eAfrica

The electronic journal of governance and innovation

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Pressuring Banks To Do the Impossible

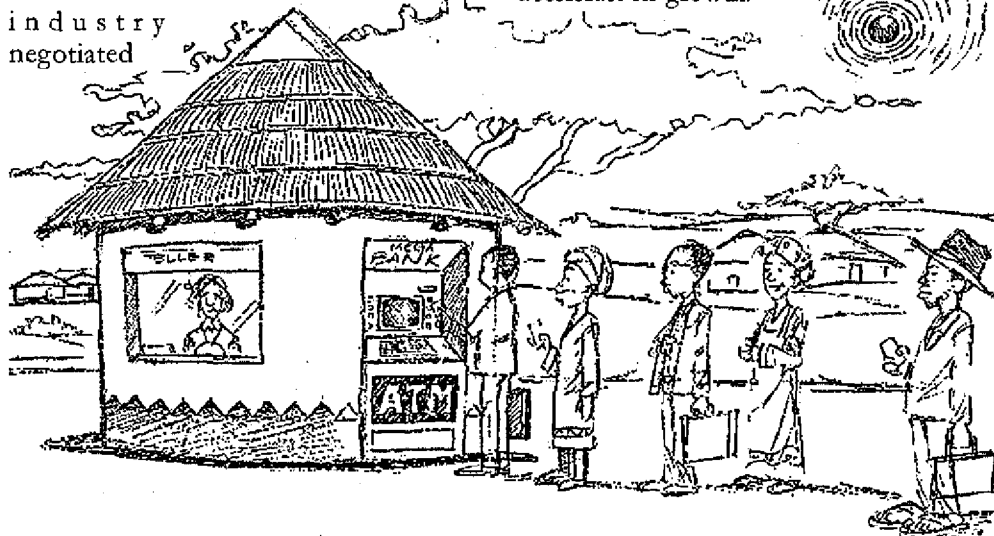
A VARIETY of surveys and studies – by the World Bank, UN Conference on Trade and Development and by *eAfrica* last year – have noted that lack of credit blocks business growth in Africa. But conventional wisdom said little could be done.

Africa has the lowest savings rate of any continent. Boosting growth, economists agree, requires boosting investment. More foreign aid and debt forgiveness can help. But they aren't the only solutions.

South Africa last year pioneered a creative solution from a new direction: boosting the pool of lendable funds by encouraging more of the poor to open bank accounts. Research shows that people with bank accounts are more likely to save than those without them. However, African banks are some of the most expensive and inefficient, deriving profits from high fees on accounts and transactions rather than lending.

Instead of forcing change through law, which can sour the investment climate, South Africa used gentle political pressure to get industries to assist with transformation. Each industry negotiated a charter under which it agreed to improve performance against various social goals. Banks agreed to boost the number of people with access to banking by slashing the fees and paperwork associated with bank accounts. The top banks collaborated to launch a jointly marketed low-cost account that has succeeded in drawing 4% of the population into the banking system. It is a banking success story and a model of business-government collaboration.

Across Africa, lack of credit is a symptom of deeper problems. Banks don't lend as it can be almost impossible to recover funds. In many countries, borrowers default on a majority of loans. Commercial courts are weak and take years to settle cases; property rights are unclear; title deeds impossible to obtain; bank regulation and accounting standards are weak; and there are no systems to track those who default on loans. But solutions can be found. Africa invests about 40% of its wealth outside the continent. With the right legal environment, those funds could be brought home and Africa would accelerate its growth.



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Verbatim

"I want to reassure our population that the train is in motion; the process is really irreversible and the elections will certainly take place." – Joseph Kabila, President of Democratic Republic of Congo, after the country's new draft constitution was presented.

"The men are standing in our way to prevent the unborn babies from the pandemic." – Edwin Bakali, Malawian district health officer for Thyolo, on how pregnant women are refusing to get tested for HIV/AIDS for fear of being attacked or left by their husbands.

"This decision wipes Pretoria off the map, in history and as the capital of the country." – Kallie Kriel, Pretoria Civil Action and Solidarity spokesperson, on the name change for South Africa's capital city. Both blacks and whites have voiced disapproval.

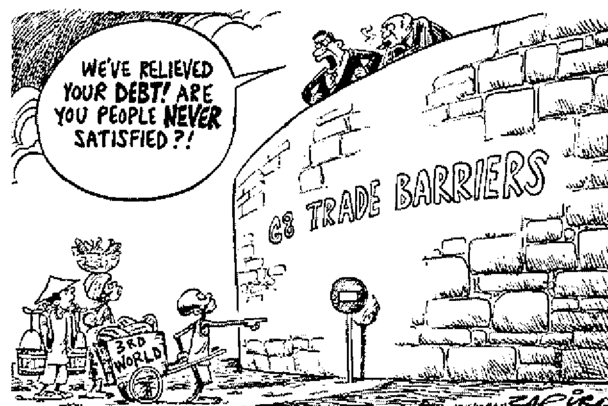
"At this time I have no fixed address." – Agathon Rwasa, Burundian rebel Forces for National Liberation leader, responding to a request to visit him at one of his camps. He only recently joined the peace talks after being in the bush for more than 25 years.

"Our job is risky. At times we go as deep as 150 feet below the ground, but what we generate from our sweat cannot sustain us." – Philip Masero, a Kenyan informal miner, on what they have to do to escape poverty and unemployment.

"I know when I became President of this country many criminals rejoiced. They were convinced that I will not pursue the policy of zero tolerance to corruption." – Levy Mwanawasa, President of Zambia.

"Our anti-corruption campaign is blind. It will hit anybody, friend or foe. It's like justice." – Olusegun Obasanjo, President of Nigeria, on his anti-graft drive, which has so far resulted in a number of top officials losing their jobs.

"I do not accept someone telling me how to run Uganda because I know Uganda better." – Yoweri Museveni, President of Uganda, lashing out at donor countries, which he said dictated management rules to recipients.



"My other sin was when I refused a cabinet that was prepared by somebody else because others thought they were born to be ministers forever." – Bingu wa Mutharika, President of Malawi, on why he quit the party that brought him to power. He was speaking at the launch of his new Democratic Progressive Party.

