# Developing Africa's Financial Services

The Importance of High-Impact Entrepreneurship

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## The Importance of High-Impact Entrepreneurship

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# Foreword

This book is very timely. Africa is at the crossroads of its development. As it is written in the introduction of this book, "Africa is not immune to shocks and fluctuations in the world economy." Economic growth has slowed down to the lowest level in two decades. Low commodity prices, weak external demand, and domestic headwinds (such as policy uncertainty, drought, and security conditions) pulled regional growth down to an estimated 1.5 percent in 2016. This is the lowest rate in over two decades.

With population growth estimated at 2.7 percent, the region will experience a decline in GDP per capita in real terms, but the situation is unequal throughout the region. The slowdown in regional growth reflects the weak performance of the region's two largest economies (Nigeria and South Africa) (Figure 1).

Although the growth outlook remains subdued, there are signs of resilience. The worst performing countries are the ones affected by low commodity prices and conflict but 41 percent of Africans live in countries with average GDP growth rates of over 5.5 percent. These countries have increasingly better quality of

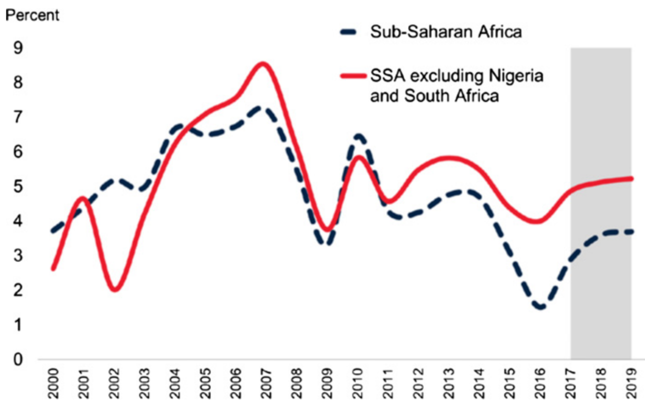


**Figure 1.** Real GDP Growth. *Source*: The World Bank (2013) Africa's Pulse.

policies and institutions and more diversified export structures. Regional growth is forecast to rebound to 2.9 percent in 2017, rising to 3.5 percent in 2018, as commodity exporters adjust to a low commodity price environment.

This situation poses a big challenge for the continent. Future growth will increasingly need to come from higher total factor productivity. This represents a change in the growth pattern from the past two decades where growth came from an accumulation of capital and other inputs. Since Africa is late in its demographic transition and stuck at a pre-dividend stage with rapid population growth and large numbers of dependent children, the continent faces a big opportunity and the challenge of providing services for this huge contingent of young people. Without the right policies and investments, this rapidly growing youth cohort can result in increased unemployment, poverty and instability. On the other hand, this youth bulge represents an unequal opportunity in terms of innovation, entrepreneurial spirit and market expansion for Africa (Figure 2).

The case studies presented in this book are perfect examples of the path Sub-Saharan Africa will have to take to revive growth and transform the region. High-impact entrepreneurship in the financial sector is key to unlock the potential for economic growth through financial inclusion and investment in the continent. The examples are even more impressive as a lot of these

