Financialisation and the liberalization of banking and finance in Africa

Experiences

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Definitions

- Accumulation in which profits accrue through financial markets and channels rather than the real sector (the production and exchange of goods) – Arrighi (1994), Krippner (2005)

The increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of the domestic and international economies" (Epstein, 2005, p.1)

Scope

- Combining the two definitions financialization covers:
- Traditional Financial system in the economy of banks, non-bank institutions such as stock markets, microfinance, savings and loans companies, insurance services and more recently money transfer services.
- Securitisation which encompasses every part of the macro-economy – debt, money supply, future growth, trade in commodities, investment flows and remittances
- Human development services – health, education, water and sanitation services among others.
- Natural resources – land, minerals under the ground, water resources, forests etc.
- Anything where a flow income can be discerned, sliced and bundled.
- Securitisation is financial sector on “crack cocaine” according The Guardian Newspaper.

Roots of contemporary Finacialisation

While the beginnings of financialisation can be traced back to the 1950s, it was the fall of the Bretton Woods monetary system (the use of gold-backed dollars as the international currency, fixed exchange rates, and limited capital mobility) in the early 1970s that accelerated growth in global liquidity and prompted a surge of financial liberalisation and deregulation. Floating exchange rates and unregulated capital flows provided opportunities for financial innovation.

This coincides, in the African context, with the combined effects of the slump in commodity prices and the sharp increase in petroleum prces, bringing a sharp end, import substitution industrialization ad setting in motion a debt crisis which came to heard in the early 1980s.

Policy foundations for financialization.

- Changing the narrative of what is good macroeconomic policies and what is right or wrong for the role of the state in the economy.
- Practical tool-kit, enforced by international aid and the BWIs: Dismantling of controls in the flows of capital, credit ceilings and interest rates +promoting floating exchange rates in monetary policy + privatisation of state banks and the lowering of the barriers to private banking and non-banking services + refocusing Central Banks purpose predominantly on inflation management market with limited prudential regulation capacity development.
- **Result:** Unprecedented growth in the numbers of banking and non-banking institutions (the latter led by microfinance institutions benefiting from astronomical interest rates), then savings and loans companies, private insurance, investment companies and securities trading companies. In many countries the rate of growth of these institutions exceeded the capacities of regulatory institutions, leading to crisis and bailouts as in Ghana, Nigeria and Kenya.
- At the macro-economic level, high nominal interest rates (except for the Francophone countries), exchange rate volatilities and mounting debt
- **Macro-economy Response?:** More of the same + “Protection” through accumulation foreign exchange reserves + government outs of failing banks.

