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Banking regulation and supervision in Africa: A conceptual framework

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This paper proposes a conceptual framework on the development of regulations and supervisory policies for regulating and supervising banks in Africa. These could contribute to the advancement of regulatory and supervisory frameworks within the banking sector in the continent. The framework is grounded on the homogeneous development, implementation, and regular cooperation among authorities in the continent (AU member states) on banking supervisory matters. The framework is derived following intensive review of both the theoretical and empirical literature on the impact of regulation and supervision on the profitability of banks in select African countries. Considering the idiosyncrasies of the nature of the environment in which banks' operate in Africa- weak economies, market size, poor socioeconomic conditions and "unstable" political conditions, it is important for the development of regulatory and supervisory frameworks that takes the uniqueness of banking operations conditions in Africa.

Key Words: *conceptual framework, bank regulations, bank supervision, banks, Africa*

1. Introduction

Cull and Mare (2020) in their contribution to the World Bank Global Financial Development Report corroborated that developing countries face a key challenge in trying to adapt international regulatory and supervisory frameworks that were designed for the banking sectors of advanced economies. This is against the background where a growing number of developing countries have espoused components of the Basel II and III international regulatory accords subsequent to the 2008 / 2009 global financial crisis, many of which choose to adopt "less" complicated aspects of the accords. This is the case in Africa, where South Africa seem to be the only country adopting the full suites of the Basel principles frameworks.

Africa as a continent has mixed economies with many of the countries in the continent operating under poor governance and economies. This could place a strain and challenge in the prioritisation of the development of financial regulations and supervision as there always tends to be competing needs. However, although, there are countries such as South Africa, which is the only country in the continent that fully implements the Basel III standards, the majority of the countries such as Egypt, Tanzania, Kenya, Senegal, Cameroon, Uganda, Nigeria and Ghana remain under lower standards (Ozil, 2019). These are probably the prudent choices given the supervisory capacity in the countries in Africa. In general, the objectives, aims and tools for banking regulation and supervision in developing countries will need to be always discussed and updated, since globalisation in financial services and rapid technological change make it increasingly challenging to provide effective oversight (Cull & Mare, 2020).

The World Bank Global Financial Development Report (2020) provides evidence on the reforms undertaken since the 2008 /2009 global financial crisis that shows that the policy interventions and regulatory changes with respect to banking have had important implications for market discipline and bank capitalisation. Capital requirements and regulatory capital holdings for banks have increased, though again the finding on holdings hinges on how assets are risk weighted. There are also indications that financial safety nets became more generous in many countries, and that supervisory capacity has struggled to keep pace with the extent and complexity of new banking regulations. In short, despite substantial progress on bank regulation in multiple areas, there is still cause for concern about future bank stability, especially among large multinational banks.

