countries. Investments in new IT-systems and the hiring of IT expertise, are expensive.
Also, the upgrading of the accounting and auditing practices, and the training of staff, requires
support from international experts. In addition, valuations, to be done in the context of
resolution, require specialist skills that are expensive.

The information exchange between all safety-net players in SSA countries needs to be
strengthened. In many of these countries the exchange of information between all stake holders

28 Such agreements often take the form of one or more Memoranda of Understanding (MOUs).
29 See also next section on cross-border cooperation.
30 See International Monetary Fund, 2015, page 33.
is ad hoc and voluntary, or the legal system prohibits an appropriate exchange of sensitive and granular non-public bank information with domestic institutions outside the supervisory realm. In addition, there are often operational obstacles prohibiting a timely and accurate exchange of information. Even more hurdles exist in many SSA countries for exchanging information with foreign supervisors, foreign resolution authorities, and other foreign safety-net players.

Cross-border cooperation

**Key attributes:** Resolution authorities should aim for cross-border cooperation and coordination and legal frameworks must accommodate it (KA 7). Where there is a significant cross-border influence in the financial sector, cooperation between home and host authorities is essential. For effective resolution, a resolution authority should be able to cooperate with foreign resolution authorities, as well as with foreign supervisors and/or deposit insurance agencies. The resolution authority should have the power to negotiate and to enter into information exchange and cooperation agreements with foreign authorities. Strong cooperation can only develop if authorities are explicitly allowed to exchange relevant information with their international counterparts to enable cross-border resolution planning and execution. As the data to be exchanged contain often market sensitive information, a high degree of confidentiality should be ensured at all times.

The resolution authority should have resolution powers over both subsidiaries and branches of foreign banks to support resolution measures of foreign home authorities or, in exceptional cases, to take measures on its own initiative to preserve the stability of its financial system (KA 7.3). The key attributes also provide that a resolution authority should be able to support foreign resolution authorities in their resolution actions or give effect to foreign resolution actions (KA 7.5). The legal basis for this should be provided in law, including an enabling clause to conclude bilateral or multilateral MOUs. Moreover, national laws should not discriminate against creditors on the basis of their nationality, location of the claim, etc. (KA 7.4).

**Challenges for Africa:** The rapid emergence of PABs across Africa underlines the need for strong cross-border resolution agreements between home and host authorities. The home authorities of PABs have an interest in securing sound resolution procedures for their SIBs to preserve the stability of their own financial system, especially when critical parts of a SIB are outside their own jurisdiction. Host authorities have a keen interest in close cooperation of resolution procedures with the home authorities when a subsidiary of a PAB is systemically important in their jurisdiction.\(^3\) In some parts of Africa supervisory colleges have been established for PABs, but in practice these arrangements are not yet very effective and trailing behind the establishment of many cross-border subsidiaries\(^3\), and resolution agreements between home and host authorities or non-existent or existing at a very elementary level. This might jeopardize a quick and efficient resolution of a failing PAB, thereby threatening the financial stability of its own and many host jurisdictions.

There is an asymmetric balance of power between the four SSA countries which are home to a systemic PAB\(^3\) and the authorities of countries which are hosting PAB’s subsidiaries. Home authorities have better and more information about the soundness of a systemic PAB, as well as more grip on its senior management. Therefore, home authorities might at first instance have fewer incentives to conclude cooperation and information exchange agreements with host authorities, in particular not if the subsidiaries in those countries are relatively small compared

\(^3\) See Financial Stability Board, 2015.
\(^3\) See International Monetary Fund, 2015, page 42.
\(^3\) The following countries are home to a systemic PAB: Morocco, Nigeria, South Africa, and Togo.
to the group’s balance sheet and no critical parts of the PAB are vested in host jurisdictions. This asymmetry might hinder the concluding of cooperation agreements in Africa, resulting in a sub-optimal resolution framework for Africa as a whole.

There are many differences between SSA countries concerning their political system, organization of government, and legal traditions, which contain additional obstacles for strengthening cooperation between the resolution authorities of these countries. For instance, financial reports and disclosures of PABs are based on different sets of accounting standards, as not all African jurisdictions apply International Financial Reporting Standards. Discrepancies in legal authority, accounting, auditing, and confidentiality regimes must be overcome, if necessary with support from international experts. Regional institutions (WAEMU, EAC, SADC, AACB) aim to overcome several of these differences, but in bank resolution they might create extra challenges as resolution powers are not always clear and spread across regional and national bodies.35

**Recovery and resolution planning – Resolvability assessment**

**Key attributes:** The recent global financial crisis has demonstrated that banks and authorities should prepare well in advance before banks get into problems. They must have plans with options in case of failing, especially for SIBs. Therefore, the Key Attributes introduce new tools consisting of a recovery planning tool, a resolution planning tool and a resolvability assessment tool (RRPs). According to the Key Attributes (KA 11), banks (senior management) should have detailed *Recovery Plans* for addressing financial problems without relying on public sources, to be updated at least annually. Such plans should indicate options for a bank to recover from financial distress as a “going concern”, while the bank remains under its management’s control. Recovery plans indicate among other measures to conserve or raise capital and/or liquidity, and measures to restructure the business of the bank to decrease the risk profile of the bank and make it profitable again. Resolution authorities should have *Resolution Plans* that provide for the resolution of a systemic bank on a “gone concern” basis when recovery plans have failed, indicating specific options and actions for resolution.36 In addition, home resolution authorities should on a regular basis evaluate the feasibility and credibility of resolution strategies (*Resolvability Assessments*), at least for SIBs (KA 10). While recovery and resolution tools and resolvability assessments are intended for G-SIBs, they might well be applied to other banks, especially D-SIBs, which could have an impact on the jurisdiction’s financial stability in the event of its failure.

**Challenges for Africa:** With the rise of PABs in Africa there is a clear need to have a well-designed and organized regime for RRPs, in particular in those jurisdictions which are home to a systemic PAB. To secure the stability of their financial systems, such home authorities should on a regular basis undertake thorough RRPs. One of the challenges is to simplify the set-up of systemic PABs to create a clear structure consisting of a few legal entities, which are well prepared for resolution; many banking groups in Africa have complicated cross-border structures making effective supervision and resolution a challenge for both home and host authorities.37 This will not be an easy task and will require the necessary will, effort and

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34 See International Monetary Fund, 2015, page 38.
35 See International Monetary Fund, 2015, page 44.
36 As recommended in the Guidance Note issued by the FSB on 21 June 2018 on “Funding Strategy Elements of an Implementable Resolution Plan”, such resolutions plans should also appropriately address the available temporary public funding in resolution, be it from the central bank (in case of emergency liquidity assistance) and/or the government (in case of solvency support).
37 See International Monetary Fund, 2015, page 37.
expertise from banks and authorities alike. However, the streamlining of these banks will be in the interest of financial stability and by making them more transparent and efficient, also in the interest of the businesses themselves.

A major obstacle for authorities to undertake RRPs in Africa is the lack of reliable granular data. To develop adequate recovery and resolution plans, and to perform sound resolution assessments, banks and authorities must possess a clear overview of all business activities and the risks associated with them. Not all supervisors in Africa have those data, especially not home supervisors of banks with many cross-border operations, in the absence of home-host cooperation agreements on bank resolution. Supervisors and resolution authorities in Africa should give priority to improve their data reporting and IT systems and improve the exchange of cross-border data using cooperation agreements.38

RRPs are not costless and might require a huge amount of resources and capacity of banks and authorities. For G/D-SIBs RRPs should be required and be completed for the sake of financial stability. However, the less complex and interconnected a bank is, the simpler RRPs should be, lastly resulting in requiring no RRPs for small banks.

So, now what to do?

The turn in the economic tide and the rise of regional systemically important banks in Africa make the strengthening of resolution frameworks more urgent. When the opportunity arises, SSA countries should use the KA’s insights and weave them into their resolution regimes for banks, in tune with the development of their financial sectors and the presence of systemically important banks. While all SSA countries should take a close look at their resolution regimes for banks, in particular SSA countries home to one or more of the PABs, should investigate whether their resolution frameworks are sufficiently capable of quickly resolving these banks, while shielding tax payers from losses and protecting critical functions, thereby ensuring the stability of the financial sector.

SSA countries that have decided to strengthen their bank resolution frameworks should focus on the following actions:

- Ensure that the pre-conditions for effective resolution regimes for banks are met, in particular an effective system of regulating and supervising banks;
- Undertake an assessment of the current insolvency framework for banks against the Key Attributes and reform the relevant legal framework (laws and regulations) taking into account the structure and complexity of the financial sector, the systemic importance of the banks, and the legal traditions of the jurisdiction;
- Establish an independent resolution authority with sufficient capacity and resources to operate and with an appropriate governance framework. In case the resolution authority will be housed at the central bank or the financial supervisor, strong fire walls are required to separate the interests of the monetary authority, the supervisor, the payment overseer, etc., from the interests of the resolution authority;
- Strengthen the quality and scope of the operational data systems to enable an effective use of the new resolution powers and tools;
- Assess the national accounting and auditing standards and, if necessary, bring them in line with international standards;

38 See the section on access to information.
• Check best options for ex ante funding by the financial industry of resolution measures;

• Strengthen international cooperation, exchange of supervisory information, and international exchange of information necessary for preparing RRPs, as a matter of urgency. This is specifically relevant for the home authorities of PABs, but also for host authorities with subsidiaries of PABs that have a systemic presence;

• The regional institutions in Africa (WAEMU, EAC, SADC, AACB) should play a key role in coordinating and harmonizing legal frameworks and operational practices in the field of bank resolution (including among other data systems, accounting and auditing practices, and RRPs);

• Home supervisors/resolution authorities of PABs should start preparing RRPs and use them, as a matter of priority, to simplify the organization structures of these banks;[39]

• What remains is a willingness to act swiftly, if needed, in the interest of protecting depositors, preserving value in the financial sector, and limiting public costs.

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[39] For some PABs, because of their structure, it is not directly clear who should take the lead, such as in the case of Ecobank; Togo or Nigeria?
Beyond the formal sector: money transfers to Africa

Ibrahim Yusuf, Dahabshiil Group

Dahabshiil is an indigenous African company, founded in 1970. It was set up as a new remittance venture to enable migrants to send money to family and friends back in the countries of East Africa. Dahabshiil has grown to be the largest African money transfer business, operating in 126 countries across the world, 40 of which are in Africa. It remains a business committed to its original values of trust, reliability, integrity and customer-focus. In addition to serving individual customers, Dahabshiil offers money transfer and banking services to businesses and international organisations, including the United Nations, World Bank, Oxfam and Save the Children. They all rely on Dahabshiil to provide payment services to their staff, contractors, government institutions and partner NGOs.

The United Nations describes Dahabshiil’s services as ‘the only safe and efficient option to transfer funds to projects’. The United Nations Development Program uses Dahabshiil to transfer money for local programs. Alvaro Rodriguez, the agency’s director for Somalia, said that such companies provide “the only safe and efficient option to transfer funds to projects benefiting the most vulnerable people of Somalia……Their service is fast and efficient.”

Cash remains king for many Money Services Businesses (MSBs), including Dahabshiil, as well as for many of the MSBs that are increasingly also providing online services. Dahabshiil Online Service was recently launched to complement the cash services, with the objective of providing a quicker, more secure service for all types of clients, with more robust end-end compliance.

MSBs are critical for the Somali private financial sector. They champion economic recovery and sustainable development for a secure and resilient future. To support such economies, urgent measures are needed to address barriers to reducing remittance costs, such as result from the de-risking by international banks, when they close the bank accounts of money transfer operators, in order to cope with the high regulatory burden aimed at reducing money laundering and financial crime.

Despite huge progress in reforming a state that has witnessed over three decades of lawlessness and anarchy, Somalis are witnessing growing isolation due to major de-risking trends, which have hit the Somali financial sector hardest. Recent progress in Somalia, including the passing of the AML/CFT law in 2016, which established a financial intelligence unit and a National AML Committee is an example of this progress. More than 20 technical assistance programmes in the financial sector have been provided by international partners including the United Kingdom, the United States (Treasury, State, Defence, and Justice Departments), IMF, World Bank, African Development Bank, Islamic Development Bank, UN, Sweden, Norway, EU, and Turkey, including regarding the promulgation of AML/CFT regulations.

In addition, assistance on third party regulation of banks and MSBs has been provided by the World Bank in support of the Central Bank of Somalia, including developing detailed and international standard examination processes of MSBs, a Suspicious Activity Reporting regime with the submission of reports to Somali Financial Intelligence Unit, and the passage of the Telecoms Law, 2017, aimed at addressing the final frontier in regulation, mobile money. There has also been increased regulation of Somali MSBs in other jurisdictions, including the United States, United Kingdom, Australia, and Sweden, raising standards across all their operations globally.
Meanwhile, recovery and stability are at great risk. Clearly the reforms are, rightly or wrongly, equated with increased punitive measures. Both the government, and international partners, and the private sector have made huge investments in rebuilding financial governance frameworks, as well as formalising the Somali financial sector to bring it into line with global standards. However, the global financial regulatory regime has tightened considerably, shifting risk to fragile, poor countries as they are systematically excluded from the global financial order. This has posed a major challenge to the provision and cost of remittance services to certain regions, like Somalia, and does not reflect the ground-breaking financial governance reforms that have transformed the regulatory landscape in Somalia.

Industry, governments and civil society have been lobbying for action on de-risking in view of growing empirical evidence that risk is in fact rising as a result of this process, as it results in transparency diminishing, thus creating greater insecurity in financial flows. This goes against the spirit and letter of laws aimed at AML/CFT. Recent studies and recommendations should provide a clear steer to policymakers, for example the recent US GAO study and the FATF/FSB report being commissioned by the G20. Solutions should be coupled with continued technical assistance and political support from international partners to buttress the financial governance/AML/CFT reform agenda in the “Third Mile” of remittances. This is the only sustainable exit from poverty and insecurity in Somalia and similar high-risk environments.

Academics, industry and policymakers should thus spend more time encouraging policy debates, to provide a framework of institutional support for different stakeholders whose experience is vital in helping adjust the policies of regulators and banks as they seek to secure financial flows, and provide access to critical services, and to profitable businesses.

In a shrinking aid landscape, remittances must be exploited more effectively. They constitute a growing and dependable resource for social welfare and economic growth, given the right institutional support. Rita Ramalho, Acting Director of the World Bank’s Global Indicators Group, stresses “Remittances are an important source of income for millions of families in developing countries. As such, a weakening of remittance flows can have a serious impact on the ability of families to get health care, education or proper nutrition.” As noted by the World Bank, remittances face increasing challenges, with statistics showing that remittances to developing countries fell for a second consecutive year in 2016, a trend not seen in three decades. The World Bank estimates that officially recorded remittances to developing countries amounted to $429 billion in 2016, a decline of 2.4 percent from over $440 billion in 2015. Global remittances, which include flows to high-income countries, contracted by 1.2 percent to $575 billion in 2016, from $582 billion in 2015. Remittances are also a key investment resource that calls for effective public/private partnerships. The Somali government needs international partner support to protect Somali remittances as the driver of recovery and growth. The key here will be to help Somalis balance financial stability, financial inclusion and financial integrity through an effective national and international payments system linked to international bank accounts.

Somalis throughout the globe, and at home, applaud the lead taken by the United States and France on the restoration of correspondent banking relationships for Somali Money Transfer Operators. This will help address obstacles to safe and secure remittance flows. Of particular note is the landmark decision by the US government to address the unintended consequences of de-risking through the US Congress passing a law (Countering America’s Adversaries Through Sanctions Act-Public Law No. 115-44- Part Ii--Enhancing Antiterrorism Tools of The Department Of The Treasury Sec. 271- Improving Anti-terror Finance Monitoring of Funds Transfers). The Law explores the potential efficacy of requiring banking regulators to establish a pilot program to provide technical assistance to depository institutions and credit unions that wish to provide account services to MSBs serving individuals in countries like Somalia. The
US Treasury is currently conducting a feasibility study as to implementation. The French authorities are also taking decisive measures. Along with FATF, they brought together 70 countries with banks and money transfer operators for a historic dialogue on de-risking and AML/CFT. This took place in Paris, 25-26 April 2018, with a view to seeking solutions to de-risking.

Dahabshiil appreciates equally, the efforts of international partners like the United Kingdom, World Bank and IMF in rebuilding the financial sector, where presently key milestones have been achieved, as reflected in recent press releases from the World Bank and IMF. It is important to support such reforms, to create peace dividends and reduce poverty to prevent displacement, insecurity and vulnerability. Securing Somali remittances involves concrete actions and commitments aimed at the causes of migration, chief amongst which is political and economic strife. Somalis have made key progress in achieving stability, and such gains are worthy of entrenchment; in this regard, a special tribute is also to be paid to the role of the diaspora and their remittances in enabling the continued survival and resettlement of displaced and vulnerable Somalis at home.
CHAPTER 6

International bond issuance in SSA: Developments and challenges
Stuart Culverhouse, Exotix

In this chapter, I provide an overview of Sub-Saharan Africa ex-South Africa (henceforth, SSA) international bond markets to give some context for the development of African capital markets, the issuance therein, and prospects going forward. I do not cover domestic bond markets in SSA, which has been another important part of the development of African capital markets over the past decade.

Various factors have contributed to the issuance of sovereign Eurobonds in SSA. Note that these are not necessarily unique to SSA; many relate to frontier markets or low-income countries in general. These factors can broadly be divided into two categories; the push factors, which are essentially externally driven, and pull factors, which are domestically driven. (See box.)

On the external side, significant debt relief delivered via the Highly Indebted Poor Country (HIPC) debt relief initiative and other more ad hoc treatments has been an incredible part of the story, essentially wiping out the debts of most SSA countries and giving the beneficiaries a clean balance sheet. The increase in commodity prices through the 2000s also played a part, boosting their export earnings, and, since the global financial crisis (GFC), the resulting global monetary stimulus has been a factor too (i.e. the search for yield).

But domestic factors should not be underestimated. These include the emergence of democratic and stronger institutions, with countries even changing governments from incumbent to opposition and back again over the course of an election cycle. We have also seen the pursuit of structural reforms. One could argue these have been partly imposed on governments because of HIPC, but I believe that domestic authorities have taken much stronger ownership over their own structural reform agendas and to strengthen macro policy frameworks, in both monetary (moving to more flexible exchange rates with independent central banks targeting inflation) and fiscal (greater budget discipline and less fiscal dominance) policy. For many SSA countries, macro frameworks have been brought up to the level we can observe in more mainstream emerging markets (EMs) over a short space of time.

