PERISA Case Study 2 Private Sector

SADC Payment Integration System

By Lesley Wentworth

On 22 July 2013 the Southern African Development Community (SADC) Integrated Regional Electronic Settlement System (SIRESS) became operational in the four countries of the Common Monetary Area (CMA): South Africa, Namibia, Lesotho and Swaziland. This is a first step to implementing a common electronic cross-border payment system across all member states of the SADC regional economic community (REC).

The implementation supports the aims of other SADC initiatives, such as harmonisation in trade tariffs, smoother and efficient border controls of trade transactions, and integration in information and communications technologies. This project introduces a regional interbank settlement system. However, there are also plans for regional clearing capability for low-value (electronic funds transfer) credits and debits; regional clearing capability for card and ATM transactions; and regional central securities settlement systems are being explored.[1]

The implementation of SIRESS has relied on the active participation of the private sector – essentially commercial banks that are members of the SADC Banking Association (SADCBA) – and the facilitation by central banks in the SADC member states. Through this

1 SADC Banking Association, 'SADC Payment Project Presentation', SADC Open Session at SWIFT ARC, Kampala, Uganda, May 2012.

electronic system, money clearance across borders can now take place within the same working day, whereas with cheques and paper-based systems the clearance period is between seven and 21 working days.

CONTEXT

Payment, clearing and settlement systems (also known as financial market infrastructures) are an essential part of the global financial system, which allows financial institutions to serve customers and clients across the world. This payment system consists of a set of instruments, banking procedures and interbank fund transfer mechanisms that ensure the circulation of money regionally in SADC and worldwide.

Successful regional financial integration (RFI) leads to an increase in capital flows moving towards an equalisation of commodity and asset prices, and returns on financial assets traded in member states. Monetary and financial integration is a complex set of processes from collaboration to co-operation, to unified financial market codes, markets and services – and is reliant on stable domestic financial systems within the particular region.[2]

RFI is considered to benefit regional member states in the following ways:

- It provides incentive for domestic reforms.
- It increases economies of scale in operation and competition.
- It promotes foreign direct investment.
- It allows local financial services institutions to grow regionally, continentally and globally.

HISTORY OF SADC FINANCIAL INTEGRATION AND THE SADC PAYMENT SYSTEM

In the late 1980s a process of financial reform and liberalisation took root in many African countries, prompted by structural adjustment programmes supporting loans from the Bretton Woods Institutions. SADC member countries have, by and large, liberalised their financial systems and have recorded solid macroeconomic performance in recent years in their common pursuit of macroeconomic convergence. The convergence targets specified in the Regional Integration Strategic Development Programme (RISDP) have the aim of maintaining macroeconomic stability in the region, thereby contributing to faster economic growth and laying the basis for an eventual monetary union.

The SADC Finance and Investment Protocol (FIP) is a vehicle for the implementation of the RISDP, which provides strategic direction to the SADC integration process. The RISDP economic targets include the creation of a free trade area by 2008, a customs union by 2010, a monetary union by 2016, and a single currency by 2018. These targets have had to be delayed, especially with the impact of the European sovereign debt crisis on the region – the latter event calling into question the long-term prudence of monetary unions.

The FIP was signed in August 2006 by 14 SADC member states (excluding Seychelles), was ratified by a two-thirds majority in 2010, and came into force on 16 April 2010 with two broad objectives.

- To improve the investment climate in each member state and improve foreign and intraregional investment flows.
- To enhance co-operation, co-ordination and harmonisation in financial sectors at national level in the region.

At the May 2009 meeting of the SADC Committee of Central Bank Governors (CCBG), approval was given for the initiation of the SADC Payment Integration System project. The project team responsible for the payments system was tasked with, among other things, involving other CCBG subgroups to ensure that the intersecting functional areas and requirements for regional integration are considered when coming up with the conceptual design of the payment system.

The official launch of the SADC Payment Integration System project took place in February 2010. The SADC CCBG has since developed a monetary and financial statistical database; developed an information bank on the policies and structures of SADC central banks; improved the national clearance, payments and settlement systems; and facilitated the repatriation of bank notes and coinage among SADC countries. The SADC CCBG adopted the SADC Central Bank Model Law in 2009, whose Chapter VI enshrines central

2 AfDB, 2010.

banks' strategies for stabilising financial systems in the SADC region. The law's provisions on 'disclosure, the accommodation of banks, emergency liquidity assistance, and central bankers' banker role, including as lender of last resort'[3] are considered robust. However, there is a perceived omission of capital and liquidity requirements.