Banking sector in Africa

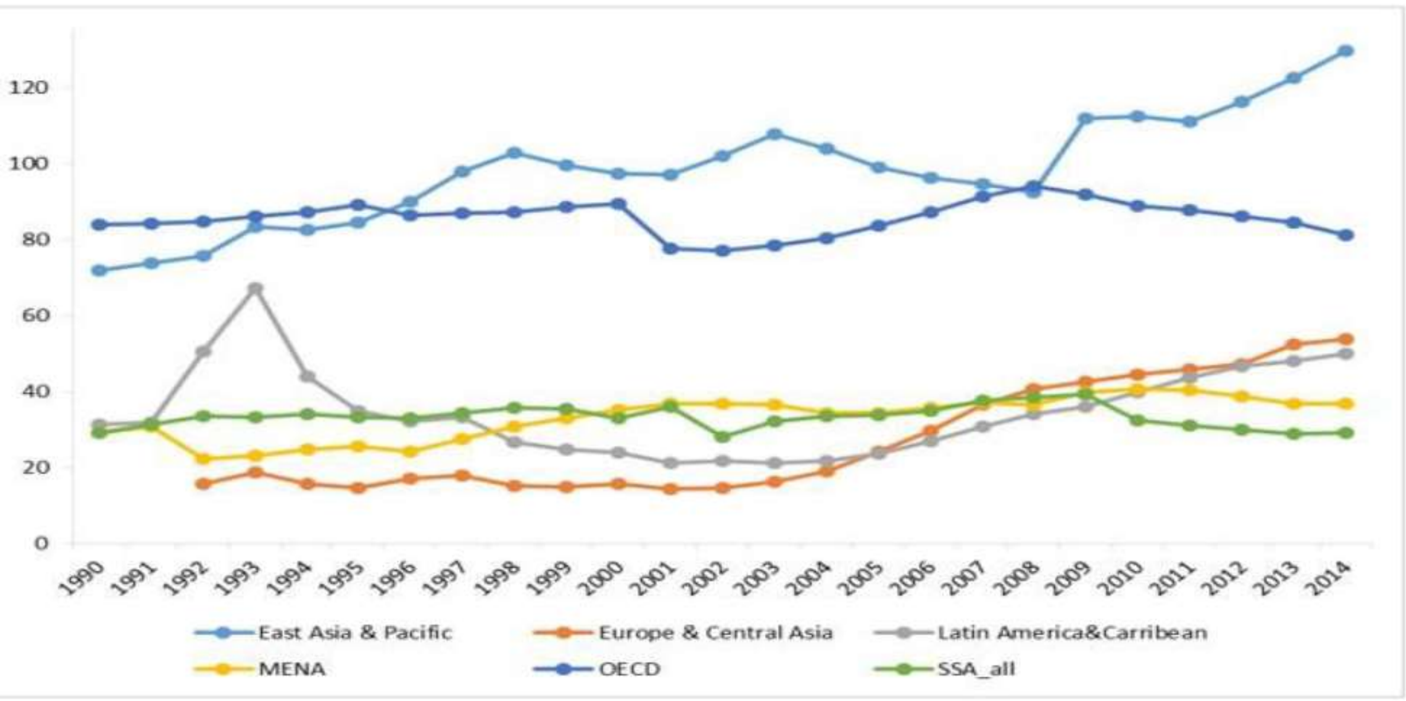
- Relatively small, fragmented and dominated (in terms of capitalization) by foreign banks, with exceptions.
- Few pan-African banks, exception Nigerian banks (Zenith and UBA) and ECOBANK to some extent.
- Large numbers of banking institutions per country relative to size of economy
- Different strategies by different countries to manage the banking sector – spreading Kenya - Deepening (Nigeria, South Africa and recently Ghana) and limited, if any regionally based prudential regulations.
- High levels of non-performing loans leading to collapse, restructuring, mergers nd acquisitions – Ghana ($2.2bn bailout).
- Nevertheless penetration (credit/GDP) similar to other developing regions but gap widening since 2008.
- Bank credit growth linked to performance of commodity markets and government deficit financing needs constrained by.

Bank lending is also pro-cyclical with little scope for reserves in times of downturns.

Traditional Financial System – The banking Sector

Private Credit by Deposit money banks (%GDP)

