intellidex

Researching Capital Markets & Financial Services

10 March 2017

Submission to the Standing Committee on Finance of the Parliament of the Republic of South Africa in respect of public hearings on financial sector transformation

To
The honourable YI Carrim, MP, Chairperson of the Standing Committee on Finance and
The honourable JL Fubbs MP, Chairperson of the Portfolio Committee on Trade and Industry

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Introduction

We welcome the opportunity to make a submission to the committee. In this submission we draw on various research projects we have undertaken and other relevant information where appropriate. Our focus is on shareholding and financial product provision.

Intellidex is a research house that undertakes a range of research on the South African financial services industry and financial markets. Founded nine years ago, we have accumulated significant insight into various aspects of our financial markets and the roles that financial institutions play within them. Among the research that we have conducted are various projects that are relevant to issue of transformation of the financial sector.

The issues we have addressed in our analysis are:

1. The impact the Financial Services Sector has on the transformation of the broader economy.
2. The transformation of the Financial Services Sector itself
3. The level of concentration in the Financial Services Sector

Intellidex's interest is in assisting the committee with information that will contribute to a thriving and sustainable financial services sector that is able to contribute positively to the country. We have aimed to outline some of the issues that are important in the financial services sector and how it can best be used to transform itself and the broader economy in the interest of eliminating poverty and reducing inequality. We trust that you will find the analysis and data we provide useful.

Should you have any questions, please contact Stuart Theobald by email on stheobald@intellidex.co.za or telephone 011 083 5114.

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1. The impact of the Financial Services Sector on transformation of the broader economy.

1.1 *South Africa has a dynamic and well-developed financial industry.*

South Africa's financial services sector is highly developed relative to the rest of the region. That means that, as a country, we are able to create and access financial services that are simply impossible in other countries. Consider how South Africa's financial banking industry compares to others in the Southern African Development Community:

Table 1: SADC banking industry selected statistics

	Domestic credit to the private sector (% of GDP)	Total assets (US$m)	% of regional total assets
Angola	27.2	97611.71	8.97%
Botswana	33.9	18450.46	1.69%
DRC	6.7	4934.67	0.45%
Madagascar	13.0	3844.43	0.35%
Mauritius	104.3	52713.00	4.84%
Mozambique	35.4	14091.60	1.29%
Namibia	53.5	18338.29	1.68%
Seychelles	23.9	1952.08	0.18%
Swaziland	20.4	2138.82	0.20%
Tanzania	15.4	21056.16	1.93%
South Africa	150.0	819954.31	75.31%
Zambia	19.6	12728.65	1.17%

Sources: World Bank, Bankscope (Bureau van Dijk), Intellidex calculations
Note: figures are for most recent year available, which was usually 2015

Perhaps the most important statistic to note in this table is domestic credit extended to the private sector. At 150% of GDP, it is significantly ahead of other countries in the region. This figure compares well to the rest of the world, where the global average is 128%. South Africa's credit extension is similar as a percentage of GDP to the OECD group of developed countries which is at 149%. This means that South African citizens are able to access credit services as easily as citizens living in more developed countries, and far more easily than those living elsewhere in our region. In this respect our banking sector makes a strong contribution to empowering South Africans, though as I will discuss in the third section, there are structural issues which make it difficult for asset-poor individuals, predominantly black, to access credit at low cost. It is nevertheless a strength of our industry that it is able to provide credit services so widely.

1.2 *South Africa's capital markets are sophisticated and deep, which makes financing of transformation possible*

The Johannesburg Stock Exchange is by far the largest capital market in Africa. That means South Africa's companies are able to raise capital far more efficiently than companies elsewhere. It also means that South African savers, such as pension fund investors and life insurance policy holders, are able to gain access to a pool of investments that generates returns that support retirees and insurance beneficiaries.

The financial services industry is both a major driver and a beneficiary of deep capital markets. Innovations by banks and other service providers provide ways for savers to obtain the risk and return profile that suits them. For example, capital guaranteed products allow savers to obtain investment upside without risking their capital, an innovation made possible by having capital markets on which derivatives can be traded, while the AltX exchange provides the opportunity to invest in higher-risk, smaller companies. South Africa is unique on the continent in terms of the variety of financial instruments and investment opportunities available to savers.

Table 2: Global capital markets selected statistics

Country/region	**Market capitalisation of domestic companies as a % of GDP**	**Value of stocks traded as a % of GDP**
South Africa	234%	74.4%
OECD members	108%	151.5%
World	97%	167.1%
China	74%	357.3%
Cote d'Ivoire	39%	1.6%
Egypt	17%	4.5%
Japan	111%	127.1%
United States	139%	229.5%

Source: World Bank. Figures for most recent year available, usually 2015

The JSE also provides a major source of funding for banks and insurance companies. They raise equity on the JSE, a form of capital that protects all other funders because it is the first to be used should a bank or insurer encounter distress. South Africa's banking sector has seen examples of how this can be important, most recently in the curatorship of African Bank and, earlier, Saambou bank. In both cases shareholders lost everything, but depositors were protected.

Banks are also able to raise debt in the form of bonds, and quasi-equity in the form of preference shares on the exchange. These additional forms of funding add to the security of depositors, as they provide additional layers of funding to be absorbed in the event of crisis.

The JSE provides liquidity so that providers of capital are able to trade their exposures. Without this ability to exit an exposure, investors would be more reluctant to invest given that they would be locked in, and so capital raising would be more expensive. The capital markets also facilitate foreign investment, enabling foreign providers of capital to support South African companies to expand activities by providing them with equity or debt. Banks are crucial enablers of this market infrastructure by arranging capital raisings and acting as guarantors to stockbrokers trading on the market, reducing settlement and other risks that investors would otherwise face. Foreign providers of capital are essential to South Africa's development, because of the low domestic savings rate. Our sophisticated financial sector makes it possible for this foreign investment to enter our economy to finance its expansion.

The government occupies a uniquely powerful position in the capital markets. It is the lowest risk investment available. Government bonds are a major part of the bond sector of the JSE and a significant amount of private savings are invested into them, both by local and foreign investors. This is essential to funding the government budget, but it is also has important developmental effect on the financial markets. Government bonds are the longest-dated instruments traded on the bond exchange, with maturities of up to 35 years from now. This has a positive impact on the financial markets, for example enabling institutions to create annuity instruments to provide an income for retirees and to "discover" expectations of future interest rates. This illustrates how government is a crucial enabler of various parts of the infrastructure of the financial system.

This financial infrastructure makes it possible to deliver funding solutions that would otherwise be impossible. Many BEE deals have used structures that ensure that black beneficiaries are able to access the benefits of ownership of shares, without being fully exposed to the downside risk. South Africa's investment banking industry developed and pioneered the technique of "notional financing" which allowed BEE schemes to gain exposure to shares without the immediate cost of financing. In the event that share price performance was subsequently weak, beneficiaries face no downside risk. When share price performance is good, beneficiaries are able to receive unencumbered shares that then form capital in their hands. As we explain in section 2 below, there has been significant wealth creation among black beneficiaries specifically because of this form of financial engineering.