A proposal by the project team set out the advantages of using the SADC CMA to test the possibility of implementing a single-currency cross-border settlement system. The introduction of this system will mean that participating banks will be able to exchange financial transactions through a single settlement authority; and cross-border payments made in the member state's currency will be denominated in the South African rand. This test case using the CMA went online in July 2013 as discussed. It is further envisioned that other SADC countries will adopt the system through a type of 'variable geometry' approach towards the SADC monetary union.

Influencing factors

Unequal political commitment from SADC member states has led to less than unanimous support – through slower than desired ratification – for the various protocols. This has resulted in regulatory inconsistencies in a variety of sectors in countries across the region. SADC countries are widely heterogeneous with different economic vulnerabilities. Smaller SADC countries are reportedly hesitant to relinquish economic (and political) sovereignty to a bloc where economics and politics are largely dominated by South Africa.[4]

Yet it is most likely that these small countries will benefit most from the risk-mitigating mechanisms of a monetary union (for example, against symmetric shocks). There is thus a misalignment of incentives, capacity and will for moving this regionalisation process among the countries – such as South Africa, Mauritius and Botswana – with effective insurance mechanisms, as well as a good monetary policy, versus the smaller countries, which stand to gain but do not have much capacity to accelerate the project.

In addition, there is some disincentive for smaller sovereign states to give up the application of their independent monetary policy to react to asymmetric shocks, which is required in the move to a monetary union. The SADC Payment Integration System project does, however, offer the opportunity for member states to develop an internationally accepted national payment system for their economies. This will facilitate the development of their domestic financial instruments and will improve trust in, and security of, their financial institutions and markets.

The overlapping membership of certain SADC member states with other RECs, as well as the probable incorporation into the Tripartite Free Trade Area (TFTA), does introduce some tension into the level of commitment some SADC members have towards financial integration – for instance, the case of Mauritius. The Central Bank of Mauritius is the settlement bank of the Regional Payment and Settlement System (REPSS) of the Common Market for Eastern and Southern Africa (COMESA), which became operational in October 2012. REPSS is an initiative of the COMESA Clearing House, which is fully endorsed by all 19 COMESA member states and which enables the faster transfer and receipt of funds within COMESA at a lower price and in a less risky manner.[5] The REPSS business model has mobilised central banks with commercial bank participation playing a much lesser role.

Success of the SADC project will thus be measured not only on the basis of the pilot project rolled out in July 2013 across the CMA, but also on the number of SADC countries that follow suite. The SADC Payment System is expected to be on a platform that is easy to use and suitable to convert, should other RECs, such as COMESA and the East African Community, wish to consider using it under the proposed TFTA. With the COMESA REPSS nearly a year established, it is an opportune time to assess the relative strengths of the two systems.

Key institutional players

South Africa acceded to the SADC Treaty on 29 August 1994 and was shortly thereafter allocated responsibility for co-ordinating the new SADC Finance

3 Zongwe D, 2011, p. 99.

4 Malhotra *et al*., 2012.

5 Bank of Mauritius, 2012.

and Investment Sector Coordinating Unit (FISCU) in 1995. In 2000 a decision was taken to centralise the work of SADC through four directorates, based at the SADC Secretariat in Gaborone. FISCU ceased to exist; however, the impetus given to financial integration by the South African-based structure was set to continue.

The Trade, Industry, Finance and Investment (TIFI) Directorate, under the deputy executive secretary of regional integration, is of greatest significance to this case. TIFI is responsible for the co-ordination of regional trade and financial liberalisation, and the facilitation of competitive, diversified industrial development; increased investment; and integration of SADC into the global economy. TIFI is focused on fostering regional integration through pursuing the objectives set out in the RISDP and FIP.

