

AMENET*

MFW4A*

OVERVIEW OF AFRICA'S FINANCIAL SECTOR

This article is the first joint collaboration between the AMENET university network and the initiative Making Finance Work for Africa (MFW4A). By way of introduction, this first article includes just an overview of the most notable advances in the development of the financial sector in Africa since the 1990s. The transformation was accelerated after the financial crisis of 2008 with the progressive replacement of the European and American banks that dominated the sector by a dynamic group of pan-African entities, mainly from South Africa, Nigeria and Morocco. This same dynamic was translated to the insurance sector and financial markets. The number of stock exchanges have grown from 9 in 1989 to 30 in 2020 and the biggest ones are at a very advanced stage of interconnection that has increased liquidity and product diversification. Two other highlights of the process have been the advancement of financial inclusion thanks to the penetration of telephone banking in which Africa is the world leader and the strengthening of regulation and supervision systems. This financial transformation is favouring the process of economic integration at the continental level and interconnection with financial markets on a global scale.

Key words: general financial markets, financial institutions and services.

JEL Classification: G1, G2.

1. Introduction

The financial sector in Africa has known a very positive development following the first

generation of reforms that took place in the 90s with the liberalization of interest rates and the privatization of state-owned financial intermediaries. Coupled with the removal of many barriers to entry and exit in the sector, as well as greater transparency and accountability and reinforced supervision since the crisis situation faced by the sector in the 1980s, financial systems across the continent have experienced a substantial transformation.

Existing analysis of African financial sector relies too heavily on the comparison with more developed markets around the World. Analyses of the banking sector, for example, highlight ▷

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The **AMENET project** (Africa, Mediterranean and Europe Network) is one of the **Jean Monnet Networks** funded by the European Union. The network gathers a multidisciplinary group of researchers from 14 African and European universities, led by the Universidad Autónoma de Madrid. The main objective of AMENET is to promote collaboration between European and African researchers, practitioners and officials in order to deepen the different ways to promote the economic integration of Africa with Europe and advance sustainable economic and social development on the African continent. The network promotes research by students and professors on all topics related to these objectives and collaboration with various institutions with similar interests. Among the activities carried out by AMENET, the holding of international congresses (Tangier, November 2019; Las Palmas, October 2020; Accra, February 2021 and Dakar, September 2021) and the two-way exchanges of students and teachers. Within this framework, several doctoral theses have already been developed.



Making Finance Work for Africa (MFW4A) is a multi-donor initiative that was established in 2007 by the then G8, and is dedicated to advancing financial sector development in Africa. With a solid foundation built on experience and a network of partners, MFW4A brings together leaders from industry, governments, development partners and academia to draw actionable insights and define thought leadership in financial sector development in Africa. The Partnership is based on a recognition that the financial sector is a key driver of private investment, employment generation and economic growth. Currently the work of MFW4A covers four main pillars: i. Inclusive & Alternative Finance; ii. Banking Systems; iii. Trade Finance; and iv. Long-term Finance. A Secretariat was established in 2008 to support the activities of the Partnership and is hosted at the African Development Bank headquarters in Abidjan, Côte d'Ivoire.

the relatively small size, the challenges to comply with regulatory capital requirements, and weaknesses of banking supervision. As for the financial markets, most publications insist on the small size of African stock markets, poor liquidity and insufficiently developed market infrastructure.

However, with hindsight, this analysis does not capture many key recent developments since the 90s that support the growth potential of the sector.

Information technologies have had a very positive impact on access to finance, diversification and expansion of financial services. Global Findex (2017) suggests that there has been good progress in the share of households with a bank account, increasing from 23 percent in 2011 to 43 percent in 2017.¹ ▷

¹ The Global Findex database (<https://globalfindex.worldbank.org/>), funded by the Bill & Melinda Gates Foundation, updates every three years since 2011 the most comprehensive set of information available on the progress of financial inclusion in the World.

The insurance industry is also growing and have attracted the attention of the global actors given the potential for growth and diversification.

This description of the financial sector focuses rather on the progress than on the comparative analysis but it also takes into account the socio-economic context in which the institutions and markets operate. Africa accounts for 16.3% of the global population, but only 2.9% of the world gross domestic product (world's GDP). Africa is traditionally noted for its dependence on agricultural sector and the exportation of raw materials. However, this situation is gradually changing. Economic growth in Africa has been trending upwards since the mid-1900s. For instance, real GDP growth increased by 4.9 percent per year on average between 2000-2008 representing twice its pace in the 1980s and 1990s (African Development Bank, AfDB, 2020). The UN estimated that, in 2050, 50 percent of the World Population under 25 will be in Africa (UN/DESA, 2017). Despite the disproportionate attention that illegal African migrants attracts in Europe, just 2.5 percent of Africans live abroad, mostly within Africa (Economist, 2020). Many indicators points to Africa as one of the largest markets of the World in the XXI century.

