February 2020

THE BANKING ASSOCIATION SOUTH AFRICA

TRANSFORMATION in banking 2016 – 2018

About this report

This report is produced by Intellidex (Pty) Ltd

1st Floor, Building 3
Inanda Greens Office Park
54 Wierda Road West
Sandton
South Africa

Email: mail@intellidex.co.za
Web: www.intellidex.co.za
Tel: +27 (0)10 072 0472

Intellidex was commissioned by the Banking Association South Africa (BASA) to produce this report from data supplied from member banks.

The report reflects transformation in the banking industry and its progress towards achieving the targets set out in the Financial Sector Code.

The publication serves as a report to society on the contribution of the banking industry to the development of the country, and as a platform for thought leadership on transformation.

It aims to serve as an authoritative annual reference book of data on banks and empowerment, complemented with a narrative that analyses and explains trends in the statistics.

Acknowledgements:
Project manager: Colin Anthony
Data & analysis: Orin Tambo and Letta Maponyane
Editorial: Londiwe Buthelezi and Colin Anthony
Design & layout: Eleonora del Grosso
Subeditor: Yvonne Fontyn

Contents

A story of progress: neither complete success nor complete failure

Hans Rosling, in his book Factfulness, talks about the strong human desire to think of things in binary terms. He says: "Human beings have a basic urge to divide things into two distinct groups, with nothing but an empty gap in between. We love to dichotomise. Good versus bad. Heroes versus villains. Dividing the world into two distinct sides is simple and intuitive, and also dramatic because it implies conflict, and we do it without thinking, all the time. Journalists know this. They set up their narratives as conflicts between two opposing people, views, or groups. They prefer stories of extreme poverty and billionaires to stories about the vast majority of people slowly dragging themselves toward better lives."

The story of the transformation of the financial system in South Africa similarly does not lend itself to one-liners, tweets or quick ripostes. It is however a story of slow, steady, meaningful and deep progress across a wide range of fronts. It is not a story of complete failure, but neither is it a story of complete success. It is a story of progress; of overcoming real-world obstacles, tackling immense social challenges and navigating complexity in a world more dynamic yet uncertain than ever before.

Transformation is and must always be seen as a multidimensional project. It encompasses the need for rising black and women equity participation and ownership of financial institutions, transformation of the boardrooms, financial inclusion, lending to small and medium-sized businesses, providing services to townships and rural areas, procuring goods and services from black- and women-owned companies and changing the racial and gender composition of the staff and management of banks and financial institutions.

While all these elements are important, what is absolutely non-negotiable is contributing to transformation of the broader South African economy and society through providing world-class products and services efficiently and effectively to an ever-wider constituency. Equally, maintaining the safety and soundness of the financial sector so that it does not impose huge costs on the economy when problems occur, costs which inevitably fall hardest on the poor, is an objective that must be considered in any discussion on the financial sector.

This report provides a granular account of how South Africa's banks and related financial institutions have navigated the complex waters in which they operate to transform themselves into truly post-apartheid institutions.

To steal another concept from Rosling, a situation can be better but still not good enough. This report will show that there has been progress, meaningful progress on most fronts. Ownership is far more diversified today with institutional and pension fund ownership the dominant feature of ownership, in contrast to pre-1994 when a few prominent families owned large shares of the banks. Boardrooms are more diverse, both in terms of race and gender but also in terms of life-experience and background. Black and women senior managers have risen in both number and prominence. Most banks have sound long-term partnerships to procure more goods and services from black- and women-owned businesses. On financial inclusion, almost 80% of South Africans now have a bank account, up from just over half in the late 1990s. On aggregate, employment in the sector has grown steadily, notwithstanding recent reductions. The sector is both more competitive and diverse today in terms of the number of players, yet it remains safe and sound from a prudential perspective. These are all worthy achievements.

But the report will also show that too little progress has been made in critical areas of transformation. Direct, meaningful ownership by black people and women remains too low. Many boardrooms are still insufficiently diverse. Top and senior management remains too white and male. There is insufficient lending to small businesses (of any colour, one may add). Township residents still feel that they are not given the kind of financial services they deserve and for which they pay.

These red marks on the scorecard must be highlighted, not to demonise the sector, but to motivate the sector to continue to walk along the journey started almost three decades ago. It is a journey that will not only determine the long-term sustainability of the financial sector but will also determine if we as a country are to succeed in overcoming the terrible legacy of race and gender discrimination that is still so visible in our society.

I wish to thank BASA for the leadership role that it has played in mobilising the sector to transform. South Africa is blessed by having organisations such as BASA and a calibre of bank CEOs who are firmly committed to transformation and with whom policy makers and regulators can regularly have mature and deep conversations about the state of the sector and its future.

Long may the transformation journey continue.

Kuben Naidoo
CEO: Prudential Authority
South African Reserve Bank

Highlights

Black board members up from 43% *to* 51%

Top black senior managers up from 32% *to* 36%

Socioeconomic development spending 6% *to* R666m

Black skills development spending 23% *to* R3.3bn

Spending on consumer education 24% R180m

Black agricultural financing up 41%

Spending on supplier development almost doubled to R795m

Exposure to black SMEs 13% *to* R28.8bn

All figures reflect growth between 2017 and 2018

Financial inclusion and transformation are now at the core of banking in SA

The Transformation in Banking report measures the progress the banking industry has made towards the targets set out in the Financial Sector Code (FSC) as well as its broader contribution to the social and economic development of South Africa. It demonstrates, with hard data, that banks play a transformative role in South Africa that goes well beyond the prescripts of the financial sector code or the BEE generic codes of good practice.

The report shows that while the performance of the industry across key transformation measurements remains uneven, it has exceeded many of the key targets set out in the FSC.

Black ownership measures – like voting rights – have declined over the three years under review (2016-2018), but on aggregate remain above the FSC targets, with the exception of black economic interest. The decline in black economic interest is mostly due to the continued exit of black shareholders who received shares through empowerment schemes established by the large banks. It is estimated that by 2015, black investors had realised R57bn in value from bank empowerment deals.

Ownership measures are likely to continue to drift down in the coming years as black investors realise value and diversify their portfolios. Because of these changes in ownership, the Financial Sector Transformation Council included black business growth funding as a new element of the code that came into effect in December 2017. This funding will contribute to transformation by supporting the growth of black businesses across the economy.

In 2018, large banks' balance sheet exposure to black small and medium enterprises (SMEs) increased by 13% to R28.8bn; black agricultural financing increased by 41% to R4.5bn; and spending on supplier development almost doubled to R795m. The increase in spending on financing SMEs, black agricultural enterprises and supplier development is far more transformational and better for the economy and job creation than ownership. Large banks are capital-intensive and all around the world their ownership is almost entirely institutional, with low levels of direct individual ownership.

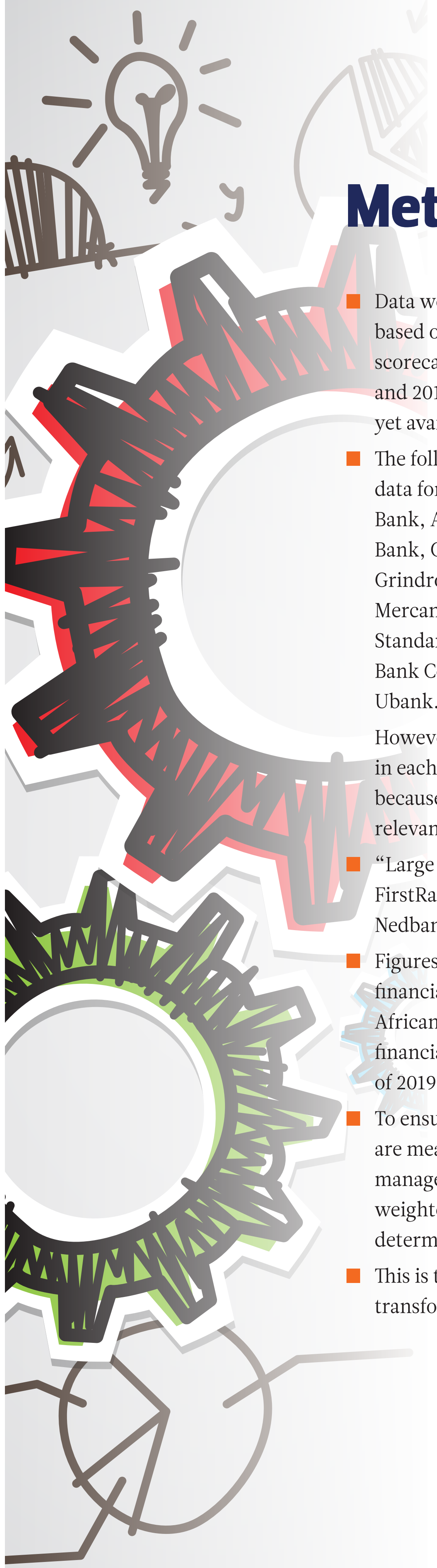
The proportion of black board directors increased from 40% to 45% in 2018, approaching the 50% industry target. In addition, junior management in banks is now 85% black. This is important as it means there is a pipeline of young black talent and experience who will transform the management and executive ranks of the industry in the coming years. Opportunities for advancement in the industry remain, despite a reduction in headcount in some operations. The South African Reserve Bank has issued three new banking licences, increasing competition and expanding the banking industry.

> While the performance of the industry across key transformation measurements remains uneven, it has exceeded many of the key targets set out in the FSC

It is not always best to assess major change of the nature that the Broad-Based Black Economic Empowerment Act envisages with annual comparisons. But even when comparing the banking industry today to when the first Financial Sector Charter was negotiated in 2002, the drastic changes in management, ownership and services of banks are there for all to see. The industry now provides affordable, accessible and appropriate transactional services to an estimated 80% of adult South Africans across income groups and geographical locations. There can be no doubt that financial inclusion and transformation are now at the core of the business of banking in South Africa, even as the industry upholds its ultimate responsibility to safeguard the deposits entrusted to them by all South Africans. As a vital part of the country's economic infrastructure, banks must operate in a way, and at a pace, that ensures they remain sustainable businesses that can offer their investors and customers a reasonable return.

BASA's mandate is to "make banking sustainable, profitable and better able to contribute to the social and economic development and transformation of the country". BASA commissioned the 2020 banking transformation report from an independent agency – Intellidex – to ensure the integrity and credibility of the findings, which are based on statistics submitted by its member banks. It will help the banking industry to show measurable progress in our efforts to transform our industry and economy and highlight where more work needs to be done in the coming year.

Cas Coovadia
Managing Director
Banking Association South Africa



Methodology

- Data were supplied by the banks, based on the Financial Sector Code scorecard methodology for 2016, 2017 and 2018. Figures for 2019 were not yet available.
- The following banks submitted data for this report: Absa, African Bank, Al Baraka, GroBank, Bidvest Bank, Capitec, Finbond, FirstRand, Grindrod, Investec, HBZ Bank, Mercantile Bank, Nedbank, Sasfin, Standard Bank, China Construction Bank Corporation, Citibank and Ubank.

  However, not all banks are included in each of the sets of analysis below because different categories are not relevant to some banks.
- "Large banks" refers to the "big six": FirstRand, Standard Bank, Absa, Nedbank, Investec and Capitec.
- Figures for all banks are for their 2018 financial years except for Capitec, African Bank and Investec, whose financial years end in the first quarter of 2019.
- To ensure that industry data are meaningful, ownership and management control data were weighted by banks' total assets to determine industry aggregates.
- This is the second annual transformation report published by BASA. Like last year, our research partners Intellidex collated data provided by South Africa's registered banks. Intellidex aggregates that data in order to produce consolidated figures for the industry, which we publish here.
- Caution needs to be taken by readers in comparing the data for 2017 and 2016 in this report with the data for those years published in last year's report. Between this year and last year there has been a change in the banks' reporting – two banks exited while four banks entered, due to foreign banks closing branches in SA and new banks opening. In order to make the data comparable on a like-for-like basis, we recalculated the figures for 2017 and 2016 as if the sample for 2018 had been the same in those years. Additionally, there were some technical changes including a change in the reporting year-end of one bank and some recalculations of historic data of some other banks. In some of the targeted financing categories, more banks were able to provide data this year compared with last year due to improvements in data management systems. An explanatory note detailing the relevant changes can be found in the affected sections.

