THE BANKING COUNCIL
South Africa

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The Banking Industry Submission
to
The Portfolio Committee on Trade and Industry

BANK TRANSACTION CHARGES
and
SMALL LOAN ORGANISATIONS

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INTRODUCTION

An unquestioned fact is that over the last few years bank charges have gone up significantly while many service standards have declined. It is therefore understandable and indeed appropriate that the Portfolio Committee on Trade and Industry, which has a direct interest in the provision of banking services, has arranged for these hearings.

Every person and every business that is commercially active has no alternative but to use the services of a bank. This means that banks are the only institutions that have a relationship with everyone who receives, spends, saves or borrows money. It is therefore not surprising that large numbers of people are concerned about the quality of service, which they get from banks and about the charges, which they have to pay.

It is ironic that, at the same time, the South African banking industry is highly regarded internationally for the sound way it is managed and the role it plays in a world characterised by financial uncertainty. The industry has therefore earned the following tributes:

- Standard and Poor, in their most recent rating of South Africa noted that:

  "..During a time when many emerging markets throughout the world have suffered the collapse of their financial services industry due to imprudent credit decision making or funding mismatches, it is instructive to consider the resilience of South Africa's banking sector."

- The World Economic Forum, in its most recent World Competitiveness Survey, noted that:

  > Although South Africa achieved a ranking of only 42 out of 53 participating nations, the banking sector's financial condition was rated 13th.

- The International Monetary Fund, in October 1998, reported that:

  > The South African banks are "well-capitalised, well-run and organised and in general have sophisticated risk-management and corporate-governance systems in place."

This was compared by the Fund to the unfavourable situation in East Asia, which triggered global turbulence.

The question is naturally raised whether there is not a contradiction between the South African and the international view of our banks. The Banking Council would argue that the answer is "No". The reason for this response is because domestic concerns about charges are uncomfortably related to international perceptions of the strength of our banking industry. Hence, it is natural that they should come into focus at the same time.

It is the deliberate strategies the domestic banking industry has adopted to maintain international standards and meet international and new local competition that are directly responsible for increased bank charges in certain segments of the market. These challenges have also led to a simultaneous revision of services which has resulted in perceptions of a decline in the quality of some services.

In a number of respects the current situation for the South African banks is similar to that experienced by all other industries that have been exposed to international competition for the first time and therefore must restructure. The motor car and textile industries are good examples of this need to move in line with Government's commitment to free competition. As the barriers have been taken down, the banks have been forced to compete on a level playing field with foreign banks and new local entrants; all of them using the best that modern technology have to offer.

Criticism, as we expect to hear this week, is good for any industry. Hopefully it will give rise to an opportunity for frank discussion and debate of the problems raised. It should also trigger introspection and self-analysis, and the banking industry has no doubt that changes will arise from this process. But, at the same time the industry is concerned that the criticism be handled in such a way as to be constructive. Moreover, it should not erode the confidence in an industry, which is so reliant on confidence for its very existence.

While this submission is primarily focused on addressing the issue of bank charges, it also intends identifying the necessary conditions for the continued existence of the large commercial banks operating within the context of a free market. This existence depends on the willingness of investors to risk their capital in a bank.

HAVE BANK CHARGES INCREASED OVER THE PREVIOUS FOUR YEARS?

The answer to this question is simply, “yes”. In a nutshell, charges have increased for the following reasons:

- While costs have been rising steadily over a number of years, charges were allowed to fall behind those costs.
- In particular, from 1993 onwards there was a sharp increase in certain specific costs, for example, in relation to moving and storing cash; and the cost of computer equipment as it was effected by the depreciation in the value of the Rand.
- The banks had been using the profits on savers' accounts to subsidise the transactors with low balances. And they had been using the profits made in the high-value segments of their market to subsidise the low-value segments.
- Newly established South African and foreign banks began competing for the high-value business of the four major banks. These banks were left with no alternative but to match the competition and stop the cross-subsidisation. Transactors would in future have to pay the full cost of the banking services they used.