Financial sector development has become the centrepiece in policy debates in Africa because of its importance in spurring inclusive economic growth needed to meet the sustainable development goals (SDGs).

The objective of this paper is to provide a summary overview of the recent evolution of African financial sector. It does not pretend to cover exhaustively all the issues. Instead, it provides just some relevant indications that illustrate the very large transformation that is underway.

After a brief description of the general evolution, the issues are grouped into four sections: a) banking sector; b) financial inclusion that analyzes the impact of new technologies; c) long-term financing that includes the evolution of the capital and debt markets and references to main institutional investors and; d) a brief review of the main aspects of financial regulation and supervision.

This introduction will be followed by two other papers. The first one focused on the analysis of the recent evolution of financial institutions. The second one will provide a more detailed description of the financial markets and how the financial innovation is serving the needs of companies and families in Africa.

The three papers are the result of a collaborative effort that marks the beginning of the association between two networks, AMENET and Making Finance Work for Africa (MFW4A) whose objective is to promote the linkages between young academic researchers in Europe and in Africa and practitioners in the African financial sector to bring theoretical techniques to bear on real-world issues.

2. Evolution of Africa's Financial System

Africa has, since the 1980s, faced a myriad of challenges affecting the development of its financial sectors. Macroeconomic and socio-political instability in the late 1970s and early 1980s sparked an unprecedented banking crisis which worsened financial stability and fiscal imbalances. Financial distress was especially acute among government-owned commercial banks and development banks. As a result, many countries fell into ▷

financial turmoil as the resolution of this crisis imposed very large costs on governments, while financial development suffered major setback.

However, the crisis at also prompted far-reaching policy reforms. Most African countries implemented structural adjustment programmes championed by the International Monetary Fund (IMF) and the World Bank with the introduction of widespread financial sector reforms as a key policy commitment (see Table 1).

These policies have successfully halted major banking crisis and led to the emergence of a more diversified financial systems with efficient deposit-taking institutions, more dynamic insurance industry and security markets. The experience of failed state-owned banks and other DFIs, led African governments to also focus on other financially viable approaches to providing finance. Key was the recognition of the role of microfinance institutions (MFIs) and developing regulatory and supervision frameworks to support their growth.

Historically, microfinance in Africa evolved in different stages. Financial intermediaries such as cooperatives, rural and postal savings banks were in existence during the 1970s, especially in East and West Africa. In the 1980s and 1990s, the sector registered the establishment of several donor-supported credit-only non-governmental organizations, transforming into new types of non-bank financial institutions (NBFIs) by the end of the 1990s. Subsequently, many countries in the continent included microfinance in their broader banking legislation and other microfinance-specific laws. The proliferation of MFIs along with other NBFIs increased access to finance, heightened competition for deposits

with the commercial banks and ultimately increased financial inclusion.²

Developments in the financial sector over the past two decades were also characterized by the proliferation of foreign banks following the early 90's privatization programs, as well as the development of Pan-African financial institutions (mostly banks and insurance companies). Pan-African banks have tripled in number across Africa between 2002 and 2017. The rapid rise of PABs was predominantly driven by the retrenchment of traditional European and US banking groups after the global financial crisis (GFC) in 2007/2008. This surge increased competition in financial intermediation and significantly stimulated Africa's interbank markets as a result, turning pan-African banks into a positive driving force of regional financial integration.

Significant progress has also been made in terms of stability. Most African banking systems showed remarkable resilience to the 2008 global financial crisis, reflecting not only their low exposure to risk emanating from the subprime crisis, but also major improvements in the quality of banking regulation and supervision of the past two decades. African governments embarked on aligning financial regulation and supervision to international best practices. As a result, financial systems became very stable well capitalised and over-liquid banking sectors.

Financial sector deepening in Africa also came with additional risks emanating from new product and service offerings, more complex financial markets, regional financial sector ▷

² Among the financial profiles that MFW4A is developing for most African countries, this trend is well illustrated by the case of Senegal, where only 28 credit institutions and 19 insurance companies have registered, but there are 208 microfinance institutions (MFIs) that lead the penetration rate of microfinance services in West Africa and reach 18.4% of the country's population (<https://www.mfw4a.org/country/senegal>).

TABLE 1
REFORMS AND POLICY OBJECTIVES

Reforms	Policy objectives
Abolishing credit ceilings and preferential interest rates	Effective financial intermediation towards productive sectors
Restructuring and privatizing state-owned banks and other financial institutions	Remove political interferences and improve efficiency of the banking sector
Instituting micro-prudential regulations and tightening Central Bank supervision	Ensure stability and profitability of financial institutions Ensure solvency and recovery of nonperforming assets
<i>Source: own elaboration.</i>	

integration and deeper links with global financial markets.