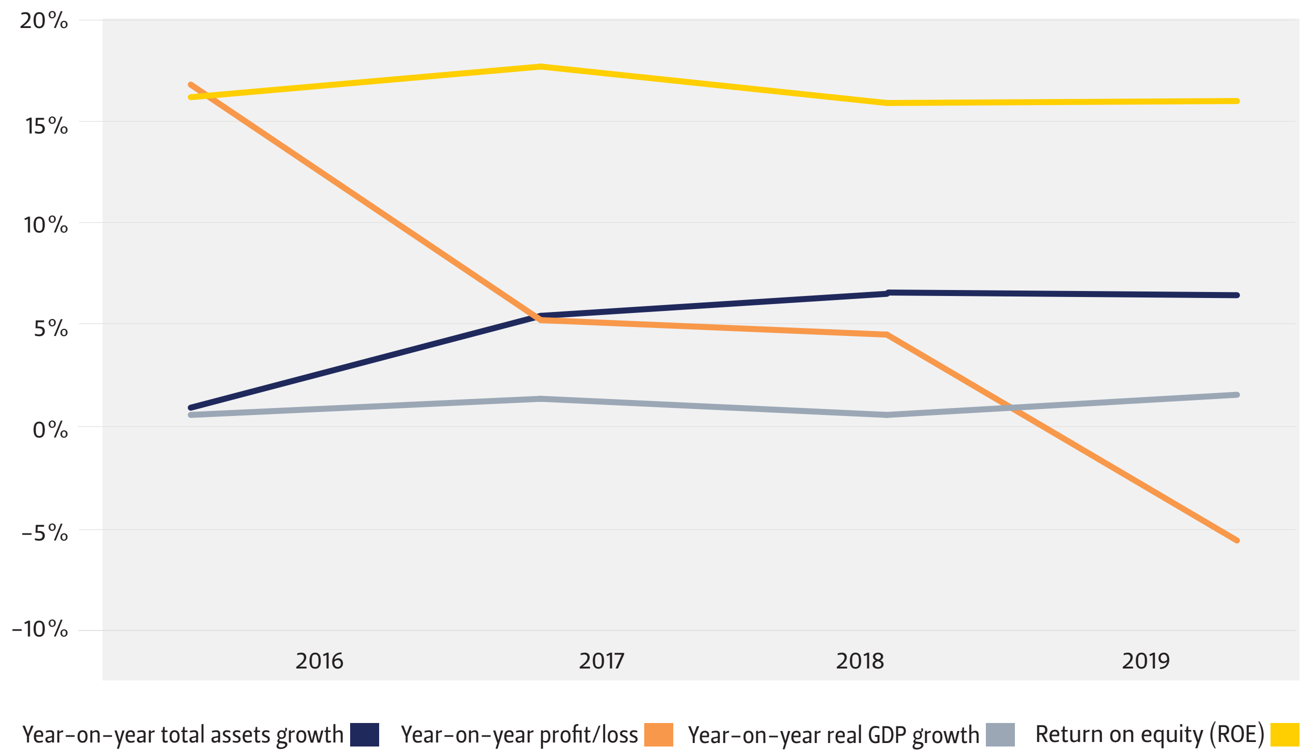
Data and analysis

The transformation progress reported in this year's annual report took place in a difficult environment for banks. Broad economic activity slowed down further with negative per capita economic growth recorded for the sixth year in a row.

The weak economic environment makes it difficult for banks to increase lending, while a conservative stance must be taken on cost control. Banks also face a worsening credit environment with significant growth in credit impairments between 2017 and 2018. This makes it difficult to drive transformation that depends, for example, on lending growth to targeted sectors, or for banks to incur the costs of enhanced skills and supplier development.

The improvements in most transformation factors that are reported here therefore should be seen as an even stronger achievement, given that they occurred in the face of strong economic headwinds that banks faced. Banks also faced a more competitive environment with the entry of three newly licensed banks. Growth in financing of affordable housing, black small businesses, BEE transactions and black agriculture all took place in a context in which overall bank balance sheets barely grew ahead of inflation, growing 6.5% in 2018. Enhanced spending on enterprise development, socioeconomic development and supplier development took place while profitability was under pressure, shown in declining return-on-equity and profit growth of only 4.7% in 2018.

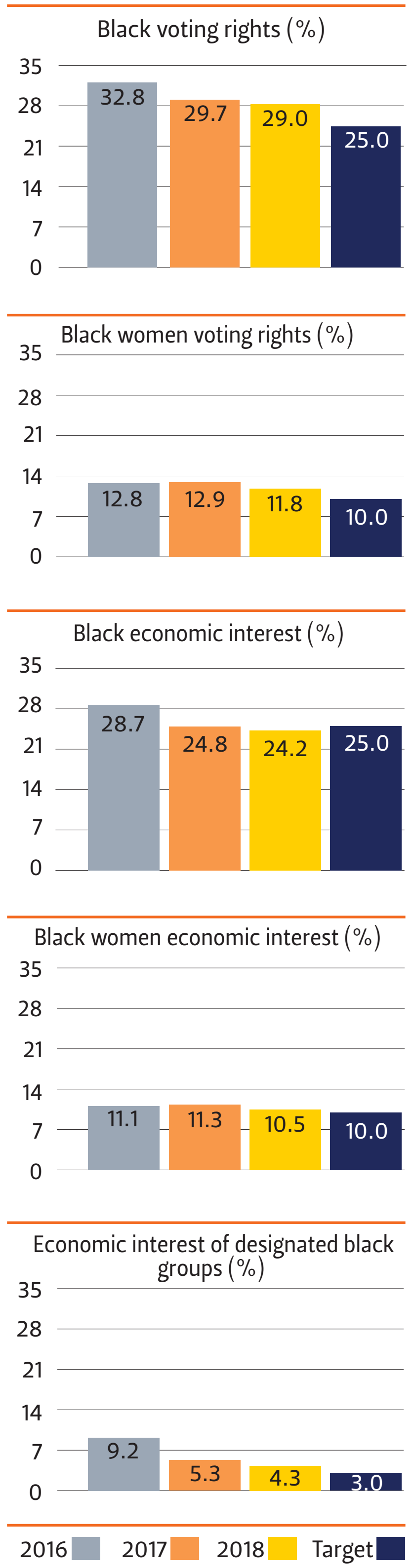
Banking sector financial performace vs GDP (% change)



Ownership

- Black ownership measures have declined across the three years on all measures.
- Capitec, Nedbank and FirstRand reported declines in their black economic interest (black ownership) while Absa, Investec and Standard Bank reported slight improvements.
- Economic interest of black women, which had improved marginally in 2017, also declined during 2018 but remains above the FSC target for individual banks of 10%.
- The decline in black interests is mostly due to a continued exit of shareholders who received shares through empowerment schemes established by the large banks in 2005. Most of those matured in 2015, at which point beneficiaries were free to dispose of their interests. Shareholders sell to realise value, which many BEE shareholders achieved. For many BEE shareholders, their bank shares were their only real asset, so selling also makes sense from a diversification point of view.
- While banks' ownership measures deteriorated during 2018, on aggregate banks remain above the FSC targets with the exception of black economic interest, which fell slightly below the 25% target.
- Based on public announcements, some banks have or are undertaking transactions that will improve aggregate black ownership for the industry. For example, Discovery Bank is implementing a transaction that will see 10% of its shares in the hands of black people; Tyme Bank (which did not submit data for 2018) has seen majority ownership taken by African Rainbow Capital; and Capitec has acquired Mercantile Bank (which had no black ownership). However, the larger banks will likely experience a continued exit by black shareholders and the net effect is difficult to anticipate.
- The 2016 and 2017 ownership figures for this year are not directly comparable with those in last year's report due to changes to the sample. Last year nine banks were in the sample, but this year there are 14. Because of different sample sizes, the weightings of different banks changed, which affected the weighted industry aggregate figures. The impact was a reduction of ownership figures for 2017 of about 0.7 percentage points and for 2016 of about 2.0 percentage points.

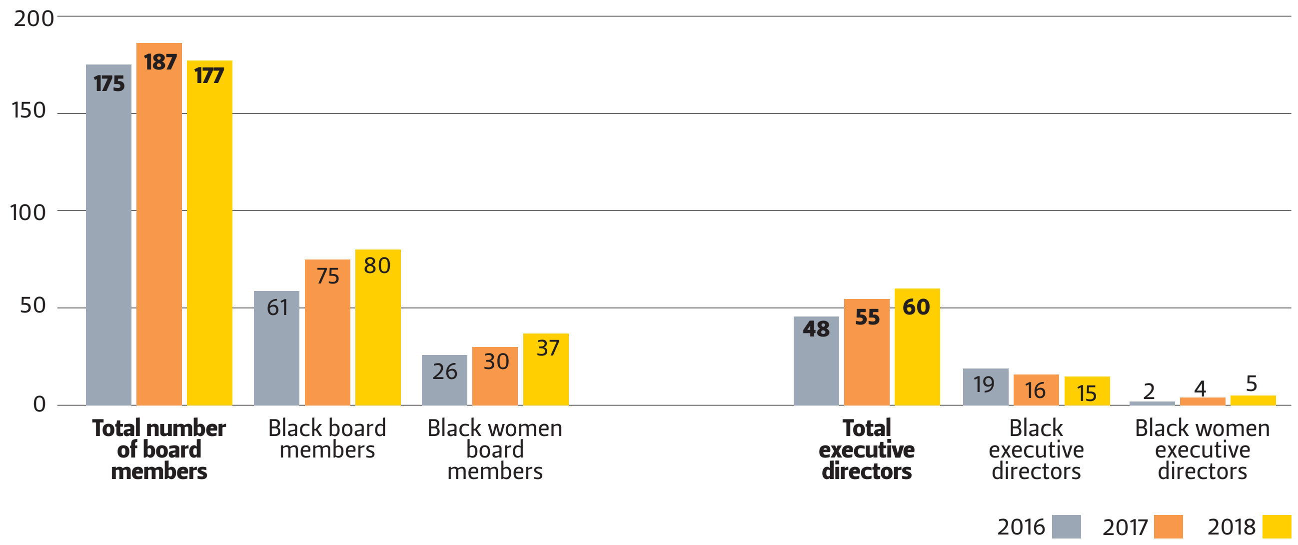
Black ownership percentage in banks



Fourteen banks reported their black economic interest. The rest of the banks are held by foreign investors and therefore do not reflect any black ownership.