The unfortunate result is that, initially at least, competition has intensified in the high-value markets, and the high-value clients are benefiting handsomely. For example, although mortgage rates have been very high as a consequence of the economic pressures to which the country is subject, they are now coming down for the wealthy, but less so for the poor. Investment opportunities are improving by the day, and the opportunity to use electronic banking systems has had a marked impact on the quality of life and of service for those who have access to those devices.

In contrast, in the low-value markets, there is not this same level of competition. That is because, on the face of it, it is unlikely that a bank can earn an adequate return on the shareholders' investment (or "Return on Equity, or ROE" as it is called) in the low-value markets. This being the case there have been no new entrants on any significant scale into the lower-end of the market. Nor has <u>a single foreign bank</u> shown any interest in the low-value market, despite a number of opportunities to enter it - even to the point of having the opportunity of taking over existing branch networks.

HOW HAVE BANK CHARGES INCREASED?

Transaction and other charges have been increasing in amount, as demonstrated in Table 1 below. The absolute increases have then been adjusted for the increase in the volume of transactions for the year in question (because increases in volume also have the effect of increasing the total transaction fees returned to the Registrar) and for inflation. This gives a notional % increase in real terms. Apart from 1994, the real increase is minimal, if not negative.

Table 1: Increases in bank charges, 1993 - 1998

	1993	*1994*	*1995*	*1996*	*1997*	*1998*
Transaction Fees Rm	**3.629**	**4.912**	**5.708**	**7.086**	**8.714**	**10.1**
Absolute Growth - %		35.4%	16.2%	24.1%	23%	16%
Volume Increase - %		11.2%	11.6%	11.4%	13.5%	11.5%
Inflation Increase - %		8.9%	8.7%	7.4%	8.6%	6.9%
Real Increase - %		**15.3%**	**-4.1%**	**5.3%**	**0.9%**	**-2.4%**

(Source: DI200's and the 4 Major Banks)

When looking at these numbers, it should also be remembered that the transaction fees returned to the Registrar include corporate fees and commissions and international fees. Across the industry, approximately 20% of the gross transaction fees do not relate to commercial banking. However, over the last five years they have remained a relatively constant percentage of the total, and so don't affect the percentage increases reflected in the table.

Transaction charges constitute very different proportions of the total income of the major banks, as set out in Table 2:

Table 2: Proportion of transaction and other charges to total income: South Africa's major banks

Banks	***%***
ABSA	34.13
FNB	48.37
SBSA	45.47
Nedcor Bank	42.29

(Source : Banking Survey Africa, 1998, KPMG)

These variations reflect the different strategies adopted by the major banks in developing a policy around bank charges. It should be noted that the ratio is determined as much by the level of interest income as it is by the level of transaction fee income. The major banks have historically had very different approaches to charging, and the increases seen, have not, by any manner of means, been attributable to banks doing the same things at the same time.

IS THIS INCREASE IN BANK CHARGES UNIFORM ACROSS THE BANKS?

In the course of preparing this submission, the Banking Council attempted to prepare a meaningful comparative analysis of the charges of the major banks. Our research revealed that there are hundreds of different products and services and a huge array of options and packages, very few of which can be directly compared with a product, service or package offered by any other bank. We therefore concluded that providing such an analysis would be totally impossible because of this enormous number of variations. What this means is that for the careful consumer there are considerable opportunities to find and exploit major differences in the charging policies and practices of the banks.

Moreover, these differences mean that it is inconceivable that there could have been collusion amongst the banks to produce such a vast and confused array of banking options. Examples of the pricing manuals of the major banks are available for the Committee to examine. We sincerely believe that this information will demonstrate the complexity in the pricing of services for a major bank.

WHAT CAUSED CHANGES IN THE BANK'S CHARGING PRACTICES FROM 1994 ONWARDS?

There are a number of reasons for the significant change in charging practice by the banks, from 1994 onwards, namely:

- The gap between the costs of providing services and the charges that the banks levied for those services had become intolerable. In particular, due to the considerable increase in the cost of moving and storing cash, and the high cost of purchasing computer equipment, which was affected by the depreciation in the value of the Rand.
- Foreign and niche players entered the high-value markets and eroded the profitability of those markets. This was the result of South Africa becoming part of the global banking market which forced banks to measure up to international standards of ROE. The banks could no longer afford to have one segment of their business dragging down the overall ROE. The result was that the major banks had to eliminate cross-subsidisation from one market segment to another.
- During the next couple of years all the banks employed international consultants and embarked on major costing and cost-saving exercises. They did this to determine more accurately what the different services in the various market segments were actually costing them, and thereafter reduced costs wherever they could. Independently they each began to adjust their charges so as to move closer to recovering the full cost of providing services in the different market segments.

