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Replicating CRA in South Africa

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South Africa's complex and often troublesome history has created a number of global perceptions about its current banking conditions and the future of its banking system. The notion that South African financial institutions have neither the capacity nor the will to actively and creatively reach their emerging markets continues to persist. In South Africa, the term "emerging market" describes potential bank customers considered to be both socially and economically disadvantaged. This emerging market represents the majority of the country's population; it is predominantly Black, has had little or no access to banking services in the past, and comprises the lowest income-brackets of the South African economy.

Further elements underscore the perception that South African banks aren't adequately serving this emerging market. Chief among them is that most bank branches are physically removed from the daily lives of low-and moderate-income populations. As a result, many South Africans believe that banks cater unduly to the whims and fancies of a well-heeled minority. The serious and resolute introduction of a banking system where disadvantaged populations have access to bank services and credit could go a long way in removing such perceptions over time.

The ABSA Group

The ABSA Group is the largest banking institution in South Africa. Upon the formal dismantling of apartheid in 1994, ABSA recognized the need to adopt “a new way of thinking” about the ways in which low-income, emerging markets would be served. At the same time, ABSA wanted to consolidate its previously established community development activities, and strengthen its position within the emerging marketplace. Although South Africa doesn’t have nearly the number of banks that the U.S. has, it should be noted that ABSA is only one of a few banking institutions addressing the needs of its lower income communities. It has done this through:

- the creation of NuBank, a subsidiary bank (with branches in township areas) that focuses on microlending;
- the establishment of a televised education system that provides adult education through a national network;
- the creation of a foundation for community development and social investment; and,
- its role in the development of affordable housing throughout the country.

These and other efforts contribute to local capacity building and support the Growth, Employment and Redistribution (GEAR) strategy of the South African government.

In addition to their work in South Africa, the research division of ABSA embarked on a multi-year, international study in 1994 to learn how financial and non-financial institutions provide banking services to low-income populations in their respective countries. After extensive research in Southeast Asia, parts of Africa and Latin America, a high-level delegation visited the United States in the spring of 1997. Assisted by staff from several

Federal Reserve Banks, the delegation toured eight cities and towns across the U.S. with the following objectives in mind:

1. to investigate the role of the U.S. Community Reinvestment Act;
2. to learn more about the process of community-based development finance; and
3. to consider how these activities might have relevance for ABSA and other South Africa's initiatives.

The South African Marketplace

Before ABSA could analyze and apply what they learned from their international study, it was important to understand the cultural and social realities that affect the banking system, the emerging market and the South African economy in general. Some of these realities include:

- South Africa has a sophisticated, "first-world" infrastructure that exists within an otherwise thirdworld economy;
- Most Black South Africans view their personal and informal business¹ finances as a single entity;
- In the urban centers, well over 50 percent of all adult Blacks are involved in, or aspire to participation in, informal business ventures;
- Principles of sharing and collectivity run deep through both urban and rural Black communities; and,
- Low levels of literacy, poor standards of formal education, and minimal exposure to the fundamentals of the mainstream economy are a reality within the emerging market segment.

Although these and other realities present very real challenges, ABSA continues to emphasize the need for disadvantaged segments of the South African population to be better integrated into the financial system. Doing so will eventually lead to more balanced trade, legal entrepreneurship and economic growth.

It must be accepted, however, that the third-world nature of the emerging market will require approaches that are less formal, less conventional and altogether different from the traditional ways in which banking has historically been conducted. Instituting these approaches may present the greatest challenge of all.

Lessons from the United States

During the U.S. study-tour, the South African delegation received a crash course in the history, regulatory requirements and oversight of the Community Reinvestment Act. In addition to meeting with senior representatives of the Fed, the delegation met with several CRA officers, CDC directors and other key stakeholders involved in U.S. community reinvestment initiatives. In addition to the CRA, the delegation learned about U.S. safety and soundness laws and considered a number of fair lending issues. The delegation toured numerous local projects and studied their financial structures—learning along the way how community-based organizations leverage financial resources to bring projects to fruition.

Loan guarantee programs like the SBA's 504 and the low-income housing tax credit also piqued the interest of the South African delegation. Although the introduction of both programs would place a heavy financial burden on the South African government, the ABSA delegation recognized the value of such "risk-mitigating" programs—especially if other banks and private investors could be enticed to participate in the emerging marketplace.