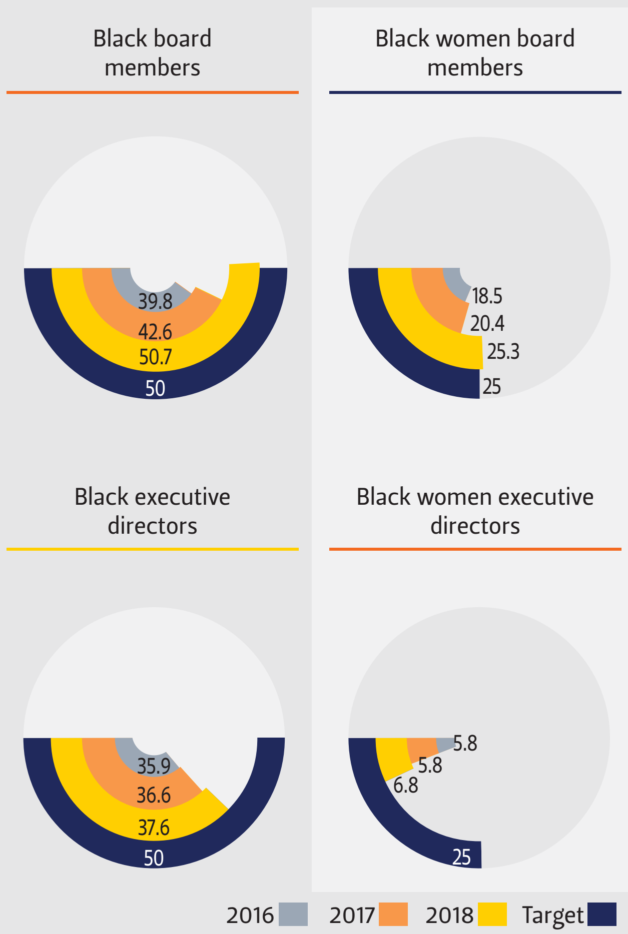
Management control

Number of directors



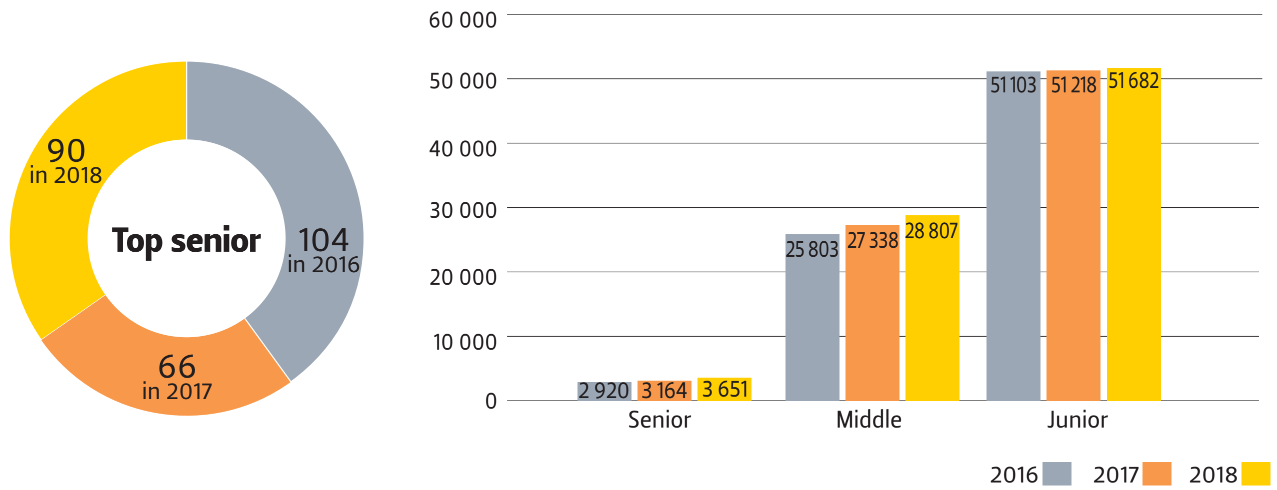
- In this report the 2016 and 2017 figures differ from those published in the previous report largely due to different banks in the sample. Two banks exited the sample and four banks entered. Furthermore, the proportions of directors who are black were weighted by banks' total assets. The previous report shows unweighted proportions. We resolved this year to apply weights to this measure to account for the different sizes of banks.
- Banks continued to make strides in transforming their boards, with the number of black board members continuing to grow and surpassing the 50% mark for the first time since the introduction of the black economic programme.
- While the total number of directors on banks' boards declined to 177 members (2017: 187) the proportion of directors who are black increased to 50.7% from 42.6% in 2017 and 39.8% in 2016 driven mostly by large banks such as FirstRand, Investec and Nedbank which have more than half of their directors being black.
- A net of five black members were appointed to banks' boards during 2018. There appears to have been a deliberate effort by banks to replace non-black members who resign with black appointees.
- Black women now account for more than a quarter of banks' board members. Women representation has also surpassed the industry target of 25%. FirstRand, Investec and Nedbank have above-average women representation on their boards.
- The proportion of black executive directors improved to 37.6% from 36.6% in the previous year, but remained well below the target of 50%.
- The proportion of black women in executive directorship roles also remains below the sector target.

Proportion of directors who are black (%)



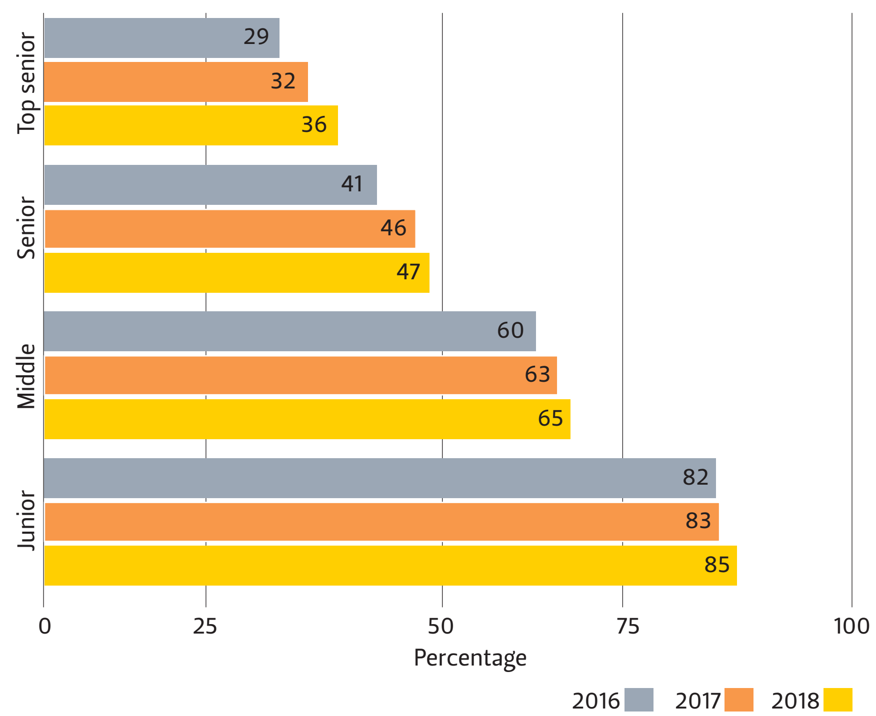
Management control

Black representation in management (total number)



- Banks in the sample had 113,430 employees (2017: 112,342) who are classified as managers according to the definitions in the FSC code.
- The sharp decline in the number of top senior managers between 2016 and 2017 is largely due to corporate grade reporting changes at Absa, where the number of top senior managers fell from 116 to 12.
- The number of black managers across all levels has not changed much over the past three years.
- During 2018 banks had 84,230 black managers, up from the 81,786 reported in 2017.

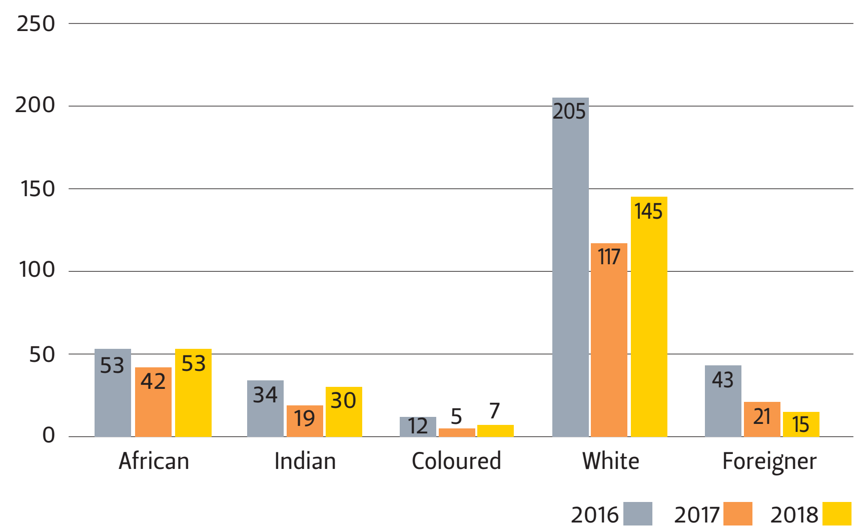
Proportion of managers who are black



- While the number of black managers at banks has not changed much over the past three years, there has been some improvement in the proportion of black managers, particularly at the top level.
- Overall, black managers accounted for 74.7% of bank management teams during 2018, up from 72.8% in the previous year.
- Black top senior management roles climbed to 36% during 2018 from 32% in the previous year.
- The number of black senior managers also increased to 3,651 (2017: 3,164), putting the proportion of black senior managers at 47% (2017: 46%).

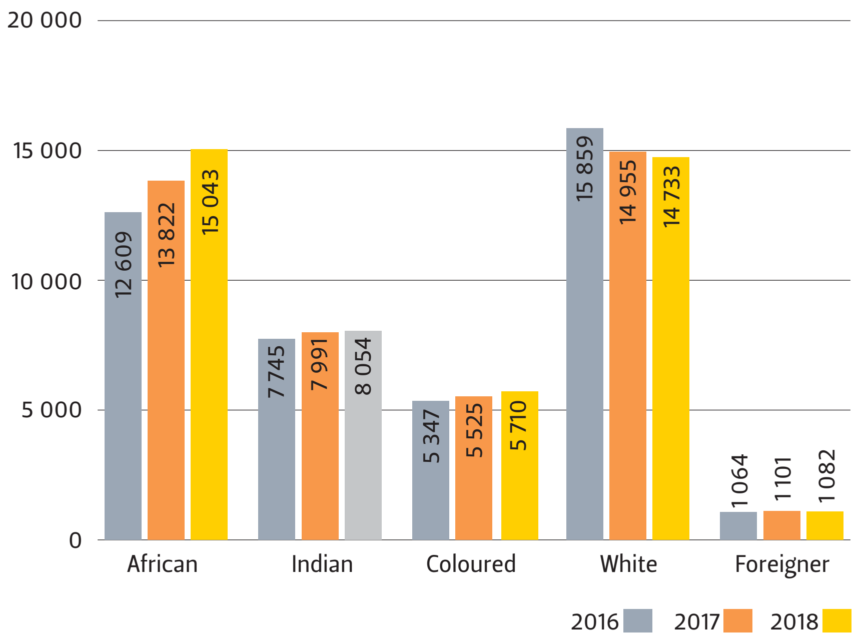
Detailed analysis of the racial breakdown of management teams

Top senior management



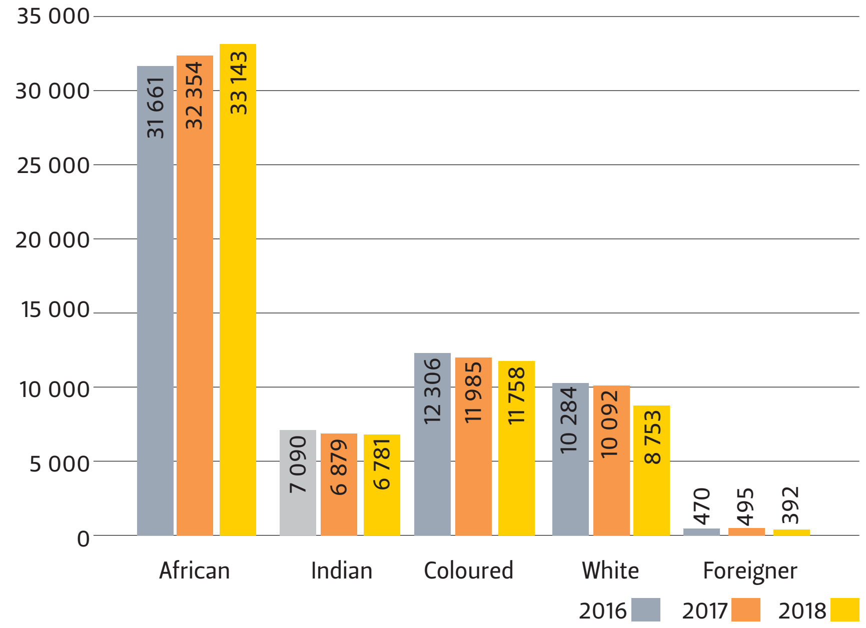
- There was an increase in the total number of top senior managers between 2017 and 2018. The proportion of whites and blacks in top senior management increased at the expense of foreigners.
- More than half of the 52 net new appointees to top senior management were whites.
- The number of black Africans increased significantly, from 42 to 53. There was also a notable increase in the number of Indians in top senior management, from 19 to 30.

Middle management



- The total number of middle managers at banks rose slightly.
- There were gains in the total number of black managers and in the proportion of black managers. This saw black Africans overtaking whites as having the largest representation in middle management of banks.