The banks were also trying to introduce electronic services as a cheaper, safer and more convenient way to bank. However, the provision of cash had been so hopelessly under-priced that they found they were actually charging less for cash than the cost of providing electronic services. The banks therefore made practically no progress in persuading clients to migrate from cash to electronics unless they began charging a realistic price for cash.

In sum, it became very clear that the banks had been cross subsidising from savers to transactors by undercharging for transaction services and under-compensating the savers for their self-discipline. It became evident that they could no longer prejudice the savers in this way. Savers had to get more value for their money, and savers are now benefiting significantly with the new approaches to pricing over the last three years. It is the transactors, <u>not the savers</u> who are unhappy, because they are no longer being cross-subsidised by the savers.

It is quite clear from the Table 2 that ABSA historically had a low ratio of transaction charges to total income. Significantly it also handles the largest number of transactions and has the highest cost ratio of the four major banks. So it was to be expected that as part of the process of integrating the various subsidiary banks into ABSA Bank, and in getting the cost ratio of the group into line with international best practice, significant changes would be made to charging policy during 1998.

Again, this reinforces the point a bank's strategies differ in purpose, content and how they are packaged. There is simply no universal logic.

IS IT POSSIBLE TO PROVIDE SPECIFIC PRICES OR COSTS FOR FREQUENT SERVICES?

The Banking Council employed an international consultant to collect the price lists of all the most frequent transactions from the major banks, and to establish the main trends that have emerged in the industry in relation to pricing over the last few years. We also asked them to establish the average price of the banks for each of the most frequent transactions.

Those trends are as follows:

- Pricing changes over the last few years have been much more firmly based on costing analyses done by the individual banks than ever before. On the basis of that cost analysis the banks have moved in the direction of ensuring that if the client is a transactor, and not a saver, the bank will recover the full cost of providing the service.
- All the major banks have adopted a policy of only opening transactor accounts where the client is in regular employment and receives a salary from an employer.
- Because the cost of moving and storing cash escalated so sharply, and because it is largely for the benefit of the transactors that this increased cost is incurred, the charges for ATM withdrawals went up significantly. Noteworthy is the fact that transactors maintain minimal balances on their accounts, and so they make no contribution to the bank's costs by way of interest margin. All of the major banks have policies that by maintaining a certain balance, ATM withdrawal charges can be minimised or even avoided.

- Banks have also started to charge for cash deposited. The charge is related to the cost of counting, storing and then moving the money back to the Reserve Bank.
- From the costing analyses, it is clear that the cost of a teller withdrawal is significantly higher than an ATM withdrawal. Yet all of the banks had historically been charging less for teller withdrawals than for an ATM withdrawal. No progress would have been made in getting the transactors to use the cheaper and more convenient services of an ATM if they were being charged less for a teller transaction. Therefore all of the banks increased the costs of teller withdrawals for transactors quite significantly, and in virtually all cases to a level higher than the charges for an ATM transaction.
- Some banks have also introduced a monthly administration charge to cover the cost of administering the account, whether it is a savings account or a chequing account. This is largely due to the fact that as long as the account is open, the banks have to keep it fully accessible – i.e. open 24 hours a day, 365 days a year. Whether a customer uses the account or not, there is ongoing maintenance and expense on the account. This can include holding liquid assets and cash reserves in respect of it; the monitoring of the account to ensure that no fraud is perpetrated - dormant accounts are notoriously vulnerable to fraud; and carrying out returns to the SARS.
- Charges for chequing have increased by and large in accord with inflation.