Large gaps still remain. Today finance in Africa remains insufficient in scale, too expensive and heavily geared towards the short end of the market. Banking systems are too small and concentrated, with low levels of savings mobilisation to finance productive activities in the real sector. Market imperfections such as information asymmetry and inefficient operations lead to high cost of borrowing, to the exclusion of large parts of the population. Insufficient depth, liquidity and market infrastructure inhibit the ability of capital markets to play their role as intermediators of finance.

Despite these constraints, the increase in diversity of financial service providers in Africa offers a tremendous opportunity for innovative ways to deliver financial services to the unbanked and underbanked. These trends, enabled by digital technologies and new business models, offer a glimpse of hope that finance in Africa is slowly starting to realise its potential as the engine of inclusive and sustainable economic growth.

3. Current State of the Banking Sector

Many African countries have seen significant growth and deepening of their banking

systems. Today, the continent is the second-fastest-growing banking market in the world, taking both retail and wholesale banking together. Commercial banks continue to dominate the banking sector in Africa, apart from South Africa, banks dominate the financial sector and therefore financial intermediation across the continent. The depth and coverage of financial systems, as measured by the ratios of private sector credit and broad money (M2) to GDP, albeit lower compared to other emerging economies, has increased over the past few decades.

Financial liberalization and related reforms, upgrades in institutional and regulatory capacity and the expansion of cross-border activities with the rapid development of pan-African banking institutions have significantly changed the African banking landscape.³

Banking sectors in Africa are now relatively deeper, more stable, and the occurrence of systemic banking crises has declined dramatically over the past two decades. From Table 2, ▷

³ The European Investment Bank (EIB) has been regularly producing a [report on banking in Africa](#) since 2013. The second edition in 2015 included a survey on pan-African banks expansion. MFW4A has collaborated with EIB in this endeavour. More recently, the [DEGRP programme of ODI](#) (Overseas Development Institute) has also analysed the expansion of pan-African groups, subsidiaries of Banks headquartered in African countries that have followed the retrenchment of European and US banking groups after the global financial crisis in 2007/2008 (Raga & Tyson, 2021a). In this process, the expansion of three Moroccan Banks (AWB, BCPE and BCME) is well analysed in a recent report issued in 2019 by the Direction des Etudes et Prévisions financières (DEPF) of the Moroccan Ministère de l'Economie et des Finances (DEPF, 2019).

TABLE 2
FINANCIAL DEEPENING IN AFRICA (2015 – 2019)

	2015	2016	2017	2018	2019
Broad money (% of GDP).....	42.44	44.14	43.72	43.06	46.23
Domestic credit to private sector (% of GDP).....	27.22	27.73	27.17	24.94	27.55
Domestic credit to private sector by banks (% of GDP).....	24.39	24.83	24.12	23.35	24.93

Source: World Development Indicator, World Bank (2020).

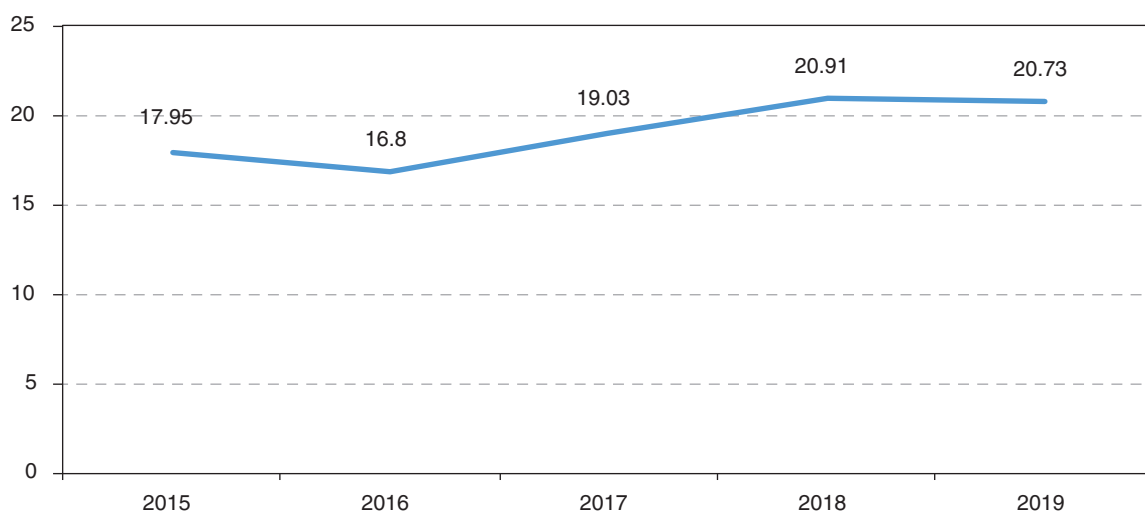
the depth of financial development, as measured by the domestic credit to private sector, is still shallow albeit with bank capital adequacy levels above the 10.5% requirement of the Basel Accord suggesting stronger banks' ability to withstand shocks (see Figure 1).

