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SUMMARY

BURUNDI'S FINANCIAL SECTOR

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1. BACKGROUND.

The recent macroeconomic developments had three major impacts on the financial sector: (i) There has been a largely unproductive excess of liquidity in Burundi's financial system until 1987. This situation was changed drastically by a surge in consumer imports in the middle of 1988, with a sudden shrinkage of the deposit base and liquid reserves of the financial system, problems attenuated by (a) foreign loans (IMF/IBRD) and (b) Central Bank lending thus creating serious problems for the entire banking establishment. (ii) The number of posted interest rates has been reduced from 94 in August 1986, to 3 in January 1989, rendering the credit operations less complex and more manageable. (iii) After abolishing the BRB a priori credit authorization system, theoretically there is now no limit to lending activities.

2. FINANCIAL ESTABLISHMENT.

Burundi's financial establishment comprises 7 banking institutions and 11 non-banking ones. The banking sector include the Central Bank, two development banks and four commercial banks. The non-banking sector includes one holding company, three deposit taking institutions, three insurance companies, a social security fund, a rural credit cooperatives system and two institutions mobilizing credit for coffee campaigns.

La Banque de la République du Burundi (BRB) was established by an Act of April 9, 1964 and assigned the typical function of a modern central bank by virtue of a January 3, 1976 Act: the design and implementation of the monetary policy, the issuing of currency, the management and control of credit, the management of foreign reserves, the management of the regulatory policies concerning the financial system, and the accounting and auditing of the Treasury. In addition to its normal functions, the BRB runs various services for banks such as a clearing house and a credit risk coordinating unit and provides banking services for public sector companies.

The two development finance institutions, Banque Nationale de Développement Economique (BNDE) and Société Burundaise de Financement (SBF), continue the expansion of credit to the economy under competent management and with sound portfolios condition. BNDE is Burundi's principal development finance institution and continues to receive strong international financial support. SBF provides term loans for housing, commercial and transport equipment.

In the commercial banking sector, there have been recent significant changes. Banque Belgo-Africaine-Burundi (BBAB) merged with Banque Commerciale du Burundi (BANCOBU) in 1988, leaving the sector with two well-established commercial banks: BANCOBU and Banque de Crédit de Bujumbura (BCB). In the second half of 1988, a new commercial bank, the Meridien Bank of Burundi SARL, started operations with an unexpectedly high participation of local investors in its equity base (48 percent). A fourth commercial bank, the Arab Burundi Bank of Commerce and Investment which started operating in 1989, faces now an uncertain future since the Saudi promoter apparently has second thoughts about his initial commitments.

The insurance sector. The total domestic insurance market is estimated at about 1.3 billion BuF. This market is now shared by two companies: Société d'Assurance du Burundi (SOCABU) 1 million BuF and a new company, Union des Compagnies d'Assurances et de Re-assurances (UCAR) 0.3 billion BuF. There is now strong competition between these companies for market shares. A new company, UCAR, ended the State monopoly of the insurance business. Again, the company was created with an unusually high participation of local private investors in its equity base (60 percent).

The non-banking sector witnessed a spectacular expansion of the Savings and Credit Rural Cooperatives, the COOPECs system. Within four years of operations, the system created 56 cooperatives in the poorest market segment of the economy with over 68 thousand members, deposits of 330 million BuF and a loan portfolio of over 4100 small loans totaling over 132 million BuF. It should be noted that the level of voluntary deposits under the COOPEC system is significantly higher than under the previous compulsory savings scheme with CADEBU's monopoly.

In the second half of 1988, a portfolio guaranty institution, the Fonds National de Garantie, started operations providing loan insurance of last resort to borrowers with insufficient collaterals to qualify for conventional banking loans. The institution needs urgently technical assistance in the area of credit risk analysis and portfolio management.

Among the three deposit taking institutions, Caisse d'Epargne du Burundi (CADEBU), whose management is very weak and whose financial statements remain unaudited since 1984, continues to create distortions in the financial system through a compulsory savings scheme involving all salaried persons, merchants, artisans and liberal professions. Another institution in the same category is CAMOFI (Caisse de Mobilisation Financière).