The Banking Council felt that it would also be helpful if the Portfolio Committee had some idea of the average prices and the costs involved in providing some of the more frequent services. This has never been done before, because it would be collusive if the banks were to share costing information in any way with each other. We therefore requested the international consultant to collect, on a strictly confidential basis, the data from the major banks, and then to average it across the industry. (The consultant has given an undertaking that it will never divulge the specific bank information and that it will destroy the separate files.)

These resultant average costs are referred to as the "Banking Council Estimated Costs" of the different banking services. It will be obvious to the Committee members that the banks can diverge around the average costs, and the basis of actually allocating costs to different activities is subjective, and varies from bank to bank. Nevertheless, the consultant is satisfied that the averages constitute a reasonable indicator of the sort of costs involved and of the prices charged, although they cannot be regarded as the actual costs or prices of any particular bank.

Table 3: Costs and prices of South African major banks

Rand	Range of average costs*		Average Revenues**
	From	To	
Opening Costs			
Cheque account without O/D	135.00	155.00	None
Traditional Savings Account	40.00	50.00	None
Mortgage loan	710.00	730.00	In terms of Usury Act
Monthly Maintenance Cost			
Cheque Account	24.00	26.00	None ***
Savings Account	4.20	4.20	None ***
Mortgage Loan	21.00	23.00	5
Teller Transactions			
Cash deposits	4.50	4.80	2.27
Cash withdrawal	5.40	5.60	5.06
ATM Transactions			
Cash Deposits	9.40	9.70	1.74
Cash withdrawal			
On own bank	1.60	1.90	2.64
On other bank	1.80	2.10	6.87
Other Transactions			
Processing a cheque	3.60	4.00	4.25
Processing a credit card transaction	2.10	2.30	None
Processing an EFT	1.00	1.30	2.12

Source : The Banking Council

* Where applicable, costs are based on transactions of R250; transaction cost figures do not include any costs related to fraud, insurance, credit risk, Y2K systems or lost interest on cash balances

** All revenues are based on transactions to the value of R250.

*** An administration or service fee of up to R16 is charged on accounts on which the aggregate of the other fees is below the administration or service fee.

HOW DO SOUTH AFRICAN BANK CHARGES COMPARE WITH THOSE IN OTHER COUNTRIES?

The Banking Council asked the international consultant to compare the revenue a bank would earn in operating a chequing account in South Africa with the cost of doing so in the UK, Australia and the USA. In all other countries, the bank takes advantage of the "float" – and the cost of the “float” is effectively borne by the recipient of the cheque and not by the drawer. In South Africa the cheque charge is borne by the drawer of the cheque. So the exercise cannot be done on the basis of the cost to the client. We did not include other countries in Europe, because their systems are very different from ours.

Table 4: Bank revenue per annum* : International comparison.

Rand	**UK**	**USA ***	**Australia**	**RSA**
Monthly Service Fee	-	223.20	-	-
Cheque Fee (50 pa)	-	-	204.42	212.25
**Float **	23.89	11.95	29.87	-
EFT Fee (50 pa)	77.48	99.20	102.21	105.88
Own ATM withdrawal (40 pa)	-	248.00	81.77	105.50
Other ATM withdrawal (5 pa)	77.48	31.00	25.55	34.36
Teller withdrawal (5 pa)	-	-	45.99	25.30
Own ATM deposit (10 pa)	-	62.00	20.44	17.43
Branch deposit (5 pa)	-	-	-	11.33
TOTAL	**178.95**	**675.35**	**510.24**	**512.04**
TOTAL (Excl. Cheques)	**154.95**	**663.40**	**275.96**	**299.79**

Source : The Banking Council

* Based on the transactions of an average customer, assuming that the typical account balance is above minimum threshold and that no special "all inclusive" packages apply; where relevant, revenues are based on transactions of R500.
** Duration of float period is 4 days in the UK, 2 days in the US and 5 days in Australia at a South African repo rate of 17%.

*** Not all US banks charge these fees: Other ATM withdrawal 91%, Monthly service fee 83%; Own ATM withdrawal and deposit 38%; revenues based on transactions of customer subject to all fees.