ABSA has no objection to, and would even support, the creation of a CRA-type law for financial institutions in South Africa. In fact, it seems possible that this kind of legislation could become reality in the near future. ABSA points out, however, that there are a number of critical differences between U.S. and South African banking environments. These differences bring to

light several key issues that must be addressed before any such legislation could be effectively enacted in South Africa:

- The U.S. banking system comprises more than 10,000 banks and is largely decentralized, while the South African system is centralized, with a few large retail lenders dominating the market. As such, initial efforts should aim at the leveling of playing fields between all financial institutions operating in South Africa's emerging market. Issues of bank asset size as well as the kinds of financial institutions that would be covered under a new law must be addressed.
- Disclosure requirements of a CRA- type law could exacerbate already negative attitudes about doing business in the emerging market. These issues would have to be resolved judiciously, and information systems for data reporting could become a critical issue. In the U.S., the careful development of data collection guidelines was paramount to ensuring the credibility and comparability of the data reported.
- The approach to bank regulation in the U.S. seems generally interventionist compared to the South African approach which is less direct and emphasizes the cost-benefit relationship in banking supervision. A regulatory structure, which includes monitoring and enforcement, will have to be developed. The agency designated to administer such a law should meet with the approval of all industry stakeholders.
- South African geographical areas targeted by legislation will also be an important issue. What geographical units will form the basis of lending activity and disclosure? Provinces, local authorities, census tracts or township areas?

Even if these and other issues are properly addressed, reaching the goals of a CRA-type law is dependent on an environment where due process of law can be consistently applied. The current environment of violence and crime in South Africa has, thus far, discouraged many low-income lending initiatives. Until a greater degree of law-and-order prevails, the chances for successful community reinvestment regulations and community development programs remains tainted.

What the Future Holds

ABSA believes that a healthy banking system in which risks are properly managed is the cornerstone of a prosperous market economy. Legislation, supported by programs like the low-income housing tax credit and loan guarantees, could certainly improve the economy in the lower-income sectors of the country. Furthermore, the financial burden borne by the South African government could be lessened by the presence of foreign investors interested in the future of community development in South Africa. Organizations like USAID, the World Bank and others could play a major role in this regard.

ABSA also believes that the disclosure of relevant data is necessary to form sound assessments of the banking system's performance over time. However, a foundation for disclosure, which considers the aforementioned issues, will have to be established. In this process, a proactive and positive rather than punitive approach will be most effective in bringing other financial institutions onto the emerging market playing field.

Finally, ABSA is aggressively forming a framework in which community development lending/investment is a specialized part of its ordinary business. The company is focused on establishing unconventional and non-traditional partnerships with communities in an effort to increase the flow of capital to the emerging market. And, as it awaits the development of

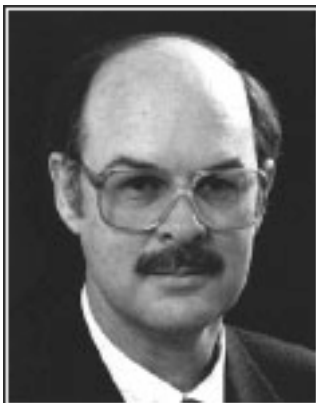
possible CRA legislation, ABSA strives to build a new world-view of South Africa's banking system.

¹In South Africa, the term "informal business" refers to one in which the income is irregular and generated through an unregistered (often illegal) business structure. Examples include unregistered domestic workers and street vendors. Official statistics in South Africa classify people involved in these businesses as having no income at all. It is, therefore, very difficult to know exactly what is earned in this sector.

The ABSA Group, listed on the Johannesburg Stock Exchange, is the controlling company of the largest banking and financial services group in South Africa. It provides a full range of retail and corporate banking, insurance, financial and property services through extensive local and international networks.

ABSA has nearly 76,600 shareholders and total assets of R134,9 billion (about \$30 billion U.S. dollars). It serves a customer base of about six million people throughout the country.

About the Author



Dr. Etienne van Loggerenberg is a General Manager of The ABSA Group. In this capacity, he is involved in the creation of

community development strategies, partnerships, and financial services/products which will better serve South Africa's emerging market.