Junior management

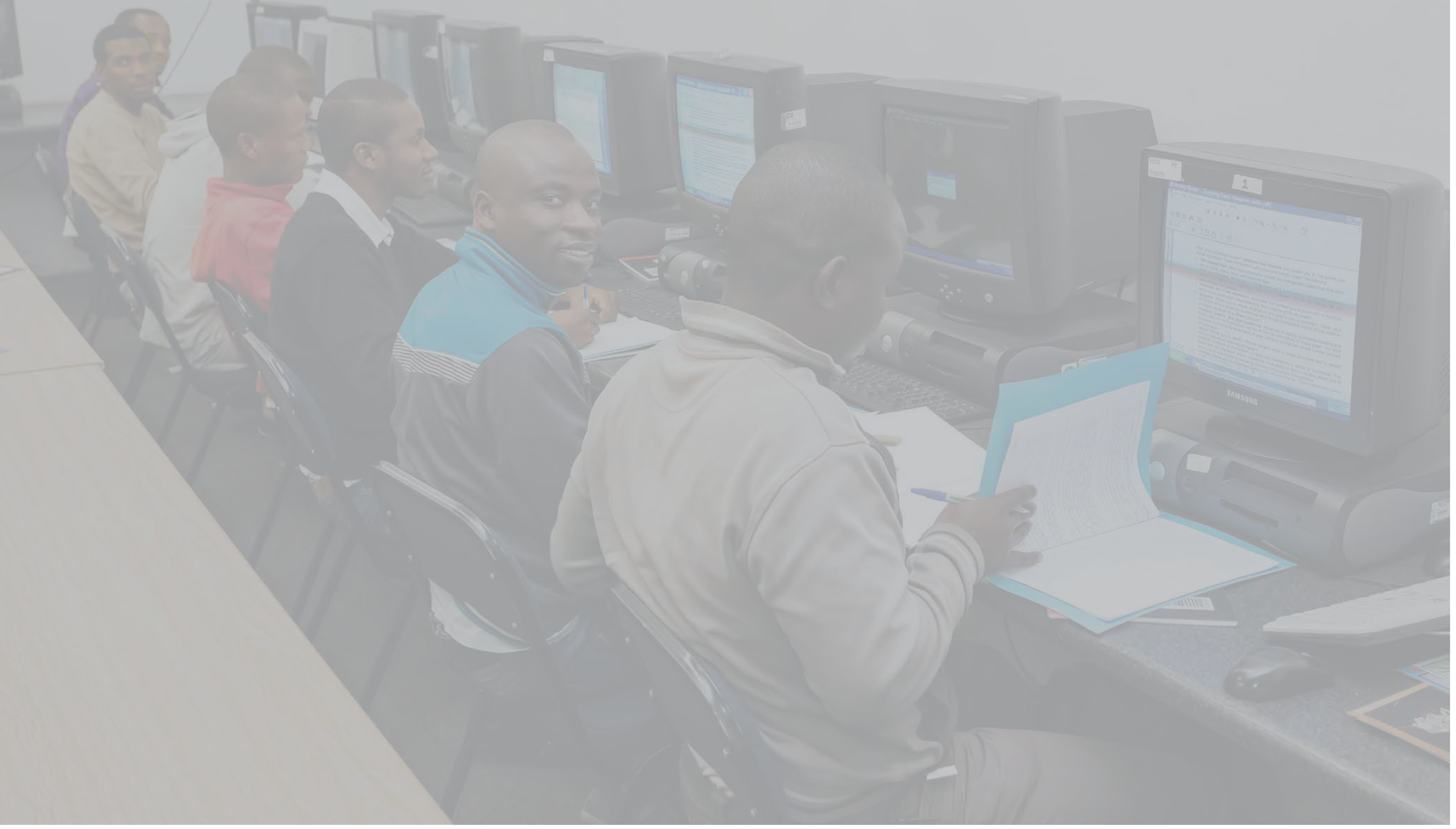


- There has been a sustained increase in the proportion of blacks (particularly African blacks) in junior management level.

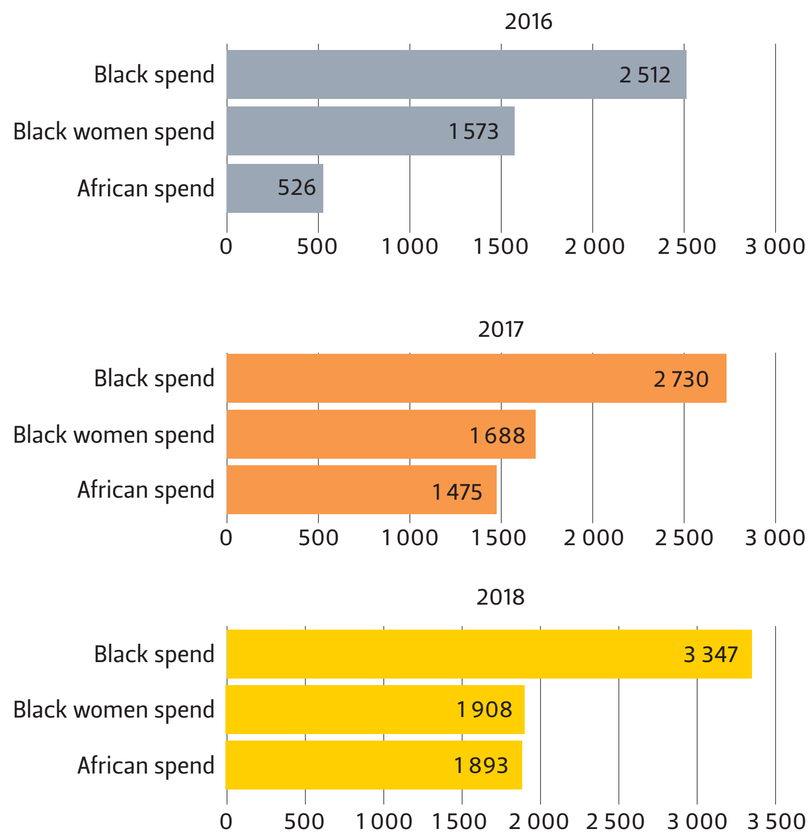
Employment equity is one area in which all local banks have managed to excel over the years, with black people constituting the majority of promotions into all job grades, with junior management, for example, now 85% black. But most banks are still struggling to replicate these successes at senior (47% black) and executive management levels (36%). On a positive note, black women representation is improving in most banks. Banks have set ambitious targets to accelerate employment equity, where progress has been slow. For instance, Standard Bank wants to have at least 40% of its executive positions in South Africa filled by women by 2021. And Capitec has put an executive succession plan in place, creating "development seats" in its executive committee for black senior employees to be groomed for executive positions.

Skills development

- Banks continued to channel more resources towards initiatives aimed at developing black skills.
- During FY18 banks spent R3.3bn on black skills development, 23% more than the previous year.
- Notably, more than 60% of banks' expenditure on skills development of black employees over the past three years was on black female employees.
- More than half of spending was on black Africans.
- Of the large banks, Capitec (up 57%), Nedbank (up 35%) and FirstRand (up 30%) reported above-average growth in spending on skills development.
- Absa was the only large bank to report negative growth during 2018.



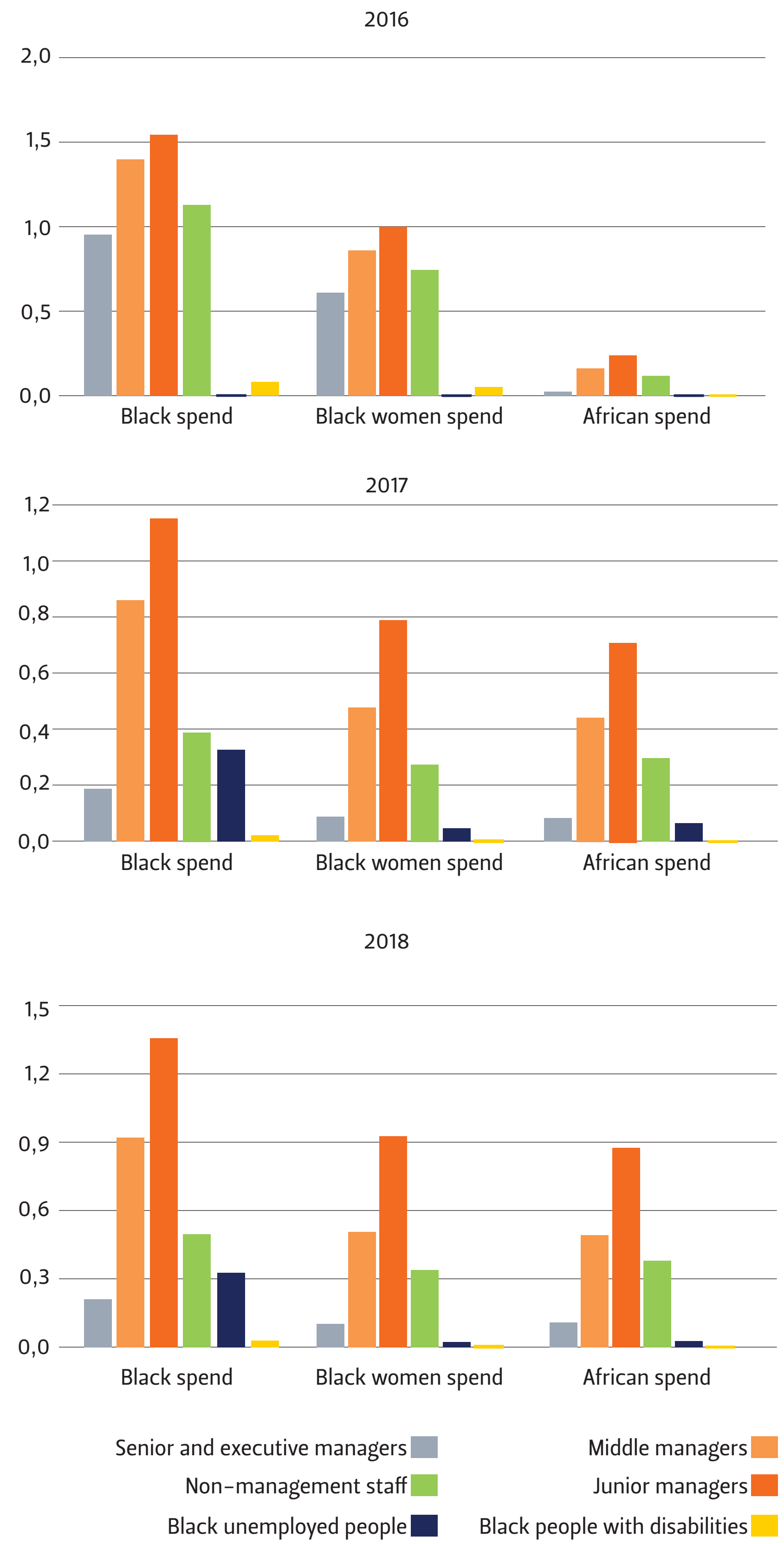
Skills development spend (Rm)



Skills development by occupational levels

- Junior managers received the largest portion of spending by banks on skills development, followed by middle managers.
- However, senior executive managers are by far the biggest beneficiaries on a per capita basis.

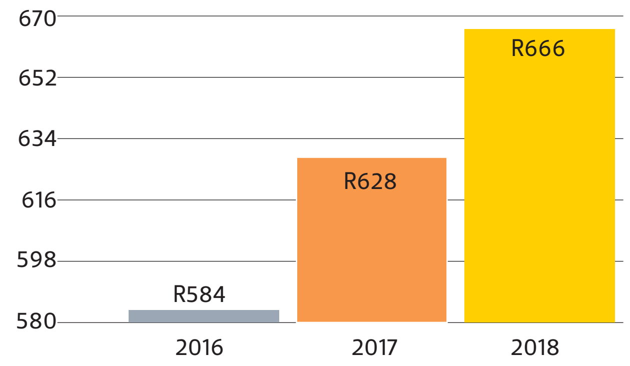
Skills development spend (Rbn)



Socioeconomic development

- Socioeconomic development spending, which includes spending on organisations that predominantly benefit black people, increased 6% between 2017 and 2018.
- Capitec, which increased its socioeconomic expenditure by 100%, had the highest growth, followed by Investec with a 33% increase.
- Absa, FirstRand and Standard Bank also increased their expenditure on socioeconomic development in 2018.
- Nedbank reported a 26% decline in its socioeconomic development spending to R77m (2017: R104m).

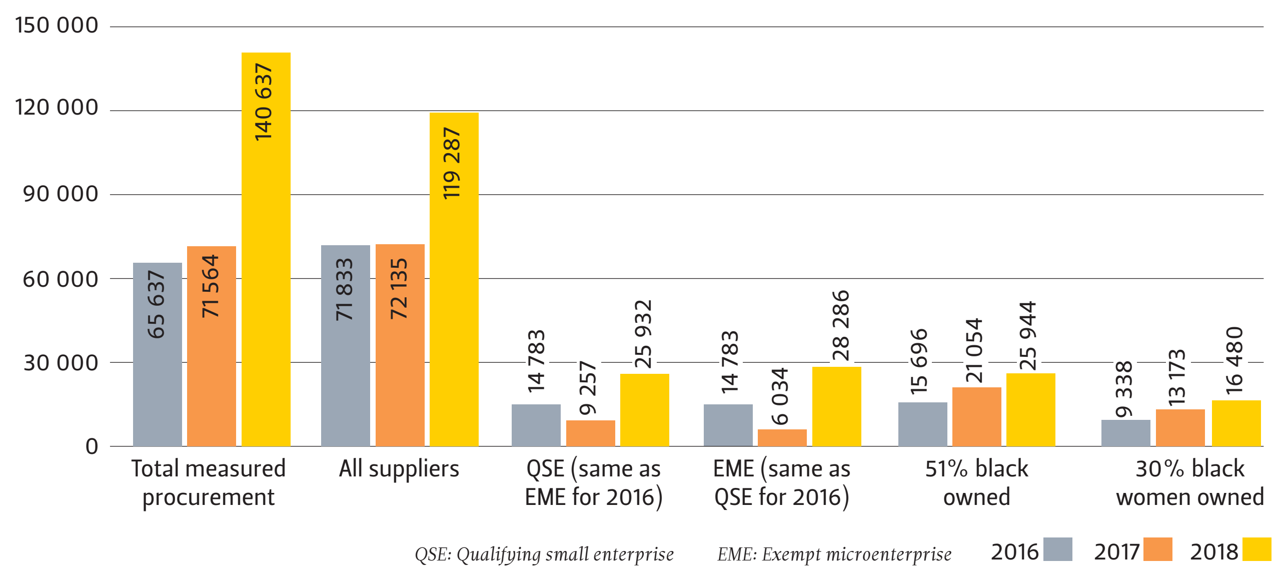
Socioeconomic development spend (Rm)



- Differences between 2016 and 2017 figures in this report and the previous one are because last year 11 banks reported figures in this category against 17 banks this year. Further differences were caused by the exit of two banks and entry of four into the sample.

