FINANCIAL SERVICES AS A CATALYST OF ECONOMIC GROWTH

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Background (I)

- The Financial Sector comprises
  - Suppliers - financial institutions such as banks, insurance investment firms;
  - Financial products, such as loans, deposits, insurance;
  - Financial services such as brokerage, ratings;

Background (II)

- The FS is a catalyst for achieving high–growth and human development depending on its depth and efficiency in respect of each of the three categories – suppliers, products and services.
- As mobilisers of funds; providers of affordable credit for household consumption, medium and large scale investment and government; improving productivity; providers of risk management services - facilitating domestic and international transactions, promoting firm entry and competition, attracting PFI.

Financial System and Economic Growth

- **The finance - growth nexus also underpinned by**
  - **Importance of universal and affordable access to financial services**
  - **Significance and elements of effective supervision, prudential regulatory and institutional framework**
  - **Significant integration into global financial networks**
  - **Development of relevant financial markets and mechanisms to: -**

- Reduce intermediation margins and costs
- Mobilize longer term savings to finance riskier and long term investment
- Raise capital productivity - value added productivity – agro based, corporate operations

Efficient and Deep Financial System

- Mobilize savings and changes the term and structure of the savings
- Channel savings into productive investment
- Improves the efficiency and productivity of investment
- Provides the integration of the domestic economy into the global financial system
- Enhances growth implementation of macro-economic policies

- **Important conclusions from empirical evidence include:**

- Countries with better developed, liberalised, competitive, complementary and well supervised and regulated financial systems tend to create better opportunities for generating faster growth
- The level of banking development, stock market liquidity and intermediation each exerts a positive influence on economic growth

FS Challenges for Growth Financing: Institutions

- Rudimentary institutions, products and services; dominance of commercial banks; modest non bank service providers
- weak microfinance associated with low risk absorption
- Poor infrastructures associated with high dependence of public investment
- High cost of intermediation – high overhead costs associated with high cost of doing business
- Lack of acceptable/bankable projects – collateralization issues
- Restrictive regulatory requirements – lending ceilings
- Information and contract enforcement constraints

FS Challenges for Growth financing: Customers

- Voluntary self exclusion
- Cash and carry approach
- Access to banking services – poor, onerous

FINANCIAL SECTOR IMPERFECTIONS

- A negative relationship between financial inequality and growth > financial market imperfections (information asymmetries, transaction costs, contract enforcement > binding more on poor > lack collateral, credit history, connections
- Credit is channeled to those with best connections, not to entrepreneurs with best opportunities (high-return projects)

MAKING FINANCIAL SECTOR RELEVANT FOR GROWTH AND POVERTY REDUCTION

- Financial system is pro-poor if financial services targeted on underserved segments of population : low-income individuals, microenterprises, small enterprises > unbanked, informal sources of financial services
- Institutional shift: commercial banks provide services that take the character of microfinance
- What then restrains banks from taking on microfinance?
  - Inability to innovate
  - Aptitude for handling risks inherent in developing new business lines
  - Weak potential for partnerships
  - Public policy toward financial access
- Private sector credit (%GDP) issued by financial intermediaries > std measure of financial development: ↑ levels of private credit > ↑ (faster) growth

Financial Sector in Sierra Leone

- The banking system dominates the financial sector in Sierra Leone, comprises
  - the Bank of Sierra Leone (BSL)
  - 10 commercial banks, with 7 affiliated international monetary transfer agencies
  - 4 community banks

- Other banks include the post office savings bank and the National Development bank
- non bank financial institutions include, Finance and Trust corporation, two (2) discount houses, three (3) non deposit taking finance companies, eight (8) insurance companies, sixty (68) foreign exchange bureaux, a National Social Security and Insurance Trust, and a relatively small number of micro finance institutions

- An interim stock exchange was launched in 2007, while several applications for the establishment of new commercial and investment banks are under consideration.
- There are also two poorly performing Housing finance companies, although a new housing finance company is being developed by the state pension scheme (NASSIT)
- There is a large but unmeasured unofficial financial sector whose activities notwithstanding contribute to the large informal economy.

Financial Sector reform in Sierra Leone

- Sierra Leone began to implement financial sector reforms in the 80s, as part of a broader market-oriented reforms in the context of IMF supported macroeconomic adjustment programmes
- These reforms were geared towards building a sound, well-functioning financial system that will both support sustainable economic growth, development and poverty reduction, as well as create a solid foundation from which the domestic economy and financial system can better integrate with the global economy
- They resulted in significant liberalisation of the FS, including key prices, capital flows and various other restrictions.

- The Banking and Bank of Sierra Leone Acts were completely revised and enacted in 2000
- New Banking regulations were issued to commercial banks in 2001 and amended in 2003 (relating to liquidity, capital adequacy, minimum paid-up capital, etc).
- The regulatory and supervisory role of Bank of Sierra Leone was extended to cover other financial institutions, which culminated in the enactment of the Other Financial Services Act 2001.

- In 2005, the Anti-Money Laundering Act was enacted to suppress money laundering and to provide for other related matters.

- In a bid to enhance medium to long term finance and facilitate the development of the private sector, an interim stock exchange was officially opened in July 2007 though it was yet to commence operations. It establishment was facilitated by the amendment of the Other Financial Services Act.

- Other Acts like Revised Companies Act, the Bankruptcy Bill, the Securities Bill, the Collective Investment Schemes Bill and the National Payments System Bill are in a draft form and will be enacted soon
- FSAP and several other financial sector related exercises were conducted by IMF/WB beginning 2005 and provide a basis for comprehensive reforms

Challenges in financial Sector Development

- Limited competition to lower costs and widen access to financial services

- Limited access to enterprise financing

- Insufficient financing of the rural economy

High costs of financing/Intermediation

- Limited financial Education

- Weak and narrow range of legislative initiatives relating to financial sector

- Narrow scope for Implementing effective monetary policy
- -Weak link between FIs

Conclusion-Strengthening the financial sector for Economic Growth

- Strengthen rural access to financial services and develop long-term financing options

Improve financial services technology and infrastructure

- Promote efficiency through real time funds transfers
- Improve monetary policy management and bank supervision

- Increase domestic savings mobilization to support investment
  - Promote long-term deposits and financing
  - Develop capital market
- Strengthen corporate governance in financial institutions

Strengthen institutional arrangements that support expansion of access to financial services

- Land and company registries
- Commercial courts

Continue to improve the conduct of monetary policy

- Strengthen liquidity management and forecasting
- Deepen financial markets
- Develop comprehensive public debt management strategies

CONCLUSION: TOWARD AN INTEGRATED FINANCIAL SECTOR

- Sierra Leone's financial sector has become much more diversified, with foreign banks and non bank institutions playing an increasingly important role.
- Build and operate an integrated financial sector , in which Financial Institutions compete and complement each other – the BIG Challenge

THANK YOU