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Financial policy for the poor: Financial inclusion and microdebt

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AGGRESSIVE LENDING AND THE CREDIT HUNGRY CONSUMER

A View of Financial inclusion

Penelope Hawkins

FINANCIAL INCLUSION IN SOUTH AFRICA

- From 1992 – when an exemption to the Usury Act allowed for uncapped pricing of "small enterprise loans" - a booming "micro-credit' industry was born in South Africa.
- At the time, the well-developed enclave banking system in South Africa, was surrounded by widespread exclusion – in 1999, estimated that only 20% of the economically active population had bank accounts.
- Loans (and bank accounts) were granted to the employed and those with liquid assets (pension-backed loans). Payments system used to ensure early repayment. Small micro-lenders retained possession of the bank card.

FINANCIAL INCLUSION IN SOUTH AFRICA

- Concerns about the consequences of fragmented regulatory environment and undesirable credit practices resulted the National Credit Act in 2005 (effective mid-2007).
- Unsolicited offers of credit, call centres offering pre-approved loans and credit cards in the mail.
- The NCA introduced a structured cap on all categories of credit, reckless lending provisions and disclosure requirements, and compulsory use of credit register.
- Unsecured loans - Term 1 month to 60 months
  - TCOC - Prior to NCA – range 27% to 360%,
  - TCOC – post NCA – range 22% to 112%

FINANCIAL INCLUSION IN SOUTH AFRICA

- Reckless lending provisions hailed by many as ground breaking – consequence would be that rights of lender to collect would be rescinded.
- Improved disclosure – but still incomplete, difficulty of comparison
- Vast majority of credit – used for aspirational consumption purposes and domestic emergencies, debt consolidation.
- A number of failures of providers and unsustainable debt for consumers – led to a debt counselling process being implemented

AFRICAN BANK: WHO WERE THEY?

- Liked to describe themselves as “on a mission to lend money to those shut out by the apartheid state.”
- Acquired a failed bank in 1998, began to offer only unsecured loans (short term and longer term and credit cards) to lower-middle class. No retail deposits, only corporate funds and bonds.
- Very successful in generating returns. Banker of the Year twice - ROE 45% and 24% respectively.
- Oversubscribed bond issues in the UK and Switzerland in 2011, as well as a successful rights issue and bond issue in 2013….

AFRICAN BANK: THEIR DEMISE

- Considered illiquid and insolvent and in curatorship by August 2014.
- Aggressive extension of loans was the logical outcome of the business model of a bank where revenue growth was essential to generating investor interest in the business –
- Competition in sector resulted in beating the bushes and quality of book deteriorated
- Aggressive accounting that effectively amounted to masking impairments and NPLs. Provisions expected to be R150m in 2012, acknowledged to be R1,5b in 2013.

CONCLUSIONS

- Access to finance at reasonable rates is a necessary – but not sufficient - condition for growth - Effective demand for the product of entrepreneurs not guaranteed
- While it was estimated that 16.7 million consumers were credit active in mid 2007, with around 64% of those in good standing, by 2017 this had increased to 24 million, of which 59% in good standing.
- Shift towards unsecured lending – only categories of credit that have grown in terms of number accounts being credit facilities, unsecured loans, developmental credit and short term loans .
- Extension of credit has created greater fragility, but little small enterprise.