Notional financing is a good example of what is made possible by South Africa's extensive capital markets infrastructure. The liquid capital market provides a means for price discovery of the value of shares, which is essential for notional financing schemes to work. Such financial technology would be impossible in any other economy in Africa.

South Africa's financial institutions should therefore be seen as enablers of transformation of the economy. The sophisticated financial infrastructure that the banking, savings and insurance industries collectively represent, in tandem with the capital market, are a national asset. That asset can be utilised in the service of developing, growing and transforming the economy.

The question is one of how to turn possibility into reality. There are some inescapable facts about the financial sector that any successful policy approach has to acknowledge. Financial institutions need to generate a profit in order to fund their own growth and ensure their own financial stability and sustainability. The right strategy is therefore one that presents transformation as an opportunity for the financial sector by creating the right incentive effects. The results can be dramatic. As an example, consider the Renewable Energy Programme, a public-private partnership through which private renewable energy producers provide electricity to the national grid. In only five years, R194bn of investment was mobilised to fund renewable energy projects across the country, six times the amount invested in infrastructure for the 2010 World Cup. Much of that was sourced from foreign investors, but the broader South African legal and market infrastructure was essential to making it happen. The programme has been recognised as the fastest rollout of renewable energy generation anywhere in the world. That rapid rollout was achieved despite the fact that until the programme, South African banks and other financial institutions had had almost no experience in funding renewable energy. It is a good example of how capable the financial sector is when given the right incentives.

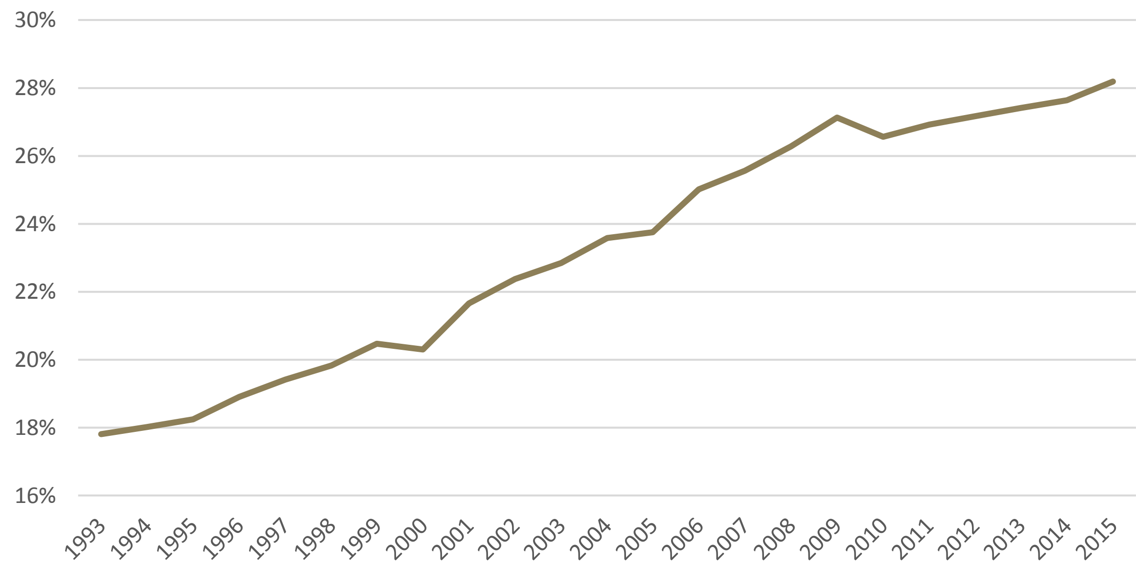
The success of the renewable energy programme was achieved by providing a clear, transparent, and reliable legal framework with the right kinds of government support. Within that, private sector operators were able to determine risks and price their services accordingly. They also developed many new financing techniques such as “green bonds” which have allowed for the mobilisation of savings specifically to fund renewable energy. The programme has stimulated a great deal of investment and employment, while helping to meet the country’s commitments to reduce climate-changing emissions.

Another remarkable piece of financial engineering currently being developed has a clear transformational impact. Standard Bank in partnership with several NGOs is developing “social impact bonds”. These allow for funding of particular projects that have specific measurable outputs, such as numbers of child vaccines, child nutrition levels and school test performances. If such projects, financed through the bonds, achieve those specific targets, then government funds the returns earned by the investors. This protects the taxpayer – government only incurs costs after the targeted social outcomes are delivered, while it harnesses the creativity of the NGO sector in finding solutions to achieve the defined objectives. Similar ideas are being developed in the effort to find solutions to the student funding crisis.

These provide some examples of what can be achieved with the right designs. Incentives won’t achieve everything that we want for the transformation of the industry and the economy at large. Clear rules that impose obligations on the banks and other institutions are certainly a part of the solution, as we will discuss in section 3. To maximise outcomes, however, we should understand where incentives are best and where rules are best. We should also understand that the financial services industry is a national asset that is crucial to the transformation of the economy at large. It is one of the best tools we have to help eliminate poverty and reduce inequality.

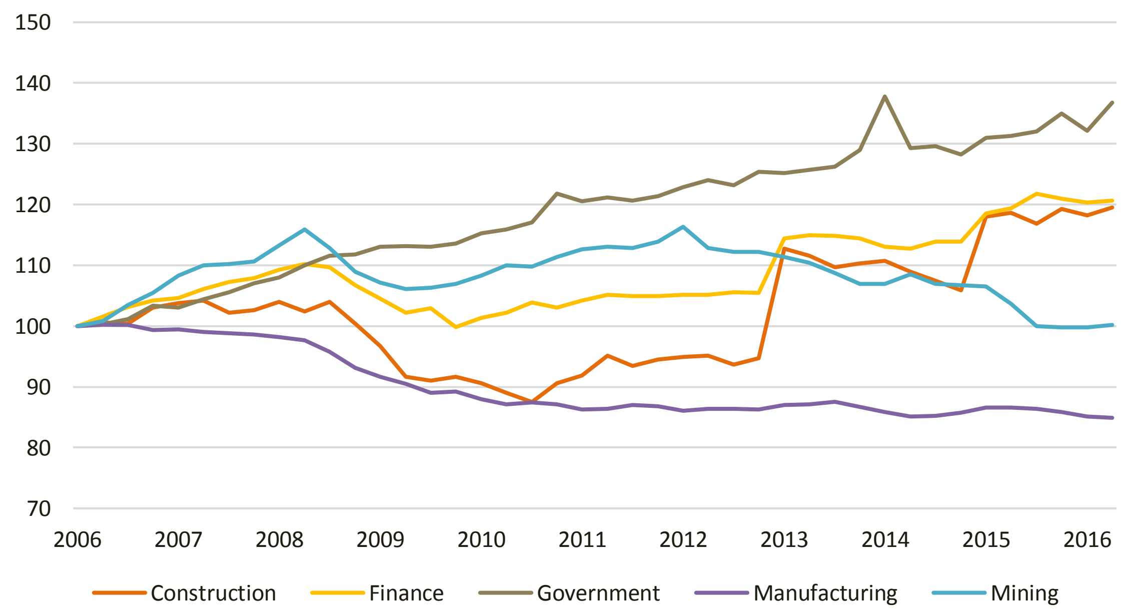
In charting a course for the financial sector, we should be careful that we do not impose rules that have unintended consequences such as harming the positive role it plays in the wider economy. The financial services sector has been a major driver of growth in the economy, growing employment and contributing to GDP growth in a larger proportion that other industrial sectors. It is crucial for employment and growth that we protect this positive contribution too.

