

Emilio Sacerdoti has held several managerial positions in connection with Africa at the IMF and has gained extensive experience in the different financing issues facing the continent. In this article, he puts forward a macroeconomic approach that allows us to take an objective look at the issue of financing Africa's private sector in general and provides us with observations on the last ten years.

# Credit to the Private Sector in Sub-Saharan Africa: Developments and Issues

*Despite signs of progress, SSA is still lagging compared to other regions when it comes to scaling up the volume of loans allocated to the private sector. If it is to catch up, some progress needs to be made in areas such as information dissemination, the appropriateness of bank products, the regulatory environment and loan securitization. The last aspect is essential for SME lending activities, as the latter generally cannot provide sound guarantees. This issue of securing loans could be overcome by applying the principles of microfinance to SME financing.*

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It is well documented that financial deepening is much less developed in SSA than in most of the emerging market countries, with some exception such as South Africa and Mauritius, which have developed financial systems. Yet great strides have been made over the last decade and this has helped boost GDP growth rates in SSA countries. Since 2000, most of these countries have seen higher growth rates for private sector credit than for nominal GDP. The trend is encouraging and has been underpinned by lower inflation in most African countries and headway in liberalizing interest rates and foreign exchange markets which has given banks more flexibility to mobilize and allocate financing to creditworthy borrowers.

## Africa lagging

Yet despite these encouraging results, the ratio of credit to the nongovernment sector to GDP remains relatively low. In most SSA countries, even those where growth performance has been high over the last decade (Benin, Burkina Faso, Ethiopia, Ghana, Mali, Mozambique, Niger, Rwanda, Tanzania, Uganda, Zambia...), the ratio of bank private sector credit to GDP was still under 20 percent in 2007 (see table p.9). Indeed, in 2007 few SSA countries reached ratios of over 20 percent: Botswana, Kenya, Nigeria, Senegal, Swaziland and Togo (20 to 25%), Seychelles (35%), Cape Verde and Namibia (roughly 50%), and Mauritius and South Africa (over 75%).

In contrast, over the last decade this ratio has risen sharply in many of the world's emerging market countries where financial intermediation had previously tended to be low. In Latin American and Asian countries such as Brazil, Costa Rica, Colombia, Mexico, India and Sri Lanka, ratios were low in 2000 but have risen by half and in 2007 topped

the 40 percent mark in most cases. Central and Eastern European countries, where ratios were also low at the turn of the decade, have experienced a credit boom which has pushed the ratio over the 40 percent mark in most countries. Hence, while Africa has seen an overall improvement in the various forms of financial intermediation, the pace of progress has been faster in the rest of the world. This is a source of concern.

There has been much analysis on how to deepen financial intermediation in Africa in order to scale up access to credit, especially for SMEs. What is needed is more reliable systems for collateral, land titles and credit guarantees, that must give sufficient security to creditors; better information systems must be implemented via well-developed credit bureaus; leasing needs to be developed by removing legal and judicial constraints that hamper repossessions; tax rules that prevent lessors from deducting capital depreciation as well as taxes applied to the repayment of principal by lessees must be suppressed; mutual guarantee schemes need to be developed so that SMEs can benefit from the support of other members; instruments are needed to mobilize long-term savings that give longer terms for investment financing; swifter judicial credit recovery procedures are required and judicial systems must be more equitable in terms of debtor protection and creditor claims.

## Signs of progress

Over the last decade the African continent has made headway in reforms to improve legal, administrative and judicial arrangements in these areas. But progress has been uneven. Credit information systems have been established in Kenya, Tanzania, Uganda, Mozambique and Zambia, although there is still room for improvement ...

<sup>1</sup> The views expressed in this article are those of the author and should not be attributed to the IMF, its Executive Board or its management.

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... in their operation, as well as in the legal environment allowing for access to this information to non banking institutions.

Accounting standards have improved in many countries and have thus strengthened account transparency. An example is the introduction of the SYSCOA uniform accounting system in Western African Economic and Monetary Union (WAEMU) member countries in 2001. The creation of a regional bond market in WAEMU countries and the start of a similar market in Central African Economic and Monetary Community (CEMAC) countries have also helped mobilize long-term financing; bond markets have deepened in Ghana, Kenya, Tanzania, Uganda and Zambia and have made it easier for larger companies and financial institutions to raise capital. SMEs may not have access to these markets, but they can benefit from their development via support from financial institutions and large firms that can enhance their financing. Payment systems have also improved throughout the continent, facilitating transaction settlements between economic agents.

While these improvements are encouraging, there is still a long way ahead to bring the various institutional arrangements close to best practices. Credit information systems still need to improve in terms of coverage and access, auditing standards need to be reinforced and the small size of markets – with some exceptions such as the WAEMU regional market or the South African capital market – still limits access to long-term financing. More progress towards establishing regional capital markets, such as the efforts underway in the East African Community, will help create deeper capital markets. Due to the limited bond market, regional development banks such as the BOAD in the WAEMU, the BDEAC in the CEMAC area as well as some public national development banks, play an important role in providing long-term financing. The risk is that non-economic factors may influence these institutions' credit allocations. Moreover, these large institutions are not sized to target

SMEs and can at best have an indirect effect on SME financing via financing for large firms.