These factors have helped to reduce country risk premiums and improve sovereign risk ratings, and to lower borrowing costs, which SSA has been able to take advantage of by borrowing on
the international bond markets. This has been hugely positive for the region’s investment story in terms of attracting new sources of private capital.

SSA bond issuance has boomed over the past decade. Figure 1 summarises the issuance from SSA sovereigns since 2007, when Ghana issued the region’s debut Eurobond (there had already been some international bonds in the region, but these had come out of default and restructuring situations). We saw a couple of other issues at that time (Gabon’s debut followed Ghana), but the global financial crisis and then the Eurozone crisis stopped everything in its tracks, with issuance only beginning to pick up again in 2013. Exotix Capital calculates that there is now (as at end-June 2018) some US$44bn of outstanding sovereign Eurobonds in hard currency (dollars and euros), with around 80% of current outstanding bonds having been issued since 2013. And the number of issuers has broadened out over time, too, from just six maiden issuers over 2007-11 (excluding bonds issued through restructurings) to 16 countries with outstanding Eurobonds today, and many now have multiple bonds outstanding (i.e. they have become repeat issuers). Moreover, the 10-year bonds issued by Ghana and Gabon back in 2007 were successfully repaid in 2017, demonstrating a track record of repayment.

2018 has been a particularly active year. There has been issuance of around US$12.7bn (equivalent) from six issuers – Nigeria, Kenya, Senegal, Cote d’Ivoire, Angola and Ghana (all repeat issuers, having previously issued before). This probably reflects a combination of relatively low yields and, hence, attractive borrowing costs, some pre-funding ahead of expected tightening in global credit conditions, and large funding needs (budget deficits).

Figure 1: SSA sovereign bond issuance* (US$bn)


Figure 2 shows the yield on selected SSA hard currency sovereign bonds (Eurobonds), summarising what has happened to borrowing costs in the region over the past few years. It is illustrative of the situation throughout much of SSA. Yields were low over the course of 2012-
14, but exploded over the course of 2015-16 because of the oil and commodity price collapse. But we then saw a sustained fall, with yields close to all-time lows by the end of 2017.

Figure 2: Selected SSA Eurobond yields (%)

![Chart showing selected SSA Eurobond yields](image)

Source: Bloomberg. Data to 4 July.

Yields on SSA Eurobonds (and on EM Eurobonds more generally) have, however, risen this year. This reflects a combination of external factors (rising US interest rates and a strengthening US dollar) and domestic factors (including concerns over the rise in government debt in the region). The movement is mirrored in most issuers, such as Angola, Cameroon, Gabon and Senegal, with Zambia being hit the most because of particular concerns over its own debt situation.

Yields across SSA are now around 5-7% for the generally stronger credits (Cote d’Ivoire, Senegal) and/or shortest tenors (2-3 years) and around 8-9% for some of the longest-duration bonds (e.g. 30-year maturities) or weaker credits. The highest-yielding performing bonds are in Zambia, with yields of 11%, whereas Republic of Congo is distressed and Mozambique is in default.

To put this in a global context, Figure 3 charts the nominal yield on EM US$ bonds (based on a benchmark index known as the Emerging Market Bond Index – EMBI). Most EM fund managers will assess their performance relative to this benchmark. The nominal yield is currently around 6.7%, having risen by 120bps this year.

The darker blue line in Figure 3 is Exotix Capital’s proprietary measure of the yield on frontier bonds, which we proxy with a simple average of a basket of B-rated medium-term hard currency sovereign bonds. It is not just exclusively SSA, but frontiers more widely. It shows that frontiers typically trade at a yield premium over their more mature EM counterparts, to compensate for
illiquidity and other factors. The graph shows that we have seen a huge compression in frontier (and, hence, SSA yields) relative to EMs during periods of search for yield. Based on our measure, frontier yields again touched their all-time lows at the beginning of 2018, but have risen sharply since then. Exotix Capital’s measure of the frontier bond yield is now 8%, having risen by 175bps this year.

Figure 3: Frontier and EM US$ bond yields (%)

![Graph showing Frontier and EM US$ bond yields](image)

Source: Exotix, Bloomberg. Data to 4 July 2018. EM nominal yield defined at EMBI spread plus US 10y bond yield. Exotix Frontier Bond yield is defined as the average yield across a sample of B-rated medium-term bonds.

However, after a renewed build-up of debt, concerns have resurfaced that the region is facing another debt crisis. We have seen a rise in government debt ratios over the past few years across SSA, and a concern that, broadly speaking, public debt burdens in SSA are now back to their pre-HIPC levels of the early 2000s.

The rise in debt burdens reflects a number of factors, not just market access. It might reflect the mistaken belief that continued easy sources of money would be permanent, so that refinancing on attractive terms would always be possible. It might also reflect policy complacency in terms of a lack of willingness of policymakers to adjust their policies in response to shocks. It also reflects generally weaker EM currencies during a period of US dollar strength. And it might also reflect fiscal weakness during election periods.

Figure 4 shows the gross government debt burden for selected SSA countries from the IMF WEO. It shows a story of two halves over the past 15 years or so. By the late 2000s, we saw a reduction in public debt burdens post-HIPC, even through the global financial crisis. These burdens tended to bottom out around 2011-12. With the oil and commodity price collapse from 2014, debt burdens began to rise again. This was due to a combination of much weaker exports...
and government revenues; hence, widening budget deficits, falling nominal GDP (due to lower commodity prices) and, in many cases, much weaker domestic currencies.

Figure 4: SSA public debt (% of GDP)

Within SSA, the government debt ratio is now around 45-50% of GDP. If we strip out Nigeria, which is so big in nominal GDP terms that it distorts the average, then it is closer to 60%. But we can see the trajectory has gone up, across the region.

However, even the average masks a whole range of different performance. At the one end, the Republic of Congo and Mozambique have seen their debt burdens rise to over 100% of GDP. At the other end of the range, Nigeria is just 25% of GDP. The median is around 58-59%. And this is just across those Eurobond issuers. There are a number of other SSA low-income countries or fragile states that we exclude here.

Figure 5 puts Africa in the context of other EMs. Africa is competing with a whole swathe of EM and frontier issuers for capital. So it is useful to compare African fundamentals (here, we use government debt ratios) with those of other regions. Public debt burdens have increased since 2013 in most regions around the world, not just SSA, with the possible exception of emerging Europe.

Source: IMF WEO, Exotix. SSA average based on countries with outstanding Eurobond issues.
So, Africa is not necessarily unique in terms of rising debt burdens, although the concern might be that the debt of African countries has increased from a relatively benign starting point since debt relief was granted, and that many of those countries are still relatively new to the market (having only issued within the past five or so years), and hence have less of a track record of responding to market shocks.

This raises the question of whether those gains from past debt relief have been lost. Although there is no doubt that debt burdens have risen, and this might constrain policy flexibility, we think the improved policy frameworks, stronger institutions and ability of governments to diversify funding sources and access private markets that have evolved over the past decade are lasting positives. However, this does suggest a need for renewed fiscal restraint, borrowing discipline and reform efforts to ensure public debt returns to more sustainable levels.

**Policy issues**

To conclude, there will still be a role for international capital markets in SSA to help countries meet massive funding needs and diversify funding sources. But there are challenges, some of which we highlight below.

First, dealing with countries in debt distress. This currently includes Mozambique and the Republic of Congo, countries that have announced the need to restructure their debts, due to over borrowing, and pursue IMF programmes to provide official financial support and help oversee adjustment processes.

Second, in particular, these two country cases also highlight an evolving theme in the international financial architecture, that is of dealing with the presence of non-traditional (eg non-Paris Club) bilateral creditors, specifically China, in these two cases, but also Russia,
Brazil, India and others. Non-traditional lenders have provided a lot of new financing to SSA countries, and because much of their lending has taken place only in the past decade, they have not played a significant role historically in many previous restructuring situations – until now. It will be interesting to see how these cases get resolved and what policy lessons they provide.

Third, other programme countries or possible programme countries. A number of SSA countries have turned to the IMF pre-emptively to help them deal with financing or debt problems, and IMF involvement (although a source of moral hazard) tends to provide comfort to investors. Some countries, such as Ghana and Kenya, are in IMF programmes, so investors will monitor programme compliance and reform implementation, as their governments aim for a successful exit. Others look constructively to the Fund for help, with Angola for example seeking a new IMF policy arrangement to help it deal with macroeconomic imbalances. Meanwhile, Zambia struggles to re-engage with the Fund to restore shaken investor confidence. The way IMF lending rules have evolved over the past few years, with stricter criteria and oversight, and greater emphasis on debt sustainability, may also shape what any new programme means for private creditors in those countries.

Fourth, strengthening debt management and public financial management (PFM). Despite the improvements in policy making mentioned earlier, I think fiscal policy and debt management in particular has tended to lag the institutional improvements we have seen in monetary policy over the past decade. One lesson over the past few years – Mozambique being an obvious example – is the need to strengthen debt management, to ensure greater transparency around borrowing on behalf of both borrowing governments and private creditors (avoiding hidden or shadow lending), more responsible and sustainable lending, greater disclosure over borrowing terms and the use of proceeds, better project appraisal, and more emphasis on debt sustainability analysis.

Fifth, how do you deal with a debt problem? It is better to avoid getting into a debt problem, but if there is one, how do you deal with it? This is not unique to SSA, but, given the rise in debt burdens, perhaps takes on extra resonance in the region. Without restructuring, which can be costly, or being able to catalyse non-debt-creating flows (such as privatisation), countries can either undertake a fiscal adjustment or grow out of their debt problem, or a combination of the two. These require structural reforms, which can be hard to do, especially over a political cycle, but will be increasingly necessary in an environment of less easy money and weaker global growth rates.
African debt: a varied landscape?

Anne-Marie Gulde-Wolf (IMF) and Reda Cherif (IMF)

The debt relief initiative of the mid-2000s helped to significantly lower the then crippling debt levels in Sub-Saharan Africa. More recently though, the renewed surge in public debt following the 2014 decline in commodity prices has raised fears of a repeat of the debt crises of the 1990s. We argue that the context in sub-Saharan Africa has changed in many ways: While debt sustainability is an immediate concern in several countries and should be tackled by many others in the medium term, the debt relief initiatives and the growth acceleration of the 2000s led to notable improvements in health, education and infrastructure, improving the region’s long-term growth prospects. The landscape of creditors has also changed with the rise of non-traditional and more market-based lenders which offer both new opportunities and challenges going forward.

Introduction

The level of public debt in sub-Saharan Africa has been creeping up since the collapse of commodity prices in 2014. This increase has pushed many observers to warn against the return of the situation prevailing in the 1980s and 1990s, before the debt relief initiatives, when most of the continent was suffering from the burden of heavy debt.

Interpreting the increase in public debt poses a dilemma. On the one hand, a rise in public can be problematic as spiralling interest and principal payments could limit the ability of governments to finance much needed social and infrastructure spending. Moreover, the rise in public debt might crowd out private investment depressing long term growth. On the other hand, public investment is key to creating the very conditions enabling growth, including by tackling major infrastructure bottlenecks, improving health and increasing human capital by investing in education and skills. An “overly conservative” approach to fiscal policy could prevent a developing economy from reaching its long-term potential.

There is an important empirical literature exploring the nonlinearity of the relationship between debt and economic growth (see for example Reinhart and Rogoff 2009, Reinhart and Rogoff 2010, Kumar and Woo, 2010 and Eberhardt and Presbitero 2015). Most studies find a threshold beyond which growth is negatively affected however, there are different threshold levels. With doubts about a universal threshold there is limited guidance from empirical studies disentangling whether and how the debt build-up can be constructively “used” to improve the key drivers of growth.

In this paper we argue that the “debt landscape” in sub-Saharan Africa is far from uniform. Debt relief initiatives and the high growth of the 2000s have helped bring about notable improvements in key drivers of long term growth in Africa (consistent with the findings of IMF 2015 and IMF 2018). Health, education and infrastructure indicators started improving at a more rapid pace around 2000. Moreover, the landscape of foreign creditors to Africa has changed compared to the 1990s. The role of private and non-traditional lenders such as China

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1 We would like to thank Miguel Pereira Mendes for his excellent help with data gathering and Cleary Haines and Seung Mo Choi for helpful comments and suggestions.

2 However, Chudik, Mohaddes, Pesaran, and Raisi, (2017) do not find evidence of a single threshold in their sample beyond which public debt negatively affect growth.
has risen significantly, giving the economies of the region access to more financing and also showing that markets have been assessing positively the prospects of these economies. At this point, rising debt is indeed worrisome in some countries, and debt sustainability needs to be tackled urgently. In others, debt levels remain manageable and the emphasis should be more on reforms that would yield sustainable growth and productivity gains.

**Long-term perspective of public debt in Sub-Saharan Africa**

A long-term perspective on public debt in sub-Saharan Africa shows that: (i) the increase in total public debt since 2014 was more pronounced in oil exporting countries as a result of the collapse of oil prices; (ii) the levels of public debt in 2017 as a share of GDP remain much lower compared to the peaks of the 1990s (iii) which the debt relief initiatives of the 2000s contributed greatly to bring down.

**Figure 1.1. Sub-Saharan Africa: Total Public Debt**

![Figure 1.1. Sub-Saharan Africa: Total Public Debt](image)

Source: IMF, World Economic Outlook database.

Note: The blue line is the simple unweighted average of total public debt as a share of GDP in Sub-Saharan Africa since 1976. The gray area covers the distance between the 25th percentile and 75th percentile. The red line is an indicative threshold at 40 percent of GDP based on Reinhart et al. (2003).

Figure 1.1 shows the long-term behaviour of total public debt in Sub-Saharan Africa since 1976. Debt started creeping up from the mid-1970s and peaked in the early 1990s around a median level of 100 percent of GDP. The level remained high until the mid-2000s when debt fell rapidly until around 2012, before rising again in the recent years. As argued below, the debt relief effort contributed to the substantial decline of the late 2000s (Figure 1.2).

Despite the recent increase in debt, SSA countries are not back to the levels of debt during the debt crises periods of the 1990s or early 2000s. The current levels of debt are equivalent to those seen in the late 1970s and early 1980s.

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3 We focus on public debt as private debt, especially foreign held, is relatively small in many sub-Saharan African economies.
Given the heterogeneity in the group, we study the distribution of debt in three standard categories: oil exporters, other resource intensive countries (typically relying on minerals exports) and non-resource intensive countries (mostly agricultural goods exporters). The breakdown uncovers similar patterns with elevated levels of debt in the 1990s, rapid decline in the 2000s and an increase in the last few years. The figure shows that the recent increase in public debt has been the fastest in oil exporting countries.

The Heavily Indebted Poor Countries Initiative (HIPC) and the later Multilateral Debt Relief Initiative (MDRI) were initiated to address the debt overhang in poor countries. These efforts eventually achieved a large reduction of the debt burden of many African nations. Specific results differ significantly by country (Figure 1.3): For example, Malawi’s public debt in foreign currency declined from 90 percent of GDP in 2005 to 13 percent in 2006. Liberia’s debt went from 150 percent in 2009 to about 12 percent in 2010. Most of the relief programs took place in the second half of the 2000s and covered 29 SSA countries.

Figure 1.3. Foreign Currency Debt Relief

Source: IMF, Debt Sustainability Analysis database; and IMF staff calculations.
Note: t corresponds to the year of debt relief for each country.
Improvements in key long-term growth drivers

The reduction in public debt together with good growth performance in the 2000s, in part thanks to higher commodity prices, allowed many African governments finance more development investment related to health, education and infrastructure. Indicators along these dimensions showed a steady improvement starting in the early 2000s until 2017.

Life expectancy at birth for example stagnated at 50 years between 1980 and 2000 when it started increasing steadily including through the recent years of relatively slower growth. By 2016 it reached 60 years (Figure 1.4). The same improvement can be seen in infant mortality and maternal deaths indicators. There is obviously still need for further improvement, but the trend has been positive for almost 20 years, and it is the result of a combination of factors: a lighter debt burden, higher GDP growth and more efficient delivery of aid.

![Figure 1.4. Sub-Saharan Africa: Life Expectancy at Birth](source: World Bank, World Development Indicators)

A similar pattern can be observed in terms of education achievements. While primary completion as a percentage of the relevant age group hovered around 55 percent through the 1990s it started increasing steadily in 2000 to reach about 70 percent in 2016 (Figure 1.5).

![Figure 1.5. Sub-Saharan Africa: Primary Completion Rate](source: World Bank, World Development Indicators)
This improvement is even more impressive in the light of the demographic dynamics in the region where the annual population growth rate was 3 to 4 percent in many countries. Improvement can also be observed for higher levels of education. However, pre-school education, which was shown to have long lasting positive effects, remains limited in most African countries. In addition, the often very low quality of education is becoming more and more a focus of policies.4

The growth of the stock of public infrastructure in SSA has also been noticeable (Figure 1.6). It has, up until 2008, been comparable to the growth of similar metrics for emerging market economies and proved more resilient compared to other emerging markets since the global financial crisis (see IMF 2018). However, three important remarks are warranted:

First, on the positive side, an even stronger effect might be in store since many large projects which suffered delays for several years have only been completed recently or will be completed in the near future.

Second, there have been unprecedented improvements in access to telecommunications as shown by the mobile phone penetration rates in SSA countries. On average, they went from about 10 percent to 70 percent in the last decade (Figure 1.7). This is an important fact as it means that despite the lag in terms of roads and railroads quality and quantity, SSA countries can contemplate harnessing the access to the global network and compete in sectors such IT.

4 There is a literature documenting that the quality of early childhood education has long lasting effect on outcomes (see Heckman 2008). Moreover, Heckman (2013) shows that early childhood education has long term effect on the test scores of children through its positive effects on non-cognitive skills such as more positive social behaviour and higher motivation for academic achievement rather than higher IQs. The positive effects of early childhood education went beyond labour market outcomes and included improved health behaviour.
Finally, and notwithstanding these improvements, full scale of the needed effort in terms of public expenditure may be higher for SSA than for other regions, given high population growth and rapid urbanization (e.g. World Bank and World Economic Forum reports). Comparably more investment is required to improve the quality of infrastructure in a city where the population and size are increasing at a rapid pace. Hence, the stock and quality of infrastructure may still be relatively low in most sub-Saharan African economies compared to regions with less rapid growth in population and urbanization. This is even more so in some large economies such as Nigeria where the growth of infrastructure and improvement in quality has been even slower than in the average SSA economy.

