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INSTITUTE OF CHARTERED SECRETARIES AND ADMINISTRATORS IN ZIMBABWE

THE 2017 EXCELLENCE IN CORPORATE GOVERNANCE AWARDS

THE THEME OF THE AWARDS

PROMOTING GOOD CORPORATE GOVERNANCE FOR SUSTAINABLE ECONOMIC DEVELOPMENT

Mr. Denys Denya, Executive Vice-President

November 2017

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Mr. Denys Denya, Executive Vice-President

The African Export-Import Bank

Dr. Paradza Paradza, President of ICSAZ,

Mr. Farai Musamba, Chief Executive Officer, ICSAZ

Fellow Members of the Institute

Dear Chief Executives and Leaders of the Business Community,

Dear Representatives of the business community,

Distinguished Guests,

Ladies and Gentlemen,

I would like to thank the leadership of the Institute of Chartered Secretaries and Administrators in Zimbabwe (ICSAZ) and particularly its President, Dr. Paradza Paradza and its CEO, Mr. Farai Musamba, for inviting the President of the African Export-Import Bank as the Guest Speaker at the 2017 Excellence in Corporate Governance Awards event this evening. I stand before you tonight representing Dr Oramah who couldn't be with us due to unavoidable circumstances.

As a Chartered Secretary myself I feel greatly honoured to be here and to serve as Guest Speaker especially for a leading institution which has been promoting excellence in corporate governance in support of economic development in Zimbabwe for more than four decades, and one of the most vibrant of the 9 Divisions of the Institute of Chartered Secretaries and Administrators at the global level. In a report of the Institute's most recent Council Meeting held in London last month, the leadership of the Council is very complimentary on the Zimbabwean Chapter, and I quote:

"*Zimbabwe continues to face the greatest challenges of all our 9 divisions, with a deteriorating economy and cash and foreign exchange shortages. Despite this, the Division continues to enjoy a vibrant and engaged membership, as evidenced by a successful and well attended annual conference in September 2017*."

Afreximbank is honoured to participate in this event because we share a mutual commitment towards the promotion of excellence in Corporate Governance in African institutions. As some of you know the African Export-Import Bank launched its Corporate Governance and Customer Due Diligence Forum to raise awareness and promote good governance across the continent in 2015 and has trained hundreds of officials in sovereign and corporate entities since then.

"**Promoting Good Corporate Governance for sustainable Economic Development**" is the theme of the Award Ceremony this year. The theme is very germane and timely, and I would like to thank the organizers of the Award Ceremony for their choice. In fact, at a time when the last Council of the Institute of Chartered Secretaries and Administrators overwhelmingly voted to introduce "**Chartered Governance Professional**" as a new programme to complement "**Chartered Secretary**" last month, the choice of the theme could not have been timelier.

Distinguished Guests,
Ladies and Gentlemen,

In a world of increasingly competing interest, it is important to stress that success requires that all stakeholders work together towards these common goals: (i) sustainable growth of the bottom line in the corporate world; and (ii) sustainable economic growth and employment creation in the public sector, creating a bigger cake so all can feed. Good governance enables the achievement of such goals as it speak to how resources, policies and procedures should be organized for the attainment of objectives, whatever the organization/enterprise's objectives are. Some will call such an aspiration a team spirit or teamwork. But this reference works if all stakeholders involved are operating on the same understanding.

However, many a time stakeholders are not all operating on the same plane or have different lines of accountability, then one needs corporate governance as the framework that will balance the overall interest of the company's many stakeholders, such as shareholders, management, customers, suppliers, financiers, government and the community.

Balancing the interests of these different stakeholders is the main objective of corporate governance and it has become axiomatic that striking the right trade-off to effectively balance the interests of all stakeholders is growth-enhancing, and doing so over time and in a sustainable manner is key to sustainable economic growth. Hence the relevance of the theme in a region where achieving robust and long growth spurts has been a real challenge.

