UNEP Finance Initiative
Innovative financing for sustainability

CEObriefing

A document of the UNEP FI African Task Force

Key Findings

- Social issues play a particularly strong part in defining sustainability in Africa.
- The financial sector has a major role to play in African sustainable development.
- Innovative financial solutions for sustainability are emerging in sub-Saharan Africa with the potential for many more.
- International trends in greater corporate governance and regulation of the financial sector have direct implications for sustainability banking in Africa.
- Enhanced capacity building on sustainability issues within the African financial sector is needed.
- Africa specific macro-economic challenges have to be addressed by public and private sectors to create a better environment for investment.
- Access to financial services is necessary to address problems in African communities.
- The SME and microfinance sectors have to be supported if the informal economy is to become part of the formal.
- The international finance sector has a contributing role to play in the improvement of their African counterparts' sustainability performance.

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Sustainability Banking in Africa

The finance sector has a pivotal role to play in the African renaissance. Across the continent a number of banks are championing sustainability and reengineering their operations to integrate environmental, social and better governance considerations.

For the first time sustainability banking practices in five African countries – South Africa, Nigeria, Kenya, Botswana and Senegal – have been surveyed in a Report backed by UNEP FI. It is clear from the Report that a number of financial institutions in sub-Saharan Africa are beginning to embrace sustainability. However, far more institutions need to adopt and adapt a dynamic business case linked to sustainability if the sector is to play a leading role in African economic and social rejuvenation.

This CEO Briefing summarises the main findings of the *Sustainability Banking in Africa Report*, produced by the African Institute of Corporate Citizenship (AICC), supported by the UNEP FI African Task Force (ATF) and funded by the International Finance Corporation (IFC), Finmark Trust, Nedbank and Deutsche Bank. The Report introduces how sustainability issues are relevant to the African financial sector and why the sector is key to sustainability in Africa. A unique production, it is intended for institutional investors, social responsible investment (SRI) fund managers, credit and project financiers and venture capitalists. It is also designed to provide a decision-making framework for policymakers, non-governmental organisations (NGOs) and corporate executives seeking to engage with the finance sector in Africa.

> "There is an implicit assumption within NEPAD that sustainability financing is a fundamental component of Africa's growth and development. Transparency and good corporate governance need to be core components of those finance institutions operating in Africa."
>
> **Mohammed Jahed**
> Chief Economist, NEPAD

About the Report

The key aims of the *Sustainability Banking in Africa Report* are to define what sustainability banking means in the African context, to analyse the current role of the finance sector in the promotion of sustainability in Africa and in so doing provide examples that are potentially replicable elsewhere across the continent.

The drivers, challenges and opportunities of sustainability banking in Africa are highlighted, along with a series of current product, process and market innovations that demonstrate the potential of sustainability practice within the African finance sector. The Report itself is not expected to represent a definitive account of all finance sector sustainability practices in Africa, but rather to provide an initial assessment of its status and hence recommendations for future innovations in the field.

It is expected that the findings will raise awareness of the achievements of ongoing work by a variety of financial institutions, and be used to energize a dialogue for action to encourage the adoption of similar innovations elsewhere on the continent. It is also hoped that it will provide a platform for the UNEP FI ATF, AICC and other relevant organisations to develop mechanisms to ensure that sustainability banking is taken forward in Africa in a manner that supports the goals of such pan-African programmes as the New Economic Partnership for Africa's Development (NEPAD).

Download the complete report at www.unepfi.org/africa

Specific Drivers for Sustainability Banking in Africa…

The Report states that as the international financial sector steadily shifts toward the implementation of sustainability banking practices, financial institutions operating in Africa are under increased pressure to meet such best practice trends. This coupled with emerging African initiatives, has created the following drivers for sustainability banking in Sub-Saharan Africa:

- **Regulatory developments** making banks and investors liable for their environmental and social impacts, create a financial incentive for the sector to incorporate sustainability issues into their risk assessments. For example legislation in South Africa can potentially hold financiers responsible for environmental pollution and other social risks, providing lenders and investors with a wake-up call that cannot be ignored.
- **Expansion of international standards, guidelines and corporate governance codes** has forced financial institutions to recognise that they no longer act independently from the societies and the environment in which they operate. Africa has begun to embrace such developments with recent shifts from a single to a triple bottom line managerial approach.
- **Pressure from various stakeholders** for greater transparency and disclosure by the financial sector, regarding their loans, investment and underwriting decisions, and the fear of negative publicity associated with these, has prompted the industry to become more committed to sustainability.
- **Social pressures** such as the need for job creation, black economic empowerment (BEE), poverty alleviation, HIV/AIDS, etc., can affect the financial viability of projects particularly in sub-Saharan Africa. There is a growing recognition within the financial sector of the necessity to deal with these issues at the financial modelling phase, to evaluate not only the effects on the projects, but also the implications they have on loan repayments and associated communities.
- **Potential for competitive advantage** underpins the growing realisation in the financial community that accounting for environmental and social issues during product development can increase new market opportunities. Progressive banks and investors are starting to gain significant competitive advantage through a systematic approach to environmental and social management and the introduction of more sustainable products and services. Likewise financial sectors at a national level are beginning to see sustainability as a potential competitive differentiator in attracting foreign direct investment.