It is obvious from Table A4 that the costs in South Africa are at much the same level as in Australia, and lower than in the USA. They are, however, nearly three times as expensive as in the UK. The costs, exclusive of cheque charges, reveal that:

- High costs in South Africa are substantially attributable to inadequate volumes to justify the infrastructure involved and the high level of cheque fraud that pushes the costs up substantially. By way of example, in 1998:
    - Banks lost R151 million on cheque fraud alone;
    - 3,200,000 cheques were returned to drawer; and
    - 173,000 cheques were lost, a high percentage of them stolen.
- In the UK, the costs of running a chequing account are clearly very low, provided that the client complies with all the rules. Penalties for not complying are very harsh – e.g. if a cheque is written for an amount for which there is no facility, the standard charge is 25 pounds (R250).

WHAT ARE THE IMPLICATIONS OF LOW PROFITABILITY IN THE COMMERCIAL BANKING SECTOR?

In Appendix 1 we have set out an analysis of the profitability of commercial banking in South Africa. The conclusion is that, if the full cost of capital utilised is taken into account, the ROE on this portion of the four major banks' businesses is inadequate, and constitutes a real drag on the rest of the bank. In fact, according to the KPMG calculation, in 1997 the four banks actually lost R181 million in the Commercial Banking market, if the cost of capital is taken into account.

The revenues from providing commercial banking services come from the net interest income and transaction charges. But net interest income is substantially determined in the market place, and if anything that margin is going to be further squeezed by the entry of new players like SA Home Loans. At the same time transaction charges are bumping into increasing public resistance to further hikes.

A commercial bank’s expenses are made up out of the operational expenses of running the branch network and systems, bad debts and the cost of the capital which is employed in doing that business.

Operating costs are therefore determined by forces largely beyond the control of the banks and have a lot to do with the historic development of the banking industry and environment in which they currently conduct this part of their business.

Bad debts are at a higher level than in developed countries, although not as high as in some other comparable countries. But the indications are that there has been a serious deterioration in the level of debt default and of debt write-off in the recent past. So, far from anticipating a reduction in bad debts and losses, it is likely that that figure will increase and negatively impact on the already poor ROE in the sector.

There is no easy solution to the banks' dilemma in relation to their commercial banking activities. It is not as easy as just pushing up their prices or cutting their costs. They really only have two real options:

- Get out of the market - which none of the major banks has yet done; <u>or</u>
- Develop focused strategies, which improve the profitability of their business in this segment. Some banks have already made considerable progress in doing this, and others will soon be seen to be doing so. As an indication of the harsh and unavoidable reality of these alternative strategies one of the major banks has indicated that it intends to close 400 branches in 1999. Another, as part of its process of focusing more tightly, closed 800,000 transactor accounts and 100 branches in 1998.

IS THERE A WAY FORWARD?

This is one of the most confusing markets to assess. The different banks have adopted very different strategies and policies in relation to the segments that they serve. There is a vast number of packages and options, and comparison is impossible. One of the things that is reasonably obvious, however, is that the banks are not deriving sufficient economies of scale.

It is also reasonably clear that for the banks that do choose to develop a focused strategy around the low-income market, it is almost certain that such a strategy will include:

- A heavy emphasis on the use of technology. Tellers are just not cost efficient in handling large volumes of low value transactions.
- Transactors having to pay the full cost of the services that he or she uses – cross-subsidisation has ceased to be a viable alternative to propping up unprofitable markets.

- Banks providing more value for money. It is not a viable strategy to simply charge more for the same old service or to see the retail market as a single market in relation to which the bank is either "in" or "out". For example, one of the banks has focused specifically onto providing transaction services for the low-income employed market. It has opened 2.5 million new accounts over the last 3 years. At the same time it has given free life cover and a variety of other benefits to all the account holders - but at a higher charge rate than was the case on its old-style savings accounts. It is satisfied that in that particular market segment it is making a satisfactory profit.
- The exclusion of the unemployed from conventional baking services. It is notable that in the USA, the banks don't even provide banking services for the employed at the bottom end of the market, and there is no such thing as a savings account as we know it. Large numbers of employed people (who cannot afford a chequing account) receive their wages in the form of a cheque, which they have to cash at cheque encashers. The cheque encashers charge between 6 and 10 percent of the value of the cheque with a minimum of US$10.

