Ecobank and the African cross-border banking gap

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Summary

Leadership changes at African retail bank Ecobank two weeks ago ended a long and debilitating governance crisis for the bank. These events offer a case-study in the complicated politics of African cross-border banking and some of the big challenges banks like Ecobank will face working with African regulators struggling to build institutional frameworks to keep up with African market developments. The question for Africa's cross-border banks, the businesses that depend on them and the investors increasingly interested by their potential is how politicians and policymakers in Africa balance the benefits of cross-border banking and supervisory concerns about risk contagion. The regulatory gap that needs closing in African banking also matters for African systemic stability. The experience of EU and ASEAN may provide lessons and ideas.

Two weeks ago the CEO of African bank Ecobank Thierry Tanoh was removed by his board after a campaign of regulator, media and investor pressure culminating in a damning report from the Nigerian Securities and Exchange Commission. Most coverage and commentary of Ecobank over the last year has focused on the governance problems and the personalities, especially vindicated Beninese whistle-blower Laurence Do Rego and unseated CEO Mr Tanoh, who Do Rego claimed had tried to raise his own bonus without board approval and had pressed for forebearance with favoured borrowers. The Nigerian SEC provided the necessary official foil for Mr Tanoh and champion for Ms Do Rego and the intervention of the South African Public Investment Corporation injected an element of shareholder activism.

But behind this drama of personalities is another equally interesting and important story about the political economy of cross border banking in Africa. Since its founding in Togo in the 1980s, Ecobank is one of a small number of publically-owned African banks that have built genuine cross-border African models. Standard Bank of South Africa now operates in 33 markets. United Bank of Africawhich is based in Nigeria) operates in 20 markets and Bank of Africa from Mali is present in 10. Ecobank has grown from its heartland in West Africa, expanding its operations into branches or subsidiaries in 35 Sub-Saharan markets. It is regulated both by its own home regulator in the West African Monetary Union (WAMU) and by a patchwork of other regulators including the Nigerian SEC. Listed in Ghana, Nigeria and the Cote D'Ivoire, Ecobank is owned by a wide range of retail and institutional investors.

Out of West Africa

The race for African market share of these big franchises has helped drive a sustained expansion in both physical and mobile banking networks and customers, many of whom are being banked for the first time (Fig 1). They are also deepening the pool of lending to the African private sector by African banks which is a useful counterbalance to growing foreign lending into the continent. Funded largely by deposits, these banks have very low levels of leverage by international standards, and they are comparatively basic vanilla in banking terms which adds to their potential resilience. Both with investors and politicians, propositions like Ecobank have been integral to a bigger market story about African growth and market evolution.

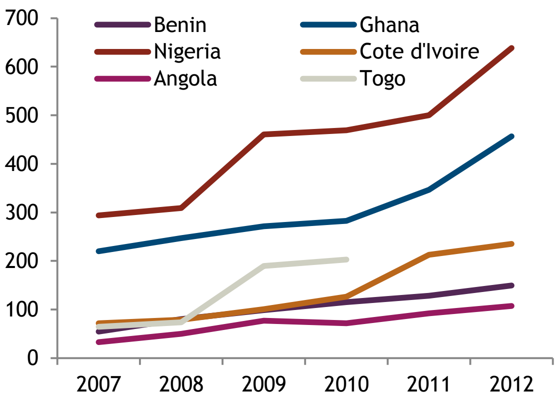

Fig 1: Depositors with commercial banks, selected Ecobank markets (per 1000 adults)
Source: World Bank, Togo data to 2010 only.

However, for African banking supervisors, Ecobank and its peers are an ambiguous proposition. The geographic spread that looks like a desirable diversification to Ecobank investors and management is for regulators a potential source of contagion risk. Arunma Oteh of the Nigerian SEC was one of the decisive figures in forcing management change at Ecobank and was motivated in large part by concern that the bank was importing operational risk into Nigeria from its West African hinterland. With just over 40% of Ecobank's assets and deposits in Nigeria, the NSEC will inevitably take the view that Nigerian prerogatives deserve particular weight with the bank.

Regulators and politicians in smaller African markets have their own reasons to eye Ecobank and similar banks with caution. Ecobank franchises in smaller markets like Togo or Benin are important lenders, often with substantial shares of the local market for credit; Ecobank probably accounts for around a quarter of all deposits and lending in both markets. As a share of Ecobank's balance sheet however, they are small (Fig 2).

We can be sure that in mobilising authorities in both Togo and his native Cote d'Ivoire in defence of his leadership of the bank Thierry Tanoh played on their anxieties that an Ecobank dominated by Nigerian regulators and South African investor interests would be less committed to these smaller franchises, especially if it was ever forced into retrenchment by a future crisis. The same anxieties will be stoked if South African Nedbank choses to convert its large debt position in Ecobank into an equity stake later this year - a shift in the ownership register that will be perceived by many as further diluting the bank's West African DNA.

The African regulatory gap

One of the big challenges for African regulators in the years ahead will be developing the frameworks to handle institutions like Ecobank without crimping the value created by a wider and deeper African banking market. The list of areas where regulatory frameworks need strengthening is dauntingly long; both updating African standards to international ones and harmonising regulatory standards across African banking markets has been slow. Most African jurisdictions still use a variant of the Basel I frameworks from 1988. Only South Africa has implemented Basel II.

