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Booming sector needs African solutions

By Chris Ogden

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A decade ago, Africa's financial services landscape was virtually dormant. But the rise of the middle class has generated staggering growth in the sector.

According to the World Economic Forum, financial services are considered one of the continent's biggest economic growth areas. This increase is in part due to financial sector development being on the agenda for policymakers (aside from profitable opportunities for investors, which, in turn, has the potential to transform the lives of millions of people across the continent.

For instance, access to insurances, secure banking, and credit for emerging entrepreneurs can provide jobs and a steady income, thereby alleviating poverty.

Enabling environment

Policy reforms in the past decade have created an environment conducive to financial sector development, and governments have made progress in introducing much needed regulatory frameworks, information systems and regulatory institutions – all with the purpose of enabling and facilitating further growth.

Transformation, however, does not happen quickly. Most African countries still lag behind the rest of the world when it comes to the adoption of banking and insurance products.

The Organisation for Economic Co-operation and Development (OECD) suggests that financial services typically make up 20-30% of total service market revenue and about 20% of the total gross domestic product in developed economies, this creates substantial opportunities for sustainable growth, which will prove profitable for investors who are willing to take on some risk and are innovative in their approach to financial services. Success depends on the ability to create new products, and creating novel ways to deliver these to the target markets across Africa.

Africa's unbanked

The banking sector in many sub-Saharan African countries has demonstrated significant growth in recent years. A contributing factor is the rapid rise of pan-African banks. The institutions that have made the biggest impact are indigenous, and come from countries on the continent with well-developed financial markets. For example, Ecobank (with its roots in Togo) has the biggest presence in Africa, with banking services in 36 countries, the United Bank for Africa (from Nigeria) operates in 19 countries, and Standard Bank has a presence in 20.

Despite strong growth in the sector, a significant proportion of the population does not make use of formal financial services. The reach of commercial banks, in terms of branches and ATMs, remains well below the global average, therefore financial services need to become innovative in reaching consumers.

Insurance markets

The insurance market, on the other hand, is underdeveloped. South Africa accounts for almost 80% of all premiums in the sub-Saharan region, and the country has an insurance penetration rate (the total value of insurance premiums as a proportion of GDP) of about 13%, well above the developed world average. Of the rest, Kenya has a penetration rate of 3%, while Nigeria, in comparison, is about 0.3%, even though it is Africa's largest economy.

Low penetration is mainly due to lack of awareness and people being too poor to afford insurance. With most people still just struggling to meet their basic food and other day-to-day needs, true penetration of the market is still a long way off.

It's for this reason that insurance companies in Africa traditionally target the richest 5% of the population. Even in South Africa, with its well-developed insurance market, less than 30% of low-income adults have insurance.

Of course, other key determinants in any particular country are income levels, political stability, the depth and sophistication of the financial sector, the level and volatility of inflation, culture, and the capacity of companies to innovate.

The markets, however, are gradually changing. A few countries already have relatively high-income levels, and therefore sizable middle classes, which is spurring the development of insurance products, and the growth in the volume of insurance premiums.

The continent's uninsured presents a myriad of opportunities for foreign and African insurance companies, but also for microinsurers, to sell low-cost products to the lower income bracket.

Mobile money

Additionally, the rise of mobile money has added a new dimension. Buying insurance using a mobile phone is an exciting growth area as it is an affordable option, especially in remote regions, to access products. The successful rollout of such goods or services, however, does require the cooperation of telecommunications companies, banks, and insurers, which can prove challenging in developing nations.

With rising incomes and a rapidly growing middle class, an increasing number of financial institutions have woken up to the potential that lies within Africa’s 1.2bn consumer base. These financial institutions have also been forced to reconsider the way in they do business and go beyond traditional banking products to shape solutions that fit African consumers’ ever-changing, financial needs.

ABOUT CHRIS OGDEN

Chris Ogden is CEO at RubiBlue

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