Procurement

Preferential procurement (Rm)



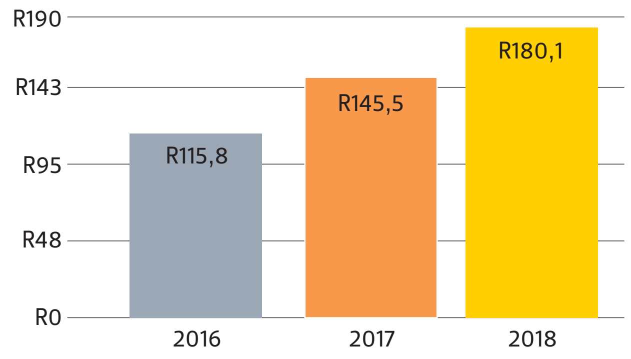
Between 2016 and 2017 the relevant definitions for small business changed and two categories replaced one: "qualifying small enterprises" and "exempt micro enterprises". These two sums should be seen as one in comparing with 2016.

- Banks' total measured procurement spending almost doubled during 2018, with a large portion of that going to black suppliers.
- All categories of black suppliers benefited from the increased expenditure.
- The small discrepancies in the 2016 and 2017 data between the 2020 and 2019 reports are due to the sample change, where two banks exited and four entered.

Banks are moving more of their procurement spending towards black-owned business and are giving notices to their other suppliers to improve their B-BBEE status. For instance, Standard Bank has asked most of its suppliers to submit B-BBEE improvement plans and says this consultation is already yielding positive results. The bank has developed a system to help it shift its procurement spending from non-compliant suppliers, who currently constitute 48% of the group's total procurement spend, to black-owned SMEs.

Consumer education

- Bank spending on various consumer education initiatives increased 24% between 2017 and 2018, driven in large part by Standard Bank (which spent R13m more than the previous year) and Capitec (R10m more).
- All banks, except Nedbank and Grindrod, increased their spending on consumer education during 2018.



Dealing with the student funding crisis

South Africa is dealing with an unprecedented student funding crisis. Even though it has been two years since the introduction of fully subsidised higher education and training for students coming from poor and working class backgrounds, tensions have not eased as funding available to the National Student Financial Aid Scheme (NSFAS) is not enough to cover all eligible students.

While the FSC requires banks to invest in skills development for their own employees, most banks are going beyond this, providing bursaries to school children at elementary level, university students and children of their employees. To deal with the heightened shortage of student funding, banks responded by contributing to new government-administered bursaries, creating new bursary schemes internally while those who were already funding external candidates committed more money.

How the banks responded

The banks responded in a big way to the student funding crisis. Absa spent R8.7m on bursaries for non-employees. That was over and above the R130m the bank has invested in 2,614 student scholarships across 21 universities, for employees and external candidates. But realising that SA's poor education outcomes have much to do with lack of institutional capacity, Absa also funds a financial management and governance training programme for school governing bodies and Department of Basic Education circuit managers to better equip them for managing school finances and resources. The programme takes place each year in different provinces in partnership with the Department of Basic Education.

Standard Bank has a long-running bursary programme for critical skills. In 2018, it funded 130 local university students.

All major banks to contributed to the Ikusasa Financial Aid Programme (Isfap), a public-private partnership between government and the private sector aimed specifically at addressing the funding gap for the so-called missing middle – families who earn too much to qualify for free education but not enough to pay for university. Through Isfap, Standard Bank funded 166 more university students.

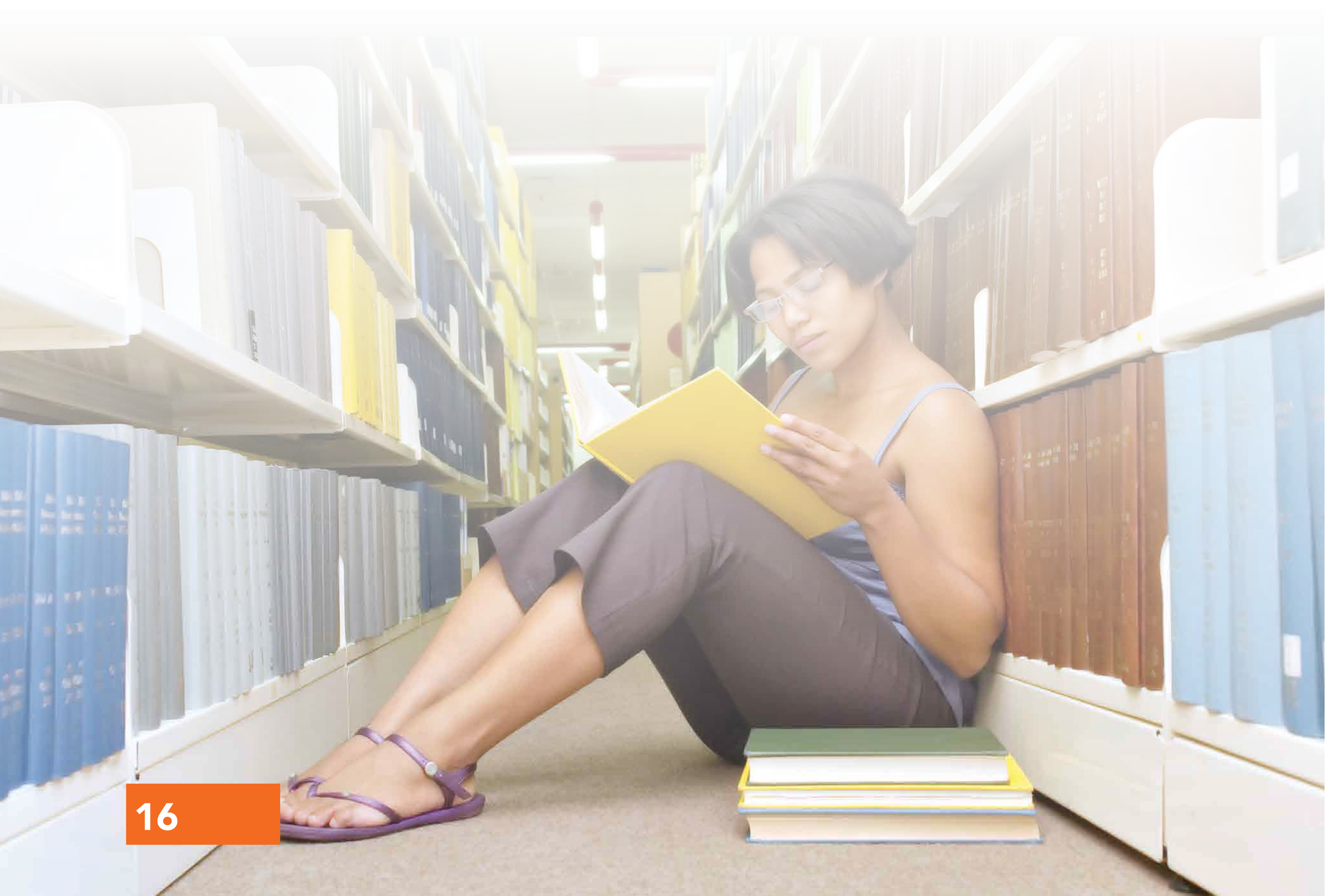
The bank also became a funder and partner of the Feenix Crowd Funding Platform, launched in June 2017. The platform allows individuals and enterprises to donate money directly to students to help them complete their studies. Standard Bank made a three-year commitment to cover set-up and operating cost shortfalls of the project. In 2018, the platform raised over R22m, which funded 650 students, 75% of whom were black and 50% women.

Nedbank, Capitec and Investec also have strong a focus on funding basic education. For instance, R35m of Nedbank's R63,9m bursaries that were given to non-employees were for elementary schoolchildren. Nedbank has been supporting the Maths and Science Leadership Academy, an initiative in Kimberley that, since 2010, has been funding afternoon classes and holiday academies for high school learners from disadvantaged backgrounds.

At tertiary level, the bank's Get me to Graduation programme committed R4,5m to cover gaps in NSFAS and to supplement other bursaries that don't cover all learning necessities. This extended to 600 students at different universities. The rationale is to reduce the number of students who drop out because their bursaries do not give them money to buy food or other essentials.

Investec, through its internal bursary scheme and its Entrepreneurship Development Trust, provided high school bursaries to underprivileged high school students so that they can attend well-established and high-performing schools. And its Promaths programme has funded more than 7,500 learners from disadvantaged backgrounds since it was established 13 years ago. In 2018, Investec established the ninth Promaths centre in Khayelitsha, Cape Town, supporting 210 learners from 11 feeder schools. The Promaths centres produced 267 maths distinctions from 1,176 learners in 2018 and 412 distinctions in science.

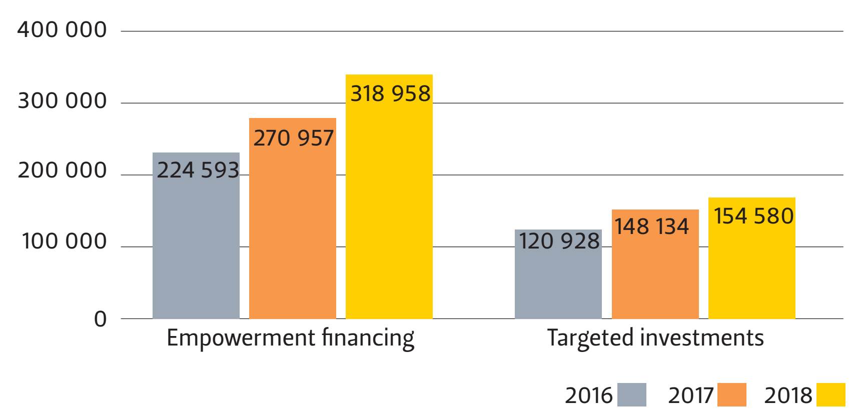
FirstRand has a staff assistance trust that pays for schooling of employees' children, from Grades R to 12. In 2019, the trust assisted 6,205 employees with their children's school expenses, to the value of R46.5m, R8.6m more than in 2018. It also provides extensive funding through the FirstRand Foundation and the FirstRand Empowerment Foundation.



Empowerment financing

- Empowerment financing consists of cumulative targeted investments and B-BBEE transaction financing for local banks. It is measured as total balance sheet exposure for new loans written from 1 January 2012 to 31 December 2017 (but including the amounts held on banks' balance sheets as at 31 December 2011).
- The graph shows aggregate balance sheet exposures of six banks – Absa, Capitec, FirstRand, Standard Bank, Investec and Nedbank – which supplied total balance sheet exposures.

Empowerment financing (Rm)

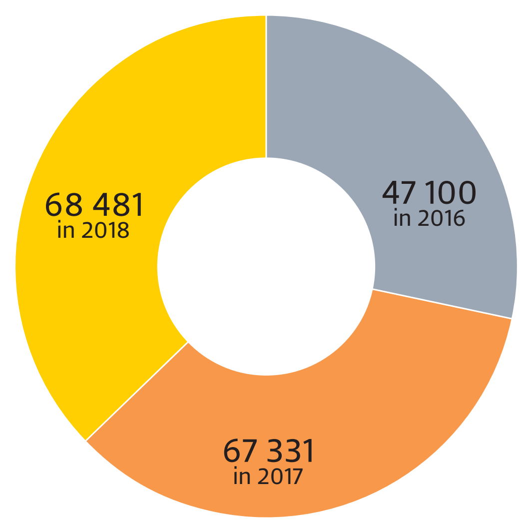


- Large banks have consistenly increased their balance sheet exposure to empowerment financing over the past three years.