In addition to the improved capital adequacy levels, banks' profitability measures –by both return on assets and equity– also continue to grow. According to McKinsey and Company (2018), Africa's banking sector is the second most profitable (trailing behind Latin America and comparable to Emerging Asia and the Middle East) with return on equity more than twice the global average of 9%.

However, the cost of lending has remained high even as competition in banking systems have increased. This is due to individual banks holding excess liquidity and government securities, mostly treasury bills. This reliance on government securities is at the expense of providing credit to the private sector that directly enhance economic growth. Thus, the high returns as well as the less risky nature of government securities crowds-out private sector access to credit from commercial banks.⁴ ▷

⁴ Most interbank markets in Sub-Saharan Africa emerged in the 1990s but they are still at the early stages of development. In Kenya, Malawi, Uganda and Zambia interbank activity has already grown to around 30% of GDP (Raga & Tyson, 2021b).

FIGURE 1
BANK CAPITAL ADEQUACY RATIO (%)



Source: World Development Indicator of the World Bank (2020).

TABLE 3
BANKS' PROFITABILITY IN AFRICA (2010 – 2017)

	2010	2011	2012	2013	2014	2015	2016	2017
Bank return on assets (% , before tax).....	25.37	25.83	25.06	24.89	23.91	24.97	25.57	27.27
Bank return on equity (% , before tax).....	25.46	25.95	25.16	24.93	23.93	25.03	25.63	27.38

Source: Data for 2017 from the [Global Financial Development](#) (2020). Authors' computation.

There have also been improvements in recent years regarding the adoption of international prudential regulations and financial sector stability. Recent evidence from European Investment Bank (EIB, 2020) shows that majority of banking groups are compliant with Basel I and II while others are either compliant or working towards compliance with the Basel III.

4. Financial Inclusion

Access to finance has improved, but disparities remain. According to the Global Findex, the percentage of adults in Sub-Saharan Africa with access to an account has increased from 34 percent in 2014 to 43 percent in 2017, still below the global average of 67 percent. The spread of mobile money services in particular, has helped boost account ownership in many countries, surpassing traditional accounts. The percentage of mobile money accounts in Sub-Saharan Africa almost doubled from 12 percent to 21 percent between 2011 and 2017, highlighting the key role of technology and innovation in expanding access to finance in the continent.

4.1. The Role of Banks and Microfinance Institutions in Improving Access to Finance

About 60 percent of Africa's population still has no access to a formal bank account with a

financial institution or mobile-money provider. Another measure of penetration of financial services is the number of bank branches per 100,000 adults, presented in Table 4 below, is even lower in SSA (except in East Africa).

Indeed, the number of bank services such as ATMs and branches has increased over the years, bringing services closer to the populations. Banks are also leveraging technologies with mobile applications and improved website to better respond to the demand. On the lending side, banks continue to play a major role, despite a high proportion of businesses do not have access to credit. The MSME finance gap is estimated above \$ 331 billion in SSA alone.⁵ In fact, the lack of strong credit information systems put the banks at a high risk on loans as they do not necessarily have sufficient information and credit history on potential clients. As a result, non-performing loans ratio (NPL) of African banks stood on the average at 11.9 percent over the past decade, three times higher than the global median.⁶ With the current pandemic, this number is projected to increase.

MFIs have been play an important role in filling the financing gap left by other financial institutions such as banks. MFIs are also key in financing SMEs which accounts for over 90% of businesses in Africa. With only 19.3% of ▷

⁵ [SME Finance Forum en 2018](#).

⁶ The following article will provide more information on the development of risk information systems and the launch of the GEMS database ([Global Emerging Markets Risk Database](#)) in 2019 that is a significant milestone.

TABLE 4
FINANCIAL PENETRATION IN AFRICA IN 2017

	Account ownership	Bank accounts per 1,000 adults	Bank branches per 100,000 adults	5-bank asset concentration
Africa.....	41.36	476.00	8.75	80.49
North Africa.....	35.89	517.68	10.36	79.11
Sub-Saharan Africa.....	42.61	465.58	8.34	80.84
West Africa.....	35.29	402.14	6.81	77.99
West Africa without Nigeria.....	34.93	358.74	6.99	79.33
Central Africa.....	32.95	230.53	6.89	84.26
East Africa.....	55.01	754.30	13.06	73.80
Southern Africa.....	52.87	—	6.62	87.31
Southern Africa without South Africa.....	53.87	475.33	5.98	85.72

Source: *Global Financial Development* (2019); Authors' computation.

firms having a bank loan or line of credit in SSA, the sector has seen significant growth and is becoming an important driver of development by providing access to financial services to individuals generally excluded from traditional banking channels with inconsistent or low income, or poor assets as collateral.