"Nothing would be more satisfying than to feel at the end of however long a term I serve here that we played a role in changing Africa from a continent of despair to a continent of hope." – Paul Wolfowitz, World Bank president.

"They can keep their dollars as long as they respect our dignity. It is not only Americans who can train our military personnel, and it is time we started looking at the EU, China, South Africa or even Japan for such training." – Paul Muite, Kenyan member of parliament, on alleged threats that the US might cut military aid to the country if Kenya does not sign an accord to protect US soldiers from the international war crimes court.

"We are not angels, but we can't be devils all the time, everywhere in Africa." – Benjamin Mkapa, President of Tanzania, at the World Economic Forum regional summit saying the continent is now cleaning up its act.

"Everything was destroyed without notice. This is the true meaning of tsunami." – Ernest Rautavaara, a Zimbabwean, after a vegetable market was destroyed during police operations against street traders and illegal housing.

"I, for one, will not risk going in the streets to be beaten while Morgan sits in his house, yet he is the one who wants to occupy State House." – A Zimbabwean, after a two-day national protest supported by the opposition Movement for Democratic Change flopped.

"It is an illusion to think that the country will be fully rehabilitated by 2006." – Virgilio de Fontes Pereira, Angolan co-ordinator of the Inter-ministerial Commission for Electoral Process, saying, though, problems would not endanger the running of elections next year.

Battle for Control of African Development Bank

DEADLOCK over the election of a new president of the African Development Bank (AfDB) at last month's annual meeting threatens the bank's bid to become a major channel for the fresh aid to Africa as proposed by UK prime minister Tony Blair and the New Partnership for Africa's Development.

Britain, which chairs the Group of Eight (G8) and European Union this year, advocates a much bigger role for the AfDB group in development financing. It has won support for this from France, Germany, Canada and the USA. The AfDB already got a vote of confidence from the donors last December when they awarded its soft-loan affiliate, the African Development Fund, its biggest-ever replenishment of $5.4 billion for operations in 2005-07. Before the annual meeting, Britain wanted the AfDB to take the lead in managing a $10 billion-a-year infrastructure fund for Africa, as part of an expansion in the bank's role recommended in Blair's Commission for Africa's report (*eAfrica* April 2005).

However, Africa and donor nations who are shareholders in the bank are deeply divided over who should be the next president. After Ghana's KY Amoako, who heads the UN's Economic Commission for Africa, failed in the early rounds of voting, the western donors backed Rwandan finance minister Donald Kaberuka, joined by South Africa, Kenya and Egypt. But most other African shareholders backed Nigerian candidate Olabisi Ogunjobi, Vice President of the AfDB. Western officials are now more guarded, talking of bringing in the European Commission and the World Bank's soft-loan affiliate, the International Development Association, alongside the AfDB.

There were no obvious policy differences between Kaberuka, an accomplished Rwandan politician, and Ogunjobi, an AfDB veteran. The Nigerian camp claimed Kaberuka was a western stooge and Ogunjobi a champion of African nationalism. It is unclear why Ogunjobi has taken so few non-regional votes, apart from China, India and Spain (all small shareholders). Opponents of the Nigerian candidate, a personal friend of President Olusegun Obasanjo, suspect he has more of a national than an African agenda. Some worry about an overbearing Nigeria, which, as the biggest African shareholder, likes to throw its weight around in the bank.

African governments own 60.1% of the AfDB, but the winner must have substantial support not only from Africa but also from the non-African shareholders, who provide vital soft loan resources. Most African states are already overburdened with debt and cannot borrow from the bank at its normal rates, which means the bank's effectiveness as a development institution is directly tied to its ability to continue to win new funding from non-African shareholders.

The deadlock over the presidency recalls the AfDB's bad old days of political infighting between the African and non-regional shareholders over who could borrow from the bank's low-interest resources, amid deteriorating finances and spreading corruption. That era ended with the election in 1995 of Omar Kabbaj, a former Moroccan finance minister, whose tenure brought stability to the AfDB and restored its triple-A credit rating from the leading international rating agencies, while earning big increases in soft loan resources from the donors. Blair's Commission for Africa recently said the AfDB combined regional credibility with much improved financial management.

The bank's shareholders are to meet on 22 July at the ADB's temporary headquarters in Tunis to try again to agree on a new president. Kaberuka and Ogunjobi will be candidates again, though the latter will have lost home advantage since the Abuja meeting. It will be considered a new contest so other candidates may now be able to enter the race. A third possibility is a transitional presidency under Kabbaj or another mutually acceptable nominee. Kabbaj's term ends on 31 August.

Until then, the AfDB can only tread water. The big question facing the bank is what the new president will do with the solid financial platform that Kabbaj and his team have built and whether he will be able to take advantage of the new funds at Africa's disposal. – **Patrick Smith**

Potrait of the Candidates

OLABISI Ogunjobi is a banker rather than a politician. Of all the candidates in Abuja, he knows the AfDB best, having worked there since 1978 – perhaps too well for some shareholders. Conservative and considered, he is more the bankers' candidate, who speaks at length of his three decades of operational experience.

Donald Kaberuka is more politician than banker but has a practical grasp of development issues. As Minister of Finance in Rwanda since 1998, Kaberuka has presided over much of his country's reconstruction after the 1994 genocide. More recently, Kaberuka was charged with improving relations between Rwanda and France, which had been accused of complicity in the genocide. He succeeded, judging by France's increased development aid to Rwanda. This, and his fluent French, won the backing of Paris in the AfDB election, after France's first choice, Gabon's Casimir Oye Mba, was knocked out.

Tragedy Intensifies in Zim

Bill Corcoran offers a first-hand look at a brutal campaign that's destroying livelihoods.

IN LATE May, the Zimbabwean army and police drove into the large informal settlement at Hatcliffe, outside Harare with bulldozers, and either burnt to the ground or flattened the 3,000 homes in which about 15,000 people lived. For days residents stayed amid the rubble, trying to protect salvageable possessions and hoping for relief. As we drove into the wrecked township, people's possessions were piled up along the dirt road next to where their homes once stood.