2. The regulatory and supervisory framework and model

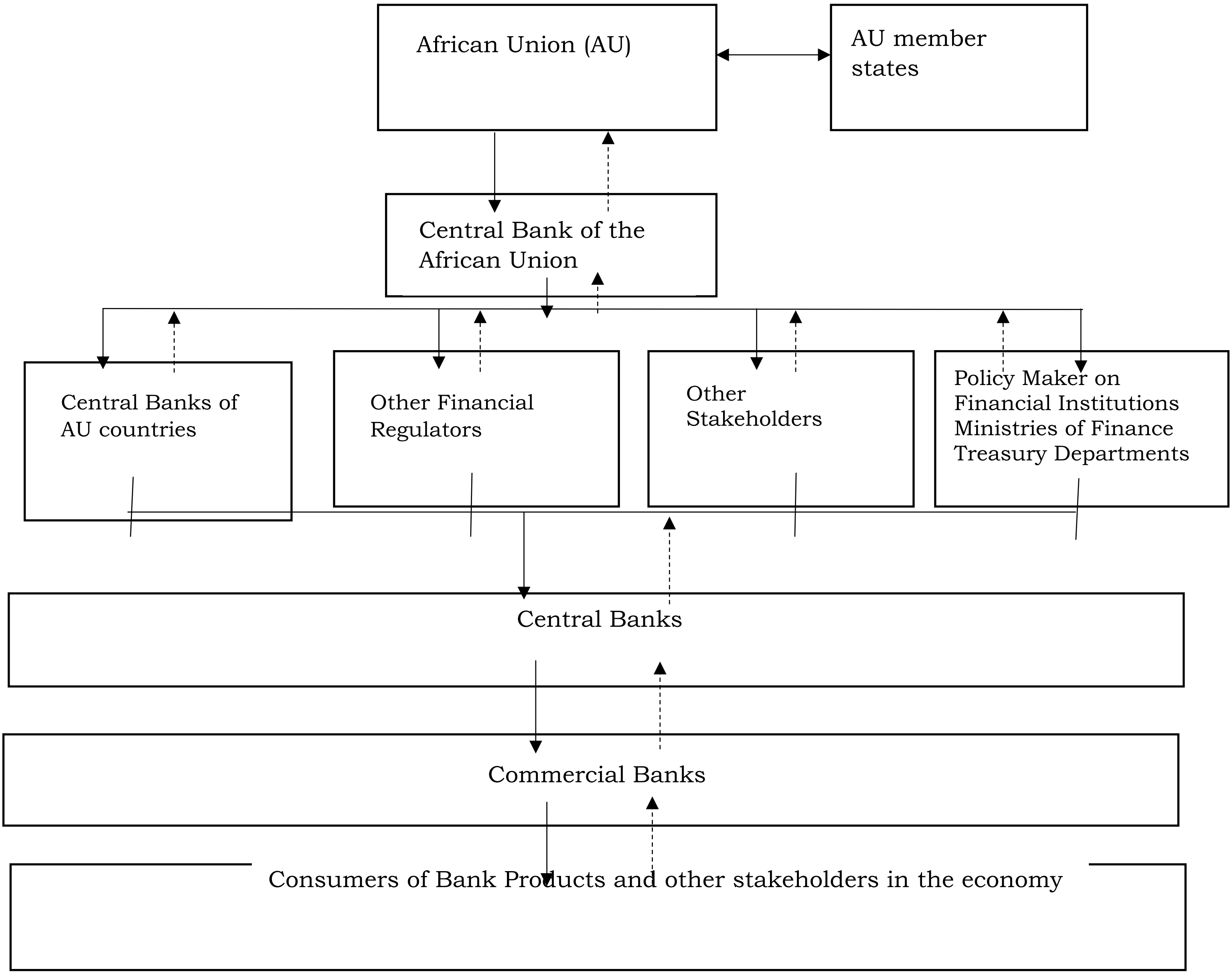
With the inception of the Africa Free Trade agreement, the following framework on regulating and supervising banks in the continent could contribute to the advancement of regulatory and supervisory frameworks in the continent. The framework is grounded on the homogeneous development, implementation and regular cooperation among Authorities in the continent on banking supervisory matters.

Developing banks' regulatory and supervisory frameworks is an arduous process. There are many stakeholders involved with divergent interests, making it almost impossible to reach consensus. The importance of the sector in the macro-economy seems to draw the various parties closer in this regard. Internationally, regulatory development tends to emanate from the discussions and agendas of the international regulatory and supervisory bodies such as the World Economic Forum, Group of 20 countries (G20), International Monetary Fund (IMF), the World Bank and indeed the United Nations. The agendas of these bodies are mainly informed by developments around various events in the world. Developments in politics, economy, natural resources, welfare, disasters including pandemics and scenarios forecasting future events dominate the discussions. These engagements aim to find solutions to issues consuming the world and attempts to refine current solutions. It is therefore not unfathomable that discussions pertaining to the financial sector in general and the banking sector in particular will form part of the discussions. Discussions during these engagements that require solutions in the financial sector tend to inform the development in regulation and supervision by the relevant international bodies. Internationally, the Bank of International Settlement (BIS) develops progressive banking regulations that guide its members to implement over a specific timeframe. These regulations tend to be broadly accepted by non- member countries as well, although it is not a requirement for them. These are developed and implemented under the various Basel Accords. The regulations and supervisory frameworks are mainly a requirement for members of the G20 countries and central banks that affiliate to the BIS.

Other developing countries tend to diverge from the Basel Accords. These divergences can be noticed largely in the way regulation in which regulatory capital base is regulated, capital adequacy in banks is measured and regulations on liquidity risk and how to deal with banking failures. In Africa, South Africa is the only country that participates and implements regulations as a full member of both the G20 and the BIS. This leaves the rest of the continent developing and implementing regulations in a heterogeneous manner, with unstructured regulatory and supervisory frameworks informed by their narrow governments' agendas and problems. It is therefore critical to develop and adopt a regulatory and supervisory framework that guides countries in Africa homogeneously (Masindi and Singh, 2021). The framework incorporates the activities of central banks and the responses by Commercial banks.