…and Challenges

Whilst the motivation for sustainable banking may be growing on the continent, there are still a number of hurdles to be overcome. The challenges to sustainability banking in Africa are markedly different from those in the rest of the world. The general presumption is that various barriers to commerce – corruption, conflict, inadequate infrastructure, currency fluctuations, lack of technical know-how, etc. – make it impossible to do business profitably in the continent . But as the findings of the Report suggest, these conditions are changing and the barriers are much lower than is typically thought. Moreover, targeted improvements in the following areas could enhance the investment environment, accelerate capital flows, and facilitate the movement of banks towards more sustainable practices:

- **Political risk:** Greater political stability can attract investors, remove fears of non-performing loans and enable financiers to move from a "quick return" mentality to longer-term commitments with better product offerings for borrowers.

- **Capacity at a government level:** Creation and enforcement of environmental and social regulations and laws can ensure the consideration of sustainability issues within private sector developments.
- **Regulatory environment:** More flexible and less restrictive financial regulatory frameworks in many African countries can encourage the development of new products and services and create better access to banking services for the poor.
- **Capacity in the financial sector:** Overall improvements within the African banking sector's understanding, implementation and ability to pre-empt new trends in sustainability banking can facilitate the continuous development of new products to service the market.

Naturally, these challenges must also be addressed within a broader climate for change. Improved corporate governance, the eradication of corruption, contract enforcement and better transparency, reporting and accountability will also require continuous attention if sustainability banking is to become a reality in Africa.

"The challenges of sustainable development must be seen within the African context. We need to be careful that we don't impose values of developed countries as far as sustainable development is concerned."

Cas Coovadia
Banking Council of South Africa, Chair
UNEP FI ATF

Innovative Financial Solutions in Africa Today

In undertaking the research for the Report, over 50 financial institutions were interviewed and a number of others consulted about their role in promoting sustainability in Africa, specifically in South Africa, Nigeria, Kenya, Botswana and Senegal. From these interviews, 19 detailed case studies were developed, reflecting a range of product and process specific innovations, throughout the five nations. For the purposes of this CEO Briefing a snapshot of some of these case studies has been provided relating to the core themes of risk management and opportunity creation, pricing assets and exercising ownership, providing new finance, and greater access to financial services.* The chosen initiatives are reflective of the current level of sustainability banking throughout the continent and emphasise lessons that could be applied elsewhere in Africa as innovations for tomorrow. It is hoped that the case studies will demonstrate achievements to date and act as a catalyst for discussion on future reforms (full case study details are available in the main Report).

* In the Report, financial innovations were structured according to the following broad financial sector functions: risk management, pricing assets and exercising ownership, providing new finance, and savings and transactions. This framework draws from the London Principles launched at the World Summit on Sustainable Development (See www.forumforthefuture.org.uk).

Towards a Definition of Sustainability Banking

Sustainability is about ensuring long term business success, while contributing towards economic and social development, a healthy environment and a stable society. There are three broad components of sustainability sometimes referred to as the triple bottom line approach, or the 'social, environmental and economic' dimensions.

Although the finance sector does not have a direct significant environmental and social (E&S) 'footprint' compared to manufacturing or extractive industry sectors, it plays a pivotal role in contributing to sustainable development. For example, when banks consider financing projects, they naturally assess and attempt to mitigate financial risk. Sustainability banking incorporates the evaluation of E&S risk and the application of a comprehensive set of E&S guidelines towards the decision to finance a project. Thus a bank undertakes to provide loans to those projects whose sponsors demonstrate the ability and willingness to comply with policies and guidelines aimed at ensuring that the projects are developed in a socially responsible manner and according to sound environmental practices. This corresponds to the movement from defensive to reactive banking. In the next "competitive sustainability advantage" phase, sustainability related issues are recognised as drivers for developing new products and services, generating additional revenue and increasing market share. In the "ultimate" sustainability banking phase, the triple bottom line approach is integrated into the bank's core business strategy. Here, it is no longer limited to risk avoidance, but is seen as a potential part of every financial risk management and competitive decision making process and representative of the responsible competitiveness phase.

Case Study 1: South Africa

The South African financial sector is generally recognised as world class in terms of its skilled workforce, adequate capital resources, infrastructure and technology, as well as its conducive operating, regulatory and supervisory environment. South African banks are considered to be global leaders, with many internationally recognised financial sector innovations originating there.

South Africa in Profile:

- 1st developing country to introduce credit cards;
- 1st African country to introduce ATMs;
- 18th most competitive country in the world (countries with pop. over 20 million);
- 8th most developed banking sector, ahead of all emerging markets (exception Brazil), and some developed countries such as France and Japan;
- 1st stock exchange in the world to endorse the use of the Global Reporting Initiative (GRI) Guidelines on sustainability reporting for listed companies.

Finance and sustainability

The Report suggests that the financial sector has a central role to play in enhanced growth and development in South Africa (SA), and that the sector has become the model example of sustainability banking for other countries in sub-Saharan Africa.

However, SA continues to be confronted by a number of challenges that, as some of the case studies showcased here will suggest, are only now beginning to be dealt with more efficiently. Some of these challenges include low levels of black participation in ownership and management, partial response to the increasing demand for access to financial services, low levels of savings and investment to support sustained economic growth, and insufficient investment towards issues of national priority, such as infrastructure.

As with the rest of the continent sustainability issues in SA are primarily considered social concerns. This is reflected in the Report's inclusion of the results of the 2003 KPMG survey on Integrated Sustainability Reporting in South Africa, which highlights that employment equity initiatives, social investment prioritisation and health and safety are the most frequently disclosed areas of 85% of Top 100 companies reporting on sustainability issues (35% coming from the financial services sector).

However, several banks are offering products to exclusively support environmental protection and conservation. **Nedbank** for example established its **Green Trust** in 1990, administered by WWF-SA, the local branch of the World Wide Fund for Nature. The Trust funds a broad range of projects with a significant focus on community based conservation aimed at alleviating conflict between people and the environment, and since its inception has raised over R47 million (US$ 7.2 million) and supported over 120 projects in SA.