Filthy babies lay amongst mounds of burnt wood and rubbish while their parents sat listlessly next to them, too traumatised to worry about hygiene. They had no shelter, running water, electricity and very little food. The local school and the medical clinic were also closed down during the operation.

Days after my visit, police returned and burned the remaining rubble and piles of possessions.

The same story played out across the country in major and minor cities. Government newspapers reported that at least 22,000 street traders were arrested. And more than 200,000 people made homeless, according to the UN.

The action was part of the government's 'Operation Murambatsvina', a Shona word meaning 'drive out the rubbish,' which has destroyed dozens of informal settlements and thousands of buildings across the country since it began in May. Zimbabwe's President Robert Mugabe says the campaign aims to clean up the country's urban areas and eradicate the flourishing black market that has arisen as a result of the country's economic collapse. Since Mugabe claimed victory in recent elections, shortages of basic goods have grown severe and the value of the local currency declined steeply.

Managed in the same violent and abrupt manner as land resettlement, Murambatsvina destroyed the livelihoods of many urban poor who make ends meet by selling basic commodities. With winter nights near freezing and no alternative shelter, food or employment offered, many are asking, why now?

HELPLESS: *Lives of women and children have been devastated in the destruction.* *Photo: Southphoto*

The opposition Movement for Democratic Change (MDC) argues that the real reason behind the campaign is to punish the urban poor who voted for the MDC in the recent elections.

When I stopped in Hatcliffe, Alex Nhema was one of those who made his way towards my car. When I asked what had happened, he said angrily that the police had destroyed everything while keeping the people away at gunpoint.

'They were very aggressive and violent and told us all that we had to take down our homes and leave this place. They said they would come back, and if any of the houses were put back they would burn all the possessions inside. They have done this because we voted for the MDC in the election,' he said.

Trudy Stevenson, MDC member of parliament for Harare North, distributed blankets to the homeless after Hatcliffe was destroyed. 'All of the [non-governmental] organisations are afraid to help because they believe that Mugabe will expel them from the country if they do,' she said.

She maintained that the Hatcliffe settlement was not illegal and the people who built the makeshift shacks leased their plots from the government at a cost of 100,000 Zim dollars a year.

'The World Bank even paid for the sewage and water services to be put in – look you can see the remains of the piping on the ground,' she said pointing at concrete pipes strewn around.

Although police ordered residents to leave following the destruction of the settlement, the majority have not done so. 'I don't have anywhere to go,' said Nhema. 'So I will stay here where my home was. We were told that the police would take us to some place, but then they told us to go back to where we came from. I am from here.'

Some of the displaced have been taken to holding camps. Local priest William Guri is so far the only person allowed to visit one such compound guarded by armed police at a deserted farm 40km outside Harare.

'They have nothing: no food, no shelter or anywhere to go and their health is worsening daily,' he said. 'The NGOs that went there to try and help were chased away, but I have been able to bring in some food. The people are being told they are being kept there while an alternative settlement is being found for them. But I think they will be there a long time.'

'We cannot support them for much longer, as I'm running out of resources. When you go into the camp, the people are just sitting around idle. The kids are playing but the adults look really distressed.' – **Bill Corcoran**

COMMENT

Taxing Africa to Death

High taxes on drugs drive up health costs and block access to treatment for Africa's poor, says medical researcher **Richard Tren**

IN RECENT years global efforts to improve access to medicines and decent medical treatment have been successful at lowering drug prices. Manufacturers have cut prices, but access to drugs, particularly for HIV/AIDS treatment, is only slowly increasing.

One factor is rarely discussed yet has a drastic negative effect on health treatment in Africa: poor countries impose high taxes and tariffs on their own citizens for medicines and medical supplies. In this way, governments fund themselves by taxing the poorest and most desperate members of society.

On a recent trip to KwaZulu-Natal province in South Africa, I met Emma (not her real name) who sat quietly waiting her turn to tell her sad story of HIV infection. Like her husband, Emma is HIV positive and her health is deteriorating. A month's supply of antiretroviral triple therapy is likely to cost R586 ($86) for the drugs alone. Of this amount, R72 ($11) is paid directly to the South African government in the form of sales tax. Emma tells us that it's a struggle to pay for medicines. To Emma, like so many of the other young women I have spoken with, the sales tax charged on her drugs means she can't afford decent food for the whole week. As she breaks down and cries: 'my two children (currently not on treatment but who are HIV-positive) also don't have enough to eat', she wails.

> **'There is little theoretical or empirical evidence to support protecting domestic industries'**

Unfortunately Emma is not alone. There are millions of Emmas in rural areas and in almost every town and city, struggling to survive and trying to make sense of the government's apparent indifference and intransigence in the face of their plight.

Tariff and tax policy

There are at least two reasons why governments impose tariffs and taxes: to protect domestic industries from international competition and to raise revenue. The main job of tariffs is protectionism. There is little theoretical or empirical evidence to support protecting domestic industries – ordinary people pay more for goods for the sake of powerful special interests. Take the odious US steel and farm subsidies – they protect US corporations by reducing their need to compete and increase the price of food and steel products for US consumers.

> **'Governments fund themselves by taxing the poorest and most desperate members of society'**

Brazil and India, with powerful local pharmaceutical industries, impose tariffs on medicines with this aim in mind. Historically, many wealthy countries imposed tariffs on medical products, but a decade ago most of the wealthiest 22 countries (including the original 15 EU members and the US), and some not so wealthy, like the Slovak Republic and Macau China, agreed to a reciprocal elimination of import tariffs under the WTO (then the GATT) on around 7,000 pharmaceutical products.

It is the sovereign right of any nation to raise revenue as it sees fit. But according to a press statement from numerous NGOs, including Africa Fighting Malaria, which I co-direct, 'taxing the poorest and sickest in society seems like an odd choice for countries that have craved aid from the international community and demanded lower drug prices from western pharmaceutical companies'.

In many countries, taxes are imposed not only on commercial sales of medicine but also on donated drugs and supplies.This hypocritical practice has caused some US Senators to introduce a clause into a newly tabled bill that will outlaw US government donations to countries that impose tariffs on donated medicines. Section 9 of the 'The Neglected Disease Results Act of 2005' states that '….no agency or department of the US may donate or otherwise supply medicines or medical devices, including insecticide-treated nets, insecticides, and other essential *consumables required for disease* control to a foreign country if such country imposes import tariffs or other import duties on such medicines or medical devices.'