Transformational infrastructure spending

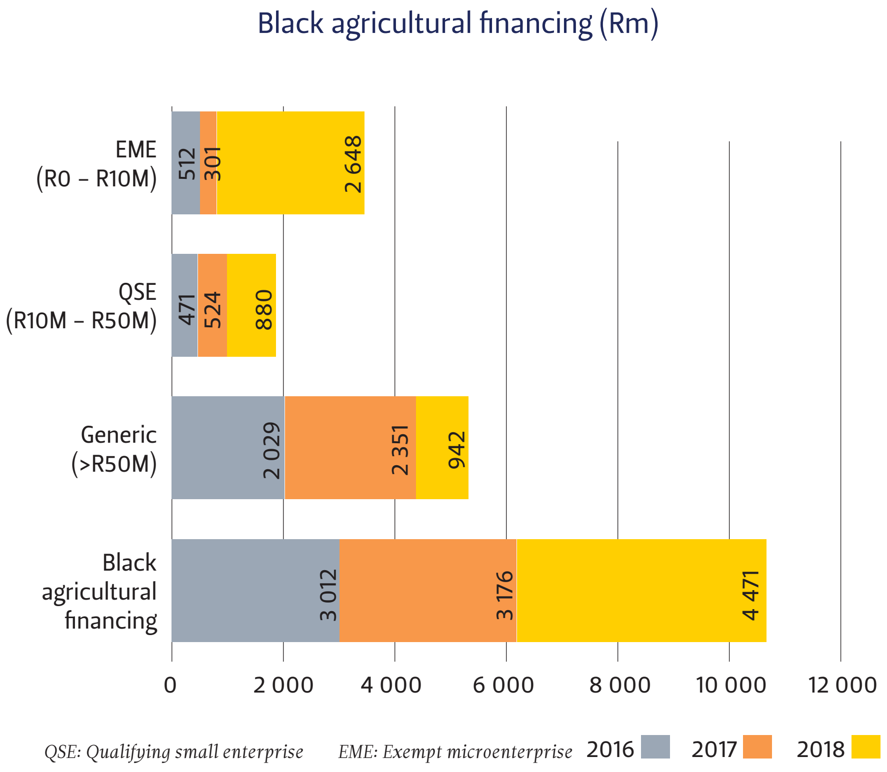
- Banks' balance sheet exposures to transformational infrastructure financing was largely flat. This includes debt financing, other forms of credit or equity investments in South African projects in areas where gaps or backlogs in economic development and job creation have not been adequately addressed by financial institutions.
- Absa (up 57%), FirstRand (up 6%), Nedbank (up 5%) reported positive growth while Standard Bank (down 16%) and Investec (down 13%) reported declines.

Transformational infrastructure spend (Rm)



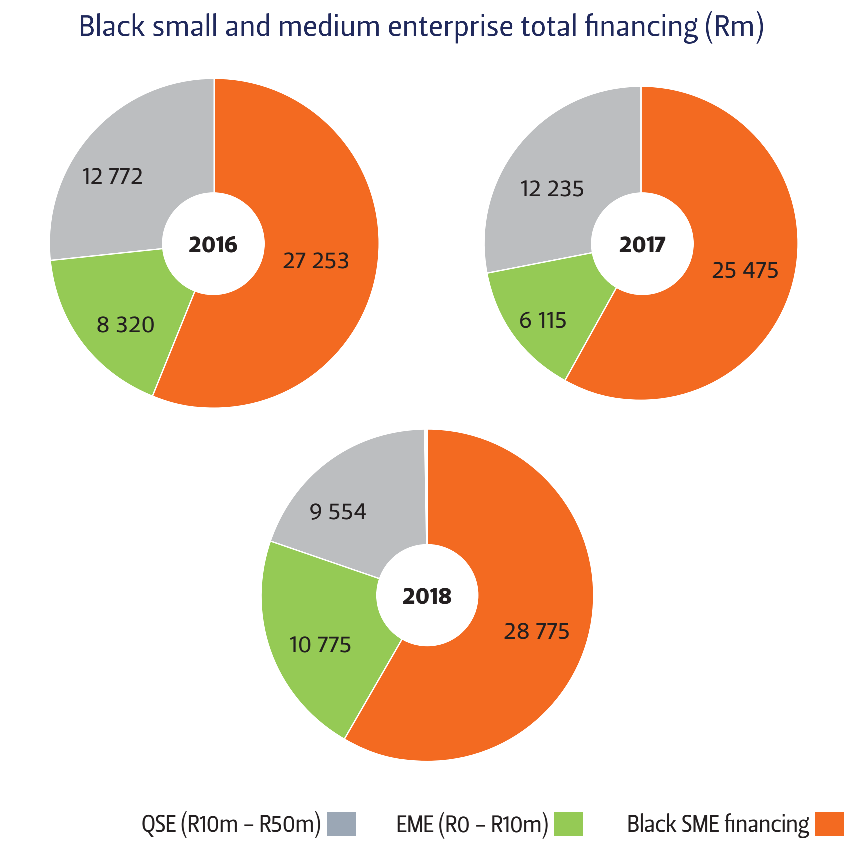
For this category we report aggregate data for four large banks: Absa, Nedbank, Standard Bank and FirstRand.

Black agricultural financing



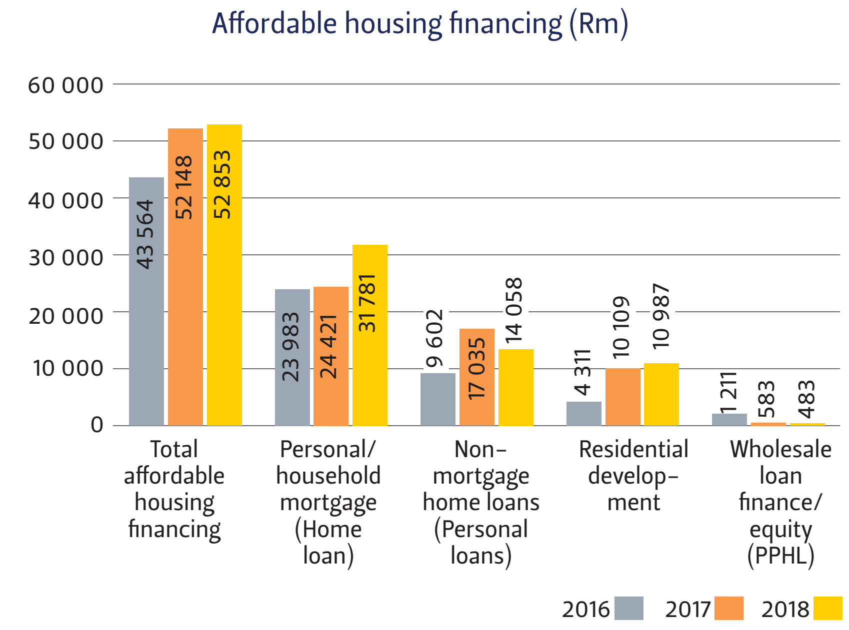
- This graph incorporates data from Absa, FirstRand, Nedbank and Standard Bank. Investec and Capitec have no exposure to black agricultural financing.
- The banks' balance sheet exposures to black farmers rose 41% on the back of significant increases in financing by Standard Bank (862%, albeit off a low base), FirstRand (40%) and Absa (23%).
- Exposure to EMEs and QSEs increased sharply at the expense of generic companies.
- EMEs accounted for more than half of banks' advances to black farmers.

Black small and medium enterprises



- Absa, Investec, FirstRand, Nedbank and Standard Bank are included in this category.
- Banks' balance sheet exposure to black SMEs jumped 13% to R28.8bn, with EMEs accounting for the lion's share of that increase.
- Outstanding loans to QSEs declined 22%.
- FirstRand and Investec increased their exposure to black SMEs by 32% and 94% respectively, while Nedbank's exposure of R13bn remains the highest.

Affordable housing financing



- Aggregate data of large banks included: Absa, Capitec, FirstRand, Standard Bank and Nedbank. Investec has no exposure to the affordable housing market.
- Balance sheet exposure to the affordable housing market increased slightly as growth in mortgage loan books and residential development loan books was offset by declines in non-mortgage home loans and wholesale loans.

Stepping into the gap

Helping people buy homes is one of the most important roles banks play in uplifting society. Unlike work done by their foundations and corporate social investment, banks for a long time looked at this as an operational matter rather than as a powerful means through which they could contribute to transformation.

Banks were advancing home loans to previously disadvantaged individuals well before the FSC guidelines for affordable and "gap" housing financing were published in 2017.

The code requires banks to provide funding/loans for affordable housing for consumers who earn a gross monthly income between R3,500 and R23,300.

What's worth noting is how the big five who offer home loans have improved their systems to better incorporate the qualifying criteria for the Finance Linked Individual Subsidy Programme (FLISP). FLISP is a government subsidy for low-income first-time home buyers, so can substantially improve buyers' ability to become homeowners. FLISP is now worked into their affordability assessment models to boost home loan lending to low-income earners who do not qualify for RDP houses. Not all banks report their share of home loans linked to FLISP, but Nedbank, which has granted more than 30% of all FLISP-related loans, has paid out approximately 3,000 subsidies to date. Absa provided home loans totalling R42m through the FLISP programme in 2018 alone.

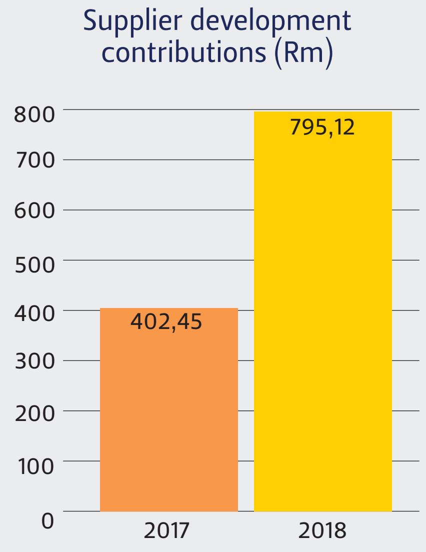
Capitec has stepped in to serve the part of the population who might not qualify for FLISP or traditional bank home loans. In its area of unsecured credit, the bank had granted over R3bn in personal loans by end-FY2019 for purchase, extension or improvement of properties. Because Capitec is now able to offer interest rates from 12.9% on personal loans – rates which were previously only accessible to people applying for secured credit – the bank says it has seen more customers earmark personal loans for housing improvements or low-cost housing purchases.

FNB's Affordable Housing Insights report shows that the affordable housing segment has displayed resilience to the depressed property market conditions.

There are many factors that this can be attributed to, including the fact that many purchases in this market segment are cash transactions driven by buy-to-let investors. But banks' increased involvement in the "gap market" – properties priced between R250,000 and R500,000 – also boosted activity. Research by the Transaction Support Centre, a pilot project in Cape Town aimed at formalising trade of RDP houses, showed that banks' involvement, through the provision of mortgages, stabilised property prices in this segment as houses sold for cash or through informal transaction fetched far lower prices.

Supplier development contributions

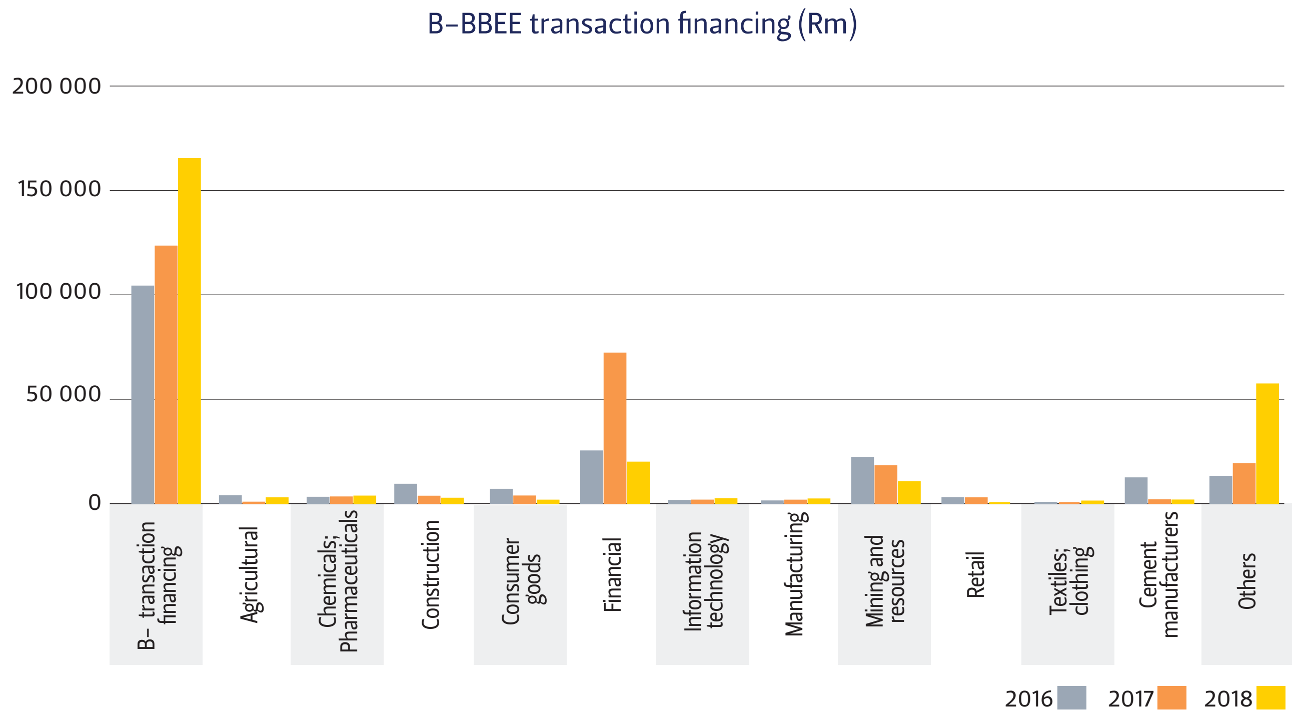
- This element was first introduced in 2017. Prior to that, related spending was accounted for under enterprise development.
- Banks have a target of contributing an equivalent of 1.8% of their net profit after tax towards supplier development.
- Banks' contributions for 2018 nearly doubled to R795m from R402m, driven by growth from the likes of FirstRand (up R220m – the bank started tracking this element in 2018); Absa (up R48.3m) and Capitec (up R32.4m).