Source: McKenzie R, Univ of Witswatersrand

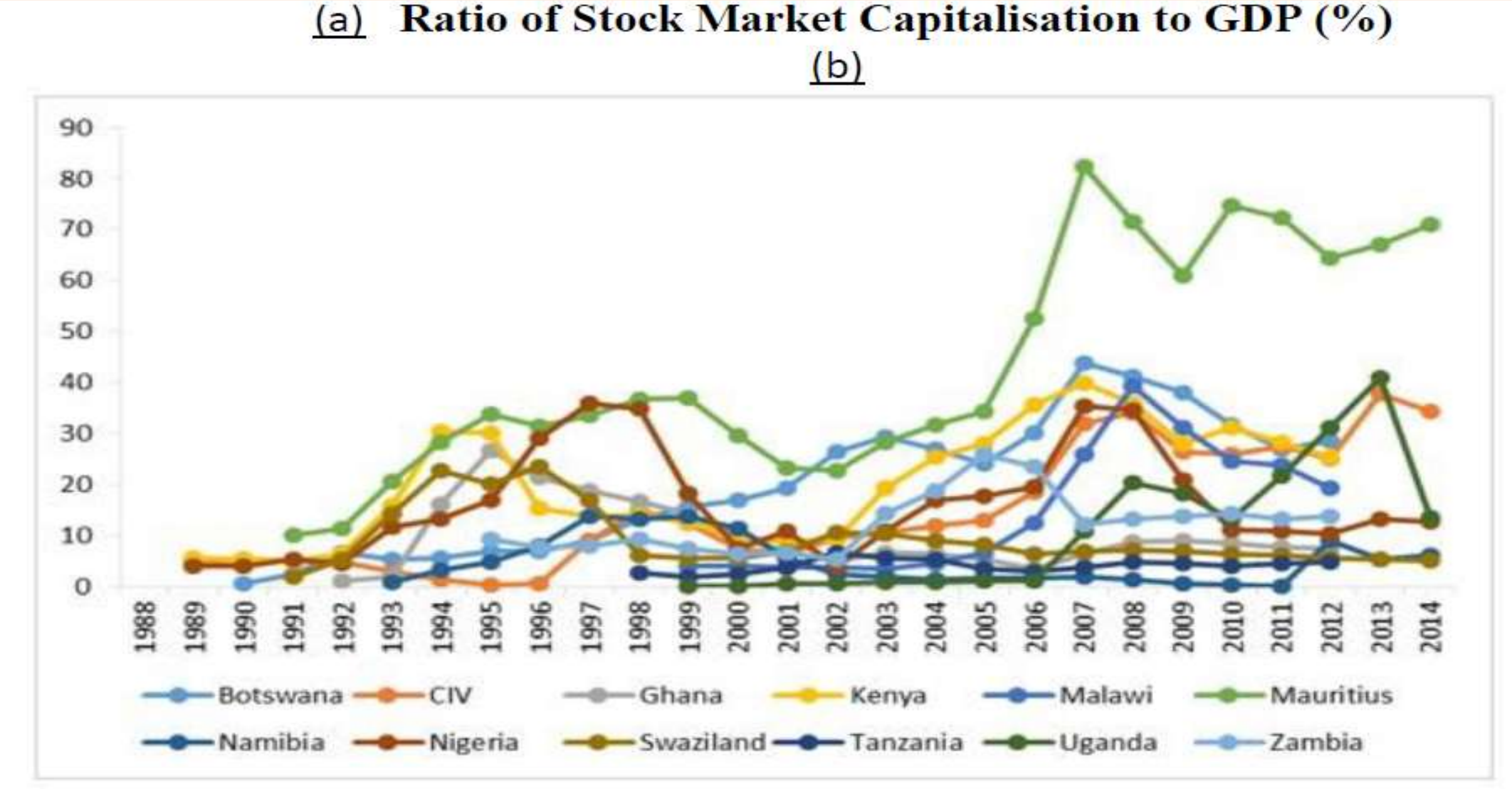


Source: World Development Indicators, 2015

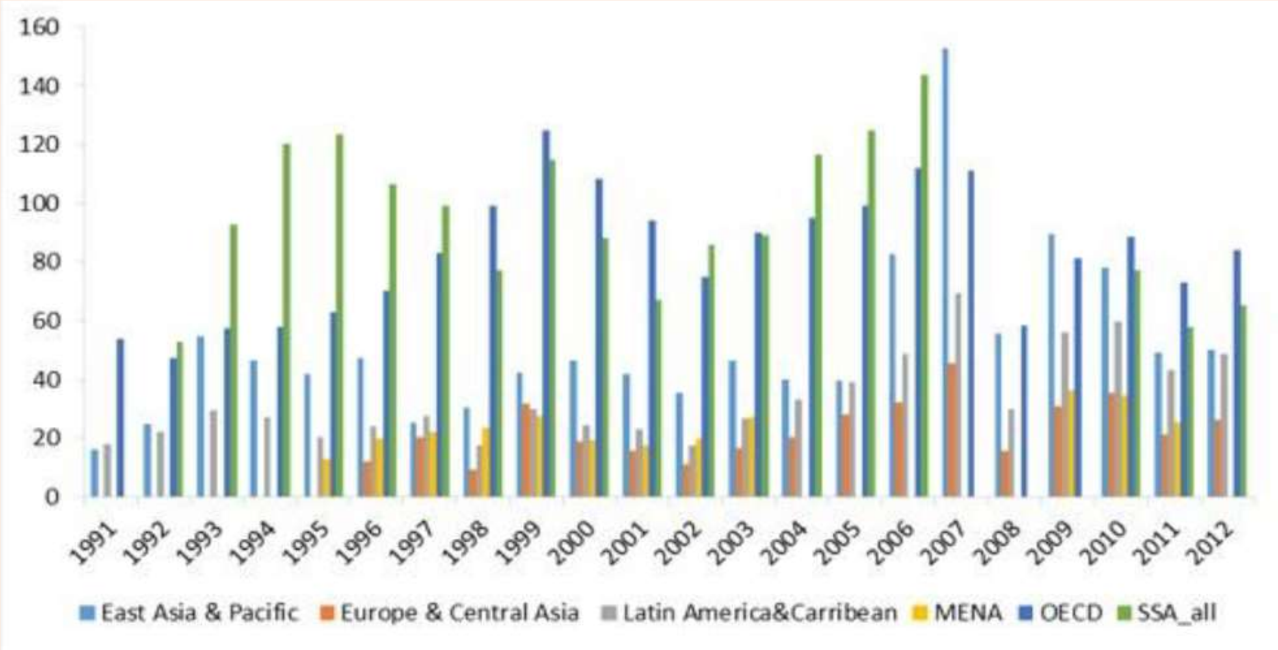
Volatilities and emerging ideas of macro-prudential regulation

- macro-prudential measures aimed at increasing the resilience of the financial system such as market reforms that drive towards centralising exchanges wherever possible at central clearing counterparties (CCPs), and structural reforms aimed at separating commercial banking from other activities.
- Centralising transactions should reduce counterparty risk and allow a better monitoring of financial flows, especially of derivatives. The concentration of transactions should reduce uncertainty about who holds what – an uncertainty which, during a crisis, can end up freezing entire markets and forcing central banks to intervene – Ghana.
- Convergence Criteria

Non-bank finance: from microfinance to expanding security markets.