Risk management, pricing assets and exercising ownership

The **King Report on Corporate Governance** for SA (King II), published in 2002, advocates inter alia a shift from the single to the triple bottom line, embracing the economic, environmental and social aspects of a company's activities. King II is a listing requirement on the Johannesburg Securities Exchange (JSE); and applies to corporations within the South African financial services sector; and enterprises that perform public functions. It sets out a code of corporate practices and conducts for corporations in SA on a wide range of issues including: boards and directors; risk management; internal audit; integrated sustainability reporting; accounting and auditing; relations with shareowners; and communications with stakeholders. King II has played a significant role in widening the definition of risk to include sustainability issues, and in encouraging the financial sector to assess, manage and report on such risks.

In addition, in 2003 the JSE launched a **socially responsible investing (SRI) index**, based on the FTSE4Good index used by the London Stock Exchange, which will act as a guide to investors. It is the first such index among international emerging markets. To be included, firms must show a good record on human rights, environmental protection and stakeholder relationships, and the index's ranking process also assesses the actions companies take to address the impact of HIV/AIDS on their operations. The index targets the top 160 shares out of the 400 plus companies listed on the JSE, representing

The Power of Public Private Partnerships (PPP)

A partnership between The Big Four banks **(ABSA, First National Bank, Nedbank Group & Standard Bank)** and the government in South Africa was initiated in 2003 to develop a low cost transaction account, enabling the banks to cover at least 70% of the unbanked market in a relatively short time. Government will provide a small subsidy to cover the cost of a very basic generic bank account ("Mzansi Account") that all the big retail banks would make available.

Targeted at people who earn less than R2,000 (US$ 307) a month, this is expected to be used for services such as the payment of social grants as a basis of extending banking services to the currently unbanked.

See the Report at www.unepfi.org/africa for more details.

99% of the exchange's market capitalisation, with 52 companies successfully being listed in the first year of the index.

Also, in an effort to address the economic inequalities arising from the apartheid in SA, the financial sector committed itself to the development of its own black economic empowerment (BEE) charter. The **Financial Sector Charter**, launched in 2004, was developed voluntarily by the financial sector, for the financial sector and establishes targets and responsibilities to track and evaluate BEE progress, small medium enterprise (SME) development, the provision of housing for low-income people and increased access to financial services (the Charter requires financial services to be within 15km of the nearest community).

Providing new finance and savings and transactions

One South African bank has embarked on international trade in carbon credits. In 2003 **Standard Bank** announced an exclusive cooperation agreement with UK-based **EcoSecurities**, one of the world's foremost carbon credits advisory groups. The partnership should pave the way to eventual trade in carbon credits, a market worth "between US$ 10 and 30 billion per annum by 2008" according to EcoSecurities London MD Pedro Moura Costa. Standard Bank hopes to realise opportunities to finance carbon efficiency projects in SA and the region, as well as trading in carbon credits, demonstrating both the provision of new financial products and services and how risks associated with climate change can be transformed into positive business transactions (SA is a ratified signatory to the 1997 Kyoto Protocol on Climate Change).

In fact Standard Bank has been in the business of providing new types of finance and exploring alternative forms of savings and transactions for sometime. In 1994 it created an affiliate – which was merged into Standard Bank in 1996 – to deliver basic banking services to the poor in SA. the **E-plan Account** successfully addressed the common preconceptions about banking the poor (i.e. difficult to make a profit, due to the low balances kept on deposits), by developing a high volume, low cost product and service offering to meet customer needs for access and convenience of financial services. The AutoBank E outlets provide no telling function, the emphasis being on the creation of electronic accounts, instant card issue and assisted ATM banking. Standard Bank now operates 146 AutoBank E's, which when combined with traditional branches, serve over 3 million low-income customers. Being within the formal banking system allows low-income customers to access and move funds, save and expand funds, protect themselves and their families and qualify for credit. In return, since there is no back office and little paperwork in the AutoBank E's, the bank's costs are nearly 30% lower than at traditional branches. E Plan technology won an award for innovation from the Smithsonian Institution in Washington DC, in 1997.

Pricing assets and exercising ownership

Launched in 1992 the **Community Growth Fund** (CGF), managed by **Unity Incorporation** and **Old Mutual Asset Managers** was the first SRI fund in SA, its philosophy being to achieve sustainable long-term growth by investing in socially responsible companies.

One of 21 SRI funds in existence in SA today, its main aim is to offer retirement funds and individual investors the opportunity to invest in companies that met the following set of 8 social responsibility criteria:

- job creation through innovation and growth;
- equity through affirmative action in the workplace;
- training and skills development;
- economic and social empowerment;
- good conditions of employment;
- high health and safety standards;
- sound environmental practices;
- open and effective corporate governance.

The information is then translated into a score. Any company that scores below 50% on the scorecard is rejected. Companies that earn more than 60% are approved, while those that earn above 70% are highlighted for special praise.

Categorised as a general equity unit trust, the CGF now boasts a ten-year track record of above-average returns, while at the same time playing a crucial role in achieving fundamental change in the way South African companies pursue relationships with their workforce.

Some constraints of the fund may be the reluctance of South African companies to be subjected to the screening process along with its limited purchase universe due to the social responsibility criteria applied. However this universe has expanded over time, from only 20 companies in 1992 to 95 companies in 2004, and as Zithulele Cindi, of Unity Incorporation has commented "the fact that some 40 constituents of the first JSE SRI Index have been involved in the CGF over the last ten years or so can only mean one thing… it pays to invest in socially responsible companies".