The survival of corporate and sovereign entities which individually contribute to aggregate output expansion, and therefore economic growth at national level depends on the quality of corporate governance. Weak or bad corporate governance environments result in the failure of large corporations to abide by best practice corporate governance standards which can be fatal, highly consequential, and even systemic in a number of particular sectors, most notably in the financial services industry. The much reported case of Eskom in South Africa is instructive.

Another illustrative example is the recurrent challenges and difficulties which have afflicted the Zimbabwean banking sector since 2004, the year Trust Bank (the face of local Wall Street) one of the most trusted and innovative financial institutions went under. Several other indigenous banks also collapsed , including United Merchant Bank, Universal Merchant Bank, Genesis, Royal Bank, FNBS, Zimbabwe Building Society, Barbican, Interfin Merchant Bank, Kingdom Bank and Renaissance

Merchant Bank. And government , through the RBZ, attempted to rescue some of the failing banks by bundling three of them (Trust, Barbican and Royal) into the Zimbabwe Allied Bank Group (ZABG), which was born out the Government Troubled Bank Resolution Act. This ultimately was not successful. It can be argued that Ultimately the cascade of bank failure and collapse of financial institutions set the Zimbabwean economy on a path to a long-term crisis and recession given the long lasting nature of financial crisis.

In effect, the costs of what has been a rather long crisis have been significant, not just for the government acting as the lender of last resort on behalf of all Zimbabwean taxpayers, but also for individuals and small depositors. These failed banks accessed billions in liquidity support through the Government Troubled Bank Resolution Act. At the individual level it has been estimated that depositors lost more than half a billion US dollars of their hard earned cash. Even with the existence of the Deposit Protection scheme, these failures resulted in net losses to poor households, most of whom continue to lose more confidence in the banking system. By reducing the purchasing power of these households, the crisis created by the banking system further lowered household consumption and growth prospects, keeping the country on a vicious cycle. More recently the increasing trust deficit in the banking system was exacerbated by the inability of depositors to withdraw cash from banks on demand even though a large proportion of deposits in banks has been in the form of demand deposits.

Ladies and Gentlemen, I am convinced that Poor corporate governance both at sovereign and corporate levels has been a major factor behind the banking crisis facing Zimbabwe. Some of the major contributing factors include: (i) regulatory forbearance, (i) fraud and insider transactions, (ii) laxity of regulatory oversight which allowed some banks to invest in highly speculative investment options, (iii) the use of more creative accounting rules in financial reporting, (iv) unmitigated investment in high-yield and high-risky investments, (v) high concentration of lending with a reliance on deposit with short maturities for funding increased risks, (vi) lack of transparency and accountability, and (vii) dereliction of duty on the part of the Board of Directors, which in some cases were made powerless by “shadow Directors”, those powerful shareholders whom personal gains and interests transcend the survival of the very banks they helped create.

It has been claimed that in the space of transparency and accountability space we have heard of financial institutions misrepresenting their financial positions and accounts to regulators, and some systematically engaging in overvaluation of assets, while still others refraining from disclosing the scale of non-performing loans in their statement of financial positions. In the realm of fraud and insider transactions we have the Reserve Bank of Zimbabwe reporting that as at December 2013 total insider loans in the banking sector were about US$175 million and of these 67% were non-performing loans. In one case we have a bank lending 69% of its deposit to its own shareholders and related parties and we are surprised by the ultimate outcome!

The Zimbabwean financial sector has been its share of poor governance and over time the economic and social costs of those institutional failures have been significant to the whole economy. In part reflecting the fact that banks and financial institutions play a major role in the process of economic development through financial intermediation. These can be significant for individual investors and depositors in case of outright bankruptcy and collapse of banks, especially in countries without Deposit Insurance providing a minimum coverage, but also for taxpayers and governments from fiscal channels.