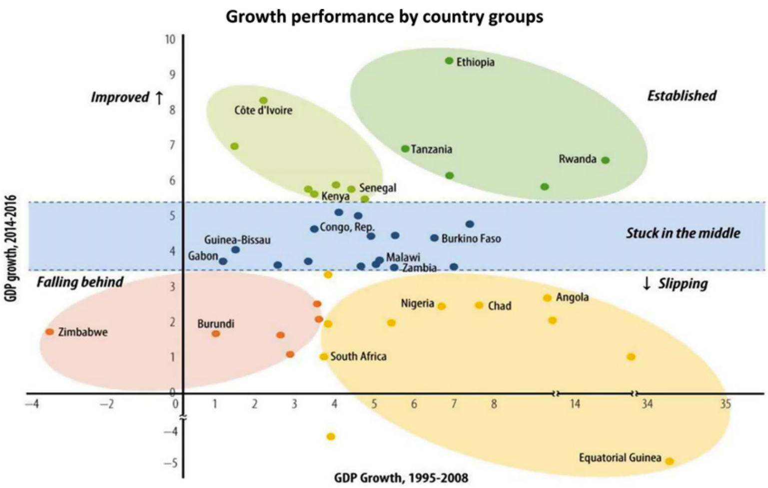


**Figure 2.** Growth Performance by Country Groups. *Source*: The World Bank (2016) World Bank Commodities Price Data.

success stories developed at a time when the developed world financial institutions were retrenching to their core markets as a consequence of the major financial crisis of 2008 and subsequent regulatory crackdown, leaving big parts of the region without access to adequate financial and banking services. This is essentially a story of African success in African markets by African entrepreneurs, managers, and workers and using African know-how and ingenuity.

The book provides us with a complete picture of the evolution of the financial sector in Africa, starting with the historical trends, from the entrepreneurial money-lending activities in pre-colonial times, passing by the colonial financial structures serving foreign shareholders and investors, to the post-independence state-owned centralized banking system. Through this historical prism, the cases presented of high-impact entrepreneurship in the financial sector – the Banco Unico in Mozambique, Fidelity in Ghana, Banco Atlantico in Angola, or the incredible journey of Kenya-based Equity – show us the opportunities that vibrant young African societies present for risk takers. The book also gives us lessons on the peculiarities of African risk management and on the differences between regions stemming from different macroeconomic arrangements like currency unions.

Going forward, entrepreneurs are exploring avenues more linked to the religious and cultural backgrounds of their societies like the example of Islamic banking in Nigeria presented. The role of social impact investments coupled with finance is highlighted and is, of course, central in Sub-Saharan Africa in order to compensate the absence of well-functioning public services. The acute communitarian sense of African societies presents an opportunity for new financial instruments like crowdfunding.

The challenge in the continent is to use technology to increase access to finance. Mobile banking and digital financial services, housing finance, SME loans, and access to insurance products and services are the means for finance to help the productivity growth that the continent needs to reduce its dependency on commodity prices fluctuations, but these financial services will not be enough. An agenda for productivity growth needs to include infrastructure improvement, a focus on agricultural productivity and a long-term commitment to investments in human capital.

The financing needs are enormous and cooperation between foreign investors, multilateral development banks and nascent vibrant domestic financial sectors will be needed to overcome this huge challenge. Some estimates from the World Bank are that

Africa's annual infrastructure needs are at US$ 93 billion (15 percent of GDP) but there is only $45 billion of annual investment.

This agenda is as much about entrepreneurship as it is about institution-building, regulatory reforms and economic integration that help create markets that can attract investment being it in the form of foreign direct investment or public-private partnership. The good news is that the case studies in this book reveal to us that there's an increasing vocal and influential constituency in African countries for reform.

Besides the issues that some parts of the continents still have related to fragility, conflict and violence, there are also other global developments that may threaten this Africa growth trajectory. The continent would pay a big price if the forces that try, in the developed world, to rollout globalization would triumph with their agenda of protectionism. Whatever happens, the growth potential of Africa is there and the ones that are able to look past current difficulties will certainly be rewarded in the long-term.

More specifically to finance, some of the effects of the 2008 global financial crisis played also against this opportunity for the continent. The regulatory (over)reaction provoked the escape of several international banks from Africa. The result has been a stalemate in the private sector contribution to the international funding of the efforts of financial inclusion in Sub-Saharan Africa which makes the cases presented in this book even more relevant as they show the strength of the domestic entrepreneurial spirits.

The Consultative Group to Assist the Poor is a global partnership of 34 leading organizations that seek to advance financial inclusion housed at The World Bank. Its recent data shows that the financial crisis reinforced the dependency of the Africa agenda for financial inclusion on donors' contributions and public funding (mainly from multilateral financial institutions) (Figure 3).

This trend needs to be reversed and donors have recently started to reorient their priorities from financing traditional microfinance ventures (which are currently already well-served by domestic private sector investors) to a focus on agriculture and energy access and efficiency. The expectation is that a focus on these areas will crowd-in some financial investment from the private sector that may help bridge the gap between needs and financial means. This shift aims at helping the productivity agenda of the countries and to complement the efforts made by some of the ventures described in this book.