> "Certain customers may be in the low income bracket, but that does not mean that they cannot save, or are financially illiterate."
>
> **Lincoln Mali**
> Director, Convenience Banking, Standard Bank

Case Study 2

Nigeria

Nigeria's 90 banks make it one of the largest banking sectors in Africa. However, 10 of these account for over half of the sector's total assets and deposits, leaving the majority weak and under-capitalised. The sector is one of the most competitive among emerging market countries and is known for its innovation and resilience. It is characterized by a high level of ownership by the private sector, directly or through the capital market.

Finance and sustainability

In 2003, a government committee was formed to initiate a series of capital market reforms while concurrently, a code of good corporate governance was also launched. Building on this, the Nigerian Securities and Exchange Commission began to develop its own comprehensive corporate governance code in 2004.

Yet, the Report indicates that to date, the focus of the Nigerian financial sector on environmental and social sustainability issues has been limited and very few banks have committed to sustainability banking in a tangible manner. Many believe that the Central Bank should drive the sustainability banking agenda, but that the finance sector, along with the oil sector, has a definite role to play in promoting the cause.

A primary challenge for the finance sector is restoring confidence in the banking system and overcoming the widespread public perceptions that corruption is pervasive throughout the sector. Another key challenge will be to create the right regulatory environment for sustainability banking, including improved access to financial markets for the poor and the development of appropriate legislation to promote sustainability investing.

Providing new finance

The Nigerian Central Bank has increasingly exercised its power as a regulator in line with internationally accepted norms and has been at the forefront of influential programmes, such as the **Small & Medium Industry Equity Investment Scheme (SMIEIS)**, aimed to boost equity investment into SMEs. Since 2001, the SMIEIS has required all Nigerian based banks to set aside 10% of their pre-tax profits for investment in Small and Medium Industries (SMIs), excluding trading companies, that qualify under the scheme. Funds are to be invested as equity, either as a cash injection, and/or conversion of existing debts owed to participating banks. SMEs in Nigeria have traditionally struggled to access appropriate financing, as what little finance is available is often short-term in nature and in the form of debt rather than equity (requiring a significant degree of upfront collateral as well as onerous interest repayment regimes). When properly supported, SMEs foster a culture of entrepreneurship and growth, reducing poverty levels through the diversification and strengthening of the economic base. Public and private policy support of SMEs is also most effective when SMEs are part of the formal sector and a key objective of the scheme is to encourage such SME migration into the formal sector.

To be successful, the scheme will have to be complemented by the development of an effective enabling environment at both the macro and micro level. The identification and development of appropriate support services for capacity building and technical upgrading are key. Professional management of the funds with due cognisance of equity issues as they relate to SMEs is also important for success.

In an attempt to address this a venture capital fund for SMEs was also established in 2001. The **SME Partnership** (11 Nigerian based banks and managed by SME Manager, an equity investment firm), is designed to only fund equity investments in SMEs that qualify for funding under SMIEIS. Total funds under management are US$ 25 – 30 million, of which US$ 7 million has currently been disbursed. The fund builds capacity in the SMEs significantly, by facilitating access to appropriate local or international expertise, or by arranging an equity partnership - often in the form

The Potential for Pensions...

The potential exists to link pension funds to equities with a focus on sustainability investing in Nigeria, as has been tried in other countries such as South Africa. Pension funds in Nigeria are traditionally under-funded with investments often only allowed in government bonds. Several interviewees expressed interest in tapping into international sustainability funds as the focus of these funds shifted towards investing in emerging markets. **SEC Trust** is currently investigating the development of an ethical investment fund for private clients, who have expressed an interest in these kinds of products. Should this fund go ahead, it would be among the first investments of its kind in Nigeria.

of a franchising arrangement or a technical support partner. As such, the fund encourages the financing of SMEs through venture capital, and could easily be refocused to target those companies with significant sustainable development benefits, hence creating the potential for a sustainability requirement to be incorporated into SMIEIS. This could mean the movement away from traditional venture capital towards sustainability venture capital, recognising key competitive trends and offering viable opportunities for international sustainability investors.

Access to finance

The **Oil Services Local Contractor Credit Scheme** is a revolving US$ 30 million facility established by **Diamond Bank**, in conjunction with the **International Finance Coorporation (IFC)** and **Delta Development Limited**, a subsidiary of Shell International. The facility aims to encourage the development of indigenous small and medium contractors providing services to Shell Nigeria. Loans range from US$ 50,000 to US$ 1.5 million, with a duration of 3-5 years.

The Credit Scheme enables qualified contractors to access competitively priced medium term US$ loans for capital investments and working capital requirements. While the loans are provided by Diamond Bank, IFC and Delta Development jointly offer a parallel facility, which is a capacity building and technical assistance programme to support contractors in the development and professionalisation of their businesses.

Successful applicants to the scheme must meet Diamond Bank's lending criteria, and may not engage in activities on IFC's Social Exclusion List or in activities that would be classified as IFC Category A Projects (having significant adverse environmental impacts, www.ifc.org/enviro).

Thus the long term sustainability and viability of these indigenous contractors and businesses may be dramatically improved, as the promotion of an understanding and awareness of risk management and sustainability business practice allows local contractors to compete more effectively with their foreign counterparts for local developments.

The scheme has also been working with stakeholders to ensure that the enabling and learning environment needed to support such an initiative is not restricted to the oil sector and in this case to the supply chain of one company, but that the lessons learnt are transferable. Ensuring that the knowledge and skills transfer process associated with this scheme is given wider applicability is critical to its the long-term success.