The following framework takes the continuous evolution in banking regulations that leads to pragmatic supervision to avoid crises in the banking system that is habitually triggered by excessive risk-taking. It should be mentioned upfront that, the framework is not a remedy for the failures in banks, as they can fail in the course of doing business.

Figure 1: Regulatory and Supervisory framework structure



Source: Researcher's illustration, 2022

In developing the regulatory and supervisory frameworks that take the need of the continent seriously, discussions at the African Union level that impact on the financial sector should be scrutinised by a central body with skills and experience to ensure that the required resolutions are expedited. This body must have powers to overhaul the current approaches and mechanisms that are adopted by member countries' central banks and the banking industry in the way regulations are developed and the implementation and supervision by commercial banks and regulators respectively.

Figure 1 provides the regulations development and implementation flow that is discussed below.

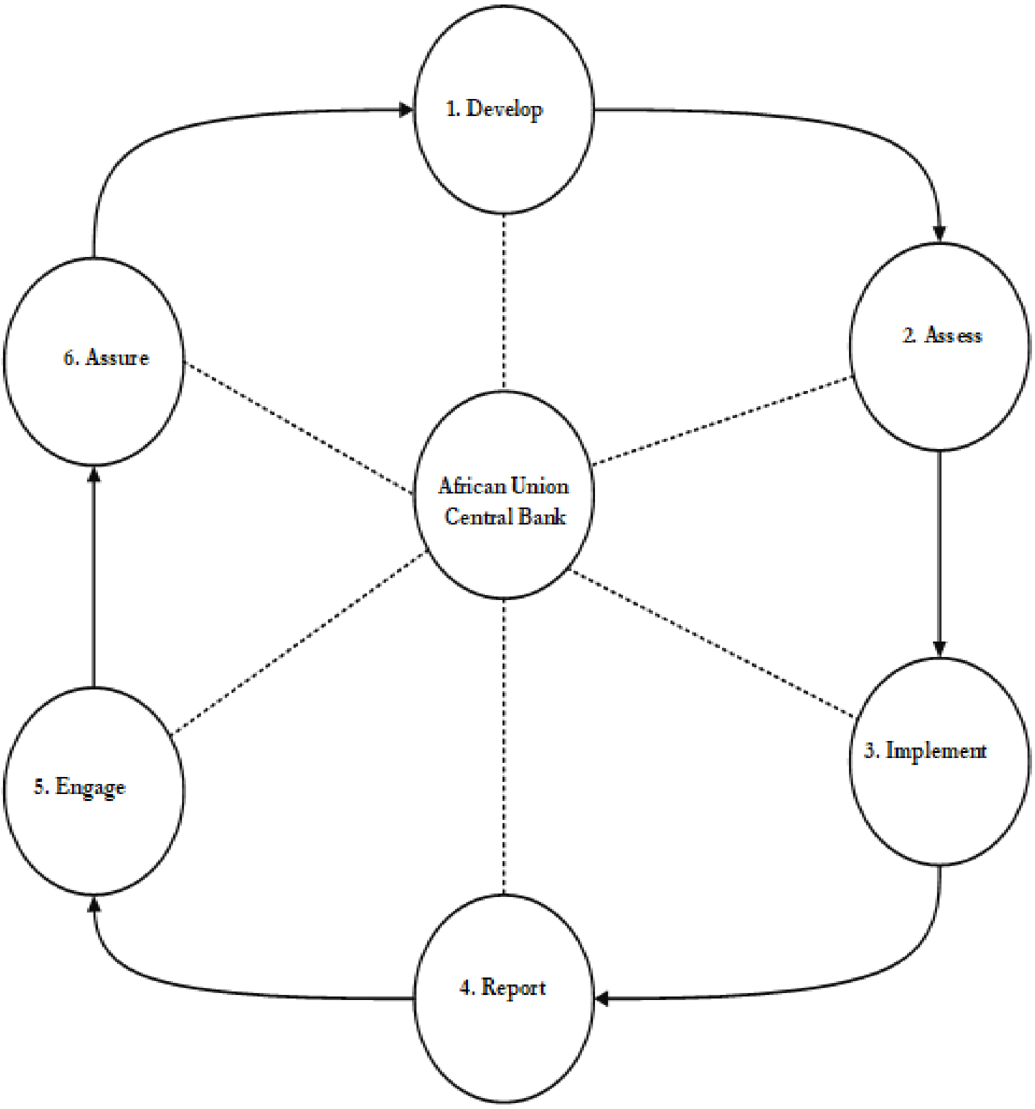
i. The discussions that take place at the African union member countries levels that are of financial services in nature, in particular the banking sector should be forwarded to a central structure that deals with the financial matters formed under the African Union. This structure that can be named the "African Union Central Bank", would be constituted by members of the member countries central banks, commercial banks, governments' ministries of finance and departments of treasury, other financial services regulators and policymakers and other stakeholders including academia. The "African Union Central Bank" should be empowered to initiate regulations and supervision guidelines that ensure the applications of similar regulatory measures to all the commercial banks in various jurisdictions in Africa. It should be resourced by skilled professionals to ensure adequacy and effectiveness in the delivery on their mandate. The chairmanship could be rotated among member countries and its mandate would incorporate considerations of the international regulatory and supervisory developments and how that should shape banking regulations and supervision in Africa.