Graph 1: Financial Services as a Proportion of GDP



Source: Statistics South Africa

Graph 2: Employment Growth per GDP Sector (rebased to 100 at start)



Source: Inet BFA

Government occupies a powerful position as the lowest-risk in the financial system. It is able to use this position to make possible many things that would otherwise be impossible. For example, government guarantees were crucial in the renewable energy programme, enabling funders to back projects that have a 20-year risk profile. This shows how government could use its risk-bearing capacity to enable financial sector innovation. This should always be done in a way that protects the government balance sheet and does not lead to liabilities for the taxpayer. There should be a cost to the private sector if it is to rely on the state for risk mitigation. Good financial innovation would accommodate such a cost.

In designing regulation to drive transformation, we believe the following considerations should be top of mind:

1. **Does the regulation support the development of the financial industry and capital markets or does it harm them?** Harms might include increasing the riskiness of financial institutions and the riskiness of the sector as a whole. Banks specialise in pricing risk and taking on risk that is justified by the price. Making banks and other institutions more risky means forcing them to take on risks at unjustified costs. If we decide that it is unavoidable that some policies will weaken financial institutions, we must be confident that this cost is worth it. We need to understand the harm in the form of reduced ability of the banking sector to fund other projects as its balance sheets have to accommodate the heightened risk that regulation can impose.
2. **Is there a "sweet spot" for regulation that both develops the financial sector and achieves the social outcomes we desire?** Is there a way that we can drive the banking system to support transformation while making it stronger than it is? The use of infrastructure bonds is a potential avenue to achieve this, using government's risk absorbing capacity to drive financial institutions to fund the development of poverty and inequality alleviating infrastructure. Government could absorb part of the risk of such bonds in return for guarantees that the infrastructure would achieve targeted objectives. South Africa's financial sector infrastructure makes this possible.
3. **Can we regulate so as to promote innovation in the market place in order to address our challenges?** Innovation should focus on solutions rather than particular products. For example, we once were concerned about providing every South African with a low-cost bank account, envisaging an account as a typical branch-based chequing account with associated transactional facilities. Then cellphone-based banking radically changed what was possible. So we should regulate for solutions, not particular products and services. The marketplace should be free to innovate to find sustainable long-term solutions that right now we couldn't imagine being possible in future.

2. Transformation of the financial services sector

While there are many elements to the broader topic of transformation, we have focused our research efforts on understanding ownership and the wealth-generating impact of black empowerment deals in the economy.

We undertook a research project in 2015 to assess black ownership of the financial services sector. In the following table we compare ownership at end-2010 and 2014, using the ownership formula from the Financial Services Charter. The formula excludes government and foreign ownership from the base in calculating the effective percentage of black ownership.

Table 4: Ownership of financial services sector

	Voting Rights		Economic Interest	
	2010	2014	2010	2014
Alexander Forbes Group (Pty) Ltd	27.5%	36.3%	27.5%	37.6%
Barclays Africa Group Ltd	10.6%	18.8%	10.6%	16.6%
Capitec Bank Ltd	15.8%	26.3%	15.8%	25.2%
Coronation Fund Managers	16.5%	21.4%	16.5%	21.4%
Discovery Limited	12.5%	24.4%	12.5%	22.9%
FirstRand Limited	14.4%	30.1%	14.4%	30.1%
Investec Limited	28.8%	28.0%	28.8%	28.0%
JSE Limited	13.7%	18.4%	13.7%	16.8%
Liberty Holdings Limited	26.1%	36.5%	26.1%	35.7%
MMI Holdings Ltd	30.9%	31.1%	30.9%	31.1%
Nedbank Ltd	30.7%	46.4%	28.1%	37.0%
Old Mutual Plc	29.5%	58.7%	0.0%	45.2%
Rand Merchant Insurance Holdings	0.0%	15.0%	0.0%	15.0%
RMB Holdings	0.0%	15.0%	0.0%	15.0%
Sanlam Limited	34.1%	34.8%	25.5%	31.3%
Santam Limited	28.0%	34.4%	26.6%	30.0%
Standard Bank Group Ltd	27.4%	37.6%	27.4%	37.6%

Source: Intellidex, based on FSC calculation methodology

2.1 The unique features of ownership in the financial sector

Generally, the shareholders of companies contribute capital to finance a company, and thereafter benefit from the profits that company is able to generate. If the company is unsuccessful, the shareholders lose their money, but they are not automatically compelled to contribute more money to the company. The shareholders always face the highest risk – employees, suppliers, banks and the revenue services always have a prior claim to the assets of a company. But for those who take credit exposure to a company, such as a supplier providing goods on credit, the shareholders are often a way for that supplier to find comfort that their risk is reasonable. A large shareholder known to have substantial resources helps to reduce the perception of risk because it is assumed that they would stand in to back the credit worthiness of the company if needed. Is seen in banking in that the cost of debt and preference shares is also affected by perceptions over the stability of shareholders.

In the financial services sector, this risk role of shareholders is especially important. Banking and, to a lesser extent, insurance, are completely dependent on confidence in order to survive. Banks accept the savings of the public, and the public have to have full faith that those deposits would be available to them when needed. Similarly, insurers cover the risks we face and we need to have full faith the insurer would be able to meet any claims. Financial infrastructure also critically relies on confidence – we would not trade on the JSE if we were unsure that counterparties would settle those trades. Confidence is the single most important factor that underpins the health of the financial system.

The financial crisis that broke out in 2008 shows just how serious a collapse in confidence can be. If people lose faith in the credit worthiness of financial institutions, as many did following the bankruptcy of Lehman Brothers, panic ensues and counterparties rapidly attempt to withdraw their exposures to financial institutions.

The implementation of Basel 3 has created further levels of risk for funders of banks with the creation of instruments that convert from debt to equity automatically in the event of bank becoming distressed. That means that shareholders are automatically diluted when banks become distressed.

This issue is not far from home. South Africa has seen several crises of its own. Here are some of them:

African Bank

Most recently, the collapse of African Bank wiped out almost all of shareholders' capital held in the holding company, African Bank Investments Limited. Tens of thousands of black shareholders who participated in African Bank's two BEE schemes, Hlumisa and Eyomhlaba, lost their money entirely. However, swift intervention from the authorities prevented a wider impact on confidence.