Public debt in Sub-Saharan Africa: Where we are now?

In almost all SSA countries debt levels in 2018 are substantially higher in 2018 than 2013 (Figure 1.8). The still widening fiscal deficits in many countries (Figure 1.9) imply that public debt will continue to rise over the short horizon while the creditors’ landscape has dramatically changed with the rise of non-traditional lenders such as China and market-based financing. The greater reliance on sovereign bond issuance (Eurobond) also implies that changes in global financial conditions have a greater impact on the debt dynamics of many sub-Saharan economies.

![Figure 1.7. Sub-Saharan Africa: Mobile Cellular Subscriptions](source)

![Figure 1.8. Sub-Saharan Africa: Total Public Debt](source)
With rising debt stocks, interest payments have also been increasing, requiring a growing share of revenues to be allocated to debt service. For sub-Saharan Africa as a whole, the median interest-payments-to-revenue ratio nearly doubled from 5 to close to 10 percent between 2013 and 2017, and for oil-exporting countries, it increased from 2 to more than 15 percent over the same period. The largest increases occurred in Angola, Benin, Chad, the Republic of Congo, Gabon, Mozambique, Nigeria, Swaziland, Uganda, and Zambia.

Over the past decade, the composition of public debt changed significantly. With the decline in the availability of concessional financing, countries have shifted away from traditional concessional sources of financing, toward more market-based debt. As a result, the share of multilateral and concessional debt in total debt declined and the share of non-Paris Club debt increased. Domestic sources of debt financing remain limited, but continued reliance on foreign currency borrowing is another source of vulnerability. External public debt increased by about 40 percent from 2010–13 to 2017 region-wide and accounted for about 60 percent of total public debt in 2017 on average.

The recent increase partly reflects the rebound in Eurobond issuance by sub-Saharan African frontier markets. The share of foreign-currency-denominated debt varies from about 10 percent of total debt in South Africa to 100 percent in Comoros and Zimbabwe (Figure 1.10). While interest rates on foreign-currency-denominated debt are generally lower than domestic interest rates in sub-Saharan Africa, reliance on borrowing in foreign currency exposes debtor countries to exchange rate volatility and heightens refinancing and interest rate risk.

**Figure 1.9. Sub-Saharan Africa: Fiscal Balance**

Source: IMF, World Economic Outlook database.

**Figure 1.10. Sub-Saharan Africa: Public Sector Debt Decomposition, 2011–17**

Sources: IMF, Debt Sustainability Analysis database; and IMF staff calculations.
The rise in bond financed public debt in Sub-Saharan Africa benefited from strong investors’ interest. Portfolio inflows increased into some, but not all, countries in 2017 especially in sovereign debt securities (Figure 1.11). Sharp increases in inflows were observed in Ghana, Nigeria, and Senegal, but levels were low relative to the recent past in Kenya and Zambia, where no Eurobonds were issued in 2017. Furthermore, with the rise in debt accompanied by an increasing share of commercial, domestic, and non-traditional sources, borrowing countries’ exposure to market risk has risen, with increased challenges for debt resolution in the countries that find their debt burdens difficult to manage. Indeed, several countries, mostly resource-intensive countries in fragile situations, have accumulated external arrears.

In terms of recent developments in debt dynamics, deficits have increased over 2013-2016 and started narrowing in 2017. Meanwhile, public debt continued to rise in sub-Saharan Africa in 2017, despite the slight growth pickup and improved external environment. The median level of public debt in sub-Saharan Africa at the end of 2017 exceeded 50 percent of GDP.

Among the non-traditional creditors, China’s rise to become SSA’s single largest trading partner and a major lender and source of FDI to the region is remarkable. It accounts for about 21 percent of African trade in 2017. China has also become one of SSA’s largest bilateral official creditors. Its lending to SSA stood at US$52.8 billion at end-2016, representing 17.1 percent of SSA’s external public debt. China is a major creditor in: Republic of Congo (87.3 percent in 2017), Togo (50.8 percent), Angola (41.3 percent), Cameroon (37.2 percent), Ethiopia (33.2 percent), Central African Republic (2.1 percent), and Gabon (20.2 percent). Moreover, the figure shows new major infrastructure projects financed by China that were planned in 2018 in selected Sub-Saharan economies (Figure 1.12). The map covers 17 countries. It gives a good idea about the trends in terms of exposure to China. Most of the financing is non-concessional in the countries surveyed and the majority of projects are related to ports, airports, energy and rail.
Following a period of steady decline over 2016–17, spreads in sub-Saharan African frontier markets have been on an increasing trend in 2018, with a widening gap vis-à-vis other emerging markets. The figure shows that the spreads in SSA were narrowing their gap with those in emerging markets until early 2018 and were close to their levels in 2014 by that time (Figure 1.13). However, over 2018, spreads started increasing again and their gap with emerging markets has widened.

The spreads reflect both “push” and “pull” factors: On the one hand, easy global financing conditions i.e. the “search for yields” have contributed to narrowing the spreads until early 2018. Meanwhile, the gradual tightening of global financial conditions over 2018 (although they remain relatively easy by historical standards) has contributed to the increase in spreads in emerging and frontier markets especially in sub-Saharan Africa. On the other hand, the drive to invest in SSA securities reflects the huge potential of these economies and the improved conditions, in particular, in terms of governance and the conduct of macro-policy. Remarkably, between 2015 and 2017, spreads compressed even for countries with high debt-to-GDP ratios.

The favourable external market conditions create an opportunity for improving the debt maturity structure and implementing other strategic debt management operations, but countries
need to remain vigilant not to over-borrow in a context of rising external debt service and gross financing needs. The increased availability of external financing should not detract countries from their medium-term fiscal plans.

Meanwhile, debt sustainability has deteriorated among sub-Saharan African PRGT eligible low-income developing countries. As of the end of 2017, six countries were assessed to be in debt distress in the context of an IMF-World Bank debt sustainability analysis. The previous moderate ratings for Zambia and Ethiopia were changed to “high risk of debt distress.” While the causes of sliding into debt distress are country specific, most of the countries in debt distress are those in fragile situations or those facing adjustment to a very large shock to the price of their major export commodity.

**What countries need to do going forward**

To leverage the improvements of the last two decades it is necessary to improve revenue mobilization to maintain an adequate level of public investment. Meanwhile, policies to spur private investment are paramount to complement improvements in infrastructure, health and education in achieving sustained growth.

A key question is whether the increase in debt has been used to “scale up” investment.

In oil exporters, where debt increased the fastest, this has not been the case (Figure 1.14). In fact, average public investment as a share of GDP declined from about 13 percent to around 4 percent between 2014 and 2017, which is a low level by international standards.

**Figure 1.14. Sub-Saharan Africa: Public Investment**

Source: IMF, World Economic Outlook database.

In contrast in the other SSA economies (other resource intensive and non-resource intensive), investment has increased slightly since 2014. It can be said that the increase in debt has helped maintain levels of public investment around 7 percent of GDP.

IMF 2018c studies revenue mobilization in Sub-Saharan Africa. It finds that over the past three decades, many sub-Saharan African countries have achieved substantial gains in revenue mobilization (Figure 1.15). For the median sub-Saharan African economy, total revenue excluding grants increased from around 14 percent of GDP in the mid-1990s, to more than 18 percent in 2016, while tax revenue increased from 11 to 15 percent. It is striking to note that these trends have been driven primarily by non-natural resource revenues, which have increased particularly sharply in the past 10 years.

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5 For country details on the assessment see https://www.imf.org/external/pubs/ft/dsa/lic.aspx?cty
The analysis also shows some of the structural conditions that may account for the lower tax-to-GDP ratios in sub-Saharan Africa compared to other regions, including the level of development, trade openness, sectoral structure, income distribution, and institutional quality. It shows that sub-Saharan African countries could, on average, mobilize about 3 to 5 percent of GDP in additional tax collection, through a combination of reforms that improve the efficiency of current systems (including through the reduction of tax exemptions), and through institutional changes (such as improvements in governance and measures to control corruption). Studying success stories in revenue mobilization efforts in the region reveals certain broad commonalities such as commitment and building support. In other words, learning from peers that managed to increase their revenue mobilization could help sub-Saharan countries benefit from different relevant experiences.

To achieve sustained growth and productivity gains, improvements in infrastructure, health and education must be complemented by policies encouraging private investment. Sub-Saharan Africa is far from its potential in terms of private investment. It has the lowest private investment rate among developing regions in the world (Figure 1.16). It is key for SSA economies to increase private investment in order to achieve sustained growth. Implementing a strong regulatory and insolvency framework, a deeper financial system and greater openness to trade are among the policies that could help spur private investment. (see IMF 2018b). While public investment can support private investment, risks should be recognized and mitigated.
Conclusion

Sub-Saharan Africa has achieved impressive progress since the debt relief of the 2000s. It managed to make big strides in key determinants of growth such as health, education and infrastructure. While there are significant differences compared to the situation in the 1990s, there is now a significant build-up of new debt, resulting from push and pull factors. In particular, new creditors arose and gave the economies of the continent more access to financing while also perhaps stimulating some of the debt build-up.

The appetite of financial markets for African bonds shows that opportunities remain, but vulnerabilities stemming from the recent debt build-up need to be addressed. Policies should focus on: (i) Achieving a complete picture of the level and nature of debt; (ii) Tackling efficiency gaps in public investment; (iii) Improving domestic revenue mobilization; (iv) Spurring private investment to achieve a sustainable growth.

References


CHAPTER 8

Ghana’s experience
Maxwell Opoku-Afari, Deputy Governor, Bank of Ghana

Introduction
The rising debt levels in most sub-Saharan African (SSA) countries, after the Multilateral Debt Relief and Highly Indebted Poor Countries (HIPC) initiatives of early 2000s is not a new phenomenon. SSA countries have been there before. Low interest rates on Euro-dollar loans in the 1970s, induced by excess funds accumulated by oil producing countries, prompted several low income countries (LICs) to take some bilateral loans under the Paris Club Arrangements. However, a slump in prices of primary commodities, especially crude oil price between 1980 and late 1990s, increased significantly the repayment risks, most of which crystallized, creating, what was referred to in the literature as, “The Third World Debt Crisis”.

Despite IMF Structural Adjustment Facility (SAF) in 1986 and Enhanced Structural Adjustment Facility (ESAF) programs and the rescheduling of debt under the Paris Club in mid 1980s, LICs were still saddled with debt by early 2000s, resulting in the MDRI and HIPC initiatives of early 2000s that provided debt relief worth US$99 billion to 36 heavily indebted poor countries, of which 30 are from Africa.

But are these recent trends different from past high levels of debt? Are there risks, and would this lead to another call for relief for SSA countries? These are questions that require careful analysis. First, we need to understand what is driving these recent trends. After HIPC completion point, several of these African countries, including Ghana, have been described as being in moderate risk of debt distress (see IMF 2015), with instant low levels of debt and debt service. This also coincided with periods of strong macro policies and strengthening of institutions, together with a wave of good governance with enormous democratic dividends available to be tapped on the continent. This paper examines how this new fiscal space has been used to close the huge infrastructure deficit on the continent and whether this has been done in a sustainable way that could explain why this new threat of rising debt levels in SSA could be different from what we have seen in the past. The paper also attempts to provide a brief response to this question using the Ghanaian case.

The rest of the paper is structured as follows: section 2 discusses Africa’s debt dynamics, trying to resolve the new debt puzzle that emerged not long after the continent has been described among the fastest growing regions of the world in recent times; section 3 traces the history of Ghana’s entry into the international capital market, while section 4 provides a snapshot of Ghana’s recent macroeconomic fundamentals; section 5 describes what Ghana is doing differently in recent times to manage its rising debt burden, while the final section concludes with some policy recommendations for Ghana and the rest of Africa.

Africa’s debt dynamics: The new conundrum
The first decade of the 21st century was characterised by improvement in good governance in most SSA countries. Rising population growth alongside increased democratic accountability meant governments in the continent had to seek new sources of funding to invest in physical and human capital, prompting the IMF to organize the Financing for Development Conference in Addis Ababa in 2015, the third of such conferences. Recovery from the Global Financial Crisis of 2008-2009, coincided with a period of strong macroeconomic performance of most
emerging markets and frontier economies in developing countries, providing these economies with some latitude to tap into international capital markets. However, the slump in commodity prices between 2014 and 2016 and the low interest rate regime in advanced economies created a debt trap for most African economies. Low interest rates fuelled the appetite of African governments to borrow from the international capital markets to close their financing gaps.

The number of sovereign and supranational bond issuance in foreign currency by SSA countries increased from 31 in 2015 to 111 in 2017, with transaction value rising from US$13.6 billion to US$31.0 billion over the same period (Figure 1). Some of the factors driving the issuance of sovereign bonds included favourable external financing conditions resulting from the supportive low interest rate environment and stability in exchange rates; the desire to close the infrastructure gap to sustain growth momentum and deliver inclusive growth; commodity price boom for major export commodities which enhanced debt sustainability and improved credit worthiness; and the existence of fiscal space created by the HIPC debt relief initiative which resulted in low debt/GDP ratios across many SSA countries.

Figure 1: Sovereign and Corporate Bonds Issuance in Africa

Source: African Capital Markets Watch by PwC, Nigeria

**Ghana’s entry into the International Capital Markets**

Ghana first tapped the international capital markets by issuing US$750 million in September 2007 and has subsequently raised a total of US$3.7 billion in Eurobonds as at September 2016 (Table 1). In May 2018, a 10-year US$1 billion and a 30-year US$1 billion Eurobonds were issued at 7.625% and 8.625%, respectively, to retire relatively more expensive Eurobonds issued in October 2015 and September 2016 and as well as for budgetary support. Ghana’s increased access to the international capital market was induced by two key factors: 1) Ghana’s successful completion of the Highly Indebted Poor Country (HIPC) Programme which provided much-needed fiscal space as public debt-to-GDP ratio fell from 181 percent in 2000 to 25 percent in 2006; and 2) the rebasing of the Ghana’s GDP that moved the country to a lower middle-income status and thus ineligible for most bilateral and multilateral concessionary loans.
Figure 2 shows that the HIPC relief enjoyed by Ghana substantially brought down the country’s external debt-to-GDP ratio from over 150 percent in 2000 to close to 10 percent in 2006. The country’s domestic debt as a percentage of GDP also declined slightly from around 25 percent to around 15 percent over the same period as domestic debt reduction became the fiscal anchor.\(^6\) Overall, the country’s total public debt as a percentage of GDP declined from around 181 percent in 2000 to about 25 percent in 2006.

However, the gains from the reduction in public debt were short-lived as subsequent large fiscal deficits and commodity price shocks led to massive currency depreciation with public debt-to-GDP ratio rising to 70.2 percent in 2014 (with a greater part reflecting exchange rate impact). The country’s new middle-income status and the “wait and see” attitude by major investors as a result of the political uncertainty created by the long legal tussle after the 2012 presidential elections resulted in significant reduction in external inflows in terms of bilateral and multilateral grants. Consequently, the country’s external reserves position deteriorated, limiting the Bank of Ghana’s ability to adequately intervene in the foreign exchange market. The depreciation of the local currency against the major international currencies passed through into inflation, fuelling interest rate hikes, and creating overall macroeconomic instability. Against this

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\(^6\) This was to crowd-in the private sector to support economic growth.
background, Ghana requested for an Extended Credit Facility Agreement with the IMF, in order to restore macroeconomic stability, in particular, to address the strong balance of payments needs that was undermining macroeconomic stability, to re-anchor stability.

**Ghana’s macroeconomic fundamentals improving**

Guided by the saying “never let a crisis go to waste”, the economic management team and the Bank of Ghana have been able to re-engineer a switch from an environment of high and volatile inflation, high interest rate, and rapid exchange rate depreciation, to a new favourable environment of low inflation, exchange rate stability, and a build-up of a cushion of international reserves.

Inflation, which reached a high of 19.2 percent in March 2016, has receded to 9.8 percent in September 2018, and currently at 9 percent in January 2019. The real GDP growth took an upward turn in 2017, propelled by rebound in growth in the oil and non-oil sectors of the economy. Both the fiscal and current account deficits have reduced from 9.3 and 4.2 percent at end-2016 respectively to 5.9 and a surplus of 2.3 percent at end-2017. Gross international reserves improved from 3.5 months of import cover at end-2016 to 4.3 months of import cover at end-2017. The strong growth combined with a number of debt management strategies yielded a decline in the total public debt as a percentage of GDP from 73.1 percent at end 2016 to 68.7 percent at end-2017, thus returning the debt dynamics to a sustainable path. These developments have boosted investor confidence in Ghana with the country’s sovereign spread currently in line with peer economies. Over the medium term, 2018-2020, economic growth rate is expected to average 6.6 percent, while end-period inflation is expected to be anchored in low single digits.

Table 2: Snapshot of Ghana’s Macroeconomic Fundamentals

<table>
<thead>
<tr>
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<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP Growth</td>
<td>3.8%</td>
<td>3.7%</td>
<td>7.9%</td>
<td>6.6%</td>
</tr>
<tr>
<td>Inflation</td>
<td>17.7%</td>
<td>15.4%</td>
<td>11.8%</td>
<td>Single digit</td>
</tr>
<tr>
<td>Fiscal Deficit (% of GDP)</td>
<td>6.3%</td>
<td>9.3%</td>
<td>5.9%</td>
<td>3.0%</td>
</tr>
<tr>
<td>Trade Balance (% GDP)</td>
<td>-8.3%</td>
<td>-4.2%</td>
<td>2.3%</td>
<td>2.0%</td>
</tr>
<tr>
<td>Primary Balance (%GDP)</td>
<td>-0.40%</td>
<td>-1.4%</td>
<td>0.5%</td>
<td>2.0%</td>
</tr>
<tr>
<td>Import Cover</td>
<td>3.5months</td>
<td>3.5months</td>
<td>4.3months</td>
<td>≥ 4.0 months</td>
</tr>
<tr>
<td>Debt to GDP</td>
<td>71.5%</td>
<td>73.1%</td>
<td>68.7%</td>
<td>&lt; 65.0%</td>
</tr>
</tbody>
</table>

Primary fiscal balance is to remain in surplus of about 2.0 percent of GDP, while overall fiscal deficit is at most 3.0 percent of GDP. The total public debt over the medium term is projected to be less than 65.0 percent, with improvement in the country’s credit rating.