3. LEGAL AND ACCOUNTING FRAMEWORK.

The legal framework remains inadequate for the needs of a modern banking system. The Central Bank's control of the banking establishment is in the form of three financial ratios whose method of computing is conceptually weak. The standards of accounting are left to the discretion of individual institutions. Certification of accounts suffers from the absence of specific auditing rules and instructions defining the standards of professional competence, auditors' rights and their liabilities vis-a-vis their clients. There persist serious dichotomies between the accounting practice and the Internal Revenue Services often arbitrary views concerning the interpretation of financial statements.

In essence, the tax authorities have their own independent views on what constitutes legitimate income and admissible business expenditures. Some of these views are accepted by custom and are included in the Tax Code, others are arbitrary ad-hoc rulings of individual tax inspectors. In some instances, the tax authorities impose equally arbitrary and unrealistic ceilings on legitimate business expenses. Examples include tax penalties and reserves for bad debts, which are considered as taxable income, and compulsory membership fees in the Chamber of Commerce, which are considered as non-deductible expenses. Moreover, business expense accounts are limited to 150 thousand BuF per enterprise, while accounts receivable and bad debts can be written off only upon presentation of court judgements pronouncing either the debtor's insolvency or his death, which is a complex and time-consuming legal process.

All this increases the costs and risks of doing business in Burundi, with particularly harsh impact on those wishing to initiate small and medium enterprises.

4. COLLATERALS AND GUARANTIES.

All bank lending is backed by some form of collateral, the mortgage of borrower's real estate property being the prevailing form. The enforceability of guaranties is legally difficult and time consuming. The situation became legally more complex with the introduction in January 1987 of the revised Code Foncier. Under this code, the Treasury has a priori claim with no ceiling on all guaranteed property even when the State has not previously laid claim to the mortgage. Legally, the State pre-emptive right is equivalent to lending without guarantee. However, it is believed, the real problem of guarantees does not reside in the legal aspects but in a sharp conflict between the jurisprudence and a strong socio-cultural tradition which rejects the entire "imported" legal theory governing the lender's claims. The importance of expanding and strengthening the portfolio guarantee scheme (FNG) should be viewed therefore from this perspective.

5. CREDIT TO SMEs.

No evidence was found of any financial institutions' discrimination against "bankable" SME projects. As a matter of fact, the concept of loan classification by the relative size of enterprise does not fit the established banking practice. The bankers make distinction between personal loans and business loans which in turn are classified by purpose: capital investments, working capital loans, etc... In the final analysis, the bankers' only concerns are the risk factor of the loan and its profit making potential, whatever the size of the loan may be. From a policy and programmatic perspective, it is certain that the risk factor may be attenuated either by the quality of the borrower's collateral or the availability of a loan guarantee scheme willing to insure the lender against a bad credit risk whenever the collaterals are deemed insufficient.

a. Commercial Banks. About 50 percent of revenues of the established commercial banks come from operations involving documentary credit transactions not posted on the Balance sheets. Short-term lending defined as that extended for up to two years in the predominant type of lending among Burundi's commercial banks. The proportion of short-term lending could be estimated in the range 85-90 percent of the portfolio, with the remaining consisting of medium-term loans defined as that extended for 2-7 years. The commercial banks do not extend any long-term credit facilities. About 30 percent of short-term credit facilities involve coffee campaigns.

Term-loans are disbursed almost exclusively to well-known clients and the capacity of commercial banks to appraise such loans is adequate. Credit analysis, although emphasizing the personality of the borrower, covers such aspects as evaluation of market potential, sales forecasts, projected financial statements and cash flows, financial ratios, quality of the management and visits to the company. For large, well-known clients, disbursement is made directly to the beneficiary. For smaller or less-known clients and for foreign goods, funds are directly disbursed to the supplier or contractor, and disbursement and procurement conditions are thoroughly checked. No fees are charged to the borrower.

b. Development Finance Banks. It could be safely assumed that, so far, the local commercial banks did not consider the SME's ventures as their market segment and it is difficult to say whether these banks will change their marketing strategy in the foreseeable future. This is why this market segment was taken over by BNDE in 1967, and by SBF in 1982. So far, BNDE disbursed 20,640 loans whose total value was 8.4 billion BuF: an average of 938 loans per year.