There were clear systemic issues that stemmed from the collapse, though these happened in an unexpected way, via money market funds. African Bank had few deposits, but instead relied on instruments it issued to institutional investors. Some of these were held in collective investment schemes that invest in instruments issued by banks and other institutions that are considered to be the same risk as cash. As concerns about African Bank increased, investors in these money market funds became wary that those funds may not be able to pay back their cash because they had some small exposure to African Bank. As a result a run on money market funds ensued, which risked disrupting a major source of funding for all banks and other financial institutions, and put at risk savings that were specifically intended to only have low risk exposures. Had the authorities not decisively intervened, a damaging collapse of confidence could have taken hold.

In the case of African Bank, the regulators implemented a rescue plan that has led to a healthy African Bank again trading.

Saambou

The collapse of Saambou in 2002 provides a clearer example of how confidence can collapse. Amid rumours of problems with Saambou's financial accounts and parts of its business, a run on deposits ensued. In the space of 24 hours, over R1bn was withdrawn from the bank. These withdrawals were largely by quasi-institutional depositors like lawyers and estate agents' trust accounts, which are often large amounts of money. The trustees of such accounts have a fiduciary responsibility to protect client money held in those accounts, so if they have any reason to believe that the money could be at risk they are compelled to try and protect it.

In the case of Saambou, the Reserve Bank and finance minister decided to put the bank into curatorship, believing that it was solvent at the time and therefore no depositors were at risk, and letting it fail would not be systemic. It chose not to attempt to rescue it, as it would later with African Bank. That decision led to the immediate closure of all branches of the bank for some time while its affairs were being managed.

Typically, when a bank becomes distressed, confidence is lost in weaker banks. A so-called "flight to quality" ensues as depositors, trying to protect their savings, move to what are perceived to be safer banks. However, in the case of Saambou, a much more serious confidence problem ensued which could be called "upward contagion". Saambou had been the seventh-largest bank and a run then ensued on the sixth-largest bank, BoE. Pressure was also experienced by the fifth-largest bank, Investec. Both of these were fully solvent banks, but that fact could not stem the confidence crisis. It was clear that a nightmare scenario might ensue.

The Reserve Bank and National Treasury took an unprecedented step in jointly announcing an unconditional guarantee for all of BoE's deposits. Technically that made BoE the safest bank in the country and eventually stemmed the loss in confidence. The only way, however, to lift the guarantee was for the bank to be sold to a larger institution, so BoE was sold to Nedbank.

In the curatorship, Saambou turned out to be insolvent by over R7bn. As part of restoring confidence, government guaranteed depositors, which cost taxpayers over R7bn. Shareholders in Saambou's holding company also lost almost everything (the bank was worth zero but there were some insurance assets at the holding company level).

The small banks crisis

In 1998 during the emerging markets crisis, interest rates in South Africa reached a peak of 26%, largely to stem a massive withdrawal of foreign capital and resulting collapse of the rand. This caused distress for many borrowers, leading to a sharp uptick in bad debts for the banks. Banks that had large amounts of shareholder capital were able to withstand the losses but depositors became worried about smaller banks that held less capital or had a mismatch in liquidity of liabilities compared to assets.

At the time several smaller banks were trading, including black-owned banks like FBC Fidelity, Real Africa Durolink and African Merchant Bank. They were the result of the deliberate encouragement of new entrants to the banking sector in the 1990s in an effort to promote competition and black-owned entrants. A Guide to the Reconstruction and Development Programme, one of the governing ANC's first economic policy documents, noted that "There is a concentration of power in the financial sector. It is quite developed and modern - which is a strength - but there is not enough participation by black people and in particular by women."[1] These considerations led the government to loosen up access to banking licenses, a step that was expected to promote competition, expand services, and facilitate the entry of black bankers into the financial sector. The move was consistent with international trends as the rapid growth of the technology sector at the time driven capital markets sharply upwards and

[1] http://www.anc.org.za/content/basic-guide-reconstruction-and-development-programme

motivated significant investment banking activity linked to new listings and capital raising for the sector.

However, the confidence crisis that ensued post-1998 saw almost every one of the banks exit the market by 2001. They were either sold to larger rivals or gave up their banking licences as they could no longer sustainably attract deposits.

Since the crisis, only one notable bank has entered the market and managed to grow, particularly in the consumer sector, namely Capitec. It is notable that Capitec's early growth was driven by unsecured lending, rather than full-service retail banking. Its funding at first relied heavily on shareholder equity. It only entered the deposit and transaction market after attaining some scale. No new institution, funded by deposits from the start, has entered the market since the small banks crisis. This is in part because of the economic realities of trying to build a bank but also because of regulator caution in licensing new banks. Reluctant entrants and regulators both seem persuaded that entry into the banking market is difficult, requiring a persuasive business case.

The link between shareholders and financial competitiveness

Most banking confidence crises exhibit a similar pattern. Funding moves out of banks that are perceived to be weakest and into banks that are perceived to be strongest. Smaller banks are usually the first to suffer, progressing up to larger banks. In several banking crises that have occurred in other developing countries, the flight to quality usually ends up at multinational banks that are perceived to be the largest and strongest in the market. It is precisely because of the shareholder profile that these banks are perceived to be high quality.

Even during normal market conditions, in markets such as Ghana and Kenya, these banks are able to attract deposits at low cost, giving them a significant funding advantage compared with local and smaller competitors. So unlike many other types of companies, the risk profile of the shareholders makes a direct difference to the fundamental economics of financial institutions. A bank or insurance company with weak shareholders will be treated as higher risk in the market place and as a result it will have higher funding costs. This renders it uncompetitive. To cover the costs of funding it ends up engaging in higher risk lending, leaving such banks more exposed to economic shocks. However, such banks can also succeed through innovation, finding ways to cope with the higher funding costs by developing new ways to reduce other costs in the business or develop more profitable products.

From an overall systemic point of view it can be risky to have too many small banks in the market place. Indeed, the small banks crisis in South Africa helped to create the environment in which Saambou and then BoE faced runs – depositors were already nervous because of the experience of small banks some years before. Regulators have to strike a balance between the innovation and competition provided by new entrants and the increased risk they introduce to the system. We will return to this issue in section 3.

The point to note is that banks, and to a lesser extent insurance companies, face special issues in thinking through their shareholder structures. Banks will be more competitive and less risky if their shareholders are perceived to be substantial institutions.

For this same reason, bank regulators often demand that banks have a "shareholder of reference", who can be turned to in the event that the bank is in distress. By this, regulators usually mean substantial institutions that have large balance sheets that can potentially inject new capital into a bank in an emergency.

2.2 Black empowerment transactions

The impact of shareholders creates particular difficulties for black empowerment transactions in the financial sector. Ideally, financial institutions would want shareholders that already have large balance sheets but there are few black investors that meet this criterion. The usual structure of BEE deals effectively involves the vendor absorbing the risk of negative share price performance. This not only means that the shareholder would be unable to be called on in the event of distress to contribute more capital, but also that the bank has a liability that is worsened if the share price falls, creating a leveraging effect on risk. BEE transactions therefore increase the riskiness of financial institutions.