Enterprise and supplier development is a tool that banks are using to groom black-owned businesses to qualify for a big share of their procurement expenditure. The strong growth was driven by the likes of Standard Bank which hosted 109 suppliers in its ESD programme in 2018.

An interesting trend in this area is the birth of in-house ESD programmes by players such as Nedbank. It shows that banks are starting to view ESD as a business opportunity rather than another compliance hurdle and this approach is producing measurable results. Since Nedbank decided to move ESD in-house in 2015, its allocation of procurement spend to black-owned businesses has increased to 24,4% from 14,9%.

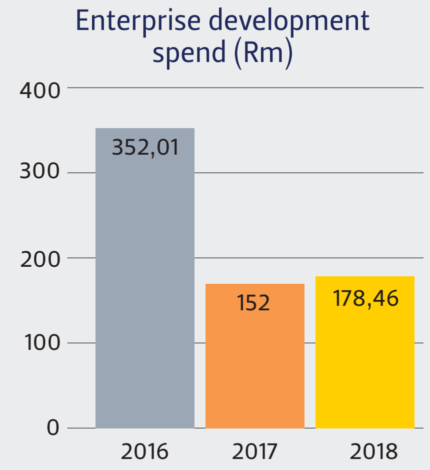
B-BBEE transaction financing



- BEE transaction financing tends to be volatile from year to year as large transactions can lead to significant changes in total values.
- Banks' balance sheet exposure to BEE deals stood at R164bn, 34% higher than the previous year.
- Banks' exposure to the financial services sector declined markedly. However, the sector remained the largest recipient of BEE transaction funding with over R19bn, followed by mining and resources with about R10bn.
- Discrepancies in figures between this report and last year's are due to some technical changes: one bank changed its verification agency, which brought in a different calculation method, while another bank changed its base year. Eight banks submitted data last year compared with six this year.

Enterprise development financing

- Banks have a spending target of 0.2% of their net profit after tax on enterprise development, which includes funding of new businesses and small businesses to increase scale and capabilities.
- A significant drop in expenditure on enterprise development between 2016 and 2017 is most likely a result of changes in the codes. Prior to the gazetting of the FSC Code in December 2017, banks were required to track their expenditure on enterprise development only. Banks are now required to track their expenditure on three elements: procurement, enterprise development and enterprise supplier development. These changes may have caused a significant drop in enterprise development figures as some of it is now being reallocated to procurement and supplier development.
- Banks' spending on enterprise development increased 18% between 2017 and 2018, with most major banks having increased the expenditure in this category.
- Discrepancies between this report and last year's are due to the fact that last year 12 banks reported figures in this category against 17 banks this year. Further differences were caused by the exit of two banks and entry of four into the sample.



Financial inclusion

One of the transformation goals of the financial sector is to make financial services more accessible to everyone. To achieve this, the sector has committed to delivering certain services to the previously unbanked and underserved segments of the population.

The established retail banks, despite challenges presented by legacy systems and the costs of running brick-and-mortar branches, have found ways to make great strides towards increasing greater access. Some have launched new entry-level bank accounts that either charge no monthly fees or subsidise the fees by giving customers monthly data, among other things.

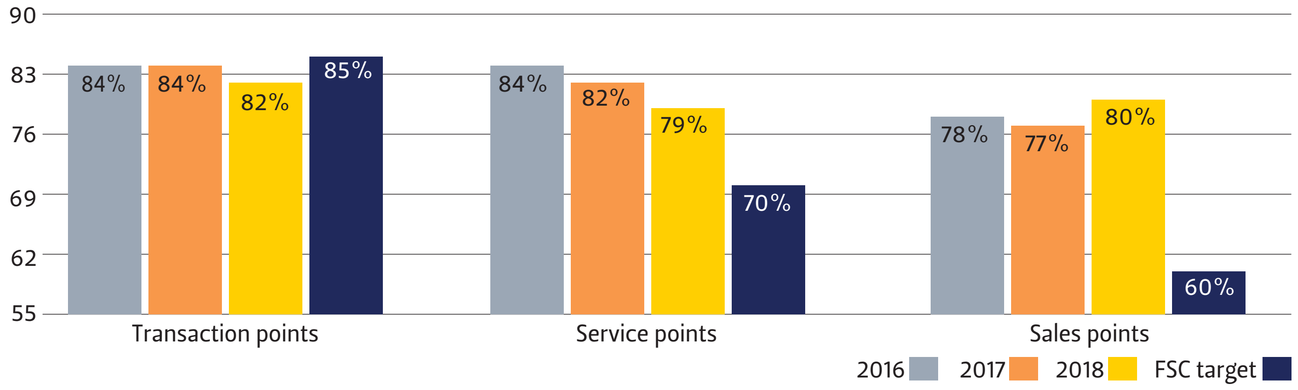
Progress on this element is measured on three key aspects: geographic reach, electronic access and product-related access. We present the major retail banks' scores on each of these below.

Geographic access

Geographic reach assesses penetration into low-income markets defined as those where 50% or more of households fall in the LSM 1-5 categories.

Progress on geographic access is measured on three points of representation: transaction points, service points and sales points.

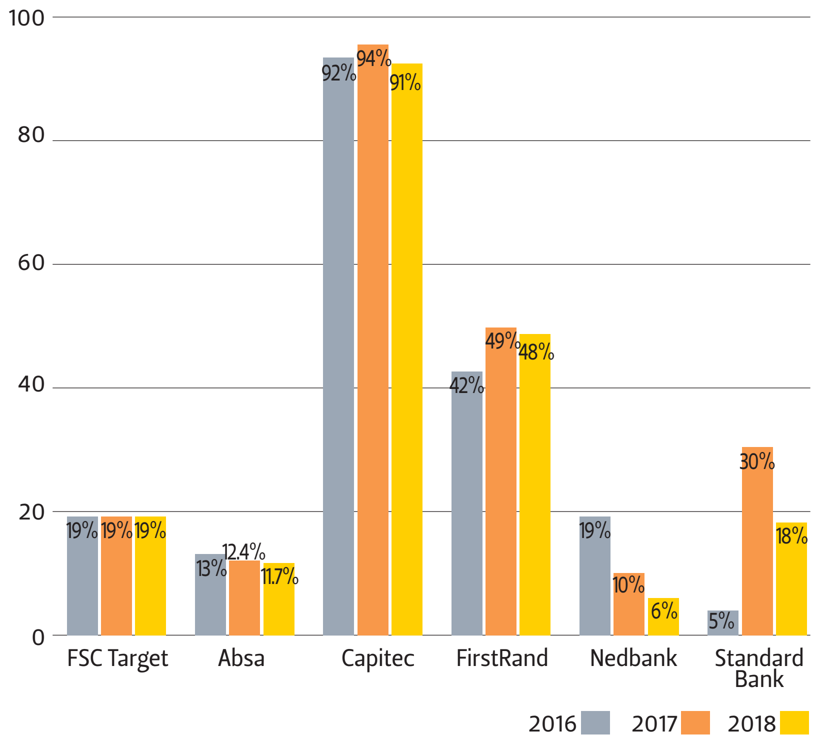
Transaction points are points at which customers can take cash or make a purchase from their accounts. Service points are points where a customer can reset a pin, execute money transfers, get a statement or initiate account queries. Sales points are points at which customers can replace a card, deposit cash into their accounts or acquire a transaction account, a funeral policy, a savings account or a loan.



- The banking industry's performance on service points and sales points is largely ahead of sector targets.
- In contrast, achievements on transactions points lag the sector target and have declined over the three years under review.

Electronic customer infrastructure access: population penetration

- Here the focus is on expanding access to services such as internet banking and cellphone/telephone banking, or any new electronic product and/or technology, for account holders who earn less than R5,000 a month (starting from 2017 and escalated by inflation).
- Similar to geographic access, electronic access is measured at industry level but with agreed targets per individual organisation. The sector has set a target of reaching 19% of the target market.
- Banks' electronic penetration within low-income groups is still low and all banks reported declines on this measure between 2017 and 2018.

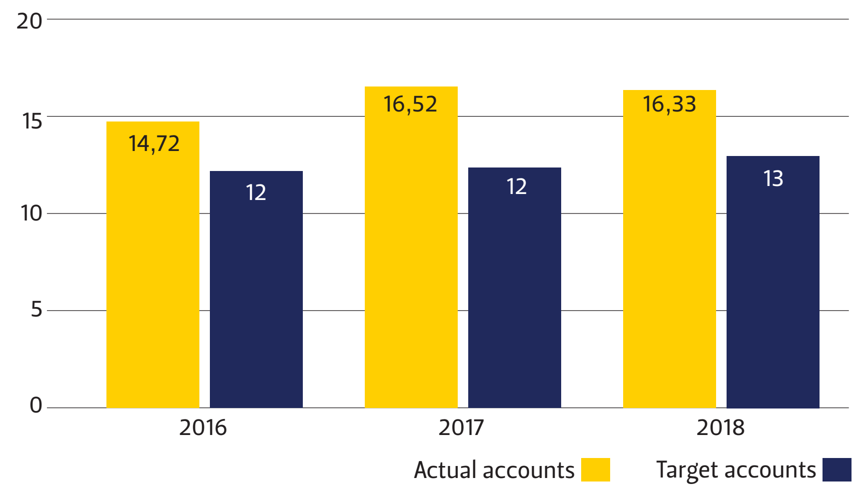


Product access

This element is measured according to the number of accounts with activity within the last 180 days, based on the level of conformity allocated by the Financial Sector Transformation Council.

Banks remain well ahead of the targets on this aspect. However, there was a slight dip in the number of qualifying accounts between 2017 and 2018.

Number of active accounts for qualifying products (millions)



Trying to keep it simple

Bank fees and access points are extremely important in the debate about transformation in a country where the FinMark Trust Finscope survey found that although 80% of consumers had bank accounts in 2018, many use them only as a type of post box, withdrawing funds as soon as they come in.

Finscope's research also found that more people are moving their savings to the informal sector.