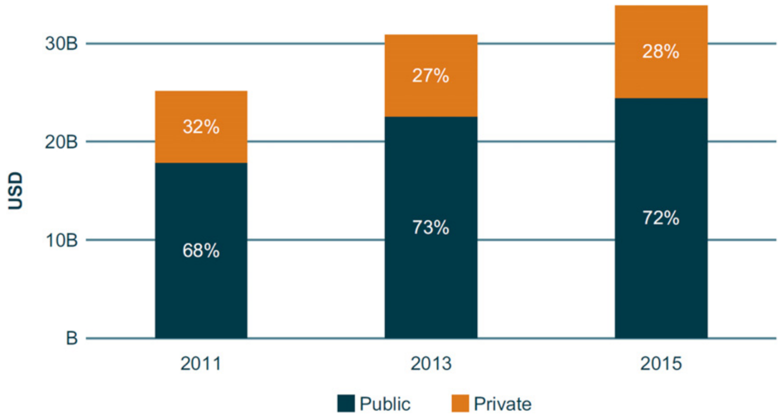


**Figure 3.** Global Estimated Commitments for Financial Inclusion. *Sources*: 2012-2016 CGAP Cross-Border Funder Survey, 2012–2016 Symbiotics MIV Survey.

A growth agenda for Africa will need the commitment of all stakeholders – multilateral financial institutions, donors, governments, entrepreneurs and civil society. The biggest contribution of this book is to show through data and practical examples that African economies provide great business opportunities for smart investors and that Africa's private sector is on the forefront of financial innovation. Thanks to technology and knowledge, Africa can make some significant leaps in terms of creating modern and growth-inducing financial sectors. The ability to allocate resources to the more productive sectors of the economy is certainly a pre-condition for progress.

The data and the case studies presented show that African entrepreneurial attitude and creativity are a force to be reckon as they launch the seeds for a more sustainable economic growth model. These are signs and stories that should capture the attention of policymakers everywhere. These examples of high-impact entrepreneurship in the financial sector tell us an optimistic story. More than describing Africa's present tepid economic situation, this book announces the vibrant future of a continent increasingly ready to fulfill its promise.

Nuno Mota Pinto
*Alternate Executive Director and*
*Member of the Board of The World Bank Group*

# Introduction

Africa's awakening on the global economic stage is in its early stages. Headlines such as "Lions on the Move: The progress and potential of African economies" (McKinsey, 2010) and "Africa Rising" (*The Economist*, 2011) are a far cry from a decade earlier, when Africa was declared "The Hopeless Continent" (*The Economist*, 2000). African countries have seen dramatic economic growth and greatly expanded their business capacity. A recent Harvard Business Review article asserts, "in many ways Africa holds the same potential that China did 20 years ago" (Chironga, Leke, Lund, & Van Wamelen, 2011, p. 122). The World Bank (2015) states that the world's average annual Gross Domestic Product (GDP) growth rate in the 10-year period, 2004–2013 was 2.65 percent during which Africa outpaced the world with an average annual growth rate of 4.99 percent. South Africa had long been the largest economy in the region, but the most vibrant growth of late has been taking place in other sub-Saharan countries. Nigeria has already surpassed South Africa as the continent's largest economy (*The Economist*, 2014). Sub-Saharan Africa is also seeing an increasing amount of foreign direct investment (FDI). According to UNCTAD (2015), FDI has increased exponentially during the 2000s, with the most recent growth of FDI inflows driven by private equity. There is good evidence to project that Africa is going to evolve into a global powerhouse, a narrative which is composed of countless individual success stories, as summarized in *The Next Africa* by Bright and Hruby (2015). This survey of success stories from across the African continent also touches on the rise of Silicon Savannah with the prospect of tech ventures. Pilling (2016) also takes up the concept of a Silicon Savannah in the Financial Times, concluding that despite still being a poor country Kenya, with its rising tech startups, is "market friendly, deregulated, chaotic and entrepreneurial, feels like a country on the move." Both popular media and academic scholars have written prolifically about Africa and its economic miracle. Why add another book to the shelf? And why focus on high-impact entrepreneurship and the financial sector?