Outside of South Africa there is also still only limited legal or practical scope for consolidated supervision of cross border banking groups. Disclosure rules on intra-group exposures – lending by one part of a banking group to cover the liquidity needs of another part – are weak. This is an area where Ecobank is thought to be active and is exactly the kind of area where supervisors will worry about contagion risk. The trading activities attached to these essentially retail banks are also likely to increasingly be subject to demands for greater transparency.

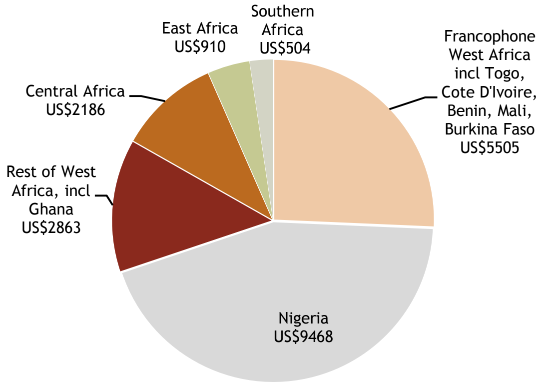

Fig 2: Ecobank assets incl loans by operational cluster(US$mn)
Source: Ecobank 9M results 2013

The temptation for supervisors like the Nigerian SEC will be to require clearer checks on contagion risk by imposing stronger forms of subsidiarisation or ring-fencing of capital, management and governance. This will especially be the case if reform-minded supervisors like Arunma Oteh begin to feel that the regulatory capacity gap between a state like Nigeria and its neighbours is getting wider.

Ecobank's smaller supervisors are likely to see the bank's substantial Nigerian exposure as a potential source of volatility. Deposit-funded banks like Ecobank may be better insulated in principle from problems with short term wholesale funding, but probably half of African depositors have had a bank account for less than five years and we have no real way of knowing how they would respond to the perception that their money was at risk. A run on deposits in Nigeria or one of Ecobank's larger markets could quickly put the bank's smaller franchises at risk. The temptation to ring-fence capital and operations at the national level will be obvious. This may be an important factor for pan-African ambitions in banking in the future.

The regulatory future is not pan-African

The question for Africa's cross-border banks, the businesses that depend on them and the investors increasingly piqued by their potential is how politicians and policymakers balance the benefits of cross-border banking and supervisory nerves. There is a trade-off coming down the line between authorities' tolerance for risk and the dynamism and freedom of manoeuvre of insurgent African banking institutions. The tension between the interests of big and small African markets will only make this more complicated.

This is obviously not a unique African problem. South East Asian regulators have struggled with regulatory harmonisation to unlock the benefits of regional scale in banking in ASEAN and have consistently stumbled on political resistance to market opening and policy parochialism. They will compromise in 2015 by creating not a harmonised and liberalised framework but a unique category of ASEAN cross-border bank that will be subject to joint supervision and its own rulebook under the ASEAN Banking Integration Framework (ABIF). This is a model that may appeal to African regulators also.

There are also parallels with the EU. European states were able to offer credible deposit guarantees that helped stall a run on

European banks in 2008, but collapsing credit bubbles in some EU markets were still transferred to others through the mechanism of the banking system. Many cross-border banks in the EU responded after 2008 exactly the way supervisors in smaller African states worry about with Ecobank: by retrenching out of smaller markets to shore up operations in larger or more core ones.

The EU's 'banking union' proposals are designed to push back against this risk of contagion and fragmentation by unifying the supervision of the EU's largest banks and cross-border banks in the European Central Bank under a newly-harmonised EU rulebook. But even in the EU, with its established institutional structures and ethos of regulatory harmonisation, the politics of this have been complex and difficult.

Although the UK uses the single EU rulebook for banks, London has opted out of ECB supervision and the UK's own banking reforms enacted in 2013 took the deliberate approach of ring-fencing the capital and governance of UK retail banks, not just from pan-European parents but from their wholesale operations. The UK experience suggests strongly that in the absence of politically palatable and credible cross border supervision and risk-sharing, the temptation of banking regulators to try and ring-fence risk at the national level will be strong. How African regulators see these problems will be very important for the future of Ecobank and its peers.

The additional problem for African regulators is also likely to be one of human capacity. Basel III is proving to be a complicated prospect for European and American regulators and will strain thinly-resourced smaller regulators in particular. Stronger regulatory frameworks for African cross-border banks on paper will still require large numbers of sophisticated and forceful supervisors to implement them. Investors are enthusiastic about cross-border potential in African banks but they also need to recognise the degree of systemic risk that is emerging with the growing regulatory gap.

Ecobank's own experience will be complicated by the political desire in many markets to hold the bank to its pan-African commitments. Ecobank may have been conceived as a privately-run bank, but it remains a highly political proposition. As noted above, Ecobank is trying to navigate a growing concern that a bank increasingly dominated by Nigerian regulatory and South African investor interests but integral to Africa's smaller credit markets could start to see its smaller franchises in detached commercial rather than quasi-political terms. Questions of probity and competence aside, the previous leadership team at Ecobank understood this anxiety well enough to mobilising sovereign stakeholders in an attempt to save their jobs.

The bigger fundamental point here is about the way in which African cross-border institutions can be developed in a way that keeps pace with underlying market dynamics. The desire and need to build scale in African businesses will inherently mean transcending small and fragmented national markets. Banking will be both an example and a facilitator of this ambition. The various African regional economic integration initiatives explicitly recognise the need to create frameworks for this but even in a grouping like WAMU – Ecobank's home regulator - which has actually pooled bank supervision in a monetary union, policy frameworks are a long way behind market reality. Ecobank's marketing material proclaims that the future is pan-African. The reality is likely to be a lot more complicated.

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