That is why we salute the ICSAZ for honouring men and women tonight who have chosen to practice good corporate governance by discharging their stewardship function with excellence. Ladies and Gentlemen, Strengthening the corporate governance culture across industries and public entities has become critical for risk mitigation, but also for economic growth. In particular, with the increasing culture of shareholder activism good corporate governance is increasingly needed to assure business integrity and create the market confidence required to attract investors, and in the context of globalization corporate governance can actually enable corporations to circumvent the difficulties of accessing financing in their local markets and go global. As a Pan-African financial institution, Afreximbank has provided financing in hard currency to many clients at a time when they could not access forex in their home countries as a result of sustained deterioration in commodity terms of trade and increasing scarcity of forex.

However, in addition to promoting the growth of companies by easing access to finance, good corporate governance also promotes overall economic growth by fostering the culture of optimal allocation and effective deployment of resources in support of growth. Historically, fostering an environment that strengthens corporate governance disclosure and reporting has been a key driver of transparency at corporate levels.

Good Corporate Governance fosters the culture of independence and accountability not only at managerial levels, but also at the level of Board of Directors to strengthen oversight and the transition from “**passive Board of Directors**” to “**Active Board of Directors**”.

Sometimes the growth of corporation depends on incentive systems in place. In a delicate balancing act taking into account the interest of all stakeholders, growth can be promoted by fostering the culture of fairness and responsibility to incentivize staff. In some cases, corporate managers have gone as far as encouraging staff to own shares in the corporation.

So important and critical is corporate governance to growth and economic development, that the last few decades have been dominated by increasing attempts to globalize corporate governance standards. The recent steps taken by the Institute of Chartered Secretaries and Administrators (ICSA) to create two qualifying programmes, with one devoted to **Chartered Governance Professional** reflects the increasing importance of the subject.

Distinguished Guests,
Ladies and Gentlemen,

At this point, I would like to provide some reflections on the challenges of corporate governance in Zimbabwe, but also outline global best practices in some priority areas, most notably corporate governance practice disclosure, shareholder activism and public sector corporate governance.

Corporate Governance Reporting: Promoting and strengthening the culture of Corporate Governance practice reporting and disclosure has been recognized as central to the promotion of good corporate governance in Zimbabwe. I would like to reassure you that it is not a Zimbabwean or African problem but a global problem. Recently, attempts to disclose executive remuneration in the US and other leading economies by way of addressing stagnant wages in the middle-class and rising wage inequality have faced a lot of resistance. However, progress has been made in other dimensions of reporting, most notably in the area of integrated reporting, corporate responsibility and narrative reporting.

In Zimbabwe the deficit of disclosure is perhaps exacerbated by the absence of a framework for reporting or a disclosure regime for corporate governance issues in Annual reports. Moreover, even in the absence of such a framework good corporate governance reporting and disclosure is good corporate governance practice and should be encouraged especially for companies which are contemplating the option of raising equity investment to sustain their growth.

Perhaps the first goal should be to revise the 2015 version of the Zimbabwean National Code on Corporate Governance to provide specific guidance on corporate reporting and disclosure. Even then it is not guaranteed that all corporate entities will step up and systemically abide by the new code. At least it will provide the framework for consistency and for monitoring progress towards reporting. Eventually, rewards in the form of access to finance for the few corporations abiding by the reporting requirements could act as incentives.

Shareholder activism is another area where Africa has been lagging vis-à-vis trends in the rest of the world. How to move from a state of "*passive shareholder*" to that of "*active shareholder*" – what is also commonly known as Shareholder Activism. Many companies and corporations have collapsed just because of the passive nature and behavior of shareholders who are not using their rights to bring about social changes or shape major investment decisions by management perhaps by influencing the Board of Directors and Management.

The apathy of Zimbabwean shareholders and those in most other countries across the African continent is at odds with development in the rest of the world, especially in advanced economies, where “activist shareholders” are increasingly using their power as company owners to examine company financial reports, monitor executive remuneration, enforce good corporate governance and push for increased sustainability and transparency.