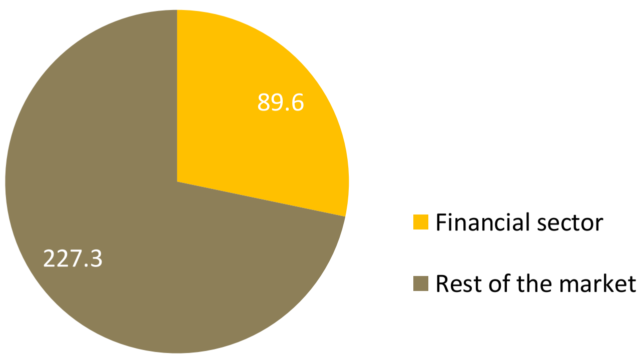
BEE transactions are nevertheless an important part of the transformation impact that financial institutions can have. But the net effect must be kept in mind – the increase in risk means banks are less able to absorb other risks such as riskier lending. Transactions also come at a cost to other shareholders, and as the shareholder base transforms this cost is increasingly carried by black shareholders, or black beneficiaries of the pension funds and life insurance companies that are shareholders.

Investments on the JSE reflect the savings of South Africans, either directly or via institutions. As the distribution of wealth in South Africa normalises, it is a natural consequence that the profile of investors on the JSE will normalise. On this view, black ownership of JSE-listed companies is a consequence rather than a cause of transformation.

BEE deals, however, have a strong wealth-creation effect. And in this respect financial institutions' BEE deals have led to significant wealth creation. Research undertaken by Intellidex has found that deals by the 15 largest JSE-listed financial institutions collectively created R89.6bn of net asset value in the hands of black beneficiaries. That is total value net of any funding. The value represents 7% of the current market capitalisations of those financial institutions.

Our research[2] found that the BEE deals done by the top 100 companies on the JSE collectively created R317bn of wealth as at the end of 2014, including both capital appreciation and dividend flows. The financial sector is responsible for 28% of the total, although the sector accounts for about 20% of GDP.

Graph 3: Wealth created by BEE deals (Rbn)



The success of BEE deals is often thought of in terms of the black ownership of companies. However, usually beneficiaries dispose of the shares they receive through BEE transactions and so do not become long-term shareholders.

[2] All of the tables and data from this research can be accessed at http://www.intellidex.co.za/bee

This is the rational outcome – it does not make sense for individuals to hold concentrated equity exposures, they should rather diversify their portfolios in order to balance risk and return. It also depends on the life stage of the beneficiary – holding equity portfolios makes sense for older beneficiaries who are saving for retirement, while younger beneficiaries might be better off using the proceeds to pay for assets or pay down debt. The capital created by BEE deals can also be used by beneficiaries to finance their own businesses.

We think it is more important to measure the success of BEE deals in terms of wealth creation rather than long-term ownership. By focusing on long-term ownership, some undesirable consequences follow that stand in the way of wealth creation and addressing inequality, specifically that companies will then do deals only with shareholders who are willing and able to remain invested for the long term. This favours large investors that will not suffer undue concentration risk from the exposure and for whom the risk/return profile of the investment makes a good fit to their investment objectives. It also favours using evergreen charitable foundations as part of the BEE deals, which is positive for dealing with inequality as they tend to benefit the poorest sectors of the population. If we want BEE deals to create wealth for black investors who do not have pre-existing balance sheets, for whom it is suboptimal to remain invested for the long term, we should not be prioritising long-term ownership for BEE deals. We should instead focus on the wealth-creating impact of BEE deals.

Table 5: Wealth created by BEE deals in the financial services sector

Company	Live/concluded at end 2014	Staff schemes (Rm)	Strategic partners (Rm)	Community/ charity schemes (Rm)	Total Value (Rm)	Share price on start date	Share price on end date
FirstRand	Concluded	R5,970.80	R2,593.74	R14,697.86	R23,262.40	1387	5014
Sanlam	Concluded	-	R7,915.28	R6,476.14	R14,391.42	930	5754
Standard Bank	Concluded	R4,367.28	R4,358.75	R2,179.37	R10,905.40	5140	14351
RMH	Live	-	R9,878.47	-	R9,878.47	2670	6370
RMI	Live	-	R7,096.45	-	R7,096.45	1402	4110
Old Mutual	Live	R3,715.55	R1,696.23	R969.27	R6,381.05	1500	3428
Nedbank	Concluded	R2,184.62	R1,742.50	R1,573.43	R5,500.55	7575	24739
MMI	Live	R446.41	R2,963.11	-	R3,409.52	1040	1920
Capitec	Live	R72.78	R3,132.33	-	R3,205.11	1700	33172
Barclays Group Africa	Concluded	-	R2,584.50	-	R2,584.50	5025	14050
Discovery	Live	R589.31	R1,805.83	-	R2,395.14	2165	11069
Liberty	Live	R933.19	R947.97	R458.13	R2,339.29	5033	12289
Investec	Concluded	R473.67	R1,418.00	-	R1,891.67	1550	5296
Coronation	Concluded	-	R1,650.70	-	R1,650.70	370	4719
Santam	Live	R265.00	R470.00	R254.00	R989.00	9033	21500
Reinet	Live	-	R534.60	-	R534.60	n/a	2544
JSE	Concluded	-	R84.16	R299.10	R383.26	1975	11979
Alexander Forbes	Concluded	R35.59	R164.39	R43.56	R243.54	n/a	n/a
Brait	Concluded	-	R175.02	-	R175.02	760	2000
HCI		-	-	-	R0.00	n/a	n/a
Total		**R19,054.20**	**R51,212.04**	**R26,950.87**	**R97,217.10**		

Wealth creation is to our minds the key step towards the normalisation of the South African economy because it addresses inequality directly. Investment in listed companies will flow from the pattern of wealth distribution in the economy. Public company ownership is a consequence, not a cause, of transformation.

Wealth creation, however, is difficult for financial companies to control. It follows from the performance of companies' share prices. Companies are better able to control a percentage of ownership than the value of their shares which can be affected by factors outside their control such as global economic conditions. The value that our study found of R317bn was the result of a fairly strong period of share price performance on the JSE, particularly after 2008. BEE deals make wealth creation possible, but it is the profitability of companies, and the consequent impact on share prices, that leads to the possibility becoming a reality. Share prices are hostage to the overall performance of the economy.

Control

Share ownership is not only a matter of economic benefit, but it also grants the holder some degree of control of the company. Therefore, a skewed pattern of ownership in the economy also means a skewed pattern of control. Shareholders control a company via the board, which appoints management. Shareholders also have a direct vote on certain resolutions.

Control is important in the debate because it is not only the economics of the economy we should be trying to transform, but also the culture of it. Different people will exercise control in different ways. While shareholders of financial companies are predominantly institutions, the people who represent those institutions will exercise that control on their behalf.

Philosophically, shareholders exercise control because they are the primary risk bearers in an institution. Where a single shareholder has more than 50% of a company, they are able to exercise control quite freely, although there are certain legal protections for minority shareholders.