But the backlash against medical taxes extends far beyond the US. The Geneva-based Global Fund to Fight AIDS Tuberculosis and Malaria inserts this clause in its donation policies: 'the *assistance financed hereunder shall be* free from any customs duties, tariffs, import taxes, or other similar levies and taxes (including value-added tax) imposed under laws in effect in the Host Country.'

The reason that US Senators, the Global Fund and assorted NGOs are angry is that their efforts to treat people like Emma are undermined by the very states they want to help. Some

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countries impose significant obstructions: Kenya, Tanzania, Uganda, India, Nigeria, Brazil, Morocco, to name a few, all impose financial barriers of over 27%.

Statistical analysis of tariff rates and access to essential medicines shows a significant relationship: a 1% reduction in tariffs will lead to a 1% increase in access. This is a tentative conclusion given the nature of data inaccuracies and inevitable time-lag for data collection. There are other possible explanations for lack of access, such as illiteracy or low healthcare expenditure, for example, although income level is included in the analysis. But the relationship strongly implies that tens of millions more people could gain access to life-saving drugs if their governments removed tariffs.

COUNTRY	ACCESS TO ESSENTIAL MEDICINES (%) '99	TARIFF	VAT	COMBINED TAXES
Kenya	36	22	16	38
Morocco	66	18.5	19	37.5
Tanzania	66	16.2	20	36.2
Uganda (EACU)	70	10	21	31
Botswana (SACU)	90	0.85	10	29
Peru	60	10	19	29
Nigeria	10	20	8	28
Brazil	40	9.6	18	27.6
Pakistan	65	12	15	27
Colombia	88	10	16	26
Bolivia	70	12	13	25
India	35	16	4	20

While India has possibly 8.5 million HIV cases – the highest in the world – it also has one of the lowest world figures for access to medicines – 35%. This sorry state has begun to change under a new government following a reduction in total financial barriers from a shocking 61% to 20%. This is still high, but at least a move in the right direction.

On the other hand, on 1 January 2005, both Kenya and Uganda imposed 10% import tariffs on all imported medicines in line with East African Customs Union protocols. The harm that these newly imposed tariffs will cause is likely to be considerable. The Kenyan government failed to meet its target of treating 45,000 patients on antiretrovirals at the end of 2004, treating only 24,000. The increased cost of treatment adds another hurdle to the government's already ambitious aim of treating 95,000 by the end of 2005. According to Dr Patrick Orege, director of the National AIDS Control Council, the tariff issue is '…problematic, this increase should be addressed urgently, so that we can meet our goals.' Meanwhile the treasuries of Kenya and Uganda remain silent.

Few Southern African countries have tariffs and the Southern African Customs Union scrapped all import tariffs on drugs several years ago. Some countries however do impose burdensome taxes on medicines. Lesotho, the poverty stricken mountain kingdom surrounded by South Africa, imposes a 10% withholding tax on all imported medicines.

If a supplier presents an invoice of $100 to the Lesotho government, it only pays $90, withholding 10% of the invoice. Inevitably the suppliers simply inflate their invoices by that amount so they are square in the end. But the tax doesn't necessarily make its way to the Ministry of Health's budget and so it is likely that fewer Basotho are treated as a result.

On the whole however, Southern African governments are not the worst tariff offenders, but most still impose sales taxes. While these taxes are simply absorbed into the general state fiscus to become an anonymous part of general expenditure, they can make a very real impact on the lives of ordinary people. The table below shows basic food items that could be bought if the sales tax on a month's supply of antiretroviral triple therapy was removed.

The survival rate of HIV patients is strongly dependent on adequate nutrition, and without eating more many HIV patients are unlikely to be able to get the full benefit. Indeed Emma's CD4 count (a measure of the strength of the immune system) is improving but not as fast as many of her better-fed peers.

The South African Minister of Health has frequently promoted a balanced diet, including plenty of garlic, olive oil and beetroot, as the best way of maintaining a high CD4 count, remaining healthy and thereby not requiring treatment. Yet her government's own taxation policy means that medicines are more expensive and good quality healthy food less available. The fact that the South African government has dragged its feet over the provision of free antiretroviral therapy in state hospitals makes these taxes on privately-bought medicines even more offensive.

Dr Anban Pillay, director of pharmaceutical economy evaluations within the South African Department of Health, alleges that the reduction or removal of VAT on medicines has been under discussion for some time.

'We've called for this ourselves but there seems to be a number of reasons why the Treasury is not willing to do so yet.'

It doesn't appear that the treasury will budge anytime soon, but pressure is building, and if the Senator's Act passes then US donations will be dependent on

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the removal of tariffs. Given that the US will be donating over $4bn in health aid this year (and a decent portion on drugs) this will be a powerful incentive to finally remove these odious tariffs and taxes.

Although there will doubtless be resistance from various departments of finance, poor country governments will probably have an easier time removing or reducing the taxes and tariffs on medicines and medical devices than the other barriers to treatment. Another such barrier is the burdensome bureaucracy that slows the registration and marketing of new medicines in many poor countries.

Bureaucratic barriers

In South Africa, a medicine that is registered for use in the US, EU and Japan can often wait for more than two years before the Medicine Control Council authorises its use. This not only adds greatly to the costs of doing business for drug companies, but constitutes a colossal opportunity cost and denies often crucially needed medicines to patients. Thousands of patients are forced to wait far too long before nameless, faceless bureaucrats satisfy themselves that the drugs are acceptable. This is not only incredibly disempowering for patients, but can be quite deadly.

Although Southern African governments were supposed to be harmonizing their medicine bureaucracies nearly a decade ago, little progress has been made. In fact, some countries have gone in the opposite direction. Several years ago Namibia dreamt up what must be one of the most pointless and burdensome new regulations in that country's history. Namibia achieved its independence from South Africa in 1990 and prior to that any medicine that was registered for use in South Africa was automatically registered in Namibia. After 1990, with a new independent department of health and a new medicine regulator, the Namibian government decided to require the re-registration of all medicines registered prior to 1990.