4.2. Digital financial services and mobile money

With only 41 percent of adult formally banked in Africa, the spread of digital and mobile technology has already improved access to financial services for unbanked populations, mostly represented by women, young people, and people living in rural areas.

According to the 2019 GSMA Report on the State of Mobile Money,⁷ mobile money accounts are widely available in 96 percent of countries where less than a third of the population have an account at a formal financial institution.

Sub-Saharan Africa (SSA) is currently leading in the adoption of mobile money, with almost 21 percent of adults owning a mobile money account in 2017, according to Global Findex (Demirgüç-Kunt et al., 2018). In 2019 only, the number of registered mobile money accounts increase by 50 million. To tap into this potential clientele, banks are collaborating with Fintech and mobile operators to introduce financial products such as insurance, loans, payment service that can be accessed using mobile phones.⁸

Cash transfer is another important aspect of digital financial services. In 2019, over USD 690 billion of transaction have been recorded globally (24%), with SSA accounting for over 60 percent of that value, increasing since the beginning of the Covid-19 pandemic.

The mobile money industry is also impacting the lives of smallholder farmers, who represent 54 percent of the labour force in SSA. The 2019 GSMA Global Adoption Survey shows that about 10% of mobile money providers globally collaborate with companies from the agriculture ▷

⁷ Global System for Mobile Communication o GSM Association. <https://www.gsma.com/sotir/wp-content/uploads/2020/03/GSMA-State-of-the-Industry-Report-on-Mobile-Money-2019-Full-Report.pdf>

⁸ In June 2020, Orange, in association with the insurance group NSIA, announced the launch of the new Orange Bank Africa in Cote d'Ivoire, planning to expand their activities in Senegal, Mali and Burkina Fasso.

sector with the aim of extending agri-finance. Of these 10 percent, 75 percent are in SSA.

Although digital financial services already help significantly in making finance more accessible, their potential is not fully tapped in because of the limited interoperability. Projects are currently underway in Africa to address interoperability issues to boost peer to peer transactions and remittance payments.⁹

5. Long-term Finance

The limited availability of long-term finance across African markets is of particular concern given the huge long-term investment gaps related to fulfilling Africa's infrastructure, housing needs and SMEs. Currently long-term funding for infrastructure in Africa is predominantly provided by foreign capital sources including official and private sector funding.

Although relatively small, shallow and undiversified, African financial markets have undergone significant changes over the last decades, with capital markets gaining a prominent role. In addition to supporting the development of additional asset classes, they play a pivotal role in providing institutional investors access to a wide range of financial products.

5.1. Securities markets

African stock exchanges remain small and fledgling compared to their counterparts in Asia

or Latin America. The market capitalization of Africa's 30 stock exchanges exceeded USD 1.5 trillion as at 2018 according to the World Exchange Federation. The Johannesburg stock exchange (JSE) in South Africa dominates the region and the five largest exchanges (South Africa, Morocco, Egypt, Nigeria, and Kenya) accounts for about 90 percent of this total. The market capitalization of the JSE accounts for 3.6 times the country nominal GDP in 2020 while GDP ratios in other African countries (e.g. Ghana 8%, Nigeria 8%, Egypt 17%, and Kenya 24%) are much lower than the ratios in excess of 100% typically seen in developed countries, reflecting the absence of a critical mass of local companies that are willing to list. However, the percentage of market capitalization to GDP has risen significantly from an average of 38 percent to 61 percent from 2011 to 2019.

Besides South Africa and to some extent Egypt, liquidity remains a challenge, irrespective of market size. Usually, trading occurs in only a few stocks, those that represent the majority of market capitalization mostly financial, telcos or real estate stocks.

The situation started to change with the cross-listing trend started in the late 90's has contributed to a modest uptick in trading volumes in both the home and foreign stock market. Regional financial markets, mainly in West and Central Africa,¹⁰ have also contributed to encourage liquidity. This integration process has received a major impulse with the interconnection of major stock exchanges in the continent to further improve depth and liquidity on Africa's capital markets by facilitating cross-border trading of securities in Africa. The ▷

⁹ On this issue there is also some progress. For instance, Ghana introduced mobile money interoperability system in 2018 which allows seamless transfer of funds from one mobile money network to another. The Central Bank of West African States (BCEAO) in collaboration with AfDB, is also working on the interoperability of the digital payment systems of the eight West African countries belonging to the West African Economic and Monetary Union (WAEMU) to increase financial inclusion in the region, trade finance, and remittances.

¹⁰ Bourse Régionale des Valeurs Mobilières (BRVM) y Bourse des Valeurs Mobilières de l'Afrique Centrale (BVMAC).