In the case of financial institutions, the power of shareholders is significantly constrained by regulations. For example, bank senior management has to be approved by the Reserve Bank, irrespective of what the shareholders choose. Banks and insurance companies are required to meet strict risk objectives such as the ratio of capital to liabilities. These factors impose responsibilities on management and the boards of institutions that are outside of the control of shareholders. However, shareholders have influence over the broad strategy of an institution, including acquisitions and remuneration policies. These are powerful rights.

Broadly, shareholders' primary objective is profit maximisation. That is why they put their capital at risk, rather than invest in risk-free instruments such as government bonds. This is the overriding interest of shareholders, and, in the case of financial institutions, this has positive and negative aspects. Profitable banks are lower risk and are able to finance their own growth by accumulating more equity to fund loans and other assets. As previous banking crises have illustrated, depositors tend to run to banks that are perceived to be safe, and profitability is one indicator of safety. However, profit-seeking shareholders may otherwise demand risky strategies that have a substantial risk of failure. As we explained in the last section, the history of banking crises in South Africa provides examples of where shareholders have lost everything, and taxpayers have additionally had to contribute to bail out depositors. As a result, banks and other financial institutions are strictly regulated.

Nevertheless, despite these significant regulatory constraints, it could be argued that the residual discretion that shareholders can exercise can help in transforming institutions and, through the activities of those institutions, broader society. There are good examples of black-owned investment firms that have used the wealth generated from BEE deals to engage in various social and economic development initiatives, as there are of shareholders pressuring companies to do more for transformation.

Shareholders exercise their control primarily through the board room, so it is important that they have board seats. However, there are governance implications to such board membership. Shareholder representatives are not considered independent and the King 3 and 4 corporate governance codes require that companies have at least 50% nonexecutive directors, of which at least half should be independent. In undertaking a review of governance of banks in 2002, Advocate John Myburgh suggested that in the case of banks, 50% of the board at large should be independent. King requires that the chairman should also be independent, or a lead independent director should be appointed. It is worth asking why Myburgh and King consider it important to have a large proportion of independent directors. Shareholder representatives are seen to have an incentive of profit maximisation. This is true also for the representatives of institutional shareholders, who are often remunerated according to the performance of investments. Independent directors do not share that incentive and are therefore thought to be more reliable agents for other priorities, including compliance with applicable regulation and to look after the interests of other stakeholders including staff and civil society. Because transformation is an objective that can be in conflict with profit maximisation, it is more naturally the preserve of independent non-executive directors to drive forward.

If the objective is to drive transformation at companies, and we believe that black directors are best positioned to achieve this, then it is better served by ensuring that boards have a significant number of black independent non-executive directors. Shareholder representatives may well provide support in the boardroom to those directors, but their incentives make this less likely, in our view. The incentive structures they face can be shaped by a board such that they include transformation objectives. It should be noted that financial institutions should also ensure that they have significant black executive directors too, as they can also be change agents.

In summary the important points to note on the debate over shareholding are the following:

- The shareholding of financial companies, particularly banks, face different issues compared with other companies such as mines or industrial companies. Having perceived strong shareholders lowers their risk, providing a competitive advantage, in the form of lower funding costs, over other institutions perceived as having a weaker shareholding base.
- BEE deals are better seen as wealth creation and redistribution mechanisms, rather than ownership mechanisms. Black wealth creation is important to transform the economy.
- BEE deals come at a cost to existing shareholders through the dilution effect of issuing new shares and a cost to the banks in terms of an increased risk profile which can constrain the transformative impact of banks in other areas of their businesses. These costs can harm transformation and have to be balanced against the benefits.
- Transformation change agents are more likely to be the independent non-executive directors of boards than representatives of shareholder groupings. The control aspect of shareholder rights, particularly when it is through a minority shareholding in a heavily regulated industry, is unlikely to drive transformation forward. Instead it is the wealth-creating impact of equity ownership that will drive transformation.

3. Concentration in the South African banking sector

3.1 Competition vs fragmentation

The committee indicated its intention to discuss the degree of concentration and/or lack of competition in financial services. The debate seems to have been focused on banks, so we will restrict our comments to these institutions.

There is a tension between the competitiveness of banks and the stability of banks. The more banks there are in an industry, the more competitive it will be, but also the less profitable and more fragmented it will be. Fragmentation has important consequences as it constrains the scale of business that banks can do. Banks cannot take on exposures that represent too large a percentage of their capital, so the smaller the capital base of the bank, the smaller the exposures they are able to take. In many countries in the rest of the continent, domestic banks are too small to handle large project finance deals, for example, and as a result their banking sectors are dominated by foreign-owned banks who can use parent balance sheets for large domestic projects.

Fragmentation also affects profitability. There are certain fixed costs that any bank must incur, particularly regulatory costs and the costs of basic infrastructure it must maintain. If the market is fragmented, fixed costs translate into a higher average cost per client for each bank. A fragmented market can therefore mean higher costs to consumers.

A good example of the problems with fragmentation is Nigeria. The country had a highly fragmented market, but in 2005 implemented a major reform programme. The number of banks operating was reduced from 89 to 25 in 2005, by increasing the minimum capital base from N2-billion to N25-billion[3]. This more-than-12-fold increase in capital requirements forced banks into mergers, leading to much larger institutions. The explicit objective of the reforms was to position the banks to be able to help drive development across the economy. Larger banks could finance projects without incurring significant single exposures, while the increased scale allowed them to reduce average costs faced by consumers.

However, competition also drives innovation, which can help to improve the overall riskiness of a sector. A competitive market ensures banks keep control of costs and operate efficiently, while reducing costs to shareholders. The right balance has to be struck. An overly competitive market leads to increased risk-taking as banks attempt to find ways to maintain profitability – a problem that was clear in the US banking sector leading to the financial crisis. A fragmented market leads to inefficient banks that are unable to take the large exposures needed to fund development of a country.

3.2 The four pillar model

In South Africa, the balance has been set at the "four pillar" model. This model was determined to be desirable in 2000 when the government had to consider the takeover bid by Nedcor for Standard Bank. Nedcor argued the transaction would lead to a national champion that would have the scale to be competitive on the global stage. At that time, banks were beginning to develop strategies to grow across Africa where the main competitive obstacle was that global majors like Barclays and Citibank could operate off a home balance sheet that was multiples the size of any South African bank's. Nedcor argued that it was in South Africa's interest to have one giant bank that would have international clout.

The Reserve Bank and National Treasury undertook a study to determine what market structure would be in the best interest of the country. The conclusion was that a "four pillar" banking structure, with

[3] https://www.cbn.gov.ng/OUT/SPEECHES/2012/GOV_WARWICK_150211.PDF

four large banks, was preferable to the structure that would have arisen had Nedbank been allowed to merge with Standard Bank. As a result, the merger was blocked.

Some years earlier, Australia undertook a similar assessment and decided to shift from a six pillar to four pillar structure[4]. It is clear therefore that regulators have come to the four pillar model from both directions – that it is more competitive than fewer pillars, and that it is better than more pillars. This suggests it is a "Goldilocks" banking market structure.

However such a concentrated market implies less price competition. It is generally thought that the big four banks have little incentive to engage in a price war with each other, though there are several examples where banks compete through price competitiveness.