Case Study 3

Kenya

"In 10 years time Kenya might only have half the number of banks largely as a result of improved governance mechanisms. The surviving banks will be those that manage to implement sound governance procedures."

John Wanyela
Executive Director, Kenya Bankers Association

There are 43 registered commercial banks in Kenya, including 13 multinational banks and six banks that have government participation. Seven of these banks control approximately 70% of the market share. The banking sector is emerging from severe financial and reputation damage resulting from corruption, economic recession and government debt of the past decades. The new government (as of 2003) however has placed an anti-corruption strategy at the top of its agenda, and has embarked on major strengthening of its governance and anti-corruption institutions, including the tabling of key governance legislation. As for the financial services sector specifically, the Central Bank has promoted the enforcement of statutory requirements, more stringent supervision and increasing capital requirements.

Finance and sustainability

The Report states that the current challenge for the banking sector is to reduce the non-performing loan portfolio, improve management abilities and introduce basic corporate governance throughout all branches and networks to help change its image. In light of this, there is the opportunity to incorporate the principles of sustainability into the financial sector as the entire system is being overhauled.

Moreover, although the Government has attempted to make environmental management a priority these efforts have not yet had significant influence as the majority of Kenyan banks still do not consider environmental or social issues a concern when providing credit.

In addition, a low level of savings in Kenya hampers capital creation. This is due in part to limited access to financial services by the majority of the population (80% of adults do not have access to such services). There are only 10 active registered microfinance institutions which have managed to reach a clientele of just 300,000. To remedy the situation the Government prepared a Draft Micro-Finance Bill in 2003 allowing the Central Bank to license and regulate microfinance

Case Study 3:
Kenya

> "There are more than 1.3 million people in the country who own small scale businesses but who have no access to banks."
>
> **Moses Banda**
> Chief Manager of Credit and Microfinance operations, K-Rep Bank

credit providers, especially those authorized to accept deposits from the public.

Despite this range of challenges, the Report suggests that the future of sustainability in the Kenyan banking sector is bright with promising examples beginning to emerge. The Nairobi Stock Exchange for instance has begun to include corporate governance as a listing criterion for companies, and shareholders are becoming more vocal through a shareholders' association launched by the Capital Markets Authority in 2003 as a forum for activism.

Providing new finance

Established in 2000, **K-Rep Bank** is a savings and loans bank for the poor. K-Rep was initially founded as an NGO, but later realised that accessing grants was not sustainable, and opted to secure a banking license. The NGO subsequently became K-Rep Development Agency and today remains an NGO, funded from K-Rep Bank's profits and other grants. The transition from an NGO to a commercial bank has been hailed as highly innovative and one of the most successful microfinance schemes in Africa. While other commercial banks have closed branches in rural areas K-Rep has managed to tap into these rural markets through its numerous branches. Keeping within the traditions of an NGO development agency, K-Rep prides itself on operating at the "grassroots" with low-income people. With 25 outlets country wide, the bank has enabled the servicing of a huge part of the unbanked population in Kenya reaching some 40,000 borrowers, 52% of whom are women.

An innovative idea being explored by K-Rep Bank is linking Small, Medium and Micro Enterprise (SMME) debt financing to sustainable development projects. This will empower SMMEs to provide such services as water, education (under governmental licence), health, and waste management to low-income areas where the state has been unable to do so.

In additon, recognising that HIV/AIDS poses a significant threat to the sustainability of the bank, K-Rep has realised that education and awareness raising are necessary to mitigate the impact. Future innovation lies in providing credit schemes to HIV/AIDS infected and affected people to develop small businesses.

Access to finance

Equity Building Society (EBS) has a unique portfolio of savings and loans directed at the poor. With 252,000 depositors and 67,000 borrowers, EBS is the largest single microfinance institution in Kenya. Equity targets economically active and salaried individuals on low and middle incomes in rural areas – consumers that are often ignored by mainstream banks.

One of EBS's key accomplishments is its innovative delivery process. The company has developed a network of 32 mobile village banking units to offer services to unbanked rural areas. The mobile units serve each area once or twice a week, providing their customers in remote areas with the financial services they would receive from a branch e.g. bank cheques, remittance processing and loan applications. The customers pay the same rates for their transactions, and are charged a modest fee for the mobile access. Each mobile bank consists of an all-terrain 4-wheel drive vehicle, staffed by 2 or 3 bank employees using solar power to run the computerised systems and scanners needed to check ID documents for account holders. Such innovation makes it possible for EBS to "take banking services to the people" in areas where internet service banking has failed due to poor infrastructure, or where rural branches have shut down.

In addition, EBS provides loan products covering farm inputs and crop advances for agricultural workers, small and micro business products, and medical and education loans. The latter are subsidised products run on a small margin as part of Equity's commitment to social responsibility. Such loans can be used to alleviate the cost of medical bills associated with HIV/AIDS, or help pay for school fees. The company also incorporates environmental concerns into its core investment principles, as illustrated by one of its products, the 'Sunpower Loan' which supports environmental improvements such as installing solar power.

The Report summarises how Equity's innovative banking approach has proven to be very successful despite Kenya's difficult economic climate, with a remarkable growth rate of between 50-70% per year over the last 8 years.