African Exchanges Linkage Project (AELP) is led by the **African Securities Exchanges Association (ASEA)** with support from the African Development Bank and the Korea-Africa Economic Cooperation.¹¹

Since the 2000s, many African countries have also developed their domestic bond markets as an alternative source of financing for their economies. Bond markets are relatively nascent with few markets hosting a secondary debt market (South Africa, Nigeria, Ghana and Botswana). Total issuance of government bonds and bills has increased from USD 28 billion in 2000 to over USD 200 billion on average per year since 2009, with the notional value of the outstanding domestic sovereign market worth approximately USD 400 billion at end-2019. High interest rate and large domestic sovereign borrowing appear to have crowded out corporate issuers.¹²

Overall, African countries are making substantial progress in developing their debt markets on the back of new products, regulatory improvements and more responsive economic policy. At countries level, several policies designed to strengthen public sector capacity are gradually improving transparency. The African Development Bank (AfDB) and other Development Finance Institutions (DFIs) are providing support to countries debt management offices to enhance disclosures, establish a credible yield curve and

increase the take-ups of local institutional investors.¹³

With yield curves not going beyond 5 years in many markets, raising the long-term local currency funding needed for investment in priority sectors such as infrastructure and housing is also receiving attention. Insufficient depth and access inhibit the ability of capital markets to play their full role as intermediators of long-term finance. In 2017, MFW4A launched the Africa Long-Term Finance Initiative (ALTFI).¹⁴

5.2. Institutional Investors

Given the reduced fiscal space and declining ODA (Official development assistance),¹⁵ achieving the SDGs in Africa will therefore require a new approach to financing development, with African institutional investors playing a pivotal role in increasing access to long-term private finance.

Institutional investors such as pension funds, sovereign wealth funds (SWFs), and insurance companies hold the necessary resources to scale-up financing of much needed infrastructure projects and basic social services.

African insurance sector is not well developed compared to other regions with ▷

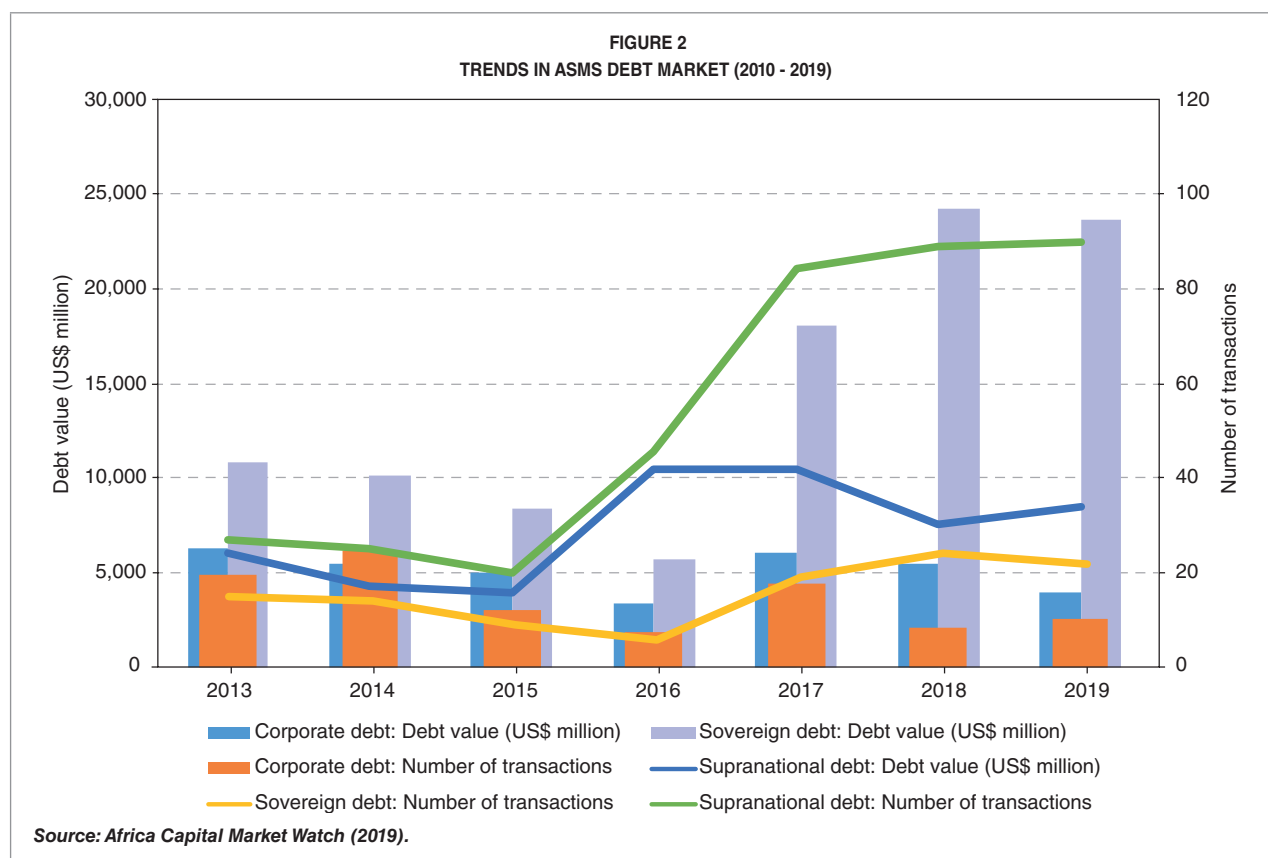
¹¹ The ASEA (African Securities Exchanges Association) was established in 1993 and is represented by 27 Stock Exchanges with the objective of promoting financial markets development and reach an average market capitalization of 123 percent by 2023. The AELP (African Exchanges Linkage Project) is the most important projects of the association that is working in collaboration with other Stock Exchanges outside the continent. The interest on green and social bonds is a key element together with the interconnection that could boost the development of African financial markets.