Companies that had been selling medicines in Namibia for years were suddenly forced into a hugely expensive, wasteful and pointless exercise that must have left head offices in the US and Europe in despair. Namibia is a tiny county with a miniscule market for drugs, and yet that government was actively discouraging any drug company from doing business there.

Changing these regulations and reforming the bureaucracy will take longer and will be more politically difficult than removing taxes and tariffs, particularly in countries that do not have a significant domestic drugs industry. Decades of shameless bureaucratic empire-building have left many civil servants clinging on to the rules and regulations that they impose. It is these rules that keep them in jobs, despite the harm that these regulations cause patients, and so making these essential reforms will require some political savvy.

Act now

In the long run, poor countries simply have to grow faster and create more jobs and wealth in order to improve the health of their population. This will require changes to economic policy and greater economic freedom, but these will not improve healthcare overnight. However, there are some further crucial steps that governments can and should take now. Removing the pernicious taxes and tariffs on medicines should be at the top of the list. Reforming the medical bureaucracy will also be essential and though difficult, any lack of leadership on these issues makes a mockery of many poor country governments' stated objectives of improving healthcare for all.

Next time a celebrity draws attention to some worthy cause, let us hope that he or she has the decency to investigate the situation fully and not to simply point the finger at the popular villain, but to champion change for what may be less reported and less obvious, yet far more harmful. – **Richard Tren**

Briefly

Overseas lifeline: Remittances to Africa and Asia from overseas workers are a key source of development funding, sometimes outpacing official development assistance, and a lifeline for millions of poor families, says a new World Bank report, 'Global Development Finance 2005: Mobilising Finance and Managing Vulnerability.' Remittances to developing countries are estimated to have risen by $10 billion last year to $126 billion, of which Africa's share is about 15%, it said.

Museveni's spin doctors: The Ugandan government is to spend about $675,000 with London-based consultancy Hill and Knowlton to improve its fading image abroad. The deal emerged after President Yoweri Museveni asked foreign donors to respect his country's sovereignty. The UK recently cancelled $10m of aid, saying not enough had been done to establish fair multi-party politics and a number of critical reports have appeared in the western media.

Playing fair? Tanzania's opposition parties questioned the National Electoral Commission's ability to conduct a free and fair election in October, after it allowed the ruling Chama Cha Mapinduzi (CCM) to break electoral rules by holding rallies for its presidential candidate, Foreign Minister Jakaya Kikwete, long before the scheduled start of campaigning in August. President Benjamin Mkapa's final term expires this year. Ibrahim Lipumba, a US-trained economist, is the candidate of the main opposition, the Civic United Front, which is strong in the semi-autonomous Zanzibar.

Yala yields not: The pre-election mood in Guinea-Bissau is volatile and ex-President Kumba Yala's demands that he be reinstated are not easing the tension. Yala briefly occupied the presidential palace, with the assistance of a group of soldiers, in late May. A transitional administration has been in power since Yala was toppled in a bloodless coup in 2003 and will hand over power after the polls on 19 June. Yala is the candidate for the leading opposition group.

SPECIAL FEATURE

Unleashing Investment By Encouraging African Savings

Africa has the world's lowest savings rate, with little capital for banks to lend to grow productive enterprise. South Africa is changing the rules by bringing the poor into the banking system.

HIGH savings rates and a strong, competitive financial sector are vital to the success of any developing economy, yet on both counts Africa lags far behind Asia. Even in the continent's most developed country – which President Thabo Mbeki describes as a nation of two economies – millions of South Africans are outside the banking system, with minimal savings and little access to the credit needed to develop small businesses.

Now, under pressure from the government, South Africa's banking sector is trying to reach that 'second economy' by encouraging the poor to use the banks to save money, which in turn could boost the credit available to expand businesses, jobs and wealth.

Across the continent, getting those second economy savings out from under mattresses and into banks – where they can contribute to economic growth – has long been blocked because of the high fees banks charge and the extensive paperwork needed to open an account. Only 47% of South Africans can afford the normal bank fees, according to research by Genesis Analytics for FinMark Trust, which promotes access to financial services in the Southern African region.

To change that, South Africa launched the Mzansi scheme to cut banking fees and paperwork. Mzansi, meaning 'south' in Nguni languages, is a collaboration between the big four banks (Absa, First National Bank, Nedbank and Standard Bank) and the Post Office's Postbank. By May this year, seven months after its launch, a million people had opened new low-cost accounts, the first access to formal banking for many. The Banking Association says the accounts have brought an extra 4% of the population into the banking system, placing the country at the same level as Argentina and a step away from Malaysia.

'The take-up has been impressive and certainly better than expected,' says Richard Ketley of Genesis Analytics, a consultancy in Johannesburg specialising in emerging markets' financial sectors. He says the real boost could come if social security payments are banked instead of drawn in cash. 'The government pays out billions [of rand] a year in welfare grants. If these were paid into Mzansi accounts rather than in cash it would make it very profitable for the banks.'

Convincing banks that they can profit from serving the poor has required a change in mindset in an industry long comfortable with high profit margins and low competition. Mzansi is an effort to get banks to test whether they can also profit from large numbers of small, low-fee accounts. The programme is the result of pressure on the big banks sector by both government and communities to meet the needs of South Africa's unbanked, of whom there are 17 million according to the central bank. Instead of passing legislation, which would force companies to change but possibly get the formula wrong, South Africa opted for a voluntary system in which industries are pressured to negotiate a charter under which they agree to meet certain social transformation goals. Under the Financial Services Charter, the banks have to attract 8 million new customers within three years.

Mzansi accounts have reduced fees and are available to customers who have low incomes or erratic incomes or are not in formal employment. They can use automated teller machines at any of the big four banks or Postbank to draw money at a much lower cost than for traditional accounts. The Banking Association estimates that Mzansi accounts are between 15% and 40% cheaper to use than normal bank accounts. The association believes that most of the million Mzansi customers were previously outside the banking system, rather than switching from an older account, although they cannot at

The Perils of Pocket Money

LOVENESS Malaluka, a domestic worker in Johannesburg, recently opened a bank account to start saving. "When I have the money in my room I spend it too quickly. I spend R20 here and R20 there, but if I have to go to the bank to get money I will spend less".