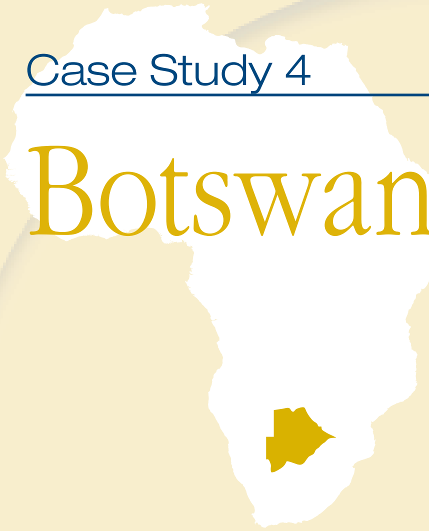
Innovations in Malawi Today for Kenya Tomorrow?

Malswitch, part of the Malawian Reserve bank, is pioneering the development of new banking services using **smartcards backed by biometrics technology**. Card users are allowed to authorise their transactions by scanning their fingerprints, as an alternative to less secure verification by PIN or signature. Malawi is the second country in Africa, after South Africa, to use such technology, which offers the following benefits:

- Access to banking: The majority of Malawi's population is "unbanked". Smartcards offer a secure and portable repository for cash.
- Economic efficiency: More money stored on smartcards translates into a larger pool of funds for banks to invest, giving borrowers access to more capital.
- Reduction in fraud and crime: Related to identification requirements and smaller cash holdings.

Case Study 4

Botswana



Over the last 30 years, Botswana has moved from one of the poorest and under-developed countries in the world to a position of middle-income. Botswana's financial sector is relatively small, reflecting the small size of the market and, perhaps, the rigorous approach to licensing and supervision. There are five commercial banking institutions which are highly profitable, two investment banks, two state-owned development finance organisations, one building society and the Reserve Bank.

The Botswana Stock Exchange (BSE) was established in 1989, and has performed remarkably well in terms of the level of capitalisation and returns on shares. In addition, between 1990 and 2000, there has been a significant growth in pension and life insurance funds, and by law, 30% of these assets must be invested in Botswana, contributing to growth on the local stock market.

Finance and sustainability

The Report outlines how the interrelationship between finance and sustainability is a very new concept for the financial sector in Botswana. However, it also states that due to the stable macroeconomic and political environment, the liquidity and profitability of financial institutions and good central bank supervision, Botswana is in a perfect position to implement and develop innovative sustainability banking and investment products, with the potential to become a regional leader in this field.

It also becomes apparent that excess liquidity has meant that banks in Botswana have largely worked in isolation of international financial institutions that may apply environmental and social criteria to their products and services/transactions, and thus any drivers for efficient sustainability banking will have to be initiated internally or from regional institutions with offices in Botswana.

Access to finance, pricing assets and exercising ownership

Deriving from its investment grade sovereign credit rating, Botswana is in a strong position to raise funds for investment in infrastructure and non-traditional industries that can help the economy develop beyond its core reliance on diamonds. Banks could play an important role in helping to realise this goal, which could have a tremendous influence in the sustainable development of the country.

A more flexible and diversified system of allocating credit and providing equity could be developed to support the emergence of Botswana-owned small and medium sized enterprises. The development of improved opportunities for SMEs to be listed on the BSE is a distinct possibility. Furthermore, it is within the power of the banks to develop strategies that will ensure citizen empowerment and strengthen the participation of citizen-owned companies in the supply chain network of the economy.

Yet, despite a relatively healthy and growing banking sector, the proportion of private sector loans going to business, in contrast to households, has declined from 70% in 1990 to 45% in 2001. This indicates a shift of resources away from productive investment towards consumption, and corresponds to the failure of the country to diversify the economy and to develop a strong network of SME, locally-owned enterprises. As such, there is concern that the banking sector is unable to adequately service potential SME growth. In response, governmental initiatives such as Citizen's Entrepreneurial Development Agency (CEDA) are taking steps to improve such efficiency.

Similarly, one of the challenges relating to the growing microfinance sector is that it is not explicitly regulated by the government and no Usury Act exists. As a result, very little is known about the industry as a whole and limited assessment has been done of the possible opportunities for consolidation and growth. Cooperation between the government and the private sector, as is the case with the South African Finance Sector Charter, could significantly enhance access to financial services in Botswana. NGOs could also play a much greater role in building such partnerships, particularly for business and housing purposes in poor rural communities.

Risk management

The quality of banking supervision in Botswana is considered to be adequate. However, the Report deduced that banks in Botswana are not yet looking beyond conventional financial risks. Social and environmental considerations are currently not on the banking agenda, despite the severe impact of issues such as HIV/AIDS on the country, and developments in sustainability risk management in neighbouring South Africa. Although some major international institutions are beginning to seriously incorporate sustainability considerations into their global risk management strategies, the localisation of these sustainability concerns has yet to be realised.

Innovative Ideas for Tomorrow

- **Training** by country-level financial associations should include a core module on sustainability banking.
- **Standards and guidelines** to manage social and environmental risk need to be established.
- **Legislation** to encourage the microfinance sector should be developed.
- **Capacity building** by banks in the SME sector could ensure long term business planning and management.
- **Partnerships** between the government, private sector and NGOs could improve acess to financial services.

Case Study 5

Senegal

Senegal's financial sector is among the better developed of the West African Economic and Monetary Union (UEMOA). It is comprised of 11 banks, some five insurance companies and more than 40 registered microfinance institutions. There is also a range of other semi-formal and informal financial institutions, including a number of micro credit institutions. With approx. 5% of the population having access to formal banking services, the expansion of retail banking services is a potentially untapped market in Senegal and there is room for further development and diversification of the financial sector. Being a commodity economy, the Senegalese financial market is dominated by short term trading finance, and much of the project finance that does exist is linked to state projects or large state-dominated industries. As a result, the longer-term end of the market is relatively under developed with weak contractual savings institutions and a nascent regional stock exchange.