The current assessment is that the yield curve has normalised with high interest rates associated with high maturity instruments. With the issuance of a 30-year Eurobond in May 2018, the maturity profile has been lengthened from 15 years to 30 years. Overall, the entire interest rate spectrum has witnessed appreciable reduction in response to a cumulative reduction of 850
basis points in the monetary policy rate since January 2017. The fiscal consolidation is taking hold with primary fiscal balance turning positive in recent times and overall fiscal position improving as the deficit narrows.

Figure 3: Improvement in key macroeconomic indicators

Ghana’s economy is increasingly becoming diversified and robust, with the emerging oil and gas sector becoming the second largest foreign exchange earner after gold. The country’s main export commodities are gold, oil and cocoa & cocoa products. Ghana is the second largest gold producer in Africa and has the second largest gold refinery on the continent. Gold accounts for over 90.0 percent of mining sector’s output and some 40.0 percent of Ghana’s total exports with estimated gold reserves of about 2,000 tonnes.
Ghana’s debt management strategy

Entrenching the recent macroeconomic gains remains a key objective of the economic management team. In the context of excessive central bank financing to government in the past, Ghana’s Central Bank and the Ministry of Finance have signed a Memorandum of Understanding to limit central bank financing of government operations to zero percent. This measure alongside initiatives to boost manufacturing activity (One District One Factory Programme), modernization of agriculture and reforms aimed at improving public service delivery is anticipated to anchor macroeconomic stability and improve the country’s competitiveness. The improvement in the macroeconomic outlook for the country has started impacting on the country’s risk profile, reflected in significant decline in sovereign spreads.

Figure 5: Performance of Ghana’s Sovereign Bond, Emerging Markets Index and those of Selected SSA Peers

Source: Bloomberg (24/11/2017)

Comparing the performance of Ghana’s sovereign bonds with those of other SSA and Emerging Markets, Ghana performed better than her peers on the back of prudent debt management, favourable economic prospects and increased fiscal consolidation. The interest rate spread on Ghana’s sovereign bonds has narrowed substantially during the period January 2016 to December 2017. Ghana’s sovereign bond interest spread has aligned well with that of Emerging Markets measured by JP Morgan Emerging Markets Bond index which tracks the spread performance of 30+ Emerging Markets’ US dollar-denominated bonds. This also indicates a significant reduction in Ghana’s country-specific risks during the 24-month period, which contributed to the recent upgrade of Ghana’s credit rating by Standard and Poor (S&P) from B-to B, while Fitch and Moody maintained theirs at B and B3, respectively, with stable outlook.

On specific measures taken to deepen the debt market, the Government of Ghana is currently focused on the issuance of longer-dated debt in order to reduce rollover risks and lengthen the yield curve. Furthermore, government has put in place strategies to opportunistically issue debt when market conditions are favourable. Lastly, government remains watchful to ensure appropriate mix between dollar-denominated and cedi-denominated debt in order to minimize the spill over risks emanating from external financing conditions to the domestic sector.
Ghana has also made gains in the public debt as a result of the measures implemented in the preceding paragraph. The yield curve has been extended from 7 years to 15 and further to 30 years recently with a more appropriate mix between local and foreign currency debt. There has been consistent effort to reduce the short-term which led to a reduction in its composition of total debt from 45 percent in 2015 to 23 percent in 2017, reducing the overall rollover risks associated with the debt.

**Figure 6: Improvement in debt level and yield curve**

![Graph showing improvement in debt level and yield curve]

**Conclusion**

In conclusion, although participation of foreign investors in African capital markets would help deepen the continent’s capital markets, increased reliance on foreign currency borrowing constitutes a key vulnerability for debt management in SSA. Ability to contain vulnerabilities would require policies directed at building buffers, including stepping up on reforms in the area of increased targeted industrialisation to allow for African economies to contain shocks, which historically has been the main drivers of explosive debt situations.

The notable shift from concessional sources to non-concessional sources of borrowing means prudent macroeconomic policies need to be implemented to serve as a bulwark against interest rate and rollover risks.

Moving forward, prioritization of domestic revenue mobilization is critical to bringing public debt on a sustainable path. It has been noted that governments in SSA have the ability to mobilize about $50-80 billion in additional revenues from revenue reforms, which greatly...
exceeds the estimated $36 billion in official development assistance received by SSA countries in 2016 according to the IMF (Chapter 2 of Regional Economic Outlook, April 2018). However, there is an urgent need to continue to build capacity in debt management to leverage the use of innovative financing mechanisms, such as public private partnerships, to lessen the burden on public debt, after a comprehensive risk assessment has been undertaken. It is only when macroeconomic stability becomes entrenched and irreversible, and when borrowing are targeted for projects that are able to pay for itself, would this surge in borrowing in SSA be different. Even then, the risks still remains high as SSA countries’ exposure to increased external debt as a proportion of total public debt increases and the proportion of non-resident holders of domestic debt increases across the continent. This comes along with significant external risks and pressures from fixed income investors without a long term view of countries in SSA.

Ultimately, domestic money and debt markets would have to be further developed in SSA to reduce the new source of risks that is spreading very fast among frontier economies in SSA.

And finally, SSA countries should work to change the structure of their economies, most of which have not changed in over five decades—very important dependent with shallow foreign exchange markets which in the past have caused volatilities in foreign exchange to drive debt dynamics and made debts unsustainable. There is a view out there that targeted-industrialization would reduce imports of goods for which these countries have both comparative and competitive advantage to produce. While the debate is still ongoing as to whether in trying to integrate into the global value chain, SSA countries cannot go the way of South East Asia, that is, “development with smoke stacks”, the unique dynamics on the continent, in particular, the demographic dividends, represents both an opportunity and a challenge, depending on how it is tapped. The skills level and demographics with a lot of younger population would call for targeted-industrialization that will tap the labor intensity of the demographic dividends, which ultimately, will reduce imports and reduce the pressure on exchange rate which explains a greater percentage of debt dynamics in most SSA, in particular, Ghana.

References


CHAPTER 9

Perspectives on debt in Africa: usability and sustainability
Hanan Morsy, AFDB and Abebe Shimeles, AFDB

Abstract
Recently most African countries experienced a spike in their debt levels along with changes in its composition and terms. As a result, there is a growing fear of default and return of the HIPC spectre. These assessments largely rely on the traditional approach to debt sustainability that often ignores significant heterogeneity existing among African countries. They also miss the fact that only countries that made up 20% of Africa’s GDP received debt relief, yet the headlines marred the image of Africa as a whole. This chapter provides a different perspective by emphasizing on the role of debt as a means to leverage investment and its sustainability critically depends on the strength of the linkage between the two, which essentially is determined by how wisely debt is utilized. Based on simple analytical framework the chapter demonstrates that sustainability of debt in every country depends on macroeconomic management, cost of borrowing and efficiency of debt in accelerating growth. To that end, the conversation need to be that debt used well indeed is likely to be paid in full.

Introduction

a) Motivation of the problem
Debt has a special place in the tumultus economic history of most African countries. The debt crises of the 1980s and 1990s are grim reminders that led to the lost decades, partly due to sweeping applications of neoliberal economic paradigm, popularly known as the Washington Consensus, led by premier financial institutions, the IMF and World Bank. The carnage left behind these policies are well known and documented (e.g. Rodrik, 2006). They also gave a clear lesson to most African countries for the need to own and implement home-grown policies that fit to their specific needs. The massive debt relief that accompanied these policies are a subject of intense debate on whether they have helped consolidate African economies and hurled them into a path of sustainable growth. Today most African countries are armed with better tools to manage their macro economy that suited their specific needs. Yet, the global economy has also made qualitative leaps in the last decades that made conventional economic analysis, and the commonly accepted policy recommendations inadequate to help African countries reap the benefits afforded and mitigate the risks associated.

b) The need to change the conversation on debt-sustainability
Today, most African countries are once again confronted with the resurgence of debt distress. Recent release by IMF as of March 2018 indicated that close to 19 out of 39 low income African countries are at high risk of debt distress. Of these, 8 are already classified as having being in debt distress. The situation seems dire and reminiscent of the HIPIC (Highly Indebted Poor Countries Initiative) that led to one of the most popular debt relief efforts since the Second World War. What is in the minds of many observers is that how did we get to this point so fast after a major debt relief in modern history had been effected? It also dispels the positive narrative Africa has received in recent years where it was hailed as coming of age and in the midst of renaissance. Suddenly the headlines are replete with fear of debt crisis and talk of austerity measures that brought many countries to the brink. The social and economic cost of another debt crisis in Africa will simply be incalculable. That being said, the most important aspect on debt dynamics that has
escaped attention is the utilization of debt, which not only determines the path of sustainability, but also has the potential to leverage investment and thereby economic growth. Changing the conversation from sustainability to usability provides a foundation for understanding one of the key developmental problems of Africa.

c) Objectives of this chapter
The main objectives of this chapter are to provide a framework for analysing the dynamics of debt in Africa from the fundamental principle that debt sustainability is predicated on whether it is devoted for productive investment or consumption. That debt accumulation is faster in economies that grow at a slower pace than the interest rate accrued to repay the debt. This fundamental equation, also predicts that the maximum debt carrying capacity of a country is driven by these two factors. It is also evident that higher and stable growth prospects further reduce future borrowing cost, putting a country in a path of net asset accumulation. The lack of such path for most African countries is explained within the general framework of efficiency of investment, which itself is driven by lack of well-developed asset grade pipeline of investment projects that could incentivize the participation of the private sector.

d) Key findings and organization of the rest of the chapter
The chapter presents empirical evidence on the evolution of debt, determines the maximum debt carrying capacity for each country, the highest growth rate and borrowing cost necessary to sustain current debt. In so doing, the chapter outlines short to long term policy options that focuses more on the utilization of debt than sustainability per se. The rest of the chapter is organized as follows: section 2 presents recent trends, and composition of sovereign debt in Africa. Section 3 provides an analytical framework to understand debt dynamics and illustrates with data the conditions under which debt can be sustainable in Africa. Section 4 highlights the link between debt, investment and growth in Africa. Section 5 concludes.

Trends and patterns of sovereign debt in Africa
While the median debt to GDP ratio increased for Africa from around 35% in 2008 to 50% in 2016 (AfDB, 2018), the debt situation tends to be very different from the peak of late 1990s and early 2000 in many ways. First, the extremities observed in the run up to the debt crisis of the 1990s and early 2000 did not exist in recent periods. As can be seen in Figure 1 the debt to GDP ratio tended to be lower in 2016 for all African countries compared with 2002 including extremities that tended to influence the narrative on debt distress. Second, the current rise in debt came on the background of more resilient and stronger economic fundamentals than the one that prevailed in the 1980s, 1990s or early 2000. Evidence show that median inflation in the period 2008-2017 was at its lowest in Africa by historical standards, deficits, both current account and budgets were contained and most importantly growth in many countries was higher than 4%. Other measures of economic fundamentals also improved. This partly was responsible for rising debt as most countries in Africa begun accessing capital from the market, albeit at higher rate of interest. The shift from concessional to non-concessional loans with short maturity period strained the economies of most African countries leading to high debt-service to exports ratio.
Analytical framework for debt dynamics

To understand the process of debt accumulation, hence its sustainability, we start from a simple but powerful debt dynamics equation.

\[ D = \text{Nominal debt} \]

\[ Y = \text{GDP} \]

\[ d = \frac{D}{Y} = \text{ratio of debt to GDP} \]

\[ P = \text{G- T} = \text{nominal primary deficit} \]

\[ p = \frac{P}{Y} = \text{ratio of primary deficit to GDP} \]

\[ r = \text{real interest rate on government debt} \]

\[ g = \text{growth rate of real GDP}. \text{ Consider only} D \text{ and} Y; \text{ and imagine primary deficit is zero.} \]

The dynamics of the debt to gdp ratio \( (d) \) depend on: i. the rate at which debt (the numerator) grows which is \( r \); and ii. the rate at which gdp (the denominator) grows which is \( g \): So the ratio of debt to gdp grows as the difference between \( r \) and \( g \) or \( (r - g) \): Considering now that the primary deficit may be non-zero, the change in the debt to gdp ratio, \( \Delta d \); depends on two factors: i. how the current dynamics are influencing the growth of the debt to gdp ratio i.e. whether \( r > g \) ii. the primary deficit as a proportion of gdp, \( p \): In fact the change in the debt to gdp ratio \( (d) \) is the simple sum of these two effects: \( \Delta d = p + (r - g)d \). or more formally, \( d_t = (1 + r_t - g_t)d_{t-1} - p_t \) …………(1)

7 See AfDB (2018) and online http://home.wlu.edu/~daviesm/debt%20dynamics%20comment.pdf
So the growth of debt to GDP depends on four variables:

i. \( r \): the real interest rate
ii. \( g \): the growth rate of real GDP
iii. \( p \): the primary deficit as a proportion of GDP
iv. \( d \): the current debt to GDP ratio.

There are two cases to consider for debt dynamics. i. \( r < g \): benign. In this case the debt dynamics ensure that debt to GDP, \( d \) converges regardless of the primary deficit, \( p \): That is, \( d \) converges to steady-state debt-to-GDP ratio determined by \( \Delta d = d(r-g) \). If \( g \) and \( r \) are close then \( d \) can be very large. Further, as long as \( r < g \) then there is no need for a balanced budget i.e. the trajectory for \( d \) is stable with a positive primary deficit, \( p > 0 \): ii. \( r > g \): unstable. In this case it is necessary to run a primary surplus (\( p < 0 \)) in order for the growth in debt-to-GDP to be stable (\( d = 0 \)) i.e. \( 0 = p + (r - g)\Delta d = p < 0 \) if \( r > g \): If a government runs a primary deficit then the debt to GDP ratio continues to rise, unless the initial debt to GDP ratio is strongly negative. Figures 2a-2c provide visual description of the debt dynamics.

Figure 2:a-c: Debt dynamics various scenarios depending on

\[ \Delta d = p + (r - g)\Delta d \]

\[ \Delta d = p + (r - g)\Delta d \]

\[ \Delta d = p + (r - g)\Delta d \]
Preliminary results indicate that most African countries currently have significant debt carrying capacity if we take into account their recent economic performance. The computations, based on solution to equation (1) basically estimated the following steady-state solution of debt to gdp ratio for each country by holding each of the arguments (r, g and p) at their historical long term levels.

\[ d^* = \frac{\bar{p}}{(\bar{g} - \bar{r})} \]  

Equation (2)

The results show that for most African countries the steady-state debt to gdp ratio is much higher than the actual debt to gdp ratio indicating the possibility that if the historical trends continue, African governments can borrow more without compromising debt sustainability. Equation 2 can also be used to compute the steady state primary balance, given actual debt to gdp ratio, interest rate and growth rate. Similarly, the optimal interest rate a country could afford to sustain debt can also be computed.

Figure 3: Steady-state debt/GDP ratio and actual debt-GDP ratio

Changing the conversations

a) Debt and investment

It is evident from the preceding section that debt sustainability critically depends on the pace of growth of the economy and the terms of the loan which often is captured by the interest rate. This simple debt dynamics is lost in the broader discussion of debt sustainability denying the opportunity to bring into the negotiation table issues of the use of debt, efficiency of public investment, and ultimately the terms of borrowing that could be informed by the returns on debt. In this section, attempt is made to provide empirical evidence or absence of it on the link between debt and investment in Africa. From the basic debt dynamics equation, we note that debt stock at any period is the sum of two parts. The part that was accumulated in the previous period, and a new loan government incurs to finance current fiscal deficit, which could be the capital expenditure (public investment) or consumption. The return of debt to the government is if it leverages investment and thereby growth. If the bulk of the debt is devoted to increase public sector pay or other current expenditure, then, the growth impact would be very limited.
Figure 4 provides a simple correlation between change in external debt stock ($\Delta d$) and public investment for selected African countries for the period 2000-2016. The result is encouraging in that the correlation is positive and statistically significant. But the strength is weak. A 10% increase in external debt leads to a 5% increase in public investment. Basically only 50% of external debt incurred by African governments on the average is devoted to the financing of public investment. Now, if we take into account the efficiency and absorptive capacity of public investment, then, the potential of debt affecting growth might be very low. Therefore, the policy discourse on debt sustainability will have to put significant emphasis on when to borrow, how much and how to make use of it, instead of when it can be paid back.

Figure 4: Debt growth and investment in selected African countries: 2000-2016

Source: authors’ computations based on AfDB statistics

b) Efficiency of public investment and GDP growth

Growth theory predicts that in capital scarce, low income countries, the return to capital tends to be relatively high, thus, accelerated capital accumulation is expected to impact growth faster. However, two factors complicate this prediction. First, most African countries start with a very low capital stock, making investment choices that guarantee higher returns a very difficult exercise. The reason is the strong complementarity (externality) observed among investment projects in low income countries is normally assumed not to exist in simple neoclassical growth models. The moment this possibility is allowed, then, the return to capital or investment depends among others on the sequencing, spatial concentration and specific needs of the economy, regardless of initial capital stock. The second reason is that the absorptive capacity of large investment projects determine the efficiency of public investments. For instance, if a country undertakes bold investment programs in building dams, large scale railway and road infrastructure, the efficient utilization of these mega projects could be affected by other factors including low skilled labour, costly maintenance and other factors. Before these investments yield sufficient growth, the maturity of debt that financed them arrives and governments find it difficult to service that debt. Therefore, governments need to know these facts before they embark on debt accumulation to enhance physical capital accumulation.

This section analyses efficiency and absorptive capacity of public investment for selected African countries to determine the level of debt that they can possibly carry in order to be able to service it and also benefit from it. Recent studies have shown that (e.g Dabla-Norris, et al.,
2011), in many African countries, the efficiency and absorptive capacity of public investment is low and this section attempts to understand why and also measure the magnitude.

**Conclusions**

The chapter outlines policy choices around the following areas:

- Debt usability is much more important than debt-sustainability. Debt-carrying capacity, among others is determined by the overall economic fundamentals. Most importantly by the rate of growth of GDP and cost of borrowing. The chapter therefore advocates for aggressive pro-growth policies in the borrower countries, and access to concessional loan to make the initial transition to sustainable debt easier.

- The debt-investment link exists but it is weak. Nearly 50% of external debt in Africa is used to finance public investment and efficiency is expected to be poor partly due to large investment complementarity that exists in these economies as well as problems of absorptive capacity that is often caused by poor choice of projects.

- Thus, the chapter advocates for the creation of asset grade investment pipeline by countries that could then be prioritized on the basis of the structure of the economy and the country’s ability to effectively utilize the physical infrastructure or investment created by the debt.
PART 3: Africa: Balancing financial inclusion, stability, and security”

The following chapters are papers presented at the Global Strategy Forum conference in London on 15 May 2018.