Globally, the number of shareholder challenges has increased dramatically rising from 520 episodes in 2013 to 758 in 2016, more than 45% increase. And around two thirds of these challenges were successful, double the rate of just about a decade ago, suggesting that activist shareholders are indeed strengthening the culture of corporate governance. Uber is a case in point.

There are a number of measures which can foster the culture of shareholder activism in the short term, including:

- Education and training of shareholders to help them transition from “***passive shareholders***” to “***active shareholders***”;
- The introduction of minorities’ rights like in the new companies Act in South Africa whereby minority shareholders with as little as 10% of holdings can call an Annual General Meeting has been a key driver of shareholder activism;
- The King Codes of Corporate Governance is also playing a key role by entrenching the idea that board of directors must act in the best interests of the company and that their responsibilities extend to shareholders and other stakeholders;
- Fostering the culture of transparency– for instance, by putting more information in the hands of shareholders and the public, Board members are likely to become even more accountable and responsible.

Corporate Governance in the Banking Sector: Another area where important reforms have been made in recent years is the banking sector, following the Amendment of the Zimbabwean Banking Act in 2015 to tackle corporate governance deficiencies and money laundering. This is probably one area where reforms undertaken are in line with changes at the global level where increasingly stringent regulatory and compliance measures have been adopted to combat money laundering and terrorism financing.

Although the cost of these reforms, most notably the ones associated with the conduct of Customer Due Diligence and Compliance with KYC have been significant for financial institutions they are necessary and should be adopted by bankers and financial institutions in Zimbabwe and across Africa. In a generalized environment of de-risking where large multinational banks are either exiting the African financial landscape or withdrawing from correspondent banking relationships to mitigate the marginal cost of compliance it is probably a step in the right direction.

I personally welcome additional steps taken by RBZ under the latest reform of the Banking Act, including step to:

- Tighten of bank supervision, monitoring and control;
- Dilute controlling individual or bank holding shareholder influence on banks;
- Regulate the acquisition of shares of a banking institution or controlling company;
- Limit the voting rights of members of a banking institution or controlling company to no more than 5 percent of total share capital or voting rights.

Still the reformed Act alone will not improve governance in the banking sector if it is not followed by concrete steps to ensure enforcement of prudential guidelines and requirements in the Banking Act as amended, in the context of Basel core principles and the emerging IFRS9, and sanction in case of violation.

At the same time good corporate governance, as far as transparency, accountability and responsibility are concerned, should guide actions taken by both Board of Directors and management because even the best intention and laws can be circumvented if one really wants to. In the banking sector it will take both the management and Board oversight to do that.

Public Sector Corporate Governance: Corporate governance is not exclusively a private sector matter, especially in region where governments continue to account for a sizable share of the economy. In line with most African countries, the private sector accounts for more than 40% of the Zimbabwean economy, suggesting promoting good corporate governance exclusively in the private sector is unlikely to result in sustainable economic development if only 60% of corporations are targeted in the best case scenario. Perhaps the government which has the responsibility of regulating banks cannot be absolved from the protracted financial and banking crisis facing the country.

But the debate between public and private sector can no longer be approached from an ideological standpoint as done in 1980s during the implementation of Structural Adjustment Programmes. Public corporations are performing very well in China and Europe. Ethiopian Airlines, Airbus and Lufthansa are still largely owned by governments and some of the best performing and globally competitive Chinese companies are state-owned.

In this regard, the challenges of weak governance, poor management and corruption which are plaguing African sovereign entities are not necessarily due to the fact that these entities are state-owned- but perhaps largely attributed to weak corporate governance standards and accountability of Management and governments in the absence of checks and balances which has given rise to excessive centralized power. And at this stage the contrast with South Africa which has relatively strong institutions is instructive: KPMG, one of the big four which has been accused of propping up the Gupta family in their drive to capture the State appeared before the South African Parliament's Standing Committee on Public Accounts. In addition to exercising its oversight function the Parliament eventually joined other major firms and institutions which are severing their ties with KPMG as part of sanctions.