As has been demonstrated by the drop in commodities prices in 2015, Africa is not immune to shocks and fluctuations in the world economy. These either help or hinder the continent's efforts to speed up integration and encourage further cross-border commerce and development (African Economic Outlook, 2015). The recent decline in commodity prices and services serve as evidence of this dynamic, with oil's sharp retreat denting the economic growth of oil-rich nations. The empowerment of a diverse generation of entrepreneurs and a well-functioning entrepreneurial ecosystem is helping Africa to overcome its dependence on resource extraction, opening up new avenues for sustainable prosperity.

Coupled with these facts is that sub-Saharan countries have some of the highest population growth rates in the world. More people means more need for goods and services which in turn will power GDP. For example, the average age of the population in Nigeria is 14 years old (*The Economist*, 2014). Furthermore, this new generation will enter the workforce, and will put further pressure on the labor market and the private sector to keep up with the creation of jobs. Going hand in hand with population and economic growth is the fact that Africa has become the continent with the fastest-growing consumer class with all the opportunities that this entails (McKinsey, 2012). Consumer goods companies are making significant long-term investments to cater to the increasing demand, with even conservative estimates, the next working-age generation will have at least as much purchasing power as the current working generation. This shows that the stakes are very high and that the long-term growth potential is strong.

A viable financial sector is a key condition for wider economic growth, and finance is a vital component of the entrepreneurial ecosystem surrounding new venture creation. The economic function of the financial services sector goes far beyond allowing people to make payments more conveniently, even though from a practical viewpoint that aspect is crucial for businesses. Just imagine all the financial transactions that even a small manufacturing company has to handle. All the payments that are to be received from customers and the supplier invoices that the company has to settle. The list grows significantly when monthly salary payments are added. The financial sector makes all of those transactions possible. But the much greater value of the financial sector lies at the core of banking: receiving deposits and returning that money back to the economy in the form of loans, where those resources contribute to real economic growth, impacting the standard of live for everyone. The financial sector also helps allocate money effectively to the most promising projects. Research thoroughly appreciates this conceptually basic but economically crucial function of the financial system (Goldsmith, 1969). Schumpeter (1911) emphasized the need for a functioning system of financial intermediaries as a precondition of innovation-driven economic development. In particular, small and medium-sized enterprises (SMEs) find that not having proper access to finance can be a growth constraint (Beck & Demirguc-Kunt, 2006). A report by the IMF (2015) on CEMAC countries (Central African Economic and Monetary Community) found that financial inclusion is particularly lacking for SMEs. Yet, it is often those smaller companies that are on a high-growth path and require significant financial resources.

A key theme of this book is that high-impact entrepreneurship represents a very distinct segment of entrepreneurship that has a disproportionately high impact on economic development. It is high-impact entrepreneurship that takes advantage of large-scale opportunities and relates the concept back to the significant cash requirements needed to pursue opportunities. Through the nature of their role as a contributor to economic growth, financial institutions themselves engage in supporting high-impact entrepreneurship by creating the conditions for entrepreneurs to benefit from the financial muscle and flexibility to grow and adapt in a business landscape. In this process, banks have great influence in shaping the future composition of African economies. Entrepreneurial bank executives can set strategic areas of investment that are considered a priority for their banks when making lending choices. Those are strategic choices, as banks' resources, while large, are not infinite. As an example, banks have to consider the importance they give to agribusiness over other sectors. Likewise, banks can shape the future of the energy infrastructure by financing either solar cells on the top of village huts (promoting the decentralization of Africa's energy infrastructure) or large infrastructure projects leading to a more conventional, centralized energy supply.

This book addresses the key question of how entrepreneurial financial institutions have been able to rise in Africa, illustrating some inspiring success stories. And, it is precisely those success stories that hold the power to encourage a new generation of entrepreneurs to pursue opportunities that help to transform societies into better places to live, work, and prosper. And those inspiring stories come at a crucial point in African's transition to the next bigger league, in light of both the challenges and opportunities facing the continent. There is no established recipe tested elsewhere that Africans can simply follow. Rather, African leaders must analyze the resources available in order to pursue the opportunities inherent to the African continent. Zoogah, Peng, and Woldu (2015) argue that there is a need for Africa-focused management research through two primary theoretical foundations: institutions and resources. This book aims to make a contribution in both of those dimensions.