Finance and sustainability

The Report highlights that the Senegalese financial sector has very limited awareness of environmental and social sustainability issues presently. When these are considered, it is mostly due to IFC or other international investors' requirements, and the focus tends to be on environmental issues arising in the large state owned export companies. Moreover, Senegalese banks are generally perceived as being over-liquid, partially as a result of the limited lending market. This liquidity means that banks do not have to predominantly rely on international capital, which could otherwise bring broader social and environmental constraints.

Generally, the shared opinion is that sustainability banking is a luxury that only richer countries can afford and that the responsibility for improving social and environmental practice lies with the government. In this regard, regulatory reform is perceived as the only tool likely to change current practices. The Report also suggests that there is the need for awareness building regarding the role of the private sector in fostering an improved enabling environment to ensure increased sustainable growth.

Access to finance

In 1993, **Alliance du Crédit et de l'Épargne pour la Production (ACEP)**, originally founded as a donor-funded credit union, became a self-sustaining commercial organisation. It rapidly expanded, becoming one of the most successful mutuals in the West African SME/microfinance sector. Between 1993 and 2001 credit volume grew from CFA 2,109 million (US$ 3.6 million) to CFA 11,846 million (US$ 20.3 million) and ACEP is now serving more than 40,000 individual credit clients.

ACEP's target clientele is upper-end micro entrepreneurs who are expanding their business and those making the transition to the formal economy which generally lack access to formal financial institutions. ACEP benefits from the business environment in Senegal, where large numbers of SMEs or micro enterprises do not wish to become a complete part of the formal tax paying economy. It also attracts clients by offering less stringent guarantee requirements and controls than its commercial counterparts. Though traditionally urban and peri urban focused, ACEP often reaches whole supply chains in the informal market and contributes substantially to job creation and poverty alleviation in the country.

The company's sustainability strategies include a range of innovative operating and management processes, such as the use of group credits for more cost-efficient processing. It also uses its most dependable clients as a proto-credit reference bureau and informal credit retailers to small and poor borrowers, who would not otherwise qualify for ACEP's programmes. As a result ACEP thrives on remarkably high repayment rates. Additional key success factors also include incentive-based remuneration where agents are required to have a minimum of a 95% loan repayment ratio before subsequent loans are released, as well as the development of a powerful technology platform suitable to meet the needs of ACEP's small-scale operations.

The Report suggests that the one key challenge for ACEP today seems to be its lack of access to stable funding, as savings are not sufficient to meet the growing credit demand of its clients. Availability of funding from Senegalese banks has so far been limited because banks are reluctant to deal with microfinance institutions without a risk-mitigating mechanism and specialised investment funds do not typically invest in mutuals. Other challenges include constrained interest rates that do not cover full cost of providing the service. Looking forward, ACEP sees its continuing success in the diversification of its activities and products.

Innovative Ideas for Tomorrow

- **Repatriated money** by the Senegalese diaspora could be used to develop sustainability funds, e.g. private equity schemes or social development funds. At present, up to 25% of the economy is derived from such funding.
- **Legislation** pertaining to the microfinance sector should encourage a more flexible financing of SMEs.
- **More targeted equity investment** into microfinance institutions (MFIs) is needed. Most Senegalese MFIs are currently set up as cooperatives and are not structured in such a way that would open them up to the introduction of external investment.
- **Equity to promote sustainability financing** is required. Changing the access conditions on the stock exchange to allow broader SME entry or improving private equity flows going to SMEs are possible areas of innovation.

In Summary...

Evidence from the Report points to the emergence of a dynamic business case for sustainability banking in sub-Saharan Africa – derived from new corporate governance standards, better regulatory frameworks, and increased financial sector capacity to implement sustainability practices and to enter or create new markets. Although there is an impressive range of financial innovations supporting sustainability in Africa, there is clearly the need for further innovation regarding efforts to understand and address African specific sustainability problems. The Report deduces that greater access to financial services and SME support can provide solutions for these problems, especially as financial "exclusion" is seen as an acute issue of concern in Africa, not simply as a matter of inconvenience, but potentially as a denial of a basic right.

The establishment of public-private partnerships are fundamental component to the creation of a better environment for change, which is crucial if negative international perceptions of Africa are to become more optimistic and investor-friendly. The Report also suggests that such bodies as Banking Councils and the UNEP FI ATF should be supported by public, private and broader NGO stakeholders to disseminate good practice and develop standards for sustainability banking in Africa. The key findings of the Report have been captured below, accompanied by some innovative ideas and recommendations on how to address these issues in the future. They serve as an indicator of the dynamic debate that currently surrounds the progression of sustainable development by the African financial services sector, and energize further dialogue on the finance-sustainability agenda in Africa.

Key findings and recommendations

1. The financial sector has a major role to play in the creation and delivery of practical solutions to the challenges of sustainable development in Africa. Numerous examples of innovative financial solutions exist, and there is the potential for many more.

2. International trends in corporate governance, regulation of the financial sector, environmental and social (E&S) liability issues and increased stakeholder pressure, are influencing the sustainability banking in Africa.

3. Africa specific macro economic challenges e.g. the legacy of corruption, failing economies, images of nepotistic banking sectors, the need for better governance and more sustainability related legislation, must be addressed to create a better environment for investment and change.

Recommendations for governments

- Expand E&S liability legislation.
- Foster an enabling framework to incentivise sustainability banking.
- Create policies for the extension of access to finance for the poor and support microfinance sectors.
- Mainstream E&S criteria for pension, life insurance and government-controlled funds.
- Adopt E&S reporting requirements for stock market listed companies and state enterprises.