Hence perhaps the first step in reforming sovereign entities and promoting the culture of good governance more generally is to make sure that accountability goes hand-in-hand with sanctions as a deterrent. The second is to make sure that sovereign entities are run and managed as profit-making and not as acceptable loss-making institutions subject to lower corporate governance standards, with management evaluated yearly against agreed growth targets. Private investors could also be invited to the shareholding structure to forge a public-private partnership with the view to strengthening the culture of good corporate governance, with emphasis on **Transparency**, **Independence** and **Accountability**.

Distinguished Guests,
Ladies and Gentlemen,

After a review of key areas outlined—most notably (i) corporate governance reporting, (ii) corporate governance systems in the banking sector, (iii) shareholder activism, and (iv) public sector corporate governance, I would like to close my keynote address with some reflections on the nature of the relationship between corporate governance and economic growth because how we integrate that relationship in our business and development model will have tremendous implications for growth and development outlook in our region and countries.

While good corporate governance is definitely growth-enhancing as I have argued in this address, implicitly the proposed theme suggests that good corporate governance could well be a pre-requisite or a necessary condition for sustainable economic development. But, is it really the case that countries first have to build good institutions and establish a good and strong corporate governance culture in order to achieve economic growth and sustainable development?

Which comes first in the process of economic development—good governance: 'that is address the corporate governance bottleneck first and growth will follow'; or economic growth: 'that is engineer economic growth and governance will automatically improve'.

Empirical evidence points to a rather complex relationship between corporate governance and growth. Growth and even robust economic growth has occurred in countries with relatively poor and weak corporate governance.

Instead, most countries in those regions with more developed and diversified economies followed a very interesting model, first, harnessing normatively "weak" institutions to kick-start markets and economic development; then drawing on the power of emerging markets to stimulate strong institutions in the second phase of their development trajectory; and in the third and last phase drawing on the strength of good institutions to preserve and regulate markets in support of economic growth and sustainable development.

At the same time, complacency for corporate and sovereign entities which have managed to establish a strong culture of good corporate governance and institutions to drive economic growth and expand the corporate balance sheets can be fatal. In effect if there is one lesson we learned from the 2007-08 Global Financial Crisis, which had the USA as the epicenter, it is that good corporate governance is neither the panacea of developed economies nor a given proposition. That is, cases and instances of poor corporate governance are not only found in developing countries at very early stage of structural transformation, and to be precise in Africa; that is once a sovereign and corporate entity is endowed with a culture of good corporate governance and institutions then these attributes become permanent features of its development or growth process.

In practice, the relationship between corporate governance and economic development has not been linear or unidirectional, systematically moving from the corporate governance to strong economic growth. While the correlation between good governance and economic growth is positive, the relationship between governance and economic performance is complex. Markets and economic environment are also shaping the institution of governance and the corporate governance culture in most regions around the world, including both in developed and developing countries.

The amendment of the Zimbabwean Banking Act in 2015 was indeed a reflection of the changing global and African economic environment. Economic transformation tends to have disrupting effects on corporate and political governance, sometimes giving rise to strong interest groups that can eventually push for more accountable leaders and effective institutions. And as countries move up the income ladder more effective institutions become affordable.

In this regard I do not expect the relationship between these two important variables—corporate governance and economic development—to follow a different path or distribution in Zimbabwe and more generally across the African continent. We should always be mindful of the complexity of the relationship between governance and economic performance as we strive to put our corporate and sovereign entities on a strong and robust growth trajectory.

Good corporate governance is a necessary but certainly not a sufficient condition for the expansion of corporate balance sheets and economic development. In this regard, it should be seen as aspirational and not as a perennial binding constraint when it is deficient. Sovereign and corporate entities can always do with what is in effect and continuously build on it. Likewise, good corporate governance once achieved is not a permanent feature of some institutions, hence the need to have strong and competent boards for oversight to ensure continuous renewal and growth.

Thank you for your attention,

Thank you.