ARE THE CONSUMERS BEING FAIRLY TREATED?

If we look at:

- the costs of providing banking services;
- the prices that the consumers are being charged for those services;
- the comparisons with the price of those services in developed countries; and
- the returns of 20 percent odd that the shareholders are earning on their capital tied up in the provision of those services – accepting that they could be earning 32 percent ROE in companies like Pick n Pay and Shoprite with a similar risk profile

it is, in the view of the Banking Council, clear that consumers are being fairly treated, given the existing structure of the industry. If they were to get a better deal within the existing structure, it would be at the expense of the shareholders, and the strength of the industry itself would be severely eroded.

But that does not mean that the public shouldn't have better disclosure of what the different options are, how their contracts are being varied, the benefit of a sound code of conduct as to how banks should conduct their business, and quick and cheap redress when they are unfairly treated. It is also clear that the industry has a heavy responsibility in relation to the education of consumers in relation to banking.

But this responsibility cannot be left solely to the banks. An understanding of the basics of commerce and of the laws that underpin commerce in the whole of the developed world, must be the primary responsibility of the education authorities.

Appendix B sets out some common misunderstandings about banking and banks. It also contains a synopsis of the Banking Council's position in relation to the development of the Banking Code of Conduct and an Independent Ombudsman.

Nor does it mean to say that the structure of the industry should remain static. There is good reason to believe that the provision of banking services would benefit by more, and not less, participants. It is also clear, that, given the appropriate dispensation and support, there are many new "institutions" which can and should play a significant and increasingly competitive role in the provision of those services.

NEW ENTRANTS SHOULD BE ENCOURAGED INTO THE MARKET

New entrants, using modern technology and methods, with low overheads and who can maintain relationships with the communities they are attempting to serve, should be encouraged and assisted. The real answer therefore is not to make this market less attractive, but more so, and to remove the barriers to entry. Some of these new entrants could include:

A New Class of Deposit-takers

The needs of this market should be met by a new class of deposit-taker, with much lower overheads and which is much closer to the people which it intends to serve. For some time into the future it is likely that the formal banks will transmit the cash to the points that it is needed, using the distribution network that has been built up for that purpose. But the recording of small amounts of individual savings for the saver requiring a 24 hour a day, on-call facility does not need or warrant a nation-wide and very expensive computer and branch network.

At the deposit taking level, the current dispensation is:

- With less than R10 million of deposits there is an exemption, provided the institution is of the nature of a club, and is a member of a regulatory type of body;
- A mutual bank with a minimum capital requirement of R10 million, or 8 percent of its assets, whichever is higher; or
- A bank with a minimum capital requirement of R50 million, or 10 percent of its assets, whichever is higher.

These are not friendly or helpful dispensations. The Board of Directors of the Banking Council has therefore resolved to commit the Banking Council to playing a constructive role in formulating a dispensation, which will be more friendly to and supportive of new and emergent institutions. Barriers to entry must be lowered and red tape will have to be removed.

A New Class of Transaction Handlers

At the transaction handling level, transaction handlers, using the best that modern technology can offer, should be encouraged to enter the market and provide transaction handling services. The qualification should be that they are not incurring systemic risk and are not creating money. That would mean that the money that they are transacting should be deposited in a registered bank at all times - the newly established service providers are currently doing this.

It would also be appropriate to stipulate that the money must be held in a "Trust Company" which has no other assets and no other liabilities than the money it is transacting for clients and a contract with the Technology Company, which handles the electronic transmissions. This new class of transaction handler should therefore be an "add-on" to the payment system of the country, and there should be totally free competition.

In addition, the Strauss Commission into the provision of rural financial services recommended a significant role for the Post Bank in providing competitive and user-friendly services in the lower-end of the market. However, the Post Office is at present contracting its branch network, and the development of an efficient and technologically advanced Post Bank will require significant resources and attention.

THE USURY ACT AND THE NEED FOR CONSUMER PROTECTION LENDING LEGISLATION

In recent years there has been very robust growth of the "micro-lending" industry. There are two main types of lending carried out by “micro-lenders”, namely:

- Secured loans which are paid off the salary role of the employer; and
- Unsecured loans, which depend on the borrower for payment. Frequently the client's bankcard (and sometimes the client’s ID document) is taken so that the micro-lender can access the client's bank account at the time that the salary is credited.