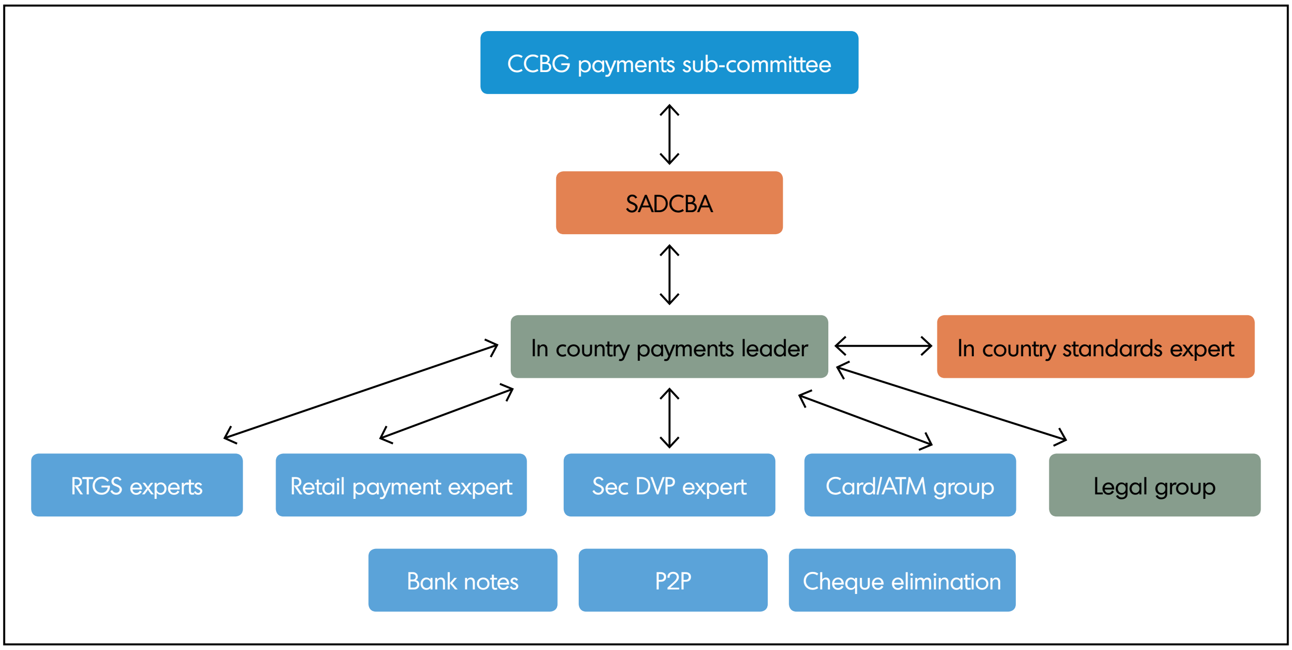
The TIFI Directorate undertakes its mandate through designated units, which include trade; customs; macroeconomic convergence; finance and investment; standards, quality assurance and metrology; and industry productive competitiveness.

The finance and investment unit has two main committees: the Committee of Senior Treasury Officials and the CCBG. The CCBG reports to the SADC Committee of Ministers responsible for Finance and Investment (COMFI), which reports to the SADC Council of Ministers.

The CCBG has five ongoing projects: the Payments Systems Project; Legal and Operational Frameworks; Exchange Control Subcommittee; Training and Development Forum; and the Information Technology Forum. Two autonomous committees report to the SADC COMFI through the CCBG, namely the SADC Committee of Stock Exchanges and SADCBA.

The SADCBA has been tasked by the SADC CCBG to establish a platform for integration of the payments and clearing system in the region. The Banking Association of South Africa is a member of, as well as the secretariat for, the SADCBA; and is responsible for executing the project. However, the participating countries are appropriately represented through voting rights and there are working groups for each of the 10 payment

Figure 1: SADCBA resources for Payments Project



Note: RTGS represents real-time gross settlements; DVP represents delivery versus payment; P2P represents person-to-person.

Source: SADCBA, SADC Open Session at SWIFT African Regional Conference, Kampala Uganda, May 2012, http://www.swift.com/resources/documents/ARC_2012_SADC_work_session_part2.pdf.

streams identified by the SADCBA.[6]

Commercial banks – members of the national banking associations in SADC – have been provided the opportunity to inform the development of financial market infrastructure that will promote interregional and intraregional trade and investment. Interventions include outlining payment instruments; business rules; and messaging standards with respect to interbank questions for improved customer service, cost savings and efficiencies in cross-border payments. The project has reportedly benefited greatly from the involvement of the private-sector banks.

Three international organisations have played a significant role in the provision of donor grants and technical assistance.

- The World Bank provided two financial grants between 1996 and 2006.
- The International Monetary Fund (IMF) has provided advice and technical assistance.
- The Bank of International Settlements (BIS) has provided advice and technical assistance.

All three organisations have also participated in the production of relevant publications. The SADC CCBG is responsible for the SADC Payment Integration System and has a project team made up of representatives from the central banks of all SADC member states. Given the relative sophistication of the South African financial services sector and the early involvement of the South African government in FISCU, the South African Reserve Bank has been an active member and agent in providing momentum to the project. The SADCBA, in particular through its secretariat (the Banking Association of South Africa), has secured the participation of its members, the commercial banking sector – especially in the pilot roll-out of the CMA Payment Systems project in South Africa, Namibia, Lesotho and Swaziland. Some of the major private banks have provided development funding and assigned individual employees as in-country payment leaders (IPLs). The responsibility of IPLs is to co-ordinate SADC Payment Integration System project activities in their countries and to be accountable for project execution, for developing governance frameworks to support project implementation, and for leading individual payment streams.