CHAPTER 10

Domestic and global dimensions of financial inclusion in Sub-Saharan Africa
Antoinette Monsio Sayeh, Distinguished Visiting Fellow, Centre for Global Development

Opening

“Thank you for that kind introduction Lord Lothian and for inviting me to join this important conference. Distinguished Participants, Colleagues, Ladies and Gentlemen: A very good morning to all. I am most pleased and honoured to be here and to have the opportunity to supplement the discussion at the Oxford Conference with some remarks on the subject of financial inclusion in Sub-Saharan Africa (SSA). The summary just presented by Charles Enoch provides an excellent backdrop to this conference and to my remarks.

Much has been said and written about financial inclusion in the region in recent years, reflecting its leadership in the area of mobile banking pioneered by Kenya’s M-Pesa. In the 15 minutes I have I will comment on the level and drivers of financial inclusion – a critical aspect of financial development, itself an important driver of sustained growth and development. And I will consider financial inclusion from both the domestic vantage point and from the perspective of recent developments in SSA’s connection to the global financial network. I will begin by indicating how SSA compares to other regions, and then quickly summarize policies needed to improve financial inclusion. The second part of my remarks will focus on the impact of what many call “de-risking” by global correspondent banks on SSA and on action needed to safeguard the region’s access to international financial services. I will then conclude my remarks by flagging the need to strengthen political will and improve capacity development for financial inclusion.

Financial inclusion on the domestic front

What then do we mean by “financial inclusion”? The term is widely understood as expanding access to formal financial services by making them available to segments of society without it. Despite progress in financial development over the years, access to traditional financial services in SSA remains low when compared to other regions and is especially limited in fragile states. Access is particularly low in rural areas, and across all SSA country groupings – whether LIC, MIC, or fragile states -- educational, income, and gender gaps are significant.

Let me now spend a few minutes describing how both mobile banking and microfinance have begun to address these deficiencies. According to the World Bank’s 2017 Global Financial Inclusion or Findex database, adult mobile account holders nearly doubled between 2014 and 2017 to 21 percent of the population, by far the highest level worldwide. The surge was especially evident in Kenya. Policies in Kenya allowed M-Pesa to operate as a parallel payment system, with the legal system flexible to allow development of other financial
products while limiting security risks to deposits. Innovations there eventually brought access for low-income households to health insurance and other savings and lending products. And a study quoted in the 2017 Findex showed that women benefited significantly. Other SSA countries have worked to follow Kenya’s example, with 6 countries in 2014 and then 15 in 2017 having the number of mobile account holders reach 20 percent of the population. This expansion was initially concentrated in East Africa but has since spread. Indeed, the share of adults with mobile accounts now exceeds 30 percent in Cote d’Ivoire and Senegal and 40 percent in Gabon. For its part microfinance has also expanded significantly in SSA, providing savings services and small loans to the poor. According to the IMF’s April 2016 Regional Economic Outlook for Sub-Saharan African, a 20 percent per year growth in the number of borrowers and depositors resulted in 45 million clients being served by microfinance institutions in 2014. These institutions have supported financial inclusion by requiring no collateral and with a marked rural outreach. They have had a positive impact on the poor in Ghana, Kenya, Malawi, Madagascar, and Uganda, but evidence of a sustained poverty reduction impact is mixed. At 60 percent, microfinance institutions’ women borrowers reached almost twice women’s share of formal bank accounts. Despite this progress and potential however, a number of weaknesses are evident from recent developments in SSA’s microfinance institutions compared to other regions’; savings mobilization outpaces lending, and these institutions have high operational expenses, declining portfolio quality, and are vulnerable to natural disasters and Ponzi schemes.

I need not comment in much detail since Charles Enoch’s summary covered the issue, but I should conclude this segment of my remarks by stressing the positive impact that the rise of Pan African banks has had on maintaining financial services as global banks left Africa and, in the process, also fostering financial inclusion. Among other contributions, their scale of operations has enhanced competition for loans and deposits, and their clients have included underserved SMEs and individuals.

**Policies to safeguard progress in inclusion in the domestic sphere**

But these positive achievements could be endangered if they allowed for too much risk taking, especially by those not yet fully financially literate. It is therefore important to foster appropriate regulation and high quality supervision, to go hand in hand with the rapid growth. Priorities would include improving credit information systems, strengthening cross-border collaboration between home and host country supervisors, and transparent entry and exit policies. Policy makers must also closely monitor the growth and complexity of mobile banking transactions with the view to protecting scarce funds of the poorest segments of their population. And it goes without saying that reducing educational, gender, and income gaps in financial access requires steadfast implementation of policies to support more inclusive growth.

**Emerging global financial exclusion**

Distinguished participants, I will now turn to the region’s global financial inclusion. In the decade of strengthened regulation since the global financial crisis and focus on Anti-Money Laundering and Combatting the Financing of Terrorism (AML/CFT), financial institutions worldwide have sought to contain compliance costs and avoid penalties for non-compliance. Directed to “know your customer’s customer”, banks have discontinued correspondent banking relationships (CBRs) for some banks in countries with actual or perceived weaknesses in financial sector surveillance. The consequence of this so-called “de-risking” has been that trade facilitation, remittances, and other payments have been under pressure and
these countries’ connections to the global financial network – i.e. their global financial inclusion -- under threat.

What has been the extent of CBR losses in Sub-Saharan Africa? Starting from an already low base, a recent Financial Stability Board (FSB) survey shows that the region saw a loss of 15 percent of previously available CBRs between January 2011 and June 2016, the second largest loss after the Middle East and North Africa region. Fragile states like South Sudan, Liberia, the Central African Republic, and the Democratic Republic of Congo, are among the most affected.

A recent survey by the Southern African Development Community (SADC) regional anti-money laundering body found that a large number of respondent banks now depends on less than two correspondent banks for processing of more than 75 percent of their transactions. The more significant extent of CBR loss in SSA fragile states is illustrated by the broad-based withdrawal in my own country Liberia. The IMF’s March 2017 report on “Recent Trends in Correspondent Banking Relationships” states that all commercial banks had lost at least one CBR since 2013, with the banking system average loss of 46 percent of CBRs and the most affected banks losing 78 percent of their CBRs. Rather than the 6-month notice usually provided for ending CBR relationships, notice was now only overnight, and the central bank itself saw some of its CBRs terminated in 2014.

So some countries have indeed been hit hard. But to date the overall macroeconomic impact of CBR withdrawals in the region has been minimal as affected countries have generally found viable alternatives of indirect or nesting CBR relationships. Having said that, the inadvertent consequences of well-intentioned international regulation and the potential negative longer-term impact of these developments on financial inclusion, growth, and development in the most severely affected countries are of major concern. The short-term alternatives countries have found are invariably more costly, with the risk of an increased volume of transactions turning to informal channels. In addition to more costly remittances, aid flows through non-profit organizations are being impeded in some very needy countries. And increased financial frailties and concentration have emerged in these countries, which may in turn undermine financial stability, financial inclusion, and growth prospects.

**Policies to safeguard global financial inclusion**

So, how can these potentially adverse macro-financial consequences be averted? Let me highlight three sets of action at the individual country or bank level, beyond more and better use of technology. AML/CFT concerns were prominent in the reasons for CBR reduction in both Liberia and the SADC regional anti-money laundering body’s survey I referred to earlier.

Addressing gaps in affected countries’ AML/CFT framework to align them with Financial Action Task Force (FATF) guidelines and fully implementing this framework is therefore the first priority. Second, countries which could be severely affected should also formulate contingency plans for use in the event of total CBR withdrawal. Third, steps also need to be taken to enhance respondent banks’ risk management capacity, strengthen tools for due diligence by correspondent banks, and improve communication between correspondent and respondent banks. Beyond the individual country/individual bank level, corrective steps are also critical in the global sphere. It is fair to say that significant attention has been paid to the CBR issue over the past three years, with more research, data gathering, and technical assistance by international institutions, as well as clarification of expectations by regulatory bodies and home country supervisors. But more action is needed. Continued efforts by home country supervisors to clarify regulatory expectations and ensure consistent implementation
and communication of those expectations could help calibrate correspondent banks’ responses. And more opportunities for voicing of the region’s observations and concerns at Basle Committee on Bank Supervision, FSB, and FATF deliberations would be helpful.

**Strengthening political will and improving capacity development for financial inclusion**

I will now conclude my remarks with a few words on the two most critical elements for the way forward: the political will to strive for better regulation and supervision and improving the effectiveness of capacity development support. There is clearly the need for some international standards to be more closely adapted to the structural characteristics of SSA financial systems and economies, and these challenges should be taken on by global regulators without delay.

Yet equally or more importantly, domestic efforts are needed to create a better financial system. These require steadfast implementation of improvements in supervision and regulation and, with it, reduced rents earned in a non-transparent and distorted financial sector. For this to happen, the political will to act and full ownership by domestic authorities will be critical. Without them neither domestic nor global financial inclusion can be achieved.

Political will is typically weakest in fragile states, which are most lagging on domestic financial inclusion and most adversely affected by CBR losses. More outreach to educate the public on the benefits of financial inclusion – and on the need to safeguard remittance channels that are so special to fragile states – can help build stronger political will. And work by both policymakers and international partners to make much better use of appropriate technical assistance and training would ensure the essential capacity wherewithal to take forward the financial inclusion agenda.”
CHAPTER 11

*Trends, challenges, implications and the way forward*

Samuel Munzele Maimbo

**Introduction**

By 2050 the global population is expected to have grown by around 2.2 billion people. More than half of this growth will occur in Africa, which will account for the highest population increases in the world, with an additional 1.3 billion people on the continent (UN DESA 2017).

Significant efforts to accelerate development in Africa are ongoing, but these efforts are hampered by low investments in the region or investments that are not efficiently channeled into productive industries. Access to long-term finance is an essential facilitator of economic growth in the region. Such access will also be essential for human development, sustainability, inclusion, and achieving the Sustainable Development Goals (SDGs) in Africa.

The overarching goals of this study are to (1) present the current data and trends of finance in Africa, (2) evaluate the underlying factors that explain why finance has remained challenging, (3) explore the relevant implications and responses to these constraints by various actors, and (4) consider what practical actions can be taken to move forward.

Solving the long-term financing gap requires multiple actions and a sustained effort across short-, medium-, and long-term horizons. Encouragingly, the data reveal the extent to which Africa’s financial institutions—banks, regulators, investors—are shaping new opportunities and fostering competition to encourage investment. More pan-African banking, regional integration of capital markets and African cross-border investment are some of shifting finance trends on the horizon.

Although institution building and financial sector capacity building are long-term objectives, immediate market solutions and innovations can overcome some macroeconomic and institutional bottlenecks. Some of these innovations present opportunities—such as mobile money accounts—that have already shown promise in the region. These opportunities should be leveraged alongside efforts to build an enabling environment, where access to long-term finance will follow.

The study concludes that the risks of investments in Africa are overstated, while significant investment opportunities exist that can be unlocked by addressing longstanding bottlenecks. This effort of significantly increasing investments in Africa can be accelerated by addressing data gaps; harmonizing Africa’s investments in registration and identification systems around common, interoperable standards; and addressing licensing, regulatory, and supervision of financial services. Failure to secure these opportunities and propel sustained, long-term finance and access to financial services could cause Africa to suffer disproportionately from the downside risks of the uncertain future.

**The state of finance in Africa: The glass half empty**

Whether the state of finance in Africa is seen as positive or negative depends a great deal on perspective and on what is being considered. It is fairly easy to see the state of finance in Africa as a glass half empty. This perspective takes in the low levels of foreign direct investment (FDI) inflows and similarly low levels of access to finance for small and medium enterprises (SMEs) and for households.

a) **Low levels of investment in the region**
Africa exhibits the lowest FDI inflows of any developing region. Investments in Sub-Saharan Africa, for example, accounted for just 1.6 percent of all global FDI in 2016 (World Bank 2016c). FDI into Africa reached its highest point of the last decade in 2008, with inflows to the region of US$60 billion, and its lowest point two years later, with inflows of US$44 billion in 2010, following the financial crisis. Since then, FDI has remained relatively stable. In 2016 FDI inflows hovered at around US$51 billion, a small decrease from the growth experienced in the years immediately following the financial crisis. There is some regional variation when taking a closer look at recent FDI data. In 2015–16 gross FDI inflows declined in 32 of 46 countries (with a median decline of 1.8 percent of GDP). The other 14 countries experienced a median increase of about 0.7 percent in the ratio of FDI inflows to GDP (World Bank 2017a).

A look at long-term historical trends shows that, since 2000, FDI in the continent has remained relatively flat compared with investment in Latin America and Asia, which have experienced a greater increase but also greater volatility.

FDI is also not distributed equally across African sub-regions and countries. Recent data from 2016 reveal that 53 percent of all FDI was concentrated in six African economies: Egypt, Nigeria, Angola, Ethiopia, Ghana, and Mozambique. In contrast, South Sudan and The Gambia and received the least FDI and experienced negative FDI inflows, at −US$17 million and −US$1.5 million respectively (World Bank 2018c). A sub-regional breakdown shows that over the past almost two decades, Southern and North Africa had a greater volume of FDI than the other sub-regions. That gap has only grown since 2000. Both Southern and North Africa sub-regions have powerhouse economies that increase the regional averages—Egypt in North Africa, and Angola and South Africa in Southern Africa. East and Central Africa have experienced the lowest volumes of FDI in the region. Africa has not seen the boom of Asia or the increases experienced in Latin America over the past decade. On the upside, although FDI flows seem concentrated in a few specific sectors, there is growing sectoral diversity, particularly in the services industry.

FDI in Africa is concentrated in a few key sectors. In 2015–16, 58 percent of all announced greenfield projects were in three sectors: electricity, gas, and water (22 percent); business services (19 percent); and construction (18 percent). FDI in agriculture, cited by 63 percent of African investment promotion agencies as one of the most promising industries for FDI, was nominal in the same period (UNCTAD 2017).

b) **Low levels of access to finance for SMEs**
Access to finance continues to be one of the greatest constraints for the growth and operation of firms in Africa, particularly SMEs. Bank credit to the private sector, as measured by percent of GDP, is also lower in Africa than in the rest of the world. The World Bank Enterprise Survey cites that 39.2 percent of firms surveyed in Sub-Saharan Africa see access to finance as their top barrier to growth—a higher percentage than in any other region.9

Small firms have less access to lines of credit than large firms. A sample from nine African countries in the Enterprise Survey database illustrates the variation in financial access across

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8 This is also true when taking a long-term look over the past decade. Investments have been concentrated in specific economies: Angola, Egypt, Nigeria, Ghana, Ethiopia, Mozambique, Morocco, and South Africa (World Bank 2018c).
9 The Enterprise Survey database is available at http://www.enterprisesurveys.org/data/exploretopics/finance#--13
countries and firm size: for example, 42 percent of firms have access to credit in Togo, but less than 4 percent of firms have this access in Guinea. Furthermore, there is variation across countries regarding firm size and financial access. The gap between firm access to credit for all firms versus for small firms varies greatly across countries on the continent. Semi-formal firm borrowing is more common in Sub-Saharan economies than in other developing regions: between 11 and 16 percent of adults surveyed across six Sub-Saharan countries have borrowed from savings clubs and credit associations,¹⁰ as opposed to an average of 3 percent of adults across other developing regions.

Underdeveloped financial infrastructure constrains access to finance, particularly long-term finance. Financial infrastructure encompasses the depth of the financial system and its intermediating capacity, supportive regulation, and supervisory practices. Studies find that firm debt maturity is heavily influenced by the depth of the financial and banking system—even more than it is by firm characteristics. The World Bank examines private credit to GDP as one proxy for determining financial intermediation and financial system depth, and finds that the depth of Sub-Saharan financial systems remains the lowest across all regions (World Bank 2015a).¹¹ The constraining intermediating capacity of banks has contributed to low firm financing. Variables such as lack of collateral, proof of creditworthiness, narrow cash flows, high-risk premiums, and transaction costs are cited as operating constraints (Otchere, Senbet, and Simbanegavi 2017).

Firm financing data are nuanced and it is difficult to assess the long-term trends for firms since there are data gaps across countries and sub-regions. More disaggregated data on the supply and demand of firm financing are needed. What the research does say is that the focus on firm financing for banks has been highly concentrated on lending to high-margin clients (older, larger firms) and that SMEs remain the “missing middle,” unable to attract many formal financing instruments (IFC 2016).

Regulatory regimes could constrain financial flows and access in Africa. The research cites restrictive prudential regulation (connected lending, liquidity management, capital adequacy, transparency/reporting, and so on) as one of the major underlying factors of poor access to credit. While African banks are gradually adopting Basel rules, it is too early to study their long-term effects on finance, although some studies point to the possibility that these regulations promote short-termism through the high capital allocation requirement. More stringent requirements for bank entry (including limits on foreign bank entry) are also negatively correlated with bank lending (World Bank 2015a).

c) Low levels of access to finance for households
Data on household finance in Africa reveal low rates of adults with accounts at formal institutions and long-term financial products (for example, health and home insurance). Data from 2017 show that more than one-third (43 percent) of adults in Sub-Saharan Africa have an account at a formal financial institution, lower than the global average of 67 percent and the lowest among emerging economies. That does show an improvement over 2011 data, however, when only 23 percent of adults had an account at a financial institution (Demirgüç-Kunt et al. 2018).

¹⁰ These six countries are Cameroon, Kenya, Liberia, Malawi, Sierra Leone, and Uganda.
¹¹ Some large emerging economies in North Africa and South Africa are the exception. South Africa, for instance, has a higher level of financial development than certain advanced economies such as New Zealand (IMF 2016).
Trends in household financial access are changing rapidly in Africa, where mobile money accounts have driven growth in overall account ownership in the past several years. Mobile account ownership rose from 12 percent to 21 percent (Demirgüç-Kunt et al. 2018).