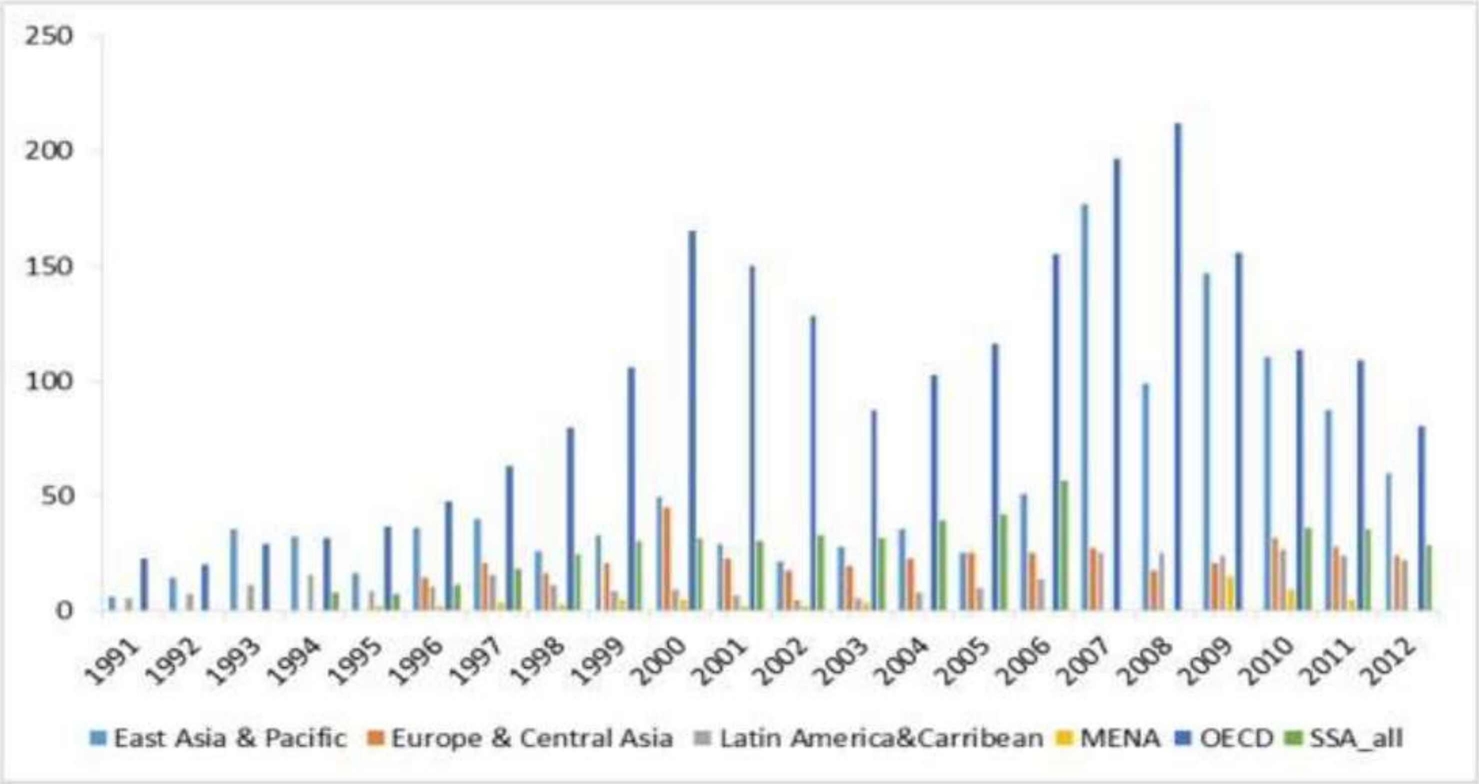


Stock Market capitalisation



Ratio of Stock market capitalisation to GDP. SSA compared with other regions

Stock market Value compared



Source: World Development Indicators

Insurance

- The insurance market in Africa under-developed as – apart from South Africa, Namibia, and Mauritius – all countries have very low penetration ratios. Africa’s share in the global market was only 1.5%. The poor performance of Africa on a global stage is particularly noticeable if South Africa is excluded, as South Africa accounted for nearly 74% ($51.6bn) of all African insurance premiums in 2013, with the other 53 countries contributing only 0.4% of the global insurance market.

Going Forward: Knowledge Gaps

- We know that derivative trading is taking place in the commodities sector – cocoa, coffee, tea: We don't know the scale, what their experience s are and the levels of risks they take:
- We know little about financial transactions that large companies – especially the trading of African commodities (palm oil, soya beans, flowers) etc – undertake on the back of Africa's commodities and the values they obtain.
- Commercial banking across the continent is largely in the form of "universal" banks – commercial banking + investment banking + plus securities trading. We don't know what scale and even less the impact of these merged functions. We know even less if any are involved in other forms of securitization.
- The banking sector benefitted more than most in the liberalization process. We know generally that they invest little in the real economy. We don't know how little.
- The Ghanaian government has embarked on "swapping" minerals on the ground for infrastructure. The DRC did similar. We don't know the real scale of these transactions across the continent.
- The human development sector as well as telecommunications may be at the forefront of future securitisation. Health insurance, education fees, etc are prone to securitisation. We don't know whether there are developments in these areas nd how we might combat further privatization of essential services through this route.
- We need better knowledge on the links between financialization, tax havens and illicit financial flows.
- We have large knowledge gaps which need filling.

Nevertheless

- We know enough about the ineffectual nature of the financial sector in economic transformation. National conversations are needed.
- There is now growing acceptance that development banking needs to be revived but learning the lessons of both successes and failures elsewhere in their design.
- The bail-outs of banks, with tax payers monies often take place with limited public discussion and without “social clauses” to rescue workers and rural financial institutions affected by banking crisis.
- We know broadly that demand constraints caused party by low and declining real wages and productivity problems in the real sector account for part of the non-performing loans. We need public discussion on economic transformation and real wages.