¹² PWC Africa publish annually since 2014 a report on African Capital Markets (PwC's Africa Capital Markets Watch). Five of the six reports published so far cover not only securities but also debt markets.

¹³ Promoted by the AfDB the initiative African Financial Markets Initiative (AFMI) contributes to provide reliable and updated information through a network of liaison officers in 30 African Central Banks. The two main elements are the African Domestic Bond Fund (ADBDF), first ETF (Exchange Traded Fund) of African debt and the African Financial Markets Database (AFMD). In 2017 took place the first debt issue sold exclusively through phone banking in Kenya (M-Akiba).

¹⁴ The main objective of ALTFI (<https://www.mfw4a.org/our-work/africa-long-term-finance-initiative-altfi>) is to promote transparency on LTF through a database and scoreboard to inform policy makers, the private sector and donors about the availability of LTF across Africa. The in-country diagnostics provide in-depth analysis of LTF markets in individual jurisdictions. The diagnostics will compass enterprise finance with a focus on SMEs, housing finance and infrastructure finance. La iniciativa realiza también diagnósticos a nivel nacional y regional. ALTFI is a joint initiative of the AfDB, the Financial Sector Deepening Trust for Africa (FSDA), the German Cooperation (BMZ/GIZ), and MFW4A.

¹⁵ Financing the UN Sustainable Development Goals (SDGs) in Africa requires about USD 600-700 billion a year UNCTAD (2016).



insurance penetration at about 2.8 percent compared to 9 percent for OECD countries and less than half of global average estimated at 6.3 percent. There are high regional disparities across the continent with South Africa having a market penetration rate of 14%. The insurance industry is valued at about \$68 billion in terms of Gross Written Premiums (GWP) in 2018.

Some countries have undertaken structural reforms, creating an enabling environment for new dynamic private pension schemes. This has led to growth in pension industry assets, for example in Nigeria where assets under management have grown from USD 7 billion in December 2008 to USD 30 billion in December 2020. Africa wide pension fund assets were projected to around USD 372 billion in 2018, from a 2008 total of USD 293 billion. The growth in the

continent's pension fund has largely been attributed to economic growth, the rise of the continent's middle class, improved access to financial markets, regulatory changes and advancements in technology that are bringing more people into the social security net. However, even when reforms of pension systems have taken place, the risk averse nature of pension trustees coupled with the limited risk diversification opportunities inhibit the growth of the fund structures in Africa.

During the last decade, new financial instruments have been developed, specialized infrastructure funds,¹⁶ structured ▷

¹⁶ Most PE Infrastructure Funds created recently are members of the African Private Equity and Venture Capital Association (AVCA, <https://www.avca-africa.org/>). In this field of infrastructure finance, the Africa50 (<https://www.africa50.com/>) is a new specialized bank established in 2015 by AfDB, 27 African States and 2 Central Banks.

financial vehicles that combine various sources of private and public financing with some type of guarantee, to attract precisely the most conservative funds. All these aspects will be developed in more detail in the next articles.

To conclude this section, it should be mentioned that the financial crisis of 2008 and the debate on the SDGs have once again put the role of the State in the economy on the table, twenty years after the liberalization of the 1990s. As a consequence, there has been renewed interest in development finance institutions (DFIs) which will also be discussed in greater detail in the following articles.¹⁷

6. Financial Sector Regulation and Oversight

The global financial crisis of 2007/2008 brought to the forefront numerous failures in regulatory and supervisory mechanisms as some financial institutions paid too little attention to future risks and appropriate capital levels. The crisis also heightened attention to the interactions and trade-offs between financial sector development and financial stability, and to the links between the financial systems and the real economy.

6.1. Aligning with global prudential standards

To ensure well-functioning financial systems, African governments embarked on aligning financial regulation and supervision to international best practices. As a result, financial systems became very stable with well capitalized and over-liquid banking sectors.