Mortgages remain limited and underdeveloped, despite Africa having the world’s fastest urbanization rate. In spite of the upward trends in this area, mortgages to GDP hovers only at 3 percent (compared to 70 percent in developed economies) (Nguena, Tchana, and Zeufack 2015). Low penetration rates are also observed with health insurance. In Sub-Saharan Africa, for example, insurance penetration rates are low, at 2.9 percent. Low penetration rates are also observed with health insurance. In Sub-Saharan Africa, for example, insurance penetration rates are low, at 2.9 percent. Household finance is changing rapidly. For household finance, the data find that Africa has the lowest percentage of adults with an account at a formal financial institution. However, if other variables of financial access are included, the picture becomes very different. Behind these low numbers there is intra-regional variation. Banking penetration remains below 20 percent in most of Eastern Africa, but is over 40 percent in South Africa. As discussed earlier, the explosion of mobile money accounts is also changing the landscape of account ownership in Africa. Sub-Saharan Africa is the region with the highest mobile money account penetration, with 21 percent of the adult population having a mobile money account. Of those with a mobile money account, 50 percent had an account at a financial institution as well. The highest penetration rates are in Kenya (73 percent), Uganda (50 percent), and Zimbabwe (50 percent) (Demirgüç-Kunt et al. 2018).

The state of finance in Africa: The glass half full

When considering activity in capital markets, albeit nascent in some countries, and taking into account both an improved understanding of risks in the African context and the effect of new, emerging technologies, there is much to celebrate in the state of finance in Africa.

a) Increasing capital markets activity

African capital markets are growing and becoming more diverse. The market capitalization of stock exchanges in Sub-Saharan Africa grew by only 4 percent in the last decade, but it is now accelerating at closer to 19 percent. Over the past five years, there have been 134 initial public offerings (IPOs) by African companies on both African and international exchanges, raising US$9.1 billion—a 37 percent increase in capital raised over 2012–16. Over the same period, there have been 385 follow-on offerings by African companies, raising US$43.6 billion on both African and international exchanges. This trend is expected to gain momentum in the coming years (World Bank 2016a). Businesses in sectors such as telecommunications, consumer goods and services, financials, and health care continue to form a significant component of African equity capital markets activity, reinforcing the growth trend away from the resources sector (PwC 2018). None of the top 10 IPOs in 2017 were companies in the resources sector.

Africa has experienced substantial growth in pension assets over the last five years. In much of Sub-Saharan Africa where pension systems are older, growth rates have been lower, ranging between 8 percent and 18 percent over the previous five years. Assets in East Africa have grown more than 20 percent on a consistent basis, overshadowed only by Nigeria, which has seen

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12 The proportion of the population who are estimated to be able to afford a prudent mortgage is around 16 percent. Most low- and moderate-income households have access only to an informal housing sector.

13 Data are based on AXCO Global Statistics, Insurance Penetration Ranking 2016 (see https://www.axcoinfo.com/media/5455/03_global_statistics.pdf and includes data based on prior 2015 information, preliminary and forecasted. Insurance penetration is classified as total written premiums as a share of the country’s GDP. South Africa has highest penetration rates at around 12 percent, whereas Guinea has a rate of 0.04 percent.
growth between 25 percent and 30 percent. These trends will continue as this young continent moves toward increased coverage and more inclusive and comprehensive systems. Kenya and Nigeria have opened their pension industries over last 8–10 years, with Ghana doing the same over the past few years and, more recently, Tanzania and Zambia. In 2014, Sub-Saharan Africa had 24 stock exchanges, 19 of which had automated trading systems in place. In the past five years, six countries implemented new central securities depositories. Similarly, insurance penetration is expected to grow significantly across all African markets over the next five years. The overall increase in assets under management of African insurance companies from 2012 to 2018 is expected to be 38 percent.

Africa is emerging as one of its own key investors. African multinationals are becoming prominent investors in the region. 2015 and 2016 together saw US$20.1 billion of announced greenfield FDI projects from African firms as investors (UNCTAD 2017). African pension fund capital has reached US$330 billion and is growing rapidly. By 2018, the increasing adoption of insurance had resulted in insurance investment of around US$279 billion.

Securities markets can facilitate flows of long-term finance and risk finance. Although trends show that these are growing, their level of capitalization is low. With the exception of the Johannesburg Stock Exchange, most African countries have a low level of equity trading and are constrained in raising new capital. However, the data from earlier years show that the capital market space is growing. This is in part due to the size and growth of domestic companies on the continent (there are an estimated 700 companies with annual revenues in excess of US$500 million, but only 40 percent maintain a listing). New entrants to the markets are anticipated in the medium term, which will help deepen the sector.

b) Improved understanding of risks
A common notion related to investments in Africa is that risk (whether actual or perceived) has deterred investors from investing in the region. However, many risks in Africa—such as the risk inherent in the political environment, currency risk, and so on—are shared across other developing regions and in some developed economies. Is Africa an outlier in terms of actual risk and perceived risks?

Data show that investors are overestimating the political risk profile in Africa. For example, a recent study conducted by Zurich’s Credit and Political Risk Program examined all political risk claims from 1997 through 2017 and showed that only a small fraction—7 percent—of all claims originated in African countries, and 60 percent of these were claims from Libya (Zurich 2017).

Risk perception for loan defaults is also overestimated. A recent Moody’s study examines the default and recovery performance of unrated project finance bank loans (Moody's 2017). Projects originating in Africa had one of the lowest default rates of all regions. Only 3.72 percent of African projects defaulted 10 years from financial close, much lower than the 12.28 percent default rate in Latin America (the region with the highest project default rates), and lower than the rate in developed economies.

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14 The most dominant sectors in which African firms invest are construction and business services, similar to sectors attractive to foreign investors. Greenfield announcements in 2015 by Africa as investors came to US$11.5 billion; in 2016 this was US$8.6 billion.
15 Some caution should be used in interpreting the claims data, since data on total exposure were not available.
16 The data set accounts for 6,389 projects, or 62 percent of all project finance transactions during the period 1983–2015.
Although risk is overestimated, risks do exist. One emerging risk specific to Africa is that posed by increasing high debt levels and credit risk. Debt levels have been increasing in the past several years: 25 Sub-Saharan African countries have 50 percent public debt as a percent of GDP (Brookings Institution 2018). Since the beginning of 2017, S&P has downgraded four Sub-Saharan countries—Gabon, Namibia, the Republic of Congo, and South Africa. This downgrading has the potential to affect long-term borrowing or borrowing at preferential rates. In addition, Mozambique and the Republic of Congo are facing repayment problems that might ultimately affect their borrowing outlook (World Bank 2017a).

Increased focus on investment project preparation and standardization in Africa contributes to better assessment of risks. Better-prepared projects supported with standard documentation improve the risk perception of investors. Significant initiatives are underway that target Africa:

- **The Infrastructure Consortium for Africa (ICA)** is a platform that facilitates infrastructure development in the water, transport, energy, and information and communication technology (ICT) sectors through both regional programs and country-specific initiatives.

- **The Project Preparation Facilities Network (PPFN)** is a network of funding facilities and institutions dedicated to developing sustainable infrastructure in Africa by improving project preparation and working to increase the number of viable, well-prepared, investment-ready infrastructure projects.

- A sector-specific solution is the World Bank Group’s [Scaling Solar](#) program, which brings together a suite of services under a single engagement aimed at creating viable markets for solar power in Africa.

- South Africa is an example of an African country that has had success with the standardization of infrastructure contracts that make use of public-private partnerships. South Africa’s manual on public-private partnerships is one of the world’s first in this area.

c) **Emerging new technologies**

Although finance trends in Africa present the view that progress is slow, new technology is one underlying factor that is changing the financial access landscape. Several technologies have been shown to provide greater access to finance to the unbanked and small businesses and to improve access to banks and efficiency of financial transactions.

Mobile technologies are altering the landscape of financial inclusion. Investors and enterprises are leveraging the large area coverage of mobile networks and key mobile services—such as messaging, mobile money, and machine-to-machine (M2M) networks—to deliver scalable and commercially viable financial services (GSMA 2017). The effect is that the gap between formal banking services and mobile money services as the basis for accessing finance is widening. For instance, 43 percent of adults in Kenya and 92 percent of adults in Sudan who report using mobile money in the last 12 months do not have a formal account.

Fintech technologies such as blockchain also have the potential to remove intermediaries in transactions, enabling the provision of new financial services and reducing transaction costs. Although still in its infancy, distributed ledger technology–based approaches may help longstanding finance bottlenecks in Africa for household finance such as identity management and land titling. There are already first-mover countries—such as Senegal, South Africa, Ghana, Kenya, and Nigeria—that have adopted policy schemes around digital currencies (IFC 2017).
These technologies also come with some constraints. Technologies, like other service delivery tools, must be harnessed in the right way to be effective. The backbone of both mobile banking and new fintech technologies is the ICT and broadband infrastructure supporting their delivery. Governments must balance the priorities of ICT investment with other social investments, and efforts still need to be made to attract private investment in order to expand greenfield sites to rural and underserved regions in Africa. Furthermore, the importance of human capital, particularly as it relates to the growth of new blockchain enterprises and use, cannot be overstated. The region needs human capacity not only to channel this technology in the right direction, but also to know how to regulate it and mitigate any risks.

Implications for financial system actors in Africa

These positive and negative views of the state of finance in Africa have some implications for financial system actors at all levels across the continent. Among these actors are regulators, development finance institutions (DFIs), private sector stakeholders, and households.

a) Regulators

African regulators are challenged to improve risk management and governance to strengthen their financial sectors, while at the same time enhancing financial broadening and inclusion (Otchere, Senbet, and Simbanegavi 2017). There are signs of regulations becoming tighter in some respects and of continuing liberalization policies in other respects. It is difficult to predict in the long term how these changing regulations will affect the financing landscape.

On the positive side, the regulation landscape in Africa has also been dynamic and innovative, responding to the specific needs of the region. In the World Bank’s Doing Business 2018 report, Sub-Saharan Africa instituted 83 reforms, the highest number of reforms of all countries in the sample for the second consecutive year. One of the effects of these reforms is to increase financial access for domestic firms. For example, South Africa, Democratic Republic of Congo, Equatorial Guinea, and Niger all instituted reforms to streamline procedures to start a business. Regulators are responding to new trends in the horizon; some of their responses concern how to regulate mobile money while protecting customer rights. Furthermore, they are also responding to the growth of regional economic integration by determining how to regulate pan-African banks and regional stock exchanges. Countries in East Africa, for example, have begun harmonizing supervisory data and practices to further integrate the economic community. These small examples highlight some of the regulations that move to provide more financial access (IMF 2017).

b) Development finance institutions

DFIs, such as the IFC, have worked on several different fronts to stimulate an increase in private finance in Africa. They have also worked to fill the financing gap by investing in projects and sectors where commercial investors do not because of higher perceived risks. They seek to encourage private investments by de-risking individual country project risk, solving upstream regulatory issues, and creating investment products (such as insurance and standardization) that let investors feel safe, while also encouraging adoption of environmental, social, and governance standards (IMF 2018).

DFIs, which often play the role of first movers, are testing new models and can help bring successful ones to market. One example is a World Bank project that is working to increase firm finance through blockchain. The project works with a South African company called Sun

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17 The category with the most reforms (22) have been on dealing with construction permits.
Exchange on peer-to-peer solar equipment leasing. The company enables anyone to buy remotely located solar cells and then earn rental income from them. Assets are recorded on the blockchain and income is paid in crypto-currency. The approach enables members of the Sun Exchange to earn income from their investments in providing solar power to urban and rural communities and industries in Africa (Sun Exchange 2018).

As a response to the vast needs of long-term finance, DFIs are urged to diversify their interventions. A recent World Bank Group report on long-term finance finds that direct interventions can be successful only if the institutional problems and market failures are addressed as well. The report urges DFIs to help shape policy agendas for institutional reform and to structure long-term financing projects that allow private lenders and institutional investors to participate while reducing project and credit risk (World Bank 2015a).

c) Private sector stakeholders
As previously discussed, obtaining finance is listed by African firms as the top constraint to growth. The intermediating capacity of banks is weak, and banks have been known to lend at short-term maturities and to a small subset of companies. Although there have been various government SME finance initiatives, such as interest rate subsidies, directed lending, and guaranteed funds, there is not much evidence that they have succeeded in improving long-term access to finance for SMEs (Quartey et al. 2017). The implications are that firms (especially SMEs) often look to nonbank institutions (such as leasing institutions) and/or the informal sector to obtain financing.

Improvement in the credit environment is one concrete way to increase access to firm finance. Difficulty in assessing creditworthiness, as a consequence of poor-quality information and data, is a major obstacle for African firms. Improving the information sharing between credit bureaus and strengthening credit rating agencies and risk assessment departments so they conduct more effective risk screening of borrowers is one way to improve firm lending. So is changing collateral structures and usability of credit collateral. The government of Nigeria considers this a top priority for firms. With support from the World Bank Group, the Central Bank of Nigeria recently established the National Collateral Registry and is currently developing a modern credit reporting system (World Bank 2017c).

Capital market actors and institutional investments are changing the landscape to a context suitable for Africa. In the Francophone Central Africa region, the member countries of the Economic and Monetary Community of Central Africa (CEMAC) took steps toward further regional integration in late 2017, with an agreement to combine Cameroon’s Douala Stock Exchange (DSX) and the Bourse Regionale des Valeurs Mobilieres (BRVM). This would help build a more liquid and efficient market in the CEMAC region, similar to that of Francophone West Africa’s BRVM. There are also signs that some capital market actors are prioritizing SME finance to offer new equity financing options for companies. For example, the Rwanda Stock Exchange (RSE) started the small and medium enterprise market segment (SMEs) in 2018 (Byumvuhore 2018). The SMEs allows Rwandan SMEs to be exposed to a vast range of international investors, including African diaspora investors.

d) Households
Household finance structures in Africa are dynamic and evolving. As illustrated in the previous section, there is a demand-side gap for household finance in many African countries. The result has been that many adults are unbanked and uninsured. However, household finance is one of the most rapidly changing areas of access to finance in Africa. It is evolving more quickly than firm finance, for example, as a result of mobile money services. Mobile money products have expanded in part because unbanked customers were no longer constrained by barriers such as
physical proximity to a banking institution, which has been one of the main barriers to financial inclusion in Africa. This rise of mobile money services is one example of an organic market evolving because the demands for household finance are not being met.

In the area of household insurance products, micro-insurance is also rapidly expanding to provide customers with different types of mortgage models using sometimes advanced technologies. Micro-insurance is a “fast changing space” in the insurance sector, designed to offer insurance access to low-income populations (University of Cambridge Institute for Sustainable Leadership 2015). A study from Lloyds predicts that the micro-insurance market could cover some 1 billion policyholders in the next 10 years (Lloyds n.d.). The Financial Times cites it as the place where “the greatest innovation and disruption is emerging,” particularly in the Africa region (Aglionby 2016).

The way forward

No single solution can increase long-term finance in Africa; multiple actions on many fronts are needed. This section focuses on three areas that could have broad impact: improving data, leveraging technology for identification, and supporting the emergence of infrastructure as a financial asset class.

a) A data revolution in Africa

At a time when high-quality data and big data are fueling artificial intelligence, risk assessments, and investment decisions, there is a risk of a widening the gap in data quality, coverage, and accessibility between Africa and advanced economies. On a positive front, the increasing use of mobile phones is boosting access to finance through mobile banking platforms and identification systems.

Unreliable, incomplete, or inaccessible data in Africa is a significant obstacle to greater investments and access to finance. Better data on risk and asset performance are needed by private investors in infrastructure—especially in emerging markets—to better asset allocation models. A joint report by the African Union, Economic Commission for Africa (ECA), African Development Bank (AfDB), and the United Nations Development Programme (UNDP) found severe data limitations in Africa, including for SDG 9, to build resilient infrastructure, promote inclusive and sustainable industrialization, and foster innovation (UN ECA 2017). In the absence of better and more accessible data, investors are likely to overestimate the financial requirements of the project and systemic risk of investments in Africa. Sharing risk metrics by stakeholders in potential transactions could help reduce information asymmetries.

High-quality data underpin all financial transactions. These data are the engine that powers financial systems. Open and easily accessible data support transparency and build investor confidence in markets. High-quality, accessible, open (freely available) data are needed to support all dimensions of financial systems: rating agencies need high-quality data to assign ratings; investors need these data to appraise risks and allocate investments; lenders, firms, and households need credit information to reduce their respective information asymmetries; and public policy institutions need data to design and implement policies and programs that support financial development and robust and inclusive economic and social policies.

Demands for standardized, high-quality data that provide more complete coverage, openness, and real-time information are increasing. Rising expectations of investors, financial managers, and policy makers are driven by the increasing use of technologies that rely on data to support trading, investment decisions, and risk assessments. Furthermore, investment managers in advanced economies have become accustomed to real-time data to track investments and project performance. Meanwhile, reporting requirements for banks have become more
stringent, responding to international regulations on reporting—such as those provided in the Basel III reforms. The growing burden of financial reporting has created a disincentive for financial service providers to do business in smaller and more remote markets. To combat this disincentive, in August 2014 UN Secretary-General Ban Ki-moon called for a data revolution to support delivery of the SDGs. The SDG framework provides the political momentum for Africa to make great strides in improving the quality of the data needed to encourage greater investments and access to finance.

**Recommendation:** Speedy acceleration of efforts by governments is urgently needed to adopt open data principles and leverage technologies that facilitate production, distribution, and access to data. African central banks should emphasize better data collection and data transparency.

**b) Identification: Leveraging new technology for financial access**

Difficulty in proving one’s identity is a major impediment to access to financial services. The ability to prove one’s identity can be thought of as a fundamental human right. Globally, the World Bank Group estimates that 1.1 billion people in the world, or one in seven people—mostly in Africa and Asia, and disproportionately affecting children and women from poor rural areas in those regions—are unable to prove their identity. Although 85 percent of unbanked adults in developing economies report having government-issued identification, only 56 percent of adults in Sub-Saharan Africa report having this (Demirgüç-Kunt et al. 2018).

The SDGs recognize the global target of providing legal identity for all by 2030. Target 16.9 of the applicable SDG is to “provide legal identify for all, including birth registration” by 2030. Providing everyone with free or low-cost access to a widely accepted, robust identity credential is also an important enabler for the attainment of many other SDG goals.

Digital identity technologies are supporting the creation of bank accounts for the unbanked, enabling access to financial services. Advances in digital and biometric identification technologies—which can now use mobile phones to verify identity—and the rapidly declining costs of technology and implementation create the opportunity for Africa to leapfrog traditional paper-based approaches and build strong and efficient identification systems on a large scale.