This book's focus is on sub-Saharan Africa, encompassing the geographic area south of the Saharan desert. By no means is sub-Saharan Africa a homogeneous geographic or cultural region. It holds an impressive diversity of cultural traditions. Even within countries there are significant regional differences. However, in high-impact entrepreneurship in the financial services sector, there are more commonalities between the entities than differences between countries in what regards the phenomenon of high-impact entrepreneurship. Sub-Saharan Africa has also seen increasing international economic integration among its many countries. This trend is going to continue in the future, creating additional opportunities for African banks to grow and act as facilitators of international trade.

The book is comprised of three sections, under each of which several thematically related chapters are collected. The first section consists of background chapters establishing the broader context. In the first chapter of that section, Johannesburg-based historian Grietjie Verhoef outlines the rich history of how the financial services sector has evolved in Africa historically, ranging from early finance to colonialization. European institutions took hold in Africa during the colonial period, which was followed by the rise of African institutions in the aftermath of the regaining of independence. In the second chapter, Dana T. Redford and Christian Wolf discuss high-impact entrepreneurship, leveraging their expertise in the field of entrepreneurship. In the third chapter, Craig Churchill and Alice Merry look at the concept of managing risk in entrepreneurship and the role of the insurance sector. The fourth chapter looks at the two common currency zones spanning more than a dozen French-speaking countries in West Africa. Authors Constant D. Beugré and Colette A. Alla base their chapter on their deep knowledge of French-speaking Africa, illustrating how challenging it is to have the right conditions in place for high-impact entrepreneurship to arise in the financial sector.

The second section explores case studies of high-impact entrepreneurial banks that have started in the past decade and have risen to become market leaders. These best-practice cases of high-impact entrepreneurship illustrate the growth and impact that they have had in their sector and in the countries where they operate. Kwaku Appiah-Adu and Christopher Boachie, from the Central Business School in Accra, Ghana, explore how Fidelity Bank rose to become a good practice in that West African country. Two case studies from Portuguese-speaking Africa are included, one from Angola, the other from Mozambique. Dana T. Redford writes about Angola's Banco Atlantico, which has risen to become a leader in financial services in that vibrant country. Portuguese writer Daniela Costa and Dana T. Redford look at Banco Unico in Mozambique, illustrating how they entered into the market as a start-up until Nedbank bought a majority share in less than five years. In Chapter 6, David B. Zoogah, a renowned African management scholar collaborates with Christian Wolf to explore how Kenya-based Equity Bank went from being declared technically insolvent to having Kenyan's largest market share.

The third section looks into new developments and trends in the financial sector in Africa that present large potential opportunities. Vrajlal Sapovadia, from the American University of Nigeria, presents non-interest banking, illustrating the rise of this form of banking, which respects various religious and cultural traditions that prohibit interest-based finance. Nigeria's Jaiz Bank aims to service the country's large Muslim population, which makes up approximately half of the country's 174 million people. Artur Kochinyan and Dana T. Redford took a look at the recent trends toward impact investing and the range of ventures that take into consideration financial as well as social return on investment. Christian Wolf, whose research area is entrepreneurial finance, explores the opportunities related to crowdfunding in sub-Saharan Africa, considering that this recent phenomenon is highly compatible with long-established African traditions of collectivist collaboration.