4. Enhanced capacity building within the finance sector on the interconnection between sustainability and core operation is needed.

Recommendations for the financial sector

- Develop policies and guidelines to integrate E&S concerns into core business activities and corporate governance strategies.
- Adopt international and locally recognised E&S codes and standards.
- Review risk assessment tools applied to portfolio investments to increase E&S and risk-return profiles.
- Increase investor engagement on sustainability issues.
- Increase SRI fund options for institutional investors and inhance trustee education on SRI issues.

5. Sustainability issues are largely associated with **social concerns** in Africa, e.g. water, food, and shelter scarcity, poverty, HIV/AIDS, etc. Pressure to address these issues is proving to be a strong catalyst for change.

6. Access to financial services for the underprivileged is a prerequisite to addressing the social imbalances and problems associated with many African communities.

Innovative ideas

- Alternative means of providing banking to rural areas.
- Customise financial products and services for societies.
- Expand postal bank services to the poor as a stepping stone to mainstream commercial banking.

7. The SME and microfinance sectors have to be supported – financially and technically - to become part of the formal economy.

Innovative ideas

- Capacity building in the SME sector by banks to ensure long term business planning and management.
- Support small-scale financial intermediaries offering sustainability venture capital.
- Encourage microfinance practioners to securitise their loan books for mainstream capital markets.
- Development of micro-leasing to promote entrepreneurship and small enterprises.

8. Public-private partnerships (PPP) are valuable mechanisms for developing practical responses to African challenges.

Innovative ideas

- Establish PPPs to provide venture capital for sustainability start-up businesses.
- PPP development of regional principles and guidelines to manage E&S risk.

9. The international finance sector has a contributing role to play in the cross–fertilisation of ideas and experiences on sustainability banking with African financiers.

Innovative ideas

- Promote new risk management techniques when investing in Africa.
- Develop more sustainable financial products and services for African markets.
- Apply a "best-in-class" approach to interactions with African banks.

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UNEP FI

The United Nations Environment Programme Finance Initiative (UNEP FI) is a unique global partnership between UNEP, financial institutions, insurance and re-insurance companies and fund managers. Based in Geneva, Switzerland, UNEP FI works closely with more than 200 member institutions worldwide to develop and promote linkages between the environment, sustainability and financial performance (see www.unepfi.org).

UNEP is headquartered in Nairobi, Kenya. UNEP has eight divisions through which it carries out it activities, including the Division of Technology, Industry and Economics (DTIE) based in Paris, France. The Economics and Trade Branch (ETB), based in Geneva, Switzerland, is a branch of DTIE. The Finance Initiative is a unit of the ETB.

UNEP FI ATF

The UNEP FI African Task Force (ATF) was launched in 2002 with the primary aim of promoting best sustainability practice across all financial sectors within a specific African context. The Task Force is comprised of members from the African financial sector, assisted by a smaller group of non-financial associates (see www.unepfi.org/africa).

AICC

The African Institute of Corporate Citizenship (AICC) is a leading non-governmental organisation based in Johannesburg, South Africa. AICC relates corporate citizenship to the private sector and to a wide range of organisations with economic, social or environmental impacts on society. It is committed to strengthening responsible growth and competitiveness in Africa through research, advocacy and network building. Sean de Cleene, AICC director, is Co-Chair of UNEP FI's ATF (see www.aiccafrica.org).

All references can be found in the Report available for download at www.unepfi.org/africa

UNEP FI ATF Members & Associates

Members:

Banking Council of South Africa
Cas Coovadia
ATF Chair
Tel. + 27 11 370 3562
casc@banking.org.za

AICC
Sean de Cleene
ATF Co-Chair
Tel. + 27 11 643 6604
sean@aiccafrica.org

Citigroup
Donna Nemer Oosthuyse
Tel. +27 11 944 0212
donna.oosthuyse@citigroup.com

Development Bank of Southern Africa (DBSA)
Elsa Kruger-Cloete
Tel. +27 11 313 3300
elsak@dbsa.org

International Finance Corporation (IFC)
Justin Pooley
Tel. +27 11 731 3000
jpooley@ifc.org

Investec Bank
Setlogane Manchidi
Tel. +27 11 286 7189
smanchidi@investec.co.za

Nedbank
Justin Smith
Tel. +27 11 294 0238
justins@nedcor.com

Standard Bank
Sandra Ainley
Tel. +27 11 636 8958
sainley@sbic.co.za

Standard Chartered
Mzinga Melu
Tel. +27 11 217 6794
mizinga.s.melu@za.standardchartered.com

Associates:

Africa Centre for Investment Analysis (ACIA)
Nicholas Biekpe
Tel. +44 151 494 9772
nbiekpe@acia.sun.ac.za

African Investment Advisory
Hubert Danso
Tel. +44 20 7462 7588
hdanso@aia.uk.com

AICC Centre for Sustainability Investing
Tel. +27 11 643 6604
info@aiccafrica.org

Industrial Development Corporation (IDC)
Portia Ngwenya
Tel. +27 11 296 3196
portian@idc.co.za

Unity Incorporation
Zithulele Cindi
Tel. +27 11 333 7545
u.incorp@mweb.co.za

UNEP

Paul Clements-Hunt
Head, UNEP FI
Tel. +41 22 917 8116
pch@unep.ch

Niamh O'Sullivan
ATF Project Manager, UNEP FI
Tel. +41 22 917 8685
niamh.osullivan@unep.ch

François Malo
ATF Secretariat, UNEP FI
Tel. +41 22 917 8764
francois.malo@unep.ch

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