The World Bank Group’s Identification for Development (ID4D) initiative is taking a systematic approach to creating identity. Launched in 2014, the ID4D supports progress on the Identification agenda, as well as the Universal Financial Access 2020 agenda’s goals to ensure that, by 2020, adults who are not currently part of the formal financial system are able to have access to a transaction account to store money and to send and receive payments. Under the ID4D initiative, an ongoing regional project for West Africa is seeking to ensure mutual recognition of IDs across countries. It is the first World Bank Regional Operation on Identification that is seeking to set the foundation for national ID systems with mutual recognition and the capacity for authentication across the Economic Community of West African States (ECOWAS) region. Country diagnostics in Africa have been conducted in Botswana, Burkina Faso, Cote D’Ivoire, Ethiopia, Guinea, Kenya, Liberia, Madagascar, Morocco, Namibia, Nigeria, Rwanda, Sierra Leone, Somalia and Zambia.

**Recommendation:** Proving identity is a prerequisite for access to finance and is an enabler of other SDGs. The World Bank together with the international community should accelerate progress on Target 16.9 in Africa through the ID4D initiative. Progress can continue to be made by harmonizing Africa’s disparate initiatives and siloed investments in registration and identification.
identification systems around common, interoperable standards, which can support access to finance within countries as well as support cross-border trade. In addition to improving access to finance, stronger identification systems could reduce the costs of access to finance and enhance service delivery across boundaries, supporting regional integration.

c) Financial services and developing new financial instruments

Signs indicate that the financial system is evolving and deepening with better market competition. Pan-African banks in the region (cross-border banking) have been expanding, capitalizing on the retrenchment of European banks, which have been dominant historically (World Bank 2018b). The growth of these banks offers an opportunity for financial deepening as well as improved competition and efficiency in the banking sectors (IMF 2015). Some countries are seeing this competition increase lending opportunities to SMEs. In Mali, for instance, because of new banking entrants in the market, lending to the largest 50 borrowers has declined from 60.0 percent to 39.4 percent of total lending, with SMEs seeing a larger share (World Bank 2015b).

Building on Africa’s leadership in innovative financial services can be delivered through mobile technologies. The development of mobile telephone–based systems has helped to incorporate a large share of the population into the financial system, especially in East Africa (Gulde-Wolf 2016). Yet a large untapped potential exists in this area in other countries; the development of this potential can compensate for some of the infrastructure and other shortcomings that most countries face. There are opportunities to build on Africa’s leadership in mobile financial services, including extending branchless banking.

Credit unions in Sub-Saharan Africa also play an important role in broadening access to finance. Working with credit unions (savings and credit cooperatives, or SACCOs, in East Africa) to help them develop products is crucial to increasing access for households excluded from the formal banking sector. A mix of technical assistance and financial incentives can be used to develop new products for the unbanked populations. Furthermore, bank managers can be trained and incentivized to underwrite informality.

Microfinance has also grown rapidly. It provides much-needed services to customers at the lower end of the income distribution. Untapped potential remains in differentiated microfinance loans, including those that focus on women entrepreneurs, education, green energy, and smallholder farmers, among others.

Affordable housing remains limited in Africa, while demand is skyrocketing and costs are high. Well-designed and affordable mortgage products that are tailored to meet the needs of all income groups are in demand. Developing and deepening resilient and affordable housing finance markets that are accessible to the lower- and informal-income and middle-income households would greatly contribute to Africa’s sustainable economic growth.

The development of infrastructure is critical to economic growth and social well-being. As such, securing the funding needed to support the global infrastructure sector—currently in the trillions of dollars—is a key issue for governments and policy makers. Fiscal constraints have limited public investment in recent years; therefore private sector finance needs to be mobilized and crowded-in to fill the finance gap.

Because of the long-lived nature of these assets, debt capital plays an important role in financing infrastructure. Evidence increasingly shows that institutional investors are interested in infrastructure debt, but hurdles remain to overcome to scale up and mainstream infrastructure investment. For a tradeable infrastructure debt asset class to emerge, standardization in product development, financing, reporting, and disclosure requirements—such as environmental, social, and governance factors—is critical.
**Recommendation:** Regulators and financial service providers need to work together—leveraging financial and mobile technologies—to develop financial products and services that are convenient, efficient, and accessible. Households need to feel confident in the available financial services to encourage increasing savings rates and reduce levels of informal financial transactions. These steps are critical for a transparent, inclusive, and efficient financial system that can provide finance for business and mortgages for homes, and to support investments in professional development, education, and health.

**Conclusions**

The analysis in this study points out the changes that two opposing trends are bringing to the current state of finance in Africa. The conservative, conventional or traditional trends include institution-based regulations that do not provide what is needed, standardized product offerings that do not reflect the reality on the ground, the influence of foreign banks from outside the region, and the obstacles presented by brick and mortar financial services. The more open, experimental or modern trends, on the other hand, are evidence of the usefulness of service-based regulations, the multitude and diversity of client-centric products now on offer in the region, the presence and effectiveness of foreign banks from within the region, and evidence of growing branchless financial services.

To take advantage of the open, experimental or modern trends, the study has ended with recommendations for ways to speed and facilitate improving data, to leverage technology for identification, and to support the evolution and deepening of the financial system by building on Africa’s innovative financial services and mobilizing the private sector to boost infrastructure, among other elements.

**Bibliography**


CHAPTER 12

‘Africa: Balancing Financial Inclusion, Stability & Security’

Rt Hon. Sir Stephen O’Brien KBE

Under-Secretary-General for Humanitarian Affairs & Emergency Relief Coordinator, United Nations (2015-2017); Parliamentary Under Secretary of State for International Development (2010-2012); Prime Minister’s Special Envoy to the Sahel (2012-2015)

“Thank you very much indeed, Michael (as a former colleague of the House of Commons, I think I am entitled to call you that!). Lord Lothian, you have been a tremendous leader of Global Strategy Forum and I know the significance it is playing in contributing to very important conversations and thinking in public policy and development. It is a delight for me to be back, particularly in the light of my experience, which most recently has been as the UN’s Under-Secretary-General for Humanitarian Affairs and the Emergency Relief Coordinator. But having previously been the UK’s Sahel Representative and a DFID Minister in the political sphere and before that, an industrialist, I have a span of those things that contribute to making decisions.

Listening to our contributors so far, who have been very much focused on the title, ‘African Finance, Opportunities And Challenges’, I am going to be focused most on the challenges, because my experience of crisis, particularly from conflicts and how you seek to manage that, is that it has a major effect on the confidence of bankers, financiers, and nations themselves, to be able to invest and take a long enough term view to go forward.

I am particularly focused on not calling it ‘Africa’, but calling it the 55 countries of Africa, because they are all different and they should not be lumped together. Too many people say ‘Africa’ as though it is a country. It is not, and I do include those in the north part of Africa, I do not just refer to sub-Saharan Africa. There are very important regions; some are more powerful than others, some are better managed than others. These countries encompass massive ranges of demographics, topographies and economies; and of climate variations and climatic conditions which are both cyclical, and increasingly climate change exacerbated which too often crowd in to overwhelm and throw off course so many of the plans and ambitions of these countries as emerging economies. Population growth and urbanization are eye-watering, and of course, a variable that is often very weak and narrowly concentrated on elites: purchasing power (thus disabling or stunting the natural economic development of a wide, ambitious stabilizing middle-class).

This belongs in the category of challenges of seeking to replicate what we know works. In the successful economies of the world, very broadly-speaking the emergence rapidly of a value-adding, ambitious middle-class has helped to underpin stability and regulate society to make it a fairer, more democratically accountable context, one which demands stability because too many of its citizens have potentially too much to lose by instability. As against those where the wealth is so narrowly shared, it means that sufficient people have vested interests to protect. That economic stabilizer helps to lessen the negative impact, inter alia, of factionalism, legacy autocrats, corruption, confessional identity leverage, and raise their sights and hopes and dreams above pure survival, protection, and subsistence.

Despite all the resources and particularly the world’s rapidly emerging new technologies and know-how, when we think about the long lessons we have all learned from Sir Paul Collier and his seminal work, “The Bottom Billion”, and in particular how to course correct away
from the inappropriate exploitation of natural resources, especially from the 55 countries of the continent of Africa, I have always argued that the problem we have in resource-rich, economy-poor states (so many of them on the Continent of Africa) is that whilst looking for financial returns and bringing technology and skills to extract the value of these natural resources for the critical use in products around the world, it has been job-less, not job-full growth (Paul Collier uses the terms ‘production’ and ‘productivity’) for those source-material nations. That has been one of the downfalls of this model, often then having a negative, activist sentiment towards globalization and its failures.

We all know financially there is nothing better - as I say, I used to be an industrialist - than having royalty income, that is the most tax efficient and it is the most helpful to get straight to the bottom line. But it is not helpful when you are trying to build an economy, particularly a fragile economy, as so many of countries are on the continent of Africa, and you need to extract a fair value for the once-only extraction of your country’s monetisable assets.

So, now turning to the crisis perspective, where I have been engaged as the UN’s Emergency Relief Coordinator rushing to all the crises around the world, that role is essentially marshalling all the human and materiel supplies and basic services in super-quick time and raising the international broadly taxpayer funding to do it, and to gain access to the most vulnerable people on our planet. Not just life survival and protection of civilians, but also making sure there are sustainable supplies of shelter, water, warmth, food, health, and of basic education. These are the things which ultimately give people, firstly, the chance to live and feel they have a life that is secure, engaged and worthwhile; and, secondly, that they and their families can have self-esteem and, above all, that they can have hope and a plan for the future – both to survive and thrive.

But none of that happens if there is instability, either caused through conflict and bad governance, or the lack of constitutionality, or through corruption, or a lack of engagement, as we see sadly in Mali now, where I was the Sahel Representative. After Operation Serval, we managed to raise 4 billion euros in Brussels in May 2015. I was there recently and I asked the Leaders of Mali from their southern capital, Bamako, ‘Where has that 4 billion gone? It was monumentally hard to raise that and came with massive international determination to be used for putting your country back on its feet by including every Malian...I want to see its impact towards re-setting a peaceful context. How is your engagement of your people in northern Mali going?’ Nothing – no answer at all; you cannot see it. Nobody has tried to. It has been basically a way of reinforcing what had gone before (reinforcing elites and the bilateral bonds with France) - so of course northern Mali now still remains one the most insecure places on earth and indeed the worst place to be a peacekeeper under the UN Blue Berets, where the most were killed last year out of the world’s peacekeepers. So, a bad result and a terrible use of precious goodwill world money – and absolutely horrendous still for the people of Timbuktu, Kidal, Gao, Taoudenni and everyone North of the River Niger. No wonder with this degree of disappointment and frustration there is severe scepticism that the world’s institutions, not least the UN, are fit for today’s world to foster peace over and above the national, regional and proxy interests we all contend with today.

A priority across Africa for financial inclusion is predictability. That is why it is fundamentally important to incentivize the rigour and adherence to a good rules-based system - there is no room for the fear of sequestration or a sudden U-turn in public policy which is going to deny those who have taken a risk of financing, even patient capital, to a point where they no longer have any prospect of return. Therefore, it is necessary to persuade those who are in charge politically - be that under good democratic institutional arrangements as well as those who are in less democratic circumstances - that good governance is in the national
interest. It is not in the ‘personal’ or the elites’ interests nor a way to cling on to power, to undermine those rules.

As for our partnership role as the UK and a Leader of the international community and order, I am very conscious that aid is a small element of financial contribution, after remittances, foreign direct investments, and above all, the main source of finance for the countries and economies of Africa being of course the domestic finances of those countries. It is vital that we recognize that for foreign money to flow into the economies of Africa, they will be looking for markets, purchasing power, good partners and returns.

From my industrial days, I well remember, whether I was choosing (normally on a pretty much monthly basis) where to put my next roof tile plant or brick plant, to go and dig aggregates or to make plasterboard around the world, I would give each country (in which I was not already a market player) a pretty clear but simple test. Had it got products which I could make available? Were they going to be affordable to a market which had purchasing power, and was it something which was going to meet a need or a want? Very simple. I then needed to look at things like good governance and that included not just the politics. Was there an independent judiciary? Could you go to court and could you get an answer from the court fast? Could you rely on a contract being honoured or was it likely to be squandered? Was it possible for everybody to be included and particularly women?

Look at Rwanda. Yes, there may be questions at times about some of its political governance and human rights (about which we should indeed be concerned and vocal), but it now has the best female representation in Parliament. But as importantly as I found out there myself, when you have DFID give money as a grant, and you then see that deployed by women who, under a programme DFID sponsored, designed, funded and organized, were granted the title to the land they tended, they then immediately were incentivized to get productivity up, to demand roads to markets, to be on the market board, to make sure they have fair pricing. Then, when you say to a woman farmer/entrepreneur, as I did, ‘What are you going to do with your first profit, your first dividend?’ and she looked at me as though I was the most stupid man on earth and said, ‘Of course I’m going to lend it to my ‘sister’, my neighbour, so she can do exactly what I’ve done. Then we will both be able to put shoes on our children, and send our children to school and make sure they have good health.’ I mean, what better answer could you ever hope for than the cascade theory alive from grant to income generation and support in a sustainable way. But what did she need above all else? She needed stability, confidence that she was a protected citizen and she needed there to be no conflict. And to be complete, it made all the difference that she was a woman with her own agency – who put her family’s, community’s interests and securing her prospects first.

So, for all of the summaries we have heard (and the clever people in the financial world can no doubt tell me exactly how we should measure everything), my main argument revolves around this need for stability. When we look at these countries of Africa, I am deeply conscious of having come from the humanitarian world, and it is the reason I brought this great, big fold-out map. This is a map of the globe, and you can all see that the reddest bit right in the middle is, of course, the continent of Africa. It is the red that represents where all the humanitarian needs are in the world today. It is by far and away in the continent of Africa where we have the highest needs of the people who need either their lives saving or their protection tonight.

Since the Cold War, this landscape has changed immeasurably. I am conscious that we could spend a lot time talking about people’s access to energy and light, or being able to make sure that they can avert the risks of a transmissible tropical disease. As some people know, I have been focused on malaria control for 40 years and we are making progress. But none of it -
none of it - works if there is instability through conflict, manmade conflict – and, yes, it is almost invariably shamefully and sadly men who cause lethal conflict. The sad fact today is, in the world that I faced going in three years ago to the UN, there has been an exponential rise in the most appalling amount of humanitarian suffering. Around the world there are 143 million people who need us tonight to either save their lives or for women’s and children’s bodies to be protected from being weapons of war. It is appalling when you think about that – these 143 million fellow human beings would be the 10th largest country in the world but they don’t have a flag, money or a President. Of the 37 countries that have received emergency humanitarian assistance in the past decade, 24 are on the African continent. At least six repeated humanitarian appeals for funding have been for 10 or more consecutive years: the Central African Republic, Chad, the Democratic Republic of Congo, the occupied Palestinian Territories, Somalia and Sudan. Five out of six on the African continent.

So, for financing in Africa, we clearly have to look at making sure that in future the bottom billion of the world can be properly serviced in stability. We have to look beyond the normal financial parameters. As far as I am concerned, the test is not just in managing crisis - there will be plenty of them - the test is managing and controlling all the risks you are capable of controlling, as I was always taught as a businessman. That is your job in business. The one thing you cannot control is what we used to call in the London Business School the ‘beta risk’ the political risk, the stuff that is outside your control.

Now, we know that we cannot control natural disasters. We know that they will occur frequently, normally without warning, quick onset, unlike the vast majority of humanitarian disasters which are from conflict which are slow onset, protracted and where we are deliberately barred from seeking to stop or enter to provide assistance. But the place on this earth which has the most natural disasters, which affect the largest number of people today, is actually the United States of America. They cope with them pretty well, but that said, sadly, many people do die of these terrible natural disasters in America. So it is not as if natural disasters cause people to have bad economies. It is that they can often deflect people from the ability to be able to make progress and they can siphon off some of the resources necessary. But, for those vulnerable 143 million people, natural disasters today only represent 10% of the suffering. 90% of humanitarian suffering is driven by what we euphemistically call ‘complex emergencies’. That is, emergencies caused by a combination of conflicts, violence, fragile institutions, corruption, contest for resources, endemic poverty and, the only one of these causes somewhat but by no means exclusively, beyond human control, the exacerbation of climate cycles and depths of climatic shock and geographies, and thus need, resulting from climate change. But, worse than that, 86% (within the 90%) is directly a result of man-made, deliberate, avoidable conflict.

Syria, of course, is the most dramatic example that we can all immediately call to mind, but think of the Central African Republic. Think of the DRC today. I was in the Tanganyika province the other day, in the Kasai region in the south; and to the north, the conflicts in the Kivus have blighted that area of DRC and its neighbours for decades. Who is thinking about going to the DRC to invest at the moment? It is not just because of the instability caused by a President who is looking to extend beyond his two terms as an abuse of his country’s constitution, therefore alienating many in his country who do not feel that they can are legitimately engaged if leaders can ride roughshod over their constitutional arrangements. It is more to do with the vacuum this has left for contestation between power groups who then want to be able to challenge that and to succeed. That is what has led particularly to the appalling humanitarian suffering in the Kasai region.

I am conscious of this because - I do not know whether this has been reversed more recently, but I suspect not - when I was a Member of Parliament up in the northwest of England, very
close to me was one of the great founding global industries of the world, Lever Brothers, Unilever, with their great model of social policy, including the model village of Port Sunlight. They made things at home, they added value at home, and they manufactured and sold abroad. Brilliant. They were able to franchise so much of their manufacturing operations. I am told that the one country from which Unilever in all its history has disinvested is DRC. Why? Because the governance arrangements and the conflict threat were so severe at all times, it simply was not possible, even when you were selling soap, to be able to give such a basic service to the people and their needs.

So, conflict seems to me to be the thing which is the biggest possible deterrent to doing all the right things. I daresay that does not come either as any surprise, shock or anything particularly revealing to any of you this morning. It is conflict that tends to lead to massive forcible displacement - another grand challenge of our age. Having focused on the terrible plight of people leaving Syria across the Mediterranean in rickety boats in which they were at great peril of their lives, today the main migration flows are from Africa, through what most people in the world regard as a barrier, the Sahara Desert. But actually, for people in Africa, it is nothing of the sort. As it happens, I have crisscrossed the Sahara many times myself and it is not a barrier. You just have to be pretty well prepared and know how to do it. Agadez today is the crossroads of Africa and it is from Agadez that you purchase everything that you need. A lorry ride and you can get to a Libyan port, and you are migrating. You only move if you have to for life or a chance at life.