ii. The 'African Union Central Bank" would set the regulatory and supervisory policies that would be used or implemented at the AU member states level through their central banks. This would act as a benchmark of what the African Union member countries would be required to implement in their jurisdictions with the assistance of the "African Union Central Bank". These will ensure conformity in areas such as the setting of capital adequacy levels and how capital is calculated, how to deal with the failures of banks at various jurisdictions in the continent, liquidity, solvency, risk management and conduct in the banking sector. Although these guidelines are developed at the central level, they incorporate international best practices and therefore their implementation should be in conjunction with the jurisdictional central banks and governments as they are closer to their respective environments. Central banks in different countries could therefore standardise the regulatory and supervisory policies of the African Union in line with the country requirements. However, this diversion should be subjected to the application and approval of the African Union central banks.

iii. Commercial banks implement the new or reviewed regulations in line with the requirements of their central banks and within the stipulated timelines. The timelines are aligned to the requirements of the African Union central banks as the overall authority in the continent. The homogeneous implementation of regulations in the continent will ensure the stability of the financial system, particularly the banking system.

iv. The formulation of the regulatory and supervisory frameworks in the continent should not be a linear process, as it should be grounded and influenced by the developments in technology, globalisation and other external factors influencing the prompt changes in banking regulations. It is therefore advised that the process should take the format articulated in figure 2 that follows:

Figure 2: Regulatory and supervisory continuum



Source: Researcher's illustration, 2022

Figure 2 above can be articulated as follows:

1. The "African Union Central Bank" proposes and facilitates the development of new banking regulations or / and supervision guidelines and amends existing ones when required. This should be an all-inclusive process that ensures the influence of international developments on the development of regulations and supervisory framework that will be implemented and monitored homogeneously throughout the continent,

2. An assessment or due diligence on the impact of the proposed regulations on the activities of the main stakeholders should be conducted. This could include a risk – return analysis of the intended regulations or supervisory framework. The stakeholders are various central banks, commercial banks operating in various jurisdictions and depositors. Governments through their central banks regulate and supervise banks to protect their citizens (depositors) and to create a stable environment in which banks can operate profitably, thereby stimulating growth in respective economies. During the assessment phase all stakeholders should get an opportunity to submit inputs that should shape the final product,

3. The new or updated bank regulation or supervisory framework is implemented by the central banks taking into consideration conditions in various jurisdictions. The "African Union Central Bank" monitors the implementation process and approves fully or partially depending on the requirements brief, within the stipulated timeline,

4. Central banks are required to report on progress and challenges to the "African Union Central Bank" and commercial banks report to their respective central banks. This ensures a seamless and unambiguous sharing of data across the continent,

5. Commercial banks engage with the central banks who are their primary regulators as part of the central banks' supervisory regimes. Central banks engage the "African Union Central Bank" for directions and clarity on aspects of the requirements of the regulations from the central body "African Union Central Bank",

6. Entails continuous assurance by all the Stakeholders to ensure that regulations and supervision thereof are embedded effectively in line with the intended objectives.

Supervision of commercial banks by their local central banks mainly starts at point 3 and is continuous, depending on the outcome of the risk assessment of the central banks to the respective commercial banks (the banking industry). The suggested framework would assist in levelling the playing field in the development and implementation of banking regulations and a supervisory framework in Africa.

Conclusion

Developing economies are confronted by some challenges when they attempt to adapt International banking regulatory and supervisory frameworks that are designed for the developed economies. Some of the developing economies become selective in what they adopt, avoiding some aspects that they deem to be more complicated in line with their supervisory capacity.

This study provides the conceptual framework to assist regulators, governments and Policymakers in Africa in the formulation of regulatory and supervisory frameworks that aligns to their developmental goals.

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