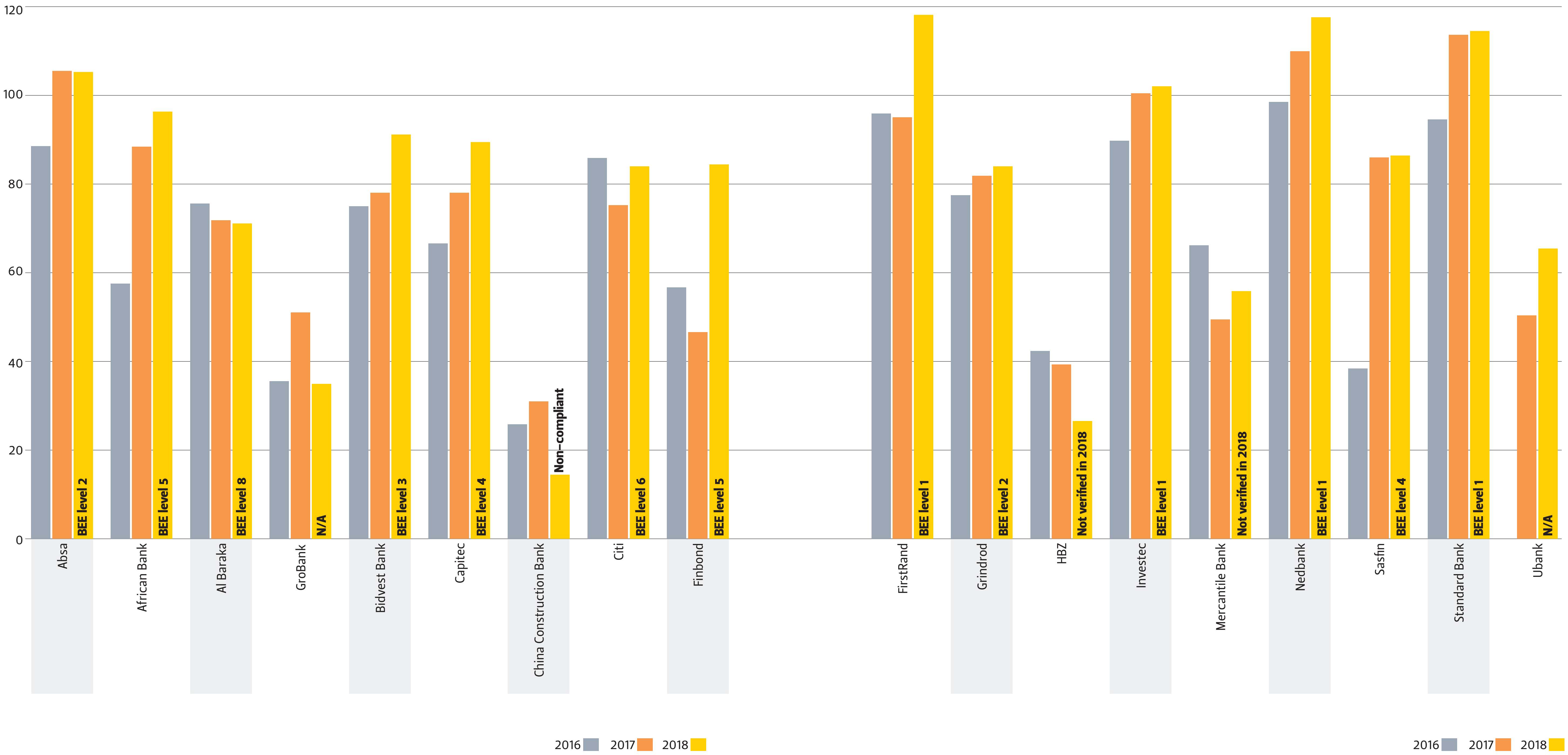
Banks have come to realise that costs, access and complicated product structures contribute to this trend of low-income consumers not keeping their money in the banks. As a result, many have tried to find simpler solutions that work better for the entry-level market.

Two examples are the conversion of FNB's e-Wallet into a bank account in 2018 and the addition of a "wallet" into Standard Bank's Instant Money product, allowing people without bank accounts to use it as one.

Improving access is one of many areas in which banking changed to benefit communities in 2018, the period under review. The 2016-2017 transformation report published last year showed how banks were already shifting from looking at transformation as a policy and compliance issue to viewing it as a catalyst for growth. In 2018, retail banks continued to uplift communities beyond what is required of them by the FSC targets.

Black economic empowerment scores

- Most banks improved their black economic empowerment scores, based on the Financial Sector Code scorecard.



B-BEE recognition levels		
B-BBEE status	Qualification	B-BBEE recognition level
Level one	≥ 100 points	135%
Level two	≥ 95 but < 100 points	125%
Level three	≥ 90 but < 95 points	110%
Level four	≥ 80 but < 90 points	100%

B-BEE recognition levels		
B-BBEE status	Qualification	B-BBEE recognition level
Level five	≥ 75 but < 80 points	80%
Level six	≥ 70 but < 75 points	60%
Level seven	≥ 55 but < 70 points	50%
Level eight	≥ 40 but < 55 points	10%

Beyond scorecards

Banks are increasingly striving to make a national impact through the initiatives they fund

Outside of their core operations and beyond the initiatives linked to BEE scorecards, the banks contribute massively to socioeconomic upliftment – both directly and through their charitable and empowerment foundations. More and more, they are seeking to make a national impact through the initiatives they fund. There is also a welcome trend emerging of collaboration – between banks and other big companies – to increase the effectiveness of their initiatives, both on the ground, making a difference to people's lives, and at policy level.

A good example is the National Education Collaboration Trust (NECT), formed in response to government's call for collaboration to accelerate the pace of national development. It aims to contribute to achieving the education targets set out in the National Development Plan. FirstRand, Absa, Nedbank, Standard Bank and Investec are all partner organisations – along with numerous other corporate entities.

Capitec promotes such collaboration. CEO Gerrie Fourie says: "We believe that through effective, collaborative efforts between the private and public sector we can achieve the tasks before us. We must work together to sculpt and refine the regulation and policies that govern transformation in South Africa. This will help to ensure we are as effective as possible."

Each of the big six banks run learnership programmes for their employees to meet regulatory requirements but they also offer learnerships to external candidates and run graduate programmes to achieve their internal skills targets.

There are numerous noteworthy initiatives. Absa and Investec were among the five corporations that co-sponsored the start of the Youth Employment Service (YES), launched by President Cyril Ramaphosa in March 2018. Investec partnered with 11 organisations to host 1,200 unemployed youth under the YES programme and further donated R2m towards the establishment of the first YES hub in Tembisa, Gauteng.

> *"Through effective, collaborative efforts between the private and public sectors we can achieve the tasks before us"*

FirstRand launched its FirstJob programme in the same year, also in response to Ramaphosa's plea to corporate SA to open doors to youth who need work-based training. The FirstJob programme initially committed to creating work experience for 1,425 youths but by the end of June 2019, it had given an opportunity to 1,547 individuals. What makes it unique though is that the learnerships graduates are placed to cover scarce skills. Specifically, 10 skills the World Economic Forum identified as necessary for the fourth industrial revolution were incorporated into the programme, which the bank designed in partnership with a leading business school.

There has also been much progress outside of the review period of this report. Early in 2019, Nedbank sponsored 3,315 unemployed youth to complete 12 months of work experience training under the YES programme. This was the biggest intake to be sponsored under the YES programme at the time. And Absa's YES programme, implemented by development agency Catalyx in December 2019, will see the bank provide work experience to more than 3,400 youth who will be placed in over 100 organisations across seven provinces in 2020.

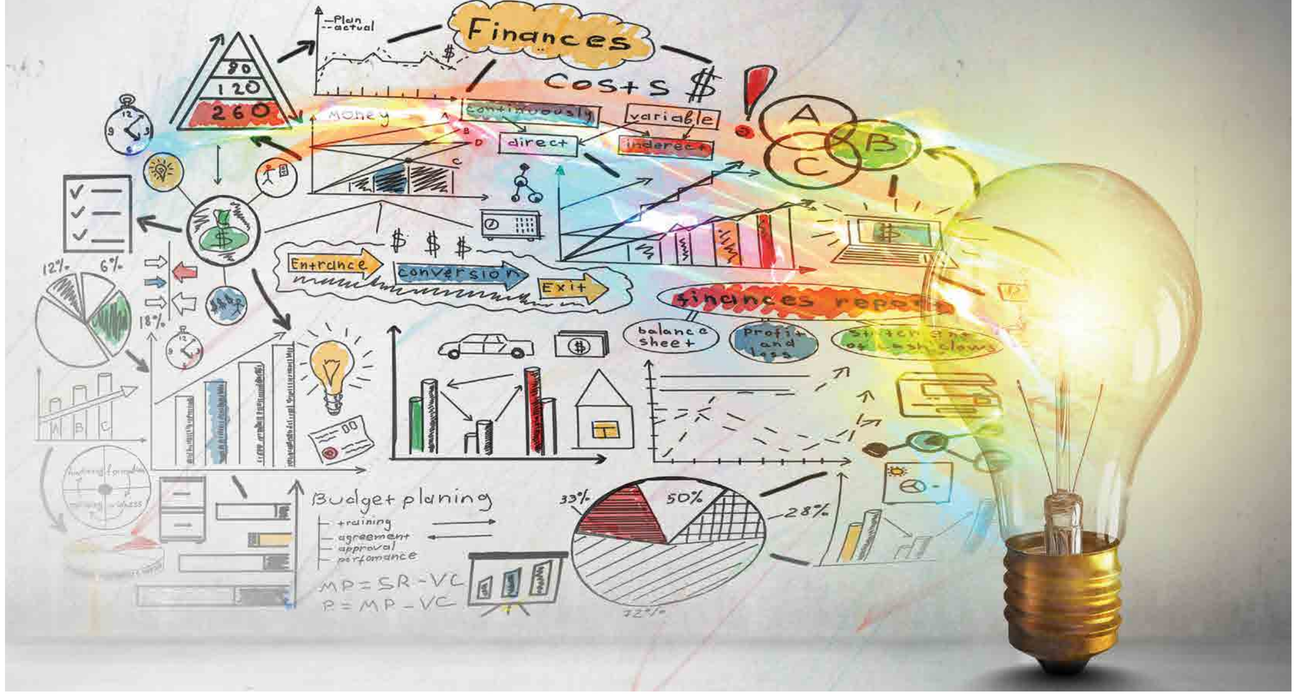
Each bank's foundation has its own focus area but education is a common underlying theme. Nedbank, for example, focuses on, among other things, supporting the implementation of the National Development Plan.

FirstRand's two foundations, the FirstRand Foundation (FRF) through policy advocacy and the FirstRand Empowerment Foundation (Fref) through the NECT, have been instrumental in improving educational systems for early childhood development. The FRF, through its support of ilifa Labantwana, a nongovernmental organisation focused on early childhood development, has achieved some successes in terms of influencing ECD policy, including a second year of compulsory early learning before school that kicks in this year. The FRF is also a major contributor to Isfap while Fref supports the NECT.

The Capitec Foundation focuses on maths tutoring, teacher development and school management development, among other things. The bank says elementary school staff and leadership remain key priorities in efforts to transform the education system. In 2019, 564 high school learners, 45 university teaching students, 63 in-service maths teachers and 199 principals and senior management teams were supported through the Capitec Foundation's initiatives.

Investec prioritises promoting six of the UN Sustainable Development Goals: quality education; clean water & sanitation; affordable & clean

> *Each bank's foundation has its own focus area but education is a common underlying theme*



energy; decent work & economic growth; industry innovation & infrastructure; and sustainable cities and communities.

CEO Fani Titi says Investec is trying to do more for empowerment, pointing out that Harvard Business Review last year illustrated how diversity yields quantifiable dividends in business. "Examples of this include having an inclusion and belonging strategy that aims to achieve a diverse workforce at all levels, thinking about unconscious bias and using our platform to champion awareness campaigns, such as women and LGBTQIA+ campaigns. We have focused on progressive people policies that live up to our culture so that you can thrive in our environment no matter who you are."

Standard Bank's Tutuwa Community Foundation is also heavily involved in educational upliftment, with a focus on youth. Its programmes incorporate the full education life cycle: early childhood development, making the schooling system more effective, tertiary education and supporting young people's transition to the work environment.

Absa, like other banks including FirstRand and Standard Bank, has shifted its approach from charitable giving towards community projects that make an impact in stimulating wider social and economic upliftment. It focuses on education and skills, enterprise development and financial inclusion.

Full details of the socioeconomic upliftment initiatives of each bank are far too extensive to cover fully here but what is clear is that they go well beyond the requirements of the B-BBEE scorecard. Indeed, Capitec's Fourie calls for recognition of such endeavours.

"The current scorecard and its implementation create challenges that hamper transformation at times," he says. "While the scorecard drives behaviour towards transformation, it only motivates for the elements included. As a result, all the initiatives that drive transformation, but are not in the code, receive no recognition." He argues that this could encourage companies to overlook many important initiatives.

Another problem, he says, is that the scorecard measures expense instead of outcome, "which means that digital learning, which has proven to be a highly efficient interactive means of learning, scores less points due to its cost efficiencies. Effective collaboration between the private and public sectors will help to address and further smooth out the policies and procedures."

"While the scorecard drives behaviour towards transformation, it only motivates for the elements included."

Recognition of all initiatives that are now outside the scorecard would certainly validate the "broad-based" part of black economic empowerment. Without doubt, however, South Africa's banks – along with other corporate entities – are making a marked difference in the country, be that on the ground at individual level in providing nutritional school breakfasts and scholarships for underprivileged children or at national policy level in improving educational systems and access to them.

Banking Association South Africa
3rd Floor Building D
Sunnyside Office Park
32 Princess of Wales Terrace
Parktown
2193

www.banking.org.za