Now, let's be clear: a quarter of a billion people migrate across the world legitimately, every year. 64 million are forcibly displaced. About 23 million of those are ones who cross a border and they are refugees, and they are very well protected by our international laws and the expectations and norms of our values and consciences. It is a terrible thing to have to see it and we manage it very carefully and we can always do a better job than we are doing. 42 million are internally displaced, a quarter of them at the moment in Syria, as you and I would rush to move - be displaced - if we could not get our children into school for the third year running or we thought a bomb was about to drop on our heads because one killed our neighbour yesterday. That is when you move, not least within your own country, let alone flog what little you have to be exploited by traffickers to cross a border - we are all normal and human. Unsurprisingly, increasingly refugees now rarely are able to go back home, even though that is by far the greatest desire, either because they can’t risk it or there is nothing to go back home to - they stay displaced for twenty years or more. This is our world today – the world of unresolved protracted conflict-driven crises.

So, the big challenge for us is: what can we do better to prevent conflict? Now we know that the UN Secretary-General has said that conflict prevention his absolute core priority, but woefully to date, no concrete initiatives or bold strokes of inspiration or leadership. The UN, not least its Secretariat, if it is to be relevant to the present day, needs to avoid being the prisoner of the P5 on conflict and security issues and its least globally cooperative members, nor trapped by the General Assembly of Member States into stunting the desperately needed reforms of the UN. The recent campaign to be Secretary-General was won, admittedly very ‘politically’, supposedly by placing the emphasis on ‘General’ not ‘Secretary’, even though it all was rushed through at the end under the Presidency and process of the Russian Federation. I am very conscious of all the discussions, speeches, engagements I had with the Security Council when you are sitting on the end of that horseshoe and you are looking at the UN ambassadors of all their countries, particularly the P5, that if there is no proxy interest, you can make a real impact to say, ‘stop’ in the unarguable case for humanitarian action. And you can see how that has come together and there has been a unity, and we are making progress in relation to, for instance, North Korea. Let's see how that goes, but that may make progress –
or will it? You can also, unfortunately, see a lack of interest or effectiveness by the Security Council when things are going wrong, as we saw for many years in Zimbabwe, if the country in question is of little strategic interest nor threatening to P5 interests.

But, where there is a proxy interest, we have complete deadlock and a causation of conflict and violence which is prolonged and protracted – Syria, Yemen, Ukraine, Libya….It is that which is causing me the greatest concern and which I think should cause you concern, when you are thinking about the future of the peoples of the countries across Africa, the future of getting finance into Africa, the future of the development of economies, and the development of stable middle classes which are going to underpin the future and the hopes of Africans across the 55 economies and nations.

It seems to me that the one thing that is going to be absolutely vital is to do a better job at conflict prevention and resolution. On the best and most expert, experienced evidence, that was the clear finding of the world’s first World Humanitarian Summit held over 2 days in Istanbul in May 2016 attended by nearly 100 Heads of Government/Heads of State and 9,000 registrants from States, Agencies, INGOs, local actors, media, technical and private sector leaders and innovators and academia, but where the P5 were notable by their under-representation (with Russia, China and Egypt actively trying to frustrate it) and the US, UK and France being lukewarm about anything that might promote international overriding principles and law, or cause humanitarian response and its imperative to cap national power interests. The template is now clearly and simply set out in the Agenda for Humanity which has its own website under that name and tracks promises, commitments and fulfilment by Member States who are willing to step up to their responsibilities as global citizens.

If we cannot do it at the Security Council - my experience with the UN is such that I cannot see any incentive whatever, however much we may all theorize, for there to be a change at the Security Council or for the P5 to feel that they should give up their veto, including the UK, of course - the only way I can see is that we are going to have to try and find a way of arbitrating some of these disputes, as you do successfully in the commercial world so you can maintain relationships, but at the same time arbitrate the disputes. We need to establish a free bank of ideas and techniques of what works and are available to Leaders without the filter of bureaucratic interests. This is very much a working thought - I am going to be the Visiting Fellow at Emmanuel College, Cambridge in the Lent Term next year, so I hope to develop some of these ideas into a practical model. I would very much welcome the support of all those who think in terms of creating the stability frameworks that are going to enable us to prevent conflicts which otherwise will send so many economies and the trends within finance off-course and thus kill the hopes and the survival of so many.

I wanted to use this morning to discuss this, recognizing that I was, if you like, the non-banker, the non-financier on the panel, but with my experience across emergency and crisis management, which is the acid test in the end as to whether you can have confidence as a banker, as a financier, as a business person, as anybody in the community with hopes for a better future. You need to be able to say, ‘There is a future, I am not going to be blown off-course and have my plans disrupted by people completely outside of my control and my risk. I want to do what we all want to do, which is to have the chance and the means to bring up my children in a way which is going to give them a better start than I had’.

I hope that you will join me in trying hard to find a way of encouraging all those around the world in political positions, in huge multinational institutions, to do this. Particularly post Brexit, the United Nations will be the United Kingdom’s only multilateral institution at a political level, outside defence institutions like NATO. So, we have got to make a better job of making these work for the new generation so that we do not unlearn lessons of history.
The UN has rightly been there for 72 years. It does, I think, fairly claim to have helped prevent another World War - global conflict, but it was designed because of the potential of conflicts between Nations. Today’s conflicts are mainly sprawling insurgencies within Nations, often hijacked by Proxies. Under its brilliantly drafted and enduring Charter, the UN is not authorized to deal with or interfere in, internal affairs. Humanitarians come up against this all the time, as we also see in the Human Rights field with the UN’s necessary but forlorn R2P (Right to Protect) programme having run into the sands. So we need to think very carefully how to make an Agenda for Humanity and an agenda for people become an agenda for stability, for markets, for hope, and for a future.”
Maxwell Opoku Afari

Maxwell Opoku-Afari is the First Deputy Governor of the Bank of Ghana. He holds a doctorate from the University of Nottingham. Until his appointment as first deputy governor of the Bank of Ghana, he was a mission chief, and also a deputy division chief at the IMF, working with the strategy, policy and review and African departments. He has been with the IMF for over 8 years. Before joining the IMF, he served as the special assistant to the Governor of the Bank of Ghana from 2006 to 2009. He also worked in several capacities at the Bank including, Head of Special Studies from 2005 to May 2006 and Senior Economist from 1996 to 2000.

Reda Cherif

Reda Cherif is a Senior Economist at the International Monetary Fund (IMF). He joined the IMF in 2008 and worked in several departments on fiscal issues and macroeconomic analysis of emerging and developing countries. Reda also conducted economics training of IMF staff and government officials. His research focuses on development economics, natural resources, fiscal policy, and growth and innovation. His recent book co-edited with Fuad Hasanov and Min Zhu, *Breaking the Oil Spell*, explores economic diversification in oil exporters. Reda holds a PhD in economics from the University of Chicago.

Stuart Culverhouse

Stuart has over twenty years experience as an Economist working in both the public and private sectors and has been covering emerging markets as a focus since 2000. He joined Exotix in July 2006 as Chief Economist and now heads the team of macro and fixed-income analysts. Before this, he worked for ten years in the United Kingdom Government Economic Service, first at HM Treasury from 1996 to 2001, where he had responsibility for Latin America, and in particular Argentina over 2000 to 2001. He also worked on domestic UK economic policy, Government debt management and public private partnerships. He then spent five years as an Economic Adviser at the Export Credits Guarantee Department from 2001 to 2006, where he covered Latin America and East Africa.

Florence Dafe

Florence Dafe is a political economist at the Chair of European and Global Governance of the Hochschule für Politik /TUM School of Governance at the Technical University of Munich (TUM). Her research and teaching cover a number of themes related to international political economy and comparative political economy, with a particular focus on global financial governance.

Her research interests revolve around finance and development, especially the domestic and external political constraints that governments in developing countries face in governing their financial sectors. The question which drives her research is how much policy space governments in developing countries have in governing their financial sectors in a context of globalisation and financialisation.

Prior to joining the Chair of European and Global Governance, Florence was a Fellow in International Political Economy at the Department of International Relations at the London School of Economics and Political Science (LSE) and lecturer in International Political
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**Charles Enoch**

Charles Enoch is presently the European Studies Centre Fellow at St Antony's College Europe. He was Director of the Political Economy of Financial Markets programme at St Antony’s, Oxford from 2017-9, having arrived at the College in late 2016. His research interests include regional economic integration and enhancing financial stability. He had previously spent a total of 25 years at the IMF, firstly as the UK Alternate Executive Director for three years and then on the IMF staff, working in around 80 countries, in all regions. Until late-2016 he was Deputy Director in the Western Hemisphere Department, and had previously been Deputy Director of both the Monetary and Capital Markets, and the Statistics Departments. He led the IMF’s Financial Sector Assessment Programs (FSAPs) for, amongst others, the European Union, Switzerland, Nigeria, Netherlands, Switzerland, and Turkey. He led the IMF’s bank restructuring team during the crises in Bulgaria, Indonesia, Mongolia, and Philippines, and led the work establishing the currency board in Bulgaria. He has published widely, and co-edited publications on “Fragmentation and Financial Integration in the European Union” and “Rapid credit growth in Central and Eastern Europe: Endless Boom or Early Warning?” Earlier he worked for 15 years at the Bank of England. Charles Enoch has an MA in economics from Cambridge, and a PhD from Princeton University.

**Anne-Marie Gulde-Wolf**

Anne-Marie Gulde-Wolf, a German national, is Deputy Director of the IMF’s African Department. She oversees the department’s work and policy priorities on a number of Southern and Central African countries, including South Africa, Botswana, Namibia, Lesotho, and Swaziland, as well as the Central African Economic and Monetary Community. She also coordinates the department’s work on financial sector issues. Before joining the African Department in 2012 she was Deputy Director of the IMF’s European Department, and held different positions in the IMF’s Monetary and Capital Markets Department. Ms. Gulde-Wolf holds a PhD in international economics from the Graduate Institute of International Studies in Geneva, Switzerland. Her publications focus on exchange rate regimes, financial stability and development issues.

**Barend Jansen**

Barend Jansen, is a Dutch national, currently working in the Front Office of the Legal Department of the International Monetary Fund (IMF). From September 2016 to September 2019 he worked as Lead Financial Sector Expert in the Financial, Competition & Innovation (FCI) Global Practice Group of the World Bank on a three-year secondment from the IMF. At the World Bank he was involved in bank restructuring and resolution matters, deposit insurance, assessments of the financial sector, climate finance and FinTech issues, among other things. Before his secondment to the World Bank he headed the Financial and Fiscal Law Unit of the Legal Department of the IMF. Trained as an economist and a lawyer, he has broad experience in financial sector policy issues and in financial sector legal reform work around the world. At the IMF his experience ranges across the areas of central banking, banking, deposit insurance, bank restructuring and resolution, financial stability frameworks, governance of financial institutions, and non-tax fiscal matters. He has worked on and headed projects in different parts of the world, especially in Asia, Africa and Europe; in Europe he worked mostly on financial sector reform projects in the context of the recent financial crisis. Before joining the IMF in 2004 he worked for 18 years at the central bank of the Netherlands.
(DNB) in economic and legal positions, lastly as Director of the Legal Department. During his stay at DNB he was involved in the creation of the European Central Bank and the preparation of the third stage of the European Monetary Union.

Mr Jansen holds graduate degrees in monetary, development economics and international law from Erasmus University Rotterdam.

**Samuel Munzele Maimbo**

Samuel Munzele Maimbo is a Zambian national, and Head of the Financing for Development Unit and Senior Advisor in the office of the Managing Director & Chief Financial Officer, IBRD/IDA. He leads a unit tasked with carrying forward the work on financing for development with new instruments established in IDA-18; supporting the strategic oversight of Finance Partners, including financial and risk management strategies of the World Bank and reporting of its financial conditions; and fostering the development of new and innovative financial products and services to increase the mobilization of private and public financial resources. Dr Maimbo also supports Finance Partners international dialogue on financial standards and best practices. Dr Maimbo holds a PhD. in Public Administration (Banking) from the University of Manchester, an MBA in Finance, (University of Nottingham), a BSc. in Accounting (Copperbelt University, Zambia) and is a Fellow Chartered Certified Accountant (FCCA, UK). Prior to joining the World Bank, he worked at the Bank of Zambia and PWC.

**Hanan Morsy**

Hanan Morsy is a renowned macro-economic and public policy expert with vast experience in international financial institutions and the private sector.

She is Director of Macroeconomic Policy, Forecasting and Research Department at the African Development Bank (AfDB). Before joining the AfDB, she was the Regional Lead Economist for Southern and Eastern Mediterranean at the European Bank for Reconstruction and Development (EBRD). Prior to that, she worked at the International Monetary Fund between 2003 and 2012 in various capacities across different departments including, Fiscal Affairs, Middle East and Central Asia, European, and Monetary and Capital Markets as well as Advisor to Executive Director. Previously, she worked as an Economic Advisor at KPMG Consulting implementing public finance reform project in Egypt.

Dr Morsy is a Member of the Economic Policy Panel for Aberdeen, a Board of Trustee Member at the London Middle East Institute, and a Research Fellow at the Economic Research Forum.

Her research interests and publications include youth unemployment and inequality, impact of structural reforms on growth and productivity, exchange rate and competitiveness, financial crisis contagion, sudden capital stops, inflation, and fiscal vulnerability and debt.

She holds a PhD in Economics from the George Washington University, USA, a Masters in Economics from University of California, USA and a Bachelor in Economics and Computer Science from the American University in Cairo, Egypt.

She holds a Ph.D. in Economics from the George Washington University (USA), a Master’s degree in Economics from the University of California, Davis (USA), and a Bachelor’s degree in Economics and Computer Science from the American University in Cairo (Egypt).

In 2020, Dr Morsy was named one of Egypt’s 50 most influential women.
**Patrick Njoroge**

Patrick Njoroge is the ninth Governor of the Central Bank of Kenya (CBK) and has been in office since June 19, 2015. He has overseen a significant overhaul of the banking system in Kenya, including the launch of the first Kenya Banking Sector Charter. He also led the country in the launch of the new generation currency banknotes and coins, thus fulfilling a much-anticipated constitutional requirement. Dr Njoroge has been keen on facilitating the growth of the Micro, Small and Medium Sized Enterprise sector, which has been the engine of growth of the Kenyan economy.

Dr Njoroge joined CBK after a 20-year career at the International Monetary Fund (IMF) in Washington, DC. Prior to his appointment as Governor, Dr Njoroge was Advisor to the IMF Deputy Managing Director from December 2012, where his responsibilities included assisting in overseeing the IMF’s engagement with a large swath of IMF members. He also served as Deputy Division Chief in the IMF’s Finance Department (2006-2012), IMF’s Mission Chief for the Commonwealth of Dominica (2005-2006) and in other capacities since 1995. Prior to joining the IMF, Dr Njoroge worked as an Economist at the Ministry of Finance (1993-1994) and as a Planning Officer at the Ministry of Planning (1985-1987).

He holds a Ph.D. in Economics from Yale University (1993), a Master of Arts in Economics (1985) and a Bachelor of Arts in Economics (1983) from the University of Nairobi. Dr Njoroge’s professional and research interests lie in Macroeconomics, Economic Policy, International Finance, Development Economics, Econometrics and Monetary Policy.

Dr Njoroge began his second four-year term in June 2019. He was appointed to the UN Task Force on Digital Financing by Secretary General Antonio Guterres in November 2018.

**Rt. Hon. Sir Stephen O’Brien**


In 2004 he founded, and then served as first chairman, of the All-Party Parliamentary Group on Malaria and Neglected Tropical Diseases. He has also been Co-founder/Chairman of the leading NGO , Malaria Consortium, Vice-President/Director of the Liverpool School of Tropical Medicine, and is now Chair of the Innovative Vector Control Consortium, Global Advocate for the UN/WHO’s inter-agency Roll Back Malaria Partnership. He was appointed to Her Majesty Queen Elizabeth II’s Privy Council in 2013.

After serving as a Conservative MP and in various shadow ministerial roles, he was appointed the Prime Minister’s Envoy and UK Special Representative to the Sahel in Africa, and later on United Nations Emergency Relief Coordinator, leading the Office for the Coordination of Humanitarian Affairs.

As the world’s leading advocate for crisis-affected people, he argued for compliance and accountability under International Humanitarian law and unimpeded access to people in need. His responsibilities included oversight of all UN humanitarian operations globally, and leadership of coordination mechanisms between UN agencies and other partners. In recognition of his leadership and achievements in humanitarian and development work, Stephen O’Brien was awarded a Knighthood (KBE) in June 2017.

Born in Tanzania, Sir Stephen was educated in Kenya and the United Kingdom, where he attended Emmanuel College, Cambridge University and qualified as a lawyer.
**Antoinette Monsio Sayeh**

Antoinette Monsio Sayeh is Deputy Managing Director of the IMF. Until February 2020, she was a Distinguished Visiting Fellow at the Center for Global Development based in Washington DC. Previously she oversaw and enhanced the International Monetary Fund’s engagement with its sub-Saharan African members as director of the African Department from July 2008 to August 2016. As Minister of Finance in post-conflict Liberia, Sayeh led the country through the clearance of its long-standing multilateral debt arrears, the HIPC Decision Point, the Paris Club, and its first Poverty Reduction Strategy, significantly strengthening its public finances and championing public financial management reform. Before joining President Ellen Johnson Sirleaf’s Cabinet, she worked for the World Bank for 17 years, including as country director for Benin, Niger, and Togo; senior country economist on Pakistan and Afghanistan, as well as an advisor in the Bank’s Operations Policy Vice-Presidency and as assistant to its principal managing director. Sayeh also worked in economic advisory positions in Liberia’s Ministries of Finance and Planning. She earned a bachelor’s degree with honors in Economics from Swarthmore College and a PhD in International Economic Relations from the Fletcher School at Tufts University.

**Abebe Shimeles**

Abebe Shimeles is Manager of the Development Research Division at the African Development Bank. Previously Mr Shimeles has worked for The World Bank, UNECA, ACTIONAID, and Addis Ababa University in different capacities. His recent research interest includes labour market integration, migration issues in Africa and impact evaluation of policy interventions. He holds a PhD in economics from University of Goteborg, MSC from Delhi School of Economics and undergraduate degree in economics from Addis Ababa University. He joined The Institute of Labour Economics (IZA) as a Research Fellow in 2011.

**Ibrahim Yusuf**

Ibrahim Yusuf has a degree in computer technology from the University of Westminster. He is a Management Consultant at Wayeel Consulting, and formerly Operations Director with Dahabshiil, UK-headquartered African money-transfer company. Dahabshiil is the largest remittance firm in Africa, and Somalia's largest private sector employer; it offers a pan-Africa service, with a particular emphasis on serving more remote and hard-to-reach regions of Africa.