## Judicial reforms slow

It is probably fair to say that progress has been slowest in judicial system reforms aiming to strengthen title regimes, particularly land titles, speed up collateral recovery procedures and enforce judgements. It is still a lengthy and difficult process to recover credit or realize guarantees in most countries what explains why banks remain extremely cautious when selecting borrowers and continue to have high collateral requirements. This is particularly true when banks deal with SMEs since it is probably more difficult to realize guarantees with these counterparties than with larger corporate clients that can post better collateral. In many countries borrowers can adopt a series of delaying tactics to block creditors' efforts to collect delinquent loans, recovery fees are high, and accountants and lawyers specialized in insolvency issues are scarce. With low confidence in the mechanisms for collecting overdue loans, it is not surprising that banks remain very liquid and prefer to invest in government bonds.

Private sector access to bank credit is consequently limited. There are no easy solutions to these difficulties, as improvement in judicial and administrative systems may run counter to important vested interests. The title regime is complex on much of the continent as property has been held in communal form and the issuance of individual land titles may go against long-standing traditions. In addition, efficient judicial systems require the allocation of important additional resources for legal personnel training, court equipment and information systems. Countries facing pressing needs in the social sectors and in basic infrastructure have traditionally neglected these areas.

## Firms reluctant to seek loans

Data on SME access to credit is not systematically available. Some information has been collected ...

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... by a series of World Bank country Investment Climate Assessment (ICA) reports which typically survey a number of firms and collect data on how many firms applied for loans, the number of loan rejections and reasons for them, why firms do not apply for loans... These assessments are, however, made infrequently and general conclusions on credit trends in SSA cannot consequently be drawn. World Bank ICA surveys in countries such as Cameroon, Kenya, Mali, Rwanda, Senegal, Tanzania and Uganda indicate that most of the collateral posted for loans is constituted by real estate (land and buildings), and, to a lesser extent, by owner's own assets, machinery and equipment and accounts receivable. In Kenya (World Bank, 2004) small firms appear to be less likely to own collateral and are reported to be more credit constrained than larger firms. A larger share of small firms never applied for a loan. It is also worth noting that the ICAs report that a majority of firms surveyed in these countries have never applied for a loan and small firms are more likely never to have applied, although the share of firms that never applied differs from one country to another (it is lower for instance in Kenya than in Tanzania and Uganda). Reasons for not applying include high interest rates, too high collateral requirements, complexity of procedures and no need for credit. It is likely that collateral requirements are heavier in

countries where contract enforcement is weaker, stronger enforcement would consequently help expand credit access.

## The way ahead

In this environment, microfinance principles, whereby groups of loan applicants are jointly responsible for loan repayments, can help unlock credit in systems where contract enforcement is weak. The main limitation of microfinance is the small size of loans. However, in a number of countries such as Senegal and Benin, the strongest microfinance networks have been able to receive credit lines from traditional banks and have consequently been able to raise loan sizes. This suggests that the development of adequate mutual guarantee schemes among firms could be an important avenue for unlocking credit and promoting credit access for SMEs.

In conclusion, the road for developing access to credit in SSA remains difficult and challenging, but experience in other regions of the world shows that the obstacles can be surmounted if appropriate reforms to address the basic needs of credit systems are implemented. This includes more accurate information, adequate accounting standards, proper product diversification, functioning credit recovery mechanisms and contract enforcement, including for collateral recovery. ●

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## Bank credit to private sector as a ratio to GDP (%)

	2000	2007		2000	2007		2000	2007
Angola	1.2	7.9	Eritrea	26.5	24.6	Namibia	42.3	55.6
Benin	10.6	17.6	Ethiopia	17.9	17.3	Niger	4.6	8.8
Botswana	12.5	17.9	Gabon	8.3	10.2	Nigeria	109	18.3
Burkina Faso	10.9	16.8	Gambia, The	11.5	14.9	Rwanda	9.5	10.2
Burundi	17.2	20.1	Ghana	1.2	16.8	São Tomé & Príncipe	4.2	27.1
Cameroon	7.8	8.9	Guinea	3.5	6.2	Senegal	16.5	21.8
Cape Verde	38.1	44.5	Guinea-Bissau	7.2	4.9	Seychelles	15.4	314
Central African Rep.	4.3	6.4	Kenya	25.2	25.3	Sierra Leone	1.9	4.5
Chad	3.5	2.7	Lesotho	13.9	9.0	South Africa	64.5	75.3
Comoros	8.4	5.7	Madagascar	8.1	9.0	Swaziland	12.0	23.1
Congo, Dem. Rep. of	0.7	2.8	Malawi	4.6	6.2	Tanzania	3.9	12.4
Congo, Republic of	5.8	2.4	Mali	15.0	17.2	Togo	16.0	18.8
Côte d'Ivoire	15.0	14.7	Mauritius	56.7	76.7	Uganda	5.5	9.6
Equatorial Guinea	2.7	2.5	Mozambique	1.5	1.2	Zambia	6.7	10.0
						Zimbabwe	14.31	157.2

Source: IMF, International Financial Statistics, [www.imfstatistics.org](http://www.imfstatistics.org)