The global prudential standards represent major efforts to increase the resilience of banking systems around the world and thus reduce the likelihood of another systemic financial crisis. Consequently, African policy makers face increased pressure to accelerate the adoption of international regulations notably the Basel II, Basel III, International Financial Reporting Standards (IFRS) and the Financial Action Task Force (FATF) recommendations.

Against this background, the continent features different levels of implementation of Basel II and III. Some African countries have chosen to move towards full implementation of the new Basel III framework, while others prefer a gradual and customized approach of Basel II & III. For example, Nigerian authorities decided to implement only the aspects determined to be well suited for their country. In contrast, South Africa and the CFA zone under the supervision of the BCEAO (Banque Centrale des États de l'Afrique de l'Ouest) have committed to the standards in their entirety.

Like central banks, the unanimous recognition of corporate governance as a key ingredient for financial sector development has compelled other key financial regulators in Africa that are insurance commissions, pension commissions and securities market commissions to adopt regulations and ▷

¹⁷ There are around 140 DFIs and National and Regional Development Banks in Africa. 67 are members of the [Association of African Development Finance Institutions](#) (AADFI) that also gathers 12 regional organizations and support the capacity building and self-evaluation of its members through the "Prudential Standards, Guidelines and Rating System for African Development Banks and Finance Institutions" (PSGRS). The general interest on DFIs received a major impulse at the Summit Finance in Common of 2020 with the launch of the new database of Public Development Banks (PDB, <https://afdshiny.shinyapps.io/developmentbanksdatabase/>).

principles of good corporate governance in areas under their purview.

6.2. Addressing regulatory gaps and more importantly building up supervisory capacities

Traditionally, credit, liquidity and market risks are major preoccupations of regulators and supervisors. However, the accelerating pace of adoption of FinTechs has real implications. The diversification of financial services has put further pressure on regulators and supervisors to set-up and enforce legislation and implement regulations.

New business models often cross the boundaries of traditional financial services and require strong cooperation between regulators and supervisors from the financial and telecommunications sectors. While harnessing the benefits of new financial technologies there is the need to ensure that the risks posed by such innovations, particularly to financial stability are adequately managed and mitigated to ensure that financial systems play their full role in supporting economic growth.

One of the constraints that has been observed is that regulators and supervisors lack the capacity and resources to keep up with market developments, and to oversee increasing complexity in the financial sector. New and emerging threats –including anti-money laundering (AML) requirements, fraud and cyber-attacks– are adding complexity to the oversight function and will demand greater investment in systems and staff capacities. It is not a problem unique to Africa, but it affects the authorities in the continent in a particular way due to the lower capacity and faster adoption of new technologies by the population.

Furthermore, recent experience, including in the 2008/2009 global financial crisis, seems to show the importance of having a risk-based financial regulation that balances the objectives of inclusion, stability, integrity, and consumer protection. The ongoing COVID-19 pandemic crisis has further revealed the vulnerability of African financial systems to endogenous and exogenous shocks.

Finally, regulatory and supervisory authorities in Africa are increasingly embracing climate change principles by integrating climate-related risks in financial stability monitoring and micro-prudential supervision. Climate change as a source of financial risk can affect the balance sheets and business models of commercial banks in different ways. The purpose is to guide the banking sector towards supporting and implementing the low-carbon transition through the application of effective regulation and appropriate supervision.

Cognizant of the need to contribute to ongoing efforts of strengthening banking regulatory and supervisory frameworks on the continent, the [Community of African Banking Supervisors](#) (CABS) was established under the [Association of African Central Banks](#) (AACB) with the support of the Making Finance Work for Africa (MFW4A) Partnership. The initiative promotes the collective voice of African regulators in the international arena and is becoming a trusted partner for cross-border supervision cooperation and priority reforms and compliance with international standards.

7. Conclusion

The weight of the financial sector in Africa is still very low both in absolute terms ▷

compared to the rest of the world and in relative terms with respect to the GDP of each country. There is great room for growth and the previous sections have outlined the main advances that have occurred in the last two decades and that are laying the foundations for a sustained and inclusive development of financial services that contributes to overall economic development.

It should be noted, by way of conclusion, that most of the aforementioned aspects are favouring greater regional integration both through the expansion of private financial groups and the interconnection of markets as well as public collaboration for the adaptation and improvement of regulation and supervision on a continental scale.

This integration, together with the significant advance of financial innovation and the adoption of communication technologies, is the main factor that will contribute to solving the fragmentation of what will foreseeably be one of the main world markets in the most populated continent as of 2050.

The development of pan-African financial groups is another important aspect that requires greater intent because of the potential implications for economic relations within Africa and with the rest of the world.

The collaboration between MFW4A and AMENET seeks to attract more African and European researchers to improve the analytical skills and enrich the political debate on these issues. This work is only a first step in that direction.

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