Nelson Ngwenya, who works as a part-time gardener in Johannesburg, says he opened a Mzansi account after he heard about it on the radio. 'I wanted to find out more because it is not safe to keep my money in my room.' Nelson lives in a flat in Hillbrow, a high crime area.

'Everybody knows you keep your money in your bedroom so if they come with guns and ask me to give them my money I will do it – I don't want to die, it's not safe.'

Nelson was attracted to Mzansi not only because it is cheaper but also because there was less of the onerous paperwork that put him off opening an account before. 'I wanted to open a bank account before but it was too expensive and they wanted all sorts of information like payslips.'

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this stage be precise. Yet, even if they are all new bank customers, Mzansi will have to continue growing at the same rate to reach its target of attracting 8 million new customers in three years.

'While we understand that even one million account holders is just a start in the grand scheme of Charter objectives, it is extremely encouraging to see that the appropriate target market is largely being reached,' says Colin Donian, director of the Mzansi Initiative at the Banking Association. Donian adds that 62% of Mzansi customers are between 25 and 54 years old, most are black, and they use their accounts 'in a similar manner to existing entry-level clients.'

Savings + bank credit = growth

The banks stand to benefit as well as the poor. The total balance in Mzansi accounts so far is about $50 million, a small fraction of South Africa's estimated $30 billion in short-term bank deposits. But, about $900 million of remittances moves around the informal economy – which includes savings tucked under the mattress, sent home by bus, or paid into stokvels (local savings cooperatives), or burial societies – which could be brought into the formal savings and lending pool. This estimate is based on research for South Africa's Financial Diaries Project conducted by the University of Cape Town.

Remittances sent home by Africans working abroad is another major source of funds outside the banking system. A recent World Bank study estimated that the continent received $12 billion in overseas remittances in 2002: $4 billion to sub-Saharan Africa and the rest to North Africa. Yet only one-third of sub-Saharan countries even report remittance data.

'There is a strong correlation between bank deposits and lending. But this requires lower-cost banking. So far no country in Africa has made that transition,' says Ketley.

Other countries on the continent with weak banking and savings performance will watch South Africa's progress keenly. A previous survey by FinMark Trust found that three quarters of bank customers save regularly, compared to only one in seven of the unbanked. There is also a clear link between high banking fees and low numbers of bank accounts in individual countries.

A country needs total savings of above 20% of GDP to support real economic growth of over 3% a year, according to the International Monetary Fund (IMF). Savings in sub-Saharan Africa average a mere 15% of gross national income compared to the 36% savings rate for South East Asia.

Improving savings and access to banking are now priorities for governments across Africa, hoping that cheap banking and greater savings will boost economic growth. The rest of Africa's banking sector trails far behind South Africa, where the banks already have a good penetration of the middle and upper income earners. The Genesis survey shows only 11% of Kenyans have bank accounts, and only 10% of Nigerians, even though banking charges in Nigeria are relatively low. In Nigeria there are an estimated 40,700 people per bank branch or ATM, compared to 2,630 people per branch or ATM in South Africa.

Because banking charges in Kenya

Creative Alternatives Can Boost Savings Rates

SOUTH Africa's Mzansi low-cost banking programme is but one of several creative new approaches to improve savings rates and participation in banking:

The Bank Account Lottery: First National Bank (FNB), South Africa's second largest bank has hit the jackpot with its latest savings initiative. Tapping into the lottery mania that has swept the country, the bank is offering a 'Million a Month' bank account that pays out monthly prizes of up to R1 million. Instead of trying to convince people of the need for long-term savings, they are offering depositors a chance to get rich overnight by saving money. For every R100 deposited the customer gets one draw in the monthly competition and stands in line to win prize money ranging from R1,000 to R1 million. Account holders must give 32 days notice before making withdrawals and receive no interest but the account carries no fees. It is based on a successful initiative in Pakistan where over 1 million accounts were opened in the first year and appeals especially to Muslim investors whose religion prevents them from earning interest.

SIMTEL: Visa, the global payment systems association, has worked with the Rwandan central bank and the six Rwandan banks to set up a joint processing system called Simtel, which acts as a joint accounting office for all six banks, cutting costs significantly. It issues and handles cards, sends out statements and handles signing up of retailers to the Visa system.

Free banking for SA's unemployed: South Africa's First National Bank, along with the Eastern Cape Provincial government, offers the 900,000 recipients of social grants in the Eastern Cape free banking. The accounts offer free withdrawals and no monthly fee. Apart from bringing cash into the formal sector it also reduces the risk of theft. FNB have rolled out thousands of mini-ATM's which are housed at retail stores where customers can draw money.

South African retail bond: Government bonds have been traditionally only traded by banks and big investors, but the South African government got ordinary citizens into the act by offering a bond that the public can purchase directly through a website or at the post office. Since May 2004, 16,550 investors have bought nearly $205 million of the bonds. The bond is effectively a fixed deposit for a two, three or five-year period and offers competitive interest rates from 7.4% to 8.25% with no transaction costs. **– Maya Fisher-French**

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remain exceptionally high, few Kenyans have bank accounts and those that do use them less. Monthly charges for bank account holders are estimated to be around 32% of the monthly salary of the average blue collar worker. A service that is almost universal for South African account-holders – the stop-order or monthly direct debit from one account to another to pay regular bills – is so expensive in Kenya (about $30 a transaction) that it is hardly ever used.

Poor national infrastructure is the main reason for banking's low penetration in many African countries, says Ketley. The unreliability of electricity and the high cost of telecommunication drive up costs and limit the ability to deploy cost-cutting computer technology.

'The service in Nigerian banks is sometimes very good, but they are forced to operate with cumbersome and outdated systems by the lack of power, telecommunications and other vital infrastructure. This means the banks just can't expand to meet the needs of the population,' he says.

'The fixed costs of setting up an electronic banking system are very high, but subsequent costs are very low. It costs much the same to process 20,000 electronic transactions as it does for the computer to process just two,' says Tony Twine of Econometrix.