The financial sector in sub-Saharan Africa has evolved to become a strong foundation for future growth across that portion of continent. Rather than simply copying the banking model of more developed countries, leaders in the financial sector in Africa have benchmarked their approach with international best practices while responding to African realities. This unique response has opened the door to African financial service sector players to become leaders in their own way. This is most notably exemplified by the extraordinary innovation that Africa has shown in mobile banking. According to KPMG (2013), about 80 percent of the population in sub-Saharan African countries do not use formal banking services and therefore are excluded from the wider benefits provided by the financial services sector. The picture is varied when comparing different regions: While more than half of the population in Southern African countries have access to financial services, less than 5 percent of adults in the Democratic Republic of Congo have a bank account (Bright & Hruby, 2015). The insurance sector in sub-Saharan Africa, which makes up only 3 percent of the global insurance market, shows a similar regional pattern. In the absence of a strong financial services sector, many Africans have resorted to more informal ways of managing their financial matters, such as informal lending. Research suggests that a reliance on informal finance increases the cost of money (Udry, 1990). The magnitude of the interest charged on a loan follows no clear patterns, but outrageously high interest rates in informal finance have been observed (Aryeetey & Udry, 1995). The higher rates are a result of limited information among informal lenders, exclusivity that limits the workings of the free market, and credit rationing in the sense that lenders do not have enough resources to satisfy exhaustively the credit demand that exist (Ray, 1998). The economic cost is high: Harrison, Lin, and Xu (2014) found that deficiencies in finance, particularly informal finance, contributed measurably to Africa's economic disadvantage. Specifically, the study found that Africa's financial sector realities alone account for "11% of the total factor productivity disadvantage, half of the labor productivity disadvantage, 59% of labor productivity growth disadvantage, all of the sales growth disadvantage, and a quarter of the export share disadvantage" (Harrison et al., 2014, p. 70).

Mobile banking improves financial inclusion for Africans, especially those living in rural areas where bank branches are non-existent. The African financial sector also plays an important role in educating people about how to manage their personal finances. Africa's new middle class is going to have the means and desire to acquire more advanced consumer goods that had previously been available only to a small elite. The financial services sector is accompanying people on this empowering journey. In terms of financial inclusion, the major economic contribution of the financial sector in sub-Saharan Africa can be boiled down to connecting existing resources, making those resources as a whole greater than the sum of the parts.

The M-Pesa story from Kenya has been told as an exemplary entrepreneurial success story countless times to illustrate the high-impact entrepreneurship phenomenon in sub-Saharan African financial services. Its case study will not be included in this book but it remains as a notable example of how the financial services sector in Africa has becoming a blended market where you have players from technology, telecoms, and financial services companies vying for the same market with a focus on innovation.

While more developed economies in North America and Europe are overburdened by private debt, Africa still boasts relatively low levels of private debt, pointing to an opportunity for banks to provide loans to fuel economic growth. According to statistics from international organizations, such as the IMF, many African countries stand out in global comparison because of their low private debt levels measured in relation to GDP. Ghana, Zambia, and Rwanda have a private debt that makes up less than 20 percent of their economies. Only South Africa stands out notably in terms of high private sector debt, as a result of the country's more established banking system.

The room for banks to grow and evolve as key societal institutions also becomes apparent when looking at the top 100 brands in Africa. According to Brand Africa, only one financial services company's brand is ranked in the top 100: Zenith Bank of Nigeria. The landscape of the top 100 brands is very different in Latin America or other parts of the developing world, where many financial services brands are ranked high in terms of brand recognition. African banks are already investing heavily in their brands, and, as good brand development takes time, the positive impact of their brand investment will likely unfold in the years to come.

As seen in this book's case studies, African banks are living up to their leadership role. A new generation has accepted the challenging task of shaping a better future. This book captures the entrepreneurial spirit inherent in those impressive developments. Most notable is the prevalence of young people among the banks' workforce, even in high leadership roles, contrasting African banks to European banks.

The financial services sector in sub-Saharan Africa represents unrivaled opportunities for growth precisely because financial services in Africa are all about reaching an underserved market and doing so in a way rooted in African economic and societal realities. The economic and financial landscape of sub-Saharan Africa 50 years from now will be fundamentally different. Africa's role on the global stage of political and economic affairs will be materially evolved. Bright and Hruby (2015) predict that five decades from now, external development assistance and the presence of foreign aid organizations and NGOs in Africa will have greatly diminished. It is entrepreneurship, and more specifically high-impact entrepreneurship, which will provide the great contribution to creating decent work, economic growth, and role models for future generations.