The two Development Finance Banks institutions under consideration, La Banque Nationale pour le Développement Economique (BNDE) and La Société Burundaise de Financement (SBF) disburse short, medium and Long-term credits to qualified borrowers. Over 50 percent of SBF short-term lending involves financing the coffee campaigns. In the BNDE's portfolio this percentage is less than 20.

Both institutions have somewhat similar lending policies and procedures. Their credit analysis capacity has improved significantly since the unsatisfactory experience concerning the implementation of IDA's Cr 731-Bu, which ended with the bulk of financing disbursed to a few large companies and eighteen SME projects turning out unsuccessful. Presently, all loans are subject to comprehensive risk analysis by competent and professional staff. All screened loans of less than 500 thousand BuF must then be approved by a management directorate. Loans exceeding this cap must be approved, in addition, by the Board of Directors. Loans over 10 million BuF must be submitted to a Credit Committee. This screening and filtering process insures a certain quality of loan portfolios: the non-performing loans represent about 10 percent of the total. Small processing fees are charged on the borrower. BNDE estimates that out of 100 applications, about 30 have a chance to enter its project pipeline, about 15 to be considered as bankable projects and 10 approved by one of its three credit review boards.

BNDE is the only development finance institution with foreign exchange resources and lines of credit provided by international development assistance organizations. About 85 percent of these resources are for specific operations or have specific conditions concerning procurement or type of projects. BNDE lending operations have been supported by concessional lines of credit from: Caisse Centrale de Coopération Economique: 15 million FF; Kreditanstalt für Wiederaufbau: 3 million DM; European Investment Bank: 3 million ECU; International Development Association: 3.4 million U.S. dollars; African Development Fund: 4 million US dollars equivalent. In addition, BNDE negotiated three new lines of credit: Caisse Centrale de Coopération Economique: 30 million FF, European Investment Bank: 4 million ECU; Belgian Administration for Development Cooperation: 50 million FB.

c. APEX. In parallel to the above, the International Development Association allocated 7.2 million US dollars to an APEX line of credit through a second-tier rediscounting window at the Central Bank to all participating financial intermediaries. This line of credit is reserved exclusively for subloans of less than 300 thousand US dollars to all qualified SMEs. It is the mission's understanding that Caisse Centrale de Coopération Economique intends to provide APEX-type credit facilities of 50 million FF. The technical assistance components include funding of experts and training in BNDE by international donors and funding of assistance and training for the Small Enterprise Bureau within the Chamber of Commerce by the World Bank with other donors' participation.

d. Guarantee Fund. Finally, the Government of Burundi established in 1988, Fonds National de Garantie (FNG) to provide lenders with credit risk insurance for qualified SMEs. The Fund has in its pipeline 17 requests covering 43 percent of the total of 43 million BuF solicited credits. The Fund needs urgently professional assistance to set up its operations on a sound basis: one credit risk analyst and one portfolio management specialist. Fonds National de Garantie. For convenience sake, this loan portfolio guaranty institution could be considered as an insurance company. FNG was established as a limited liability company with a capital of 300 million BuF by a special Decree of 14 June, 1988, to insure high-risk loans or loans without sufficient collateral. The ownership structure of the subscribed capital is the following: the Government of Burundi: 70.67 percent; local banks: 12.66 percent. The FNG has about 17 loans in the pipeline with the following average loan characteristics: Project cost: 2.5 million BuF; loan request: 1.9 million BuF; leverage: 76 percent; terms: 4.1 years; grace period: 1.3 years; guarantee requested: 1.1 million; risk coverage: 58 percent of the loan requested.