Competition can happen in three primary ways:

1. Transaction and account fees
2. Interest rates offered on loans
3. Risk level that is accepted

Often in debates about competitiveness, it is only the first of these that is considered. In our experience, banks go through cycles of competing on fees, and then competing in interest rates offered. When fees became the focus of public attention during the Banking Enquiry held by the Competition Commission in 2006 and 2007, we saw a swing toward banks competing on fees and away from competing on interest rates. That was compounded by the 2008/2009 recession when banks incurred significant losses in home lending. Interest rates available to consumers subsequently increased, while fees decreased. We are currently seeing a swing of the pendulum back to increased competition in interest rates and less in fees. Home loan lending tends to be quite competitive as consumers are highly price conscious and shop around, while other bank products tend to see less consumer discretion, particularly personal loans. In personal loans the competitive pressure seems to be in risk rather than price, so providers compete in a "race to the bottom" for consumers of increasingly lower credit worthiness.

Table 6: Concentration of SA banking market

Balance sheet item	Percentage of market held by big four
Short Term Deposits	84.40%
Total Deposits	83.63%
Mortgage Lending	89.26%
Credit Cards	92.31%
Total Assets	82.71%
Personal Loans	61.11%

Source: SA Reserve Bank, Intellidex calculations

Note: Based on December 2016 DI900s. Only includes licensed banks – non banks compete in some

[4] https://www.resbank.co.za/Publications/Speeches/Detail-Item-View/Pages/default.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=a01d874c-c3f6-4b93-a9dc-c984cf8652cf&sarbitem=160

market areas, particularly credit cards and personal loans, so effective market concentration in those areas will be lower.

3.3 Market concentration and transformation

A narrative has arisen that the banking sector consists of "monopoly capital" and that this stands in opposition to transformation of the economy. This can be interpreted in several ways, including:

- That the level of concentration restricts the provision of services particularly to black customers
- That the concentration of the market prevents new entrants into it, such as a black-owned bank

We address each of these issues in turn.

Racism in financial services

We live in a society that feels beset by racism. Exposure of racist comments on social media has made it clear that racist attitudes continue to be deeply entrenched among some in society. There have been shocking examples of racist violence inflicted on poor black workers and others. The Apartheid system aimed to cement its legitimacy among whites by convincing them that blacks were a threat and inferior. This legacy is still with us.

Financial services are a part of our society. We have clear evidence of racism in many parts of the services industry, such as restaurants and hotels, where black customers are treated appallingly by usually white, racist, service providers. It would be bizarre if these same attitudes weren't found in the financial services industry too. The solutions in such cases seem to be threefold: vigorously prosecute racist acts; proactively confront racist attitudes; and promote and direct our business to black service providers.

Racism may well play a part in the treatment of black customers in their efforts to obtain financial products. For example, loan officers may lack the ability to properly understand a business case put forward by black entrepreneurs because that loan officer has attitudes about the abilities of the potential client or the viability of a market made up mostly of black consumers.

Obviously, there are also legitimate reasons to turn down loan applications, purely on the basis of the credit risk the client represents. Many loans are turned down legitimately, many of which will inevitably be from black applicants. However, when the decision involves a party with no insight into black lives and market places, it is simply not possible for that decision maker to properly assess the risk an applicant represents. Such loan decision makers may not be racist in an overt sense, but are simply not equipped to judge the creditworthiness of black applicants. Their failure is first and foremost a failure of risk assessment, though the consequence is racist.

This is why part of the solution to eliminating racism in financial services is to ensure there are more black decision makers in financial services, people who share the background and worldview of black applicants and are therefore better able to judge their creditworthiness. There is both a clear business case and a moral case for such change. Banks that are better at assessing risk are better banks.

Employment equity targets, therefore, are not only important as a means of transforming the workforce, but also as a business imperative for banks.

Many banks and other institutions do proactively engage with staff through various programmes to challenge racism. The business incentive, however, may not be enough to drive the behaviour that would eliminate racism. There has also been significant change in the racial profile of staff in financial institutions, as the committee will be aware. Financial institutions share a responsibility with all of us to proactively fight against racism, a fight that cannot be won by any one institution on its own. However, there are ways to drive financial institutions into more proactive efforts to eliminate what racism may be at work in their treatment of clients. This is in the form of targeted financing.

One of the important elements of the Financial Sector Charter was the commitment by financial institutions to extend financial services to and to target certain recipients for funding. By specifying targets, for example, for funding of black entrepreneurs, banks are forced to implement the systems that would enable them to make the best decisions possible to service black entrepreneurs. Banks would need to develop and appoint decision makers who can judge the riskiness of black applicants appropriately. We therefore believe that targeted financing is an important element of the transformation commitments that financial institutions should make. We are aware of good examples in banks of targeted financing units that have developed this capability, along with mentorship and other support to further add to the creditworthiness of such clients. Those should be applauded and more should be encouraged.

A further kind of racism present in financial services is a structural one. A key risk-mitigation tool of any financial services industry is to hold security for loans. The holding of security lessens the risk of a bank because they can recover their exposure if a client defaults by taking receipt of some or other asset that is held. The fear of loss of the asset can also be a strong incentive for clients to be cautious in taking on debt and ensuring they can manage it appropriately. However, it is clear that when clients lack any collateral, their access to finance is constrained. This is despite the growth of unsecured lending, which always comes at a higher cost, reflecting the increased risk of not having any collateral.

Because of the skewed distribution of wealth in our society, white applicants are more able to offer collateral than black applicants. This results in a compounding of this skewed wealth distribution: white applicants can access lower cost financing more easily than black applicants. This is a real problem for addressing race-based inequality.

We do not see easy solutions. Targeted financing is one part, in that it requires financial institutions to focus on identifying and backing black borrowers. Another part is for government to speed up the granting of title deeds to black property owners. This would immediately solve the problem for those consumers by providing them with a form of collateral. That collateral could be made even more valuable by driving the development of rural and township-based property markets so that price discovery is possible. By setting financing targets for banks, there should be an incentive for them to support such market development.

A black-owned bank

Various parties have called for the creation of a black-owned bank. This stems in part from frustration over the inability of black entrepreneurs to access financial services, as well as the belief that a black-owned bank would be a better use of black capital than leaving it in the traditional banking sector.

In section 2, above, we discussed the challenges that face new entrants into the financial services sector. In the case of banks, particularly, an institution that is perceived as risky is always at a competitive disadvantage because it has to pay more for funding from risk-averse depositors. So a key challenge for a black-owned bank is how to overcome this problem. The history of black-owned banks in South Africa does not provide strong encouragement for the viability of this approach.

During Apartheid, black banking was clearly extremely difficult. Some banks were established in the homeland states, ostensibly independent countries that served the Apartheid government's ambition to control the movement of black people within South Africa. In South Africa itself, in March 1974, Sam Motsuenyane led the formation of a black-controlled bank, branded African Bank, and capitalised with R1m, which was 30% held by the large commercial banks and 70% held by several prominent black businessmen. The bank had initially been proposed 10 years earlier by the National African Federated Chambers of Commerce (Nafcoc), which had used the decade to raise the capital to back the bank. An Indian-run bank, New Republic Bank, was also operating at that time with assets of R8.5m having been founded in Durban in 1971.