Clearing houses in SADC, including BankServe Africa, are gearing up to provide regional SADC clearing and settlement services for payment stream participants in the region. This project is aimed at enhancing trade, investment and tourism in SADC by reducing cross-border processing costs while providing greater certainty of settlements. SADC states have approved the legal framework needed to operationalise the system. Each country has domestic policy objectives, and an oversight institution will be assigned the responsibility to ensure participants in the system are operating in a 'sound environment of best practices and standards'.[7]

ANALYSIS

The SADC initiative to implement national payments systems in each of the SADC countries was launched in 1996 with the assistance of the IMF, World Bank and the BIS to help SADC member states to define their domestic strategies and development plans. In addition, the project was aimed at defining a co-ordinated regional approach to cross-border payment, taking into consideration the implications for trade, central-bank policy and foreign-exchange control. Based on the premise that a sound and robust domestic system is a prerequisite for a cross-border payment strategy and regional payments system, the SADC project was structured to ensure that each SADC country has an efficient and effective payment system that can be linked with those of other SADC member states.

Delays in RISDP monetary targets have been acknowledged by the CCBG; but rather than postpone the implementation of the SADC Payment Integration System indefinitely, the CMA pilot has been undertaken. Although the process is led by the South African Reserve Bank, it apparently has the support of the entire project team (made up of all member states). The CCBG has been able to leverage the SADCBA to operationalise many of the tasks and activities in the SADC Payment

6 High-value payment; cash leg of stock market trades, cash settlements of financial market transactions, low-value payments, direct debits for utility bills, ATM cross-border withdrawals, credit or debit cards issued to SADC cardholders, cheques, bulk repatriation of bank notes, person-to-person and commercial payments.

7 Ramokopelwa K, 2013.

Table 1: Three phases of the SADC Payment Integration System project

Commencement	Including a period of sensitisation of the various stakeholders in the financial systems in each SADC member state. All 15 SADC member countries are represented on the SADC Payment Integration System project. This phase has also included information gathering and institutional assessments to identify capacity-building needs.
Vision and strategy development	Conceptualisation of the vision for implementation of the payment, clearing and settlement system at a national level, based on each county's unique circumstances and economic objectives.
Long-term objectives and strategy implementation	Development of the project implantation plan in each country supporting the overarching objective of free trade in SADC. This includes the harmonisation of national payment, clearing and settlement systems across member states. The steps in this phase are as follows. • Agreement among countries on the acceptable cross-border model for payment systems in the region. • Financial sector assessment programmes that will identify strengths and weaknesses in countries' national payment systems, allowing them to make improvements where applicable. • Other initiatives including, inter alia, countries' legal frameworks, payment systems oversight mechanisms, and establishment of memorandums of understanding.

Source: Adapted from Masela T, 'SADC Payment System Integration: Roadmap and constraints', 19 August 2011, Protea Balalaika Hotel, Sandton, South Africa, http://www.finmark.org.za/wp-content/uploads/Pres_SADC%20PaySys%20IntegrationRdmap082011.pdf.

project. This has meant that the private-banking sector has been involved through the process – perhaps not surprisingly, as they will benefit greatly from the integrated cross-border payment and settlement system.

CONCLUSION

SADC countries are among the most diverse economies in a geopolitical region. The REC is made up Africa's largest economy (South Africa), along with some of the least-developed, small, landlocked economies (Lesotho, Swaziland and Malawi), and small island states (Seychelles, Madagascar and Mauritius). Financial integration in the region is highest among the CMA countries, where the currencies of Lesotho, Namibia and Swaziland are pegged at par to the South African rand. Interest rate movements in these four countries are highly synchronised, and South African financial institutions account for between 60% and 90% of banking system assets and deposits in the smaller CMA members. South African banks, especially the big four – ABSA, Standard Bank, First National Bank and Nedbank – are also active in the rest of the region.

The current crisis in the EU has led to a questioning of the wisdom of monetary unions. Especially in light of the overlapping membership of countries in different RECs, SADC member states will probably continue to be tempted by alternatives to SADC regional integration, such as the TFTA. This may lead to competing policy and regulatory requirements, which will make compliance more difficult to ensure. Inconsistencies in commitment to regional financial integration objectives vis-á-vis long-term fiscal stability needed to achieve a monetary union will create tensions in domestic policy processes. Moreover, the hegemonic relationships among SADC countries, embedded in the differing sizes and levels of economic and political influence of SADC members, is likely to threaten economic and financial integration. South Africa, as the economic and financial economic locomotive, has significant political clout in shaping SADC activities, schedules, and outcomes of the project. In this light, it seems the pilot SIRESS project may also represent a test of the variable geometry approach to regional processes in SADC, and may provide lessons for the RECs for the future.

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