The high start-up cost of electronic banking is not the only hurdle to delivering low-cost banking to a broader customer base in Africa.

'Some governments say they want electronic banking systems but want to control them. They want a nation-alised system, which takes away the inter-national connectivity as well as the advanced technology and economy of scale which organisations like Visa can offer.

'You can't put a national fence around electronic banking if you want all the benefits. You have to be part of the big bad world,' says Twine. – **Maya Fischer French**

New Technology Expands Banking Access

AFRICAN banks are caught in a vicious cycle: lack of infrastructure and weak technology mean poor service and high costs. Few customers can access bank services, so savings levels remain low and businesses cannot borrow to expand.

But new computer, smart-card and telecommunication technologies are changing the face of banking, bringing faster, more efficient services to many people who could never before afford to hold a traditional bank account.

Mobile telephones let customers carry their banks in their pockets. Hundreds of retailers for beverages from Zambian Breweries now pay delivery drivers by sending text messages on mobile telephones. In South Africa, MoPay has launched a service allowing payments to be sent and received via 'SMS cheques'. Participants pre-register their bank details, and a password. When a payment request is received, computers verify the user and transmit the funds to the right account.

Revolutionising banking

In Kenya, the number of new credit and debit cards issued grew by 40% for the year ending June 2004. Mozambique reported a 52% increase in cards issued with a 213% growth in card transactions, including ATM withdrawals. Although much of the increase comes from issuing cards to existing bank account holders, Kenya's greater use of electronic banking has boosted the growth of bank customers from 6% to 11% of the population in the past four years.

New technology can cut costs. High banking costs are the result of paper-based payment systems, high labour costs and markets too small to enjoy economies of scale. Introduction of electronic payment systems can cut transaction times and staff levels bringing more money into the formal financial environment, according to a report by the Commonwealth Business Council and Visa International. New technology can speed the growth of banking services as it does not require construction of new bank branches, the report says.

New technology, including electronic and cell phone banking, also speeds up the circulation of money through an economy and can accelerate GDP growth, according to research by Econometrix, a South African consultancy, and Visa International. Electronic banking in many African countries not only helps savings, but reduces the bundles of cash people have to carry, especially in countries which have suffered years of hyperinflation, says Anthony West of Visa Southern Africa.

Improved Security

Banks are still educating customers as to the benefits of using debit cards at a point of sale terminal. In South Africa this makes up only 7% of debit card transactions. But fear of crime is causing many customers to carry plastic.

'I like it that I can use the card at Checkers [grocery store] then I don't have to get money from the bank and I don't have any extra money in my pocket which I will spend. I think it is also safer than carrying money on the taxi,' said Lindiwe Ndlovu, a domestic worker in Johannesburg.

Sometimes, fairly low technology leads the way. Much as mobile phone users load pre-paid airtime, debit or charge cards with an embedded computer chip can be loaded with money. Users then spend the funds by swiping the card at point-of-sale machines. A shop owner simply needs a machine that can read the card and update the chip. The retailer downloads the information to the bank at the end of the day or week, reducing its calls to the bank a hundred fold.

This pre-paid, bank-on-a-card system became common in Lagos, Nigeria, several years ago even though credit and debit cards linked to bank accounts are still rare there because of fraud, lack of ATMs and poor communications links. In October 2004, international payment organisation Mastercard, in partnership with low-end retail bank Capitec, launched the first pilot project for these cards in South Africa. If the pilot is successful it will be rolled out across South Africa with the intention of introducing it to the rest of Africa. – **Maya Fisher-French**

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What Ails Africa's Banks

Lack of credit and underdeveloped financial services prevent growth in Africa, businesses say.

FILLING the gap between street-level informal traders and the big corporations run by multinationals or the state, Africa's small and medium-sized firms could be the driver of jobs and economic growth. But an essential element is lacking: affordable credit.

'The difficulty in obtaining credit is consistently rated by firms as one of the greatest barriers to operation and growth. ... In particular, small business, women and the poor face the greatest difficulty in obtaining finance,' says a World Bank study, 'Doing Business in 2005: Removing Obstacles to Growth'.

The conclusion was backed up by an *eAfrica* survey of 56 business organisations in 31 African countries (*eAfrica,* February 2004). Respondents cited lack of credit as the top obstacle to growth.

In Africa's cash-based economies, weak financial sectors prevent small businesses from borrowing the capital they need to expand. Mostly, the banks make money through high fees, big margins and trade finance deals, but rarely lend long-term project finance to local firms, businesses say.

Fixing the problem needs fundamental change. Cutting the cost of banking fees is a vital step to bring more Africans into the banking sector, which can boost the amount of savings available for lending. But even when banks have funds, a variety of structural, regulatory and legal problems hinder lending.

Weak systems, low lending

The banking sector in Africa is small, and there's a limit to which it can fund large projects, says Richard Ketley of South African economics research firm Genesis Analytics. Expensive and unreliable electricity and telecommunications limit the reach of African banks, Ketley says.

'Financial deepening has not taken place,' says John Macaskill, head of First National Bank's operations in Botswana, Namibia, Swaziland and Lesotho, who agrees that the lack of access to banking services undermines economic growth.

Part of the solution would be to increase the ratio of deposits used for lending. South African banks tend to lend out well in excess of 80% of their deposit base, but this can be as low as 20% to 40% of deposits elsewhere in Africa, where economies are mainly cash-based, says Macaskill.

'It's possible that there is a mistrust of banks and that there's a cultural shift that needs to take place,' he says. But administrative conditions are also unfavourable to banking; legal and taxation systems hard to deal with and property rights not always recognised.

'Some countries don't even have national IDs. Compliance and the regulatory environment have become more stringent, and all this adds to the cost of finance,' Macaskill says.

By developing-world standards, Africa is under-banked, except South Africa, where just over half the population have bank accounts. Consumer finance, such as mortgage bonds for houses and loans for vehicles, is rare outside South Africa. Deposits also tend to be short-term, with concerns about macro-economic stability and volatile interest rates making banks reluctant to offer long fixed-term rates. Reg Rumney, of Johannesburg-based consultancy BusinessMap, blames poorly developed debt markets. African governments issue mostly short-term Treasury bills, with little long-term debt being issued.