It cannot be denied that the micro-lenders have provided access to credit at a level that the banks could not offer. Since access itself is frequently more critical than the cost of access at the low end of the market, it is hardly surprising that the industry has flourished.

However, there are a number of specific abuses and general practices which give rise to concern. Among these is the rate of interest that is paid for the loan. It is not uncommon for that rate to be 40 percent per month for an unsecured loan. The practice of taking the clients ATM card, and at times even his ID document, is patently undesirable.

But the general practice to make these loans available to people in employment in order to "bridge" them in relation to other debt, and solely for purposes of consumption, is very dangerous. Once on the debt "treadmill" it is very difficult for the consumer to get off. The result is that a high percentage of take-home pay is going to cover the interest on the loan because at some time in the past, bridging finance had to be obtained.

For the above reasons it is reasonably clear that the major banks would not engage this business themselves. If they were to enter the market, it would almost certainly be through existing micro-lenders. It is also unlikely that they would, to any significant extent, take advantage of an increase in the Usury exemption to R50, 000 loans.

At the same time there is, in the view of the banking industry, a measure of confusion in the purposes of different pieces of existing and proposed legislation. In our view, the Usury Act never afforded any real protection to the consumer. It was used to "persecute" institutions for technical non-compliance where they were charging way below the maximum rate (no matter how that rate was calculated). At the same time the real rogues were severely abusing the low-income communities.

A Usury Act on its own is not real protection to the public. There is vastly more to protection, including the way in which the Credit Bureaux function, prohibition of discriminatory lending practices, and so on.

That basic protection to which the public is entitled is as relevant to the banks as it is to the furniture retailers and the micro lenders. And protection of the public is not something which should be attached to an exemption from an archaic piece of legislation, or which is abrogated by the State in favour of an informal association of a particular group of lenders, which affords no real protection and frequently frustrates access to credit for the poor.

SO WHAT DOES THE BANKING INDUSTRY PROPOSE?

Borrowing by the public should be protected by a single piece of integrated legislation, regardless of who is the lender. Moreover there should not be any exemptions from such legislation. The Banking Council is aware that the Department of Trade and Industry has researched best practices in relation to consumer protection around the world, and we understand they will soon be making proposals in that regard. In the meantime, no further exemptions should be granted until those proposals have been debated and implemented.

The State cannot be allowed to abrogate its responsibility for the protection of the public. There may, however, be good reason, including the cost and efficiency in carrying out the regulation and supervision, to "privatise". However, such an approach would have to ensure that the State maintained ultimate authority and responsibility, similar to what has occurred with the Financial Services Board. It is our belief that this constitutes a sound model for the regulation and supervision of consumer lending.

The establishment and development of micro-lenders is important, and in the view of the banking industry they will play an ever-increasing role in the provision of credit to the lower-income communities. And, if nurtured carefully there is no reason why, in the future, they should not provide all-important competition to the higher value markets as well. Micro-lenders should therefore be encouraged to form their own associations and to develop them. Such associations are, in the view of the Banking Council, no substitute for the State's responsibility.

As far as the Usury Act itself is concerned, it should be repealed and those components of it which are useful as instruments for the protection of the public should be incorporated into the new consumer lending protection legislation. Until then, we will work with the

Department to find workable solutions to the difficulties that arise from the provisions of this outdated legislation – e.g. such as a formula to determine the maximum interest rates.

CONCLUSION

We would like to thank the Portfolio Committee for creating this opportunity for us to disclose more about the intricacies of banking in South Africa than has ever been done before.

We acknowledge that there is much to be done, and that the image of the banking industry in the eyes of the banking public "leaves much to be desired". Patently this is either due to:

- genuine grievances, which we need, as an industry to address; or
- a lack of understanding, for which we also bear heavy responsibility.

At the same time, we believe that as a nation we have very strong formal banks and the beginnings of very strong new institutions which can play a meaningful and significant role in the provision of banking services for all South Africans.

We need to look after both sets of institutions and find ways in which they can complement each other.