The notional independence granted the homeland states was only ever on a tight leash held by Pretoria. Some development efforts were made in the homelands, centred on developing the homeland states as agricultural economies. The Development Bank of Southern Africa was created with a mandate to fund infrastructure development in the homelands, and the bigger homelands also founded their own agricultural development banks. The Transkei, Ciskei, Venda, and KwaZulu homelands, for example, founded such agricultural development focused banks with significant funding from Pretoria. The transition to democracy and reincorporation of the homelands into South African presented difficult challenges for these institutions. The banks were generally found to be operating highly inefficiently, relying on subsidised funding from the South African government that no longer made sense to provide in a democratic South Africa. The solution for the two Eastern Cape banks, Ciskeian Agricultural Bank and the Bank of Transkei was proposed in the Eastern Cape Bank's Restructuring Report of 1997. In 1998 the assets of Bank of Transkei were transferred into a new bank holding company, Meeg Bank, under the chairmanship of Wiseman Nkuhlu.

The KwaZulu Finance and Investment Corporation was transformed into the non-bank Ithala as a development agency for the KwaZulu-Natal province.

At the dawn of democracy, there were therefore four black-controlled banks, the African Bank founded by Motsuenyane, New Republic Bank, Venda Building Society and Bank of Transkei, which was to become Meeg Bank. These banks found it very difficult to compete in the post-apartheid environment.

One of the first black-owned financial services companies in post-Apartheid South Africa was Metlife, which in 1999 had an asset base of R11bn, making it the 26th largest company in the country[5]. But the early phase of black capitalist development was severely undermined by the emerging markets crisis of 1998. The value of black empowerment firms fell from R21bn involving 110 firms in 1998 to R3.4bn among 45 surviving firms in 1999.

The small banks crisis followed which saw African Merchant Bank give up its license, FBC Fidelity sold to Nedbank, and Real Africa Durolink sold to PSG. In those cases it was primarily a loss of confidence by depositors that rendered the banks unviable. Meeg bank had earlier been incorporated into Absa having been unable to sustain its profitability.

A black-owned bank will have to think carefully about how it will avoid the same pressures all of these institutions suffered. The homeland banks of the 1980s received subsidised funding from the government, but their subscale size meant they could never become profitable and were a drain on state resources. If our concern is primarily to overcome racism in the financial services sector, we are likely to be better served by focussing on the existing industry and transforming it.

A state-owned bank

There have also been calls for a state-owned bank to enter the market place. Again, these are at least in part motivated by the view that the existing market fails to cater adequately for black customers.

We think these calls are ill-founded, given that the state is already heavily involved in the financial services industry. Consider that there are already the following state-owned institutions:

- **The Public Investment Corporation** is already by far the largest fund manager in South Africa.
- **The Industrial Development Corporation** is a substantial development finance institution investing widely in the South African economy.
- **The National Empowerment Fund** is specifically focused on financing black entrepreneurs and businesses. According to a recent announcement it is being incorporated into the IDC.
- **The Southern African Development Bank** is a substantial development finance institution that finances infrastructure across the country and region.
- **The Postbank** is a consumer-focused bank that operates through the 2700 branches of the Post Office. It is currently being corporatised and has applied for a banking license.
- **The Land Bank** is a specialist agricultural financier.
- **The Road Accident Fund and Sasria** are significant providers of insurance.

The IDC, DBSA, Land Bank and Post Bank between them hold approximately R280bn in assets, which would make them the sixth biggest bank in SA.

The question for a state-owned bank is just what gap it would fill. The NEF and IDC are already mandated to fund black businesses. The Postbank is mandated to extend financial services into rural areas and other under-serviced sectors. All of the issues raised in debates about a state-owned bank

5 https://www.researchgate.net/profile/Roger_Southall/publication/237800101_The_ANC_black_capitalism_in_South_Africa/links/0deec52ef75e4c3fd7000000/The-ANC-black-capitalism-in-South-Africa.pdf

can be addressed by expanding and supporting existing state institutions. These institutions have experience and skills that would be difficult to replicate in a new institutions. While there may be weaknesses in these institutions, it is surely easier to focus on addressing these weaknesses than introduce a whole new institution that may come with a raft of unanticipated weaknesses of its own.

We do not believe a new black-owned bank or a state-owned bank will be able to address the problems that exist in the sector. The above arguments support a view that all of the concerns about concentration in the financial services sector are best addressed through supporting the targeted financing provisions of the Financial Sector Charter. These should be reviewed regularly as envisaged in the charter. We should also turn to the existing raft of state institutions in the financial services sector and support their capacity to fill gaps in the market that may exist.

4. Conclusion and the Financial Sector Charter

The discussion above points to the trade-offs that are inevitable in the discussion around transforming the financial services sector. While we think there has been significant progress, there is more that can be done. We think that the best mechanism to achieve this is the Financial Sector Charter.

The Charter is the correct mechanism to deal with the unique features of the financial services industry. In particular:

- Financial institutions are unique in that shareholding is not only a question of ownership and control, but also of the competitiveness and systemic soundness of institutions.
- Financial institutions can be transformed, and drive transformation in the wider economy, by innovating new products that promote financial inclusion and the financing of black businesses and individuals.

These particular features of the financial industry are best served by having a purpose-built charter. The Charter made a significant and positive impact following 2003 when it was implemented. The negotiating process itself was highly effective in promoting introspection in the industry and getting industry leaders to recognise the issues that banks, insurance companies and asset managers face in transforming themselves and the economy. However, with the expiry of the Charter at end 2008 following the failure to bring it in line with the broad-based black economic empowerment codes, the energy and focus it had promoted has dissipated. The recent regazetting of the amended codes is an opportunity to reenergise the transformative efforts of the sector, as is this parliamentary hearing.

We recommend, however, that parliament also think about the opportunities there are for government to help support innovation and unlock other barriers to further transformation. In particular it can:

- Help unlock structural barriers to black financing by giving land holders title deeds to their properties.
- Promote innovation by using its balance sheet to absorb risks that the financial sector cannot bear alone. This should be done at a cost to financial institutions that compensates the tax payer for this risk.

We also have argued that:

- The creation of new banks has to overcome significant barriers to entry including the higher cost of funding. We believe that the creation of a new black-owned bank would face this same challenge. If the objective is to drive change it is better achieved by transforming the existing industry.
- The government currently has a set of significant financial institutions that broadly straddle the financial services sector. Where there are gaps it is preferable to develop these institutions to fill such gaps than to introduce a new state-owned bank.

Ultimately, we believe that the financial sector is a national asset that can contribute dramatically to the development of the country, insuring that it can eliminate poverty and reduce inequality. To realise that potential it needs the right policy environment.

We trust these insights are helpful to the commission. Please do not hesitate to contact us if we can be of further assistance.