Dana T. Redford
*Editor*

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CHAPTER

# 1 The Rise of Financial Services in Africa: An Historical Perspective

Grietjie Verhoef


## ABSTRACT

The development of banking in Africa followed the demand of exchange networks from traditional indigenous economies to colonial exchange with the European world. The establishment of European banking institutions reflected the needs of the capitalist economy introduced by colonialism. The banking management of late nineteenth century and early twentieth century European banks adhered to the interests of shareholders. This chapter shows the emergence of well-managed banks in Africa, but after decolonization the political economy of African independence resulted in state capturing of financial institutions in most African countries. The South African banking system developed in close adherence to the British model. State-owned post-independence banks in Africa failed to deliver the development envisaged. The chapter shows the adverse impact of global economic developments on Africa, resulting in high debt levels. Structural adjustment of African economies and new market-oriented policies allowed the development of locally owned private banking institutions. The high-cost structure of the formal banking system from the dominant South African banks incentivised the mobile money innovation, an arena where African entrepreneurs lead global markets. Financial inclusion remains low in Africa.

**Keywords:** Africa; banking institutions; post-independence; mobile money

# Introduction

Exchange and credit formed an integral part of the economic activities of African societies. Traders, rulers and financiers wove a network of interlocking relationships that facilitated trade, exchange and wealth accumulation. Trading networks served as the intersection of culture, power and wealth. Financial services developed alongside commercial sophistication and global expansion. African systems of finance and credit provision were confronted by European systems of financial services as soon as colonial penetration linked Africa to the wider world of commercial and imperial expansion in the eighteenth and nineteenth centuries. European banks introduced new concepts of money, credit and savings, which formed a corollary to the economic changes on the continent. Trade, mineral extraction and emerging industrialization encouraged a closer relationship between emerging business in mining, industry and trade. The banking system that developed in Africa during the second half of the nineteenth and twentieth century marginalized traditional savings and credit systems, while presenting entrepreneurial opportunities to the participants in the second wave of globalization.

This chapter explains the entrepreneurial agency in the transition from traditional African accumulation of "currency" to the opportunities of formal European banking institutions. The chapter explains that the introduction of modern finance and banking as a non-African phenomenon developed within the framework of advanced capitalist economies. Modern financial services were designed to serve the capitalist colonial economies. When proto-industrial economies emerged in post-1940s and later in independent Africa, banking services were subjected to ideological suspicion and capture by the new African states. The chapter explains that a dichotomy developed between traditional African monetary exchange and European-based banking services in the colonial economies through the application of prudent conservative banking principles and cartel-like collusion. The most sophisticated banking system developed in racially segregated South Africa to support the most advanced industrial economy in Africa. The chapter explains the development of a structural relationship between the European banking system and African societies after decolonization as the new desire for economic "independence" resulted in nationalization of banks and state-ownership of most banks, which resulted in inefficiencies and regulatory divergence from international best practice. The chapter then shows how the macro-economic policy environment changed toward the end of the twentieth century, enabling African entrepreneurial opportunity in the banking sector. As African states embraced the basic principles of the market economy, entrepreneurial opportunities were grasped by a new generation of African entrepreneurs, also in the banking sector. The principles of sound banking in Africa are no different from banking in other parts of the globe – it only took African entrepreneurs the transitional period after decolonization to align to the market. The chapter shows the successful development of banking in Africa since the late 1990s as new entrepreneurial opportunities are taken advantage of by the new African entrepreneurial class. The chapter underlines the vital role of market-oriented policies to private enterprise and the rule of law as conditional to the sustainability of the modern banking system in Africa. Banking in Africa now develops in the context of the global financial sector, but aligned to the needs of the emerging African economies. These developments offer entrepreneurial opportunities in the delivery of financial services suitable to the needs of African society and business, such as the mobile money innovations where Africa is a global leader. The chapter illustrates the dual nature of Africa's needs for financial services, widespread financial inclusion, as well as sophisticated financial services for an emerging corporate and industrial business sector.

## African Savings and Credit: Socio-Cultural Foundations of Money

During the early years of commercial development in Africa, no formal banking institutions existed. Entrepreneurial opportunities