'This raises the cost of debt for the government, and leads to inflexibility,' Rumney says. 'You need marketable, liquid debt, so that you can buy and sell it, in a mix of long- and short-term. You need to bring down the cost of capital. How you do it is another question.'

Inadequate legal systems

Zimbabwean entrepreneur Strive Masiyiwa, whose Econet Wireless firm operates in several African countries, says the rule of law is also critical.

'The people in power don't consider themselves subject to the law. The courts don't work,' he told *eAfrica.* 'The reality is that there are only about five

The Bad Debt Crisis

THE failure of customers to repay loans, particularly among government-owned or politically-connected banks, has contributed to severe banking crises in many countries. Contributing factors include high inflation, excess government borrowing, rapidly declining foreign exchange rates, commodity price shocks and the inability of legal systems to enforce loan contracts.

- Cote d'Ivoire: 1988-91 – non-payment of loans at four largest banks reached half of total credit outstanding. Cost to government to fix the problem: 25% of GDP
- Benin: 1988-90, all three national banks collapsed, 78% of bank loans were non-performing at end of 1988
- Kenya: 1993-95 – solvency problems in banks accounted for over 30% of financial system assets.
- Tanzania: 1987-90 – 60-80% of all loans non-performing at end-1994.
- Uganda: Half the banking system faced insolvency problems in 1994.

Source: IMF Working Paper, April 2004: 'Banking in Sub-Saharan Africa: What Went Wrong?'

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countries in the sub-continent where the courts work to protect legal rights.'

If a bad debt judgment can take years to get from the courts, banks are reluctant to lend – or when they do, they demand high levels of collateral from clients. 'In the US it takes less than a day to get a judgment against someone,' Richard Ketley says. 'In Africa, it can take years. Tanzania is impossible, Uganda is OK, and in Nigeria, who pays wins.'

The World Bank says the difficulty of recovering debts is a key obstacle to African business development. Its report, 'Doing Business in 2004: Understanding Regulation', examined the business environment in 130 countries. It found that in many emerging markets it was costly to enforce a simple commercial contract. While the cost of enforcement was just 1% of the disputed amount in the UK, Canada and Australia, it was over 100% in countries such as Malawi, Madagascar, Burkina Faso and Indonesia. Resolving a payment dispute took more than 500 days in eight African countries and cost on average nearly 10 times as much relative to national per capita income in sub-Saharan Africa than in the developed world.

African credit is hard to find, in part, because there are no systems to track credit repayment histories of borrowers and blacklist bad debtors. Out of 36 African countries surveyed by the World Bank, only three countries – South Africa, Namibia and Botswana – had any meaningful private or public credit registry systems, according to the bank's 'Doing Business in 2005' study.

The World Bank also says that excessive red tape puts businesses in poor countries at a big disadvantage. Before businesses can borrow, they must formally register their ownership of land or other assets. But the process itself is exceedingly slow and costly in Africa. The bank found that in sub-Saharan Africa, the cost of registering collateral to get credit averaged 41.8% of per capita income, although the range was huge – in Benin it was 80% and 3% in Kenya. The average cost for leading industrialised countries is 5.2%.

The effect is to reduce the supply and raise the cost of bank loans. In much of Africa, banks only lend to the largest local firms and subsidiaries of multinationals because it is so hard to recover debt from defaulters and they pass on the cost of high loan risk to borrowers through higher interest rates and levels of required collateral. Informal businesses, which need credit to grow, are too risky for banks to finance as they often lack collateral, management skills or even literacy.

High risk, high returns

Banks also demand high rates of return on big project finance in Africa because they perceive country risk to be high, taking into account currency, inflation, legal and political risks. In South Africa, projects need to make a real return of 10% to clear their risk, but in China, only 2% is required.

'Just imagine how many projects we've lost to China,' says Michael Power, from South African financial services provider Investec. 'Africa received $13 billion in foreign direct investment last year, as a continent. China was probably receiving that every month.'

The risk also pushes up the cost of project finance. 'The very high cost of capital means that only certain projects get done, and those tend to be in the natural resources sector,' Power says. 'It's a very mathematical process. Politicians don't understand this, they can't believe it's so cut-and-dried. But they're not the ones who make the decisions. Decisions are made by businessmen, using strict processes to determine whether their numbers add up. And all the goodwill in the world isn't necessarily going to help.'

Using Power's formula, between 50% and 70% of 'bankable' projects are in the oil sector. 'For instance, Angola received the most foreign direct investment (in Africa last year) and that's because of the offshore oil projects,' Power said.
– Jocelyn Newmarch

Briefly

Zim land U-turn?: As Zimbabwe's economic crisis deepens, the government is considering a plan to entice back the white farmers, whose land was seized in the past five years, in a bid to end the collapse of its agriculture. Governor of the Reserve Bank Gideon Gono proposed this after devaluing the Zimbabwe dollar by 31%, adding that skilled white farmers and other investors would be guaranteed uninterrupted tenure of five to 10 years. Gono denied this was an admission that Zimbabwe's land reform had failed.

Consultants' gravy train: Much of the West's official aid is being recycled back to donor countries, according to British aid agencies Action Aid and Oxfam, citing France and the US as the worst offenders. Their recent report, 'Millstone or Milestone', was supported by the World Bank which said western consultants receive $20 billion from global aid budgets, which is around 40% of the total global development assistance.

Despite all odds: Africa managed economic growth of more than 5% in 2004, the highest in eight years, boosted by high commodity prices, according to a report from the OECD Development Centre. High oil prices and expansion of oil and gas production, greater political stability and more official development aid were the main factors, it said. Meanwhile, the world's richest countries, ahead of the G-8 summit in July, have written off $40 billion of debt owed by 18 countries, most of which are African.

Bingu on track: Malawi's macroeconomic stability, control of public expenditure and anti-corruption drive since Bingu wa Mutharika became president last year have boosted its chances of getting official aid donors to renew funding. Sweden has broken a four-year aid freeze and given the country about $5.5 million in budget support. Since 2001 the International Monetary Fund and other western donors had barred developmental aid to the country, due to the previous government's overspending.